Rating Methodology

TRIS RATING
A Strategic Partner of S&P Global

Sovereign Credit Rating Methodology

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OVERVIEW AND SCOPE OF THE CRITERIA

The criteria describe the methodology TRIS Rating uses to determine a sovereign rating for a government. TRIS Rating assigns a credit rating to a sovereign to reflect our opinion regarding the sovereign's willingness and ability to repay government debts, in full and on time. Government debts in the rating assessment are debts owed to commercial creditors. The assessment does not reflect debts owed to other governments, public-sector enterprises, and other supranational institutions. Quantitative and qualitative risk factors will be assessed to project the present and future repayment risks of the government. Sovereign ratings assigned by TRIS Rating are comparative with the credit risk of the Thai government. They are not compared with the international scale sovereign ratings assigned by international credit rating agencies.

The criteria is applicable to countries in the Asia Pacific region, particularly the country members of the Association of Southeast Asian Nations (ASEAN) with which TRIS Rating has credit rating service exposures.

This article supersedes the rating methodology for "Sovereign Credit Rating" published by TRIS Rating, dated 26 August 2022.

CHANGES TO THE CRITERIA

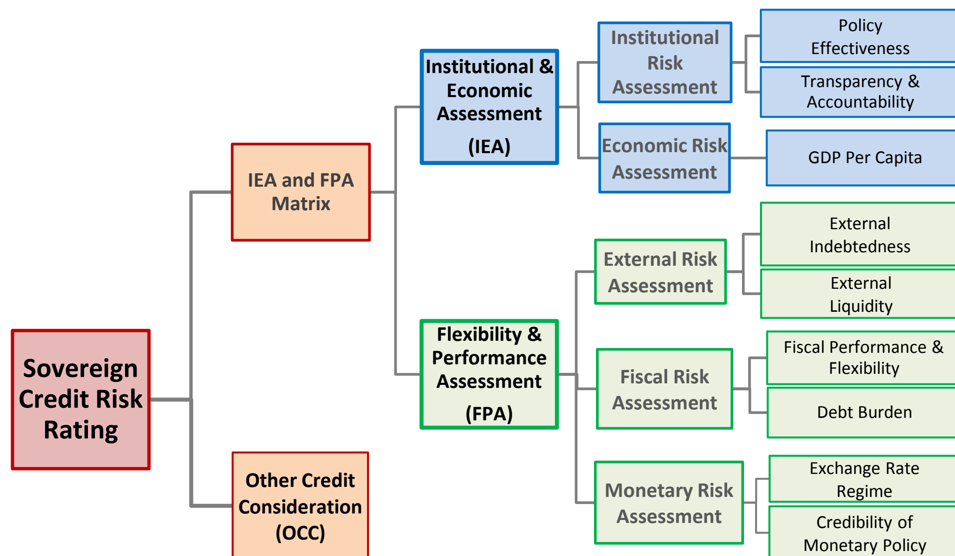
We have made a few adjustments to the previous criteria. Changes are as follows:

Topic	Previous Criteria	Current Criteria
Fiscal Risk Assessment	1. Government Indebtedness 2. Government fiscal management 3. Contingent Liabilities	1. Potential Growth of Government Debts 2. Government Indebtedness
Monetary Risk Assessment Factors	1. Monetary Policy 2. Foreign Exchange Policy 3. Capital Market Development	1. Exchange Rate Regime 2. Monetary Policy Credibility
Modification of Terms	Sovereign Performance Assessment (SPA)	Flexibility and Performance Assessment (FPA)

1. The fiscal assessment includes two factors: 1) potential growth of government debts and 2) government indebtedness. Consideration on the contingent liabilities is now under the government indebtedness.

2. The monetary assessment includes two factors: 1) exchange rate regime, and 2) monetary policy credibility. Consideration on the capital market development is now part of the monetary policy credibility.
3. A slight modification of the term "Sovereign Performance Assessment (SPA)" to "Flexibility and Performance Assessment (FPA)".
4. Overall refinements for better clarity.

