

RATING ACTION COMMENTARY

Fitch Affirms BOAD at 'BBB'; Outlook Negative

Tue 18 May, 2021 - 13:07 ET

Fitch Ratings - Paris - 18 May 2021: Fitch Ratings has affirmed Banque Ouest Africaine de Developpement's (BOAD) Long-Term Issuer Default Rating (LT IDR) at 'BBB' with Negative Outlook.

A full list of rating actions is below.

KEY RATING DRIVERS

BOAD's 'BBB' rating is primarily driven by extraordinary support from key shareholders, the Banque Centrale des Etats de l'Afrique de l'Ouest (BCEAO, 47%) and Cote d'Ivoire (B+/Positive, 6%). Fitch assesses the capacity of the key shareholders to provide support at 'bbb-', taking into account their average credit quality. The ability of BCEAO to tap the fiscal resources that it manages on behalf of the regional member states to secure payment of capital increases translates into an 'exceptional' propensity to support, and a one-notch uplift over the capacity to support, leading to an overall support assessment of 'bbb'.

The Negative Outlook reflects the risk of weakening support from the bank's shareholders. The Outlook on France's sovereign LT IDR (AA) is Negative. Given the role played by France in the CFA franc monetary arrangement as the guarantor of the convertibility of the currency against the euro, a downgrade of France's rating to 'AA-' would affect our assessment of the credit quality of the bank's largest shareholder, BCEAO. In turn, this would lead to a downward revision in our assessment of BOAD's

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evident in the performance of BOAD's sovereign and non-sovereign loan book. As a result, Fitch now expects stronger risk and capitalisation profiles in the medium term. Our 'bb+' intrinsic assessment is driven by BOAD's 'bbb+' solvency and a three-notch negative adjustment for a high-risk business environment. BOAD's 'bbb+' solvency assessment reflects 'strong' capitalisation and a 'moderate' risk profile. Fitch assesses the bank's liquidity at 'a'.

Fitch's two capitalisation ratios - equity-to-assets and the usable capital-to-risk-weighted assets (FRA) - were both 29% as of end-2020, consistent with a 'strong' assessment. The agency expects the two ratios to gradually decline in the medium term, to 23%-28%, primarily as a result of a projected increase in the loan book. The bank's own capital adequacy framework includes a 25% floor for the equity-to-asset ratio. Fitch's forecasts assume regular paid-in capital payments under the current capital increase programme. Although discussions on a potential new capital increase are ongoing, our projections do not factor in such an increase. A new capital increase that significantly strengthens our assessment of the bank's capitalisation could support stronger solvency.

Fitch has revised its assessment of credit risk to 'moderate' from 'high'. The average rating of loans was 'B' as of end-2020, unchanged from the previous review, which Fitch expects the bank to maintain in the medium term. The credit quality of the loan book is supported by the fairly strong economic performance of the West African Economic and Monetary Union (WAEMU) region through the Covid-19 crisis and the limited exposure of the bank to the most affected sectors: 0.7% of the total loan book or 2.6% of the non-sovereign sector loan book (4% of the private-sector loan book excluding public companies) is exposed to the 'tourism' sector (hotel and transport)). In addition, 29% of loans are in countries where the sovereign is on Positive Outlook (Benin, 'B', and Cote D'Ivoire).

The revised assessment of credit risk also reflects the resilience of loan performance in 2020. Non-performing loans (NPLs)-to-total loans fell to 2.7% as of end-2020 from 2.97% as of end-2019. BOAD is one of the few MDBs with non-sovereign operations that have not granted suspension of debt payment to its non-sovereign borrowers. In Fitch's view, the lack of payment holiday is further evidence of the resilience of BOAD's loan performance.

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been sustained through the crisis (even though seven out of eight sovereigns in WAEMU benefited from the Debt Service Suspension Initiative on bilateral debt).

The overall assessment of risks remains 'moderate'. Concentration is 'moderate', with the bank's top-five largest exposures (all sovereigns) accounting for 48% of total exposures in 2020. The bank hedges its USD/XOF exchange-rate risk (arising from its US dollar Eurobond issuance) with cross-currency swaps. Equity participation was 4.25% of total banking exposure (TBE) in 2020. The bank's main capital adequacy metrics are a Basel-type ratio and a leverage limit that caps debt at three times the level of equity. The bank will start using its new economic capital model, including limits by counterparties, sectors and countries, this year.

Fitch assesses the bank's liquidity at 'a'. The assessment reflects 'strong' coverage of short-term debt by liquid assets, which we expect to remain between 100% and 150% over the forecast period. Fitch only views as liquid the deposits held at the regional central bank and regional sovereign debt securities that the bank can refinance with BCEAO (with a 10% haircut). BOAD's access to the regional central bank's refinancing window is a rare feature for an MDB and enhances Fitch's overall liquidity assessment.

