CREDIT OPINION
16 July 2024

Update

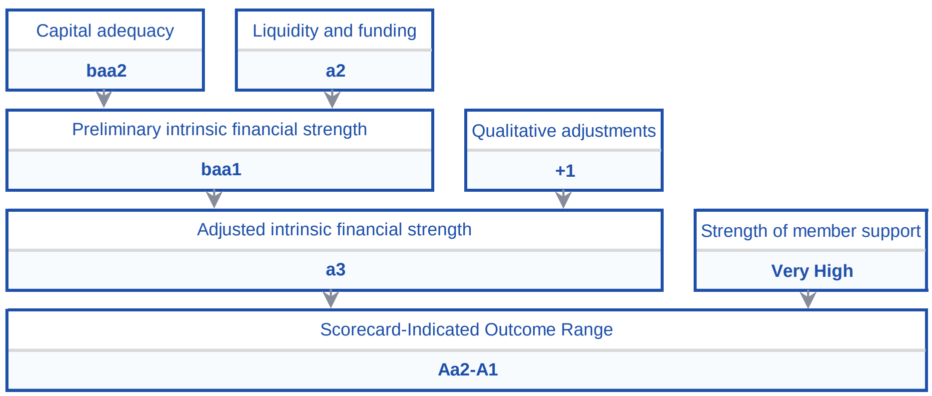
The Currency Exchange Fund NV (TCX) – Aa3 stable

Update following rating upgrade, outlook changed to stable

Summary

The credit quality of The Currency Exchange Fund NV (TCX) reflects the strong liquidity and solid support it receives from mostly highly rated shareholders, which are also the main users of TCX's currency-hedging products, and its strong risk management policies and practices. These strengths are counterbalanced by TCX's volatile asset performance and weak asset quality because of its focus on emerging- and frontier-market currencies.

Exhibit 1
TCX's credit profile is determined by three factors



Source: Moody's Ratings

Credit strengths

» Very large liquidity buffers invested in highly rated and liquid instruments

» Very strong support from a diverse group of mostly highly rated shareholders

» Sophisticated and prudent risk management

Credit challenges

» Unusually risky and inherently volatile business profile

» Capital instruments are not permanent and contain redemption option which somewhat weakens capital adequacy assessment

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RATINGS

TCX

	Rating	Outlook
Long-term Issuer	Aa3	STA
Short-term Issuer	--	--

Analyst Contacts

Kathrin Muehlbronner +44.20.7772.1383
Senior Vice President
kathrin.muehlbronner@moodys.com

Katia Garnier-Luna +44.20.7772.5598
Ratings Associate
katia.garnier-luna@moodys.com

Dietmar Hornung +49.69.70730.790
Associate Managing Director
dietmar.hornung@moodys.com

Marie Diron +44.20.7772.1968
MD-Global Sovereign Risk
marie.diron@moodys.com

CLIENT SERVICES

Americas	1-212-553-1653
Asia Pacific	852-3551-3077
Japan	81-3-5408-4100
EMEA	44-20-7772-5454

Rating outlook

The rating was upgraded to Aa3 on 12 July in response to the continued strong financial support that shareholders and sponsors provide to the Fund. Last year, the European Commission (representing the European Union, Aaa stable) more than doubled its guarantee for TCX's operations, which we consider similar to callable capital. In addition, several development finance institutions and governments are considering becoming shareholders and financial backers of the Fund. Secondly, TCX has managed to substantially grow its business volumes – a clear indication of the relevance of its hedging products – while remaining profitable and without compromising its robust capital and liquidity metrics. The outlook is now stable.

Factors that could lead to an upgrade

Upward rating momentum could develop if TCX managed to substantially raise its business volumes while maintaining its strong capitalization and liquidity buffer. Such a scenario would require substantial capital injections from new and/or existing shareholders. TCX is considering the issuance of Class D shares that could be purchased by governments, which could be one avenue to raise its size and relevance. A substantial extension to the maturity of the capital instruments could also support a higher rating.

Factors that could lead to a downgrade

The rating would come under downward pressure in a scenario of much higher leverage, which could be the result of TCX's inability to hedge its exposures or of severe losses and sharply deteriorating asset performance, coupled with evidence that shareholders were unwilling to provide additional capital. In a remote scenario, TCX's capital levels would approach the trigger levels at which shareholders would have to decide on the voluntary winding-down of the Fund.

Key indicators

Exhibit 2

TCX	2018	2019	2020	2021	2022	2023
Net Asset Value (US$ million)	508.6	751.3	795.5	829.2	838.2	989.0
Development-related Assets (DRA) / Usable Equity [1]	231.8	192.4	184.6	186.0	193.9	196.1
Non-Performing Assets / DRA	4.4	4.9	4.2	4.8	4.8	5.3
Return on Average Assets	-4.3	12.2	2.1	9.6	0.8	10.8
Liquid Assets / ST Debt + CMLTD	--	--	21,508.4	--	--	--
Liquid Assets / Development-related Assets [1]	53.3	57.3	63.0	59.8	57.8	56.1
Callable Capital / Gross Debt	0.0	0.0	42.3	111.8	189.8	196.8

[1] We define development assets as the notional value of the local currency primary and hedging portfolios, excluding the €:$ hedges

Source: Moody's Ratings

Profile

The Currency Exchange Fund NV (TCX), based in Amsterdam, is a specialized finance vehicle that provides hedging mainly in the form of non-deliverable cross-currency swaps on illiquid emerging market currencies. It was set up in 2007 by a group of development finance institutions to support their development mandate, by enabling them to lend in local currency while removing the currency risk from their balance sheet. It is currently owned by 19 multilateral and bilateral development finance institutions and microfinance investment vehicles that are also its primary clients.

