GCR RATINGS

**Credit Rating Announcement**

# GCR upgrades Fonds Africain de Garantie et de Coopération Economique (FAGACE) long-term issuer rating to AA(WU) from AA-(WU) on its regional scale. The outlook is Positive.

## Rating Action

Dakar, 29 November 2023 – GCR Ratings (GCR) upgraded Fonds Africain de Garantie et de Coopération Economique (FAGACE) long-term issuer rating to AA(WU) from AA-(WU) on its regional rating scale. The outlook is Positive. Furthermore, GCR affirmed the short-term issuer rating of A1+(WU).

| Issuer | Rating Type | Rating Scale | Rating | Outlook |
|---|---|---|---|---|
| African Guarantee and Economic Cooperation Fund | Long-term Issuer | Regional | AA(WU) | Positive |
| | Short-term Issuer | Regional | A1+(WU) | - |

## Rating Rationale

The rating upgrade of Fonds Africain de Garantie et de Coopération Economique (FAGACE) evidences the improvement of its risk profile as a result of enhanced exposure management practices and efforts to settle off its development-related asset portfolio which enabled to reduce its non-performing asset rate brought to a level comparable to that of its peers. Furthermore, FAGACE has undertaken a process of developing its intervention portfolio to support the delivery of its mandate. The positive outlook stems from the GCR's opinion according to which the FAGACE's rating could be further improved if the Fund succeeds in increasing its equity to strengthen its financial leverage in line with the GCR criteria, while significantly reducing the share of non-performing assets in its intervention portfolio.

GCR observes that since 2021 FAGACE has reinforced its risk management framework by implementing a risk and credit assessment and classification model. Therefore, the quality of the FAGACE's development-oriented asset portfolio has improved, with the non-performing asset rate decreased to 2.5% in September 2023 (2022: 8.3%). This initiative together with the upcoming adoption of policies aimed at identifying and mitigating exposure to various risks as well as the use of credit insurance for its exposures, starting in 2023, are likely to set up a solid foundation for managing intervention-related risk. In this context, despite a foreseen increase in interventions, GCR expects the share of non-performing assets to remain low, around 3%, in the short term over the next 12 to 18 months, thanks to the Fund's incremental steps to strengthen the management of counterparty risk.

The Agency views the FAGACE's capitalisation as very solid, given a good level of the GCR financial leverage (41%), compared to the country risk of the areas where it operates. This robust capitalisation is supported by equity sufficient to cover the current level of the Fund's portfolio. However, GCR anticipates a deterioration in the Fund's capital position from 2023, due to the rapid growth of its intervention portfolio, despite an increase in equity expected in 2024 through the capital subscriptions by new Member-States and institutions. Nevertheless, the pace of equity increase will remain moderate due to the lack of a solid track record regarding paying up of capital (paid-up capital rate of around 45% at the end of 2022), which will only be offset by earnings if the Fund succeeds in generating profitability less volatile than that registered over the last five years and significantly higher than that recorded in 2022.

The FAGACE's liquidity indicators are also very robust, in line with its very conservative investment policy giving priority to liquid investment vehicles. This provides the Fund with significant cushions of liquid assets, a large part of which is available in the short term (18.68% of total assets in 2022). GCR observes that the short-term needs for cash flows do not put pressure on the FAGACE's liquid assets. However, the continuous expansion of the development portfolio is expected to be going hand in hand with a decline in quality of the development-oriented assets and an increasing risk of collateral calls, which will require the Fund to maintain liquidity at a high level. GCR foresees the large part of the Fund's liquid assets to be maintained over the next 12-18 months to meet its cash flow needs.

The FAGACE's credit profile is weakened by the still modest level of its exposures and cumulative approvals concentrated in Côte d'Ivoire (19%), Senegal (21%) and Benin (25%). Moreover, its gross guarantee commitments focus on the five business segments accounting for more than half of its interventions (Agro-industry: 17%, Industry: 16%, Telecommunications: 12%, Energy: 14%, Finance: 12%). The predominance of gross guarantees (above 95% in 2022) exacerbates the weak geographical and sector diversification of the Fund's interventions. This comes with the absence of a clear track record demonstrating the Fund's success in delivering the mandate that it has been entrusted with.

GCR views the FAGACE's management and governance as appropriate, given that they are anchored in its statutes which are those of a multilateral development financial institution. The Fund is entrusted with a strong mandate, aimed at supporting the Member-States' economic development, and has an active commitment to implementing strategies to achieve its objectives. GCR anticipates an improvement in the Fund's management and governance through the FAGACE's measures taken to strengthen its governance bodies. Those include the revision of its fundamental documents and the creation of an additional supervisory body gathering representatives of the four central banks of the Fund's intervention areas.

