CRITERIA FOR RATING FINANCIAL INSTITUTIONS

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Scope of the Criteria

1. The criteria titled '*Criteria for Rating Financial Institutions*', primarily applies to ratings on entities defined, and regulated as banks, including but not restricted to universal banks, retail banks, commercial banks, investment banks and policy banks and other non-bank financial institutions, which may not be exposed to the same level of regulatory requirements/ oversight and advantages as banks, but where the primary risks are the same (asset quality, capital adequacy, and funding/liquidity). Examples may include financial lease companies and other non-bank lenders. GCR have chosen to separate the criteria on other 'bank like' entities into the appendices to allow ease of reference.

2. The criteria typically will not apply to financial service entities that are primarily exposed to cash flow like risks. These will be covered under the criteria titled '*Criteria for Rating Financial Services Companies*'. Nor does it apply to multilateral development banks, which will be covered under 'Criteria for Rating Supranational Institutions'. Nor does it apply to fund ratings nor asset management companies, which will be covered under separate criteria pieces.

Summary of the Criteria Changes

3. This criteria is based on the fundamentals used in the last updated criteria, Global Credit Rating Co. – Global Master Criteria for Rating Banks and Other Financial Institutions, last updated in March 2017.

4. The major change to the criteria is its alignment to the broader GCR ratings framework (see below). Specific changes for analyzing banks include incorporating resolution factors, where relevant, into the Capital & Leverage factor. Furthermore, GCR has added specific key ratios such as the GCR core capital and financial leverage ratios. The criteria also include a foundation for rating debt instruments (see page 22).

An Overview of the Ratings Framework

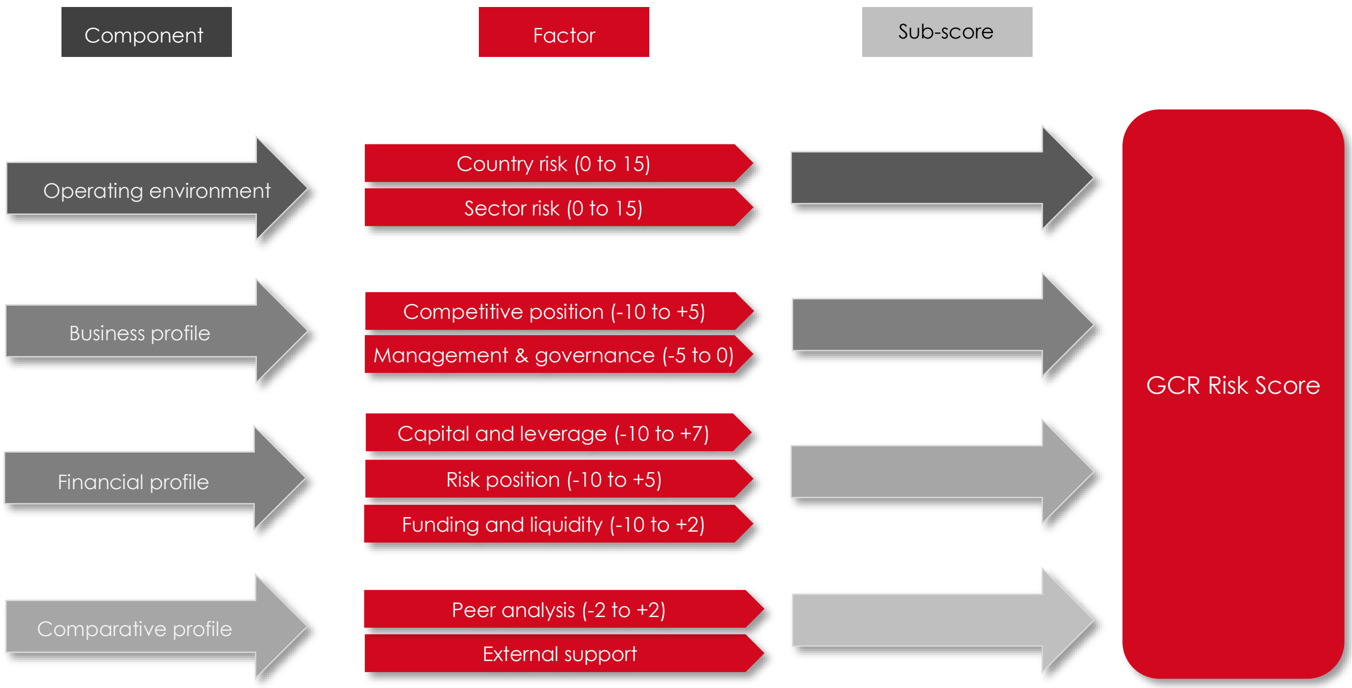
5. In order to improve the comparability and transparency of the ratings, GCR have adopted a framework (see below) with publicly available scoring for the major rating components. The goal is to allow each stakeholder (issuer, investor, regulator, counterparty etc.) to know in detail, each of the major rating drivers and ultimately what factors may change the ratings in the future.

6. To achieve this, GCR has adopted four major rating components (operating environment, business profile, financial profile and comparative profile), which are all broken down into two or three major factors and sub-factors, with a public positive or negative score assigned to each. The summation of the scores determines the GCR Risk Score, which is translated using the GCR Anchor Credit Evaluator into the Anchor Credit Evaluation, and then using final rating adjustment factors into issue(r) credit ratings. It is important to note that there are no fixed weightings for the components, factors or sub-factors.

7. To understand the following criteria, GCR recommends that it is read in conjunction with the '*GCR Ratings Framework*', which will provide a more detailed view on Country Risk, Group Classification & Support, Management & Governance, and the GCR *Rating Scales, Symbols & Definitions and the Anchor Credit Evaluator*, which is published on the GCR Website and will help translate the GCR Risk Score to the international and national scale ratings.

8. The way the key rating concepts interact with each other and result in an issue(r) credit rating is best illustrated in Figure 1, below.

Figure 1: GCR New Ratings Framework Diagram, Financial Institution Criteria



*There are no fixed weightings to the components or factors above.

Component 1: Operating Environment

(0 TO 30: 30 BEST)

9. The core of the GCR rating framework is based on our opinion that an entity's operating environment largely frames its creditworthiness. As a result, the operating environment analysis anchors the underlying risk score for the GCR rating methodology. Financial institutions are especially vulnerable to these factors. In essence, GCR combine elements of the country risk and sectoral risk analysis, blended across countries for entities operating across multiple jurisdictions, to anchor a financial institution to its current operating conditions.

Operating Environment

Factor A: Country Risk (0 to 15)
- GDP Per Capita
- World Bank Governance Indicators
- WEF

Factor B: Sector Risk (0 to 15)
- Asset Risk & Diversification
- Regulation, Governance & Policy Certainty
- Sector Structure
- Systemwide Funding

10. Furthermore, GCR are cognizant of the operating environment factors when scoring the traditional financial institution fundamentals (such as capital, earnings, asset quality, funding and liquidity), i.e. the scores in the business and financial profile (below) are analyzed through the lens of the bank's operating environment. This may be reflected in the financial institution's market position versus peers or capital it needs to hold against the riskiness of the environment.

Component 1, Factor A: Country Risk Score

(0 to 15: 15 best)

11. The Country Risk score is scored on a 0 (worst risk score) to 15 (best risk score) scale. To assess the score, GCR applies the '*Country Risk*' methodology, as highlighted in the '*GCR Ratings Framework*', published here.

12. When the rated Financial Institution/ group operates across multiple jurisdictions, GCR will blend the weighted average of the loan book or exposure at default by geography.

13. Example: A bank's loan book is spread across three countries. The first country has a country risk score of 6 and contributes 75% of total loans, the second has a country risk score of 4 and contributes 20% of loans and the third has a country risk score of 2 and contributes 5% of loans. In this case, the weighted average country risk score would be 5.4 or ((6*0.75) +(4*0.2)) + (2*0.05). The analyst would have the ability to round up or down depending on the expected growth of the exposures or country risk trends going forward.

Component 1, Factor B: Financial Institutions Sector Risk Score

(0 to 15: 15 BEST)

14. Financial institutions (particularly banks) are fundamentally exposed to systemic risk due to the confidence sensitive nature of their liabilities and the high level of interconnectedness within the financial system. Even if a financial institution is performing well, the failure of a peer/ counterparty bank or system-wide credit event could materially affect its creditworthiness.

15. The Financial Institution's 'Sector Risk' score amalgamates four separate subfactors, using a mixture of qualitative and quantitative factors. These risks include asset risk & diversification, regulation, governance and policy certainty, sector structure, appetite and profit and financial system funding risks. Sector risk is scored between 0 (weakest) and 15 (strongest).

16. GCR formulate a view of sector risk by weighting by loan book, across jurisdictions, if necessary, against the entity's major operating environment(s).

17. Asset Risk is the most significant sector risk assessment because such risks are typically, the largest risks facing financial institutions. Furthermore, details regarding asset price bubbles, private sector indebtedness and foreign currency risks, for example, provide a good view of economic imbalances, either existing or building up in an economy.

18. **The Asset Risk & Diversification assessment** focuses on, but is not limited to the following:

I. Economic diversification and wealth levels of the country.

II. *The debt burden of the government and the public sector:* When assessing this factor, GCR looks at the total public-sector debt stock and growth, as well as the financing costs as a percentage of total government revenues.