The main shareholders are highly rated and include Kreditanstalt für Wiederaufbau (KfW, Aaa stable); the European Bank for Reconstruction & Development (EBRD, Aaa stable); FMO, the development agency of the government of the Netherlands (Aaa stable); the International Finance Corporation (IFC, Aaa stable); and the European Investment Bank (EIB, Aaa stable). TCX also receives funding from several highly rated governments in the form of convertible subordinated loans.

TCX only offers hedging solutions where no market exists or only at longer maturities than the market offers (additionality principle). TCX prices its products in accordance with prevailing market pricing principles to provide its counterparties with competitive prices while avoiding distorting existing markets or hindering potential market developments (market-based pricing principle). TCX only transacts to offset open currency exposures (non-speculation principle). In 2023, TCX transacted in 53 currencies.

Detailed credit considerations

Our determination of a supranational's rating is based on three rating factors: capital adequacy, liquidity and funding, and strength of member support. For Multilateral Development Banks (MDBs), the first two factors combine to form the assessment of intrinsic financial strength, as shown on the cover page graphic. Additional factors can affect the intrinsic financial strength, such as risks stemming from the operating environment or the quality of management. The strength of member support is then incorporated to yield a rating range. For more information, please see our Multilateral Development Banks and Other Supranational Entities Methodology, published in February 2024.

FACTOR 1: Capital adequacy score: baa2

Our "baa2" score for TCX's capital adequacy balances solid levels of paid-in capital and other funding support against a high exposure to market risk, in particular foreign-currency risk, and its inherently volatile operating performance. The score is in line with that of the Emerging Africa Infrastructure Fund (EAIF, A2 stable) and Africa Finance Corporation (AFC, A3 negative).

Moderate leverage as increasing hedging activity mitigates portfolio growth

Last year, TCX has substantially grown its swap portfolio after several years of more moderate growth. The gross local currency portfolio (both long and short positions) reached $6.2 billion versus $4.4 billion a year earlier (excluding €:$ hedges), a clear indication of TCX's competence and the relevance of its products. We consider the net portfolio in our metrics, as the short or hedging portfolio is used as a risk management tool to stabilise TCX's net exposure and free up capacity to provide more primary transactions. The hedges have to match the currency and maturity of the primary exposures, and in our view are effective in reducing TCX's market risk exposure while supporting the Fund's mandate to develop local currency bond markets.

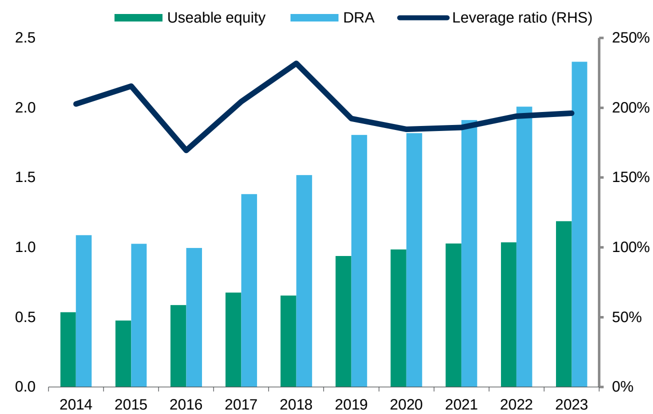
Hedges are done with both commercial banks and some shareholders via local-currency bonds. In those transactions, a shareholder issues a synthetic local-currency bond on offshore markets. The issuer then swaps back its cash flow into dollars with TCX, effectively reducing the Fund's net exposure to the local currency. Hedges done with commercial banks grew by 73% last year and now account for the largest share of hedging. The net local currency portfolio grew to the largest ever size of $2.3 billion, versus $2 billion a year earlier. Underlying this growth was a record volume of $2.3 billion in primary (long) transactions (versus $1.4 billion in 2022), 65% of which was hedged away through short transactions.

We calculate leverage as development-related assets in relation to usable equity; in TCX's case, we consider as development assets the notional net value of its primary and hedging portfolio. Leverage stood at just below 200%, similar to 2022 and lower than at the peak of 232% in 2018. We recently changed our calculation of useable equity and now include the full outstanding value of Class A shares and the convertible subordinated loans (CSLs) with maturity in December 2045 instead of our previous recognition of 75% of these instruments only (see more detail below).

While shareholders' redemption rights are unchanged, few shareholders have ever redeemed their share and none of TCX's anchor shareholders has ever done so. Redemptions are limited to a maximum of 20% of the share capital per year. Also, TCX has the right to reject capital redemption requests when the resulting capital ratio after redemption falls below 18%. Useable equity as per our definition stood at close to $1.19 billion at end-2023; TCX also includes in its internal capital calculation two facilities provided by the Dutch government and also the European Commission's (EC) unfunded commitment. In terms of risk-weighted assets TCX's capital ratio was robust at 24.6% as of end-2023 and 26% at the end of May 2024. As of May 2024, the Fund had a substantial buffer of $458 million available for future portfolio growth without the need for additional capital.

