Paris, December 16, 2022 – Moody's Investors Service ("Moody's") has today placed the Council of Europe Development Bank's (CEB) Aa1 long-term Issuer and Senior Unsecured ratings as well as its (P)Aa1 Senior Unsecured Shelf and Senior Unsecured MTN program ratings on review for upgrade. Concurrently, CEB's Commercial Paper rating has been affirmed at P-1.

The decision to place the ratings on review for upgrade is driven by the CEB Governing Board's approval on 2 December 2022 of a very significant increase of the bank's paid-in and callable capital. In Moody's view, the capital increase will improve CEB's capital adequacy and is also a signal of very strong shareholder support. CEB will use its improved capital position to initiate lending in Ukraine (Caa3 negative), continue to support neighbouring countries in managing migrant flows as well as address other social challenges in Europe.

The review period, which is expected to last up to three months, will allow Moody's to gain greater clarity around CEB's operational and strategic plans for the coming years. The Governing Board on 2 December also approved a new Strategic Framework for 2023-2027, of which the capital increase forms a key component. Moody's expectation is that CEB's updated strategic plan will not increase risk to its balance sheet in a way that jeopardises the clear benefit its credit profile will derive from the capital increase.

RATINGS RATIONALE

RATIONALE FOR INITIATING THE REVIEW FOR UPGRADE ON CEB's Aa1 RATINGS

On 2 December 2022, the Governing Board of the CEB (composed of representatives of its shareholding member states) approved a €4.25 billion increase of the bank's subscribed capital, a 78% increase from its current level. Of the total capital increase, €1.2 billion is to be provided in the form of paid-in capital with the remainder made available as callable capital. Once fully provided, CEB's total paid-in capital will roughly triple to €1.8 billion from just over €600 million today, while Moody's estimates that its total equity (including retained earnings added to reserves) will increase by close to 40% compared to end-2021 levels. Moreover, the €3.05 billion addition of callable capital will lead to a total increase of the bank's callable capital of more than 60%.

The very substantial increase of both paid-in and callable capital marks a step change for CEB. This is the first increase of paid-in capital in the more than 65-year history of CEB, which so far has exclusively relied on retained earnings and the accession of new shareholders to boost its useable equity. Moody's expects that the increase in paid-in capital will lower CEB's elevated leverage ratio, which has long been a key weakness of the credit profile.

Moreover, the magnitude of the capital increase is testament to shareholding member states’ very strong support for CEB as well as the bank's enhanced relevance in tackling key social
challenges in Europe. This, in turn, has a direct and marked positive impact on Moody's assessment of the strength of member support, both in its contractual and non-contractual forms.

The increase in capital is provided to allow CEB to play a more active role in tackling social challenges such as health and social care, affordable housing and education and vocational training across CEB's 42 shareholding member states. However, Moody's expects that a key part of the bank's activities in coming years will be focused on lending to tackle such challenges both in Ukraine, which will soon likely be confirmed as a shareholder of the bank, and for persons having fled Ukraine to neighbouring countries. Lending to Ukraine in particular is likely to entail a higher level of risk for the bank's loan portfolio. However, Moody's expects that the high quality of CEB's management and its long track record of prudently and successfully managing the risks of its loan portfolio entails that risk will not increase to the extent that it offsets the many benefits to CEB's credit profile stemming from the capital increase.

The capital increase becomes effective once 67% of the offered shares have been subscribed. Moody's expects member states to complete their respective national approval processes for signing off on the capital increase by mid-year 2023, although the payment of funds to CEB will materialise over up to four years. However, Moody's considers the risk of shareholders not fully providing the funds agreed by the Governing Board to be very low.

ENVIRONMENTAL, SOCIAL AND GOVERNANCE CONSIDERATIONS

CEB's credit impact score is positive (CIS-1), reflecting the positive impact on its credit profile of very strong governance and its social mandate, and low environmental risk exposure.

CEB's environmental issuer profile score is neutral to low (E-2), reflecting neutral-to-low exposure across all five environmental risk categories. CEB tracks the carbon footprint of projects approved, and since 2017 the emission savings from mitigation projects approved have mostly exceeded the emission levels from all other projects. In line with other MDBs, CEB is in the process of aligning its project portfolio with the Paris Agreement on Climate Change.

CEB's social issuer profile score is positive (S-1). CEB's explicit mandate is to be a social bank, and social policy objectives are central to its mission which positions it well to benefit from demographic and societal trends and supports our assessment of responsible production. CEB has been an early adopter of Social Inclusion Bond issuance. Given its policy role and reputation, it has a strong relationship with its customers.

CEB's governance issuer profile score is positive (G-1). CEB adheres to very strong risk management processes, which has resulted in a pristine track record of asset performance. The bank's management is highly credible and has a strong track record in implementing CEB's strategy. CEB's strong governance profile will be a key factor in helping the bank to manage the increase in risk of its loan portfolio which Moody's expects will occur over coming years.

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

FACTORS THAT COULD LEAD TO AN UPGRADE

The review period will allow Moody's to assess in greater detail the bank's lending and financial plans over the coming five-year period. If Moody's expectations that this will not lead to an excessive increase of risk are met, Moody's is likely to upgrade CEB's ratings by one notch to Aaa.
FACTORS THAT COULD LEAD TO A DOWNGRADE

Given the review for upgrade, the prospect of a downgrade of the ratings is remote. That said, over time, a sharp and renewed increase in leverage as well as a marked deterioration of CEB's asset quality and performance or a marked weakening of shareholder support for the institution could put downward pressure on the ratings.

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

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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Moody's general principles for assessing environmental, social and governance (ESG) risks in our credit analysis can be found at https://ratings.moodys.com/documents/PBC_1288235.

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