S&P Global Ratings

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Research Update:

IDB Invest Outlook Revised To Positive On Support For Enhanced Mandate And Governance; 'AA+/A-1+' Ratings Affirmed

June 26, 2024

Overview

- In March 2024, IDB Invest's (IDBI) board of governors unanimously approved a capital increase of $3.5 billion to support the new business model aimed at scaling up mobilization.
- This follows the successful execution of its expanded mandate since 2015 to manage all private-sector lending within the Inter-American Development Bank (IADB) Group.
- We are thus revising our outlook on IDBI to positive from stable and affirming our global scale 'AA+/A-1+' ratings, and our 'mxAAA' national scale rating.
- The positive outlook reflects prospects for an upgrade in the next two years if the capital increase includes key shareholders, enhancing IDBI's mandate, while superior risk management practices accompany implementation of the new business plan.

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Rating Action

On June 26, 2024, S&P Global Ratings revised its outlook on IDBI (legal name: Inter-American Investment Corp.) to positive from stable. At the same time, we affirmed our 'AA+/A-1+' issuer credit ratings. We also affirmed the 'mxAAA' national scale rating and the outlook on it remains stable.

Outlook

The positive outlook reflects a one-in-three chance that we could raise our ratings on IDBI in the next two years. We believe that the approved capital increase suggests enhancements to how shareholders view the institution, its value to the global development agenda aimed at expanding the scale and impact of private capital. While it implements its new institutional strategy, we also expect IDBI to strengthen its risk framework and operational structure to manage increased lending volumes, something we believe is essential to reduce the execution risk.

Upside scenario

We could raise the rating if the capital increase is subscribed by key shareholders in the next two years, in essence expanding IDBI's overall role and reach in the private-sector multilateral lending (MLI) sector. This would have to be combined with IDBI's execution in line with targets and superior risk management practices. Under this scenario, we would continue assessing IDBI's financial risk profile as extremely strong.

Downside scenario

We could revise the outlook to stable should there be uneven support for the capital increase during the subscription and payment period, hampering IDBI's business expansion. Downward pressure on the rating could also stem from a marked deterioration in the lender's financial risk profile, for example, should IDBI's nonperforming assets rise markedly.

Rationale

The positive outlook is based on developments in the shareholder relationship that underpin how members view the role of the institution and its greater value in the global development agenda. This includes support through a capital increase approved by all members in March 2024. Shareholders are expected to formally subscribe to the capital increase over the coming year, with the first instalment payment due November 2025, and regular capital instalments payments expected until 2031. While still a comparatively small institution, IDBI has bolstered its relevance within the IADB Group: IDBI currently accounts for half of the group's approvals.

During the 2024 annual meeting, the board of governors unanimously approved a capital increase of $3.5 billion to support IDBI's new business model aimed at scaling up mobilization. The IADB Group's new institutional strategy has three core objectives: reduce poverty and inequality, address climate change, and bolster sustainable regional growth. The capital increase will allow IDBI to increase its mobilization and ability to channel resources to the region to around $19 billion annually in the coming decade from the current level of approximately of $8 billion.

IDBI's new business model will deploy capital to private investment projects via an "originate-to-share" model instead of a "buy-and-hold" model. It will have additional capacity to provide more equity and domestic-currency loans. Through IDBI, IADB Group will have greater investment power to mobilize much needed investment to development goals, and help countries be part of the solution of global challenges, such as promoting the energy transition and climate change resilience, reducing food insecurity, and promoting biodiversity and nature.

IDBI has successfully executed its expanded mandate following a full-scale reorganization in 2015 to manage all private-sector lending within the IADB Group. The mandate broadened IDBI's direct lending to corporate and infrastructure sectors and was accompanied by a $2.03 billion capital increase to support larger lending volumes. Shareholders committed to $1.3 billion over seven years (2016-2022) and $725 million in transfers from IADB on behalf of its shareholders during 2018-2025. IDBI's larger presence in the region has also been central to its expanded mandate.

IDBI has demonstrated its franchise value and has become an important partner in key projects in the region, mobilizing third-party co-invested funds in IDBI projects. Core mobilization reached a record $5.4 billion for 2023 from $3.1 billion in 2022, exceeding the $2.5 billion target. The two largest mobilizations in the last four years were executed in 2023: a loan to Liberty Costa Rica for digital access and broadband quality ($400 million) and a liquidity facility for tariff stabilization in

Chile ($1.1 billion). Record short-term mobilization reached $1.4 billion in 2023 from $869 million in 2022.

We believe IDBI's focus on private-sector mobilization underpins its important role that cannot be readily fulfilled by other private or domestic public lenders. Following the uptick in mobilization in 2023, the planned capital increase is explicitly linked to further scaling up in mobilization, which should be a positive structural development. This comes in the context of global mobilization volumes in low- and middle-income countries that have only grown to $65 billion in 2022 from $60 billion in 2017 (see "Shareholders Are Calling On Multilateral Lending Institutions To Increase Private-Sector Capital Mobilization For Climate And Development" May 28, 2024).

IDBI's development-related investments (at cost) increased by 28% to $8.3 billion in 2023 from $6.5 billion in 2022. During 2023, the majority of the growth came from loans to the financial institutions (FI) sector, while major developmental impact was seen in credit to the water and sanitization sector. From overall investments, 36% is in FIs, followed by the energy sector (20%), manufacturing (10%), agribusiness (10%), transport (8%), digital economy (7%), and water and sanitation (3%).

