
Policy Guideline

for Internal Rating of Commercial Customers

(Based on the new PD models)

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Table of Contents

CHAPTER 1: INTRODUCTION.....	4
1. GENERAL DESCRIPTIONS.....	4
1.1 Objectives.....	4
1.2 Scope of the Manual of Risk Rating for commercial Customers	4
1.3 Manual Compliance.....	4
1.4 Related Regulations and Laws.....	4
1.5 Compliance Exception.....	5
1.6 Effective Date.....	5
1.7 Manual Review.....	5
2. DEFINITIONS.....	5
CHAPTER 2: RISK RATING PRINCIPLES.....	7
3. RISK RATING DESCRIPTIONS	7
4. EXCEPTIONS FOR RISK RATING.....	7
5. CUSTOMER SEGMENTATION	8
CHAPTER 3: INTERNAL RATING ASSESSMENT.....	11
6. VARIABLES USED IN INTERNAL RATING ASSESSMENT	11
6.1 Standard Customer Segments.....	11
6.2 Specialized Customer Segments.....	11
7. FINAL RISK RATING ADJUSTMENT.....	12

8. FINANCIAL INSTITUTIONS	13
CHAPTER 4 : INTERNAL RISK RATING LEVELS	14
9. LEVEL OF INTERNAL RISK RATING	14
10 INTERNAL RATING TREATMENT BASED ON PAYMENT STATUS	17
10.1 Normal and Special Mention debtors.....	18
10.2 NPL debtors.....	18
10.3 TDR Customers.....	19
10.4 Ceased Operations.....	19
10.5 Sugarcane customers.....	19
11. CONDUCTING THE COMMERCIAL RISK RATING	19
11.1 Documentation and Recording the Rating.....	20
11.2 Risk Rating review.....	20
Appendix.....	21

Chapter 1: Introduction

The bank has developed internal rating grades with associated probability of default to evaluate potential risks that might occur from transactions with its customers and to support effective credit risk management. This is a new internal rating scale and will run parallel to the existing internal rating scale, for a period of 1 year or till deemed appropriate by the Risk Management Committee and the Board of Directors.

1. General Descriptions

1.1 Objectives

- 1.1.1 To establish internal risk rating criteria applicable to commercial customers
- 1.1.2 To calculate the Probability of Default (PD) for all commercial customers and to evaluate potential risks to which the Bank may expose as a result of entering into transactions with its customers
- 1.1.3 To be used as one of the guidelines while considering the appropriateness of interest rates and fees that are commensurate with the Bank's risk level
- 1.1.4 To support effective credit risk management of the Bank
- 1.1.5 As an input into the stress testing framework for credit risk stress tests

1.2 Scope of the Manual of Risk Rating for Commercial Customers

- 1.2.1 This manual covers internal risk rating criteria for all commercial customers.

1.3 Manual Compliance

- 1.3.1 Officers of the Bank who are responsible for assigning internal risk rating for commercial customers must comply with this policy.

1.4 Related Regulations and Laws

- 1.4.1 The Bank's Credit Risk Management Policy
- 1.4.2 The Bank's Credit Risk Management Manual

1.4.3 BOT's Credit Risk Guideline – Sor Gor Sor. (03) Wor. 227/2548 Dated 4 February 2548

1.5 Compliance Exception

1.5.1 Customers as per section 4. are not subject to risk rating.

1.6 Effective Date

1.6.1 This Manual of Risk Rating for commercial customers is deemed effective once approved by the Bank's Board of Directors through the Risk Management Committee, and the Bank employees are informed of the same.

1.7 Manual Review

1.7.1 The Credit Policy and Credit Risk Management Department shall review the Internal Rating manual for commercial customers and seek approval from the Risk Management Committee at least once a year.

2. Definitions

2.1 **Commercial customer** shall mean a customer who is a juristic person or an individual and meets one of the following criteria.

2.1.1 An annual revenue of more than or equal Baht 10 million based on either audited or pro-forma financials for standard customer segments (Refer to section 5 : Customer Segmentation)

2.1.2 Specialized customer segments (Including Construction, Real Estate (Sale/ Rent) or Hotels) (Refer to section 5 : Customer Segmentation)

2.1.3 FI "Financial Institutions" (Bank, Saving Co-operatives, Credit Card & Personal loan, Factoring, Leasing, Securities, Insurance, Mutual Funds)

2.2 **Credit line** refers to credit facilities, investment facilities or obligations but not including Spot / Forward / Derivative.

