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Summary: Asian Development Bank

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Primary Credit Analyst: Takahira Ogawa, Singapore (65) 6239-6342; takahira_ogawa@standardandpoors.com

Credit Rating: AAA/Stable/A-1+

Rationale

The issuer credit ratings on Asian Development Bank (AsDB) reflect its solid financial profile, conservative financial policies, and strong shareholder support.

Founded in 1966, AsDB promotes the economic and social development of its members in the Asia-Pacific region through loans, technical assistance, equity investments, grants, and guarantees. As of April 30, 2006, 47 members from the Asia-Pacific region owned 63.5% of the bank, and 18 non-regional members owned 36.5%. The largest shareholders are Japan and the U.S., each with 15.7% of capital (and 12.9% of the voting power). The bank continues to enjoy strong shareholder support from both donor and borrowing members, as indicated by the doubling of its subscribed capital since 1994.

AsDB is the fourth-largest rated multilateral lending institution (MLI), with US$24.0 billion of disbursed loans and equity investments as at Dec. 31, 2005. It has a solid financial profile, and it has consistently posted some of the strongest financial ratios of all MLIs over the past five years. At Dec. 31, 2005, adjusted shareholders' equity and provisions for losses were 49.4% of gross loans, equity investments, and guarantees. Gross debt to adjusted shareholders' equity was 198.4%; liquid assets to gross debt, 50.5%; and operating income to average equity was 0.9%.

Although there is embedded credit risk in AsDB's loan portfolio, the bank had no provisions against public sector risk until 2003, when it first set aside US$240,000. These provisions increased to US$2.3 million in 2005. There is a concentration risk of its loan portfolio to some of the lower rated sovereigns. Lending to Indonesia (whose foreign currency borrowing from commercial lenders is rated 'B+' by Standard & Poor's Ratings Services) represents 36% of AsDB's disbursed loan portfolio and 68% of the bank's equity. Pakistan, whose commercial borrowing is also rated 'B+', represents 8% of the bank's loan portfolio and 15% of its equity. AsDB's historical credit experience, however, has been exemplary, with only two sovereigns—Myanmar (1998-2003) and Nauru (from 2001)—falling into nonaccrual status.

AsDB's statutory gearing policy limits total loan commitments (outstanding loans and undisbursed commitments), equity investments, and guarantees to 100% of subscribed capital, reserves (excluding special reserve), and surplus. To better manage its financial risk, AsDB introduced a risk-based capital policy in February 2004 with a 35% target for the equity-to-loan ratio. This replaced its previous policy of maintaining a reserve-to-disbursed-loan ratio of at least 25%. In addition, AsDB set up a loan loss reserve of US$218.8 million from its net income in 2004 to absorb any expected losses from public sector loan and guarantee portfolios. This reserve fell to US$167 million in 2005, based on the estimated expected loss calculation using AsDB's credit risk model. The bank's current liquidity policy is to maintain its prudential minimum liquidity at 40% of the next three years' net cash requirement (the sum of net disbursement and debt redemption).

Outlook

The outlook is stable. The ratings assume that the bank's major borrowers will continue to treat AsDB as a preferred creditor and that the bank will continue to execute its mission effectively, earning the continued financial support of its shareholders.