MOODY'S

Rating_Action: Moody's affirms EBRD's Aaa rating, outlook remains stable

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London, February 03, 2023 -- Moody's Investors Service ("Moody's") has today affirmed the long-term issuer rating and senior unsecured debt rating of the European Bank for Reconstruction and Development (EBRD) at Aaa. Concurrently, the foreign-currency senior unsecured MTN program rating has been affirmed at (P)Aaa and the short-term issuer rating has been affirmed at Prime-1. The outlook remains stable.

The decision to affirm EBRD's Aaa rating reflects the following key factors:

1. EBRD's very strong liquidity position coupled with very robust market access as well as its outstanding risk management framework and practices. EBRD's high capital buffer ensures that its leverage remains at moderate levels compared to Aaa-rated peers, balancing higher asset performance risks given its primary exposures are to the private sector.

2. Very strong support by highly-rated shareholders, as has been evidenced for instance by the substantial funding being provided by key shareholders to enable the EBRD to increase lending to Ukraine (Caa3 negative).

The stable outlook reflects Moody's expectation that the bank will be able to maintain its solid financial metrics and in particular contain any further deterioration of its asset performance. Most of its current exposures to Ukraine, Russia and Belarus (Ca negative) are already either non-performing or on the bank's internal watchlist, and the bank has raised its provisioning levels accordingly, limiting further negative pressure on capital. Importantly, around half of the EBRD's additional €3 billion financial support commitment to Ukraine and neighbouring countries will be covered by grants and guarantees from highly-rated shareholders, thus limiting the EBRD's own exposure and risk of losses.

Moody's also expects that the bank will return to profits after a loss-making year 2022, allowing it to rebuild its capital buffer again in the coming years. As of September 2022 the accumulated loss for the year stood at close to €1.66 billion, mainly reflecting the impact of the Russia/ Ukraine military conflict on its portfolio, via valuation losses on its equity portfolio and impairment charges. However, EBRD's underlying profitability – before impairment charges and equity valuation changes – is solid and much more stable, benefitting from good net interest margins on its lending. Interest income will benefit from higher lending volumes in the coming years, while its treasury income will benefit from rising market interest rates.

Please click on this link https://www.moodys.com/viewresearchdoc.aspx?docid=PBC_ARFTL472831 for the List of Affected Credit Ratings. This list is an integral part of this Press Release and identifies each affected issuer.

RATINGS RATIONALE

RATIONALE FOR AFFIRMING THE Aaa RATING

VERY STRONG FINANCIAL METRICS, INCLUDING VERY STRONG LIQUIDITY METRICS AND RISK MANAGEMENT AS WELL AS MODERATE LEVERAGE

The first driver for affirming the EBRD's Aaa rating is its very strong liquidity position, with unquestioned access to market funding as well as a very substantial cushion of liquid assets, supported by conservative internal requirements. The bank has a long-established presence in international bond markets and issues in a variety of markets and currencies, as well as in diverse formats and at consistently low costs. Its investor base is very diversified across both regions and types of investors, including a large share of buy-and-hold investors and central banks.

EBRD has a large stock of liquid assets, amounting to over €34 billion as of unaudited Q3 2022 financial accounts, a similar level to a year earlier. Treasury assets are predominantly invested in highly-rated securities. Moody's assessment of EBRD's liquidity is also supported by its prudent liquidity policies which compare well to peers. Under its internal guidelines, net liquid assets must cover a minimum of 75% of projected net cash requirements over the next two years. The bank consistently exceeds this threshold by a wide margin, with its 2-year liquidity coverage standing at 178% as of Q3 2022.

The bank's risk management framework and practices are very prudent, which has allowed the institution to successfully navigate periods of acute stress in large countries of operation, such as in Russia in 2014-15 and more recently Turkiye (B3 stable). Similarly the strong quality of management has helped the institution to respond swiftly to shocks, as seen during the pandemic and currently in the Russia-Ukraine military conflict. More specifically, capital and liquidity are managed such that the bank preserves at all times some distance between its actual operational targets and minimum policy requirements

Also, EBRD's leverage is moderate compared to most Aaa-rated peers, effectively mitigating its weaker and more volatile asset performance. Besides its substantial cushion of paid-in capital, the EBRD has accumulated profits and reserves of €14.1 billion up to 2021, providing the bank with a large cushion to absorb losses. Following a record profit of €2.5 billion in 2021, the bank is likely to record a substantial loss for 2022, which would bring its useable equity buffer (paid-in capital and accumulated retained earnings and reserves) back to the – very solid - 2020 level.

At the same time, the EBRD extended record levels of loans in 2022, amounting to around €13 billion last year, versus its more typical €10-11 billion over the previous few years, confirming its strong counter-cyclical role. While leverage – defined as development-related assets and treasury assets rated A3 and lower relative to useable equity – has consequently risen somewhat in 2022, the ratio remains close to its 2020 level of around 210%. Given its higher-risk focus on lending to the private sector and also investing in equity participations, the EBRD maintains a lower leverage ratio than those among its Aaa-rated peers that lend predominantly to sovereigns.

VERY STRONG SHAREHOLDER SUPPORT AS EVIDENCED BY SUBSTANTIAL SHAREHOLDER FUNDING FOR INCREASING UKRAINE EXPOSURE

The second driver for the rating affirmation is the clear evidence of very strong shareholder support for the EBRD. In March 2022, the bank announced a financial support package for Ukraine and neighbouring countries affected by Russia's invasion of Ukraine, amounting to €2 billion for the 2022-23 period. Since then, the bank has increased the size of its commitment to up to €3 billion, with shareholders and donors agreeing to provide approximately €1.4 billion in funding to guarantee around 50% of EBRD's investments. Signed contributions from donors currently stand at over €1.23 billion. Around half of donor funding comes from the European Union (Aaa stable) with the government of the United States (Aaa stable) contributing a further $500 million, while other highly-rated shareholders have provided smaller amounts.

