Rating Methodology

TRIS RATING
A Strategic Partner of S&P Global

Sovereign Rating Methodology

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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 include government debts and obligations from commercial creditors, excluding debts and obligations at state-owned enterprises. 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.

This article supersedes the rating methodology for "Sovereign Credit Rating" published by TRIS Rating, dated 8 October 2013.

CHANGES OF THE CRITERIA

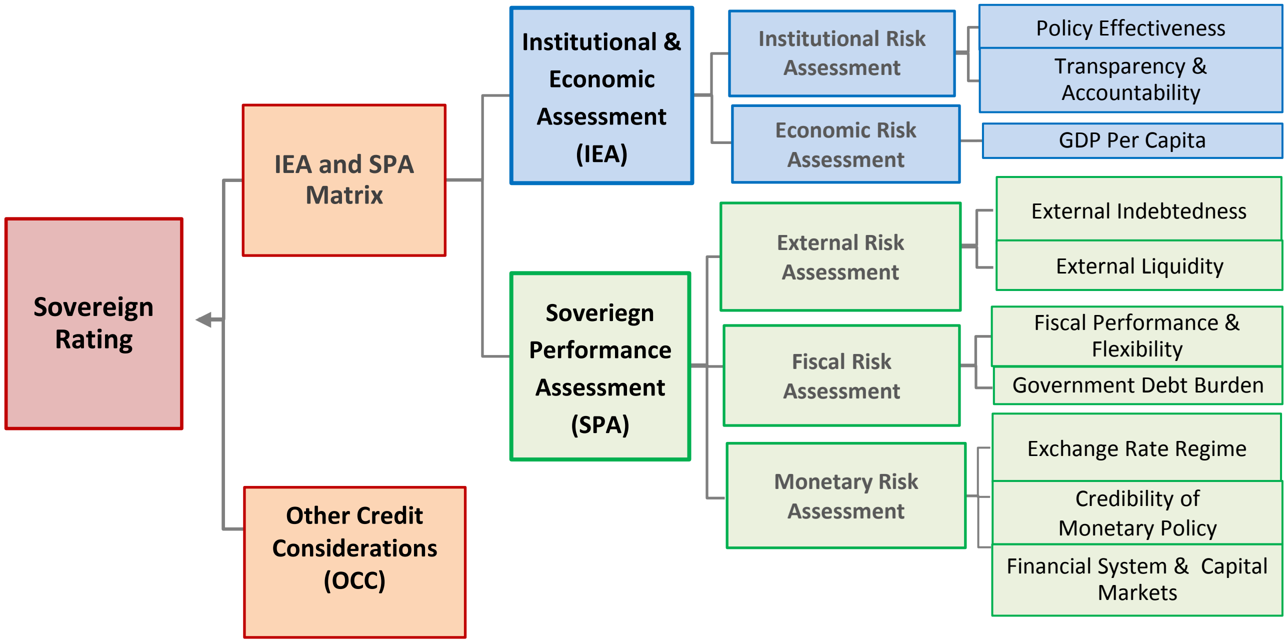
Topic	Previous Criteria	Current Criteria
Key Rating Factors	1. Political and Social Risk 2. Economic Risk 3. Fiscal Risk 4. Monetary Risk	1. Institutional Risk 2. Economic Risk 3. External Risk 4. Fiscal Risk 5. Monetary Risk
Performance Evaluation	Not stated	One-year actual performance and two-year projected performance
Other Credit Considerations	None	Applied

KEY RATING FACTORS

1. **Institutional risk factors** including institutional frameworks, political and social stability, continuity and effectiveness of government policies, efficiency of bureaucratic and legal systems, transparency, accountability, and governance.
2. **Economic risk factors** including economic status and standard of living, measured in terms of gross domestic product per capita.
3. **External risk factors** which can be considered by the country's external indebtedness, external debt serviceability, and external liquidity.
4. **Fiscal risk factors** covering fiscal position, government debt burden, external debt burden, and growth of government debts.
5. **Monetary risk factors** including effectiveness of monetary and exchange policy, government ability to control inflation and maintain interest rates at appropriate levels, and alternative sources of funds for the government and private sectors.

SOVEREIGN RATING METHODOLOGY

RATING FRAMEWORK



SCOPES OF THE METHODOLOGY

Sovereign ratings assigned by TRIS Rating are relative to the Thai government's sovereign risk. The highest creditworthiness will be rated "AAA". Based on TRIS Rating's national scale rating concept, the sovereign ratings assigned by TRIS Rating will be compared with Thailand's sovereign risk and comparable to other credit ratings assigned by TRIS Rating. As the national scale rating, ratings assigned by TRIS Rating cannot be compared with international scale ratings assigned by other international credit rating agencies.

The sovereign rating reflects the government's willingness and ability to service financial obligations to commercial creditors in full amount and on time. The criteria are applicable to all countries in Asia, particularly the country members of Association of Southeast Asian Nations (ASEAN) with which TRIS Rating has the credit rating service exposure.

KEY RATING FACTORS

TRIS Rating evaluates sovereign risk factors in two main areas: 1) Institutional and Economic Assessment (IEA) and 2) Sovereign Performance Assessment (SPA), with five key risk factors. Each risk factor is assessed on a six-point numerical scale from "1" (the lowest risk) to "6" (the highest risk). Details are explained as follows.

