Council of Europe Development Bank

AAA STABLE OUTLOOK

Credit strengths

- Excellent asset quality
- Very high liquidity buffers
- Strong shareholders
- Increasing strategic importance

Credit challenges

- High leverage compared to peers

Rating rationale and Outlook:

The Council of Europe Development Bank's (CEB) AAA rating reflects its 'excellent' intrinsic strength and 'high' shareholder support. In detail:

- **Institutional profile:** The CEB benefits from the increasingly strategic role it plays for its shareholder governments and excellent governance. The bank's social mandate – unique among European supranational institutions – has served shareholders well in helping finance their responses to the 2015 refugee crisis, the Covid-19 pandemic, and Russia's war in Ukraine.
- **Financial profile:** The CEB benefits from excellent asset quality with no non-performing loans and high average borrower quality. It also benefits from preferred creditor status for its sovereign exposure and good geographical diversification. The CEB's liquidity profile is exceptionally strong, and its funding profile benefits from strong market access. The bank reports broadly stable annual net profit, allowing it to strengthen its capital base with retained earnings. The main rating challenge is the CEB's high leverage.
- **Shareholder support:** The CEB benefits from highly rated key shareholders (A) and a record of timely shareholder support. The CEB's coverage of assets by callable capital of highly rated shareholders is moderate.
- **Outlook and triggers:** The Stable Outlook reflects a balanced set of risks over the next 12 to 18 months. The ratings/Outlooks could be downgraded if, individually or collectively: i) the CEB records sustained losses leading to a marked deterioration of the capital base; ii) its liquidity buffers are significantly reduced; and/or iii) key shareholders are downgraded.

Figure 1: Our assessment of the CEB's rating drivers

Positive rating-change drivers

- N/A

Negative rating-change drivers

- Losses that reduce the capital base
- Significant reduction in liquidity buffers
- Downgrades of key shareholders

Ratings and Outlook

Foreign currency

Long-term issuer rating	AAA/Stable
Senior unsecured debt	AAA/Stable
Short-term issuer rating	S-1+/Stable

Lead Analyst

Alvise Lennkh, CFA
+49 69 6677389-85
a.lennkh@scoperatings.com

Team Leader

Dr Giacomo Barisone
+49 69 6677389-22
g.barisone@scoperatings.com

Scope Ratings GmbH

Neue Mainzer Straße 66-68
60311 Frankfurt am Main

Phone +49 69 6677389-0

Headquarters

Lennéstraße 5
10785 Berlin

Phone +49 30 27891-0
Fax +49 30 27891-100

info@scoperatings.com
www.scoperatings.com

Bloomberg: SCOP

Credit profile

We determine a capitalised supranational's rating by assessing its intrinsic strength based on its institutional and financial profiles and its shareholder support. We map these two assessments to determine an indicative rating range that can be adjusted by up to one notch to determine the final rating. For details, please see our methodology.

Intrinsic strength – Institutional profile: Very Strong

Scale	**Very Strong**	Strong	Moderate	Weak	Very Weak

When assessing the credit risk of supranationals, we place significant emphasis on the importance of their mandate for their shareholders and associated environmental, social and governance (ESG) considerations.

The CEB's institutional profile is assessed as 'Very Strong'. This reflects its excellent governance and its social development mandate putting the bank at the forefront of promoting social cohesion and integration in Europe. The bank has made important contributions to shouldering the costs of looking after refugees from the war in Ukraine.

Mandated activities

Promoting social cohesion and strengthening social integration

Established in 1956 and owned by 42 shareholders, the CEB is the only European multilateral development bank with an entirely social purpose. In line with this mission, the bank's activity consists of granting loans to co-finance economically and socially viable projects that promote social cohesion across Europe, including in a target group of 22 countries of central, eastern and south-eastern Europe. The bank's total assets amounted to nearly EUR 30bn at end-2021.

Social factors

Activities contribute to 10 of 17 SDGs

The CEB's mandate is to support social cohesion in Europe through the implementation of socially oriented investments. The bank provides funding and expertise for projects with high social impact in its member states, in key areas including social housing, education or healthcare. The bank has also set three priorities for its lending: inclusive growth, support for vulnerable groups and environmental sustainability. The bank has also integrated a set of 10 sustainable development goals, as defined by the United Nations, within its project screening framework, since 2020. The CEB cemented its unique social mandate when in early 2022 the bank became an implementing partner of the European Commission's InvestEU Programme 2021-2027, which should allow the bank to reach new clients and support its development strategy.

Swift response to Covid-19 and Ukraine crisis

Recent crises have bolstered the importance of the bank's social mandate, as it supported EU member states in dealing with emergency situations. Between 2020 and 2021, the CEB approved loans totalling EUR 3.8bn to support pandemic-related projects. These efforts were in part funded through two 'Covid-19 Response Social Inclusion Bonds' (EUR 1.5bn in total) to provide financial support for public healthcare and other pandemic-related measures.

The CEB proved equally supportive in responding to the large flows of refugees resulting from the Russia-Ukraine war, in line with its core mandate. The bank disbursed more than EUR 5m in grants from its 'Migrant and Refugee Fund' to support the most impacted member states in their immediate response to the high flows of refugees. As of June 2022, the bank had approved EUR 1.2bn in loans to help countries hosting displaced persons from Ukraine and issued two social bonds totalling about EUR 2bn. Overall, social factors are strongly incorporated into the CEB's statutory priorities.

Environmental factors

Alignment with Paris Agreement to facilitate green transition

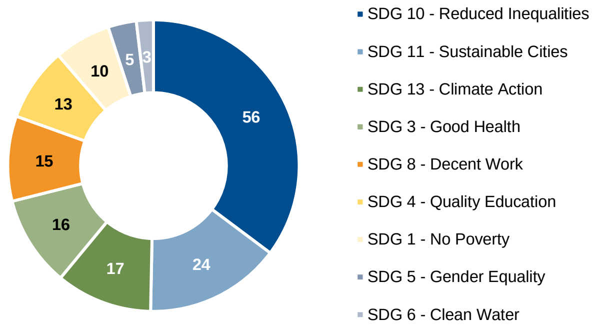
Environmental concerns have gained in importance to the CEB's activities over recent years. The bank carries out annual reviews of its investments and activities to prevent contradiction with its environmental objectives. As part of its 2020-2022 development plan, the bank is committed to align its activities with the goals and principles of the 2015 Paris Agreement on climate change. Making good on this strategy will gradually reduce the risk of stranded assets and the reputational risk of pursuing activities, directly or through counterparties, that are contradictory to the CEB's environmental objectives. The starting point of our analysis is a high-level assessment of the potential environmental risk exposure versus that of its peers.

Low transition and physical risks in line with social mandate

Our assessment looks at the CEB's top 10 countries of operation and uses our transition and physical risk scores at the country level to compare the potential risks across MDBs. Transition and physical risks are low in comparison with similar institutions. The CEB is relatively less exposed to counterparties vulnerable to climate change.

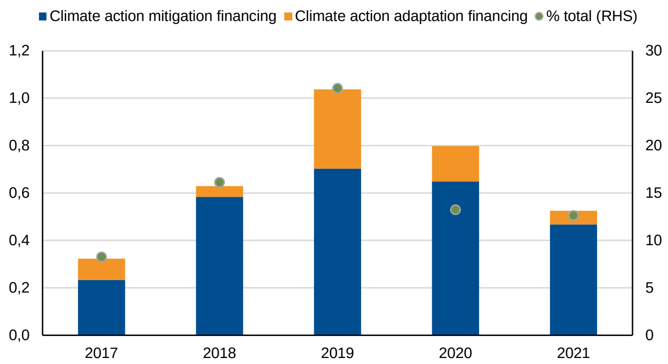
In a second step, we assess mitigating factors, including risk-management policies. Relatively low transition risks are further offset by the gradual enhancement of the CEB's policies to better align its activities with climate change objectives.

Figure 2: Sustainable Development Goals
Number of projects approved for each SDG



Source: CEB, Scope Ratings

Figure 3: Climate finance lending
USD bn (LHS); % of total approved that year (RHS)



Source: CEB, Scope Ratings

Dealing with social inclusion–climate change nexus

The CEB has taken action to define a dedicated approach to align its social mandate and business model with the Paris Agreement as climate change has disproportionate consequences on lower income and vulnerable groups.

