Research Update:

Eurasian Development Bank Rating Affirmed At 'BBB-/A-3'; Outlook Remains Stable

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Overview
• Our measure of Eurasian Development Bank's (EDB's) risk-adjusted capital (RAC) ratio has increased over the past 12 months, thanks to the bank's return to profitability.
• This improvement was offset by the bank's failure to achieve its current investment portfolio growth targets, which has pressurized EDB's policy importance, in our view.
• We are affirming our 'BBB-/A-3' ratings on EDB.
• The stable outlook reflects our expectation that EDB's RAC ratio will remain above 23% and the loan portfolio will demonstrate moderate growth.

Rating Action
On Oct. 12, 2017, S&P Global Ratings affirmed its long- and short-term foreign currency issuer credit ratings on Eurasian Development Bank (EDB) at 'BBB-/A-3'. The outlook remains stable. At the same time, we affirmed our Kazakhstan national scale rating on EDB at 'kzAA'.

Rationale
Our ratings on EDB incorporate our assessments of the bank's financial profile as very strong and business profile as very weak. These profiles lead us to derive a stand-alone credit profile (SACP) of 'bbb-'.

We have revised EDB's financial profile to very strong from strong. The return to profitability and growing diversification of exposures have strengthened the bank's risk-adjusted capital (RAC) ratio. EDB's RAC ratio after adjustments specific to multilateral lending institutions (MLIs) improved to 27.6% as of end-June 2017 from 22.4% as of end-June 2016. After a $144 million loss in 2015, EDB returned to profitability with a net income of $164 million in 2016 and $18 million in the first half of 2017. The increase in profits was largely driven by the release of Belaz provisions ($54.5 million) and by the net realized gain of financial assets available for sale ($26.6 million).

Currently, nonperforming loans (NPLs, defaulted and overdue more than 90 days) stand at $86 million, representing 4.9% of EDB's balance sheet portfolio, down from 5.9% at end-2016. In line with management's expectations, we don't anticipate this ratio will rise over the next 12 months. We note that the increase in provisions in the first half of 2017 relates to more conservative risk estimation for some of the existing NPLs.
Similar to other MLIs, EDB depends heavily on wholesale market funding. After a gap of more than a year due to a tenge (KZT) liquidity deficit in Kazakhstan's stock exchange market, on May 24, 2017, EDB issued KZT15 billion ($43 million) three-year bonds. Importantly, the issuance was 3x oversubscribed, highlighting EDB's ability to attract funds locally to support tenge-denominated loan generation and an easing of the pressures on liquidity in Kazakhstan's local debt market. Future fundraising will depend on the loan disbursement pace and on interest rates in the local markets.

EDB has historically maintained a conservative liquidity management policy. On June 30, 2017, EDB held $1.763 billion, or 51% of its balance sheet, in liquid assets. This enabled the bank to meet its policy target stipulating that liquid assets should cover not less than one year's projected net loan disbursements (loans disbursed less repayments) if greater than zero, less bilateral commitments, plus the annual cost of financial debt. We anticipate that the bank will be able to continue providing loans, even if market access worsens. EDB's liquidity ratios compare favorably with those of other regional MLIs.

We have revised our assessment of EDB's business profile to very weak from weak. We believe that EDB's policy importance has diminished. EDB failed to achieve its current investment portfolio target of $2.9 billion at end-2016, and in the first eight months of 2017 it grew only marginally. Growth was mostly stunted by loan prepayments, specifically $130 million prepaid in August 2017.

EDB's current investment portfolio stood at $2.6 billion as of end-August 2017 and the bank expects it to grow to $3.3 billion as of end-2017. We believe that EDB might miss this target as it had in the past.

We note that economic pressures on EDB's main shareholders, Russia and Kazakhstan, have abated in 2017. On March 17, 2017, we revised the outlook on Russia to positive from stable, and on Sept. 8, 2017, we revised the outlook on Kazakhstan to stable from negative.

Established in 2006 by an intergovernmental agreement, EDB is owned by the Russian Federation (66%), Kazakhstan (33%), Belarus (1%), Armenia (0.01%), Tajikistan (0.03%), and Kyrgyzstan (0.01%). It is the key MLI for the Eurasian Economic Union (EAEU) countries and manages a separate $8.5 billion fund for balance-of-payment support.

EDB also manages the Eurasian Fund for Stabilization and Development (EFSD), which was established specifically to address the impact of the global financial crisis on member states of the Eurasian Economic Union. In our view, EDB's role as the manager of the EFSD, which has $8.5 billion under management, underscores its importance for member states, in particular for Russia, the dominant member. EDB had disbursed $4.3 billion in loans as of June 30, 2017, $4 billion of which was to Belarus. The EFSD, which provides budgetary and balance-of-payments support to member states, as well as financing national and regional projects, has its own balance sheet, managed separately from EDB's balance sheet.
Our ratings on EDB do not incorporate any uplift for callable capital. Although callable capital can, in principle, enhance an MLI's SACP and result in a higher issuer credit rating, we factor in no explicit uplift in EDB's case. This is mainly because of EDB's highly unique ownership structure, which exacerbates the principal-agent problem related to capital calls.

**Outlook**

The stable outlook reflects our expectation that EDB's RAC ratio will remain above 23% and the loan portfolio will demonstrate some growth.

We could raise the ratings if EDB were to strengthen its mandate through substantial growth in its current investment portfolio (in line with the management's targets), while the capital position remains robust.

We could consider a negative rating action if EDB's asset quality deteriorates or if it relapses into losses.

**Related Criteria And Research**

**Related Criteria**

- General Criteria: S&P Global Ratings' National And Regional Scale Mapping Tables - August 14, 2017
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings - April 07, 2017
- General Criteria: National And Regional Scale Credit Ratings - September 22, 2014
- Criteria - Governments - General: Multilateral Lending Institutions And Other Supranational Institutions Ratings Methodology - November 26, 2012
- Criteria - Financial Institutions - Banks: Bank Capital Methodology And Assumptions - December 06, 2010
- General Criteria: Use Of CreditWatch And Outlooks - September 14, 2009

**Related Research**

- Research Update: Russian Federation 'BB+/B' And 'BBB-/A-3' Ratings Affirmed; Outlooks Positive - September 15, 2017
- Research Update: Kazakhstan Outlook Revised To Stable On Improved Monetary Policy Flexibility; 'BBB-/A-3' Ratings Affirmed - September 08, 2017
- Research Update: Outlook On Russia Revised To Positive On Improving Growth Prospects - March 17, 2017
- Eurasian Development Bank - February 16, 2017
- Supranationals Special Edition 2016: Five-Year Comparative Data For Multilateral Lending Institutions - September 29, 2016

**Ratings List**
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<td>BBB-/Stable/A-3</td>
<td>BBB-/Stable/A-3</td>
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Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. Complete ratings information is available to subscribers of RatingsDirect at www.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column. Alternatively, call one of the following S&P Global Ratings numbers: Client Support Europe (44) 20-7176-7176; London Press Office (44) 20-7176-3605; Paris (33) 1-4420-6708; Frankfurt (49) 69-33-999-225; Stockholm (46) 8-440-5914; or Moscow 7 (495) 783-4009.

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