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Asian Infrastructure Investment Bank - Aaa stable

Annual credit analysis

RATINGS

Asian Infrastructure Investment Bank

	Rating	Outlook
Long-term Issuer	Aaa	STA
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OVERVIEW AND OUTLOOK

The credit profile of the Asian Infrastructure Investment Bank (AIIB, Aaa stable) reflects our view that the bank is evolving in a manner consistent with the highest-rated multilateral development banks (MDBs), as it incorporates changes to operational capabilities, governance and market access.

Investment operations have accelerated as the bank has built up its staff, developed its internal processes and systems and focuses more on sector-specific strategies. We expect that AIIB will maintain strong capitalization despite near-term challenges to the credit quality of some of its borrowing sovereigns, including Oman (Ba3 negative), Pakistan (B3 stable) and Turkey (B2 negative). At the same time, we expect that AIIB will enjoy preferred creditor status, which will contribute to strong asset quality.

In 2019, AIIB formally commenced its borrowing program, establishing access to international capital market funding well ahead of any imminent need, given the bank's ample liquidity. Shareholder support will also remain strong as the bank's membership and, consequently, its capital base, expand beyond the levels at its founding in 2015. The likelihood of further, extraordinary support being made available by higher-rated shareholders with a strategic interest in sustaining AIIB operations – including, but not limited to China (A1 stable) – further enhances the bank's credit profile.

AIIB's credit profile could be downgraded if the bank's underwriting and risk management processes are not implemented in a manner consistent with those of the highest-rated MDBs. This could include corporate governance factors, such as interference by shareholders or a shift in strategy that results in a greater geographic concentration of lending and investment than we expect. A deterioration in asset performance incompatible with its presumed preferred creditor status and evidence of diminished capacity or willingness to support from key shareholders would also weigh on the credit profile.

This credit analysis elaborates on AIIB's credit profile in terms of capital adequacy, liquidity and funding and strength of member support, which are the three main analytical factors in our Supranational Rating Methodology.

Special topic

AIIB's response to the coronavirus pandemic

MDBs play an important role in mitigating the economic and financial impact of the coronavirus pandemic on their borrowers. Since the outbreak of the crisis, many of the largest MDBs have announced acceleration of disbursements, additional credit facilities and a repurposing toward COVID-19-related projects. Overall, across rated MDBs, lending priorities generally fall into four areas with the aim to (1) strengthen health infrastructure; (2) provide support to viable businesses, either directly or via banking systems; (3) provide direct financial assistance to vulnerable households; and/or (4) offer budgetary support to sovereign borrowers. [1]

In April 2020, AIIB created a Crisis Recovery Facility, which offers up to $13 billion, to support AIIB's members and clients in alleviating and mitigating economic, financial and public health stresses arising from COVID-19. The facility includes traditional financing, lines of credit to financial intermediaries, and provision of working capital and liquidity support to the borrowing banks' clients.

Financings under the Facility can cover the following areas which are consistent with the AIIB's Articles of Agreement:

1) **Immediate health sector needs.** The bank would support the development of health system capacity, and provision of essential medical equipment and supplies to combat COVID-19, and well as the long-term sustainable development of the health sector of the member.

2) **Economic resilience.** The Bank would provide financing to supplement government productive expenditures to support the social and economic response and recovery.

3) **Financings to address liquidity constraints for clients in infrastructure and other productive sectors.** With such support, clients can overcome liquidity constraints and maintain critical long-term investments that may have to be curtailed, delayed or suspended in the absence of AIIB financing.

Under the COVID-19 Crisis Recovery Facility, AIIB also established the Special Fund Window to provide interest-rate buy-downs for sovereign-backed financing for eligible lower-income members, because lower-income countries have become particularly vulnerable to the impact of COVID-19.

Organizational structure and strategy

AIIB was established in June 2015 by 57 founding member countries and began operations in January 2016. As of August 2020, it had approved 103 members since inception. Based on capital subscriptions as of August 2020, the top five shareholders are China (30.8% of total subscriptions), India (Baa3 negative, 8.6%), Russia (Baa3 stable, 6.8%), Germany (Aaa stable, 4.6%) and Korea (Aa2 stable, 3.9%).

The bank has a public policy mandate to meet Asia's infrastructure funding gap. Through the development of infrastructure and other productive sectors, AIIB's purpose as set out in its articles of agreement is to

- Foster sustainable economic development, create wealth and improve infrastructure connectivity in Asia by investing in infrastructure and other productive sectors; and
- Promote regional cooperation and partnership in addressing development challenges by working in close collaboration with other multilateral and bilateral institutions.

The composition of AIIB's membership supports its status as an international financial institution. Its broad membership base is larger than the Asian Development Bank (ADB, Aaa stable, 68 members) and other regional MDBs, such as the African Development Bank (AfDB, Aaa stable, 81 members), European Bank for Reconstruction and Development (Aaa stable, 65 members), the Islamic

Development Bank (IsDB, Aaa stable, 57 members) and the Inter-American Development Bank (Aaa stable, 48 members). However, the number of AIIB's shareholders is materially lower than the World Bank Group's International Bank for Reconstruction and Development (IBRD, Aaa stable, 189 countries).

The distribution of voting power between member countries is in line with other large regional and global MDBs, where non-borrowers collectively hold significant voting power. Major decisions require consent from at least 75% of total voting share, which is broadly in line with members' capital subscriptions. Key decisions require the support of “members not expected to borrow,” who together hold around 35% of voting shares. This percentage includes highly rated non-regional members, the largest being Germany (4.2% voting share), France (Aa2 stable, 3.2%) and the UK (Aa2 negative, 2.9%). Much of the remainder is comprised of regional members not expected to borrow, including high-income economies such as Korea (3.5%), Australia (Aaa stable, 3.5%), Hong Kong (Special Administrative Region)(Aa3 stable, 0.8%), New Zealand (Aaa stable, 0.6%), and Singapore (Aaa stable, 0.4%). However, China holds an effective veto with its 26.6% voting share.

Among Group of 20 (G-20) leading economies, only the US (Aaa stable), Japan (A1 stable) and Mexico (Baa1 negative) are not members. Argentina (Ca stable), Brazil (Ba2 stable) and South Africa (Ba1 negative) have successfully applied for membership, although their respective national ratification processes have yet to be completed. Aside from the US, all of Aaa-rated sovereigns have attained membership.

Developing institutional capacity and policy framework

Our rating reflects an assessment of AIIB's current and future creditworthiness, as the institution ramps up its operations over the next five to 10 years. We look, in particular, at how its standalone credit metrics will evolve against the development of its governance.

AIIB's management envisions two distinct phases in the bank's development: a startup phase through 2020, followed by a growth phase through to 2027. The startup phase focused on building institutional capacity, including staffing, establishing governance and promoting a distinct culture. During this phase, the bank's need to borrow has been low because of its large base of paid-in capital and the lag between loan approvals and disbursements. The lag reflects the long implementation periods associated with infrastructure projects. In the growth phase, loan disbursements are likely to accelerate and borrowing is likely to expand to meet liquidity needs. In the absence of a general capital increase, the expansion of the organization and the bank's balance sheet are likely to stabilize beyond 2027.

Since its establishment, AIIB has made rapid progress on staffing and on the design, formalization and refinement of its governance framework and risk management architecture. It revised its original risk management framework in late 2016 to incorporate the use of economic capital to measure risk across all its activities (see description in section on capital adequacy). In addition, the subsequent introduction of a risk appetite statement and stress testing procedures operationalizes the bank's policy mandate to maintain solvency and grow its balance sheet with adequate buffers against severe shocks.