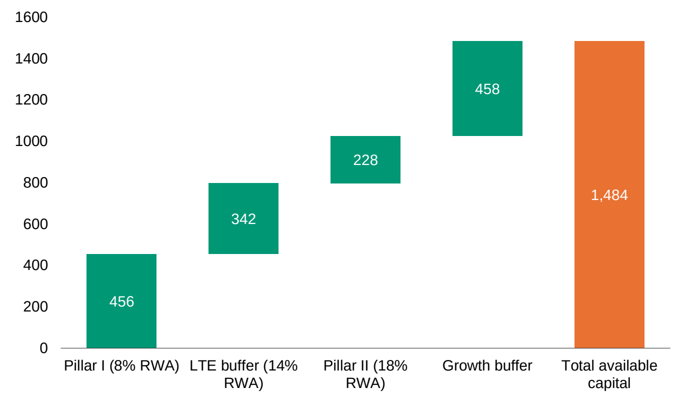
TCX's shareholders have introduced an effective minimum capital ratio of 14% of RWA, at which they would need to consider whether to inject additional capital or wind down the Fund. To avoid reaching this situation, a substantial additional Pillar II capital buffer of 4% of RWA is added (18% redemption gate), plus another 2% of RWA (total 20% of RWA) as an internal trigger for management action.

Exhibit 3
Portfolio has grown rapidly in recent years, supported by equity injections
($ billions and %)



Sources: TCX and Moody's Ratings

Exhibit 4
TCX has sufficient capital buffers to grow further
(In $ millions, May 2024)



Shareholders established a so-called Liquidation Trigger Event (LTE) at a capital ratio of 14%, at which they would need to decide whether to wind down TCX.
Sources: TCX and Moody's Ratings

Apart from Class A shares with a total outstanding amount of $989 million as of end-2023, TCX has obtained convertible subordinated loans (CSLs) worth $199 million maturing on 31 December 2045 from the governments of Germany (Aaa stable), Switzerland (Aaa stable), the United Kingdom (UK, Aa3 stable) and since 2022 also from Proparco, one of the government of France's (Aa2 stable) development agencies. The CSLs automatically convert into Class B shares upon a voluntary wind-down scenario, in which they rank junior to Class A shares and can only be redeemed after all shareholders have redeemed their initial investment plus a return equal to three-month compounded SOFR+26 basis points. Therefore, they provide a first-loss protection to trading counterparties and Class A shareholders, and enhance the risk-return of their investment to attract new shareholders.

Given the similarities and the junior treatment to Class A shares in a wind-down scenario, we consider the CSLs as similar to equity. We do not include a convertible subordinated loan of $70.6 million nor a first-loss loan of $10.9 million that writes down to zero in a wind-down scenario, both provided by the government of the Netherlands because these facilities mature much earlier, in 2025.

Focus on emerging market currencies results in weak asset quality...
Our assessment of Development Asset Credit Quality (DACQ) starts with an anchor point of “caa” for the equivalent of a weighted average borrower rating, because of TCX's focus on illiquid emerging market currencies. The fund is widely diversified across currencies, which leads to a higher DACQ score of “b”. The score is in line with that of peers such as GuarantCo (A1 stable) and International Islamic Trade Finance Corporation (ITFC, A1 stable).

The top 10 currencies accounted for 56% of the net portfolio in April 2024, broadly similar to previous years. As of April 2024, the top three currencies were the Jordanian dinar (7.2%), the Tanzanian shilling (7%) and the Jamaican dollar (6%). The currency composition changes frequently as TCX responds to shareholder needs, but limits are strictly enforced and the number of actively traded currencies has remained consistently high at around 40-55 over the past several years. Since its inception, TCX has offered swaps in more than 100 currencies.

Exposure to a single currency cannot exceed the lower of (i) 25% of the capital base and (ii) 10% of the maximum potential portfolio size.[1] On a regional basis, the fund has set limits at 30%-50% of its notional exposure. The Fund consistently remains well below its limits and the increased use of hedging instruments has helped TCX reduce its exposure to single currencies.

...and drives volatile asset performance
TCX has no nonperforming assets (NPA) as such. All losses — including unrealised mark-to-market losses — on its portfolio directly flow into its financial results and directly affect the net asset value (NAV) of the Fund and its usable equity. We use TCX's value at risk (VaR) calculations for market risk as a proxy for NPAs, because market risk is the Fund's dominant risk exposure (93% of RWA). This

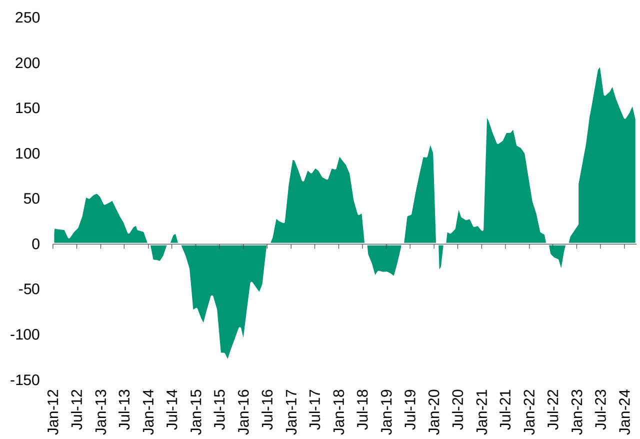
metric is based on the calculation of the worst historical losses assuming the current portfolio composition, and translates into a score of "baa3" for asset performance.

