S&P Global Ratings

RatingsDirect®

Council of Europe Development Bank

Primary Credit Analyst:
Gabriel Forss, Stockholm (46) 8-440-5933; gabriel.forss@spglobal.com

Secondary Contact:
Maxim Rybnikov, London (44) 20-7176 7125; maxim.rybnikov@spglobal.com

Research Contributor:
Harshleen K Sawhney, CRISIL Global Analytical Center, an S&P Global Ratings affiliate, Mumbai

Table Of Contents

Council of Europe Development Bank

Stand-alone credit profile	aaa	+	Extraordinary shareholder support	0	+	Holistic approach	0

Enterprise risk profile

Extremely strong	Very strong	Strong	Adequate	Moderate	Weak	Very weak

Financial risk profile

Extremely strong	Very strong	Strong	Adequate	Moderate	Weak	Very weak

Issuer credit rating

AAA/Stable/A-1+

Outlook

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

The stable outlook reflects S&P Global Ratings' expectation that the Council of Europe Development Bank (CEB) will be able to maintain its newfound positive lending dynamics over the coming two years, such that its policy relevance and funding importance remain unquestioned. We also assume CEB will continue to enjoy excellent PCT and maintain its extremely strong financial profile.

We could downgrade CEB if its policy relevance for shareholders significantly deteriorated, as seen, for example, through lack of shareholder engagement or support for the current activities of the bank. If we observed that CEB's financing contribution was not sufficiently unique or meaningful for its shareholders, illustrated by notably declining lending activity, momentum for a downgrade could build. A significant deterioration in CEB's funding and liquidity assessment could also have a negative impact on the ratings, while a significantly deteriorating capital ratio would most likely be mitigated by the existing callable capital provided by highly rated sovereigns.

Rationale

We base our ratings on CEB's extremely strong enterprise risk and financial risk profiles. Over the past two years, CEB has comfortably maintained its capital ratios despite more dynamic lending activity, supported by the widening of its mandate and higher disbursements to non-target countries. At the same time, CEB's risk-adjusted capital (RAC) ratio and its funding profile have continued to strengthen, with the move last year to two-way credit support annexes on its derivatives portfolio opening up additional markets, and further enlarging its investor base thanks to increasing issuance volumes. As a result, we have revised our assessment of CEB's financial risk profile to extremely strong, and its stand-alone credit profile to 'aaa'. Because 'aaa' is the highest level, we no longer incorporate extraordinary shareholder support from CEB'S callable capital in our assessment.

Over the past few years, CEB has increased its efforts to broaden its activities, resulting in a continuous increase in disbursements and project approvals. We expect CEB's solid momentum for loan disbursements will continue, because the bank's more dynamic approach to its lending mandate will allow it to improve its lending footprint through the pent-up demand for social investments throughout Europe. As a result, the bank will be able to cement its position as a key social infrastructure financer. At the same time, CEB's history of demonstrated preferred creditor treatment (PCT) also underlines its overall enterprise risk profile. Specifically, the CEB has, since its creation, benefited from an excellent track record of PCT by the countries in which it operates, and we expect this will remain the case.

We believe sustained longer-term growth would likely prompt a medium-term build-up in financial capacity. That said, the bank's current activity levels in higher-rated communities outside of its original target group will likely continue to sustain the RAC ratio above the 23% threshold over the next few years. Although modest, earnings will also continue to support the internal capital generation rate and the capital ratio.

Enterprise Risk Profile: Strong Shareholder Recognition And Track Record Of Preferred Creditor Treatment

- A broadening mandate and increasing role as a social investor in member countries' budgets, which underline relevance as a funding agency.
- Excellent history of preferred creditor treatment (PCT).
- Experienced and conservative management, catering for a prudent transition to more sophisticated derivatives management.

