The Pakistan Credit Rating Agency Limited

Financial Institutions Rating

Methodology

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Summary

PACRA's methodology documents lay out the umbrella framework guiding its credit ratings. This document provides an overview of PACRA's approach to assigning credit ratings to commercial banks and Development Finance Institutions (DFIs) in Pakistan.

PACRA's opinions is based on a mix of qualitative and quantitative assessment factors, including: Profile, Ownership, Governance, Management, Business Risk and Financial Risk. While standalone credit quality is addressed, PACRA incorporates the relative positioning of a financial institution to arrive at the final rating.

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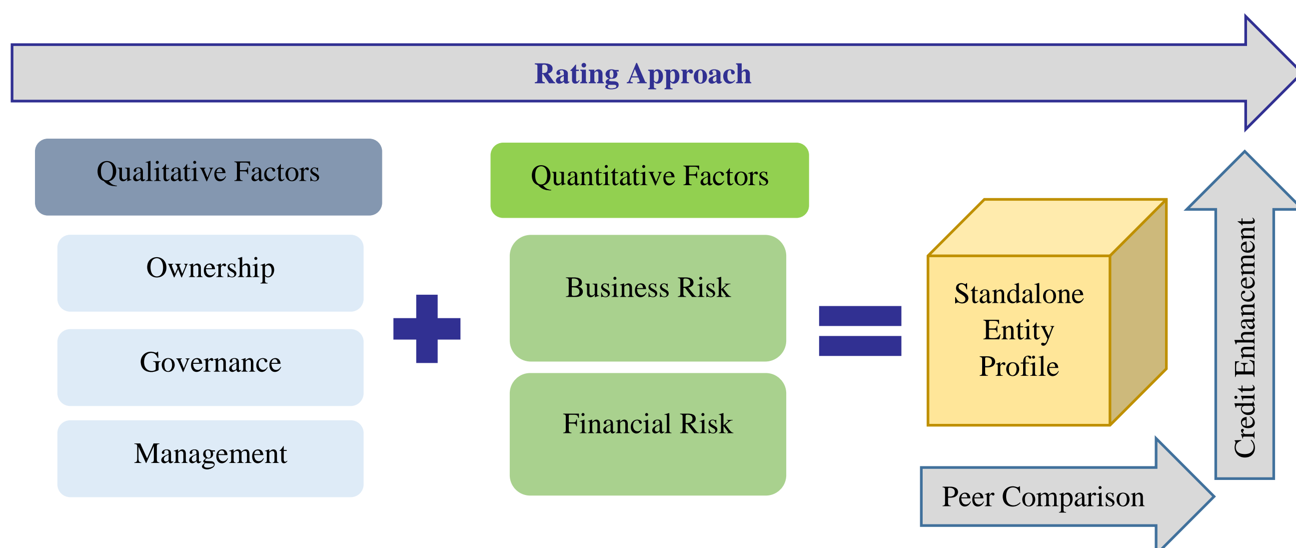
1. Introduction

1.1 Scope: This methodology applies to financial institutions (FIs) regulated by State Bank of Pakistan (SBP), the central bank. The scope of this methodology covers all commercial banks and Development Financial Institutions (DFIs). These institutions are mainly licensed to mobilize deposits and provide credit among other financial services. The regulatory framework consists of the laws and regulations designed by SBP to ensure a sound financial system.

1.2 Rating Framework: PACRA's framework for assessing credit quality of financial institutions employs a mix of qualitative and quantitative analyses. The quantitative factors help in achieving objectivity in the rating assessment while the qualitative factors help establish the sustainability of the rating in the foreseeable future. Neither can all factors be quantified, nor do quantitative metrics portray the complete picture. PACRA seeks to employ an optimal combination of both and applies it consistently to ensure comparability between ratings over time. The assessment is categorized within six key areas: Profile, Ownership, Governance, Management, Business Risk and Financial Risk.

