

African Development Bank

Primary Credit Analyst:

Christian Esters, CFA, Frankfurt (49) 69-33-999-242; christian_esters@standardandpoors.com

Secondary Contact:

Matthew Pirnie, London (44) 20-7176-7238; matthew_pirnie@standardandpoors.com

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Major Rating Factors

Strengths:

- Strong liquidity and capital position.
- Prudent financial management and policies.
- Strong support from members, including 12 'AAA' rated countries, contributing Special Drawing Rights 5.3 billion in callable capital.

Counterparty Credit Rating

Foreign Currency
AAA/Stable/A-1+

Weaknesses:

- Relatively risky loan portfolio with nonperforming loans larger than those of multilateral peers.
- The inability of the governments of most African countries to borrow from the bank.

Rationale

The ratings on African Development Bank (AFDB) are based on its strong liquidity and capital position, prudent financial management and policies, and strong support from its members, which include 12 'AAA' rated countries, and which contribute Special Drawing Rights (SDR, international foreign exchange reserve assets, allocated by the International Monetary Fund) 5.3 billion in callable capital. These factors offset the bank's relatively risky loan portfolio and high level of nonperforming loans, as well as the inability of the governments of most African countries to borrow from the bank.

AFDB, a regional multilateral development finance institution (MDFI), was established in 1964 by 29 African countries. Nonregional members were admitted from 1982, and AFDB's membership now includes all 53 African and 24 nonregional countries. AFDB is the keystone of the African Development Bank Group (AFDB Group), which includes soft-loan windows as African Development Fund (AFDF) and Nigeria Trust Fund (NTF). AFDF and NTF make grants and loans at concessional rates; their loans and grants help to maintain support for AFDB in countries not currently eligible to borrow from the bank. However, while AFDB has an equity investment in AFDF, it is not responsible for the financial obligations of either of these funds, both of which are unrated.

Historically AFDB has provided medium- and long-term loans primarily to African governments and other public-sector entities with sovereign guarantees; however, its focus on the private sector has been increasing over the past few years. The bank also makes equity investments and has provided a few small guarantees. At year-end 2009, 97% of the bank's development-related exposure (DRE) was loans, 2% equity investments, and 1% development-related debt securities. Of outstanding loans, 82% were to governments or were government guaranteed. Financing approvals to private sector entities increased to above SDR1 billion in 2009, but their proportion relative to total lending decreased to 21% owing to a sharp rise in public sector lending.

Since 1995, AFDB has restricted its sovereign lending to its most creditworthy regional member countries. In principle, 15 African countries are eligible to borrow from the bank; however, of these 15 Zimbabwe (unrated) is ineligible for new disbursements due to ongoing arrears and Libya (A-/Stable/A-2) has never borrowed. The other 38 African countries have been able to borrow only from AFDF and NTF since 1995. Lending to the private sector, however, is not restricted to eligible countries. AFDB's outstanding loan exposure increased significantly by 24.6%

during 2009 to SDR7,538 million, following annual growth rates of 4%-5% in the two preceding years. Growth was driven by budget support loans and loans to private sector entities for infrastructure projects. As AFDB increased its treasury investments, outstanding loans remained at 46% of total assets.

Reflecting the weak credit-standing of many of its regional members, SDR256 million of public sector loans (4% of total public sector loans) had principal or interest payments past due by more than six months at year-end 2009, mostly from Zimbabwe; the amount of arrears was significantly reduced as Côte d'Ivoire (unrated) eliminated its arrears of SDR309 million in March 2009. Of private sector exposure, 2% was in arrears at year-end 2009.

In our view, the expected losses embedded in AFDB's loan portfolio are much smaller than they might appear. Standard & Poor's expects AFDB to receive preferential treatment on its sovereign and sovereign-guaranteed loans compared with that received by commercial and bilateral lenders in line with its status as a preferred creditor. Given the economic distress of many of its borrowing members, however, this special status may be of limited value. More important are the payments AFDB expects to receive on behalf of its borrowers through the Highly Indebted Poor Countries (HIPC) Initiative of the International Monetary Fund and the World Bank. Twenty-one member countries had achieved HIPC "completion point" status and eight had achieved "decision point" status by year-end 2009 and a further four had been designated "predecision point" status. These groups of countries accounted for 1.2%, 13.2%, and 1.0%, respectively, of AFDB's public-sector loans at year-end 2009. Under the HIPC framework, the HIPC Trust Fund repays a substantial portion of eligible loans. In addition, we expect other debt relief initiatives to place these countries in a better position financially to service their external debts, including those to AFDB.

AFDB's narrow risk-bearing capacity (provisions for losses plus adjusted shareholders' equity) dropped to 61% of DRE at year-end 2009, owing to a strong increase in DRE. AFDB's financial strength is bolstered by its callable capital, of which close to SDR5.3 billion was from countries rated 'AAA' by Standard & Poor's at year-end 2009.