Policy importance

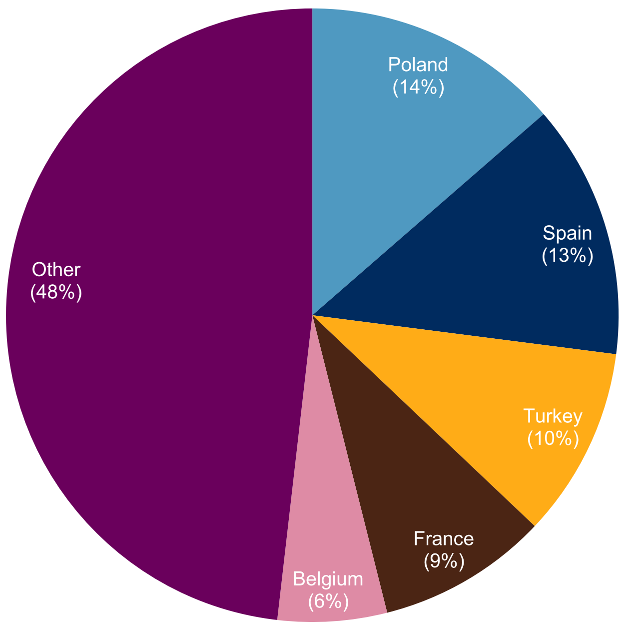
CEB was founded in 1956 as the Council of Europe Resettlement Fund for National Refugees and Over-Population in Europe, with a mandate to help refugees and other displaced persons after World War II. Its current role of supporting social infrastructure investment in Europe involves loans to support job creation in small and midsize enterprises, vocational training, social housing, health care, environmental projects, correctional facilities, natural catastrophe relief, and educational reform. Even though parts of CEB's lending activity could be performed by other MLIs, we believe CEB holds a key position because of its established history, role, and the core essence of its mandate.

In particular, the institution performs a key role for small member countries, although its expansion is partly through relaxation of a rule favoring traditional target 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). CEB's average loan size is significantly smaller than that of highly rated peers with large project-finance portfolios. Moreover, CEB offers additional expertise in a number of social domains (such as housing and education), technical design support, and technical assistance through the project cycle.

With its broadening mandate and increasingly tangible role as a social investor in member countries' budgets, CEB has managed to scale up its operations. In sharp contrast with its lackluster activity levels after the 2007 financial crisis, the bank is now responding swiftly to high demand for investments in social infrastructure. In particular, in 2017 and 2018, we observed strong momentum in CEB's disbursements and project approvals, with both at record highs. Approvals of €3.9 billion in both years exceeded the bank's target of €3.5 billion annually. The higher disbursements in 2017 were offset by almost equally high scheduled reimbursements, resulting in fairly flat loan book growth. However, we observe an ongoing positive trend in lending activity, as depicted by a 6% increase in outstanding loans in 2018.

Chart 1

Council Of Europe Devleopment Bank's Five Largest Purpose-Related Exposures By Country*



Data as a percentage of gross purpose-related assets plus guarantees. Source: S&P Global Ratings.

We believe this robust momentum will continue, since the bank's more dynamic approach will allow it to improve its lending footprint, thanks to demand for social investments throughout Europe. In addition, the EU has proposed a specific social investment window in its 2021-2027 budget, which we believe could help CEB further fulfill its mandate and sustain its policy relevance.

CEB's history of demonstrated PCT also underlines its overall enterprise risk profile. Since its creation, CEB has benefited from an excellent track record of PCT, and we expect this will continue. Despite the CEB's concentrated loan portfolio, loan losses have been minimal. CEB has experienced only one sovereign default, that of a debt owed by the former Yugoslavia. The principal amount was fully recovered (including arrears) as of July 2004, representing a net present value loss to the CEB of 0%. We consider this a confirmation of the PCT afforded to CEB.

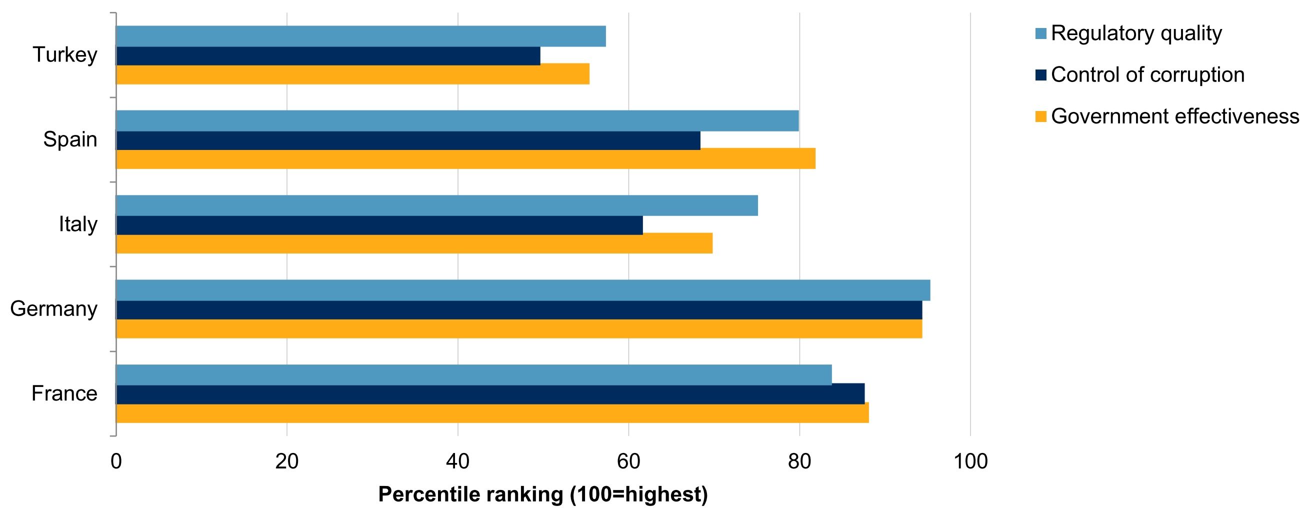
Governance and management expertise: Experienced management secures prudent transition to two-way derivatives management