1.2.1 PACRA also achieves a clear perspective on the relative position of a financial institution in its peer group. In addition, a sensitivity analysis is performed through several "what if" scenarios to assess its capacity to cope with changes in the operating environment. PACRA's analysis typically involves at least three years of operating history and financial data as well as entity and rating agency forecasts of future performance. The assessment culminates in the assignment of a long-term and short-term credit rating to an entity. More information on the distinction between the long-term and short-term ratings and the relationship between them may be found in PACRA's Criteria document titled "Correlation between Long-term and Short-term Rating Scales".



1.2.2 This methodology helps in identifying key rating drivers that may create vulnerability in a financial institution's capacity and willingness to service financial obligations in a timely manner. Key rating drivers are pivotal for assessing the financial flexibility of the financial institution, which depends, in large part, on the financial institution's ability to generate cash from operations.

2. Profile

2.1 Background: PACRA reviews the background of the financial institution to understand its evolution, from where it started to where it currently stands. While the majority of banks aim to cater to the banking and financial services needs of the general population, some financial institutions are established to cater to a niche market or with a predefined purpose. This is often the case with DFIs which may be established by sovereigns to focus on a particular set of economic activities or areas. In all cases, the underlying objective and vision of the institution is understood to gauge its progress in realizing that vision and strategy. We analyze how and through what means the institution has achieved its desired expansion. The significant factor here for PACRA is to assess whether the institution has achieved the desired expansion through organic growth or acquisitions. Meanwhile, the source of funding for desired growth is also critical.

2.2 Operations: The assessment of operations of a financial institution depends on the exposure of business segments and the stage the business is in. Here, PACRA reviews the diversity in terms of advances and deposits, geographic spread of operations, product offering in terms of the types of accounts, range of loans, and services offered by the financial institution, asset mix, borrower profile, size of the franchise/portfolio and track record of operations. Size can be an important factor if it confers major advantages in terms of operating efficiency and competitive position.

3. Qualitative Factors

3.1 Qualitative assessment helps to establish the sustainability of the rating in the foreseeable future. Qualitative considerations here refer to rating factors which do not pertain to an entity's business or financial risk. Rather, they focus more on internal processes, people and systems, and thus are essential to incorporate a forward-looking perspective into rating opinions. This section is meant to provide a brief overview of how PACRA generally factors qualitative considerations into its assessment, insofar as they can impact an issuer's ability to meet financial obligations. PACRA's detailed approach undertaken to conduct this analysis is documented in its methodology titled "Qualitative Considerations".

3.2 Incorporating the potential impact of qualitative considerations into the rating opinion can be challenging because it is generally inferred or estimated based on information which may not be standardized and is difficult to quantify. This often requires some degree of subjectivity and analyst judgement, supplemented by PACRA's own experience and experience of the underlying entity or other entities with similar risks. Three factors underlying PACRA's qualitative analysis at entity level include: Ownership, Governance and Management. The scope of analysis for each category is briefly described below.

3.3 **Ownership:** This section provides an overview of the risks pertaining to the structure and stability of the entity's ownership structure, owners' experience and prowess in the entity's industry, and willingness and ability to extend extraordinary financial support in distressful circumstances. The ability of the financial institution to raise capital from key shareholders, as and when required, is an important credit driver. Ratings of financial institutions established or supported by sovereigns may benefit if existing support or likelihood of support from sovereign/s can be established with certainty. Support factors, inter-alia, include percentage of ownership, control over governance framework, provision or arrangement of concessionary funding and some sort of promise to support given certain contingencies. In case of newly established or small financial institutions where capitalization requirements are yet to be met, PACRA critically analyses the willingness and ability of the sponsors to support the institution to comply with the applicable regulatory requirements within required

timeframes. Furthermore, the institution's importance in the domestic financial system also has a bearing on the possibility of sovereign support in times of financial distress.

3.4 Governance: This section provides an overview of the risks pertaining to the Board of Director's role in establishing a robust oversight and control framework to ensure appropriate management oversight, alignment between shareholder and management objectives, transparency in reporting and disclosures, and establishment of strong systems to ensure compliance with all regulatory requirements set by the SBP.

