S&P Global Ratings

RatingsDirect®

Research Update:

International Bank for Reconstruction and Development 'AAA/A-1+' Ratings Affirmed On Revised Criteria; Outlook Stable

Primary Credit Analyst:
Lisa M Schineller, PhD, New York (1) 212-438-7352; lisa.schineller@spglobal.com

Secondary Contact:
Alexis Smith-juvelis, New York + 1 (212) 438 0639; alexis.smith-juvelis@spglobal.com

Table Of Contents

Research Update:

International Bank for Reconstruction and Development 'AAA/A-1+' Ratings Affirmed On Revised Criteria; Outlook Stable

Overview

- Following a review of International Bank for Reconstruction and Development (IBRD) under our revised criteria for multilateral lending institutions, we are affirming our 'AAA/A-1+' long- and short-term issuer credit ratings on the bank and removing them from under criteria observation (UCO).
- In addition to passing measures to bolster organic capital generation, last year IBRD's shareholders agreed to a historically high $7.5 billion increase in paid-in capital over the next five years.
- This shareholder support and prudent management benefit IBRD's enterprise risk profile, while the bank's S&P Global Ratings risk-adjusted capital ratio after adjustments of 28% in June 2018 supports its financial risk profile.
- The stable outlook reflects our view that IBRD's credit strengths, notably its extremely strong enterprise risk profile and extremely strong financial risk profile, will remain in place over the next several years.

Rating Action

On Feb. 13, 2019, S&P Global Ratings affirmed its 'AAA/A-1+' long- and short-term issuer credit ratings on International Bank for Reconstruction and Development (IBRD). The outlook remains stable. At the same time, we removed the ratings from under criteria observation (UCO), where we placed them on Dec. 14, 2018, following publication of our revised MLI criteria.

Rationale

We affirmed our ratings on IBRD based on our assessment of its extremely strong enterprise risk profile and extremely strong financial profile. IBRD's financial profile has strengthened following a recalibration of our approach to preferred creditor treatment (PCT), including the bank's favorable history of nonaccruals and its impact on our calculation of the risk-adjusted capital (RAC) ratio. We outline these factors in our revised criteria, "Multilateral Lending Institutions And Other Supranational Institutions Ratings Methodology," published Dec. 14, 2018.

Our improved assessment of IBRD's financial profile reflects our calculation of its RAC ratio of 28% after adjustments for concentration risk and PCT, as well as the bank's funding and liquidity. The RAC incorporates all new parameters as of Feb. 4, 2019, based on financial data as of June 2018. The main adjustment in IBRD's RAC is its single-name exposure to borrowing member countries, partially offset by our expectation for PCT and geographic diversification. In March 2011, IBRD's board of governors approved a 44% increase in both subscribed capital (US$87 billion) and paid-in capital ($5.1 billion). At fiscal year-end 2018, $84.5 billion in additional capital had been subscribed and $5 billion had been paid in, demonstrating robust shareholder support.

We consider IBRD's PCT to be robust, as evidenced by our calculated arrears ratio of 0.3%, reflecting one sovereign, Zimbabwe, that is currently in arrears. IBRD's track record is strong and in line with some of its 'AAA' rated peers. Besides Zimbabwe, it latest arrears surpassing 180 days occurred in 2008, and we expect a stable and low level of nonpayments.

Supporting IBRD's enterprise risk profile is its very strong policy importance and strong governance and management that remains among the highest of supranational institutions globally. IBRD's unrivaled franchise value, countercyclical lending, and the commitment of its shareholders support our expectations that the bank will continue to benefit from PCT. IBRD is the keystone of the World Bank Group, which includes International Development Association (IDA), International Finance Corp. (IFC), Multilateral Investment Guarantee Agency, and International Centre for Settlement of Investment Disputes. IBRD, which commenced operations in 1946, is the world's oldest and largest multilateral lending institution (MLI). As of June 30, 2018 (fiscal year-end 2018), it had 189 member countries, more than twice that of any other rated MLI, except its affiliates, IDA (173 members) and IFC (184 members).

IBRD had $403 billion in total assets at fiscal year-end 2018, reflecting its global reach and underpinning our assessment of its extremely strong enterprise risk profile. In fiscal 2018, IBRD committed $23 billion of new purpose-related exposures, an increase of 2% from 2017. The bank's commitments remain below the recent countercyclical peak in 2010 of $44.2 billion.

IBRD's exposures continue to be diversified globally. The top five exposures are unchanged from the prior fiscal year: Brazil, Indonesia, Mexico, China, and India, and we do not expect any short-term change to the main borrowers. As noted, the bank currently has only one borrowing country in nonaccrual status as of June 2018--Zimbabwe, which has been in nonaccrual since October 2000. The bank is still in discussions with the government of Zimbabwe to clear these arrears (currently $0.4 billion in principal). The country cleared its arrears with the International Monetary Fund in October 2016. Iran is the other country that was in nonaccrual status during the last 10 years (cleared in 2014).

At IBRD's spring meetings in April 2018, the board of governors endorsed a $60.1 billion package, which includes a general capital increase (GCI) and a selective capital increase (SCI) that includes $7.5 billion in additional paid-in capital. Importantly, this capital increase has been accompanied by policies to bolster organic capital generation. This includes updates to the bank's pricing policy and single borrower limit in 2018, on the back of administrative cost-reduction measures, a revised transfer to IDA, and balance sheet optimization with an exposure exchange agreement (with the Inter-American Development Bank and African Development Bank) in recent years.

