

**AIB Directive on
Sovereign Risk Rating
December 11, 2018**

1. Overriding Objective

1.1. This Directive on Sovereign Risk Rating (Directive) establishes rules, processes and parameters to ensure the appropriate assessment and monitoring of internal sovereign risk ratings of members of the Asian Infrastructure Investment Bank (AIIB).

2. Definitions

2.1. "Sovereign Direct Financing" denotes a loan made by AIIB to a member of the bank.

2.2. "Sovereign Guaranteed Financing" denotes a loan made by AIIB with the guarantee of a member of the bank.

3. Governance

3.1. Roles and Responsibilities

3.1.1. Risk Management Department (RMD)

- (a) Develops assessment and monitoring processes on sovereign risk rating.
- (b) Measures the sovereign risk inherent in all on- and off-balance sheet activities and performs detailed analysis to justify the sovereign risk rating.

3.1.2. Strategy, Policy and Budget Department (SPB)

- (a) Provides economic analysis to support the sovereign risk rating process.
- (b) Monitors the compliance of AIIB's lending with the International Monetary Fund Debt Limits Policy and the World Bank Non-Concessional Borrowing Policy on borrowing and appraises the RMD of its findings.

3.1.3. The Sovereign Rating Panel (SRP)

- (a) Assesses and proposes sovereign risk ratings to the Chief Risk Officer (CRO).
- (b) Reviews the sovereign risk ratings on a periodical basis.
- (c) Undertakes ad hoc reviews as it may deem necessary from time to time.

3.1.4. The Chief Risk Officer (CRO)

- (a) Approves the key assumptions and limitations to assess sovereign risk ratings.
- (b) Constitutes the SRP, a cross-department panel comprising designated staff from RMD and SPB.
- (c) Assigns sovereign risk ratings to AIIB's members and updates or affirms sovereign risk ratings at least annually.

3.2. Matters arising under this Directive that cannot be resolved between the respective functions shall be brought to the Risk Committee (RC).

4. Risk Assessment

4.1. CRO establishes the methodology to derive risk parameters such as probability of default (PD), loss given default (LGD) and the exposure at default (EAD). RMD continuously reviews the methodology as well as the assumptions, reporting to the RC.

4.2. RMD employs sovereign risk ratings for sovereign-backed financing operations.

- (a) For Sovereign Direct Financings, the sovereign risk rating will be applied as the rating of the project.
- (b) For Sovereign Guaranteed Financings,¹ the sovereign risk rating will be applied as the rating of the guarantor.

5. Risk Monitoring and Reporting

5.1. RMD is responsible for monitoring and reporting AIB's overall sovereign risk profile to RC, the President and the Board of Directors.

6. Information Disclosure by AIB

6.1. AIB's Policy on Public Information and its related Directive and Administrative Guidance govern the disclosure of all information in the bank's possession, including with respect to this Directive.

7. Implementation

7.1. The CRO monitors the implementation of this Directive. The CRO shall prepare and issue the Administrative Guidance that (a) establishes a detailed methodology for sovereign risk rating and (b) provides additional content where required to ensure the efficient implementation of this Directive.

8. Authority

8.1. The CRO shall make all final decisions regarding the application of this Directive.

¹ The final rating of a sovereign-guaranteed loan is a blended rating of the project/borrower and the sovereign government.