S&P Global
Ratings

RatingsDirect®

Research Update:

FONPLATA 'A-' Long-Term Rating Affirmed On Solid Operating Performance; Outlook Remains Stable

Primary Credit Analyst:
Alexis Smith-juvelis, New York + 1 (212) 438 0639; alexis.smith-juvelis@spglobal.com

Secondary Contact:
Constanza M Perez Aquino, Buenos Aires (54) 544-891-2167; constanza.perez.aquino@spglobal.com

Table Of Contents

Research Update:

FONPLATA 'A-' Long-Term Rating Affirmed On Solid Operating Performance; Outlook Remains Stable

Overview

- In our view, FONPLATA has a very strong financial profile supported by robust levels of capital and solid liquidity.
- We view FONPLATA as making steady progress achieving its operational and lending targets, and shareholders continue to support the fund with timely capital payments.
- We are affirming our 'A-/A-2' long- and short-term issuer credit ratings on FONPLATA.
- The stable outlook reflects our view that over the next two years, FONPLATA will maintain high capitalization levels to support the growth in its loan book, shareholders will continue to support the fund through timely capital contributions and treat the fund as a preferred creditor, and management will continue to achieve its growing lending and operational targets.

Rating Action

On July 26, 2018, S&P Global Ratings affirmed its 'A-/A-2' long- and short-term issuer credit ratings on Fondo Financiero para el Desarrollo de la Cuenca del Plata (FONPLATA). The outlook remains stable.

Rationale

Our 'A-' long-term issuer credit rating on FONPLATA reflects our view of its moderate business profile and very strong financial profile. These combined factors result in a stand-alone credit profile of 'a-'. The issuer credit rating on FONPLATA does not incorporate uplift for potential extraordinary support from shareholders because we rate all of FONPLATA's member shareholders lower than the institution.

Over the past few years, FONPLATA has made steady progress achieving its operational and lending targets. Historically, the fund's ability to fulfil its mandate had been constrained by gaps in governance and management structure. The institutional overhaul and reform beginning in 2012, followed by the creation of the executive presidency and the first strategic business plan in 2013, have strengthened FONPLATA's capacity to increase the pace of lending and have bolstered shareholder support.

Approval levels and disbursements grew by 3.6% and 34.6% in 2017, reaching US$327 million and US$171 million, respectively, in line with planned targets. This compares with approval levels under US$100 million a decade ago. Over the medium term, we expect FONPLATA to double its approval size, in line with its Institutional Strategic Plan 2018-2022, which largely focuses on expanding its lending portfolio and incorporating new members. While we believe the fund is well-positioned to fulfill its plan, which will increase its relevance in the region, we would look for a longer track record of the institution meeting these lending targets.

Shareholders continue to show support for the fund. Following FONPLATA's 2012 reform, shareholders approved its first general capital increase in 2013 for $1.15 billion, of which 30.4% is paid-in capital, with installments beginning in 2014 and ending in 2018. As of December 2017, members have paid on time and in full, including Brazil, which experienced payment delays on its second and third installments. Notably, the governors approved the second general capital increase, in 2016, for $1.375 billion, including $550 million of paid-in capital paid over seven yearly installments beginning in 2018.

Founded in 1974 by its five member countries Argentina, Bolivia, Brazil, Paraguay, and Uruguay, through the ratification of the River Plate Treaty, FONPLATA's mission is to support the integration of member countries and achieve inclusive development within the geographical boundaries of the River Plate basin area. As such, FONPLATA is particularly active in local municipalities and subregions on countries' borders, providing mainly loans for small and medium-size projects. Its niche focus favorably positions it to work with other funding organizations.

To strengthen its presence in the region and support larger ticket sizes, FONPLATA has engaged in various partnerships and co-financing arrangements with other multilateral lending institutions (MLIs). We have seen progress on this front as FONPLATA executed its first co-financed projects with Corporacion Andina de Fomento (CAF) and the OPEC Fund for International Development (OFID) in 2017. A Memorandum of Understanding (MOU) for strategic cooperation was signed with the New Development Bank (NDB) in 2017 to focus on financing in Brazil.

On June 18, 2018, FONPLATA signed an agreement with Mercosur to provide technical and financial assistance to the Fund for the Structural Convergence of Mercosur (FOCEM). The goal of the agreement is to optimize and enhance aspects of FOCEM's management and establish a co-financing framework for infrastructure projects in smaller, less developed countries. This arrangement could support an increased scale for FONPLATA's project size, though we would expect this to take some time to materialize.

Our business assessment also incorporates our assumption that all members will grant FONPLATA preferred creditor treatment (PCT). In our view, FONPLATA's track record of PCT and the treatment of nonperforming loans are somewhat weaker than peers in the region. All of FONPLATA's subnational loans are guaranteed by the respective sovereign. FONPLATA cancels disbursements on loans to the sovereign government if arrears exceed 90 days, and to all operations that the government guarantees if arrears exceed 120 days. Between 2002-2004, Argentina, Brazil, and Paraguay arrears exceeded 90 days. Furthermore, we have seen recurrent arrears with Brazilian municipalities over the past three years but these were paid within the 90-day period. As of December 2017, FONPLATA had one loan in arrears with a Brazilian municipality, which was subsequently cured in February 2018 and, thus, did not require the sovereign guarantee to be called upon.

