

Criteria | Financial Institutions | General:

Financial Institutions Rating Methodology

December 9, 2021

(Editor's Note: On March 31, 2022, we republished this criteria article to make nonmaterial changes. See the "Revisions And Updates" section for details.)

OVERVIEW AND SCOPE

1. This article presents S&P Global Ratings' global criteria for rating financial institutions. It should be read in conjunction with "Banking Industry Country Risk Assessment Methodology And Assumptions," Dec. 9, 2021, where we outline our criteria for determining a Banking Industry Country Risk Assessment (BICRA). The glossary contains definitions of terms we use in the criteria.
2. Financial institutions (FIs) include banks as well as nonbank financial institutions such as securities firms and finance companies (which include business development companies) when we consider that their greatest risks relate to asset quality, funding and liquidity, and tangible capital.
3. Entities that are registered as banks or bank holding companies, or that carry out nonbank financial institution activities, are in scope of the criteria, even when we classify the entities as government-related entities (GREs).
4. The criteria do not apply to insurers, or to financial services companies for whom the greatest risks relate more to their ability to generate cash flow than to the amount of capital they may need to withstand credit losses (such as asset managers and financial services finance companies). The sections on additional loss-absorbing capacity and resolution counterparty ratings (RCRs) apply to financial market infrastructure companies (FMIIs), but otherwise FMIIs are out of scope of the criteria.
5. The criteria:
 - Apply to all global-scale foreign and local currency, long-term issuer credit ratings on FIs;
 - Apply to ratings on financial obligations, including RCRs, issued by FIs, other than hybrid capital instruments; and
 - Do not apply when determining the stand-alone credit profile (SACP) or issuer credit rating (ICR) on any company with unsustainable financial commitments or that has financial obligations vulnerable to nonpayment (though we may use the criteria to assess the individual SACP factors for that entity). Instead, we use our 'CCC' rating criteria (see Related Criteria).

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KEY PUBLICATION INFORMATION

- Effective date: These criteria are effective Dec. 9, 2021, except in jurisdictions that require local registration. In those jurisdictions, the criteria are effective only after the local registration process is completed.
- This updated methodology follows our request for comment, "Request For Comment: Financial Institutions Rating Methodology," published June 8, 2021. For the changes between the RFC and the final criteria, see "RFC Process Summary: Financial Institutions Rating Methodology," Dec. 9, 2021.
- These criteria supersede the articles listed in the "Fully Superseded Criteria" and "Partly Superseded Criteria" sections at the end of this article.

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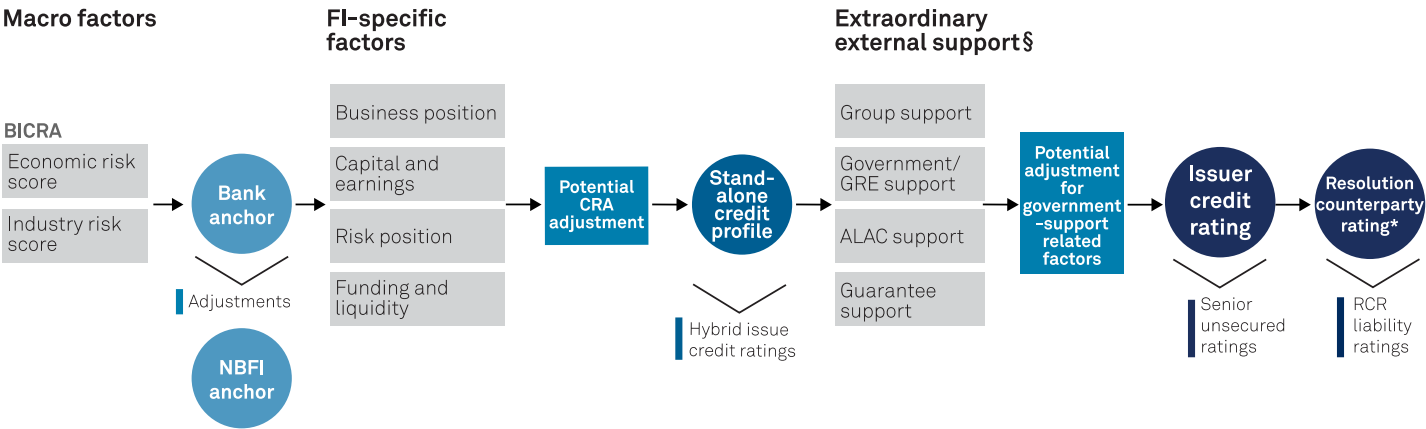
METHODOLOGY

SECTION 1: STRUCTURE OF THE METHODOLOGY

- 6. Section 1 provides an overview of the framework for determining the ICR on an FI, starting by assessing the SACP, and then incorporating any extraordinary external support (or negative influence). The approach also applies when assessing the group SACP and the group credit profile (GCP) of an FI group. Each part of the criteria indicates whether it applies to all FIs or to certain sectors.
- 7. We use the economic risk and industry risk scores to determine the anchor for an FI, which is the starting point of a rating. We adjust for factors specific to the FI--business position, capital and earnings, risk position, funding and liquidity, and a potential comparable ratings analysis adjustment--to determine the SACP. We then consider the potential for extraordinary external support (such as from a parent, a sovereign government, or investors in additional loss-absorbing capacity [ALAC] instruments) to determine the long-term ICR (see chart 1). Issue credit ratings are typically related to either the SACP or ICR.

Chart 1

Financial Institutions Ratings Framework



Note: Issue credit ratings on hybrids typically reference the SACP, while issue ratings on senior unsecured instruments typically reference the ICR unless they are guaranteed by a higher-rated entity or are RCR liabilities (see "Hybrid Capital Methodology And Assumptions," published July 1, 2019 for more details on hybrids). *Subject to jurisdictional assessment and expected resolution strategy. §In some cases, an FI may also qualify for an additional support adjustment. BICRA--Banking industry country risk assessment. NBFI--Nonbank financial institution. FI--Financial institution. CRA--Comparable ratings analysis. GRE--Government-related entity. ALAC--Additional loss-absorbing capacity. Copyright © 2021 by Standard & Poor's Financial Services LLC. All rights reserved.

8. In all cases, long-term ratings and SACPs are no lower than 'B-' or 'b-', respectively, unless the default scenarios in the 'CCC' criteria apply. We use "Methodology For Linking Long-Term And Short-Term Ratings" to determine the short-term ICR. We also describe how we assign issue credit ratings and RCRs.
9. The criteria for analyzing the creditworthiness of FIs is both forward-looking and informed by past experience. Our analysis uses financial metrics as well as qualitative information and expectations. Regarding financial metrics, we typically use our expectations for the current year and the upcoming one to two years, as informed by historical data as relevant, unless otherwise stated, and typically take into consideration:
 - Developments since the most recent financial statements; and
 - Developments that have a reasonably high degree of certainty of occurring.

Stand-Alone Credit Profile (SACP)

10. We assess the SACP based on the following factors and a potential comparable ratings analysis adjustment:
 - Anchor (derived from our economic risk and industry risk assessments under our Banking Industry Country Risk Assessment criteria, see "Banking Industry Country Risk Assessment Methodology And Assumptions"),
 - Business position,
 - Capital and earnings,
 - Risk position, and
 - Funding and liquidity.
11. The anchor represents the strengths and weaknesses of an FI's broader operating conditions and is the starting point for determining the SACP. The four other factors represent specific strengths and weaknesses of an FI. Based on the analysis of these factors, the SACP can be higher or lower than the anchor.

Ongoing External Support And Interference In The SACP

12. The SACP includes ongoing external support or interference from a government or a group. This differs from our assessment of potential extraordinary external support, which is not included in the SACP.
13. The SACP includes the following types of government support:
 - System support: The support that a government provides to all banks in a financial system. We assess this as part of our economic risk and industry risk analysis in the BICRA criteria, which feeds into the anchors for banks.
 - Direct support: The targeted support that a government provides to a specific entity in crisis. Such support may benefit any one or several of the FI-specific SACP factors.
14. Governments may provide direct support to an individual bank by, for example, providing liquidity or capital injections, or by buying or insuring risky assets.
15. We include direct support in the SACP once the government has made a commitment to provide it.

We treat it as committed when it has received the appropriate political approvals, such as from the executive or legislative authority in the country. In some countries, laws exist to give the administration the authority to act without further approvals.

16. The SACP also includes ongoing government interference that may take the form of directed lending and actions that create market distortions. We capture these in industry risk (and therefore the anchor) and in the FI-specific SACP factors where relevant.
17. Ongoing support from a parent or group member is also included in the relevant FI-specific SACP factor when it is ongoing, stable, and expected to continue.

Comparable Ratings Analysis (CRA) Adjustment

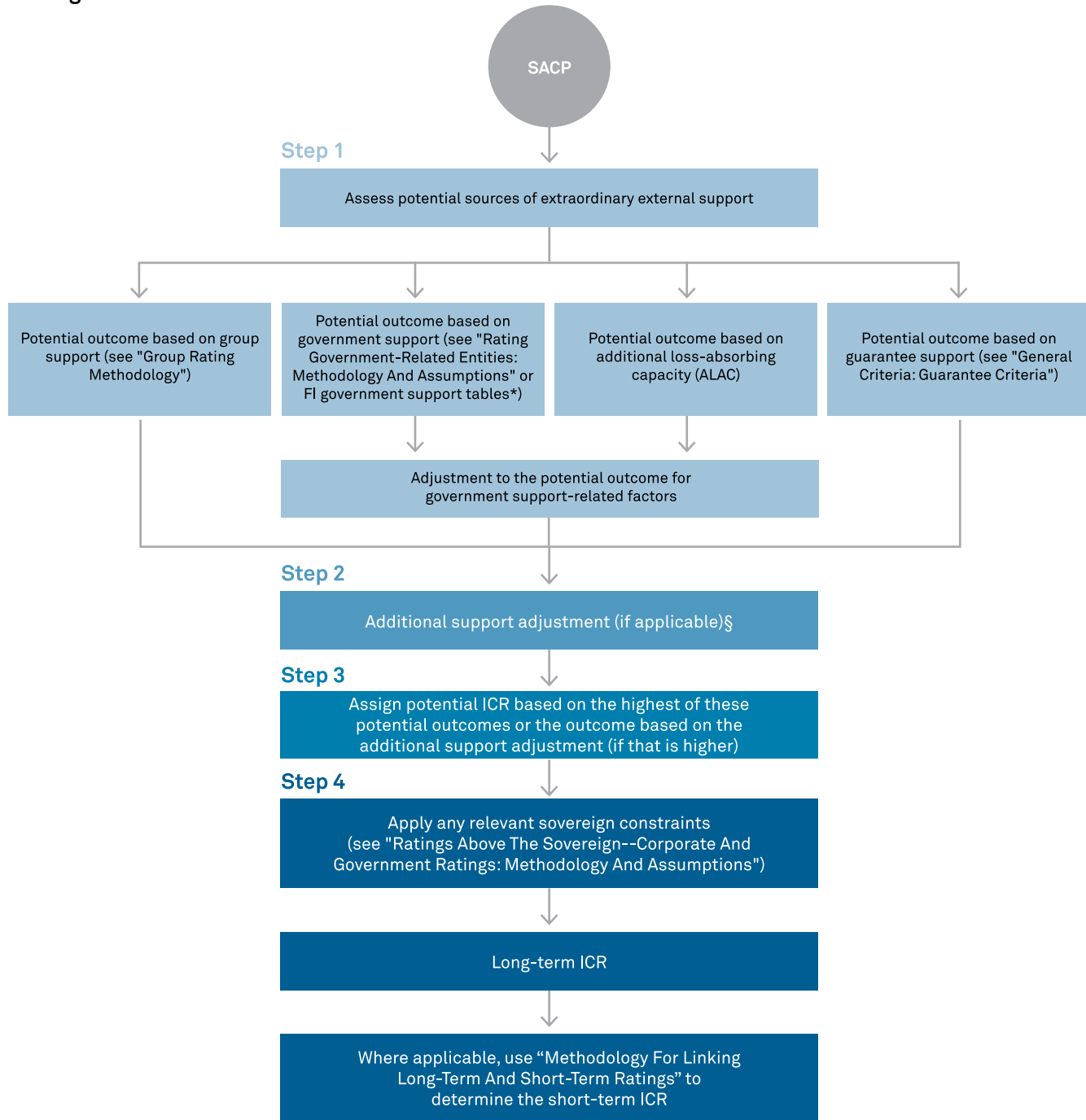
18. We may apply an adjustment of up to one notch in either direction to arrive at the SACP, capturing a more holistic view of creditworthiness. We make this adjustment based on our comparable ratings analysis. Our CRA incorporates additional credit factors, which may be transitional or more structural elements of an FI's creditworthiness, that the criteria do not separately identify. In addition, we incorporate in our CRA existing credit factors not fully captured in the other SACP factors, which may be informed by peer analysis.
19. We don't make an adjustment to the SACP for potential external support or negative intervention if it is extraordinary, but we can make an adjustment when such support or negative intervention is ongoing--if it has not already been reflected in the SACP factors. The CRA cannot be used to raise the SACP above the caps associated with the regulatory capital assessment of the FI within our capital and earnings assessment.
20. The CRA peer analysis assesses an FI's relative credit standing among FIs with similar SACPs (that is, the same or one notch higher or lower). For example, if an FI has an SACP of 'a-', we compare it with FIs with SACPs of 'a', 'a-', and 'bbb+'. And we may compare a group with a group SACP of 'a-' with groups that have group SACPs of 'a', 'a-', and 'bbb+'.
21. An example of a CRA adjustment based on credit factors not fully captured in the assessments of the other SACP factors could be an FI for which we decide to apply a one-notch positive adjustment because we believe that several SACP factors are close to a higher assessment, without material offsetting negative factors, such that the cumulative effect is representative of a higher SACP.

Moving From The SACP To The ICR

22. We derive the ICR by combining the SACP and the support framework, which determines the extent of uplift, if any, for potential extraordinary external support, or the risk of extraordinary negative intervention or sovereign-related risks (see chart 2).
23. The support framework considers both the relationship between an entity and its external parties--such as the parent group, government, or the loss-absorbing characteristics represented by ALAC securities--and how this affects overall creditworthiness. The potential ICR is the same as the SACP unless the FI is likely to receive additional capital, funding, liquidity, or risk relief from external parties in a crisis. Such support can arise from a parent group or government but can also come from a guarantor or from investors in ALAC-eligible instruments.
24. The potential ICR on an FI is the highest outcome resulting from the criteria assessment of these forms of potential support.

Chart 2

Moving From The SACP To The ICR

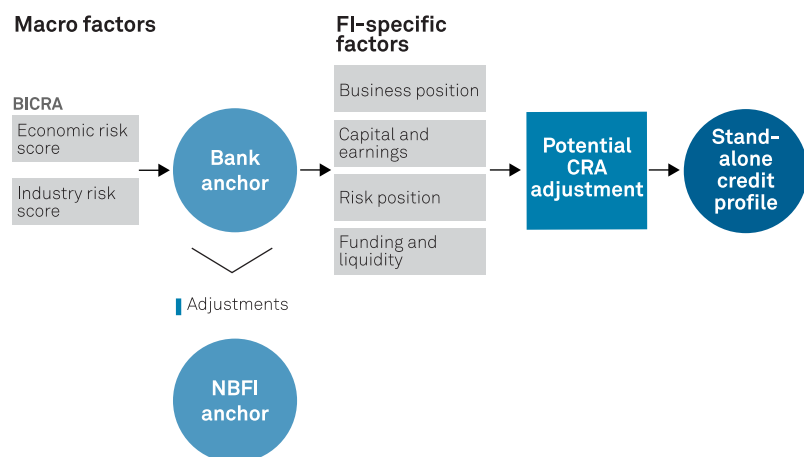


Note: The same approach applies to moving from the group SACP to the GCP when assessing an FI group. In some cases, an SACP is not needed to determine an ICR--see our group rating methodology, government-related entities, or guarantee criteria. *Certain NBFIs are eligible for support under the FI government support tables. §Additional support uplift may apply even if there is no uplift based on the potential government support tables or no uplift for ALAC. SACP--Stand-alone credit profile. ICR--Issuer credit rating. Source: S&P Global Ratings. Copyright © 2021 by Standard & Poor's Financial Services LLC. All rights reserved.

Adjustment For Government Support-Related Factors

25. We may apply an adjustment of one notch in either direction when we consider that the potential outcome (for example, arrived at via the FI government support tables--21, 22, and 23) understates or overstates the potential for extraordinary government support. We take into account the ICRs on peers (those with similar ICRs--i.e., the same or a notch higher or lower) and the ability of the relevant government or other authorities to provide extraordinary support when deciding whether to make this adjustment.
26. We may also use this adjustment in transitional situations. For example, we could make an adjustment if we are changing our assessment of a government's supportiveness, or an FI's systemic importance, and that would lead to a multiple-notch movement in the ICR that we do not think represents the entity's creditworthiness.
27. We may also use the adjustment to reflect our assessment of long-standing government policy. A negative adjustment for government support-related factors does not reduce our view of group or guarantee support, however. We do not use the adjustment for government support-related factors to raise the ICR above the sovereign rating on the government that would provide this support.
28. The adjustment for government support-related factors is in addition to the CRA adjustment. The reasons for each adjustment are mutually exclusive. Ongoing external support does not influence the use of the government support-related adjustment because we reflect this type of support in the SACP.
29. An example of where we may make a positive one-notch adjustment is for an FI whose ramp-up of ALAC in response to regulatory requirements will continue beyond our two-year ALAC projection period. This adjustment occurs when we consider that the potential for extraordinary government support could make up for a shortfall in ALAC, relative to the level required for the first notch of uplift, in the early years of a regulatory transition period.
30. In this situation, the potential for extraordinary government support provides a maximum of one notch of uplift over the SACP and may be considered over a projection period of typically three to four years (i.e., from year five, the potential for extraordinary government support typically does not offset the ALAC shortfall). In our projections, we only include future issuance up to levels consistent with explicit regulatory requirements during the phase-in period. We remove this uplift if, during the transition period, the FI does not meet its regulatory requirements for ALAC issuance, or increasing S&P Global Ratings risk-weighted assets (S&P Global RWAs) weaken prospects for meeting the ALAC thresholds.
31. Another example of where we could make a positive adjustment to the potential outcome for most or all banks in a jurisdiction is when the following characteristics all apply:
 - We assess the government as highly supportive of its banking system.
 - There is a very strong track record of proactive or preemptive interventions that protect senior creditors from losses, including creditors of small banks operating in the system, in a timely manner.
 - The banking system plays a very important role in the financing of the economy, and the local capital market is still being developed or not broad and deep enough to provide a viable alternative.

SECTION 2: DETERMINING THE SACP



BICRA--Banking industry country risk assessment. NBFI--Nonbank financial institution.
FI--Financial institution. CRA--Comparable ratings analysis.

Section 2 describes the criteria for determining the SACP.

Anchor

32. We use the BICRA's economic risk and industry risk scores to determine a bank's anchor (see table 1), the starting point in assigning an ICR. The anchor is a globally consistent, relative ranking of creditworthiness across national banking markets and ranges from 'a', the least risky, to 'b-', the riskiest. For nonbank financial institutions (NBFIs), we adjust the anchor to account for differences between the bank and NBFI sectors as well as potentially for country/sector- and entity-specific factors.

Table 1

Determining The Anchor From Economic Risk And Industry Risk

Industry risk*	--Economic risk*--									
	1	2	3	4	5	6	7	8	9	10
1	a	a	a-	bbb+	bbb+	bbb				
2	a	a-	a-	bbb+	bbb	bbb	bbb-			
3	a-	a-	bbb+	bbb+	bbb	bbb-	bbb-	bb+		
4	bbb+	bbb+	bbb+	bbb	bbb	bbb-	bb+	bb	bb	
5	bbb+	bbb	bbb	bbb	bbb-	bbb-	bb+	bb	bb-	b+
6	bbb	bbb	bbb-	bbb-	bbb-	bb+	bb	bb	bb-	b+
7		bbb-	bbb-	bb+	bb+	bb	bb	bb-	b+	b+

Table 1

Determining The Anchor From Economic Risk And Industry Risk (cont.)

Industry risk*	--Economic risk*--									
	1	2	3	4	5	6	7	8	9	10
8			bb+	bb	bb	bb	bb-	bb-	b+	b
9				bb	bb-	bb-	b+	b+	b+	b
10					b+	b+	b+	b	b	b-

*On a scale from 1-10, lowest to highest risk where economic risk and industry risk scores are rounded to the nearest whole number prior to the application of the table.

Economic risk

33. An entity's economic risk is determined by the BICRA economic risk score of the country or countries where the entity operates. The BICRA economic risk scores range from '1' (very low risk) to '10' (extremely high risk).
34. When an entity is active in more than one country, we calculate the economic risk score as a weighted average of the economic risk scores--called weighted-average economic risk. We use the proportion of an entity's business in each country that represents its main economic risks to weight the economic risk scores.
35. We typically calculate the weighted average using weights derived according to the geographic breakdown of lending exposures, exposures at default, or potentially other metrics, depending on what we consider the best proxy for the geographic risk profile of the FI. For example, we may base the weighting on the adjusted exposure used to reflect the geographic risk of that FI in measures such as regulatory capital ratios or in "Risk-Adjusted Capital Framework Methodology" or could use other metrics including revenues if we consider they are the best proxy. If we expect that the entity's risk footprint is likely to change--for example, as a result of acquisitions in new countries--then we use the expected geographic risk to calculate the weighted average.
36. When an FI operates in more than one jurisdiction, the economic risk score used to determine the anchor is weighted to reflect a forward-looking view of its economic risks. The calculation typically only includes countries where it conducts more than 5% of its business, but we may also use economic risk scores assigned to regions or groups of countries where relevant. All weightings are rounded to the nearest 5% before averaging.

Table 2

Hypothetical Example Of Weighted-Average Economic Risk For An FI

Country	Weighting (% of business)	Economic risk*	Weighted economic risk
Country A	45	2	0.9
Country B	20	4	0.8
Country C	15	1	0.15
Country D	10	5	0.5
Country E	10	2	0.2

Table 2

Hypothetical Example Of Weighted-Average Economic Risk For An FI (cont.)

Country	Weighting (% of business)	Economic risk*	Weighted economic risk
Weighted-average economic risk	--	--	2.55 (rounded to 3 in our analysis of the FI)

*Example scores, on a scale from 1-10, lowest to highest risk.

Industry risk

37. An entity's industry risk is determined by the BICRA industry risk score for the country where it is domiciled and primarily regulated. The BICRA industry risk scores range from '1' (very low risk) to '10' (extremely high risk).
38. We do not calculate a weighted average industry risk when an entity operates in more than one country.
39. If the nonoperating holding company (NOHC) of a bank moves to a different country than where the bank is domiciled, the relevant industry risk score changes to that of the new country only if the regulator in that new country becomes the lead regulator of the group. The reason for this is that an entity's industry risk is determined by the BICRA industry risk score for the country where it is domiciled and primarily regulated.
40. The country of domicile typically determines the applicable industry risk for an NBFI. But for an NBFI that is not subject to consolidated prudential regulation and that operates in multiple countries, we may use the industry risk of the country that we view as having the most influence on the entity's creditworthiness. For NBFIs that operate in multiple jurisdictions, we apply the country/sector-specific adjustment, if any, that applies to the NBFI sector in the country used to determine the industry risk score.

Additional considerations for NBFI anchor

41. We establish preliminary anchors for NBFI sectors relative to the bank anchors in the same country (as described above). We then may apply a country/sector-specific adjustment and/or an entity-specific adjustment to arrive at the final anchor for an NBFI. However, the final anchor for an NBFI entity cannot be higher than the relevant bank anchor.
42. **NBFI--preliminary anchor.** The preliminary anchors for the NBFI sectors reflect the typical incremental risks that NBFIs face relative to banks. As such, in all countries, we set the preliminary anchor for fincos--including business development companies (BDCs)--three notches below the bank anchor, and the preliminary anchor for securities firms two notches below the bank anchor, subject to a floor at 'b-'.
43. As an example, if the bank anchor in a given country is 'bb+', the preliminary anchor for fincos in that same country is 'b+', and for securities firms 'bb-'. In our view, the incremental industry and economic risks for NBFIs relative to banks typically include the following:
 - Both fincos and securities firms typically lack access to a central bank, which increases liquidity and funding risk relative to banks.
 - Both fincos and securities firms typically face strong competition from banks because of banks'

lower cost of financing.

- In addition, fincos and securities firms have higher competitive risk, both among themselves and relative to banks, because of lower barriers to entry as well as more volatile or fragmented business conditions.
- Fincos usually lack the regulatory oversight that banks have, which heightens their sensitivity to changes in investor confidence.
- Securities firms typically benefit from more regulatory oversight than fincos, but less than banks do.
- Securities firms' economic risks may exceed those that banks face because they are exposed to equity market volatility, given their dependence on market liquidity to monetize assets they own.

44. **NBFI--country/sector-specific adjustment.** In some cases, a country/sector-specific adjustment results in the NBFI anchor being higher or lower than the preliminary anchor. Securities firms and fincos are examples of sectors within a country. We may further divide these sectors into subsectors for the country/sector-specific adjustment if a subsector has elements in common that are markedly different from the wider sector in that country. The adjustment at the subsector level can be different than at the sector level. For an NBFI sector or subsector in a given country, we make a positive country/sector-specific adjustment when we consider the incremental risks relative to banks are materially lower than those identified in the preliminary anchor, and vice versa.
45. We may make a positive adjustment of one or two notches for securities firms (this also applies to subsectors within the securities firms sector) and of one to three notches for fincos (this also applies to subsectors within the fincos sector). (Take, for example, a bank anchor of 'bbb'. The corresponding finco sector preliminary anchor in the same country is three notches lower, at 'bb'. Based on our analysis here, we may reduce that three-notch gap using a positive country/sector-specific adjustment so that the NBFI anchor is 'bb+', 'bbb-', or 'bbb'.) Situations where we may make a positive adjustment include:
- The NBFI sector or subsector benefits from a stronger institutional framework (government oversight) than is typical for such sectors. In some countries, fincos are regulated or have other supportive institutional framework elements.
 - Funding is stronger for the specific NBFI sector or subsector than we typically observe for NBFIs (e.g., the sector or subsector has access to central bank funding). In some countries, fincos have direct access to central bank funding, or indirect access to central bank funding, for example through government-sponsored development banks.
 - Regulations preserve competitive position (and, hence, reduce competitive risk) for the sector or subsector. In some countries, government regulators restrict the number of licenses they grant to NBFIs to enter into certain businesses.
46. Another situation where we make a positive adjustment is when the bank anchor is low and already reflects some of the incremental risks we typically see in the NBFI sector. The differential between the bank and NBFI anchors decreases in countries where banks and NBFIs face similar levels of risk. Specifically, in countries where the bank anchor is between 'b-' and 'bb+', we may reduce or eliminate the differential.
47. Conversely, we make a negative adjustment of one notch if the NBFI sector or subsector faces additional funding, economic, or competitive risks, or if it has a weaker institutional framework,

than assumed in the preliminary anchor. For example, for securities firms, we typically make a one notch negative country/sector-specific adjustment when no regulatory oversight exists, or if economic and funding risks are heightened by less liquid or more volatile capital markets.

48. **NBFI--entity-specific anchor adjustment.** An NBFI entity-specific anchor adjustment can result in an entity's anchor being higher or lower than the anchor for the rest of the sector.
49. The entity-specific anchor adjustment may apply to GREs that have a very high, extremely high, or almost certain likelihood of receiving extraordinary government support, as described in the GRE criteria (see Related Criteria). Even if not prudentially regulated as banks, these GREs benefit, on an ongoing basis, from more favorable funding given their relationship to the government, from regulatory oversight, or from lower competitive risk, if they are regulated or de facto monopoly (or oligopoly) industry participants. If such GREs make up a subsector in a country, then we incorporate the impact of their relationship with the government through a sector-specific adjustment and only use an entity-specific adjustment if the GRE has markedly different characteristics to the other GREs in that subsector.
50. For certain non-GRE fincos, we may apply an entity-specific anchor adjustment to reflect these entities' markedly different characteristics from most other fincos in the same country. This may, for example, apply to fincos benefiting from an NOHC regulated by a banking supervisor or a quasi-monopoly status granted by or influenced by a regulator. We also make a positive adjustment of one notch for a BDC that maintains a 200% regulatory asset coverage ratio and does not adopt the 150% modified asset coverage ratio permitted by the Small Business Credit Availability Act of 2018.
51. We generally do not apply an entity-specific adjustment for securities firms.