2.3 **Juristic person** refers to a limited company, a public company limited, a limited partnership, a registered ordinary partnership, or other types of juristic persons.

2.4 Parent company refers to a company with controlling power over business of other company, either directly or indirectly, in one or more of the following manners.

- 2.4.1 Holding more than 50% of the total issued and paid-up shares in a company.
- 2.4.2 Has the power to control majority votes in the shareholders' meeting of a company.
- 2.4.3 Has the power to control an appointment or removal of a person with managing authority or directors at least half of the total number of directors in a company.
- 2.4.4 Has the power to control in other manners as specified by the Bank of Thailand.

Holding of 20% or more of total shares sold, either directly or indirectly, is assumed as having the power of control unless it can be proven otherwise.

2.5 Subsidiary shall mean a company, which meets one of the following criteria.

- 2.5.1 A company having another company as its parent company.
- 2.5.2 A subsidiary of the company at every tier.

Chapter 2: Risk Rating Principles

3. Risk Rating Descriptions

All commercial customers must have an internal rating, with the exception of customers in section 4. An appropriate model based on the customers business type and also annual revenue must be used to calculate the internal rating. Refer to section 5 for the segmentation criteria.

The meaning “commercial loan” that excluding retail portfolio such as housing loan or personal loan etc.

4. Exceptions for Risk Rating

Customers who meet any of the following criteria are exempt from internal rating

Exceptions for Risk Rating	Rating result in KFS
4.1 Customers with only bill discounting/ aval/ acceptance by commercial banks.	Waive
4.2 Customers with SBLC or providing not less than 100% collateral of a fixed deposit with BAY or government bond pledged to BAY and other collateral such as bank guarantee, counter guarantee, state government bond with fully guarantee by the government.	Waive
4.3 Customers who are government authorities, non-profit state enterprises/government organizations or non-profit organizations.	Waive
4.4 SME R customers	Waive
4.5 A new juristic persons (juristic persons who have been established for not more than 1 year from the date of registration and therefore do not have annual financial statements) or juristic persons who have not started operations, (non-operational period / factory construction process which is in line with project plan and revenues or sales from main business are not incurred) during the credit approval request process. A Rating of KRUNGSRI(NEW) will be	KRUNGSRI(NEW)

Exceptions for Risk Rating	Rating result in KFS
assigned to them. After operations have commenced and a full year revenues or sales from main business have been registered, and Financial statements (either audited or pro-forma) are available, the risk rating for these customers must be updated.	
4.6 FI's with either no external rating or ratings from ECAI other than S&P and Moody's.	NON RATING
4.7 Juristic person or an individual with annual revenue less than Baht 10 million for standard customer segments (Refer to section 5 : Customer Segmentation)	NON RATING
4.8 Any other specific cases as found appropriate by the credit committee	Waive
4.9 Existing NPL accounts	KRUNGSRI12

Exceptions for risk rating, assessors must prepare credit rating in Risk module of Krungsri Financial Spreading. The system will provide rating of KRUNGSRI(NEW), NON RATING, Waive or KRUNGSRI12 automaticly. Reason of exception for risk rating must be documented in the risk rating summary

5. Customer Segmentation

The Internal rating models have been segmented based on homogenous customer segments. The Credit Manager / relationship manager must determine the appropriate segment before initiating the rating process. The segments are as follows

5.1 Customers in business other than construction, real estate (sale/ rent) or hotels. This group is segmented into three sub-categories and will be called **standard customer segments** going forward.

5.1.1 Annual Revenue > = Baht 400 million

5.1.2 Annual Revenue \geq Baht 50 million, but less than Baht 400 million

5.1.3 Annual Revenue \geq Baht 10 million, but less than Baht 50 million

To determine the revenue segments use the highest revenue over a period of 5 Years.

If customer has various across multiple industries select industry with highest revenue as main industry.

5.2 Customers in the business of construction, real estate (sale/ rent) or hotels. These customers will be called **specialized customer segments** and are further segmented as follows

5.2.1 Business Type = construction, and Audited financial statements available
(Industry code 70102xx)

5.2.2 Business Type = construction, and pro forma financial statements available
(Industry code 70102xx))

5.2.3 Business Type = Real estate for sale, and Audited financial statements available (Industry code 70201xx, 70203xx, 70204xx, 70205xx)

5.2.4 Business Type = Real estate for sale, and pro forma financial statements available (Industry code 70201xx, 70203xx, 70204xx, 70205xx)

5.2.5 Business Type = Real estate for rent, and Audited financial statements available (Industry code 70202xx)

5.2.6 Business Type = Real estate for rent, and pro forma financial statements available (Industry code 70202xx)

5.2.7 Business Type = hotel, and Audited financial statements available (Industry code 90101xx)

5.2.8 Business Type = hotel, and pro forma financial statements available (Industry code 90101xx)

5.2.9 If a customer is operating across multiple industries, the industry with the highest proportion of income should be used as the core industry to determine the model to be used. If the customers have multiple projects in the

same industry segment i.e real estate for sale entries information for each project independently.