Constraining our assessment of FONPLATA's business profile is its shareholder concentration in its five borrowing members. We believe that this presents an agency problem, which, in an extreme scenario, could pose governance risks. Argentina and Brazil are FONPLATA's two largest shareholders (holding 66% of the capital participation combined). However, each member country has equal voting rights, with all approvals and policies requiring four out of five votes in favor.

The creation of the executive presidency in 2011, tasked with leading the institutional transformation, has also led to enhanced accountability and transparency in decision-making. The fund strengthened its financial and risk management framework; implementation of this new set of policies, in our view, should support a pickup in the growth of its lending activities. This includes conservative limits to manage the growth in lending set at 3x equity, as well as exposure limits by country aiming at a more balanced loan portfolio composition. Recently, the fund hired a chief risk officer to separate planning and risk functions of the bank. Moreover, the first executive president of FONPLATA, Juan Notaro, took office in September 2012 and has been reelected for a second term from 2017-2022.

FONPLATA currently has offices in Bolivia and Paraguay, but it expects to open an office in Argentina in 2018. We view this as a positive development that will support its growth plans over the medium term and increase operational efficiencies. While we are likely to see some cost pressures and personnel bottlenecks during this expansionary phase, we believe FONPLATA will prudently manage these.

The other main factor we consider in our rating on FONPLATA is its very strong financial profile, reflecting its high capitalization and liquidity.

As of December 2017, FONPLATA's risk-adjusted capital (RAC) ratio after applying MLI adjustments was 43%, compared with 45% in 2016. The reduction resulted mainly from the growth of its outstanding loans, which were up by 22% to US$622 million, as well as the downgrade of Bolivia to 'BB-' on May 23, 2018. (The RAC ratio after diversification does not reflect the criteria correction published on July 11, 2017. We believe the impact of the correction on the ratio is not material to the rating.)

We expect the RAC ratio to deteriorate as FONPLATA increases lending activities at a faster pace to its five borrowing member countries, which will also weigh on the single-name concentration adjustment. At the end of 2017, the loan distribution was Uruguay (28%), Bolivia (26%), Paraguay (18%), Argentina (17%), and Brazil (11%). However, we assume that management will manage the fund prudently in line with its conservative financial limits and remain above the 23% threshold over the next two years.

FONPLATA is mainly equity funded, with total adjusted equity to adjusted total assets at 96% as of December 2017. We estimate that FONPLATA is structurally able to cover its scheduled loan disbursements without recourse to debt issuance. Since the fund has no significant debt liabilities, by definition its funding profile is undiversified. In 2018, it continues to diversify its funding sources, relying primarily on development bank financing, such as CAF with a contingent line for US$75 million, followed by a line of credit for US$100 million with the Inter-American Development Bank (IADB), as well as with the European Investment Bank (EIB) for US$60 million and the French Development Agency for US$20 million. Although the fund has no funding needs until October 2018, it recently registered with the Paraguay stock exchange for an issuance of US$100 million and is looking to issue in the international markets in the near term. We also see some positive developments in terms of funding source diversification with other MLIs (Asian Infrastructure Investment Bank and KfW Development Bank) and central banks.

FONPLATA follows a conservative liquidity policy, under which it's required to maintain a minimum level of liquidity sufficient to cover all liability payments and disbursements over the next 12 months. It holds high-quality liquid assets, which complies with its investment guidelines.

Our calculations of FONPLATA's liquidity incorporate stressed market conditions and assume no market access. Under these conditions, we calculate that FONPLATA's liquid assets are sufficient to service its borrowing and maintain operations through the next year without slowing the pace of planned disbursements. According to our calculations, FONPLATA's liquidity at the one-year horizon under stressed market conditions and assuming scheduled disbursements was 1.2x as of Dec. 31, 2017. However, we estimate that the bank would need to slow down planned disbursements under a stress scenario.

Outlook

The stable outlook is based on our view that over the next two years, FONPLATA will maintain its high level of capitalization. We expect its RAC ratio after diversification to remain well above 23%, even if the asset quality of the loan book weakens. Furthermore, the stable outlook incorporates our expectation that FONPLATA will continue increasing its lending activity, maintain solid support from shareholders, and remain a preferred creditor among its borrowers.

We could raise the ratings in the next two years if the fund maintains ample liquidity and robust capitalization levels while significantly enhancing multiple aspects of its business profile. This includes evidence of a stronger presence in the region; robust track record of shareholder support, including full and timely payment of capital installments due under recently approved general capital increases; and growing lending and disbursement in line with its targets. We could also raise the ratings if we see better loss experience as well as improved credit and risk monitoring.

We could lower the ratings if, in the next two years, we see a significant deterioration in the creditworthiness of member countries, as well as evidence of weakening capital support from shareholders, including signs of weakening PCT. We could also lower the ratings if FONPLATA's capital adequacy or liquidity deteriorates and the RAC ratio falls below the 23% threshold.