In 2018, the bank approved an enhanced accountability framework to be phased in from the beginning of 2019. Among other changes, this has turned the investment committee into a voting body that requires unanimous approval. AIIB also expanded its treasury function ahead of its maiden debt issuance earlier in 2019 and in anticipation of more active management of its treasury holdings, particularly to diversify away from a predominance of bank deposits.

Our credit assessment does not encompass the activities of special funds administered by AIIB. That includes the Special Fund for Project Preparation, which AIIB established in 2016 to provide member governments with technical assistance to prepare projects for its consideration. According to AIIB's founding documents, its ordinary resources, which include its borrowings, income and capital, may only be used to finance its ordinary operations excluding activities under the purview of the Project Preparation Fund or any other special fund that may be subsequently established.

In April 2020, AIIB announced a COVID-19 Crisis Recovery Facility to react to the fast-evolving COVID-19 situation, which demonstrates the bank's adaptability and responsiveness to its clients' changing needs tackling external shocks. The facility will operate only during the 18 months to 16th October 2021, reflecting the temporary nature of the increased flexibility that the bank would provide.

Credit profile

» Our determination of a supranational's rating is based on three rating factors: capital adequacy, liquidity and funding and strength of member support. For Multilateral Development Banks, the first two factors combine to form the assessment of intrinsic financial strength. Additional factors that can impact the intrinsic financial strength, including risks stemming from the operating environment or the quality of management, are also considered. The strength of member support is then incorporated to yield a rating range. For more information please see our Supranational Rating Methodology.

Capital adequacy score: aa1

Factor 1: Capital adequacy

Scale	aaa	aa1	aa2	aa3	a1	a2	a3	baa1	baa2	baa3	ba1	ba2	ba3	b1	b2	b3	caa1	caa2	caa3	ca	c	
+		Assigned																				-

Sub-factor scores

Capital position	aaa
Development asset credit quality	a
Asset performance	aaa

Capital adequacy assesses the solvency of an institution. The capital adequacy assessment considers the availability of capital to cover assets in light of their inherent credit risks, the credit quality of the institution's development assets and the risk that these assets could result in capital losses.

Note: In case the Adjusted and Assigned scores are the same, only the Assigned score will appear in the table above.

AIIB's "aa1" capital adequacy score reflects its large capital base and our expectation – driven by the continued development and implementation of a rigorous risk management framework – that the bank over the next decade will maintain low leverage, moderate development asset credit quality and robust asset performance consistent with its presumed preferred creditor status. The bank's strong capital position suggests ample capacity to absorb losses and weather near-term challenges to the credit quality of some of its current investments.

Paid-in capital subscriptions largely met

AIIB was founded with a subscribed capital base of $100 billion. According to its articles of agreement, capital subscriptions are scheduled to be paid in five equal installments, such that the initial subscription of $20 billion of paid-in capital will be largely fulfilled by 2019 and completed by 2024. In 2019, paid-in capital received increased to $18.6 billion from $14.8 billion in 2018, with another $700 million pledged, for a total of $19.3 billion. Over the first three months of 2020, members remitted an additional $200 million, bringing paid-in capital received to $18.8 billion.

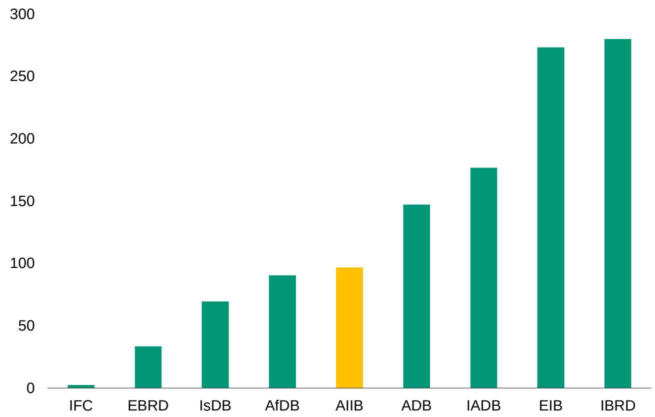
Both total capital subscriptions see (Exhibit 1) and paid-in capital as a proportion of subscribed capital (see Exhibit 2) are already higher than for some more established Aaa-rated MDBs. Subscribed capital, which includes both paid-in and callable capital, amounted to $96.7 billion as of the end of 2019, up from $96.3 billion in 2018.

With the addition of three new prospective members since September 2019, AIIB now has 103 approved members. The countries approved for membership include Liberia, Croatia (Ba2 positive) and Senegal (Ba3 negative).

Exhibit 1

AIIB's subscribed capital is larger than some more established MDBs

Subscribed capital in $ billion, 2019

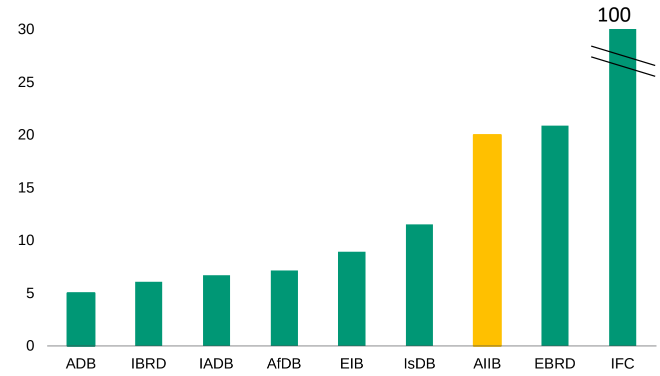


IFC=International Finance Corporation; EBRD=European Bank for Reconstruction and Development; IsDB = Islamic Development Bank; AfDB = African Development Bank; ADB = Asian Development Bank; IADB = Inter-American Development Bank; EIB = European Investment Bank; IBRD = International Bank for Reconstruction and Development.
Source: Moody's Investors Service

Exhibit 2

AIIB has a high proportion of paid-in capital relative to total subscribed capital

Paid-in capital as a % of subscribed capital, 2019



Source: Moody's Investors Service

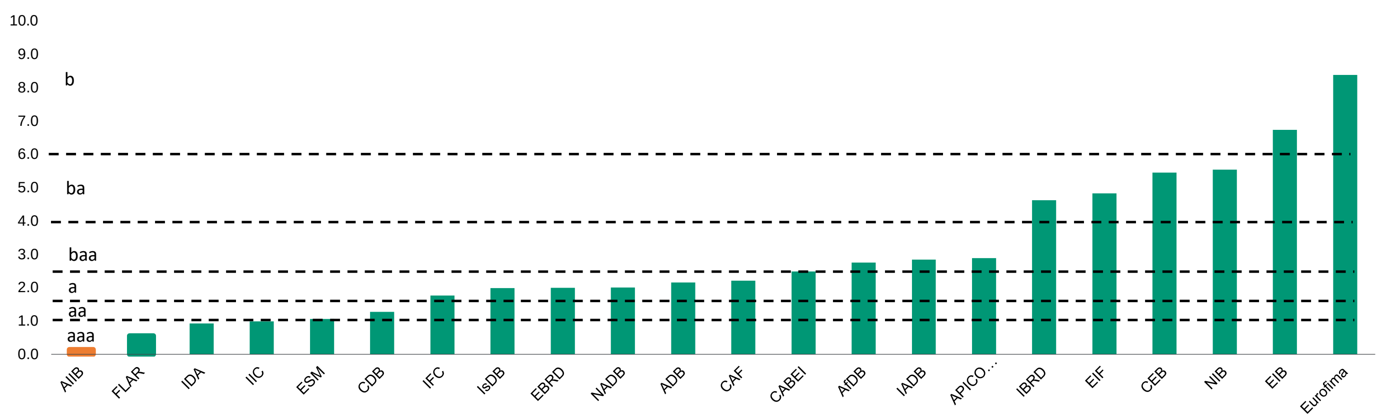
Capital position subfactor score – "aaa"

We use the leverage ratio to measure an MDB's capital position, comparing the size of its development-related assets and treasury assets rated A3 and below against its usable equity. AIIB's leverage ratio is the lowest among its rating peers (see Exhibit 3) because of its combination of a large capital base at establishment and a relatively limited portfolio of outstanding development assets, although the latter has grown rapidly over the past three years.