3.5 Management: This section provides an overview of the risks pertaining to the management team's proficiency in executing strategy, maintaining strong information systems and utilizing the same for efficient decision making, and ensuring adherence to the entity's ethical and quality standards.

3.5.1 Risk Management Framework/ Control Environment: This includes an analysis of the financial institution's appetite for risk and the systems in place to manage these risks. PACRA examines the independence and effectiveness of the risk management function, the procedures and limits that have been implemented, limits setting authority and the degree to which these procedures are adhered to. In recent years, there has been a noticeable upgradation in the risk management systems of financial institutions, in the face of increasing guidance and supervision from the SBP. In case of bank, SBP efforts to implement Basel III further improves it.

Credit Risk

- Asset quality Indicators: Primary tool to assess the level of risk being taken.
- These indicators are viewed in the context of returns achieved
- Credit risk management is assessed to determine how the risk return equation evolve in different phases of financial instituions business cycle.

Market Risk

- Asset and liabilities management strategy is reviewed.
- Board and management policy limits, typically expressed as earnings at risk, are evaluated along with reports from management systems.
- Market risk on its own may not be a rating driver. However, poor market risk management or aggressive market risk-taking without mitigants would likely pressurize an institution's ratings.

Operational Risk

- Operational Risk analysis include,
- Financial institution's definition of such risk,
- The quality of its organizational structure,
- Operational risk culture,
- Approach to the identification and assessment of key risks
- Data collection efforts, and
- Overall approach to operational risk quantification and management.

Reputational and other Risks

- May emanate from operational problems or failure in any risk management systems
- Results in withdrawl of deposits in case of strain on reputation.
- Difficult to evaluate but could adversely affect an institution's rating in cases where it is significant.
- Any regulatory non-compliance may lead to potential legal ramifications as well.

4. Business Risk

4.1 Industry Dynamics: The process for anchoring credit rating of a financial institution builds on PACRA's understanding of the industry dynamics. This understanding, following an in- depth research approach, is documented as a sector study. The analysis captures the placement of the local industry in the international context to see the points of identity and distinction. In points of identity, the risks and challenges identified for the international industry are re-evaluated for the local industry players, with a view to see whether the local players have established effective mitigant's against those risks and taken due measures to meet the challenges. At the same time, we identify the risks and challenges specific to the local context of the industry. While conducting the analysis, PACRA takes a view on the industry alone, independent of the market players.

4.1.1 PACRA explores the possible risks and opportunities resulting from social, demographic, regulatory and technological changes. It considers the effects of geographical diversification and trends in industry expansion or consolidation required to maintain a competitive position. The analysis includes the role of the regulator, its supervision of regulated entities, reporting requirements and regulations relating to specific type of financial institutions and to specific financial products.

4.1.2 Economic Risk: PACRA analyzes basic economic indicators of the country including size and composition of economy, performance of important sectors, gross domestic product (GDP) growth, inflation, saving and investment trends and potential credit demand. An important part of economic analysis is positioning of industry and impact assessment of economic risk factors on the industry.

4.1.3 Regulatory Environment: A well-regulated and supervised system is pivotal for credibility and stability of financial institutions even when the operating environment may become unfavorable. PACRA's evaluation of the regulatory system involves evaluation of criteria related to capital and other countercyclical measures to absorb risk and the extent of regulatory supervision and changes in response to the macro environment. This includes looking at key norms (such as Non-Performing Loan (NPL) recognition, provisioning, capital adequacy, liquidity, benchmark lending rate and expansion) and prospective regulatory changes.

4.2 Relative Position: Relative position reflects the standing of the financial institution in the related industry. The stronger this standing is, the stronger is the financial institution's ability to sustain pressures on its business prospects and profitability. This standing takes support from three major factors including: i) market share, ii) growth trend, and iii) franchise/brand value.

