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Research Update:

African Trade Insurance Agency 'A' Ratings Affirmed On Criteria Revision; Outlook Remains Stable

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Overview

- Following a review of African Trade Insurance Agency (ATI) under our revised criteria for multilateral lending institutions, we are affirming our 'A' ratings on ATI and removing them from under criteria observation.
- In our opinion, ATI's preferred creditor treatment has stabilized, which, combined with positive developments concerning membership growth, consolidates our view of its enterprise risk profile.
- We are also affirming our 'A' financial strength rating.
- The stable outlook reflects our expectation that over the next two years, ATI will prudently manage sovereign claims. Additionally, we expect ATI will continue consolidating its role and relevance on the continent through steady progress expanding its shareholder base and underwriting activities balanced by the strengthening of key risk management functions.

Rating Action

On April 2, 2019, S&P Global Ratings affirmed its 'A' issuer credit rating and financial strength rating on African Trade Insurance Agency (ATI). The outlook remains stable.

At the same time, we removed the ratings from under criteria observation (UCO), where we placed them on Dec. 14, 2018, after publishing our revised multilateral lending institution (MLI) criteria.

Rationale

We affirmed our ratings on ATI based on its strong enterprise risk profile and adequate financial risk profile. ATI has no callable capital, so the long-term issuer credit rating reflects our assessment of ATI's stand-alone credit profile of 'a'. We outline these factors in our revised criteria, "Multilateral Lending Institutions And Other Supranational Institutions Ratings Methodology," published Dec. 14, 2018.

Established by treaty in 2001, ATI supports trade and investments in African member-state nations by providing comprehensive risk solutions such as political risk insurance (PRI) and commercial insurance products.

ATI's enterprise risk profile is informed largely by its preferred creditor treatment (PCT). ATI's statutes, as well as its participation agreement, confirms that sovereign members are responsible for reimbursing ATI for losses paid by the agency under its noncommercial insurance contracts.

During 2016 and 2017, ATI experienced growing sovereign claims that were not recovered within the 180-day recovery period we consider in our revised criteria. As of today, these have all been recovered, including an outstanding claim from the government of Tanzania of US$4.2 million, which was deducted from the country's capital contributions and has now been reinstated. Our calculated arrears ratio is 9%, reflecting the reimbursement delays that occurred in its sovereign exposure within our 10-year lookback period.

ATI has been proactive in reinforcing its preferred creditor status through a series of measures. Mandatory notifications and no objection requests for PRI transactions were introduced, as well as a sanctions regime involving interest charges on payment delays that exceed 180 days. Furthermore, ATI has worked to strengthen strategic partnerships with members, hiring a full-time membership liaison officer and actively engaging ministers of finance. We therefore expect that ATI will manage recoveries on sovereign claims and stabilize its PCT--crucial to its business and competitive advantage over other insurers in the region.

ATI's growing shareholder base reinforces the agency's strong policy importance, reflected by increased market penetration and membership growth, as well as its ties with key multilateral development banks.

Gross exposure has grown rapidly, increasing by 23% in 2017 to $2.4 billion, compared to $872 million in 2013. The bulk of ATI's exposure comes from its political risk insurance products relating to sovereign payment obligations and pure political risk, which account for 59.9% of exposure, followed by the single obligor credit risk insurance product, accounting for 32.3% as of December 2017. While exposure remains highly concentrated (20% of net exposure in Kenya as of December 2018), ATI reinsures a significant portion of its exposure and in 2016 began underwriting limited volumes of business in non-member countries, which has gradually supported the diversification of the portfolio.

ATI's expansion and relevance in the region is bolstered by its strong shareholder support. It currently has 23 paid-up shareholders, including the African Development Bank (AFDB), and its shareholder base has grown from seven initial member countries to 14 fully fledged member countries. In the past two years alone, Ethiopia, Côte d'Ivoire, South Sudan, and Zimbabwe joined.

In recognition of ATI's role as a catalyst in African economies, several multilateral institutions, such as the World Bank and the AFDB, will continue to offer unsecured concessional loans to eligible low-income African states to finance their acquisition of ATI shares.