Commitments to, involvement in multilateral initiatives

In March 2021, the CEB approved high level principles for a just transition alongside other MDBs, which are expected to incorporate further considerations related to climate change mitigation and resilience into due-diligence processes. Subsequently, the bank signed a statement on 'collective climate ambition' together with nine MDBs during the COP26 in November 2021. The CEB has also an observer status with the United Nations' Framework Convention on Climate Change, which supports the growing importance of climate change considerations for its social activities.

Internal procedures incorporate Paris Alignment Framework

The CEB has adopted its own Paris Alignment Framework, organised around four pillars: i) orient the financing to projects that do no significant harm to the environment; ii) identify opportunities to promote a just and socially inclusive climate transition; iii) align internal activities, governance mechanisms, as well as policies; and iv) enhance transparency and reporting on climate-related topics.

Direct lending to be aligned with climate objectives by end 2022

More precisely, the CEB has adopted a phased roadmap to progressively align its direct lending with its climate objectives by the end of 2022. The CEB already assesses the environmental impact of the projects it finances to determine the degree of alignment with the Paris Agreement throughout the project cycle. Projects misaligned with the Paris Agreement are ineligible for financing.

Projects categorised by GHG emissions potential

The CEB undertakes a screening of projects to establish an estimate of expected GHG emissions and the relative decrease in GHG emissions for mitigation projects. Projects are ranked in three categories: i) high emission > 20 000 tonnes CO_2; ii) medium 10 000 to 20 000 tonnes CO_2; and iii) low < 10 000 tonnes CO_2. Additionally, a carbon footprint analysis is performed for all projects having 'medium' or 'high' GHG emissions.

Internal guidance to assess environmental risks

Currently, the CEB relies on widely accepted principles to identify green projects such as those developed by the European Union taxonomy and the MDB joint methodology for reporting climate change mitigation and adaptation finance. However, the approach taken by the CEB is still expected to be detailed in an internal guidance document adapted to the specificities of its operations.

Climate finance accounts for a limited share of funding

Despite initiatives and proactive policies to incorporate climate change considerations, environmental projects are not at the core of the CEB's lending strategy. In 2021, the CEB approved 57 projects for a total financing of EUR 4.2bn of which EUR 0.5bn were for climate mitigation and adaptation (13% of the total volume of financing approved). Among those projects, 24 contributed to climate change mitigation (89% of the total volume of climate action financing approved) and six (11%) contributed to strengthen climate change resilience and adaptation.

Proactive policies support high environmental credibility

Overall, additional adjustments will need to be introduced to better manage transition and physical risks at an operational level. However, the CEB has demonstrated a very strong credibility to increasingly incorporate climate change considerations into its due diligence and complement its existing project selection policies, supporting our positive assessment of the CEB's environmental factors and institutional profile.

Governance

Relatively diversified, mostly European shareholder base

The CEB is owned by 42 countries and all countries (46) belonging to the Council of Europe could become member states. Voting rights correspond to each shareholder's respective share of the CEB's subscribed capital. Shareholder concentration is moderate, with no member state being able to dominate the decision-making process on its own, thus resulting in no negative adjustment per our methodology. Most voting shares are held by G7 countries. France, Germany and Italy hold more than half (50.2%, or 16.7% each) of the subscribed capital. Overall, the shareholder structure is titled towards larger European countries, with Spain (10.9% of capital), Netherlands (3.6%) and Belgium (3.0%) also counting among the key shareholders. Apart from Turkey (7.1%), other members hold a relatively small share of the subscribed capital.

Strong governance, with internal and external controls

Each member state has an individual representative on the CEB's governing board that has the full authority over the bank's strategic decisions. The board has 42 members who appoint the Governor and the chair of the administrative council. The Secretary General of the Council of Europe may participate in meetings. Beyond strategic considerations, the governing board delegates all its powers to the administrative council that is tasked to give its opinion on decisions with financial consequences. Most decisions require a qualified majority of more than half of members holding two thirds of votes casts, with a quorum of two thirds of votes cast. The governing board and administrative council are assisted by an independent auditing board in charge of certifying the balance sheet and the operational accounts, which are also reviewed by an external auditor.

Intrinsic strength – Financial profile: Excellent

We assess a capitalised institution's financial profile along three rating factors: i) capitalisation; ii) asset quality; and iii) liquidity and funding.

Scale	Excellent	Very Strong			Strong			Adequate			Moderate			Weak			Very Weak		
		+		-	+		-	+		-	+		-	+		-	+		-

The CEB's financial profile is assessed as 'Excellent'. This reflects its: i) 'high' capitalisation and ability to generate and retain capital; ii) 'very strong' portfolio quality, 'excellent' asset performance and low equity exposure compared to peers; and iii) 'excellent' liquidity coverage and funding profile.

Capitalisation

Scale	+6	+5	+4	+3	+2	+1	0	-1	-2	-3

Our analysis focuses on the supranational's capacity to absorb losses, taking into account the long-term and counter-cyclical nature of its operations and its ability to generate and retain capital.

Our assessment reflects the CEB's conservative capital framework and its track record of generating and retaining capital. We use an implied leverage ratio as the cornerstone of our capitalisation assessment, which assumes that the bank operates at maximum capacity as defined in its prudential framework, setting a maximum gearing ratio limiting the amount of outstanding loans to 2.5 times subscribed capital, reserves and net profit.

Strong capitalisation; high and increasing leverage ratio

For the numerator, we include paid-in capital (EUR 613m), accumulated reserves and retained earnings (EUR 2.6bn), net profits (EUR 94.8m), and deduct losses recognised directly in equity (EUR 102m) at end-2021. Altogether, resources amount to EUR 3.2bn. For the denominator, we use the bank's total capitalisation (or the potential mandated assets), which amounted to EUR 20.5bn at end-2021.

The resulting capitalisation ratio of about 16% is high and has increased markedly since 2011 (12%), driving our positive assessment. The CEB operates at a slightly higher actual capitalisation level of around 17%, based on total mandated assets of about EUR 19bn. Following a period of steady increase since 2011, the capitalisation ratio has moderated in recent years, down from a peak of 21% in 2017, following a large increase in disbursed loans over the same period (+37%). This has led to a narrower gap between the actual and floor levels of capitalisation, implying the bank is operating close to its full capacity. This already high and increasing leverage ratio represents a key credit challenge, which is only partially mitigated by its retained profits.

Figure 4: Capitalisation vs peers
%, latest figure

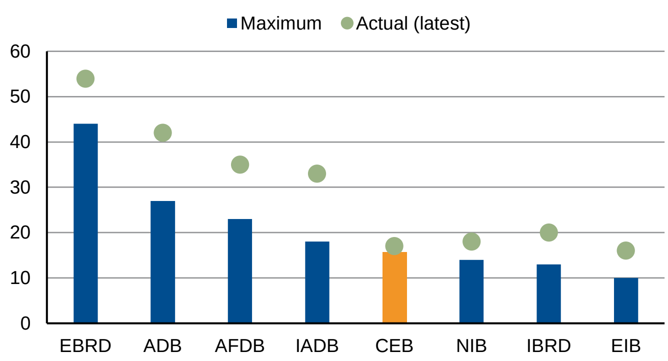
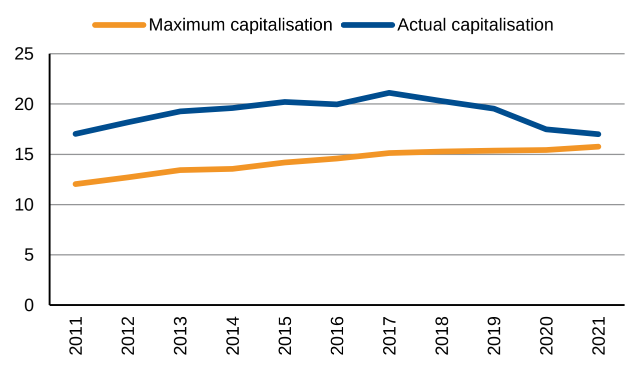


Figure 5: Capitalisation over time
%



Maximum refers to capitalisation under full capacity. Source: CEB, Scope Ratings

Capitalisation levels in line with CEB's own targets and policies

The CEB's self-reported gearing ratio, based on total loans outstanding (after swaps and guarantees) stood at 2.31 at end-2021. This is a significant increase since 2014 (1.67), though it remains comfortably below the bank's ceiling of 2.5. Similarly, the bank's self-reported risk-based capital adequacy ratio rose to about 29% in 2021, up from 25.5% in 2014, and is still significantly above the prudential floor of 10.5% as well as the bank's self-target of maintaining a ratio of above 20%.

