FitchRatings

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Fitch Revises Outlook on Afreximbank to Positive; Affirms at 'BBB-'

Fitch Ratings - London - 28 Jun 2021: Fitch Ratings has revised the Outlook on African Export-Import Bank's (Afreximbank) Long-Term Issuer Default Rating (IDR) to Positive from Stable and affirmed the IDR at 'BBB-'. Fitch has also affirmed the bank's Short-Term IDR at 'F3' and senior unsecured debt at 'BBB-'.

Key Rating Drivers

The revision of the Outlook on Afreximbank's Long-Term IDR to Positive from Stable primarily reflects the bank's growing importance as the main multilateral development bank (MDB) providing funding to non-sovereign borrowers in Africa. In Fitch's view, the significant capital increase (USD6.5 billion, of which USD2.6 billion paid-in) approved by the board of directors in June this year highlights the increased strategic relevance of the bank for its African shareholders. Timely disbursement of capital payments, which are set to start in 2021, combined with continued evidence of resilience of the bank's solvency to the aftermath of the Covid-19 crisis would lead to an upward revision of our assessment of the bank's business profile and ratings.

Afreximbank's ratings are driven by its Standalone Credit Profile (SCP), including solvency and liquidity, both assessed at 'a-'. The 'high risk' business environment that the bank operates in translates into a three-notch negative adjustment to our assessment of the bank's solvency and liquidity, resulting in a SCP assessed at 'bbb-'.

The 'a-' solvency assessment is driven by Afreximbank's 'strong' capitalisation and 'moderate' risk profile. Strong capitalisation is underpinned by the equity to assets and guarantees ratio at 17% at end-2020, marginally down from a year earlier (18%). Fitch's usable capital to risk-weighted assets (FRA) ratio also weakened to 18% from 20%. The decline in both ratios reflected a significant increase in lending operations, driven by high disbursements under the bank's Pandemic Trade Impact Mitigation Facility (PATIMFA) policy response. The bank disbursed USD6.5 billion of PATIMFA loans, which were funded through reallocation of existing resources, raising new capital and additional debt.

Fitch expects the equity-to-assets and FRA ratios to improve from current levels but remain below 20%, consistent with 'strong' and 'moderate' assessments, respectively. Fitch's projections assume 18% yoy growth in the banking operations and capital injections under the general capital increase, approved by the board of directors in June 2021. The bank plans to raise USD6.5 billion, which would be split between paid-in and callable capital (40%/60%). Class A shareholders are expected to inject USD1.5 billion, with the paid-in capital payments starting shortly. Fitch notes that the African Union has advised its members to use their share of the expected new special drawing rights allocation (endorsed by the G20 countries in April 2021 and totalling USD650 billion equivalent globally) to participate in the capital increase in a timely manner.

Afreximbank's overall exposure to risks is 'moderate', and reflects a 'moderate' credit risk profile and risk management policies, balanced against 'low' concentration risk and 'very low' equity and market risks.

Fitch has revised its assessment of the bank's credit risk to 'moderate' from 'high', owing to the stronger than expected resilience of the bank's asset quality and loan performance to the pandemic. The average rating of loans and guarantees before accounting for credit risk mitigants was unchanged at 'B-' as of end-2020. Since our last rating review in September 2020, Fitch has downgraded two sovereigns, namely Ethiopia (CCC) and Zambia (RD), which combined account for less than 0.5% of the bank's country exposures. The Outlook on Nigeria (B/Stable, 29% of country exposures) was revised to Stable, while the Outlooks on six sovereign ratings that account for 10% of the country exposure remain Negative.

Fitch expects the average rating of loans and guarantees to remain at the current level of 'B-' (before adjusting for risk mitigants) by the end of its 2023 forecasts. This expectation reflects a high degree of loan collateralisation (77% of total loans at end-2020) and limited exposure to sectors (e.g. hospitality, accounting for 1.1% of total exposure) that were hit hardest by pandemic. Fitch incorporates the benefit of the credit risk mitigants used by the bank via an uplift of three notches above the average rating of loans to 'BB-' by 2023.

Non-performing loans (NPL), as reported by the bank, increased to 3.2% of gross loans at end-2020 from 2.8% at end-2019, driven by non-sovereign NPLs. Stage 3 loans, closer to Fitch's own definition of NPLs, increased in absolute terms, but declined as a percentage of gross loans (2020: 3.7% vs 2019: 4.0%) reflecting the growth in the lending portfolio. Fitch expects NPLs and Stage 3 loans to rise moderately but to remain below 6% of gross loans in the medium term, reflecting the lingering impact of the pandemic on certain sectors.

