



Wholly owned by RAM Holdings Berhad – affiliate of Standard & Poor's

---

## **RATING METHODOLOGY: FINANCIAL INSTITUTION'S RATINGS**

---

### **SUMMARY**

*This paper provides an overview of RAM Ratings' generic approach to financial institutions' ratings, which encompass the assessment of commercial banks, merchant banks, finance companies and development banks.*

---

### **CONTACTS:**

Prakash Jerome  
Financial Analyst  
+9411 2503551  
prakash@ram.com.lk

RAM Ratings' approach to the rating of financial institutions or "FIs" (i.e. commercial banks, merchant banks, finance companies and development banks) involves the analysis of both quantitative and qualitative factors. These factors are analysed to determine the level of risk in an FI's ability to meet its financial obligations in a timely manner.

The first step in the rating process is the assessment of the FI's operating environment, which focuses on the well-being of the economy and the regulatory framework before conducting any FI-specific analysis. FI-specific analysis centres on the FI itself, rather than the group. This is premised on the fact that different banking groups may have different set-ups and business activities that will complicate any comparison analysis. RAM Ratings, however, will conduct a cursory examination of the subsidiaries as well as the consolidated statements of the banking group to assess possible drains on the resources of the FI.

RAM Ratings only conducts solicited ratings, which will require the full co-operation of the FI in providing detailed information on its operations. The analysis will involve charting financial data and compiling a set of financial ratios to detect the trends and anomalies in the FI's market and financial positions. While quantitative analysis is an important consideration when determining the strength of an FI's credit standing, qualitative factors - which zoom in on issues beyond numbers and ratios - play a critical role in assessing the creditworthiness of an FI.

# O

## PERATING ENVIRONMENT

---

Before attempting to assess an FI, there are many external market influences which the analyst should be aware of. Evaluation of an FI's credit strength takes into consideration the operating environment in which it conducts its business activities. An understanding of this environment involves analysis of the economic scenario, Government policies, the Central Bank's guidelines and the level of competition among the various types of FIs. Other factors that are examined include the FI's market position and financial flexibility.

### **Industry Characteristics and Trends**

Analysis of the existing economic scenario and expected future economic developments is important as the banking sector's performance hinges on the well-being of the country's economy, given its exposure to the various economic sectors. The rating exercise will look into several indicators like the growth trend in gross domestic product ("GDP") as well as the historical and expected performance of the various economic sectors.

Another important area of contemplation is the level of competition among the various types of FIs moving forward, taking into consideration any impending liberalisation or threat from global players. The analyst will also need to understand the structure of the banking industry.

### **Regulatory Environment**

Understanding Government policies and their effect on the banking sector's regulatory structure are crucial in analysing the performance of FIs. We view effective regulatory supervision as essential towards ensuring the integrity of information received. This is deemed important, as we are unable to undertake a detailed review of an FI's operations.

Integrity aside, assessment of the FI's regulatory environment will focus on the Central Bank's guidelines on banking operations which include prudent controls on liquidity, portfolio requirements, capital adequacy requirements, provisions for bad and doubtful debts, and classification of non-performing loans.

### **Market Position**

There are different types of institutions within the market; attempting to identify the potential problems each kind may face provides a better understanding of an FI's strength and/or weakness. Our evaluation will consider the degree of rivalry within the banking industry and the challenges posed by non-bank institutions as well as the presence of international foreign banks. Analysis of market position takes the following factors into account:

- Asset size and market share by product type (i.e share of the banking system's retail deposit structure)
- Diversity of business operations and network
- Level of information technology ("IT") and its integration
- Niche market
- Franchise value

### **Financial Flexibility**

Assessment of financial flexibility identifies the financing options available to an FI under stress. Factors considered in such analysis include the following:

- Affiliations to other organisations and shareholders (i.e. ownership quality and likelihood of support from shareholders)
- Ability to access various financial markets within a difficult environment (depends on the FI's credit strength and inter-bank relationships)
- Ability of internal reserves to cover losses
- Ability to liquidate investments to obtain funding

Shareholders' support in the form of adequate financial resources and willingness to provide backing in difficult times are important considerations. Nevertheless, strong shareholders' support alone cannot over-shadow the fundamentals of an FI although the level of enhancement may vary. This is also true for Government- or state-owned FIs. The issue of shareholders' support deals with the provision of short-term funds, such as temporary loans or the injection of more permanent capital. An indication of the parent's willingness and likelihood of support stems from its track record in terms of answering cash calls. Another avenue of flexibility is the ability of a financially beleaguered FI to tap the capital market for funds. This would also depend on the FI's credit strength and its relationships with its peers.

