Research Update:

The OPEC Fund For International Development Ratings Affirmed At 'AA/A-1+'; Outlook Positive

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Overview

- We consider the OPEC Fund for International Development's (the OPEC Fund) recent addition of supplementary lending envelopes to address food security and climate change could enhance its ongoing expansion agenda and strengthen its overall developmental impact over 2022-2025.
- That said, we believe that elevated macroeconomic risks, still-high geopolitical uncertainty, and erratic financial markets could test the execution of the OPEC Fund's expansion plans in 2023. The OPEC Fund has yet to establish itself in the capital markets, having delayed its expected entry to public benchmark funding to 2023.
- At this point, however, we assess that the multiple dimensions of the Russia-Ukraine conflict have not impacted the fund's asset quality, with the stability underpinned by a continued adherence to preferred creditor treatment (PCT) and high degree of risk mitigation for non-sovereign lending.
- We therefore affirmed our 'AA/A-1+' ratings on the OPEC Fund.
- The positive outlook reflects our view that the OPEC Fund's extremely strong financial profile, risk-averse management team, and planned entry in the public capital markets could allow it to become a dynamically disbursing and more relevant development institution, without assuming unnecessary risk.

Rating Action

On Dec. 22, 2022, S&P Global Ratings affirmed its 'AA/A-1+' long- and short-term issuer credit ratings on the OPEC Fund for International Development (the OPEC Fund). The outlook remains positive.

Outlook

The positive outlook reflects our view that the OPEC Fund could solidify its developmental relevance and strengthen its policy relationship with shareholders over the next 12 months if the bank successfully executes under its revamped expansion agenda in a turbulent market. The positive outlook assumes that the institution's financial risk profile will remain extremely strong, and that the OPEC Fund will manage financial risks prudently as it begins to leverage its balance sheet and meaningfully access market funding in 2023.

Upside scenario

We could raise the rating if the OPEC Fund's development impact and public policy role strengthened sustainably. We would expect this scenario to entail continued dynamic lending growth and for the fund to establish a presence in public capital markets, supporting its increased disbursements. Confirmed engagements from shareholders, for example a reduction in capital arrears from key members or an expansion of the institution's membership base, would also increase the likelihood of an upgrade.

Downside scenario

We revise our outlook to stable if the OPEC Fund's expansion agenda underwhelms or if we observed a meaningful reduction in the shareholder's support toward the OPEC Fund, for example if shareholders lessened their interest in the policy function of the OPEC Fund to focus their developmental ambitions through other channels. In addition, although unlikely, pressures on its financial risk profile or an erosion of the OPEC Fund's very strong PCT could also result in us revising the outlook to stable.

Rationale

The affirmation reflects our assessments of the OPEC Fund's strong enterprise risk profile and extremely strong financial risk profile. Our assessment of the OPEC Fund's strong enterprise risk profile is anchored by our PCT assessment. By policy, the OPEC Fund does not write off or reschedule sovereign loans. Myanmar was the only sovereign with arrears in the past decade, corresponding to less than 0.4% of outstanding sovereign exposures. We consider the OPEC Fund's PCT status to be well-tested. Over 2011-2022, nine sovereigns defaulted to commercial lenders (most recently Sri Lanka in 2022) while continuing to pay the OPEC Fund, reflecting its established role and position in the global development finance space.

We continue to believe that the OPEC Fund's policy relevance could strengthen sustainably if the entity builds a track record under its ongoing expansion agenda. We understand that the OPEC Fund's revamped near-term growth plan includes a meaningful step-up in loan book growth this year, with continued dynamic disbursements over 2023-2025. If successfully executed, we estimate that the OPEC Fund's outstanding loans could increase to close to 12% in 2022 and settle at a growth rate of almost 10% per year over the next three years, extending the loan book to €6.5 billion by 2025, up from €4.5 billion at year-end 2021. These growth rates would mark a comprehensive step-up compared with the annual average of 4.5% growth in outstanding loans over the past three years.

That said, we believe the elevated global macroeconomic risks, still-heightened geopolitical uncertainty, and erratic financial markets could present risks to the OPEC Fund's expansion. Even so, we consider these risks largely mitigated by the OPEC Fund's extremely strong financial risk profile that we believe gives the bank the possibility to expand its lending footprint while providing flexibility to adapt to adverse market conditions. We note that the OPEC Fund has delayed its anticipated entry to the wholesale public funding markets to 2023, owing to the market volatility exhibited since the war in Ukraine commenced in February 2022. It has instead leaned on its substantial liquidity to satisfy the majority of its disbursements in 2022. The fund placed its inaugural funding transaction in December 2022, with a $50 million private placement marking its debut transaction. Even so, we believe the OPEC Fund will have to establish itself in the public markets in the first half of 2023, to not lose momentum for its lending expansion.

Importantly, we have not seen any impact on OPEC Fund's asset quality following the back-to-back crisis scenarios over the last three years, with the bank's nonperforming loans (NPLs) declining to 1.5% of the total loan portfolio in June 2022, from 2.2% one year prior. In our view, the OPEC Fund's risk-management policies are conservative and all current NPLs relate to the non-sovereign portfolio. We believe the OPEC Fund's very strong track record of PCT and high degree of risk mitigation for non-sovereign lending will continue to help the bank mitigate the multiple dimensions of the Russia-Ukraine conflict. We understand that the OPEC Fund targets the largest loan growth in the years ahead in the sovereign portfolio, with the non-sovereign portfolio slated to remain below 30% of total loans, which we believe will help mitigate asset-quality concerns.

