European Bank for Reconstruction and Development

RATINGS:
AAA/Stable/A-1+
Initial rating (1991) ....AAA

BASIC DATA (END-DEC. 2006):
Total assets.............€30,691 mil.
..........................(US$40,420 mil.)
Development-related exposure..................€13,802 mil.
Adjusted paid-in capital ....€5,006 mil.
Adjusted shareholders' equity ....€11,980 mil.
Paid-in capital receivable.....................€192 mil.
Callable capital from 'AAA' shareholders ...€9,275 mil.
Date last general capital increase approved..............1996
Amount of increase ....€10 bil.
Amount to be paid in ...€2.25 bil.
Date last scheduled payment due........................2009
Total shareholders (countries plus EU, EIB)...........63
Countries where development-related exposure 29

PURPOSE:
To foster the transition to market economies by the Central and Eastern European and Commonwealth of Independent States countries by promoting private and entrepreneurial initiatives. EBRD pursues these objectives principally by lending (primarily to the private sector and to public sector projects supporting the private sector), making equity investments, and providing guarantees.

ISSUER WEBSITE:
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Rationale

The ratings on the European Bank for Reconstruction and Development (EBRD) are based upon:

- An extremely strong capital position, enhanced by among the highest-quality callable capital of any multilateral development finance institution (MDFI), and ample liquidity;
- Prudent financial management and policies; and
- Excellent franchise value, reflecting EBRD's status as the largest multilateral provider of financing to its countries of operation.

EBRD began operation in 1991 with a mandate to help the countries of Central and Eastern Europe and the Commonwealth of Independent States (CIS) transition to market economies, principally by lending (primarily to the private sector), making equity investments, and providing guarantees. Following the division of the Republic of Serbia and Montenegro (now the Republic of Serbia and the Republic of Montenegro) in June 2006, its shareholders consist of 61 countries plus the European Community and the European Investment Bank. Its member countries include the 27 members of the European Union, 10 of which are countries of operation, where EBRD currently has loans, equity investments, and/or guarantee exposure (development-related exposure [DRE]); 19 other countries of operation, including Mongolia, which became a country of operation in October 2006; five other European countries (including the Swiss Federation); and 10 non-European countries, including the U.S. and Japan.

The bank's assets totaled €30.7 billion at year-end 2006, of which €8.3 billion was loans and debt securities issued by its clients and €5.1 billion was equity investments; EBRD also issued €438 million in guarantees.

At year-end 2006, 28% of EBRD's loans and equity investments were to/in the nine countries classified for internal management purposes as advanced, 37% to/in the 19 countries classified as early/intermediate, and 26% to/in the Russian Federation (the remainder was regional). EBRD's exposure to/in Russia and the early/intermediate countries was relatively concentrated in loans, while that to/in the advanced countries was relatively concentrated in equity investments. In keeping with the emphasis on private sector development, only 24% of EBRD's loans was sovereign or sovereign-guaranteed; the sovereign loans were relatively concentrated in the early/intermediate countries and were typically for infrastructure projects that support the private sector.

EBRD's DRE at year-end 2006 had relatively low country concentration compared to that of most MDFIs. That to/in Russia, its largest country of exposure, equaled 26% of the total (and 30% of reserves for losses plus adjusted shareholders' equity [narrow risk-bearing capacity {NRBC}]); Romania (10%), Croatia (8%), and Poland (8%) were the countries of next largest exposure. EBRD's portfolio was seemingly less diversified with respect to sector of activity, with finance accounting for 46% of outstanding loans and equity investments at year-end 2006; however, this percentage is misleading, since a portion of the lending to financial institutions is on-lent to other sectors. Other important sectors include transportation and construction (13%), manufacturing (13%), energy and power generation (8%), and extractive industries (3%).

About 37% of EBRD's equity investments of €5.1 billion at year-end 2006 represented holdings in equity funds. Less than 47% of EBRD's direct investments were unlisted, a marked decline from the more than 61% at year-end 2005. EBRD regularly sells a portion of its equity investments and realized gains of more than €1.3 billion during 2006, in contrast to €640 million and €122 million during 2005 and 2004.

Since most of EBRD's loans are private sector, there is far more risk embedded in its loan portfolio than in those of most MDFIs (all or most of whose loans are sovereign or sovereign-guaranteed). EBRD has written off €122 million of loans over the past five years. However, by all measures, the quality of EBRD's loan portfolio has increased in recent years.

