MOODY'S
INVESTORS SERVICE

Rating Action: Moody's assigns first-time rating of A1 to The Currency Exchange Fund NV (TCX), outlook is stable

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London, 19 July 2021 -- Moody's Investors Service ("Moody's") has today assigned an A1 foreign currency long-term issuer rating to The Currency Exchange Fund NV (TCX). The outlook is stable.

The main factors underpinning TCX's A1 rating are:

(1) The strong support from a diverse group of mostly highly rated shareholders and government supporters;

(2) TCX's very strong liquidity profile with very large liquidity buffers and prudent liquidity policies;

(3) Its moderate capital adequacy which reflects solid levels of paid-in capital and other funding support in order to mitigate market risk, in particular foreign-currency risk; and

(4) Prudent and high-quality risk management policies and practices, which are however essential for TCX's risky and highly volatile business model.

The stable outlook reflects Moody's expectation of solid growth in TCX's business volumes over the coming years coupled with continued strong shareholder support. It also balances the volatile business profile with prudent and high-quality risk management policies and practices Hence, risks are broadly balanced as reflected in the stable outlook.

Moody's considers that governance considerations have been a key factor in this rating action.

RATINGS RATIONALE

ORGANIZATIONAL STRUCTURE AND STRATEGY

TCX is a specialized finance vehicle, providing currency hedging solutions on illiquid emerging market currencies to Multilateral Development Banks (MDBs) and Development Finance Institutions (DFIs). It is owned by a group of more than 20 MDBs, DFIs as well as several microfinance investment vehicles, and also receives financial support from a group of highly rated governments.

TCX's mandate is to support the shareholders' development activities by enabling them to provide their borrowers in emerging and frontier markets with financing in their own currency, while shifting the currency risk to TCX. Since its inception in late 2007, TCX has hedged approximately $9 billion worth of loans provided to borrowers in emerging and frontier markets. The company operates as public limited liability company and is based in Amsterdam, the Netherlands.

TCX's primary products are (typically non-deliverable) cross-currency swaps and to a lesser extent FX forwards. The basis of its transactions is that TCX must be additional to existing financial markets solutions, i.e. TCX only offers hedging solutions where no market exists or only at longer maturities than the market offers. TCX gives preference to its shareholders or their designated entities, with shareholders typically accounting for 85-90% of business volumes. TCX commits on a best-effort basis to execute hedging transactions per year with each of its shareholders of at least their respective capital contribution. As of end-2020, TCX provided hedging on 55 currencies. Given its developmental focus and multilateral shareholder structure, Moody's rates TCX under its Multilateral Development Banks and Other Supranational Entities Methodology.

RATIONALE FOR THE A1 RATING

FIRST FACTOR: STRONG SUPPORT FROM DIVERSE GROUP OF MAINLY HIGHLY RATED SHAREHOLDERS AND GOVERNMENT SUPPORTERS

The first driver of today's rating action relates to TCX's member support. TCX benefits from a group of very highly rated shareholders, with currently 76% (end-2020: 69%) of shareholders rated Aaa. The largest shareholders are Kreditanstalt fuer Wiederaufbau (KfW, Aaa stable), the European Bank for Reconstruction &

Development (EBRD, Aaa stable) and the Development Agency of the Government of the Netherlands (FMO, Aaa stable) with a share of around 16% each. The European Investment Bank (EIB, Aaa stable) and the International Finance Corporation (IFC, Aaa stable) are also significant shareholders with around 10% each.

Moody's key indicator for the ability of shareholders to provide support to an entity in case of need is the weighted average shareholder rating which in TCX's case stands at "A1", being skewed lower by the presence of small impact/microfinance investors who are unlikely to provide additional support for TCX in case of need (given their own size and other limitations). But the support from the highly rated MDB and DFI shareholders has been long-standing and increasing over time. TCX performs a crucial service for them, which helps them to achieve high developmental impact with limited financial cost.

In addition, TCX received an unfunded commitment from the European Union (Aaa stable) for a total amount of €145 million in December 2020, which Moody's considers to have some similarities to callable capital and therefore considers in its assessment of contractual willingness to support.