Exhibit 3

AIIB's leverage ratio is the lowest among the Aaa-Aa3 rated MDBs

Leverage ratio, %, 2017-19 average



Source: Moody's Investors Service

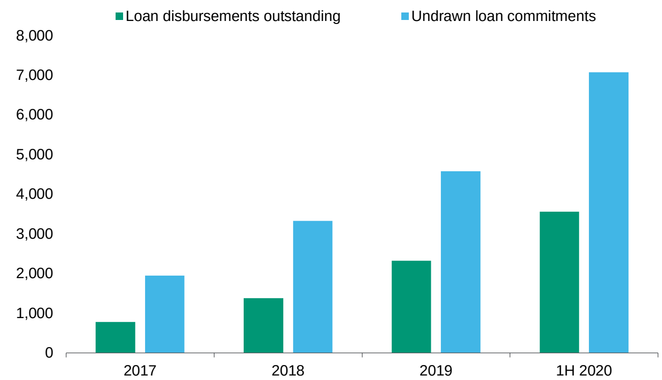
The bank's investment operations continue to gather pace with gross loan disbursements outstanding increasing to $2.3 billion in 2019 from around $1.4 billion in 2018 (see Exhibit 4). The implementation of COVID-19 Crisis Recovery Facility further accelerated the already rapid growth of investment operations, with disbursed loans standing at $3.6 billion in the first half of 2020.

Cumulative project approvals rose to $19.8 billion as of August in 2020 from $12.04 billion in 2019 and $7.5 billion in 2018. Reflecting the ongoing maturation of its investment operations and the larger volume of project approvals, undrawn loan commitments also grew rapidly to $7.1 billion in the first half of 2020 from $4.6 billion in 2019 and $3.3 billion in 2018.

Exhibit 4

Investment operations increased substantially year on year in the past three years

$ millions

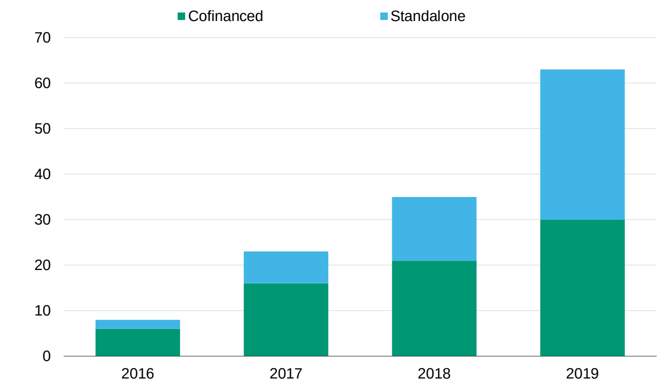


Sources: AIIB and Moody's Investors Service

Exhibit 5

Standalone projects outpaced cofinanced projects

Number of approved projects, cumulative year-end figures



Sources: AIIB and Moody's Investors Service

Projects cofinancing with other large MDBs, including the ADB, EBRD and IBRD, have aided the rise in AIIB's development exposure in the context of its relatively small number of staff. By 2019, the cofinanced proportion had shrunk to less than half of the bank's total projects, while standalone projects increased significantly (see Exhibit 5). The bank approved 28 projects worth $4.5 billion in investments in 2019, with 19 standalone projects and nine cofinanced projects.

Geographical diversification has improved as the bank's development exposure grows. The bank's three largest country exposures are to Azerbaijan (Ba2 stable), India and China as of the end of 2019.

Equity investments remain small compared with the bank's total development-related assets. Outstanding equity investments include investment into the India Infrastructure Fund, and the International Finance Corporation's (IFC, Aaa stable) Emerging Asia Fund.

Apart from its direct lending and equity investment exposures, AIIB has also established a $500 million Asia ESG Enhanced Credit Managed Portfolio to invest in corporate bonds as a way to catalyze private investment into infrastructure with a strong environment, social and governance (ESG) focus.

At the outset of the bank's operations, AIIB has sought to finance infrastructure on a large scale. However, it has sharpened its strategic focus in the past two years with the board of directors approving a number of sector-specific strategies, including sustainable energy (first approved in June 2017, amended April 2018); the mobilization of private capital (February 2018); transportation (September 2018); sustainable cities (December 2018); and water strategy (May 2020). The bank also approved its Digital Infrastructure Strategy in June 2020. The operationalization of these strategies has been apparent in the patterns of project approvals, with the bank expecting investments in energy and transport to represent between 60%-70% of total exposure.

Reflecting the expansion of AIIB's membership, as well as demand for infrastructure finance beyond Asia, the bank has also started lending to non-regional members with the approval of projects to Egypt (B2 stable). Unlike other MDBs, which differentiate between their members in their eligibility to receive financing, AIIB explicitly authorized investments in any member, regional or non-regional, in its founding articles of agreement. Nevertheless, the board of directors approved a Strategy on Financing Operations in Non-Regional Members in February 2018 that imposes a ceiling on non-regional exposure "to preserve the Asian character of the institution and to ensure sufficient availability of financing for its regional members." This ceiling is currently set at 15% of total approved bank financing.

Growth in AIIB's portfolio of development assets will be guided by both a statutory limit specified in the articles of agreement and its risk management framework. In AIIB's Articles of Agreement, the total outstanding amount of loans, equity investments, guarantees and other types of financing provided by the bank should not exceed the total amount of unimpaired subscribed capital, reserves and retained earnings. This 1:1 ratio incorporates callable capital, whereas our calculation of the leverage ratio includes only paid-in capital.

Because paid-in capital comprises 20% of AIIB's total capital base, its leverage ratio can be no higher than 5x, which corresponds to a “ba” score for the leverage subfactor. In practice, however, we expect leverage will remain much lower in the context of the bank's internal rules on capital adequacy.

