CREDIT GUARANTEE INVESTMENT FACILITIES PLC

No. 151/2018
10 October 2018

SUPRANATIONALS

Company Rating:	AAA
Outlook:	Stable

Company Rating History:

Date	Rating	Outlook/Alert
28/08/14	AAA	Stable

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RATIONALE

TRIS Rating affirms the company rating on Credit Guarantee and Investment Facility (CGIF), a trust fund of Asian Development Bank (ADB), at “AAA”. The rating reflects CGIF’s status as a supranational institution owned by the governments of the ASEAN+3 countries and ADB, together referred to as “contributors”. The rating also reflects CGIF’s strong capital, viable business model, and conservative risk management framework. The rating takes into consideration CGIF’s short operational track record and the challenges it faces as it expands.

KEY RATING CONSIDERATIONS

Supranational institution

The rating on CGIF reflects its status as a supranational institution. TRIS Rating believes there is a high likelihood that CGIF will receive financial support from its major contributors in times of financial distress.

The strong credit profiles of the major contributors to CGIF reflect their ability to provide support. S&P Global Ratings rates the top four contributing countries, which have contributed almost 90% of CGIF’s capital, in the “A+” to “AAA” range. The contributors have demonstrated their willingness to support CGIF. In late 2017, they approved a capital increase of US$500 million to be injected by 2023, which will raise CGIF’s capital base to US$1.2 billion. CGIF also serves strategically important objectives of the contributors by promoting development of the regional bond markets.

Viable business platform

CGIF’s organisational structure adequately supports its policy objectives and functions. The internal credit risk assessment guidelines, governance framework, and audit policies are developed under international standards. Risk management is also conservative, in our view, with well-defined risk parameters and concentration limits on underwriting and investment exposures. CGIF also continually refines its risk management guidelines and strengthens its internal capacity to manage risks.

There has been no record of credit default since its inception in 2010. However, credit risk still needs to be monitored given the short track record of CGIF’s operation. We also think CGIF’s developmental focus on countries with weaker credit profile and less developed bond markets could expose it to credit risks.

Strengthening capital base

We expect CGIF’s capital adequacy to further strengthen over the next few years as a result of the capital increase. Its Basel II capital adequacy ratio, net of reinsurance, was 32.5% at the end of June 2018, up from 28.0% at the end of June 2017.

The strong capital adequacy also reflects the size of CGIF’s guarantee portfolio, which remains well below the maximum guarantee capacity (MGC) of 2.5 times the total available capital. As of June 2018, CGIF’s total guarantee exposure was US$873 million, 0.97 times the total available capital, compared with MGC of US$2.3 billion.

Good asset quality

We believe conservative risk management will help maintain the good asset quality of CGIF's guaranteed portfolio. There has been no default so far on any of CGIF's guarantee bonds requiring its payment. We also think credit risk concentration will less likely become an issue. A capital increase will raise concentration limits on CGIF's guarantee exposure, computed as percentages of MGC or paid-in capital. As of June 2018, CGIF's guarantees were well within concentration limits.

We also believe the asset quality of CGIF's investment portfolio is strong. ADB manages CGIF's capital as trustee under a conservative investment policy. The portfolio is largely comprised fixed-income securities with high credit ratings. CGIF also limits portfolio duration at five years to control market and liquidity risks.

CGIF increased the average effective duration of its investment portfolio to 2.9 years at the end of 2017, from 2.6 years in the previous year. As a result, returns from the investment portfolio improved to 1.60% per annum (p.a.) in 2017, up from 1.46% p.a. in 2016. Although a higher duration may expose CGIF to market risk during the upturn of the interest rate cycle, we believe the risk is still low as it generally pursues a held-to-maturity investment. As a long-term policy, CGIF targets the average effective duration of its investment portfolio at two to four years.

Liquidity is very high

We expect CGIF's liquidity profile to remain very strong. We expect cash inflows from investments and guarantee fees to cover cash outflows from operating expenses over the next 12 months. Investment portfolios comprise marketable fixed-income securities with high credit ratings. CGIF can also engage in repurchase transactions to manage its liquidity needs. Further, CGIF regularly applies stress scenarios to assess its liquidity position.

RATING OUTLOOK

The "stable" outlook reflects TRIS Rating's view on the ability and willingness of the major contributors to support CGIF and our expectation that CGIF will continue to serve its strategic roles. The outlook also reflects our expectation that CGIF will maintain a strong financial profile and a prudent risk management framework.

RATING SENSITIVITIES

The rating could face downward pressure if losses in the guarantee portfolio cause CGIF's financial profile to deteriorate significantly, or if there is evidence of weakening supports from the contributors.

COMPANY OVERVIEW

CGIF was founded in November 2010 by the governments of the ASEAN+3 countries (10 ASEAN countries plus China, Japan, and Korea) and ADB, together referred to as "contributors". CGIF's main objective is to provide credit guarantees which allow eligible issuers to access local currency bond markets. Issuers can thus avoid currency and maturity mismatches by issuing bonds within the region. Establishment of CGIF was a continual development process following the Asian Bond Markets Initiative (ABMI) introduced in 2003 by the ASEAN+3 countries. The aims of ABMI are to develop and strengthen the local currencies and regional bond markets to promote economic growth and financial development, and to prevent disruptions to the international financial order so as to enable savings in the region to be used within the region.

CGIF has four business functions:

1. Guaranteeing bonds in local currencies, issued by entities with local-scale and investment-grade ratings, to help issuers reduce currency and maturity mismatches;
2. Guaranteeing bonds not in local currencies, issued by entities with local-scale and investment-grade ratings, given that issuers have natural or financial hedges in place, such as a currency matching their underlying business;
3. Making investments for the development of the regional bond markets; and
4. Undertaking other activities and services consistent with the objectives.

Since its inception, CGIF has focused mainly on the first two functions. The latter two functions are for the future.

In a typical guarantee contract, CGIF's insurance services will provide coverage only when an issuer breaches the non-payment event clause. In addition, when a non-payment event occurs, CGIF retains the sole right to decide whether it will early redeem the bonds or continue to pay bondholders according to the original bond schedule. Upon payment by CGIF of all or any part of the guaranteed amounts, CGIF will be entitled to all the rights, powers, and security that bondholders had against the issuers and co-indemnity providers to an amount equal to the paid guaranteed amount.

CGIF finances its operations solely from capital contributions. CGIF is not allowed to borrow from any source, except for cash management purposes.

FINANCIAL STATISTICS AND KEY FINANCIAL RATIOS

Unit: US$ million

		------------Year Ended 31 December ----------			
	Jan-Jun * 2018	2017	2016	2015	2014
Income on investment	9.2	12.5	10.4	9.4	8.8
Income from guarantee	4.1	8.4	7.7	4.8	1.3
Total revenue	13.8	21.0	19.2	14.8	10.1
Net income from operations	8.5	10.7	10.8	8.2	3.6
Total assets	930.1	779.1	772.0	751.6	740.5
Total liabilities	37.1	39.3	44.5	29.0	24.0
Shareholders' equity	893.0	739.2	727.5	722.6	716.5

** Unaudited and not annualised*

Credit Guarantee Investment Facility (CGIF)

Company Rating:	AAA
Rating Outlook:	Stable

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