

## OPERATIONS MANUAL BANK POLICIES (BP)

*These policies were prepared for use by ADB staff and are not necessarily a complete treatment of the subject.*

### EXPOSURE AND INVESTMENT LIMITATIONS ON NONSOVEREIGN OPERATIONS

#### A. Introduction

1. This section describes the exposure and investment limitations applicable to ADB's nonsovereign operations. The exposure limit framework aims to safeguard ADB's financial strength and is based on three objectives: (i) maintenance of ADB's AAA rating; (ii) a capital adequacy commensurate with that rating, designed to reduce the risk of a call on callable capital; and (iii) an adequate diversification of the portfolio, leading to efficient use of economic capital.

2. The limits applicable to nonsovereign operations are classified into three main groups: (i) limits that are stipulated in ADB's Charter, which ensure that the aggregate outstanding exposure does not exceed the amount of risk-bearing capital; (ii) strategic and medium-term limits adopted by ADB, which determine the maximum exposure for certain operations; and (iii) prudential exposure limits, which ensure a certain level of diversification and cap the maximum amount of correlated loss.

#### B. Definitions

3. Terms used in this OM section are defined as follows:

- (i) B-Loan means a loan made by ADB funded by a third party or parties without the borrower or third parties having any recourse to ADB.
- (ii) Credit Guarantee means a guarantee given in favor of a party providing debt financing in respect of a project or transaction, covering all or a pro rata share of the credit (including political) risks associated with the underlying loan, thus representing a direct credit substitute.
- (iii) Credit Conversion Factor means a multiple used for the purpose of recognizing the exposure effect of off-balance sheet commitments when monitoring limits.
- (iv) Dollar (\$) means US dollar.
- (v) Eligible Counterparty means an entity with a credit rating of not less than A- as assigned by at least one international rating agency on a globally comparable scale or the equivalent of such an A- rating as assigned by a reputable local rating agency domiciled in the same country as the borrower or guarantee beneficiary, including any of the following:

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- (a) official export credit agencies, export–import banks or similar entities that are guaranteed by or carry the full faith and credit of their respective governments,
  - (b) multilateral development banks or bilateral development institutions,
  - (c) public and private risk insurers or reinsurers, as agreed by the ADB Office of Risk Management (ORM) on a case-by-case basis, and
  - (d) public or private commercial corporate entities, as agreed by ORM on a case-by-case basis.
- (vi) Exposure means with regard to any time period:
- (a) for a loan or other debt instrument, the disbursed and outstanding loan balance;
  - (b) for a guarantee, the present value<sup>1</sup> of the guaranteed obligations; and
  - (c) for an equity investment, the market value or fair value<sup>2</sup> of such investment.

With regard to subparagraphs (a) and (b), where relevant to an obligor, industry or country, the Exposure will be reduced by the amount that has been guaranteed by, insured by or otherwise transferred to an Eligible Counterparty under risk participation or a similar arrangement.

Exposure does not include any amounts under B-loans, Guarantees of Record or any other financing instrument under which neither the financing recipient, the beneficiary under the Guarantee of Record, nor a third party has recourse to ADB.

- (vii) Fair Value means the amount for which an asset could be exchanged or a liability settled, between knowledgeable and willing parties in a transaction at arm's length distance.

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<sup>1</sup> To derive the present value for credit and partial risk guarantees, the discount rate must be currency-specific, incorporate the credit spread appropriate for the credit rating of the guaranteed party, and take into account the tenor of the guarantee. This should be equivalent to the interest on the guaranteed loan or bond. The principle behind incorporating the credit spread in the discount rate is to return an exposure value of the guarantee that is identical to the principal value of the guaranteed loan into which ADB will subrogate.

