Exposure Limits and Surcharges: Implications on Pakistan Program

Sameer Kamal
Strategy and Policy Department, ADB

August 2024| ADB Headquarters, Philippines

ADB

Impact of new Capital Adequacy Framework (CAF)

Additional lending headroom

Increase in ADB's capacity to lend OCR and COL

Additional **$100 billion** over ten years

Exposure limits framework

Limits for sovereign borrowers introduced

Countercyclical lending buffer

Available for unexpected Regional or Global Crises

Size: **$12 billion**

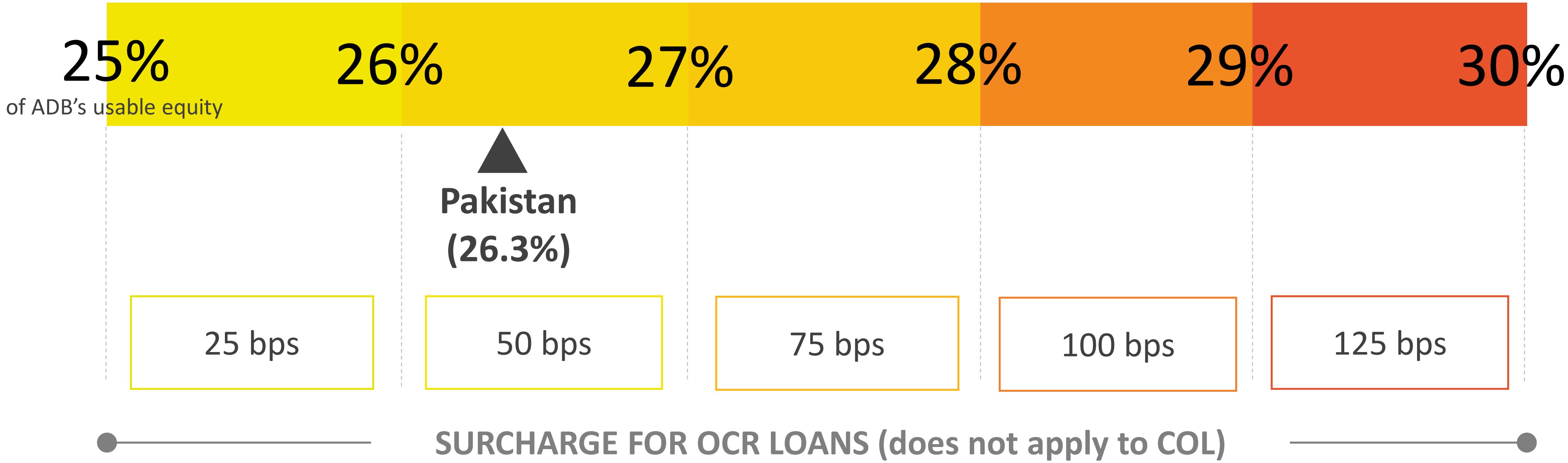
Exposure Limits

ADB has introduced **sovereign exposure limits** to manage concentration risk

FOR "HIGH-RISK" COUNTRIES:

RISK APPETITE (for outstanding exposure)
Exposure ADB is comfortable accepting
New OCR lending after 2026 incurs surcharges

RISK TOLERANCE
Maximum exposure ADB is willing to assume
No new lending allowed



Key Factors Impacting the Exposure Limit

- Country’s Credit Rating
  Countries with higher risk rating have lower limits. If Pakistan’s credit rating were to improve to B/B2, risk appetite and risk tolerance would increase by 5%.

- ADB’s Financial Capacity (Usable Equity)
  Depends on factors such as the size of ADB’s overall balance sheet, interest rates, and currency movements.

Programming Considerations

$$\frac{Outstanding\ Exposure}{Usable\ Equity}$$

$Disbursements\ (+)$

- Disbursements for existing and new commitments
- Disbursement schedule depends on modality: Policy-based loans (PBL) disburse much faster (1-2 years) than project loans (7-8 years)

$Repayments\ (-)$

- Repayments and prepayments for existing and new commitments

Risk transfers $(-)$

- Risk transfers to eligible third parties

Programming Considerations: Sovereign Program

- The size of the country program, and its composition (PBLs verses Projects), impacts exposure and future pricing (after 2026)
- With assumptions on future disbursements and repayments, and on ADB’s future usable equity, it is possible to **indicatively assess** how programming impacts exposure and future pricing.
- Exposure limits will be reviewed in about 3 years

Scenario 1: Firm Pipeline

Key Features of 2025-2027 program:

- Volume: 6,090 million
- Modalities: 66% Projects and 34% PBL.
- Resources: 52% COL and 48% OCR.