At year-end 2006, EBRD maintained provisions for impairment of 0.7% on its outstanding sovereign loans (despite never having written off a sovereign loan); and general and specific provisions of 4.9% and 0.3%, respectively, of nonsovereign loans. Because of accounting changes, EBRD no longer maintains a reserve against losses on its equity investments or guarantees.

EBRD's €341 million in provisions for impairment on loans at year-end 2006 was buttressed by €11,980 million in shareholders' equity, adjusted for the €192 million in receivables from members (mostly for capital contributions not yet due) carried as an asset. NRBC was more than 89% of EBRD's DRE at year-end 2006, up from 79% one year earlier. When EBRD's 'AAA' callable capital is added to NRBC (the sum being broad risk-bearing capacity), this percentage increases to almost 157%. EBRD expects to receive its remaining capital contributions by year-end 2009; however, it anticipates no additional general capital increases in the future.

With the exception of 1998, when it suffered a loss as the result of taking provisions of €553 million for its exposure in its countries of operation, EBRD has been profitable every year since it began operating. Net income increased sharply in 2006, to €2,389 million from the restated €1,522 million and €393 million of 2005 and 2004, respectively. This €867 million increase was principally the result of a nearly €700 million increase in realized gains on the sales of equity investments. Net interest income before loan-loss provisions increased a more modest €92 million.

Outlook

The outlook for EBRD's 'AAA' rating is stable. Even with its large and growing exposure to the private sector and its increased focus on financing in its early and intermediate countries of operations, the bank's capital position and liquidity are strong enough to withstand a period of severe global financial stress. EBRD will also benefit from the receipt of modest additional installments of paid-in capital and has, to date, received preferred creditor treatment from its countries of operations.

A full analysis on the **European Bank for Reconstruction and Development** is available to RatingsDirect subscribers at www.ratingsdirect.com. ■

European Bank for Reconstruction and Development

Selected financial information (Mil. €, unless otherwise indicated)	2006	2005	2004	2003	2002
	—Year ended Dec. 31—				
Assets					
Placements with and advances to credit institutions	3,135	3,800	685	2,165	990
Collateralized placements	2,573	1,475	1,645	1,465	2,933
Debt securities	8,595	7,618	6,126	5,971	5,197
Outstanding loans and debt securities*	8,311	7,819	7,613	6,803	6,824
Provisions for loans and debt securities	(341)	(323)	(508)	(465)	(534)
Outstanding share investments	5,053	4,179	2,652	2,611	2,620
Provisions for outstanding share investments	0	0	0	(593)	(639)
Paid-in capital receivable	192	327	568	848	1,248
Derivative financial instruments	2,130	2,318	2,622	2,736	652
Other assets	1,043	1,171	629	505	823
Total assets	30,691	28,384	22,032	22,045	20,112
Liabilities					
Borrowings, of which:	16,816	16,908	13,879	14,223	13,362
Portion of gross debt maturing during the next year	5,972	5,295	3,144	4,025	2,604
Derivative financial liabilities	506	356	570	926	136
Other liabilities	1,197	1,239	700	710	756
Total liabilities	18,519	18,503	15,149	15,859	14,254
Capital					
Paid-in capital	5,198	5,197	5,197	5,197	5,197
Other capital	6,974	4,684	1,686	990	661
Shareholders' equity	12,172	9,881	6,883	6,186	5,858
Other items					
'AAA' callable capital	9,275	9,277	9,277	8,439	8,291
Impaired loans	19	35	86	125	205
Guarantees	438	465	495	588	526
Provisions for guarantees	0	0	(32)	(40)	(36)
Committed but not yet disbursed operational assets	6,769	6,679	5,179	5,665	5,474
Interest expense and similar charges	603	410	223	200	303
General administrative expenses	212	202	173	142	159
Net profit for the year	2,389	1,522	393	333	86
Exposure in five countries of largest exposure	8,104	7,136	5,921	5,096	5,292
Exchange rate: year-end (US$/€)	1.3170	1.1797	1.3621	1.2630	1.0487
Exchange rate: annual average (US$/€)	1.2556	1.2458	1.2433	1.1308	0.9444

*Securities issued by countries of operation.