4.2.1 Market Share: Market share represents the financial institution's penetration in the chosen market. There is a positive correlation between a financial institution's absolute and relative size and its market position and brand value. Key factors that are evaluated to assess the market share of a financial institution include its share in the sector's total advances, total deposits and franchise presence. In a dynamic industry, which is not characterized by concentration, PACRA believes that relative size rather than absolute size would better capture the strength of the financial institution's standing.

4.2.2 Growth trend: While evaluating the size, PACRA looks at the rate of growth. Growth is important as it shows that the financial institution continues to demonstrate ability to meet industry benchmarks. As the industry grows, it uplifts the scale of its operational context which may be reflected in an increase in the total value of advances and deposits, allowing the financial institution to grow and diversify its loan portfolio. PACRA monitors higher-than-industry growth to understand the quality of the incremental business including impact on

key business segments and if it has resulted in higher concentration due to added business. High growth at the expense of declining portfolio quality is perceived negatively.

4.2.3 Franchise/Brand Value: The strength of a franchise determines its capacity to grow while maintaining a reasonable cost to income ratio and profitability, thus providing resilience to earnings. PACRA evaluates the franchise strength in terms of scale of operations and market share for various activities, performance and strengths relative to competition, complexity of key segments, diversification across various performance metrics like branches, advances, liabilities, sources of other income etc. and access to special Government support or privileges relative to other financial institutions. A strong franchise is expected to result in a granular asset and liability base. PACRA also considers the brand recognition and life of institution for its franchise strength analysis.

4.3 Revenues: In measuring revenue quality of a financial institution, diversification and stability are very important factors. A financial institution with a diverse product slate with more than one revenue streams is considered better than a financial institution with a concentrated earning profile. Composition of revenue from core business activities i.e., advances and investments, is considered critical. The analysis of target markets to which a financial institution serves forms a part of the assessment. Stability is measured through historical trend analysis of the financial institution's revenues. Financial institutions that rely more on generating income from risky business lines like trading activities will typically display more volatile revenue trends. Stability in revenue is considered critical for sustainability of the financial institution.

4.3.1 Diversification: Diversification is desirable since it enhances the entity's ability to meet challenges, both present and upcoming. Lack of diversification gives rise to concentration risk, reflecting vulnerability of the financial institution to few elements. At the same time, it enhances the risk of disruption in if the area of concentration goes wrong. This does not entail that an entity specializing in a certain product/segment would necessarily be at a disadvantage. The disadvantage would only arise if the institution's business gives rise to concentration risk. At the same time, diversification into riskier segments may not improve resilience and, therefore, may not translate into superior ratings. In assessing diversification, common factors include loan mix, portfolio granularity, sectoral mix, share of domestic and overseas exposure and borrower profile. Meanwhile, diverse geographical presence bolsters competitive position as it could offset the credit risks arising from unfavorable regional developments.

4.3.2 Investment Income: Investment income is the alternative revenue stream. It supplements a financial institution's profitability. Profits derived from investments can include interest, dividends and capital gains. Quality of investments is gauged through analysis of the investments from risk viewpoint: credit, market and liquidity risks are the prime ones. Financial institutions invest a significant portion of their investment portfolio in government securities that notably diminishes credit risk. Low rated investments and highly volatile and illiquid investments are considered risky. The quality of the investment book is analyzed to assess the degree of concentration in high-risk avenues.

4.3.3 Non-Mark-Up Income: For most financial institutions, income from advances and investments makes up much of revenue. However, non-interest income from fees, service charges, commissions and foreign exchange etc. may also be an important source of revenue. PACRA views earnings profiles comprised primarily of interest income favorably given the relative stability of this income stream. However, PACRA also assesses the financial institution's ability to complement its core income with fee income. A large fee income allows greater diversification which can improve the financial institution's resilience of earnings and earning profile.