AFDB's ratio of reserves for losses, adjusted shareholders' equity, and 'AAA' callable capital (its broad risk-bearing capacity) to DRE was 126% at year-end 2009. AFDB's board of governors approved a sixth general capital increase in May 2010, which, once subscribed by shareholders, would triple the bank's authorized capital, and double its paid-in capital in the long run if shareholders pay in the planned proportion of 6%.

In recent years, AFDB has distributed most of its net income for various developmental or humanitarian purposes. AFDB's income before transfers approved by its board of governors was SDR231 million during 2009, down from SDR305 million a year earlier, resulting in a return on average assets plus guarantees of 1.6% and a return on average adjusted shareholders' equity of 5.0%. The bank's liquidity position continues to be one of the strongest among rated MDFIs. Its capital adequacy, despite weakening due to strong asset growth in 2009, is still strong compared with that of other MDFIs.

In 2009, AFDB issued \$7.5 billion of debt, up significantly from previous years.

Outlook

The outlook is stable. We expect AFDB's liquidity to remain very strong and its high franchise value to increase, given the attention Africa is receiving from the international donor community. Further weakening of capital adequacy could be mitigated with the subscription and payment of the recently approved capital increase by AFDB's shareholders, which in our view would demonstrate shareholder support. Our view on shareholder support could

change if shareholders do not subscribe to the capital increase, or do not pay in the expected amounts.

Organization, Ownership, And Management

All powers of the bank are vested in its board of governors, which, among other things, sets policy, admits new members, determines the bank's capital structure, and elects the president. Each member country appoints a governor and an alternate, who serve nominal five-year terms. However, these terms may be abbreviated or extended by the appointing member country. The board of governors delegates most of its operational responsibilities to the board of directors, although it retains the power to override their decisions.

The board of directors consists of 13 regional and seven nonregional members, none of whom may be governors or alternates. They may serve a maximum of two three-year terms. The largest single voteholder in the bank at year-end 2009 was Nigeria (B+/Stable/B), with 8.7% of total votes; the next largest voteholders were the United States (AAA/Stable/A-1+, 6.5%), Japan (AA/Stable/A-1+, 5.4%), Egypt (BB+/Stable/B, 5.1%), and South Africa (BBB+/Negative/A-2, 4.5%). Shares are allocated such that when all are subscribed, regional member countries will own 60% of the shares and non-regional member countries 40%, although voting power does not precisely mirror share ownership.

The president of the bank may serve a maximum of two five-year terms. Donald Kaberuka, formerly a minister for finance and economic planning for Rwanda (unrated), assumed the presidency on Sept. 1, 2005 and was re-elected for a second term in May 2010. AFDB's staff numbered 1,654 at year-end 2009.

The bank has formally been headquartered in Abidjan, Côte d'Ivoire since its inception; however, political unrest in that country prompted the bank to temporarily relocate to its backup facilities in Tunis, Tunisia (BBB/Stable/A-3) in February 2003, where it remains pending more settled conditions in Côte d'Ivoire. The bank has 25 field offices.

Balance Sheet

The bank's financial statements are expressed in UA. Under the agreement establishing the bank, UA1 is defined as the equivalent of SDR1. Financial statements are prepared in accordance with International Financial Reporting Standards. The 2009 statements were audited by KPMG, Paris. Year end is December 31.

On Dec. 31, 2009, AFDB had total assets of SDR17.184 billion (\$26.9 billion at SDR1 to \$1.56769), split evenly between loans and securities. The bank's assets grew by a rapid 36.7% in 2009, reflecting its response to increased demand from borrowers. We consider continued growth at 2009 levels to be unlikely over the medium term, as such levels would quickly threaten the bank's capital covenants.

Table 1

African Development Bank--Summary Balance Sheet					
(Mil. SDR)	--Year ended Dec. 31--				
	2009	2008	2007	2006	2005
Assets					
Cash, due from banks, demand obligations	323	596	99	133	74
Treasury investments	7,412	4,576	5,329	6,093	5,155
Accrued income and charges receivable on loans	294	452	436	456	431
Accumulated provision for impairment on accrued income and charges receivable on loans	-125	-116	-169	-223	-198

Table 1

African Development Bank--Summary Balance Sheet (cont.)					
Loans disbursed and outstanding	7,538	5,835	5,540	5,291	5,512
Accumulated provision for impairment on disbursed and outstanding loans	-102	-103	-196	-214	-195
Equity participation, of which:	250	210	192	123	172
Participation in African Development Fund	62	64	64	63	97
Accumulated provision for losses on equity investments	-16	-21	-2	-4	-3
Securities issued by entities in regional member countries	71	69	95	0	0
Non-negotiable instruments on account of capital	8	12	15	20	26
Derivative assets	764	736	425	273	286
Other assets	767	325	319	383	340
Total assets	17,185	12,571	12,082	12,332	11,601
Liabilities					
Borrowings, of which:	10,581	6,707	6,199	5,870	5,940
Portion of gross debt maturing during the next year	1,196	924	1,154	323	252
Derivative liabilities	477	360	591	482	317
Other liabilities	1,386	843	584	1,527	965
Total liabilities	12,443	7,911	7,374	7,879	7,223
Capital					
Paid-in capital	2,188	2,185	2,176	2,147	2,112
Other capital	2,553	2,475	2,532	2,305	2,266
Shareholders' equity	4,741	4,660	4,708	4,453	4,378
Off-balance-sheet items					
Callable capital from 'AAA' rated member countries	5,294	5,466	5,466	5,491	5,484

SDR—Special Drawing Rights

Capital And Risk Bearing Capacity

Capital

AFDB's authorized capital (that which its board of governors has authorized to be issued) totaled SDR22.12 billion at year-end 2009; of this amount, SDR21.82 billion--more than 99%--was subscribed (claimed by members). However, less than SDR2.4 billion of the latter amount was actually paid in (after adjustments for exchange rate changes).