TCX's solid diversification provides some protection against economic and financial shocks. On average, TCX has made a small positive return in its 17 years of existence and its monthly performance is skewed towards marginally positive returns. The fund generates positive financial results from three sources: the net interest spread (carry) originating from the difference in local versus hard currency and from the bid-ask spread locked in when positions are hedged; the appreciation of local currencies against the US dollar; and interest income on its large liquidity portfolio, although this tends to be relatively moderate because of the high credit quality of the assets.

However, TCX has been founded to absorb losses that would otherwise have to be absorbed by the clients of its investors. Longer-lasting regional crises tend to leave the biggest impact on TCX. Its largest-ever loss over a 12-month period was $130.5 million between October 2014 and September 2015, as a result of the slump in oil prices at the time. Losses on just three currencies (the Kyrgyz som, the Tajik somoni and the Armenian dram) accounted for 60% of the losses in 2014 and 2015 because of their high interconnectedness with Russia and Kazakhstan (Baa2 positive) through remittances and trade.

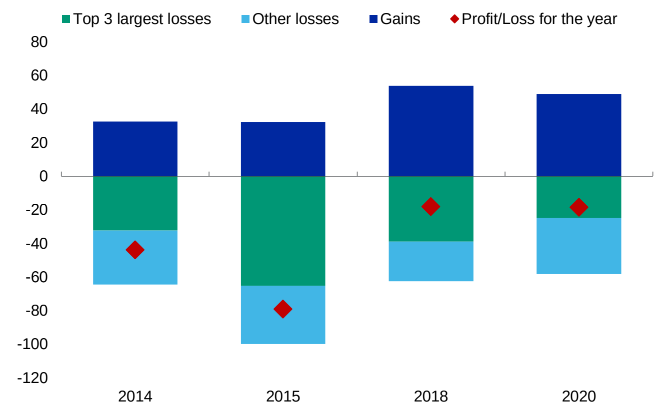
In contrast, the Covid pandemic - while resulting in a loss of $128 million for TCX in March 2020 - has not had a longer-lasting impact on TCX's financial results. In the months after March 2020 the strong rebound in markets led to an (investment) profit of $111 million over the period April-August 2020. The impact of the pandemic was thus far from severe.

Exhibit 5
TCX tends to post profit in most months except during 2014-15
(12-month rolling sum of monthly change in net asset value in $ million)



Sources: TCX and Moody's Ratings

Exhibit 6
Losses tend to be driven by a small number of currencies
(In $ millions)



Excludes USD:EUR hedges.
Sources: TCX and Moody's Ratings

FACTOR 2: Liquidity and funding score: a2

TCX's liquidity and funding score is set at "a2" and reflects very strong liquidity, with large liquidity buffers and prudent policies. The score also incorporates a funding profile in line with that of peers such as GuarantCo, which, similar to TCX, does not raise funds in capital markets.

Very strong liquidity buffers mitigate liquidity risks stemming from margin calls

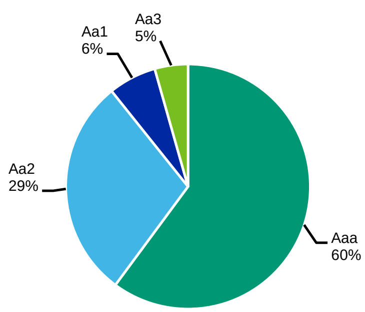
TCX has very solid liquidity, which is essential because of its high-risk business profile. Its available liquidity was $1.3 billion (2022: $1.16 billion). Per the Fund's guidelines, investments are limited to bonds with a minimum rating of Aa3, as well as cash deposits, money market funds and commercial papers, which can quickly be converted into cash. Deposits can only be held in large systemic banks rated A2 or above. The credit quality of TCX's liquidity buffer is very high, so as to not add to the fund's already high exposure to market risk. 60% of assets are invested in Aaa-rated securities or cash deposits, and roughly 94% of assets have a remaining term shorter than one year.

Liquidity risk primarily arises from margin calls on the swap portfolio. TCX only offers non-deliverable swaps, which eliminates convertibility risk because all transactions are settled in US dollars or euro and do not involve any local currency. As a result of fluctuations in the underlying rates of derivative instruments (foreign exchange rates, local interest rates and dollar interest rates), the fund regularly posts and receives collateral, with TCX typically posting more collateral than it receives.

In addition to conservative asset allocation guidelines, liquidity policies are very prudent and rely on frequent and sophisticated stress testing. Under its internal guidelines, TCX uses a liquidity coverage ratio inspired by Basel III to define its liquidity requirements under a stress scenario, defined as liquid assets of high credit quality/net stressed cash outflows over the next 12 months. The stress case assumes the worst historical portfolio performance over 12 months, rising margin calls and shareholder redemptions of 20% of their capital. The fund targets a liquidity coverage ratio of more than 150% and has consistently stayed well in excess of this requirement. As of year-end 2023, the ratio was 177% (2022: 186%).