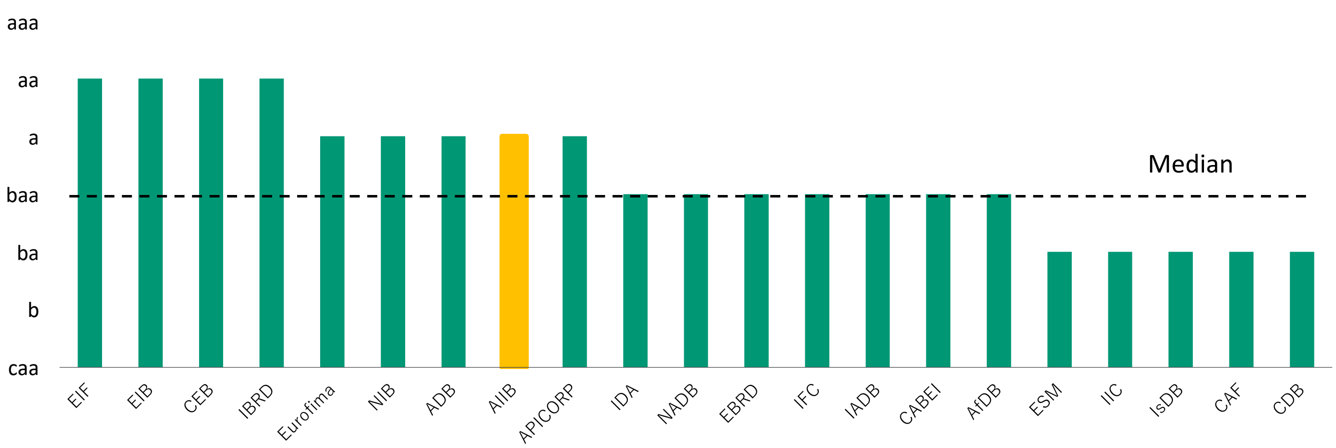
The risk management function uses the concept of “economic capital” as a tool to quantify the amount of risk inherent in AIIB’s operations. Against the backdrop of the statutory limit noted above, the framework determines the minimum amount of capital required for the bank to remain solvent and maintain a credit profile comparable with Aaa-rated peers. This minimum amount, or economic capital, is defined by the AIIB as the “capital AIIB is required to hold to protect its net asset value from falling below zero after a worst-case fair-value loss over one year, with the worst case posing an extreme event with a minimum probability of 1:10,000”. The bank determines an additional buffer through stress testing, which in turn is added to economic capital to arrive at an even more prudent requirement, which must not exceed its level of “available capital”.

There are also other considerations concerning the consumption of capital. Available capital also needs to exceed economic capital plus planned required capital in any subsequent three-year period, according to planned lending.

Developing asset credit quality subfactor score — “a”

AIIB’s development asset credit quality subfactor score of “a” incorporates a forward-looking view that the bank's portfolio of loans, equity investments, and treasury holdings is likely to expand in line with parameters that mitigate credit risk, lower concentration risk and preserve asset performance. At present, AIIB's development asset credit quality score is above the median for Aaa-Aa3 rated MDBs (see Exhibit 6).

Exhibit 6
AIIB's development asset credit quality is above the median for Aaa-Aa3 rated MDBs (2019)



Source: Moody's Investors Service

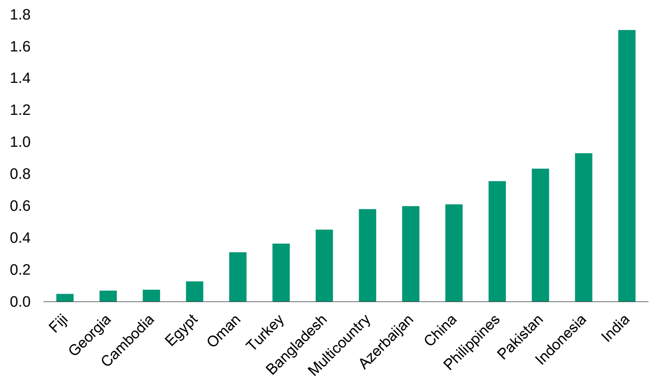
At the outset of its operations, AIIB's portfolio of development assets was concentrated in lower-rated credits, with its weighted average borrower rating (WABR) of B3 in 2016 reflecting outstanding loan disbursements to Pakistan and Tajikistan (B3 negative) only.

Subsequently, in line with progress on the execution of approved projects, AIIB's WABR has risen gradually to Ba2 in 2019; a gas pipeline project backed by Azerbaijan was the bank's largest outstanding exposure. Partly due to the implementation of COVID-19 Crisis Recovery Facility, loan disbursements have accelerated in the first eight months of 2020, with the largest exposure being India, Indonesia (Baa2 stable), Pakistan and the Philippines (Baa2 stable)(see Exhibit 7).

We expect that the deterioration in sovereign credit quality due to the impact of the coronavirus outbreak will add substantial pressure on AIIB's WABR. So far in 2020, large borrowers including India, Turkey, and Oman have been downgraded, though these downgrades have been partly offset by the rapid growth in projects in higher-rated jurisdictions such as Indonesia, China and the Philippines (see Exhibit 8). However, we expect that the bank's lending activities will continue to incorporate larger exposures to higher-rated sovereigns, helping to maintain the current WABR of its sovereign-backed portfolio at or above the target of Ba2 specified in AIIB's risk limits policy.

Exhibit 7

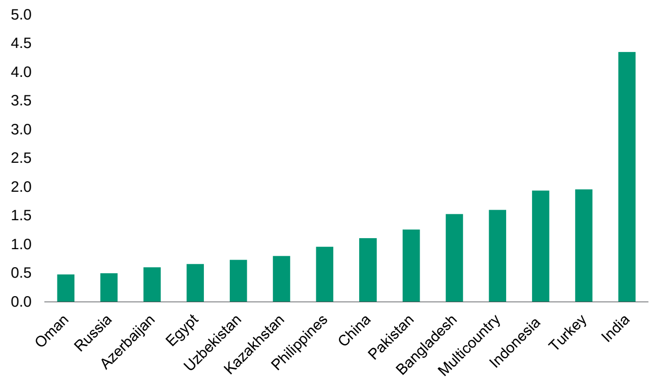
India has received the largest amount of disbursed loans
$ billions, August 2020



Sources: AIIB

Exhibit 8

... and India has also seen the most approved loans
$ billions, as of August 2020



Source: AIIB

Because of AIIB's infrastructure-development mandate, the bank has a heavy concentration within a single asset class. Although AIIB has approved a number of nonsovereign projects, including investments in managed funds, the sectoral concentration still skews heavily to sovereign exposure. Similarly, despite lending to clients and sovereigns part of the Gulf Cooperation Council (GCC) – which the Articles of Agreement consider to be part of Asia – and Egypt, regional and top 10 exposures are heavily concentrated.

Over time, given similar membership in terms of borrower eligibility, AIIB's country concentration should be close to that of the ADB as the former expands its development activities to more countries.

Asset performance subfactor score — "aaa"

Through its first four years of operations, AIIB has neither recorded any nonperforming loans nor incurred any realized losses on its equity investments. As lenders are likely to treat the bank in line with other MDBs that we consider to have preferred creditor status, we expect AIIB's asset performance to remain strong, even as its portfolio of loans expands significantly over the next few years. In particular, we project AIIB's lending portfolio to eventually encompass a similar set of borrowing countries as the ADB and exhibit similar borrower quality and asset performance. We assess asset performance of both the ADB and AIIB as "aaa".

The Articles of Agreement entered into by AIIB's members are modeled after those of other MDBs and spell out the obligations of shareholders, including borrowing members. We therefore consider the conditions of membership to be similar, if not identical, to those of other MDBs.

AIIB's implementation of a strong risk management framework, which encompasses origination, means we do not expect the bank to experience high losses before its preferred creditor status is tested.

Liquidity and funding score: aa2

Factor 2: Liquidity and funding

Scale	aaa	aa1	aa2	aa3	a1	a2	a3	baa1	baa2	baa3	ba1	ba2	ba3	b1	b2	b3	caa1	caa2	caa3	ca	c	
+			Assigned																			-

Sub-factor scores

Liquid resources	aaa
Quality of funding	aa

An entity's liquidity is important in determining its ability to meet its financial obligations. We evaluate the extent to which liquid assets cover net cash flows over the coming 18 months and the stability and diversification of the institution's access to funding.
Note: In case the Adjusted and Assigned scores are the same, only the Assigned score will appear in the table above.