SECOND FACTOR: STRONG LIQUIDITY PROFILE REFLECTING LARGE BUFFERS AND PRUDENT POLICIES

The second factor driving the A1 rating is TCX's very strong liquidity profile with a very large liquidity buffer of over $1 billion, which is invested in highly rated instruments and cash, as TCX strives to minimize any other risks apart from the market risks inherent in its business. Treasury assets are also highly liquid, with around 80% having a remaining tenor of less than one year. TCX's liquidity buffers are sufficient to withstand even severe stress scenarios; Moody's key indicator for the availability of liquid resources is therefore assessed at the highest level.

Also, Moody's considers TCX's liquidity policies to be very prudent, with frequent and sophisticated stress testing being undertaken.

THIRD FACTOR: MODERATE CAPITAL ADEQUACY METRICS REFLECTING SOLID LEVELS OF PAID-IN CAPITAL AND OTHER FUNDING SUPPORT

The third factor underpinning TCX's A1 rating relates to its moderate capital adequacy which reflects solid levels of paid-in capital and other funding support, counterbalanced by a risky and highly volatile business model. Since inception, shareholders have provided substantial paid-in equity in the form of Class A shares, totaling $795.5 million as of end-2020, including earnings which are fully retained. However, shareholders can redeem their shares on a quarterly basis, subject to an annual cap of 20% of total outstanding shares and several other restrictions under TCX's control. In addition, shareholders have a one-off option to redeem their shares in full in 2045. These are unusual features compared to the typically permanent provision of capital for MDBs. Moody's reflects these by only accounting 75% of the shares as capital in its capital adequacy calculations. Several shareholders have over the past years redeemed shares, although they tended to not actively use TCX. None of the original and large Aaa-rated shareholders has ever redeemed shares.

In addition, the governments of Germany (Aaa stable), Switzerland (Aaa stable) and the United Kingdom (Aa3 stable) have provided financial support in the form of convertible subordinated loans which mature in December 2045 and amount to $189.3 million. The subordinated loans convert into Class B shares in a scenario in which TCX's shareholders decide to wind down the Fund. They then rank junior to Class A shares. For this reason, Moody's aligns their treatment with that of the Class A shares, by assigning 75% equity credit to the loans.

While the Dutch government has provided similarly subordinated loans (for an amount of $81.5 million) Moody's does not incorporate these into its calculation of equity, given that they mature on 31 December 2025. Useable equity of $738.6 million compares to development-related assets of $1.8 billion; these include both the primary and the hedging portfolio, which reflects Moody's view that the hedging is effective in reducing TCX's market risk exposure.

TCX's solid levels of paid-in capital and other funding support provide buffers to TCX's risky and highly volatile business model. Asset quality is low given TCX's focus on emerging and frontier market currencies and the most illiquid parts of currency hedging, while the performance of the currency portfolio is highly volatile. The large number of currencies in which TCX trades provides some risk diversification as do concentration limits that are strictly enforced. That said, the effectiveness of diversification is constrained by the correlation of some of the traded currencies.

In most years, TCX generates a profit, which is fully retained and added to useable equity, but Moody's also considers the years in which regional or global currency crises have generated significant losses for the Fund, in particular 2014/2015 and 2018. That said, last year TCX generated a small profit, despite the highly synchronized deprecation of most of its traded currencies in the early months of the pandemic.

FOURTH FACTOR: PRUDENT AND HIGH QUALITY RISK MANAGEMENT POLICIES AND PRACTICES

The company's comparatively high risk profile requires a sophisticated risk management, and in Moody's view TCX's policies and practices are of high quality and appropriate for its business model. Its practices and standards closely follow Basel rules for commercial banks and are adapted to reflect TCX's specificities and its predominant exposure to market risk. TCX performs tailored, extensive and frequent stress testing, which supports long-term capital planning and a high awareness of the business risks across the firm.

The company makes use of specialized external expertise such as an independent Pricing Committee, which validates the Fund's pricing methodologies and valuation of the Fund's positions. Reporting, data availability and transparency are of very high quality and frequency.

ENVIRONMENTAL, SOCIAL AND GOVERNANCE CONSIDERATIONS

Environmental considerations are not material to TCX's rating profile. That said, the currencies of emerging markets in which TCX is active might be negatively affected by natural disasters.

Social considerations are not material to TCX's rating profile. Even though social considerations can have an impact on a country's exchange and interest rates, thereby impacting TCX's development asset credit quality as well as liquidity through additional margining requirements, the impact is only indirect and the diversification of its currency exposure offsets this risk.