AFDB's SDR19.458 billion of callable capital at year-end 2009 could be called by its board of governors, but only to meet obligations created by the bank's borrowings or guarantees. A capital call would oblige all members to contribute their pro rata shares of the amount called, but one member's failure to meet a call would not release other members from their obligations to do so. If a first-round call did not raise the amount required, subsequent calls could be made, but no member would be obliged to pay more than the amount to which it subscribed. No multilateral lending institution has ever issued a capital call to avoid default, and the willingness and ability of members to respond to such a call is undemonstrated. Accordingly, Standard & Poor's uses the callable capital from 'AAA' rated member countries as a proxy for the expected amount that would be forthcoming if there were a call on all callable capital.

AFDB's paid-in capital was supplemented by SDR2.55 billion of reserves as at Dec. 31, 2009, bringing shareholders' equity to SDR4.74 billion at the same date. The reserves are supported by modest but stable internal capital generation. No dividends are paid but the board of governors releases profits for development purposes. In 2009, SDR162.7 million was released for such purposes. This was down from SDR257.3 million in 2008 and reflected a reduction in core earnings.

In our opinion, AFDB's on balance sheet capital provides good coverage for risk undertaken. On Dec. 31, 2009, capital covered 28.5% of adjusted assets and, when included with loan loss reserves, was equal to 62.5% of gross loans. The major threat to capital is high concentrations to sovereign borrowers with low investment grade ratings. On Dec. 31, 2009, the bank's five leading borrowers, all of which had foreign currency ratings below 'A-', accounted for borrowings amounting to more than 100% of the bank's total equity. Positively, concentrations of lending to private sector borrowers are much smaller.

Risk-bearing capacity

Risk-bearing capacity is a measure of the losses that an MDFI can sustain before its liabilities exceed its assets (narrow risk-bearing capacity (NRBC)) or its assets plus 'AAA' callable capital (broad risk-bearing capacity (BRBC)). AFDB's NRBC is calculated by adding adjusted shareholders' equity and provisions for losses on its DRE.

Two adjustments are made to AFDB's reported shareholders' equity. First, AFDB's year-end 2009 balance sheet carries SDR8 million of non-negotiable instruments on account of capital as an asset; however, cash from these instruments may not be immediately available to the bank in a time of financial stress. Second, the balance sheet also carries AFDB's SDR62 million net equity holding in AFDF as an asset; this asset is illiquid and of uncertain value, and even more so in an event of severe financial stress. Accordingly, these two asset classes are assigned a value of zero, and reported shareholders' equity and total assets are reduced by the sum of the two to obtain adjusted shareholders' equity and adjusted total assets.

AFDB has three types of provisions for losses on its DRE. First, the bank's accrued income and charges receivable on loans--SDR294 million at year-end 2009--are treated as DRE. Accordingly, the provision for losses on these items--SDR125 million--is included in provisions for losses. Second, the bank had an accumulated provision for impairment of loans of SDR102 million--1.4% of loans disbursed and outstanding. Third, AFDB had an accumulated provision for impairment of equity investments of SDR16 million against its equity investments excluding AFDF at year-end 2009.

AFDB's NRBC is the sum of adjusted shareholders' equity plus provisions for losses on DRE and totaled SDR4.9 billion at year-end 2009, up by 2% from the previous year.

AFDB's BRBC is calculated by adding its 'AAA' callable capital to its NRBC. Of AFDB's callable capital of SDR19.5 billion at year-end 2009, SDR5.3 billion was from countries rated 'AAA' by Standard & Poor's. Accordingly, AFDB's BRBC totaled SDR10.2 billion at year-end 2009.

With the strong increase in DRE, the ratio of NRBC to DRE fell to 61% from 74% a year earlier. At the same time, BRBC was 126% of DRE. This is still strong compared with the capacities of other 'AAA' rated MDFIs.

