Shelter Afrique

Final Rating Report

Agusto&Co.

Research, Credit Ratings, Credit Risk Management

Shelter Afrique

Issuer Ratings:

A+$_{(ken)}$

Aa-$_{(ngr)}$

Outlook: Stable
Issue Date: 19 Sep 2024
Expiry Date: 30 Jun 2025
Previous Rating: A$_{(Ken)}$ A+$_{(ngr)}$

Industry:
Real Estate Finance

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RATING RATIONALE

Agusto & Co. upgrades the national scale ratings assigned to Shelter Afrique ("SHAF" or "the Company") to "**A+$_{(ken)}$**" and "**Aa-$_{(ngr)}$**" with a stable outlook. The rating is hinged on the Company's multilateral legal ownership and relationship with 44 African Governments as well as the critical developmental mandate to drive affordable housing demand and supply in Africa. Our ratings upgrade and stable outlook stem from the impending treaty-based establishment of Shelter Afrique Development Bank (SHAFDB) replacing the existing Act of Parliament foundation which should raise SHAF to a preferential creditor status and forestall the inconsistent capital contributions from the member countries in the near to medium term. As at 31 July 2024, 29 out of the 44-member countries have signed the agreement to establish SHAFDB. The Company's low leverage and acceptable liquidity and capitalisation profiles also support the ratings upgrade. However, SHAF's ratings remain constrained by weak asset quality which has been negatively impacted by legacy delinquent loans.

SHAF is a supranational development financial institution owned by 44 African governments, Africa Development Bank and African Reinsurance Corporation. The Company is governed by an 11-member Board comprising seven Class 'A' directors representing the interests of the member countries, two Class 'B' directors representing the institutional shareholders and two independent directors. SHAF's two largest shareholders are the Republic of Kenya and the Federal Republic of Nigeria with 16.3% and 15.3% equity stakes respectively. The African Development Bank, which is rated "**Aaa**" is the third largest shareholder with an 11.7% stake. The Company has a mandate to support affordable housing and urban development in Africa through the provision of lines of credit to fund mortgage related activities and project finance loans for the construction of housing estates, commercial buildings and infrastructure.

As at the 2023FYE, the Company's gross loans stood at $223.2 million, a significant 17.2% decline from the prior year, largely due to the negative impact of the depreciation of the Naira by 50.12% and the translation of loans to US$. However, non-performing loans (NPLs) remained significant and accounted for 51% of gross loans. The NPLs were legacy exposures largely to developers who were unable to complete projects after SHAF stopped funding following breaches in the terms of the loan agreement. The Company has continued to drive recoveries with collections of $929,966 in 2023, marginal in comparison to the $2.8 million reported in 2022. SHAF's cumulative loan loss provisions covered 75.2% of NPLs, with the uncovered amount equating to 17% of shareholders' funds, which we consider significant. In our opinion, the Company's asset quality is weak – constrained by the legacy non-performing credits and the expected high loan impairment charges. We expect the impending treaty-based agreement to elevate SHAF to a preferred creditor status which should aid loan recoveries and forestall future delinquencies.

As at the 2023 FYE, SHAF's liquid assets to total assets ratio was 26.5% (2022: 32.1%), which was below our minimum expectation of 30% but higher than the Company's internal benchmark of 15%. However, we view positively that SHAF has a $20 million contingent facility with a Nigerian bank that has international authorisation. Thus, in our opinion, the Company's liquidity profile is acceptable.

As at 31 December 2023, SHAF had $166 million in shareholders' funds, which funded a higher 74% (2022: 58.6%) of total assets. The Company's shareholders' funds predominantly comprised issued share capital given the sizeable accumulated losses of approximately $31.5 million as at the same date. Nonetheless, as at the 2023 FYE, SHAF recorded a better Basel II capital adequacy ratio of 34.4% (2022: 25.7%), which was above our minimum benchmark of 20% and higher than the internal minimum standard of 25%. Capitalisation profile in the review period was supported by equity injection totalling $8 million. However, the injected equity represented only 28% of the 2023 target of $26 million due to unresponsiveness from member countries as a result of events including elections, weakness in macroclimate, civil unrest and the lingering effect of COVID on the finances of many African governments. The Company is actively engaging shareholders to raise a target amount of $20 million in 2024 which the management team believes is achievable.

Excluding the reliance on shareholders for funding through periodic capital calls, SHAF has an internal maximum leverage ratio (debt to equity) set at 300% of called capital. In 2022, the Company issued a $110 million (₦46 billion) bond in Nigerian Naira with tranche A due in 2027 and tranche B due in 2029 at interest rates of 13% floating and 13.25% fixed per annum respectively. Thus, as at the 2023 FYE, SHAF's debt financing, which funded 26% of total assets, primarily (90%) comprised borrowings while other liabilities made up a small share (10%). Nevertheless, as at the 2023 FYE, leverage remains low, with a debt-to-equity ratio of 0.3x (2022: 0.7x), which was significantly below our threshold for DFIs. The Company is in discussions with DFIs to raise additional borrowings to fund up to 80% of total assets in the medium term, while equity, commercial bank borrowings and debt issuances will finance the balance of 20%.

SHAF's developmental objective of promoting and financing affordable housing and urban development in Africa makes profitability a secondary goal. However, the Company's profitability indicators have been volatile in the last five years with a swing to profits in the 2023FY, evidenced by a profit before tax (PBT) of $0.9 million (2022: $11.8 million loss), which we view positively. Thus, profitability indicators – return on average assets (ROA) and return on average equity (ROE) improved to 0.4% (2022: -5.4%) and 0.6% (2022: -7.4%) respectively. Whilst we recognise that profit maximisation is secondary to SHAF's developmental objectives, the profitability indicators were significantly below our expectations for DFIs. Based on unaudited accounts for the first six months of 2024, the Company's recorded a PBT of $5 million and annualised ROE and ROA were higher at 4.6% and 5.9% respectively. In our view, SHAF's profitability is weak. Nevertheless, we believe that profitability will improve in the near term given the aggressive delinquent loan recovery drive and plans to accelerate lending.

