

## Council of Europe Development Bank

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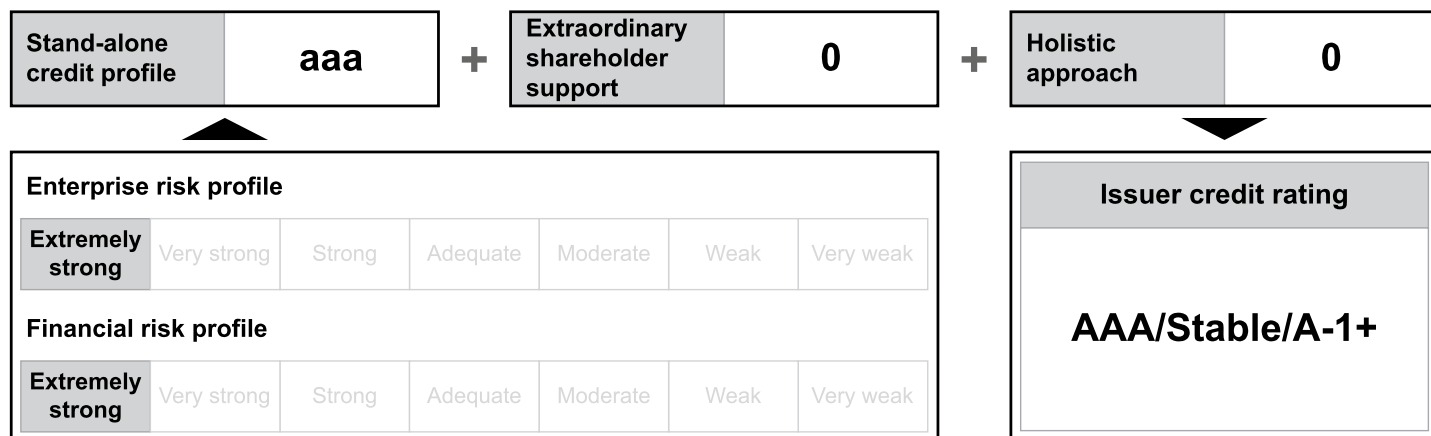
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# Council of Europe Development Bank

This report does not constitute a rating action.



## Credit Highlights

Issuer Credit Rating
<i>Foreign Currency</i>
AAA/Stable/A-1+

Overview	
Key strengths	Key risks
Timely and solid response to the COVID-19 pandemic and Ukrainian conflict underline relevance as a funding agency.	Strong capital and ample liquidity enable sustained lending growth, nimbleness, and high reactivity to disruptive events.
Structurally improving disbursement levels and growing funding needs following the outbreak of the Ukrainian war.	An excellent loan-loss track record and asset quality support capital ratios.
Impeccable track record of preferred creditor treatment (PCT).	Well-diversified funding, boosted by modernized derivatives management that broadens investor and counterparty depth.
Experienced and conservative management.	Strong liquidity, with sufficient buffers to allow acceleration of committed disbursements.

***Ukraine's admittance and lending support provided amid war time is set to bolster the bank's relevance.*** Following Council of Europe Development Bank's (CEB's) rapid and important ramp-up in COVID-19-related lending, the institution's policy relevance was further illustrated by the disbursement of large financial packages to provide assistance to refugees fleeing the ongoing conflict in Ukraine, and CEB's granting membership to Ukraine on July 8, 2022.

***The bank's financial profile will remain solid, although capital injections would support the bank's willingness to raise disbursement levels in response to the Ukrainian conflict.*** CEB entered 2021 from a position of financial strength, with an extremely strong stand-alone capital position, and very strong liquidity and funding, despite its swift response to the

COVID pandemic in 2020. In addition, we expect an excellent asset quality track record and low cost of risk will continue to support CEB's capitalization. We believe this will provide sufficient buffers for the bank to provide funding to countries most impacted by the Ukraine-Russia conflict. That said, once Ukraine has become a member state of CEB and has thus become eligible for its funding, a capital increase would allow unabated lending expansion in connection with the Ukraine-Russia conflict and clarify shareholders' intent.

***CEB's history of demonstrated PCT also underlines the bank's overall enterprise risk profile.*** Specifically, CEB has benefited since its creation from an excellent track record of PCT by the countries in which it operates, as the bank has experienced only one sovereign default for which the principal amount was fully recovered (including arrears). We expect this will continue.

