Paris, March 10, 2023 – Moody’s Investors Service (“Moody’s”) has today upgraded 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 to Aaa and (P)Aaa, respectively. Concurrently, CEB’s Commercial Paper rating has been affirmed at P-1. The outlook on CEB is stable.

The decision to upgrade the ratings to Aaa is driven by Moody's assessment that CEB's creditworthiness is materially improved by the significant capital increase approved in December 2022. In particular, this will lead to a reduction in the bank's leverage and has resulted in an improvement to Moody’s assessment of the strength of member support. While CEB on the back of the capital increase will continue to grow its balance sheet, including by lending to Ukraine (Ca stable), Moody's expects that it will do so in a way that does not offset the benefits its credit profile will derive from the capital increase. The review for upgrade was initiated on 16 December 2022, 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.

The stable outlook reflects Moody's expectation that the benefits CEB will derive from the recently agreed capital increase will continue to strengthen the bank's credit profile, and outweigh any potential increase in risks to its asset portfolio from a gradually increasing exposure to Ukraine. It also reflects Moody's expectation that member states' strong level of support for the bank will continue to manifest itself in the formal subscription to the capital increase over the course of 2023, while Moody’s does not foresee any material changes to CEB’s Liquidity and Funding profile over the medium term.

RATINGS RATIONALE

RATIONALE FOR UPGRADING COUNCIL OF EUROPE DEVELOPMENT BANK’S RATINGs TO Aaa

On 2 December 2022, the Governing Board of CEB (composed of representatives of its sharing 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 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. CEB's elevated leverage ratio has long been a key weakness of the credit profile and Moody's expects that the increase in paid-in capital will gradually lower CEB's leverage until 2026 when all the new shareholder contributions have to be paid in.

Moreover, the magnitude of the capital increase is testament to shareholding member states' 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 capital increase complements CEB's operational plans until 2027 laid out in the Strategic Framework which was approved by the Governing Board in December and published in January 2023. The plan sets as CEB's overarching objectives for the coming five years the response to evolving social development and inclusion challenges; assistance and integration of refugees and migrants; and support for the reconstruction and rehabilitation of Ukraine's social sectors.

The bank's focus on lending to Ukraine, which Moody's expects will be formally confirmed as a shareholder of CEB in coming months, will entail a higher level of risk for the bank's loan portfolio. However, Moody's expects that the size and nature of the exposure to Ukraine as well as the high quality of CEB's management and its long track record of prudently and successfully managing the risks of its loan portfolio, will limit overall risks from the exposure in a way that it does not offset 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 over the course of 2023, although the payment of funds to CEB will materialise over up to four years. However, the majority of CEB's shareholders are highly rated European sovereigns and Moody's considers the risk of these governments not fully providing the funds approved by the Governing Board to be very low.

RATIONALE FOR THE STABLE OUTLOOK

The stable outlook reflects Moody's expectations that CEB's Capital Adequacy will balance an excellent asset performance and a declining leverage ratio against somewhat increasing risks to its asset portfolio in coming years, while the bank's very strong Liquidity and Funding profile will remain largely unchanged for the coming 12 to 18 months. Meanwhile, Moody's expects that the level of shareholder support will remain strong in the wake of the recently agreed capital increase, with member states continuing to subscribe to the capital increase over the course of 2023 in line with their national ratification processes.

ENVIRONMENTAL, SOCIAL AND GOVERNANCE CONSIDERATIONS

CEB's credit impact score is positive (CIS-1). On the one hand, this reflects the positive impact on its credit profile of the bank's very strong governance profile, a feature shared with most other Aaa-rated supranationals. More uniquely, CEB's role as a dedicated development bank for social policy objectives enhances its role and relevance in addressing common social challenges for instance related to demographic change. Furthermore, CEB's exposure to environmental risks is generally low.

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

An upgrade of CEB's ratings is not possible as its Aaa ratings are at the highest level on Moody's rating scale.

FACTORS THAT COULD LEAD TO A DOWNGRADE

Downward pressure on the Aaa rating would build if CEB's asset quality deteriorates materially beyond Moody's current expectations or if there is a material deterioration of its asset performance, most likely as a result of its increasing exposure to Ukraine. Downward pressure could also build if the growth of CEB's loan portfolio in coming years significantly exceeds the plans laid out in the Strategic Framework, leading to a smaller than expected decline in the bank's leverage ratio. A failure by member states to provide significant amounts of the recently approved funding would also put negative pressure on the ratings, as would any emerging weaknesses in its liquidity and funding profile. A downgrade of major shareholders such as Germany (Aaa stable), France (Aa2 stable), Italy (Baa3 negative) and Spain (Baa1 stable) would also add to negative credit pressures.

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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Petter Bryman
Vice President - Senior Analyst
Sovereign Risk Group
Moody's France SAS
96 Boulevard Haussmann
Paris, 75008
France
JOURNALISTS: 44 20 7772 5456
Client Service: 44 20 7772 5454

Dietmar Hornung
Associate Managing Director
Sovereign Risk Group
JOURNALISTS: 44 20 7772 5456
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