



Rating Release

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PACRA DEFINES *DEFAULT* AND ELABORATES IT'S POLICY ON RECOGNIZING DEFAULT

The Pakistan Credit Rating Agency (PACRA) defines Default and elaborates its policy on recognizing default. The Policy titled “**What is *DEFAULT***”, after undergoing some refinement via a stakeholder comment solicitation exercise, is available on PACRA’s website.

The purpose of this rating policy 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.

A clear definition of default is pivotal in the *timely* recognition of the event of default, when it occurs. Furthermore, defining default is essential as it facilitates both greater transparency for the users of ratings of a particular rating agency and also comparability across agencies. 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 rating agency’s default statistics.

Default, in plain terms, is a failure to fulfill a contractual obligation and all raters unanimously agree upon this basic definition. Thus, “Default” essentially means a borrower 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 each rating agency’s interpretation of the credit event.

The policy document describes five types of credit events underlying PACRA’s definition of default. Subsequently, with these forming a basis, implications for ratings are explained separately for borrowings (instruments and bank loan facilities) and entities.

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