RATING METHODOLOGY

NON-BANKING FINANCE COMPANIES (NBFCS) RATING

[LEASING COMPANIES, HOUSING FINANCE COMPANIES, INVESTMENT FINANCE COMPANIES, AND MODARABAS]

An independent forward looking opinion on credit worthiness of an NBFC

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0. INTRODUCTION

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A sound financial ecosystem is critical for functioning of any economy. It is defined by interaction of providers of funds - savers, users of funds - borrowers, financial institutions, and regulators. This system ensures smooth flow of funds between savers and borrowers; wherein, financial institutions provide platform for their interaction. Regulatory oversight safeguards the sanctity of this system. Like all systems, financial system has its own set of challenges. The most prominent being "Risk"; the risk that some participant may not be able to meet its commitments. Although risk is an opportunity embedded within the context of uncertainty and all participants do their best to manage this risk to maximize their return. However, confidence on risk quantification and its consequence management is not possible unless we have independent information on this risk. Here comes expertise of rating agencies, providing independent opinion on credit risk. Flow of funds is only possible when the provider of funds has confidence that user of funds will be able to return these in a timely manner and as committed. Ratings help build this confidence. A higher rating means higher likelihood of timely repayment compared to a low rating. PACRA's ratings are forward-looking and reflect our expectations for future financial and operating performance. However, historical results are helpful in understanding patterns and trends of an entity's performance as well as for peer comparisons.

0.1 Scope: Non-banking finance companies (NBFCs) are an important part of the financial system. The operations of most of these NBFCs are not much different from that of the banking companies in the local environment. Traditionally, they used to have their separate space to operate but as the concept of universal banking gained momentum, distinction gets blurred. This implies high competition business environment for NBFCs, thus greater impediments for growth. The key difference between the banks and NBFCs is that the latter cannot offer check-in deposit accounts. NBFCs, as defined in Companies Ordinance 1984 and NBFC& NE Regulation, 2008, include the companies offering leasing, investment finance services, housing finance, venture capital, discounting, investment advisory, and asset management companies. This methodology mainly covers leasing companies, housing finance companies, and investment finance companies. Modarabas carry similar risk factors as by other NBFCs, thus this methodology equally applies to them. Securities and Exchange Commission of Pakistan (SECP) has been acting as the sector regulator since FY03, when a comprehensive regulatory framework was designed for NBFCs. Modarabas are covered under a separate law issued by SECP.

0.2 The services that an entity can offer are linked with the license it acquires subject to fulfilling regulatory capital requirements. A single entity may acquire multiple licenses, e.g. investment finance, leasing, and housing finance. Thus the company having more than one license can diversify their operations. However, related risks are to be managed accordingly.

0.3 Rating Framework: The risk assessment process for NBFCs comprises comprehensive analysis of the particular segment in which the entity operates, profile of the entity, and its relative position in its respective segment. Analyzing the profile of the entity includes comprehensive coverage of both quantitative and qualitative factors. In its assessment, PACRA's quantitative analysis helps to reach an anchor rating. This rating can then be affected by qualitative factors – the modifiers. After standalone rating is finalized, the entity's rating is concluded while incorporating sponsor's assessment of financial strength and expected / agreed level of support. PACRA's framework for assessing credit quality makes use of both qualitative and quantitative analyses. Overall factors are categorized under these key areas.

NBFC Rating Framework

0.4 The quantitative factors helps in achieving objectivity in the rating process while the qualitative side helps in establishing the sustainability of the relevant factors in the foreseeable future. Neither all factors can be quantified nor do quantitative values portray the whole story. PACRA, therefore, seeks to employ a best combination of both and would stick to it to ensure comparability on historical as well as synchronic basis.

While our rating process does not include an audit of a financial institute's financial statements, it does examine the control environment to establish to which extent they accurately reflect a financial institute's financial performance and balance sheet integrity. We make adjustments where necessary to make a financial institute's financial data comparable with those of its peers. In order to carry out adequate analysis of a particular financial institute, it is helpful to establish a "peer group" of comparable financial institutes. Short-term and long-term ratings are based on an entity's fundamental credit characteristics, a correlation exists between them (see PACRA's Criteria document "Correlation between Short-term and Long-term Rating Scale").

