



The Pakistan Credit Rating Agency Limited

## **WHAT IS *DEFAULT*?**

## **RATING POLICY**

DECEMBER 2011

## 1. STATEMENT OF PURPOSE

- Recognizing *DEFAULT*

1.1 The purpose of this criteria paper is to present PACRA's *Definition of Default* and the policy for *Recognizing Default* based upon it. This exercise underlies: (i) PACRA's *continuing* commitment to *promote best practices*, (ii) facilitate *market transparency*, and (iii) ensure *high information content* from its credit ratings.

## 2. NEED TO ARTICULATE "WHAT IS *DEFAULT*?"

- Clear and consistent* parameters of recognizing *default*
- Information content* of credit ratings

2.1 For the users of credit ratings, the key quality determinant is the "*prospectiveness*" of these ratings as to *predicting the probability* of default. Default and transition statistics are widely accepted as the most objective measure of the *performance* of credit rating agencies (CRAs). These, in turn, rest upon the *definition* of "*what is default*?" and the consequent manner of *recognizing* default. However, *comparability* across CRAs has remained complicated as, apart from the most obvious scenario of a debt instrument missing an interest or principal payment, there exists no *universally accepted definition* for *default*. As such, it remains the discretion of individual CRAs to *define, articulate* and *interpret* default according to their own rating systems along with the *distinct* dynamics of the business and economic environment, they operate in.

2.2 Furthermore, the recent crisis in global credit markets has *renewed* focus on the rating systems of CRAs as it has *undermined* confidence in the *information content* and hence the *quality* of credit ratings. In this context, a clear articulation of *WHAT IS DEFAULT* has become all the more critical.

2.3 Defining default is *essential* as it facilitates both *greater transparency* for the users of ratings of a particular CRA and also *comparability* across CRAs. Not only that, based on *this* definition, a consistent adherence to the stated policy of *recognizing default* is critical to the credibility and consistency of the CRA's default statistics.

## 3. RECOGNIZING *DEFAULT* – *Definition*

- HOW PACRA* defines default?
- HOW PACRA'S* definition of default *compares* with Interregional / Global Peers?

3.1 *Default*, in plain terms, is a *failure to fulfill a contractual obligation* and all CRAs unanimously agree upon this basic definition. Thus, "*Default*" essentially means a debtor has *not* paid a debt which it is required to have paid. However, the *point in time* or the "*instance*" at which the default is deemed to have "*occurred*" *differs* as per a CRA's interpretation of the **credit event**. Other things being equal, a rating system that recognizes default *earlier* is better than one that recognizes default *later* as the former is more likely to support high levels of post-default recovery.

3.2 A **credit event** may be defined as a *tangible* (negative) change in a borrower's credit standing which brings into question *the borrower's ability to repay* its financial obligations. A related term, sometimes used as a *synonym*, is **event of default**, *generally* used in commercial loan documentation. Events of default *include* both an actual default (*that is, the failure to pay principal or interest when it falls due for payment*), and prospective default (*when payment is not yet due, but it is clear that it will not be paid when it does fall due – as in the case when the entity / issuer has already begun liquidation proceedings*). In most cases, it so happens that the *occurrence* of a credit event acts as a *pre-cursor* to an event of default, thus serving as a "*red flag*" for the rating agency to take appropriate rating action.

**3.3** Five types of **credit events** are taken into account under PACRA’s definition of default. These are:

- (i) A *missed payment* that remains “*unremedied*” after the grace period
- (ii) A *failure* to honor the corporate guarantee
- (iii) *Bankruptcy* filing or legal receivership by the entity / issuer
- (iv) *Distressed* restructuring whereby:
  - i. An entity / issuer offers creditors a *new* or *restructured* debt, or a new package of securities, cash or assets, that amount to a *diminished financial obligation* relative to the original obligation, and
  - ii. The restructuring has the effect of allowing the entity / issuer to *avoid an immediate bankruptcy* or payment default
- (v) *Exhaustion* of lenders’ forbearance

**3.4** While missed payments, dishonoring corporate guarantees, and bankruptcy filings are relatively *straightforward* credit events to pick up, *identifying* distressed restructuring is more *subjective* and *challenging*. In most cases, evaluating whether a restructuring constitutes default *inherently* involves a judgment call on whether the entity / issuer would have *ultimately* filed for bankruptcy or missed a payment *absent* the restructuring occurring.