4.4 Cost Structure: Cost structure is analyzed for the amount of flexibility provided when market conditions are less favorable. In this regard, PACRA considers how much of the cost base is variable. PACRA also evaluates the financial Institution's performance ratios relative to those of its peers to understand whether costs have been contained while growing assets and revenue. If expense ratios are high, it could be an indicator that the financial institution has a significant fixed cost burden. In this context, key measure that PACRA looks at is the (Non-Mark-Up Expenses / Total Income) ratio. Whereas, Non-Mark Up expenses comprise i) Compensation expense, ii) Infrastructure expense (including Property & Information Technology expenses), iii) Other Operating expenses. Non-mark-up expenses are also compared where possible with earning assets, to the number of branches and to the number of employees. Performance measures are not assessed in isolation as there may be variations that are caused by business model differences and the importance of ongoing investment in the financial institution's franchise. A low-cost base relative to peers offers the financial institution greater flexibility to deal with competitive pricing pressures. PACRA also considers provisioning levels, together with the capacity of the financial institution's earnings to absorb provisions.

4.4.1 Margins: PACRA looks at the historical trend of a financial institution's performance, the stability and quality of its earnings and its capacity to generate profits. The future profitability of a financial institution is evaluated by analyzing its interest spreads (asset yields minus cost of funds). While taking indicators for a financial institution with those of its peers. Where possible, PACRA also analyses earnings for each of the financial institution's business lines. In this context, it looks at the trends in:

- **i.** Net Interest Revenue including evolution of interest spreads in each business lines, trends in lending volumes and evolution in funding cost.
- **ii.** Non-Interest Income, including more stable revenues in the form of fee and commissions, on inherently more volatile trading revenues.
- **iii.** Exceptional income and expenditure items, as well as developments in taxation incidence.

Where necessary in its rating analysis, PACRA makes adjustments to a financial institution's reported income statement figures, so that financial performance indicators are as comparable as possible from one financial institution to another.

4.5 Sustainability: Earnings prospects are closely examined based on budgets and forecasts provided by a financial institution, as well as any medium-term plan it may have. External factors, which may influence future earnings trends, are taken into account.

4.5.1 Event Risk: Incorporating the risk of unforeseen events into a financial institution's rating opinion is challenging, given unpredictable nature and magnitude of impact of the underlying event. These events may be external (M&A's, regulatory changes, litigations or natural disasters) or may be internally driven (unrelated diversification, system breakdown leading to significant operational risk or strategic restructuring) and can lead to substantial rating changes. PACRA applies its analytical judgment in assessing the likelihood of such occurrences and potential impact, insofar as may be possible, and assesses the financial institution's track record, expertise of management team and level of financial discipline to incorporate the same into its ratings.

Information Required on Business Risk

- Financial statements of the financial institution for the last three years and latest four quarters
- Projections of two years, with details of underlying assumptions
- Break-up of fee, commission & brokerage income
- Spread calculation
- Details of investment book

Business Risk – Key Ratios

Relative Position	• Number of branches • Total Deposits/Sector's Total Deposits (%) • Total Advances/Sector's Total Advances (%)
Revenues	• Advance Yield (%) • Deposits Cost (%) • Core Spread (%) • Net Mark Up Income/Total Income (%) • Other Comprehensive Income/Total Income(%)
Cost Structure	• Return on Average Equity (%) • Return on Average Assets (%) • Asset Yield (%) & Cost of Funds (%) • Intermediate Efficiency (Spreads) % • Non-Mark Up Expenses/Total Income (%) • Compensation Expense/Total Income (%)

5. Financial Risk

5.1 Credit Risk: PACRA looks at all areas that give rise to credit risk whether arising from on- balance sheet activities (including loans, investments, inter-financial institution deposits and placements) or off-balance sheet transactions (letter of credit, guarantees etc.). We examine the structure of the financial institution's balance sheet, including the relative proportions of different asset categories. Generally, but not always, the loan book constitutes the most significant portion of a financial institution's assets and thus a comprehensive review of this is essential (even if it does not account for the bulk of the balance sheet, it is generally where most risk lies). In this context, we ask for a breakdown of lending by type of loan, size, maturity, currency, economic sector and geographical distribution. We also look at concentrations of credit risk, including large exposures (generally top 20 individual and group exposures) and credit risk concentrations in particular industries or sectors.