Table 2

African Development Bank--Capital, Risk-Bearing Capacity, And Capital Adequacy					
(Mil. SDR, unless otherwise indicated)	--Year ended Dec. 31--				
	2009	2008	2007	2006	2005
Capital					
Authorized capital	22120	21,870	21,870	21,870	21,870
Subscribed capital	21817.6	21765.1	21,693	21,795	21,636
Callable capital, of which:	19458.3	19,4091	19,342	19,437	19,367
From 'AAA' rated member countries	5294	5,466	5,466	5,491	5,484
Paid-in capital*	2,188	2,185	2,176	2,147	2,112
Reserves	2,553	2,475	2,532	2,305	2,266
Shareholders' equity	4,741	4,660	4,708	4,453	4,378
Risk-bearing capacity					
Non-negotiable instruments on account of capital	-8	-12	-15	-20	-26
Participation in African Development Fund	-62	-64	-64	-63	-97
Adjusted shareholders' equity	4,671	4,585	4,629	4,369	4,255
Accumulated provision for impairment on accrued income and charges receivable on loans	102	103	169	223	198
Accumulated provision for impairment on loans disbursed and outstanding	125	116	196	214	195
Accumulated provision for losses on equity investments	16	21	2	4	3
Narrow risk-bearing capacity	4,915	4,824	4,996	4,810	4,651
Callable capital from 'AAA' rated member countries	5,294	5,466	5,466	5,491	5,484
Broad risk-bearing capacity	10,209	10,290	10,462	10,301	10,135
Development-related exposure					
Accrued income and charges receivable on loans	294	452	436	456	431
Loans disbursed and outstanding	7,538	5,835	5,540	5,291	5,512
Securities issued by entities in regional member countries	71	69	95	0	0
Equity investments excluding participation in African Development Fund	189	146	128	60	75
Guarantees	0	0	0	0	0
Total development-related exposure	8,092	6,501	6,198	5,806	6,019
S&P capital adequacy calculations					
Narrow risk-bearing capacity/adjusted total assets** (%)	28.7	38.6	41.6	39.3	40.5
Broad risk-bearing capacity/adjusted total assets** (%)	59.6	82.4	87.2	84.1	88.3
Narrow risk-bearing capacity/development-related exposure (%)	60.7	74.2	80.6	82.8	77.3
Broad risk-bearing capacity/development-related exposure (%)	126.2	158.3	168.8	177.4	168.4

SDR—Special Drawing Rights. *After cumulative gains and losses arising from exchange rate movements affecting NRM's capital contributions. **Total assets less non negotiable instruments on account of capital less participation in the African Development Fund.

Credit And Market Risk

Credit Risk

AFDB lends only to African countries and to public- and private-sector entities domiciled in African countries. Since 1995, AFDB has used the same eligibility criteria as the World Bank Group for determining which countries may

borrow from the bank. Under these criteria, only 13 of AFDB's 53 regional member countries are currently eligible in principle to borrow from AFDB, and one of these, Libya, has never borrowed from the bank. Two countries, Nigeria and Zimbabwe (unrated) are eligible for a blend of AFDB and AFDF lending, although Zimbabwe is currently barred from borrowing because it is under sanctions for delays in servicing its obligations. Thirty-eight countries are eligible to borrow from AFDF.

AFDB's DRE consists of its outstanding loans, including the accrued income and charges receivable on its loans; securities issued by entities based in its regional country members; its equity investments, excluding its investment in AFDF (since we in effect value that at zero); and guarantees outstanding. As of year-end 2009, the bank's DRE totaled SDR8.1 billion, significantly up by 24% from a year earlier. The strong growth reflected increased demand, and highlights AFDB's countercyclical role.

Historically, AFDB has focused on lending to the public sector. As of year-end 2009, 82% of outstanding loans were to public-sector borrowers. As of Dec. 31, 2009, AFDB's five largest sovereign borrowers accounted for 68% of the bank's total loan book. Alone, the largest sovereign borrower, Morocco (BBB-/Stable/A-3), accounts for 24% of the total loan book. Positively, with the overall loan portfolio having grown, the loan concentration on the five largest borrowers was 5% lower than in the preceding year. The bank's geographic concentrations remain in the more creditworthy north and south of Africa, where lending accounted for 51% and 26% of total lending respectively as at Dec. 31, 2009.

The bank is focusing increasingly on lending to private sector borrowers, which accounted for 18% of the total loan book on Dec. 31, 2009. In 2009, private sector lending grew by 27%, which was much faster than public sector growth in the previous two years. In terms of distribution by sector, loan and grant approvals in 2009 were concentrated in infrastructure (52%) and the multi-sector (29%), reflecting the medium-term strategy of the bank, and finance (11%), reflecting the adverse effects of the global financial crisis.

The bank invests in certain debt instruments issued by entities in its regional member countries for the purpose of financing development projects and programs. The fair value of investments in debt instruments issued in regional member countries as at Dec. 31, 2009 was UA70.8 million or 1.5% of adjusted total equity.

The bank also exposes itself to equity through its banking book to facilitate the development of the private sector in regional member countries. Consequently, a majority of the exposures are to regional development banks or investment funds. The bank does not seek to take a controlling stake in these companies but rather uses its presence to encourage others to participate. Internal regulations restrict equity investments to less than 15% of the aggregate amount of the bank's paid-in capital, reserves, and surplus in terms of used risk capital. As at Dec. 31, 2009 such exposure accounted for less than 5% of adjusted total equity.