**3.5** There exists considerable difference of opinion amongst CRAs as to what constitutes “*credit events*”, as illustrated below:

Credit Events underlying PACRA’s Definition of Default	Unanimity with CRAs	
	Unanimous (✓)	
	Not unanimous (✗)	
	Regional CRAs <sup>i</sup>	Global CRAs <sup>ii</sup>
Missed payment that remains “ <i>unremedied</i> ” after the grace period	✗	✓
A failure to honor the corporate guarantee	✓	✓
Bankruptcy filing or legal receivership by the entity/issuer	✓	✓
Distressed restructuring	✓	✓
Exhaustion of lenders’ forbearance	✗	✗

## 4. CREDIT EVENTS

- Description and Explanation

**4.1** A *description* and *explanation* of each credit event underlying PACRA’s definition of default follows:

**4.2** **Missed payment that remains “*unremedied*” after the grace period:** This is an “**actual**” *missed interest* or *principal* payment on any contractual financial obligation after the lapse of *originally contracted* deferral(s) in accordance with documentation and the consequent grace (*also termed “remedy” or “cure”*) period(s). The moment of *occurrence* of such an event is the “*First instance of the first Rupee default after the lapse of the grace period*”. However, payments made within the *originally contracted grace period* do not constitute default.

- This credit event is irrespective of:
  - *The extent of default* (what portion of debt obligation is not met, be it interest or principal), *OR*
  - *The period of default* (the number of days for which the debt service obligation has *not* been met taking into account *typical* payment days<sup>iii</sup>)

4.2.1 PACRA defines a grace period as the time period ***stipulated*** in a loan contract / instrument indenture / term sheet *and / or* lenders' prudential regulations during which a late payment will not result in any *penal* (interest) charges, *cancellation* of loan / instrument agreement and *triggering* of a credit event.

4.2.2 All credit rating agencies (CRAs) are unanimous upon recognizing default at the "*first instance*" of a missed contractual payment. Such a credit event accounts for the vast majority of defaults globally and is, thus, *easier* to recognize, when it occurs. However, there exists *difference of opinion* amongst regional and global CRAs in terms of *whether* payments made *within* grace periods are *considered* default or not.

**4.3 A failure to honor the corporate guarantee:** PACRA considers *a failure to honor a corporate guarantee* a credit event. This credit event is relevant for: (i) an upstream guarantee<sup>iv</sup>, and (ii) a downstream guarantee<sup>v</sup>. The credit event triggers an event of default for both the issuer / entity (*whose guarantee is dishonored*) and the entity *issuing* the corporate guarantee, *that is*, the guarantor.

**4.4 Bankruptcy filing or legal receivership by the entity / issuer:** PACRA defines bankruptcy as a *filing of insolvency in a court of law*. As such, it is expected to result in a legal finding that imposes *court supervision* over the financial affairs of those who are insolvent or in default. Both *voluntary* and *forced* bankruptcy<sup>vi</sup> is considered a credit event.

4.4.1 In respect to bankruptcy, *if any other credit event has not taken place*, certain *insolvency<sup>vii</sup>-related events* such as a board meeting / shareholder meeting to consider the *filing* of a liquidation petition as being *in furtherance* of an act of bankruptcy may trigger the occurrence of the credit event.

**4.5 Distressed restructuring:** PACRA includes distressed restructuring in its definition of default in order to *capture* credit events whereby entity / issuers *effectively* fail to meet their debt service obligations, but *yet* do not *actually* miss an interest or principal payment. These events can be thought of as being similar to ***out-of-court*** restructurings.

