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Research Update:

Outlook On International Finance Facility for Immunisation Revised To Negative; 'AA/A-1+' Ratings Affirmed

Primary Credit Analyst:

Elie Heriard Dubreuil, London (44) 207-176-7302; elie.heriard.dubreuil@standardandpoors.com

Secondary Contact:

John B Chambers, CFA, New York (1) 212-438-7344; john.chambers@standardandpoors.com

Analytical Group Contact:

SovereignEurope; SovereignEurope@standardandpoors.com

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Overview

- International Finance Facility for Immunisation (IFFIm) is a funding vehicle for the GAVI Alliance (formerly the "Global Alliance for Vaccines and Immunisation", GAVI). While we assess that donor governments' willingness to support IFFIm will remain strong, the outcome of the GAVI replenishment early next year could inform our view of the ongoing policy importance of IFFIm, positively or negatively.
- We revised the outlook on France to negative on Oct. 10, 2014. France is IFFIm's second-largest donor government, representing more than one-quarter of IFFIm's total expected future cash receipts.
- We are revising our outlook on IFFIm to negative and affirming the long- and short-term 'AA/A-1+' issuer credit ratings.
- The negative outlook reflects our view of potential downside risks that we believe could diminish the credit quality of IFFIm's grant receivables.

Rating Action

On Nov. 14, 2014, Standard & Poor's Ratings Services revised the outlook on the International Finance Facility for Immunisation (IFFIm) to negative from stable. At the same time, we affirmed the issuer credit ratings at 'AA/A-1+'.

Rationale

The outlook revision reflects our view of potential downside risks that could weigh on the capacity and willingness of donor governments to honor their pledges to IFFIm. On Oct. 10, 2014, we revised to negative the outlook on France, IFFIm's second-largest donor government, representing more than one-quarter of IFFIm's total expected future cash receipts.

However, IFFIm could have a significant role to play in the fight against the ebola epidemic--and thereby reinforce its role--if manufacturers manage to develop an approved vaccine and IFFIm emerges as the vehicle of choice to finance its distribution to poor countries. Also, in January 2015 we expect donors to announce their potential commitments to GAVI and IFFIm for 2016-2020 during the second replenishment of the program. We anticipate the bulk of the contributions for the second replenishment will come from existing donors.

IFFIm is a multilateral institution established as a charity in the U.K. in

2006. Its purpose is to fund the immunization and vaccine procurement programs of GAVI, a public-private partnership whose members include the World Health Organization, the U.N. Children's Fund, International Bank for Reconstruction and Development (IBRD, commonly referred to as the World Bank), the Bill and Melinda Gates Foundation, governments of both developing and industrialized countries, research and health institutes, vaccine producers, and civil society organizations.

The ratings on IFFIm reflect our view of the commitment of its highly rated contributors to its mandate of supporting child immunization programs in the world's poorest countries. While we believe donor governments' willingness to support IFFIm will remain strong, the outcome of the GAVI replenishment early next year could inform our view on the ongoing policy importance of IFFIm, positively or negatively. In addition, general elections are to be held in 2015 in the U.K. The rise of UKIP, a right-wing populist party that advocates a dramatic reduction in foreign aid, might affect the support of IFFIm's largest contributor as mainstream political parties risk catering to populism.

IFFIm has been an important source of funding for GAVI since 2006. During 2006-2013, it provided 39% of GAVI contributions. Through raising debt against future Official Development Assistance (ODA) for vaccinations, IFFIm has allowed GAVI to accelerate its immunization programs. Having reached a greater critical mass, GAVI is now entering into steadier territory for vaccinations and support for public health, implying less reliance on IFFIm for front-loading funding. We note, however, that IFFIm will still disburse funds to GAVI throughout the life of its borrowing program, extending through to 2030.

Under our criteria, we determine support for IFFIm by evaluating the support of IFFIm's strongest contributors. The U.K. is the largest contributor; it has pledged more than 50% of the funds still to be received by IFFIm. France follows, with close to 27% of pledges. Other highly rated contributors include Australia, Norway, The Netherlands, and Sweden with respectively slightly less than 5%, 3%, 2%, and 1% of the ODA to be received. Other contributors are Italy (with 8%), Spain (3%), and South Africa (less than 1%).