Related Criteria

- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings , April 7, 2017
- Criteria - Governments - General: Multilateral Lending Institutions And Other Supranational Institutions Ratings Methodology, Nov. 26, 2012
- Criteria - Financial Institutions - Banks: Multilateral Lending Institutions Capital Methodology And Assumptions, Dec. 6, 2010
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009

Related Research

- Sovereign Ratings History, July 5, 2018
- 2017 Annual Sovereign Default Study And Rating Transitions, May 8, 2018
- Introduction To Supranationals Special Edition 2017, Oct. 20, 2017
- How Brexit Could Impact Ratings On Supranational Institutions, April 10, 2017
- How Much Can Multilateral Lending Institutions Up The Ante?, April 12, 2016
- The Heat Is On: How Climate Change Can Impact Sovereign Ratings, Nov. 25, 2015
- How An Erosion Of Preferred Creditor Treatment Could Lead To Lower Ratings On Multilateral Lending Institutions, Aug. 26, 2013

Ratings List

Ratings Affirmed

FONPLATA

Sovereign Credit Rating	
Foreign Currency	A-/Stable/A-2

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. Complete ratings information is available to subscribers of RatingsDirect at www.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column.

Copyright © 2018 by Standard & Poor's Financial Services LLC. All rights reserved.

No content (including ratings, credit-related analyses and data, valuations, model, software or other application or output therefrom) or any part thereof (Content) may be modified, reverse engineered, reproduced or distributed in any form by any means, or stored in a database or retrieval system, without the prior written permission of Standard & Poor's Financial Services LLC or its affiliates (collectively, S&P). The Content shall not be used for any unlawful or unauthorized purposes. S&P and any third-party providers, as well as their directors, officers, shareholders, employees or agents (collectively S&P Parties) do not guarantee the accuracy, completeness, timeliness or availability of the Content. S&P Parties are not responsible for any errors or omissions (negligent or otherwise), regardless of the cause, for the results obtained from the use of the Content, or for the security or maintenance of any data input by the user. The Content is provided on an "as is" basis. S&P PARTIES DISCLAIM ANY AND ALL EXPRESS OR IMPLIED WARRANTIES, INCLUDING, BUT NOT LIMITED TO, ANY WARRANTIES OF MERCHANTABILITY OR FITNESS FOR A PARTICULAR PURPOSE OR USE, FREEDOM FROM BUGS, SOFTWARE ERRORS OR DEFECTS, THAT THE CONTENT'S FUNCTIONING WILL BE UNINTERRUPTED OR THAT THE CONTENT WILL OPERATE WITH ANY SOFTWARE OR HARDWARE CONFIGURATION. In no event shall S&P Parties be liable to any party for any direct, indirect, incidental, exemplary, compensatory, punitive, special or consequential damages, costs, expenses, legal fees, or losses (including, without limitation, lost income or lost profits and opportunity costs or losses caused by negligence) in connection with any use of the Content even if advised of the possibility of such damages.

Credit-related and other analyses, including ratings, and statements in the Content are statements of opinion as of the date they are expressed and not statements of fact. S&P's opinions, analyses and rating acknowledgment decisions (described below) are not recommendations to purchase, hold, or sell any securities or to make any investment decisions, and do not address the suitability of any security. S&P assumes no obligation to update the Content following publication in any form or format. The Content should not be relied on and is not a substitute for the skill, judgment and experience of the user, its management, employees, advisors and/or clients when making investment and other business decisions. S&P does not act as a fiduciary or an investment advisor except where registered as such. While S&P has obtained information from sources it believes to be reliable, S&P does not perform an audit and undertakes no duty of due diligence or independent verification of any information it receives. Rating-related publications may be published for a variety of reasons that are not necessarily dependent on action by rating committees, including, but not limited to, the publication of a periodic update on a credit rating and related analyses.

To the extent that regulatory authorities allow a rating agency to acknowledge in one jurisdiction a rating issued in another jurisdiction for certain regulatory purposes, S&P reserves the right to assign, withdraw or suspend such acknowledgment at any time and in its sole discretion. S&P Parties disclaim any duty whatsoever arising out of the assignment, withdrawal or suspension of an acknowledgment as well as any liability for any damage alleged to have been suffered on account thereof.

S&P keeps certain activities of its business units separate from each other in order to preserve the independence and objectivity of their respective activities. As a result, certain business units of S&P may have information that is not available to other S&P business units. S&P has established policies and procedures to maintain the confidentiality of certain non-public information received in connection with each analytical process.

S&P may receive compensation for its ratings and certain analyses, normally from issuers or underwriters of securities or from obligors. S&P reserves the right to disseminate its opinions and analyses. S&P's public ratings and analyses are made available on its Web sites, www.standardandpoors.com (free of charge), and www.ratingsdirect.com and www.globalcreditportal.com (subscription), and may be distributed through other means, including via S&P publications and third-party redistributors. Additional information about our ratings fees is available at www.standardandpoors.com/usratingsfees.

STANDARD & POOR'S, S&P and RATINGSDIRECT are registered trademarks of Standard & Poor's Financial Services LLC.