4.5.1 It is *noteworthy* that PACRA does not consider restructuring, *per se*, as a credit event. However, restructuring is considered *tantamount* to default, when it could be established with reasonable certainty the presence of "*harmful intent*" on the part of the entity / issuer, hence, making the restructuring exercise "*distressed*", even though no payment has *actually* been missed. This holds true, notwithstanding the creditors' *apparent* acquiescence, since, *generally*, the restructuring happens to be the *only* viable option open to them to *contain* their losses.

4.5.2 To *establish* a "*distressed restructuring*", PACRA assesses *whether* the restructuring is likely to allow the entity / issuer to *avoid* bankruptcy or imminent default and considers the following factors:

- **Entity / Issuer creditworthiness:** Entity / issuer creditworthiness is examined to assess whether debt service burdens are expected to be *sustainable* and whether the entity / issuer is currently *experiencing financial distress*. PACRA measures *coverages, leverage, liquidity, profitability, cash flows* and *covenant* levels to assess whether the entity / issuer has the ability to meet *upcoming* debt service payments. It is *noteworthy* that the entity / issuer rated in speculative grade *and / or* a low investment grade category is more prone to undertake distressed restructuring.
- **Characteristics of restructuring:** The characteristics of restructuring usually indicate the *intent* of the move, when viewed in combination with the entity / issuer's current creditworthiness. As such, PACRA examines characteristics of restructuring focusing upon:

  - Whether the restructuring is *resorted to* in times of *economic distress* or *buoyancy*
  - Presence or otherwise of *formal consent* to restructure by the instrument investor(s) / lenders sought by the entity / issuer sufficiently before a repayment date
  - The **size** of debt *relative* to total debt to be restructured
  - The **severity of potential loss** to be suffered by investors / lenders, had no restructuring took place
  - The **magnitude of the change** in debt burden / interest cost post-restructuring
  - **Inclusion of any subordination clause** in the restructured term sheet (*materially depleting economic value*) *OR* any other form of coercion (*for instance, pushing the maturity of the instrument / bank loan too far off from the original maturity, extending grace period on coupon / principal repayment etc.*)
  - Whether the restructuring is **voluntary** (entity / issuer initiated) or **forced** (lenders' initiated)
  - **Times** the entity / issuer has used restructuring as an option for: (i) the instrument / loan facility under consideration, and (ii) other financial obligations

4.5.3 **Technical Default – a non-event:** Restructuring accomplishing a revision in debt covenants<sup>viii</sup> in response to an existing or anticipated technical default<sup>ix</sup> is not considered a material credit event. However, its impact, if any, on the creditworthiness of the entity / issuer, would be reflected in the rating.

4.6 **Exhaustion of forbearance:** PACRA makes *provision* for forbearance on the part of lenders / creditors before *recognizing* a credit event on a missed contractual obligation of the nature of an instrument / bank loan facility. A credit event is triggered when lenders' forbearance is considered *exhausted*.

**5. LENDERS' FORBEARANCE – DESCRIPTION & EXPLANATION**

■ *Implications for RECOGNITION of Default.....*

**5.1** Lenders' forbearance is said to be "offered", ***when after the lapse of a grace period***, the lender(s) *voluntarily* delay its right to exercise foreclosure if the borrower can catch up to its payment schedule within a revised (*mutually negotiated*) period of time. Forbearance is *de facto restructuring*, usually offered post-credit event. This period and the new payment plan depend on the details of the agreement, *usually not formalized*, that are accepted by both parties. Forbearance is usually for temporary financial problems.

**5.2** In Pakistan, given a *less developed financial market*, lack of *well-developed bankruptcy laws*, and relatively *immature behavior of borrowers*, lenders' forbearance is prevalent as a *tacit* norm. Hence, it implies a special agreement between the lender and the borrower to delay a foreclosure. The concept of lenders' forbearance is more relevant to the *bank loan* market than to the *bond / instrument* market.

