CREDIT OPINION
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Update

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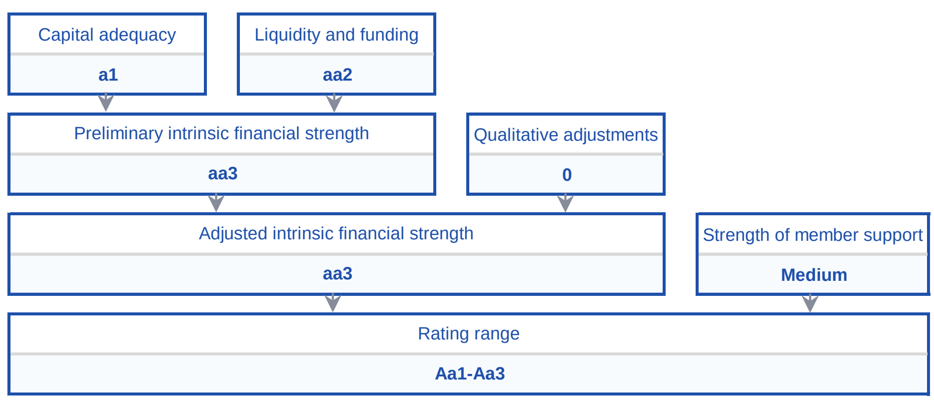
Inter-American Investment Corporation - Aa1 stable

Regular update

Summary

The Inter-American Investment Corporation's (IIC) – commercially rebranded as IDB Invest – credit profile reflects strengths such as robust capitalization and financial management in addition to strong asset performance despite its private sector focus. The institution's close relationship with the Inter-American Development Bank (IADB, Aaa stable) also supports the credit profile. The IIC's conservative risk management practices, which are often even more conservative than the institutional limits set in its charter, keep the IIC's leverage low and capital adequacy ratios very strong.

Exhibit 1
Inter-American Investment Corporation's credit profile is determined by three factors



Source: Moody's Investors Service

Credit strengths

» Strong capitalization and adequate financial management

» Strong asset performance despite the private sector focus

» Close funding relationship with the Inter-American Development Bank

Credit challenges

» Lending without sovereign guarantees to riskier segments of the private sector

» Moderate concentration risks stemming from the portfolio

Rating outlook

The stable outlook reflects our view that the IIC will continue to effectively manage credit risks as it expands its mandate in a challenging operating environment due to the countries in which it carries out its lending and investment activities. The outlook also incorporates the moderate credit quality of the IIC's borrowers, as well as the country, regional and sector concentration risks of the lending and equity-investment portfolios that are present as in other multilateral development banks (MDBs) with similar business profiles.

Factors that could lead to an upgrade

Further upward credit pressures are limited by the challenging operating environment in which the IIC carries out its lending and investment activities, in addition to potential risks stemming from the IIC's private sector focused operations. Although unlikely, the introduction of callable capital as an additional backstop for investors would enhance the IIC's credit profile and could place upward pressure on the credit profile.

Factors that could lead to a downgrade

Downward credit pressures would emerge should there be significant credit losses that materially affect the IIC's financial performance, or a weakening of support from the IADB or highly-rated shareholders.

Key indicators

IIC	2013	2014	2015	2016	2017	2018
Total Assets (USD million)	1,786.8	1,989.5	1,505.3	2,146.7	2,185.4	3,209.3
Development-related Assets (DRA) / Usable Equity [1]	124.2	124.5	115.6	86.7	70.2	96.5
Non-Performing Assets / DRA	0.5	2.1	1.3	1.6	0.9	0.7
Return on Average Assets	1.1	0.7	0.2	1.0	0.8	0.9
Liquid Assets / ST Debt + CMLTD	621.3	180.3	912.9	297.1	5,861.1	290.0
Liquid Assets / Total Assets	42.1	48.4	35.1	59.4	54.6	45.8
Callable Capital / Gross Debt	0.0	0.0	0.0	0.0	0.0	0.0

[1] Usable equity is total shareholder's equity and excludes callable capital

Source: Moody's Investors Service

Detailed credit considerations

The IIC's "a1" **capital adequacy** score reflects its strong capital metrics due to very conservative policies, which balance its exposure to riskier development-related assets (DRA). Strong capitalization is a distinctive characteristic of the IIC's financial profile, which is necessary to mitigate the risks from its portfolio of loans and equity investments. IIC's leverage ratio, which measures the coverage of its DRA provided by its equity, has remained below 100% during the past three years (2016-18). We expect that this ratio will deteriorate over the coming years as the Corporation expands its operations but still remain very strong. The ongoing capital increase will also support these dynamics.