IFFIm operates by issuing bonds, backed by sovereign government commitments, to provide annual grants over two decades and by disbursing the bond proceeds to GAVI to fund its programs. This not only front-loads GAVI's funds, but also enhances its ability to provide multiyear grants to recipient governments. IFFIm would be at risk if countries in a reference portfolio, representing 72 of the world's poorest nations, go into protracted arrears to the IMF. If this happens, contributor governments are released from a portion of their scheduled annual payments under their pledges, which means that fewer funds will be available to reimburse IFFIm's debt holders.

To measure IFFIm's risk-adjusted leverage, we calculate the coverage of the outstanding debt by pledges from highly-rated sovereigns under a severe stress scenario. This coverage ratio improved to 1.7x as of Oct. 31, 2014, compared to 1.2x as of year-end 2013, due to debt maturing and absence of new issuance.

When assuming that IFFIm will increase its gearing in the coming six years to reach a limit agreed with the IBRD, this ratio decreases to 1.2x by 2020. Our coverage ratio includes only pledges from contributors rated at the level of IFFIm or above (that is, currently rated 'AA' or above). When excluding France, we expect the ratio to fall below 1x as of year-end 2014. A ratio below 1x indicates a shortfall of highly rated pledges under our severe economic stress scenario (see appendices to our criteria "Understanding Standard & Poor's Ratings Definition" for examples and specifications of a severe 'AA' stress scenario). Under this scenario, we estimate that a portion of countries included in the IFFIm reference portfolio would enter in protracted arrears with the IMF, and IFFIm's sovereign pledge receivables would therefore decrease accordingly.

IFFIm's board of directors has established its own limit for maximum gearing using different assumptions. IBRD calculates this ratio for the board at least quarterly. In 2013, IBRD introduced an additional risk management buffer in this calculation, due to its large uncollateralized swap exposure to IFFIm. Under this formula, IFFIm's maximum gearing ratio is currently set at 57%. The actual gearing ratio has been significantly below this limit--at about 40% for the past five years--but we expect IFFIm to gradually gear up toward that limit by 2020.

Although IFFIm had previously experienced payment delays from several contributors, we also note that all payments have been received in full as of Oct. 31, 2014. Delays of more than a few days have generally arisen from donors rated lower than IFFIm. We consider the rare delays from highly rated countries to have been administrative in nature and not to have reflected the contributors' ability or willingness to support IFFIm.

IFFIm also incurs rollover risk as its debt financing is for shorter tenors than its receivable pledges. To allay part of this funding risk, IFFIm maintains a minimum liquidity equivalent to its cumulative contracted debt service payments for the next 12 months. In addition, the management can stop disbursements if the 12 months' debt service is not covered. IBRD recalculates and resets this limit quarterly. At Dec. 31, 2013, cash and funds held in trust totaled \$1,025 million.

Outlook

The negative outlook reflects potential downside risks that we believe could diminish the credit quality of IFFIm's grant receivables.

We could stabilize the ratings if risk-adjusted leverage were commensurate with the rating level. This could occur, for example, if we were to revise the outlook on the long-term rating on France to stable. We could also stabilize the ratings on IFFIm if we assessed its policy importance as reinforced, for example following a successful second replenishment in which a large proportion of GAVI pledges was made to IFFIm.

We could lower the ratings on IFFIm if highly rated contributors were to reduce their support (say by falling into arrears on donor grants); if substantially more grant-recipient governments go into protracted arrears to the IMF; if IFFIm experiences funding pressure; or if we were to lower the sovereign credit ratings on France. The latter would imply our risk-adjusted coverage ratio falling below the threshold required to maintain the rating at the current level in our stress scenarios.

Related Criteria And Research

Related Criteria

- Multilateral Lending Institutions And Other Supranational Institutions Ratings Methodology, Nov. 26, 2012
- Understanding Standard & Poor's Rating Definitions, June 3, 2009

Related Research

- International Finance Facility for Immunisation Long-Term Rating Lowered to 'AA' On France Downgrade; Outlook Stable, Nov. 8, 2013
- France Outlook Revised to Negative; 'AA/A-1+' Ratings Affirmed, Oct. 10, 2014
- Supranationals Special Edition 2014, Oct. 8, 2014

Ratings List

Ratings Affirmed; CreditWatch/Outlook Action

	To	From
International Finance Facility for Immunisation		
Sovereign Credit Rating		
Foreign Currency	AA/Negative/A-1+	AA/Stable/A-1+
Senior Unsecured	AA	AA

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