Building On The Anchor

52. After determining the anchor for an FI, we analyze the entity's individual characteristics. If the assessment of each entity-specific factor has a neutral impact, then the preliminary SACP will be at the same level as the anchor. The preliminary SACP will be higher than the anchor if the net effect of the entity-specific factors is positive, and lower than the anchor if the net effect is negative. The assessment of each factor can have a positive or negative effect on the preliminary SACP of one or more notches--or have no effect (see tables 3 and 13 for the notch impact arising from each entity-specific factor assessment).

Table 3

Impact Of The Entity-Specific Factors On The SACP Or Group SACP

Assessment	Business position	--Capital and earnings*--			Risk position
		Bank anchor of 'bbb-' or higher	Bank anchor of 'bb+' to 'bb-'	Bank anchor below 'bb-'	
Very strong	+2 notches	+2 notches	+2 notches	+ 2 notches	+2 notches
Strong	+1 notch	+1 notch	+1 notch	+2 notches	+1 notch
Adequate	0 notches	0 notches	0 notches	+1 notch	0 notches
Moderate	-1 notch	-1 notch	0 notches	0 notches	-1 notch
Constrained	-2 to -3 notches	-2 to -3 notches	-1 notches	0 notches	-2 to -3 notches

Table 3

Impact Of The Entity-Specific Factors On The SACP Or Group SACP (cont.)

Assessment	Business position	--Capital and earnings*--			Risk position
		Bank anchor of 'bbb-' or higher	Bank anchor of 'bb+' to 'bb-'	Bank anchor below 'bb-'	
Weak	-4 to -5 notches	-4 to -5 notches	-2 to -3 notches	-1 to -2 notches	-4 to -5 notches

Note: We assess the entity-specific factors at the group level when determining the group SACP. See table 13 for the impact of the funding and liquidity assessment on the SACP. There are caps on the SACP within the capital and earnings assessment. To arrive at the final SACP after scoring each of the entity-specific factors, the CRA adjustment can raise or lower the SACP by one notch. The final SACP is no lower than 'b-' unless 'CCC' criteria applies. *We use the bank anchor to determine the impact of capital and earnings on the SACP or group SACP for both banks and NBFIs.

53. In addition to using peer groups when considering whether to make a CRA, we also may use peer groups when considering the factors that contribute to the SACP (see table 4). Peers are chosen to give insight into a specific aspect of the SACP analysis.
54. The entities within the peer groups may not be direct peers in all aspects of each entity-specific factor (for example, one entity may be a good peer for business position but not for funding) but inform our assessment of the FI. Peer groups are typically based in the same region or country, or else have similar activities. Peers typically include entities in countries with the same or similar anchor (where similar means plus or minus one notch). The comparison may include entities in other countries or FI sectors for global and regional comparability, such as when similarities exist with banks or NBFIs in other countries or sectors or, for example, when there are not enough domestic banks or NBFIs.
55. For NBFIs, the peer group is typically NBFIs that are in the same sector and have similar SACPs or group SACPs (i.e., the same or one notch higher or lower). However, the peer groups may include others. For example:
 - The peer group may include banks in the same country, for example, when the SACP or group SACP is close to the bank anchor.
 - The peer group may include NBFIs in the same sector but in different countries if there's an insufficient number of domestic peers or because regional or global peers form a better comparison.
 - The peer group may include NBFIs from other sectors, or financial services finance companies, when the entity's business overlaps with or is adjacent to other NBFI sectors or to the business of other entities, such as financial service finance companies. (An example would be a finco that executes cash and collateral business similar to securities firms.)

Table 4

Typical Peers For Each SACP Factor

SACP factor	Banks	NBFI
Business position*	We typically compare a bank with other entities that have the same or similar industry risk scores, typically those in the same region or country or that have similar activities.	We typically compare an NBFI with other entities that have the same or similar anchors, typically in the same country or that have similar activities. (Generally, it would be NBFIs in the same sector.)
Capital and earnings	This assessment is informed by a comparison with banks that are either in the same country or have similar activities.	This is an assessment informed by comparison with NBFIs in the same sector.

Table 4

Typical Peers For Each SACP Factor (cont.)

SACP factor	Banks	NBFI
Risk position*	We typically compare a bank with other entities that have the same or similar economic risk scores, typically those in the same region or country or that have similar activities.	We typically compare an NBFI with other entities that have the same or similar anchors, typically in the same country or that have similar activities. (Generally, it would be NBFIs in the same sector.)
Funding*	We typically compare a bank with other banks in the same country.	This assessment is informed by a comparison with NBFIs in the same sector.
Liquidity	This assessment can be informed by a comparison with banks either in the same country or with similar activities.	This is an absolute assessment.
Comparable ratings analysis adjustment*	We compare FIs that have the same or similar SACPs.	We compare FIs that have the same or similar SACPs.

Note: A similar anchor or SACP is one that is one notch higher or lower. *The comparison can include entities in other countries or FI sectors, for example, when there are not enough domestic banks or NBFIs or when similarities exist with banks or NBFIs in other countries.

Business Position

56. Our assessment of business position measures the strength of an FI's business operations. An FI's business operations can add to or mitigate its industry risk score (or NBFI anchor in the case of an NBFI). The criteria consider three subfactors for business position:
- Governance, management, and strategy;
 - Business stability; and
 - Diversification.
57. We assess relative strength through a number of indicators (see table 5). We use a mix of quantitative metrics and qualitative judgment to determine the strength of a company's business franchise.

Table 5

Business Position Subfactors

Subfactors	Explanation	Examples of indicators
Governance, management, and strategy	The quality of corporate governance, management, and strategy	Governance and transparency, ownership structure, quality of management, strategic positioning, operational effectiveness, financial management, and policies
Business stability	The stability or fragility of an FI's franchise	Revenue stability, market position, and customer base
Diversification	The concentration or diversification of business activities	Contributions of different business lines and geographies

58. The business position assessment considers all three subfactors, which may reinforce or weaken each other. However, stronger areas do not automatically offset or average out weaker areas. We focus on identifying risks or attributes and determining whether they combine to further increase or reduce overall risk.

59. For each FI, we assign an overall business position assessment on a scale from very strong to weak (see table 6).

Table 6

Business Position Assessment

	What it typically means
Very strong	An FI's business operations make it materially better placed to withstand adverse operating conditions than the industry risk score (or NBFI anchor in the case of an NBFI) indicates.
Strong	An FI's business operations make it better placed to withstand adverse operating conditions than the industry risk score (or NBFI anchor in the case of an NBFI) indicates.
Adequate	An FI's business operations are representative of the industry risk score (or NBFI anchor in the case of an NBFI).
Moderate	An FI's business operations make it more vulnerable to adverse operating conditions than the industry risk score (or NBFI anchor in the case of an NBFI) indicates.
Constrained*	An FI's business operations make it significantly more vulnerable to adverse operating conditions than the industry risk score (or NBFI anchor in the case of an NBFI) indicates.
Weak§	The industry risk score (or NBFI anchor in the case of an NBFI) is not representative of the FI's high vulnerability to adverse operating conditions.

*The impact on the SACP is a deduction of two or three notches. We deduct two or three notches according to our relative assessment of how significantly more vulnerable the FI is to adverse operating conditions than the industry risk score indicates. §The impact on the SACP is a deduction of four or five notches. We deduct four or five notches depending on how highly vulnerable we think the FI is to adverse operating conditions. The determination of the number of notches for a constrained or weak assessment is informed by the three business position subfactors. If we identify a single, dominating weakness in any subfactor, we decide the appropriate deduction according to our view of the extent to which this weakness increases the FI's vulnerability to adverse operating conditions.

60. Entities that are in run-off typically have a business position of moderate or lower. Although, the assessment can be higher, for example depending on the ongoing benefits of group or government ownership for such entities, or the industry risk assessment and anchor.

Governance, management, and strategy

61. This subfactor considers ownership and governance, management's ability to execute operational plans in a consistent manner, and the consistency of strategy with organizational capabilities and marketplace conditions. Management's strategic competence, risk management, and operational effectiveness shape an FI's competitiveness in the marketplace and its financial condition.
62. If management plays a positive role in determining an FI's operational success, it is more likely to be able to manage important strategic and operating risks in the future. Alternatively, a weak management with an ineffective operating strategy or inability to execute its business plan effectively increases risk.
63. Examples of favorable characteristics for governance, management, and strategy include:
- Governance and conduct standards compare positively with the industry average;
 - Independent directors have strong influence, and a robust system of checks and balances exists in decision-making;
 - Management is more prudent and conservative than average in the industry. Management has proven execution capabilities and is a stable team. There is a track record of avoiding the strategic mistakes of other FIs (for example due to more positive governance characteristics than other FIs in the same industry);
 - Performance has been, and is likely to be, less volatile than average in the industry. Both

compensation and financial targets are focused on long-term value;

- Effective management of the cost structure that shows flexibility to manage costs and still addresses risks and investment needs; and
- Effective management of emerging and existing risks (for example due to technological, social, geopolitical, or climate-related developments) that could disrupt the FI's business and earnings, and emerging opportunities to strengthen the FI. Management proactively identifies emerging risks, assesses the impact of such risks under hypothetical situations, and takes timely action to mitigate their adverse impact as well as reacting decisively to risks that do arise. Additionally, management proactively identifies and assesses emerging opportunities to strengthen the FI's business and financial profiles and takes timely action to leverage such opportunities.

64. Examples of unfavorable characteristics for governance, management, strategy (any could weaken our assessment if material) include:

- Governance and conduct standards compare negatively with the industry average, for example in terms of planning for contingent risks such as cyber risk, or because of large-scale governance failures (for instance arising from the interaction of poor incentive structures and limits on managerial oversight);
- Management's strategies (including acquisition strategies) and financial targets--such as return on equity (ROE) and growth in earnings per share--are more aggressive than average for the industry;
- The entity depends on continuing service from key individuals or small teams;
- The entity shows limited checks and balances in decision-making processes, such as oversight over senior management;
- The organization operates with more complex corporate, legal, or tax structures, including relationships with controlling entities (this could be through loans to owners or owner-related entities, or owner-directed transactions with other owned-entities);
- Compensation schemes encourage short-term profit-taking;
- There is unplanned management turnover in critical senior positions;
- The FI has made recent acquisitions at prices that we consider aggressive compared with prices paid for recent transactions of comparable size and nature;
- There is ineffective management of the cost structure due to inflexible costs or cost management approaches that may generate future risks; and
- Management shows limited sensitivity to emerging and existing risks and opportunities (such as for example due to technological, social, geopolitical, or climate-related developments). The FI is often reactive and late in responding to emerging issues compared with peers.

Business stability

65. Business stability is the predictability of continuing business volumes in the face of economic and market fluctuations, including changes in customer preferences.
66. The criteria use measures of revenue stability, sustainability of market share, and the customer base to compare business stability with peers'. The comparative analysis focuses on the contribution of business lines to total revenues and earnings and on our estimates for their future

contribution. Business lines with recurring fee income and sustainable net interest income are more stable. Loss-making activities are generally more fragile than those contributing sustainable profits, while activities with thin margins may also be more fragile unless we determine that their contributions are sustainable.

67. We may also assess the extent to which an FI's business model or practices expose it to disruption or opportunities from existing or emerging developments (for example due to technological, social, geopolitical, or climate-related factors).
68. While larger market shares are not automatically more stable in terms of size or profitability, business lines with smaller numbers of customers may be vulnerable to changing conditions.
69. The following are examples of less stable income sources:
 - Trading income, including interest income from trading activities;
 - Net interest income coming from above-average asset-liability mismatches;
 - Other market sensitive income; and
 - Fee income from off-balance-sheet financing.
70. Favorable characteristics for business stability include:
 - The customer base is demonstrably "sticky," that is, there are long-standing customer relationships and they generate a high proportion of revenues. There is strong evidence that customers are likely to stay with the bank during a financial stress;
 - An FI is less reliant than the industry on pricing to retain customers;
 - Revenues are less sensitive to market perceptions of creditworthiness;
 - Favorable contractual terms, such as credit-related termination events or triggers, exist in many contracts with customers and counterparties; and
 - We consider that the FI has technological advantages for serving customers' developing needs, which may include that the FI has a sustainable automated end-to-end process for business execution.
71. Characteristics that suggest a potential instability of business lines include:
 - The relationship between customers and an FI is based on a series of one-off transactions open to market tender;
 - There are few or no direct relationships between the end customer and the FI. It relies on third parties to supply business volumes;
 - Recurring fee or interest income from long-standing customer relationships represents a lower proportion of revenues than average in the industry;
 - Revenues are more sensitive to market perceptions of creditworthiness than for the industry;
 - Customers may become more likely to switch to another entity due to social credit factors (such as consumer engagement or human capital management that could have a negative influence on the FI's reputation, or factors such as regulatory changes may reduce the entity's ability to originate or collect loans);
 - An FI relies more heavily on pricing to attract and retain customers than for the industry;
 - The FI has challenges maintaining its automated end-to-end process for business execution; and

- Unfavorable contractual terms such as financial covenants, credit triggers, and collateral requirements that are more demanding than for FIs with a similar industry risk score carrying out the same types of trades.

Diversification

72. Diversification of business activities is measured by the contributions of business lines and geographies to an FI's revenues and profits, compared with peers. An entity with a broader mix of business activity is generally lower risk, and an entity with a narrower mix is generally higher risk. Concentration in business activities can partly offset many of the strengths in the business position assessment.
73. Although it is possible for an FI with concentrated business to have a stable and sustainable business model, we consider whether concentrated business volumes or revenues may lead to less stable and predictable revenues.
74. Business diversification can be neutral to or a strength or weakness in an FI's business position. Successful and continuing diversification in established businesses supports a stronger business position. Successful international business diversification only arises if there is evidence that the international operations make the FI overall less susceptible to volatility in domestic business and economic conditions than is average for FIs in the home industry.
75. Successful diversification typically means that an FI's earnings have been more stable than the industry, particularly during periods of adversity, and management has not increased the FI's exposure or risk appetite materially. Another example could be if an FI develops expertise and becomes an industry leader in a climate change or transition-related niche that strengthens revenue stability.
76. Poor quality diversification weakens the overall business position. For example, an FI may weaken its overall business position if it enters new products and countries where it has limited expertise and lacks critical mass to be a real competitor to the incumbent market leaders. The weakness is greater when the new products or markets are riskier than the traditional core business.
77. We treat an FI as more concentrated than average for the industry when it has a more limited product range or geographic breadth, particularly for an FI with significant regional, product, or customer concentrations. Even if concentration is in a region, product, or customer segment that generally performs well, it may still be a weakness. We consider regional presence in the context of the size of the local or regional economy.
78. For example, a regional presence in a large diversified region in a very large country is less likely to give rise to concentration concerns than a presence in a small less diversified region. Another example may be if an FI's business activities and revenues are:
 - Heavily concentrated in geographies that are more prone to natural catastrophes, or
 - Originate from lending activities that may be socially sensitive (such as high exposures to unsecured consumer finance loans with very high interest rates or catering to a more financially vulnerable clientele) and exposed to material claims from clients, regulatory investigations, or reputational sensitivity regarding commercial and collection practices.

Capital And Earnings

79. Our assessment of capital and earnings reflects an FI's ability to absorb losses based on its level of capital and ability to replenish that capital through earnings and other sources (excluding extraordinary external support). This capital and earnings cushion provides protection to senior creditors while the entity remains a going concern. The analysis of capital and earnings comprises three steps.
80. **Step 1:** Determining whether the entity has breached or is in danger of breaching minimum regulatory requirements (where they apply) in order to maintain a bank license, other relevant regulatory license in the case of NBFIs, or BDC asset coverage requirements for BDCs. This assessment may cap the SACP. When a cap applies, then we do not carry out steps two and three, except when we are determining whether capital and earnings are constrained or weak.
81. **Step 2:** Setting an initial score for capital and earnings (subject to any cap that applies based on step one) based on the expected risk-adjusted capital (RAC) ratio before diversification for banks, securities firms, and certain fincos, or a leverage ratio for other fincos and BDCs. (We also use the debt-to-EBITDA ratio for certain securities firms.)
82. **Step 3:** Considering an adjustment to the initial capital and earnings score based on the impact of the FI's:
- Strength and quality of capital, which includes not only the composition of total adjusted capital (TAC) (such as reliance on hybrid capital and other potentially weaker forms of capital) but also other factors, such as its approach to capital management, the relative strength or weakness demonstrated by other capital metrics (including regulatory capital metrics where these apply), and financial flexibility; and
 - Earnings capacity and quality, largely reflecting the entity's ability to absorb losses and build capital through stable earnings.
83. Based on the three steps, we then assess capital and earnings on a six-point scale (see table 7).

Table 7

Capital And Earnings Assessment

--What it typically means*--			
	Bank anchor of 'bbb-' or better	Bank anchor of 'bb+' to 'bb-'	Bank anchor below 'bb-'
Very strong	We consider capital and earnings to be a material strength to the SACP, and the capital metric typically falls within the range for very strong shown in table 9, 10, or 11--depending on the type of FI.	We consider capital and earnings to be a material strength to the SACP, and the capital metric typically falls within the range for very strong shown in table 9, 10, or 11--depending on the type of FI.	We consider capital and earnings to be a material strength to the SACP, and the capital metric typically falls within the range for very strong shown in table 9, 10, or 11--depending on the type of FI.
Strong	We consider capital and earnings to be positive to the SACP, and the capital metric typically falls within the range for strong shown in table 9, 10, or 11--depending on the type of FI.	We consider capital and earnings to be positive to the SACP, and the capital metric typically falls within the range for strong shown in table 9, 10, or 11--depending on the type of FI.	We consider capital and earnings to be a strength to the SACP, and the capital metric typically falls within the range for strong shown in table 9, 10, or 11--depending on the type of FI.

Table 7

Capital And Earnings Assessment (cont.)

--What it typically means*--			
	Bank anchor of 'bbb-' or better	Bank anchor of 'bb+' to 'bb-'	Bank anchor below 'bb-'
Adequate	We consider capital and earnings to be neutral to the SACP, and the capital metric typically falls within the range for adequate shown in table 9, 10, or 11--depending on the type of FI.	We consider capital and earnings to be neutral to the SACP, and the capital metric typically falls within the range for adequate shown in table 9, 10, or 11--depending on the type of FI.	We consider capital and earnings to be positive to the SACP, and the capital metric typically falls within the range for adequate shown in table 9, 10, or 11--depending on the type of FI.
Moderate	We consider capital and earnings to be marginally negative to the SACP, and the capital metric typically falls within the range for moderate shown in table 9, 10, or 11--depending on the type of FI.	We consider capital and earnings to be neutral to the SACP, and the capital metric typically falls within the range for moderate shown in table 9, 10, or 11--depending on the type of FI.	We consider capital and earnings to be neutral to the SACP, and the capital metric typically falls within the range for moderate shown in table 9, 10, or 11--depending on the type of FI.
Constrained	We consider capital and earnings to be negative to the SACP, and the capital metric typically falls within the range for constrained shown in table 9, 10, or 11--depending on the type of FI. The impact on the SACP is a deduction of two or three notches depending on the degree to which we consider capital and earnings to be negative to the SACP. A relatively more negative impact leads to a deduction of three notches.	We consider capital and earnings to be marginally negative to the SACP, and the capital metric typically falls within the range for constrained shown in table 9, 10, or 11--depending on the type of FI.	We typically consider capital and earnings to be neutral to marginally negative to the SACP, and the capital metric typically falls within the range for constrained shown in table 9, 10, or 11--depending on the type of FI.
Weak	We consider that capital and earnings materially constrains the SACP, and the capital metric typically falls within the range for weak shown in table 9, 10, or 11--depending on the type of FI. The impact on the SACP is a deduction of four or five notches depending on the degree to which we consider capital and earnings to materially constrain the SACP. A relatively greater constraint leads to a deduction of five notches.	We consider that capital and earnings is negative to the SACP, and the capital metric typically falls within the range for weak shown in table 9, 10, or 11--depending on the type of FI. The impact on the SACP is a deduction of two or three notches depending on the degree to which we consider capital and earnings to be negative to the SACP. A relatively more negative impact leads to a deduction of three notches.	We consider that capital and earnings is negative to the SACP, and the capital metric typically falls within the range for weak shown in table 9, 10, or 11--depending on the type of FI. The impact on the SACP is a deduction of one or two notches depending on the degree to which we consider capital and earnings to be negative to the SACP. A relatively more negative impact leads to a deduction of two notches.

*For banks and NBFIs, we use the bank anchor to decide which column to use.

Compliance with regulatory capital requirements

84. The first step in analyzing capital and earnings is establishing how an FI performs against its regulatory capital requirements, using the regulatory capital definitions applicable to that FI. (This step does not apply for entities not subject to regulatory capital requirements, and they therefore receive a score of not applicable for this step.)
85. Meeting these requirements is a prerequisite for operating as a going concern, and a breach or potential breach can cap the SACP. An FI operating with capital close to or in breach of the

minimum requirements of the local regulator receives one of the following scores: at risk, subject to regulatory forbearance, or in breach. The caps on the SACP associated with these scores are 'bb+' when the score is at risk, and 'b-' for the other scores. If the 'CCC' criteria apply, the SACP is set according to the default scenarios in that criteria. An FI operating with capital that is not close to or in breach of the minimum requirement is scored as not at risk. (See table 8 for further details.)

Table 8

Regulatory Capital Requirement Assessment For FIs Other Than BDCs

What it typically means	
Not at risk	The FI meets, and is expected to continue to meet, the regulatory capital requirements for its license by more than a narrow margin. There is no cap on the SACP due to this score.
At risk	The cap on the SACP is 'bb+' when we expect an FI to meet regulatory capital requirements for its license--but by a narrow margin. For example, we typically consider less than 100 basis points to be a narrow margin. Although, if we think the ratio is calculated very conservatively under the relevant regulations and expect the ratio to be stable even under more stressed conditions, we may not consider a margin of less than 100 basis points as narrow. At this point, we regard an FI as at risk of breaching its regulatory requirements in case of plausible adverse developments. When the FI is at risk, capital and earnings are constrained at best.
Subject to regulatory forbearance	The cap on the SACP is 'b-' when the regulator allows an FI to continue operating even though it is in breach of minimum regulatory capital requirements to maintain its license. However, the SACP will be lower if the FI meets the conditions outlined in the 'CCC' criteria for an SACP in the 'ccc' or 'cc' categories. The regulator may allow an FI to continue operating when there is a breach if it gives it a waiver or a ruling that calculates regulatory capital requirements more generously than usual. The category also includes FIs that would be in breach of regulatory minimum requirements if they had reported losses in accordance with accepted accounting principles but did not. However, we would classify an FI as at risk if we expect the breach to be temporary and there is a credible plan in place agreed with the regulators to boost capital above minimum levels in the near term. We classify capital and earnings as weak when an entity is subject to regulatory forbearance.
In breach	The cap on the SACP is 'b-' when an FI is in breach of legal regulatory minimum requirements and there are no prospects for reaching them or for regulatory forbearance. However, the SACP will be lower than 'b-' if the FI meets the conditions in the 'CCC' criteria for an SACP in the 'ccc' or 'cc' categories. When using "in breach," we do not rule out that regulators may eventually intervene before the insolvency or closure of the FI--for example, to trigger a recapitalization--and we classify capital and earnings as weak.

SACP--Stand-alone credit profile.

86. To assess whether an FI meets regulatory capital requirements for its license, we consider the regulatory capital metric that the regulator uses to decide whether the FI meets licensing requirements or could have its license revoked. This minimum metric to maintain a license is often set at a lower level than ratios that regulators expect FIs to maintain for prudential purposes. (This would be lower than the entity-specific capital requirements that a regulator may impose on an FI to reflect its position within the financial system--for instance, a minimum regulatory capital requirement that includes buffers such as the domestic systemically important bank capital buffer, capital conservation buffer, and countercyclical capital buffer.)
87. For example, a regulator may require a bank to maintain at all times a common equity Tier 1 capital ratio of 4.5%, in line with typical Basel requirements, but may apply a higher requirement to a specific bank to reflect the various buffer expectations. We assess whether we expect the bank's license would be revoked if it breached its higher buffer requirements or whether a lower ratio would be applicable.
88. For banks, the minimum regulatory capital requirement is often expressed using ratios such as the regulatory common equity Tier 1 ratio, the Tier 1 ratio, and the total capital ratio, but

regulators may use other metrics, such as leverage ratios. If a regulator uses several regulatory capital metrics to assess whether an FI meets licensing requirements, then we consider each capital metric that would lead to the license being revoked.

Regulatory capital for BDCs

89. For BDCs, the consequences of breaching the asset coverage ratio, while less onerous than those for a bank breaching its capital requirements, are still meaningful, in our view, especially compared with fincos that have no prudential capital requirements.
90. When a BDC is at risk of breaching its regulatory asset coverage ratio, we typically limit the SACP or group SACP to 'bb+'. This is typically the case if there is less than a 10% cushion to our prospective estimate of the BDCs' asset coverage ratio, meaning 200%-220%, or 150%-165% if the BDC has adopted a modified asset coverage ratio of 150%. We typically score the BDC as not at risk when the asset coverage ratios are higher than these ranges. When a BDC is in breach of its applicable regulatory asset coverage ratio, we typically limit the SACP or group SACP to 'b+'. We do not score BDCs as subject to regulatory forbearance.
91. For a BDC that does not publicly report its asset coverage ratio, we may estimate the ratio based on the entity's financial statements, or use reported debt to equity as a proxy.
92. In addition, we may limit the SACP or group SACP to 'b-' (or lower if 'CCC' criteria apply) and capital and earnings to weak if, in our view, the BDC is at risk of having to sell substantial portfolio assets to meet the asset coverage ratio again and the prospects for such market transactions are uncertain.

Initial capital and earnings score

93. The initial capital and earnings score is determined by assessing capital using the expected RAC ratio before diversification for banks, most securities firms, and certain fincos (see table 9).
94. The expected RAC ratio reflects our expectations for the balance sheet, including earnings (except for securities firms) and anticipated capital management initiatives typically over the next one to two years, informed by the current year. The exposures and TAC used are based on recent complete financial or regulatory reporting, updated for new information and revisions to our estimations of components of TAC or the exposure inputs used to calculate S&P Global RWAs.
95. For banks, we forecast earnings, earnings retention, balance sheet growth, and other factors to arrive at the expected RAC ratio. The volatility in the earnings or balance sheets of many securities firms and fincos can make forecasting their capital more difficult than forecasting bank capital, which is typically subject to regulatory targets. For securities firms and fincos, we start with the RAC or leverage ratio from the most recent period and consider whether any factors, such as acquisitions, debt issuances, and large shareholder payouts, could significantly alter that measure on a forward-looking basis. For securities firms, the RAC ratio that we use in the initial score typically takes into account a material earnings buffer deficit.

Table 9

Initial Capital And Earnings Score For Banks, Securities Firms, And Certain Fincos Based On The RAC Ratio Before Diversification

Expected RAC ratio (%)	Initial score
>15	Very strong
>10 and <=15	Strong

Table 9

Initial Capital And Earnings Score For Banks, Securities Firms, And Certain Fincos Based On The RAC Ratio Before Diversification (cont.)

Expected RAC ratio (%)	Initial score
>7 and ≤10	Adequate
>5 and ≤7	Moderate
>3 and ≤5	Constrained
≤3	Weak

96. For certain securities firms that meet the following conditions, the initial capital and earnings score typically reflects our expectations for their debt to EBITDA (see table 10), which focuses on the key balance sheet risk that comes from their financing structures. This is the case for securities firms that:
- Have very limited credit and market risk associated with their business model (i.e., those where the following activities are minimal: amount of securities on their balance sheets, cleared or held customer positions, and counterparty risk or other credit and market risks),
 - We consider can operate on a going-concern basis without consolidated tangible equity, and
 - Have an initial assessment under table 9 of moderate or below.

Table 10

Initial Capital And Earnings Score For Certain Securities Firms Based On The Debt-To-EBITDA Ratio*

Debt to EBITDA (x)	Initial score
<3	Adequate
>=3 and <4	Moderate
>=4 and <6	Constrained
>=6	Weak

*We do not use this table when the initial score based on table 9 is adequate or better.