5.3 Customer in business of Financial Institutions. These customers are further segmented as follows:

5.3.1 Business Type = Financial Institution (Industry code 601xxxx, 602xxxx except industry code 6020406 and 6020407 (pawnshop))

Chapter 3: Internal Rating Assessment

6. *Variables used in Internal Rating Assessment*

The variables used for the calculations of the internal ratings are determined based on statistical analysis of the bank's existing data and credit expert feedback for the standard customer segments and the specialized customer segments.

6.1 Standard Customer Segments

The variables used for the calculation of the internal rating for the standard customer segments are coded into Krungsri Financial Spreading, no separate financial information is required to be filled in to determine the internal risk rating. The Risk Rating Engine will pick up the information directly from the Spreading system. It is critical to ensure the data in the spreading system is filled in accurately.

The latest annual financial statements will be used to calculate the internal ratings. It is critical to update the financial information in Krungsri Financial Spreading.

6.2 Specialized Customer Segments

The variables used for the development of PD models for specialized customer segments are based on inputs given by credit risk experts in the bank and then validated using statistical methods. The models are based on financial and non-financial information about both the borrower and the project being financed. The information regarding these details must be entered into the rating engine on Krungsri Financial Spreading.

It is also important to understand the definition of reliable financials to complete the models.

The customers to be specialized customer segment but don't have the information of the project being financed for every projects, these customers will be assessed the same way as the standard customer segments. The reason shall be specified in the risk rating summary.

The information of the project being financed can be the best estimate of information.

Type of financial statement for risk rating assessment as follows:

- **Reliable financial statements**

Reliable financial statements refer to financial statements that have been audited by certified public auditors and/or the assessor considers that they reflect actual operating results and financial status and can be used for credit consideration and for risk rating assessment

- **Unreliable financial statements**

Unreliable financial statements refer to financial statements that have not been audited by certified public auditors or financial statements that have been audited by certified public auditors but the assessor considers that they do not reflect actual operating results and financial status and the assessor has to prepare projected operating results, projected balance sheet and projected cash flow with reliable assumptions to be used for credit consideration. This is referred to as pro forma financial statements

For one pro forma financial statement that combined from more than one customer, these customers will have the same rating and PD.

7. Final Risk Rating Adjustment

Assessors can downgrade / upgrade risk rating of commercial customers provided that there are reasonable grounds to support such an override.

Rating Can only be upgraded one level. The reason for upgrading the rating must be documented in the risk rating summary.

The Credit committee can override the risk rating for commercial customers where found appropriate. The reason for the same must be documented in the Full Credit Write-up.

The Risk Rating must be down graded one level if the financial used are more than 15 months old. (Difference between the date of the last fiscal year end and the date the rating is conducted). Only exception under section 10.4 where possible recent and final annual financial statements must be used. The Credit manager may also propose to downgrade a rating if he/she deem it fit. The rating may be downgraded a maximum of 1 level. Reason for a downgrade must be documented in the risk rating summary

8. *Financial Institutions*

For financial Institutions, the rating provided by external rating agencies must be looked up and entered in to the system, If the customer has not been rated by S&P or Moody's the customer must be left un-rated. If the customer has been rated by both S&P and Moody's and the ratings are not the same the rating of S&P must be used.

Chapter 4 : Internal Risk Rating Levels

9. *Level of Internal Risk Rating*

The probability of default based on the bank's internal rating methodology can be divided in to the following groups. These groups have been calibrated to the S&P and Moody's external scale.