## Outlook

The stable outlook reflects our expectation that over the next two years, CEB will maintain an extremely strong financial profile, despite greater disbursement levels prompted by the coronavirus pandemic, the conflict in Ukraine, and a strong lending dynamic. We do not expect the bank's policy relevance and funding importance will diminish, with ongoing solid shareholder engagement with its activities. We also assume CEB will continue to enjoy excellent PCT.

### Downside scenario

We could downgrade CEB if its policy relevance for shareholders significantly deteriorated; as evidenced, for example, through significant decline in lending activity and a lack of shareholder engagement and support for the bank's activities, notably linked to the Ukrainian conflict. If the bank's excellent track record of PCT eroded, momentum for a downgrade could build.

A significant deterioration in CEB's funding and liquidity assessment could also have a negative impact on the rating, while a deteriorating capital ratio would most likely be mitigated by the existing callable capital from highly rated sovereigns.

## Environmental, Social, And Governance

In our view, CEB's strong social focus and execution, and strong support from the bank's broad, 42-country shareholder base, more than offsets its relatively small size. Since 2017, the bank has significantly accelerated delivery on CEB's exclusively social mandate, which we see as one of the strongest among multilateral lending institutions (MLIs). Recent social emergencies in Europe, notably the need to help refugees, have complemented the bank's more traditional goal of supporting housing, health care, and education, and focusing on less wealthy countries. Specifically, the COVID-19 pandemic further accentuated CEB's policy role, as it stepped in to urgently finance COVID-19 vaccines, medical supplies, and equipment, and offered support with the implementation of COVID-19 vaccination strategy. Additionally, the bank swiftly responded to the outbreak of the Ukraine-Russia conflict, first with grants for migrant care in neighboring member states, and then by July 2022 with €1.3 billion in fast-track emergency loans for the same purpose.

Like other MLIs, CEB has a strong environmental focus that supports its policy role. It endeavors to control its own greenhouse gas emissions per employee, despite its increasing activity. Climate action financing (mitigation and adaptation) represents about 13% of projects approved in 2021, in line with 2020. The bank will likely increase its focus on environmental issues because it is implementing a Paris Alignment approach to identify a higher number of projects with an environmental focus.

CEB's governance supports the rating, as highlighted in our assessment of the bank's governance and management as strong. We incorporate the strong shareholder support for its social mandate execution in our assessment.

## Enterprise Risk Profile

### **Policy importance: the Ukraine-Russia conflict could bolster the bank's policy relevance**

We believe the bank holds a key position because of its established history, role, and the core essence of its mandate. CEB was founded in 1956 as the Council of Europe Resettlement Fund for National Refugees and Over-Population in Europe, with a mandate to help refugees and other displaced persons after World War II. Its current role of supporting social infrastructure investment in Europe involves loans to support job creation in micro, small, and midsize enterprises, vocational training, social housing, health care, environmental projects, prisons, natural catastrophe relief, and educational reform.

With a broadening mandate and increasingly tangible role as a social investor in member countries' budgets, the bank has scaled up its operations over the past five years. Since 2017, we have observed a meaningful upward trend in CEB's disbursements and project approvals. This trend significantly gained traction in 2020 due to the bank's responsiveness in helping member countries address the COVID-19 pandemic, bringing disbursements and project approvals well above targets set by the bank's development plan. As part of its response to the pandemic outbreak, CEB approved €3.8 billion of COVID-19-related projects over 2020-2021, and instituted a fast-track procedure to process COVID-19-related loan requests promptly. As a result, loan disbursements totaled €4.5 billion and €4.0 billion in 2020 and 2021, while the loan portfolio grew by 22% in just two years, to €18.9 billion as of year-end 2021 from €15.5 billion as of year-end 2019. This significant extension of commitments stands out in the MLI community, where most institutions are limiting their pandemic response to already-agreed-to pre-COVID-19 volumes.

CEB's lending trajectory will be linked to its role in the Ukraine-Russia conflict. The 2023-2027 strategic plan to be finalized in December 2022 should reflect the bank's more dynamic approach leveraging on increased demand for social investments throughout Europe and new partnerships forged through the pandemic with other international organizations. For instance, CEB has been designated as an implementing partner of the InvestEU Program 2021-2027, which will contribute to support the investment in the EU and the development of CEB's partnership with European institutions. That said the ongoing conflict in Ukraine should significantly impact the trajectory of CEB's lending. In June 2022, the bank swiftly responded to the conflict through the approval of almost €1 billion in fast-track emergency loans to support member states dealing with significant refugee inflows from Ukraine and approved an additional €345 million in July. This reflects the high reactivity of the bank and its nimble operating structure.