97. For fincos, the initial capital and earnings score reflects our expectation for either the entity's RAC ratio (see table 9) or leverage ratio (see table 11). The risk weightings in RAC are calibrated using historical data for banks. Therefore, we typically use the RAC ratio for fincos that hold assets with similar risks to the assets of banks in their given jurisdiction. We use the leverage ratio in other cases, typically when we view a finco's assets as materially riskier than a typical bank's assets in its jurisdiction.
98. Although fincos often do not underwrite the same assets as banks, we still use the RAC ratio where we can address relevant differences in risk position. Additionally, we could use the RAC ratio when a finco is subject to prudential regulation or has:
- Historical net charge-offs broadly in line with the normalized losses of the entity-specific portfolio under the RAC framework (RACF);
 - Significant off-balance-sheet exposures, such as provisions of guarantees or unutilized committed lines; or

- Material size of investments in junior or equity positions of securitized assets.
99. We may also use the RAC ratio when a finco holds assets with significantly lower loss expectations than those assumed in our leverage ratio. For example, this may apply when a significant portion of a finco's loans are credit enhanced by highly rated guarantors.
100. We may use the leverage ratio in other cases, typically when we view a finco's assets as materially riskier than a typical bank's assets in its jurisdiction. Examples of when we may use the leverage ratio include when a significant proportion of a finco's exposures include:
- Nonprime consumer loans (such as unsecured personal loans and deep-subprime auto loans);
 - Significant second-lien, subordinated, or mezzanine loans;
 - Unsecured commercial and industrial loans, particularly leveraged loans;
 - Concentration in development, transitional, and construction real estate loans;
 - Non-lending assets, such as equity and real estate investments; or
 - Other nontraditional or esoteric assets that are not addressed directly in RACF.
101. We typically use the leverage ratio when the majority of the finco's exposures include these items. The choice of RAC or leverage ratio is typically consistent for fincos in the same market subsector with similar business models and exposures.
102. Regardless of which measure we apply for our initial capital and earnings score, we use the risk position assessment to refine our view of an FI's actual and specific risks, including lending and underwriting standards of fincos relative to banks in their markets.
103. For BDCs, we use leverage because they mainly invest in leveraged loans, and in some cases second-lien loans and/or equity.

Table 11

Initial Capital And Earnings Score For A Finco (Including BDCs) Based On The Leverage Ratio

Leverage (debt to adjusted total equity) (x)	Initial score
<= 1.5	Very strong
>1.5 and <=2.75	Strong
>2.75 and <=4.5	Adequate
>4.5 and <=6.5	Moderate
>6.5 and <=12	Constrained
>12	Weak

Adjustment to the initial capital and earnings score

104. In the final step, we may adjust the initial capital and earnings score by one category up or down based on the quality, management, and flexibility of capital, as well as our view of earnings capacity and quality. This is to arrive at the final capital and earnings assessment, which considers the degree to which capital and earnings are positive, neutral, or negative to the SACF. The capital measures in the second step are important indicators in our analysis of an FI's ability to absorb losses, though we also consider our view of both capital and earnings to provide a more robust picture of an entity's ability to absorb losses.

105. In deciding whether to factor in an adjustment, we consider an FI's capital measures relative to the initial scoring thresholds in the step two tables. The focus is on whether the relative strength or weakness demonstrated by other relevant metrics, such as leverage, the ability to build capital through earnings and other sources, or regulatory metrics, suggest that the initial score materially under- or overstates capital and earnings.
106. We base our analysis of the quality, management, and flexibility of capital on a number of factors and ratios--some applicable to all types of FIs and some particular to certain types of FIs. For all FIs, examples of factors we may consider include:
- What portion of capital is made up of hybrid instruments, which typically have a lower ability to absorb losses than common equity;
 - Whether other measures of capital not considered in step two, such as regulatory metrics or other measures of leverage and capital, may reflect a stronger or weaker capital position than that reflected in the capital measure in step two;
 - The level of reserves for loan losses and whether they may add significantly more or less to loss absorption ability (perhaps because of differences in accounting standards);
 - The approach to capital management exercised by the entity's management, board, and shareholders and whether the capital measure in step two could change materially over a longer period;
 - The proximity of the entity's regulatory capital metrics to any regulatory requirements and how this affects its flexibility to manage capital;
 - Financial flexibility--the degree to which we consider that the entity could plausibly materially boost capital by reducing share repurchases, calling committed capital, or through other means that would not significantly damage its franchise, earnings capacity, or investor confidence;
 - Double leverage to the extent that this is not captured in the ratio used in the initial score and when the initial score is based on the ratio of an entity owned by a nonoperating holding company; and
 - Any material constraints on the flow of loss-absorbing capital among group members.
107. When assessing whether the capital measure in step two could change materially over a longer period, we look beyond the forecast period incorporated in the initial score.
108. When assessing double leverage, we define it in accordance with our group rating methodology. Double leverage renders the NOHC dependent, in part, on dividends to meet interest payments on external debt. Double leverage is relevant particularly when the measure of capital that we use in step two is not calculated on fully consolidated accounting data that combines holding company financials with those of its operating subsidiaries.
109. High double leverage is a sign of aggressive capital management and may lower the quality of an FI's capital. We typically see 120% or more as high double leverage, depending on the extent to which this ratio is inflating the capital ratios associated with the subsidiaries.
110. We base our analysis of earnings capacity and quality on a number of factors and ratios--some applicable to all types of FIs and some sector-specific. We look at quantitative and qualitative indicators of an FI's ability to internally generate capital to support its business franchise and cover losses.
111. For all FIs, we consider reported and expected core earnings relative to either regulatory risk-weighted assets (RWAs), S&P Global RWAs, or reported assets, depending on the sector. Our

assessment of earnings quality considers factors such as the proportion of revenues from stable, recurring sources; earnings volatility; and the frequency of nonrecurring revenue and expenses. We can also consider other relevant metrics, including cost metrics and net interest margins. We may also use this adjustment to take account of the capacity for earnings to cover normalized losses.

112. For entities for which we use the RAC ratio, we may use the earnings buffer to measure the capacity for earnings to cover normalized losses as part of our assessment of the quality of earnings and our expected ratios. Normalized losses, which are calculated as part of our RAC criteria, are an estimate of what we expect an entity to report in credit losses on average throughout a credit cycle.
113. For securities firms, we typically use a three-year historical annual average of the earnings buffer. For banks, we typically average the most recent financial year plus our expectations for the current year and the next year. We typically do not calculate an earnings buffer for fincos. We calculate the earnings buffer in a given year in the following steps.

Calculation Of The Earnings Buffer In A Given Year

Preprovision operating income

+/- One-off items that are included in preprovision operating income

- Normalized credit losses

= Normalized operating income

Earnings buffer = Normalized operating income/S&P Global RWAs

114. In contrast to credit losses, other market or operational losses are generally unexpected and therefore intended to be covered by capital. Consequently, when earnings are most sensitive to market and operational risks, we interpret the earnings buffer with caution. For FIs with significant market risk, the earnings buffer may look relatively strong, but the measure may not take into account the volatility associated with market risk. This volatility is assessed more qualitatively in quality of earnings.

Additional considerations for the capital and earnings adjustment

115. **Additional considerations for banks.** When considering whether other measures of capital may reflect a stronger or weaker capital position than that reflected in the initial capital and earnings score, we may consider regulatory ratios such as Tier 1 and leverage ratios where these apply. For instance, a particularly strong leverage ratio, materially in excess of peers, could contribute to a positive adjustment, particularly when the RAC ratio is at the higher end of the range factored in the initial assessment. Other metrics only move our view of capital and earnings if their highlighting of other factors has a sufficiently material effect on our initial view derived from RAC.
116. We view favorably bank earnings that have high levels of risk-adjusted core earnings driven by strong and stable sources of revenues (with limited dependence on market-sensitive income), low credit loss experience even during adverse periods, and dividends that are unlikely to materially offset capital generation from earnings. We typically consider core earnings relative to S&P Global RWAs or regulatory RWAs.

117. In other words, we view favorably banks that could likely build meaningful capital--without reducing their dividends--even after absorbing some decline in revenue and a level of credit losses likely to occur under adverse conditions. We view unfavorably banks that would likely significantly deplete capital under such a scenario.
118. In addition, we consider supplemental data that may assist us in determining the level and stability of these ratios. For instance, we may assess how various sources of fees may change in adverse scenarios. Cost and net interest margin metrics can also inform our view.
119. **Additional considerations for finance companies (including BDCs).** When a finco's RAC ratio or leverage ratio, as applicable, is near the threshold of a higher initial capital and earnings score, we could raise the assessment if all of the following apply:
- The issuer, because of strong and stable earnings, has a high capacity to absorb losses through the credit cycle--meaning that its earnings before credit and market losses are likely to exceed credit and market losses even when those charges peak in the credit cycle;
 - The issuer generates sufficient earnings to support its balance sheet growth without substantial increases in leverage; and
 - The issuer has the willingness and ability to build capital through retained earnings.
120. When a finco's RAC ratio or leverage ratio, as applicable, is near the threshold of a lower initial capital and earnings score, we could lower the assessment if any of the following apply:
- The issuer, because of weak or volatile earnings, has a poor capacity to absorb losses through the credit cycle--meaning that credit and market losses will likely exceed earnings before such charges at points in the credit cycle;
 - The issuer doesn't generate sufficient earnings to support its balance sheet growth without substantial increases in leverage;
 - The issuer's willingness and ability to build capital through retained earnings may be limited. For example, requirements to distribute earnings to maintain favorable tax treatment (such as REITs) or shareholder expectations for returns of capital; or
 - The presence of private equity ownership is expected to add substantial leverage.
121. When analyzing earnings capacity and quality as part of considering an adjustment, we primarily consider performance over the last three to five years (or longer), as well as our forward-looking expectations for:
- Return on average assets (%),
 - Net interest margin (%),
 - Loan loss reserves to gross receivables (%), and
 - Net interest income to operating revenues (%).
122. We may also consider the following metrics for BDCs:
- Realized return on average portfolio investments (%),
 - Non-deal-dependent income interest coverage (x), and
 - Non-deal-dependent income coverage of both interest and dividend (x).

123. **Additional considerations for securities firms.** When considering the strength and quality of capital and whether other measures of capital not considered in the initial capital and earnings score may reflect a stronger or weaker capital position than that reflected in the capital measure in step two, we consider non-risk-adjusted leverage using the below leverage ratio. We typically consider a leverage ratio below 3% to be indicative of excessive leverage that weakens the overall assessment.

Leverage Ratio

We calculate a securities firm's leverage ratio in one of the two ways below, based on the level of detail provided in financial reporting to address netting for reported balance sheet derivatives:

A: Leverage ratio = ACE/adjusted assets. For firms that report derivative positions net by counterparty (as under U.S. generally accepted accounting principles)

B: Leverage ratio = ACE/(adjusted assets – 90% of derivatives receivables). For firms that report balance sheet derivatives on a gross basis (as under IFRS)

124. When analyzing earnings capacity and quality of a securities firm, we also typically consider:
- Three-year average core earnings to average S&P Global RWAs before diversification,
 - Recurring revenue to total revenue,
 - Dividend payout ratio,
 - Asset-liability mismatches,
 - The flexibility of the expense base relative to the variability of revenue,
 - Trading income to total revenues,
 - Investment banking revenue to net revenue,
 - Other market-sensitive income to total revenues,
 - Other revenues to total revenues, and
 - Cost-to-income ratio.
125. For a securities firm, a ratio of three-year average core earnings to S&P Global RWAs above 2% typically indicates stronger earnings capacity, while a ratio below 75 bps typically starts to indicate weaker earnings capacity. Limited debt service capacity, as measured by net interest margin or interest coverage, would also typically be an indication of weaker earnings capacity. For securities firms operating for fewer than three years, earnings capacity is, at best, considered neutral to the assessment.
126. Financial sponsor ownership (for example, by a private equity company) could lead to a negative adjustment to the capital and earnings score if we expect it to lead to higher leverage over time.
127. When considering double leverage for a securities firm, we also look at total equity double leverage, defined as holding company investments in subsidiaries divided by holding company (unconsolidated) common shareholders' equity, minority interest, and preferred stock.
128. When we use the debt-to-EBITDA ratio, the quality of earnings and cash flow, and debt service

capacity are important in determining the adjustment as well as the impact of capital and earnings assessments of constrained and weak (in number of notches). Weakness in the quality of earnings or cash flow, or in debt service capacity, could lead to a negative adjustment to the initial score and could influence the impact on the SACP, in number of notches, of a constrained or weak assessment. Securities firms with negative tangible equity at the consolidated level would typically not have a final capital and earnings assessment above adequate.

129. When analyzing securities firms on the basis of debt to EBITDA, we consider gross debt and calculate EBITDA as revenue minus operating expenses (excluding interest expense on the gross debt used, stock-based compensation, depreciation, amortization, and nonrecurring or noncash items on a case-by-case basis). However, we typically do not adjust for the amortization of loans to retain or recruit financial advisers. We focus on historical data while also considering whether any factors (such as acquisitions, debt issuances, and large shareholder payouts, among other things) could significantly alter the measure.

Risk Position

130. We use the risk position assessment to refine our view of an FI's risks beyond the capital and earnings analysis. As such, we assess factors other than those reflected in the capital and earnings adjustment, such as asset quality and risks related to other exposures. We do not have any set weighting on these factors, which are listed below, and instead take a holistic approach depending on the nature of the entity and its exposures. These factors are:

- Risk appetite: This covers growth and changes in exposures, including to environmental, social, and governance-related risks;
- Loss experience and expectations: A comparison of past and expected losses on the current mix of business with those of peers and the loss experiences during past economic downturns. Greater-than-average losses may indicate a weaker risk position;
- Concentrations: The impact of risk concentrations or risk diversification;
- Complexity: How increased complexity adds risk;
- Other material risks that are not addressed within our capital and earnings assessment (such as environmental risks that are difficult to quantify or capture within the timeline of the expected RAC ratio--for example, potential losses due to the effects of climate transition and weather events on lending and investment portfolios);
- For fincos and BDCs, lending and underwriting standards relative to banks in their markets; and
- For securities firms, sector-specific aspects relating to credit and market risk management.

131. For an FI, we combine our views of these factors to arrive at an overall risk position assessment (see table 12). The subfactors may reinforce or weaken each other. The focus is on identifying risks or attributes and determining whether they combine to further increase or reduce overall risk.

Table 12

Risk Position Assessment

	What it typically means
Very strong	FI-specific risks or attributes mean that it is materially better placed to withstand economic stress than the capital and earnings assessment indicates.

Table 12

Risk Position Assessment (cont.)

	What it typically means
Strong	FI-specific risks or attributes mean that it is better placed to withstand economic stress than the capital and earnings assessment indicates.
Adequate	FI-specific risks or attributes mean that it is able to withstand economic stress in line with the capital and earnings assessment.
Moderate	FI-specific risks or attributes mean that it is somewhat less able to withstand economic stress than the capital and earnings assessment indicates.
Constrained*	FI-specific risks or attributes mean that it is less able to withstand economic stress than the capital and earnings assessment indicates.
Weak§	FI-specific risks or attributes mean that it is considerably less able to withstand economic stress than the capital and earnings assessment indicates.

Note: The determination of the number of notches for a constrained or weak assessment is informed by our assessment of the risk position elements and the extent to which these affect the representativeness of the capital and earnings assessment. *The impact on the SACP is a deduction of two or three notches. We deduct two or three notches according to our relative assessment of how less able the entity is to withstand economic stress than the capital and earnings assessment indicates. §The impact on the SACP is a deduction of four or five notches. We deduct four or five notches depending on our relative assessment of how less able the entity is to withstand economic stress than the capital and earnings assessment indicates.

Risk appetite

132. We monitor an FI's risks and whether any risks have increased or decreased as an indicator of changes in future exposures and losses. A change in risk appetite or profile could mean that traditional expertise that has helped an FI in previous market or economic downturns may not help as much in the future.
133. Over time, quantifiable measures of risk can typically demonstrate a management's risk appetite and tolerance across its activities, including measures of credit, market, and operational risk. However, we take a prospective view of risk levels and exposures, which management's demonstrated risk appetite and tolerances inform. We also seek to look through what may be temporary variations in risk metrics to assess longer-term risks.
134. We assess recent trends in risk measures and management's stated risk goals to determine whether a firm's risks are growing, shrinking, or otherwise changing materially from what was incorporated in the capital and earnings assessment. We consider the degree to which these are indicative of a material change in risk appetite or tolerance or simply a response to short-term environmental factors. We may consider how lending and underwriting and business approval standards and practices link to risk appetite, as well as the robustness of the techniques used in monitoring and managing exposures.
135. The following are examples of features that may suggest that an FI has good capacity to manage growth and changes in exposures:
- Showing lower recent organic or acquisitive growth and modest prospects for future growth than in the past and compared with peers, when the lower growth is based on avoiding risk and declining riskier growth opportunities that other FIs are willing to take;
 - Maintaining lending and underwriting standards despite competition;
 - Reducing its risk exposure, for example by exiting risky activities or tightening underwriting standards;

- Remaining focused on serving its core customer base with traditional expertise and limiting opportunistic proprietary activities; or
- Keeping a similar portfolio of risks that limited losses experienced in previous economic downturns.

136. Management may not have the capacity to manage additional risk presented by growth or other changes in exposure when an FI is displaying one or more of the following trends:

- Showing more aggressive recent organic or acquisitive growth and more significant prospects for future growth than in the past and compared with those of peers;
- Moving significantly into new product, customer, or market activities outside of its traditional area of expertise; or
- Displaying weakening underwriting standards relative to peers with similar economic risk scores. Examples of this include a prime mortgage lender materially weakening its standards on a loan applicant's capacity to pay, borrower credit standing, or collateral coverage. (This could be measured by a loan-to-value ratio, a senior secured commercial real estate lender underwriting more mezzanine or corporate development loans, or an entity increasingly underwriting larger or riskier transactions.)

Loss experience and expectations

137. Here we consider the outcomes resulting from an entity's risk position. A stronger risk position is typically associated with relatively lower projected losses than for peers with a similar economic risk score and similar product mix, and a better-than-average track record of losses during periods of similar economic stress. Conversely, weaker risk positions are typically associated with losses that are greater than average for peers with a similar economic risk score and similar product mix, or a worse-than-average track record of losses during recent periods of similar economic stress. We compare NBFIs with peers with similar anchors instead of similar economic risk scores.

138. When we use our RAC framework or leverage to assess capital and earnings for an FI, we also consider whether the loss experience (and loss expectations if we expect them to differ materially from past experience) is above or below the RAC loss assumptions or above or below those of peers with similar leverage.

139. Examples of information that may inform our view of loss experience and expectations include:

- Credit provisioning and loss recognition that may be more or less aggressive than for peers, incorporating historical and expected nonperforming assets, including where this may be due to regulatory or other customer forbearance measures;
- The potential impact of ongoing fiscal, monetary, and government policy measures on credit losses;
- Volatility in an equity portfolio that may be lower or higher than the regulatory capital or RACF charges incorporated in the capital and earnings assessment; and
- Legal or regulatory costs or fines that can be higher or lower than for peers in the same lines of business.

Concentrations

140. We assess the diversity of risk exposures because risk concentrations are one of the primary reasons for FI failures. Demonstrated diversity of risks can lead to lower overall losses relative to less diverse peers if the diversification is effective. Whereas the business position assessment captures concentrations or diversification in revenue contribution by business line, risk position focuses on the concentration of exposures to individual borrowers, counterparties, industries or sectors, or asset classes and risk types.
141. There is a risk diversification benefit when, for example:
- Geographic diversification arises from exposures that are clearly connected with a client franchise abroad and not from opportunistic product, tax, regulatory, or currency arbitrage; and
 - Sector or risk-type diversification arises from operations in activities that are no more risky than the FI's traditional core business.
142. Material risk concentrations arise, for example, from one or more of the following:
- Risk exposures by sector, country, or single name in the loan portfolio, investment portfolio, and the trading book are significantly more concentrated than for peers with similar economic risk scores (for example due to material environmental or climate transition-risk-related exposures including those related to fossil fuels or environmentally damaging physical commodities or to assets that act as collateral for loans, such as residential properties with weak insulation features or that are subject to flood risk). Other examples could include overexposure to an agricultural sector with heightened vulnerability to climate change or to a sector that is likely to see a material disruption from customer or behavioral changes or changing environmental or social regulations, including high carbon transition risks.
 - Underlying risk exists that affects several risk types.
 - The FI transacts with a limited number of counterparties and maintains a material amount of counterparty or other trading party exposure in contracts such as derivatives, lending facilities, or repurchase agreements with margin arrangements or other potential exposure. Such exposures are material and concentrated across few trades and/or counterparties.
143. We assess material risk concentrations using metrics such as:
- TAC compared with the largest 20 obligor exposures, and
 - Regulatory capital (when applicable) compared with the largest 20 obligor exposures.

Complexity

144. Complexity either is neutral to or weakens our view of risk position, depending on the degree to which it increases or obscures risks. However, the absence of complexity, in and of itself, is rarely sufficient to improve overall risk position.
145. Greater scale may bring diversification benefits but may also increase complexity. An ever-increasing level of complexity in products, business lines, regions, and organizational structure may outpace capacity to manage risk. Complex organizational structures, product offerings, revenue sources, funding structures, and intragroup exposures all heighten an FI's risk profile. We do not give credit for diversification to highly complex institutions that are most difficult to manage.

146. We consider how complexity may add or obscure risk, including from factors such as:

- Amount of business in complex products, such as derivatives, securitizations, and structured credit such as collateralized debt obligations (other examples of complex products may be those involving significant legal or regulatory risks or the potential for costly litigation arising from weaknesses in governance, risk appetite, or the control framework, for instance due to risks such as money laundering or mis-selling to retail clients);
- Transparency of underlying risk positions, risk management, earnings generation, or asset valuations, including off-balance-sheet activities;
- Reliance on mathematical models and their underlying assumptions to measure and manage risk and to value assets and liabilities;
- Dependence on model-controlled or otherwise automated trading technology to execute a high volume of trades or as part of complex trading strategies;
- Exposure to low probability of occurrence but high-loss severity event risk, otherwise known as tail risk;
- Use of regulatory arbitrage to manage the balance sheet;
- Span of operations across jurisdictions, business lines, organizational structure, or legal entities, which may stretch management's capacity to observe and address risk; and
- Whether silos in the approach to risk management may hinder a consistent measurement and management of risk exposure.

147. Examples of information that we may look at when considering potential trading-related risks include reviews of the results from an entity's stress and scenario testing, policies, risk limits, practices, and the organizational structure in trading risk management, as well as policies and practices regarding risk measurement. We may also consider factors such as accounting Level 3 assets held by the FI, back-testing exceptions, risk limits that are especially large or frequently exceeded, and volatility in value at risk (VaR).

Other material risks

148. If other risks (including those associated with the trading book, illiquid or difficult to value securities, and underwriting-related risk) represent material additional risk beyond that reflected in the capital and earnings assessment, this may support a lower risk position assessment. Common risks that are not addressed within the capital and earnings assessment include structural interest rate and currency risk and the volatility of employee benefit funding.

149. There also may be other, less common risks relevant to an individual FI or segment of the market that the capital and earnings assessment either does not capture or may not fully reflect. For instance, operational risk (including operational risks that could lead to conduct-related regulatory and compliance actions such as fines) may be more significant than reflected in capital and earnings. If we consider such risks to be material for an entity, they may influence the overall risk position assessment.

150. **Interest rate and currency risk.** The assessment of interest rate risk includes structural interest rate risk, which arises based on the nature of assets, and strategic interest rate risk, including stemming from funding choices (such as short-maturity funding for longer-maturity assets).

151. The assessment of currency risk includes the sensitivity of projected earnings and capitalization to changes in currency exchange rates. For example, this may occur when a firm has a material

currency mismatch between a capital base denominated in local currency and assets denominated in foreign currency. The risk position assessment is weaker when currency risk is larger than for peers with similar economic risk scores.

152. Factors that we may review when assessing interest rate risk include:

- The sensitivity of an FI's projected earnings and reserves to changes in interest rates or the shape of the yield curve based on its own stress testing;
- Senior management's engagement and awareness for setting and managing the amount of interest rate risk;
- The degree of maturity gap between repricing assets and liabilities; and
- The adequacy of an FI's risk management based on a review of its scenario and stress testing as it pertains to shifts in interest rates, its exposure to assets or liabilities with embedded options held by counterparties including prepayment or extension options, or other behavioral characteristics that differ from contractual ones.

153. **Volatility of employee benefit obligation funding.** This factor considers whether an FI faces additional risk from potential movements in the values of the employee benefit schemes' assets and liabilities, particularly for defined benefit pensions, above those incorporated in the capital and earnings assessment.

154. This additional risk depends on the size of the scheme's liabilities; key actuarial assumptions, including the discount factor and other investment return assumptions, life expectancy, or future salary increases; and other variables such as the investment policy and amount of reinsurance used. The combined impact of the size of the scheme's liabilities and the sensitivity to changes in one of these variables can have a material impact on the entity. Pension scheme valuation reports typically identify the impact on scheme liabilities from changes in some of the assumptions and variables. An example of such a sensitivity test is the impact on liabilities by increasing participant life expectancy by one year.

155. **Operational risk.** We consider here whether there are material or recurring operational risks over the level incorporated in capital and earnings. Examples of operational risk that could be material to creditworthiness include losses attributable to technology failures (including cyber risk), operational errors, fraud, and legal or regulatory actions (for example, related to consumer protection shortcomings).

156. Our assessment is typically neutral when we consider that an FI has adequate systems, policies, and practices to manage its operational risks. Material operating risks, or inadequate systems, policies, or practices, contribute to a weaker risk position assessment.

157. **Risks associated with non-FI businesses.** We also consider situations where an entity may have to provide material support to non-FI businesses within its group, because of, for example, capital shortfalls at these entities.

Lending and underwriting standards for fincos and BDCs

158. For a finco or BDC, we compare its lending and underwriting standards with those of banks in the same country. Underwriting to a weaker standard than that of the typical bank suggests that the loss assumptions in RAC underestimate potential losses. If a finco has superior lending and underwriting standards relative to the typical bank, this may contribute to a stronger risk position assessment.

159. Fincos often do not underwrite the same assets as banks and focus on niches. We use the bank standards to consider what level a finco would write to if it were to underwrite the same types of assets as banks given what we see in the standards applied to the asset classes the finco finances.
160. The assessment of lending and underwriting standards is qualitative and guided by the factors relevant to the loan book, such as:
- Exposure to subprime consumer loans;
 - Exposure to second-lien, subordinated, mezzanine, leveraged, and/or cash flow commercial loans;
 - Exposure to higher-risk development, construction, and transitional commercial real estate loans; and
 - Holdings of non-lending assets, such as equity and real estate owned.

Additional considerations for BDCs

161. We typically assess risk position as no better than constrained for a BDC if we expect it to maintain an at-cost concentration to a single obligor in excess of 15% of ATE or in excess of 50% of ATE for its top five exposures (unless already deducted from capital dollar for dollar as outlined in our definition of ATE), and if we expect these concentrations to continue for more than two quarters. When assessing a BDC's exposure to a single obligor, we may consider the total investments (whether loans, debt securities, or equities) in a portfolio company and its closely related affiliates.
162. For a BDC, we also consider the risk associated with the volatility that mark-to-market assets add to the balance sheet. Significant volatility of marks, relative to peers, if indicative of a portfolio weakness not already addressed elsewhere, typically results in a risk position assessment no stronger than moderate.

Additional considerations for securities firms

163. **Risk appetite.** The higher a firm's risk appetite, the less reliable even recent results or metrics (including static financial information used as a base case for our RAC) are as a measure of its prospective risk levels, losses, or capital adequacy. To consider how growth and changes in exposure or risk appetite can affect prospective risk beyond that captured in the RACF, we consider both indications of the level of and changes in risk appetite, as well as trends in the level and type of risk exposures.
164. A management's risk appetite is manifested in the trade-offs it is willing to make between profitability and risk, especially during periods of heightened market or credit risk. We consider a firm's risk appetite in the context of our outlook for market and economic conditions and relative to peers with similar anchors. Management that is willing to reduce risk and lower profitability in anticipation of heightened market or credit risk or otherwise challenging business conditions can support a stronger risk position. Management that takes on risk and is unwilling to accept lower profitability, or to slow organic or acquisitive growth, suggests an aggressive risk appetite and a lower risk position assessment.
165. External oversight of a firm's risk management data and methodology, from particularly strong regulatory oversight, audited regulatory reporting, or other strong external confirmation of the risk oversight, can help us better draw conclusions on the level and trend in exposures and risk

appetite. In the absence of this, a particularly strong risk appetite assessment by itself would typically only be able to raise the risk position assessment to strong.

166. We also consider whether recent growth or shrinkage in S&P Global RWAs (where applicable) may be a short-term response to a change in business or market environment and not represent a material long-term change in risk appetite.