Governance considerations are material to the rating and are a driver for assigning the A1 rating. The riskiness of TCX's activities requires sophisticated risk management. In Moody's view TCX's policies and practices are appropriate for its business model, and incorporate strict exposure limits, stress testing, the existence of an independent pricing committee and very conservative liquidity management.

RATIONALE FOR THE STABLE OUTLOOK

The stable outlook reflects Moody's expectation of solid growth in TCX's business volumes over the coming years coupled with continued strong shareholder support. TCX's business volumes have been significantly below expectations in 2020 due to the pandemic and the resulting inability of many of its investors to generate their intended business volumes. In addition, MDB/DFI borrowers had to restructure their loans, with the consequent need to also restructure the related derivatives. The volume of new primary deals was $985 million, lower than the target of $1.3 billion as per TCX's current strategy for 2019-2022. TCX now targets a primary production portfolio of $1.25 billion for 2021 and has pencilled in an annual production target of close to $2.7 billion by 2025, implying annual portfolio growth of 20%. While ambitious, Moody's expects that the portfolio growth will continue to be accompanied by further capital injections so as to ensure a sufficiently high capitalisation; during the pandemic shareholders continued to support TCX with additional capital injections of $44 million from several existing and one new shareholder. Late last year, the unfunded guarantee with the European Union was signed, and will likely be activated to a large extent or fully in 2021.

The stable outlook also reflects Moody's view that risk management will remain prudent and of high quality, limiting the risks to the business and to TCX's senior counterparties.

FACTORS THAT COULD LEAD TO AN UPGRADE OR DOWNGRADE OF THE RATINGS

Upside rating potential could develop if paid-in equity was made permanent and shareholder support became more skewed towards very highly rated entities. While TCX has solid levels of capital and subordinated loans at its disposals, we do not give full credit to these given shareholders' redemption rights. Upside rating potential could also emerge if callable capital increased significantly.

Downside rating pressure could develop in a scenario of severe losses and sharply deteriorating asset performance coupled with evidence that shareholders were unwilling to provide additional capital. In such a scenario, TCX's capital levels would trend lower, potentially approaching the trigger levels at which shareholders would have to decide on the voluntary winding-down of the Fund.

The principal methodology used in this rating was Multilateral Development Banks and Other Supranational Entities Methodology published in October 2020 and available at https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_1232238 . Alternatively, please see the Rating Methodologies page on www.moodys.com for a copy of this methodology.

REGULATORY DISCLOSURES

For further specification of Moody's key rating assumptions and sensitivity analysis, see the sections Methodology Assumptions and Sensitivity to Assumptions in the disclosure form. Moody's Rating Symbols and Definitions can be found at: https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_79004.

For ratings issued on a program, series, category/class of debt or security this announcement provides certain regulatory disclosures in relation to each rating of a subsequently issued bond or note of the same series, category/class of debt, security 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 credit rating action on the support provider and in relation to each particular credit 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.

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This rating is solicited. Please refer to Moody's Policy for Designating and Assigning Unsolicited Credit Ratings available on its website www.moodys.com.

Regulatory disclosures contained in this press release apply to the credit rating and, if applicable, the related rating outlook or rating review.

Moody's general principles for assessing environmental, social and governance (ESG) risks in our credit analysis can be found at http://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_1288435 .

At least one ESG consideration was material to the credit rating action(s) announced and described above.

The Global Scale Credit Rating on this Credit Rating Announcement was issued by one of Moody's affiliates outside the EU and is endorsed by Moody's Deutschland GmbH, An der Welle 5, Frankfurt am Main 60322, Germany, in accordance with Art.4 paragraph 3 of the Regulation (EC) No 1060/2009 on Credit Rating Agencies. Further information on the EU endorsement status and on the Moody's office that issued the credit rating is available on www.moodys.com.

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Kathrin Muehlbronner
Senior Vice President
Sovereign Risk Group
Moody's Investors Service Ltd.
One Canada Square
Canary Wharf
London E14 5FA
United Kingdom

JOURNALISTS: 44 20 7772 5456
Client Service: 44 20 7772 5454

Alejandro Olivo
MD-Sovereign/Sub Sovereign
Sovereign Risk Group
JOURNALISTS: 1 212 553 0376
Client Service: 1 212 553 1653

Releasing Office:
Moody's Investors Service Ltd.
One Canada Square
Canary Wharf
London E14 5FA
United Kingdom
JOURNALISTS: 44 20 7772 5456
Client Service: 44 20 7772 5454