## Outlook Statement

**The outlook associated with the FAGACE's rating is positive**: The positive outlook stems from the GCR's opinion according to which the FAGACE's rating could be further improved if the Fund succeeds in increasing its equity to strengthen its financial leverage in line with the GCR criteria, while significantly reducing the share of non-performing assets in its intervention portfolio.

## Rating Triggers

**An upgrade of the FAGACE's rating will depend on:** i) improving risk profiles of the countries and/or their financial sectors; reinforcing Member-States' credit profiles; ii) its business profile improving, for example, through a controlled increase in the level of its development-related portfolio supporting the delivery of its mandate; iii) strengthening of its equity likely to back up its capitalisation ratio; or iv) significantly enhancing quality of its portfolio.

**A downgrade of the FAGACE's rating would be the consequence of**: i) deteriorating risk profiles of the countries and/or their financial sectors; ii) worsening Member-States' credit profiles; iii) its business profile deteriorating, for example, through a materially decreasing development-related risk; iv) significantly declining quality of its portfolio, characterised among other things by an increase in the gross deterioration rate of the credit portfolio and/or a rise in its concentration level; v) capitalisation dropping below 15% of the adjusted total assets; or vi) ongoing volatility of profitability and the pursuit of its practices of adjustment to retained earnings.

## Analytical Contacts


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## Related Criteria and Research

Criteria for the GCR Ratings Framework, January 2022
Criteria for Rating Supranational Institutions, January 2022
GCR Rating Scales, Symbols and Definitions, May 2023
GCR Country Risk Scores, August 2023
GCR Sector Risk Scores for the WAEMU Area, September 2023
USD/XOF = 600.9836. Source: Bloomberg, 17 November 2023

## Ratings History

| African Guarantee and Economic Cooperation Fund | | | | | |
|---|---|---|---|---|---|
| Rating Type | Review | Rating Scale | Rating | Outlook | Date |
| Long-term Issuer | Initial | Regional | AA-(WU) | Stable | November 2021 |
| | Latest | Regional | AA-(WU) | Stable | November 2022 |
| Short-term Issuer | Initial | Regional | A1+(WU) | - | November 2021 |
| | Latest | Regional | A1+(WU) | - | November 2022 |

## Risc Score Summary

| **Rating Components and Factors** | |
|---|---|
| **Operating Environment** | **9.00** |
| Country Risk Score | 3.50 |
| Sector Risk Score | 2.75 |
| Strength and Diversity of Shareholders | 1.75 |
| Preferential Treatment | 1.00 |
| **Business Profile** | **(2.25)** |
| Status and Diversification | (1.25) |
| Mandate and Track Record | (1.00) |
| Management and Governance | 0.00 |
| **Financial Profile** | **3.25** |
| Capital Structure and Financial Leverage | 3.00 |
| Risk | (1.75) |
| Refinancing and Liquidity | 2.00 |
| **Comparative Profile** | **0.00** |
| Callable Capital | 0.00 |
| Peer Analysis | 0.00 |
| **Total Score** | **10.00** |

## Glossary

| | |
|---|---|
| Capitalisation | Provision of capital for a business or conversion of income or assets into capital. |
| Cost | What a thing costs; its cost price. |
| Equity | See *Equity Capital* |
| Equity Capital | Capital contributed by shareholders or acquired as a result of the economic activity. |
| Liquidity | Measure of a debtor's ability to repay its debts assuming it continues to operate. |
| Mandate | Power entrusted by a higher authority. |
| Profitability | Relationship between an income obtained or expected and the resources used to generate it. |
| Refinancing | The issue of new debt to replace maturing debt. New debt may be provided by existing or new lenders, with a new set of terms and conditions in place. |
| Subsidiary | A company controlled by another company called a parent company. |

## SALIENT POINTS OF THE ASSIGNED RATING

GCR affirms that a.) no part of the rating process was influenced by any other business activities of the credit rating agency; b.) the ratings were based solely on the merits of the rated entity, security or financial instrument; and c.) these ratings were the result of an independent evaluation of the risks and merits of the rated entity, security or financial instrument.

The credit ratings were communicated to FAGACE. The above ratings were solicited by, or on behalf of, the rated entity, and, therefore, GCR was compensated for providing its rating services.

FAGACE participated in the rating process through virtual meetings and other written correspondence. Furthermore, the quality of the received information was considered adequate and independently verified to the extent possible. The information received from FAGACE and other reliable third parties to assign the credit rating included:

- The FAGACE's financial statements and annual reports for the 2017-2022 period;
- Written presentations regarding detailed elements for the 2017-2022 period;
- Reports of interviews with the management of the rated entity taking place in 2023.

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