167. Examples of how risk appetite or growth and changes in exposure may increase prospective risk relative to what is captured in the RACF, particularly when combined with insufficient management capacity to manage it, that would typically weaken the risk position, include:

- Showing more aggressive recent organic or acquisitive growth and more significant prospects for future growth than in the past or compared with peers with similar anchors;
- Moving materially into new product, customer, or market activities outside of its traditional area of expertise;
- Increasing S&P Global RWAs, VaR, trading assets, and trade and underwriting volumes, or decreasing its ratio of adjusted common equity (ACE) to total managed assets relative to historical levels and peers';
- High volatility of daily or weekly trading profit/loss figures or VaR compared with peers, or outsize daily and weekly trading losses versus peers;
- Management's stated return/risk objectives, limits, and growth (such as trends in market volumes and portfolio holdings) are higher than peers or are increasing relative to historical levels;
- Frequent or large changes in or breaches of stated risk limits or standards (i.e., securities inventory aging, position losses [actual or stressed], customer credit, or margin rules or position limits);
- Regulatory compliance track record or recent material issues;
- Increasingly offering bridge financings, underwriting more on a committed basis, or otherwise increasing the amount of the firm's capital committed to generate business or otherwise high or increasing direct exposure to investment banking clients;
- Increasingly acting as principal in trades for clients as opposed to acting as an agent;
- Displaying weakening credit underwriting standards relative to peers with similar anchors; and
- Taking on riskier, more marginal clients or supporting riskier client activity.

168. Examples of risk appetite and growth and changes in exposure that can demonstrate decreasing prospective risk relative to what is captured in the RACF and therefore support an adequate or stronger risk position include:

- Reducing or exiting risky activities (for example, acting more as an agent for clients than as a principal in transactions);
- Shrinking total exposure by reducing the amount or improving the quality of positions;
- Remaining more focused on serving its core customer base with traditional expertise and limiting opportunistic proprietary activities;
- Keeping to a similar portfolio of risks that limited losses in previous economic or market downturns; and
- Decreasing S&P Global RWAs, VaR, trading assets, and trade and underwriting volumes, or

increasing its ratio of ACE to total managed assets relative to historical levels and peers', which we expect to continue.

169. **Complexity.** For securities firms, a quantitative indicator--a high ratio of total managed assets to ACE that is not mirrored in a low and declining RAC ratio--can indicate additional risk from complexity. The ratio of total managed assets to ACE is a measure of leverage, insensitive to risk and susceptible to definitional accounting inconsistencies. Nevertheless, high multiples may capture risk exposures that other metrics do not capture. In such cases, the risks, which weaken creditworthiness, likely are the result of off-balance-sheet activities or large derivative positions, implying complexity and opaque risks.
170. **Risks not fully covered in capital and earnings.** For securities firms, in addition to pension and interest rate risks, we may also consider the materiality of additional risk beyond that reflected in the capital and earnings assessment, particularly associated with the trading book, illiquid or difficult to value securities, and underwriting-related risk. When these represent material additional risk beyond that reflected in the capital and earnings assessment, it would support a lower risk position assessment. These risks (which may also be relevant for assessing risk position for banks with trading operations) may include:
- Less reliable information is used to calculate RAC (i.e., the entity has a history of material errors or restatements of VaR).
 - There may be a challenge assessing prospective intraday and intra-period exposure levels (for example, when intra-day or intra-period exposures may exceed the risk captured in end-of-day or end-of-period metrics, such as VaR, used in RAC).
 - Substantial potential exposure is not covered by RAC (i.e., underwriting is "committed" and thus payment is obligated, as opposed to underwriting that is on a best-efforts basis).
 - The firm has experienced outsize historical volatility of its S&P Global RWAs and RAC results (including due to seasonality).
 - Adjusting S&P Global RWAs or TAC for the following would materially lower the RAC ratio: illiquid positions (e.g., illiquid currencies or illiquid stocks) for which the one-year capital horizon in the RAC framework is not appropriate; Level 3 assets in excess of 25% of TAC; significant exposure to very low probability potential losses not captured by the 99%-VaR but captured by other metrics such as stress tests or expected shortfalls; and materially deficient loan loss reserves.
171. **Credit and market risk management.** Credit and market risk management considers a firm's capacity to manage the principal risks it faces: credit, counterparty, and market risks. We consider whether a securities firm's risk oversight and control capabilities are sufficient for the level, nature, and complexity of its credit and market risk exposures and management's stated risk appetite.
172. Successful credit and market risk management is typically confirmed through loss history comparable or superior to peers' and loss expectations equal to or below the assumptions underpinning the RAC framework. Good risk management by itself does not raise the risk position assessment, but it supports an adequate or higher risk position when there are other strengths. We typically assign a risk position assessment of no higher than moderate if we see material deficiencies in risk management.
173. We consider a firm's credit and market risk management policies, resources, infrastructure, and history to assess its capacity to assess, monitor, and control exposures to these risks. Effective

risk management for firms with complex or higher credit or market risk requires heightened efforts, including model validation and other stress-testing policies and procedures, back testing, and refining of methodology and assumptions used in risk measures and stress testing. We consider a firm's trading results and exposures compared with risk measures and limits, as well as risk managers' authority, oversight, and ability to monitor and control limits in real time.

174. Examples of credit and market risk management deficiencies that could lower the risk position assessment, and possibly cap it at moderate, include:

- Incomplete scope or reach of risk-monitoring capabilities, including record keeping that lacks complete, detailed data on material breaches of controls or policies and how they are remedied, or inaccurate risk measures;
- A high number of back-testing exceptions;
- Materially large or frequently exceeding stated risk limitations (i.e., securities inventory aging, position losses, margin rules, or desk position size);
- Undue volatility in VaR, for example, reflective of weaker hedging, including a wide gap between the highest observed VaR and the average VaR in recent periods; and
- Risk limits that frequently change or are outsize on an individual trader or desk basis.

175. **Loss experience and expectations.** Even what appears to be particularly strong risk management capabilities can only support a stronger risk position assessment when confirmed by lower historical and expected losses.

176. Other indications of weaker loss experience and expectations include:

- Credit provisioning and loss recognition that may be more or less aggressive than for peers;
- Volatility in the valuation of the securities portfolio that suggests that the RACF may underestimate capital needs;
- Legal or regulatory costs or fines that are high in an absolute sense, or materially higher than for peers in the same lines of business; and
- Trading losses that are above peers or not reflected in RACF.

Funding And Liquidity

177. We assess funding and liquidity separately and then combine them to determine their aggregate impact on the SACP or group SACP (see table 13). In assessing funding, we mainly consider the stability of an entity's funding sources and the likelihood they will be available to fund existing and new assets over an extended period. In assessing liquidity, we mainly consider an entity's ability to meet potential liquidity outflows that could occur over a short period during a time of stress. (See tables 31 and 32 in the appendix for details of the assumptions used for securities firms.)

Table 13

Funding And Liquidity Impact On SACP Or Group SACP

--Funding--	--Liquidity--			
	Strong	Adequate	Moderate	Weak\$
Strong	+1*	0	-1	-2 or more
Adequate	0	0	-1	-2 or more

Table 13

Funding And Liquidity Impact On SACP Or Group SACP (cont.)

--Funding--	--Liquidity--			
	Strong	Adequate	Moderate	Weak§
Moderate	0	-1	-2	-3 or more
Weak	-1	-2	-3	-3 or more

*Securities firms may receive +2 only when we determine that a firm exhibits exceptional funding through having a gross stable funding ratio of greater than 120% as well as direct access to central bank funding, low reliance on wholesale or short-term funding, and no material risk from funding concentrations. §We deduct more than the minimum number of notches (-2 for strong and adequate, -3 for moderate and weak) if we consider the entity to be less able than other entities with a liquidity assessment of weak to withstand a stressed outflow of liquidity without significantly utilizing emergency sources of liquidity.

Funding

178. Our funding assessment focuses largely on the stability and diversity of an FI's funding sources, how well those sources match its assets, and the likelihood and extent they will be available over an extended period to fund existing and new assets, including during times of market or idiosyncratic stress.
179. We use a variety of quantitative metrics and qualitative considerations specific to each type of FI to assess funding.
180. We typically assess funding more favorably for entities with diverse stable funding sources that are likely to remain available to fund existing and new assets during times of market or idiosyncratic stress; have a lack of concentration by source, provider, or tenor; and match well with their assets. We may also assess funding favorably if an entity has a track record of using a single or limited number of highly dependable government funding sources.
181. We typically view funding sources as stable when they have characteristics such as:
- A low likelihood of run-off because they have long tenors, insurance schemes, are provided by the government or a strong and stable related party, or other unique characteristics;
 - A long track record of consistent availability even during periods of market stress; and
 - A long track record of limited volatility of cost.
182. We typically consider that an entity's funding sources match well with its funding needs when they:
- Significantly limit the possibility the entity could suffer liquidity outflows on its liabilities without offsetting liquidity inflows on its assets, and
 - Allow the entity to earn an adequate return with limited interest-rate risk.
183. **Additional considerations for banks.** We assess the relative strength and potential volatility of funding by reviewing a bank's liabilities. This involves assessing the mixture of liability types, such as retail and wholesale deposits, interbank loans, and secured and unsecured borrowing in capital markets, including assessing risks relating to the currency denominations of the liabilities in the context of the assets they are funding.

Table 14

Funding Assessment For Banks

What it typically means*	
Strong	In our view, the entity has strong and materially better-than-peers access to stable funding sources that match well with its assets. This typically means that the entity has good funding diversity (or, in some cases, access to what we consider to be a highly dependable source, which could, for example, be a government) with sources that have a low likelihood of run-off, consistent availability, and costs that have limited volatility.
Adequate	In our view, the entity has access to stable funding sources that is roughly in line with or stronger than that of peers, and funding sources match well with its assets. This typically means that the entity has relatively good funding diversity with sources that have limited likelihood of run-off, consistent availability, and costs that have limited volatility.
Moderate	In our view, the entity has access to stable funding sources that is somewhat weaker than that of peers or its funding sources may have greater mismatches with its assets than entities with a stronger assessment. This means that the entity may lack funding diversity or rely meaningfully on some sources with significant run-off risk, have proven to lack availability during times of stress, or have shown significant volatility of cost.
Weak	In our view, the entity has access to stable funding sources that is clearly weaker than that of peers or its funding sources may have significant mismatches with its assets. This means that the entity may lack funding diversity or rely more heavily on some sources with significant run-off risk that have proven to lack availability during times of stress or shown significant volatility of cost.

Note: If a bank does not have access to a central bank's funding mechanism, the funding assessment is limited to moderate at best unless we consider that the bank maintains an appropriately prudent funding profile to mitigate the lack of central bank access. We would typically assess this by comparing the maturity profiles of its assets and liabilities, and identifying whether there were material gaps that could be a source of risk in a stress. *We assign a bank to one of the categories on a best fit basis.

184. For banks, we typically consider quantitative metrics such as:

- Long-term funding ratio,
- Short-term wholesale funding to total funding base,
- Stable funding ratio,
- Regulatory net stable funding ratio where applicable,
- Core deposits to funding base, and
- Customer loans (net) to customer deposits.

185. For banks, we typically consider the following qualitative factors:

- Overall funding mix (the mix between different sources including retail and wholesale deposits, interbank loans, and secured and unsecured borrowing in capital markets),
- Likelihood and track record of deposit stability,
- Composition and concentration of wholesale funding base,
- Management of the impact on funding stability of structural interest rate and foreign exchange exposures, and sensitivity to adverse market movements,
- Intragroup fungibility of funding across legal entities and considering regulatory constraints,
- Dependence on central bank or government-provided term funding facilities,
- Quality of management information and governance,
- How the bank sets its funding limits, and

- Signs of constraints in access to one or more sources of funding.

186. When assessing the likelihood and track record of deposit stability, we typically consider items such as:

- What percentage of the deposit base is repayable on demand;
- What percentage comes from nonresident or uninsured deposits;
- Concentration of deposits by distribution channels compared with peers;
- How the bank's deposit pricing compares with peers;
- Whether the bank is overly dependent on a few large depositors; and
- How the bank assesses the strength of its deposit franchise, stickiness, and price sensitivity, including the depth of its relationships with depositors, and what is our view of its assessment.

187. When analyzing the composition of the wholesale funding base, we typically consider:

- Extent of concentration/diversification by funding source, type of investor, currency, geography, and maturity;
- Exposure to cross-border and short-term funding; and
- Access to untapped funding sources.

188. When assessing signs of constraints in access to one or more sources of funding, we typically consider:

- Increased margins or collateral,
- Increased challenges in issuing long-term debt,
- Increased withdrawal of deposits or wholesale funds/lines, and
- Adverse movements in market signals.

189. **Additional considerations for fincos and BDCs.** For fincos and BDCs, the qualitative assessment includes an evaluation of how well the assumptions made in the stable funding ratio (SFR) represent the finco's position, as well as firm-specific funding strengths and weaknesses. Since the assumptions made in the SFR do not vary by firm or country, the qualitative assessment is important.

Table 15

Funding Assessment (Fincos And BDCs)

	What it typically means*
Strong	Reflects our view that there is strong excess capacity of stable long-term funding sources relative to needs given the firm's assets, businesses, and markets. The SFR is generally 110% or higher, and funding is well-matched with asset maturities and well-diversified by type (secured and unsecured) and lender. The entity has demonstrated regular access to unsecured debt markets, and unsecured maturities are well-staggered.
Adequate	Reflects our view that there is adequate capacity of stable, long-term funding sources relative to needs given the firm's assets, businesses, and markets. Funding is matched well with asset maturities and is well-diversified by type and lender. Typically, the entity has good access to unsecured debt markets or has deep and stable secured funding with diverse facilities and providers. Unsecured maturities are well-staggered. The expected SFR typically is about 90% or higher, or we expect the company could easily access multiple sources of secured and unsecured funding.

Table 15

Funding Assessment (Fincos And BDCs) (cont.)

	What it typically means*
Moderate	Reflects our view that the company may fund a modest amount of long-term illiquid assets with less stable funding sources. Funding is generally matched well with asset maturities but may have limited diversification of funding types and sources or limited track record accessing unsecured debt markets.
Weak	Reflects our view that funding risk is excessive because the entity funds a large portion of long-term illiquid assets with less stable sources, which raises the potential for funding gaps. Funding may be significantly shorter than asset maturities or concentrated by type and lender. The entity may have limited access to unsecured debt markets, or we believe it may have difficulty retaining funding over the next year.

*We assign an entity to one of the categories on a best fit basis. SFR--Stable funding ratio.

190. For fincos and BDCs, we typically consider the SFR and the following qualitative factors:

- Mix of deposits, government-provided debt, and unsecured debt versus secured debt;
- Access to secured and unsecured funding;
- Currency mismatches or reliance on foreign creditors;
- Extent that assumptions used to calculate the SFR accurately reflect the stability of the company's funding relative to its assets;
- If deposits are significant, extent to which they are insured deposits;
- Maturity or single-creditor concentrations (debt maturity profile);
- How the funding strategy takes into account potential exposure to margin calls;
- Reliance on funding sources that have proven unstable in the past;
- Risk of a sharp increase in cost of funding that could substantially impair earnings capacity; and
- Ability to retain funding over the next year.

191. **Additional considerations for securities firms.** Excess stable funding can create liquidity buffers, which supports the funding and liquidity assessment. We use the gross stable funding ratio (GSFR) as our key metric of a firm's stable funding sources relative to its stable funding needs.

192. Some securities firms benefit from ongoing direct access to funding from central banks. The presence of this backstop may support an adequate or higher funding assessment, but if the entity is dependent on central bank funding, the funding assessment is typically no higher than moderate.

Table 16

Funding Assessment (Securities Firms)

What it typically means*	
Strong	Reflects our view that there is strong excess capacity of stable long-term funding sources relative to needs given the firm's assets, businesses, and markets. The gross stable funding ratio (GSFR) is expected to be above 110%, or if below that level, additional sources of stable funding or asset liquidity not reflected in the GSFR's standard assumptions provide a similar coverage of funding needs, including derivatives. To assign strong, any indications of additional funding risk in the qualitative assessment are also not material and are more than offset by excess stable funding or access to dependable external sources, with no material funding currency mismatches.
Adequate	Reflects our view that there is adequate capacity of stable, long-term funding sources relative to needs given the firm's assets, businesses, and markets. GSFR is expected to be between 90% and 110%, or if below that level, additional sources of stable funding or additional asset liquidity not reflected in the GSFR's standard assumptions provide a similar coverage of funding needs, including any derivatives. Any indications of additional funding risk are offset by excess stable funding or access to dependable external sources.
Moderate	Reflects our view that the company may fund a modest amount of long-term illiquid assets with less stable funding sources, or have other funding weaknesses. Typically, GSFR is expected to be near 90% with any qualitative strengths or weaknesses offsetting. Or, GSFR is expected to be well below 90% but additional sources of stable funding or asset liquidity not reflected in the GSFR provide a similar coverage of funding needs including derivatives, and any qualitative weaknesses are offset by strengths. Or, GSFR is expected to be above 90%, but there are material additional funding risks.
Weak	Reflects our view that a firm's funding risk is excessive because it funds a large portion of long-term illiquid assets with less stable sources, which raises the potential for funding gaps, or it has other material funding weaknesses. This is typically indicated by a GSFR below 90% without compensating qualitative factors, or a GSFR above 90%, but material qualitative weaknesses or funding risks not captured in the GSFR that outweigh any strengths.

*We assign an entity to one of the categories on a best fit basis.

193. For securities firms, we typically consider the GSFR and the following qualitative factors:

- Currency mismatches;
- Data quality, including whether disclosures are adequate relative to the complexity of a firm's funding risk;
- A firm's position relative to any regulatory funding requirements or standards;
- The extent to which asset encumbrance constrains funding flexibility;
- The stability and maturity of funding sources;
- The appropriateness of GSFR standard assumptions for a particular firm;
- The quality of stable funding, including diversification and concentrations;
- Access to central bank funding, particularly when not reflected in the anchor;
- The analysis of material contractual investment or funding commitments; and
- The presence of a large prime brokerage or derivative business.

194. Examples of when the quality of stable funding is supportive of the funding assessment derived from the GSFR include:

- If a deposit franchise exists, the deposit franchise and mix are not materially weaker or more confidence sensitive than peers. Deposits included in stable funding are stable customer deposits;

- If the firm can pledge or otherwise use brokerage customer assets to fund customer activity, brokerage customer balances are predominantly retail or otherwise stable and not more confidence sensitive than peers; and
- There is no material additional risk from large funding concentrations as measured by: source (i.e., number of providers) or tenor (i.e., maturity concentration), funding tools (e.g., dependence on secured funding such as covered bonds, repo, central bank funding, or securitization or use of confidence-sensitive funding such as commercial paper, bank deposits, or short-term notes that could reduce funding flexibility), and the firm's funding needs relative to the markets in which it operates.

195. Our view of the quality of stable funding typically weakens the funding assessment below that suggested by the GSFR when any of the following apply:

- If a deposit franchise exists, the deposit franchise and mix are materially weaker or more confidence sensitive than peers. Deposits included in stable funding are wholesale or brokered customer deposits;
- If the firm can pledge or otherwise use brokerage customer assets to fund customer activity, but brokerage customer balances are predominantly wholesale, brokered, or otherwise not stable and more confidence sensitive than peers;
- Large funding concentrations, an overreliance on secured funding, or dependence on confidence-sensitive funding such as commercial paper, bank deposits, or short-term notes present material additional risks; or
- The firm does not, in our view, maintain a safe cushion above financial covenants on material portions of its debt.

196. The presence of a large prime brokerage or over-the-counter derivative business without access to additional stable funding sources (which could include the central bank) is a funding risk. Without excess funding, large exposure to these businesses is a weakness not reflected in the GSFR.

197. If funding currency mismatches are unhedged and material, the funding assessment is typically limited to adequate.

Liquidity

198. Our liquidity assessment focuses largely on an FI's ability to withstand liquidity outflows that could occur typically under stress over the coming 12 months by considering the entity's:

- Potential liquidity sources--on- and off-balance-sheet;
- Potential liquidity uses--on- and off-balance-sheet; and
- Liquidity sources compared with liquidity uses.

199. We consider a variety of metrics specific to each type of FI to assess potential liquidity sources and liquidity uses and to give insight into the potential sensitivity of an entity. The metrics often incorporate quantitative assumptions pertaining to such factors as the liquidity value of asset types and the liquidity outflows that may occur on a liability type under stress scenarios.

200. We may also consider other quantitative and qualitative factors that could affect the overall liquidity assessment. Examples may include:

- Ability to access contingent sources of liquidity not reflected in the primary metrics;

- Contingent uses of liquidity that are not reflected in the primary metrics but that increase liquidity risk;
- Whether the assumptions in the primary metrics are too liberal or conservative based on the qualitative characteristics of the entity's sources of liquidity or liquidity risks (e.g., considering the stability of a bank's deposits);
- The complexity of the entity's liquidity risks;
- The confidence sensitivity of the entity;
- The robustness of the entity's liquidity stress testing and contingency planning;
- Significant liquidity risks that could arise beyond the time horizon captured in relevant metrics;
- Market signals that may suggest a rising inability to access certain types of sources of liquidity;
- Significant ongoing dependence on central bank resources; and
- Potential lack of fungibility or barriers to intragroup movements of liquidity across a firm's entities.

201. We consider more favorably high levels of on-balance-sheet liquid assets relative to potential liquidity uses and as a percent of assets when this provides a strong ability to absorb the types of outflow that might be expected to occur under stress scenarios. Clear access to secondary and emergency sources of liquidity would further support the assessment.

202. For FIs that have short-term liabilities such as commercial paper (CP) programs, our liquidity assessment also considers how the FI manages the potential maturity rollovers and the arrangements that the FI has to ensure timely payment, including in markets where the FI does not have access to central bank liquidity in the currency of the obligation. We do not set rules regarding the type or size of arrangements that an FI should have. We assess the capacity and nature of these arrangements, including an FI's contingency planning, as an indicator of an FI's liquidity risk appetite.

203. We expect FIs to maintain sufficient backup, in the form of liquid assets or access to liquidity from a central bank or other entity (such as via committed bank lines of credit), against short-term liabilities, including its CP programs and other short-term funding. Arrangements to ensure timely payment in other jurisdictions may include swing lines from banks in that jurisdiction, or an FI could maintain a portfolio of liquid securities in that jurisdiction that are unencumbered, available, and have a proven value in the secondary market.

204. Noncontractual or reputational contingencies arising from management's perceived need to preserve franchise value may be important when assessing potential liquidity uses. Examples include:

- The repurchase of commercial paper in advance of maturities;
- Calling long-term debt at the first call date, despite having no contractual obligation to do so;
- The provision of support to money market funds, securitizations, tender option bonds, and auction rate securities;
- Support of secondary markets in assets as a market-maker; and
- Protecting investors from losses on asset-backed securitizations that the entity originates.

Table 17

Liquidity Assessment

What it typically means	
Strong	In our view, the entity will withstand a stressed outflow of liquidity (based on the type of liquidity risk it bears) completely or largely by utilizing on-balance-sheet sources of liquidity.
Adequate	In our view, the entity is highly likely to withstand a stressed outflow of liquidity (based on the type of liquidity risk it bears), but our confidence in that assessment is somewhat lower than for an entity with strong liquidity. The entity may also need to utilize secondary sources of liquidity under some plausible stress scenarios.
Moderate	In our view, the entity has a lower likelihood than an entity with adequate liquidity of withstanding a stressed outflow of liquidity (based on the type of liquidity risk it bears) and a higher likelihood of having to access secondary or emergency liquidity sources.
Weak	We have limited confidence that the entity could withstand a stressed outflow of liquidity (based roughly on the type of liquidity risk it bears) without significantly utilizing emergency sources of liquidity. For a finco or business development company, a weak liquidity assessment may reduce the SACP to 'b-', or lower if 'CCC' criteria apply.

205. **Non-deposit-taking institutions that have bank licenses.** In some jurisdictions, an FI may have a specialized banking license that provides a different level of access to central bank liquidity to other banks and that may restrict the FI from engaging in particular activities, such as deposit-taking. In this case, we assess the nature of the FI's access to central bank liquidity, and the amounts we expect to be accessible on a sustained basis, given the central bank rules and the FI's access to eligible collateral.

206. **Additional considerations for banks.** We typically start with the following quantitative factors subject to data availability:

- Broad liquid assets to short-term wholesale funding,
- Broad liquid assets to total assets,
- Broad liquid assets to customer deposits,
- Net broad liquid assets to short-term customer deposits, and
- Regulatory liquidity coverage ratio (LCR).

207. In considering sources of liquidity, we may also consider:

- Systemwide liquidity facilities at central banks or other government sources, both routine and extraordinary, determined by unencumbered assets that the central bank would qualify as collateral and liquidity available in exchange for these assets after central bank haircuts;
- Drawdown of committed credit facilities, subject to financial covenants and headline considerations;
- The sale or repo of unencumbered high-quality liquid securities in the open market. Because banks make different assumptions about what qualifies as liquid, we typically compare them to those in our market value criteria (see Related Criteria) for rating transactions backed by securities;
- The amount of cash or securities that may be encumbered (for example, deposits posted to clearinghouses or derivatives counterparties);
- Liquidation of short-term advances to other financial institutions sold and reverse repos;
- Cash available from maturing advances to customers;

- Accessing the debt and stock markets to the extent still possible; and
- Accessing securitization or covered bond markets through established facilities or asset sales programs and whole loan sales.

208. In considering uses of liquidity for banks, we may also consider:

- Deposit composition: Insured versus uninsured, domestic versus international, retail versus corporate, relationship-based versus rate-based. In each case, we typically consider the first more stable than the second, although this can vary by entity;
- Drawdown of credit commitments: The ability of a bank to reduce limits and the extent of undrawn commitments to customers;
- The maturity profile of wholesale liabilities: Inability to roll over short-term unsecured borrowings (e.g., commercial paper, certificates of deposit, promissory notes) or to refinance maturing long-term unsecured debt;
- Market-driven inability to roll over maturing short-term secured debt or repurchase agreements. That is, the market can dry up altogether for lower-quality securities or, short of that, seek increased margins, collateral requirements, or credit spreads;
- The potential for margin calls due to rising market volatility, a change in parameters or company-specific, credit-driven increases in margin and collateral requirements, for example resulting from a breach of rating triggers;
- Calls under guarantees to unrelated third parties such as standby letters of credit, performance guarantees, securities lending indemnifications, and custody guarantees; and
- Run-off of other customer funds, such as prime broker free credit balances.

209. **Additional considerations for fincos and BDCs.** When we are considering an assessment of strong, we apply an additional assessment, the liquidity coverage metric (LCM), to determine whether liquidity shows greater capacity. The LCM is the ratio of broad liquid assets plus available committed unsecured lines to short-term wholesale funding. We use the same definitions of broad liquid assets and short-term wholesale funding that we use for banks. An LCM above 2x supports an assessment of strong when combined with qualitative assessments supportive of strong. An LCM of more than or equal to 1.5x could also support a strong assessment when the analysis of qualitative and quantitative factors combined reveals material liquidity strengths that our metrics don't capture.

210. For fincos and BDCs, we may also consider the following qualitative factors where relevant:

- Effectiveness of liquidity management systems, which may be informed by a review of companies' forecasted sources and uses, if available;
- Degree and effectiveness of liquidity stress testing;
- Asset or liability concentrations;
- Contingent liabilities;
- Funding based-triggers, such as collateral call in a margin agreement or acceleration provisions in facilities;
- The amount of cash or securities that may be encumbered (for example, deposits posted to clearinghouses or derivatives counterparties);
- Reliance on bank funding, particularly in a stress scenario;

- Market signals that suggest restricted access to nonsecured funding;
- Liquidity-based triggers, such as liquidity maintenance covenants;
- Market signals that indicate weaker liquidity of assets; and
- Large or unusual liquidity needs in the next 12-24 months.

211. We may lower our liquidity assessment to weak if a finco or BDC faces imminent acceleration of or loss of access to its credit facilities, for example due to violation of covenants (including minimum consolidated tangible net worth) when the acceleration could result in essentially all borrowings outstanding being immediately due and payable.

212. **Additional considerations for securities firms.** We use table 18 when assessing liquidity for securities firms.

Table 18

Liquidity Assessment For Securities Firms

Assessment	Guidance
Strong	Typically, we expect the liquidity coverage metric (LCM) to be $\geq 1.5x$, or access to additional liquidity beyond that reflected in the LCM provides a similar coverage of liquidity needs, including for derivatives. Any qualitative weakness is more than offset by excess liquidity buffers. Contingent liquidity needs are more than offset by access to unencumbered liquidity.
Adequate	Typically, we expect the LCM to be $\geq 0.9x$ and $< 1.5x$, or access to additional liquidity beyond that reflected in the LCM provides a similar coverage of liquidity needs, including for derivatives; qualitative factors do not indicate material additional risk; and contingent liquidity needs like margin or collateral call exposure is offset by unencumbered liquidity.
Moderate	Reflects our view that a firm will meet its liquidity demands under normal conditions over the next 12 months, but is vulnerable to more severe or prolonged market or other stress. Typically, we expect the LCM to be below $0.9x$, but not significantly below, and qualitative strengths and weaknesses are offsetting.
Weak	Reflects our view that a firm's liquidity is vulnerable under expected conditions or is highly dependent on official liquidity support, which is available but may be finite. Typically, we expect the LCM to be below $0.9x$, with additional indications of substantial liquidity risk not captured in the LCM.