Given the geographic scope of its activities, AFDB's asset quality compares poorly with that of other institutions of this type; however, loss-making loans have historically been very low as defaulted debt exposure has been restructured and repaid. Nonperforming assets (defined as impaired loans plus accrued income and charges receivable on loans) accounted for 5.2% of total loans and accrued income and charges receivable on loans as of Dec. 31, 2009. At the same date, loans overdue by more than 180 days accounted for 5.8% of the gross loan book. Reflecting the dynamics of lending, a majority of the bad debt consists of sovereign loans which were granted before a change to credit policy in 1995 and are more likely to be restructured or repaid than private sector debt. Positively, asset quality has improved since 2007 when the bank had a nonperforming loan ratio of 14.3% at year end. This

improvement reflects a lowering of nonperforming loan stock in 2008 and quick loan growth in 2009. The loan book is split into public and private sector lending at 82% and 18% respectively. Public sector loans overdue by more than 180 days represent 4% of total public sector loans, while private sector loans overdue by more than 180 days represent 1.9% of private sector loans.

In our opinion, loan loss reserves cover a moderate amount of AFDB's nonperforming loan book. While 56% would seem low for a financial institution operating in Africa, we view the bank's preferred creditor status as a key benefit in the recovery of nonperforming loans. This status means only that AFDB's loans are likely to be repaid before those of commercial or official bilateral lenders; it does not ensure that they will be repaid in full or on time. Given the economic distress of many of the bank's borrowing members, they have occasionally fallen behind on their payments. However, the bank has never had to write off any sovereign debt.

Table 3

African Development Bank--Financing By Purpose					
(Mil. SDR, unless otherwise indicated)	--Year ended Dec. 31--				
	2009	2008	2007	2006	2005
Approvals					
Project lending	3,791	1,373	1,462	515	597
Public and publicly guaranteed	2,780	642	646	245	459
Private and non-publicly guaranteed	1,010	731	816	270	138
Policy-based lending	1,522	136	20	411	148
Equity investments	142	146	185	0	35
Other	149	152	3	119	89
Total	5,604	1,807	1,670	1,045	869
Outstanding loans, development-related securities, and equity investments					
Private sector loans*	1,372	503	350	316	362
Public sector project loans*	2,577	2,432	2,459	2,587	2,849
Policy-based loans*	2,866	2,139	2,042	1,679	1,559
Other public sector loans*	724	760	690	1,025	1,104
Total outstanding loans	7,538	5,835	5,540	5,291	5,512
Securities issued by entities in regional member countries	71	69	95	0	0
Equity investments	250	210	192	123	172
Memo items					
Public sector as a % of total loans	81.8	91.4	93.7	94.0	93.4
Policy-based loan approvals as a % of total financing approvals	27.2	7.5	1.2	39.3	17.0
Policy-based loans as a % of total outstanding public sector loans	46.5	40.1	39.3	31.7	28.3

SDR—Special Drawing Rights. *Does not include accrued income and charges receivable on loans.

DRE quality and provisions for losses

Our index of DRE quality is an exposure-weighted average of the default rates associated with the respective long-term foreign currency sovereign credit ratings (see table 5). This figure is adjusted for the preferred creditor treatment that obligations to AFDB are expected to receive; the higher the index, the greater the risk embedded in the portfolio. The index has fallen since 2005, but it remains the case that by this measure, AFDB's DRE portfolio contained more embedded credit risk in percentage terms at year-end 2009 than all other 'AAA' rated MDFIs with

the exception of the Islamic Development Bank. This measure does not differentiate between public- and private-sector loans (the latter ordinarily carry more risk and thereby favor those institutions with relatively large private-sector DRE portfolios. This has been of limited significance in recent years, given the small percentage of private-sector loans in AFDB's portfolio. However, the bank expects private-sector loans to grow as a percentage of total loans over the medium term, and this measure would not reflect any resulting deterioration in the quality of the loan portfolio.

By some measures the historical performance of AFDB's loan portfolio has been worse than the performances of other rated MDFIs. The bank has never written off a sovereign loan and has written off no loans of any kind over the past five years. However, past-due payments of principal have been high; at year-end 2009, they stood at SDR238 million or 3% of outstanding loans. About 93% of the past-due principal was on public-sector loans. In addition, past-due interest and other charges were SDR210 million. Although this is still high for this type of institution, arrears were reduced significantly in March 2009, when Côte d'Ivoire's arrears were cleared by a combination of payments by the country, assisted by a donor country, and contributions from AFDB's Fragile States Facility.

As exemplified by the case of Côte d'Ivoire, AFDB's actual losses are likely to be substantially lower than the portfolio figures suggest; the bank has never written off a sovereign or sovereign-guaranteed loan. However, it did clear the Democratic Republic of the Congo's loans in arrears in 2002, albeit in such a way that the present value of the scheduled repayments equaled that of the original payments.

AFDB's credit risk is mitigated by the HIPC Initiative. At year-end 2009, 21 regional member countries were "completion point countries", eight were "decision point countries", and four were "pre-decision point countries".