# F

## I-SPECIFIC ANALYSIS

---

In rating an FI, the foremost consideration is to assess the likelihood that it may face difficulties in repaying its financial obligations in a timely manner. During the course of the rating procedure, attention is focused on the financial strength and payment capacity of the FI based on its historical trends, typically going back 5 years, and compared against its peers. The analysis, however, will not be complete without an evaluation of the expected performance of the FI in the future. Therefore, the rating will also cover the FI's projected business and financial profiles over the next 2 - 3 years.

FI-specific analysis seeks to determine the institution's business and financial fundamentals. The appraisal focuses on the modified elements of the classic CAMEL model where:

**C** stands for **Capital Adequacy**

**A** stands for **Asset Quality**

**M** stands for **Management Quality**

**E** stands for **Earnings Quality**

**L** stands for **Liquidity and Funding**

The CAMEL model incorporates analysis of both quantitative and qualitative values, with quantitative meaning financial ratios while qualitative refers to the subjective elements driving the FI's operations. Being inter-related, the elements in the CAMEL model cannot be applied singularly. Any movement or decision on one element will definitely affect the others. In light of this, a very clear and in-depth understanding of their inter-relationship is crucial in analysing an FI. Meanwhile, a highly rated FI need not necessarily have the best attributes in each of the CAMEL elements. By the same token, having the best accomplishments in terms of the quantitative elements of the CAMEL model also does not automatically guarantee an FI the highest rating.

# C APITAL ADEQUACY

| Factors Considered   | Key Financial Ratios   |
|--|--|
| <ul style="list-style-type: none"> <li>• Capital structure</li> <li>• Capital adequacy ratios</li> <li>• Policy on capital adequacy ratios</li> <li>• Growth strategy and its affect on future capital adequacy ratios</li> <li>• Internal rate of capital generation</li> </ul> | <ul style="list-style-type: none"> <li>• Shareholders' funds / Total assets</li> <li>• Shareholders' funds / Net loans &amp; advances</li> <li>• Tier-1 capital / Risk-weighted assets</li> <li>• Capital base / Risk-weighted assets</li> <li>• (Net profit + General loan loss provisions) / Average shareholders' fsunds</li> </ul> |

From a credit rater's perspective, analysis of the FI's capital adequacy focuses on its ability to absorb future credit losses. Seen from that angle, it is imperative to also understand the kind of risk an FI takes with respect to credit, market, liquidity and operations. The assessment will begin with a review of the composition of the FI's capital. A higher level of core capital is viewed more favourably as it is permanent in nature and would be available to set off credit losses. An FI's health is typically gauged through the capital adequacy requirements of the Central Bank. Therefore, if an FI's capital is impaired, it is at risk of being perceived to have failed in the eyes of the regulators.

Analysis of capital adequacy takes into consideration the Bank for International Settlement's ("BIS") standards which express capital adequacy in relation to the FI's risk-weighted assets<sup>1</sup>. This ratio is commonly known as the risk-weighted capital adequacy ratio or RWCAR. The basic principle of the RWCAR involves the standardisation of credit risks by assigning weight to different classes of assets, with those deemed risky being assigned a greater weight (as more capital must be made available to support such assets).

It is important to have an understanding of the FI's policy on capitalisation and its ability to maintain its level of capital through internal capital generation and growth of risk assets vis-à-vis its capital and total assets. The analyst will also attempt to ascertain if erosion of its capital is imminent as a result of the FI's business strategy in respect of risk and earnings potential.

<sup>1</sup> In the next couple of years, a new capital adequacy requirement, BASEL II, by BIS will be implemented. This will require FIs to also set asset capital for market and operational risks.