III. The private sector leverage of households (household debt to disposable income and debt service to disposable income) and the corporate sector (debt to EBITDA): Whilst GCR benchmarks these data points against peers, the assessment is largely qualitative as it needs to be placed in context with debt tolerance of its population.

IV. Asset price bubbles (residential real estate, commercial real estate or equity price bubbles) or if the financial sector has been rapidly extending loans to any sectors or to the private/ public sector as a whole: Regardless of private sector leverage, rapid growth in any asset class (typically, performance well above inflationary growth) is questioned regarding is sustainability and the imbalances it may be creating.

V. Key risk indicators across the sector: these include (but are not restrained to) sector wide lending concentrations by industry and single obligor, the amounts of foreign currency lending, average and new loan to values for secured lending, related party lending and the percentage of loans extended to other vulnerable or cyclical sectors.

VI. Asset quality across the sector including non-performing loans, restructuring and provisioning: Ultimately, GCR estimate the sector wide credit loss expectations on a three-year forecasted basis using economic and industry expectations. These expectations are used in the risk position of the rated entity.

Table 1: Asset Risk & Diversification

Assessment	Typical characteristics*
Highest	The banking sector operates in a diversified economy, with no major industry or commodity concentrations. This diversification can be seen in the banking sector's loan book, with strong diversification between retail and corporate lending. Public and private sector debt capacity appears to be robust given the fiscal strength of the sovereign and the indebtedness versus wealth of the private sector. GCR sees no material asset bubbles. Credit losses are expected to be below 1%, through the cycle. There is a limited amount of foreign currency lending to domestic entities.
High	The banking sector operates in a diversified economy, with no major industry or commodity concentrations. This diversification can be seen in the banking sector's loan book, with strong diversification between retail and corporate lending. Public and private sector debt appears to be sustainable given the strength of the sovereign and debt capacity of the private sector. GCR sees no material asset bubbles. Credit losses are expected to trend between 1%-2%, through the cycle. There is a limited amount of foreign currency lending to domestic entities.
Intermediate	The banking sector operates in an economy where there may be some concentrations, either to industries, obligors or commodities. However, GCR don't expect the risk concentrations to materialize as credit losses. Retail, and especially mortgage, lending is a relatively small part of banking sector loan books. Public and private debt capacity maybe showing signs of stress or there is an obvious asset bubble forming. Credit losses are expected to be between 2%-3%, through the cycle. There may be some foreign currency lending.
Low	The banking sector operates in a concentrated economy, with significant concentrations to industries, obligors or commodities that could materially affect sector wide credit losses. The indebtedness versus the wealth of the private sector or fiscal position of the sovereign is fragile. Foreign currency lending is high, typically above 35% of total loans. Credit losses are expected to be above 3% through the cycle.
Lowest	The banking sector is exposed to a sovereign that is defaulting or has severe fiscal restraints, which have or are expected to spill over into the private sector.

**The above highlights typical characteristics of a highest, high, intermediate, low and lowest assessments. It is likely that an entity has one or more characteristics. GCR allows analytical decision making to decide what the most pertinent factors for each rated entity are. However, to achieve a stronger score, the entity is likely to have a number of cumulative strengths. Conversely, any one risk can bring the score down to the lowest levels.*

19. Although the next three sub-factors in Sector Risk (a, b & c below) involve an element of quantitative analysis, essentially these assessments will be viewed as benchmarking sector strengths against one

another. For example, South Africa's banking regulation versus that of Burundi. The below subfactors are exclusively based on the home market of the rated entity's core operations/ holding company.

a) Regulation, governance & policy certainty, including:
    i. A qualitative benchmarking of banking regulation and supervision against global best practice,
    ii. the adoption of regulatory best practice, such as the Basel principles on capital and funding and the most recent IFRS accounting updates,
    iii. the scope and quality of the regulatory oversight,
    iv. political interference within the financial system,
    v. Central Bank independence,
    vi. government directed lending, and
    vii. monetary policy uncertainty or limited control over inflation or asset price bubbles.

b) Sector structure, including:
    i. Competitive dynamics (number of banks and competitive trends),
    ii. barriers to entry (competition versus the control of market pricing),
    iii. source's & stability of earnings over time,
    iv. significant market distortions (large non-bank competitors, regulatory caps/ lending etc.) or disruptions, and
    v. the frequency, timeliness and quality of financial reporting information on a sector wide basis.

c) Financial System funding, including:
    i. The structure of banking sector funds within the country. GCR view positively the presence of retail and corporate customer deposits, less positively a dependency on external funding (including non-resident deposits), large public-sector funds, financial sector deposits or wholesale funding,
    ii. the sectors reliance on foreign currency funding, specifically how the market manages potential asset liability mismatches/ currency translation risks, and
    iii. the depth and liquidity of the domestic fixed income capital market.

Component 2: Business Profile

(-15 to +5: +5 BEST)

20. The business profile assessment is based on a series of qualitative factors meant to ascertain the robustness of the financial institutions' business model versus peers. This includes examining the diversity and stability of earnings against the complexity of operations and quality of management/ governance relative to peers operating in the same or similar markets.

Business Profile
Competitive Position (-10 to +5)
• Franchise Strength & Market Share
• Business line, product and geographic diversification
• Revenue Stability
Management & Governance (-5 to 0)

Component 2, Factor A: Competitive Position

(-10 to +5: +5 BEST)

21. Competitive position is the first entity specific score. It is based on a scale from 'lowest' (-10) to 'highest' (+5) using the four (4) characteristics below. Each factor is benchmarked to peers in a similar industry, being cognizant of the *Sector Structure* risks. The competitive position is an overall assessment of anticipated business stability through economic cycles against sector and global peers. Only a global systemically important financial institution may attract the highest score to reflect their position in global finance. The very top and very bottom of the ranges will typically only be used for more developed and fragmented markets, unless the financial institution is close to failing, when it would typically attract the lowest scores.

22. The four subfactors below are used to assess a bank's competitive position. GCR cover the additional non-bank financial institutions subfactors in Appendix 1:

a) Assessing the franchise strength and market share in core banking products, which for most banks are loans and deposits, is an important factor signifying the competitive strength of the bank. One of the key benefits will be setting market prices for its key products, aiding growth and long-term earnings stability. GCR also take a view of the customer numbers, loyalty and trends. For entities that focus of non-traditional lines, GCR takes a view on the share within its niche and the mechanisms available to protect its business. Generally, GCR views a strong franchise and market share in a stable and diversified developed market to be more positive than a similar position within an emerging or frontier market.

b) Business line, product and geographic diversification: Judging the sensitivity to stress within a single business line, product or geography. Typically, GCR uses revenue breakdown as the core measure. Although GCR generally views diversification as a strength relative to concentration, expansion into business areas or geographies could bring about additional risk. To achieve a company profile score above 4, regardless of other competitive strengths, the entity should typically have strong geographic diversification, to a point where no one sovereign jurisdiction contributes more than 33% of total revenues.

c) Revenue stability: GCR looks at the historic trend of revenue consistency for the banking group, concentrating on the absolute returns and the stability of sources for revenue. Business lines with recurring fee income and net interest income that have a strong annuity characteristic are considered to be more stable versus volatile activities such as trading or investment banking. GCR will also consider any anticipated competitive or strategic shifts.

d) GCR may also make any adjustments seen for Environmental or Social risks facing the entity. GCR will make adjustments for these factors, on a case by case basis.

Table 2: Competitive position and management		
Assessment	Score	Typical characteristics*
Highest	4,5	Very strong market share/ franchise across core business lines, with the associated pricing power in stable, in developed markets. A significant outlier to the industry, in regards to business and geographic diversity. To achieve the highest scores the FI needs to be a G-SIFI, with no core market accounting for more than 33% of total assets or revenues, superior track-record of earnings stability and absolute returns.
High	2,3	Strong market shares/ franchise versus domestic industry in core banking lines, with some pricing power in developed markets or monopolistic market share in emerging or frontier markets. Better than the industry in regards to business and geographic diversity superior track-record of earnings stability and absolute returns or has a defined government role and protected status.
Intermediate	1, 0, -1	Average market share, within industry norms for diversification, earnings stability and returns.
Low	-2, -3, -4	Smaller or more concentrated (by product or customer) than market peers, in regards to business line and revenues. Or it has weaker revenue stability and diminished franchise than the sector average (by assets).
Lowest	-5 to -10	Significantly smaller entity within a fragmented and competitive market. Entity maybe very concentrated in terms of customer, product or location. The lowest scores will typically be associated with long term weak earnings and /or failed or close to failing.

**the above highlights typical characteristics of a highest, high, intermediate, low and lowest assessments. It is likely that an entity has one or more characteristics. GCR allows analytical decision making to decide what the most pertinent factors for each rated entity are. However, to achieve a stronger score, the entity is likely to have a number of cumulative strengths. Conversely, any one risk can bring the score down to the lowest levels.*

Component 2, Factor B: Management & Governance

(-5 to 0: 0 BEST)

23. Scored between 0 to -5. Please see the universal management & governance criteria.

Component 3: Financial Profile

(-30 to +12: +12 BEST)

24. Within the financial profile, GCR assesses three subfactors, using a mixture of quantitative benchmarks that lead to qualitative assessments: Capital & leverage, Risk and Funding Structure versus Liquidity. Each subfactor is also measured on a scale, from 'lowest' (-10) to 'highest' (+7/+5/+2). As described above, these fundamental rating factors provide a guide regarding how well a bank will weather its current and expected operating environment.