AFDB maintains provisions for losses on both accrued interest and charges on loans and on the principal amount of the loans themselves. The accumulated provision on total outstanding loans was a low 1.5% at year-end 2009, down from 1.8% a year earlier. The small size of the accumulated provision reflects the fact that the bank expects the principal, interest, and charges of all of its public-sector loans to be repaid.

Table 4

African Development Bank--Development-Related Exposure Country Concentration					
--Year ended Dec. 31--					
Largest country exposures*/ratings*	2009	2008	2007	2006	2005
Largest	Morocco/BB+	Morocco/BB+	Morocco/BB+	Tunisia/BBB	Tunisia/BBB
Mil. SDR	1,824	1,445	1,229	1,180	1,227
% DRE	22.5	22.2	19.8	20.3	20.4
% Narrow risk-bearing capacity	37.1	30.0	24.6	24.5	26.4
2nd largest	Tunisia/BBB	Tunisia/BBB	Tunisia/BBB	Morocco/BB+	Morocco/BB+
Mil. SDR	1,177	1,087	1,145	1,095	853
% DRE	14.5	16.7	18.5	18.9	14.2
% Narrow risk-bearing capacity	23.9	22.5	22.9	22.8	18.4
3rd largest	Egypt/BB+	DR Congo/NR	DR Congo/NR	DR Congo/NR	DR Congo/NR
Mil. SDR	734	760	690	709	743
% DRE	9.1	11.7	11.1	12.2	12.3
% Narrow risk-bearing capacity	14.9	15.8	13.8	14.7	16.0
4th largest	DR Congo/NR	Egypt/BB+	Egypt/BB+	Nigeria/BB-	Nigeria/NR

Table 4

African Development Bank--Development-Related Exposure Country Concentration (cont.)					
Mil. SDR	724	653	561	401	463
% DRE	8.9	10.0	9.0	6.9	7.7
% Narrow risk-bearing capacity	14.7	13.5	11.2	8.3	10.0
5th largest	Botswana/A	Cote d'Ivoire/NR	Nigeria/BB-	Cote d'Ivoire/NR	Cote d'Ivoire/NR
Mil. SDR	642.622	311.975	375	360	362
% DRE	7.9	4.8	6.0	6.2	6.0
% Narrow risk-bearing capacity	13.1	6.5	7.5	7.5	7.8
Share of DRE of five countries of largest exposure	63.0	65.5	64.5	64.5	60.6
Percentage of narrow risk-bearing capacity of five					
countries of largest exposure	103.8	88.3	80.1	77.9	78.4

SDR—Special Drawing Rights. DRE—Development-related exposure. *Ratings as of balance sheet dates

Table 5

African Development Bank--Loan Quality And Accumulated Provisions For Losses					
(Mil. SDR, unless otherwise indicated)	--Year ended Dec. 31--				
	2009	2008	2007	2006	2005
Indicators of DRE quality					
Index of quality of development-related country exposure	9.6	12.9	13.3	14.4	15.1
Private sector loans as a % of total loans	18.2	8.6	6.3	6.0	6.6
Arrears on public sector loans and charges					
Côte d'Ivoire	0	346	331	292	222
Zimbabwe	302	279	245	222	199
Sudan	97	94	77	71	67
Somalia	12	12	11	10	10
Liberia	0	0	0	124	125
Comoros	0	0	0	13	13
Seychelles	0	0	0	0	22
Central African Republic	0	0	0	0	4
Total arrears on public sector loans and charges	412	731	664	731	661
Arrears on private sector loans and charges	29	26	23	16	5
Total arrears on loans and charges	441	757	687	747	666
of which: Principal payments in arrears	238	451	418	419	378
As a % of total outstanding loans	3.2	7.7	7.5	7.9	6.9
of which: Interest and other charges in arrears	12	306	269	328	300
Impaired/nonaccrual loans	270	275	603	670	702
As a % of total loans	3.6	4.7	10.9	12.7	12.7
Provisions for losses					
Accumulated provision for impairment on disbursed and outstanding loans	102	103	196	214	195
Accumulated provision for loans as a % of disbursed and outstanding loans	1.4	1.8	3.5	4.0	3.5
Accumulated provision for sovereign loans	90	90	184	199	179
As a % of sovereign loans	1.5	1.7	3.5	4.0	3.5
Accumulated provision for private sector loans	12	12	12	15	16

Table 5

African Development Bank--Loan Quality And Accumulated Provisions For Losses (cont.)					
As a % of private sector loans	0.9	2.5	3.5	4.9	4.4
Accumulated provision for loans as a % of impaired loans	37.7	37.3	32.5	32.0	27.7
Accumulated provision for accounts receivable for accrued income/charges receivable on loans	125	116	169	223	198
As a % of accounts receivable for accrued income/charges receivable on loans	42.7	25.6	38.7	48.9	45.8
Accumulated provision for equity losses	66.1	68.7	50.7	52.6	18.1
As a % of total equity investments	22.0	26.7	21.1	30.6	9.7

SDR—Special Drawing Rights

Market Risk

AFDB's investment portfolio is very diverse. As at Dec. 31, 2009 the treasury portfolio consisted of government and agency bonds (49%), supranational bonds (13%), and financial institutions and corporate bonds (21%). The portfolio is of good quality, with 65% rated 'AAA', 25% 'AA' and 10% 'A' or lower as of year-end 2009. In addition, the bank has a small asset-backed security portfolio, on which it incurred fair value losses in 2009.