Once the process of Ukraine's admission to CEB, which is currently ongoing, has been completed, this will open the door for submitting projects to be financed directly in the country. While current war-related projects solely targeted

surrounding and already-CEB-member countries, Ukraine's membership will enable the bank to finance projects directly in Ukraine. We expect the size of operations should remain limited in 2022 as CEB already grew its lending portfolio aggressively over the past two years. That said, we understand that in the context of the forthcoming strategic framework, a potential capital increase is under consideration to enable potentially significant financial support to Ukraine coupled with sustained high lending. In our view, this would demonstrate CEB's enhanced role as war hits the European continent.

CEB also leads a number of projects and funds as part of its fiduciary activity. The Migrant and Refugee Fund, the Regional Housing Program, and the Facility For Refugees in Turkey are the main programs in which CEB is involved, and are a priority to its mandate. In 2021, the bank launched two new funds, Housing and Empowerment of Roma (HERO), aiming at reducing socioeconomic exclusion of the Roma people in Bulgaria, Romania, and Slovakia, along with the Partnerships and Financing for Migrant Inclusion (PAFMI) to support the inclusion of migrants and refugees. Meanwhile, 22 projects benefitted from nonlending services, for example grants and technical assistance, in 2021 and €97 million in grants was attributed.

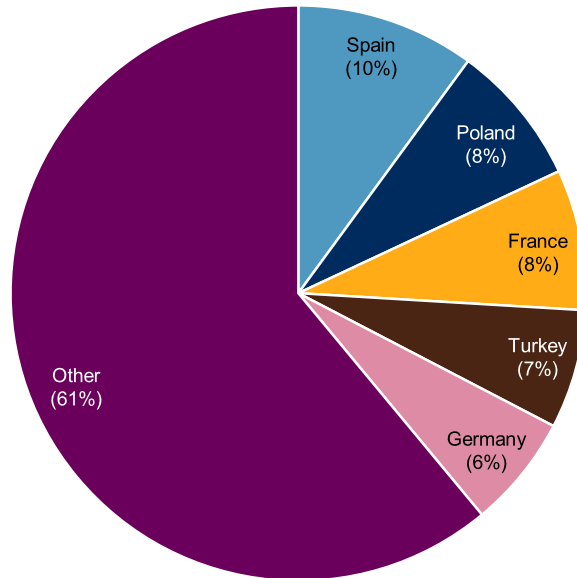
CEB's uniqueness is also rooted in the role it performs for small member countries. For example, in some small member countries, alternative financing solutions for social projects are scarce. A significant portion of CEB's lending focuses on projects in target countries where the associated project costs, loan sizes, and business expertise deter many other institutions (both commercial and government owned). The bank's average loan size is significantly smaller than that of highly rated peers with large project-finance portfolios. Moreover, CEB offers expertise in several social domains (such as housing and education), technical design support, and technical assistance through the project cycle. CEB's recent lending expansion occurred partially through relaxation of a rule favoring traditional target countries, although those received about 46% of total loans disbursed in 2021.

Finally, CEB's history of demonstrated PCT underlines its overall enterprise risk profile. Since its creation, the bank has benefited from an excellent track record of PCT, and we expect this will continue. Despite CEB's concentrated loan portfolio, loan losses have been minimal. The bank has experienced only one sovereign default, that of a debt owed by former Yugoslavia. The principal amount was fully recovered (including arrears) as of July 2004, representing no net present value loss to CEB. We consider this to be confirmation of the PCT afforded to the bank.

**Chart 1**

**CEB's Five Largest Countries Purpose-Related Exposures**

As a percentage of gross purpose-related assets plus guarantees



Source: S&P Global Ratings.