KEY RATING FACTORS



The assessment under the Sovereign Credit Risk Rating covers five assessments under two areas: the Institution and Economic Assessment (IEA) and Flexibility and Performance Assessment (FPA), and Other Credit Considerations (OCC). Each of the five risk factors is assessed on a six-point numerical scale from '1' (strongest) to '6' (weakest). These include:

1. Institutional risk factors include institutional frameworks, political and social stability, the continuity and effectiveness of government policies, efficiency of bureaucratic and legal system, transparency, accountability, and governance.
2. Economic risk factors include economic status and standard of living, measured in terms of gross domestic products per capita.
3. External risk factors can be considered by the country's external indebtedness, external debt serviceability, and external liquidity.
4. Fiscal risk factors cover fiscal position, changes in public debts, and public debt burden.
5. Monetary risk factors include exchange rate regime and credibility of monetary policy.

INSTITUTIONAL AND ECONOMIC ASSESSMENT (IEA)

1. Institutional risk assessment

TRIS Rating will primarily consider qualitative factors including political stability, government policies continuity, and effectiveness of bureaucratic system. These factors reflect the rated government's ability to prevent or handle with economic and monetary volatility which could be caused by the country's internal and external factors. Other credit factors comprise the government's economic policies that will support sustainable economic development, sovereign debt

repayment culture, past record regarding government defaults, governance issues, and credibility, reliability and up-to-date regular disclosure of relevant data base and information.

Enforceability and reliability of legal systems, and transparency and accountability of the country's institutions are also major rating factors. In addition, government cooperation with and supports from multinational organizations and creditors, including, but not limit to, International Monetary Fund (IMF), Asian Development Bank (ADB) and World Bank (WB), and any kinds of government-to-government financial assistance, will be considered as supportive credit factors during ongoing stage of country development and during financial crisis.

To understand a country's fundamentals in economic, monetary, financial, and political status, TRIS Rating will arrange meetings with important entities and authorities related to economic, fiscal, monetary, and key economic and real sectors.

2. Economic risk assessment

TRIS Rating will assess the country's structure of the economy and growth prospect and volatility of the economy. The degree of distribution of economic sectors is a major supportive factor in mitigating concentration risk of the economy from downside scenarios of any specific sectors. The economic risk factor is ultimately measured by the country's income level, and gross domestic products per capita (GDP per capita) is the key indicator.

FLEXIBILITY AND PERFORMANCE ASSESSMENT (FPA)

3. External risk assessment

External position indicates the country's status of international transaction performance that can enhance the country's external debt serviceability and external liquidity condition. To estimate the sufficiency of foreign currency to repay external debts and liabilities, the assessment incorporates the size of foreign exchange reserves as a cushion for the country's external debt services, and the country's current account receipts comparing with its net external debts. External liquidity will be considered by comparing gross external financing needs with current account receipts plus foreign exchange reserves.

The assessment also considers current account performance over a sustained period, access to external funding, risks of financial outflows and availability of the country's liquid external assets.

4. Fiscal risk assessment

4.1. Potential growth of government debts. TRIS Rating measures growth in the government debts relative to GDP. This measure captures the fiscal performance, the impact of exchange rates movements, the recognition of contingent liabilities, and other factors not captured in the headline fiscal performance. The assessment takes into consideration the available government liquid assets and government capability to reduce budget deficit to manageable level.

4.2. Government indebtedness. TRIS Rating measures a government's indebtedness using the ratios of public debt as a percentage of GDP and government interest expenses to government revenues. These ratios will be analyzed together with the evaluation of debt structure in terms of currencies diversification (or concentration). Structure of the creditors is another qualitative rating consideration. Public debt structure with the combination of multilateral creditors and/or bilateral loans usually offer lower than market rates and more relax and negotiable credit terms. A large share of foreign-currency and non-resident creditors could expose the government to refinancing risk. Sizable exposure of the banking sector's balance sheet to the government debt could risk crowding out credits available to the private sector.

Contingent liabilities refer to obligations that have the potential to become government debt, or more broadly affect a government's fiscal profile, if they materialize. This includes, for instance, capital injection to troubled financial institutions during a financial crisis or non-financial government-related entities during a distressed scenario.

5. Monetary risk assessment

The monetary assessment reflects our view on the monetary authority's ability to fulfil its mandate in sustaining price stability and a balanced economic growth, while attenuating any major economic or financial shocks. It focuses on the extent to which the monetary authority can execute independent monetary policy and how credible and effective the

monetary policy is in achieving this goal. The assessment also considers the impact of high dollarization, health of the domestic financial sector, and presence of foreign exchange restrictions.