As a fully specialized private-sector lender, IDBI doesn't benefit from preferred creditor treatment (PCT), which we only apply to sovereign exposures. Consequently, we do not incorporate PCT in our assessment of IDBI's enterprise risk. However, there is a track record of member governments providing preferential treatment by not restricting borrowers' access to foreign exchange for debt service or dividend payments to IDBI.

IDBI has a diverse and balanced composition of government shareholders and well-established governance standards. Its ownership structure consists of 48 government shareholders and no private-sector shareholders. Following IDBI's 2015 restructuring, shareholder concentration has been declining, although the voting power of regional borrowing members represents 54%, which is the minimum established by the Busan Resolution adopted by the board of governors. The U.S. is the largest shareholder (14%), followed by Brazil (13%), Argentina (12%), Mexico (7%), and China (6%) as of the end of 2023. The last capital increase resulted in a redistribution of voting shares. The weight of U.S. shares was diluted in favor of those of other nonborrowing members (China, Canada, South Korea, and Spain).

We think the institution generally has a robust governance system. However, the slightly larger concentration of regional member countries--combined with somewhat lower assessments in governance effectiveness, control of corruption, and regulatory quality--could be a source of agency risk.

We believe the institution has strengthened its risk management framework. To support its significant loan growth, IDBI retooled and upgraded its operational capabilities, risk practices, and systems. In our view, IDBI has been successful in implementing its business plan as defined by its 10-year strategic framework through an increased, reorganized, and decentralized workforce. It also developed and continued to fine-tune its financial risk framework and risk taxonomy, while establishing and meeting lending and development targets. IDBI's president, Mr. Ilan Goldfajn, who took the role in December 2022, is aligned with IDBI's new vision and business model.

IDBI's risk-adjusted capital (RAC) ratio dropped to 30.2% as of December 2023 from 34.1% as of December 2022, given increased exposure especially to corporations and FIs, not entirely counterbalanced by higher equity. In 2023, IDBI posted its eighth consecutive year of profits; the net income jumped by 57% to $164 million in 2023 from $105 million in 2022, contributing to capital and the RAC. Continued growth in outstanding loans, combined with taking on more risk in projects to support mobilization, could decrease the RAC ratio over the next few years, but we expect it to remain above our threshold for the capital adequacy assessment of extremely strong,

because the institution targets an annual sustainable lending level and manages its capital according to its internal financial risk framework.

Asset quality metrics are strong, with lower nonperforming loan (NPL) ratio than those of peers, particularly other private-sector lenders, even though it ticked up in 2023. IDBI's NPLs increased to $145.7 million at the end of 2023 from $30.1 million at the end of 2022. The NPL ratio rose to 1.8% from 0.5% during the period, not driven by any specific sector. The bank has comprehensive risk management oversight.

We think IDBI has a conservative funding profile and is gradually expanding its activity in local and international capital markets. Total borrowing increased to $7.3 billion in 2023 from $5.8 billion in 2022. In 2023, its new borrowings were denominated in eight currencies with final contractual maturities ranging from one to 20 years. In 2023, IDBI issued over $1.2 billion in sustainable bonds, raising the total amount outstanding of this kind of security to $5.1 billion, or 69% of its total outstanding borrowings.

IDBI's liquidity is high. Our calculated 12-month liquidity ratio including loan disbursements was 1.5x as of December 2023, in line with the 2022 level. The six-month ratio was 2.6x as of December 2023. IDBI has maintained higher liquidity than our additional stress test, which considers 50% of all undisbursed loans coming due in the next 12 months. Therefore, we expect the lender to accommodate unplanned disbursements.

Ratings Score Snapshot

Issuer credit rating	AA+/Positive/A-1+
Stand-alone credit profile	aa+
Enterprise risk profile:	Strong
Policy importance	Strong
Governance and management expertise	Adequate
Financial risk profile:	Extremely strong
Capital adequacy	Extremely strong
Funding and liquidity	Very strong
Extraordinary support	N/A
Callable capital:	-
Group support:	-
Holistic approach	-

Related Criteria

- General Criteria: National And Regional Scale Credit Ratings Methodology, June 8, 2023
- Criteria | Governments | General: Multilateral Lending Institutions And Other Supranational Institutions Ratings Methodology, Jan. 31, 2022
- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021
- Criteria | Financial Institutions | General: Risk-Adjusted Capital Framework Methodology, July

20, 2017

- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

Related Research

- Shareholders Are Calling On Multilateral Lending Institutions To Increase Private-Sector Capital Mobilization For Climate And Development, May 28, 2024
- How Would MLIs' Participation In Sovereign Debt Restructurings Affect Our Preferred Creditor Treatment And Ratings?, Nov. 28, 2023
- Supranationals Special Edition 2023, Oct. 12, 2023
- Introduction To Supranationals Special Edition 2023, Oct. 11, 2023
- IDB Invest, June 20, 2023
- A Closer Look At The G-20 Expert Panel Review Of MLIs' Capital Adequacy Frameworks, Oct. 11, 2022

Ratings List

Ratings Affirmed; CreditWatch/Outlook Action

	To	From
IDB Invest		
Issuer Credit Rating		
Foreign Currency	AA+/Positive/A-1+	AA+/Stable/A-1+
Ratings Affirmed		
IDB Invest		
Issuer Credit Rating		
CaVal (Mexico) National Scale	mxAAA/Stable/--	
IDB Invest		
Senior Unsecured	AA+	
Senior Unsecured	mxAAA	
Commercial Paper	A-1+	

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