Commitments	**2024**	**2025**	**2026**	**2027**	**2028+**
OCR - PBL	750	400	900	420	550
OCR - Project	355	200	200	830	545
COL - PBL	-	-	200	150	-
COL - Project	880	1,040	900	850	855
Total ($ million)	1,985	1,640	2,200	2,250	1,950

	2023	**2024**	**2025**	**2026**	**2027**	**2028**	**2029**	**2030**	**2031**	**2032**	**2033**	**2034**
Outstanding Exposure		14,930	15,474	15,986	16,088	16,353	16,684	17,156	17,692	18,200	18,712	19,141
Usable equity	54,443	55,054	56,247	57,195	58,144	59,173	60,159	61,127	62,148	63,211	64,272	65,326
Outstanding % usable equity		27.4%	28.1%	28.4%	28.1%	28.1%	28.2%	28.5%	28.9%	29.3%	29.6%	29.8%
Excess Risk Appetite		2.4%	3.1%	3.4%	3.1%	3.1%	3.2%	3.5%	3.9%	4.3%	4.6%	4.8%
Surcharge Pricing		~~75 bps~~	~~100 bps~~	~~100 bps~~	100 bps	100 bps	100 bps	100 bps	100 bps	125 bps	125 bps	125 bps

- Surcharge Pricing of 100 basis points (bps) for 2027 and 125 bps for 2032 onwards.
- Exposure remains just within risk tolerance for planning horizon of ten years.

Scenario 2: Firm Pipeline +$600m Project Loan (2025)

Key Features of 2025-2027 program:

- Volume: 6,690 million
- Modalities: 60% Projects and 40% PBL.
- Resources: 48% COL and 52% OCR.

Updated Commitments	2024	2025	2026	2027	2028+
OCR - PBL	750	400	900	420	550
OCR - Project	355	800	200	830	545
COL - PBL	0	0	200	150	-
COL - Project	879.78	1040	900	850	855
Total ($ million)	1984.8	2240	2200	2250	1,950

Impact of increase in commitments

	2023	2024*	2025*	2026*	2027	2028	2029	2030	2031	2032	2033	2034
Outstanding Exposure		14,930	15,474	16,061	16,270	16,645	17,078	17,592	18,156	18,672	19,169	19,572
Usable equity	54,443	55,054	56,247	57,195	58,144	59,173	60,159	61,127	62,148	63,211	64,272	65,326
Outstanding % usable equity		27.4%	28.1%	28.6%	28.4%	28.6%	28.9%	29.2%	29.7%	30.0%	30.3%	30.5%
Excess Risk Appetite		2.4%	3.1%	3.6%	3.45%	3.6%	3.9%	4.2%	4.7%	5.0%	5.3%	5.5%
Surcharge Pricing		~~75 bps~~	~~100 bps~~	~~100 bps~~	100 bps	100 bps	100 bps	125 bps	125 bps	X	X	X

- Adding a new project loan will gradually increase ADB's exposure over 7-8 years
- Surcharge Pricing of 100 basis points in 2027, but 125 bps pricing applies earlier (in 2030)
- Risk tolerance (hard limit) would be breached in 2032, leading to suspension of new loans

Scenario 3: Firm Pipeline +$600m PBL (2025)

Key Features of 2025-2027 program:

- Volume: 6,690 million
- Modalities: 57% Projects and 43% PBL.
- Resources: 48% COL and 52% OCR.

Updated Commitments	2024	2025	2026	2027	2028+
OCR - PBL	750	1000	900	420	550
OCR - Project	355	200	200	830	545
COL - PBL	0	0	200	150	-
COL - Project	879.78	1040	900	850	855
Total ($ million)	1984.8	2240	2200	2250	1,950

Impact of increase in commitments

	2023	2024*	2025*	2026*	2027	2028	2029	2030	2031	2032	2033	2034
Outstanding Exposure		14,930	16,016	16,552	16,662	16,890	17,182	17,606	18,092	18,550	19,012	19,391
Usable equity	54,443	55,054	56,247	57,195	58,144	59,173	60,159	61,127	62,148	63,211	64,272	65,326
Outstanding % usable equity		27.4%	29.1%	29.4%	29.1%	29.0%	29.0%	29.3%	29.6%	29.8%	30.1%	30.2%
Excess Risk Appetite		2.4%	4.1%	4.4%	4.13%	4.0%	4.0%	4.3%	4.6%	4.8%	5.1%	5.2%
Surcharge Pricing		~~75 bps~~	~~125 bps~~	~~125 bps~~	125 bps	125 bps	125 bps	125 bps	125 bps	125 bps	X	X

- Adding a new PBL will rapidly increase exposure over 1-2 years
- Surcharge Pricing of 125 basis points applies for 2027 to 2032
- Risk tolerance (hard limit) would be reached in 2033, leading to suspension of new loans
- Risk tolerance is reached later vs. Scenario 2 as PBLs assumed to be repaid earlier than project loans