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## METHODOLOGY FOR ASSIGNING CORPORATE CREDIT RATINGS (NON-FINANCIAL NON-HOLDING COMPANIES) – SHORT VERSION

**The Methodology presented is a short public version.**

### 1. General definitions

**Credit rating** of a company represents the opinion of Rating-Agentur Expert RA GmbH on the ability of the company to fulfill its financial liabilities to the full extent and in a timely manner, *taking into account external stress- and support-factors*.

**Stand alone credit rating** of a company represents the opinion of Rating-Agentur Expert RA GmbH on the ability of the company to fulfill its financial liabilities to the full extent and in a timely manner, *without taking into account external stress and support-factors*.

This methodology is used to assign ratings to **non-financial non-holding companies** (by defining in which creditworthiness class the company belongs to).

The level of creditworthiness of the company must be assessed as equal to the level of creditworthiness of another entity<sup>1</sup> in the following cases:

- The company's creditworthiness must be assessed based on the financial statements of the parent company, if the following conditions are satisfied:
  - the company raises funds in the bond market where the parent company is located
  - the parent company is a guarantor of the rated company's obligations
- The company's creditworthiness must be assessed based on the financial statements of the subsidiary company, if the following conditions are satisfied:
  - the company does not carry out operating activity
  - the company owns stocks or shares in the authorized capital of only one subsidiary "operating" company, and its share in the ownership structure exceeds 95%
  - consolidated financial statements are not prepared;
  - the amount of debt not translated to the level of the subsidiary, does not exceed 10% of the equity

The main users of the rating are creditors. Other users are investors and counterparties of the company whose interest is focused on the possibility of full and timely fulfillment of the company's liabilities, as well as the company's prospects for fulfillment of new liabilities (taking into account possible changes in the economic environment).

The rating assessment of the company can be used for organizing and conducting tenders.

The rating is also useful for managers of the company and its founders as an indicator of the management performance.

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<sup>1</sup> In exceptional cases, the rating can be assigned on the basis of the company's own financial statement even if indicated conditions are satisfied.

## 2. Sources of information

2.1 While assigning a rating score, the following sources of information are used:

- Standard questionnaire
- Forms of financial statements № 1, 2, 3, 4, 5 (according to RAS) for three completed years
- Forms of financial statements № 1, 2 (according to RAS) as of the last reporting date
- Consolidated financial statements according to IFRS or US GAAP with auditor reports for the last three completed years, and as of the last reporting date (if any)
- Market researches for the key markets for the rated company prepared for the last 12 months (if any)
- Description of the organizational structure in form of a chart
- Officially approved company's development strategy or excerpt from this document with key quantitative and qualitative indicators
- Forecasted cash flow for the next 2 years, broken down by quarters
- Appraiser's report on the value of fixed assets, portfolio of securities and other assets, prepared not earlier than 3 years ago

2.2 The Rating Agency does not control the correctness of accounting and statistical forms, and the reliability of information included in these forms.

2.3 The Agency shall contact the company for an explanation of the indicators provided in the financial statements and questionnaire. If differences between internal statements and official reporting forms are found, the Agency shall prioritize the analysis of the internal statements. The presence of these differences is considered as an additional risk factor.

2.4 The Agency has the right to use other sources of information in case of data incompleteness.

### 3. Structure of the rating analysis

3.1 The creditworthiness analysis of the company has several levels. The final **credit rating** of the company is the assessment of the company’s creditworthiness taking into account support- and stress-factors, which have external nature. The **stand alone credit rating** is based on the analysis of company’s **financial stability** taking into account only support- and stress-factors, which have internal nature.

3.2 The analysis of the company’s **financial stability** includes analysis of three sections: business risk analysis (1), financial risk analysis (2) and corporate risk analysis (3). Each section is divided into several large integral factors.

3.3 Several indicators are assessed within the framework of the analysis of each integral factor. Indicators within each integral factor may be equal to one of the following values:

1	The factor (indicator) has a positive influence on the creditworthiness level
0,5	The factor (indicator) has moderately positive influence on the creditworthiness level
0	The factor (indicator) has neutral influence on the creditworthiness level
-0,5	The factor (indicator) has moderately negative influence on the creditworthiness level
-1	The factor (indicator) has a negative influence on the creditworthiness level

3.4 The score for each integral factor is determined as a sum of scores for separate indicators within a group being weighted in a certain manner. Weights of each section are provided in the **List of indicators and corresponding weights** (see Annex 2).

3.5 The rating score is determined as a weighted sum of scores of all integral factors.

3.6 To determine the **stand alone credit rating of the company**, the rating score must be adjusted taking into account internal support- and stress-factors. To determine the **credit rating of the company**, the rating score for stand alone credit rating must be adjusted taking into account external support- and stress-factors (positive and negative external influence of the owners and the government) (see Part 5).

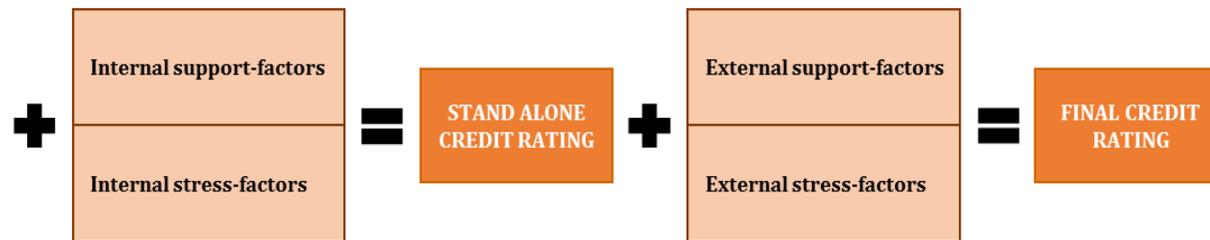
3.7 The ratings assigned in accordance with the national scale (both stand alone and final) shall be transferred to the international scale through the adjustment for Country credit environment rating (CCE) in foreign currency (according to the “Instruction for transferring rating from national to international scale”). Rating-Agentur Expert RA GmbH publishes **only final ratings in accordance with the international scale** (stand alone rating may be published only upon specific request from the rated entity).