Level	Corporate Risk Rating	S&P equivalent	Moody's equivalent	Definition
1	KRUNGSRI1	AA- or better	AAA to A2	Highest Credit Quality
2	KRUNGSRI2	A+ to A-	A3	Very High Credit Quality
3	KRUNGSRI3	BBB+, BBB	Baa1 to Baa2	High Credit Quality
4	KRUNGSRI4	BBB-	Baa3	High Medium Credit Quality
5	KRUNGSRI5	BB, BB+	Ba1 to Ba2	Medium Credit Quality
6	KRUNGSRI6	BB-	-	Low Medium Credit Quality
7	KRUNGSRI7	B+	Ba3 to B1	Relatively Low Credit Quality
8	KRUNGSRI8	B	B2	Low Credit Quality
9	KRUNGSRI9	B-	B3 to Caa1	Very Low Credit Quality
10	KRUNGSRI10	CCC or below	Caa2 to Caa3	Lowest Credit Quality
11	KRUNGSRI11	CCC or below	Ca to C	Extremely Lowest Credit Quality
12	KRUNGSRI12	D	D	Class of debt is Substandard / doubtful / doubtful of loss

Definition of each level of risk rating is as follows:

	Rating	Descriptor	Definition
Investment Grade	KRUNGSRI1	Highest Credit Quality	'KRUNGSRI1' ratings denote the lowest expectation of default risk. It indicates that the borrower has exceptionally strong capacity for payment of financial commitments. Although the debt protection factors may change, this capacity is highly unlikely to be adversely affected by any foreseeable event. 'KRUNGSRI1' is the highest borrower credit rating assigned by BAY.
Investment Grade	KRUNGSRI2	Very High Credit Quality	'KRUNGSRI2' ratings denote expectations of very low default risk. It indicates that the borrower has very strong capacity for payment of financial commitments. Although due to its relatively higher long-term risk, this capacity is not significantly vulnerable to any foreseeable event.
Investment Grade	KRUNGSRI3	High Credit Quality	'KRUNGSRI3' ratings denote expectations of relatively low default risk. The capacity for payment of financial commitments is considered sufficient. However, this capacity may be more vulnerable than those of the higher ratings to adverse business or economic conditions due to any foreseeable event.
Non-Investment or Speculative Grade	KRUNGSRI4	High Medium Credit Quality	'KRUNGSRI4' ratings indicate that expectations of default risk are currently low and it has medium default risk. In normal conditions, the capacity for payment of financial commitments is considered adequate, whereas under adverse business or

	Rating	Descriptor	Definition
			economic conditions risks of default are more likely to exist under this scale.
Non-Investment or Speculative Grade	KRUNGSRI5	Medium Credit Quality	'KRUNGSRI5' ratings indicate that the borrower faces major ongoing uncertainties and exposure to adverse business financial or economic conditions, which could lead to the obligor's inadequate capacity to meet its financial commitments.
Non-Investment or Speculative Grade	KRUNGSRI6	Low Medium Credit Quality	'KRUNGSRI6' ratings indicate that expectations of default risk are relatively high but a limited margin of safety remains. Adverse business, financial, or economic conditions with likely impair the obligor's capacity or willingness to meet its financial commitments. An obligor rated 'KRUNGSRI6' is more vulnerable to adverse developments than the obligors rated 'KRUNGSRI5'.
Non-Investment or Speculative Grade	KRUNGSRI7	Relatively Low Credit Quality	'KRUNGSRI7' ratings indicate very high default risk. The borrower is currently vulnerable, and is dependent upon favorable business, financial, and economic conditions to meet its financial commitments.
Non-Investment or Speculative Grade	KRUNGSRI8	Low Credit Quality	'KRUNGSRI8' ratings indicate that the borrower is currently highly vulnerable and entities with this rating have a seriously high risk of default.
Non-Investment or Speculative Grade	KRUNGSRI9	Very Low Credit Quality	'KRUNGSRI9' ratings indicate that the borrower is currently extremely vulnerable. Borrower might not have required financial flexibility to continue meet obligations; however, continuance of timely repayment is subject to external support.

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	Rating	Descriptor	Definition
Non-Investment or Speculative Grade	KRUNGSRI10	Lowest Credit Quality	'KRUNGSRI10' ratings indicate the extremely speculative in timely repayment of financial obligations. This rating also indicates borrowers with very serious problems and unless external support is provided, they would be unable to meet financial obligations.
Non-Investment or Speculative Grade	KRUNGSRI11	Extremely Lowest Credit Quality	'KRUNGSRI11' ratings indicate the highest default risk and the borrower is currently unable to meet its financial commitments or may even be in the process of compulsory debt re-structuring.
Non-Investment or Speculative Grade	KRUNGSRI12	In Default	An obligation is rated 'KRUNGSRI12, when it is in payment default, or the obligor has filed for bankruptcy. The "KRUNGSRI12" rating is used when interest or principal payments are not made on the date due, even if the applicable grace period has not expired, unless the bank believes that such payments will be made during such grace period.