Based on the aforementioned factors, we hereby attach a "**stable**" outlook to the rating.

Positive Rating Triggers

- Full resolution of the legacy loan portfolio
- Sustained profitability indicators
- Shareholders' clearance of outstanding capital arrears and enhanced capitalisation metrics
- Improved credit ratings of the two principal sovereigns
- Obtaining the necessary amount of signatories to establish SHAFDB

Negative Rating Triggers

- Non-performing loan ratio above 25% by the 2025 FYE
- Loss before tax by 2024 financial year end
- Significant deviation from the 'New Dawn' strategy plan
- High staff turnover (above 5%) in senior management cadre in the 2024 FY
- Any change in the impending treaty based agreement to establish SHAFDB

Figure 1: Strengths, Weaknesses and Challenges

Strengths

- Strategically important developmental mandate
- Multilateral legal ownership and relationship with 44 African Governments
- Significant tax benefits including full exemption from any taxation in Kenya
- Strong brand recognition in most countries with a SHAF presence
- Adequate capitalisation
- Acceptable liquidity profile
- Low leverage

Weaknesses

- Sluggish capital receipts from member countries
- Asset quality is constrained by the high volume of impaired legacy loans
- Weak profitability
- Frequent changes on the Board

Challenges

- Improving income sustainably
- Raising considerable (and inexpensive) funding
- Challenging macro environment in member countries
- Growing competition from larger DFIs in the housing space
- Weak investment climate and regulatory environment for housing in Africa

Table 1: Financial Data for SHAF

	31 December 2022	31 December 2023
Total Assets	$270 million	$224 million
Net Earnings	$475,354	$9.5 million
Pre-tax return on average assets	-5.4%	0.4%
Pre-tax return on average equity	-7.4%	0.6%

COMPANY PROFILE

Shelter Afrique ("SHAF" or "the Company"), also known as the Company for Housing and Habitat in Africa, is a pan-African housing finance and development institution. SHAF was established by African Governments, the African Development Bank, the African Reinsurance Corporation and the CDC Company Plc to address the need for innovative and sustainable housing delivery systems in Africa. The Company is an international body with a juridical personality and full legal capacity established by the Constituent Charter of Shelter Afrique. SHAF began operations on 23 December 1985 following the assent of the Shelter Afrique Act, which is an Act of Parliament of the Republic of Kenya.

Table 2: Board of Directors

Directors	Position	Country/Representing
Dr. Chii Akporji	Board Chairperson	AfDB
Mr Ahmed Belayat	Vice Chairperson	Algeria/Group 4 countries
Mr Babatunde Sanda	Member	Nigeria/Independent
Mr Lionel Zinsou	Member	Benin/Independent
Mr Ephraim K. Bichetero	Member	Uganda/Africa Re
Mr Issa Sissoko	Member	Mali/Group 7 countries
Mr Said Athman Mtwana	Member	Kenya/Group 1 countries
Dr Jack Ngarambe	Member	Rwanda/Group 2 countries
Mr Chris Pobee Abbey	Member	Ghana/Group 3 countries
Mr Tchelu M. Laurent	Member	DRC/Group 10 countries
Mrs Eucharia Alozie	Member	Nigeria/Group 6 countries

SHAF provides financial and technical assistance for housing and urban development activities in Africa. The Company supports integrated affordable solutions for mixed-use, mixed-income housing developments, rental housing developments and construction of large-scale housing projects. SHAF also supports social housing programmes in member countries. SHAF's principal office is located at the Shelter Afrique Centre, Longonot Road, Upper Hill, Nairobi, Kenya. The Company has two regional offices situated in Abuja, Nigeria and Abidjan, Cote d'Ivoire.

In October 2023, there was a special resolution to establish the Shelter Afrique Development Bank ("SHAFDB"), at the extraordinary general meeting of the Company's shareholders in Algeria. SHAFDB is to be established by a treaty and this would lead to a change of name for SHAF. In the territory of each member country, SHAFDB shall possess full juridical personality and full capacity to contract, acquire and dispose of immovable and movable property and institute and defend legal proceedings. The purpose of SHAFDB will remain to promote the financing of affordable housing and urban development in Africa, taking into consideration the evolving development needs across the continent. As at 31 July 2024, 29 out of the 44-member countries have signed the agreement to establish SHAFDB. The Company's target is to secure participation from 15 countries, which represent at least of 51% of the shareholding by Q1'2025.

Business Strategy

'Stabilisation, modest growth towards sustainable resilient and inclusive development' is SHAF's key theme for the near to medium term. This theme has been broken down into three broad goals: enhancing housing development impact and shareholders' value, achieving financial sustainability and improving organisational sustainability, which will help the Company deliver its mandate and returns to shareholders. In line with these goals, four business units will drive the execution of SHAF's strategy for affordable housing finance solutions: Financial Institutions Group (FIG), Project Finance Group (PFG), Public Private Partnerships (PPP) & Sovereign and Fund Management Group (FMG). These units will focus on investments with financial institutions, project finance structuring and direct investments, collaboration with member states and raising concessional/blended funding respectively to provide solutions for affordable housing demand and supply. The special resolution to establish SHAFDB via a treaty, which is a more binding agreement between nations, provided the opportunity to review the statutes to address gaps, ambiguities, interpretation issues and inconsistencies with the aim of reducing the existing challenges around capital arrears and legacy delinquent loans.