1) INSTITUTIONAL AND ECONOMIC ASSESSMENT (IEA)

1.1. Institutional Risk Assessment

TRIS Rating will primarily consider qualitative factors including political stability, continuity of government policies, and effectiveness of the bureaucratic system. These factors reflect the rated government's ability to prevent or handle economic and monetary volatility which could be caused by internal or external factors. Other credit factors comprise the government's policies in support of 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 and information. These factors are considered to enhance the country's business enabling environment.

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

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

1.2. Economic Risk Assessment

TRIS Rating will assess the structure as well as the growth prospects and volatility of the country's 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 factors are ultimately measured by the country's income level, and gross domestic product per capita (GDP per capita) is the key indicator.

2) SOVEREIGN PERFORMANCE ASSESSMENT (SPA)

TRIS Rating evaluates a country's sovereign performance by assessing the external, fiscal, and monetary risk positions, with both quantitative and qualitative considerations. Each risk factor is assessed on a six-point numerical scale from "1" (the lowest risk) to "6" (the highest risk). Sovereign performance may improve or deteriorate each year subject to changes in the domestic and global economic and financial environment, changes in government policies, and event risks. TRIS Rating evaluates sovereign performance by assigning an equal weight of one-year actual performance and two-year projected performance.

2.1. External Risk Assessment

The external position indicates the country's status of international transaction performance that can enhance the country's external debt serviceability and external liquidity. 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 compared with its net external debts. External liquidity will be considered by comparing gross external financing needs with current account receipts plus foreign exchange reserves.

2.2. Fiscal Risk Assessment

2.2.1. Government indebtedness. TRIS Rating measures a government's indebtedness using the ratios of government debt as a percentage of GDP and government interest expenses as a percentage of government revenues. These ratios will be analyzed together with the evaluation of debt structure in terms of currency diversification (or concentration). The structure of the creditors is another qualitative rating consideration. A government debt structure with a combination of multilateral creditors and/or bilateral loans usually offers lower than market rates and more relaxed and negotiable credit terms.

2.2.2. Government fiscal management. Countries with potential increases in government debt compared with GDP generally reflect inefficient fiscal management and, thus, expose the government to high debt burden and high debt repayment risk. The assessment qualitatively takes into consideration the government's available liquid assets and its capability to reduce budget deficits to manageable levels.

2.2.3. **Contingent liabilities.** Obligations or liabilities of the government may increase in the future, depending on the degree of government support in terms of capital injections to problematic financial institutions during financial crises. Contingent liabilities of the government also include the money that government needs to inject into non-financial government-related entities during distress scenarios.

2.3. Monetary Risk Assessment

2.3.1. **Monetary policy.** TRIS Rating will consider the monetary policy effectiveness to sustain a balanced economy and lessen the impacts of any major economic or financial shocks. The inflation rate may rise due to relaxed monetary policy or inefficient economic policy management.

2.3.2. **Foreign exchange policy.** A country's exchange rate regime will influence the flexibility of the economic and monetary policy of the government. In general, countries that closely peg their currencies to other sovereigns will have limited ability to implement effective monetary policies to handle domestic economic volatility.

2.3.3. **Capital market development.** The capital market is an essential alternative source of funds for government, facilitating effective government management of economic, fiscal, and monetary policies. Indicators that are used to analyze this factor include the amount of long-term government bonds outstanding in the domestic bond market and roles of the secondary market, as well as the ratio of local currency debt to total debt of the country.

The IEA and SPA assessment results will be compositely considered in terms of IEA and SPA matrix, yielding a preliminary sovereign rating. To get the sovereign rating, TRIS Rating takes other credit considerations; one or several notches, negative or positive, into the preliminary sovereign rating.

3) OTHER CREDIT CONSIDERATIONS (OCC)

Apart from the above-mentioned credit factors for the IEA and SPA matrix, the sovereign rating may be adjusted upward or downward by other credit considerations (OCC) that, in our view, should be captured in assessing the sovereign rating. OCC can be considered when 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 stemming from large public investment projects, which, if successful, would be expected to improve economic growth potential over the medium term. Another example of OCC would be when TRIS Rating has concrete evidence regarding the government's financial flexibility and accessibility during financial stress periods.

Major negative OCC are as follows.

- Extremely weak external liquidity which is expected to further deteriorate for an extended period.
- Extremely weak fiscal position, significantly worse than the weakest benchmark.
- Very high institutional, political, and governance effectiveness risk.
- Significant deterioration of credit profiles due to event risks or debt rescheduling risks.

SUFFICIENT AND RELIABILITY OF THE DATA

Sufficient, up-to-date, and reliable information and data are essential to allow TRIS Rating to assess the sovereign credit risk of any specific nation. In general, TRIS Rating will use data and information related to economic and fiscal performance provided by the rated government. Other sources of information will be gathered from multinational organizations including ADB, IMF, and World Bank. Most of these organizations provide updated information about the economic, financial, and fiscal budget positions of the member countries on a regular basis. A country that does not provide reliable data will limit our ability to understand the success of government policies and restrict the accuracy of our predictions of the future risks of the country. TRIS Rating reserves the right to refuse rating services for countries that are unable to provide sufficient and reliable information.

SOVEREIGN RATING SYMBOLS

Sovereign rating symbols are the same as the credit rating symbols TRIS Rating assigns to other rated issuers and rated issues. The rating symbols are classified into “AAA”, “AA”, “A”, “BBB”, “BB”, “B”, “C” and “D”. The highest creditworthiness sovereign can be assigned is “AAA” while the lowest is “C”. The “D” rating or “Default” is for sovereign that suspends repayments of government debt and obligations to commercial creditors. 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 SOVEREIGN PERFORMANCE RATIOS

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

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