213. The standard assumptions underpinning the LCM may not fully capture the liquidity risks a firm faces, or they may overstate those risks. LCM standard assumptions are supportive of the assessment when they do not understate short-term liability outflows or overstate asset liquidity. When our analysis reveals material liquidity weaknesses or strengths that our metrics do not fully capture, the liquidity assessment can be higher or lower than indicated in table 18.

214. When, all else being equal, the haircuts used to assess the liquidity of securities or other financial assets materially understate the asset's liquidity and do not understate the firm's liquidity demands, the assessment can be raised above that indicated by the LCM. Conversely, if the LCM standard assumptions overstate the liquidity of a firm's assets or understate potential liquidity demands, it typically lowers the liquidity assessment below that derived from the LCM.

215. For example, the liquidity assessment can be stronger when the LCM overstates a firm's liquidity risk, contingent liquidity risks are well covered, and market indicators do not suggest to us that creditors' and/or shareholders' have lost confidence in the firm. An example where the LCM may overstate liquidity risk is a firm whose assets almost entirely comprise very low risk, very highly rated asset-backed securities in a country where these are traded actively, such as U.S. student loans or credit card receivables, which may make them a source of liquidity that is not fully captured in the LCM.

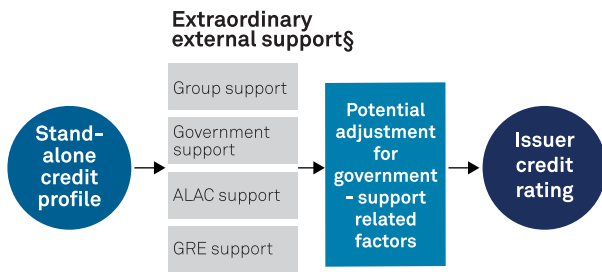
²¹⁶. For securities firms, we may also consider the following qualitative factors:

- A firm's position relative to any regulatory liquidity requirements or standards;
- The appropriateness of LCM standard assumptions for a particular firm;
- Material liquidity mismatches or undue concentrations;
- Access to or dependence on central bank borrowing;
- Fungibility or barriers to intra-group movements of liquidity across a firm's entities, particularly if major subsidiaries have material liquidity mismatches;
- Exposure to additional liquidity risk from customers; and
- Management of off-balance-sheet and stressed liquidity risks, including the scope and complexity of contingent liquidity demands from: derivatives or prime brokerage businesses that require excess liquidity or access to additional external liquidity because they are not reflected in the LCM, and the firm's potential stress liquidity needs including collateral and margin calls relative to its available unencumbered liquidity.

²¹⁷. For securities firms engaged primarily in principal trading and market-making, we may also look at the ratio of required margin to net trading capital. Required margins include those required by central counterparty clearinghouses (CCPs), prime brokers, and derivatives counterparties to support a firm's exposures. We typically define net trading capital as the sum of common equity, minority interest, and long-term preferred equity and debt, minus the amount of non-trading assets (including goodwill).

²¹⁸. A high required margin-to-net trading capital ratio (for example, consistently over 85%, without any mitigating considerations or liquidity sources such as committed lines of credit or client assets that can be pledged) typically suggests that, in a stress scenario, the entity may have more limited available cash capital to fund incremental margin requirements at CCPs, prime brokers, and derivatives counterparties, which may require it to liquidate positions or seek additional external liquidity. Conversely, a consistently low ratio typically suggests that the entity has a relatively stronger capacity to meet an increase in its margin requirements in a stress scenario, without the need to tap external sources or liquidate positions. In assessing this ratio, we also take into account the risk and liquidity of the trading book portfolio, available portion of committed lines of credit, and other potential liquidity needs a firm may have beyond its trading book.

SECTION 3: MOVING FROM THE SACP TO THE ICR: EXTRAORDINARY EXTERNAL SUPPORT



§In some cases, an FI may also qualify for an additional support adjustment. GRE--Government-related entity. ALAC--Additional loss-absorbing capacity.

Section 3 describes the criteria for moving from the SACP to the ICR.

219. The support framework factors in the likelihood of support from an external party into the rating on an FI by assessing the relationship between the parties. The support can take the following forms, each where applicable incorporated into the ICR, not the SACP:

- Extraordinary government support for a government-related financial institution that fulfills a public policy role or where the government ownership is strategic and long term, which is addressed in our GRE criteria (can apply to banks and NBFIs);
- Extraordinary group support, which is addressed in our group rating methodology (can apply to banks and NBFIs);
- Extraordinary support from a guarantor, which is addressed in our guarantee criteria (can apply to banks and NBFIs);
- Extraordinary government support for a bank or NBF that is systemically important;
- Extraordinary support arising from the loss-absorbing characteristics of ALAC securities (can apply to banks and FMI); and
- Extraordinary additional support from a government (can apply to banks and NBFIs).

220. Also, we're able to make an adjustment to the potential outcome for government support-related factors as shown in chart 2 and described earlier.

221. The rest of this section describes the forms of extraordinary external support that are specific to banks and NBF, that is extraordinary government support due to systemic importance, ALAC, and the use of the additional support adjustment.

Extraordinary Government Support For Banks And NBFs Due To Systemic Importance To The Financial System

222. The criteria for determining rating uplift from the expectation of extraordinary government support for banks (and NBFs where applicable) based on systemic importance comprise four parts:

- Assess a government's tendency to support banks (and NBFIs where applicable) based on systemic importance.
- Determine the degree of a bank's systemic importance (or NBFI where applicable).
- Establish the likelihood that the government will provide support to a particular bank or NBFI based on this systemic importance, which determines the potential uplift based on the application of the government support tables 21, 22, and 23 (and the adjustment for government support-related factors where appropriate).
- Determine whether additional support is available (see the "Additional support adjustment" section).

223. NBFIs are eligible for rating uplift based on the expectation of this extraordinary government support if we consider them systemically important financial institutions and there are public statements by regulators supporting this systemic importance (which may include the regulator or government having the NBFI on a list of systemically important entities).

224. A bank or NBFI is classified as having high, moderate, or low systemic importance. A government's tendency to support such a bank (or NBFI where applicable) based on this systemic importance falls into one of three categories: highly supportive, supportive, or uncertain. The criteria then combine the two classifications to determine the likelihood of direct government support in the future.

Government tendency to support banks (and NBFIs where applicable) based on systemic importance

225. We assess the capacity and willingness of sovereigns to support failing banks (or NBFIs where applicable) during a crisis based on their systemic importance, classifying sovereigns into three groups: highly supportive, supportive, and uncertain (see table 19). We may still classify a government as highly supportive or supportive if it has implemented an effective bank resolution regime, depending on our assessment of whether the provision of support is still a sufficiently likely policy option.

Table 19

Tendency Of A Government To Bail Out Banks (And NBFIs Where Applicable) Based On Systemic Importance

Assessment	Typical characteristics
Highly supportive	The government tends to be explicit about its willingness to continually support entities with high and moderate systemic importance, even in the case of bank- or nonbank financial institution (NBFI)-specific crises.
	There is a track record of frequent interventions that protect senior creditors from loss.
	The interventionist policy is likely to continue.
	The sovereign has sufficient financial resources to support banks (and applicable NBFIs) and a reasonable framework in place for monitoring its risk to the financial system.
	Interventions are typically direct capital or liquidity injections, guarantees, or risk-protection schemes.
	Government interventions are typically not subject to authorization or restrictions by supranational agencies (such as the EU or IMF).
Supportive	The government has no explicit policy of support for the financial sector.

Table 19

Tendency Of A Government To Bail Out Banks (And NBFIs Where Applicable) Based On Systemic Importance (cont.)

Assessment	Typical characteristics
	There is a track record of sovereign actions to support entities with high and moderate systemic importance, particularly during a systemic crisis, protecting senior creditors from loss. Rather than providing support directly, the sovereign tends to encourage or organize a market-led solution where possible. The sovereign is likely to act in the future to provide similar support.
	The government has authorization to provide support, but has to comply with particular conditions or is subject to authorization from parliament, legislatures, or supranationals.
	The sovereign has sufficient financial resources to support banks and applicable NBFIs.
	The government will typically have a range of policy alternatives for reacting to banking or NBFIs sector stress, which may include legislation that requires creditors to share the burden of providing support to a distressed bank (such as by discounting creditors' obligations).
	The type of crisis typically shapes the form of support.
Uncertain	The government has no explicit policy of support, or there is an unambiguous policy or legislation that prevents direct support for banks (or NBFIs where applicable).
	Senior creditors are required and expected to share in the losses resulting from the failure of the entity.
	There is no reliable track record of sovereign support actions during past financial crises, or there is evidence that support does not extend to unsecured senior creditors.
	There are doubts about the sovereign's capacity to support systemically important financial institutions.

Systemic importance

226. Systemic importance is the degree to which a bank or NBFIs failure affects all or parts of the financial system and the real economy of the country where the entity operates. We classify a bank or NBFIs as having high, moderate, or low systemic importance based on our view of how adverse we expect the impact of the entity failure would be.
227. An FI classified as having high or moderate systemic importance might not receive support in a time of stress because no one can predict with certainty whether a sovereign will provide it. A government may, however, decide to support an FI in the event of a crisis, even though it may have low systemic importance.
228. **High systemic importance:** We define this as when the failure of an FI is likely to have a significant adverse impact on the financial system and the real economy.
229. For example, an FI has high systemic importance if a default of its senior unsecured obligations is likely to weaken the country's financial system, limit the availability of credit for the private sector, and trigger a significant financial stress at several other financial institutions.
230. Size is not the only determining factor. It is also a factor of the level of interconnectedness, or the linkages of a financial institution with other parts of the financial system. For example, the entity may be a significant counterparty within the country and international financial system or play a critical role in the national payments system, such that its failure will lead to a loss of confidence in the financial system and significant losses among other counterparties in the market. Another example may be if no other institution can step into an FI's key role in the economy if it fails.

231. **Moderate systemic importance:** We define this as when the failure of an FI is likely to have a material, but manageable, adverse impact on the financial system and the real economy.
232. For example, this may apply if a default on its senior unsecured obligations is likely to lead to disruption in the provision of financial services to a specific region or sector of the economy but be more manageable at a national level. A classification of moderate systemic importance for an FI means that if it fails, other counterparties are more likely to be able to take on the failed entity's market role.
233. **Low systemic importance:** We define this as when an FI does not fit the definition of high or moderate systemic importance.

Likelihood of extraordinary government support

234. We then classify the likelihood that a bank or NBFI would receive extraordinary government support in the future as high, moderately high, moderate, or low based on the combination of its systemic importance and a government's tendency to support systemically important banks (or NBFIs where applicable).

Table 20

Likelihood Of Extraordinary Government Support In The Future

Systemic importance	--Government's tendency to support banks*--		
	Highly supportive	Supportive	Uncertain
High	High (table 21)	Moderately high (table 22)	Low
Moderate	Moderately high (table 22)	Moderate (table 23)	Low
Low	Low	Low	Low

*And certain nonbank financial institutions that we consider to be systemically important.

235. We combine the SACP on the FI and the rating on the sovereign according to table 21, 22, or 23 (the FI government support tables)--depending on the likelihood of government support based on systemic importance--to arrive at the potential outcome. We then factor in any adjustment to the potential outcome for government support-related factors and any additional support adjustment, if applicable, to determine the potential ICR.

Table 21

High Likelihood Of Extraordinary Government Support Based On Systemic Importance

SACP	--Government local currency rating--															
	AAA	AA+	AA	AA-	A+	A	A-	BBB+	BBB	BBB-	BB+	BB	BB-	B+	B	B-
aaa	AAA															
aa+	AA+	AA+														
aa	AA+	AA	AA													
aa-	AA	AA	AA-	AA-												
a+	AA-	AA-	AA-	A+	A+											
a	AA-	A+	A+	A+	A	A										
a-	AA-	A+	A+	A	A	A-	A-									

Table 21

High Likelihood Of Extraordinary Government Support Based On Systemic Importance (cont.)

	--Government local currency rating--															
SACP	AAA	AA+	AA	AA-	A+	A	A-	BBB+	BBB	BBB-	BB+	BB	BB-	B+	B	B-
bbb+	A+	A+	A	A	A	A-	BBB+	BBB+								
bbb	A	A	A	A-	A-	A-	BBB+	BBB	BBB							
bbb-	A-	A-	A-	A-	BBB+	BBB+	BBB+	BBB	BBB-	BBB-						
bb+	BBB+	BBB+	BBB+	BBB+	BBB+	BBB	BBB	BBB	BBB-	BB+	BB+					
bb	BBB	BBB	BBB	BBB	BBB	BBB	BBB-	BBB-	BBB-	BB+	BB	BB				
bb-	BBB-	BBB-	BBB-	BBB-	BBB-	BBB-	BBB-	BB+	BB+	BB+	BB	BB-	BB-			
b+	BB+	BB+	BB+	BB+	BB+	BB+	BB+	BB+	BB	BB	BB-	BB-	B+	B+		
b	BB	BB	BB	BB	BB	BB	BB	BB	BB	BB-	BB-	BB-	B+	B	B	
b-	BB-	BB-	BB-	BB-	BB-	BB-	BB-	BB-	BB-	BB-	B+	B+	B	B-	B-	B-
ccc+	B+	B+	B+	B+	B+	B+	B+	B+	B+	B+	B	B	B-	B-	B-	*
ccc	B	B	B	B	B	B	B	B	B	B	B-	B-	B-	*	*	*
ccc-	B-	B-	B-	B-	B-	B-	B-	B-	B-	B-	*	*	*	*	*	*
cc	B-	B-	B-	B-	*	*	*	*	*	*	*	*	*	*	*	*

Note: The issuer credit rating may differ from the potential outcome shown in this table if the potential outcome based on another form of extraordinary support is higher, or if there is an adjustment to the potential outcome for any government support-related factors, or due to the application of additional support. *These combinations may suggest a potential outcome in the 'CCC' or weaker rating categories. We only assign issuer credit ratings for FIs in these rating categories when the scenarios outlined in "Criteria For Assigning 'CCC+', 'CCC', 'CCC-', And 'CC' Ratings" apply; otherwise, a 'B-' rating is appropriate. SACP--Stand-alone credit profile.

Table 22

Moderately High Likelihood Of Extraordinary Government Support Based On Systemic Importance

	--Government local currency rating--															
SACP	AAA	AA+	AA	AA-	A+	A	A-	BBB+	BBB	BBB-	BB+	BB	BB-	B+	B	B-
aaa	AAA															
aa+	AA+	AA+														
aa	AA	AA	AA													
aa-	AA	AA-	AA-	AA-												
a+	AA-	AA-	A+	A+	A+											
a	A+	A+	A+	A	A	A										
a-	A+	A	A	A	A-	A-	A-									
bbb+	A	A	A-	A-	A-	BBB+	BBB+	BBB+								
bbb	A-	A-	A-	BBB+	BBB+	BBB+	BBB	BBB	BBB							
bbb-	BBB+	BBB+	BBB+	BBB+	BBB	BBB	BBB	BBB-	BBB-	BBB-						
bb+	BBB	BBB	BBB	BBB	BBB	BBB-	BBB-	BBB-	BB+	BB+	BB+					
bb	BBB-	BBB-	BBB-	BBB-	BBB-	BBB-	BB+	BB+	BB+	BB	BB	BB				
bb-	BB+	BB+	BB+	BB+	BB+	BB+	BB+	BB	BB	BB	BB-	BB-	BB-			

Table 22

Moderately High Likelihood Of Extraordinary Government Support Based On Systemic Importance (cont.)

	--Government local currency rating--															
SACP	AAA	AA+	AA	AA-	A+	A	A-	BBB+	BBB	BBB-	BB+	BB	BB-	B+	B	B-
b+	BB	BB	BB	BB	BB	BB	BB	BB	BB-	BB-	BB-	B+	B+	B+		
b	BB-	BB-	BB-	BB-	BB-	BB-	BB-	BB-	BB-	B+	B+	B+	B	B	B	
b-	B+	B+	B+	B+	B+	B+	B+	B+	B+	B+	B	B	B	B-	B-	B-
ccc+	B	B	B	B	B	B	B	B	B	B	B-	B-	B-	*	*	*
ccc	B-	B-	B-	B-	B-	B-	B-	B-	B-	B-	*	*	*	*	*	*
ccc-	*	*	*	*	*	*	*	*	*	*	*	*	*	*	*	*
cc	*	*	*	*	*	*	*	*	*	*	*	*	*	*	*	*

Note: The issuer credit rating may differ from the potential outcome shown in this table if the potential outcome based on another form of extraordinary support is higher, or if there is an adjustment to the potential outcome for any government support-related factors, or due to the application of additional support. *These combinations may suggest a potential outcome in the 'CCC' or weaker rating categories. We only assign issuer credit ratings for FIs in these rating categories when the scenarios outlined in "Criteria For Assigning 'CCC+', 'CCC', 'CCC-', And 'CC' Ratings" apply; otherwise, a 'B-' rating is appropriate. SACP--Stand-alone credit profile.

Table 23

Moderate Likelihood Of Extraordinary Government Support Based On Systemic Importance

	--Government local currency rating--															
SACP	AAA	AA+	AA	AA-	A+	A	A-	BBB+	BBB	BBB-	BB+	BB	BB-	B+	B	B-
aaa	AAA															
aa+	AA+	AA+														
aa	AA	AA	AA													
aa-	AA-	AA-	AA-	AA-												
a+	AA-	A+	A+	A+	A+											
a	A+	A+	A	A	A	A										
a-	A	A	A	A-	A-	A-	A-									
bbb+	A-	A-	A-	A-	BBB+	BBB+	BBB+	BBB+								
bbb	BBB+	BBB+	BBB+	BBB+	BBB+	BBB	BBB	BBB	BBB							
bbb-	BBB	BBB	BBB	BBB	BBB	BBB	BBB-	BBB-	BBB-	BBB-						
bb+	BBB-	BBB-	BBB-	BBB-	BBB-	BBB-	BBB-	BB+	BB+	BB+	BB+					
bb	BB+	BB+	BB+	BB+	BB+	BB+	BB+	BB+	BB	BB	BB	BB				
bb-	BB	BB	BB	BB	BB	BB	BB	BB	BB	BB-	BB-	BB-	BB-			
b+	BB-	BB-	BB-	BB-	BB-	BB-	BB-	BB-	BB-	BB-	B+	B+	B+	B+		
b	B+	B+	B+	B+	B+	B+	B+	B+	B+	B+	B+	B	B	B	B	
b-	B	B	B	B	B	B	B	B	B	B	B	B	B-	B-	B-	B-
ccc+	B-	B-	B-	B-	B-	B-	B-	B-	B-	B-	B-	B-	B-	*	*	*
ccc	*	*	*	*	*	*	*	*	*	*	*	*	*	*	*	*
ccc-	*	*	*	*	*	*	*	*	*	*	*	*	*	*	*	*

Table 23

Moderate Likelihood Of Extraordinary Government Support Based On Systemic Importance (cont.)

--Government local currency rating--															
SACP	AAA	AA+	AA	AA-	A+	A	A-	BBB+	BBB	BBB-	BB+	BB	BB-	B+	B-
CC	*	*	*	*	*	*	*	*	*	*	*	*	*	*	*

Note: The issuer credit rating may differ from the potential outcome shown in this table if the potential outcome based on another form of extraordinary support is higher, or if there is an adjustment to the potential outcome for any government support-related factors, or due to the application of additional support. *These combinations may suggest a potential outcome in the 'CCC' or weaker rating categories. We only assign issuer credit ratings for FIs in these rating categories when the scenarios outlined in "Criteria For Assigning 'CCC+', 'CCC', 'CCC-', And 'CC' Ratings" apply; otherwise, a 'B-' rating is appropriate. SACP--Stand-alone credit profile.

236. For a bank or NBFI with a low likelihood of support based on systemic importance, the potential ICR based on government support is the same as the SACP, unless we apply an adjustment to the potential outcome for government-support-related factors or an additional support adjustment applies.

External Support From ALAC

237. To determine whether and to what extent ALAC support may lift an ICR above the SACP, we assess:

- Whether, based on legislative and regulatory features, we expect that ALAC will reduce default risk on the FI's senior unsecured obligations, supporting its ICR;
- The features of instruments that are eligible for inclusion in ALAC; and
- The quality and quantity of ALAC liabilities as a proportion of S&P Global RWAs that will uplift a bank ICR above its SACP.

238. ALAC is a source of incremental credit strength for an FI's senior unsecured obligations that, in some jurisdictions, can absorb losses of an FI at or near nonviability--for example, in the event of a resolution--addressing unrecognized losses and recapitalizing an FI as necessary in a way that reduces the risk of it defaulting, according to our definitions, on its senior unsecured obligations. An FI's ALAC is the sum of:

- Its hybrid capital instruments not included in TAC that have the capacity to generate common equity, through conversion into common equity or a principal write-down, at the initiative of the authorities when the FI is failing; and
- In some jurisdictions, senior and subordinated obligations of its NOHC.

239. The conversion into common equity or the write-down of ALAC instruments occurs as a result of external regulatory intervention, and these instruments, like other types of support that we view as extraordinary intervention, are excluded from the SACP. ALAC raises the potential ICR above the SACP only if, in our view, the resolution framework that governs the issuing entity is sufficiently effective and the ALAC amount meets one of the thresholds specified below.

Effectiveness of ALAC under a resolution framework

240. We assess a resolution framework as sufficiently effective for ALAC uplift if all four of the following conditions are met:

- We expect that the resolution authorities would apply a well-defined resolution process that involves loss-absorption by the ALAC instruments, which typically we expect would only be used for a systemically important entity.
- We assess the authorities as having the ability and intent to permit an FI that is near or at the point of nonviability to continue its operations as a going-concern after absorption of losses by junior creditors and/or NOHC financial obligations in a manner that avoids a default, as per our definition, on its senior unsecured debt, or for the senior unsecured obligations to be transferred to another entity in such a way as to avoid a default.
- The relevant authorities have the ability and intent to provide the relevant operating company access to the necessary funding and liquidity mechanism to cope with the likely loss of access to market funding in the resolution process, provided that the FI has sufficient instruments that can be bailed in to recapitalize it and that it has sufficient assets to pledge as collateral.
- The relevant authorities require designated FIs to comply, in effect, with minimum ratios for the amount of instruments that can be bailed in at the point of nonviability, constituting a significant buffer absorbing losses ahead of senior unsecured obligations of the operating company. These instruments could be various types of hybrid capital instruments and, in some situations, NOHC financial obligations that are subject to resolution authority requirements. Thus, we expect redemption of such an instrument to take into account applicable bail-in requirements.

Assessing resolvability

241. In determining whether to include ALAC uplift, we focus explicitly on the resolution approach that we expect for an entity and the prospective size of its bail-in buffer. Resolvability is a multifaceted concept. A resolution action has a greater chance of being successful when an entity has not only sizable contingent financial resources (bail-in capacity and funding), but also removes practical and legal impediments to its operational continuity in resolution.

242. If we identify structural or persistent material impediments that would likely undermine a resolution action, we reflect this at a systemwide or entity-specific level, as appropriate. For example, we may determine a system to have a resolution framework that is not sufficiently effective, or that is ineffective because the entity's resolution process is unlikely to reduce default risk on its senior unsecured obligations.

Characteristics of instruments that are eligible for inclusion in ALAC

243. ALAC includes instruments that have the capacity to absorb losses as a bank enters a resolution process (and before the FI is insolvent). The types of instruments that are eligible for inclusion in ALAC are those we identify as hybrid capital instruments but that are not included in TAC for an entity, as well as liabilities that an NOHC issues, provided they meet the characteristics in this section. Because we concentrate on the loss-absorption capacity of an instrument when an FI enters resolution, rather than on the financial flexibility that it provides on a going-concern basis, ALAC may include hybrids with no equity content and NOHC financial obligations.

244. A senior unsecured instrument is not a hybrid capital instrument, even if it could be bailed in as part of the resolution of a distressed entity. However, it would be considered hybrid capital if, though labeled as "senior" in liquidation, it is part of a class that is different from other senior unsecured obligations in the event of a resolution and would be converted to equity or written down without triggering a default on the latter.
245. When assessing whether to include an instrument in ALAC, we consider not only the instrument's mandatory clauses, but also discretionary clauses that we expect regulators to enforce. However, we exclude an instrument from ALAC if both the contractual clause is discretionary and we do not expect regulators to enforce it. To be included in ALAC, an instrument must either:
- Have a mandatory contingent capital clause leading to common-equity conversion or a principal write-down, or both, that meets conditions a to c below, or
 - Be subject to a regulatory or legal framework that creates the equivalent of such a clause (including, for example, the regulatory authority to put an NOHC into receivership).
246. The contingent capital principal write-down or common-equity feature must meet all of the following conditions:
- a) The instrument must be subject to conversion or write-down at or before a regulatory determination of an FI's nonviability, or at the FI's entry into resolution. (If the instrument allows for a temporary write-down on a going-concern basis, supervisors should also have the ability to impose a permanent write-down at the point of nonviability or in resolution.)
 - b) Not cause a default of the operating entity or trigger a revision of the operating entity ICR to 'SD' (selective default) or 'D' (and not have cross-default or guarantee provisions relating to the operating entity and its senior unsecured debt obligations).
 - c) Be exercised at the discretion of the supervisors or responsible authorities under a resolution regime.
247. By contrast, we exclude certain hybrid instruments from ALAC if an FI operates in a regulatory environment where, upon distress, it is likely to receive extraordinary government support in a preemptive manner at a relatively early stage of its deterioration. Also, based on relevant regulator announcements, such preemptive government support would not constitute a nonviability event for the certain classes of hybrids in that jurisdiction. As such, the provision of support would not lead the instruments to be written down or converted into common equity.
248. When the loss absorption of an instrument cannot exceed a portion of the principal (for instance, 25%), ALAC only includes this amount. The amount of ALAC is not tax-adjusted unless we expect the conversion or write-down to have a tax impact that would alter materially the amount of common equity generated.
249. To support the sustainability of ALAC, for an ALAC instrument that is subject to specific regulatory requirements governing aggregate outstandings and redemptions, we typically set the following two conditions:
- Remaining life must be at least 12 months for inclusion in ALAC; and
 - If an FI has the option to redeem an instrument earlier than the maturity date, that instrument can be included in ALAC only if the regulator has oversight giving it the ability to prevent any redemption at the call date. When considering the effective maturity (and therefore the remaining life) of these instruments, we treat the final maturity date (not the call date) as the effective maturity, provided that there is no step-up at the call date (or other incentive to redeem early). This also depends on the regulatory treatment--if the regulator uses the call date as the effective maturity, we typically do the same.

250. If an FI has issued an instrument that meets the requirements based on contractual conversion or write-down provisions (to be activated by regulators no later than the point of nonviability), but that instrument is not subject to specific regulatory requirements governing aggregate outstandings or redemptions, we apply the residual maturity standards of our hybrid capital criteria.

ICR uplift above the SACP

251. ALAC uplift does not apply to an FI with an SACP in the 'aa' category because of the uncertainty regarding how the resolution would be handled in an extreme or severe stress scenario given that such an FI is far from potential distress. Also, the incremental benefit to senior unsecured obligations is not commensurate with a notch of uplift at this point in the rating scale.
252. For an FI with an SACP of 'a' or 'a+', the maximum ALAC uplift is one notch.
253. The maximum ALAC uplift for an FI with an SACP of 'a-' or below is two notches.
254. When assessing the sufficiency of ALAC, we take into account an FI's public commitment to maintaining a certain buffer of eligible ALAC instruments outstanding by assessing the credibility of these targets. Subject to all other conditions in this ALAC section, we determine the notches of ICR uplift for ALAC based on our typical ALAC-to-S&P Global RWAs thresholds outlined in table 24. We would typically look for an FI to maintain, or reach and thereafter maintain, the ALAC threshold over approximately the next two years. When up to one or two notches are possible, we may apply less uplift if we consider that outcome to better reflect the creditworthiness of the FI. If we expect that a subsidiary would go through its own resolution, we determine an anchor and SACP for that subsidiary in order to assess direct ALAC uplift to that subsidiary.

Table 24

ALAC Headline Quantitative Thresholds

Uplift thresholds expressed as percent of S&P Global RWAs before diversification	--ALAC-to-S&P Global RWAs typical cumulative thresholds for ICR uplift*--	
	Up to one notch (%)	Up to two notches (%)
Anchor of 'bbb-' or higher	3.00	6.00
Anchor in 'bb' category	2.50	5.00
Anchor of 'b+' or lower	2.00	4.00

*The headline thresholds can be adjusted up or down due to qualitative factors. If the SACP is 'a' or higher, then uplift is subject to limits.
ALAC--Additional loss-absorbing capacity. ICR--Issuer credit rating. RWAs--Risk-weighted assets.