The credit profile of the IIC's loan portfolio reflects risks derived from its development mandate and the regional market segment it serves. The starting point of our analysis is the weighted average borrower rating, which, for the IIC, was Ba3 as of 31 December 2018. We also note that equity investments represent a relatively low share of DRA for the IIC, mitigating potential risks. Additionally, we consider that IIC's DRA display a broad diversification in terms of country and sectors. These elements point to a moderate credit quality of its development assets portfolio.

Importantly, while IIC's operations focus solely on the private sector, asset performance has improved in recent years and remains stronger than other MDBs with similar missions. The ratio of nonperforming assets (NPA) fell to 0.7% of total DRA in 2018, compared to 2.1% for the (International Finance Corporation (IFC, Aaa stable) and 4.5% for the European Bank for Reconstruction and Development (EBRD, Aaa stable).

Our “aa2” assessment for **liquidity and funding** reflects high liquidity levels and strong market access. We assess IIC's liquidity coverage to be strong in case of a stress scenario, which would include the Corporation not being able to tap financial markets and for members to suspend the ongoing capital contributions. IIC's liquid resources ratio, which sizes its high-quality liquid assets relative to its net outflows from uninterrupted net loan disbursements, debt repayment and administrative costs, shows that the Corporation holds enough assets to sustain its functioning for 18 months. That said, we consider that IIC's liquidity is stronger than this ratio indicates because in case of severe stress it could tap its contingent credit line with the IADB (for which we include a positive adjustment), and, also, members have continued to provide their capital contributions on a timely basis (with some prepaying).

A second element related to liquidity is the quality of the MDB's funding. We score the IIC's at strong “aa” level. While the IIC's borrowing program is still relatively small, but will increase over time as its operations expand, we consider that it can access various markets – both global USD and regional markets – and that it has a diverse investor base. This also points to relatively favorable borrowing costs.

Combining capital adequacy and liquidity and funding scores, we position IIC's intrinsic financial profile at “aa3”, among the highest in our rated universe. The qualitative factors that we additionally consider include an MDB's operating environment and the quality of its management. We do not apply an adjustment for the operating environment. While we also do not apply an adjustment for the quality of management, we consider that the IIC has continued to strengthen its risk management practices, particularly in the context of the consolidation of the IADB Group's private sector operations. Nonetheless, these conservative policies and risk management practices are reflected in its strong credit metrics.

We score **strength of member support** as “Medium”. This assessment incorporates a moderate ability to support the entity as reflected by a weighted average shareholder rating (WASR) of Ba1. The absence of callable capital contributes to low assessment of contractual support. However, we consider that the IIC has very high noncontractual willingness to support from members as shown by the interest by non-regional and highly-rated members to increase their shareholding in the Corporation. The expansion of the IIC's mandate indicates continuing support of its development and confirms the IIC's economic importance for members. Therefore, we assign a score “Medium”, above the scorecard-indicated score of “Low”, based on this very strong support shown by members and our expectation, that as highly rated non-regional members increase their shares, the WASR metric will also improve.

ESG considerations

How environmental, social and governance risks inform our credit analysis of IIC

Moody's takes account of the impact of environmental (E), social (S) and governance (G) factors when assessing supranational issuers' credit profile. In the case of the Inter-American Investment Corporation, the materiality of ESG to the credit profile is as follows:

Environmental considerations are not material for IIC's rating. However, we note that as part of its mission, the IIC supports several private sector projects, including renewable energy generation, that look to address or mitigate climate change risks in the Latin American region.

Social considerations are not material for IIC's rating. We do not expect that social risks affecting its borrowers will affect IIC's capital adequacy or liquidity.

Governance is strong and manifests through very strong capital adequacy and liquidity metrics that underpin its Aa1 rating.

All of these considerations are further discussed in the “Detailed credit considerations” section above. Our approach to ESG is explained in our cross-sector methodology General Principles for Assessing ESG Risks. Additional information about our rating approach is provided in our Rating Methodology for Multilateral Development Banks and other Supranational Entities.

