Rating Action: Moody's downgrades International Finance Facility for Immunisation to Aa1 from Aaa, negative outlook maintained

Global Credit Research - 05 Mar 2013

Actions follow weakening of UK sovereign credit profile

New York, March 05, 2013 -- Moody's Investors Service has today downgraded the long-term issuer rating of the International Finance Facility for Immunisation (IFFIm) to Aa1 from Aaa and is maintaining a negative outlook on the rating. The short-term issuer rating of IFFIm remains unchanged at Prime-1.

Moody's decision to downgrade the rating follows the recent downgrade of the UK to Aa1 from Aaa. For more details, please refer to Moody's press release: http://www.moodys.com/research/Moodys-downgrades-UKs-government-bond-rating-to-Aa1-from-Aaa--PR_266844. The UK is the single largest donor to IFFIm, pledging around 50% of remaining donor payments. This donor concentration allows for a low-probability, but high-severity event risk in IFFIm's credit profile. The deterioration in creditworthiness of the UK sovereign caused the weighted median rating of IFFIm's donor base to fall from Aaa to Aa1.

The negative outlook on IFFIm's long-term rating reflects the negative outlook on five of IFFIm's nine donors, namely France, Italy, Spain, the Netherlands and South Africa. The donors' negative outlooks indicate a marginal reduction in the certainty that these sovereigns will fulfil their financial obligations, which could negatively affect IFFIm's market access.

RATIONALE FOR DOWNGRADE

The one-notch downgrade of IFFIm's rating to Aa1 from Aaa follows the downgrade of the UK's government bond rating to Aa1 from Aaa on 22 February 2013. The UK is the largest of IFFIm's nine donors with a share of around 50% of remaining payments. As a result of the deterioration in the UK's creditworthiness, the weighted median rating of IFFIm's donor base went from Aaa to Aa1.

Further significant concentration results from Moody's belief that there is correlation between three of IFFIm's euro area donors. France, Italy, and Spain pledge 27%, 9%, and 3%, respectively, of remaining donor payments. As a result of the correlation assumption, Moody's considers these three sovereigns' combined 39% of remaining pledges to be a concentration risk. Therefore, combined with the UK, IFFIm's donor structure is 89% concentrated around two risks, both rated Aa1. France's rating maintains a negative outlook due to the protracted euro area sovereign debt crisis, as do the ratings of Italy and Spain.

Moody's notes that IFFIm has four donors with a Aaa rating (the Netherlands has a negative outlook and Australia, Norway, and Sweden have stable outlooks) and there is an exceptionally low chance that these four sovereigns would renege on their commitments to IFFIm. Each sovereign donors' pledge to IFFIm is legally binding. However, as there is no additional legal requirement for the donors to support IFFIm above and beyond each one's contractual commitment, Moody's cannot consider the strength of the four remaining Aaa-rated donors as a rationale for IFFIm's rating exceeding those of the UK and France.

IFFIm's rating is closely linked to the creditworthiness of its sovereign donors because IFFIm's revenue structure is reliant on the receipt of donors' pledges. Unlike multilateral development banks (MDBs), IFFIm does not have paid-in capital. Paid-in capital allows MDBs to potentially carry sufficient intrinsic financial strength to cause their ratings to exceed the ratings of their sovereign shareholders.

Moody's does note, however, that IFFIm's risk-management function provides strength to its structure. To mitigate the risk of donor commitments falling short of the original committed amount, IFFIm is subject to a gearing ratio limit -- a solvency model over the remaining life of IFFIm -- that restricts net debt to around 70% of the net present value of remaining donor payment amounts. The strength of the gearing ratio limit is not only a function of how well the risks are modelled in order to set the limit, but a function of the flexibility of the limit to account for increasing risks, and, more importantly, the flexibility for IFFIm's treasury manager to delay debt issuance and grant disbursements in order to respect the gearing ratio limit.

While the actual gearing ratio level is currently around 43%, Moody's does not consider it to be a substantial-enough solvency buffer to absorb the increased event risk represented by the downgrade of IFFIm's largest donors.

RATIONALE FOR NEGATIVE OUTLOOK

The negative outlook on IFFIm's long-term rating reflects the negative outlook on five of IFFIm's nine donors, namely France, Italy, Spain, the Netherlands and South Africa. The negative outlooks indicate a marginal reduction in the certainty that these sovereigns will fulfil their financial obligations, which, among other things, could negatively affect IFFIm's market access.