AIIB's "aa2" liquidity and funding score reflects our expectation that the bank will strictly adhere to its conservative liquidity policy and that its access to market funding will strengthen over time.

Liquid resources subfactor score - "aaa"

AIIB holds ample liquid resources to cover loan disbursements, debt servicing and other potential cash outflows.

We measure the availability of liquid resources by comparing projected net outflows over the next 18 months to discounted liquid assets. The composition and size of a supranational institution's liquid assets are important indicators of its capacity to readily sell assets to offset a deterioration in its cash inflows or access to funding. Liquid assets comprise cash, deposits with a term of less than one year held by financial institutions rated Baa3 or higher, treasury assets rated A2 or higher and committed credit lines with a maturity greater than 18 months.

AIIB's liquidity policy is in line with, and in some cases more stringent than, those of rating peers. It requires the maintenance of liquidity portfolio in excess of 40% of the projected net cash flow requirements for the coming 36 months. In practice, actual liquidity levels will be maintained significantly higher than the required policy level to provide flexibility for meeting operational cash flow and in accessing funding markets. In addition, AIIB maintains an adequate stock of high-quality liquid assets to meet potential liquidity requirements for a 30-day stress scenario and its Risk Appetite Statement requires that, in the case of extreme stress, it can meet its payment obligations even in the absence of market access for a period of 12 months.

By comparison, the net cash requirements for ADB and AfDB typically cover 100% of projected needs for 12 months. The requirement for the European Investment Bank (EIB, Aaa stable) is even less at 25% of net cash outflow needs, although our assessment of EIB's strong liquidity position is supported by its access to the European Central Bank's liquidity operations, among other mitigants. Regardless of specific policy requirements, Aaa-rated MDBs typically maintain liquid resources well above their estimated net cash outflows corresponding to "aaa" or "aa" scores for their liquidity position.

AIIB's adherence to its liquidity policy ensures an availability of liquid resources score no lower than "aa."

Quality of and structure of funding subfactor score – "aa"

In addition to availability of liquid resources, we also take into account an MDB's ability to raise funds. AIIB formally commenced its borrowing program in May 2019 with a $2.5 billion five-year bond at a fixed coupon of 2.25%. The deal attracted over $4.4 billion in orders from over 90 investors worldwide representing 27 countries, in line with our previous assumption of favorable access to debt capital markets.

In December 2019, AIIB launched its Global Medium-Term Note Program with which the associated payment obligations are direct, unsecured obligations of AIIB ranking pari passu with all its other unsecured and unsubordinated obligations.

In line with our view of the evolution of a strong funding franchise, AIIB's issuance activities have taken off in 2020; the global medium-term notes, representing drawdowns from the program, were issued in various currencies, including Russian ruble (RUB 2 billion), Thai baht (THB 350 million), Hong Kong dollar (HKD 1,175 million), Turkish lira (TRY 1,360 million), and Chinese yuan (CNY 700 million) as of the end of September 2020.

Although the bank has received large amounts of paid-in capital and it has no ostensible borrowing need, we expect regular issuance as AIIB further expands its investor base. As the bank has established hedging mechanisms, loans are denominated in any currency in which the bank can efficiently hedge itself.

The investor base for AIIB's debt issuance resembles that of the ADB, including Asian central banks and institutional investors in other jurisdictions with portfolio allocations for highly rated Asian exposure. AIIB projects that most of its funding will come from markets and investors outside of China, aided by the regulatory treatment of its debt issuance for the purpose of assessing bank capital requirements. Specifically, the Basel Committee on Banking Supervision has assigned a zero risk weight for AIIB in line with that for long established and highly rated MDBs, such as the ADB, AfDB, EBRD and IADB.

Qualitative adjustments

Qualitative adjustments to intrinsic financial strength

Adjustments	
Operating environment	0
Quality of management	0

The capital adequacy and liquidity and funding factors represent the key drivers of our assessment of an institution's intrinsic financial strength (IFS). However, assessments of the operating environment and the quality of management are also important components of our analysis. To capture these considerations, we may adjust the preliminary IFS outcome that results from the capital adequacy factor and the liquidity and funding factor. The result of this analysis is the adjusted IFS outcome.

Because of its short track record of operation, we have not applied a positive adjustment for AIIB's quality of management. Nevertheless, we assess the bank's operational capabilities and governance frameworks to be evolving in a manner consistent with the highest-rated MDBs. Our evaluation of the quality of AIIB's risk management framework, and the quality and diversity of its loan and investment portfolio, rests on the assumption that AIIB will retain full operational autonomy from its largest shareholders including China, and that its operational strategy will remain broadly focused on infrastructure development across a wide range of emerging markets. Full autonomy also implies immunity from expropriation, moratoriums and capital account restrictions.

Among recent changes in AIIB's risk management framework has been the introduction of an annual risk appetite statement in 2018, which integrates an overarching view of risks associated with the bank's various activities according to the economic capital methodology and allocates risk accordingly. The bank also introduced an Asset Liability Management Policy in December 2017 that supersedes the previous liquidity policy, the borrowing, liability management and derivatives policy, and portions of the risk management policy pertaining to currency and interest-rate risks.

To manage the implementation of approved projects, AIIB approved a policy in December 2018 emphasizing its commitment to its Environmental and Social Framework (ESF) that was adopted at the founding of the organization. The bank highlights that because the ESF was implemented before lending operations commenced, it has screened and assessed every development asset for its environmental and social soundness and sustainability. Therefore, AIIB's has no legacy assets that do not meet it current criteria for ESG considerations.

Billing itself as the first MDB to begin operations after the Paris Agreement Under the United Nations Framework Convention on Climate Change (the 'Paris Agreement'), the bank has further operationalized its ESF by regularly publishing reports on individual projects' compliance with the environmental and social measures called for by their corresponding loan agreements. Environment and social risk is embedded within the risk management framework as approved in the annual risk appetite statement (it is considered "low appetite" in terms of risk allocation). The use of the economic capital framework allows for the integration of environment and social risk in stress testing.

In addition to its overarching policies, the bank has developed and refined a set of directives that operationalizes its risk management framework and ensures compliance with risk requirements and the risk appetite statement. In the first few months of 2019, it approved specific directives on the management of liquidity risk, market risk, operational risk and anti-money laundering/ combating the financing of terrorism.

