Research Update:

Black Sea Trade And Development Bank 'A-' Ratings Affirmed; Outlook Positive

July 17, 2019

Overview

- The Black Sea Trade and Development Bank (BSTDB) is delivering on its recent strategic move to increase lending to public infrastructure.
- The bank’s heightened focus on public-sector lending has the potential to improve its contribution to economic development and regional cooperation.
- However, we believe execution risks remain and any strengthening of BSTDB’s relevance and policy role in 2019-2022 would be gradual.
- We are affirming our ‘A-/A-2’ ratings on BSTDB and maintaining our positive outlook.

Rating Action


Rationale

The ratings are based on our assessments of BSTDB’s extremely strong financial and moderate enterprise risk profiles. Although the bank’s financial strength underpins the ratings, credit constraints stem from its policy role and the overall relevance of its funding contribution. This reflects its modest balance sheet of about €2 billion, which limits policy relevance compared with peers.

In February 2019, BSTDB’s board of governors approved a 2019-2022 business plan to extend its funding contribution and expand its disbursement levels through heightened direct funding of the real economy via sovereign-sponsored infrastructure projects. We believe this is an important inflexion point for bank and has the potential to strengthen its policy role, but there are also key execution risks.

Specifically, we view the bank’s strategic shift to public-sector lending as posing risks to
profitability in a highly competitive market, with other multilateral lending institutions (MLIs) and national development banks present. Furthermore, if not successfully executed, the plan could signal a deterioration of the institution's policy relevance. If BSTDB proved unable to meaningfully increase funding for the public sector, while deemphasizing the private sector, this would diminish its policy importance and overall relevance, in our view.

We also believe there are risks to the sustainability of BSTDB's financial risk profile, due to instances of heightened macroeconomic stress in countries where it operates. These include stress faced by the Turkish private sector, which accounts for almost 10% of BSTDB's total lending. We conceptualize these two risks in our holistic analysis, leading to a negative one-notch adjustment to our assessment of the bank's stand-alone credit profile.

Under its recently approved medium-term strategy plan, BSTDB is increasing its public-sector lending. We understand it has granted a €160 million loan to a Greek state-owned transmission utility company in first-half 2019, with additional sovereign-focused business in the immediate pipeline. Transactions in excess of €100 million are large for an entity of BSTDB's size and can quickly transform its loan book. We cannot exclude that the proportion of sovereign-related loans could extend beyond 25% of total loans (from 15% at year-end 2018) over the coming years. This means we could eventually incorporate considerations of preferred creditor treatment into our enterprise risk profile assessment. If this shift appeared structural, we could re-label BSTDB a public-sector-focused MLI.

Therefore, although we expect the transition to more public-sector-directed lending to be gradual, we will monitor mandate renewal and lending trends over the coming two years. Greater commitment to the public sector will require updated procurement processes, alongside enhanced legal expertise and underwriting competence to engage with the official stakeholders.

The ratings on BSTDB do not include potential extraordinary support from shareholders, since we rate all of BSTDB’s sovereign shareholders lower than the bank. In addition, our view of the bank’s moderate policy importance precludes the notion of extraordinary callable capital support.

Outlook

The outlook is positive because we believe BSTDB’s limited role as a regional supranational could strengthen over the coming two years, thanks to its recently introduced expansion strategy. In addition, we believe that BSTDB’s extremely strong financial profile and competent risk management will carry the bank through challenges linked to the credit quality of private-sector borrowers.

Upside scenario

We could raise the ratings over the next two years if BSTDB's loan disbursements increased under its new mandate, confirming its broader public-policy role, while maintaining its extremely strong financial risk profile. In such a scenario, we would expect higher disbursement levels will amplify BSTDB's support of funding for economic development across its footprint.

Downside scenario

We would revise the outlook to stable if BSTDB is unable to cement its public-policy role over the coming two years, with disbursement levels remaining at lackluster levels. We could take similar action if we observed pressure on the bank's financial risk profile, for example, due to a material
deterioration of its loan portfolio's credit quality, resulting in an accumulation of nonperforming loans and credit-impaired loans. In such a scenario, we would likely reassess our view of the bank's loan underwriting standards and loan book performance, which would weigh on our assessment of the bank's financial risk profile.

Ratings Score Snapshot

Issuer credit rating: A-/Positive/A-2
Stand-alone credit profile: a
Enterprise risk profile: Moderate
- Policy importance: Moderate
- Governance and management expertise: 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: -1

Related Criteria
- Criteria | Governments | General: Multilateral Lending Institutions And Other Supranational Institutions Ratings Methodology, Dec. 14, 2018
- 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
- Criteria Guidance: Multilateral Lending Institutions And Other Supranational Institutions Ratings Methodology, Dec. 14, 2018
- Supranationals Special Edition 2018, Oct. 11, 2018
Ratings List

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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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