10. Internal Rating treatment based on payment status

10.1 Normal and Special Mention debtors

10.1.1 Risk rating of debtors classified as normal / SM shall be carried out by the Credit Managers, as outlined in the document. (For SME customers the Credit Managers must validated the financial information provided by the Relationship managers in KFS before assessing the customers rating)

10.1.2 Customers who are the Bank's normal debtors or special mention but are classified as NPL by the Bank of Thailand or by Credit Review Department but have financial statement data, must be rated as indicated above section 3 to

5. The NPL Officer /CM must leave a comment in the risk rating summary that the customers are the Bank's normal debtors or special mention but are classified as NPL debtors by the Bank of Thailand, or by Credit Review Department.

10.2 NPL debtors

The Bank's customers who are classified as NPL debtors shall be subject to risk rating whereby variables shall be assessed as much as possible and the risk rating shall be based on the following debt classification.

Debt classification	Risk Rating
Substandard	KRUNGSRI 12
Doubtful	KRUNGSRI 12
Doubtful of loss	KRUNGSRI 12

Risk assessment of NPL to classified by credit review department or BOT and don't have financial statement data ,risk rating will be Krungsri 12 as well.

NPL customers of other financial institutions shall be rated according to normal criteria but the remark of "This customer is an NPL customer of (name of financial institution)." shall be made in the risk rating summary.

10.3 TDR Customers

Risk Rating treatment for TDR customers is as follows:

- 10.3.1 Customers whose debts are classified as Normal or Special Mention : These customers shall be rated in the same manner as normal customers.
- 10.3.2 Customers whose debts are classified as Substandard, Doubtful or Doubtful of Loss shall be rated in the same manner as NPL customers.
- 10.3.3 Customers under approved rehabilitation or rehabilitation under consideration shall be rated in the same manner as TDR customers if they are meeting payment obligations. For customers who have not yet entered a rehabilitation

plan, they shall be considered as NPL customers and, as such, shall be rated in the same manner as NPL customers.

10.4 Ceased Operations

10.4.1 Customers who have ceased operation but who continue to pay should be rated based on the last available financial statement. The CM must make a comment in the rating summary of the same.

10.4.2 Customers who have closed down their businesses or ceased operations and are not paying must be considered as doubtful according to BOT and shall be rated as KRUNGSRI12 based on debt classification and remarks shall be specified in the risk rating summary.

10.5 Sugarcane farmer

Customers discounting cheques payable to sugarcane farmers, or cheques issued to sugarcane farmers (Clean Bill Discount – purchase sugarcane / Clean Bill Discount – sugarcane credit), shall have the same ratings as ratings of the sugar companies who issue those cheques. If the customer has other facilities in addition to sugarcane the customer must be rated independently. If the sugar cane farmer is dealing with multiple sugar mills the lowest rating must be used. The documentation pertaining to the sugar mill must be maintained by the CM as required in section 11.1

11. *Conducting the Commercial Risk Rating*

11.1 Documentation and Recording the Rating

The Risk rating in KFS must be completed by the credit manager. The credit manager must keep all evidence and documents relating to the risk rating. In case no documentary evidence is available because information is derived from inquiries / interviews, the CM must document his/her finding in the risk rating summary. Supporting documents and evidences shall be kept in the file of each particular

customer for the benefit of future assessments and for further examination / review in compliance with the guidelines prescribed by the Bank of Thailand. After all variables are assessed and the conclusion of the risk rating of the customer has been reached, the Credit Manager must print and sign the summary form to attach as a part of the Credit Write-Up Report. Exceptions only allowed in the case of sugarcane farmers refer to section 10.5. The assessor shall also keep the summary form as well as the assessment form in the customer's file.

11.2 Risk Rating review

The Credit Manager shall review customer's risk rating every fiscal year or when there are changes in the following:

11.2.1 In cases where customers are affected by risk factors which may significantly alter their financial status and debt servicing ability, the assessor shall review the customers' risk rating to reflect their actual status.

11.2.2 When there is modification in customer's debt class:

11.2.2.1 From a normal or SM class to NPL

11.2.2.2 From NPL to Normal or SM

Debt classification adjustments shall be in line with the Bank's debt classification policy.

Appendix

A.1 Schematic Representation of data flow in KFS rating system

DataFlow Diagram Level 0