ADFB is exposed to structurally high exchange and interest rate risk, but the bank monitors and controls this risk well. The agreement establishing AFDB requires liabilities in any currency to be matched with assets in the same currency. Because the bank borrows disproportionately in U.S. dollars and Japanese yen, it employs currency and cross-currency swaps to achieve the required matching; to avoid creating new currency mismatches, the bank requires borrowers to service their loans in the currency disbursed. However, since much of AFDB's assets are funded by shareholders' equity, the bank is still left with a net asset position that is exposed to translation risk when exchange rates fluctuate. It addresses this problem by matching, to the extent practicable, the composition of its net assets with the composition of SDRs. These policies resulted in translation adjustments of less than 0.1% of average assets at the ends of each of the past three years, despite sharp movements in the values of major currencies.

Interest rate risk is minimized by matching assets and liabilities. About two-thirds of loans and investments are floating rate and match the bulk of AFDB's liabilities. A smaller proportion of the loan book has variable lending rates, repriced at year end, and this is matched to a smaller borrowing pool. The fixed rate loan and investment component is limited to match the equity portion of funds. When direct matching is not available the bank uses interest rate swaps, with creditworthy counterparties, to manage the risk.

AFDB generally executes International Swaps and Derivatives Association master agreements and netting agreements with its derivative counterparties. Its bank and corporate investment counterparties are required to have ratings of 'A' or higher for exposures of six months or less, 'AA-' for exposures of six months to five years, and 'AAA' for exposures beyond 10 years.

Funding

AFDB's funding needs grew rapidly in 2009, with senior borrowings increasing by 65%, largely as a result of four \$1 billion issues in the course of the year. Positively, there were clear signs of continued appetite for AFDB paper, and spreads trended downwards towards year end.

In our opinion, AFDB's debt is very diverse in terms of investor base, currency, and maturity. Of the bank's bonds issued in 2009 58% were purchased by central banks and other official institutions, 17% by commercial banks, and 23% by fund managers. These investors were evenly split geographically, albeit with a concentration in the Americas. Consequently the U.S. dollar remains the major currency of funding (55%), followed by the Japanese yen (19%), the South African rand (9%), and Canadian dollar (8.4%). After swaps, the euro is also a major funding currency. The maturity profile of borrowings is fairly evenly spread. The largest refinancing needs occurring in the two-three year bucket when 25% of borrowings fall due. As of Dec. 31, 2009, 12% of the bank's funds matured within one year.

AFDB's internal capital framework caps total outstanding debt at 100% of usable capital (equity plus callable capital from non-borrowing members rated 'A-' or higher). At Dec. 31, 2009, outstanding debt represented 85% of usable capital. Consequently, funding, and therefore lending growth, is likely to be somewhat limited in 2010, although if the sixth capital increase is effective, this would increase AFDB's lending capacity under its capital framework.

Leverage

Standard & Poor's calculates four leverage ratios for comparative purposes:

- Gross debt to adjusted shareholders' equity (227% at year-end 2009);
- Gross debt to adjusted shareholders' equity plus 'AAA' callable capital (106%);
- Gross debt net of liquid assets to adjusted shareholders' equity (61%); and
- Gross debt net of liquid assets to adjusted shareholders' equity plus 'AAA' callable capital (29%).

All of these ratios increased substantially during 2009, reflecting the debt-financed expansion of AFDB's loan book. Having said that, they remain in line with the leverage ratios of other 'AAA' rated multilateral lending institutions.

Table 6

African Development Bank--Leverage					
(Mil. SDR, unless otherwise indicated)	--Year ended Dec. 31--				
	2009	2008	2007	2006	2005
Gross debt/adjusted shareholders' equity	226.5	146.3	133.9	134.4	139.6
Gross debt/adjusted shareholders' equity + 'AAA' callable capital	106.2	68.1	61.4	59.5	61.0
Gross debt net of liquid assets/adjusted shareholders' equity	60.9	33.5	16.7	(8.1)	16.7
Gross debt net of liquid assets/adjusted shareholders' equity + 'AAA' callable capital	28.6	15.6	7.6	(3.6)	7.3

SDR—Special Drawing Rights

Liquidity

AFDB's liquidity policy calls for maintaining liquidity in excess of a "prudential minimum level", which is defined as the sum of debt-service payments over the next year, the projected net loan disbursements for the next year, the loan equivalent of guarantees, and undisbursed equity investments. The bank typically carries liquidity far above the prudential minimum level. For instance, at year-end 2009, prudential minimum liquidity was SDR5.4 billion, while the bank's actual liquidity was SDR6.5 billion.