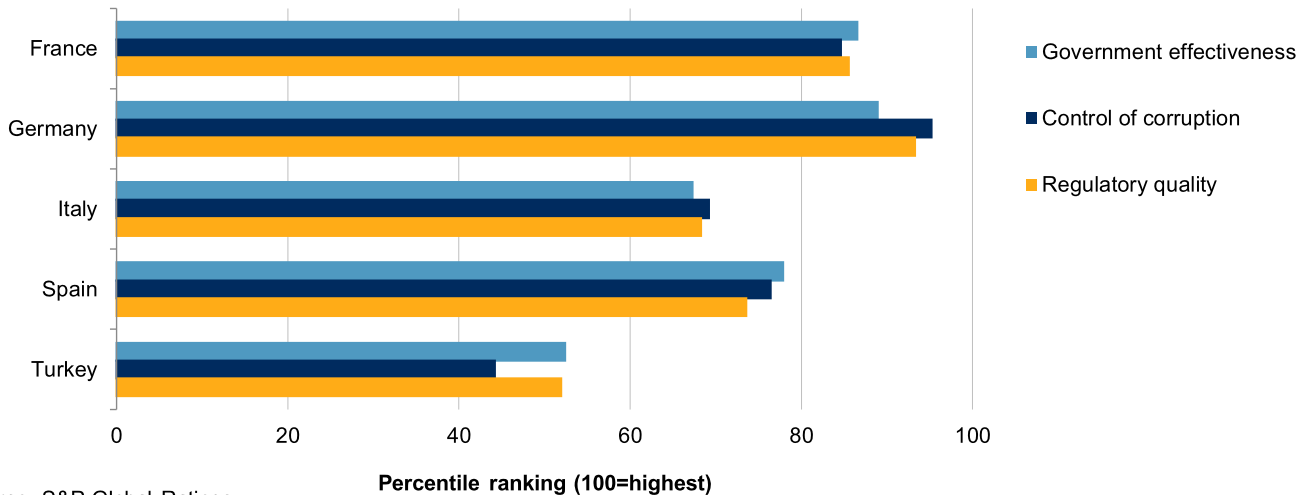
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**Governance and management expertise: Experienced management team**

In our opinion, CEB benefits from strong governance and risk management standards. Shareholders remain supportive and acknowledge the bank's importance as a key contributor in its niche financing segment. Member countries are directly involved in defining CEB's policy. While all shareholders are eligible to borrow from the bank, we believe agency risk is mitigated by the high standards on transparency, rule of law, and governance that are observable in many of its shareholders, including the largest sovereigns.

Operationally, we think CEB has conservative risk and liquidity management policies. The bank maintains up-to-date financial policies, introducing more advanced, dynamic liquidity management and stress tests. This has proven valuable as the bank transitioned to two-way credit support annexes (CSAs) on most of its derivatives counterparty portfolio in 2018 and 2019.

We view the bank's policy of not paying dividends as a sign of ongoing shareholder support. Nevertheless, we also understand CEB's increased activity and potential deployment of projects in Ukraine might be supported by a capital increase from shareholders. In recent years, windfall capital improvements from the stronger credit quality of exposures and high scheduled repayments have reduced the need such financial support.

**Chart 2****CEB's Five Largest Shareholders**  
Selected world bank governance indicators**Financial Risk Profile****Capital adequacy: Upcoming war-related lending could pressure the resilient capital adequacy but which is still digesting the pick-up in pandemic-related lending**

The bank entered 2021 from a position of financial strength, with an extremely strong stand-alone capital position. In our view, this will provide sufficient buffers for the bank to absorb the pressures resulting from its short-term ramp-up in lending. We compute its risk-adjusted capital (RAC) ratio at 24.7% as of end-2021 after adjustments for concentration risk and PCT. While heightened disbursement levels consumed capital, they also benefited our RAC ratio after adjusting for diluted concentration risks. In spite of a 12% increase in risk-weighted assets in 2021, the risk-weighted assets after diversification adjustments grew by only 7%, reflecting higher granularity.

Of note, the asset quality of the bank remained strong, despite the pandemic and large exposures to low-rated countries like Turkey. We expect the bank's asset quality to remain strong, with no credit events and excellent PCT recognition. These expectations underpin our assessment of a resilient RAC position. Although not our base-case, a large lending package to Ukraine with no additional capital support from shareholders could play negatively on the bank's asset quality and capitalization. We understand the bank is keen to preserve its strong financial profile and will mitigate additional financial risks coming from Ukraine, adopting a cautious stance.

Given the expected lending growth, CEB's earnings will fall short of supporting strong capital ratios in the long term in the absence of any capital support. In 2021, net profit stood at €94.8 million. We expect sustained lending to support core earnings and partly offset the run-off of the bank's long-term fixed-interest portfolio. We expect earnings to

stabilize around €70 million-€80 million over the next two years.