In our opinion, CEB benefits from strong governance and risk management standards. Shareholders remain supportive and acknowledge the importance of CEB as a key contributor in its niche financing segment. The CEB's member countries are directly involved in defining CEB's policy. Operationally, we think CEB has conservative risk and liquidity management policies. Over the past two years, the bank has modernized its 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 the majority of its derivatives counterparty portfolio in 2018, which is due to be completed in 2019.

We view the bank's policy of not paying dividends as a sign of ongoing shareholder support, and we expect this will continue. In 2012, CEB benefited from additional capital subscriptions linked to a capital increase approved on Feb. 4, 2011. This increase required no disbursement of cash from member countries and had no effect on adjusted shareholders' equity. Windfall capital improvements from the stronger credit quality of exposures and high scheduled repayments have reduced the imminent need for a capital increase from shareholders. Nevertheless, we believe CEB's sustained growth would likely prompt a medium-term buildup of financial capacity.

Chart 2

Council Of Europe Development Bank's Five Largest Shareholders*



*Selected World Bank governance indicators. Source: S&P Global Ratings.

Financial Risk Profile: Strong Capital Sustains Lending Growth

- An excellent loan loss track record, sound profitability, and improving asset quality that support capital ratios.
- Well-diversified funding, boosted by modernized derivatives management that broadens investor and counterparty depth.

- Strong liquidity, with sufficient buffers to allow acceleration of committed disbursements.

Capital adequacy has strengthened

CEB's stand-alone financial risk profile has strengthened, thanks to its more stable capitalization despite brisk lending. We estimate CEB's RAC ratio at 25.3% as of end-2018 after adjustments for concentration risk and PCT, and it displays very strong funding and liquidity. Over the past few years, CEB has increased efforts to broaden its activities, which has resulted in a continuous increase in disbursements and project approvals. We note that, although the amount of outstanding loans increased by 6% in 2018, the RAC ratio remained stable from 25.2% as of end-2017. This demonstrates CEB's stronger engagement in non-target countries in Northern Europe, which has a positive impact on the risk weight of loans.

About 10% of CEB's outstanding loans are to counterparties in Turkey, where domestic lenders are struggling with a weak and volatile lira and economic contraction. Extensive use of credit enhancement, primarily guarantees from the Turkish government, somewhat limits credit risk from CEB's Turkish exposure. Moreover, Turkey is the CEB's fifth largest shareholder, signaling its key stake in the institution.

We believe that CEB will maintain the current level of yearly disbursement by widening the scope of social investments to include refugee-related projects, sustainable development, housing, and education. Its current activity in higher-rated countries outside its original target group will likely keep the RAC ratio above 23% over the next few years. Although modest, CEB's earnings will also continue to support internal capital generation and the capital ratio.