Business Structure

In line with the new strategic focus, SHAF is structured along seven major units:

- Corporate Functions (comprising Internal Audit, Company Secretary and Enterprise Risk Management)
- Office of the Managing Director (comprising the Executive Assistant, Communications & External Affairs, Investor Relations, Strategy, Policy, Research & Partnerships and Advisory)
- Business Sector/Industries (FIG, PFG, FMG and PPP & Sovereign)
- Finance
- Credit and Operations
- Human Capital Management
- Legal & General Counsel

The four business sector units – FIG, PFG, FMG and PPP & Sovereign – are led a Chief Business Officer, who reports directly to the CEO. All heads of departments at SHAF report to the CEO except for the heads of the Enterprise Risk Management, Company Secretary and Internal Audit units, who report functionally to the Board and administratively to the CEO.

Information Technology

SHAF uses Oracle Cloud Enterprise Resource Planning (ERP) as the core enterprise application for treasury, procurement, human resources & performance management and accounting. The ERP also incorporates Oracle Loans for credit administration. Other solutions used by the Company include Microsoft Office365, World Check One AML, Auto Audit, ICT Helpdesk and Intranet. The "SHAF Anywhere" programme enables staff to work from any location using solutions such as virtual private networks, video conferencing and DocuSign e-signature. In the review year, SHAF integrated the SWIFT payment system with the Oracle Cloud ERP and the application is undergoing tests ahead of full deployment in December 2024. The Company plans to improve disaster recovery processes by implementing a cloud-based storage system and automate loan management, monitoring and compliance processes in the near to medium term.

MANAGEMENT TEAM

Mr Thierno-Habib Hann is SHAF's Chief Executive Officer. He joined Shelter Afrique from the International Finance Corporation, where he served as the Asia/Pacific Lead for housing finance, based in Bangkok, Thailand. Mr Hann has extensive international experience in housing finance, capital markets/investment banking and structured finance spanning over 20 years. He began his career at Arthur Andersen, LLC as a Consultant in Financial Services and Capital Markets in New York, USA. Mr Hann also worked at JPMorgan Chase and Goldman Sachs as Manager and Vice President respectively and led investment teams issuing mortgage-backed securities (RMBS/CMOs) and credit derivatives (CDS). He has also served at the World Bank Group as the Private Sector Development Program Manager in Guinea, responsible for designing and implementing the investment climate improvement program while developing a bankable pipeline of investments and government advisory projects.

Mr Hann holds a Master's degree in Accounting and Finance (M.S.T.C.F) and a Bachelor's degree in Management and Applied Economics (GEA) from the University of Paris IX Dauphine, France. He also holds an MBA in Finance & Investments from the Zicklin School of Business, Baruch College, New York, USA.

Other members of SHAF's senior management team include:

▪ Mrs Beatrice Mburu	Chief Finance Officer
▪ Mrs Juliet Kavaruganda	Company Secretary
▪ Mr Christopher Chege	Head of Credit and Operations
▪ Mr Bernard Oketch	Head of Enterprise Risk Management
▪ Mr Gibson Mapfidza	Chief Business Officer
▪ Ms Marianne Koly	Head of Internal Audit
▪ Mr Nabil Mahfoudh	Head of Treasury
▪ Mr Charles Kazuka	Head of Human Resources and Administration
▪ Dr Muhammad Gambo	Head of Policy, Research and Partnerships
▪ Mrs Natasha Koli	Acting Head of Legal Services
▪ Ms Nisan Abdulkader	Head of Communications
▪ Mr Ibrahim Mamadou Diop	MD/ CEO Advisor

ANALYSTS' COMMENTS

OWNERSHIP, MANAGEMENT & STAFF

SHAF is a pan-African development finance institution (DFI) that exclusively supports the development of the housing and real estate sector in Africa. The Company is owned by 44 African governments and two African financial institutions – the African Development Bank (AfDB) and Africa Reinsurance Corporation ('Africa Re'). We believe that SHAF's ownership shows moderate concentration, with the five largest shareholders – Kenya, Nigeria, AfDB, Ghana and Mali – holding the bulk (53.3%) of the equity while a smaller balance (46.7%) is held by the other 40 African countries and one institution. We expect moderate dilution of the Company's ownership in the near term, with the onboarding of new shareholders. This includes the buy-ins of Fonds de Solidarite Africain (a proposed Class B shareholder) and South Sudan (a proposed Class A shareholder) ratified by the Annual General Assembly in 2021 and 2022 respectively.

We expect SHAF's shareholder base to be further diluted in the medium term following the special resolution of October 2023. SHAFDB's authorised share capital of $1 billion of one million ordinary shares at a par value of $1,000 shall be divided into three classes – A, B and C, which shall be available for subscription. Class A shares shall constitute at least 45% of the authorised and issued share capital and would be offered, allotted and issued to African countries. Class B shares shall constitute up to 30% of the authorised and issued share capital and would be offered to African continental, regional and sub-regional organisations. Class C shares shall constitute up to 25% of authorised and issued share capital and would be offered to non-African countries and African and non-African public and private sector entities and individuals not otherwise falling into Class A or Class B above. All Class A, Class B and Class C shares shall rank "pari passu" in all respects. We believe that this share structure gives the Company access to a broader universe of potential shareholders.

SHAF is governed by an 11-member Board of Directors ("the Board"), which is chaired by Dr Patience Chika Akporji, who represents AfDB. The members of the Board are all non-executive directors. The Board comprises seven Class 'A' directors representing the interests of the member countries, two Class 'B' directors representing the institutional shareholders and two independent directors. The Company has established and documented terms of reference and process for the appointment of independent directors including a maximum tenure of two terms of three years, which we view positively. In the review year, the Board elected Mr Ahmed Belayat as the Vice Chairperson for a 1-year renewable tenure. We believe that there is a satisfactory representation of shareholders on the Board. However, we note that the frequent changes on the Board can negatively impact the stability and oversight of SHAF's strategic direction.