Figure 6: Capitalisation vs self-imposed limits
EUR bn (LHS); % (RHS)

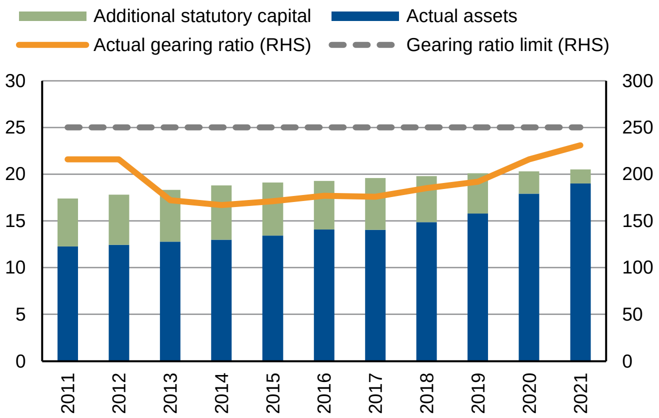
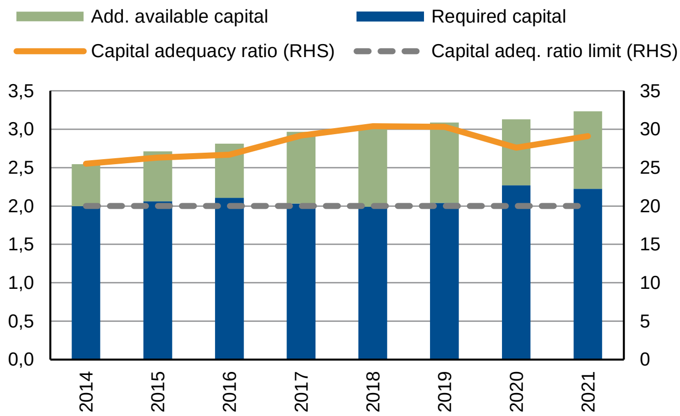


Figure 7: Risk-based capital utilisation
EUR bn (LHS); % (RHS)



Note: The bank's capital adequacy ratio was computed differently pre-2014.
Source: CEB, Scope Ratings

Robust, albeit declining, profit generating capacity

Additionally, we view the CEB's proven ability to generate and retain profits positively, with the bank remaining profitable in recent decades despite multiple economic crises affecting its member states. Robust and steady profitability averaging EUR 108m over the past 10 years supports a stable growth of equity as profits are allocated to reserves. The CEB recorded a net profit of EUR 94.8m in 2021, up from EUR 74.8m in 2020, which was largely due to the adverse macroeconomic environment.

However, the CEB's profitability, as measured by its return on equity, has been on a decreasing trend, declining from 5.1% in 2011 to 2.9% in 2021, largely related to the low-interest rate environment, which weighed on net interest income and ultimately net profit while increasing leverage. Looking ahead, the trend is likely to reverse given the gradual increase in interest rates in the near term.

Figure 8: CEB's return on equity
EUR m (LHS); % (RHS)

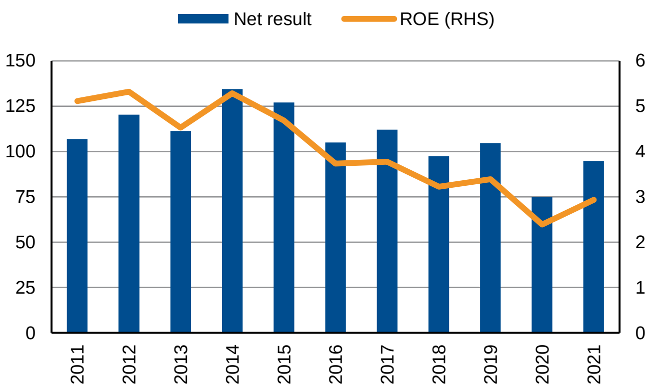
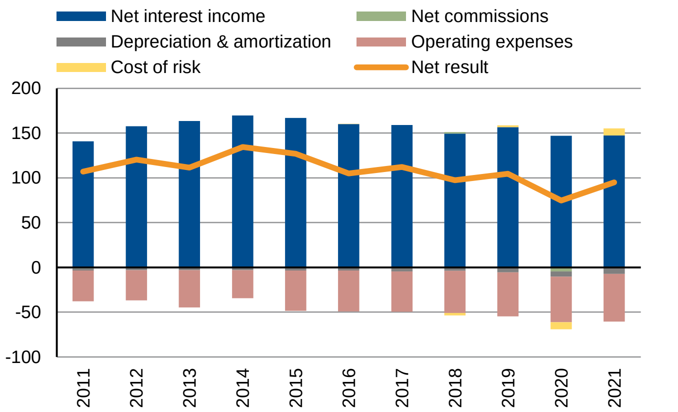


Figure 9: CEB's retained net result
EUR m



Source: CEB, Scope Ratings

Asset quality

Scale	+5	+4	+3	+2	+1	0	-1	-2	-3

Our analysis is structured around a forward-looking qualitative assessment of the supranational's portfolio quality, including an evaluation of possible credit enhancements, and a quantitative assessment of the portfolio's past asset performance.

Excellent asset quality reflects conservative lending and preferred creditor status

The CEB's 'very strong' asset quality reflects its low-risk business profile, underpinned by its focus on highly rated public sector borrowers, a moderate share of private sector exposure and absence of any equity exposure. The bank has not recorded any non-performing loans over the past 12 years. We also account positively for its relatively diversified portfolio across geographies, sectors, and counterparties.

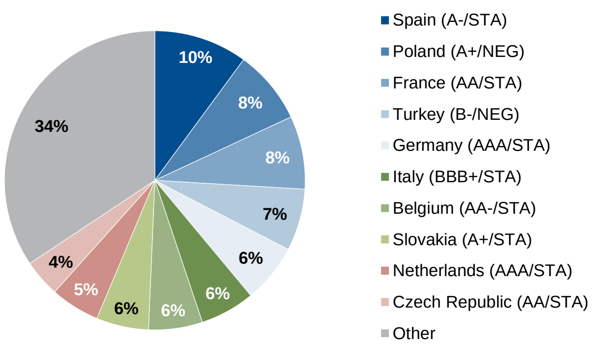
Portfolio quality

Loans to European countries and limited private sector exposure

The CEB's total signed loan portfolio increased to about EUR 18.9bn at end-2021, up from EUR 17.9bn at end-2020. The bank's loan portfolio expanded markedly in the past five years, growing by 45% since 2015, though it remains moderate relative to peers. More than 80% of CEB's loans relate to public sector institutions, including sovereign and sub-sovereign entities, as well as to their promotional financial institutions. Private sector exposure is low and represents around 19% of the total loan portfolio. Looking ahead, we expect the CEB's activities to remain broadly unchanged under the upcoming Strategic Framework 2023-2027.

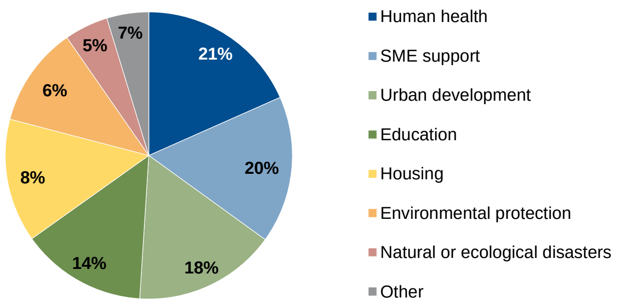
With respect to geographical exposure, we note that the CEB's top-10 country exposure constitute around two thirds of total loans at end-2021, with Spain, Poland, France, and Turkey together accounting for around one third of loans. Specifically, Turkey (B-/Negative) is the fourth largest exposure, though its share in total loans has declined from around 10% in 2016 to 7% in 2021. Based on our sovereign ratings, the weighted average rating of the top 10 borrowers is assessed as 'a' still in line with previous years and it remains one of the highest levels among similar institutions.