Financial Profile

Capital & Leverage (-10 to +7
- Capitalization (up to +4)
- Earnings (up to +1)
- Resolution (up to +2)

Risk Position (-10 to +5)
- Credit Risk
- Concentration Risk
- Operational Risk
- Market Risk

25. The application of the criteria, from paragraph 26 to 33, will typically be more suitable for a regulated bank or banking group. Non-bank financial institutions will typically be assessed on a leverage indicator, as per the guidance in Appendix 1.

Component 3, Factor A1: Capital & Leverage

(-10 to +5: +5 BEST)

26. A financial institution is expected to maintain capitalisation commensurate with the nature and extent of the risks it is exposed to. There are a number of ways to measure capital adequacy. However, broadly they can be characterized as either risk adjusted approach or an unweighted leverage approach.

27. GCR believe that the risk adjusted approach is a more accurate measure of capitalization, because by its very definition it compares nominal capital to the risk the bank assumes. Furthermore, it has the additional advantage of being closer to the regulatory capital adequacy measure, which ultimately affects a bank's ability to operate as a going concern entity. GCR has adopted the GCR Core Capital Ratio to measure this type of capitalisation.

28. However, GCR has also adopted the financial leverage ratio to use as an adjustment to the core ratio, should it be required. The financial leverage ratio (equity to assets) has the advantage of not depending on the regulatory treatment of both the numerator (the classifications of equity) and denominator (classification and treatment of risk weighted assets (RWAs)), as well as the assumptions of a bank's own internal modelling.

29. Accordingly, GCR begins its review of capital adequacy by calculating our assessment of nominal core capital, which GCR believe has to be completely and unambiguously loss bearing. GCR core capital reflects core equity (share capital, share premium, distributable and loss bearing reserves, loss bearing minority interests and retained profits) plus a percentage of any qualifying debt instruments with strong equity like characteristics (such as high trigger contingent capital instruments and other recognised additional Tier One instruments; see adjustment '*h*', below for more details), minus intangibles, equity / equity like investments in non-consolidated financial companies, and deferred tax assets. Revaluation reserves may also be haircut, if GCR consider them to be overstated.

30. Subsequently, GCR compare the GCR core capital to the regulatory weighted assets determined by the bank's domestic regulator, to create the GCR Core Capital Ratio. At this point, GCR take cognisance (and can adjust for) of the adopted capital approach, i.e. Basel I versus Basel II or even the standardised or internal ratings-based approach under Basel II or Basel III, and may make adjustments accordingly. Finally, GCR weight the GCR Core Capital Ratio against the FIs blended operating environment (scoring of which is detailed above). The theory being that a financial institution needs to hold a greater amount of capital as the riskiness of the operating environment increases and vice versa.

31. For example, for a financial institution to achieve the highest assessment (+4) it needs to have a GCR core capital ratio in excess of 30%, when operating within an operating environment with a score between 10 and 20. Whereas, a bank would require a GCR core capital ratio in excess of 35% to achieve the same assessment, when operating within an operating environment with a score of less than 10. See capital table below for more details.

32. When assessing the capital and leverage score, GCR will score the assessment according to our forward-looking, two-year, assumptions made on a financial institution's internal capital generation, dividend payout and risk asset growth.

Table 3: Capital Adequacy: GCR Capital Ratio v Operating Environment Score

Assessment	Score	>20	10-20	<10
Highest	4	>25%	>30%	>35%
High	2, 3	17.5%-25%	20%-30%	25%-35%
Intermediate	1, 0, -1	10%-17.5%	10%-20%	15%-25%
Low	-2, -3,	7.5%- 10%	7.5%- 10%	10%-15%
Lowest	-4 to -8	<7.5%	<7.5%	<10%

33. GCR also have the option to make adjustments to the initial capital assessment score, as detailed below:

a) (Negative) Regulatory capital forbearance: When a bank's regulatory capital ratio(s) are close to regulatory minimum levels, there is increased risk of some form of regulatory intervention which may significantly reducing its financial flexibility, impair market confidence in the bank and even trigger default of certain capital instruments. As the risk of regulatory intervention increases, then the initial capital assessment score will typically be pressurised downwards. Depending on the operating environment and expected reaction by the regulator, GCR can bring the assessment down to the lowest levels (-9 or -10), albeit in extreme circumstances. For non-bank financial institutions, the covenant levels may be used in a similar way to regulatory minimums when appropriate.

b) (Negative): GCR can adjust the initial capital assessment, applying the GCR financial institutions leverage ratio (GCR core capital to adjusted on and off-balance sheet assets (excluding cash in hand)), if GCR believes RWAs over or understate the capital strength of a financial institution versus peers operating in similar jurisdictions. To do this, GCR takes an average score of the two ratios (using table 3 and table 4), as the new initial starting point for the assessment. *For example, if an entity had a GCR Core Capital Ratio of 21% in an operating environment of 12 (attracting a score of 2) and a financial leverage ratio of 4.5% (a score of -2), the initial starting point for the capital assessment would be close to 0.*

Table 4: GCR financial institutions leverage ratio

Assessment	Score	Financial Institutions Leverage Ratio
Highest	3, 4	>10%
High	2	7.5%-10%
Intermediate	1,0, -1	5%-7.5%
Low	-2, -3	>3%-5%
Lowest	-4 to -8	<3x

c) (**Negative**) If the nominal size of capital is small, at less than USD50mln, the financial institution could be more vulnerable to a single-event/ stress loss even if the ratios are relatively strong. GCR may choose to cap the capital score at the maximum within the intermediate category or lower the score by up to two. However, this is a qualitative judgement call and will balance the size of loans, diversity of business and quality of risk management.

d) (**Negative**) Limited capital fungibility: Published consolidated capital ratios can sometimes be misleading because they imply perfect capital fungibility, while in reality there can be regulatory, accounting or tax impediments to such intra-group capital mobility. For example, if there are strong minority interests in the major operating subsidiaries.

e) (**Negative**) Undercapitalized operating subsidiaries/ associates: If we consider a groups subsidiary to be undercapitalized and dependent on capital from the group, or is close to breaching a covenant, GCR could deduct the shortfall from group capital. This includes insurance subsidiaries. GCR do not double count the investment amounts already stripped from the GCR Core Capital number for the investments in the capital of banking, insurance or other financial institutions outside consolidation.

f) (**Negative**) Unfunded benefit schemes can be deducted from nominal capital if we see no other risk protection in place. Typically, these are contingent / off balance sheet liabilities.

g) (**Negative**) Reserve coverage: General or specific reserves are formulated on the balance sheet to cover expected losses originating from the loan book or other risk / fixed assets. GCR takes a view on the sufficiency of reserves in both nominal and percentage terms. If there is a deficiency in the reserving, whether observable in the audited accounts, expected losses in the future, occurring due to failure to recognise impaired or non-performing loans, or overvalued collateral levels, GCR can subtract the shortfall from nominal capital. This is a negative adjustment to capital only.

h) (**Positive**) Going concern loss bearing capital instruments are rare in GCR's core markets. However, where additional Tier 1 instruments or contingent convertibles that have been designed with trigger points which cause the mandatory and permanent write down or conversion of the instrument to support capitalization well before a point of non-viability (typically for Tier 1 regulatory instruments only), GCR can uplift the capital score. Additionally, from time to time, GCR may include elements of permanent group or government funding which could be converted to capital if there is a stress GCR core capital for a regulated bank (presuming the instrument is recognized by the regulator) and 50% for an unregulated non-bank financial institution.

Component 3, Factor A2: Quality and Quantity of Earnings

(-2 to +1: +1 BEST)

34. A financial institution's earnings track-record is one of the key elements to consider when assessing the viability and future capital stability of any organization. Financial institutions that benefit from high quality, stable earnings, will generally be more robust than those institutions with low or volatile earnings, all else being equal. This adjustment will be rarely used, only for entities that are true outliers to peers.

35. Positive Adjustments typically come from the following (maximum +1):
    - Material outperformer in its industry, in regards to returns on assets.
    - Earnings are predictable throughout economic and interest rate cycles.
    - There are strong levels of revenue diversification from its business units, with a good mix of retail and corporate revenues.
    - Market leading efficiency and therefore low cost to income ratio. Coverage of operating costs by stable 'risk free' earnings is significant.
    - High proportion of core earnings (net interest income or fees and commissions) to revenues in comparison to peers.

36. Negative Adjustments, typically come from the following (maximum -2):
    - Material underperformer in its industry, in regards to return on assets and equity.
    - Aggressive dividend extraction or share-buy backs.
    - Concentrated revenues, either by business line or single counterparty.
    - Inefficiency, as shown by a high cost to income ratio.
    - High proportion of volatile earnings (trading gains or other market sensitive income) to revenues.
    - Revenues that rely on once-off items, such as (un)realised capital gains on securities or fixed assets.
    - There are significant below the line adjustments to other comprehensive income.