Finally, we do not see any currency mismatch, because CEB is hedging its foreign currency balance sheet exposure, or interest rate risks.

**Table 1**

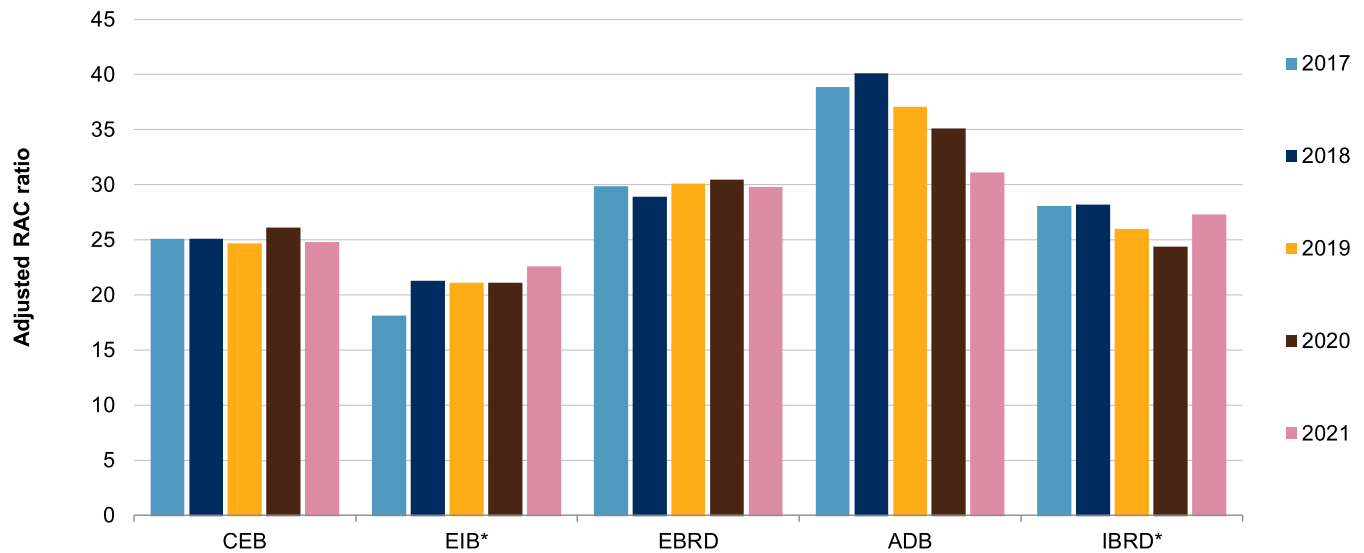
<b>Council of Europe Development Bank--Risk-Adjusted Capital Framework Data: End-December 2021</b>			
<b>(Mil. €)</b>	<b>Exposure</b>	<b>S&amp;P Global Ratings RWA</b>	<b>Average S&amp;P Global Ratings RW (%)</b>
<b>Credit risk</b>			
Government and central banks	24,671.5	7,111.8	28.8
Institutions	8,308.7	2,084.2	25.1
Corporate	987.6	866.0	87.7
Total credit risk	33,967.7	10,062.0	29.6
Total operational risk		293.5	
RWA before MLI Adjustments		10,355.5	100.0
<b>MLI adjustments</b>			
Single name (on corporate exposures)		979.7	113.1
Sector (on corporate portfolio)		110.7	6.0
Geographic		(966.9)	(8.7)
Preferred creditor treatment (on sovereign exposures)		(4,288.4)	(60.3)
Preferential treatment (on FI and corporate exposures)		(75.2)	(2.6)
Single name (on sovereign exposures)		6,754.4	95.0
Total MLI adjustments		2,514.3	24.3
RWA after MLI adjustments		12,869.9	124.3
		<b>Total adjusted capital</b>	<b>S&amp;P Global Ratings RAC Ratio (%)</b>
Capital ratio before adjustments		3,180.4	30.7
Capital ratio after adjustments		3,180.4	24.7

MLI--Multilateral lending institutions. RW--Risk weight. RWA--Risk-weighted assets. RAC--Risk-adjusted capital.