**Logic scheme:**

Business risk analysis
Degree of business diversification
Growth prospects and trends in key sales markets
Trends of the company's business volume
Investments in fixed assets
Relations with the counterparties

Financial risk analysis
Dynamic of assets
Accounts receivable
Equity
Liquidity
Accounts payable
Debt load
Profit and profitability
Cash flow analysis
Currency risks

Corporate risk analysis
Owners
Current decision-making practices
Efficiency of relations with subsidiaries and affiliated entities
Degree of information disclosure
Quality of strategic business planning
Risk management organization
Insurance coverage



#### **4. System of Indicators**

##### 4.1 Business risk analysis:

- Degree of business diversification
- Growth prospects and trends on key sales markets
- Trends of the company's business volume
- Investments in fixed assets
- Relations with counterparties

##### 4.2 Financial risks analysis:

- Dynamics of assets
- Accounts receivable
- Equity
- Liquidity
- Accounts payable
- Debt load
- Profit and profitability
- Cash flow analysis
- Currency risks

##### 4.3 Corporate risks analysis:

- Owners
- Current decision-making practice
- Efficiency of relations with subsidiaries and affiliated entities (SA)
- Degree of information disclosure
- Quality of strategic business planning
- Risk management organization
- Insurance coverage

## 5. Rating score adjustments

5.1 To determine the **stand alone credit rating of the company**, the rating score must be adjusted taking into account internal support- and stress-factors. To determine the **credit rating of the company**, the rating score for stand alone credit rating must be adjusted taking into account external support- and stress-factors (positive and negative external influence of the owners and the government).

5.2 In case of identifying a moderate internal stress-factor (internal support factor) the rating score can be reduced (increased) by half of a rating level (10 points). In case of a strong internal stress-factor (internal support factor) the rating score can be reduced (increased) by one rating level (20 points). The following internal stress- and support factors are used for rating score adjustments:

### Internal stress factors:

- Funds in "troubled" banks<sup>2</sup>
- Effect of non-monetary transactions
- Short period of the company's existence
- Influence by debt burden
- Poor asset quality
- Other stress factors (according to the expert's opinion there are some facts which are not considered in the methodology but which can have a moderate/ strong negative effect on the company's stand alone creditworthiness)

### Internal support factors:

- Market position (the company is included in the Ranking "Expert 400" from RAEX (Moscow) (open source<sup>3</sup>) and the company is included in the list of "Strategic Russia enterprises<sup>4</sup>")

5.3 External stress-factor (external support factor) is a factor which is not directly connected with the financial condition of the company, but it is able to have a significant negative (positive) impact on the level of the company's creditworthiness. In case of identifying a moderate external stress-factor (external support factor) the rating score can be reduced (increased) by half of a rating level (10 points). In case of an external strong stress-factor (external support factor) the rating score can be reduced (increased) by one rating level (20 points). The following internal stress- and support factors are used for rating score adjustments:

### External stress factors:

- Influence by the owners
- Other stress factors (according to the expert's opinion there are some facts which are not considered in the methodology but which can have a moderate / strong negative effect on the company's creditworthiness)

### External support factors:

- Support from the government
- Support from the owners

<sup>2</sup> Banks which have credit rating at the "B++" level or below according to the national scale from RAEX (Moscow) (or with comparable rating from another rating agency with good reputation), or banks without rating.

<sup>3</sup> [http://raexpert.org/related\\_activities/researches/expert400/](http://raexpert.org/related_activities/researches/expert400/)

<sup>4</sup> This list was developed by the Government Commission on Sustainable Development of the Russian economy in February 2015. The List includes 199 enterprises. The Organizations included in the list have a priority for government support in case of economic crisis or financial problems.

## Annex 1. List of indicators and corresponding weights

Factor	Weight
<b>I. Business risks analysis</b>	<b>20,0%</b>
Degree of business diversification	
Growth prospects and trends on key sales markets	
Trends of the company's business volume	
Investments in fixed assets	
Relations with counterparties	
<b>II. Financial risks analysis</b>	
Dynamics of assets	
Accounts receivable	
Equity	
Liquidity	
Accounts payable	
Debt load	
Profit and profitability	
Cash flow analysis	
Currency risks	
<b>III. Corporate risks analysis</b>	<b>20,0%</b>
Owners	
Current decision-making practice	
Efficiency of relations with subsidiaries and affiliated entities (SA)	
Degree of information disclosure	
Quality of strategic business planning	
Risk management organization	
Insurance coverage	
<b>IV. Internal stress-factors*</b>	
Funds in "troubled" banks	
Effect of non-monetary transactions	
Short period of company's existence	
Influence from debt burden	
Poor asset quality	
Other stress factors	
<b>V. Internal support factors*</b>	
Market position	
<b>TOTAL - STAND ALONE RATING</b>	
<b>VI. External stress-factors*</b>	
Influence by the owners	
Other stress factors	
<b>VII. External support factors*</b>	
Support from the government	
Support from the owners	
<b>TOTAL - FINAL CREDIT RATING</b>	

\*See Point 5 "Rating score adjustment" in the description above.