Strength of member support score: Very High

Factor 3: Strength of member support

Scale	Very High	High	Medium	Low	Very Low
+	Assigned	Adjusted			-

Sub-factor scores

Ability to support	**baa1**
Willingness to support: Contractual	**aaa**
Willingness to support: Non-contractual	**Very High**

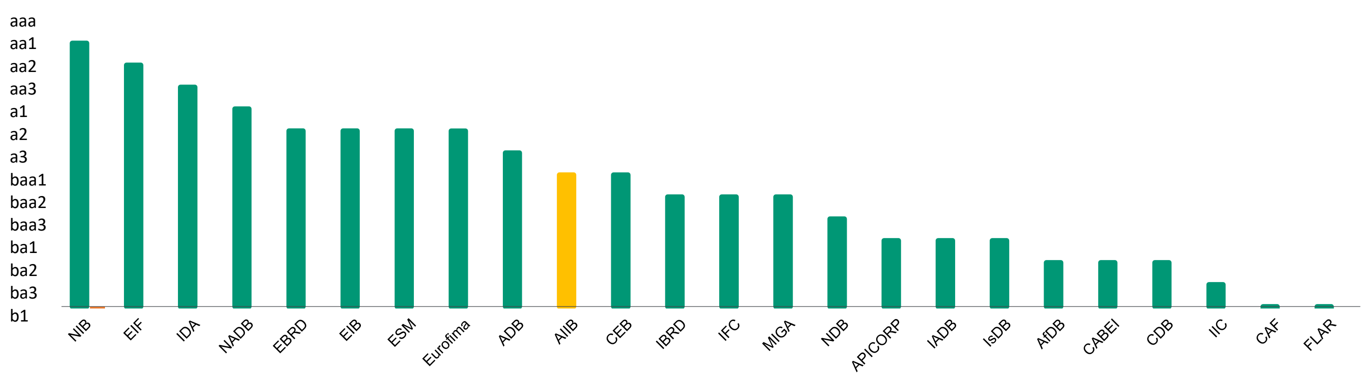
Shareholders' support for an institution is a function of their ability and willingness. Ability to support is reflected by the shareholders' credit quality. Willingness to support takes into consideration (1) the members' contractual obligations that primarily manifest in the callable capital pledge, a form of emergency support, and (2) other non-contractual manifestations of support to the institution's financial standing and mission. Strength of member support can increase the preliminary rating range determined by combining factors 1 and 2 by as many as three scores.

We have adjusted our score for AIIB's strength of member support to Very High from a scorecard-indicated outcome of High. This adjustment reflects the stronger ability of China and the bank's non-borrowing members, which together comprise about 70% of capital subscriptions, to provide support than that is currently implied by the weighted average shareholder rating of the total membership base.

Ability to support subfactor score – "baa1"

Our assessment for ability to support is based on a weighted average shareholder rating (WASR) of "baa1" in 2019, unchanged from the previous year, as the sovereign rating downgrades of Turkey offset the upgrades for Russia (Baa3 stable), Malta (A2 stable), and Greece (B1 stable) over 2019. The addition of new, lower-rated members does not materially affect our assessment given their comparatively small shareholdings. The stable outlooks on the ratings of most large regional and non-regional members impart support for the WASR at its current level (see Exhibits 9 and 10). In 2020, the downgrade for India, AIIB's second largest shareholder, and near-term challenges to the credit quality of some of other AIIB's members because of the global coronavirus impact put strain on the WASR. However, we do not expect any substantial deterioration in the WASR.

Exhibit 9
AIIB members' ability to provide support is broadly in line with Aaa-Aa3 rated MDBs
Weighted average shareholder rating, 2019



Sources: AIIB and Moody's Investors Service

Exhibit 10

Stable outlooks on most of AIIB's top shareholders support the weighted average shareholder rating

Country	Subscribed Capital, $ Billion, end-2019	% Grand Total, end-2019	Sovereign Issuer Rating, end-2019
China	29.8	30.8	A1 stable
India	8.4	8.7	Baa2 negative Baa3 negative (Jun 2020)
Russia	6.5	6.8	Baa3 stable
Germany	4.5	4.6	Aaa stable
Korea	3.7	3.9	Aa2 stable
Australia	3.7	3.8	Aaa stable
France	3.4	3.5	Aa2 positive Aa2 stable (Feb 2020)
Indonesia	3.4	3.5	Baa2 stable
United Kingdom	3.1	3.2	Aa2 negative
Turkey	2.6	2.7	B1 negative B2 negative (Sep 2020)
Top 10 Shareholders	69.0	71.3	
Weighted Average Shareholder Rating			Baa1

Sources: AIIB, Moody's Investors Service

Willingness to support: Contractual subfactor score – "aaa"

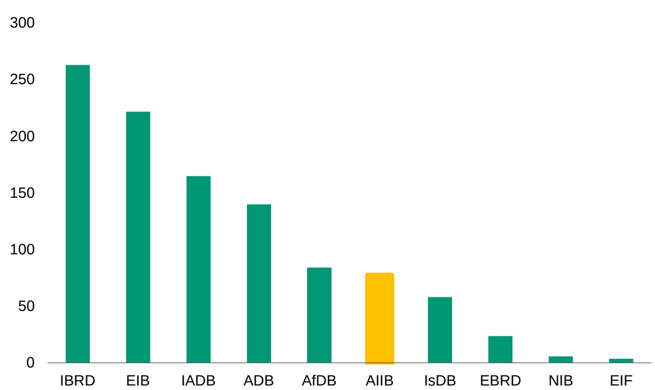
To assess the potential effectiveness of callable capital as a support mechanism, we calculate the ratio of callable capital/total debt. Over 2019, AIIB added around $300 million in addition to its already formidable stock of callable capital. The "aaa" contractual support score incorporates the size of callable capital pledged by its members, both in absolute terms (see Exhibit 11) and as a proportion of debt outstanding (see Exhibit 12).

Shareholders' current and future commitment to AIIB is illustrated by the high level of paid-in and callable capital to which shareholders have subscribed. We expect that AIIB will abide by statutory requirements that limit the size of its development portfolio to the sum of its unimpaired subscribed capital, reserves and retained earnings. This would obviate the need for shareholder support beyond that furnished by callable capital.

Exhibit 11

At its founding, AIIB's stock of callable capital was significant compared with other regional Aaa-rated peers

$ billion, 2019



Source: Moody's Investors Service

Exhibit 12

... and its stock of callable capital to debt is high compared with Aaa-rated peers

Callable capital/total debt, 2019

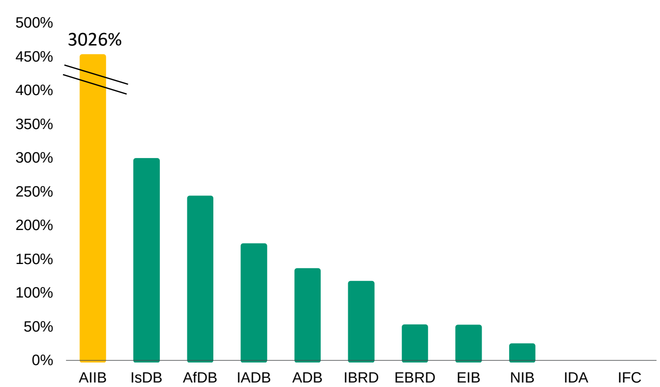


Figure shown for AIIB reflects callable capital and gross borrowings as of June 2019.
Source: Moody's Investors Service

Willingness to support: Non-contractual subfactor score – Very High

We also assess AIIB's non-contractual support at Very High. We believe that there is a strong likelihood that shareholders with a strategic interest in sustaining the bank's operations will provide extraordinary support beyond committed amounts represented by callable capital. This is particularly true for China given its role in founding AIIB and its large shareholding.

In addition, AIIB's broad shareholder base – at 103 approved countries, its membership is larger than that of some other Aaa-rated regional MDBs – mitigates concentration risks arising from economic and financial linkages that could impede the provision of extraordinary support in the event of need.

Membership in the bank can be seen as a financial investment that transcends related geopolitical considerations. Amid territorial disputes in the South China Sea, for example, claimants such as Malaysia(A3 stable) the Philippines and Vietnam (Ba3 negative) have retained their membership despite periodic bilateral tensions with China. Similarly, despite tensions related to projects under China's Belt and Road Initiative (BRI), Malaysia, the Maldives (B3 negative) and Sri Lanka (Caa1 stable) have also continued to engage AIIB. India, AIIB's largest borrower and its second-largest shareholder, has thus far declined to join the BRI, while many of the bank's non-borrowing members have been critical of the Chinese initiative.