In our opinion, AFDB's management of liquidity is adequate, aided by the high amount of liquid assets the bank holds on balance sheet. At year-end 2009, liquid assets (including all cash and deposits and treasury investments, regardless of maturity) accounted for more than 45% of total assets and more than 73% of total borrowings; liquid assets as a percentage of undisbursed loans and equity investments and projected one-year debt service stood at 119%.

AFDB's access to emergency liquidity largely comes through callable capital from its shareholders. The only alternative source is a long-established euro commercial paper program, although this has been used infrequently.

Early in 2010, the program was increased to €2 billion from €1 billion. The bank does not intend to use the program as a primary funding source, but rather to bridge possible cash flow mismatches. Given the bank's ample liquidity and T+2 settlement convention, there are no backup lines in place for this program.

Table 7

African Development Bank--Liquidity					
(Mil. SDR, unless otherwise indicated)	--Year ended Dec. 31--				
	2009	2008	2007	2006	2005
AFDB liquidity*					
Prudential minimum liquidity	5,400	1,102	1,600	1,430	1,260
Liquidity	6,500	1,540	2,680	3,060	3,020
Liquidity as a % of prudential minimum liquidity	120.4	139.7	167.5	214.0	239.7
S&P liquidity measures					
Liquid assets/total assets	45	41	45	50	45
Liquid assets/gross debt	73	77	88	106	88
Liquid assets/undisbursed loans + equity investments + estimated one-year debt service	119	139	178	240	225

SDR—Special Drawing Rights. *Data for 2009 not comparable with previous years as AFDB revised the definition of eligible liquidity to include a larger portion of liquid assets in the held-to-maturity portfolio.

Profitability

As a development institution, AFDB does not seek to maximize income, but rather to earn a sufficient return to ensure its financial strength and to permit it to meet its development and other financing goals. Nevertheless, AFDB achieves moderate and stable returns for the risks undertaken. Profitability dipped in 2009 with core earnings amounting to 1.55% of average adjusted assets as at Dec. 31, 2009 compared with 2.47% a year earlier. The deterioration of operating revenues was predominantly caused by a reduction in interest income, which fell by 8% in 2009. Furthermore interest expenses increased by 20% during the year. In our opinion, a 25% reduction in net interest margin reflects the fact that AFDB does not pass on interest rate increases to customers during a time of stress, as two-thirds of total lending is floating rate lending and the bank has some flexibility to raise interest income if required. Instead, interest income from loans declined by 18% despite a 25% increase in loan volumes. Lower yields on treasury investments also suppressed the net interest margin. However, given the importance of interest income to total revenues (85.7% as at Dec. 31, 2009), the impact of the decision not to raise rates was significant.

Positively, investments performed more resolutely throughout the year and mitigated the fall in net interest margin. The bottom line was further eroded by a 26.7% increase in operational expenses. However, efficiency at AFDB is very high, with noninterest expenses accounting for only 22.1% of total revenues. Furthermore, the cost of risk remains low, reflecting the very low amount of loan losses.

Table 8

African Development Bank--Summary Income Statement					
(Mil. SDR, unless otherwise indicated)	--Year ended Dec. 31--				
	2009	2008	2007	2006	2005
Income from loans and debt securities	296	362	347	329	324
Income from investments and related derivatives	223	203	232	214	155
Interest and amortized issuance costs	-306	-252	-268	-245	-219
Other borrowing-related expenses	-76	-70	-7	-3	-22
Provision for impairment on loan charges	-11	62	53	-29	-7
Provision for impairment on loan principal	-0	101	17	-23	21
Provision for impairment on equity investments**	-2	-18	-1	-35	1
Provision for impairment on investments	3	-38	0	0	0
Other income (net)	27	9	-2	28	17
Administrative expense	-63	-47	-42	-37	-42
Other expense	-5	-7	-6	-5	-8
Operating income	231	305	324	194	221
Distribution of income approved by the board of governors	-163	-257	-120	-139	-144
Net income	68	47	204	55	77
(Loss)/gain on available-for-sale investments taken to equity	-19	-18	33	-9	6
Actuarial gains/losses on defined benefit plans	28	-86	-11	-7	-4
Total recognized income	77	-56	226	39	80

SDR—Special Drawing Rights

Ratings Detail (As Of September 15, 2010)***African Development Bank**

Counterparty Credit Rating

Foreign Currency

AAA/Stable/A-1+

Certificate Of Deposit

Foreign Currency

AAA

Commercial Paper

Foreign Currency

A-1+

Senior Unsecured (220 Issues)

AAA

Subordinated (6 Issues)

AA+

Counterparty Credit Ratings History

24-Jul-2003

Foreign Currency

AAA/Stable/A-1+

06-Jun-2001

AA+/Stable/A-1+

09-Aug-2000

AA+/Negative/A-1+

*Unless otherwise noted, all ratings in this report are global scale ratings. Standard & Poor's credit ratings on the global scale are comparable across countries. Standard & Poor's credit ratings on a national scale are relative to obligors or obligations within that specific country.

Additional Contact:

Sovereign Ratings; SovereignLondon@standardandpoors.com

Additional Contact:

Sovereign Ratings; SovereignLondon@standardandpoors.com

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