

RATING ACTION COMMENTARY

Fitch Affirms BOAD at 'BBB'; Outlook Stable

Thu 04 May, 2023 - 12:22 ET

Fitch Ratings - Paris - 04 May 2023: Fitch Ratings has affirmed Banque Ouest Africaine de Developpement's (BOAD) Long-Term Issuer Default Rating (LT IDR) at 'BBB' with a Stable Outlook.

A full list of rating actions is detailed below.

KEY RATING DRIVERS

SCP Drives Rating: Fitch has revised BOAD's Standalone Credit Profile (SCP) to 'bbb' from 'bb+' following a series of improvements. BOAD's ratings are now driven by its SCP, instead of support from shareholders. The 'BBB' LT IDR reflects BOAD's solvency of 'a-' and a two-notch negative adjustment to reflect the 'high' risk business environment in which the bank operates. BOAD's liquidity is assessed at 'a'.

Capital Increase Supports Solvency: BOAD's shareholders have approved a new capital increase of XOF554 billion, equivalent to 50% of subscribed capital. Existing shareholders will subscribe 75% of the capital increase, while new non-regional shareholders are set to subscribe the remaining 25%.

The bulk of the capital increase (80%) will be in the form of paid-in capital, which will support BOAD's capital ratios in the medium term. The participation of non-regional shareholders in BOAD's capital will increase to at least 14%, from 6% currently, increasing the highly rated callable capital that Fitch considers in its assessment of its usable capital to risk-weighted assets (FRA) ratio.

Capitalisation Ratios to Strengthen: Fitch expects BOAD to operate with stronger capital ratios over the medium term. As of end-2022, capital ratios had markedly increased following a XOF90 billion transfer to the bank's own funds from a fund owned by BOAD used to subsidise loans to member states ('mécanisme de bonification'). Following this transfer and a previous one in 2019, the 'mécanisme de bonification' is partly depleted, meaning no equivalent transfer will be possible in the next few years.

BOAD's equity-to-asset ratio was 33% in 2022, up from 29% in 2021. The FRA ratio increased to 31% from 27% over the same period. Fitch expects the two capital ratios to moderately strengthen in the medium term, reflecting paid-in capital payments spread over up to five years from 2023 and continued expansion of the bank's operations. These projections only factor in paid-in capital payments by existing shareholders.

Resilience in Risk Profile: Fitch has revised its assessment of credit risk to 'moderate' from 'high', principally reflecting the resumption of payments and clearance of all arrears by the Malian sovereign (8% of the loan book) to the bank after financial sanctions on the country were lifted in July 2022.

The average rating of the loan book was 'B' as of end-2022, an improvement from 'B-' at the previous review. After accounting for BOAD's preferred creditor status, the average rating of loans is 'BB-'. Non-performing loans (NPLs) were 2.9% as of end-2022 and Fitch expects they will remain just below 3% over the medium term, in line with the bank's record in recent years.

'Moderate' Risk Overall: The bank's top-five largest exposures (all sovereigns) accounted for 48% of total loans as of end-2022. The bank hedges its US dollar and CFA franc exchange rate risk with cross-currency swaps. The bank's main capital adequacy metrics are a Basel-type ratio and a leverage limit caps debt at three times the level of equity.

Access to Central Bank Refinancing: Fitch assesses the bank's liquidity at 'a'. The assessment reflects 'strong' coverage of short-term debt by liquid assets and the bank's proven access to capital markets. Fitch only considers as liquid the deposits held at the regional central bank and regional sovereign debt securities that the bank can refinance with the central bank. The liquidity assessment is enhanced by BOAD's access to the regional central bank's refinancing window.

Improvement in Business Environment: The business environment is 'high risk', leading to a notching down from the solvency assessment by two notches, versus three notches previously. The reduction in the negative notching reflects the rising policy importance

of the bank, as underlined by the growing size of its balance sheet and the new capital increase approved by shareholders.

We expect non-borrowing highly-rated shareholders to play a growing role in the bank's governance. The overall assessment of BOAD's business environment remains 'high risk', primarily due to the low income, low credit quality and high political risks in the countries in which the bank operates.

BCEAO Dilution Could Affect Support: Fitch assessment of BOAD shareholders' capacity to support is based on the average rating of key shareholders, ie those largest shareholders whose capital contribution totals at least 50% of subscribed capital. As of end-2022, BOAD's key shareholders were the Banque Centrale des Etats de l'Afrique de l'Ouest (BCEAO, owning 47% of BOAD's capital) and Cote d'Ivoire (BB-/Stable, 6%) resulting in a support capacity assessment at 'bbb-'. The dilution of BCEAO in line with the ongoing capital increase could lead to a weakening in this assessment unless one of the non-regional highly-rated shareholders becomes a key shareholder.

