Rating Methodology

Group Rating Methodology

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This criteria is an update of the Group Rating Methodology published on 13 January 2021, with additional details on how TRIS Rating assigns ratings to an insurance group member (see "Rating an insurance group member" below).

OVERVIEW AND SCOPE OF THE CRITERIA

The criteria apply to entities that are part of corporate and financial institution groups, where we recognize the likelihood of the group or parent company providing extraordinary financial support on a timely basis to mitigate the default risk of the entities or exert influence through negative intervention on the entities due to the importance of the entities to the group. The criteria may apply to other forms of relationship between the entities and the group such as dedicated supplier-purchaser structures. The criteria supplement other sector-based rating methodologies announced by TRIS Rating and supersede our "Group Rating Methodology" published on 10 July 2015.

METHODOLOGY

The process involves the steps shown in the framework below.

Group Rating Framework

Identify group structure / relations between relevant group member and parent (the group)

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Assign group stand-alone credit profile (group SACP) and Group Credit Profile (GCP)

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Determine group status of relevant group member

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Assign SACP to the group member, if required

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Assign ICR to the group member

The process starts with an assessment of the group structure and the relations among the relevant group members with their immediate group parent and/or ultimate parent (collectively referred to as the "group"). We then assign a group stand-alone credit profile (group SACP) and GCP to the group as if it were a single entity. The group SACP is defined as the group's creditworthiness in the absence of extraordinary support (or negative intervention). Generally, the group SACP is equalized to the GCP. However, if we believe that there is potential for extraordinary support (or negative intervention) available to the group, the GCP could be higher (or lower) than the group SACP. The next step is to assess the group status by evaluating the importance of the relevant member to the GCP. Depending on the assessed group status, we may assign a stand-alone rating (the Stand-Alone Credit Profile, SACP) to the relevant group member, based on industry-specific rating criteria, as a rating component to determine the Issuer Credit Rating (ICR) or the final rating.

Identify group structure and relations among group members

We define "the group" as the group parent, which includes the immediate parent and/or ultimate parent, and the group members or the entities over which the group parent has direct or indirect control or influence on strategy, operations, cash flows and resources as well as the group members' creditworthiness. Such control or support may exist even if the parent owns less than 50% of the group members' equity. Determinants of control, other than ownership, may include the parent's representation on the group members' board of directors or management, ability to direct the flows of capital or cash, funding and liquidity, risk management integration, as well as sharing of brand name or reputation risk. In addition, the parent may provide explicit support via formal channels, such as letters of guarantee or cross-default provisions.

Assign Group Credit Profile

After we identify the group structure and relations among the group members and the parent, we assess the group's overall creditworthiness or the Group Credit Profile (GCP) by assessing the credit risk of the group on a consolidated basis as though the group were a single entity.

GCP represents a rating component that forms a basis for the assignment of the group members' ICRs based on our view of their status relative to the parent. The ICR of a group member could be equal to the GCP if its SACP is higher or equal to the GCP, regardless of the group status. If the group member's SACP is lower than the GCP, its SACP could only be enhanced by up to one notch below GCP (GCP -1). In rare cases, the ICR could be higher than the GCP if the group member is insulated from the group, i.e. there is a restriction that prevents the group or parent from directing the member's resources to support the parent or other members within the group. The GCP can range from 'aaa' to 'd' and is on the same rating scale as that of the ICRs, which rank from 'AAA' to 'D'. Like the ICR, the GCP can be modified with ' + ' or ' - '.

The rating criteria to be applied in determining GCP are the same as those applied under our industry-based criteria for corporates, banks, non-bank financial institutions (NBFIs), securities companies, savings cooperatives and insurers. The criteria to be applied for a group with multi-sector operations are dictated by the sector/industry that we believe best represents the credit profile of the consolidated parent. The benchmarks to consider can be revenue, capital, earnings, cash flow, dividend contribution or other factors we deem most relevant. For example, we may apply "Corporate Rating Methodology" to a corporate business group even though the group has subsidiaries engaging in financial services with sizeable revenue contributions to the group. For a group with subsidiaries engaging in diverse business operations that are equally important to the group, we may assign a SACP to each subsidiary using applicable sector-specific criteria respective to each subsidiary and then combine the SACPs to derive the GCP.

We may also incorporate potential extraordinary support or negative intervention from external sources other than the immediate group parent into the GCP, if applicable. This could be the situation where other group members with strong credit profiles, other than the immediate parent, have the capacity and propensity to provide formal financial support, such as letters of guarantee or other forms of explicit support, directly to the relevant group members.

In some cases, the GCP may be constrained by the sovereign rating we assign to a specific country based on our "Sovereign Credit Rating Methodology". This would be the case where the group primarily operates in a country in which the sovereign rating assigned by us is at a level lower than the GCP.