Recently, the AFDB approved a US$14.2 million loan to Nigeria to support its membership with ATI, and Ghana's parliament approved ATI membership is expected to be finalized in 2019--a positive development as this would open up access to West African markets.

We view the agency's governance as prudent and transparent. ATI has been reinforcing its underwriting standards and risk management with an international consultancy enabled by a grant from the European Investment Bank. In 2017, the board approved a revision to its credit risk framework and, notably, increased its maximum net exposure to 8x from 6x equity.

We view this leverage limit as somewhat more aggressive than other peers we rate and consider that relaxing its risk limits to create additional underwriting capacity as a substitute for paid-in capital from new members or a general capital increase may point to weakened risk management standards and support from shareholders. Currently, ATI's actual leverage based on net exposure is under 4x as of December 2018.

Equally important, large dividend payouts--particularly given ATI's capital consumption trajectory--can, in our view, also weigh on our enterprise risk profile assessment. In 2018, ATI issued its first dividend payment to shareholders, but this is balanced by the agency's objective to help shareholders service loans related to their ATI share acquisitions.

ATI maintains a strong capital and earnings assessment. While its capitalization is extremely strong, this is balanced by our view of ATI's evolving enterprise risk management framework--which we assess at intermediate--as the entity expands and increases underlying risk exposure.

The agency experienced a rise in commercial arrears. In 2018, ATI recorded net incurred arrears of $5.1 million, compared to $4.7 million in 2017 and $1.6 million in 2016. In part explained by larger underwriting volumes and an increase in its statistical reserves, these levels are commensurate with other private insurers operating in Africa.

ATI has plans to hire key personnel to support its risk management capabilities congruent with its growth trajectory. ATI recently hired a claims and recovery officer and is looking to hire more personnel in this area. In 2019, the agency expects to hire a compliance and risk officer. We view the full staffing of these functions alongside measures to improve the holistic risk overview and the ability to demonstrate a track record of their application as crucial to support a stronger capital and earnings assessment.

We view ATI's liquidity as robust. In our view, liquid assets will remain generously in excess of the likely and stressed claim outflow.

Outlook

The stable outlook reflects our expectation that over the next two years, ATI will manage sovereign claims within the 180-day recovery period threshold. Additionally, ATI will continue consolidating its role and relevance on the continent through steady progress expanding its shareholder base and underwriting activities.

We could raise the ratings if ATI significantly expands its shareholder base, supporting exceptional market penetration in the region, and maintains a solid record of PCT combined with strengthening key managerial and risk functions to support its growth.

We could lower the ratings if evidence of weakening shareholder support were to emerge, such as a reemergence of diminishing preferred creditor status, indicated by sizable or prolonged sovereign claims from sovereign members. Furthermore, ATI's role and ability to fulfil its public policy mandate could be constrained by significant delays in membership growth and paid-in capital installments, which, if not compensated by a general capital increase, could weigh on the rating. Also, relaxing risk constraints, without a more robust risk management framework in place, to support the underwriting business could also lead to a downgrade.

Ratings Score Snapshot

Issuer Credit Rating	A/Stable/--
SACP	a
Enterprise Risk Profile	Strong
Policy Importance	Strong
Governance and management	Adequate
Financial Risk Profile	Adequate
Extraordinary Support	0
Callable capital	0
Group Support	0
Holistic Approach	0

Related Criteria

- Criteria | Governments | General: Multilateral Lending Institutions And Other Supranational Institutions Ratings Methodology, Dec. 14, 2018

- Criteria | Insurance | Specialty: Trade Credit Insurance Capital Requirements Under S&P Global Ratings' Capital Adequacy Model, Dec. 6, 2013
- Criteria | Insurance | General: Enterprise Risk Management, May 7, 2013
- Insurers: Rating Methodology, May 7, 2013
- Criteria | Insurance | General: Refined Methodology And Assumptions For Analyzing Insurer Capital Adequacy Using The Risk-Based Insurance Capital Model, June 7, 2010
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009
- General Criteria: Understanding S&P Global Ratings' Rating Definitions, June 3, 2009

Related Research

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

Ratings List

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Ratings Affirmed

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