

18 MAY 2022

Fitch Affirms European Investment Fund at 'AAA'; Outlook Stable

Fitch Ratings - Paris - 18 May 2022: Fitch Ratings has affirmed European Investment Fund's (EIF) Long-Term Issuer Default Rating (IDR) at 'AAA' with a Stable Outlook and Short-Term IDR at 'F1+'.

Key Rating Drivers

Rating Reflects Strong Support: The affirmation and Stable Outlook reflect the strong extraordinary support Fitch believes the fund would receive from its shareholders, including the European Investment Bank (EIB; AAA/Stable; 59% of subscribed capital as of end-2021), and the European Union (EU; AAA/Stable; 30%) as well as 38 large financial institutions based in EU, the UK and Turkey.

Fitch assesses EIF's shareholders' capacity to support at 'aaa', in line with the rating of its key shareholder, the EIB. The 'strong' propensity of shareholders to support translates into a zero-notch adjustment to the support capacity, and reflects EIF's strategic importance for its shareholders. EIF has played a key role in leveraging funds for SMEs in the EU, through its participation in the European Fund for Strategic Investments (EFSI), European Guarantee Fund (Covid-19 policy response initiative) and expected involvement in the long-term InvestEU programme.

Exceptionally Strong Capitalisation: Fitch assesses EIF's Standalone Credit Profile (SCP) at 'aa-', based on its Insurance Rating Criteria. Our assessment primarily reflects 'exceptionally strong' capitalisation and 'very strong' business profile. The fund's net par-to-capital ratio broadly remained stable at 1.1x in 2021 (2020: 1.0x), as the significant increase in guarantee exposure-at-risk was offset by a large EUR2.8 billion capital increase (including EUR2.2 billion callable capital) and EUR661 million share premium increase. Fitch expects EIF's net par-to-capital to remain stable, in line with the 'AAA' rating category.

Medium-risk Guarantee Portfolio: Although EIF's guarantees are predominantly related to SMEs, credit quality is materially improved through credit enhancement (first loss tranche held by the EU). Therefore, the majority of guarantee exposure is investment grade, mainly in the low 'A' and 'BBB' categories, based on EIF's internal risk assessment. Non-investment grade exposure is small.

Private Equity Drives Asset Risk: The risky-assets ratio (2021:44%) is driven by EUR1.5 billion in private equity assets and EUR197 million in non-investment grade asset-backed securities. The largest share of the private equity portfolio is layered and EIF holds only senior tranches, which reduces the risk of potential losses to EIF, as junior tranches held by the EU absorb first losses. The rest of the investment portfolio primarily consists of investment grade sovereign and corporate bonds with an average 'A+' rating. The Ukraine-Russia conflict has so far had no effect on the bond portfolio.

Very Strong Liquidity: EIF's liquidity profile is 'very strong', reflecting the very low level of liquidity needs. The fund has no debt and limited cash requirement for meeting guarantee calls on own-risk exposures. At end-2021, the fund's liquid assets surged to EUR2.6 billion from EUR1.4 billion at end-2020. This was driven by the receipt of EUR1.22 billion cash from the capital increase. The fund's liquidity position is also enhanced by an EUR250 million standby repo facility provided by EIB.

Very Strong Business Profile: EIF acts as an implementing vehicle of EU policies, with a mandate to provide debt, equity and guarantee products to SMEs, and to act as an intermediary for realising the development and cohesion initiatives of the EU through special mandates. As such, business profile characteristics are expected to be stable and not influenced by prevailing market conditions and the competitive landscape.

Strong but Volatile Profitability: Fitch has revised its assessment of EIF's financial performance and earnings to 'a-' from 'bbb-' previously, owing to strong and resilient financial performance. We primarily consider EIF's financial performance from a viability perspective and this has an overall low importance to the rating. Unlike other profit-oriented institutions, EIF does not have a target for return-on-equity (ROE), which has been volatile (2021: 19%; 5-year average: 9.3%) due to fair value changes on private equity investments. Fitch expects run-rate ROE (ROE excluding fair value changes on assets) to stabilise at 4%-5% range over the forecast period, due to expected strong underwriting, a low level of incurred credit losses and guarantee calls.

RATING SENSITIVITIES

Factors that could, individually or collectively, lead to positive rating action/upgrade:

- The ratings are at the highest level on Fitch's scale and cannot be upgraded

Factors that could, individually or collectively, lead to negative rating action/downgrade:

- Adverse change in our assessment of EIF's key shareholders' capacity or propensity to provide support to the EIF.
- Downward revision of EIF's SCP, which could result from weakening in capitalisation and/or pressures on liquidity and investment risks. A downward revision of the SCP below 'aa-' would result in negative rating action as the uplift above the SCP for extraordinary support is already at the maximum of three notches permitted under our criteria.

Best/Worst Case Rating Scenario

International scale credit ratings of Sovereigns, Public Finance and Infrastructure issuers have a best-case rating upgrade scenario (defined as the 99th percentile of rating transitions, measured in a positive direction) of three notches over a three-year rating horizon; and a worst-case rating downgrade scenario (defined as the 99th percentile of rating transitions, measured in a negative direction) of three notches over three years. The complete span of best- and worst-case scenario credit ratings for all rating categories ranges from 'AAA' to 'D'. Best- and worst-case scenario credit ratings are based on historical performance. For more information about the methodology used to determine

sector-specific best- and worst-case scenario credit ratings, visit <https://www.fitchratings.com/site/re/10111579>.

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

Public Ratings with Credit Linkage to other ratings

EIF's ratings take into account the rating of its key shareholder, EIB.

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Rating Actions

ENTITY/DEBT	RATING	RECOVERY	PRIOR	
European Investment Fund	LT IDR	AAA 	Affirmed	AAA 

ENTITY/DEBT	RATING	RECOVERY	PRIOR
	ST IDR	F1+	Affirmed
			F1+

RATINGS KEY OUTLOOK WATCH

POSITIVE	⊕	◇
NEGATIVE	⊖	◇
EVOLVING	◊	◆
STABLE	⦿	

Applicable Criteria

[Insurance Rating Criteria \(pub.26 Nov 2021\) \(including rating assumption sensitivity\)](#)

[Supranationals Rating Criteria \(pub.11 Apr 2022\) \(including rating assumption sensitivity\)](#)

Additional Disclosures

[Solicitation Status](#)

Endorsement Status

European Investment Fund EU Issued, UK Endorsed

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