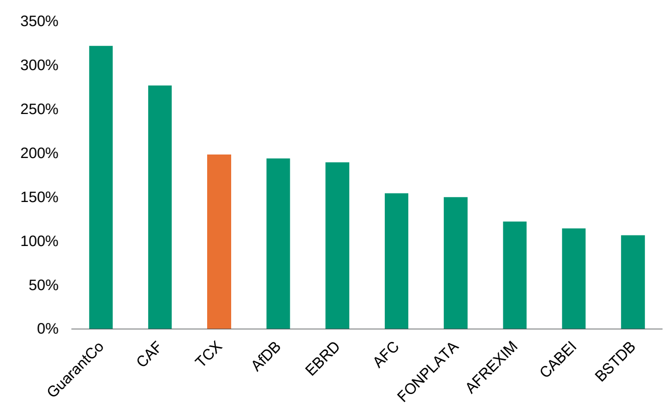
Our measure of liquidity coverage differs somewhat from the fund's own metrics. We use its calculations of stressed cash outflows and only consider highly liquid assets such as cash and short-term bank deposits, and securities rated A2 or higher. TCX's ratio of available liquid resources was 198% of liquid assets as of year-end 2023 (2022: 210%), higher than that of most peers, and reflected in a “aa1” score on this metric.

Exhibit 7
Liquidity is held in highly rated instruments
(Liquid assets, as of year-end 2023)



Sources: TCX and Moody's Ratings

Exhibit 8
Availability of liquid resources is stronger than that of most peers
(Liquid assets/net cash outflows, latest)



Sources: MDBs and Moody's Ratings

In the absence of debt, we assess quality of funding as moderate

Our assessment of the quality of funding is typically based on considerations such as the track record of bond issuance, the cost of funding compared with peers, the availability of credit lines, and the diversity of funding sources and the investor base. We score TCX's quality of funding at “baa”, in line with that of GuarantCo, the Fondo Latinoamericano de Reservas (FLAR, Aa2 stable) and the EAIF. Similar to those entities, TCX has never issued any bonded debt but receives all its funding from development finance institutions and governments. We assume that TCX would have reasonably good market access should it want or need to do so based on solid support from a group of highly rated shareholders and very strong liquidity metrics, while paying a moderate risk premium.

Qualitative adjustments to intrinsic financial strength

Quality of management

We apply a one-notch upward adjustment to TCX's intrinsic financial strength on account of the high quality of management and particularly risk management. TCX's policies and standards follow a very prudent approach, even compared with many higher-rated MDBs. Its framework closely follows Basel rules for commercial banks, and is adapted to reflect its specificities and predominant exposure to market risk. We positively note the existence of the independent valuation committee, but also the tailored stress testing of the portfolio, long-term capital planning and very prudent liquidity management. Reporting and transparency are of very high quality and frequent. The Fund performs an annual internal capital adequacy assessment process (ICAAP) to ensure that all risks are fully captured, and it has sufficient capital at hand to implement its strategy and ensure its continued existence. At the same time, the inherent riskiness of TCX's activities requires a correspondingly higher degree of sophistication.

Operating environment

We do not apply any such adjustment for TCX. Although TCX's operating environment is highly risky because of its exposure to emerging and frontier market currencies, the diversification of its derivative portfolio limits those risks.

FACTOR 3: Strength of member support score: Very High

Our assessment of strength of member support is "Very High", reflecting the strong ability and willingness of its main shareholders to provide additional support if needed, as well as the availability of callable capital in the form of a first-demand guarantee from the European Commission. Other MDBs with a "Very High" strength of member support include Aaa-rated peers such as the European Bank for Reconstruction & Development (Aaa stable) or the Nordic Investment Bank (Aaa stable).

A diverse group of highly rated shareholders and supporters has strong ability to provide support

With a weighted shareholder rating of A1, TCX's group of shareholders is among the strongest of rated MDBs.[2] As of year-end 2023, nearly 75% of Class A shares were held by Aaa-rated institutions, while nearly 80% of the CSLs are provided by Aaa-rated governments (excluding the Netherlands). The average shareholder rating is skewed lower by the presence of small and unrated microfinance investment vehicles and impact investors, which account for 6.6% of total capital and to which we assign an implicit Caa1 rating in line with our methodology. We do not expect those entities to provide additional support for TCX in case of need given their small size and other limitations.

Callable capital in the form of EU guarantee provides an additional buffer

Our key metric to assess the contractual willingness to provide support is the ratio of callable capital to the stock of debt. In the case of TCX, we define as debt the CSL and first-loss loan provided by the Dutch government. We include into our calculation of callable capital the unfunded commitment from the EU in the form of a guarantee extended through the European Fund for Sustainable Development (EFSD) for €145 million. The guarantee is structured in the same way as the CSLs. In case of a decision to wind down the Fund, the activated guarantee amount will be disbursed and turned into Class B shares, which will rank junior to Class A shares. The additional guarantee of €245 million that the EFSD has approved in 2023 would further increase TCX's callable capital cushion. Our score for contractual willingness to support is already at "aaa", which also incorporates a one-notch upward adjustment to reflect the strength of the guarantee, which is a timely and unconditional guarantee with a clear trigger.