The liquidity assessment also accounts for the bank's proven access to capital markets. BOAD has issued several Eurobonds in US dollars and issued its first euro-denominated bond in January 2021 (EUR750 million). The bank is considering a programme to access the short-term money market in France. BOAD also has access to funding in the form of loans from bilateral and multilateral creditors. As of end-2020, 60% of BOAD's debt was in the form of Eurobonds, 34% loans by multilateral and bilateral institutions and 6% debt issued on WAEMU regional capital markets.

BOAD's 'high risk' business environment primarily reflects the low income and high political risks in the countries in which it operates, including Togo where the bank's headquarters are located. The assessment also reflects exposure to non-sovereign risk (33% of banking exposure at end-2020), the small size of BOAD and the importance of its public mandate: in recent years, the BOAD has been the second-most important provider of funds for infrastructure in WAEMU, just behind the World Bank.

The Short-Term IDR of 'F2' is the higher option at the 'BBB' cusp point on Fitch's long-term rating correspondence table. The choice of the higher option results from the

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RATING SENSITIVITIES

Factors that could, individually or collectively, lead to negative rating action/downgrade:

Support (capacity): A weakening in the support assessment, which could stem from deterioration in the credit quality of BOAD's main shareholders or an assessment of reduced support from France for the CFA franc monetary arrangement.

Intrinsic (solvency): Deterioration in BOAD's solvency assessment, potentially stemming from a worsening of the bank's credit risk profile and/or weaker than-expected capitalisation in the medium term.

Intrinsic (liquidity): A material deterioration in Fitch's liquidity assessment, which could result from a weakening in coverage of short-term debt by liquid assets and/or a weakening in the quality of treasury assets.

Factors that could, individually or collectively, lead to positive rating action/upgrade:

Support (capacity): A strengthening in Fitch's assessment of BOAD's key shareholders' capacity to provide support to BOAD. This could stem from an improvement in the credit quality of BOAD's current key shareholders or a change in the structure of the bank's capital that leads to a marked increase in the share of capital owned by one or several non-regional highly-rated shareholders.

Intrinsic (solvency/business environment): Material improvement in the bank's solvency assessment. This could result from a combination of significant strengthening in the capitalisation and risk profiles or an improvement in Fitch's assessment of the bank's business environment.

BEST/WORST CASE RATING SCENARIO

International scale credit ratings of Sovereigns, Public Finance and Infrastructure issuers have a best-case rating upgrade scenario (defined as the 99th percentile of rating transitions, measured in a positive direction) of three notches over a three-year rating horizon, and a worst case rating downgrade scenario (defined as the 99th percentile of

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determine sector-specific best- and worst-case scenario credit ratings, visit <https://www.fitchratings.com/site/re/10111579>.

KEY ASSUMPTIONS

The ratings and Outlook are sensitive to a number of assumptions:

-The global economy will develop in line with Fitch's Global Economic Outlook published on 17 March 2021, including marked improvement in GDP growth in 2021 as economies adapt to social distancing and vaccination programmes gather momentum.

-The key features of the WAEMU and the monetary arrangement with France, including the peg to the euro, the pooled regional reserves and the convertibility guarantee from the West African CFA franc to the euro, will remain unchanged in the medium term. We also assume that the parity of the West African CFA franc with the euro will remain unchanged.

-BOAD's borrowing sovereign member states, even if experiencing severe difficulties, will preserve the bank's PCS should they decide to default selectively on their debt.

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

PUBLIC RATINGS WITH CREDIT LINKAGE TO OTHER RATINGS

BOAD's 'BBB' rating is primarily driven by extraordinary support from key shareholders, BCEAO and Cote d'Ivoire.

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BOAD has an ESG Relevance Score of '4' [+] for Policy Status and Mandate Effectiveness. It has access to BCEAO's refinancing window, which is a rare feature for supra-nationals and supports the bank's liquidity profile. This has a positive impact on the credit profile, and is relevant to the ratings in conjunction with other factors.

BOAD has an ESG Relevance Score of '4' for Rule of Law, Institutional & Regulatory Quality. All supra-nationals attract a score of '4'. Supra-nationals are neither subject to bank regulation nor supervised by an external authority. Instead, supra-nationals comply with their own set of rules. Fitch pays particular attention to internal prudential policies, including compliance with these policies. This has a negative impact on the credit profile, and is relevant to the ratings in conjunction with other factors.

BOAD has an ESG Relevance Score of '4' for Governance Structure. High capital ownership by borrowing countries with weak credit fundamentals and limited access to external funding have led to pressure to increase lending. This risk has been partly mitigated by a fairly high share of voting rights held by non-regional members at the board. This has a negative impact on the credit profile, and is relevant to the ratings in conjunction with other factors.

Unless otherwise disclosed in this section, the highest level of ESG credit relevance is a score of '3'. This means ESG issues are credit-neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity. For more information on Fitch's ESG Relevance Scores, visit www.fitchratings.com/esg

RATING ACTIONS

ENTITY / DEBT ⚡	RATING ⚡	PRIOR ⚡
Banque Ouest Africaine de Developpement	LT IDR BBB Rating Outlook Negative Affirmed	BBB Rating Outlook Negative

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senior unsecured

LT BBB Affirmed

BBB

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