The Company has four board committees: the Audit and Risk Committee, the Finance, Credit & Investments Committee, the Strategy, Business Conduct and Ethics Committee, and the Human Resources, Governance and Nominations Committee, which are all chaired by Class 'A' and 'B' directors. However, we believe that at least one of the committees – the Audit and Risk Committee, should be chaired by an independent member of the Board in line with corporate governance best practice.

There were changes to the Company's executive management in the review period. Following the resignation of Mrs Houda Boudlali, the Head of Legal Services on 15 March 2024, Mrs Natasha Koli has been appointed as the Acting Head of the legal department. In addition, Mr Benson Ngare, the acting Head of Internal Audit has been replaced by Ms Marianne Koly who joined in January 2024. Agusto & Co. remains concerned about the frequent changes in the senior management team, which could significantly disrupt the implementation of SHAF's turnaround strategy. Nonetheless, we note that the Company's management team comprises skilled professionals, with over 15 years of experience on average. In 2023, SHAF had 55 employees (2022: 48), who are citizens of 17 of the member African countries. Staff productivity, measured by the number of times net earnings covered staff cost, was 2x (2022: 0.1x), which was below our expectation of at least 3x for a DFI. Nevertheless, we believe that the Company's management has good depth of experience.

ASSET QUALITY

SHAF focuses on originating lines of credit and project finance loans while ensuring sufficient liquid assets to meet disbursement requirements. As at 31 December 2023, the Company's total assets stood at $224.3 million, a 17% decline from the end of the prior year. The drop in total assets was largely due to the impact of the 50.12% devaluation of the Nigerian Naira (₦) from a rate of ₦448.55 to the US Dollar ($) in 2022 to a rate of ₦899.39 to $1 in 2023. The Nigerian Naira depreciation negatively impacted the US Dollar translation of asset values – especially cash and equivalents and the loan portfolio. Nevertheless, as at 31 December 2023, the Company's gross loans stood at $223.2 million (2022: $269.5 million), representing the dominant asset class and constituting 99.5% of total assets. In the year under review, notwithstanding the Naira devaluation's effect on loan portfolio valuation, SHAF's net loan disbursements stood at $19.1 million (2022: $80.7million), which was conservative in our view. Based on unaudited accounts as at 30 June 2024, the Company's loan book stood at $227.8 million, with the growth remaining relatively small at 2%. In our opinion, SHAF's conservative approach to loan disbursements constrains profit margins and its developmental impact. However, we expect notable growth in the loan book in the near term, as the Company aims to deploy the residual funds from the proceeds of the debut bond by December 2024.

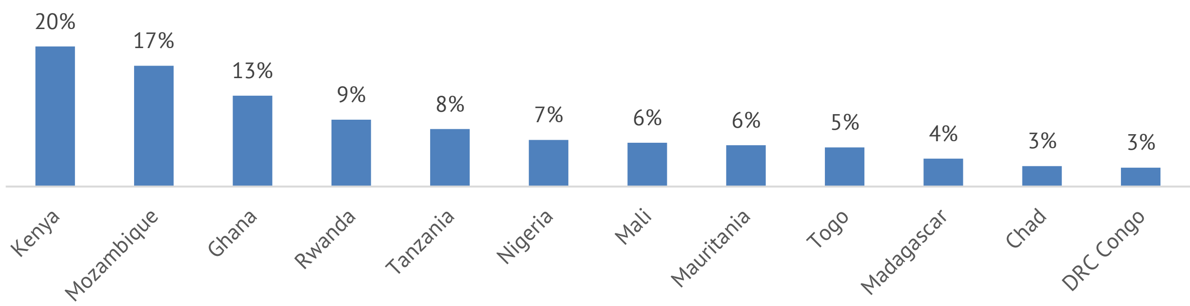
As at the 2023 FYE, the Company's exposures showed concentration by obligor, with the top 20 borrowers constituting 74% of the loan portfolio. In addition, SHAF's loans were dominated by US Dollar and Euro-denominated exposures, which represented 85% of the portfolio while matched exposures in the currencies of member countries (Kenyan Shillings, CFA and Naira) made up a relatively small balance of 15%. We expect to see greater concentration of the loan portfolio in USD in the near term given plans to fund up to 80% of total assets with borrowings from international DFIs. To mitigate FX risks on the proposed borrowings, loans will be given to clients who can repay both principal and interest in US$ to ensure that the assets are perfectly matched to liabilities. However, for certain markets, loan disbursements in US$ would not be tenable and therefore, local currency bonds will be raised to fund those obligors. In addition, the Company plans to utilize FX hedges including swaps to mitigate foreign exchange risks. We note that some African governments reject the pricing of real estates in US$ and thus, we expect significant FX risks in the disbursements of the DFI dollar borrowings.

SHAF's lending activities as at the 2023 FYE were largely (51%) skewed to Francophone West/Central Africa and Anglophone West Africa (27%), with loans to borrowers in these regions jointly accounting for the bulk (76%) of the portfolio. Exposures to obligors in Eastern (12%) and Southern Africa (10%) made up a smaller balance of the loan book. We do not expect significant changes in the concentration of the loan book by region especially with the implementation of SHAF's "VIRAL" strategy to scale up operations. VIRAL – an acronym for Vision, Institutions, Regulations, Actors and Local Initiative Support, will initially be implemented in six countries (Zambia, Democratic Republic of Congo, Guinea-Conakry, Nigeria, Lesotho and the Republic of the Congo) and eventually across the 44-member countries. With VIRAL, SHAF's vision remains affordable housing for all but in collaboration with institutions such as central banks, mortgage refinance companies and collateral registries. Local initiatives and regulations including housing subsidy schemes and mortgage foreclosure laws will be key to bringing onboard actors such as banks, cooperatives, insurance companies and development finance institutions. Consequently, the implementation of the VIRAL model will culminate with the design of a partnership strategy that will guide the execution plan for each member country. Thus, overall, we expect the implementation of the VIRAL model in the first six countries to maintain the concentration by region in the near term. However, we expect better diversification of the loan portfolio in the medium term as SHAF prioritises a more even spread of its developmental impact across the 44-member countries.