# A

## ASSET QUALITY

| Factors Considered   | Key Financial Ratios   |
|--|--|
| <ul style="list-style-type: none"> <li>• Credit risk management</li> <li>• Portfolio of non-performing loans (“NPLs”)</li> <li>• Reserving policies</li> <li>• Sectoral risks</li> <li>• Large loan exposure including to related parties</li> <li>• Asset composition and growth</li> </ul> | <ul style="list-style-type: none"> <li>• Net loans &amp; advances / Total assets</li> <li>• Risk-weighted assets / Balance sheet assets</li> <li>• Gross NPLs / (Total loans &amp; advances - IIS<sup>2</sup>)</li> <li>• Net NPLs / (Total loans &amp; advances - IIS - Specific LLR)</li> <li>• Net NPLs / Total assets</li> <li>• Net NPLs / Shareholders’ funds</li> <li>• Loan loss reserves / Gross NPLs</li> <li>• General loan loss reserve / (Total loans &amp; advances - IIS - Specific LLR + General LLR)</li> </ul> |

In rating an FI, asset quality is viewed as one of the most critical elements of the CAMEL framework. While impairment of the other quantitative factors of CAMEL can also lead to an FI’s failure, deterioration in asset quality is typically the root of the problem. Asset quality is the greatest source of variability in an FI’s earnings because its primary business is in providing credit. From this viewpoint, it follows that an FI’s credit culture and philosophy have to be thoroughly understood. Improvement or deterioration in the portfolio of assets can result in changes to profitability, liquidity and - ultimately - the FI’s capitalisation.

An important consideration in asset quality assessment is the evaluation of the FI’s risk profile and how it manages these risks. Due diligence is thus essential in attempting to understand the FI’s credit risk management. Assessment would include a good understanding of its underwriting standards, security documentation procedures, monitoring mechanisms, problem loan identification processes, collateral management system, and provisioning policies.

Our analysis is to ascertain whether there are sufficient checks and controls in an FI’s approval and monitoring procedures, to manage the level of risk that exists in its asset portfolio. The assessment will also focus on the adequacy and effectiveness of the FI’s credit control process in mitigating the incidence of delinquent loan assets. The effectiveness of the FI’s management information system in complementing the administration of its asset portfolio is another important factor.

<sup>2</sup> Interest-in-suspense

The FI's non-performing or problem loans, loan loss reserve policies and coverage for problem accounts will also be evaluated. The analysis will cover the FI's delinquency experience and reserving policy over a sufficiently long period, and compared against those of the industry over the same period. Analysis of the trend of newly classified problem loans and the rate of recovery for problematic accounts will provide an indication of the quality of the FI's loan portfolio.

The vulnerability of an FI's loan profile, through analysis of its exposure to the various industry sectors and single customers, will also be examined. The analysis attempts to identify excessive loan concentration on any particular sector or geographical location and large clients, and how these risks are managed. Intra-group exposure is also analysed as intra-group lending may not be based on sound credit evaluation procedures and thus may expose the FI to contagion risk.

**Off-Balance Sheet Exposure ("OBS")**

| Factors Considered   | Key Financial Ratios  |
|--|---|
| <ul style="list-style-type: none"> <li>• Composition of off-balance sheet exposure</li> <li>• Size of off-balance sheet exposure</li> <li>• Limits (e.g. proprietary trading account, dealers, overnight and cut-loss)</li> <li>• Internal control system</li> </ul> | <ul style="list-style-type: none"> <li>• Off-balance sheet risk-weighted assets / Risk-weighted assets</li> </ul> |

Off-balance sheet exposures are analysed to determine the level of credit and market risks. Of particular importance is the area of derivatives, i.e. foreign exchange and interest rate contracts and swaps. Other aspects include dealers' trading limits, loss limits and system competence in early detection of unauthorised transactions. Therefore, internal controls are of utmost importance. Our analysis will attempt to understand the controls that are in place to mitigate the risks inherent in such trading activities. Large trading limits on proprietary accounts and large open positions are generally viewed negatively.

# M

## ANAGEMENT ASSESSMENT

---

Essentially, there are no clear quantitative measures to ascertain a FI's management quality. Nevertheless, it remains an extremely critical component of the FI's credit analysis. This is because the setting of goals as well as the development and implementation of business plans, which will eventually determine the performance of the FI, lie in the hand of its management.

The management team, particularly those making lending decisions, should possess a high degree of integrity and have adequate knowledge, training and experience to discharge their responsibilities. Additionally, FIs should ensure the presence of good internal controls and management information systems so that informed decisions can be made in the interests of the bank and established policies and procedures are adhered to.