Component 3, Factor C: Resolution Regimes

(0 to +2: +2 BEST)

37. In one of the more recent waves of global regulation, countries are slowly introducing a host of laws and regulations to ensure that failing financial institutions can be resolved (meaning recapitalised or wound down in an orderly manner). Ideally, this is anticipated to be accomplished without severe systemic disruption or exposing taxpayers to loss and whilst protecting vital economic functions through mechanisms, which make it possible for shareholders and unsecured and uninsured creditors to absorb losses in a manner that respects the hierarchy of claims in liquidation. Due to this, it can fundamentally change the probability of default and the loss given default of an entity and its instrument(s). *Typically, this adjustment will apply to bank ratings only.*

38. If GCR believe that a bank within a given market could benefit from resolution, **in such a way that it continues operating as a going concern entity,** this could be reflected in the ratings in the following ways:
    a) An uplift in the legal entity ratings and therefore senior unsecured ratings, if GCR considers that there is a big enough going concern loss bearing cushion (i.e. subordinated debt, low trigger hybrids etc.) to be written down or converted to recapitalize the bank and keep it as a 'going concern'.
    b) A lowering in the ratings on subordinated and hybrid debt instruments (below), depending on the characteristics of the instrument because the proximity of default is made closer by regulation.
    c) Changing the amount of support or lowering the ratings on entities in consolidated groups, including non-operating holding companies, because the approach regarding single and multiple points of entry can change the sequence and severity of default on group companies.

39. In practice, GCR will take a jurisdictional approach to resolution, as regulatory approaches and resolution planning change from market to market and even from bank to bank. In the future, the regulatory disclosures may provide a guideline to the anticipated resolution process (including bail-in hierarchy) of a banking group. However, where relevant, GCR may rely on its own assumptions.

40. Firstly, GCR must ascertain whether resolution is effective for each jurisdiction. If not, GCR presumes that 'normal' liquidation or government support would apply. Although possible in reality, banks that benefit from uplift for being in an 'effective resolution' market do not also benefit from government support. This is because GCR expect some element of bail-in for issued debt may occur before state support kicks in. Furthermore, given the low bail-in buffers and immature capital markets in Africa, it is unlikely that many systems will qualify for such support over the medium term.

41. Our approach to notching operating bank issuer ratings/ senior unsecured issue ratings for resolution effective markets is simple, partially as an antidote to the uncertainty around the resolution process. Fundamentally, GCR will include the regulatory recognised/ permissible bail-in-able cushion (including all regulatory Tier 1, Tier 2 and Tier 3 instruments that not have been included in the initial GCR Core Capital ratio but nothing that ranks alongside senior unsecured claims) as a percentage of risk weighted assets (see below) and add notches to the initial score using the table below. We cap the overall capital uplift provided by this assessment to a score of 2 to reflect the relative low quality of the instruments and uncertainty regarding the resolution process.

Table 5: Instrument ratings

Assessment	Risk Score	Loss bearing instruments/ RWAs
Highest	2	>15%
High	1	>10%

45. Our approach for bank subsidiary and holding company issuer ratings, and their corresponding issues, will depend on the resolution planning and legislative environment. For example, if the non-operating holding

company looks like it may take losses before the operating bank, even on a like for like instrument, we will make a relative negative adjustment to the former ratings. Bank subsidiaries will typically not benefit from group support which is derived from positive resolution scoring, i.e. we will limit the uplift to ACE minus the scoring uplift from resolution. This is because we cannot be sure that the subsidiaries will have access to such support in a time of stress.

Component 3, Factor B: Risk position

(-10 to +5: +5 BEST)

46. When assessing the risk position of a financial institution, GCR benchmark the below individual factors against the rated entities operating environment score. For example, in a sector where banks operate with inherently high lending concentrations, a large amount of foreign currency lending and very high credit losses, then the country wide ***sector risk*** would be typically low. If a financial institution is within the industry norm, it would be exposed to high levels of risk, but be within the 'intermediate' range (1, 0 or -1) of the sector.

47. Only significant outliers, both positively and negatively, will ever achieve the 'lowest' or 'highest' scores. For the 'lowest' assessment to be appropriate, the risk position of a financial institution should compare poorly to peers and/ or have the potential to bring about sudden capital erosion through credit or other losses.

48. For a financial institution to achieve the highest scoring levels, it will typically not only compare well to peers and have little anticipated threat to capital adequacy, but it should also be somewhat dislocated from single jurisdiction or product risk, largely through significant diversification of risk assets (including government debt).

49. Credit Risk is the first of all risks in terms of importance for most financial institutions. This largely equates to default risk in the banking book but could also refer to changes in value of a loan/ bond if in the trading book or held at fair value.

    I. Estimated Credit losses: GCR will estimate a future range of expected credit losses for each rated financial institution. This takes a holistic view of the likely loss on risks assets against the likely and stressed economic / industry scenarios facing the financial institution. Viewing historic and current non-performing loans can be a good guide for future credit losses but they can also materially overstate or understate the risk depending on the restructuring approach, surveillance and monitoring of credit risk by the institution, and the ultimately the write off policy. A stronger risk position score will typically only be reflected when there have been lower recent and projected losses for the financial institution than for peers with similar economic scores and similar product mix, and a better-than-average track-record of losses during periods of similar economic stress.

    II. Risk asset concentrations can be a significant source of risk to financial institutions, including the risk of large single obligor default(s), or stress from industry(s), within sectors (households or corporates) or geographic concentrations. A company with low credit losses historically, may have specific concentrations that raise credit costs through the cycle or idiosyncratic risks. Diversity of risks generally leads to lower credit losses through the cycle. GCR explicitly looks at the top twenty loans against capital and total loans to view the underwriting capabilities, concentration risks and single obligor risks.

    III. Risk asset growth: The rapid growth of loans is nearly always a risk, either because it strains the underwriting capabilities of the institution or it signifies potential credit or asset bubbles or a significantly higher risk appetite of the financial institution versus peers. Also, fundamentally rapid growth can hide the seasoning of the loan book and make non-performing loans and credit losses appear artificially low. Furthermore, even when lending growth is modest, there can be parts of the loan book, which are growing very quickly and expose the financial institution to risk. Lastly, moving materially into a new product, customer, or market activities outside of its traditional area of expertise can raise risk for an institution.

IV. Related party lending is often hard to find for financial institutions. However, often regulators could enforce the publication of such activities. Largely, any related party lending is seen as a negative for a financial institution even if the institution says such deals are 'arms-length'. Anything more than 10% of total lending to related parties is likely to be a negative for the factor.

V. Underwriting: Judging standards relative to peers with a similar economic risk score. Examples of weak activities include a prime mortgage lender materially weakening its standards on a loan applicant's capacity to pay, borrower credit standing, or collateral coverage (e.g., as measured by a loan-to-value ratio), a senior secured commercial real estate lender increasingly underwriting mezzanine or corporate development loans, or a commercial bank increasingly underwriting larger or riskier transactions.

50. Trading/ Investment risk: the risk of adverse deviations of the mark to market value of the trading portfolio and other investment securities, including unlisted equities. Entities with significant trading operations, when revenues from such activities account for more than one third of revenues or trading assets more than 50% of assets, will typically attract a lower score than peers. Furthermore, GCR views significant exposure to listed and unlisted equity investments to be a weakness because it can add volatility to earnings and capital from a market and credit perspective. If private equity and / or other Level 3 assets account for 15% of capital or GCR have concerns over the valuation or quality of those investments, GCR could make a negative adjustment for risk (which may be mitigated by other factors).

51. Operational risk: The risk of direct or indirect losses resulting from the inadequate or failed internal processes, people and systems of from external events. Additional complexity of a financial group can raise operational and other key risks. In recent years, much of the added complexity has stemmed from the growing use of derivatives (looking for over-the-counter versus exchange traded, or if gross derivatives are multiples of capital), off-balance-sheet activities (can hide lending exposures or significant non-banking risks), securitisations, legal or reputational risks and exotic products.

52. Foreign exchange risk: The currency risk is that of incurring losses due to changes in exchange rates. The losses can occur in one of three ways:
    I. Credit losses: A sharp change in exchange rates can deteriorate a counterparty's ability to pay as leverage becomes artificially higher or access to foreign currency (FX) becomes harder in a time of stress. Typically, if more than 30% of loans are in FX, GCR would consider this to be a weakness, depending on the sector wide trend.
    II. The changing value of currencies has a direct impact on the value of the balance sheet. Depending on the type and classification of the assets this can be accounted either through trading income in the income statement or other comprehensive income ((if they fair value loans which are backed by fair valued debt or have foreign subs (*which can materialise upon sale of foreign subs*)). Both can quickly deteriorate capitalization and therefore ascertaining the management of the banking books 'open position' is an important factor.
    III. Trading risks, especially if they are trading hard, volatile currencies.

53. Interest rate risk: the impact on earnings due to the movements of interest rates, either directly from interest earning assets or interest-bearing liabilities or indirectly from the impact on loan losses from changes to base rates.