<sup>2</sup> The fair value is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction. Quoted market prices in an active market are the best evidence of fair value and should be used, where they exist (marked-to-market). If a market is not active, fair value should be established making maximum use of market inputs, including recent arm's length market transactions, reference to the current fair value of another instrument that is substantially the same, discounted cash flow analysis, and option pricing models. An acceptable valuation technique incorporates all factors that market participants would consider in setting a price and is consistent with accepted economic methodologies for pricing financial instruments (i.e., marked-to-model). If there is no market available and the range of reasonable fair values is significant and the estimate cannot be made reliably, then the equity instrument should be measured as at cost less impairment (International Accounting Standards, 39).

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- (viii) Financing Recipient means any borrower, investee, or guaranteed obligor under an ADB loan, an ADB equity investment, or an ADB guarantee, respectively.
- (ix) Group means two or more persons, whether natural or legal, to which ADB has exposure, and which are mutually associated in that (a) one of them directly or indirectly holds power or control over the other; or (b) their cumulated exposures represent a single risk to ADB because they are so interconnected<sup>3</sup> that if one of them experiences financial problems, the other or all of them are likely to encounter similar problems.
- (x) Guarantee of Record means a guarantee in ADB's name, under which the guarantee-holder has no recourse to ADB and where the guarantee-holder assumes the credit risk of a participating third-party guarantor or insurer.
- (xi) Guaranteed Obligations means the guaranteed percentage of the outstanding amount of a guaranteed loan or other debt instrument plus the interest thereon.
- (xii) Independent Counterparty means an Eligible Counterparty other than a Related Counterparty, which has issued a guarantee in favor of ADB or otherwise entered into a risk participation or similar risk-sharing agreement.
- (xiii) Nonsovereign Exposure means exposure to Nonsovereign Operations.
- (xiv) Nonsovereign Operations means any loan, guarantee, equity investment, or similar financing arrangement that ADB provides from its ordinary capital resources that is: (a) without a sovereign guarantee or counter-indemnity provided by an ADB member; or (b) with a member's sovereign guarantee or counter-indemnity, under terms that do not allow ADB to accelerate, suspend, or cancel upon default by the sovereign of such guarantee or counter-indemnity, any other loan, or guarantee between ADB and the related sovereign.<sup>4</sup>
- (xv) Partial Risk Guarantee means a guarantee that does not cover all the risks associated with the extension of a loan. It typically covers one or more of the risks of currency inconvertibility or nontransferability, political violence, expropriation and breach of contract, but could also cover other clearly defined risk events which in aggregation are judged not to constitute the full spectrum of credit risks.

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<sup>3</sup> Through common ownership, common directors, cross-guarantees or a direct commercial interdependency which cannot easily be substituted in the short term.

<sup>4</sup> A cross default clause provides that should a borrowing member country default on any of its obligations to ADB under any loan agreement or guarantee agreement with ADB, ADB is entitled to suspend or cancel all other loan and guarantee agreements with that borrower.

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- (xvi) Related Counterparty means an Eligible Counterparty that has issued a guarantee in favor of ADB or otherwise entered into a risk participation or similar risk sharing agreement, and is a member of the Group to which the Financing Recipient belongs.
- (xvii) Sovereign Exposure means exposure to Sovereign Operations.
- (xviii) Sovereign Operations means any loan, guarantee or similar financing arrangement that ADB provides from its ordinary capital resources, excluding Treasury and Nonsovereign Operations.
- (xix) Strategic Limit is the maximum exposure to Nonsovereign Operations that is consistent with ADB's Strategy 2020 and its Capital Adequacy Framework.

### C. Applicable Exposure Limits

4. The limits set out below apply to each transaction proposal and, as applicable, to the entire nonsovereign portfolio at each point in time. Certain limits set out in this OM Section are restatements of either the Charter or the exposure limit policy.<sup>5</sup> Certain other limits set out below, particularly in relation to single obligor exposure, are additional to the Charter and policy requirements. On a case-by-case basis, considering the objectives, structure, and risk-mitigating factors of a proposed transaction, the operations department may seek a waiver from the President in respect of such additional limits.

