

CARE's Issuer Rating

[In supersession of "CARE's Issuer Rating" issued in [June 2017](#)]

1. Scope

CARE's Issuer Rating (CIR) is issuer specific assessment of credit risk. While the scope of CIR is similar to long term instrument ratings, the main difference between CIR and other ratings is that CIR is not instrument specific but issuer-oriented. Issuer rating factors in expected performance of the entity over a medium term time horizon of around three years and reflects the capability of the entity as regards timely servicing of its financial obligations. Once accepted, the rating is subject to periodic reviews. The rated company will have to provide a written request to CARE Ratings giving a notice period of one year for withdrawal of an accepted rating.

2. Methodology

2.1. Manufacturing Companies

The methodology mainly focuses on the entity's future cash generation capability and consequently its ability to honour its financial obligations. The entity's past audited financials for five years are studied and analysis of its projections for the next three financial years is carried out under various sensitivity scenarios. To determine the entity's cash generation capability, various aspects of the entity's operations as mentioned hereunder are taken into consideration:

Industry Dynamics

- Demand Supply scenario
- Trend in realizations
- Availability of substitutes
- Level of competition
- Economic Cycles
- Government support to the sector

Operational Performance

- Availability of required infrastructure facilities
- Availability of manpower
- Manufacturing technology
- Marketing setup and consumer mix
- Analysis of cost components
- Research & Development Activities
- Working capital Management
- Compliance with environment norms
- Comparison with other players on the basis of various parameters

Financial Risk analysis

- Quality of Accounts and Accounting policies
- Contingent liabilities
- Debt servicing track record
- Financial Ratio analysis
- Cash Flow analysis
- Financial flexibility & liquidity
- Validation of projections and sensitivity analysis

Management Capability

- Organization structure
- Succession Planning
- Management Competence
- Track record
- Corporate strategy & roadmap to achieve corporate objectives
- Internal control and Audit systems
- Performance of group companies
- Personnel policies

Project Risk Analysis

- Size of the projects
- Project debt-equity and tie-up of financial resources
- Project implementation Risk
- Post implementation risk

2.2. Banks, Financial Institutions and NBFCs

Issuer rating of Banks, Non-Banking Finance Companies (NBFCs) or Financial Institutions (FI) depends on a range of quantitative and qualitative factors. CARE's assessment can be broken down into the following elements:

2.2.1. Operating Environment

Economic and Industry factors

- 1) Macroeconomic environment including growth prospects for the economy and the rate of monetary and credit growth, Liquidity & credit demand in the system, structure, composition and trends of the banking system, strength and efficiency of the legal system with specific stress on bankruptcy laws, recovery of NPAs etc.
- 2) Regulation: Existing regulatory framework, international regulatory environment and expected changes in India on account of global regulatory trends

2.2.2. Business Fundamentals

CARE Ratings analyses the business fundamentals of an institution using the CRAMELS model which stands for Capital adequacy, Resource raising ability, Asset quality, Management quality, Earnings quality, Liquidity and Systems. This is a variation of the CAMEL model, used by regulatory agencies all over the world for supervising operations of banks. The key factors examined as part of the analysis, under each of the following aspects, are listed below:

Capital Adequacy

- Capital to Risk Weighted Assets Ratio (CRAR), also known as Capital Adequacy Ratio (CAR)
- Extent of 'Tier I' capital
- Components of capital including equity, CET, preference shares, subordinated bonds, perpetual bonds etc.
- Current and expected CRAR vis-à-vis minimum regulatory requirements and economic capital required for the entity
- Stressed CRAR for probable losses

Resources

- Cost of funds and their composition in terms of short term or long term, retail and wholesale, domestic or foreign currency etc.
- Extent of core and low cost deposits
- Hedging (if any) on the borrowings
- Ability to raise funds from different sources and under diverse market conditions

Asset Quality

- Quality and seasoning of portfolio
- Gross and Net NPA: Movement of NPAs, write offs, provision coverage, slippage ratio
- Delinquencies on a specified time period say 90 days past due basis
- Distribution of portfolio on the basis of credit rating, sectors, major projects etc
- In case of retail portfolio, granularity, asset classes, geographical regions, loan to value (LTV) etc
- Profile of major exposures
- Recovery post defaults experience in the past

Management Strategy

- Shareholding pattern
- Composition of the board, Organisational structure, personnel policies and extent of delegation of powers
- Organisational objectives
- Relationship with subsidiaries
- Support from Group/ Government

Earnings Quality

- Composition of income: fee based or fund based
- Diversification of earning sources
- Extent of competition and sustainability of income
- Total income vs. Net interest income
- Installment to income (IIR) ratios
- Extent of provisions required for NPAs
- Net Interest Margin
- Interest Rate Risk and its impact on profitability
- Impact of treasury operations on profitability
- Expense Ratios and provision requirements
- Return on total assets
- Accounting policies

Liquidity

- Asset Liability Maturity Profile
- Extent of core assets and liabilities
- Financial flexibility in terms of unutilised lines of credit
- Off balance sheet products and their cash flow implications.

Systems

- Risk Management systems and controls for
 - Credit risk
 - Operational risk and
 - Market risk
- Asset Liability Management and Interest rate risk management

The Issuer rating process is ultimately an assessment of the fundamentals and the probabilities of change in the fundamentals. Rating determination is a matter of experienced and holistic judgment, based on the relevant quantitative and qualitative factors affecting the credit quality of the issuer.

[Last updated on August 28, 2018. Next review due in August- September 2019]

Disclaimer

CARE's ratings are opinions on credit quality and are not recommendations to sanction, renew, disburse or recall the concerned bank facilities or to buy, sell or hold any security. CARE has based its ratings/outlooks on information obtained from sources believed by it to be accurate and reliable.

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