Figure 10: CEB's portfolio by geographic exposure
EUR bn, end-2021



Source: CEB, Scope Ratings

Figure 11: CEB's loan portfolio split by sector
% total, end-2021



Source: CEB, Scope Ratings

We estimate the average borrower quality of the overall portfolio in the high 'bbb' range, which corresponds to an 'adequate' assessment per our methodology. We use the average sovereign rating of the top 10 country exposure as a starting point. We then adjust the average borrower quality for sub-sovereigns and for banks downwards by one category and, conservatively, two categories for corporates and others.

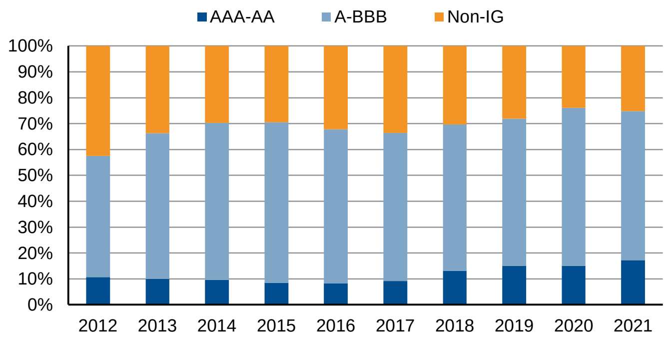
Figure 11: CEB's estimated average borrower quality before credit enhancements

Portfolio	EUR bn	%	Est. avg. quality
Sovereign	10.0	50.0	a
Sub-sovereign	5.4	28.8	bbb
Banks	3.2	16.9	bbb
Other	0.3	4.4	bb
Overall estimated portfolio quality	18.9	100.0	bbb

Source: CEB, Scope Ratings. Estimated borrower qualities in lower case.

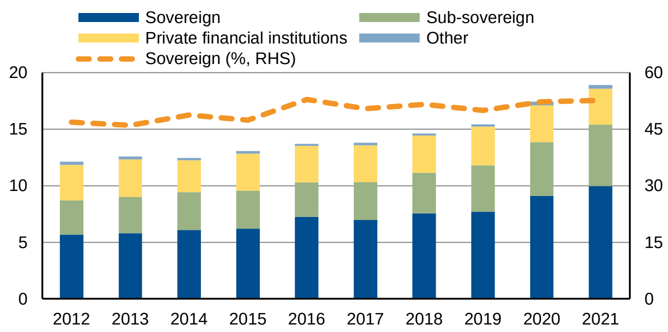
This conservative estimate is supported by the CEB's internal grading system, according to which about a quarter of its exposure is considered non-investment grade, before taking into account credit enhancements such as guarantees and collateralised loans.

Figure 12: CEB's portfolio by credit risk profile
%



Source: CEB, Scope Ratings

Figure 13: CEB's loan portfolio split by sector
EUR bn (LHS), % total (RHS)



Note: Scope estimates for 2012
Source: CEB, Scope Ratings

Portfolio quality – credit enhancements

We provide some uplift to our initial estimate given credit enhancements, which improve our final assessment of portfolio quality to 'very strong' from 'adequate' (see Annex III). This balances the CEB's Preferred Creditor Status (PCS) for its sovereign exposure, additional protections for more than one third of its total exposure through security arrangements, and its relatively well-diversified portfolio across countries and sectors, with a relatively limited share of non-investment grade exposure.

Consistent record of benefiting from preferred creditor status

Specifically, for the CEB's sovereign and public sector exposure, which constitutes about 81% of the portfolio, we acknowledge the bank's record of being exempt from sovereign debt restructurings. This was most recently the case during the default episode of Greece. In addition, following the 1992 resolution of Yugoslavia, the bank was able to fully recover the debt that it was owed, thus demonstrating the *de facto* PCS granted to the CEB by the international financial community. The CEB's sovereign exposure clearly benefits from preferred creditor status and, similarly, its public sector exposure is well protected.

About 80% of the loan portfolio assessed as well protected

In addition, the CEB has security arrangements for about EUR 6.7bn (or 35% of its total loan exposure). This consists mainly of guarantees (EUR 6.5bn) and collateralised loans (EUR 0.2bn), which enable the CEB to transfer around 11% of its portfolio from non-investment to the investment-grade category. Overall, after including credit enhancements, the CEB's asset quality improves markedly, with about 86% of its portfolio at investment grade.

Portfolio diversification

High portfolio diversification across regions, more limited across sectors and counterparties

The CEB's loan portfolio is well diversified across regions, with a steady decline in the share of the portfolio related to its top-10 country exposure to 66% in 2021, down from 79% in 2016. In addition, internal lending policies set counterparty limits to ensure sufficient diversification of the loan portfolio. Among the 12 counterparties or groups of counterparties viewed as large exposure as of end-2021, none of them exceeded the 25% limit of the CEB's prudential equity (or the 800% limit when considering counterparties collectively). Overall, the top-10 individual nominal exposure amounts to less than one third of the portfolio. Finally, given its mandate, the portfolio is more concentrated across sectors, however, when compared with similar lenders.

Equity exposure

No equity exposure

In line with the CEB's mandate, the absence of any equity exposure results in no negative adjustment to our asset-quality estimate.

Asset performance

Excellent asset quality record as most exposure refer to sovereigns

The CEB benefits from strong asset quality. The bank has only registered one non-performing loan – defined as amounts more than 90 days in arrears – since its inception in 1956. This related to the failure of an Icelandic counterparty to meet its commitments on capital and interest in 2009, representing a total amount of EUR 0.2m. During that year, the CEB passed provisions covering the totality of the outstanding loan, amounting to EUR 1.8m. In addition, the portfolio has been remarkably resilient through adverse economic conditions and weathered the Covid-19 crisis without any material deterioration in asset quality. This reflects the strong credit profile of the bank's main counterparties (mostly sovereign and sovereign-related entities), recognition of PCS, as well as effective risk management and monitoring practices. Accordingly, the level of provisions for credit risk is relatively low, standing at around EUR 7.8m at end-2021.

Tail risk relates to high exposure to Turkey

The CEB's exposure to entities domiciliated in Turkey (B-/Negative) is material, at about 7% of the total loans in 2021. Although this credit risk has not materialised yet, the steady deterioration of Turkey's credit rating and the negative outlook signal a heightened risk of possible impairments related to these loans. However, the share of loans to Turkish entities has decreased in the past five years, down to 7% from about 10% in 2017. Additionally, the entirety of this exposure – among which State-owned banks – relates to the Turkish sovereign due to credit enhancement mechanisms and thus benefits from the CEB's PCS. Finally, the CEB has never recorded an impairment on loans related to Turkish entities at the time of previous domestic financial crises. All these factors support our view that this exposure is manageable.

Figure 14: No NPLs

% total loans, 3Y average

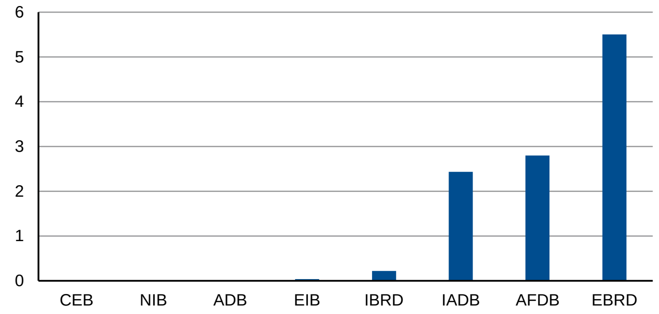
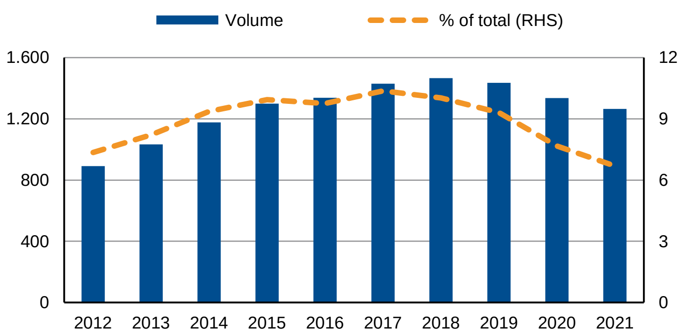


Figure 15: Evolution of the exposure vis a vis Turkey

EUR m (LHS); % total (RHS)



Source: CEB, Scope

Liquidity and funding

Scale	+8	+7	**+6**	+5	+4	+3	+2	+1	0	-1	-2	-3	-4

Our analysis focuses on the supranational's: i) available liquid assets to meet financial obligations and expected disbursements over an extended period; and ii) funding operations, including the stability and diversification of its market access.