Determine group status of a group member

We evaluate the status of a group member in relation to the group based on six key aspects:

(1) the likelihood of the relevant group member being divested by the parent

(2) the commitment from the group parent to provide support

(3) the level of integration with the group

(4) operating performance of the relevant group member

(5) revenue or cash flow contribution from the relevant group member to the group

(6) the relevant group member's potential impact on the group's reputation.

Note that the assessments are based on our opinions which are founded on various sources. These may include, for instance, evidence of formal support, track records of past financial support, company data, corporate communications, and discussions with management.

We categorize the group status into "Core", "Highly strategic", "Strategically important", "Strategic" and "Non-strategic". Our evaluation, based on the six key aspects above, will determine which category of group status is most applicable to the group member.

Core entity

A "Core" entity is expected to be strongly integrated with the group in terms of business strategy or functions, such as financing and risk management, and in some cases serves the same customer base or target markets. Thus, it is highly likely the entity will remain a long-lasting crucial member of the group. There is evidence of strong, long-term commitment to provide extraordinary support on a timely basis from top management or major shareholders if the core entity is under financial stress. A cross-default provision on the obligations of both the parent and the entity provides a good example. The entity is able to achieve the group's performance targets. It also operates in line with the group's strategy and contributes a significant portion of its revenue or cash flows to the group or parent. There must be close association with the group through a shared brand name and reputation risk. For most cases, the entity has been in operation more than five years or has been set up as a separate legal entity for special functions, e.g. as a treasury center of the group, or for specific purposes, e.g. tax or regulations.

Highly strategic entity

A "Highly strategic" entity is a crucial member of the group. It shares most characteristics of the "Core" entity. There is sufficiently strong, long-term commitment from management to provide extraordinary support, but this may be to a lesser degree than in the case of a "Core" entity. An example is issuance of a letter of guarantee or some form of formal support, rather than a cross-default provision. The contribution in terms of revenue or cash flows may still be significant, e.g. at least 20% of the group's total revenue or EBITDA, but may not be as high as that of the "Core" entity. In some cases, its revenue contribution may not be meaningful or financial performance may not be as strong but it still performs its role to meet certain strategic objectives of the group. Also, a "Highly strategic" entity may or may not share the same brand name, but the linkage is close enough that its reputation has a direct bearing on the group. Lastly, the entity should have been in operation more than five years or was otherwise set up for special purposes.

The ICR of the "Highly strategic" subsidiary is usually one notch below the GCP. However, if its SACP is equal to or higher than the GCP, the ICR will be at the same level as the GCP. As with the "Core" entity, we may or may not assign a SACP to the entity depending on whether or not the integration and group support are strong enough to suggest that its credit risk is more likely to be aligned with the group's credit profile than its own.

Strategically important entity

A "Strategically important" entity is likely to remain an important member of the group for the foreseeable future. The entity is important to the group's long-term strategy but may be less integral with the group in some respects compared to a "Core" entity or "Highly strategic" entity. The entity has a commitment from management to provide long-term support or is part of the group's financing strategy and operations. Revenue or cash flow contribution to the group is one factor to consider but not as important as the integration with the group's operations or reputation. The revenue or cash flow contribution may be less than that of a "Highly strategic" entity, e.g. representing at least 10% but less than 20% of the group's total revenue or EBITDA. Sometimes the contribution may not be considered significant if it is a subsidiary of a large conglomerate or a major multi-national corporation. The entity may or may not share the brand with the parent but is strongly linked to the group's reputation.

Strategic entity

A "Strategic" entity is considered important to the group for the foreseeable future, similar to a "Strategically important" entity. Therefore, it also needs to have long-term commitment from management to provide support, if needed. Its products or services complement the group's diversification strategy. Its revenue contribution to the group is considered small relative to other key entities within the group. The entity is less integral with the group than a "Strategically important" entity. For example, its overall strategy or risk management may be aligned with the group's, but it is more independent with respect to financing or operations. However, for an entity to be viewed as a "Strategic" entity, there needs to be evidence that the parent has control over the entity, based on the determinants of control discussed in the "Identify group structure and relations among group members" section. Meanwhile, long-term funding or financial support from the group is available but is often less committed.

Non-strategic entity

An entity is considered "Non-strategic" if it exhibits none of the characteristics described in other categories of group status.

