

RATING METHODOLOGY

FINANCIAL INSTRUMENTS

Alpha Credit Rating Limited

This methodology describes the framework within which Alpha Credit Rating Limited (ACRL) assigns credit rating to financial instruments issued by institutes. We define institutes that are permitted by BSEC to issue such instruments.

ACRL Rating Perspective

In the context of the two-dimensional rating system, if the rating is to be assigned to a securities issue the transaction structure should be taken into account as it can impact the likelihood of preferential recoveries for the transaction being rated relative to other obligations outstanding (or which may become outstanding in the future) and thus affect the loss given default (“LGD”). The Transaction Dimension Score is converted into a Transaction Dimension Impact Score, which may either be added to or subtracted from the Borrower Dimension Score (associated with the borrower’s senior unsecured rating, which we may call its “natural” or “stand alone” rating). The sum of the Borrower Dimension Score and Transaction Dimension Impact Score is defined as the Composite Rating Score, which is associated with one of the long term Categories. The Transaction Dimension rating methodology profile elements are Priority, Security, and Covenants.

Framework:

- the rating on the issuer or bank group or a credit assessment of the collective owners of the issuer,
- The treatment of all instruments in the creditor hierarchy;
- The national regulatory framework;
- The ability of the issuer’s timely principal and interest payments;

Issuer Rating

Repayment capacity for the instruments is linked to the credit quality of the issuer. This reflects ongoing ability to provide capital and liquidity and managing debts. ACRL’s issuer ratings are forward-looking assessments that incorporate macroeconomic conditions, key risk appetite strategies and management, competitive position, and key earnings and loss performance indicators, as outlined in “RATING METHODOLOGY BANKS AND FINANCIAL INSTITUTIONS” and rating methodologies for respective corporate entities. Together, these qualitative and quantitative analyses result in an indicative credit assessment for the issuer. We complement

these analyses with peer comparisons, temporary or transitional impacts and ownership considerations to provide an issuer rating.

Transaction Risk Factor

The Transaction Risk Factors capture the impact that certain elements of a transaction will have on the risk of the financing as a whole.

3 – Enhances probability of preferential recovery

2 – Neither enhances nor reduces probability of preferential recovery

1 - Reduces probability of preferential recovery

Transaction Risk Factor	Weight	Weighted Score
Priority	30%	from 0.30 to 0.90
Security	50%	from 0.50 to 1.50
Covenants	20%	from 0.20 to 0.60
Total	100%	from 1.00 to 3.00

Each Transaction Risk Factor is thus scored either 3, 2, or 1 and then weighted as indicated above, producing a Transaction Dimension Score of between 1.00 and 3.00. Through a conversion process described below, a Transaction Dimension Score is converted to a Transaction Dimension Impact Score. The Impact Score is added to or subtracted from the Borrower Dimension Score to arrive at the Composite Rating Score and hence the Rating (see below). 7 There is some overlap between borrower and transaction for project financings because the borrower is generally a special-purpose corporation and analysis of both the borrower and transaction dimensions rely on analysis of the transaction structure and documentation rather than an organic borrower with a historical track record.

Priority:

Priority simply means the rank of an obligation in an entity's capital structure. Senior secured debt has priority over senior unsecured debt, which has priority over subordinated debt, which has priority over preferred stock.

Security:

Security can be in the form of specific collateral or a lien on all assets. For an issue secured with specific collateral to be rated above the "nature" or "stand alone". If the security is separated from the estate of the company in the event of bankruptcy and the security will maintain value regardless of the company's fortunes, then the risk of the bond might be minimized.

Covenants:

Covenants are defined broadly as provisions contained in the transaction documents agreed by all parties to the transaction. Some covenants are borrower representations and warranties that provide some comfort that the borrower will not act to cause impairment of the credit quality of the transaction. The inclusion of such covenants is a statement by the borrower that it is willing to operate within certain boundaries, and as such should be viewed positively. Of course, a firm's agreeing to abide by indenture covenants doesn't necessarily mean that it will be able to do so.

Converting Transaction Dimension Score to Transaction Impact Score on Borrowers Dimension

Transaction Dimension Score	Transaction Dimension Impact Score
Between 2.70 and 3.00	Add 3.00 to Borrowers Dimension
Between 2.40 and 2.69	Add 2.00 to Borrowers Dimension
Between 1.60 and 2.39	No Impact
Below 1.60	One notch lower from Borrowers Dimension

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