1. PROFILE

- *Structure*
- *Background*
- *Operations*

1.1 Structure: PACRA evaluates the legal structure of the entity. Legal status determines the level of expected stability. In cases where the entity is a large financial institute and has a complex business structure, there are unique challenges in evaluating credibility of the entity. PACRA considers the characteristics of the entity as at times a public company structure might operates like a private company. Meanwhile, the level of perceived stability gradually increases from a private entity to a listed entity. However, unnecessarily complex structures when compared to asset size, scale and peers of the same industry would have an adverse effect on the credit scoring of the entity.

1.2 Background: PACRA looks at the progress of the entity since its inception in order to understand the evolution of the entity from where it started to where it currently stand at. The background of the entity helps PACRA in assessing how and through what means the entity has achieved the desired expansion. However, it also help PACRA in establishing the scope of work in terms of its complexity.

1.3 Operations: The assessment of operations of the entity depends on the type of the industry and the stage the business is in. Here PACRA reviews the diversity, geographic spread of operations, and diversification of major borrowers and lenders. Later, PACRA places the entity within its relative universe to evaluate critical factors that provide competitive advantage. Size may be an important factor if it confers major advantages in terms of operating efficiency and competitive position.

2. OWNERSHIP

- *Structure*
- *Stability*
- *Business Acumen*
- *Financial Strength*

2.1 Structure: The assessment of ownership begins with an in-depth study of the shareholding mix in order to disentangle structure of the ownership. This process includes analyzing the detailed chart. Key factors that are considered for this purpose, inter-alia include, i) shareholding structure which includes whether the individual own the entity directly or indirectly, ii) foreign or local shareholders, iii) whether the entity is owned by a single group or through a combination of entities and individuals, and iv) part of a group or a standalone entity. All these deliberations are done to identify the man of the last mile. Secondly, analyzing shareholding structure is also important as clarity on ownership generally lacks in a joint venture agreement.

2.2 Stability: In order to analyze the stability of the ownership, a particularly important factor to be taken into account is the succession planning. A very important part of our background analytical work is an attempt to assess whether, and under right of succession, an entity future prospects would be supported, and by whom. This is particularly relevant for support in case of larger sized banks, whose failures could have a contagious effect on the confidence in the overall financial system.

2.3 Business Acumen: Here PACRA gauge the Sponsor's business skills. Having a strong business skill set has been critical for the sustainable success of the entity. PACRA analyze the business acumen through two primary areas; i) Industry-specific working knowledge and ii) Strategic thinking capability. Meanwhile, a deep and applicable understanding of the system is critical in order to determine how a business achieves its goals and objectives. The scope includes the assessment and understanding of how the apex of the entity think about and successfully make the right business decisions.

2.4 Financial Strength: We analyze the ability and willingness of either its owners or the government / regulator to bail out the entity in case of need. Particularly in case of small financial institute, where capitalization requirements are yet to be met, PACRA critically analyses the willingness and ability of the major shareholder to support the entity to comply with regulatory requirements within required timeframe. Ongoing support is considered more likely in these cases. However, for large financial institutions, external support from government / regulator becomes more important. PACRA gives due importance to, i) the behavior of the major shareholders to provide timely and comprehensive support in times of need in the past, ii) prospective view of key shareholders, incase such need arises, iii) other businesses of sponsors, and iv) the level of commitment of the major shareholder with the entity in providing capital support. In case of no explicit commitment, PACRA attempts to form a view on availability of likely support. The scope for other business of sponsors includes overall profiling of the key sponsor in the context of identifying the resources they have, outside the entity.

Information Required

- *Shareholding Pattern*
- *Details of sponsors' other businesses*
- *Sponsor's financial information*
- *Past pattern of sponsor support*

3. GOVERNANCE

- *Board Structure*
- *Members' Profile*
- *Board Effectiveness*
- *Financial Transparency*

3.0 PACRA's assessment of governance involves both systematic analyses of governance data and information, and the more contextual reviews of an entity's governance practices. PACRA considers four main factors while assessing the board structure of an entity: (i) board structure, (ii) members profile, (iii) board effectiveness, and (iv) financial transparency.