ESG considerations

How environmental, social and governance risks inform our credit analysis of Asian Infrastructure Investment Bank

We take account of the impact of environmental, social and governance (ESG) factors when assessing supranational issuers' credit profile. In the case of AIIB, the significance of ESG to the credit profile is as follows:

Environmental risks are not significant for AIIB's rating, as the bank's credit profile is unlikely to be affected despite generally high environmental risks in the region. Moreover, AIIB has set high targets for operations on environmental initiatives with sustainable infrastructure being one of the three thematic priorities.

Social risks are not significant for AIIB's rating, amid the relative social and political stability in the region and the diversification of its portfolio. We regard the coronavirus pandemic as a social risk under our ESG framework because of the substantial implications for public health and safety. We expect that the outbreak of the coronavirus will lead to a temporary weakening of economic and fiscal strength across the Asia-Pacific, which could lead to a temporary deterioration in asset quality and performance. However, we do not see the impact as significant to the AIIB's credit profile for now.

AIIB's sound governance framework is illustrated by its prudent risk-management policies, and high standard governance principles.

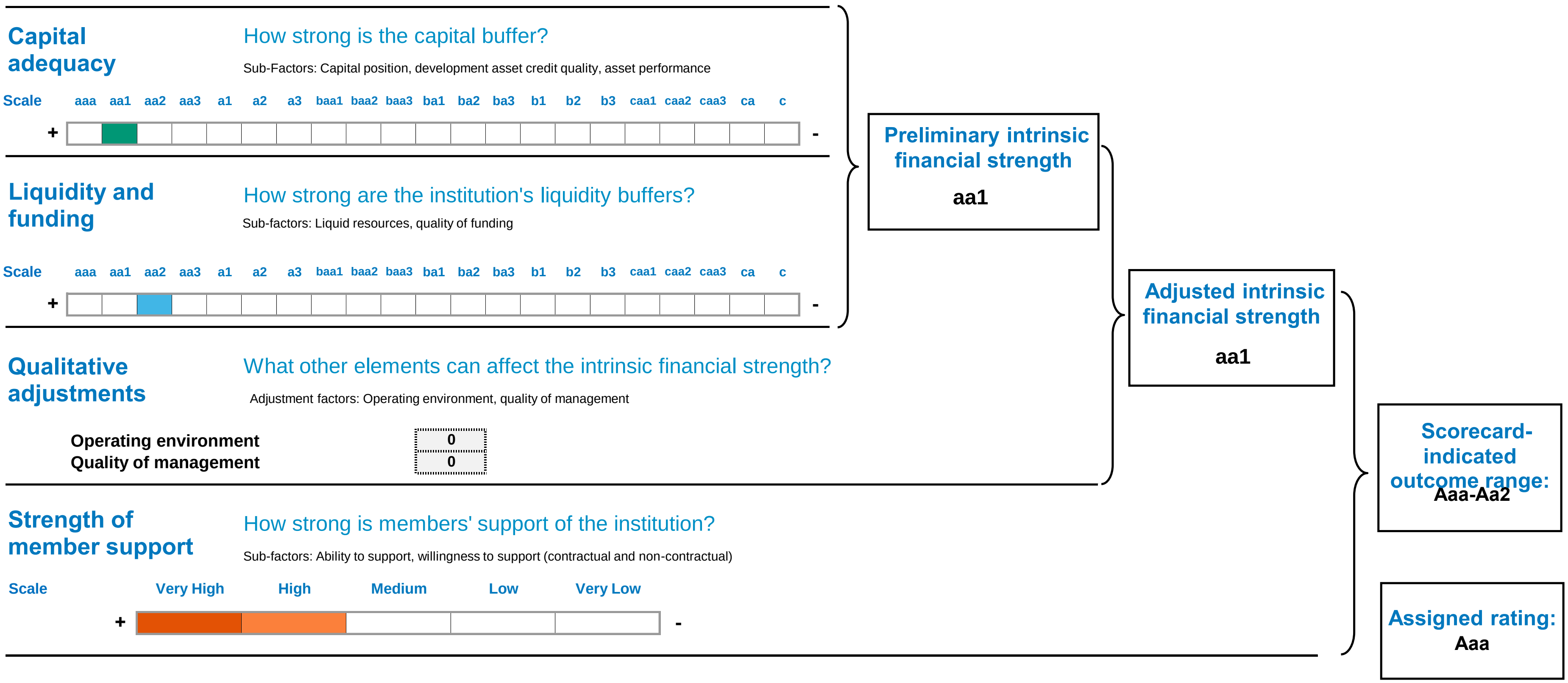
All of these considerations are further discussed in the "Credit profile" section above. Our approach to ESG is explained in our cross-sector methodology General Principles for Assessing ESG Risks. Additional information about our rating approach is provided in our Supranational Rating Methodology.

Rating range

Combining the scores for individual factors provides an indicative rating range. While the information used to determine the grid mapping is mainly historical, our ratings incorporate expectations around future metrics and risk developments that may differ from the ones implied by the rating range. Thus, the rating process is deliberative and not mechanical, meaning that it depends on peer comparisons and should leave room for exceptional risk factors to be taken into account that may result in an assigned rating outside the indicative rating range. For more information please see our Supranational Rating Methodology.

Exhibit 13

Supranational rating metrics: Asian Infrastructure Investment Bank (AIIB)



Source: Moody's Investors Service

Comparatives

This section compares credit relevant information regarding AIIB with other supranational entities that we rate. It focuses on a comparison with supranationals within the same rating range and shows the relevant credit metrics and factor scores. AIIB's strong capital adequacy, even among Aaa-rated peers, primarily reflects the large amount of equity relative to its existing portfolio of development assets, although we expect a degree of convergence versus peers over time. Moreover, the bank is likely to share preferred creditor status with other highly rated peers, bolstering its asset performance. AIIB's short track record of access to capital market financing accounts for its relative positioning for liquidity and funding than its peers, while our assessment of Very High strength of member support is on a par with other more established MDBs.

Exhibit 14

Asian Infrastructure Investment Bank compare with key peers

	Year	AIIB [1]	ADB	AfDB	IADB	IsDB	NADB	Aaa Median
Rating/Outlook		**Aaa/STA**	**Aaa/STA**	**Aaa/STA**	**Aaa/STA**	**Aaa/STA**	**Aa1/STA**	
Total assets (US$ million)	2019	21,883	221,866	48,387	136,358	32,598	2,007	87,937
Factor 1: Capital adequacy		**aa1**	**aa3**	**baa1**	**a1**	**a3**	**a3**	
DRA / Usable equity[2] [3] [5]	2019	12.2	223.9	298.6	287.0	172.0	190.6	255.5
Development assets credit quality score (year-end)	2019	a	a	baa	baa	ba	baa	baa
Non-performing assets / DRA[2]	2019	0.0	0.1	2.7	0.4	1.0	1.1	0.4
Return on average assets[5]	2019	2.2	0.8	0.2	1.0	1.1	1.5	0.7
Net interest margin (X)[5]	2019	1.8	1.0	1.4	1.3	3.0	2.1	1.2
Factor 2: Liquidity and funding		**aa2**	**aa1**	**aa1**	**aa1**	**aa1**	**a1**	
Quality of funding score (year-end)	2019	aa	aaa	aaa	aaa	aa	a	aaa
Liquid assets / ST debt + CMLTD[4][5]	2019	--	201.5	--	187.9	258.2	295.2	201.5
Liquid assets / Total assets[5]	2019	89.2	18.5	35.3	25.2	30.0	37.5	29.5
Preliminary intrinsic financial strength (F1+F2)		**aa1**	**aa2**	**a1**	**aa2**	**aa3**	**a2**	
Adjusted intrinsic financial strength		**aa1**	**aa1**	**aa3**	**aa1**	**aa3**	**a2**	
Factor 3: Strength of member support		**VH**	**VH**	**VH**	**VH**	**H**	**VH**	
Weighted average shareholder rating (year-end)	2019	baa1	a3	ba2	ba1	ba1	a1	--
Callable capital / Total debt	2019	3,025.6	132.9	240.3	170.0	296.1	392.2	132.9
Callable capital (CC) of Baa3-Aaa members/Total CC[5]	2019	90.3	91.6	48.3	66.9	49.3	100.0	90.9
Scorecard-indicated outcome range (F1+F2+F3)		**Aaa-Aa2**	**Aaa-Aa2**	**Aaa-Aa2**	**Aaa-Aa2**	**Aaa-Aa2**	**Aa1-Aa3**	