**5.3** PACRA, while *recognizing a payment missed* on a financial obligation (*an instrument or bank loan facility; whether rated or unrated*) as a credit event, forms a view with *reference* to existence of lenders' forbearance *prior* to calling it an *event of default*. In case of *non-existence of forbearance*, default would be recognized immediately. However, if forbearance exists, the recognition of default would be *delayed* till the lenders' forbearance is *considered* exhausted. PACRA takes into account **four** conditions as *vital* and *significant (on a stand-alone basis)* in order to identify that the forbearance has exhausted. Presence of **ANY ONE** or **ALL** of these conditions trigger recognition of default:

- i. Pace of progress on restructuring:** Absence of *any tangible progress* on the management's re-organization / restructuring plan (shared with PACRA earlier)
- ii. Litigation:** Majority of the lenders / creditors (*more than one-third*) have taken recourse in litigation against the company
- iii. Liquidation/cessation of core business activity of the entity / issuer:** Business operations of the entity / issuer have come to a halt and there are serious concerns as to its going-concern status. *Moreover* margins from the core operations have turned negative
- iv. Expiry of prudential / regulatory forbearance period:** Forbearance available to the lenders under the country's *prudential / other respective regulations* for recognition of default expires:
  - a.** In case of **bonds / instruments which are tradable**, particularly where mutual funds can invest, a default has to be recognized, *if remains uncured*, after **fifteen (15) calendar days<sup>x</sup>** of *first* missed payment
  - b.** In case of **bank loans / facilities, residing only on bank books**, a default is reported, *if remains uncured*, after **ninety (90) calendar days<sup>xi</sup>** of *first* missed payment
  - c.** PACRA *retains* the right to use *judgment call* and recognize an event of default even before the prudential / regulatory forbearance period available to lenders expires, if it considers such forbearance period would be *unable* to cure the default

**6. PACRA’S POLICY FOR RECOGNIZING DEFAULT**

- *Implications for ratings*

**6.1 Recognizing default for a PACRA rated issue:** PACRA credit ratings, *in case of entity ratings*, indicate only *probability of default*. However, for *issue ratings*, in addition to the above, the recovery prospects and expected loss (*loss given default*) is also indicated. The term “*issue*” includes: (i) Bonds / instruments (*listed, privately placed with multiple institutions OR with a single institution*) and, (ii) Bank loans / facilities.

- When PACRA establishes that an event of default has occurred, which *usually* means that *a payment is missed and couldn’t be OR unlikely to be cured* within the *forbearance period*, it revises the issue rating to “**D**” (**Default**) irrespective of *ultimate recovery prospects*. So there is *no notching*, hence, well secured, senior unsecured and subordinated issues are all rated “**D**”.
- Corresponding entity / issuer rating is revised to “**SD**” (**Selective Default**), OR “**D**” (**Default**) depending upon the *size and impact* of *said* default on the overall entity

**6.2 When a PACRA rated entity defaults on any one of their unrated financial obligations (instruments / bank loans / facilities):** When an entity with PACRA ratings misses a payment on any of its *unrated borrowings*, PACRA considers the event putting *significant downward pressure* on *outstanding* instrument / bank loans / facilities ratings and entity / issuer ratings as historical evidence shows that an entity / issuer defaulting on one contractual obligation is *highly likely* to default on others as well.