#### 1. Charter Limits

5. Article 12.1 of the Charter imposes a ceiling on the aggregate<sup>6</sup> amount of outstanding loans, guarantees, and equity investments, which may not exceed ADB's unimpaired subscribed capital, reserves, and the surplus included in its ordinary capital resources (exclusive of certain reserves, as further elaborated in the Charter).

6. Article 12.3 imposes a limit on the total amount of funds invested in equity capital out of the ordinary capital resources of ADB, which may not exceed an amount equal to 10% of the aggregate amount of ADB's unimpaired paid-in capital stock actually paid up at any given time together with the reserves and surplus included in its ordinary capital resources (exclusive of special reserves).

#### 2. Strategic and Medium-term Limits

7. The strategic and medium-term exposure limits aim to ensure that the level of credit risk accepted by ADB is consistent with its risk appetite, its target business volume, and its AAA

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<sup>5</sup> ADB. 2009. *Review of the Asian Development Bank's Exposure Limits on Nonsovereign Operations*. Manila.

<sup>6</sup> Both sovereign and nonsovereign.

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rating objective. They also ensure that the aggregate risk undertaken in nonsovereign operations does not exceed the capital available to support this risk.

8. The strategic and medium-term limits are linked to Strategy 2020, which envisages a rapid growth in nonsovereign operations, and to ADB's long-term capital adequacy framework, under which ADB adheres to a minimum equity-to-loan ratio (ELR) of 26%.<sup>7</sup> The ELR of 26% is consistent with a strategic limit for the nonsovereign operations expressed as a 25% share of the aggregate operations exposure.

9. In order to provide ADB with a cushion against the uncertainty of the quality of the nonsovereign portfolio, nonsovereign operations should grow gradually, in a phased manner. To achieve this objective, the Board has imposed a medium-term limit for nonsovereign exposure (footnote 5). In the period to 2014, disbursed and outstanding balances in the nonsovereign operations may not exceed the amounts in Table 1.

**Table 1: Medium-term Limit for Nonsovereign Exposure**

(\$ million)				
2010	2011	2012	2013	2014
7,700	8,700	9,600	10,100	10,600

10. The medium-term limit is subject to ADB maintaining an adequate risk-bearing capacity, as defined by the capital adequacy framework.<sup>8</sup> When deriving the minimum ELR under the long-term capital adequacy framework, it was assumed that the nonsovereign portfolio would maintain an average credit quality of 7 (Ba2/BB<sup>9</sup>). It was also assumed that the nonsovereign portfolio would be adequately diversified, thus using economic capital efficiently.

11. ADB will be guided by the average credit quality of the nonsovereign portfolio when undertaking new nonsovereign transactions, as well as when managing the nonsovereign debt portfolio. This will not preclude ADB from accepting transactions with a higher risk, but such transactions will need to be balanced either by lower-risk transactions or by keeping a larger amount of equity as a buffer.

### 3. Prudential Limits

#### a. Country Limits

12. Nonsovereign Exposure to a single country is limited to the lower of:

(i) a risk-based allocation as per Table 2; or

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<sup>7</sup> ADB. 2009. *The Asian Development Bank's Long-Term Capital Adequacy Framework*. Manila.

<sup>8</sup> ADB. 2008. *Review of the Asian Development Bank's Capital Adequacy Framework*. Manila; ADB 2009. *The Asian Development Bank's Long-Term Capital Adequacy Framework*. Manila.

<sup>9</sup> As expressed by the international rating agencies.

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**Table 2: Country Allocations for Nonsovereign Operations**

Rating <sup>a</sup>		Limit
Normal Risk	1-8	US\$ 2,100 million
Significant Risk	9-11	US\$ 1,400 million
High Risk	12-13	US\$ 600 million

<sup>a</sup> See Appendix for rating definitions.

- (ii) 10% of GDP,<sup>10</sup> less the amount of Sovereign Exposure. Should 10% of GDP be lower than \$25 million, the limit for Nonsovereign Operations shall be calculated as \$25 million less the Sovereign Exposure.