Table 6: Risk position		
Assessment	Score	Typical characteristics *
Highest	4, 5	As well as all of the characteristics of the high score, to achieve this scoring the entity must have diversification away from any one sovereign. Typically, no one jurisdiction would account for more than 33% of total exposures at default.
High	2,3	A significant market/ peer outlier in terms of credit losses through the cycle. Typically has good asset and loan diversification by industry and obligor in comparison to the market(s) it operates in. Top scores will typically have some geographic diversification. Has a history of modest growth, excellent underwriting and limited complexity. Limited market risks and good control over operational and interest rate risks. Lower FX risks than the market(s) it operates in.
Intermediate	1, 0, -1	Broadly within the average range of the industry for credit losses, concentrations, underwriting standards, credit growth and FX lending. Limited market risks and good control over operational and interest rate risks. Minimal related party lending.
Low	-2, -3, -4	Credit losses are weaker than the sector average. The entity has been lending very quickly, has greater lending concentrations by industry and single obligor, the amounts of foreign currency lending maybe higher, loan to values are weaker, related party lending is higher than the market, or the financial institution has a high percentage of loans to other vulnerable or cyclical sectors.
Lowest	-5 to -10	Risk based losses are materially weaker than the sector average and unsustainably high for the current capital/ earnings of the entity. Large loans have gone bad or a significant currency devaluation has taken place for a financial institution exposed to FX risks. The lowest risk entails a potentially high sovereign stress event.

**the above highlights typical characteristics of a highest, high, intermediate, low and lowest assessments. It is likely that an entity has one or more characteristics. GCR allows analytical decision making to decide what the most pertinent factors for each rated entity are. However, to achieve a stronger score, the entity is likely to have a number of cumulative strengths. Conversely, any one risk can bring the score down to the lowest levels.*

Component 3, Factor C: Funding Structure & Liquidity

(-10 to +2: +2 BEST)

54. The application of the criteria, from paragraph 45 to 47, on funding structure, will typically be more suitable for a regulated bank or banking group. Non-bank financial institutions typically do not take deposits and therefore the analysis of funding structure is more reliant on the diversification, length and stability of wholesale funds. Broadly, the liquidity analysis is the same for banks and non-bank financial institutions.

55. This assessment is measured on a scale from 'lowest' (-10) to 'highest' (+2). However, given the confidence sensitive nature of bank funding, exacerbated by asset liability mismatches and inherently high exposure to direct sovereign risk, few entities are expected to achieve the highest score. Similarly, only the weakest of institutions, those that have failed or are close to failure, will be accorded the lowest scores.

56. The funding structure of a bank is measured relative to peers that have similar profiles or operate in the same jurisdictions. For example, in a sector where banks generally rely on wholesale funding, then a wholly retail deposit funded institution will typically score better. If a bank is funded in line with the sector funding breakdown, it will likely be closer to the 'intermediate' range (1, 0 or -1).

57. Conversely, liquidity is absolute and will be viewed only in the context of the banks funding structure. A bank will fail without appropriate liquidity quicker than a bank with a capital shortfall or asset quality issues (all else being equal). However, a bank can reasonably be funded by less stable sources or have shorter term funding than market peers, if it has a correspondingly higher liquid asset mix. Whilst peer analysis is important for differentiating banks within a given system, many banks operating within a system could have idiosyncratically low liquidity.

58. **Funding structure:** There are many sources of funding, each with their own characteristics. Good diversification of funding sources is usually considered to be a strength. However, for GCR, there is a clear hierarchy of stability for bank funding.

59. GCR typically view funding sources in this order of stability:

a) Capital and reserves are definitely the most stable source of funding for the banks. This is especially true of core equity or hybrids with perpetual characteristics.

b) Customer deposits are usually the main funding source for traditional banking models. Within this category, there are also strong elements that affect stability. Sources are important. Generally, GCR views retail deposits (insured and then uninsured) to be the most stable, followed by non-financial corporate deposits, public sector deposits (permanent government funding is higher quality but unusual) and finally, financial corporate deposits (excluding the interbank and money market, which can be viewed as market funding). However, the stability of sources can change for each market and our definition of a 'core deposit' could differ across markets.

60. As such, the core deposit to total funds ratio is often a strong guide for the stability of funding. However, there may be need for qualitative overlays. The breakdown between demand and term deposits need to be carefully analysed, as does the currency of the deposit and residency of the depositor. If available, information on single name depositor concentrations can illuminate the stability of funds as well. The GCR core deposit to total deposit ratio will determine the quality of the deposit base for a bank.

c) Market funding is typically less reliable than deposit funding. However, the spectrum of wholesale funding is wide, depending on the instrument, investor type and other market specific factors. Typically, GCR views long term, local currency, funding from resident counterparties to be the most stable source of wholesale funding. Conversely, short term, foreign currency, or external funding can be relatively unstable. Secured funding can be stable, but it can also create asset encumbrance that subordinates other liabilities and it depends on the type of collateral used. GCR have come up with two secondary ratios to differentiate banks based on the stability of funding, these are the GCR stable funding ratio and GCR long-term funding ratio.

d) Reliance on Central Bank funding is an inherent weakness for the rating, as it questions the sustainability of the business model.

61. Covenant risk: The presence and proximity to covenants is an important factor when assessing the stability of funds. Covenants that trigger funding accelerations, events of default or cross defaults clauses are of particular importance and the notching downwards will likely reflect this.

62. **Liquidity:** The sufficiency of liquidity can only be judged in the context of a banks funding structure. As a result, the analysis focuses on the sufficiency and quality of sources to cover anticipated and stressed uses of liquidity. Due to a bank's primary function, as a transformer of short-term liquidity into long-term funding, a significant asset liability mismatch can be typical. This is why Central Bank's often provide long and short-term support, for systemically important institutions.

63. GCR ascribe to the following factors to analyse the sufficiency of liquidity:

I. Regulatory coverage: GCR takes into account compliance with banks Liquidity Coverage Ratio or other regulatory equivalents.

II. Liquid asset coverage of liabilities: The starting point for this analysis is the loan to deposit ratio, which provides an indication of how leveraged the bank is in comparison to peers. Secondly, GCR assesses the liquid asset coverage of the more confidence sensitive liabilities, including short-term and wholesale liabilities. To this end, GCR takes into account the quality of the liquid assets and how easily they can be realised. GCR disregards in our liquidity analysis all encumbered assets, loan repayments, and any illiquid investments (for example level 3 assets).

III. Foreign currency mismatches: Having a significant currency mismatch on the balance sheet exacerbates the asset-liability mismatch risks of a bank. Typically, GCR would expect banks to either keep appropriate liquid asset coverage of each currency of funding, or have strong committed lines, or derivatives in place to manage the risk. This score does not focus on the open position of the banking book or trading book (which is a factor in risk factor) but rather the ability to survive a major withdrawal or refinancing in a foreign currency.

IV. Fungibility of liquidity within a group is an important consideration. If there are any potential regulatory barriers to the use of liquidity, GCR could adjust downwards.

V. Off balance sheet liabilities and lines, can either mitigate or exacerbate risks depending on the nature of the exposures. Undrawn off-balance sheet credit facilities, if material, will typically be added to loans to receive a true view of the leverage numbers. Conversely, committed bank lines can be added as stable funding sources, but are not typically used to create a positive overall score.

Table 7: Funding & liquidity

Assessment	Score	Typical characteristics*
Highest	2	A significant market outlier, very rarely used. Funding is entirely from stable or long-term sources at better than market related pricing, with no reliance of less stable sources. Liquid assets cover multiples of short & medium-term funding risks. There is no asset liability mismatch, on both local and foreign currency balance sheets. No covenants. Liquid assets typically not concentrated (33% of total) to one sovereign jurisdiction.
High	1	Funding is very stable, with sources better than the market average. Liquidity is robust, with liquid assets covering all confidence sensitive and short-term funding risks. There is a minimal ALMM and FX risk. No covenants that exacerbate liquidity risk.
Intermediate	0, -1	The funding structure appears to be broadly within the average range of the industry. Liquidity is appropriate for the funding structure, with strong coverage of sensitive funding. No material covenants.
Low	-2, -3, -4	The structure of funds is weaker than the market average and / or confidence from the market appears to be low. There appears to be a shortfall in balance sheet or committed liquidity, although it is not expected to be a short or medium-term risk. Covenants that accelerate funds or an event of default are present but they are remote.
Lowest	-5 to -10	If the bank does not comply with any regulatory liquidity ratios. It is experiencing funding outflows or there are significant liquidity shortfalls for the bank, including large and mounting refinancing risks. Breach of covenant or other triggers is likely. Sovereign / regulator may have established currency controls or limited access to funds on an idiosyncratic or sector wide basis.

**the above highlights typical characteristics of a highest, high, intermediate, low and lowest assessments. It is likely that an entity has one or more characteristics. GCR allows analytical decision making to decide what the most pertinent factors for each rated entity are. However, to achieve a stronger score, the entity is likely to have a number of cumulative strengths. Conversely, any one risk can bring the score down to the lowest levels.*

Component 4: Comparative Profile

(Various)

Comparative Profile
External Support (various)
Group Support
Sovereign Support
Peer Comparison (+2 or -2)

64. The last factor allows GCR to include ongoing group or extraordinary sovereign support and to capture event risks.

Component 4, Factors A & B: External Support for a Financial Institution

65. Due to their critical economic function, banks often receive extraordinary support that allows them to continue as going concern entities. Support comes from shareholders/ affiliates and/ or governments. However, if both elements of support apply GCR only apply the higher of the two support options.