Moody's considers these commitments as a sign of very strong shareholder support for the EBRD and believes that the EBRD's long-established presence in Ukraine and proven private-sector expertise is raising the bank's already high profile among key shareholders. The rating agency expects the bank to be one of the key financiers of Ukraine's reconstruction once hostilities end. Also, shareholders have consistently supported the bank's gradual expansion into new countries and regions. The EBRD's shareholder base is among the higher rated of its peer group, with its weighted average shareholder rating at "a3", and it has one of the highest ratios of non-borrowing members (85.5%). Moody's also believes that if needed shareholders would be willing to provide additional paid-in capital.

RATIONALE FOR STABLE OUTLOOK

The stable outlook reflects Moody's expectation that the EBRD's key credit metrics will remain strong over the coming years. More specifically, it expects that the EBRD will be able to maintain its solid capital adequacy and contain any deterioration of its asset performance.

Credit risks in some of its major countries of operation are high, and the risk of rising non-performing exposures in Ukraine in particular is substantial. That said, the bank has pro-actively raised its loan loss provisions to 1.1x the gross value of impaired loans, limiting further negative pressure on capital. Also, new lending to Ukraine will benefit from donor funding and guarantees, which roughly halves EBRD's own exposure at risk. Also, non-performing exposures in Turkiye (B3 stable), the EBRD's single-largest country of operation, have started to decline over the course of 2022, although they remain elevated at 11.2% of the total loan portfolio.

Moody's also expects that the bank will return to profitability again after a loss-making year 2022, allowing it to rebuild its capital buffer – which remains sizeable – in coming years. Financial results for the third quarter 2022 were already significantly stronger than the first two quarters, with a net profit of €528 million, helped by a recovery in equity valuations and a small release of provisions. EBRD's underlying profitability – before impairment charges and equity valuation changes – is solid, benefitting from good net interest margins on its lending and higher lending volumes. EBRD also benefits from rising market interest rates via interest income on its capital.

ENVIRONMENTAL, SOCIAL AND GOVERNANCE CONSIDERATIONS

The EBRD's credit impact score is positive (CIS-1), reflecting its strong ESG profile with low exposure to environmental risks, a strong social profile which benefits from the EBRD's support for private enterprises in transition economies and a very strong governance profile as exemplified by conservative financial management and high management credibility, further supported by strong shareholder support.

EBRD has a neutral-to-low environmental issuer profile score (E-2). While some of its countries of operation have high exposure to carbon transition and physical climate risk, the EBRD is one of the leaders in 'green' financings to date, with total green economy financing amounting to 50% of total business volumes last year. The EBRD has also achieved its commitment to align its new financings with the Paris Agreement by the end of 2022.

The EBRD's positive social issuer profile score (S-1) reflects strengths in the area of responsible production as well as benefits from demographic & societal trends, supporting private enterprise in transition economies, often acting as anchor investor or lender. Use of public consultation processes contributes to ensure buy-in from key stakeholders. EBRD does not face any issues attracting highly skilled personnel and there are no health & safety considerations that would negatively or positively affect the issuer profile.

The EBRD's positive issuer profile score for governance (G-1) reflects prudent and very strong risk management, including liquidity management. Credibility of management and its track record are very strong, reflected among others in the continuing expansion of the bank's membership and successive endorsement by the board to extend the geographical remit of the bank. It has a very high level of transparency and quality of reporting.

FACTORS THAT COULD LEAD TO AN UPGRADE OR DOWNGRADE OF THE RATINGS

WHAT COULD MOVE THE RATINGS UP

An upgrade of the EBRD's ratings is not possible as its Aaa ratings are at the highest level on Moody's rating scale.

WHAT COULD MOVE THE RATINGS DOWN

Downward pressure on the EBRD's rating would emerge if the bank experienced a significant deterioration in asset quality and losses over several years – possibly in the context of a broadening of the current Russia-Ukraine military conflict -, combined with a lack of shareholder response in the form of additional paid-in capital.

The principal methodology used in these ratings was Multilateral Development Banks and Other Supranational Entities Methodology published in October 2020 and available at https://ratings.moodys.com/api/rmc-documents/69182. Alternatively, please see the Rating Methodologies page on https://ratings.moodys.com for a copy of this methodology.

REGULATORY DISCLOSURES

The List of Affected Credit Ratings announced here are a mix of solicited and unsolicited credit ratings. For additional information, please refer to Moody's Policy for Designating and Assigning Unsolicited Credit Ratings available on its website https://ratings.moodys.com. Additionally, the List of Affected Credit Ratings includes additional disclosures that vary with regard to some of the ratings. Please click on this link https://www.moodys.com/viewresearchdoc.aspx?docid=PBC_ARFTL472831 for the List of Affected Credit Ratings. This list is an integral part of this Press Release and provides, for each of the credit ratings covered, Moody's disclosures on the following items:

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• Issuer Participation

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• Releasing Office

For further specification of Moody's key rating assumptions and sensitivity analysis, see the sections Methodology Assumptions and Sensitivity to Assumptions in the disclosure form. Moody's Rating Symbols and Definitions can be found on https://ratings.moodys.com/rating-definitions.

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