13. Country exposure excludes exposure to Eligible Counterparties domiciled in any country that is a member of the Organisation for Economic Co-operation and Development (OECD).<sup>11</sup>

### b. Industry Exposure Limits

14. Nonsovereign Exposure to any one listed industry is limited to 30% of the total Nonsovereign Exposure. The list of industries applicable for limits management purposes is maintained by ORM and is subject to periodic updates.

15. Nonsovereign Exposure to the financial sector<sup>12</sup> is further limited as follows:

- (a) in aggregate, to \$3,200 million; and
- (b) per country, to 30% of the applicable country limit.<sup>13</sup>

16. Industry Exposure includes Exposure to Eligible Counterparties, regardless of domicile.

### c. Private Equity Funds - Portfolio Limit

17. Exposure to equity investments in private equity funds is limited, in aggregate, to 5% of ADB's unimpaired paid-in capital plus reserves and surplus, calculated at the time of investment.

### d. Obligor Limits

18. Nonsovereign Exposure to any one obligor or project shall not exceed at any point in time:<sup>14</sup>

<sup>10</sup> Gross domestic product, here defined as the International Monetary Fund's most recently published GDP in current prices in US dollars.

<sup>11</sup> Or other non-developing member countries, as deemed appropriate by ORM.

<sup>12</sup> The financial sector includes all exposures to banks and financial institutions, but excludes investments in equity funds.

<sup>13</sup> This limit is not applicable to trade finance instruments with a maturity of less than 1 year.

<sup>14</sup> ADB shall thus not commit to provide an amount of financing that may lead to a breach of this limit.

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- (i) for loans or Credit Guarantees<sup>15</sup> that are not guaranteed<sup>16</sup> by an Eligible Counterparty: the lesser of \$250 million or an amount equal to:
  - (a) 25% of the total project cost, in the case of a limited recourse project financing;<sup>17</sup>
  - (b) 25% of the total assets, including the amount to be financed,<sup>18</sup> in the case of a corporate loan;<sup>19</sup> or
  - (c) 50% of tangible net worth, in the case of a loan to a bank.<sup>20</sup>
- (ii) for loans or Credit Guarantees that are comprehensively guaranteed by an Eligible Counterparty: the lesser of \$400 million or an amount equal to 70% of (a) the total project cost, in the case of a limited recourse project financing; or (b) the total assets of the borrower, in the case of a corporate loan;
- (iii) for Partial Risk Guarantees: the lesser of \$400 million or an amount equal to 40% of (a) the total project cost, in the case of a limited recourse project financing; or (b) the total assets of the borrower, in the case of another type of financing; and
- (iv) for equity investments:<sup>21</sup> the lesser of \$75 million or an amount equal to:
  - (a) 25% of the net worth of the investee (inclusive of ADB's investment), when investing in a project, financial institution or corporate entity; or
  - (b) 25% of committed amounts, when investing in a private equity fund.

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<sup>15</sup> As regards guarantees, the limit applies to the guaranteed amount, i.e., by applying the guarantee percentage to the guaranteed credit instrument.

<sup>16</sup> In this context, the term "guaranteed" refers also to risk participations and other types of risk-sharing agreements with eligible counterparties.

<sup>17</sup> If total project costs are less than \$50 million the amount to be financed may equal 50% of project costs. For project costs between \$50 million and \$250 million, the percentage allowed is given by the linear function  $y = -0.125x + 56.25$ . In the case of a project expansion, the limit is checked through the ratio  $[(\text{Existing ADB loan} + \text{expansion loan}) / (\text{existing assets of special purpose vehicle} + \text{project cost for expansion})]$

<sup>18</sup> When checking compliance with the limit, only funds that are irrevocably committed from sources external to the borrower may be included. This means that expected future cash flows from the borrower will generally not be part of the denominator. Approval for amounts in excess of 25% of [existing assets + committed funding] may, however, be sought contingent on the inclusion in the loan agreement of a loan disbursement test. In such cases, ADB shall check prior to each disbursement that  $[(\text{ADB outstanding balance} + \text{planned disbursement}) / (\text{borrower total assets} + \text{planned disbursement})] < 25\%$ .