3.1 Board Structure: This comprises assessment of board on various criteria including overall size, presence of independent members, association of board members with the entity, overall skill mix and structure of committees of the board. Size of the board may vary as per the scope and complexity of the business operations of the entity. As too small board is not considered good, similarly reaching on a decision in an effective and efficient manner may not be possible in case of a larger board. A healthy composition of board includes the presence of independent / non-executive members having limited relationship with the sponsoring group of the entity. Meanwhile, same individual holding chairman and CEO positions is considered weak governance practice. Thus these should be separate persons. The chairman is expected to have a non-executive role. Compliance of code of corporate governance is also examined. PACRA also examines the independence of management from major shareholders. Lastly, PACRA evaluates number of board committees, their structure, and how these committees are providing support to the BoD. The board with higher total number of members should have higher number of committees in place to achieve efficiency in performing role of the board.

3.2 Members' Profile: PACRA collects information regarding profile and experience of each board member. This helps in forming an opinion about the quality of overall board. Moreover, diversification in terms of knowledge background and experience is considered positive. However, a fair number of board members should have related experience. Here, director's trainings conducted by the entity are considered good. This is expected to equip the board members in fulfilling their role in an effective manner.

3.3 Board Effectiveness: PACRA considers the role of the board is to work with management in steering the entity to its performance objectives and to provide critical and impartial oversight of management performance. Board members' attendance and participation in meetings is considered a measure to assess the effectiveness. Moreover, PACRA analyses the type and extent of information shared with the board members, and quality of discussions taking place at board and committee level. Effective oversight requires frequent sharing and detailed information than required by statue. Meanwhile, PACRA also review the number of board meeting held during the year as number of board meetings should be justified with the number of issues/matters arising.

3.4 Financial Transparency: Quality of governance framework is assessed by the procedures designed by the board to ensure transparent disclosures of financial information. The board may establish controls to ensure transparency through strengthening the role of audit committee, the quality of internal audit function, and effectiveness of external audit.

Information Required

- *Profile of BoD members*
- *Details of committees including TORs*
- *Minutes of the board meetings*
- *Information packs for the boards (MIS)*
- *Auditor details*

4. MANAGEMENT

- *Organizational Structure*
- *Management Team*
- *Effectiveness*
- *MIS*
- *Risk Management framework*

4.0 Good quality management, effective systems and controls, and well-defined strategy are essential ingredients for a successful entity.

4.1 Organizational Structure: The assessment of management starts with PACRA conducting an in-depth analysis of organizational structure of the entity. On a standalone basis, PACRA looks into the hierarchal structure, reporting line, dependence of the management team on one or more persons, coherence of the team. However, PACRA also places the organizational structure in the entity's relative universe for comparison in order to form opinion of optimal structure within the sector in context of its complexity.

4.2 Management Team: Analysis of management includes evaluating experience profile of key individuals, management's track record to date, in terms of building up sound business mix, maintaining operating efficiency and strengthening the entity's market position. Although judgment about management is subjective, performance of entity over time provides a more objective measure. PACRA analyses the quality and credibility of management's strategy, examining plans for internal or external growth. When evaluating future plans, significant credit is given for delivering on past projections and sticking to strategies.

4.3 Effectiveness: Management effectiveness plays a significant role in empowering the organization through positive results. Effectiveness makes decision making process systematic. Robustness of control systems is considered a reflection of strong management. Number of management committees are established to monitor performance and assure the adherence to the policies and procedures. PACRA measures the effectiveness of the entity by forming an opinion on the quality of management committees. PACRA further assesses whether management has developed any critical success factors (CSF) to evaluate performance of various business segments. The efficacy of these CSF is gauged. Thus PACRA conducts a qualitative review of policies and procedures, technology infrastructure to assess the effectiveness and strength of the management system.

4.4 MIS: One of the key tools available to the management to effectively run an organization is the information provided to it. PACRA closely monitors the type and frequency of information used by the management. The critical aspect is for the information to be concise, clear, and timely so the management can understand and respond accordingly. System generated – real time based – MIS reports add more efficiency in performance monitoring. PACRA evaluates the quality and frequency of the MIS reports used by the department heads.

4.5 Risk Management Framework: This includes an analysis of the entity's appetite for risks 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. PACRA endeavors to assess senior management's understanding of and involvement in risk management issues and examine the reporting lines in place. In recent years, there has been a noticeable upgradation in the risk management systems of the financial institutes, in the face of increasing guidance and supervision from the SBP and SECP.

