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Research Update:

International Investment Bank Long-Term Rating Raised To 'BBB+' On Very Strong Financial Profile; Outlook Stable

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Overview

- Multilateral lending institution International Investment Bank (IIB) has demonstrated low credit costs and low levels of nonperforming loans since its re-launch in 2012, and has meaningfully increased the quality of its liquid assets.
- We are therefore raising our long-term rating on IIB to 'BBB+' from 'BBB' and affirming the 'A-2' short-term rating.
- The stable outlook reflects our view that IIB will continue expanding its loan portfolio to reach its target while maintaining a very strong capital position and ample liquidity.
- We have corrected the miscalculation of the risk-adjusted capital ratio, which had no impact on our ratings or outlook, which we published in our previous research.

Rating Action

On April 12, 2018, S&P Global Ratings raised its long-term foreign currency issuer credit rating on International Investment Bank (IIB) to 'BBB+' from 'BBB'. The outlook is stable. At the same time, we affirmed the 'A-2' short-term foreign currency issuer credit rating.

Rationale

We revised our assessment of IIB's financial profile to very strong from strong, which led us to raise the rating. The revision reflects the low level of nonperforming loans (NPLs; loans overdue by 90 days or more) over the past five years since the bank's re-launch in 2012, low credit costs, and the sustained improvement of the quality of the treasury portfolio.

Our ratings on IIB are based on its business profile, which we still consider weak, and its financial profile, which we now consider very strong. Together, these factors lead us to assess IIB's stand-alone credit profile (SACP) at 'bbb+'. Our ratings on IIB do not incorporate any explicit uplift for extraordinary shareholder support in the form of callable capital.

We note IIB's low level of NPLs, which represented 4.5% of the gross loan portfolio at year-end 2017. This level is below the peer group average. The bank's re-launch in 2012, when the entire management team was replaced, fundamentally shifted the risk appetite and monitoring of risk at IIB. In 2013, NPLs made up more than 70% of IIB's gross loan portfolio when the bank was turned over, and most of its toxic loans were either written off or sold. We positively view that IIB's management is committed to keeping NPLs below 5% of the gross loan portfolio.

We believe IIB adequately manages its liquidity and has for the second year in a row improved the quality of its treasury portfolio, with the share of 'A' to 'AAA' rated assets increasing to 49% of the total treasury assets in the first quarter of 2018, from 43% in the last quarter of 2017. The management is committed to sustaining the improved quality, and even to increasing the share of 'A' to 'AAA' instruments to 65% by year-end 2020. Our liquidity ratios for IIB indicate that it would be able to cover all committed lending and debt repayments for at least one year, even under stressed market conditions, without access to the capital markets.

We still consider IIB's business position as weak, mainly owing to its size relative to peers. Its governance and risk management weighs on the assessment, as well. However, we note IIB's ongoing work to improve its governance standards, processes, and systems, which is already delivering tangible improvements. While still very small in relation to the economies of its nine members--and as such with a limited scope--IIB is becoming more important to the region and is improving its competitive position. This can be seen in its strong loan portfolio growth in 2017, which exceeded our expectations. While growth was high, however, the portfolio only amounts to €725.6 million. IIB's operations focus on four countries, with Russia dominating (25% in loan portfolio), followed by Romania (11%), Slovakia (9%), and Mongolia (9%).

The above-mentioned portfolio growth prompted a need to raise quite significant amounts of new funding in 2017. We believe IIB benefits from an increased diversification trend in its funding sources. Among new placements in 2017 was a two-tranche debt issue on the Romanian market, one tranche denominated in Romanian lei (RON300 million [about €65 million]) and the other tranche denominated in euros (€60 million), with a maturity of three years. All issues in local currency are swapped into dollars or euros.