<sup>19</sup> If the sum of total assets and the proposed loan is less than \$50 million, up to 50% of the sum may be financed. For sums between \$50 million and \$250 million, the percentage allowed is given by the linear function  $y = -0.125x + 56.25$ .

<sup>20</sup> A bank is defined as an institution whose business it is to receive deposits and/or close substitutes for deposits including external funding and grant credits or invest in securities on its own account. This limit may be exceeded for very small institutions in poorer countries, subject to credit quality and the presence of adequate safeguards. The acceptable limit for structured finance transactions will be assessed on a case-by-case basis, subject to the limit of \$250 million.

<sup>21</sup> Article 12.4 of ADB's Charter states that ADB shall not seek to obtain by such an investment a controlling interest in the entity or enterprise concerned (except where necessary to safeguard the investment of ADB).

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19. When ADB provides more than one form of financing to an obligor or project, Nonsovereign Exposure to the obligor or project shall not exceed \$400 million, provided however that:

- (i) the aggregate amount of loans, Credit Guarantees and equity investments does not exceed \$250 million and further, that the amount invested as equity does not exceed \$75 million, or
- (ii) the aggregate amount of loans, Credit Guarantees and equity investments further does not exceed:
  - (a) 25% of total project costs, when investing in a project,
  - (b) 25% of total assets, when investing in a corporation, or
  - (c) 35% of tangible net worth, when investing in a bank.

20. To ensure that the amount of economic capital used to support any Exposure is capped at a consistent level:

- (i) The limit of \$250 million referred to in paras. 18 (i) and 19 (i) is applicable only to projects and obligors rated 1–7.<sup>22</sup> Obligors rated 8–11 are subject to more restrictive limits (Table 3). Obligors rated 12 and 13 are generally not eligible for new financing from ADB,<sup>23</sup> and
- (ii) The limit of \$400 million referred to in paras. 18 (iii) and 19 is applicable only to projects and obligors rated 1–11. Obligors rated 12 and 13 are generally not eligible for partial risk guarantees from ADB (footnote 23).

**Table 3: Single Obligor Limits by Rating**  
 (\$ million)

Risk Rating <sup>a</sup>	Loans and Credit Guarantees	Partial Risk Guarantees
1	250	400
2	250	400
3	250	400
4	250	400
5	250	400
6	250	400
7	250	400
8	200	400
9	150	400
10	125	400
11	100	400

<sup>22</sup> In order to ensure fair and equitable access for borrowing member countries to financing from ADB, the creditworthiness of the obligor is measured before application of the country ceiling. For purposes of limit compliance, the creditworthiness of projects selling to a government-owned off-taker may be measured before the application of (i) the rating of the government-owned off-taker and (ii) the country ceiling.

<sup>23</sup> Except when deemed necessary in connection with work-out and restructuring of distressed project.

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12	0	0
13	0	0

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<sup>a</sup> See Appendix for rating definitions

**e. Counterparty Limits**

21. When provided with a Credit Guarantee or similar risk-sharing agreement from an Eligible Counterparty, ADB will recognize the guaranteed exposure as belonging to the Eligible Counterparty ("a transfer of risk"). Subject to compliance with (i) country exposure limits, (ii) industry exposure limits, (iii) group exposure limits, and (iv) the limits set out in paragraphs 22 and 23 below, such arrangements will increase the amount that can be proposed to the Board for approval in relation to a single obligor or project. Given a comprehensive Credit Guarantee or similar risk-sharing arrangement with an eligible counterparty, the maximum exposure that may be proposed in relation to a single obligor or project will be the lesser of \$400 million or an amount equal to 70% of (i) the total project cost in the case of a limited recourse project financing, and (ii) the total assets of the borrower in the case of another type of financing.