Table 1

Council Of Europe Development Bank Risk-Adjusted Capital Framework Data: 2018

(Mil. €)	Exposure	S&P Global Ratings RWA	Average S&P Global Ratings RW (%)
Credit risk			
Government and central banks	18,116	5,550	31
Institutions	8,048	1,823	23
Corporate	331	312	94
Retail	-	-	-
Securitization	-	-	-
Other assets	50	57	113
Total credit risk	26,545	7,743	29
Operational risk			
Total operational risk		301	
Risk transfer mechanisms			
Risk transfer mechanisms RWA		-	
RWA before MLI Adjustments		8,044	100
MLI adjustments			
Single name (on corporate exposures)		1,294	414
Sector (on corporate portfolio)		96	6
Geographic		(790)	(9)
Preferred creditor treatment (on sovereign exposures)		(3,456)	(62)

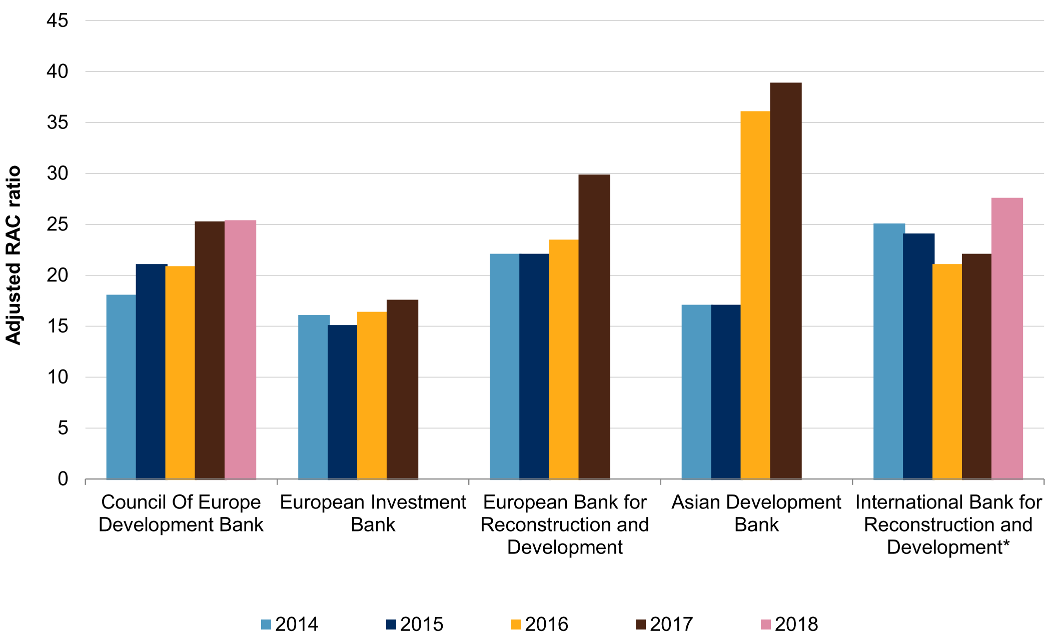
Table 1

Council Of Europe Development Bank Risk-Adjusted Capital Framework Data: 2018 (cont.)		
Preferential treatment (on financial institution and corporate exposures)	(39)	(2)
Single Name (On Sovereign Exposures)	6,906	124
Total MLI adjustments	4,011	50
RWA after MLI Adjustments	12,055	150
	Total adjusted capital	**S&P Global Ratings RAC Ratio (%)**
Capital ratio before Adjustments	3,049	37.9
Capital ratio after Adjustments	3,049	25.3

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

Chart 3

Council Of Europe Development Bank--Risk-Adjusted Capital Ratio Peer Comparison



Source: S&P Global Ratings. *Year-end for IBRD is June 30.