Given that IFFIm does not have paid-in capital, its structure is dependent on market access in order to obtain the funds with which to operate. As a result of a front-loading of bond issuance at the very start of its operations and a relatively shorter-term maturity structure of its debt (around 4-5 years), it is essential that IFFIm retain access to markets in order to service its debt, including for refinancing. While IFFIm has not experienced funding stress to date, and has maintained strong market access during the global financial crisis and throughout the prolonged euro area debt crisis, Moody's considers there to be non-negligible refinancing risk in the event that a tail risk event were to occur. Namely, should one of the sovereign donors renege on its commitment to IFFIm, it is possible that IFFIm's market access could be negatively affected. While its liquidity policy protects bondholders for one year, should IFFIm not be able to regain market access quickly enough to refinance the following years' debt service, bondholders could face a loss after the liquid funds and other resources were exhausted.

WHAT COULD MOVE RATINGS DOWN/UP

Downward pressure on IFFIm's rating could be driven by a deterioration in the creditworthiness of its sovereign donors. IFFIm's rating is particularly sensitive to changes in the ratings of its two largest donors: the UK and France. A downgrade of the rating could also be triggered by a weakening of the gearing ratio limit mandate or a change in treasury manager, neither of which Moody's considers likely.

Given that the outlook on IFFIm's Aa1 rating is currently negative, the rating is unlikely to experience upward pressure in the near term. However, Moody's could change the outlook for IFFIm's ratings to stable if the euro area debt crisis were to stabilise or France's rating outlook were to return to stable.

RATING METHODOLOGY

IFFIm is a financing facility whose purpose is to accelerate and facilitate funding for immunisation programmes carried out by the Global Alliance for Vaccines and Immunisation (GAVI) in the world's poorest countries. IFFIm issues bonds to finance GAVI programmes, and sovereign donor payments are used to repay the bonds. The amount and timing of donor payments are predetermined and outlined in legally-binding grant agreements while amounts and maturities of bonds issued are set according to the recommendation of the treasury manager, which has been, from inception, the International Bank for Reconstruction and Development (IBRD).

The rating of IFFIm was assigned by evaluating factors that Moody's considers relevant to the specific characteristics of the facility, reflecting its dual nature as a financing facility and a vehicle of international public policy. These factors include the issuer's (i) governance and risk management policies and processes; (ii) capital adequacy, asset quality and liquidity management; and (iii) ability to rely on shareholders or members to fulfil financial commitments and for financial support. Moody's compared these attributes against other issuers with similar mandates which Moody's believes incur similar credit risks, and believes the rating of IFFIm is consistent with those of other issuers with similar credit risk.

REGULATORY DISCLOSURES

For ratings issued on a program, series or category/class of debt, this announcement provides certain regulatory disclosures in relation to each rating of a subsequently issued bond or note of the same series or category/class of debt or pursuant to a program for which the ratings are derived exclusively from existing ratings in accordance with Moody's rating practices. For ratings issued on a support provider, this announcement provides certain regulatory disclosures in relation to the rating action on the support provider and in relation to each particular rating action for securities that derive their credit ratings from the support provider's credit rating. For provisional ratings, this announcement provides certain regulatory disclosures in relation to the provisional rating assigned, and in relation to a definitive rating that may be assigned subsequent to the final issuance of the debt, in each case where the transaction structure and terms have not changed prior to the assignment of the definitive rating in a manner that would have affected the rating. For further information please see the ratings tab on the issuer/entity page for the respective issuer on www.moodys.com.

For any affected securities or rated entities receiving direct credit support from the primary entity(ies) of this rating action, and whose ratings may change as a result of this rating action, the associated regulatory disclosures will be those of the guarantor entity. Exceptions to this approach exist for the following disclosures, if applicable to jurisdiction: Ancillary Services, Disclosure to rated entity, Disclosure from rated entity.

Please see www.moodys.com for any updates on changes to the lead rating analyst and to the Moody's legal entity that has issued the rating.

Please see the ratings tab on the issuer/entity page on www.moodys.com for additional regulatory disclosures for each credit rating.

Annette Ching-See Swahla
Analyst
Sovereign Risk Group
Moody's Investors Service, Inc.
250 Greenwich Street
New York, NY 10007
U.S.A.
JOURNALISTS: 212-553-0376
SUBSCRIBERS: 212-553-1653

Bart Jan Sebastian Oosterveld
MD - Sovereign Risk
Sovereign Risk Group
JOURNALISTS: 212-553-0376
SUBSCRIBERS: 212-553-1653

Releasing Office:
Moody's Investors Service, Inc.
250 Greenwich Street
New York, NY 10007
U.S.A.
JOURNALISTS: 212-553-0376
SUBSCRIBERS: 212-553-1653