Component 4, Factor A: Group Support

66. For details on group support please see the GCR Ratings Framework Criteria.

Component 4, Factor B: Government Support

67. For details on government support, please see the GCR Ratings Framework Criteria.

Component 4, Factor C: Peer Analysis

68. GCR allows for a maximum of two positive or negative risk score changes for peer analysis to create greater credit differentiation within a market. Typically, this factor may be used when a financial institution is a generally better or worse performing company than its peer group across a number of sub-factors, but no one component or factor has created ratings differential.

Final Rating Adjustment Factors

69. Once the risk score and the ACE have been established, on either/ both the national or international scale, GCR can then determine the formal ratings on legal entities. In this stage, GCR move off the risk scoring framework and start adjusting the national/ international ratings on a scale basis because GCR are trying to establish the most applicable credit ratings hierarchy within a financial group and best hierarchy within a market.

Rating Adjustment Factor 1: Financial Institutions Specific Structural Factors

70. GCR will typically base the credit scoring on the financial and business characteristics of the closest consolidated group (when there is one) around that legal entity. This is because GCR believe there is tangible likelihood of risk transfer either up from subsidiaries, across from sister companies or down from a holding company/ parent. It is in this section that GCR address these risks, to hone in on the correct rating for that legal entity.

71. The Group Classification and Support Criteria is the predominant guide for this decision-making process. The following ***are the principles of the adjustments:***

72. Typically, there will be no adjustment from the ACE for the **major operating entity**, of the analyzed analytical entity. An example of this is the major operating bank within a financial group, which usually constitutes 51% of total group assets or capital. However, it could be smaller and still be operationally critical to the group.

73. **Branches** typically attract ratings linked to the ultimate parent's ACE, especially if they are within the same country. However, for foreign branches operating in a higher risk country, there may be transfer and convertibility restrictions imposed by the government/ regulators in a stress situation. To reflect this risk, the ratings on branches will typically be capped at the top end of the hurdle, established in the Country Risk methodology (see Criteria for GCR Ratings Framework).

74. **Minor group Subsidiary / Affiliates** are analyzed on a standalone basis and then allocated support uplift, if necessary, in line with the Group Support & Classification Criteria.

75. **Non-operating holding companies (NOHC),** in non-resolution effective markets are viewed as structurally subordinated from the major operating entities within a regulated financial institutions group. This is because they are reliant on dividends or the upstreaming of cash (via loans or other payments) to pay debt, which can be interrupted by regulatory or legal actions. In a non-resolution effective market (which will be most markets), the ratings on banks will typically be notched down at least once to reflect this risk. The notching may increase if the NOHC has a significant amount of double leverage (defined as equity investments in subsidiaries, plus holding company intangibles, to holding company core equity of over 100%) and/ or weak liquidity. For unregulated financial institutions, GCR don't automatically notch down but will check to view any structural or legal impediments to cash flow.

76. The treatment for **NOHCs** operating in effective resolution markets will depend on the information gathered in the resolution section and the view GCR take on the resolution credit hierarchy.

77. **Operating holding companies ('OHC')** typically will be treated like NOHC. However, if the leverage is immaterial, potential regulatory intervention is expected to be minimal, and the operations of the OHC are integral to the group then GCR can match the ratings to the group credit profile.

78. **Intermediate non-operating holding companies ('INOHC')** typically will be treated like a NOHC. However, if the group benefits from parent or government support and that support has to flow through the INOHC, then the ratings would typically match the group ACE.

Rating Adjustment Factor 2: Instrument Rating(s)

79. The notching from the legal entity rating will depend on the nature of the instrument, whilst always respecting the credit hierarchy.

Table 8: Instrument ratings

Debt Rating Types	Notching	Typical Characteristics
Preferred liabilities	+1	Liabilities preferred by regulatory intervention or statutory protections, typically for banks of systemic importance. Examples of these include but are not restricted to insured deposits, collateralized notes, short-term obligations, derivatives, employee benefits or exchange traded transactions. However, these will change for every jurisdiction. Typically, we will notch up once (1x) for such exposures as they rank higher in the credit hierarchy than senior unsecured entities.
Senior unsecured	0	Reflects the relevant legal entity rating on the financial institution issuing the debt. GCR would typically exclude any potential government support uplift (if applicable) if the bank is in a resolution market.
Senior subordinated	-1	Contractually subordinated debt, potentially a regulatory tier two capital instrument, but it typically will not have any discretionary/ mandatory/ statutory nonpayment, conversion or write down clauses.
Junior subordinated	-2	Contractually subordinated debt, usually a regulatory tier two capital instrument, likely to have a discretionary/ mandatory/ statutory nonpayment, conversion or write down clauses that mean the instrument will take losses as the financial institution remains a going concern.
Hybrids (a)	-4	Contractually subordinated debt, additional tier one capital instrument, typically perpetual even if potentially callable by management after 5 years, non-cumulative, likely to have a discretionary/ mandatory/ statutory non-payment, conversion or write down clauses with trigger points that mean the instrument will take losses as the financial institution remains a going concern. GCR may choose to exclude the impact of sovereign or group support notches to the starting point, if support is not expected to be forthcoming before losses on the instrument.
Hybrids (b)	-5 or more	All of Hybrids (a) plus the presence of capital / liquidity or rating triggers that would mean the instrument could take losses on a going concern basis. GCR would typically notch down according to the proximity of the trigger, whilst respecting the credit hierarchy. Typically, GCR would remove any sovereign or group support from the ratings on such notes.

Appendix 1: Criteria differences for other non-bank financial Institutions

84. **Scope:** GCR classify NBFIs to be under scope of this criteria and appendix, where balance sheet use and risks are the predominant consideration. They are often not deposit taking, but they do supply medium to long-term loans, they are typically not as prudentially regulated as banks. Liquidity typically relies on balance sheet assets, repayments and some elements of cash flow (but not to the same degree as financial service companies).

85. Country Risk Score: No Change

86. **Sector Risk Score**: GCR will typically make up to three (3) negative adjustments for non-bank financial institutions (NBFIs) in the sector risk score. This is because NBFIs may operate with specific structural disadvantages or could be exposed to greater risks or competitive pressures than banks operating in the same market. As a result, we can make negative adjustments if any of the following exist:

- There is less prudential regulatory oversight for the NBFI than a commercial bank operating in the same country and/ or the NBFI has no access to the Central Bank funding mechanisms,
- The NBFI is exposed to higher market conduct scrutiny or potentially sensitive to regulatory or legislative changes,
- Access to market funding is typically weaker,
- Replacement risk is very high or barriers to entry are lower than commercial banking.

87. Conversely, there may be a counteracting positive adjustment if the industry of the entity is prudentially regulated or has a protected or critical market infrastructure role or if the bank sector starting point is already very low.

88. **Company profile:** Alongside the factors listed above, GCR look at the customer diversification, usually by revenues or loans, to see if there is any additional counterparty / concentration risk. GCR also look at the stability, control and diversification of the entity's distribution channels. Negative elements would include (but not exclusively) a reliance on agents or other 3rd parties without very strong controls and long-term stable arrangements, a small or concentrated network or a high degree of price sensitive. Furthermore, if there is an element of additional regulatory or legislative risk for the entity, the business profile score may be lowered.

89. **Capital & Leverage:** Typically, for NBFI, GCR will replace the GCR Core capital ratio with a straightforward assessment of financial leverage (GCR Core capital to on and off-balance sheet assets excluding cash in hand). This is because NBFI entities are not usually regulated and some may not have the capacity to drive a risk-based capital adequacy measure, whilst for others it may not be appropriate to do so. Therefore, the section of regulatory forbearance may also not applicable, although covenants may work in a similar manner.

90. In some cases, the debt leverage (below; net debt to GCR capital) ratio can be used to ascertain the leverage position of a NBFI, especially if the company is financially weak or the funders have constricted the entity will leverage or debt service covenants. The decision-making process regarding whether GCR look at debt or financial leverage is done on a case by case basis, and may be subject to change as a company changes its balance sheet.

Table 9: Leverage			
Assessment	Score	Financial institutions Leverage Ratio	Net Debt/ GCR total Capital (equity)
Highest	3, 4	>20%	<1x
High	2	15%-20%	1x-2.5x
Intermediate	1, 0, -1	5%-15%	2.5x to 5x
Low	-2, -3	3% – 5%	5x-7.5x
Lowest	-4, -5	<3%	<5x

91. **Risk:** No change. However, the range of risks can be very diverse and non-obvious peers may exist. Therefore, GCR consider whether the risk undertaken is a strength or weakness to the creditworthiness of the entity. This will be detailed in full in the analysis.

92. **Funding Structure & Liquidity:** NBFIs often have a higher reliance on market funding, typically cannot take deposits nor do they have central bank access. As a result, the funding profile of NBFIs typically compare poorly to that of commercial banks and therefore the analysis will focus on the diversification (particularly of counterparty and type of debt) and length of market funding, unless there is significant external support.