Recent developments

IIC continues to increase its capital base, with two new members joining in 2019

The IIC is currently increasing its equity via a general capital increase, a process that was initiated in March 2015. The process is ongoing until 2022, when shareholders will have paid in $1.3 billion to share capital, while the Inter-American Development Bank will have paid in an additional $725 million on behalf of its member countries (ending in 2025). The IADB Governors' approval of the IADB transfers on behalf of its member countries will take into account the IADB's revised capital adequacy policy, ensuring that the Aaa credit rating of the IADB is safeguarded.

Total paid-in capital rose to $1.701 billion in June 2019, up from $1.622 billion in 2018 and $858 million in 2016. During the first six months of 2019, the IIC received $29 million in Annex A shares contributions. Also, the IADB's Board approved and transferred $49.5 million as part of the Annex B shares contribution. Through June 30, 2019, total capital contributions of $995 million have been received under the Second General Capital Increase. Additionally, in April 2019, Croatia (Ba2 positive) and Slovenia (Baa1 positive) became full members of the IIC. The expansion of the Corporation's capital base is in line with its growing operations and supports the IIC's creditworthiness by providing a large equity buffer to protect against losses.

Development related operations rose in H1 2019

Gross loans expanded by 22% to $1.842 billion during the first half of 2019 from $1.513 billion as of end 2018. Total DRA expanded 21% to $2.139 billion. The balance sheet saw a corresponding decline in liquid assets as these were used to deploy resources to finance the new DRA, as well as to repay debt. Borrowings fell to $1.042 billion in June from $1.286 billion at end 2018. We note that despite the strong expansion of the DRA, coverage provided by equity remains very strong.

In terms of asset performance, nonperforming loans past 90 days declined to $11.95 million as of June, representing 0.65% of the loan portfolio, down from $12.83 million (0.85% of total loans) in December 2018. During the first six months of 2019, equity investments posted net gains, while no guarantees provided by the IIC were called (this has been the case since the inception of the guarantees program). This points to an overall improvement of the NPA ratio so far in 2019.

IIC issues in regional markets

In addition to expanding its local currency funding through borrowings, international and local bond issuances in Brazilian Reais, Colombian Pesos, Mexican Pesos and Paraguayan Guaranies, during H1 2019 the IIC further expanded its borrowings in Brazilian Reais and Colombian Pesos. Additionally, the IIC increased the outstanding amount of an existing USD Bond maturing in 2021 by issuing an additional $250 million. The IIC also paid down a $500 million floating-rate USD bond.

Rating methodology and scorecard factors

Rating factor grid - Inter-American Investment Corporation	Initial score	Adjusted score	Assigned score
Factor 1: Capital adequacy (50%)		a1	a1
Capital position (20%)		aaa	
Leverage ratio	aaa		
Trend	0		
Impact of profit and loss on leverage	0		
Development asset credit quality (10%)		ba	
DACQ assessment	ba		
Trend	0		
Asset performance (20%)		a1	
Non-performing assets	a1		
Trend	0		
Excessive development asset growth	0		
Factor 2: Liquidity and funding (50%)		aa2	aa2
Liquid resources (10%)		a1	
Availability of liquid resources	a2		
Trend in coverage outflow	0		
Access to extraordinary liquidity	+1		
Quality of funding (40%)		aa	
Preliminary intrinsic financial strength			aa3
Other adjustments			0
Operating environment	0		
Quality of management	0		
Adjusted intrinsic financial strength			aa3
Factor 3: Strength of member support (+3,+2,+1,0)		Low	Medium
Ability to support - weighted average shareholder rating (50%)		ba1	
Willingness to support (50%)			
Contractual support (25%)	ca	ca	
Strong enforcement mechanism	0		
Payment enhancements	0		
Non-contractual support (25%)		Very High	
Rating range			Aa1-Aa3
Rating			Aa1

Note: While the information used to determine the grid mapping is mainly historical, our ratings incorporate expectations around future metrics and risk developments that may differ from the ones implied by the rating range. Additional considerations that may not be currently captured by the metrics used in the scorecard can be reflected in differences between the adjusted and assigned factor scores. Thus, the rating process is deliberative and not mechanical, meaning that it depends on peer comparisons and should leave room for exceptional risk factors to be taken into account that may result in an assigned rating outside the indicative rating range.
For more information please see our Multilateral Development Banks and Other Supranational Entities rating methodology.

Moody's related publications

- **Credit Analysis**: Inter-American Investment Corporation, 26 March 2019
- **Rating Methodology**: Multilateral Development Banks and Other Supranational Entities, 25 June 2019

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