255. For a given FI, by assessing qualitative factors, we may also adjust the ALAC thresholds when we consider the FI's ALAC to be materially different from that indicated by the ALAC-to-S&P Global RWAs measure. This adjustment reflects that qualitative considerations can limit the quantity or potential efficacy of ALAC, as well as the ability of ALAC to absorb losses when the FI is under economic stress. The qualitative adjustments therefore assess the degree to which the headline quantitative metrics may over- or underestimate an FI's loss-absorbing capacity.
256. We make an adjustment to the ALAC thresholds if, for a given FI, we consider that there are factors that potentially meaningfully affect the availability or efficacy of ALAC or the magnitude of loss-absorption capacity needs incorporated in our analysis. We can adjust the ALAC thresholds upward or downward by up to 100 bps for the first uplift notch and up to 200 bps for the second uplift notch. While these are the standard adjustments, we may make a larger basis point adjustment when we consider the underlying impact of the factor or factors driving the

adjustment to be particularly significant.

257. Factors that could lead us to raise the typical ALAC thresholds include the following. A combination of two or more could affect the amount or efficacy of ALAC so severely as to remove any ALAC uplift:

- Any concentration of maturities of ALAC instruments, with particular emphasis on maturities within five years.
- If an instrument's loss-absorbing efficacy has limitations because of prepositioning requirements set by host regulators of material subsidiaries, and any other material obstacles to deploying ALAC flexibly within a group in a stress scenario. For example, we typically consider raising the ALAC thresholds if the ALAC we would consider in determining a certain GCP (and, thus, the parent operating entity ICR) significantly overstates the loss-absorption capacity of the group. This could be the case if a group's ALAC is significantly concentrated in a subsidiary, whose ALAC is subject to restrictions limiting its use to cover losses in other parts of the group, and if that subsidiary has significantly stronger creditworthiness (as indicated by its SACP) than the group (as indicated by the group SACP) or the parent operating entity.
- If we consider that there is a potential significant constraint to ALAC efficacy because of the way a parent entity downstreams external loss-absorbing capacity internally. For example, it could be a negative factor if a parent entity downstreams external ALAC to operating subsidiaries in the form of senior liabilities. If double leverage is created because an NOHC downstreams external ALAC to operating subsidiaries in a more subordinated or equity-like form, the external ALAC benefits the GCP and, thus, the ICRs on the operating subsidiaries. But, the ICR on the NOHC may be a greater number of notches below the GCP than the minimum standard to reflect the double leverage.

258. Factors that we could consider in making adjustments to the typical ALAC thresholds include:

- The bail-in capacity from ALAC is sufficiently different from that suggested by the ALAC to S&P Global RWAs metric because of the extent to which our standard risk assumptions overstate or understate the potential for losses in a stressful environment given the risk characteristics of a particular FI. For example, we typically consider raising or lowering the typical ALAC threshold if we consider the ALAC-to-S&P Global RWAs ratio to materially under- or overestimate the bail-in capacity. This may be because our view of the past and expected losses on the current mix of business, as well as the risk concentration and diversification, of a given FI materially deviates from our systemwide calibrated risk assumptions embedded in the S&P Global RWAs (denominator of the ALAC thresholds). We may also use this adjustment when we consider that the amount of ALAC included in the numerator sufficiently over- or underestimates the actual loss-absorbing capacity.
- We could lower the ALAC threshold for an FI if it has business operations outside the scope of required bail-in capitalization that materially raise the FI's S&P Global RWAs, including, for example, an insurance subsidiary that is subject to independent prudential capital adequacy oversight.
- We could lower the ALAC threshold for an FI if a prefunded resolution fund has the potential to increase the effective loss-absorbing capacity of FIs in a given jurisdiction, and if the fund ensures full and timely payment of FIs' senior unsecured obligations. (We would not do so when the fund is for use in liquidation only, or its use is conditional on partial bail-in of senior unsecured obligations.) In certain jurisdictions, if at least 8% of a failed FI's liabilities (including capital) at the time of resolution must be bailed in before such a resolution fund can contribute, the potential ICR benefit of such a fund is relevant only for an FI that we expect to meet this threshold without defaulting on a senior unsecured obligation.

259. Even if ALAC includes financial obligations raised by an NOHC, ALAC uplift only applies to the ICR on the operating entity--and not to the ICR on the NOHC, except if we consider that ALAC instruments reduce the likelihood of default on NOHC senior unsecured obligations. ALAC-related uplift to NOHC ratings requires:
- That the NOHC has enough junior liabilities to absorb losses at the operating entity and act as a cushion reducing the risk of default on senior unsecured bonds issued at the NOHC level, and
 - That the resolution approach the authorities follow would not lead to a default on any NOHC senior unsecured debt at or around the time the NOHC subordinated obligations default.
260. ALAC uplift raises an FI ICR or associated GCP above the relevant sovereign local or foreign currency rating only if the FI meets the conditions to be rated above the sovereign (see the group rating and rating above the sovereign criteria articles). These conditions include that ALAC would enable the FI to survive the sovereign stress scenario without defaulting. For this, the stress event would need to trigger a resolution that would lead to the conversion or write-down of the ALAC resources. Stress testing under the rating above the sovereign criteria takes into account any ALAC instruments already issued, but not expected issuance.
261. A prudentially regulated subsidiary is eligible to be rated higher than the GCP because of ALAC issued by the subsidiary if all of the following features are met:
- We expect that the subsidiary would be subject to a separate resolution process;
 - We consider that, because of its resolvability, the subsidiary will be able to continue operating without defaulting on its senior unsecured obligations in the event of a failure or resolution of the parent; and
 - The ALAC of the subsidiary is not usable to recapitalize another part of the group and, therefore, is not included in the measure of ALAC for the group (as such, the subsidiary's ALAC does not support the GCP).
262. In line with the group rating criteria, if group ALAC is available to support a subsidiary, the subsidiary ICR is based on the GCP including the benefit of ALAC. Otherwise, it is based on the group SACP.

ALAC considerations for multiple-point-of-entry groups

263. Among the entities that we see as likely to be subject to a well-defined resolution process, most of the time we expect the underlying resolution planning to follow a single-point-of-entry (SPE) approach. That is, there would be a single resolution entity (usually at the top of the group) that issues substantially all of the loss-absorbing capacity for the group. Under a resolution action, the group would remain substantially intact--at least in the initial bail-in and stabilization phase. This approach lends itself to an ALAC calculation based on consolidated group data, which typically aligns with the basis on which we assess the group SACP.
264. We expect a minority of groups to be subject to a multiple-point-of-entry (MPE) approach to resolution. In this approach, resolution planning identifies multiple resolution subgroups and entities within the group, each of which would, to some extent, issue and control its own loss-absorbing capacity. Under a resolution action, the group would fragment into multiple resolution subgroups if parts of it became nonviable.
265. For MPE groups (where we would typically determine subgroup GCPs for the different parts of the group), we assess the loss-absorbing capacity and the potential ALAC uplift within each subgroup. This means ALAC uplift will be applied to the ICRs on the relevant entities within the subgroup.

(See the group rating criteria for more detail on how we assess subgroups.) Specifically for the parental subgroup, our assessment of ALAC uplift could be based on an adjusted consolidated (top-down) approach, or else a solo (bottom-up) approach. Both may require the use of threshold adjustments or estimates where an entity's loss-absorbing capacity disclosure is limited.

266. Where a group is subject to a blended SPE and MPE approach to resolution planning or is in transition between the two, we apply SPE or MPE approaches to it as we consider appropriate.

Additional Support Adjustment

267. We may incorporate additional support into an FI's potential ICR (beyond, for example, the uplift from the FI government support tables 21-23 or ALAC, if applicable) using an additional support adjustment when we expect a government to provide additional support in the near term above the level already incorporated into our analysis. We determine this based on our assessment of the policy environment and the stress the FI faces, as well as whether we think the sovereign has sufficient capacity to provide this support.
268. In practice, it can take some time for a government to make a specific commitment to provide additional support after a financial problem surfaces. In such cases, we estimate the amount or range of support that we expect to be provided.
269. To establish the number of notches of additional support adjustment to include in the ICR, we estimate how much higher the SACP would be once the expected support has been received by building the expected support into our evaluation of the FI-specific SACP factors. Until the government has committed the support, we include this support in the ICR. After the government commits the support, we factor it into the SACP.
270. We also may incorporate an additional support adjustment in the ICR for an FI that has ALAC support in its ICR when we consider a resolution to be a near-term outcome. To establish the number of notches of temporary uplift for an additional support adjustment, we estimate the combined impact of the support that we expect to arrive in the event of a resolution, without differentiating whether support is from the government or junior creditors.
271. We can factor an additional support adjustment into the ICR on an entity even if we have classified it as having low systemic importance. This is because the support uplift is based on having more visibility regarding what we can expect the government to do to support a specific entity, and government policy decisions can be situation-specific.
272. When we estimate what the SACP could be following the provision of support, we base this either on our expectation incorporating information provided by the government or by our calculation of the amount of fresh capital or liquidity required to restore capital or liquidity to the regulatory minimum. We base the regulatory minimum on the amount that will keep the entity a going concern according to the regulator but can factor in a different amount of support if the regulator expects the entity to comply with a different requirement.
273. When estimating what the SACP could be following the provision of support, we incorporate the benefit of the support into the relevant SACP factor or factors that will benefit from the support. Depending on the nature of the support, this could apply to any of the SACP factors, including our assessments of capital, risk position, funding, and liquidity.
274. When factoring in an additional support adjustment for an FI that has ALAC support in its ICR, the potential uplift above the SACP due to the additional support adjustment reflects the sum of ALAC and government support we expect to be provided. The uplift is based on the SACP that we expect after recapitalization and after other support has been received.
275. This approach reflects that the details of the potential recapitalization of the FI are clearer when

failure is a less remote prospect. For example, if after absorbing losses, we expect ALAC to generate US\$2 billion of capital for a bank and the government to provide US\$1 billion of a capital injection following the ALAC activation, then we set the ICR at the level that we estimate the SACP would be if the bank were recapitalized by US\$3 billion. If the bank does not have enough ALAC resources to meet an ALAC threshold for ICR uplift, we may still include the amount of ALAC resources that it does have in our assessment of the recapitalization, if we expect that these instruments would be bailed in as part of the recapitalization.

SECTION 4: ICRs ON BANK BRANCHES

Section 4 provides the criteria for determining the ICRs on bank branches.

276. If a bank branch does not benefit from a guarantee covering all its liabilities and meeting our rating substitution criteria, the ICR on the branch is the same as that on the bank, except if the branch is located in a different country than the "parent" bank. A parent bank is the bank from which the branch emanates.
277. A bank branch located in the same country as its parent bank has, in our view, the same creditworthiness as the bank from which the branch emanates. We typically do not assign ratings to those branches since the branch and its parent bank form a single legal entity. But if rated, the branch has an ICR equal to that on the parent.
278. For foreign bank branches--that is, those located in a different country than that of the parent bank--we consider the potential for adverse host sovereign actions. Our foreign currency rating on the host sovereign therefore caps our view of the branch's creditworthiness, unless we consider that the risks of freezing deposits or implementing other controls will not affect the parent bank's ability to support full and timely payment of financial obligations by the group member. In this case, the ICR on the branch can be up to two notches above the foreign currency host sovereign rating. Other caps apply for foreign branches located in certain offshore banking centers, as well as branches of EU banks based in another EU member state. This section should be read in conjunction with "Additional Considerations For Assigning Ratings To Foreign Branches And Their Financial Obligations" in the appendix.

Jurisdictions Whose Sovereign Foreign Currency Ratings Are 'CCC+' Or Lower

279. The ICR on a branch located in a jurisdiction whose sovereign is rated 'CCC+' or below is the lower of 'B-' or the ICR on the parent bank, unless sovereign intervention risk implies a lower rating as per our 'CCC' criteria.

Branches Located In Offshore Banking Centers

280. Branches located in offshore banking centers are unique, in our view, in that the sovereign has very high incentives not to interfere in the branch meeting its financial obligations, even in a stress situation for the host sovereign. Such branches are typically a local branch of an international bank that is neither allowed to take deposits nor lend to local companies or persons, and operates under a restricted special category offshore license. For branches meeting these conditions, the ICR on the branch is the same as that on the parent bank.
281. We define offshore banking centers as jurisdictions where the activities of international bank branches are restricted through a special category offshore banking license that prohibits taking local deposits or making local loans.

Branches Of EU Banks That Are Located In Another EU Member State

282. We don't consider that branches of EU banks located in another EU country are immune to local sovereign intervention risk. However, this risk is reduced because such branches are not subject to host country supervision and can avail themselves of the so-called "passport approach." This allows the branches to operate in other EU countries without a separate banking license or full host country supervision. The institutional and legal arrangements that create the single EU market reduce member states' ability to unilaterally impose restrictions on the flows of resources across borders within the EU, and ensure a single insolvency proceeding of an EU bank rather than multiple proceedings in the various EU jurisdictions where the bank operates.
283. Our view of the creditworthiness of, or ICR on, a branch of an EU bank based in another EU jurisdiction is the lower of:
- The ICR on the bank; or
 - Four notches above our foreign currency rating on the host sovereign if that rating is 'BBB-' or higher, or two notches above if not.
284. However, we rate the branch as if it were a non-EU branch if the host sovereign is a member of the eurozone but we consider an exit from the eurozone to be a material likelihood.

SECTION 5: ISSUE CREDIT RATINGS ON INSTRUMENTS OTHER THAN HYBRID CAPITAL

Section 5 provides the criteria for determining the issue credit ratings on instruments other than hybrid capital.

285. We rate financial obligations issued by FIs, including NOHCs of such groups, using the following principles:

- For hybrid capital instruments, we apply our hybrid capital criteria (see Related Criteria).
- We assign RCRs to instruments using the section on RCR liabilities.
- For an ICR of 'B-' and higher, we rate senior secured (except covered bonds) and senior unsecured at the ICR level unless they are RCR liabilities, or unless certain conditions apply for an NBFI issuer, as addressed in the next section.
- If the ICR is 'CCC+' or lower, we assign an issue credit rating in line with 'CCC' rating criteria. We do not rate senior debt obligations below 'CC' or subordinated instruments below 'C' unless a 'D' issue credit rating applies.
- If an instrument benefits from a guarantee consistent with our guarantee criteria or has more than one unconditional obligor (unless it is in scope of "Methodology And Assumptions For Rating Jointly Supported Financial Obligations"), then we rate the instrument at the level of the ICR on the highest-rated obligor or guarantor, except when 'CCC' criteria apply.
- We rate short-term obligations that are not RCR liabilities at the same level as the short-term ICR (unless, potentially, the ICR is 'D' or 'SD') and do not raise or lower short-term issue credit ratings relative to the short-term ICR to reflect recovery prospects or subordination.
- We do not assign recovery ratings.
- We do not classify conventional nondeferrable subordinated debt (NDSD) as a hybrid. If an FI ICR is 'BBB-' or higher, we rate its conventional NDSD one notch below the ICR. If the ICR is 'BB+' or lower, the issue credit rating is two notches below the ICR, subject to a floor at 'C', unless 'D' applies.
- For how we assign 'CCC+' issue credit ratings and below to subordinated instruments, see "Credit FAQ: Applying "Criteria For Assigning 'CCC+', 'CCC', 'CCC-', And 'CC' Ratings" To Subordinated And Hybrid Capital Instruments."
- We assign a local currency issue credit rating when the obligation is denominated in the currency of the country where the FI is located, which may differ from the operating currency of the FI. Otherwise, we assign a foreign currency issue credit rating. The local currency of a bank's foreign branch can differ from that of the bank because it is resident in its host country, so its local currency is the same as that of the host country.

Additional Considerations For NBFI--Senior Secured, Senior Unsecured, And Junior Secured Debt

286. If an NBFI is not prudentially regulated or would likely not be covered by a regulatory or official resolution process (which often includes NBFI NOHCs that issue debt), we rate senior secured or

unsecured debt at the same level as the ICR when the ICR is 'BBB-' or higher. We rate first-lien senior secured debt at the same level as the ICR. We rate junior secured debt at the same level as the ICR when the ICR is 'BBB-' or higher. When the ICR is 'BB+' or lower, we rate the most senior obligation at the same level as the ICR and senior unsecured or junior secured (such as second lien or debt secured by a blanket lien) obligations lower than the ICR by one or two notches when specified scenarios are met, as outlined below. These notches reflect that the debt is subordinated in these scenarios--and not an increased likelihood of default versus the ICR. If the scenarios do not apply, we rate the obligations at the same level as the ICR.

287. For these scenarios, we adjust reported assets by limiting the amount of goodwill to 10% of included assets.

288. **Scenario A:** When the ICR is 'BB+' or lower, we rate debt instruments one notch below the ICR when either of the following conditions apply:

- Priority debt (see glossary) is greater than 15% of adjusted assets and we expect unencumbered assets to be less than the rated unsecured or junior secured debt, or
- Priority debt is greater than 30% of adjusted assets and we expect unencumbered assets to be greater than the rated unsecured or junior secured debt.

289. **Scenario B:** When the ICR is 'BB+' or lower, we rate debt instruments two notches below the ICR when both of the following conditions apply:

- Priority debt is greater than 30% of adjusted assets, and
- We expect unencumbered assets to be less than the rated unsecured or junior secured debt.

However, under scenario B, if an issuer exceeds--but is close to--both thresholds, then we may rate the instruments one notch below the ICR.

290. When considering scenarios A and B, we deduct nonrecourse secured debt from priority debt, and deduct the assets pledged to that debt from adjusted assets. When we make that adjustment, in addition to applying the rating approaches under these scenarios, we also rate the most senior remaining debt instrument one notch lower than the ICR if we expect unencumbered assets to be less than the amount of the most senior debt.

291. When considering these scenarios, we take a prospective view when the calculation is close to the thresholds (the 15% or 30% thresholds, or where unencumbered assets are close to covering unsecured debt). For example, if we expect that the issuer is likely to pledge unencumbered assets toward payment of the nonrecourse secured debt (likely to maintain franchise or maintain equity cash flows), and the calculation is close to a threshold, we likely rate the issue assuming that threshold is crossed.

292. **Scenario C:** We also may rate senior unsecured debt or junior secured debt one or two notches below the ICR if the issuer has meaningful amounts of netted, contingent, or complex exposures on its balance sheet (such as securities repurchase and reverse repurchase agreements or open derivative positions). "Meaningful" means an amount sufficient to make the determination of available unencumbered assets uncertain.

293. Our estimate of priority debt and adjusted assets is forward-looking and includes scheduled debt amortizations over the subsequent 12-month period. For example, regarding revolver draws, when a draw results in a level of priority debt to adjusted assets exceeding 15% or 30%, and we expect it would remain so, we lower the issue credit rating and maintain that level for a minimum of four quarters, irrespective of short-term fluctuations in the priority debt.

SECTION 6: RESOLUTION COUNTERPARTY RATINGS

294. Section 6 provides the criteria for assigning RCRs. RCRs are a special-purpose rating type applicable to FIs globally that are likely to be subject to an effective resolution regime in the event of distress. They are generally relevant for institutions eligible for ALAC uplift but may also be applicable to other FIs subject to resolution regimes. We do not assign RCRs to covered bonds, rather we use our covered bonds criteria (see Related Criteria). In most cases, RCRs are assigned to rated operating entities of a financial group.
295. The term RCR liabilities refers to the relevant obligations of issuers that may be protected from default in an effective resolution process. An RCR is a forward-looking opinion of the relative default risk of these certain senior financial institution liabilities that may be protected from default in an effective resolution process. We set the RCR either at the same level as the ICR or higher than the ICR. It indicates our view of the default risk of RCR liabilities relative to the default risk represented by the ICR and associated senior liabilities.
296. An RCR addresses the likelihood of default and does not provide an opinion on recovery prospects or expected loss following a default on some or all of an FI's liabilities that are addressed by the RCR. RCRs are based on the long- and short-term global ratings scales. The short-term RCR on an FI is determined in reference to its long-term RCR, based on "Methodology For Linking Long-Term And Short-Term Ratings." RCRs do not have rating outlooks. We may place RCRs on CreditWatch, using the same approach we use to place ICRs or debt issue ratings on CreditWatch.

Jurisdictions, Liabilities, And Issuers Where An RCR Is Relevant

297. RCRs only apply to FIs operating in jurisdictions whose resolution frameworks are sufficiently effective, as defined in our ALAC framework. Only these frameworks provide the necessary conditions for a likely successful resolution of certain entities, in our view, which may differentiate between the default likelihood of RCR liabilities and that of other senior liabilities represented by the ICR. As a result, we can assign an RCR above the relevant ICR.
298. When an entity operates in a jurisdiction whose resolution framework is sufficiently effective, but the likelihood of default of RCR liabilities will, in our view, not improve, we do not assign an RCR higher than the relevant ICR. This would be the case, for example, where we consider that additional capacity, be it from the balance sheet or external sources, is insufficient to change the likelihood of default relative to the ICR.
299. Within jurisdictions that have sufficiently effective resolution frameworks, and where we have identified RCR liabilities meeting the conditions in the following paragraphs, RCRs apply only to issuers that are likely to be subject to a resolution process were they to reach nonviability. This is because we expect the base-case default risk scenario for the entity and relevant liabilities would be determined by the resolution of the institution, and therefore the provisions of the resolution regime would likely be activated.
300. For each jurisdiction with a sufficiently effective resolution framework, we assess whether any senior liability categories may be protected from default by an effective process beyond the elements we measure in our ALAC analysis. The RCR addresses liabilities benefiting from such elements that provide for a credible and likely continuation for those types of obligations, without

them defaulting in a resolution process.

301. For a senior liability category to be considered protected beyond what we address in our ALAC analysis, it must be likely to continue to perform on a complete and timely basis in the resolution scenario. We could consider this to be the case if:
- It is explicitly excluded by regulation from those liabilities that may be bailed in if the obligor enters a resolution, or
 - We consider the liabilities' resolution-driven default is unlikely because of all of the following: The type of liability is earmarked in the resolution framework for potential exclusion from bail-in at the discretion of the national regulator, other creditors in our view are unlikely to legally challenge such an exclusion (for example due to the "no creditor worse off" principle), and the type of liability meets at least one of the characteristics listed in the following paragraph.
302. The assessment of these characteristics typically takes into account how that liability type is either described in the legislation or regulations or viewed by the regulators:
- We view the continuity of the operations of that type of liability as critical for financial stability in that jurisdiction.
 - We consider that the steps to carry out a bail-in of that type of liability would involve such high operational complexities that would make its bail-in unlikely in a reasonable time.
 - We consider that the performance of that type of liability is critical for the resolved entity to continue operating.
 - We consider that the bail-in of that type of liability would not provide any economic benefit to the resolution or would even destroy value.
303. We take a different approach for jurisdictions where we do not have sufficient clarity on the mechanisms that provide protection from default for certain senior liabilities (beyond what we incorporate in our ALAC analysis) or for the liabilities that these mechanisms are designed to protect. In these instances, for issuers that are likely to be subject to a resolution process were they to reach nonviability, we assign only issuer-level RCRs--at the same level as the ICRs.
304. Our RCR jurisdictional assessment encompasses relevant aspects of a country's resolution framework and the expected treatment of different liability categories within that framework.
305. Typically, a distinct RCR is assigned to each legal entity in the group when the resolution framework applicable to that entity and the resulting identification of RCR liabilities meet the conditions outlined above. NOHCs of financial groups would be eligible for an RCR if RCR liabilities are at the NOHC level and the resolution framework specifically provides the same conditions aimed at preserving those NOHC liabilities without a default through a resolution process as it does for operating entity liabilities.
306. A single RCR is assigned to a given legal entity, covering all its RCR liabilities. This is because the default risk of these liabilities depends on a common factor: the potential for a successful resolution process. If a specific bond has an issue credit rating and is also an RCR liability, the issue credit rating on the bond is assigned at the same level as the RCR on that issuer.

Uplift Above The ICR

307. RCR uplift--the extent to which an RCR may be higher than the relevant ICR--primarily depends on the amount of insight we have into:

- Possible resolution scenarios, and
- Whether resolution authorities, in trying to preserve financial stability, are likely to succeed in resolving the entity so that RCR liabilities continue to perform on a complete and timely basis as if the obligor was a going concern.

308. Subject to applicable conditions in the following paragraphs, RCR uplift is up to one notch if the ICR is 'BBB-' to 'A+' or up to two notches if the ICR is 'B-' to 'BB+'. RCR uplift does not apply to FIs with ICRs in the 'AA' and 'AAA' rating categories.
309. RCR uplift is limited to one notch for issuers rated 'BBB-' to 'A+' to reflect the uncertainty about how resolution may be handled in an extreme or severe stress scenario for issuers that are far from potential distress. For the same reason, we consider that the incremental benefit to RCR liabilities is not commensurate with uplift for financial institutions with ICRs in the 'AA' and 'AAA' rating categories.
310. When we determine that RCR uplift is warranted for issuers rated 'B-' to 'BB+', we typically apply two notches of uplift unless factors contribute, in our view, to reduced visibility or likelihood of a successful resolution outcome, taking into account the evolving adequacy of the institution's loss-absorbing capacity relative to similarly rated peers and other relevant factors. We assign one notch of uplift if, despite the reduced visibility or likelihood of successful resolution, we consider the likelihood that the resolution process would preserve the institution's operational capacity is moderate.
311. For an issuer with an ICR of 'CCC+' or below, the RCR is either:
- Up to two notches above the ICR, similar to issuers rated between 'B-' and 'BB+' (inclusive) as described in the previous paragraph; or
 - At the rating level consistent with the default risk of RCR liabilities, incorporating any additional support adjustment and taking into account the default scenario associated with the ICR according to the scenarios in the 'CCC' rating criteria.
312. We use a different approach to determining RCR uplift when the resolution framework establishes mechanisms of protection from bail-in for substantially all types of instruments that are not part of the total loss-absorbing capacity (TLAC) cushions (or similar regulatory concepts). We would assess whether the framework offers a comparable reduction in default risk relative to that of the RCR liabilities of entities operating in jurisdictions that have ICR-level liabilities that can be bailed in.
313. This can occur when, in our view, other forms of support are available that result in a comparable reduction in default risk, such that the ICR on an institution may be raised to a level consistent with the level of support the RCR implies. In such cases, the RCR on an institution is typically aligned with the ICR, and both ratings incorporate the same amount of uplift that would otherwise be applied only to the RCR. Otherwise, neither the ICR nor RCR benefit from any RCR uplift.
314. If we consider that an institution is approaching nonviability, and we expect the application of resolution measures in the near term, RCR uplift may exceed the limits outlined above, because of a positive additional support adjustment, to reflect our expectation of additional support for the RCR liabilities (which may differ from the level of additional support expected for the ICR).
315. Otherwise, our assessment is informed by our expectations regarding the likelihood of a resolution that would affect the default risk on the RCR liabilities. In such a scenario, the extent of RCR uplift for such expected near-term support is determined by our estimate of the combined impact of the support that will be made available to the RCR liabilities by the resolution authorities, including capital support from the activation of loss-absorbing capacity. This assessment of an additional

support adjustment therefore considers the potential impact of a resolution on the RCR liabilities even when there is no additional support adjustment uplift for the ICR.

316. For all issuers, the RCR uplift is subject to the following conditions:

- An institution cannot benefit from RCR uplift if it is expected to be materially noncompliant with applicable regulatory requirements for debt cushions that can be bailed in (for example, TLAC for some issuers; minimum requirement for own funds and eligible liabilities for others) that would be required to activate a resolution process.
- An RCR is at the same level as the ICR if, in our view, the resolution framework or the likely institution-specific resolution scenario we envisage does not support a clear expectation that the issuer's RCR liabilities will continue to perform beyond a default of other senior liabilities whose default risk is addressed by the ICR, including its senior unsecured debt. This could be the case if, for example, we think it's doubtful that the resolution process would preserve the entity's operational capacity.

Assigning RCRs With No Uplift Above The ICR

317. We typically do not consider any RCR uplift when we think that there is no material difference in default risk for RCR liabilities relative to other senior liabilities we rate in line with the ICR. This applies if we lack sufficient visibility on either the mechanisms that provide protection from default to certain senior liabilities beyond what we incorporate in our ALAC analysis or on the liabilities these mechanisms are designed to protect, or both. It also applies if the likelihood of a successful resolution for any specific case protecting RCR liabilities from default (either tied to resolution scenario, regulatory, or issuer-specific factors) is meaningfully uncertain.