The bulk (65%) of the Company's loans comprised medium-term project finance loans to developers while short to medium-term lines of credit to financial institutions to on-lend for mortgage related activities also made up a significant share (32%). We expect this trend to continue in the near term in line with the Company's mandate as, the Project Finance Group (PFG), Public Private Partnerships (PPP) & Sovereign units are properly resourced and ramp up activities.

As at 31 December 2023, SHAF's stage three or non-performing loans (NPLs) remained significant at $112.8 million, albeit recording a 20% year-on-year decline due largely to the write-off of $19.1 million of legacy delinquent credits. Nevertheless, NPL to gross loan ratio remained high at 50.6%, albeit, slightly lower than the 52.6% recorded in the prior year. We note that over 70% of NPLs were project finance loans, with the bulk comprising legacy loans related to incomplete projects that had funding withdrawn because the obligors were in breach of terms of the loan agreement.

Figure 2: NPLs by Obligors' Countries



To satisfactorily address the issue of the legacy NPLs portfolio, SHAF's management is leveraging the support from governments of member countries where the obligors are domiciled. The Company has also engaged KPMG Kenya to supplement the efforts of the internal teams for the resolution of the NPLs. KPMG will be instrumental in the establishment of a good and a bad book to ensure that the legacy NPL portfolio is ring-fenced and given special attention. SHAF also continues to drive recoveries, with collections of $929,966 in 2023, a marginal result compared to the recoveries of $2.8 million reported in 2022. In our view, given the Company's member countries' limited foreclosure laws and drawn-out court processes, the NPLs are unlikely to be recovered in the near to medium term. Therefore, we expect the NPL ratio to remain high in the near term. Unaudited accounts as at 30 June 2024 indicate that the NPL ratio remained stagnant at 50.7%, with a 2% growth in stage 3 loans (in absolute terms) due largely to newly classified exposures. However, we expect that SHAF's transition to a treaty-based establishment, along with entering into strategic agreements with governments of the countries where legacy delinquent loans are rife might address the NPL challenges in the medium term.

As at 31 December 2023, the Company's loss provisions covered 75.2% of NPLs, with the uncovered amount equating to 17% of shareholders' funds, which we consider significant. We expected a minimum NPL coverage ratio of 100% which indicates a proactive recognition of losses to limit the impact of impairments on future earnings. Nonetheless, the Company's management has affirmed that the uncovered portion is fully secured through the legal charges on property and this should mitigate any impact on future earnings.

As at the 2023 FYE, liquid assets totalling $59.4 million constituted the second largest asset class and predominantly (91%) comprised placements with well-rated financial institutions. Federal Government of Nigeria (FGN) Naira bonds made up a relatively small balance (9%). In the year under review, a significant 52% of placements were denominated in USD and domiciled primarily with Kenyan banks of investment grade credit quality on the national rating scale. This provided more value retention relative to the soft domestic currencies of member countries. A significant (34%) share of placements was held as Naira placements with investment grade Nigerian banks on a national rating scale to support the disbursements and repayments of the Naira bonds. A relatively small balance of 14% was held as deposits – mainly in CFA, Euro and Kenyan Shilling, in banks across different countries. We view positively the short tenured nature of the placements (with maturities of 90 days or less), which supports the Company's liquidity needs.

However, overall, we consider SHAF's asset quality to be weak given the large portfolio of legacy NPLs, which remains a drag. We believe that charge offs on the legacy NPLs will continue until the problematic loans have been eliminated from the Company's books.

Risk Management

The Board is responsible for the establishment and review of the effectiveness of the Company's risk appetite, risk management framework and system of internal control. The Board carries out this responsibility through the four standing committees. The Board also delegates some powers to ad-hoc committees where necessary. The responsibility for the day-to-day running of SHAF is delegated by statute to the CEO, who is supported by a team of ten professionals. The business units are the first line of defence in the management of risks while the Enterprise Risk Management (ERM) unit and the Internal Audit team provide the second and third lines of defence respectively.

In the review year, a credit department was created to enhance credit underwriting and portfolio monitoring and the new Head of Credit and Operations, Mr Christopher Chege took office on 2 April 2023. Based on the updated structure, the Financial Institutions Group, Project Finance Group and Public-Private Partnerships & Sovereign business units are responsible for loan origination while the Treasury team manages the placements. Credit origination relies on internal credit risk assessments conducted by the credit and ERM teams, which appraise the prospective counterparties using financial and non-financial criteria covering areas including governance, capital, earnings and liquidity. The Treasury unit only makes placements in eligible currencies including the US Dollar, Nigerian Naira and Kenyan Shilling. Placements are largely made with tier one and tier two Kenyan and Nigerian banks deemed to have acceptable risk.

The origination process for project finance loans is more intensive, involving multiple stages and requirements including due diligence, KYC, valid and unencumbered title to the land, project documentation (social impact assessment, cash flow analyses and financial projections), technical information and on-site reviews. Project finance loans must be reviewed by SHAF's technical committee and loans committee and secured to the tune of at least 130% of the loan amount either by collateral such as prime property and fixed income securities or guarantees. Unsecured lines of credit may be provided depending on the risk profile of the institution. The Company only provides lines of credit to financial institutions deemed to be of acceptable risk. All lines of credit and project finance loans must be approved by the Board.

The Internal Audit unit reviews business and risk management processes and reports to the Board through the Audit and Risk Committee, which approves the annual work programme. SHAF conducts regular Risk and Control Self Assessments (RCSA) for all the units, with the business teams collaborating with ERM to record and mitigate the identified risks. The departmental risk & compliance champions drive the RCSA process and the ERM team further assesses the likelihood and impact of identified risks crystallising to provide an overall risk rating. The results are reported to the executive management team and board committees quarterly.

