Nordic Credit Rating

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Group and Government Support Rating Methodology

INTRODUCTION

1. Our group and government support methodology describes the analytical framework within which Nordic Credit Rating AS (NCR) considers owner and government support in the credit ratings of corporate and financial institution entities and guaranteed debt instruments.

2. The methodology is designed to be used in connection with our rating methodologies for non-financial corporates, financial institutions and other relevant sectors. It is designed to be robust, continuous and systematic and consequently produce ratings that are relevant and comparable with other assigned NCR ratings.

3. These criteria provide guidance for the rating impact of anticipated owner and government support or structural subordination that may exist among the entities of a group. The criteria also provide definitions of the status and standard 'notching' guidelines for various group members and holding companies within a group structure. Notching is the practice of adjusting the rating level of issuers and issues along NCR's rating scales.

4. For a full explanation and definitions of NCR rating scales and the rating process, see NCR's *Rating Principles* methodology, which can be found at www.nordiccreditrating.com.

OWNER SUPPORT

5. The ownership profile may have a pronounced impact on the credit quality of a rated entity. The impact may be viewed as positive if we assess it as likely that the parent company will support the rated entity in the event of financial stress. Conversely, it may be viewed as negative if we think the parent has a weaker credit profile than the rated entity and is dependent on the cash flows of the latter for servicing its own debt. We generally consider the potential for owner support an important factor when the rated entity is majority owned (>50% of votes) by another entity, but it could also be a key factor if ownership is 50% or below and the shareholder is deemed to have significant influence over the rated entity.

6. While support may take different forms, the most important aspect is whether support will be timely and sufficient to help the rated entity avoid a default. The rating impact of the potential for owner support is assessed on a case-by-case basis by the rating committee.

7. Our assessment of owner support differentiates between support received from a group parent and support received from an owner that we do not consider a group member. For instance, we typically do not regard private individuals, family-owned or private-equity firms, foundations, or diversified funds as parents in a group structure. We may, nevertheless, notch up a rated entity's standalone credit assessment to reflect support from a non-group parent where guarantees, capital commitments or other factors are deemed to enhance the overall creditworthiness of the rated entity. We may also reflect the negative impacts of non-group parents in downward notching where these are not adequately captured in an entity's standalone credit assessment.

8. In cases where we believe that the investment horizon of a parent company is limited, reducing the likelihood of support, we typically do not view the parent as a group parent and typically do not notch up the rated entity's standalone credit profile.

9. We typically do not regard a sovereign, regional or local government owner as a group parent. The likelihood of government support could, however, have a material impact on the credit quality of a rated entity, as described in paragraphs 22 to 28 of these criteria.

10. In cases where we define a parent company as a holding company outside a group structure, owning shares in one or more group parents, our approach for rating the holding company and its debt instruments is outlined in paragraphs 29 to 47 of these criteria.

11. In cases of diversified ownership, the rating on an entity may be notched up to reflect owner support even if the standalone credit assessment is higher than the credit quality of any or all its owners. For example, this is possible for jointly owned financing vehicles or financial services alliances where material credit enhancement and/or legally binding support agreements are in place.

12. Unless characterised by the definitions of 'CCC', 'CC', 'C' or 'D' ratings as set out in NCR's *Rating Principles* methodology, issuer and issue ratings affected by owner support are floored at 'B-' level.

OWNER SUPPORT IN A GROUP

13. When we consider an entity as part of a group, its issuer rating is dependent on the credit quality of the group parent, which, in turn, depends on our assessment of the credit quality of the overall group. To assess the group's credit quality, we first define the operating entities that are material to the group and then assess the standalone credit profiles of these entities using relevant sector methodologies.

14. In cases where NCR cannot assess the group's credit quality due to a lack of relevant sector methodology for material operating entities or the parent company, we may, nevertheless, notch a rated entity's standalone credit assessment either up or down to reflect the parent's impact on the overall creditworthiness of the entity where this impact is not adequately captured in the entity's standalone credit assessment.

15. Figure 1 sets out four different types of subsidiaries and the likely rating impact resulting from potential group support. The rating impact is partly dependent on both the group parent's ability and willingness to provide support and is, in many cases, a subjective assessment of the importance, relevance and relationship of the rated entity to the parent.

16. Depending on the strategic importance of the rated entity and relative credit quality of the rated entity to its group parent, we could raise the entity's standalone credit assessment by several notches. In cases where we assess support to be virtually certain and timely, we may equalise the rating of the entity with the rating on or NCR credit assessment of its parent company. We may, however, elect to be conservative in our notching if we think that support is uncertain and, in some cases, we may see the rationale for an entity rating that is higher than the credit quality of the parent (as described in Figure 2).