5.1 Exchange rate regime. The exchange rate regime influences a sovereign's ability to have an independent monetary policy tailored to the needs of its domestic economy. Generally, the more actively traded and free-floating the currency, the more accommodating it is for the monetary authority to execute independent monetary policy. the countries that closely peg their currencies with other sovereigns will have limited ability to implement effective monetary policies to handle with domestic economic volatilities.

5.2 Monetary policy credibility. Monetary policy credibility reflects sovereign's ability to maintain a stable price level, which is largely a function of the monetary policy tools and effectiveness, the development of the domestic financial systems and capital markets, perceived independence of the monetary authority, and records of price stability relative to peers.

OTHER CREDIT CONSIDERATIONS (OCC)

In addition to the above-mentioned credit factors for IEA and FPA matrix, there could be other credit considerations (OCC) that, in our view, should be captured in assessing the sovereign credit rating. OCC can be considered in the case that the sovereign is a sustained and projected over/underperformer in its peer group for at least one of the key rating factors, unless already captured elsewhere. We view the change in a particular score as temporary and expect it to be offset (over the medium to long term) by an opposite dynamic in other scores. For instance, deterioration in the external score is stemming from large public investment projects, which we expect, if successful, to improve economic growth potential over the medium term. The other example of OCC is when TRIS Rating has concrete evidence regarding the government's financial flexibility and accessibility during financial stress period.

Negative OCCs include:

- Extremely weak external liquidity and expected to further deteriorate for a sustain basis.
- Extremely weak fiscal position, significantly worse than the weakest benchmark.
- Very high institutional and governance effectiveness risk and high debt burden
- Significant deterioration of credit profiles due to event risks or debt rescheduling risk.

Positive OCCs include:

- Very strong institutional risk assessment and economic risk assessment
- The government is in a net asset position and has very large liquid financial assets

SUFFICIENCY AND RELIABILITY OF DATA BASE

Sufficient, up-to-date, and reliable information and data base are essential to allow TRIS Rating to undergo sovereign credit risk of any specific nations. In general, TRIS Rating will mainly gather data information related to economic and fiscal performance provided by the rated governments.

Other sources of information will be gathered from multinational organization, including the Asian Development Bank (ADB), the International Monetary Fund (IMF), the World Bank (WB) and the ASEAN+3 Macroeconomic Research Office (AMRO). Most of these organizations will provide updated information about economic, financial, and fiscal budget position of member countries on regular basis. The country that does not have reliable data will limit our ability to understand the successful of government policies and our accurate prediction of future risks of the country. TRIS Rating reserve rights to turn down rating service to the country that could not provide sufficient and reliable information.

SOVEREIGN RATING SYMBOLS

Sovereign rating symbols are same as credit rating symbols TRIS Rating assigns to other rated issuers and rated issues. TRIS Rating symbols are classified into AAA, AA, A, BBB, BB, B, C and D. The highest creditworthiness sovereigns will be assigned AAA. The lowest ones will be C. The rating D or 'Default' will be for sovereigns that suspend public debt repayment. The ratings from AA to B may be modified by the addition of a plus (+) or minus (-) sign to show relative standing within a rating category.

KEY FINANCIAL RATIOS

Ratios	Definition
GDP per capita (USD)	Gross domestic products divided by number of population
Debt services/Foreign exchange reserves (%)	Debt services both interest and principal as a percentage of foreign exchange reserves
Net external debts/ Current account receipts (%)	Gross external debts (both public and private) net foreign exchange reserves as a percentage of current account receives. Current account receives are sum of receives from exports of goods and services, and compensation and transfer receipts.
Gross external financing needs/CAR and useable foreign exchange reserves (%)	Gross external financing needs as a percentage of current account receives plus usable foreign exchange reserves. Gross external financing needs are sum of current account payments, foreign currency deposits and public debt services. Current account payments are sum of payments for imports of goods and services, and compensation and transfer payments.
Change in government debt / GDP (%)	Increases or decreases in government debts as a percentage of gross domestic products.
Government interest expenses /government revenues (%)	Government expenditures for interest payments as a percentage of government revenues
Government debts/ GDP (%)	Government debts as a percentage of gross domestic products.

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