Exceptional Propensity to Support: BCEAO's ability to tap the fiscal resources it manages on behalf of the regional member states to secure payment of capital increases translates into an 'exceptional' propensity of shareholders to support, and a one-notch uplift over the capacity to support, leading to an overall support assessment of 'bbb'.

Short-Term Rating: The Short-Term IDR of 'F2' is the higher of two options mapping to a LT IDR 'BBB'. This reflects the bank's liquidity assessment of 'a', which is above the level equivalent to the minimum Long-Term IDR (BBB+), at which the higher Short-Term IDR (F2) would apply.

RATING SENSITIVITIES

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

Given that BOAD's ratings are underpinned by the SCP and support, a negative rating action would require a deterioration in our assessment of both BOAD's SCP and support.

SCP (solvency): Deterioration in BOAD's solvency assessment, potentially stemming from a worsening of the bank's credit risk profile or weaker capitalisation and loss absorption capacity in the medium term

Support (capacity): A weakening in the support assessment, which would stem from a deterioration in the credit quality of BOAD's main shareholders or a dilution in the

share ownership of BCEAO not offset by the participation of a non-regional highly-rated shareholder as key shareholder

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

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

SCP (solvency): Material improvement in the bank's solvency assessment. This could result from a combination of stronger-than-expected capital ratios (beyond the participation in the bank's capital of new non-regional shareholders) and significant strengthening in the risk profile

Support (capacity): A strengthening in Fitch's assessment of BOAD's key shareholders capacity to provide support. This could stem from an improvement in the credit quality of BOAD's key shareholders

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 rating transitions, measured in a negative direction) of three notches over three years. The complete span of best- and worst-case scenario credit ratings for all rating categories ranges from 'AAA' to 'D'. Best- and worst-case scenario credit ratings are based on historical performance. For more information about the methodology used to determine sector-specific best- and worst-case scenario credit ratings, visit <https://www.fitchratings.com/site/re/10111579>.

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.

ESG CONSIDERATIONS

BOAD has an ESG Relevance Score of '4[+]' for 'Human Rights, Community Relations, Access and Affordability'. BOAD provides concessional loans to its member states funded by concessional resources provided by its shareholders. This supports BOAD's policy importance and shareholders' propensity to support the bank. 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 'Governance Structure'. A high share of capital ownership by borrowing countries with weak credit fundamentals and limited access to external funding has led to pressure to increase lending. This risk has been somewhat 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.

BOAD has an ESG Relevance Score of '4' for 'Rule of Law, Institutional and Regulatory Quality'. All supranationals attract a score of '4'. Supranationals are neither subject to bank regulation nor supervised by an external authority. Instead, supranationals 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 'Policy Status and Mandate Effectiveness'. BOAD has access to the BCEAO refinancing window. This is a rare feature for supranationals 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.

Except for the matters discussed above, the highest level of ESG credit relevance, if present, 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 to 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 Stable	BBB Rating Outlook Stable
	Affirmed		
	ST IDR	F2 Affirmed	F2

senior unsecured

LT BBB Affirmed

BBB

VIEW ADDITIONAL RATING DETAILS**FITCH RATINGS ANALYSTS****Arnaud Louis**

Senior Director

Primary Rating Analyst

+33 1 44 29 91 42

arnaud.louis@fitchratings.com

Fitch Ratings Ireland Ltd

28 avenue Victor Hugo Paris 75116

Hawa Ly

Senior Analyst

Secondary Rating Analyst

+44 20 3530 1280

hawa.ly@fitchratings.com

Paul Gamble

Senior Director

Committee Chairperson

+44 20 3530 1623

paul.gamble@fitchratings.com

MEDIA CONTACTS**Peter Fitzpatrick**

London

+44 20 3530 1103

peter.fitzpatrick@thefitchgroup.com

Additional information is available on www.fitchratings.com**PARTICIPATION STATUS**

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APPLICABLE CRITERIA

Supranationals Rating Criteria (pub. 11 Apr 2023) (including rating assumption sensitivity)

ADDITIONAL DISCLOSURES

Dodd-Frank Rating Information Disclosure Form

Solicitation Status

Endorsement Policy

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Banque Ouest Africaine de Developpement

EU Issued, UK Endorsed

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