Our assessment reflects the CEB's 'excellent' liquid assets coverage and market access, given its benchmark issuer status for social bonds and diversified funding base.

Liquidity coverage

Conservative liquidity policies: liquid assets are high…

The CEB's prudent liquidity management relies on comprehensive risk indicators and the accumulation of liquid assets to face adverse market conditions. The CEB follows two main liquidity indicators as part of its liquidity risk management. It aims to maintain a 'self-sufficiency period', i.e. during which it is able to meet its cash outflows without accessing markets or selling assets for a six month minimum. It also aims to maintain a 'survival horizon', i.e. a period during which it is able to meet its cashflows without accessing markets but is able to sell assets with a maturity above 12 months. As of March 2022, both metrics were comfortably above their limits, at 13 and 18 months, respectively.

The CEB's conservative liquidity management results in a stable, high level of liquid assets, which we estimate at about EUR 9.2bn at end-2021, up from EUR 8.1bn in 2020. We include assets which are least sensitive to sudden market or interest changes, specifically, cash and deposits (EUR 2.0bn), debt securities maturing within one year (EUR 4.0bn) as well as longer-term, highly rated debt securities with a minimum rating of AA- (EUR 3.2bn).

… compared to liabilities due within the next 12 months

Conversely, liabilities maturing within a 12-month period amounted to EUR 5.2bn in 2021 (EUR 3.8bn in 2020), while gross disbursements for 2022 are estimated at EUR 3.6bn, representing a decrease from the elevated levels of disbursements registered during the Covid-19 crisis, at EUR 5.5bn and EUR 4.5bn in 2021 and 2020, respectively. This brings our proxy of total liabilities due within one year to around EUR 8.8bn at end-2021. We include disbursements over the next 12 months to reflect the CEB's social mandate to continue its activities when economic and financial circumstances deteriorate.

Figure 16: Liquid assets, liabilities and disbursements

EUR bn, %

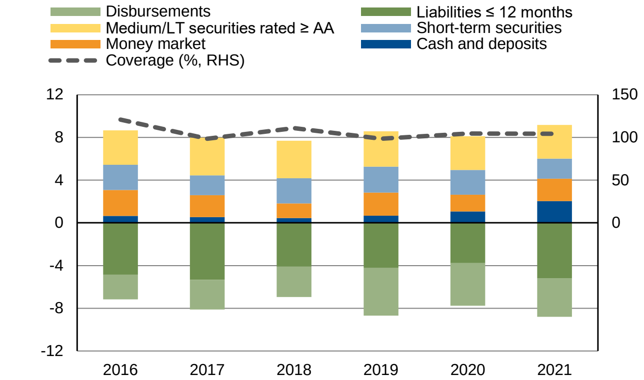
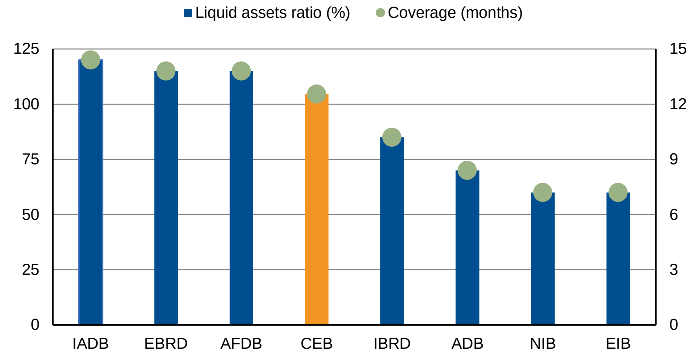


Figure 17: Liquid assets ratio and coverage of obligations

% (LHS); coverage without market access in months (RHS)



NB: 50% implies coverage of all obligations for a period of six months without the need to access capital markets. Weighted three-year average.
Source: CEB, Scope Rating

Excellent liquidity coverage

On this basis, we calculate a three-year weighted average liquid assets ratio of about 105% for 2019-21. This ratio implies that all outstanding liabilities and all committed disbursements due within a year can be financed for 12 months using available liquid assets, without needing to access capital markets, a key strength in a rising interest rate environment. This ratio is elevated, even compared with similar lenders, standing above 100% in eight of the past 10 years: the exceptions were 2017 (98.5%) and 2019 (98.7%). However, over the long term, this ratio has declined from 188% at end-2011, driven mainly by the now higher disbursements.

Funding

Regulatory preference and inclusion in ECB's bond purchase programmes

The CEB benefits from excellent market access, reflecting its frequent issuer status, with 19 bonds issued in 2021. The bank pursues a diversified funding strategy, in terms of currencies and instruments, providing the CEB with a stable source of funding for its operations. Bonds issued by the CEB are designated as high-quality liquid assets under the Basel Framework and thus eligible for a 0% risk weight, and in addition, are also eligible for the ECB's asset purchase programmes.

Regular market issuer with moderate authorised borrowing capacity

The CEB's annual funding volume has increased in recent years though it remains low relative to peers. In 2021, the volume issued reached EUR 5.5bn, including EUR 0.9bn of prefinancing. The CEB's borrowing authorisation for 2022 has been set at EUR 6.5bn, up from EUR 5.5bn in 2021 (EUR 4.5bn in 2020) to meet strong demand from shareholders.

One of the lending social bond issuer

The CEB is a leading supranational social bond issuer with a total issuance of about EUR 6bn since 2017, building on its social inclusion bond framework that is aligned with the ICMA Social Bond Principles. The CEB's social framework sets categories for the use of proceeds around: i) affordable housing, ii) access to essential services (including healthcare and education), and iii) education and vocational training.

The CEB issued two social inclusion bonds in 2021 for almost EUR 2bn equivalent and published a related impact report in March 2022. In addition, the bank intends to widen its impact assessments by reporting on its entire portfolio of social bonds and eligible social loans from 2023. Given rising demand for social investment in Europe and the unique mandate of the CEB, we expect the size and the frequency of social inclusion bonds issued by the bank to rise further.

Figure 18: Annual funding volume vs peers
EUR bn, three-year average 2019-21

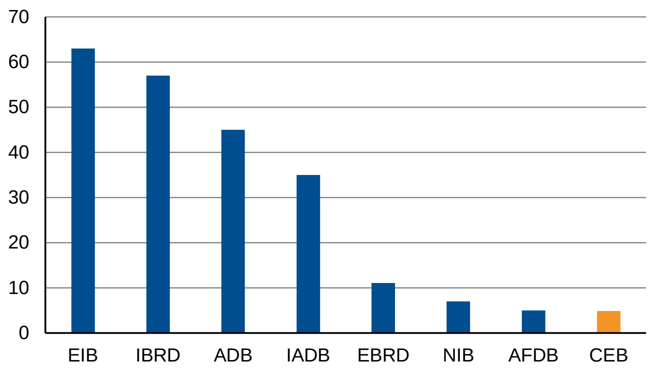
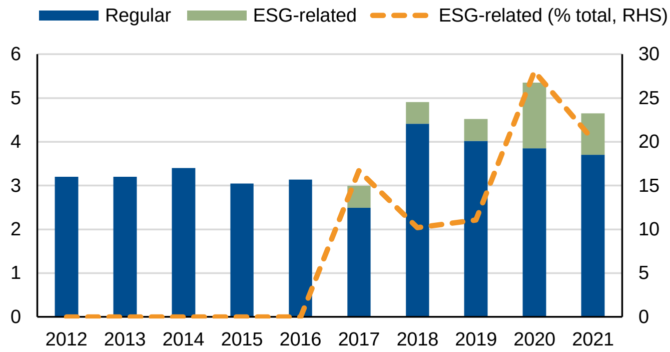


Figure 19: Rising funding volume, including ESG-related
EUR bn (RHS); % total (LHS)



Source: Bloomberg, Scope Ratings, respective supranationals

Diversified investor base but mostly centred around Europe

The CEB benefits from a large and well-diversified investor base, including asset managers and banks committed to environmental, social and governance factors, and official institutions (central banks, international organisations). Increasing bond issuance tends to enlarge the CEB's investor base, especially with socially responsible investors (SRI), attracted by the enhancement of the CEB's social bond framework and impact assessments.