93. Liquidity analysis for NBFIs are similar to bank analysis, if the entity holds liquid assets on balance sheet. If the loan book is a of short to medium term, with reliable cash flows, a degree of cash flow from operations and principal repayments maybe included in the liquidity analysis.

94. **External Support:** Parental or group support works in the same manner as the core criteria. However, government / donor support is only likely if the NBFI conducts an important policy or critical infrastructure role

GLOSSARY OF TERMS/ACRONYMS USED IN THIS DOCUMENT AS PER GCR'S GLOSSARY

Accounting	A process of recording, summarising, and allocating all items of income and expense of the company and analysing, verifying and reporting the results.
Agent	An agreement where one party (agent) concludes a juristic act on behalf of the other (principal). The agent undertakes to perform a task or mandate on behalf of the principal.
Annuity	A contract that provides a series of payments for a specified period of time which may or may not be contingent on the survival of the annuitant.
Asset Quality	Refers primarily to the credit quality of a bank's earning assets, the bulk of which comprises its loan portfolio, but will also include its investment portfolio as well as off balance sheet items. Quality in this context means the degree to which the loans that the bank has extended are performing (ie, being paid back in accordance with their terms) and the likelihood that they will continue to perform.
Asset	A resource with economic value that a company owns or controls with the expectation that it will provide future benefit.
Assets	A resource with economic value that a company owns or controls with the expectation that it will provide future benefit.
Balance Sheet	Also known as Statement of Financial Position. A statement of a company's assets and liabilities provided for the benefit of shareholders and regulators. It gives a snapshot at a specific point in time of the assets the company holds and how they have been financed.
Banking Book	Assets on a bank's balance sheet that are expected to be held to maturity. Banks are not required to mark these to market. Unless there is reason to believe that the counterparty will default on its obligation, they are held at historical cost.
Basel I	Basel Committee regulations, which set out the minimum capital requirements of financial institutions with the goal of minimising credit risk.
Basel	Basel Committee on Banking Supervision housed at the Bank for International Settlements.
Benefits	Financial reimbursement and other services provided to insureds by insurers under the terms of an insurance contract.
Bond	A long term debt instrument issued by either a company, institution or the government to raise funds.
Borrower	The party indebted or the person making repayments for its borrowings.
Callable	A provision that allows an Issuer the right, not the obligation, to repurchase a security before its maturity at an agreed price. The seller has the obligation to sell the security if the call option holder exercises the option.
Capacity	The largest amount of insurance available from a company. In a broader sense, it can refer to the largest amount of insurance available in the marketplace.
Capital Adequacy	A measure of the adequacy of an entity's capital resources in relation to its risks.
Capital Gain	Profit realised on the sale of securities. An unrealised capital gain is an increase in the value of securities that have not been sold.
Capital Gains	An increase in the price of a capital asset or investment such as property, land or securities.
Capital Markets	The part of a financial system concerned with raising capital by dealing in shares, bonds, and other long-term debt securities.
Capital	The sum of money that is invested to generate proceeds.
Capitalisation	The provision of capital for a company, or the conversion of income or assets into capital.
Cash Flow	The inflow and outflow of cash and cash equivalents. Such flows arise from operating, investing and financing activities.
Cash	Funds that can be readily spent or used to meet current obligations.
Claim	1. A request for payment of a loss, which may come under the terms of an insurance contract (insurance). 2. A formal request or demand (corporate finance).
Collateral	Asset provided to a creditor as security for a loan or performance.
Commission	A certain percentage of premiums produced that is received or paid out as compensation by an insurer.
Commodity	Raw materials used in manufacturing industries or in the production of foodstuffs. These include metals, oil, grains and cereals, soft commodities such as sugar, cocoa, coffee and tea, as well as vegetable oils.
Concentrations	A high degree of positive correlation between factors or excessive exposure to a single factor that share similar demographics or financial instrument or specific sector or specific industry or specific markets.
Conditions	Provisions inserted in an insurance contract that qualify or place limitations on the insurer's promise to perform.
Contract	An agreement by which an insurer agrees, for a consideration, to provide benefits, reimburse losses or provide services for an insured. A 'policy' is the written statement of the terms of the contract.

Country Risk	The range of risks emerging from the political, legal, economic and social conditions of a country that have adverse consequences affecting investors and creditors with exposure to the country, and may also include negative effects on financial institutions and borrowers in the country.
Covenant	A provision that is indicative of performance. Covenants are either positive or negative. Positive covenants are activities that the borrower commits to, typically in its normal course of business. Negative covenants are certain limits and restrictions on the borrowers' activities.
Coverage	The scope of the protection provided under a contract of insurance.
Credit Rating	An opinion regarding the creditworthiness of an entity, a security or financial instrument, or an issuer of securities or financial instruments, using an established and defined ranking system of rating categories.
Credit Risk	The possibility that a bond issuer or any other borrowers (including debtors/creditors) will default and fail to pay the principal and interest when due.
Credit	A contractual agreement in which a borrower receives something of value now, and agrees to repay the lender at some date in the future, generally with interest. The term also refers to the borrowing capacity of an individual or company
Creditor	A credit provider that is owed debt obligations by a debtor.
Creditworthiness	An assessment of a debtor's ability to meet debt obligations.
Currency Risk	The potential for losses arising from adverse movements in exchange rates.
Customer Deposit	Cash received in exchange for a service, including safekeeping, savings, investment, etc. Customer deposits are a liability in a bank's books.
Debt	An obligation to repay a sum of money. More specifically, it is funds passed from a creditor to a debtor in exchange for interest and a commitment to repay the principal in full on a specified date or over a specified period.
Default Risk	The probability or likelihood that a borrower or issuer will not meet its debt obligations. Credit Risk can further be separated between current credit risk (immediate) and potential credit risk (deferred).
Default	A default occurs when: 1.) The Borrower is unable to repay its debt obligations in full; 2.) A credit-loss event such as charge-off, specific provision or distressed restructuring involving the forgiveness or postponement of obligations; 3.) The borrower is past due more than X days on any debt obligations as defined in the transaction documents; 4.) The obligor has filed for bankruptcy or similar protection from creditors.
Derivative	A financial instrument that offers a return based on the return of another underlying asset.
Distribution Channel	The method utilised by the insurance company to sell its products to policyholders.
Diversification	Spreading risk by constructing a portfolio that contains different exposures whose returns are relatively uncorrelated. The term also refers to companies which move into markets or products that bear little relation to ones they already operate in.
Dividend	The portion of a company's after-tax earnings that is distributed to shareholders.
Environment	The surroundings or conditions in which an entity operates (Economic, Financial, Natural).
Equity Investment	An instrument that signifies an ownership position of shares of stock in a company that is either listed or traded on a stock exchange (also known as a counter) or are unlisted.
Equity	Equity is the holding or stake that shareholders have in a company. Equity capital is raised by the issue of new shares or by retaining profit.
Exchange Rate	The value of one country's currency expressed in terms of another.
Expected Loss	Losses that a bank expects to bear over a certain period (generally a year). These losses are a consequence of doing business, namely the bank's role as financial intermediary.
Exposure	Exposure is the amount of risk the holder of an asset or security is faced with as a consequence of holding the security or asset. For a company, its exposure may relate to a particular product class or customer grouping. Exposure may also arise from an overreliance on one source of funding. In insurance, it refers to an indvdual or company's vulnerability to varous risks
Fair Value	The fair value of a security, an asset or a company is the rational view of its worth. It may be different from cost or market value.
Financial Flexibility	The company's ability to access additional sources of capital funding.
Financial Institution	An entity that focuses on dealing with financial transactions, such as investments, loans and deposits.
Financial Lease	A lease, where the risk and reward is transferred from the lessee to the lessor.
Financial Leverage	The degree to which a company uses debt and equity in its capital structure.

