

Rating Action: Moody's affirms the Inter-American Investment Corporation's Aa1 ratings; maintains stable outlook

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New York, March 20, 2020 -- Moody's Investors Service ("Moody's") has today affirmed the Aa1 issuer and senior unsecured ratings of the Inter-American Investment Corporation (IIC) -- commercially rebranded as IDB Invest -- and maintained the stable outlook. The short-term issuer rating of the IIC was affirmed at Prime-1 (P-1). The senior unsecured MTN program's rating was also affirmed at (P)Aa1.

The key drivers underpinning today's rating affirmation are:

1. IIC's capital adequacy and liquidity metrics compare favorably to its Aa-rated peers and to MDBs with similar focus on private sector operations;
2. Member support has remained strong despite the deterioration in the credit profiles of some key regional members.

The stable outlook reflects Moody's 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 incorporates Moody's expectations that while leverage will increase, the IIC will maintain a strong capital adequacy. This combined with still strong liquidity will continue support the IIC's high intrinsic financial strength, a key feature of its credit profile.

RATINGS RATIONALE

FIRST DRIVER: IIC'S CAPITAL ADEQUACY AND LIQUIDITY METRICS COMPARE FAVORABLY TO ITS Aa-RATED PEERS AND TO MDBS WITH SIMILAR FOCUS ON PRIVATE SECTOR OPERATIONS

The IIC has expanded its balance sheet in the context of the consolidation of the Inter-American Development Bank (IADB) Group's private sector operations at the IIC and the general capital increase (GCI-II) process that began in 2016. Moody's notes that the IIC has effectively managed this transition and that its capital adequacy and liquidity metrics have remained strong relative to Aa-rated peers.

Mainly funded by increased paid-in capital, the IIC has increased its portfolio of development-related assets (DRA) to \$2.5 billion as of end 2019 from \$887 million in 2016. This has led to an increase in the IIC's leverage ratio -- which sizes a multilateral development bank's (MDB) usable equity relative to its DRA and treasury assets rated A3 or lower -- in line with Moody's expectations when the GCI-II process began. The leverage ratio was 125% in 2019, up from 71% in 2017. At this level, the IIC leverage ratio is in line with the Aa1-median (129%) and much lower than the median for Aa-rated peers (208%). We expect the IIC will continue to gradually increase its leverage over the coming years but will continue to have a relatively strong capital position relative its peers.

Another important credit strength of the IIC is its strong asset performance. Given that the IIC's business model focuses on the development of the private sector in the Latin American and Caribbean region it does not benefit from the same preferred creditor treatment that MDBs that lend primarily to the public sector enjoy. However, the IIC's non-performing asset (NPA) ratio -- which takes into account non-performing loans, realized losses on equity investments and called guarantees -- was a low 0.6% in 2019 (0.7% on average in 2017-19). Moody's notes that the IIC has a long track record of strong asset performance, with the non-performing loans ratio averaging 0.9% since 2006. At 0.6%, the IIC's NPA ratio is in line with the Aa-median but it is better than other peers that also focus on the private sector such as the International Finance Corporation (IFC, Aaa stable; 3.3%) and the European Bank for Reconstruction and Development (EBRD, Aaa stable, 4.5%). Even though asset performance will likely deteriorate due to more challenging macroeconomic conditions in the region caused by the coronavirus shock, Moody's expect the NPA ratio to remain at levels unlikely to pressure the IIC's overall credit profile.

In terms of liquidity, this also remains strong as guided by the IIC's conservative liquidity policy. Moody's considers that in a severe stress scenario where the IIC was unable to issue debt or receive any additional

capital contribution from its shareholders, its liquid assets would cover more than 18 months of debt service, planned disbursements and operational costs. The IIC's contingent line with the Inter-American Development Bank (IADB, Aaa stable) also provides an additional support to its liquidity. Moody's expects that the IIC will continue to maintain a robust liquidity buffer as it expands its development portfolio and borrowing program. Moody's also notes that the IIC has demonstrated an ability to fund itself in the markets at favorable rates despite the still relatively small size of its borrowing program compared to other highly-rated MDBs, and enjoys a diversified pool of investors. These factors support the IIC's high quality of funding, a key credit feature it shares with Aa1-rated peers.

SECOND DRIVER: MEMBER SUPPORT HAS REMAINED STRONG DESPITE THE DETERIORATION IN THE CREDIT PROFILES OF SOME KEY REGIONAL MEMBERS

The decision by shareholders to consolidate the IADB Group's private sector operations within the IIC, and the supporting general capital increase denote the high economic importance its members have placed on the Corporation. Usable equity has risen to \$2 billion in 2019 from \$857 million in 2015 before the GCI-II process began. Moody's considers that this continued flow of new equity will allow the IIC to expand its operations over the coming years while also maintaining strong financial metrics.

Moody's also notes that highly-rated non-regional members will increase their share of subscribed capital during the GCI-II process and new members joined the IIC in 2019 -- Slovenia (Baa1 positive) and Croatia (Ba2 positive). Importantly, while regional members Argentina (Caa2 RUR-) and Ecuador (Caa1 stable) have faced financial stress in recent years, they have continued to make timely capital payments to the IIC. These factors support Moody's assessment of "Medium" strength of member support based on shareholders' moderate ability and strong willingness to provide non-contractual support.

RATIONALE FOR THE STABLE OUTLOOK

The stable outlook incorporates our expectation that the IIC's leverage ratio will continue to increase gradually over the coming years but, with the infusion of new capital, the IIC is expected to maintain a high capital adequacy commensurate with the current rating. Similarly, Moody's anticipates that the IIC will continue to comply with its conservative liquidity policy and maintain a strong liquidity buffer, while also further developing its access to market. This will allow the IIC to preserve a high intrinsic financial strength that is a key feature of its credit profile.

ENVIRONMENTAL, SOCIAL, GOVERNANCE CONSIDERATIONS

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.

WHAT COULD CHANGE THE RATINGS UP/DOWN

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.

Downward credit pressures would emerge should there be significant credit losses, for instance stemming from a more acute challenging operating environment, that materially affect the IIC's financial performance, or a weakening of support from the IADB or highly-rated shareholders. A deterioration in sharp capital adequacy driven by an excessive increase in leverage would weigh on the IIC's credit profile.

The principal methodology used in these ratings was Multilateral Development Banks and Other Supranational Entities published in June 2019. Please see the Rating Methodologies page on www.moodys.com for a copy of this methodology.

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