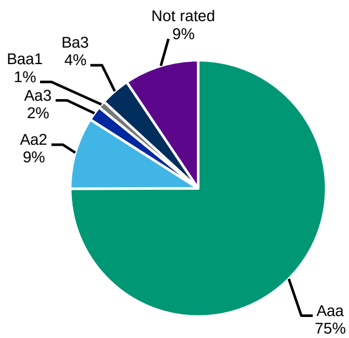
Unique relationship with shareholders supports high non-contractual willingness to support

We assess shareholders' non-contractual willingness to support as "High" to reflect the fact that support from highly rated shareholders through capital injections has been long-standing and increasing over time. TCX was explicitly set up to assume specific risks that shareholders would otherwise have to assume themselves at higher cost and risk. Some would not be able to extend local-currency loans to their borrowers at all without TCX, which would reduce their own development impact. Hence, their interest in the continued existence and solidity of TCX is very strong.

Shareholders have the option to redeem their shares, although under very strict conditions. So far, eight shareholders, mostly small microfinance investment vehicles, have redeemed all or parts of their shares. Japan Bank for International Cooperation (JBIC, A1 stable) and the African Development Bank (AfDB, Aaa stable) were the largest shareholders to depart from the Fund in 2021, but neither was an active user of TCX's services and the redemption did not affect our assessment of shareholder support.

Exhibit 9

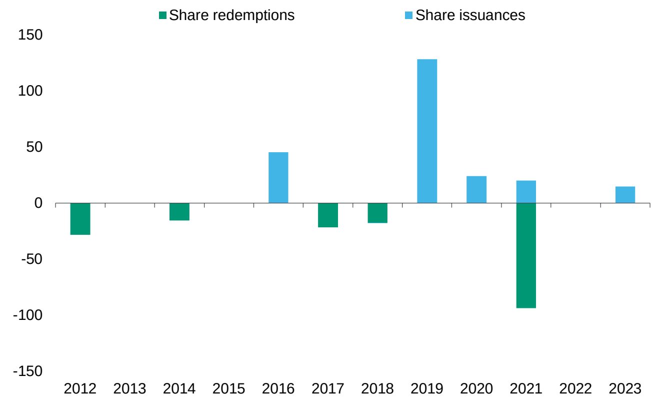
Shareholder base comprises mostly highly rated entities
(Paid-in equity capital by rating, year-end 2023)



Sources: TCX and Moody's Ratings

Exhibit 10

Redemptions are infrequent and typically smaller than capital subscriptions
(In $ millions)



Sources: TCX and Moody's Ratings

None of the large shareholders that actively use TCX has ever redeemed any shares. Over the years, TCX's shareholder base has expanded significantly and paid-in equity under our definition increased to close to $1.19 billion in 2023 from close to $612 million in 2012, indicating the relevance of the institution and its mandate. Several shareholders have repeatedly raised their stakes, while new shareholders join on a regular basis. TCX's government supporters have also repeatedly shown their support, in particular the German government, which extended the maturity of its CSLs by 20 years to 2045 in 2019.

ESG considerations

The Currency Exchange Fund NV (TCX)'s ESG credit impact score is CIS-1

Exhibit 11

ESG credit impact score

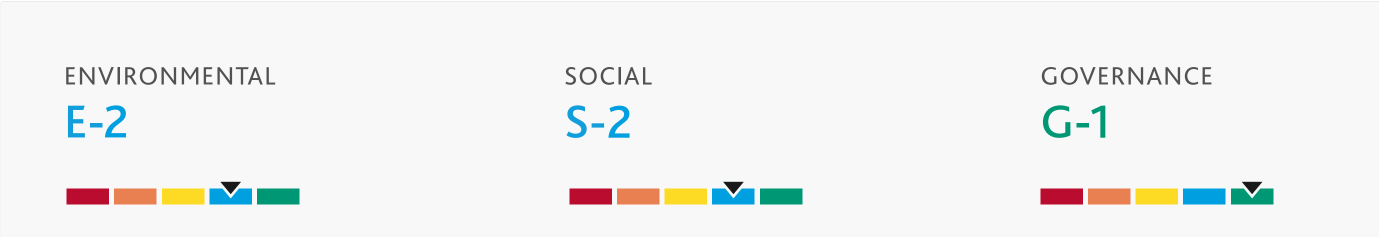
CIS-1

ESG considerations have a positive impact on the current rating which is higher than it would have been in the absence of ESG considerations.

Source: Moody's Ratings

CIS-1 indicates that the credit rating is higher than it would have been in the absence of ESG considerations. This primarily reflects TCX's very strong governance framework, specifically in terms of financial strategy and risk management, and credibility of management. Our assessment is also based on the very limited environmental and social risks TCX is faced with. In addition, very strong backing by shareholders provides material support to the rating.

Exhibit 12
ESG issuer profile scores



Source: Moody's Ratings

Environmental
TCX's exposure to environmental risks is low across all five categories, resulting in an overall **E-2** environmental issuer profile score. While active in emerging markets and frontier economies with often high exposures to environmental risks, TCX's exposure is further removed from these risks than most other MDBs due to its business focus on providing hedging solutions to other MDBs and DFIs.

Social
TCX has limited exposure to most social risks, resulting in a **S-2** social issuer profile score. We consider TCX's 'responsible production' to be a positive feature of its issuer profile, given the high developmental impact of TCX's hedging operations, which allow its shareholders and investors to lend in local currencies, avoiding to burden borrowers with foreign-currency risk.