[1] AIIB excludes paid-in capital receivables from usable equity and total assets
[2] Development-related assets
[3] Usable equity is total shareholder's equity and excludes callable capital
[4] Short-term debt and currently-maturing long-term debt
[5] Ratio not used in Scorecard
Source: Moody's Investors Service

Data and references

Rating history

Exhibit 15

Asian Infrastructure Investment Bank [1]

	Issuer Rating		Senior Unsecured	Outlook	
	Long-term	Short-term			Date
Outlook Assigned	--	--	--	STA	Jun-17
Rating Assigned	Aaa	P-1	--	--	Jun-17

Notes: [1] Table excludes rating affirmations. Please visit the issuer page for AIIB for the full rating history.
Source: Moody's Investors Service

Annual statistics

Exhibit 16

Asian Infrastructure Investment Bank

Balance Sheet, USD Millions	2013	2014	2015	2016	2017	2018	2019
Assets							
Cash & Equivalents	0	0	0	3,574	6,991	10,476	14,978
Securities	0	0	0	3,180	3,236	3,293	4,546
Other current assets	0	0	0	1	2	2	53
Net Loans	0	0	0	10	773	1,365	2,273
Net Equity Investments	0	0	0	0	19	33	30
Other Assets	0	0	0	11,031	7,952	4,394	751
Total Assets	**0**	**0**	**0**	**17,795**	**18,973**	**19,562**	**22,632**
Liabilities							
Borrowings	0	0	0	0	0	0	2,557
Derivative Liabilities	0	0	0	0	0	0	0
Other Liabilities	0	0	0	6	14	50	88
Total Liabilities	**0**	**0**	**0**	**6**	**14**	**50**	**2,645**
Equity							
Subscribed Capital	0	0	0	89,826	95,001	96,340	96,718
Less: Callable Capital	0	0	0	72,262	76,001	77,072	77,375
Less: Other Adjustments	0	0	0	0	0	0	0
Equals: Paid-In Capital	0	0	0	18,065	19,000	19,268	19,344
Retained Earnings (Accumulated Loss)	0	0	0	7	119	315	658
Accumulated Other Comprehensive Income (Loss)	0	0	0	0	0	0	0
Reserves	0	0	0	-283	-160	-70	-16
Other equity	0	0	0	0	0	0	0
Total Equity	**0**	**0**	**0**	**17,790**	**18,959**	**19,512**	**19,986**

Note: Assets may not equal the sum of liabilities and equity as shown due to rounding.
Source: Moody's Investors Service

Exhibit 17
Asian Infrastructure Investment Bank

Income Statement, USD Millions	2013	2014	2015	2016	2017	2018	2019
Net Interest Income	**0**	**0**	**0**	**23**	**124**	**251**	**400**
Interest Income	0	0	0	23	124	251	436
Interest Expense	0	0	0	0	0	0	35
Net Non-Interest Income	**0**	**0**	**0**	**175**	**193**	**173**	**148**
Net Commissions/Fees Income	0	0	0	0	-1	13	12
Income from Equity Investments	0	0	0	0	0	0	0
Other Income	0	0	0	175	194	160	136
Other Operating Expenses	**0**	**0**	**0**	**31**	**56**	**85**	**126**
Administrative, General, Staff	0	0	0	31	56	85	126
Grants & Programs	0	0	0	0	0	0	0
Other Expenses	0	0	0	0	0	0	0
Pre-Provision Income	**0**	**0**	**0**	**168**	**261**	**339**	**423**
Loan Loss Provisions (Release)	0	0	0	0	9	40	22
Net Income (Loss)	**0**	**0**	**0**	**167**	**252**	**300**	**401**
Other Accounting Adjustments and Comprehensive Income	0	0	0	0	0	0	0
Comprehensive Income (Loss)	**0**	**0**	**0**	**167**	**252**	**300**	**401**

Source: Moody's Investors Service

Exhibit 18
Asian Infrastructure Investment Bank

Financial Ratios	2013	2014	2015	2016	2017	2018	2019
Capital Adequacy, %							
DRA / Usable Equity	--	--	--	0.1	7.2	9.4	12.2
Development Assets Credit Quality (Year-End)	--	--	--	--	--	a	a
Non-Performing Assets / DRA	--	--	--	0.0	0.0	0.0	0.0
Return On Average Assets					2.8	2.3	2.2
Net Interest Margin	--	--	--	0.3	1.1	1.7	1.8
Liquidity, %							
Quality of Funding Score (Year-End)	0.0	0.0	0.0	0.0	--	aa	aa
Liquid Assets / ST Debt + CMLTD	--	--	--	--	--	--	--
Liquid Assets / Total Debt	--	--	--	--	--	--	763.5
Liquid Assets / Total Assets	--	--	--	99.5	92.8	90.7	89.2
Strength of Member Support, %							
Weighted Average Shareholder Rating (Year-End)	0.0	0.0	0.0	A3	Baa1	Baa1	Baa1
Callable Capital / Gross Debt	--	--	--	--	--	3,084.9	3,025.6
Callable Capital (CC) of Baa3-Aaa Members/Total CC	-	-	-	84.9	83.7	83.7	90.3

Note: Usable equity is total shareholders' equity and excludes callable capital and paid-in capital receivables. Liquid assets include cash and securities.
Source: Moody's Investors Service

Moody's related publications

» Moody's assigns program (P)Aaa to AIIB's Global Medium-Term Note Program, 18 December 2019

» Supranationals – Global: Stress-testing confirms broad resilience of MDB ratings, 1 September 2020

» Supranational issuers – Global: FAQ on MDB credit quality in the context of the coronavirus outbreak, 13 May 2020

» Multilateral Development Banks and Other Supranational Entities, 25 June 2019

To access any of these reports, click on the entry above. Note that these references are current as of the date of publication of this report and that more recent reports may be available. All research may not be available to all clients.

Related websites and information sources

» Sovereign and supranational risk group web page

» Sovereign and supranational rating list

» Asian Infrastructure Investment Bank web page

»

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Endnotes

1 See Supranational issuers - Global: FAQ on MDB credit quality in the context of the coronavirus outbreak, May 2020

This publication does not announce a credit rating action. For any credit ratings referenced in this publication, please see the ratings tab on the issuer/entity page on www.moodys.com for the most updated credit rating action information and rating history.

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