MOODY'S RATINGS

Rating Action: Moody's Ratings changes the outlook on CAF to positive, affirms the ratings at Aa3

30 May 2025

New York, May 30, 2025 -- Moody's Ratings (Moody's) has today changed the outlook to positive from stable on Corporacion Andina de Fomento (CAF) and affirmed the long-term issuer rating at Aa3. CAF's foreign currency senior unsecured rating has also been affirmed at Aa3, as well as its foreign-currency senior unsecured shelf and MTN programs at (P)Aa3. Its short-term foreign currency commercial paper rating, backed foreign currency commercial paper rating and other short-term ratings have been affirmed at P-1, while its foreign currency other short-term rating has been affirmed at (P)P-1.

The change in outlook to positive from stable reflects the broadening of CAF's shareholder base and associated improvement in its capitalization. By the end of 2025, CAF will likely have 24 member countries, compared to 15 in 2022. In combination with the 2022 capital increase, the inflow of capital payments has improved CAF's capital position while the broader membership base will also support the diversification of CAF's development assets. Secondly, CAF's declining exposure to Venezuela supports asset performance and has contributed to lower cost of funding, which we expect will be maintained going forward.

The affirmation of the Aa3 rating reflects CAF's very strong liquidity and funding profile that benefits from its well-established presence in international bond markets and strong liquidity position, as well as strong capital adequacy with moderate leverage and robust asset performance. Our assessment of member support is constrained by CAF's relatively low amount of callable capital, mitigated by a demonstrated willingness to support the institution as illustrated by regular capital contributions from its membership base. While CAF's loan book remains somewhat concentrated when compared to higher-rated MDBs, it continues to rapidly diversify its lending portfolio.

RATINGS RATIONALE

RATIONALE FOR THE CHANGE IN OUTLOOK TO POSITIVE

CAF CONTINUES STRENGTHENING ITS CAPITAL BUFFERS AND DIVERSIFYING MEMBERS AND ASSETS

A rapid expansion of CAF's membership is supporting increased capital contributions and further diversification of assets. The incorporation of new members since 2023 has strengthened CAF's mandate in the region, its capital base and is helping to drive business diversification in various areas. By 2024 the shareholder base expanded to 22 countries, while in 2025 one new member has joined CAF such that there are 23 member countries represented in the Board of Directors. The incorporation of new members in 2023-25 has yielded over $3 billion in pledged capital contributions. This expanded membership alongside the $7 billion 2022 general capital increase that is to be fully allocated to paid-in capital, have led to a steady inflow of capital, providing a predictable inflow of cash to support balance sheet growth that is likely to continue in 2025 and 2026. The expansion of CAF's membership also reflects the solid shareholder support for CAF's mandate and its growing importance in the region, enabling the bank to expand its operations while maintaining robust credit metrics. As a result, the bank's leverage ratio improved to 225.1% in 2024 from 235.2% in 2023.

In addition to the capital contributions, strong profitability in recent years is further enhancing capital growth, more than offsetting the consumption of Venezuela's shares that have now been exhausted. The strong profitability is likely to continue in 2025 and 2026, albeit marginally lower, as global interest rates are likely to remain near current levels or ease slightly.

There has been an improvement in CAF's portfolio and shareholder credit quality that will likely continue in 2025. Since December 2023, overall sovereign credit quality in Latin America has improved. By the end of 2024, the share of investment grade loan exposure had increased to 40% from 31% at the end of 2023. At the same time, CAF's exposure to Venezuela continued to decline in 2024, both in terms of loans outstanding and Venezuela's equity stake. Also, CAF recently agreed a first Exposure Exchange Agreement (EEA) that will help to further diversify the bank's lending portfolio and management is actively exploring other credit enhancements to further support asset credit quality.

DECLINING EXPOSURE TO VENEZUELA SUPPORTS ASSET PERFORMANCE AND HAS CONTRIBUTED TO LOWER COST OF FUNDING

The total amount of loans outstanding to Venezuela declined to $1.9 billion at year end 2024 from a peak of over $3.7 billion in 2019, the year prior to when CAF began repurchasing Venezuela's shares and applying the proceeds to Venezuela's debt service. Venezuela's equity stake was reduced to $1.7 million out of CAF's total paid-in capital of $5.8 billion (0.03% of paid-in capital). CAF's increased capital buffers and quicker balance sheet growth will decrease the relative weight of the Venezuela portfolio such that we now see non-performing assets peaking at approximately 3% of the total development portfolio in 2030 as the remaining Venezuela loans mature, down from our prior forecast of 4%. The declining exposure to Venezuela has contributed to a lower cost of funding.