RCRs On Entities Benefiting From Group Or Government Support

318. We typically do not assign RCRs to entities for which the expectation of extraordinary external government support is incorporated into the ICR, except, for example, where we include an additional support adjustment. When ratings include uplift for extraordinary government support, even though an effective resolution framework may be in place, the default risk on senior liabilities (including RCR liabilities) is typically driven by the relevant support mechanism rather than by a resolution process activated by the relevant authorities.

319. We only assign an RCR to a subsidiary FI when we determine that the subsidiary's RCR liabilities have the potential to benefit from resolution powers being applied to either the group it belongs to, to the subsidiary itself, or to both.

Incorporating An Additional Support Adjustment Into An RCR

320. We can incorporate an additional support adjustment to provide flexibility in determining the RCR when an issuer is approaching nonviability and there is greater clarity about the potential application of resolution measures.

321. This allows us to set an RCR at a level that anticipates the imminent bail-in recapitalization of a bank, taking into account statements by government authorities, applicable resolution processes, etc. The resulting RCR considers the impact of support arising from the bail-in of junior creditors, along with any other potential external support applicable in that situation.

322. The additional support adjustment is applicable to either the ICR or the RCR. If an additional

support adjustment is incorporated in the ICR, the prior differential (in number of notches) between the ICR and RCR typically remains. Alternatively, when there is imminent risk of default of ICR level liabilities, the additional support adjustment is used to expand the gap between the ICR and RCR if the default risk of the RCR liabilities has not increased in line with that on the ICR level liabilities. In such a case, the long-term RCR can be more than one or two notches higher than the long-term ICR.

323. Generally, the additional support adjustment provides a preliminary view on the rating levels that an issuer can achieve immediately following a resolution process, while recognizing that this assessment is subject to significant information constraints arising from the situation of a systemically important bank rapidly approaching nonviability.
324. In the following example of the use of an additional support adjustment, Bank A initially has an SACP of 'b', an ICR of 'BB-', and an RCR of 'BB+'. If the bank's stand-alone performance deteriorates, suggesting imminent nonviability, we reduce the SACP to 'ccc' based on the specific default scenarios applicable to that bank. Based on an assessment of the pending bail-in recapitalization, we use an additional support adjustment to maintain the ICR at 'BB-' and the RCR at 'BB+'.
325. In an alternative example, Bank B also has an SACP of 'b', an ICR of 'BB-', and an RCR of 'BB+'. Assessing a similar deterioration, we conclude the impending resolution process is likely to lead to default of some ICR-level liabilities, but not of its RCR-level liabilities.
326. In this case, we revise the SACP to 'ccc' and lower the ICR to 'CCC', reflecting our assessment of default likelihood for the bank. Despite the underlying deterioration, we only lower the RCR to 'BB' because of our assessment of the potential of the bail-in recapitalization to restore the bank to a viable state and ensure timely payment on RCR liabilities. We take into account an additional support adjustment, including an estimate of the liabilities converted to equity (relative to losses to be absorbed) and a consideration of other aspects of support (if any) that we expect will accompany the resolution.
327. In both examples, immediately following the successful bail-in, the ICR is raised to 'BB' and aligned with the RCR. The RCR would not be raised above the ICR until the bank reestablishes capacity to undergo a successful future bail-in.

Foreign And Local Currency RCRs

328. We typically assign the same RCR to foreign currency RCR liabilities as we do for local currency RCR liabilities, since liabilities subject to foreign law are usually not at a greater risk of loss from actions of foreign authorities than of domestic authorities in a resolution scenario. RCRs are generally based on the foreign currency ICR in the event an institution has a different (typically higher) local currency ICR. A distinct local currency RCR may be assigned if there is sufficient visibility that the default risk of local currency RCR liabilities is lower than the default risk of liabilities rated at the local currency ICR level.

RCRs That Exceed The Sovereign Rating

329. An RCR can be up to two notches above the foreign currency sovereign rating on the institution's country of domicile if we expect RCR liabilities to avoid default under the applicable sovereign stress test, as described in our ratings above the sovereign criteria (see Related Criteria). This assessment considers the likelihood of an orderly resolution and of whether supranational institutional arrangements would be available and extended to the entity to avoid such a default, with the objective of supporting financial system stability. If the sovereign foreign currency rating

is 'B-' or below, the limits of table 2 in the ratings above the sovereign criteria apply to RCRs. The analysis includes considering the potential operational impact of a sovereign default on the resolution authority's ability to successfully handle the resolution.

330. We assign an ICR and RCR above the foreign currency sovereign rating if we conclude that both ICR liabilities and RCR liabilities would pass the stress test. This could happen, for example, because the loss-absorption capacity provided by more junior liabilities of the bank means that the ICR and RCR liabilities can withstand a sovereign default while keeping the bank viable.
331. If this is not the case, the ICR will not exceed the foreign currency sovereign rating. However, we assign an RCR that exceeds the foreign currency sovereign rating if we determine that the shortfall could be covered by other liabilities that can be bailed in and that are not RCR liabilities. As part of this analysis, we do not intend to indicate the exact amount that would be sufficient to meet the applicable stress test since that would be highly situation-specific. We also assess whether bailing in ICR level liabilities could undermine an orderly resolution.
332. To assign an RCR above the sovereign rating, we therefore also analyze whether, in resolution, the shortfall could be covered through other sources. We consider this could be envisaged if, for example, the entity is a systemically important financial institution operating in a developed-market country that is a member of a monetary and banking union, with an effective resolution framework. In such a situation, if we conclude that there is a reasonable likelihood that bank failures can be managed in an orderly manner and that external authorities will provide sufficient capital and liquidity to withstand the impact of a sovereign default, then the RCR can be higher than the sovereign rating.

RCRs On Bank Branches

333. We follow the same approach to assign an RCR to a branch as we do to assign an ICR to a branch. Therefore, the RCR on a domestic branch is the same as the RCR on the parent bank. The RCR on a foreign branch is the same as the RCR on the parent bank, unless it is subject to a cap linked to the host sovereign foreign currency rating. We apply the same caps to RCRs and ICRs on foreign branches because we consider that they could be equally vulnerable to potential adverse actions by the host sovereign. For example, depending on their scope, a deposit freeze or payment moratorium could negatively affect both RCR liabilities and ICR liabilities.
334. We cap the RCRs and ICRs on branches of EU banks based in another EU country at prescribed levels above the host sovereign foreign currency rating. This is because EU member states have limited ability to restrict flows of resources in the event of the resolution of the parent affecting the branch.
335. We do not cap the RCRs or ICRs on foreign branches located in certain offshore banking centers. We consider that the host sovereign has very high incentives not to interfere in the branch meeting its financial obligations, even in the event of a resolution of the parent affecting the branch.
336. The following examples illustrate how we determine the ICR and RCR on a branch of a hypothetical EU bank with an 'A' ICR and 'A+' RCR:
- The bank has a rated branch in a country that is not an EU member state, on which our long-term sovereign foreign currency rating is 'BBB+'. The ICR and RCR are the lower of: the ICR and RCR on the parent bank, or up to two notches above the foreign currency rating on the host sovereign based on our view of potential support. (Two notches applies in this case because we consider that the risks of introducing a deposit freeze or other controls will not affect the parent bank's ability to support full and timely payment of financial obligations by the branch.) Therefore, the ICR and RCR on the branch are 'A'.

- The bank has a rated branch in a country that we classify as an offshore banking center. The branch is neither allowed to take deposits nor lend to local companies or persons, and it operates under a restricted special category offshore license. The ICR and RCR are set at the same level as those on the parent bank. Therefore, the ICR on the branch is 'A' and the RCR is 'A+'.
- The bank has a rated foreign branch in an EU member state on which our current long-term sovereign foreign currency rating is 'B-'. The ICR and RCR are the lower of: the ICR and RCR on the parent bank, or two notches above the foreign currency rating on the host sovereign. Therefore, the ICR and RCR on the branch are 'B+'.

Assigning RCRs And ICRs When There Are No Outstanding Liabilities At The ICR Level

337. An FI may have no outstanding liabilities at the ICR level due to jurisdictional or issuer-specific considerations. Certain resolution frameworks establish protection from bail-in for substantially all types of instruments, other than those that are part of the cushions explicitly earmarked for bail-in (typically those serving as ALAC). Alternatively, an FI may issue only liability types that are explicitly protected from bail-in or that are explicitly earmarked for bail-in under the applicable resolution framework.
338. To address these situations, we can raise the ICR on an institution to a level consistent with the level of support in the RCR, when we consider that other forms of support are available. Our assessment of whether to raise the ICR considers:
- The institution's overall balance sheet composition,
 - Possible other elements of support for successful resolution (such as a resolution fund), and
 - Possible responses of national and supranational authorities to the resolution process when all capacity that can be bailed in is absorbed but successful resolution remains in some doubt.
339. In considering whether to raise the ICR on an institution, we assess whether any features of the resolution regime would entail a comparable reduction in default risk for senior liabilities, commensurate with the insulation from default for issuers in other jurisdictions in connection with RCR liabilities.

Table 25

Examples Of Assigning RCRs And ICRs Where There Are Limited Or No Outstanding Liabilities At The ICR Level

(% of S&P Global risk-weighted assets)	Bank A	Bank B	Bank C	Bank D
ALAC	9	11	9	9
Senior debt (non-TLAC, but can be bailed in)	2	N/A	N/A	N/A
Senior liabilities (exempt from bail-in)	5	5	7	7
Additional source of default risk mitigation	N/A	N/A	N/A	Additional mechanisms for external support (including a state-backed resolution fund)
SACP	bbb+	bbb+	bbb+	bbb+

Table 25

Examples Of Assigning RCRs And ICRs Where There Are Limited Or No Outstanding Liabilities At The ICR Level (cont.)

(% of S&P Global risk-weighted assets)	Bank A	Bank B	Bank C	Bank D
ICR	A	A+	A	A+
RCR	A+	A+	A	A+

ICR--Issuer credit rating. N/A--Not applicable. SACP--Stand-alone credit profile. RCR--Resolution counterparty rating. TLAC--Total loss-absorbing capacity.

340. For example, Bank A is an institution with sufficient ALAC to lift its ICR two notches above its SACP. The institution has some liabilities (2% of S&P Global RWAs) that are rated at the ICR level (but could be bailed in if necessary, once TLAC is fully depleted), as well as various categories of senior liabilities considered RCR liabilities and rated at the RCR level, one notch above the ICR.
341. Banks B, C, and D are in another jurisdiction, and ICR-level liabilities are formally exempt from bail-in, even though they are potentially subject to losses in a liquidation. We raise the ICRs on these banks to the same level as the RCRs if we consider that the bail-in framework provides a reduction in default risk for these senior liabilities comparable to the reduction in default risk of RCR liabilities of Bank A and other comparable institutions.
- Bank B receives the RCR-equivalent uplift because it has additional ALAC comparable to the ICR-level liabilities of Bank A, suggesting that the most senior liabilities have roughly equivalent protection from default.
 - Bank C does not receive the RCR-equivalent uplift because it lacks the overall loss-absorbing capacity that Banks A and B have, and there are no other features that mitigate the default risk of the most senior liabilities.
 - Bank D is similar to Bank C but receives the RCR-equivalent uplift in its ICR because there are additional mechanisms for external support (including a state-backed resolution fund) that represent a potential additional source of default risk mitigation for Bank D.

Moratorium Powers Included In A Resolution Framework

342. Resolution frameworks sometimes include in their legislation or regulation a potential moratorium tool that can be part of a resolution. If that is the case, we assess nonpayment based on a declared moratorium against our benchmark of a standard five-day grace period, based on our established timeliness standards. Our rating definitions specify certain time limits we use when assessing whether a payment made after the due date can be considered timely (see "S&P Global Ratings Definitions").
343. Also see "Ratings Definitions" for how a temporary moratorium tool declared as part of a resolution affects an RCR. For example, if RCR liabilities are subject to a two-day nonpayment period due to a resolution-linked moratorium, we would not revise the RCR to 'D' or 'SD' if we expect that missed payments will be made within five days.
344. In jurisdictions with moratorium powers linked to a resolution, the grace period standards could restrict RCR uplift in certain circumstances. For example:
- For eligible institutions with long-term and short-term ICRs, we would not position the RCRs above the ICRs if we expect that the aggregate moratorium period in a resolution scenario is

likely to exceed five business days. This is because both RCRs would go to 'D' or 'SD' if the institution failed to make a payment on a short-term obligation within the time limit under our grace period standards.

- If we initially considered that a moratorium period was unlikely to exceed the applicable time limit but subsequently changed our view, we would remove RCR uplift from the relevant ICRs and issue ratings.

345. The maximum moratorium period is relevant if we expect that resolution authorities will impose a moratorium of that length. We focus on the likely duration of a moratorium rather than the maximum period possible under the applicable legislation. For systemic banks that would be resolved through a bail-in process rather than a traditional insolvency, we think that a moratorium would most likely be used for a period of less than five business days. For example, if a resolution authority determines on a Tuesday that a bank is failing or likely to fail (which is one of three preconditions for a resolution under EU law), and a resolution scheme is adopted the following day (Wednesday), a moratorium power could be used to bridge the gap to the weekend to allow more time for the design and implementation of the resolution.

Applying The RCR Criteria To Complex Groups

346. Here we address how we apply the RCR criteria to complex groups, particularly when entities are split between jurisdictions with effective and noneffective resolution regimes. An RCR is assigned to a specific legal entity and can be assigned to parent entities of financial institution groups as well as subsidiaries of such groups that meet the applicable criteria. An RCR is assigned to a legal entity when the resolution framework applicable to that entity and the resulting identification of RCR liabilities meet the conditions outlined in these criteria.
347. Typically we only assign an RCR to a subsidiary financial institution when we determine that the subsidiary's RCR liabilities can benefit from resolution powers being applied to either the group it belongs to (which is generally more likely when the subsidiary is core or highly strategic to the group), to the subsidiary itself, or to both. For this to apply, the subsidiary must itself be subject to an effective resolution framework. A subsidiary can still be assigned an RCR, even if not core or highly strategic, when it is itself subject to an effective resolution framework.
348. Subsidiary financial institutions include covered bond subsidiaries that are separately incorporated because of covered bond regulatory requirements and that have ICRs, even though the covered bonds themselves are rated using covered bond criteria.
349. We can assign an RCR to a subsidiary financial institution even when we don't assign an RCR to the parent bank, and the RCR can be higher than the ICRs of the subsidiary and parent bank. This could be the case, for instance, if the parent bank operates in a jurisdiction where we assess the resolution regime to be ineffective, while the subsidiary operates in a jurisdiction where we consider that certain of its senior liabilities are likely to be protected from default in an effective resolution process.
350. Also, some subsidiaries of a group may be assigned RCRs (possibly higher than their ICRs) while others may not. One key consideration is whether the subsidiary is located in a jurisdiction with effective resolution regimes and whether these regimes may protect certain types of liabilities from bail-in.
351. Global banks incorporate SPE and MPE resolution strategies. For groups with SPE resolution strategies, we can assign RCRs to the parent bank and subsidiaries that are part of its resolution perimeter (the collection of legal entities within a group that would be subject to the resolution process). We would assign RCRs to these entities if we see a material chance that the RCR

liabilities of all these entities could benefit from exemption from bail-in, through the application of bail-in powers at the group. For MPE groups, resolution authorities expect each subsidiary to have the capacity to absorb losses under TLAC requirements.

- ³⁵². For an MPE group, we can assign RCRs to some of the operating entities of the group and not to others, and the uplift may vary. Some of the factors our analysis will consider include the identity of the entities most likely to be designated as a point of entry for resolution, the effectiveness of the resolution regimes in the jurisdictions where these entities are located, and the existence of certain senior liabilities that may be protected from default in an effective resolution process.

SECTION 7: GLOSSARY

This section 7 glossary provides definitions of terms we use in the criteria.

Adjusted assets

353. Assets as reported, less insurance statutory funds, nonservicing intangibles, and allowance for loan losses in countries where such reserves are represented as a liability account.

Adjusted total equity

354. Total adjusted capital plus reserves deemed to be general or unallocated, plus unrealized gains, less equity in unconsolidated subsidiaries, capital of insurance subsidiaries, and any adjustments for securitized assets.
355. We make some adjustments to adjusted total equity (ATE) for a BDC. We exclude from ATE any unrealized appreciation or depreciation by excluding the impact of fair value adjustments. We also exclude from ATE equity investments in all fincos and equity in structured vehicles (collateralized loan obligations and collateralized debt obligations) to account for the higher risk associated with such leveraged investments. We may decide not to deduct equity investments in a finco, if the finco is leveraged less than 1x as measured by debt to reported equity.

Asset coverage ratio under the 40 Act (BDCs)

356. The Investment Company Act Of 1940 permits BDCs to issue senior debt securities and preferred stock (collectively, senior securities) in amounts such that asset coverage (market value of assets, less all liabilities and indebtedness not represented by senior securities divided by the aggregate amount of senior securities) is at least 200% after each issuance of senior securities, unless the BDC has adopted a modified asset coverage ratio (in which case it must be at least 150%).

Asset encumbrance

357. Assets are encumbered when contractually allocated or legally secured to specific funding issues or other repayment obligations. When assets are encumbered, they are not available to help repay unsecured debt or other repayment obligations, until the secured debt has been repaid.

Average adjusted assets

358. The average of the prior and current periods' adjusted assets.

Banks

359. Include deposit-taking entities, such as building societies, as well as entities that have banking licenses (unless the bank-licensed entity is in scope of another criteria for purposes of

determining the SACP, such as "Public-Sector Funding Agencies: Methodology And Assumptions," May 22, 2018, due to the nature of its business model).

Broad liquid assets

- ³⁶⁰. The sum of unrestricted cash, short-term interbank loans and reverse repurchase agreements and securities borrowing with banks maturing in less than one year, short-term reverse repurchase agreements and securities borrowing with nonbanks net of haircut maturing in less than one year, and securities holdings net of haircut. We apply this definition unless an FI's available financial reporting includes maturities of exactly one year in the same category as maturities of less than one year. When this occurs, we may classify maturities of exactly one year in the "less than one year" category for that FI. For haircuts, see "Metrics Definitions" in the appendix.

Business development company (BDC)

- ³⁶¹. BDCs are a type of closed-end investment fund in the U.S. that the U.S. Congress created in 1980 with amendments to the Investment Company Act of 1940. BDCs invest primarily in the debt and equity of small and medium-size, mostly private businesses.

Confidence sensitivity

- ³⁶². A qualitative assessment of an entity's sensitivity or vulnerability to an erosion of market confidence. Some entities are more vulnerable to market confidence than others because of their business models or funding mix.

Conventional nondeferrable subordinated debt (NDSD)

- ³⁶³. A nondeferrable subordinated instrument that has the same default risk as senior debt, has no contingent capital clause, and does not absorb losses before a legal default of the issuer.

Directed lending

- ³⁶⁴. A form of government intervention via ownership, regulation, or other measures to direct banks to lend to particular borrowers or sectors for political purposes, which may lead to higher credit losses than lending based on the bank's assessment of the borrowers' ability to repay.

Economic risk

- ³⁶⁵. One of the two main analytical components (along with industry risk) that determines our Banking Industry Country Risk Assessments (BICRA), designed to evaluate and compare global banking systems. The economic risk of a banking sector is determined by the structure and stability of the country's economy, along with the central government's macroeconomic policy flexibility, actual or potential imbalances in the economy, and the credit risk of economic participants--mainly households and enterprises.

Eligible portfolio companies and designated assets (BDCs)

366. Private U.S. companies or thinly traded public U.S. companies with a public float (amount of shares with public investors) of less than \$250 million.

Extraordinary external support or intervention

367. External support or interventions are "extraordinary" when they are issuer-specific, related to the issuer's financial stress, and nonrecurrent. Such intervention could be in the form of support to the FI from groups or governments or interference with the FI from groups or governments--for example, to protect such groups' or governments' credit quality--that weaken an issuer. See "Stand-Alone Credit Profiles: One Component Of A Rating," Oct. 1, 2010, for more details.

Finance companies

368. Most financial companies in scope are finance companies (fincos). We define fincos as financial institutions that are typically not registered as banks and that make loans to individuals or businesses. They typically fund their investment and lending activities from the sale of securities or bank borrowings. They primarily lend to consumers, businesses, and the commercial real estate sector. Fincos are neither special purpose vehicles (SPVs) nor investment funds.

Financial market infrastructure companies (FMIs)

369. Principally exchanges, clearinghouses, central security depositories (CSDs), and payment networks that process and clear credit or debit card transactions and cash payments.

Gross stable funding needs (securities firms)

370. The sum of customer loans, short-term reverse repurchase agreements and securities borrowing with customers maturing in less than one year net of haircut, long-term interbank loans receivable and reverse repurchase agreements and securities borrowing maturing in one year or more, securities holdings net of haircut, restricted cash (excluding amounts segregated for customers), receivables from customers, brokers and clearing organizations net of haircuts, all other non-insurance company-related or otherwise excluded assets, and off-balance-sheet credit equivalents net of haircut. We apply this definition unless an FI's available financial reporting includes maturities of exactly one year in the same category as maturities of less than one year. When this occurs, we may classify maturities of exactly one year in the "less than one year" category for that FI.

Gross stable funding ratio (securities firms)

371. GSFR is available stable funding to gross stable funding needs.

Industry risk

372. One of the two main analytical components (along with economic risk) that determines our Banking Industry Country Risk Assessments (BICRA), designed to evaluate and compare global banking systems. Industry risk is determined by the quality and effectiveness of bank regulation

and the track record of authorities in reducing vulnerability to financial crises, the competitive environment of a country's banking industry--including the industry's risk appetite, structure, and performance--and possible distortions in the market. Industry risk also addresses the range and stability of funding options available to banks, including the role of the central bank and government.

Investment banking

373. Investment banking activities are debt and equity underwriting, mergers and acquisitions advisory, sales and trading, principal investment, and proprietary trading.

Leverage ratio (fincos and BDCs)

374. Debt to adjusted total equity.

Leverage ratio (securities firms)

375. Measures simple balance sheet equity leverage. It is calculated one of two ways based on the accounting regime's use of netting for reported balance sheet derivatives. For firms that report derivative positions net by counterparty (as under U.S. generally accepted accounting principles [GAAP]), it is calculated as adjusted common equity divided by adjusted assets. For firms that report balance sheet derivatives on a gross basis (as under International Financial Reporting Standards [IFRS] accounting), it is calculated as adjusted common equity divided by adjusted assets minus 90% of derivatives receivables.

Liquidity coverage metric (securities firms)

376. A ratio of balance sheet liquidity sources divided by balance sheet liquidity needs, used when assessing securities firms. Balance sheet liquidity sources are broad liquid assets, excluding segregated assets plus available committed unsecured lines net of haircut. Balance sheet liquidity needs are short-term wholesale funding plus payables to customers, brokers, and clearing organizations net of haircut, and off-balance-sheet commitments net of haircut.

Liquidity coverage metric (fincos)

377. The ratio of broad liquid assets plus available committed unsecured lines to short-term wholesale funding.

Net interest margin (NIM)

378. Net interest income divided by average interest earning assets on an annualized basis.

Nonbank financial institutions (NBFIs)

379. For the purposes of these criteria, nonbank financial institutions include entities such as securities firms, finance companies, and business development companies when we consider that their greatest risks relate to asset quality, funding and liquidity, and tangible capital. They do not include entities such as asset managers or financial services finance companies where the

balance sheet risks are more corporate-like. They also do not include FMI, although FMI are in scope of the ALAC and RCR sections of this article.

Non-deal-dependent income (BDCs)

- ³⁸⁰. Earnings before interest (excluding payment-in-kind interest), taxes, depreciation, amortization, and stock-based compensation, and excluding all realized and unrealized gains and losses, as well as related incentive fees accrued or paid on the realized and unrealized gains and losses, when disclosed.

Payment-in-kind (PIK) interest (BDCs)

- ³⁸¹. All PIK interest income, including PIK interest accrued in the current period and PIK interest collected in cash that was accrued in previous years, since we consider that neither is a reliable source of income.

Priority debt

- ³⁸². Debt that is more senior to the issue being considered (i.e., senior secured debt has a priority claim ahead of senior unsecured debt, as does first-lien debt versus second-lien debt).

Prudentially regulated

- ³⁸³. A prudentially regulated entity (or group) is subject to regulation that includes the adequacy of its capitalization.

Realized return on average portfolio investments (BDCs)

- ³⁸⁴. Net income minus unrealized gains and losses divided by average portfolio investments. We also deduct accrued incentive fees on unrealized gains and losses from expenses, when disclosed.

Return on average assets (ROAA)

- ³⁸⁵. Net income divided by average total assets.

Revenue stability

- ³⁸⁶. An assessment of the volatility and predictability of overall revenues and its components.

Risk-adjusted capital (RAC) ratio

- ³⁸⁷. Total adjusted capital divided by total S&P Global risk-weighted assets.

Securities firms (or brokers)

- ³⁸⁸. Retail- and wholesale-focused independent broker-dealers that typically do not have banks in their organizational hierarchies, or, if they do, the bank is not the main factor in the business

profile. They may benefit from prudential bank regulation, but lending is not the driver of their business. Financial institutions with material securities operations that benefit from prudential bank regulation, but where lending or other non-brokerage activities are the drivers of the business, or that are global, large, and complex, we typically treat as banks.

Short-term wholesale funding

389. The sum of short-term interbank and debt market funding maturing within one year, repurchase agreements and securities lending, acceptances, and nonderivative trading liabilities.

Stable funding needs (SFN)

390. Includes customer loans, a proportion of short-term reverse repurchase agreements with nonbanks, interbank loans and all reverse repurchase agreements with banks and nonbanks maturing in one year or more, potentially more risky and/or less liquid securities holdings depending on their asset type, restricted cash, all other nonderivative assets, and a proportion of off-balance-sheet credit equivalents. We apply this definition unless an FI's available financial reporting includes maturities of exactly one year in the same category as maturities of less than one year. When this occurs, we may classify maturities of exactly one year in the "less than one year" category for that FI.

Stable funding ratio (banks and fincos)

391. SFR is available stable funding sources relative to stable funding needs.

Stand-alone credit profile (SACP)

392. An SACP is our opinion of an issue's or issuer's creditworthiness, in the absence of extraordinary intervention from its parent or affiliate or related government, and is one component of a rating. See "Stand-Alone Credit Profiles: One Component Of A Rating," Oct. 1, 2010, for more details.

Unencumbered assets

393. Assets not pledged to a specific debt obligation, or assets in excess of the amount necessary for repayment of the creditors that rank ahead of the debt being analyzed.

Value at risk (VaR)

394. A measurement of the potential loss in value of all or a subset of the trading book over a defined period for a given confidence interval.

SECTION 8: APPENDIX

This section 8 appendix describes the additional considerations for assigning ratings to foreign branches and their financial obligations, as well as metrics definitions.

Additional Considerations For Assigning Ratings To Foreign Branches And Their Financial Obligations

Determining the local currency of a foreign branch

395. Because a foreign branch is resident in the host country, its local currency is the same as that of the host country. For example: If a French bank has a branch in Switzerland, then the branch's local currency is the Swiss franc, even if it uses the euro as its operating currency.
396. The local currency of a foreign branch will be different from the local currency of the parent bank, unless the home and host countries have the same currency.
397. This applies even if the home country is a dollarized economy, such as Panama. U.S. dollar bonds issued by a Panamanian bank are assigned foreign currency ratings, as are U.S. dollar bonds issued by a non-U.S. branch of a Panamanian bank. Similarly, if a branch based in a dollarized economy (for example, a Panamanian branch of a foreign bank) were to issue a U.S. dollar-denominated bond, we would assign the bond a foreign currency rating.
398. We take the same approach for nonbank issuers in Panama, such as the government or corporate issuers. The risks associated with the home country's dollarized economy are thus reflected in the home country sovereign rating, the home country BICRA, and our rating on the bank.

Local and foreign currency issue credit ratings on branch bonds

399. The issue credit rating assigned to a branch-issued bond is capped by the ICR on the branch. We do not assign different foreign and local currency ICRs to banks or bank branches, except in some limited cases such as where the bank is a government-related entity.
400. We list the issue credit rating on a branch bond as being either a local currency or foreign currency rating, depending on whether it is issued in the local currency of the host country or not. The local currency of the foreign branch is the local currency of its host country.
401. We take this approach even when a branch carries out limited activities in the host country, such as only acting as a funding vehicle. The branch, as a legal entity in the host country, is subject to potential government intervention. The nature of government intervention in the banking sector can differ, depending on whether bank liabilities are denominated in the local or foreign currency. Under our approach, all ratings on bonds issued by entities in the host country are consistently designated as either local or foreign currency.
402. Table 26 provides examples of when a bank branch based in a different country is rated below the parent bank. The bond rating is capped at the branch ICR, even when we have assigned a higher local currency sovereign rating to the host country.