Operational Risk: *Operational risk has historically been defined as all other risks other than market, credit and liquidity risk. In the context of Basel II, definition of operational risk is: "the risk of loss resulting from inadequate or failed internal processes, people and systems or external events". This definition includes legal risk but excludes strategic and reputation risk.*

Our analysis of operational risk focuses on a number of issues, including (a) an entity's definition of such risk (b) the quality of its organizational structure (c) operational risk culture (c) the development of its approach to the identification and assessment of key risks (d) data collection efforts; and (e) overall approach to operational risk quantification and management.

Other Risks: *As already indicated, a risk often not encapsulated in the above categories is reputation risk, which can be significant for some entities, particularly those active in private banking. A good name and brand image are often an important differentiator of long-term performance in an industry which is becoming increasingly commoditized.*

Information Required

- *Latest Organogram*
- *Profile of senior management*
- *Redundancy pattern*
- *MIS reports*
- *Management meeting minutes*
- *Entity's policies and SOP*

5. BUSINESS RISK

- ***Industry Dynamics***
- ***Relative Position***
- ***Revenues***
- ***Performance***
- ***Sustainability***

5.1 Industry Dynamics: The process for anchoring credit rating of an entity 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 players are re-evaluated for the local 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. This exercise helps PACRA to form a view on industry's significance in the economic environment of the country, its attractiveness to entrepreneurs, barriers to entry, and the power of suppliers and customer.

5.1.1 PACRA explores the possible risks and opportunities in an entity 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 supervisory authority, its supervision of regulated entities, reporting requirements and regulations relating to specific type of financial institutions and to specific financial products.

5.1.2 PACRA determines an entity's rating within the context of its industry fundamentals. Segments that are in decline, highly competitive, capital intensive, cyclical or volatile are inherently riskier than stable with oligopolistic structures, high barriers to entry, national rather than international competition and predictable demand levels. Major industry developments are considered in relation to their likely effect on future performance. The inherent riskiness and/or cyclicality of an industry may result in an absolute ceiling for ratings within that industry. Therefore, an entity in such an industry is unlikely to receive the highest rating possible ('AAA') despite having a conservative financial profile, while not all entities in low-risk segments can expect high ratings. Instead, many credit issues are weighed in conjunction with the risk characteristics of the industry to arrive at an accurate evaluation of credit quality.

5.1.3 Economic Risk: While analyzing economy, PACRA evaluates economic policies, GDP growth, performance of important sectors in the economy and potential credit demand. An important part of economic analysis is positioning of industry and impact assessment of economic risk factors on the industry.

5.2 Relative Position: Relative position reflects the standing of the entity in the related market. The stronger this standing is, the stronger is the entity's ability to sustain pressures on its business volumes and profit margins. This standing takes support from two major factors including a) market share, b) growth trend.

Market Share: *Market size represents the entity's penetration in the chosen market. Size is advantageous as it provides ability to acquire larger business, pricing power and better expense management. There is a positive correlation between an entity's absolute and relative size and its market position and brand value. The large entities exercise greater power over the pricing, while ensuring commensurate profits. Small entities struggle to obtain business; and with less flexibility in the cost structure, their profits remain low. While absolute size is important, it is basically the relative proportion which provides a clear yardstick to analyze the comparative strength of the market players. The more distant a player is from the average on the positive side, the stronger is its ability to reflect the characteristics just mentioned. In a dynamic industry, which is not characterized by concentration, PACRA believes that relative size would better capture the strength of the entity's standing in the related market.*

Growth Trend: *While evaluating the size, PACRA looks at the rate of growth. Growth is important as it ensures that the entity continues to have the ability to meet the industry's benchmarks. As the industry grows, it uplifts the scale of its operational context. This reflects in the ability of the players to invest in human resource, upgrade the control environment, enhance the product slate, increase the outreach and improve the quality of product/service. To lag the industry's growth trend means to remain short on these avenues, putting pressure on the market position.*

5.3 Revenues: In measuring earning's quality of an entity, diversification and stability are very important factors. An entity with a diverse product slate with more than one revenue streams is considered better than an entity with a concentrated earning profile. PACRA sees concentration at both product and customer levels. In addition, the analysis of target markets to which an entity serve s forms a part of the assessment. Stability is measured through historical trend analysis of the entity's revenues. PACRA assessment also covers earning profile of an NBFC, which is dependent on its assets mix and ability to generate non-fund based revenues, mainly fee based income. Fund based income mainly includes, i) interest or profit on advances, loans, ii) interest or profit on fixed income investment or government securities, and iii) dividends or gains (both realized and unrealized) on investments. Non-fund based income may comprise fee, and commission on either off-balance sheet exposures (mainly guarantees), advisory or other services. Financial institutes that relies on more risky business lines like trading, will typically result in a more volatile revenues. Stability in revenue is consider critical for sustainability of the entity.