We also recognize that the OPEC Fund in 2020 separated its concessional lending into a Special Capital Resources (SCR) window, which provides long-term and low-cost loans to the least developed partner countries. This separation helps to de-risk the engagements financed by the existing capital resources of the OPEC Fund, named Ordinary Capital Resources (OCR), under which the fund deploys financing to developing countries with greater economic development and to private-sector clients. These windows are kept separate, and we view OCR as not bearing any liability for SCR's activities. Our ratings are therefore based on the OPEC Fund's OCR only.

We view the OPEC Fund's introduction of supplementary lending envelopes to address food security and climate change as key frameworks strengthen its overall developmental impact over the medium term. More specifically, the bank has committed $1.0 billion toward imminent food security needs in partner countries and a $5.0 billion framework for climate action, on top of its regular energy-related lending, to be executed within its Climate Change Action Plan through 2030. We recognize that these initiatives are part of a broader mobilization exercise within the Arab Coordination Group, a body that coordinates the efforts of regional and international financial institution, in which the OPEC Fund has played a leading role. We view the fund's strengthening role as a catalyst to broader mobilization to further support its developmental relevance.

We believe the need for developmental assistance and demand for OPEC Fund services within its partner regions and countries could increase significantly over the next couple of years on the basis of both near- and medium-term factors. Over the near term, there are acute needs to provide food security, due to for example disrupted grain supply chains from the war in Ukraine, while the medium term will require substantial assistance in adaptation to climate change and transition to sustainable energy production. We therefore consider that the demand for OPEC Fund's developmental financing will be substantial over the medium to longer term.

Overall, we consider the OPEC Fund to benefit from adequate shareholder commitment and support of its activities. Ownership is concentrated, with three countries holding 64% of the shares, led by Saudi Arabia at 35.2% at year-end 2021. We note that the OPEC Fund's shareholders rank lower in terms of World Bank transparency and governance indicators than those of peer multilateral lending institutions (MLIs). That said, we consider it key that none of the shareholders borrow from the fund, since we believe this mitigates the risk of potential political influence over lending decisions.

Throughout the history of the OPEC Fund, the shareholders have shown their support toward the institution with four general capital increases (GCI) since its inception. However, currently 11% of the fourth GCI payments stands in arrears, including from main shareholder countries. The meaningful level of capital arrears from key shareholders weighs on our assessment of shareholder support. In this regard, we also acknowledge a wide discrepancy in financial strength and capacity across the limited group of shareholders. We consider that some shareholders' weak financial positions could constrain their ability to support the OPEC Fund.

The OPEC Fund's credit standing is underpinned by its extremely strong financial risk profile, largely supported by our assessment of its extremely strong capital. As of June 30, 2022, the OPEC Fund's risk-adjusted capital (RAC) ratio stood at 81% (using rating parameters as of Nov. 9, 2022), incorporating adjustments specific to MLIs. The OPEC Fund's RAC ratio is higher than that of most other MLIs and benefits from geographical and sectoral diversification as well as the PCT adjustments. Capitalization is supported by very high levels of equity, considering that the OPEC Fund held no debt liabilities on its books in June 2022.

The OPEC Fund currently has no funding gap, with assets outnumbering liabilities by 80x. This reflects that the OPEC Fund's funding structure as of June 2022 consisted only of capital contributions and retained earnings. Although a very conservative financing structure, the institution lacks a track record of market funding, which will require effort to establish.

We expect the OPEC Fund to start tapping the public funding markets in 2023. The fund has an operational global medium-term note program and has board approval to put a euro commercial paper program in place, when required, for bridge financing purposes. We anticipate the buildup of debt to be gradual and that debt to equity will remain substantially below the 150% policy limit over the medium term. We forecast the RAC ratio will remain comfortably above our 23% threshold for an extremely strong capital position based on the current expansion plans, suggesting that the capital position will remain a pillar of the institution's financial risk profile.

On Dec. 1, 2022, the OPEC Fund placed a $50 million private placement, marking its debut-funding transaction. However, the OPEC Fund's postponement of benchmark-sized funding to 2023 means the fund has tapped into its liquidity holdings to finance its dynamic disbursements for 2022. We project that the net growth in outstanding loans will increase by €500 million in 2022, the majority financed by drawdowns of the OPEC Funds treasury assets. Even so, today its six- and 12-month liquidity ratios surpass our threshold for a strong liquidity assessment, at 1.76 and 1.26x, respectively, proving that its current cash inflows and securities holdings (after 'AAA' stress scenario haircuts) comfortably exceed its scheduled disbursements. We expect the OPEC Fund's liquidity to remain solid as it expands the liability side of its balance sheet over 2023. We also expect the OPEC Fund to calibrate its financial policies as it expands its capital market activity over the next two years.

The OPEC Fund does not have callable capital and, therefore, we don't give any additional support over the SACP.

The OPEC Fund for International Development Ratings Score Snapshot

Issuer credit rating	AA/Positive/A-1+
SACP	aa
Enterprise risk profile	Strong
Policy importance	Strong
Governance and management	Adequate
Financial risk profile	Extremely strong
Capital adequacy	Extremely strong
Funding and liquidity	Strong
Extraordinary support	0
Callable capital	0
Group support	0
Holistic approach	0

SACP--Stand-alone credit profile.

Related Criteria

- Criteria | Governments | General: Multilateral Lending Institutions And Other Supranational Institutions Ratings Methodology, Jan. 31, 2022
- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021
- 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: Principles Of Credit Ratings, Feb. 16, 2011

Ratings List

Ratings Affirmed	
The OPEC Fund For International Development	
Sovereign Credit Rating	
Foreign Currency	AA/Positive/A-1+

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. A description of each of S&P Global Ratings' rating categories is contained in "S&P Global Ratings Definitions" at https://www.standardandpoors.com/en_US/web/guest/article/-/view/sourceId/504352 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

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