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

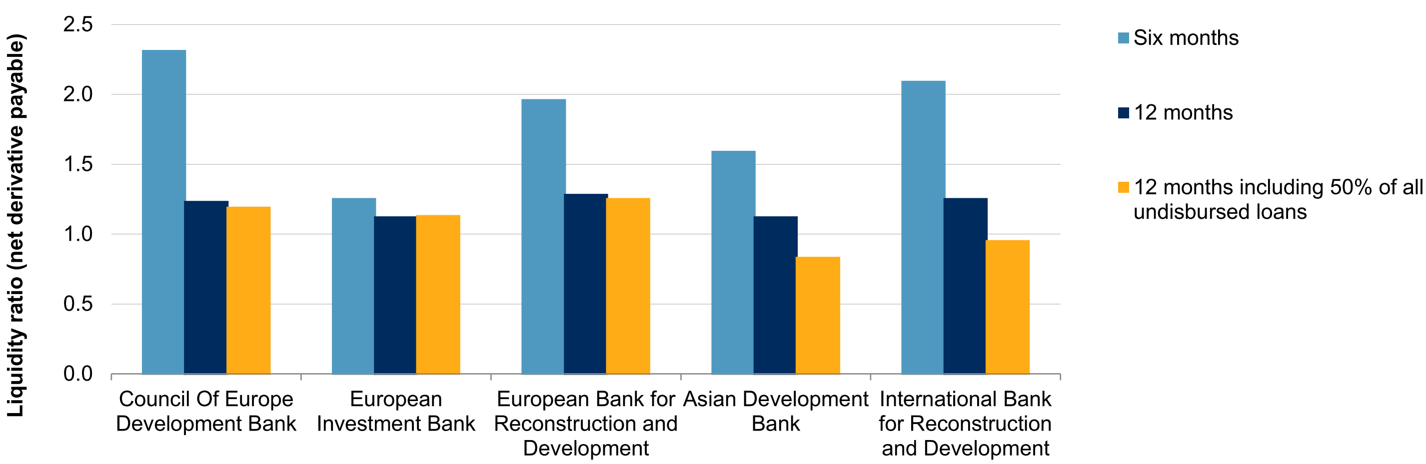
Funding. We see a positive impact on CEB's funding profile from its more active funding strategy after the switch to two-way CSAs on the majority of derivative counterparties in 2018. CEB also increased its borrowings by 64% during 2018 to €4.9 billion. This year, the bank had already completed €2.9 billion of its planned €5.0 billion of funding by April, and has furthered its already comprehensive access to the funding markets. For example, CEB issued its first Norwegian krone benchmark bond in February, returned to the Australian market in first-quarter 2019 with its first transaction since 2014, and placed two instruments denominated in New Zealand dollars, the first in over a decade, in

April 2019. Moreover, CEB issued its second €500 million seven-year social inclusion bond in 2018 and its third in April 2019, further diversifying its investor base. Additionally, our funding ratios indicate that CEB is structurally able to cover its scheduled short-term debt repayments without recourse to new issuance.

Liquidity. Owing to a deleveraging initiative, CEB's liquidity ratios started to decline. However, the move to two-way CSAs in 2018 has required the buildup of an additional liquidity buffer. Under our liquidity stress scenario, at all horizons up to one year, CEB would fully cover its balance-sheet liabilities without market access. Using year-end 2018 data, our 12-month liquidity ratio was 1.23x including scheduled loan disbursements, while the six-month ratio was 2.3x. In terms of committed disbursements, CEB's project financings tend to have a shorter time to disbursement than for 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

Council Of Europe Development Bank--Liquidity Stress Test Ratios Peer Comparison



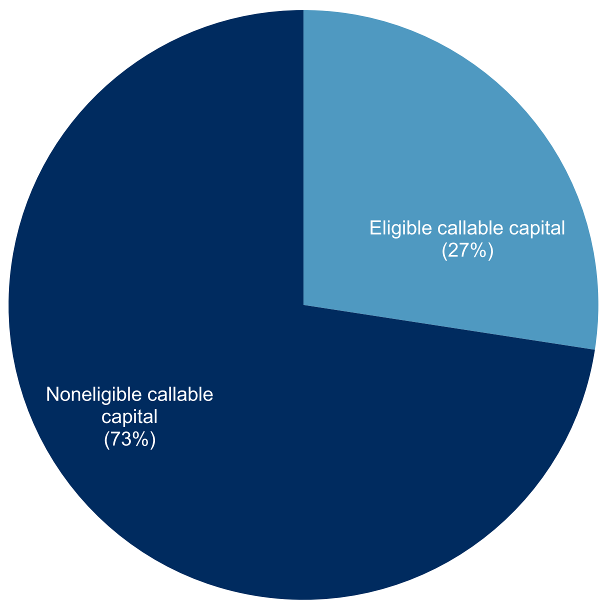
Data for CEB is as of Dec. 31,2018; EIB, EBRD, and ADB as of Dec. 31, 2017, and IBRD as of June 30, 2018.

Extraordinary Shareholder Support: No Uplift Needed

We no longer factor extraordinary support in the form of callable capital into the long-term rating because CEB, on its stand-alone merits, achieves our highest assessment. This notwithstanding, callable capital from CEB's highly rated shareholders would enhance our RAC ratio and mitigate the impact on the bank's financial profile in the event that its capital adequacy were to deteriorate. Currently, CEB has eight 'AAA' shareholders and one 'AA+' shareholder.

Chart 5

Council Of Europe Development Bank's Callable Capital*



*Data as a percentage of total callable capital. Source: S&P Global Ratings.