5.3.1 Diversification: Diversification is a holistic perspective. It encompasses many aspects which govern the business model of the entity. Multiple array of product provider against mono-line product provider is perceived to have less business risk. Diversification is utmost desirable. The rationale for this is that diversification enhances the ability to meet challenges, both present and upcoming. The lack of diversification gives rise to concentration risk, reflecting vulnerability of the entity to few elements. Concentration is considered a major negative because it limits the entity's ability to ensure sustainability in its business let alone expand it. At the same time, it enhances the risk of disruption in the operations if the area of concentration goes wrong. This does not entail that a company specializing in a certain product/segment would be put at a disadvantage. The disadvantage would only arise, if the company's business gives rise to concentration risk.

5.4 Performance: While evaluating the entity's ability to convert its earnings into profits, efficiency ratios, e.g. cost-to-total net revenue, are considered. The drag of provisioning expense is incorporated to see the level of pre-tax profitability for the current as well as future periods. Where necessary in its ratings analysis, PACRA makes adjustments to the entity's reported income statement figures, so that financial performance indicators are comparable across similar entities.

5.5 Sustainability: Earning prospects are also monitored, based on budgets and forecast prepared by the NBFC. A reality check is performed while analyzing underlying assumption taken by the management as well as management's track record in providing reliable budgets and forecasts.

6. FINANCIAL RISK

- *Credit Risk*
- *Market Risk*
- *Liquidity and Funding*
- *Capitalization*

6.1 Credit Risk: Importance of credit risk is significantly more in case of lending institutions including investment finance companies, housing finance companies, leasing companies, and modarabas, because of generally second tier client base of these institutions as compared to commercial banks' borrowers. However, credit risk can arise from both on-balance sheet and off-balance sheet business of the entity. On balance sheet credit risk can materialize from loans, investment in fixed-income securities, and inter-bank deposits. Off-balance sheet credit risk includes non-performance of the counter party on the guarantees issued by the entity. Out of entities covered in this section, generally investment finance companies expose themselves to off-balance sheet risk factors. PACRA analyze both risks in similar manner. However, as quantum of risk taken on balance sheet is higher, particular emphasis is placed on it. Moreover, investments in fixed income securities of private corporates are considered part of the overall financing portfolio for the purpose of credit risk analysis. This is because of their nature, which is very much similar to the financing operations of entity.

6.1.1 The review of credit risk involves assessment of policies and procedures before taking an exposure, post-disbursement monitoring mechanism, criteria for ongoing surveillance, and recovery process.

6.1.2 Credit risk analysis includes review of credit portfolio at all levels. Portfolio is evaluated to calculate market share, to analyze type of counter party e.g. consumer or corporate etc., and product mix in terms of secured and unsecured. Meanwhile, concentration level is given high importance. Concentration is assessed at all levels i.e. sector, borrower, and type of product. The level of concentration is considered to have positive correlation with the degree of risk, i.e. the higher the concentration, more risk the portfolio carries. Thus high level of diversification can shield NBFCs from the impact of downturn in any single segment. Moreover, diversification into riskier segments does not necessarily provide any help to improve the risk profile of the portfolio; it may negatively impact the ratings.

6.1.3 Asset Quality: Assessing quality of assets is an important pillar of credit risk. The portfolio is analyzed with respect to size of the exposure, mainly top 20 exposures, and sectoral division. In addition, watch-list accounts and sectors that are still performing, and non-performing accounts are reviewed to analyze the current asset quality as well as future impact of any expected delinquencies on the overall quality of the portfolio. Post-delinquency, the level of reserves maintained for provisioning requirements is considered important. Meanwhile, asset quality is assessed using both absolute and relative criteria, and where applicable, ratios are compared with the peers.