6.2.1 However, no rating action is taken until and unless an *investigation* of the event, which begins immediately upon discovery of the said event, *uncovers* a material deterioration in the entity / issuer creditworthiness. Also, judgment call is made as to the likely extent / length of *potential forbearance forthcoming*. Hence, PACRA requires very strong mitigating factors to conclude that: (i) this *one* default is an *isolated event* and will not spill over to disrupt other obligations due to the presence of any *cross default*<sup>xii</sup> or *obligation acceleration*<sup>xiii</sup> clause triggered by the event, and (ii) the situation would be “*remedied*” soon. PACRA’s policy for *recognizing default* and *Implications for ratings* are as follows:

- Outstanding Instrument / bank loan / facility ratings (*that are still performing*) are revised into **speculative grade** levels, if adequate mitigants are not seen / found
- Outstanding entity / issuer ratings are immediately revised to “**SD**” (**Selective Default**) depending upon the *size and impact* of *said* default on the overall entity

**6.3 Restructuring (Instruments / loan facilities):** Whenever a PACRA rated instrument / loan facility undergoes restructuring, the event warrants *revisiting* the rating opinion.

6.3.1. PACRA employs judgment call to form an opinion as to the impact of restructuring in terms of *default avoidance* by the entity / issuer based upon the following considerations:

- If restructuring is deemed *opportunistic* (taking advantage of lower interest rates, etc.), ratings are likely to be “*maintained*” or even “*adjusted higher*” as post-restructuring, the entity / issuer is seen having a stronger base to service its obligations. However, the *provision* for such restructuring is usually identified in the *original* instrument term sheet / loan arrangement
- If restructuring is deemed *an attempt to avoid default* or is *coercive* in nature (*no formal written consent by the investors, initiated by the lender and / or takes place at terms inferior to those of the original*) and *points* towards *fundamental weaknesses* in the financial strength of the *underlying* entity, the ratings are *immediately* revised, usually into **speculative grade** categories. However, if *default avoidance* is clearly established, the ratings are revised into “**D**” (**Default**)
- The corresponding entity / issuer ratings are adjusted accordingly

**ALSO REFER** to Annexure – *Recognizing Default – Course of Events*

## 7. What PACRA’S *DEFAULT RATINGS* DENOTE?

- Default ratings *definitions*
- Default ratings are *not prospective ratings*

**7.1 Explanatory Information of PACRA’s *Default ratings*:** PACRA’s Standard Rating Scale contains two categories indicating default. These are: (i) **Selective Default “SD”**, and (ii) **Default “D”**. The rating definitions for both are as follows:

- **Selective Default “SD”:** An *uncured*<sup>xiv</sup> failure to pay a specific issue or class of obligations when it came due but continues to meet its payment obligations on majority issues or class of obligations in a timely manner
- **Default “D”:** An *uncured* failure to pay all or substantially all obligations (*a general default*) when they came due

**7.1.1** PACRA “*assigns*” default ratings where it has *reasonably* determined that payment has not been made on an obligation in accordance with the requirements of the obligation’s documentation, and *ALSO* where it *believes* that default ratings, *consistent* with PACRA’s definition of default, are the *most appropriate* ratings to assign. As such, both “**SD**” and “**D**”, unlike other ratings (*from AAA – C*) are *not prospective*, rather, they are used only when a default has *actually* occurred *OR* is imminent.

**7.2** PACRA withdraws ratings when: (i) the rating relationship is terminated at the client’s request or made to terminate by PACRA on account of a lack of cooperation, particularly at a time when the company is experiencing financial distress and refuses to provide all the information needed to continue surveillance on the ratings, (ii) when an entity ceases to exist as a result of a merger / acquisition, and (iii) when a debt instrument reaches maturity and is fully redeemed. As per PACRA Policy, entity ratings, put on the default counter (*whether D or SD*), remain under surveillance on a best-effort basis and updated using both public and non-public sources, till the time (i) and / or (ii), as mentioned above, occurs. An entity rating, hence withdrawn, marks the end of the rating relationship with PACRA. Thereafter, a fresh rating mandate is agreed in order for entity ratings to be assigned. Instruments, assigned a **D** rating, remain under surveillance (*till fully settled*) and are updated using both public and non-public sources, on a best effort basis.