CAF's cost of funding relative to that of higher-rated MDBs has decreased, which will support interest margins and buffer its quality of funding. The spread on CAF's US dollar bonds has tightened continuously since early 2024 as CAF's presence in global markets solidifies. As a frequent issuer of large denomination bonds, CAF's debt instruments are some of the most liquid among Aa-rated supranational issuers. The spread on most of CAF's US dollar bonds has narrowed by 32-50 basis points since the beginning of 2024. Similarly, the spread on CAF's bonds to those of Aaa-rated Supranational issuers has also narrowed from approximately 80 basis points in 2024 to 40 basis points. This compression in the relative cost of funding will allow CAF's lending to remain competitive, keeping interest expense in check, and is likely to support interest margins and profitability, such that capital growth can remain apace.

RATIONALE FOR THE AFFIRMATION OF CAF'S RATING AT Aa3

The affirmation of the Aa3 rating reflects CAF's robust intrinsic financial strength that is underpinned by its very strong liquidity and funding profile, and its favorable capital adequacy. We expect that CAF will maintain an ample liquidity buffer, as it has done over many years, over-complying with its liquidity policy of holding a minimum of 12 months of net cash requirements, given that in practice CAF continued to hold over 24 months of net cash outflows at the end of 2024, in line with the liquidity buffers kept by most highly rated Supranational institutions. This prudent practice suggests that even in a stress case in which the bank would be unable to access financial markets, it could continue to cover its expenses, loan disbursements and debt service for a period of two years. The bank's liquidity is also supported by its strong market access, diversified investor base by type and geography, as well as the various markets it can tap and various types of bonds it issues, including sustainable instruments.

CAF's strong capital buffers are reflected by its modest leverage, sound growth and robust asset performance. The bank's leverage – measured as the ratio of its (development-related assets + treasury assets rated A3 or lower) to equity – reached 225.1% and remained well in line with the median for Aa-rated Supranational entities. Asset performance remains solid with NPAs remaining well below 1% of development assets. Our assessment of member support is constrained by CAF's relatively low amount of callable capital but underpinned by a demonstrated willingness to support the institution as illustrated by regular capital contributions from its membership base. We expect that the bank will continue to balance loan growth with adequate liquidity and capital buffers, while successfully managing credit risks from its operating region as CAF expands its operations.

ENVIRONMENTAL, SOCIAL AND GOVERNANCE CONSIDERATIONS

CAF's credit impact score (CIS-2) indicates that ESG risks are not material to the rating. This reflects sound governance and a low exposure to social risks, that offset a moderate exposure to environmental risk. This assessment also reflects CAF's proactive policies to contain credit risks from uneven economic performance throughout its operating region.

CAF's environmental issuer profile score (E-3) reflects carbon transition risks through its lending exposure within hydrocarbon-producing countries in Latin America. These risks affect CAF's balance sheet indirectly given that CAF has had a longstanding commitment to developing sustainable projects, including hydroelectric generation and clean energy. Exposure to other environmental risks remains contained, reflecting CAF's diversified lending exposures throughout Latin America.

CAF's social issuer profile score (S-2) reflects a strong track record of customer relations that has helped the institution grow its member base and lending portfolio substantially. CAF's public consultation processes are an integral part of its lending decisions and include affected communities and key stakeholders, which supports our assessment of responsible production.

CAF's governance issuer profile score (G-2) reflects its prudent risk management and the proactive approach to dealing with problematic loan exposures, in line with sector best practices. The bank continually explores credit enhancement tools to mitigate risks from possible shocks.

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

CAF's rating could be upgraded if the observed improvements to date continued as expected. Specifically, we expect the sustained capital contributions to lead to a gradual decline in CAF's leverage as well as a continued diversification of the loan portfolio. An improvement in CAF's weighted average shareholder rating that signals increased member support or a proven improvement in asset credit quality through continued exposure exchange agreements, other credit enhancements or improving sovereign credit quality, would also support improved creditworthiness.

The outlook could be reverted back to stable if CAF was to face a strong deterioration in asset quality due to credit events involving borrowers other than Venezuela, jeopardizing the balanced growth that has led to a gradual strengthening of its credit profile.

Downward credit pressure would arise if CAF were to experience an erosion of its capital and liquidity buffers due to a rapid expansion of its loan book not sufficiently compensated for by additional capital contributions.

The principal methodology used in these ratings was Multilateral Development Banks and Other Supranational Entities published in February 2024 and available at https://ratings.moodys.com/rmc-documents/414557. Alternatively, please see the Rating Methodologies page on https://ratings.moodys.com for a copy of this methodology.

The weighting of all rating factors is described in the methodology used in this credit rating action, if applicable.

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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