The CEB has continued to enjoy favourable financing terms in recent months, despite the worsening market environment. The latest social inclusion bond issued by the CEB in June 2022 (USD 1bn, 7-year) was met with strong demand, being more than two times oversubscribed. Participation was well diversified across geography and investor types and more than 75% of the issue was allocated to SRIs.

Increasingly diversified currency mix

The CEB's funding activities combine the issuance of large liquid, benchmarks in US dollars and euros, with regular issuances in British pounds and several other currencies. The bank is also issuing bonds denominated in an encouragingly diverse set of currencies. with eight used in 2021, up from three on average over 2012-16. Total debt outstanding (excluding interest payable) amounted to EUR 24.2bn at end-2021 and is exclusively denominated in euro, after accounting for currency swaps.

Limited risks from longer-term liabilities coming due

Finally, we also note that the CEB has a stable redemption profile over the coming years. Liabilities coming due over one to five years (EUR 14.4bn) are largely covered by assets with the same maturity (EUR 10.3bn), resulting in moderate funding risk. The resulting coverage ratio at end-2021 (72%) is adequate and in line with similar lenders but has declined from a peak of 89% in 2017.

Figure 20: Distribution by currency
% total outstanding

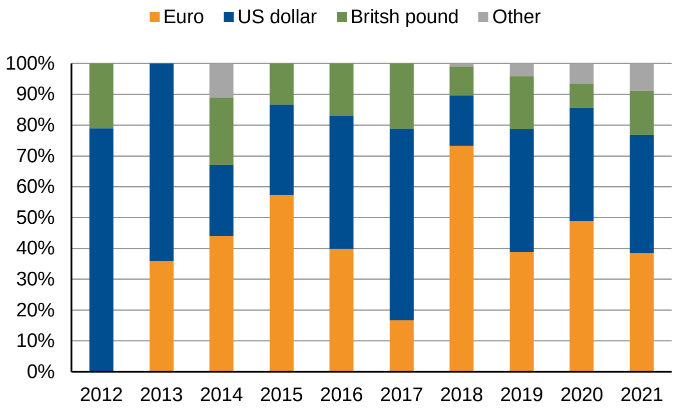
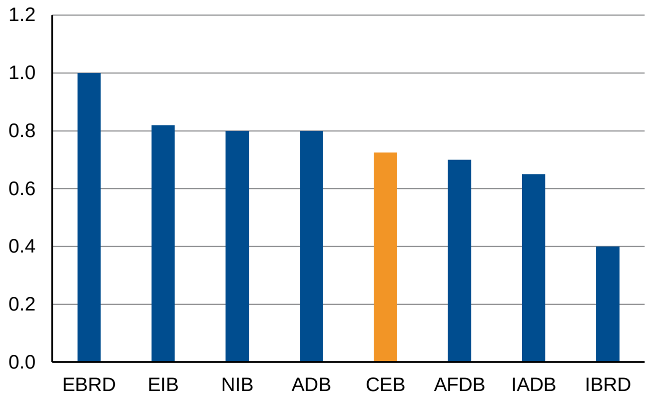


Figure 21: Coverage of medium-term liabilities
%, three-year average



Source: CEB, Scope Ratings, respective supranationals

Additional liquidity considerations

To complete our liquidity assessment, we look at contingent liabilities, interest rate and foreign exchange rate risks, derivatives, and collateral management practices.

No adjustment for rising contingent liabilities

The CEB uses its Social Dividend Account to support high social impact projects via technical assistance, loan guarantees, interest-rate subsidies and investment grants, located mainly in the bank's target countries. The resources of the fund amount to EUR 144m at end-2021. Outstanding guarantees on loans are very low at EUR 23.3m while guarantees for subsidised interest rates amount to EUR 7.5m.

No adjustments for interest rate, foreign exchange, or derivatives exposure

The CEB's main source of interest rate risk stems from movements in funding or lending spreads. The bank has defined limits on the duration of Own Funds (limit 11Y; actual 6.5Y), the Economic Value Sensitivity (limit +/- EUR 18.5m; actual EUR -6.3m) and the Earnings Sensitivity (limit +/- EUR 3m; actual EUR -0.4m). The CEB provides most of its financing to member states and clients in euros, but it manages the foreign exchange risk through a strict limit on the net open position for each currency (less than EUR 1m) and uses currency swaps to hedge market risk. Similarly, derivatives are used to manage interest rate and/or foreign exchange risk, but not for trading.

Shareholder support: High

We assess an institution's shareholder support primarily via the weighted average rating of its key shareholders. This may be adjusted in case of a meaningful overlap between the key shareholders providing support and the countries of operation, as well as for any extraordinary support measures.

Scale	Very High	**High**	Moderate	Weak

The CEB's shareholder support is assessed as 'High'. This reflects its key shareholders' ability and proven willingness to provide financial support in case of need.

Key shareholder rating

Highly rated key shareholders apart from one exception

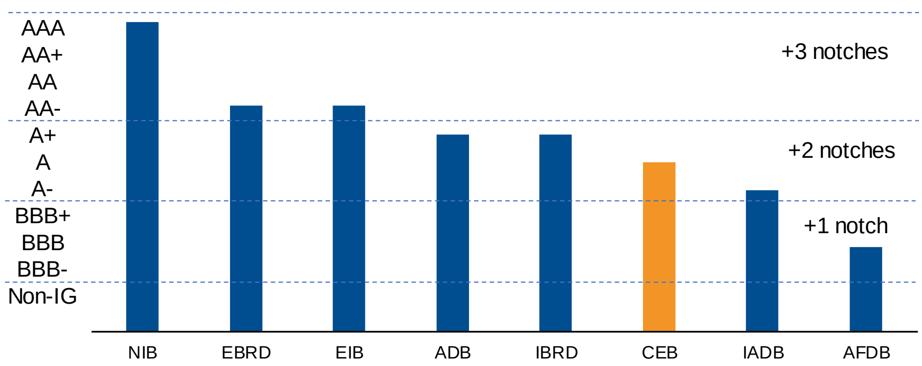
The CEB's key shareholder group comprises the largest European economies – Germany (AAA/Stable), France (AA/Stable), Italy (BBB+/Stable), Spain (A-/Stable), the Netherlands (AAA/Stable), Belgium (AA-/Stable) and Greece (BB+/Stable) – and Turkey (B-/Negative). This results in a weighted average rating of A based on Scope's sovereign ratings, slightly below similar supranational lenders, but still signalling the capacity to support the CEB if needed. Of the bank's 42 member states, 15 are rated AA- or above[1], constituting more than 50% of its subscribed capital. This provides additional confidence about shareholders' ability to provide support.

Figure 22: Key shareholders

Key shareholders	Rating	Capital subscription (%)	
		Original	Adjusted
France	AA/Stable	16.7	21.5
Germany	AAA/Stable	16.7	21.5
Italy	BBB+/Stable	16.7	21.5
Spain	A-/Stable	10.9	14.0
Turkey	B-/Negative	7.1	9.1
Netherlands	AAA/Stable	3.6	4.7
Belgium	AA-/Stable	3.0	3.9
Greece	BB+/Stable	3.0	3.9
		77.8	**100.0**
Key shareholder rating			**A**

Source: CEB, Scope Ratings. Figures may not add up due to rounding.

Figure 23: CEB's key shareholder rating vs peers



Source: Scope Ratings, respective supranationals

[1] We rely on internal estimates for sovereigns not publicly rated.

Some overlap between key shareholders and main countries of operations

While the CEB's operations in the jurisdictions of its key shareholders constitute about 49% of its total operations, we exclude the operations in countries rated AA- or above. The credit quality of such highly rated shareholders is unlikely to deteriorate materially even in times of financial distress. The CEB's operations in Spain, Turkey, Italy and Greece together account for about 24% of its total operations. This reflects a moderate risk of material credit deterioration arising simultaneously in countries that are expected to provide support if needed.