5.2 Asset Quality: We analyze loans considered to be "problem" loans, whether they are "sensitive" or "watchlist" (i.e., still performing) loans, non-performing or restructured loans. In assessing the underlying risk of problem loans, the adequacy of any security and reserve coverage is taken into account. As far as loan loss reserves are concerned, we examine different types of risk reserves in place (specific, general, etc.), trends of the financial institution's provisioning, loan losses, write-offs and recoveries. Asset quality is assessed using both absolute and relative criteria and, where possible, we compare ratios with those of peer financial institutions.

5.2.1 With reference to the quality of other assets, we analyze the fixed income securities portfolio in terms of the general quality of the securities, their maturity, any undue concentration or particularly large individual exposures and the valuation of these securities. Likewise, an analysis of a financial institution's inter-financial institution deposit and loan book takes into account size, maturity, and concentration of the book as well as the creditworthiness of the counter parties.

5.2.2 Financial institutions' off-balance sheet commitments are important to analyze. Such commitments include guarantees and letters of credit (LCs) as well as derivatives. Similarities exist when analyzing LCs and guarantee exposures. Regarding derivative instruments, PACRA looks at the gross notional and net fair values of a financial institution's derivative portfolio; it also considers the types of derivative instruments the financial

institution uses and the purpose for which it uses them. As far as credit risk is concerned, it examines the systems used by financial institutions for measuring credit exposure, their valuation policies and the quality of counter parties. Apart from credit risk, derivative instruments also give rise to market, legal and operational risks, which also have to be taken into account, separately.

5.3 Market Risk: Analysis of market risk covers all structural and trading risks across a financial institution's entire business (including on- and off-balance sheet business). As far as structural risks are concerned, we examine the financial institution's asset and liability management strategy, the role of position taking, hedging and accounting in this strategy. We look at the levels of interest rate, foreign exchange and market (equity and fixed income) risks on and off-balance sheet and how these compare with the limits set for each of these risks. On the trading side, we examine the general strategy of the financial institution in regard to its trading activities (is it a significant position taker or are its trading activities mainly related to client business or hedging transactions).

5.4 Liquidity and Funding: Main areas to analyze in this section are the structure and diversification of a financial institution's funding base. This includes identifying any marked concentration in deposit base and borrowings, as well as identifying significant trends in funding sources. Composition of the deposit base is analyzed in terms of: retail vs. institutional, current vs. savings/fixed term, and deposits by group (financial institutions, corporates, etc.). The yardstick to gauge concentration is usually proportion of top 20 deposits as a percentage of total customer deposits. The main risk for a financial institution's funding side is not being able to renew or replace maturing liabilities, either at all or at a reasonable cost. A well-diversified and stable funding base and a good spread of suppliers within each source type can limit this risk. It is thus important to analyze the composition of a financial institution's deposit base and other sources of borrowing by size, maturity, geographical source and currency.

5.4.1 As far as liquidity is concerned, we analyze both the financial institution's internal sources of liquidity (marketable securities, maturing loans, etc.) and external sources (such as access to money markets, stand-by lines from other financial institutions and rediscount facilities at the central bank). Against a possible liquidity crunch, most financial institutions hold a portfolio of marketable securities and other assets, which can be sold quickly for cash in case of need. It is, however, important to assess how marketable a financial institution's securities portfolio really is, and whether such securities would be sufficiently liquid in case of a crisis. Finally, financial institutions should have a clear contingency plan, in case they run into difficulties, specifying who is responsible for the management of liquidity in a crisis, what action is to be taken and at what point, and what arrangements exist with "last resort" lenders.