**8. OTHER JUDGMENT CONSIDERATIONS**

- The “Intent / Willingness” to default
- Default of Parent / (Group Company) / Subsidiary
- Appropriate rating actions, while “anticipating” default

**8.1 “Intent / Willingness” to Default:** CLEAR and APPARENT exhibition of the “Intent to default” by the entity / issuer overrides all indentures, credit enhancements, provisions for default protection and grace periods as a consideration for recognizing default. However, judgment call has to be exercised in order to formulate the extent of impact of exhibiting such intent upon ratings of the entity / issuer and all its rated instruments/bank loans and other contractual obligations.

8.1.1 It is noteworthy that *even* when the “intent to default” is **clear** and **apparent**, a “**D**” (**Default**) rating is not assigned *prospectively*. However, in such an eventuality, while moving ratings to **near-default** categories, no grace/remedy period (*contained within the originally contracted term sheet*) is taken into account. Hence, ratings are revised into default categories “at the first instance of the first Rupee” default.

**8.2 Parent (Group) / subsidiary / associate default:** When a rated/unrated parent (group) / subsidiary / associate defaults, the event exerts *significant pressure* upon the ratings of subsidiaries / associates (group companies) / parent company and warrants *heightened vigilance* and an immediate review of the group’s creditworthiness and the nature of parent/subsidiary/associate relationships alongwith the stand-alone creditworthiness of each subsidiary / associate (group company). Event of default would be *recognized* only when *cross default* and *obligation acceleration* provisions are *present* within the subsidiaries / associates (group companies) / parent company relationship. Otherwise, outstanding ratings are revised *as per respective implications*.

8.2.1 **Securitization:** The formation of a “*special purpose entity (SPE)*” as a funding vehicle by the parent (group) does not necessarily “fireproof” the SPE and / or its parent against the spillover risk of default. The business relationship and the extent of credit risk *still* emanating from the parent and / or the subsidiary despite the *theoretical* “bankruptcy remote” status of the SPE would be considered carefully to infer the implications upon ratings.

**8.3 Accounting for economic losses suffered as a result of changing market conditions:** Importantly, *economic losses* suffered as a result of changing market conditions or changes in the credit quality of the entity / issuer are not events of default, as long as the entity / issuer is meeting the terms of its debt obligations. However, the *respective impact* of such a development would be captured in the entity / issuer rating.

**8.4 Putting commercial forbearance in perspective:** Commercial forbearance is a special agreement (*through a tacit / informal understanding*) between the trade debtor and the creditor to alter the terms of payments, hence delaying a foreclosure. Commercial forbearance is generally:

- Manifested in the form of *revised payment terms and conditions* in response to an existing or anticipated payment default
- Offered industry-wide in response to an entity’s failure to honor its commitments as a direct result of *bottlenecks in the government machinery or temporary changes in an industry’s dynamics* and not weakness in its own credit profile

**8.5 What happens to ratings Post-default ?:** Default is an “*all consuming*” event and the defaulted rating ceases to exist at the time of *occurrence* of such event. Hence, *subsequent to default*, there cannot be any revision to ratings. Once the default is *cured*, the rating is assigned anew as an initial rating based on the post-default fundamentals.

### 9. POLICY REVIEW

- Review & updation considerations

**9.1** The rating policy “**What is Default?**” *undergoes* period review and updation as per *Review Calendar* (in this case, on an annual basis). Such a review may also be *undertaken* at any time (other than the scheduled review date), if a change in either the *operating* or *regulatory* environment warrants it.

**9.2** A policy review exercise may not *necessarily* result in an updation of the policy. However, if the review results in any *material change / refinements* in the policy, then the policy is *updated*. Subsequently, the updated policy is released on PACRA website with an *accompanying* press release.