Limited risks related to highly speculative credit among key stakeholders

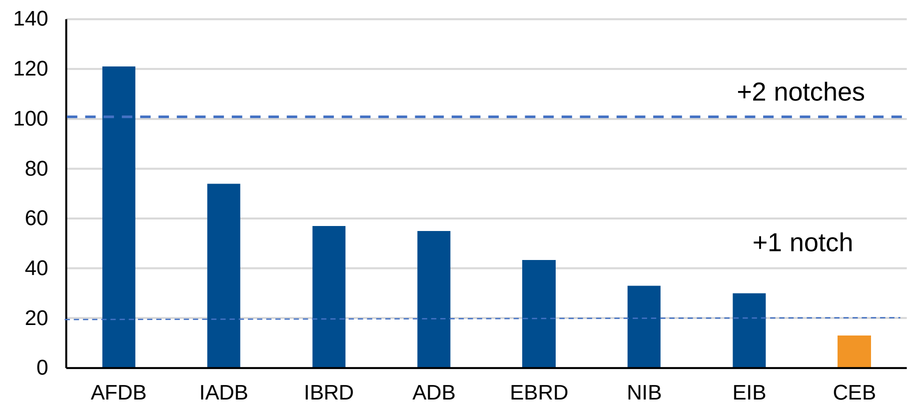
The CEB includes Turkey (B-/ Negative) among its main shareholders, responsible for about 7% of the subscribed capital as well as being the fourth country of operations with outstanding loans of EUR 1.27bn in 2021. However, the share of loans granted to Turkey has declined overtime, from 10% in 2016 to 7% in 2021. We also consider that other key shareholders will be willing and able to provide support and additional financial resources if needed.

Extraordinary support

Lower than peers but adequate high-quality callable capital coverage of mandated assets

To complement our assessment of shareholder support, we also look at the quality of the CEB's callable capital in relation to its mandated outstanding assets. Here, we note that EUR 2.5bn in callable capital is provided by sovereigns rated AA- or above, which covers about 13% of the CEB's total mandated assets of EUR 19bn. This coverage is adequate in our methodology, though it is low in a peer-comparison context.

Figure 24: Adequate coverage of mandated assets by high-quality callable capital
%, callable capital rated ≥ AA-/mandated assets



Source: Scope Ratings, respective supranationals

Moderate paid-in capital share mitigated by regular and successful capital increases

We also note that shareholders have paid in 11.2% of subscribed capital, one of the lowest ratios among development banks rated AAA. However, the CEB has a record of regular capital increases (six since its inception), demonstrating shareholders' economic strength and political commitment to the bank's mandate.

In February 2011, the governing board approved the CEB's 6th capital increase following a recommendation by its administrative council; 38 countries participated, representing 98% of the CEB's capital. Subscribed and paid in capital thus rose by 65% as of December 2012, increasing respectively to 5.5bn from EUR 3.3bn and to EUR 613m from EUR 370m. Finally, in the context of Andorra's accession, the CEB's subscribed capital increased by EUR 4.9m in 2020, of which two instalments of EUR 0.5m each that were paid in in 2020 and 2021.

Indicative rating: AAA

We first map the assessments for the institutional and financial profiles to determine the supranational's intrinsic strength. In a second step, we map this assessment against shareholder support to determine the indicative rating.

Figure 25a: Mapping institutional and financial profiles for the CEB

	Intrinsic Strength	Institutional Profile				
		Very Strong	Strong	Moderate	Weak	Very Weak
Financial Profile	*Excellent*	Excellent	Excellent	Excellent	Very Strong (+)	Very Strong
	Very Strong (+)	Excellent	Excellent	Very Strong (+)	Very Strong	Very Strong (-)
	Very Strong	Excellent	Very Strong (+)	Very Strong	Very Strong (-)	Strong (+)
	Very Strong (-)	Very Strong (+)	Very Strong	Very Strong (-)	Strong (+)	Strong
	Strong (+)	Very Strong	Very Strong (-)	Strong (+)	Strong	Strong (-)
	Strong	Very Strong (-)	Strong (+)	Strong	Strong (-)	Adequate (+)
	Strong (-)	Strong (+)	Strong	Strong (-)	Adequate (+)	Adequate
	Adequate (+)	Strong	Strong (-)	Adequate (+)	Adequate	Adequate (-)
	Adequate	Strong (-)	Adequate (+)	Adequate	Adequate (-)	Moderate (+)
	Adequate (-)	Adequate (+)	Adequate	Adequate (-)	Moderate (+)	Moderate
	Moderate (+)	Adequate	Adequate (-)	Moderate (+)	Moderate	Moderate (-)
	Moderate	Adequate (-)	Moderate (+)	Moderate	Moderate (-)	Weak (+)
	Moderate (-)	Moderate (+)	Moderate	Moderate (-)	Weak (+)	Weak
	Weak (+)	Moderate	Moderate (-)	Weak (+)	Weak	Weak (-)
	Weak	Moderate (-)	Weak (+)	Weak	Weak (-)	Very Weak (+)
	Weak (-)	Weak (+)	Weak	Weak (-)	Very Weak (+)	Very Weak
	Very Weak (+)	Weak	Weak (-)	Very Weak (+)	Very Weak	Very Weak (-)
	Very Weak	Weak (-)	Very Weak (+)	Very Weak	Very Weak (-)	Very Weak (-)
	Very Weak (-)	Very Weak (+)	Very Weak	Very Weak (-)	Very Weak (-)	Very Weak (-)

Figure 25b: Mapping intrinsic strength and shareholder support for the CEB

	Indicative Rating		Shareholder Support			
			Very High	High	Moderate	Weak
Intrinsic Strength	Excellent		AAA	AAA	AAA / AA	AA+ / AA-
	Very strong	+	AAA	AAA / AA	AA+ / AA-	AA / A+
			AAA / AA	AA+ / AA-	AA / A+	AA- / A
		-	AA+ / AA-	AA / A+	AA- / A	A+ / A-
	Strong	+	AA / A+	AA- / A	A+ / A-	A / BBB+
			AA- / A	A+ / A-	A / BBB+	A- / BBB
		-	A+ / A-	A / BBB+	A- / BBB	BBB+ / BBB-
	Adequate	+	A / BBB+	A- / BBB	BBB+ / BBB-	BBB / BB+
			A- / BBB	BBB+ / BBB-	BBB / BB+	BBB- / BB
		-	BBB+ / BBB-	BBB / BB+	BBB- / BB	BB+ / BB-
	Moderate	+	BBB / BB+	BBB- / BB	BB+ / BB-	BB / B+
			BBB- / BB	BB+ / BB-	BB / B+	BB- / B
		-	BB+ / BB-	BB / B+	BB- / B	B+ / B-
	Weak	+	BB / B+	BB- / B	B+ / B-	B / CCC
			BB- / B	B+ / B-	B / CCC	B- / CCC
		-	B+ / B-	B / CCC	B- / CCC	CCC
	Very Weak	+	B / CCC	B- / CCC		
			B- / CCC	CCC	CCC	
		-	CCC	CCC		

Source: Scope Ratings

Additional considerations

We acknowledge the heterogeneity of supranationals and include in our assessment idiosyncratic factors that may affect the creditworthiness of the supranational.

In the case of the CEB, we have not made an adjustment to our indicative rating.

Rating history

Date	Rating Action	Outlook
2 October 2020	AAA	Stable

Source: Scope Ratings

I Shareholders: Council of Europe Development Bank

EUR m

CEB shareholders	Paid-in capital	Callable capital	Subscribed capital	Key (%)	Rating	Callable capital ≥ AA-
France	101.66	814.11	915.77	16.7	AA/Stable	814,114.0
Germany	101.66	814.11	915.77	16.7	AAA/Stable	814,114.0
Italy	101.66	814.11	915.77	16.7	BBB+/Stable	
Spain	66.30	530.96	597.26	10.9	A-/Stable	
Turkey	43.10	345.20	388.30	7.1	B-/Negative	
Netherlands	22.07	176.74	198.81	3.6	AAA/Stable	176,743.0
Belgium	18.24	146.08	164.32	3.0	AA-/Stable	146,083.0
Greece	18.24	146.08	164.32	3.0	BB+/Stable	
Key shareholders*	**472.92**	**3,787.41**	**4,260.31**	**77.8**	**A**	**1,951.1**
Other 34 shareholders	140.50	1,076.77	1,216.82	22.2		505.5
Total	**612.96**	**4,864.18**	**5,477.14**	**100.0**		**2,456.6**

* We include shareholders whose cumulative capital share, starting from the largest shareholder, comprises at least 75% of the supranational's capital. We add all marginal shareholders with identical capital subscription to calculate the key shareholder rating.

Source: CEB, Scope Ratings. Figures may not add up due to rounding.