Table 2

Council of Europe Development Bank Selected Indicators

	2018	2017	2016	2015	2014
ENTERPRISE PROFILE					
Policy importance					
Total purpose-related exposure (loans, equity, etc.)	14,649.5	13,828.3	13,752.4	13,109.8	12,607.3
Public-sector (including sovereign-guaranteed) loans/purpose-related exposure (%)	76.2	75.0	75.1	73.2	75.2
Private-sector loans/purpose-related exposures (%)	23.8	25.0	24.9	26.9	24.8
Gross loan growth (%)	5.9	0.6	4.9	4.0	(0.1)
PCT ratio	0.0	0.0	0.0	0.0	0.0
Governance and management expertise					
Share of votes controlled by eligible borrower member countries (%)					
Concentration of top two shareholders (%)	33.5	33.5	33.5	33.5	33.5
Eligible callable capital	1,332.8	1,394.9	1,392.5	1,392.5	1,392.5

Table 2

Council of Europe Development Bank Selected Indicators (cont.)

	2018	2017	2016	2015	2014
FINANCIAL RISK PROFILE					
Capital and earnings					
RAC ratio	25.3	25.2	20.8	21.0	18.0
Net interest income/average net loans (%)	1.1	1.2	1.2	1.3	1.3
Net income/average shareholders' equity (%)	3.3	3.9	3.8	4.8	5.4
Impaired loans and advances/total loans (%)	0.0	0.0	0.0	0.0	0.0
Funding and liquidity					
Liquidity ratios					
Liquid assets/adjusted total assets (%)	33.1	35.5	35.5	35.9	39.6
Liquid assets/gross debt (%)	42.2	45.8	46.6	47.7	51.5
Liquidity coverage ratio (with planned disbursements):					
Six months (net derivate payables)	2.3	2.1	1.9	3.6	2.1
12 months (net derivate payables)	1.2	1.2	2.0	2.2	1.5
12 months (net derivate payables) including 50% of all undisbursed loans	1.2	1.2	1.9	2.2	1.5
Funding ratios					
Gross debt/adjusted total assets (%)	78.6	77.5	76.0	75.2	76.9
Short-term debt (by remaining maturity)/gross debt (%)	18.5	25.9	17.1	15.8	26.5
Static funding gap (without planned disbursements)					
12 months (net derivate payables)	1.4	1.3	1.8	1.8	1.3
SUMMARY BALANCE SHEET					
Total assets	24,348.0	23,798.3	25,602.8	25,116.4	25,545.4
Total liabilities	21,324.8	20,831.5	22,790.9	22,404.9	22,999.9
Shareholders' equity	3,023.2	2,966.8	2,811.9	2,711.5	2,545.5

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

Table 3

Council of Europe Development Bank Peer Comparison

	CEB	EIB	EBRD	ADB	IBRD
Total purpose-related exposure (€ Mil)	14,649	442,628	27,912	89,965	158,846
PCT	0	0.1	0	0	0.3
RAC	25.3	17.5	29.8	38.8	27.5
Liquidity ratio 12 months (net derivate payables)	1.23	1.12	1.27	1.12	1.25
Funding gap 12 months	1.42	1.21	1.58	1.01	1.32

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

* Data for CEB is of Dec-2018, EIB, EBRD and ADB as of Dec-2017 and IBRD as of June-2018

Ratings Score Snapshot

Enterprise risk profile	**Extremely strong**	Very strong	Strong	Adequate	Moderate	Weak	Very weak
Policy importance	**Very strong**	Strong	Adequate	Moderate	Weak		
Governance and management	**Strong**	Adequate	Weak				
Financial risk profile	**Extremely strong**	Very strong	Strong	Adequate	Moderate	Weak	Very weak
Capital adequacy	**Extremely strong**	Very strong	Strong	Adequate	Moderate	Weak	Very weak
Funding and liquidity	**Very strong**	Strong	Adequate	Moderate	Weak	Very weak	

Related Criteria

- Criteria | Governments | General: Multilateral Lending Institutions And Other Supranational Institutions Ratings Methodology, Dec. 14, 2018
- 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
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009

Related Research

- What Our New Criteria Has Meant For Multilateral Lending Institutions, April 12, 2019
- Supranationals Special Edition 2018, Oct. 11, 2018

Ratings Detail (As Of August 12, 2019)*		
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+

Ratings Detail (As Of August 12, 2019)*(cont.)	
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.