5.5 Capital Structure: A financial institution's capital provides a cushion to absorb unreserved losses, or, in case of insolvency, absorbing losses which would otherwise have to be borne by depositors. Both the absolute size of a financial institution's equity capital and its capital adequacy (i.e., the size of its capital in relation to its risks) are thus fundamental considerations when analyzing its creditworthiness.

5.5.1 Meanwhile, the framework for domestic systemically important banks (D-SIBs) is considered to have a material impact on the capital adequacy of D-SIBs. Here PACRA reviews the compliance status of the financial institution and forms a forward-looking view and any material adverse effect that may have subsequent consequence on CAR. Any regulatory change and its impact on the financial institution is reviewed in comparison with management's track record on such matters.

5.5.2 Besides regulatory capital requirements, PACRA has its own standard quantitative measures of capitalization. These are applied to financial institutions across the board, the principal one being pure common equity as a percentage of total assets. PACRA also examines closely the quality of capital: what percentage of the capital base is pure common equity and how much is in the form of subordinated debt, perpetual debt, and other forms of quasi-equity (such as revaluation reserves, unrealized gains, underprovided non-performing loans and overvalued assets). Management's policies with regard to minimum capital ratio objectives, share buyback programs and dividend payouts are also taken into account, as are the financial institution's ability to raise new capital and its internal capital generation record.

5.5.3 PACRA additionally looks at the trends in a financial institution's regulatory capital ratios, both in absolute terms and in relation to those of its main peers. Moreover, PACRA analyses capital formation rate of a financial institution to form a view on the financial institution's ability to strengthen its capitalization. This is determined on the basis of net retained profits of the financial institutions after deducting the impact of dividend.

5.5.4 Credit Enhancement: The financial institution that carry third party commitment to make good an amount obligated to the lenders may provide additional support to its financial risk profile. In this case, in determining the impact on rating, key factors to assess are the financial profile of the third party and the extent of coverage – quantum and duration – it provides.

Information Required on Financial Risk

- Top performing private group exposures
- Statement of credit exposures by type of security
- Latest Internal Risk Rating of facilities obligors
- Party wise detail of classified loan portfolio
- Latest statement of marginal / watchlist accounts
- Category wise break-up of FSV benefit availed by the bank
- Details of top 20 group-wise deposits and sponsor deposits separately
- Breakup of deposit base
- Capital Adequacy Ratio Statement

Financial Risk – Key Ratios

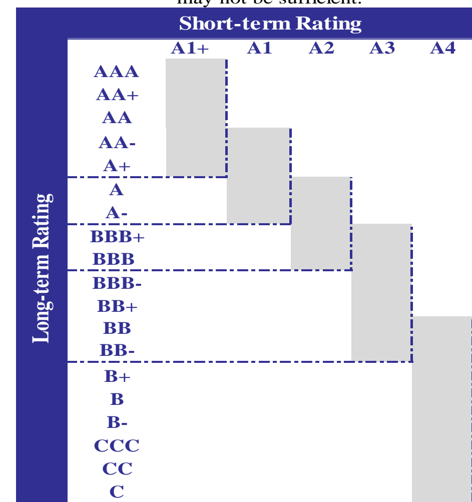
Category	Key Ratios
Credit Risk	•Top 20 Advances / Advances (%) •Non-Performing Advances / Gross Advances (%) •Non-Performing Finances / Gross Finances (%) •Risk Weighted Assets / Total Assets (%) •Loan Loss Provisions / Non-Performing Advances (%)
Market Risk	•Government Securities / Investments (%) •Risk Weighted Assets / (Investments + Debt Instruments) (%) •(Investments + Debt Instruments) / Total Assets (%)
Liquidity and Funding	•Liquid Assets / Deposits and Borrowings (%) •Advances / Deposits (%) •Finances / Deposits and Borrowings (%) •Top 20 Deposits / Deposits (%) •Government and PSE Deposits / Deposits (%)
Capitalization	•Equity / Total Assets (%) •Tier-I Capital / Risk Weighted Assets (%) •Tier-II Capital / Risk Weighted Assets (%) •Capital Formation Rate (%)