II Scope's supranational scorecard: Council of Europe Development Bank

		Risk factors		Variables	Unit	+4	+3	+2	+1	0	-1	-2	CEB Value	CEB Assessment	CEB Notches
Intrinsic Strength	Institutional Profile	Mandate & ESG (-2; +2)	Mandate	Importance of mandate	Qualitative	--	--	--	Very High	High	Declining	--	--	Very High	1
				Social factors	Qualitative	--	--	--	Strong	Medium/ N/A	Weak	--	--	Strong	
				Environmental factors	Qualitative	--	--	--	Strong	Medium/ N/A	Weak	--	--	Medium/ N/A	
			Governance	Shareholder concentration	HHI	--	--	--	--	≤ 1500	> 1500	--	1100,0	Strong	1
				Shareholder control	%	--	--	--	--	≤ 25	> 25	--	17,0	Strong	
				Strategy and internal controls	Qualitative	--	--	--	Strong	Medium	Weak	--	--	Strong	
		Institutional Profile												**Very Strong**	
	Financial Profile	Capitalisation (-3; +6)	Capital/ Potential assets		%	≥ 30	< 30; ≥ 20	< 20; ≥ 15	< 15; ≥ 10	< 10; ≥ 7.5	< 7.5; ≥ 5	< 5	16,0	High	2
			Capital/ Actual assets*		%	--	--	--	≥ 40	< 40	--	--	17,0	Adequate/ No uplift	0
			Profitability (Return on equity)		%	--	--	--	≥ 3	< 3; ≥ 0	< 0	--	3,0	Strong	1
		Asset quality (-3; +5)	Portfolio quality	Incl. risk mitigants	Qualitative	--	--	Very Strong	Strong	Adequate	Moderate	Weak	Very Strong	Very Strong	2
			Asset performance	NPLs	% total loans	--	≤ 0.5	> 0.5; ≤ 1	> 1; ≤ 3	> 3; ≤ 5	> 5	--	0,0	Excellent	3
		Liquidity & funding (-4; +8)	Liquid assets ratio		%	> 100	≤ 100; > 75	≤ 75; > 50	≤ 50; > 25	≤ 25; > 15	≤ 15; > 10	≤ 10	105,0	Excellent	4
			Funding	Maturity gap	Multiple	--	--	--	≥ 0.75	< 0.75; ≥ 0.50	< 0.50	--	0,7	Adequate	0
				Funding volume	EUR or USD bn	--	--	≥ 25	< 25; ≥ 5	< 5; ≥ 2	< 2	--	5,0	Strong	1
				Currency diversification	Top 1 share	--	--	--	≤ 70	> 70	--	--	42,0	Strong	1
		Financial Profile												**Excellent**	
		Intrinsic Strength												**Excellent**	
Shareholder Support		Shareholder strength (0; +3)	Weighted average rating of key shareholders		Avg. rating	--	≥ AA-	≥ A-	≥ BBB-	< BBB-	--	--	--	A	2
			Share of portfolio related to key shareholders		%	--	--	--	--	≤ 50	> 50	--	24,0	Low / No adjustment	
			Adjusted key shareholder rating		Avg. rating	--	--	--	--	--	--	--	--	A	
		Extraordinary Support (0; +2)	Callable capital [rated ≥ AA-]/ Actual assets		%	--	--	≥ 100	< 100; ≥ 20	< 20	--	--	13,0	Adequate	0
			Additional support mechanisms		Qualitative	--	--	Very Strong	Strong	N/A	--	--	N/A		
		Shareholder Support												**High**	
				Indicative Rating										**AAA**	
		Additional considerations (-1; +1)												Neutral	
				Final Rating										**AAA**	

Figures in the financial profile relate to a weighted three-year average for 2019-21.

Source: Scope Ratings

III Asset quality assessment

Portfolio quality (initial assessment)*	Very Strong	Strong	Adequate	Moderate	Weak
Indicative borrower quality	aaa/aa	a	bbb	bb	b/ccc
Notches	+2	+1	0	-1	-2

Adjustments		**Indicator**	**Assessment/ Thresholds**								
Points			+5	+4	+3	+2	+1	0	-1	-2	-3
Credit Protection	Sovereign PCS Private sector secured	*% of loan portfolio*	100	≥ 80	≥ 60	≥ 40	≥ 20	< 20			
Diversification	Geography	*HHI*				≤ 1000	≤ 2000	> 2000			
	Sector	*HHI*					≤ 2000	> 2000			
	Top 10 exposures	*% of loan portfolio***				≤ 25	≤ 75	> 75			
Equity Exposure		*% of equity*						≤ 25	> 25	> 50	> 75

Total points	+7
Adjustments	+2 categories

Portfolio quality (final assessment)	Very Strong	Strong	Adequate	Moderate	Weak
Notches	+2	+1	0	-1	-2

N.B. * Based on Scope's estimate of the geographical and sectoral distribution (sovereigns, sub-sovereigns, state-owned banks and commercial banks) of the CEB's loan portfolio before any credit enhancements via collateral or guarantees, and Scope's sovereign ratings. ** Taking into account the exposure to Turkey and the largest non-sovereign loan exposure.

Source: Scope Ratings. Three points usually correspond to one assessment category. In the case of the CEB, this implies up to two higher categories from the initial portfolio quality assessment based on the estimated average borrower quality.

IV Statistical tables

	2016	2017	2018	2019	2020	2021
Capitalisation (EUR bn)						
Mandated potential assets	19.3	19.6	19.8	20.1	20.3	20.5
Mandated (disbursed) assets	14.1	14.1	14.9	15.8	17.9	19.0
Capitalisation ratio, potential (%)	14.6	15.1	15.3	15.4	15.4	15.8
Capitalisation ratio, disbursed (%)	20.0	21.1	20.3	19.5	17.5	17.0
Profitability (EUR m)						
Net income	104.9	112.0	97.5	104.7	74.8	94.8
Return on equity (%)	3.7	3.8	3.2	3.4	2.4	2.9
Asset quality (EUR bn)						
Total loans (net)	13.7	13.8	14.6	15.4	17.4	18.9
Non-performing loans (EUR m)	-	-	-	-	-	-
Non-performing loans ratio, %	-	-	-	-	-	-
Liquidity (EUR bn)						
Assets ≤ 12 months	5.4	4.5	4.2	5.3	5.0	6.0
Treasury assets > 12 months (rated at least AA-)	3.2	3.5	3.5	3.3	3.1	3.2
Liabilities ≤ 12 months	4.9	5.3	4.1	4.2	3.8	5.2
Disbursements over the next 12 months	2.3	2.8	2.8	4.5	4.0	3.6
Liquid assets ratio (%)	120.8	98.3	110.7	98.6	104.4	104.3
Funding (EUR bn)						
Volume	3.1	3.0	4.9	4.5	5.4	4.6
Share of total (%)						
EUR	39.9	16.7	73.3	38.9	48.9	45.5
USD	43.2	62.2	16.4	39.8	36.6	27.0
GBP	16.9	21.1	9.4	17.2	7.9	16.9
ESG issuance	-	0.5	0.5	0.5	1.5	0.9
% total	-	16.7	10.2	11.1	28.0	20.3
Equity (EUR bn)						
Paid-in capital	0.6	0.6	0.6	0.6	0.6	0.6
Reserves	2.1	2.3	2.4	2.5	2.6	2.6
Total equity	2.8	3.0	3.0	3.3	3.3	3.4
Shareholders						
Average capital-key weighted rating of key shareholders	A+	A+	A+	A+	A	A
Shareholders rated at least AA- (%)	49.4	49.4	49.4	49.4	50.6	50.6
Callable capital [rated ≥ AA-] / Mandated assets	17.0	17.1	16.1	15.2	13.7	12.9

Scope Ratings GmbH

Headquarters Berlin

Lennéstraße 5
D-10785 Berlin

Phone +49 30 27891 0

Frankfurt am Main

Neue Mainzer Straße 66-68
D-60311 Frankfurt am Main

Phone +49 69 66 77 389 0

Paris

23 Boulevard des Capucines
F-75002 Paris

Phone +33 6 62 89 35 12

Oslo

Karenslyst allé 53
N-0279 Oslo

Phone +47 21 62 31 42

Madrid

Paseo de la Castellana 141
E-28046 Madrid

Phone +34 91 572 67 11

Milan

Via Nino Bixio, 31
20129 Milano MI

Phone +39 02 30315 814

Scope Ratings UK Limited

London

52 Grosvenor Gardens
London SW1W 0AU

Phone +44 20 7824 5180

info@scoperatings.com
www.scoperatings.com

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