22. Unless otherwise limited by country, industry or Group exposure limits, the aggregate exposure to any one related counterparty is limited, at any point in time, to \$600 million.

23. The aggregate exposure limit to any one Independent Counterparty will be determined on a case-by-case basis by the Investment Committee,<sup>24</sup> subject to prevailing medium-term, country, industry, and Group limits.

**f. Group Limit**

24. Nonsovereign Exposure to a Group is limited:

- (i) for loans, credit guarantees and equity:
  - (a) in general, to \$400 million;
  - (b) with adequate assurances from a Related Counterparty, to \$600 million provided further that the amount of aggregate equity investments (valued by reference to initial investment cost) do not exceed \$125 million.
- (ii) for Partial Risk Guarantees: if the Group is active in more than one country, the Investment Committee may determine the acceptable aggregate exposure on a case-by-case basis, provided a limit of \$600 million per country is adhered to at each point in time.

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<sup>24</sup> OM Section D10 (Nonsovereign Operations).

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### **D. Exposure monitoring and management**

25. Exposure limits are set on the basis of disbursed and outstanding amounts to ensure that losses will not exceed what ADB's capital can sustain. Although losses can only occur on amounts that have actually been disbursed, it is necessary to recognize that all of ADB's commitments may have an effect on future exposure. To ensure that nonsovereign exposure will comply with the limits imposed by policy at all times, ORM monitors and projects the development of nonsovereign exposure as described below.

#### **1. Commitments to lend**

26. Loans are monitored using the actual and projected disbursement and repayment patterns.

#### **2. Other Commitments: Credit Conversion Factors**

27. Off-balance sheet commitments other than commitments to lend will be converted to credit exposure equivalents as follows:

- (i) the amount of a credit or partial risk guarantee corresponding to the undisbursed portion of the underlying loan will be monitored using a Credit Conversion Factor (CCF) of 100%;
- (ii) commitments to direct equity investments that have not yet been paid in will be monitored using a CCF of 100%;
- (iii) commitments to invest in equity funds that have not yet been paid in by ADB will be monitored using a CCF of 90%;
- (iv) other commitments (such as unfunded risk participation agreements or stand-by credit facilities), with an original maturity of more than 1 year will receive a CCF of 50%;
- (v) other commitments (such as unfunded risk participation agreements or stand-by credit facilities), with an original maturity of less than 1 year will receive a CCF of 20%; and
- (vi) commitments that are unconditionally cancellable by ADB at any point in time without prior notice will receive a 0% CCF.

28. The CCF for commitments limited by forms of conditionality not covered by subparas (iv)–(vi) above will be set by the Investment Committee between 0% and 50% on a case-by-case basis.

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29. Although B-loans, Guarantees of Record, and other similar arrangements do not constitute credit exposure, ORM will monitor disbursed and outstanding amounts under such arrangements in order to measure ADB's risk of Loss Given Default. These amounts will be broken down by country.

### **3. Counterparty Exposure**

30. To reduce net exposure to countries, industries and single obligors, the risks that ADB assumes by issuing guarantees or providing loans can be reduced through guarantees, reinsurance, or other unfunded risk participations. The amount of risk transferred by ADB to eligible third parties is monitored and subject to the limitations set out in paras. 21-23.

### **4. Passive Breaches and Remedies**

31. Subsequent to the decision to invest, "passive breaches" may occur, i.e., limit breaches caused by factors outside the control of ADB and the obligor. For example, such breaches may occur because of a rise in the value of equity investments or because of currency fluctuations. With regard to the country limit, breaches may occur also because of increased sovereign lending or because of a country's deteriorating creditworthiness.

32. In the case of a limit breach due to deterioration of the creditworthiness of a country, ADB shall take reasonable efforts to reduce its exposure so it conforms with the limit framework provided herein. Within 18 months from the date of the limit breach and subject to legal or contractual restrictions, ADB may take steps that include stopping the processing of new nonsovereign transactions, selling or initiating risk-sharing of existing transactions, or purchasing insurance for the amount in breach.