6.1.4 Quality of fixed income securities portfolio is measured. In addition to the size of the exposures, business dynamics of the sector of counterparty and security structure of the instrument is considered. Similarly, other exposures are analyzed on the basis of nature, size, and credit worthiness of the counter party.

6.2 **Market Risk:** Many of the NBFC's, in addition to regulatory investments (applicable on deposit taking entities), maintain their own investment book. The book may comprise investments in fixed income securities, government papers, and direct exposure to equity markets. PACRA evaluates market risk with particular emphasis on trading book of the entity. While potential loss lying on the balance sheet that is yet to materialize stands as a risk of drag on performance of the entity, any available unrealized gain on investments held for sale is considered as a cushion to unforeseen losses that may arise due to price movements.

6.3 **Funding and Liquidity:** NBFCs are classified into two main segments for funding and liquidity assessment, i) NBFCs that finance their assets through either deposits or borrowings from financial institutions or a combination of both, and ii) NBFCs that meet their requirement either from internal sources (equity) and / or from sponsor loans.

6.3.1 In case of first kind of NBFCs, PACRA analyses funding mix, i) short-term vs long-term; the maturity profile of liabilities is seen in tandem with related asset base to analyze liquidity profile, ii) fixed rate vs floating rate; this has direct implications on business margins in case of mismatch with assets, and iii) retail vs institutional; retail deposits are considered sticky as compared to institutional deposit. While concentration level in funding base is analyzed, due importance is given to liquidity management. PACRA believes higher asset turnover as compared to liabilities is good for liquidity management.

6.3.2 In other scenario, where the assets are financed from equity, sufficiency of free capital available to the entity is assessed as discussed in Capital Adequacy section. While in case of sponsor loan, the terms of loan, its repayment flexibility, and the entity's plan to meet the repayment terms are analyzed.

6.4 **Capitalization:** PACRA evaluates an NBFC's capitalization as a cushion to absorb unreserved losses. These include impact of foreseeable future business losses, if any, and expected level of provisioning on bad loans and nonperforming investments. Where necessary in such cases, PACRA requires comfort from major shareholders of the entity as to ability and willingness to provide support, if the need arises.

6.4.1 While analyzing capital, PACRA excludes the amount that is tied up in fixed assets and, where applicable, any strategic investments from available capital to assess the adequacy and sufficiency of equity of the entity. As ratings are not point-in-time, PACRA also sees the ability of the company to generate capital from internal sources. Meanwhile, dividend payout policy is considered important to evaluate as it may have a significant bearing on potential capital formation rate. Additionally, PACRA considers compliance with regulatory requirements important for an NBFC.

Information Required

- *Top 20 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*

Credit Rating Scale & Definitions

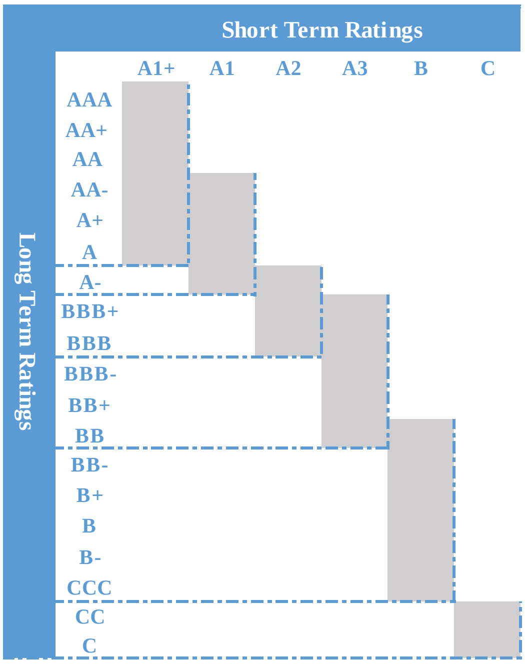
Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

Long Term Ratings

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 Ratings

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 conditions.
B	The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions.
C	An inadequate capacity to ensure timely repayment.



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, a) some material identifiable event and/or b) deviation from expected trend. 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 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) cessation of underlying entity, c) the debt instrument is redeemed, d) the rating remains suspended for six months, e) the entity/issuer defaults., or/and f) 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.