Group status based on key aspects

	Core	Highly strategic	Strategically important	Strategic	Non-strategic
Unlikely to be sold	Highly unlikely	Highly unlikely	Unlikely	Unlikely	
Strong, long-term commitment from the parent/ major shareholders to provide timely support if needed	Strong, long-term	Long-term	Long-term	Long-term	
Integral with group's business/functions, risk management, financing, target customers	Highly integral	Highly integral	Less integral than "Highly strategic"	Less integral than "Strategically important"	
Performing in line with the group's financial targets	Meet the group's financial targets and strategic objectives	Meet the group's financial targets or at least meet the group's objective	Meet the group's stategic objectives		
Contributing significant revenues/cash flows to the consolidated group parent	Significant contribution	Lower contribution than "Core" but still significant (e.g. EBITDA > 20%)	Lower contribution than "Highly strategic" but still significant (e.g. EBITDA = 10%-20%)		
Linked to the group's reputation, brand or risk management	Closedly linked, share brand name	Linked to the group's reputation	Linked to the group's reputation		
Potential ICR	ICR = GCP	ICR = GCP-1	ICR = SACP+3	ICR = SACP+1	ICR = SACP

Source: TRIS Rating

Assign SACP to a group member

In cases where the SACP is a key rating component, particularly where the group status of a relevant group member is assessed to be "Strategically important" or "Strategic" or "Non-strategic", determining the SACP of the relevant group member will be fundamental to the assignment of the entity's ICR. The SACP is determined in accordance with the sector/industry-specific rating criteria applicable to the relevant group members.

For a “Core” entity or “Highly strategic” entity, we may not assign a SACP to the entity if we believe that the SACP would not be relevant. This would be the case if the entity’s creditworthiness is predominantly influenced by the parent’s to the extent that any change in the SACP has no bearing on the ICR assigned to the entity.

Assign ICR to a group member

We generally assign an ICR to a “Core” entity at the same rating level as the GCP. An exception, where the ICR could be higher than the GCP, is when the “Core” entity’s SACP, if assigned, is higher than the GCP, and the entity is insulated from the group due to restrictions on the flow of capital, funding or liquidity from the entity to the group parent or other group members. This could be the case for an insurance subsidiary of a financial group, for instance.

We typically assign an ICR to a “Highly strategic” entity at one notch below the GCP (GCP-1). As with the case of a “Core” entity, we may not assign an SACP if the business integration of a “Highly strategic” entity to the group and potential group support are assessed to be strong enough to suggest that its credit risk is more likely to be aligned with the group’s credit profile than its own. In cases where we assign a SACP and the SACP is higher than the GCP, the ICR will be set at the GCP level.

We typically incorporate a three-notch enhancement to the SACP of a “Strategically important” entity (SACP+3) and a one-notch enhancement to the SACP of a “Strategic” entity (SACP+1). However, the rating enhancement will be capped such that the ICR or final rating will not be higher than one notch below the GCP (GCP-1). An exception is when the entity’s SACP is higher than the GCP, in which case the ICR could be at the same level as the GCP. Therefore, in some cases, the actual rating enhancement could deviate from that suggested by the group status, or there may not be any enhancement at all if the SACP is already at a level of one-notch below the GCP.

RATING AN INSURANCE GROUP MEMBER

Insurance subsidiary of financial group

TRIS Rating considers an operating insurance subsidiary of a financial group in Thailand as an insulated entity due to the strong regulatory restrictions preventing the entity from supporting the group. This allows the insurer’s Financial Strength Rating (FSR) and ICR to be rated above the GCP in cases where the insurer’s SACP is higher than the GCP. We would typically assign FSR and ICR higher than the GCP by up to two notches, provided that the insurer’s SACP is also higher than the GCP by at least two notches. When the SACP is equal to the GCP or only one notch above the GCP, the FSR and ICR will be assigned at the same level as the SACP. When the SACP is below the GCP, and we expect the insurer to receive extraordinary support from the group, we may equate its FSR and ICR to that of the GCP.

Holding company of insurance group

The ICR assigned to the holding company of a prudentially regulated financial group is typically one notch lower than the GCP (GCP-1), given structural subordination. As for the holding company of an insurance group, our standard notching is two notches below the GCP (GCP-2) due to the stronger regulatory restrictions on dividend payments from operating insurance subsidiaries to the holding company.

For the notching of an insurance group’s holding company to be narrower or for the ICR to be equal to the GCP, control of dividend payments by the regulator should be substantially weaker compared to other prudentially regulated entities. Also, we would expect the holding company to be able to service its own obligations by: 1) having control over several diversified and independent major operating entities, and each entity should generate substantial earnings or cash flows so that any disruptions at a single entity would not materially impact the group credit profile or the holding company; 2) generating sufficient cash flows from its own operations or from other operating subsidiaries; or 3) maintaining significant amounts of unencumbered cash or a high-grade fixed-income investment portfolio to meet its financial obligations. On the contrary, the notching could be wider than two notches if we have concerns over: 1) risks relating to liquidity or balance sheet position or there is a high degree of double leverage (holding company’s investments in subsidiaries compared with its own equity); 2) risk of tighter regulation on dividend payments from an operating insurance subsidiary; or 3) there exists external support outside of the group that we believe may not be extended to the holding company, in which case the GCP could be higher than the group SACP, and therefore the notching would be from the group SACP instead of the GCP.

METHODOLOGY UPDATE

We have added details on how we assign ratings to an insurance group member, including an insurance subsidiary of a financial group and a holding company of an insurance group. See the “Rating an insurance group member” section.

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