### **5. Management of Equity Investments**

33. Exposure to equity investments held by ADB will be recalculated from time to time by reference to market value (if a market quotation is available) or the fair value of such an investment. If, as a result of such an adjustment, ADB's exposure to a single equity investment exceeds \$250 million, or \$400 million in respect of aggregate equity investments in a group, ADB will use reasonable efforts (subject to legal or contractual restrictions) to reduce such equity exposures to conform with these limits within 12 months from the date the limit was breached.

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- Basis:** This OM section is based on  
  
ADB. 2009. Doc. R168-09 and Corrigendum 1, *Review of the Asian Development Bank's Exposure Limits on Nonsovereign Operations*. Manila.
- Compliance:** This OM section is subject to compliance review.
- For inquiries:** Questions may be directed to the Head, Office of Risk Management.

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Rating	Rating Definitions: Nonsovereign Operations
1	This is the lowest expectation of credit risk in ADB's nonsovereign operations. The repayment of a facility rated 1 is highly unlikely to be adversely affected by foreseeable events.
2	Very low credit risk. The borrower's capacity to meet its financial commitments in a timely manner is considered very strong. The repayment of a facility rated 2 is unlikely to be adversely affected by foreseeable events.
3	Low credit risk. The borrower's capacity for payment of financial commitments in a timely manner is considered strong. This capacity may however be vulnerable to changes in circumstances or in economic conditions.
4	Low credit risk. The borrower's capacity for payment of financial commitments is considered strong; however adverse changes in business and economic conditions may weaken this capacity over time.
5	Low to medium credit risk. The borrower has a good debt service capacity; however, adverse changes in business and economic conditions may weaken this capacity over time.
6	Medium credit risk. The borrower has a good debt service capacity. There is a possibility of credit risk developing, particularly as the result of adverse economic change over time; however, business or financial alternatives may be available to allow financial commitments to be met.
7	Medium credit risk. The borrower has adequate debt service capacity. There is a possibility of credit risk developing, particularly as a result of adverse economic change over time; however, business or financial alternatives may be available to allow financial commitments to be met.
8	Medium credit risk. The borrower has adequate debt service capacity. There is a possibility of credit risk developing, particularly as a result of adverse business or economic change.
9	Significant credit risk. The borrower has adequate debt service capacity; however, adverse changes in business or economic circumstances would probably impair the borrower's capacity to meet its financial commitments in a timely manner. Alternatively, there is a distinct possibility of a country or external event that could hinder repayment of the facility.
10	Significant credit risk. The borrower has weak debt service capacity. Adverse changes in business or economic circumstances would probably impair the borrower's capacity to meet his financial commitments in a timely manner. Alternatively, there is a distinct possibility of a country or external event that could hinder repayment of the facility.
11	Significant credit risk. The borrower has a very weak debt service capacity. The borrower appears able to meet its financial obligations during the next 12 months, but adverse changes in business or economic circumstances would impair its capacity to meet its financial commitments in a timely manner. Alternatively, there is a distinct possibility of a country or external event that could hinder repayment of the facility.
12	High credit risk. The borrower is dependent upon favorable business or economic conditions to meet its financial commitments. There is a high likelihood, within the next 12 months, of the borrower becoming unable to meet its debt service obligations, or of a country or external event that would hinder the timely repayment of the facility.
13	Very high credit risk. It appears unlikely that the borrower will be able to repay the facility in accordance with the contract. The borrower's capacity for meeting its financial commitments is solely reliant on sustained favorable business or economic conditions. The borrower may be in technical default or may have defaulted to some commercial lenders.
D	The borrower has defaulted and the facility is placed in non-accrual status



**OPERATIONS MANUAL  
OPERATIONAL PROCEDURES (OP)**

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*These procedures were prepared for use by ADB staff and are not necessarily a complete treatment of the subject.*

**INVESTMENT LIMITATIONS ON NONSOVEREIGN OPERATIONS**

This OM Section does not contain operational procedures.