Chart 3

## Risk-Adjusted Capital Ratio Peer Comparison



\*Data as of June 30, 2021, for EIB (European Investment Bank) and IBRD (International Bank for Reconstruction and Development). June is the year end for IBRD. EBRD--European Bank for Reconstruction and Development. ADB--Asian Development Bank. RAC--Risk-adjusted capital. Source: S&P Global Ratings. Copyright © 2022 by Standard & Poor's Financial Services LLC. All rights reserved.

### Funding and liquidity: Funding depth has improved from active funding strategy

**Funding:** We see a positive impact on the bank's funding profile from its more active funding strategy after the switch to two-way CSAs on most derivative counterparties in 2018. Because of the modernized derivatives management, additional funding markets have opened for CEB, improving the investors' pool diversification and the funding conditions for the bank. Since 2019, the bank became more active in several currencies outside the traditional U.S. dollar and euro, such as British pound sterling, Hong Kong dollar, Norwegian krone, Australian dollar, and Swedish krona. In 2021, it issued for the first time in Canadian dollar under its shelf registration with the U.S. SEC.

Over 2021, CEB's €5.5 billion annual borrowing authorization was fully used. CEB's issuances benefited from very strong demand with spreads in line with other well-established MLIs. CEB has furthered its already-comprehensive access to the funding markets with its eligibility for the European Central Bank's public sector purchase program as an additional credit-supportive element.

In line with its social mandate, CEB has established a strong track record and expertise as a social-bond issuer, attracting a strong interest from investors. To that end, in 2021, the bank has continued to issue in the social bond market with two new Social Inclusion Bond benchmarks for €500 million and US\$500 million, raising the outstanding volume of CEB's Social Inclusion Bonds to almost €4 billion equivalent since the program's establishment in 2017.

As of June 30, 2022, the bank had already completed 82% of its required full-year funding, for which the annual borrowing authorization is set at €6.5 billion. This includes two new social inclusion bonds of €1 billion in April and

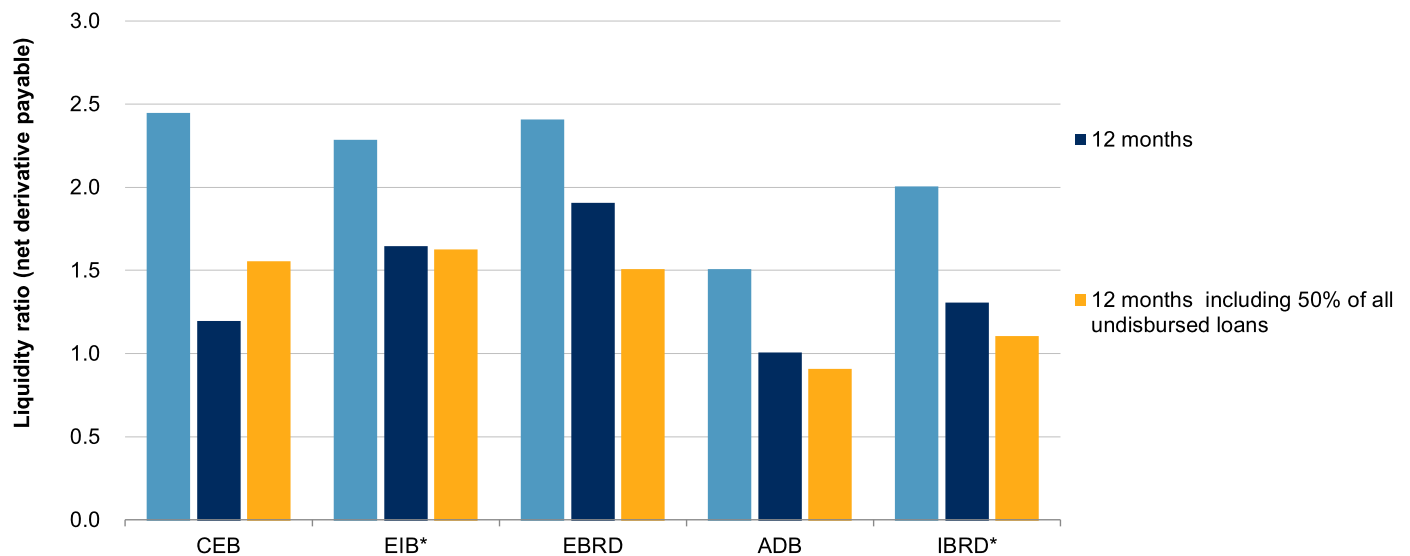
US\$1 billion in June. In our view, this will somewhat shield the bank from current rising rates. Our funding ratios indicate that CEB is structurally able to cover its scheduled short-term debt repayments without recourse to new issuance.