<sup>i</sup> **Regional CRAs:** **CRISIL** - Credit Rating and Information Services of India Ltd. (CRISIL) is India's leading Ratings, Research, Risk and Policy Advisory Company. CRISIL's majority shareholder is Standard & Poor's, **RAM** - RAM Rating Services Berhad ("RAM Ratings") is Malaysia's premier rating agency

<sup>ii</sup> **Global CRAs (GCRAs):** The three major US rating agencies namely, Standard and Poor's, Moody's and Fitch Ratings

<sup>iii</sup> **Typical payment days:** Period of processing a payment otherwise made fully, in which "non payment" is condoned. In Pakistan, the general practice followed by lenders is to offer such relaxation for a period of about seven (7) days

<sup>iv</sup> **Upstream guarantee:** A contingent liability on a subsidiary's financial statements in which the subsidiary guarantees its parent company's debt. Upstream guarantees are performed to get better financing terms for the parent or to initiate financing

<sup>v</sup> **A downstream guarantee:** A guarantee on behalf of the borrowing party by its parent company or stockholder. By guaranteeing the loan, the parent company provides assurance to the subsidiary company's lenders to repay the loan. The guarantee requires the parent company to repay the loan if the subsidiary is unable to. A downstream guarantee can be undertaken in order to help a subsidiary company obtain debt financing that it otherwise would be unable to obtain, or to obtain funds at interest rates that would be lower than it could obtain without the guarantee from its parent company

<sup>vi</sup> **Voluntary and forced bankruptcy:** Voluntary bankruptcy is filed by the debtor itself, whereas, forced bankruptcy is filed as a petition by the creditor(s) against the debtor to force the latter into bankruptcy

<sup>vii</sup> **Insolvency:** Insolvency is a legal term meaning that a debtor is unable to pay their debts. Insolvency is not a synonym for bankruptcy

<sup>viii</sup> **Covenants:** Affirmative covenants are clauses in debt contracts that require firms to maintain certain levels of capital or financial ratios. The most commonly violated restrictions in affirmative covenants are tangible net worth, working capital/short term liquidity, and debt service coverage. Negative covenants are clauses in debt contracts that limit or prohibit corporate actions (e.g. sale of assets, payment of dividends) that could impair the position of creditors. Negative covenants may be continuous or incurrence-based. Violations of negative covenants are rare compared to violations of affirmative covenants

<sup>ix</sup> **Technical default:** Technical default happens when an affirmative or a negative covenant is violated

<sup>x</sup> **Fifteen (15) calendar days:** As per AMC provisioning criteria via circular 6 of 2009 – *provisioning criteria for non-[performing debt securities* – stating that a debt security shall be classified as non-performing, if the interest and / or principal amount is past or overdue by 15 calendar days from the due date

<sup>xi</sup> **Ninety (90) calendar days:** As per State Bank of Pakistan Prudential regulations via BSD Circular no. 07 of 2005 – *classification & provisioning for loans and advances* – stating that the loans / advances overdue by 90 days will be classified (*as substandard*)

<sup>xii</sup> **Cross default clause:** Default in one obligation triggers default in other obligation(s)

<sup>xiii</sup> **Obligation acceleration clause:** The credit event can be triggered when an occurrence such as a covenant breach on one debt instrument leads to the acceleration of other debt obligations. Acceleration means the holders of a debt obligation can demand immediate repayment either in full or of material outstanding amount

<sup>xiv</sup> **Uncured:** An obligation OR entity / issuer in "default" not returning to "performing" status at the end of grace / forbearance period

## Selected Reference List (By CRA)

**Standard & Poor's:** (General Criteria) Rating implications of exchange offers and similar restructurings, (Criteria Paper) Guarantee Criteria

**Moody's:** (Moody's global credit policy) Moody's approach to evaluating distressed exchanges, (Rating methodology) Financial Guaranty Policies – What is needed for credit substitution