Table 26

Bank Branches Based In Host Countries Rated Below The Parent Bank

Risk assessments	Case 1	Case 2	Case 3
Bank ICR	BBB	BBB	BBB
Home country	U.S.	U.S.	U.S.
Issuing branch's host sovereign long-term rating	Foreign currency: B+ and local currency: BB-	Foreign currency: B+ and local currency: BB-	Foreign currency: B+ and local currency: BB-
Branch ICR	BB	BB	BB
Issuing currency	U.S. dollar	Host country currency	Euro
Nature of risk	Foreign currency	Local currency	Foreign currency
Issue rating	BB	BB	BB

Note: Rating levels are for illustrative purposes. The bank is not an EU bank. In each case, the expected support is considered consistent with a branch ICR two notches above the host sovereign foreign currency rating. In these cases, we assume that a default or government intervention is not imminent. ICR--Issuer credit rating.

403. Our base case is likely to include an assumption of government intervention that will differentiate by currency only if the branch ICR were in the 'CCC' category or below. Indeed, we are likely to have sufficient visibility to make this assumption only at this rating level. At such a rating level, we may have a clearer expectation about whether the host country authorities would not allow local banks (and resident branches) to pay foreign currency liabilities but would allow them to pay local currency liabilities. In that situation, a default on a foreign currency obligation would not automatically lead to a default on local currency obligations.
404. In such a case, a domestic currency bond could be rated higher than a foreign currency bond (and above the branch ICR) if we were clear that failure to pay on the foreign currency bond would not lead to an event of default and the acceleration of covenants and clauses on other liabilities. In our 'CCC' criteria, we give more details on assigning ratings in those categories.

How the parent bank ICR and the home country sovereign rating affect foreign branch ratings

405. The ICR on a branch is always capped by the ICR on the parent bank. Thus, where the ICR on a parent bank is constrained by the sovereign rating on the home country, that constraint will carry across to the branch. A bank domiciled in a country with a local currency rating of 'BBB+' and a foreign currency rating of 'BBB' will typically have its rating capped at 'BBB'. Even if it has a branch based in a country rated above 'BBB', for example, a country rated 'AA', the branch rating will be capped at 'BBB'.
406. The ICR on the parent bank will also incorporate the risk associated with the currency mix of the bank's funding. If a bank raises funding in a foreign currency, particularly when it has limited assets in that currency, this could constrain our assessment of its funding and, thus, could affect the SACP and ICR.
407. Our bank ratings consider the risk that the government in a jurisdiction where a bank is domiciled could impose restrictions preventing the bank from paying its foreign currency liabilities. For example, our rating on a Turkey-based parent bank will incorporate the risk that the Turkish authorities could stop or restrict payments on non-Turkish lira obligations.
408. In this case, the rating on any foreign branch obligations not denominated in lira would automatically be constrained. This even affects branch-issued bonds denominated in the local

currency of the host country.

409. In rating the parent bank, we incorporate the risk that the bank might not be able to access enough foreign currency to pay its foreign currency liabilities, even when no formal restrictions exist. For example, if an Argentine bank has a branch in the U.S. that raises funding in U.S. dollars but does not carry out any other business activities in the U.S., our rating on the Argentine bank will incorporate the risk that it will not be able to access enough U.S. dollars to service the branch obligation. The ICR on the parent bank will then constrain the rating that can be assigned to the branch.
410. In the following examples, the host country branch of Bank Z has a local currency bond rating capped at the 'B-' ICR level of Bank Z, even though it is denominated in the host country currency and the host country has a local currency sovereign rating of 'BB-'.

Table 27

Examples Related To Host Country Branches

Risk assessments	Case 4	Case 5	Case 6
Bank name (ICR)	Bank Y (B+)	Bank Y (B+)	Bank Z (B-)
Home country rating	Foreign currency: B+ and local currency: BB-	Foreign currency: B+ and local currency: BB-	Foreign currency: B- and local currency: B
Long-term ratings on the issuing branch's host country	Foreign currency: B+ and local currency: BB-	Foreign currency: B+ and local currency: BB-	Foreign currency: B+ and local currency: BB-
Branch ICR	B+	B+	B-
Issuing currency of Host Country branch bond	Home country currency	Host country currency	Host country currency
Nature of risk	Foreign currency	Local currency	Local currency
Issue rating	B+	B+	B-

Note: Rating levels are for illustrative purposes. ICR--Issuer credit rating.

Rating debt co-issued by two bank branches

411. Here we address how we rate debt co-issued by two bank branches, in different jurisdictions, neither of which is in the jurisdiction of the parent bank. If two branches are, in effect, dual obligors with respect to the issue, we rate the issue at the higher of the two branch ratings, taking into account the general provisions of the bank branch criteria. The second branch would have to commit to timely payment of the obligation when the primary branch cannot make required payments, even if the commitment is conditional in some other respect. The second branch's commitment should include timely payment even if the primary obligor has suffered a negative sovereign intervention. We expect the roles of both branches to be disclosed to bondholders.
412. Under this arrangement, we would lower the rating on the issue to 'D' if neither of the obligated branches could ensure timely and full payment in line with the terms and conditions of the issue. The ICR on the bank itself would be lowered to 'SD', unless the nonpayment stemmed from government intervention by both of the host countries that made it impossible for the obligor branches to legally pay on the instrument. In such a case, we would lower our ICRs on the obligor branches to 'SD', but not the ICR on the bank itself.

Foreign and local currency ratings on obligations that have more than one branch as an unconditional obligor

413. Having more than one branch as an obligor carries advantages. In the event of stress arising in one of the host jurisdictions but not in another, the investor is protected from the risk on intervention by an individual host government if payment can be made from another host country.
414. In some cases, only one branch is the clear obligor. While other branches may be involved, they might not take on the obligation in the event of a sovereign stress, or would not be able to ensure timely payment. In such a situation, we would rate the bond as though it were an obligation of one branch only.
415. The issue credit rating on a co-issued bond is capped at the level of the highest ICR on the obligor branches. Branch ratings are capped by the ICR on the parent bank, but may be rated below the parent. Therefore, the branch that constrains the rating on the bond could change over the life of the instrument.
416. A bond issued in the local currency of one of the unconditional obligor branches is assigned a local currency rating. It is assigned a foreign currency rating if it is denominated in any other currency.
417. Thus, if one of the obligor branches is in the home country, then a bond denominated in the home country's local currency will have a local currency rating. It will have a foreign currency rating if it is not denominated in either the home country's currency or that of another obligor branch.
418. For example, if an Indian bank has a branch in Delhi and that branch is an unconditional obligor of a bond denominated in rupees, the bond will have a local currency rating. If the bank has a Paris branch that is also an obligor, the bond could be euro-denominated instead and would still have a local currency rating. We would assign it a foreign currency rating if denominated in another currency.
419. In some cases, the issue rating on the bond will differ from the rating on some of the obligor branches because it is based on the highest of the ICRs on the obligor branches. The ICR on the parent bank caps all branch ratings.
420. For example, if a bond is an unconditional obligation of more than one foreign branch of an Indian bank, but none of these branches are in India, then the bond is assigned a local currency rating only if it is denominated in the local currency of one of the host countries. Thus, a bond issued by the Bahrain and Hong Kong branches of an Indian bank would have a local currency rating if denominated in Bahraini dinar or Hong Kong dollars. If it is denominated in a currency that is not the local currency of any of the obligor branches, then we assign it a foreign currency rating.
421. The issue credit rating is capped at the level of the highest ICR of the obligor branches, which in turn is capped by the ICR of the parent bank. However the ICRs on the Hong Kong and Bahrain branches can differ because we assign them based on the branch criteria and would reflect any differences in the relevant sovereign rating benchmark levels.

Agencies

422. In some jurisdictions, a bank's operation might not be formally labelled a branch but, in substance, be considered a branch of the parent bank for the purposes of these criteria--when it's part of the same legal entity as the parent bank. For example, under New York regulation, a foreign agency is an agency of a foreign bank that is part of the same legal entity as the parent, is licensed to conduct banking business in New York, and has many of the same powers and capacity to enter financial contracts as a foreign bank branch, except in the case of deposits.

Metrics Definitions

423. We use financial statements, including footnotes, other financial and reporting disclosures, regulatory filings, and information that FIs may provide to S&P Global Ratings. When no specific firm-reported figures are available, we use estimates. We typically consider operating and finance lease liabilities to be part of an FI's debt.
424. As a general principle, we base our analysis on consolidated financial statements prepared under accounting regimes used for general reporting purposes, such as U.S. GAAP and IFRS.
425. In some instances, our analysis uses financial statements and information prepared for regulatory purposes because this information provided is more granular than that provided under U.S. GAAP or IFRS. In addition, the information provided on a regulatory basis (such as Y9-C and related schedules in the U.S.) can often be more comparable across banks because it has a standardized reporting format.

Table 28

Metrics

Metric name	Metric description
Earnings	
1. Core earnings	Net income (before noncontrolling interest) (-) nonrecurring/special income (+) nonrecurring/special expense (+) goodwill and M&A-related intangibles impairment or amortization (+) allocation to funds for general banking risk (-) distributions due on all equity hybrid instruments accounted for as equity (+/-) other adjustments (+/-) tax impact of all adjustments above
2. Total revenue(s)	All revenues net of interest expense and nonrecurring income
3. Fees and commissions	Fees and commission income earned, net of commissions paid where those commissions are closely related to commissions earned
4. Other market-sensitive income	Income from appreciation of financial assets sold, such as gains or losses on private equity holdings, realized gains or losses on nontrading securities, gains or losses on loan sales, or securitizations that are from ongoing business lines. Other gains on sale of fixed assets or business lines are categorized as nonrecurring income.
5. Cost-income ratio	Salaries and general administrative expenses before any nonrecurring expenses, divided by total revenue(s)
6. Net operating income before loan loss provisions/assets	Revenues net of all expenses except provisions, before any nonrecurring gains/losses, divided by average assets
7. Core earnings/assets	Core earnings divided by average assets
8. Other revenues/total revenues	Revenues other than net interest income, fees and commissions, trading gains and other market-sensitive income, divided by total revenue(s)
Funding	
9. Loan-to-deposit ratio (%)	Customer loans (net), divided by customer deposits
Customer loans (net)	Customer loans (gross) net of loan loss reserves and net of reverse repurchase agreements and net of securities borrowing
Customer deposits	Customer deposits net of repurchase agreements and net of securities lending
10. Long-term funding ratio (%)	Available stable funding divided by the sum of the funding base and total equity net of intangibles
Available stable funding	The sum of total equity net of intangibles, customer deposits, and long-term interbank and debt market funding including hybrid instruments with no equity content maturing in one year or more\$

Table 28

Metrics (cont.)

Metric name	Metric description
Funding base	The sum of customer deposits, interbank and debt market funding including hybrid instruments with no equity content, repurchase agreements and securities lending, and nonderivative trading liabilities and acceptances
Total equity	The sum of common shareholders' equity, minority interest-equity, and hybrid instruments with high or intermediate equity content
11. Short-term wholesale funding/funding base (%)	Short-term wholesale funding divided by funding base
Short-term wholesale funding	The sum of short-term interbank and debt market funding maturing in less than one year\$, repurchase agreements and securities lending, acceptances, and nonderivative trading liabilities
12. Stable funding ratio (%)	Available stable funding (as defined in No. 10) divided by stable funding needs
Stable funding needs	The sum of customer loans (net), short-term reverse repurchase agreements and securities borrowing with nonbanks maturing in less than one year\$ net of haircut*, long-term interbank loans and reverse repurchase agreements and securities borrowing maturing in one year or more\$, securities holdings net of haircut*, restricted cash (see table 29), all other assets net of haircut*, and off-balance sheet credit equivalents net of haircut*
Liquidity	
13. Broad liquid assets to short-term wholesale funding (%)	Broad liquid assets divided by short-term wholesale funding (as defined in metric No. 11)
Broad liquid assets	The sum of: cash, short-term interbank loans and reverse repurchase agreements and securities borrowing with banks maturing in less than one year\$, short-term reverse repurchase agreements and securities borrowing with nonbanks net of haircut* maturing in less than one year\$, and securities holdings net of haircut* less restricted cash (see table 29)
14. Net broad liquid assets/short-term customer deposits (%)	Broad liquid assets less short-term wholesale funding, divided by short-term customer deposits net of repurchase agreements and net of securities lending maturing in less than one year\$
15. Short-term wholesale funding/total wholesale funding (%)	Short-term wholesale funding (as defined in ratio No. 11) divided by the difference between the funding base and customer deposits
16. Liquid assets to wholesale funding (%)	Broad liquid assets divided by total wholesale funding

*For haircuts, see table 29. \$We apply this definition unless the available financial reporting for maturities of exactly one year differs from the definition in this table for an FI. When this occurs, we may classify maturities of exactly one year in the relevant "less than one year" category for that FI. M&A--Mergers and acquisitions.

Table 29

Assumptions To Compute Stable Funding Ratios And Broad Liquid Assets To Short-Term Wholesale Funding Ratios For Banks And Fincos (Including BDCs)

	Proportion that requires stable funding (%)
Stable funding needs	
Loans to banks (net) maturing in less than one year±	0
Loans to banks (net) maturing in one year or more±	100
Customer loans (net) (all maturities)	100

Table 29

Assumptions To Compute Stable Funding Ratios And Broad Liquid Assets To Short-Term Wholesale Funding Ratios For Banks And Fincos (Including BDCs) (cont.)

Reverse repurchase agreements (and securities borrowing) with banks maturing in less than one year±	0
Reverse repurchase agreements (and securities borrowing) with banks maturing in one year or more±	100
Reverse repurchase agreements (and securities borrowing) with nonbanks maturing in one year or more±	100
Reverse repurchase agreements (and securities borrowing) with nonbanks maturing in less than one year±	50
Illiquid portion of securities owned (unencumbered and encumbered):	
Home sovereign and government agencies	0
Subsovereign	0
Certificates of deposit or commercial paper	0
Foreign government	0
Government-sponsored MBS, policy banks	0
Covered bonds excluding own covered bonds	0
Bank debt	50
Corporate debt	50
MBS other and mutual funds	50
Other debt securities	50
Equities and gold	50
Loans	100
ABS (other than MBS such as CDO, CLO, CMBS)	100
Commodities (exclude gold if disclosed)	100
Other (for example, equity stakes; not listed equities)	100
Cash	0
Restricted cash = % of customer deposits depending on geographic region*	1-5
Derivative assets	0
Insurance assets	0
Intangibles	0
All other assets	100
Off-balance-sheet commitments, guarantees, letters of credit	5
Proportion considered stable funding (%)	
Available stable funding	
Customer deposits (all maturities)	100
Deposits due to banks maturing in less than one year±	0
Deposits due to banks maturing in one year or more±	100
Repurchase agreements (and securities lending) (all maturities)§	0

Table 29

Assumptions To Compute Stable Funding Ratios And Broad Liquid Assets To Short-Term Wholesale Funding Ratios For Banks And Fincos (Including BDCs) (cont.)

Debt issued maturing in one year or more±	100
Derivative liabilities	0
Nonderivative trading liabilities (for example, short positions)	0
Total equity net of intangibles	100
Proportion considered liquid (%)	
Broad liquid assets	
Cash	100
Loans to banks (net) maturing in less than one year±	100
Reverse repurchase agreements (and securities borrowing) with banks maturing in less than one year±	100
Reverse repurchase agreements (and securities borrowing) with nonbanks maturing in less than one year±	50
Securities owned net of illiquid portion of securities owned (unencumbered and encumbered)	100
Derivative assets	0
Net of restricted cash = % of customer deposits depending on geographic region*	1-5
Proportion considered to pose liquidity risk (%)	
Short-term wholesale funding	
Deposits due to banks maturing in less than one year±	100
Deposits due to banks maturing in one year or more±	0
Debt issued maturing in less than one year±	100
Repurchase agreements (and securities lending) (all maturities)	100
Derivative liabilities	0
Acceptances	100
Nonderivative trading liabilities (for example, short positions)	100

*The proportion of customer deposits considered restricted cash that requires stable funding is: 1% if no regulatory minimum exists; and if one exists, the regulatory one, floored at 1% and capped at 5%. §Certain repurchase agreements greater than a year, where substantial loss of access is considered unlikely, such as some credit facilities used to finance commercial real estate loans, may be considered as a long-term borrowing and included as a source of stable funding. ±We apply this definition unless the available financial reporting for maturities of exactly one year differs from the definition in this table for an FI. When this occurs, we may classify maturities of exactly one year in the relevant "less than one year" category for that FI.

Table 30

Other Funding Metrics

Amount included in other funding metrics (%)	
Total wholesale funding	
Deposits due to banks (all maturities)	100
Debt issued (all maturities)	100
Repurchase agreements (and securities lending) (all maturities)*	100

Table 30

Other Funding Metrics (cont.)

	Amount included in other funding metrics (%)
Acceptances	100
Nonderivative trading liabilities (for example, short positions)	100
Hybrid capital instruments	100
Funding base	
Total wholesale funding net of hybrid capital instruments	100
Customer deposits (all maturities)	100

*Certain repurchase agreements greater than a year, where substantial loss of access is considered unlikely, such as some credit facilities used to finance commercial real estate loans, may be considered a long-term borrowing and included as a source of stable funding.

Table 31

Assumptions For Securities Firms--Gross Stable Funding Ratio

(B) Available stable funding/(A) gross stable funding needs

Line item	Proportion that requires stable funding (%)
A. Gross stable funding needs = total of:	
Unrestricted cash	0
Reverse repo with financial institutions maturing in less than one year*	0
Reverse repo with financial institutions maturing in one year or more*	100
Reverse repo with customers maturing in one year or more*	100
Reverse repo with customers maturing in less than one year*	50
Receivables from brokers and clearing organizations	10
Receivables from brokerage customers (including margin loans)	10
Loans to banks maturing in less than one year*	0
Loans to banks maturing in one year or more*	100
Customer loans (net) - all maturities (other than margin loans)	100
Derivative assets	0
Insurance assets and excluded consolidated variable interest entities	0
Intangibles	0
All "other assets" (fixed, illiquid assets, like property plant and equipment, etc.)	100
Off-balance-sheet commitments, guarantees, letters of credit	5
Illiquid portion of securities owned (unencumbered and encumbered):	
Home sovereign and government agency debt	0
Subsovereign government	0
Certificate of deposit/commercial paper	0
Foreign government	0
Government-sponsored mortgage-backed securities (MBS), policy banks	0
Covered bonds, excluding own covered bonds	0

Table 31

Assumptions For Securities Firms--Gross Stable Funding Ratio (cont.)

Bank debt	50
Corporate debt	50
MBS other and mutual funds	50
Other debt securities	50
Equities and gold	50
Loans	100
Asset-backed securities (other than MBS)	100
Commodities (exclude gold if disclosed)	100
Other (e.g., not listed equities)	100
Proportion considered stable funding (%)	
B. Available stable funding = total of:	
Customer deposits - all maturities	100
Deposits of other banks maturing in less than one year*	0
Deposits of other banks maturing in one year or more*	100
Payables to brokers/dealers and clearing organizations	0
Brokerage clients payable	0
Repurchase agreements - all maturities	0
Nonderivative trading liabilities (e.g., short positions)	0
Derivative liabilities	0
Debt, hybrids, and minority interest, with puts or maturing in less than one year*	0
Debt issued maturing in one year or more*	100
Total equity net of intangibles	100

Note: Where material, we typically include securities or cash collateral posted as margin to CCPs and other trade counterparties (excluding the amount related to securities financing and repo transactions) in "Receivable from brokers and clearing organizations." *We apply this definition unless the available financial reporting for maturities of exactly one year differs from the definition in this table for an FI. When this occurs, we may classify maturities of exactly one year in the relevant "less than one year" category for that FI.

Table 32

Assumptions For Securities Firms--Liquidity Coverage Metric

(C) Available liquidity/(D) balance sheet liquidity needs	Proportion considered liquid (%)
C: Available liquidity = total of:	
Unrestricted cash	100
Loans to banks (net) maturing in less than one year*	100
Reverse repo with financial institutions maturing in less than one year*	100
Reverse repo with customers maturing in less than one year*	50
Accessible capacity of committed credit lines maturing in one year or more*	75
Liquid portion of securities owned (unencumbered and encumbered):	
Home sovereign and government agencies	100

Table 32

Assumptions For Securities Firms--Liquidity Coverage Metric (cont.)

Subsovereign government	100
Certificate of deposit/commercial paper	100
Foreign government	100
Government-sponsored mortgage-backed securities (MBS), policy banks' debt	100
Covered bonds, excluding own covered bonds	100
Bank debt	50
Corporate debt	50
MBS other and mutual funds	50
Other debt securities	50
Equities and gold	50
Loans	0
Asset-backed securities (other than MBS)	0
Commodities (excluding gold if disclosed)	0
Other (e.g., equity stakes; not listed equities)	0
Proportion posing liquidity risk (%)	
D. Balance sheet liquidity needs = total of:	
Customer deposits - all maturities	0
Other banks' deposits maturing in less than one year*	100
Other banks' deposits maturing in one year or more*	0
Payables to brokers/dealers and clearing organizations	5
Brokerage clients payable	5
Short-term debt and debt maturing in less than one year*	100
Repurchase agreements - all maturities	100
Acceptances	100
Nonderivative trading liabilities (e.g., short positions)	100
Derivative liabilities	0
Debt and other capital with puts or maturing in less than one year*	100
Off-balance-sheet commitments, guarantees, and letters of credit	5

Note: Where material, we typically exclude securities and cash collateral posted as margin to CCPs and other trade counterparties (apart from that related to securities financing and repo transactions) from "Liquid portion of securities owned (unencumbered and encumbered)" and "Unrestricted cash." *We apply this definition unless the available financial reporting for maturities of exactly one year differs from the definition in this table for an FI. When this occurs, we may classify maturities of exactly one year in the relevant "less than one year" category for that FI.

SECTION 9: INFORMATION RELATED TO THE PUBLICATION OF THE CRITERIA

Section 9 discusses the changes from the previous criteria and the impact on outstanding ratings.

CHANGES FROM PREVIOUS CRITERIA

426. The criteria generally maintain the fundamental concepts of the existing analytical framework and include several updates. The criteria update does not involve a recalibration of our ratings approach. Most of the changes relate to enhancing consistency of format and terminology, including the use of subfactors and caps, given the consolidation of content previously contained in eleven criteria articles into this single article. We have also clarified the use of peer comparisons. The key analytical changes are:

- We introduced a potential one-notch adjustment at the SACP for banks.
- The criteria incorporate an increased ability to make a qualitative adjustment to the capital and earnings score, as well as clarify the role of the assessment of regulatory capital.
- For certain securities firms, we clarified the role of cash flow leverage in our capital and earnings assessment.
- We made some adjustments to ALAC calculations, including the removal of the "excess TAC" amount from ALAC and associated changes to the thresholds.
- The criteria identify when we may decide not to rate an NBF's senior unsecured debt two notches below the ICR due to the level of priority debt and unencumbered assets.
- A foreign branch of a bank can be rated at the same level as that of a core subsidiary in the same country.
- The FI government support tables (21, 22, and 23) can be applied even when the entity is a GRE, given that these tables reflect potential extraordinary government support due to systemic importance (which is not the focus of our GRE assessment).
- Other than funding and liquidity (for which there is a combined impact), for all SACP factors we take a more granular approach to determining the negative impact that the two lowest assessments have on the SACP. (These were called weak and very weak in the previous criteria, but we have changed the names to constrained and weak, respectively.) This is -2 or -3 notches for a constrained assessment and -4 or -5 notches for a weak assessment. (The capital and earnings impact continues to vary by anchor.)
- We assess each of funding and liquidity on a four-point scale but do not cap the SACP based on the funding and liquidity assessment. We also eliminated the base-case and stress case cash flow forecasts that were done for fincos and BDCs.
- We aligned our approach to setting the anchor for banks that we previously referred to as stand-alone investment banks with the approach for other banks. Also, risk position can now be assessed as better than moderate for banks even if trading activities are material.
- We extended the scope of the ALAC approach to include FMIs given that some FMIs may become subject to effective resolution regimes that involve the bail-in of loss-absorbing capacity instruments.

- We removed specific backup coverage requirements for commercial paper programs because we assess how such programs are managed within our liquidity assessment.

IMPACT ON OUTSTANDING RATINGS

427. We expect a limited impact on ratings because this criteria article is an update that retains the fundamental concepts of the prior analytical framework. We believe that, based on our testing and assuming entities maintain their current credit characteristics, no more than 5%-10% of ICRs within the scope of these criteria will potentially be affected, with the majority of these due to changes in our approach to ALAC. We do not expect any rating changes because of BICRA scores. We expect very few, if any, rating changes of more than one notch, and the one-notch changes to be more upgrades than downgrades. Most FIs and banks do not have RCRs, but if we change our ICR on a bank and the bank has an RCR, then it is likely that we will change the RCR in the same way.
428. We also expect that issue credit ratings on hybrid instruments issued by up to six banking groups (representing about 3% of FI hybrid issue credit ratings) may change because of changes in SACPs due to the proposal to factor in a CRA adjustment at the SACP level. We expect the potential impact on these issue credit ratings will be a one-notch change. In addition, based on our testing and assuming that entities maintain their current credit characteristics, less than 5% of SACPs could be affected by the proposals. We expect the majority of these SACP changes will be by one notch. Hybrid ratings on these issuers will likely be affected by the changes in the SACPs. Again, we expect that the majority of rating changes will be one notch.

REVISIONS AND UPDATES

This article was originally published on Dec. 9, 2021.

Changes introduced after original publication:

- On March 31, 2022, we republished this criteria article to make nonmaterial changes by adding "Sector And Industry Variables: Banking Industry Country Risk Assessment Update: March 2022" in Related Publications.

RELATED PUBLICATIONS

Fully Superseded Criteria

- Methodology For Assigning Financial Institution Resolution Counterparty Ratings, April 19, 2018
- Bank Rating Methodology And Assumptions: Additional Loss-Absorbing Capacity, April 27, 2015
- Nonbank Financial Institutions Rating Methodology, Dec. 9, 2014
- Key Credit Factors For U.S. Business Development Companies, Dec. 9, 2014
- Assessing Bank Branch Creditworthiness, Oct. 14, 2013
- Quantitative Metrics For Rating Banks Globally: Methodology And Assumptions, July 17, 2013

Criteria Financial Institutions General: Financial Institutions Rating Methodology

- Banks: Rating Methodology And Assumptions, Nov. 9, 2011
- Methodology For Analyzing Funding And Liquidity Positions Of Bank-Licensed Investment Companies, July 2, 2010
- Commercial Paper I: Banks, March 23, 2004
- Commercial Paper II: Finance Companies, March 22, 2004

Partly Superseded Criteria

- Hybrid Capital: Methodology And Assumptions, July 1, 2019
- Issue Credit Rating Methodology For Nonbank Financial Services Companies, Dec. 9, 2014

Fully Superseded Guidance

- Guidance: Assessing Bank Branch Creditworthiness, March 18, 2019
- Guidance: Methodology For Assigning Financial Institution Resolution Counterparty Ratings, April 19, 2018
- Guidance: Nonbank Financial Institutions Rating Methodology, March 22, 2018

Related Criteria

- Banking Industry Country Risk Assessment Methodology And Assumptions, Dec. 9, 2021
- Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021
- Group Rating Methodology, July 1, 2019
- Risk-Adjusted Capital Framework Methodology, July 20, 2017
- Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- Guarantee Criteria, Oct. 21, 2016
- Rating Government-Related Entities: Methodology And Assumptions, March 25, 2015
- Covered Bonds Criteria, Dec. 9, 2014
- Ratings Above The Sovereign--Corporate And Government Ratings: Methodology And Assumptions, Nov. 19, 2013
- Methodology And Assumptions For Market Value Securities, Sept. 17, 2013
- Criteria For Assigning 'CCC+', 'CCC', 'CCC-', And 'CC' Ratings, Oct. 1, 2012
- Principles Of Credit Ratings, Feb. 16, 2011
- Stand-Alone Credit Profiles: One Component Of A Rating, Oct. 1, 2010

Related Sector And Industry Variables Reports

- Sector And Industry Variables: Banking Industry Country Risk Assessment Update: March 2022, March 31, 2022

Related Research

- RFC Process Summary: Financial Institutions Rating Methodology, Dec. 9, 2021
- S&P Global Ratings Definitions, Nov. 10, 2021
- Credit FAQ: Applying "Criteria For Assigning 'CCC+', 'CCC', 'CCC-', And 'CC' Ratings" To Subordinated And Hybrid Capital Instruments, July 16, 2014

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