**Liquidity:** Under our liquidity stress scenario, at all horizons up to one year, CEB would fully cover its balance-sheet liabilities without market access. This includes the additional need for liquidity to cover needs of posting collateral under its two-way CSA arrangements. Using year-end 2021 data, our 12-month liquidity ratio was 1.19x, including scheduled loan disbursements, while the six-month ratio was 2.44x. CEB's dynamic funding activity over 2021 was sufficient to maintain equally strong liquidity ratios while accommodating COVID-19-related disbursements.

In terms of committed disbursements, the bank's project financings tend to have a shorter time to disbursement than those of peers with large project-finance books. Therefore, CEB has lower committed disbursements taking longer than 12 months. As a consequence, CEB's liquidity position can comfortably cater for the acceleration of 50% of scheduled disbursements over a 12-month period.

**Chart 4**

**Liquidity Stress Test Ratios Peer Comparison**



\*Data as of June 30, 2021, for EIB (European Investment Bank) and IBRD (International Bank for Reconstruction and Development). June is the year end for IBRD. EBRD--European Bank for Reconstruction and Development. ADB--Asian Development Bank. Source: S&P Global Ratings Copyright © 2022 by Standard & Poor's Financial Services LLC. All rights reserved.

**Extraordinary Shareholder Support**

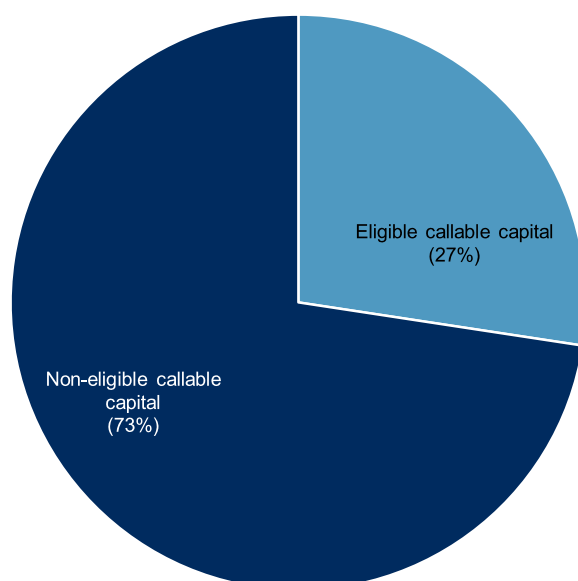
We assess CEB's stand-alone credit profile (SACP) as 'aaa' based on the bank's stand-alone merits. Because the SACP fully supports the 'AAA' long-term issuer credit rating, that rating does not rely on the expectation of extraordinary

support in the form of callable capital. This notwithstanding, callable capital from the bank's highly rated shareholders would enhance our RAC ratio and mitigate the impact on CEB's financial profile in the event that its capital adequacy were to deteriorate. Currently, the bank has eight 'AAA' rated shareholders and one 'AA+' rated one.

### Chart 5

#### CEB Callable Capital

As a percentage of total callable capital



Source: S&P Global Ratings.

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**Table 2**

#### Council of Europe Development Bank--Selected Indicators

	2021	2020	2019	2018	2017	2016
<b>ENTERPRISE PROFILE</b>						
<b>Policy importance</b>						
Total purpose-related exposure (loans, equity, etc.) (mil. €)	18,940.5	17,433.0	15,453.4	14,649.5	13,828.3	13,752.4
Public-sector (including sovereign-guaranteed) loans/purpose-related exposure (%)	81.4	79.5	76.5	76.2	75.0	75.1
Private-sector loans/purpose-related exposures (%)	18.6	21.0	23.5	23.8	25.0	24.9
Gross loan growth (%)	8.6	12.9	5.5	5.9	0.6	4.9
PCT ratio	0.0	0.0	0.0	0.0	0.0	0.0
<b>Governance and management expertise</b>						
Share of votes controlled by eligible borrower member countries (%)	100.0	100.0	100.0	100.0	100.0	100.0