In our opinion, SHAF has an adequate risk management framework for affordable housing financing in member countries with weak macroeconomic and credit profiles. However, the Company's risk management structure is yet to witness significant underwriting activities due to the restricted operations over the last six years.

CAPITAL & LEVERAGE

SHAF relies on its shareholders for funding through periodic capital calls. The Company has a callable capital of $500 million and an internal maximum leverage ratio (debt to equity) of 300% of called capital. In our opinion, the relatively small callable capital and conservative leverage ratios are significant contributors to SHAF's minimal developmental impact.

As at 31 December 2023, the Company had issued and called capital of $288.2 million with $129.8 million fully paid. SHAF's policy is to give shareholders a period of five years to meet capital call obligations. However, we note that only nine countries namely: Republic of Congo, Morocco, Democratic Republic of Congo, United Republic of Tanzania, Zimbabwe, Namibia, Togo, Mali and Kingdom of Lesotho are fully paid members as at 31 December 2023. We believe that the Company's shareholders need to demonstrate greater consistency in the payment of the capital call arrears to achieve the developmental mandate. Consequently, we do not factor in SHAF's callable capital as tier 2 or hybrid capital in our rating. Notwithstanding, we expect that the issue of capital arrears will be eliminated with the establishment of SHAFDB by a treaty, which is a more binding agreement between nations. The treaty makes every member liable for every capital call and gives SHAFDB the right to set-off any amounts due against dividends or other amounts or assets payable to such member.

As at 31 December 2023, SHAF's shareholders' funds stood at $166 million, up by 4.8% from 2022 due to the capital receipts of $7.5million from seven countries (see table below). The injected equity represented only 28% of the 2023 target of $26 million, with unresponsiveness from members due to events including elections, weakness in macroclimate, civil unrest and the lingering effect of COVID on many African countries' finances. The Company is actively engaging the shareholders to raise a target amount of $20 million in 2024. SHAF's management has also affirmed that continuous efforts are being made to complete the onboarding of new shareholders: Fonds de Solidarite Africain (Class B) and South Sudan (Class A), which were ratified by the Annual General Assembly in 2021 and 2022 respectively. Discussions have also been held and keen interest shown from non-member African countries including Egypt, Ethiopia, South Africa and Angola to join Shelter Afrique. As the finances of African governments improve and shareholders show greater willingness to inject more equity into the Company, we expect capitalisation to improve. We also believe that the transition to SHAFDB will help drive significant growth in capital.

Table 3: Equity injection in 2023

Member Countries	Equity Injected in 2023 (in $'M)
Congo	3.9
Gabon	0.5
Lesotho	2.0
Uganda	0.1
Burkina Faso	0.5
Eswatini	0.3
Rwanda	0.3
Total	**7.5**

Nevertheless, SHAF's shareholders' funds of $166 million funded 74% (2022: 58.6%) of total assets as at the 2023 FYE and predominantly comprised issued share capital given the significant accumulated losses of about $31.5 million. The Company also recorded a Basel II capital adequacy ratio (CAR) of 34.4% (2022: 25.7%) as at the 2023 FYE. SHAF's CAR was better than our least expectation of 20% and the internal minimum standard of 25%, due to the low amount of risk weighted assets in the review period. The Company also had a debt-to-equity ratio of 0.3x (2022: 0.7x), which was significantly below our threshold for DFIs. However, we expect a rise in leverage in the near term as SHAF obtains borrowings predominantly from DFIs, commercial banks and issuing bonds in member countries' capital markets to drive developmental impact.

Overall, SHAF's leverage is low and capitalisation is acceptable. In our view, additional capital will be required to record significant development impact.

LIQUIDITY & FUNDING

SHAF is a non-deposit taking DFI and is mainly funded by long-term capital from shareholders and borrowings. As at the 2023 FYE, the Company's debt financing, which funded 26% of total assets, primarily (90%) comprised borrowings while other liabilities made up a small share (10%). In 2022, SHAF issued a $110 million (₦46 billion) bond in Naira in the Nigerian debt capital markets with tranche A due in 2027 and tranche B due in 2029 at interest rates of 13% floating and 13.25% fixed per annum respectively. The Company is in discussions with existing and potential DFI partners to raise additional borrowings to fund loans in the medium term that will account for 80% of total assets, while equity, commercial bank borrowings and debt issuances will finance the balance of 20%. SHAF expects to secure funding of up to US$80million in the 2024FY from various development financial institutions. There will also be targeted thematic opportunities such as fundraising from climate green funds, Islamic ring-fenced funds, Trade Finance, SMEs and diaspora funds and diaspora funds. We expect the newly established Fund Management Group to play a significant role in these concessional funds raising activities to drive affordable housing supply and demand.

As at 31 December 2023, SHAF had liquid assets[1] of $59.4 million, representing a 31% decline from the prior year primarily due to the disbursement of proceeds of the bond issuance which were previously placed in short term investments. Consequently, the liquidity ratio (liquid assets to total assets) declined to 26.5% (2022: 32.1%), which was below our minimum expectation of 30% but higher than the Company's internal benchmark of 15%. Unaudited accounts as at 30 June 2023 indicated that SHAF's liquidity ratio declined significantly to 18.5% due to the liquidation of short-term placements for loan disbursements. We note that SHAF's clients typically pay their principal and interest payments quarterly and semi-annually and thus, liquidity ratio is cyclical. Management has also confirmed the receipt of capital inflows of US$5million from Nigeria, which has been invested in short term placements and bolstered the liquidity ratio to 23% as at 31 July 2024.