**FitchRatings:** (Global Criteria) Coercive debt exchange criteria

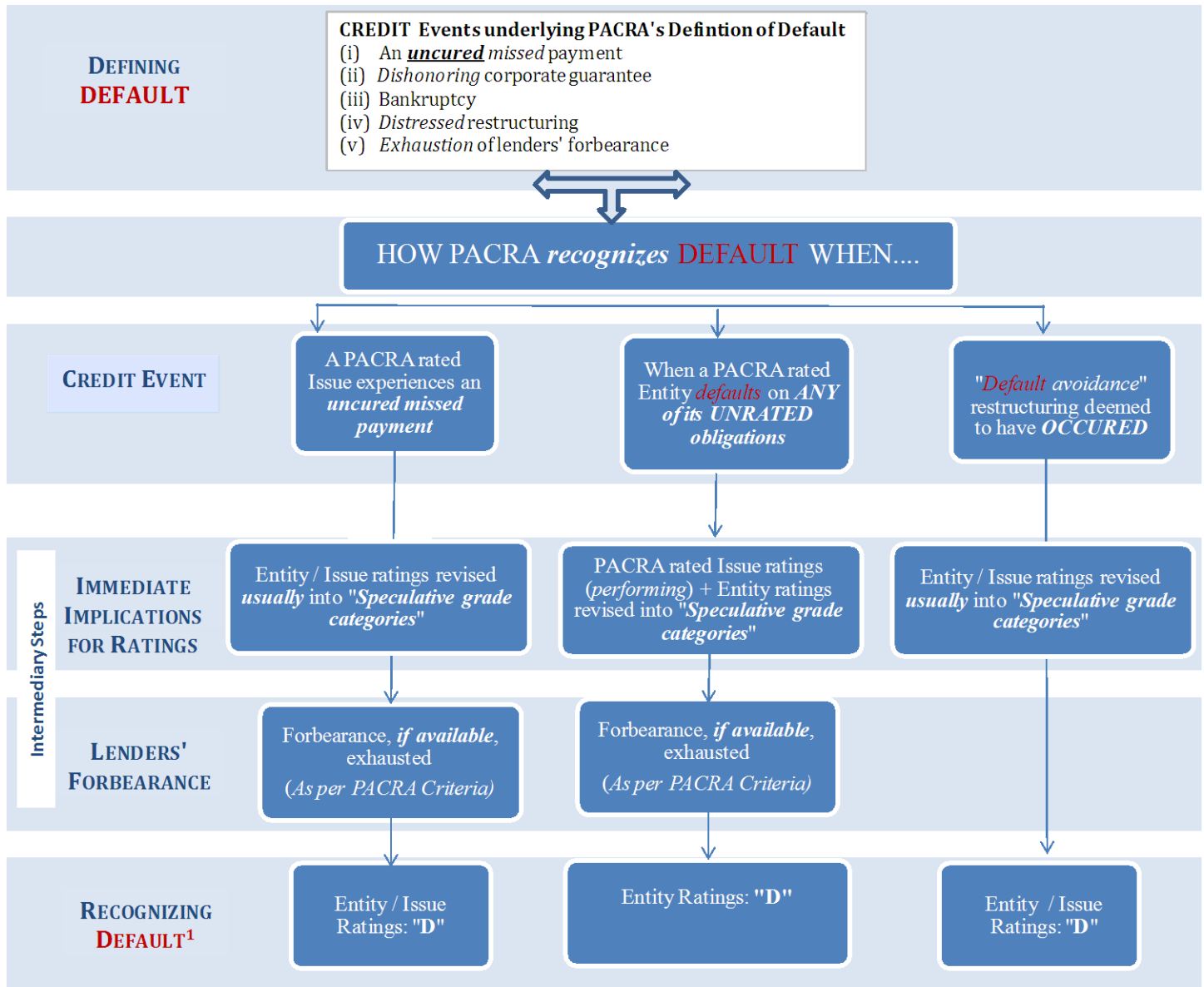
**CRISIL:** Clear default definition critical for reliable credit rating, Crisil's approach to recognizing default, CRISIL's rating approach towards restructuring of bank loans

**Rating Agency Malaysia Berhad:** Corporate-default & rating-performance study (1992 – 2008)

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<sup>1</sup> After the occurrence of the credit event, PACRA retains the right to recognize default immediately, without observing any intermediary steps

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