Credit Rating

Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

Long-term Rating	
Scale	**Definition**
AAA	**Highest credit quality.** Lowest expectation of credit risk. Indicate exceptionally strong capacity for timely payment of financial commitments
AA+ AA AA-	**Very high credit quality.** Very low expectation of credit risk. Indicate very strong capacity for timely payment of financial commitments. This capacity is not significantly vulnerable to foreseeable events.
A+ A A-	**High credit quality.** Low expectation of credit risk. The capacity for timely payment of financial commitments is considered strong. This capacity may, nevertheless, be vulnerable to changes in circumstances or in economic conditions.
BBB+ BBB BBB-	**Good credit quality.** Currently a low expectation of credit risk. The capacity for timely payment of financial commitments is considered adequate, but adverse changes in circumstances and in economic conditions are more likely to impair this capacity.
BB+ BB BB-	**Moderate risk.** Possibility of credit risk developing. There is a possibility of credit risk developing, particularly as a result of adverse economic or business changes over time; however, business or financial alternatives may be available to allow financial commitments to be met.
B+ B B-	**High credit risk.** A limited margin of safety remains against credit risk. Financial commitments are currently being met; however, capacity for continued payment is contingent upon a sustained, favorable business and economic environment.
CCC CC C	**Very high credit risk.** Substantial credit risk "CCC" Default is a real possibility. Capacity for meeting financial commitments is solely reliant upon sustained, favorable business or economic developments. "CC" Rating indicates that default of some kind appears probable. "C" Ratings signal imminent default.
D	Obligations are currently in default.

Short-term Rating	
Scale	**Definition**
A1+	The highest capacity for timely repayment.
A1	A strong capacity for timely repayment.
A2	A satisfactory capacity for timely repayment. This may be susceptible to adverse changes in business, economic, or financial conditions.
A3	An adequate capacity for timely repayment. Such capacity is susceptible to adverse changes in business, economic, or financial
A4	The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions. Liquidity may not be sufficient.



**The correlation shown is indicative and, in certain cases, may not hold.*

Outlook (Stable, Positive, Negative, Developing) Indicates the potential and direction of a rating over the intermediate term in response to trends in economic and/or fundamental business/financial conditions. It is not necessarily a precursor to a rating change. 'Stable' outlook means a rating is not likely to change. 'Positive' means it may be raised. 'Negative' means it may be lowered. Where the trends have conflicting elements, the outlook may be described as 'Developing'.

Rating Watch Alerts to the possibility of a rating change subsequent to, or, in anticipation of some material identifiable event with indeterminable rating implications. But it does not mean that a rating change is inevitable. A watch should be resolved within foreseeable future, but may continue if underlying circumstances are not settled. Rating watch may accompany rating outlook of the respective opinion.

Suspension It is not possible to update an opinion due to lack of requisite information. Opinion should be resumed in foreseeable future. However, if this does not happen within six (6) months, the rating should be considered withdrawn.

Withdrawn A rating is withdrawn on a) termination of rating mandate, b) the debt instrument is redeemed, c) the rating remains suspended for six months, d) the entity/issuer defaults., or/and e) PACRA finds it impractical to surveill the opinion due to lack of requisite information.

Harmonization A change in rating due to revision in applicable methodology or underlying scale.

Surveillance. Surveillance on a publicly disseminated rating opinion is carried out on an ongoing basis till it is formally suspended or withdrawn. A comprehensive surveillance of rating opinion is carried out at least once every six months. However, a rating opinion may be reviewed in the intervening period if it is necessitated by any material happening.

Note. This scale is applicable to the following methodology(s):

a) Broker Entity Rating
b) Corporate Rating
c) Debt Instrument Rating
d) Financial Institution Rating
e) Holding Company Rating
f) Independent Power Producer Rating
g) Microfinance Institution Rating
h) Non-Banking Finance Companies Rating

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