Governance
We consider governance to be a positive feature of TCX's issuer profile, resulting in a **G-1** governance issuer profile score. This mostly reflects TCX's very strong financial strategy and risk management practices, as well as very solid management credibility and a strong track record of profitability despite its high market risk exposures.

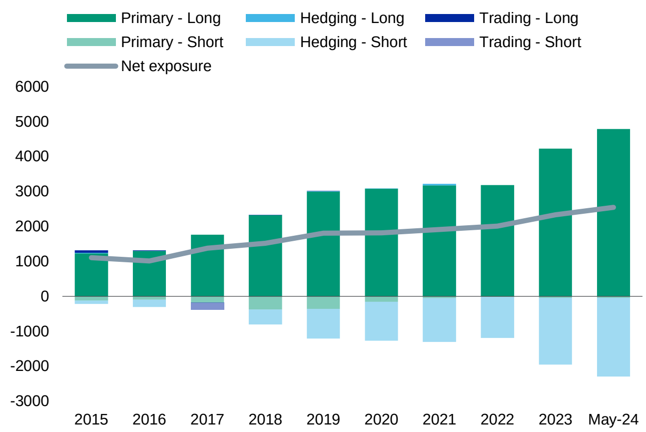
ESG Issuer Profile Scores and Credit Impact Scores for the rated entity/transaction are available on Moodys.com. In order to view the latest scores, please click here to go to the landing page for the entity/transaction on MDC and view the ESG Scores section.

All of these considerations are further discussed in the “Detailed credit considerations” section above. Our approach to ESG is explained in our cross-sector methodology General Principles for Assessing Environmental, Social and Governance Risks. Additional information about our rating approach is provided in our Supranational Rating Methodology.

Recent developments

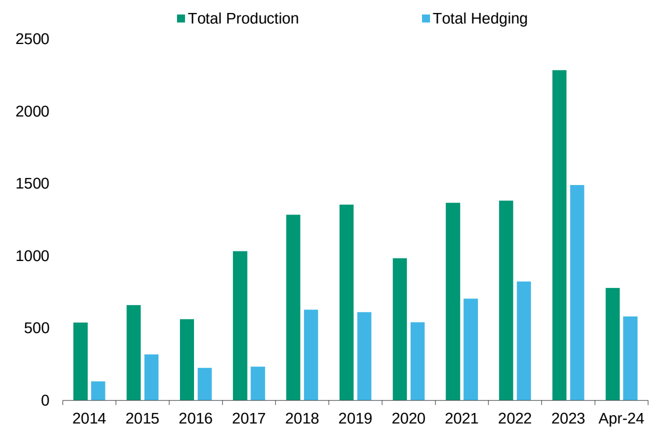
Strong portfolio growth in 2023 confirms competence and relevance of TCX's products
TCX saw strong growth in its portfolio last year, as indicated earlier. Growth continued at a strong page in the early months of this year, with primary (long) transactions of $1.1 billion closed up to end-May (versus a budget of $2 billion) and the total net local currency outstanding at close to $2.55 billion. The growth in the net portfolio is more moderate, as TCX continues to be able to hedge a substantial part of its primary swap transactions, mostly with commercial banks and to a lesser extent with shareholders.

Exhibit 13
Strong growth in primary swap portfolio is indicative of demand for TCX's business
(Derivatives portfolio excluding EUR/USD: net exposure in $ millions)



Sources: TCX and Moody's Ratings

Exhibit 14
Availability of hedging allows TCX to grow its primary production fast
(In $ millions)



Sources: TXC and Moody's Ratings

According to its latest ICAAP exercise, TCX aims to increase its swap portfolio from $2.3 billion in 2023 to $5 billion by 2028, with the long portfolio at $10 billion and the short (hedging) portfolio at $5 billion. These are ambitious targets, translating into average annual growth of 17% for the primary portfolio over the 2024-2028 period. According to TCX's capital planning, such a growth trajectory will require additional capital of $637 million over the five years to 2028 for the capital ratio to stay above 18%; capital needs would be higher at $893 million for a capital ratio of above 20%.

While targets are purely indicative and used only for risk management purposes, we expect TCX to be able to manage such growth without significant impact on its credit profile because of continued support from shareholders and continued hedging activity. TCX plans to continue selling its local-currency exposure, with a target of offsetting 47% of the swap portfolio by the end of this year, rising to 51% by 2028. Additional capital will be needed in early 2026, assuming that the Dutch loans will not be extended.