Fix	The setting of a currency or commodity price for trade at a future date.
Fixed Assets	Assets of a company that will be used or held for longer than a year. They include tangible assets, such as land and equipment, stake in subsidiaries and other investments, as well as intangible assets such as goodwill, information technology or a company's logo and brand.
Forbearance	A temporary suspension of repayments, granted by a creditor to a debtor.
Forecast	A calculation or estimate of future financial events.
Going Concern	An accounting convention that assumes a company will continue to exist and trade normally for the foreseeable future. In practice this is likely to mean at least for the next 12 months.
Haircut	The percentage by which the market value of an asset is reduced. The size of the haircut reflects the expected ease of selling the asset and the likely reduction necessary to realised value relative to the fair value.
Hybrid	A form of security that has characteristics of various types of transaction or product.
Illiquid	Markets or financial instruments are described as being illiquid if there are few buyers and sellers. Assets may also be considered illiquid. It may be difficult, or even impossible, to find a reliable price for an illiquid security.
Income Statement	A summary of all the expenditure and income of a company over a set period.
Income	Money received, especially on a regular basis, for work or through investments.
Insurance	Provides protection against a possible eventuality.
Interest Rate Risk	The potential for losses or reduced income arising from adverse movements in interest rates.
Interest Rate	The charge or the return on an asset or debt expressed as a percentage of the price or size of the asset or debt. It is usually expressed on an annual basis.
Interest	Scheduled payments made to a creditor in return for the use of borrowed money. The size of the payments will be determined by the interest rate, the amount borrowed or principal and the duration of the loan.
International Scale Rating.	An opinion of creditworthiness relative to a global pool of issuers and issues.
Investment Risk	The risk of a decline in the net realisable value of investment assets arising from adverse movements in market prices or factors specific to the investment itself (eg, reputation and the quality of management).
Issue Ratings	See GCR Rating Scales, Symbols and Definitions.
Issuer Ratings	See GCR Rating Scales, Symbols and Definitions.
Issuer	The party indebted or the person making repayments for its borrowings.
Junior	A security that has a lower repayment priority than senior securities.
LC	An LC is a guarantee by a bank on behalf of a corporate customer that payment will be made if that entity cannot to meet its obligations.
Lease	Conveyance of land, buildings, equipment or other assets from one person (lessor) to another (lessee) for a specific period of time for monetary or other consideration, usually in the form of rent.
Lender	A credit provider that is owed debt obligations by a debtor.
Leverage	With regard to corporate analysis, leverage (or gearing) refers to the extent to which a company is funded by debt.
Liabilities	All financial claims, debts or potential losses incurred by an individual or an organisation.
Liability	All financial claims, debts or potential losses incurred by an individual or an organisation.
Liquid Assets	Assets, generally of a short term, that can be converted into cash.
Liquidation	Liquidation is the process by which a company is wound up and its assets distributed. It can be either compulsory or voluntary. It can also refer to the selling of securities or the closing out of a long or short market position.
Liquidity Risk	The risk that a company may not be able to meet its financial obligations or other operational cash requirements due to an inability to timeously realise cash from its assets. Regarding securities, the risk that a financial instrument cannot be traded at its market price due to the size, structure or efficiency of the market.
Liquidity	The speed at which assets can be converted to cash. It can also refer to the ability of a company to service its debt obligations due to the presence of liquid assets such as cash and its equivalents. Market liquidity refers to the ease with which a security can be bought or sold quickly and in large volumes without substantially affecting the market price.
Loan To Value	Principal balance of a loan divided by the value of the property that it funds. LTVs can be computed as the loan balance to most recent property market value, or relative to the original property market value.
Loan	A sum of money borrowed by a debtor that is expected to be paid back with interest to the creditor. A debt instrument where immovable property is the collateral for the loan. A mortgage gives the lender a right to take possession of the property if the

	borrower fails to repay the loan. Registration is a prerequisite for the existence of any mortgage loan. A mortgage can be registered over either a corporeal or incorporeal property, even if it does not belong to the mortgagee. Also called a Mortgage bond.
Long-Term Rating	A long term rating reflects an issuer's ability to meet its financial obligations over the following three to five year period, including interest payments and debt redemptions. This encompasses an evaluation of the organisation's current financial position, as well as how the position may change in the future with regard to meeting longer term financial obligations.
Long-Term	Not current; ordinarily more than one year.
Loss Given Default	This is an estimate of the amount of the exposure at default that will not be recovered. It also includes other costs such as legal costs.
Loss	1. A tangible or intangible, financial or non-financial loss of economic value. 2. The happening of the event for which insurance pays (insurance).
Market Risk	Volatility in the value of a security/asset due to movements in share prices, interest rates, currencies, commodities or wider economic factors.
Market	An assessment of the property value, with the value being compared to similar properties in the area.
Monetary Policy	Measures taken by the central bank to influence the quantity of money or the rate of interest with a view to achieving stable prices, full employment and economic growth.
National Scale Rating	National scale ratings measure creditworthiness relative to issuers and issues within one country.
Notching	A movement in ratings.
Obligation	The title given to the legal relationship that exists between parties to an agreement when they acquire personal rights against each other for entitlement to perform.
Obligor	The party indebted or the person making repayments for its borrowings.
Off Balance Sheet	Off balance sheet items are assets or liabilities that are not shown on a company's balance sheet. They are usually referred to in the notes to a company's accounts.
Operational Risk	The risk of loss resulting from inadequate or failed internal processes, people or systems or from external events. This includes legal risk, but excludes strategic risk and reputational risk.
Option	An option gives the buyer or holder the right, but not the obligation, to buy or sell an underlying financial asset at a pre-determined price.
Over The Counter	An OTC market or trade is one conducted directly between dealers and principals rather than via an exchange.
Performing Loan	A loan is said to be performing if the borrower is paying the interest on it on a timely basis.
Performing	An obligation that performs according to its contractual obligations.
Policy	The legal document issued by the company to the policyholder, which outlines the conditions and terms of the insurance.
Portfolio	A collection of investments held by an individual investor or financial institution. They may include stocks, bonds, futures contracts, options, real estate investments or any item that the holder believes will retain its value.
Premium	The price of insurance protection for a specified risk for a specified period of time.
Pricing	A process of determining the price of a debt security.
Principal Repayments	Scheduled payments and prepayments.
Principal	The total amount borrowed or lent, e.g. the face value of a bond, excluding interest.
Private	An issuance of securities without market participation, however, with a select few investors. Placed on a private basis and not in the open market.
Probability	The likelihood or relative frequency of an event expressed in a number between zero and one. The throw of a die is an example. The probability of throwing five is found by dividing the number of faces that have a five (1) by the total number of faces (6). That is a probability of one-sixth or one divided by six, which is .17. See also Degree of Risk, Law of Large Numbers, and Odds.
Provision	The amount set aside or deducted from operating income to cover expected or identified loan losses.
Real Estate	Property that consists of land and / or buildings.
Refinancing	The issue of new debt to replace maturing debt. New debt may be provided by existing or new lenders, with a new set of terms in place.
Regulatory Capital	The total of primary, secondary and tertiary capital.

Repayment	Payment made to honour obligations in regards to a credit agreement in the following credited order: 3.) Satisfy the due or unpaid interest charges; 4.) Satisfy the due or unpaid fees or charges; and 5.) To reduce the amount of the principal debt.
Reputational Risk	The risk of impairment of an entity's image in the community or the long-term trust placed in it by its shareholders as a result of a variety of factors, such as performance, strategy execution, the ability to create shareholder value, or an activity, action or stance taken by the entity.
Reserve	(1) An amount representing actual or potential liabilities kept by an insurer to cover debts to policyholders. (2) An amount allocated for a special purpose. Note that a reserve is usually a liability and not an extra fund. On occasion a reserve may be an asset, such as a reserve for taxes not yet due.
Reserves	A portion of funds allocated for an eventuality.
Revaluation	Formal upward or downward adjustment to assets such as property or plant and equipment.
Risk Management	Process of identifying and monitoring business risks in a manner that offers a risk/return relationship that is acceptable to an entity's operating philosophy.
Risk	The chance of future uncertainty (i.e. deviation from expected earnings or an expected outcome) that will have an impact on objectives.
Seasoning	The age of an asset, the time period passed since origination.
Securities	Various instruments used in the capital market to raise funds.
Securitisation	A process of repackaging portfolios of cash-flow producing financial instruments into securities for sale to third parties.
Senior	A security that has a higher repayment priority than junior securities.
Shareholder	An individual, entity or financial institution that holds shares or stock in an organisation or company.
Short Term	Current; ordinarily less than one year.
Sovereign Risk	The risk of default by the government of a country on its obligations.
Spread	The interest rate that is paid in addition to the reference rate for debt securities.
Statutory	Required by or having to do with law or statute.
Subordinated Debt	Debt that in the event of a default is repaid only after senior obligations have been repaid. It is higher risk than senior debt.
Surveillance	Process of monitoring a transaction according to triggers, covenants and key performance indicators.
Systemic Risk	Risk of failures within the financial system that relate to settlement, payment or a default of a financial institution.
Term Deposit	A savings account held for a fixed term. Also called a time deposit. Generally, there are penalties for early withdrawal.
Total Capital	The sum of owner's equity and admissible supplementary capital.
Trading Book	This comprises positions in financial instruments and commodities, including derivative products and other off-balance-sheet instruments that are held with trading intent or to hedge other elements of the trading book. It includes financial instruments and commodities that: are held for short-term resale; or are held with the intention of benefiting from price variations; or arise from broking and market making; or are held to hedge other elements of the trading book.
Transaction	A transaction that enables an Issuer to issue debt securities in the capital markets. A debt issuance programme that allows an Issuer the continued and flexible issuance of several types of securities in accordance with the programme terms and conditions.
Underwriting	The process of selecting risks and classifying them according to their degrees of insurability so that the appropriate rates may be assigned. The process also includes rejection of those risks that do not qualify.
Unsecured Claim	Debt securities that have no collateral.
Upstream	A term referring to the exploration and extraction of a commodity, in contrast with the downstream manufacturing and processing.
Valuation	An assessment of the property value, with the value being compared to similar properties in the area.
Weighted Average	An average resulting from the multiplication of each component by a factor reflecting its importance or, relative size to a pool of assets or liabilities.
Weighted	The weight that a single obligation has in relation to the aggregated pool of obligations. For example, a single mortgage principal balance divided by the aggregated mortgage pool principal balance.