Table 2

Council of Europe Development Bank--Selected Indicators (cont.)						
	2021	2020	2019	2018	2017	2016
Concentration of top two shareholders (%)	33.4	33.5	33.5	33.5	33.5	33.5
Eligible callable capital	1,332.8	1,332.8	1,332.8	1,332.8	1,394.9	1,392.5
<b>FINANCIAL RISK PROFILE</b>						
<b>Capital and earnings</b>						
RAC ratio	24.7	26.0	24.6	25.3	25.2	20.0
Net interest income/average net loans (%)	0.8	0.9	1.0	1.1	1.2	1.2
Net income/average shareholders' equity (%)	3.0	2.4	3.4	3.3	3.9	3.8
Impaired loans and advances/total loans (%)	0.0	0.0	0.0	0.0	0.0	0.0
<b>Funding and liquidity</b>						
<b>Liquidity ratios</b>						
Liquid assets/adjusted total assets (%)	31.7	30.0	34.2	33.1	35.5	35.5
Liquid assets/gross debt (%)	38.3	38.2	43.4	42.2	45.8	46.6
Liquidity coverage ratio (with planned disbursements):						
Six months (net derivate payables)	2.4	3.2	2.4	2.3	2.1	1.9
12 months (net derivate payables)	1.2	1.3	1.4	1.2	1.2	2.0
12 months (net derivate payables) including 50% of all undisbursed loans	1.6	1.6	1.3	1.2	1.2	1.9
<b>Funding ratios</b>						
Gross debt/adjusted total assets (%)	82.8	78.7	78.9	78.6	77.5	76.0
Short-term debt (by remaining maturity)/gross debt (%)	18.6	15.4	17.4	18.5	25.9	17.1
Static funding gap (without planned disbursements)						
12 months (net derivate payables)	1.4	1.5	1.7	1.4	1.3	1.8
<b>SUMMARY BALANCE SHEET</b>						
Total assets	29,714.9	27,959.3	26,141.8	24,348.0	23,798.3	25,602.8
Total liabilities	26,481.2	24,827.1	23,053.0	21,324.8	20,831.5	22,790.9
Shareholders' equity	3,233.7	3,132.2	3,088.8	3,023.2	2,966.8	2,811.9

PCT--Preferred creditor treatment. RAC--Risk-adjusted capital.

Table 3

	Council of Europe Development Bank	European Investment Bank	European Bank for Reconstruction and Development	Asian Development Bank	International Bank for Reconstruction and Development
Total purpose-related exposure (Mil. €)	18,940.5	449,440.4	37,492.0	123,229.0	191,451.0
PCT	0.0	0.2	0.0	0.2	0.2
RAC	24.7	22.5	29.7	31.0	27.2
Liquidity ratio 12 months (net derivate payables)	1.2	1.6	1.9	1.0	1.3

Table 3

Council of Europe Development Bank--Peer Comparison (cont.)					
	Council of Europe Development Bank	European Investment Bank	European Bank for Reconstruction and Development	Asian Development Bank	International Bank for Reconstruction and Development
Funding gap 12 months (net derivate payables)	1.4	1.6	2.4	1.0	1.4

PCT--Preferred creditor treatment. RAC--Risk-adjusted capital. \* RAC, Funding & Liquidity ratios for EIB are as of end June 2021. † Data for IBRD are as of end June 2021.

## Related Criteria

- Criteria | Governments | General: Multilateral Lending Institutions And Other Supranational Institutions Ratings Methodology, Jan. 31, 2022
- 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
- Principles Of Credit Ratings, Feb. 16, 2011

## Related Research

- Abridged Supranationals Interim Edition 2022: Comparative Data For Multilateral Lending, May 27, 2022
- Supranationals Edition 2021: Comparative Data For Multilateral Lending Institutions, Oct. 27, 2021

### Ratings Detail (As Of September 12, 2022)\*

#### Council of Europe Development Bank

Issuer Credit Rating

*Foreign Currency* AAA/Stable/A-1+

Commercial Paper

*Foreign Currency* A-1+

Senior Unsecured

AAA

#### Issuer Credit Ratings History

15-Feb-2019 *Foreign Currency* AAA/Stable/A-1+

30-Jun-2017 AA+/Positive/A-1+

27-Dec-2012 AA+/Stable/A-1+

\*Unless otherwise noted, all ratings in this report are global scale ratings. S&P Global Ratings' credit ratings on the global scale are comparable across countries. S&P Global Ratings' credit ratings on a national scale are relative to obligors or obligations within that specific country. Issue and debt ratings could include debt guaranteed by another entity, and rated debt that an entity guarantees.

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