The flip side of the robust loan portfolio growth in 2017 was the decline in the risk-adjusted capital (RAC) ratio before adjustments to 27.7% at the end of 2017, from 40.4% as of year-end 2016. As of Dec. 31, 2017, IIB's RAC ratio stood at 24.1% (compared with 28% a year ago), with adjustments specific to multilateral lending institutions in our methodology--mostly for single-name concentration on corporates. We have corrected the RAC ratio miscalculation we published in our previous research update on June 28, 2017, in which we erroneously indicated that the RAC ratio stood at 37.7% when it actually stood at 28.0%. The increased diversification of the loan portfolio helped the RAC ratio stay above our 23% threshold for capital adequacy. We expect these ratios might decline over the next year, due to further loan portfolio growth in the absence of fresh capital injections. However, we think they will still stay comfortably above 15%, supporting our assessment of the bank's very strong financial profile.

IIB was established in 1970 by a treaty and the bank enjoys supranational status. It is exempt from custom duties, direct taxes, and restrictions on export/import operations, as well as being immune to the sanctions currently imposed on Russia. Its shareholder structure comprises nine member states. IIB's shareholding is dominated by four countries (Russia, Bulgaria, Hungary, and Czech Republic), which account for about 85% of paid-in capital. The other shareholders are Cuba, Mongolia, Vietnam, Slovakia, and Romania. Russia dominates the structure with 48% of the paid-in capital (down from 58% in 2013). We believe that the current "one country, one vote" agreement protects the interests of the minority shareholders.

IIB's mission is to promote social and economic development of the member states. Its credit lending covers lending to small and midsize enterprises, export-import operations, project financing, and mergers and acquisitions, primarily through leading domestic publicly owned banks, development banks, and other financial institutions.

We assess positively the stability and strength of the relationship between IIB and its shareholders. In the past 16 years, the only change in the number of shareholders has been Hungary's rejoining the IIB. The bank is open for new members to join and aims to grow its shareholder base by one or two countries in the next two years.

IIB has callable capital, but we don't incorporate any uplift for extraordinary shareholders' support.

Outlook

The stable outlook reflects our view that IIB's credit strengths, coupled with its supranational status, will help the bank to achieve its loan portfolio growth target while maintaining a very strong capital position and ample liquidity.

We could consider an upgrade in the next 12-24 months if we were to observe an improving business position. This could be the result of a growing loan portfolio that is supported by shareholder capital injections. This would most likely only be achieved if the bank's RAC ratio remained between 15% and 23%, which we expect to be the case.

Conversely, we could lower the ratings in the next 12-24 months if, due to the further loan portfolio growth, the bank were unable to maintain its solid capital adequacy, with the RAC ratio falling below 15%.

Related Criteria And Research

Related Criteria

- Criteria - Governments - General: Multilateral Lending Institutions And Other Supranational Institutions Ratings Methodology - November 26,2012
- General Criteria: Use Of CreditWatch And Outlooks - September 14,2009
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings - April 07,2017
- Criteria - Financial Institutions - Banks: Multilateral Lending Institutions Capital Methodology And Assumptions - December 06,2010

Related Research

- Supranationals Special Edition 2017: Comparative Data For Multilateral Lending Institutions - October 20, 2017

- Introduction To Supranationals Special Edition 2017 - October 20, 2017
- How An Erosion Of Preferred Creditor Treatment Could Lead To Lower Ratings On Multilateral Lending Institutions, Aug. 26, 2013
- Request For Comment: Multilateral Lending Institutions And Other Supranational Institutions Ratings Methodology, Oct. 11, 2017

Ratings List

	Rating	
	To	From
International Investment Bank		
Issuer Credit Rating		
Foreign Currency	BBB+/Stable/A-2	BBB/Stable/A-2

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. Complete ratings information is available to subscribers of RatingsDirect at www.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column. Alternatively, call one of the following S&P Global Ratings numbers: Client Support Europe (44) 20-7176-7176; London Press Office (44) 20-7176-3605; Paris (33) 1-4420-6708; Frankfurt (49) 69-33-999-225; Stockholm (46) 8-440-5914; or Moscow 7 (495) 783-4009.

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