The management assessment would look into areas such as: the track record of the existing management team; management stability, continuity and experience level; the reasonableness of the FI's goals and management strategies to achieve these goals given the available resources; the decision-making process; and the influence of any critical individuals on the goals and strategies of the FI.

Management information systems have assumed increased importance in the management of FIs. To this end, our analysis would also turn to the quality, depth and relevance of the information made available to the management, in a timely manner, to track the performance of the FI.

# EARNINGS QUALITY (PERFORMANCE)

| Factors Considered  | Key Financial Ratios   |
|---|--|
| <ul style="list-style-type: none"> <li>• Contribution of core and non-core income</li> <li>• Growth in income and profits</li> <li>• Strength of underlying profits</li> <li>• Profitability ratios</li> <li>• Interest margins</li> <li>• Cost efficiency</li> <li>• Investment portfolio</li> </ul> | <ul style="list-style-type: none"> <li>• Pre-tax profit / Average total assets</li> <li>• Pre-tax profit / Average risk-weighted assets</li> <li>• Pre-tax profit / Average shareholders' funds</li> <li>• Net interest income / Average total assets</li> <li>• Non-interest income / Average total assets</li> <li>• Cost / Income</li> <li>• Dividend payout</li> </ul> |

An important factor in assessing the long-run viability of any organisation is its earnings/profitability. Analysis of earnings quality attempts to evaluate the FI's profitability and how well it utilises available resources to generate returns. The analysis will focus on the composition of the FI's income and contributions from its core and non-core activities.

Various ratios are analysed at different levels to determine the ability of the FI to create value to shareholders' funds. In addition, it is a useful quantitative measure of the management's past performance in the critical areas of asset quality, cost control and income generation.

The analysis will cover the level of income that is sustainable in the future and the underlying strength of the FI's profitability. Underlying profitability can be affected by, amongst other things, recoveries of non-performing loans and the level of provisioning. A high level of recoveries would overstate an FI's profitability while provisioning above the legal requirement would understate its profitability.

# L

## LIQUIDITY & FUNDING

| Factors Considered   | Key Financial Ratios   |
|--|--|
| <ul style="list-style-type: none"> <li>• Composition of funds (customer vs other types of deposits)</li> <li>• Growth in deposits</li> <li>• Liquid assets in relation to financing commitments and maturing deposits</li> <li>• Reliance on stable funds</li> <li>• Reliance on large depositors</li> </ul> | <ul style="list-style-type: none"> <li>• Liquid assets / Customer &amp; short-term funds</li> <li>• Net loans &amp; advances / Customer deposits</li> <li>• Net loans &amp; advances / Stable funds</li> <li>• Customer deposits / Total interest-bearing funds</li> </ul> |

Assessment of an FI's funding and liquidity position focuses on its ability to raise funds to overcome short-term difficulties. A high level of liquidity can keep funding lines open for a weak FI that is in financial distress, and provides financial support to capitalise on available opportunities.

The liquidity of an FI depends on its ability to meet daily expenses and satisfy demands for deposit withdrawals while keeping its assets funded. On a longer-term basis, this is measured by the degree to which core assets are funded with stable liabilities. A capital-impaired FI can remain liquid, which clearly suggests that satisfactory liquidity alone is not an indication of the financial health of an FI. Nevertheless, satisfactory liquidity is a characteristic of a healthy FI. There are primarily 3 components to an FI's liquidity: its expected cash flow, its capacity to borrow in the inter-bank market, and its stock of readily realisable high-quality liquid assets. Liquidity management is primarily directed towards ensuring that the asset structure is liquid enough to provide room for the FI to manoeuvre in meeting the short-term demands of depositors and borrowers.

Funding is basically looked at from the deposit structure of an FI. A large retail deposit base generally gives rise to stable funding while a high amount of wholesale deposits is generally viewed as unstable. Of equal importance is the evaluation of the FI's market position vis-à-vis deposit taking and its reliance on large depositors, to determine if the movement of funds by these large depositors would create a large enough vacuum to render the FI illiquid.