[1] Liquid assets exclude equity investments in Pan African Housing Fund LLC (Mauritius); Caisse Régionale de Refinancement Hypothécaire (CRRH), Togo; the Tanzania Mortgage Refinance Company Limited, Kenya Mortgage Refinance Company Limited and FundCo Capital Managers Limited.

Furthermore, we view positively that the Company has a $20 million contingent facility with a Nigerian bank that has international authorisation. Overall, in our opinion, SHAF's liquidity and funding profile is acceptable.

EARNINGS AND PERFORMANCE

The Company's earnings are predominantly generated from the interest charged on project finance loans and lines of credit granted for real estate related activities. SHAF also generates considerable interest income from holding a portfolio of liquid assets which are largely placed with financial institutions domiciled in Kenya and Nigeria. Recoveries have also been a major source of income as the Company has prioritised the collection of legacy delinquent assets as part of its turnaround strategy.

In the financial year ended 31 December 2023, SHAF generated interest income of $25.7 million, a 48% growth from the prior year, with the bulk (69%) representing earnings from core lending activities while a significant balance (31%) was realised from bank placements. Growth in core income from lending was supported by disbursements of up to $19.1 million in the review year. SHAF plans to grow the loan portfolio by at least $31 million (14%) to reach $254 million as at 31 December 2024. However, contrary to growth in interest income, during the 2023FY, interest expense grew at a slower pace and remained at $10.1 million (2022: $10 million). The Company also recorded lower loan loss expense of $4.6 million (2022: $8.2 million) supported by impairment recoveries of $0.93 million (2022: $2.8 million). Consequently, SHAF's net interest income improved to $11.1 million, which was 13.6 times the amount recorded in the prior year. This translated to a significantly higher net interest spread (NIS) of 60.8% compared to the 42.5% recorded in the prior year. In the near term, we anticipate a higher contribution to NIS from interest income from core lending activities given plans to ramp up disbursements.

In the review year, the Company recorded FX losses on investment in the Federal Government of Nigeria's bonds and loss in some joint ventures with Kenyan real estate companies which totalled $2.8 million. Nevertheless, overall, in the 2023 FY, SHAF's net earnings of $9.5 million, was 19.9 times the previous year. In the short term, we expect moderate growth in net earnings supported by income from investments given the higher yield environment.

In 2023, SHAF incurred lower operating expenses of $8.5 million, which represented an 11% decline from 2022 due to reduced travels for official missions and lower business promotion, consultancy and legal expenses. Thus, in 2023, the cost-to-income ratio (CIR) declined considerably to 89% (2022: 2577%), albeit higher than the Company's target of 70%. In the review year, SHAF also recorded a profit before tax of $0.9 million (2022: $11.8 million loss), which we view positively. Thus, profitability indicators – return on average assets (ROA) and return on average equity (ROE) improved to 0.4% (2022: -5.4%) and 0.6% (2022: -7.4%) respectively. Whilst we recognise that profit maximisation is secondary to the Company's developmental objectives, the profitability indicators were significantly below our expectations for DFIs and have been volatile in the last five years. Based on unaudited accounts for the first six months of 2024, SHAF's recorded a profit before tax of $5 million, with the annualised ROE and ROA improving to 4.6% and 5.9% respectively. In our view, the Company's profitability is weak. However, we believe that profitability will continue to improve in the near term given the aggressive recovery drive and plans to increase lending.

OUTLOOK

To fully embody its role as an international development finance institution, in October 2023, there was a special resolution agreed to establish the Shelter Afrique Development Bank (SHAFDB), at the extraordinary general meeting of shareholders held in Algeria. As SHAFDB, the Company should attain the Preferred Creditor Status (PCS) and be given priority for the repayment of debt in the event of a borrower experiencing financial stress. Under a broader approach to PCS, SHAFDB's loan servicing will also be protected against restrictions on foreign exchange in a particular country. Thus, we expect a lower number of newly classified impaired loans in the medium term. A better-quality loan book will also be supported by aggressive recoveries, more efficient on boarding of clients and vigorous credit underwriting as well as the institution of Environmental, Social and Governance (ESG) standards.

Given the new treaty-based agreement to establish SHAFDB, Agusto & Co. anticipates a modest increase in shareholders' equity bolstered by capital calls from member countries and higher reserves from more profitable operations with the creation of better-quality risk assets. Furthermore, with plans to obtain additional borrowings from DFIs and in the domestic debt capital markets of other member states in the near term, we expect the Company's funding to improve and leverage to rise but remain within acceptable limits. We also believe that SHAF's liquidity profile should remain satisfactory in the near term supported by the contingent credit line from the commercial bank.

We hereby attach a "**stable**" outlook to the rating.

FINANCIAL SUMMARY

SHELTER AFRIQUE						
STATEMENT OF FINANCIAL POSITION AS AT	**31-Dec-21**		**31-Dec-22**		**31-Dec-23**	
	$		**$**		**$**	
ASSETS						
Cash & equivalents	5,912,851	4%	3,400,643	1.3%	3,768,295	1.7%
Quoted investments		0%	10,392,317	3.8%	5,494,640	2.4%
Short-term placements	25,677,981	15%	72,961,707	27.0%	50,169,333	22.4%
Liquid Assets	31,590,832	19%	86,754,667	32.1%	59,432,268	26.5%
Gross Loans	244,246,753	146%	269,541,177	99.7%	223,161,442	99.5%
Less: Cumulative loan loss provision	(131,655,081)	-79%	(114,529,205)	-42.4%	(84,860,080)	-37.8%
Total loans & advances - net	112,591,672	67%	155,011,972	57.3%	138,301,362	61.7%
Interest receivable	294,495	0.2%	153,274	0.1%	67,763	0.0%
Other prepayments	488,235	0.3%	540,613	0.2%	590,652	0.3%
Other accounts receivables	2,146,621	1.3%	3,482,371	1.3%	1,508,029	0.7%
Unconsolidated subsidiaries & associates	4,086,707	2.4%	2,823,239	1.0%	2,505,135	1.1%
Other long-term investments	5,458,000	3.3%	5,445,000	2.0%	5,557,000	2.5%
Fixed assets & intangibles	11,809,420	7.1%	17,421,783	6.4%	16,313,690	7.3%
Total Assets	**167,317,852**		**270,422,450**		**224,275,899**	
CAPITAL & LIABILITIES						
Shareholders' Funds	161,603,767	97%	158,399,320	59%	166,012,818	74.0%
Total Borrowings		0%	105,195,956	39%	52,463,873	23.4%
Other Liabilities	5,714,085	3%	6,827,264	3%	5,799,208	2.6%
Total Capital & Liabilities	**167,317,852**		**270,422,450**		**224,275,899**	
AUDITORS	**PWC**		**PWC**		**PWC**	
Opinion	**Clean**		**Clean**		**Clean**	