Concentration risk is 'low', with the bank's five largest exposures accounting for 25% of total banking portfolio at end-2020. The 'very low' assessment of market risk reflects the bank's use of derivative instruments in managing FX and interest rate risks and the short-term tenor of its trade finance facilities. The 'moderate' risk management policies primarily reflect the use of credit risk mitigants that have helped maintain a relatively low NPL ratio, despite the high-risk environment that the bank operates in.

Afreximbank's 'a-' liquidity assessment reflects the 'moderate' size of liquidity buffers and quality of liquid assets. At end-2020, liquid assets covered 88% of short-term debt, down from a year earlier (106%). This is due to maturing bonds and short-term deposits attracted under the Africa Resource Mobilisation Program (CENDEP). The bank has recently refinanced USD945 million of bonds with two new Eurobond issuances totalling USD1.3 billion. In addition, Afreximbank has rolled over more than 70% of maturing CENDEP deposits, some of which are held as collateral for loans extended to central banks and non-sovereign entities.

The quality of liquid assets is deemed 'moderate', with the share of the treasury assets rated 'AA' to 'AAA' at 39% of the total in 2020. This is an improvement yoy (2019: 31%). Fitch assesses the bank's access to capital markets and other alternative sources of liquidity as 'moderate', reflecting diversified funding sources, which include credit lines, deposits, and the short duration of the loan portfolio. We expect the liquidity buffer and quality of liquid assets to remain within thresholds of 'moderate' assessments, respectively.

Afreximbank's business environment is deemed 'high risk', primarily reflecting its high-risk operating environment in Africa and the rapid expansion of banking operations in lowly rated countries. The assessment also accounts for the growing importance of the bank's public mandate. The recent decision of the African Union committee to authorise Afreximbank to procure Covid-19 vaccine doses for African nations highlights the bank's growing institutional role in Africa. Fitch has revised its assessment of governance risk to 'medium' from 'high' following a record of operations under governance practices consistent with that of rated peers.

The bank's ratings do not benefit from shareholders' support, which is assessed at 'bb'. This assessment reflects the average quality of key shareholders after a one-notch enhancement for callable capital credit enhancement (70% of USD1.4 billion), and 'strong' propensity to support. The latter primarily reflects ongoing capital injections and the recent approval of a significant increase to the bank's capitalisation.

RATING SENSITIVITIES

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

Business Environment: Further strengthening in the importance of the bank's public mandate, as evidenced by successful delivery of the capital increase by member states and execution of the various initiatives set by the African Union as well as continued growth in banking operations while maintaining strong capitalization metrics. Evidence of successful execution in these areas would potentially lead to a positive revision in our assessment of the bank's business profile and reduction in the current three-notch negative adjustment.

Solvency: Strengthening of the solvency assessment, which could stem from a record of stronger capitalisation metrics and/or strengthening in the bank's credit risk profile as a result of improvement in the credit quality of the loans and guarantees and a decline in the NPLs/Stage 3 loans below 3% of gross loans.

Liquidity: Higher coverage of short-term debt by liquid assets and improvement in the share of 'AA'-'AAA' rated treasury assets (above 40%) over the medium term.

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

Business Environment: Marked delays or lower-than-expected payments under the recently approved capital increase or other factors that negatively affect our assessment of the importance of the bank's public mandate.

Solvency: Weakening in our assessment of solvency as the result of a lower-than-expected capital increase and/or deterioration in asset quality and loan performance, for example stemming from higher-than-anticipated NPLs.

Liquidity: Deterioration in Fitch's assessment of liquidity, which could result from weaker coverage of short-term debt by liquid assets, decline in the share of 'AA'-'AAA' rated treasury assets, or deterioration in access to capital markets and other sources of liquidity.

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.

Key Assumptions

We assume that the global economy develops in line with our Global Economic Outlook, the latest version of which was published on 15 June 2021.

Fitch assumes that the bulk of paid-in capital payments under the USD6.5 billion general capital increase, approved by the bank's board of directors in June 2021, will be disbursed by 2023.

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

Afreximbank has an ESG Relevance Score of '4' for 'Governance Structure'. 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 operations, at the expense of prudent growth objectives. This has a negative impact on the credit profile, and is relevant to the ratings in conjunction with other factors.

Afreximbank 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.

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.

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Rating Actions

ENTITY/DEBT	RATING			RECOVERY	PRIOR
African Export-	LT IDR	BBB-	Affirmed		BBB-

ENTITY/DEBT	RATING			RECOVERY	PRIOR
Import Bank					
	ST IDR	F3	Affirmed		F3
• senior unsecured	LT	BBB-	Affirmed		BBB-

RATINGS KEY	OUTLOOK	WATCH
POSITIVE		
NEGATIVE		
EVOLVING		
STABLE		

Applicable Criteria

Supranationals Rating Criteria (pub.20 May 2021) (including rating assumption sensitivity)

Additional Disclosures

Solicitation Status

Endorsement Status

African Export-Import Bank	UK Issued, EU Endorsed

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