Comprehensive income was $1.7 billion (3.9% of adjusted common equity) in fiscal 2018 versus $2.5 billion in 2017. Comprehensive income gains reflected net actuarial gains on benefit plans (due to higher asset returns and an increase in interest rates used to discount the pension liabilities) and a positive currency translation adjustment (due to the appreciation of the euro against the U.S. dollar in fiscal 2018). Given cost-reduction targets, lower transfers to IDA, and a new differentiated pricing policy, we expect earnings, excluding market value effects on derivatives and pension plans, to remain solid over the coming years.

During fiscal 2017, IBRD's board of directors approved a formula-based approach for determining IBRD's transfers to IDA. Coupled with the terms for the 18th replenishment of IDA, IBRD's transfers to IDA will be lower over the next three years (beginning fiscal 2018) than they were in the prior three years. Using the formula approach, the board approved a transfer of $248 million for fiscal 2018, which will appear in its fiscal year-end 2019 financial results.

The World Bank Group has committed to deliver cost-saving reforms. IBRD's management achieved important cost savings under its budget anchor policy, as net loan spread revenues fully covered net administrative expenses in fiscal 2018. Net administrative expenses declined by 12% in fiscal 2018 after an increase of 1% in fiscal 2017, mainly because of decreased pension costs.

Our funding ratios for 2018 indicate that IBRD does not have a funding gap below the one-year horizon: IBRD's assets exceed its liabilities at all horizons up to five years, supporting its robust funding. Furthermore, we view IBRD's funding as broadly diversified by both geographic market and type of investor, given its frequent issuance in many markets and currencies. For example, it made its inaugural block chain issue in Australia in 2018, following a Mulan issue, an SDR (special drawing rights)-denominated bond issued in the Chinese local market, in 2016. Investors perceive IBRD as a safe haven and an issuer of benchmark bonds, including green bonds.

IBRD revised its liquidity policy effective June 2017 to cover its projected outflows over the next 12 months, rather than six months. Our calculation of IBRD's liquidity incorporates stressed market conditions and assumes no market access. Under these conditions, we conclude that IBRD's liquid assets are sufficient to service its obligations through the next year without slowing the pace of planned disbursements. According to our calculations, IBRD's liquidity ratio, assuming scheduled disbursements, was 2.1x at the six-month horizon and 1.3x at the one-year horizon as of June 30, 2018. Under this same stress scenario, we estimate IBRD may need to spread out any unforeseen increase in its potential disbursements while meeting other obligations.

Even without accounting for extraordinary shareholder support, we assess IBRD's stand-alone credit profile (SACP) at 'aaa', our highest level. Should IBRD's stand-alone capital adequacy weaken, the issuer credit rating would benefit from uplift. We would expect 'AAA' rated shareholders to answer one or more calls on their subscribed callable capital. Ten 'AAA' rated shareholders subscribed $36.9 billion of callable capital (18% of total gross debt as of fiscal year-end 2018). If IBRD's stand-alone capital ratios were to decline, the effect on its SACP could be counterbalanced by up to two notches of uplift from callable capital in an enhanced financial risk profile, all else being equal. This would reflect the (currently latent) benefit of IBRD's 'AAA' callable capital.

Outlook

The stable outlook reflects our view that IBRD's enterprise risk profile, capital levels including callable capital, funding, and liquidity are sufficiently robust that there is a less than one-in-three probability that we would lower our issuer credit rating on IBRD in the next two years.

That said, if IBRD's enterprise risk profile weakens or the financial risk profile deteriorates, the ratings would come under pressure. This could happen if management--contrary to our expectations--adopts more aggressive financial policies, if IBRD's derivative activities generate significant losses as a result of mismanagement, or if several members cease treating IBRD as a preferred creditor.

Ratings Score Snapshot

Issuer Credit Rating	AAA/Stable/A-1+
SACP	aaa
Enterprise Risk Profile	Extremely strong
Policy importance	Very strong
Governance and management	Strong
Financial Risk Profile	Extremely strong
Capital adequacy	Extremely strong
Funding and liquidity	Strong
Extraordinary Support	0
Callable capital	0
Group support	0

Holistic Approach	0

Related Criteria

- Criteria | Governments | General: Multilateral Lending Institutions And Other Supranational Institutions Ratings Methodology, Dec. 14, 2018
- 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: Use Of CreditWatch And Outlooks, Sept. 14, 2009

Related Research

- Ratings On 32 Multilateral Lending Institutions And Supranationals Placed Under Criteria Observation On Criteria Update, Dec. 14, 2018
- Guidance: Multilateral Lending Institutions And Other Supranational Institutions Ratings Methodology, Dec. 14, 2018
- Supranationals Special Edition, Oct. 11, 2018

Ratings List

Ratings Affirmed

International Bank for Reconstruction and Development	
Issuer Credit Rating	
Foreign Currency	AAA/Stable/A-1+
Senior Unsecured	AAA
Senior Unsecured	AAAp
Short-Term Debt	A-1+

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. Complete ratings information is available to subscribers of RatingsDirect at www.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column.