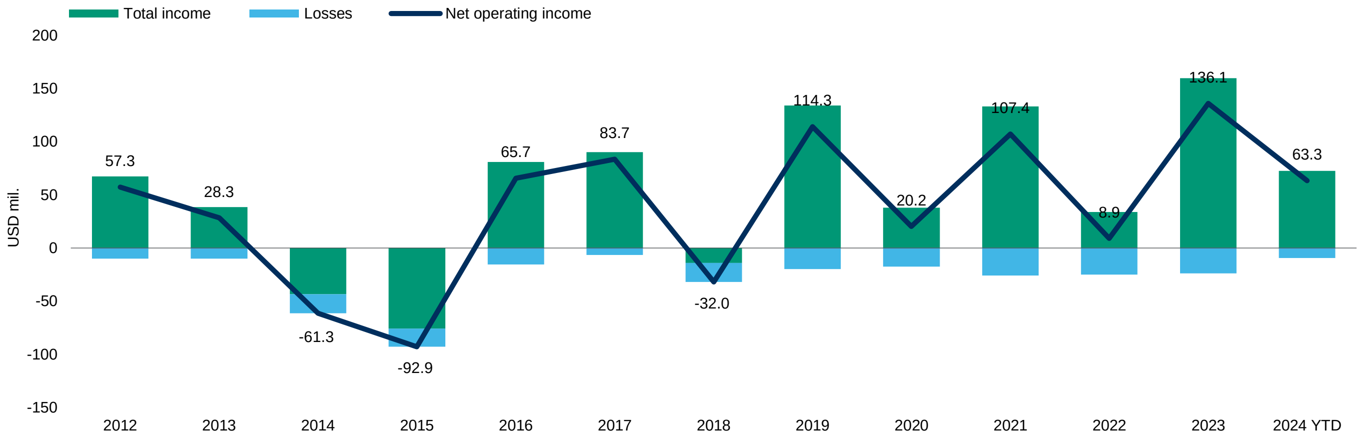
There is strong interest from other DFIs and governments to support the Fund's pioneering work, amid a growing recognition among development finance institutions that lending in local currencies has significantly higher development impact than leaving the borrowers exposed to currency risk. TCX is a well-established and competent counterpart in this area. It aims to broaden its transformational impact to development finance in general, and climate, sustainable infrastructure and sovereigns in particular. This is fully aligned with the interests of its shareholders and government sponsors.

As stated above, risk management is prudent and the full internalisation of the risk function – which was completed in 2023 – is unlikely to weaken TCX's sophisticated risk management. The main instrument to contain risk is the wide diversification by currencies, with strict limits in place. Also, TCX performs regular and frequent stress testing of its capital and liquidity positions in the context of its annual ICAAP exercise.

TCX posted robust profit in 2023

TCX reported a profit of $136 million last year, and a cumulative profit of $63.3 million in the first five months of the year, much higher than in 2022 when profits were only $8.9 million. However, the Fund's financial results are highly volatile and will likely remain so, given the demand-driven nature of the Fund's business in that it responds to its shareholder requirements for local-currency hedges. The Fund has not distributed any dividends since 2014 and earnings since then have been fully retained. Cumulative retained earnings stand at nearly $468 million as of April 2024.

Exhibit 15
TCX has been profitable in most years



YTD 2024 refers to January-May.
Source: TCX and Moody's Ratings

According to the 2023 financial report at the 2023 level of capital, TCX could sustain a loss of $614 million (equivalent to 10.6% of RWAs) before causing a Liquidation Trigger Event. This amount is 6.6 times the worst annual result ever experienced by TCX ($93 million in 2015) and 2.4 times the “12-month diversified risk” (or potential future annual loss) estimate reported at year-end 2023 ($259 million). These multiples demonstrate the Fund's robust capital position.

Rating methodology and scorecard factors

Factor / Subfactor	Metric	Initial score	Adjusted score	Assigned score
Factor 1: Capital adequacy (50%)			baa2	baa2
Capital position (20%)			a2	
	Leverage ratio	a2		
	Trend	0		
	Impact of profit and loss on leverage			
Development asset credit quality (10%)			b	
	DACQ assessment	b		
	Trend	0		
Asset performance (20%)			baa3	
	Non-performing assets	baa3		
	Trend	0		
	Excessive development asset growth	0		
Factor 2: Liquidity and funding (50%)			a2	a2
Liquid resources (20%)			aa1	
	Availability of liquid resources	aa1		
	Trend in coverage outflow	0		
	Access to extraordinary liquidity	0		
Quality of funding (30%)			baa	
Preliminary intrinsic financial strength				baa1
Other adjustments				+1
Operating environment		0		
Quality of management		+1		
Adjusted intrinsic financial strength				a3
Factor 3: Strength of member support (+3,+2,+1,0)			Very High	Very High
Ability to support (50%)			a1	
	Weighted average shareholder rating	a1		
Willingness to support (50%)				
	Contractual support (25%)	aaa	aaa	
	Strong enforcement mechanism	+1		
	Payment enhancements	0		
	Non-contractual support (25%)		High	
Scorecard-Indicated Outcome Range				Aa2-A1
Rating Assigned				Aa3

Note: Our ratings are forward-looking and reflect our expectations for future financial and operating performance. However, historical results are helpful in understanding patterns and trends of an issuer's performance as well as for peer comparisons. Additional considerations that may not be captured when historical metrics are used in the scorecard may be reflected in differences between the adjusted and assigned factor scores. Furthermore, in our ratings we often incorporate directional views of risks and mitigants in a qualitative way. For more information please see our Multilateral Development Banks and Other Supranational Entities rating methodology.

Source: Moody's Ratings

Related websites and information sources

» Moody's Supranational web page

» Moody's Sovereign and supranational rating list

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Endnotes

1 The potential portfolio is estimated assuming the portfolio grows to the point the capital ratio reaches 18% and there are no resulting changes in the portfolio composition.

2 In line with our treatment of TCX's capital instruments, we use both the Class A shares and the CSLs to calculate the weighted average shareholder rating.

REPORT NUMBER 1414129