### **Asset-Liability Management**

The asset-liability management of an FI is normally assessed through the effectiveness of its treasury operations. Analysis will focus on understanding the role and function of the asset-liability management committee ("ALCO") and the effectiveness of the FI's risk management system in controlling these risks.

Critical to the analysis is the balance between the FI's interest-sensitive assets and liabilities. The management of off-balance sheet activities, covering interest rate-sensitive and foreign exchange-sensitive products, is also analysed. Factors considered include the matching of its funds and the maturity structure of its loans and deposits. Interest rate sensitivity on both loans and deposits is examined to evaluate the impact of interest rate movements on its profitability, while foreign exchange risk is analysed to determine the FI's risk tolerance.

## **S**PECIAL RISK OF BANK HOLDING COMPANIES

---

The principal assets of a bank holding company (“BHC”) generally comprise equity investments in banking institutions and non-bank FIs. So long as the BHC’s investments in its subsidiaries are financed through debt, the BHC is said to be double-leveraged. This means that the BHC’s equity is geared once at the company level, and again at the subsidiary level through debt-financing by the subsidiary. There are several risks associated with double-leveraging.

Firstly, dividends from subsidiaries may not be sufficient to service the interest and maturing principal of a parent company’s debt. Additionally, regulations may exist that prohibit payment of dividends from subsidiary to parent.

Secondly, the BHC’s financial flexibility could be negatively impacted as a result of using debt to finance an investment that may not be liquid.

The third risk is that should any of the banks (or FIs) or other subsidiaries in the group become insolvent, the BHC’s claims are implicitly subordinated to those of the FI’s creditors with respect to the principal assets of the consolidated group.

An important consideration when analysing the fundamentals of a BHC is that a problem of an affiliate within the group may have a negative impact on the other entities within the group.

During the course of assessing these risks, the analyst will evaluate the subsidiaries’ credit quality. Essentially, the evaluation of the banking subsidiaries’ credit quality involves conducting an FI-specific analysis. The objective of the analysis is to predict the stability of the FI’s earnings potential because the main source of revenue for a BHC generally stems from dividend and interest income from its banking (or FI) subsidiaries. The analyst will attempt to predict the likelihood of regulatory intervention in relation to dividend upflows, in attempts to conserve the FI’s capital. This again would depend on the analysis conducted on the FI’s business and financial risk profile.

Cash flow analysis is an important consideration in the assessment of a BHC’s risk profile. Is there sufficient upstream dividend and interest income to cover the BHC’s operating overheads, to service interest or principal obligations, and to make dividend payments? The analyst will examine the BHC’s cash flow requirement and the ability of its banking subsidiaries to support this need through dividend income or alternative sources.

The analysis also covers an assessment of the liquidity profile of the BHC in the event of financial distress. Here, important factors are: financial flexibility in the form of financing options available to an institution under stress; and shareholders’ support in the form of adequate financial resources and willingness to provide support during difficulties.

## **S**PECIAL RISK OF MERCHANT/INVESTMENT BANKS

---

Overall, the bigger picture of assessing an investment bank is not dissimilar to that for a commercial bank. However, the focus is different, given the contrasts in the key business activities of investment banks vis-a-vis commercial banks.

At the outset, it seems that merchant or investment banks may have less inherent risks with fewer loan assets (thus less capital requirements), and tend to have **more liquid balance sheets** (with significant exposure to marketable securities). Nonetheless, we should also be mindful that investment banks may be **exposed to more market risks**, via their exposures to these instruments which are highly sensitive to market movements. In this aspect, assessment of investment banks' risk management procedures becomes imperative.

### **Asset Quality**

In terms of asset quality, the traditional assessment of non-performing loans and credit costs will now take a back seat as the bulk of the investment banks' assets currently comprise investment and dealing securities.

Analysing the trend in an investment bank's asset composition gives an indication of the activities it undertakes. In some cases, treasury assets have superseded loan assets as the dominant asset class in an investment bank's balance sheet. In addition, OBS exposures have also grown in absolute values, particularly for interest rate-related contracts. Therefore, analysis should focus on these key areas instead of loan assets. In this regard, assessment of the investment bank's securities portfolio is essential, particularly its quality.