INCOME STATEMENT FOR THE YEAR ENDED	**31-Dec-21**		**31-Dec-22**		**31-Dec-23**	
	$		**$**		**$**	
Interest income	12,092,354	89.8%	17,393,315	93.1%	25,689,330	106.7%
Interest expense	(2,022,873)	-15.0%	(10,001,243)	-53.5%	(10,067,618)	-41.8%
Loan loss expense	(88,216)	-0.7%	(8,203,110)	-43.9%	(4,561,184)	-18.9%
Non-interest income	1,377,322	10.2%	1,286,392	6.9%	(1,607,624)	-6.7%
NET EARNINGS	**11,358,587**	**84.3%**	**475,354**	**2.5%**	**9,452,904**	**39.3%**
Staff costs	(5,388,860)	-40.0%	(4,635,973)	-24.8%	(4,732,380)	-19.7%
Depreciation expense	(392,770)	-2.9%	(501,038)	-2.7%	(302,103)	-1.3%
Other operating expenses	(3,766,052)	-28.0%	(7,112,975)	-38.1%	(3,424,372)	-14.2%
TOTAL OPERATING EXPENSES	(9,547,682)	-70.9%	(12,249,986)	-65.6%	(8,458,855)	-35.1%
PROFIT (LOSS) BEFORE TAXATION	1,810,905	13.4%	(11,774,632)	-63.0%	994,049	-4.1%
TAX (EXPENSE) BENEFIT	-		-		-	
PROFIT (LOSS) AFTER TAXATION	**1,810,905**	**13.4%**	**(11,774,632)**	**-63.0%**	994,049	-4.1%
GROSS EARNINGS	**13,469,676**	**100%**	**18,679,707**	**100%**	**24,081,706**	**100%**

THE COMPANY FOR HABITAT AND HOUSING IN AFRICA (SHELTER - AFRIQUE)			
KEY RATIOS	**31-Dec-21**	**31-Dec-22**	**31-Dec-23**
PROFITABILITY & EARNINGS			
Net interest spread	83.3%	42.5%	60.8%
Loan loss expense/Interest income	-4.4%	-82.0%	-45.3%
Operating expenses/Net Earnings (excluding loan loss expense)	81.4%	129.6%	60%
Return on average assets (pre-tax)	1.1%	-5.4%	0.4%
Return on average equity (pre-tax)	1.2%	-7.4%	0.6%
Net interest income/average earning assets	5.1%	-0.3%	3.3%
LIQUIDITY & FUNDING			
Loans/Total Assets	67.3%	57.3%	61.7%
Liquid assets/Total borrowings (times)	N/A	0.8	1.1
Liquid Assets/Total Assets	18.9%	32.1%	26.5%
ASSET QUALITY RATIOS			
Performing Loans ($'Million)	63.7	127.8	110.3
Non-Performing Loans ($'Million)	144.5	141.8	112.8
Non-performing loans /Total loans - Gross	59.2%	52.6%	50.6%
Loan loss provision/Total loans - Gross	53.9%	42.5%	38.0%
Loan loss provision/non-performing loans & mortgages	91.1%	80.8%	75.2%
CAPITAL ADEQUACY & LEVERAGE RATIOS			
Risk-weighted assets/Total assets & contingents	9.2%	22.7%	27.4%
Debt/Equity (Gearing Ratio)	0.0	0.7	0.3
Core capital/ Total Assets - Leverage	94.6%	57.8%	73.2%
Interest Cover	1.9	-0.2	1.1
STAFF INFORMATION			
Average number of employees	46	48	55
Staff cost per employee ($)	117,149	96,583	86,043
Net earnings per staff ($)	246,926	9,903	171,871
Staff costs/Operating expenses	56.4%	37.8%	55.9%

RATING DEFINITIONS

Aaa	A financial institution of the best financial condition and strongest capacity to meet obligations as and when they fall due relative to all other issuers in the same country.
Aa	A financial institution of very good financial condition and strong capacity to meet its obligations as and when they fall due relative to all other issuers in the same country.
A	A financial institution of good financial condition and strong capacity to meet its obligations relative to all other issuers in the same country.
Bbb	A financial institution of satisfactory financial condition and adequate capacity to meet its obligations as and when they fall due relative to all other issuers in the same country.
Bb	A financial institution with satisfactory financial condition but limited capacity to meet obligations as and when they fall due relative to all other issuers in the same country.
B	A financial institution with weak financial condition and weak capacity to meet obligations as and when they fall due relative to all other issuers in the same country.
C	A financial institution with very weak financial condition and very weak capacity to meet obligations as and when they fall due are relative to all other issuers in the same country.
D	In default.

Rating Category Modifiers

A "+" (plus) or "-" (minus) sign may be assigned to ratings from 'Aa' to 'C' to reflect comparative position within the rating category. Therefore, a rating with + (plus) attached to it is a notch higher than a rating without the + (plus) sign and two notches higher than a rating with the - (minus) sign.

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