To further complement asset quality assessment, an overview of the risk management framework adopted by the investment bank is also essential. The overall and specific policies and risk management tools the particular investment bank uses form the backbone of the analysis. We should be satisfied with whether the risk management framework has clearly defined objectives and a proper structure, the existence of comprehensive policies and risk management tools, as well as the investment bank's compliance with and adherence to such policies.

On the other hand, there is also a need to gauge the investment bank's risk appetite vis-a-vis its activities. We have to be comfortable with the identified risk parameters and it needs to show strict compliance by operating within these boundaries.

**Capital Adequacy**

As most local investment banks gradually shift from lending to fee-based activities, this has indirectly resulted in substantially higher RWCARs; corporate advisory activities attract minimal capital requirements, if any. In this instance, we believe the more critical assessment should be on risk management, which covers a broad spectrum of risks (including market, operational, credit and liquidity), which the current RWCAR is unable to capture entirely (i.e. it only covers the credit aspect at this point). As such, BASLE II's proposal to have a more refined way of determining RWCAR will definitely provide a more complete picture from the perspective of risk-related capital.

**Performance**

Investment banks' profits are likely to be more volatile than those of commercial banks. Without a stable net interest income (or a much smaller quantum compared to a commercial bank), analysis of an investment bank's earnings would primarily be based on non-interest income, i.e. fee and investment incomes.

Given this, we need to be able to determine the cause of the volatility in earnings. The starting block of performance analysis is to assess the composition of an investment bank's income. In this regard, franchise and market position are the critical factors for sustainable fee income. Further analysis of various fee income compositions must also be carried out to appreciate the strength of the investment bank's fee-generating capacity. Fee-based income, although dependent on the business environment to a certain extent, is generally perceived as being more stable in comparison to investment income.

The other key component of non-interest income is investment income. The ability to consistently earn a sizeable investment income is closely linked to the competency of the investment bank's treasury team. Even so, treasury income is more volatile as it is tied to the bank's risk appetite. The main risk areas are market risk and, to a smaller extent, credit risk. To this end, it is crucial to analyse the bank's treasury activities to ascertain the sustainability of its bottom line.

**Funding and Liquidity**

Most investment banks will have reasonably liquid asset profiles. The advantage of having more treasury assets in an investment bank's books (in comparison to its commercial counterpart, which has a bigger proportion of loan assets) is that these treasury assets can be liquidated easily. Even so, we acknowledge that the disposal of treasury assets may result in losses for an investment bank as this would depend on the prevailing market prices at that juncture.

**Franchise**

Franchise is deemed an important factor when determining an investment bank's ability to sustain its fee income. While there is no fool-proof method to evaluate a bank's franchise, our approach is

centred around its ability to consistently and successfully make sales pitches on corporate advisory and capital market activities. A broad indication in this regard is its market share relative to the industry's performance as well as its peers'.

### **Management Assessment**

In most instances, the business activities of an investment bank are derived from the management's expertise and capability rather than branch network or products, as in the case of a commercial bank. Given this, human capital becomes a crucial element when appraising an investment bank.

## **S**PECIAL RISK OF FINANCE COMPANIES

---

**Generally, the assessment of a finance company is very similar to the way RAM Ratings assesses commercial banks.** The only difference is that finance companies take more consumer finance risks, such as hire-purchase loans, compared to typical commercial banks.

## **S**PECIAL RISK OF DEVELOPMENT BANKS

---

The primary objective of development banks is to promote social objectives, as dictated by the authorities. Because of this, profit maximisation and risk diversification may not necessarily be the guiding principles behind their business operations.

**Overall, the bigger picture of assessing a development bank is not dissimilar to that for a commercial bank.** Despite the perceived riskiness of developments, such entities are typically owned or controlled by the Government. In this instance, the strength of Government ownership is also considered.

**RAM RATINGS' CREDIT RATING DEFINITIONS  
(Financial Institutions)**

RAM Ratings' rating of a financial institution is an assessment and current opinion on the strength and performance of the rated institution.

---

**LONG-TERM RATINGS**


---

|  |   |
|--|---|
| <b>AAA</b>                               | Financial institutions rated in this category are adjudged to offer the highest safety for timely payments of financial obligations. This level of rating indicates entities with strong balance sheets, favourable credit profiles and consistent records of above-average profitability. Their capacities for timely payments of contractual financial obligations are unlikely to be impacted seriously by any foreseeable changes in economic conditions.   |
| <b>AA+</b><br><b>AA</b><br><b>AA-</b>    | Financial institutions rated in this category are adjudged to offer high safety for timely payments of financial obligations. This level of rating indicates entities with sound credit profiles and without significant problems. Entities rated in this category are, however, considered to be somewhat more vulnerable to adverse changes in economic conditions than those entities rated in the highest category. The signs plus (+), flat and minus (-) indicate that the financial institution ranks at the higher, mid or lower end within this generic rating category respectively.  |
| <b>A+</b><br><b>A</b><br><b>A-</b>       | Financial institutions rated in this category are adjudged to offer adequate safety for timely payments of financial obligations. This level of rating indicates entities with adequate credit profiles, but which possess one or more problem areas, giving rise to the possibility of future riskiness. Entities rated in this category have generally performed at industry average and are considered to be more vulnerable to changes in economic conditions than those rated in the higher categories. The signs plus (+), flat and minus (-) indicate that the financial institution ranks at the higher, mid or lower end within this generic rating category respectively. |
| <b>BBB+</b><br><b>BBB</b><br><b>BBB-</b> | Financial institutions rated in this category are adjudged to offer only a moderate degree of safety for timely payments of financial obligations. This level of rating indicates entities which have been significantly underperforming in some areas. These entities are, however, considered to have the capability to overcome such problems in the short term, though adverse changes in economic conditions could impair their ability to make timely payments of financial obligations. The signs plus (+), flat and minus (-) indicate that the financial institution ranks at the higher, mid or lower end within this generic rating category respectively.               |
| <b>BB+</b><br><b>BB</b><br><b>BB-</b>    | Financial institutions rated in this category are adjudged to lack key protection factors, which could result in inadequate safety for timely payments of financial obligations. This level of rating indicates that the entities may need certain favourable economic changes in order to meet financial obligations in a timely fashion. The signs plus (+), flat and minus (-) indicate that the financial institution ranks at the higher, mid or lower end within this generic rating category respectively.   |
| <b>B+</b><br><b>B</b><br><b>B-</b>       | Financial institutions rated in this category are adjudged to be of high risk. Timely payments of financial obligations are impaired by serious problems which the entities face. Whilst entities rated in this category might be currently meeting obligations on time, continuance of this would depend upon favourable economic conditions or some degree of external support. The signs plus (+), flat and minus (-) indicate that the financial institution ranks at the higher, mid or lower end within this generic rating category respectively.  |
| <b>C+</b><br><b>C</b><br><b>C-</b>       | Financial institutions rated in this category are adjudged to be of very high risk in relation to timely payments of financial obligations. This level of rating indicates entities with very serious problems and, unless external support is provided, they would be unable to meet their financial obligations in a timely fashion. The signs plus (+), flat and minus (-) indicate that the financial institution ranks at the higher, mid or lower end within this generic rating category respectively.   |
| <b>D</b>                                 | Financial institutions rated in this category are either currently in default or expected to be in default, whether or not formally declared. This level of rating indicates that the entities are unlikely to meet maturing financial obligations, which calls for immediate external support of a high order.   |

---

**SHORT-TERM RATINGS**

---

- P1** Financial institutions in this category have superior capacities for timely payments of obligations.
- P2** Financial institutions in this category have strong capacities for timely payments of obligations.
- P3** Financial institutions in this category have adequate capacities for timely payments of obligations. The ability to honour the obligations is more vulnerable to adverse changes in business, economic or financial conditions.
- NP** Financial institutions in this category have doubtful capacities for timely payments of obligations.

**Analyst** **Phone**

Prakash Jerome +9411 2553089

## **RATING METHODOLOGY: FINANCIAL INSTITUTIONS' RATINGS**

No statement in this methodology is to be construed as a recommendation to buy, sell or hold securities, or as investment advice, as it does not comment on the security's market price or suitability for any particular investor.

While every effort has been made to incorporate the salient points of RAM Ratings' experience in relation to the methodology, we note that the information contained could be updated and altered depending on changes in our internal views, market conditions, accounting practices and regulations. The methodology is also based on factors relevant to Malaysia and may require adaptation to local conditions.

Published by RAM Ratings (Lanka) Ltd. Reproduction or transmission in any form is prohibited, except by permission from RAM Ratings