Figure 1. Notching principles for owner support in a group

Status of rated entity	Characteristics	Rating impact*
Vital	• Key long-term component of the parent company's corporate strategy, with very high likelihood of timely and sufficient support. • Strong link with the group's reputation and brand. • History of support and integration, or legally binding mechanisms incentivising support. • Significant reputational downside of failure to provide support.	Aligned with the parent issuer rating.
Significant	• Similar to vital entity, though less likely to receive support due to modest contributions in terms of cash flow, earnings or business profile, a short operating history or uncertain long-term commitment. • Likely to be supported in most scenarios.	One notch below the parent issuer rating, or equal to the parent issuer rating if the standalone credit assessment is equal to or higher than the parent issuer rating.
Minor	• Minor component of the parent company's corporate strategy due to lack of scale, materiality, or alignment with other group members. • Nevertheless, a rationale for support exists, the strength and likelihood of which determines upward notching.	Up to two notches above the rated entity's standalone credit assessment, capped at one notch below the parent issuer rating, or equal to the parent issuer rating if the standalone credit assessment is equal to or higher than the parent issuer rating.
Non-essential	• Not important to group creditworthiness due to lack of scale, materiality or alignment with other group members.	No notching, capped at the parent issuer rating.

*In relation to the parent issuer rating or NCR credit assessment.

17. In cases where we assess the status of a rated entity to be 'minor', in accordance with Figure 1, we consider the perceived likelihood of support and the relative credit quality of the parent and the rated entity in determining how many notches of support are included in the subsidiary rating. In cases where the standalone credit assessment already takes account of the rated entity's relationship to its parent, we tend to take a conservative approach to notching.

18. The issuer rating on an entity may be raised to the rating or NCR credit assessment of the parent company, even if it is not assessed to be vital to the parent company, if the rated entity's financial obligations are guaranteed through legally binding mechanisms from the parent company.

19. If the group parent's credit quality is assessed as weaker than the rated entity, we generally cap the rated entity's issuer rating at the level of the parent company, as outlined in Figure 1. However, in some instances, as described in Figure 2, we may see the rationale for a group entity having a rating higher than the parent or other members of the group. These cases would require the entity's standalone credit profile to be stronger than that of the parent and there to be barriers reducing or preventing stress in the parent or other group entities from spreading to the entity.

Figure 2. Notching principles for rating above the level of the parent

Potential notching above the parent issuer rating	Characteristics*
One notch	• Standalone credit assessment is at least one notch higher than the parent issuer rating. • The rated entity operates and finances itself as a standalone entity, despite sharing a parent with other group members. Likely the case for listed companies without operational integration with the wider group. • Defaults by other group members are not expected to lead to a default by the rated entity.
Two notches	• Standalone credit assessment is at least two notches higher than the parent issuer rating. • The rated entity operates and finances itself as a standalone entity, despite sharing a parent with other group members. Likely the case for listed companies without operational integration with the wider group. • Defaults by other group members are not expected to lead to a default by the rated entity. • Material minority ownership influence over the entity and its financial policies, such as with a listed company, limits the parent's ability to weaken the rated entity in order to support failing group members.
Three notches	• Same as for two notches, but standalone credit assessment is at least three notches higher than the parent issuer rating.
No limit	• Regulated entity, such as a financial institution, where owners are limited in their ability to demand dividends or provide financing to other group members. • Legal protections for creditors, preventing the parent from weakening the financial standing of the entity.

*In relation to the parent issuer rating or NCR credit assessment.

20. Notching of individual debt instruments for rated entities affected by group support follows the principles outlined in the corporate and financial institutions rating methodologies.

21. Unless characterised by the definitions of 'CCC', 'CC', 'C' or 'D' ratings as set out in NCR's *Rating Principles* methodology, issuer and issue ratings affected by group support are floored at 'B-' level.

GOVERNMENT SUPPORT

22. NCR's approach to government support is dependent on our evaluation of the sovereign, local or regional government's ability and willingness to support an entity, but also on the value of the goods or services provided for the government's objectives. In cases where we assess government support to be virtually certain, entities are notched down from the government entity's rating level.

23. Alternatively, an entity may be notched up from its standalone credit assessment where government support is less certain but reasonably likely. In these instances, the government support is viewed as providing a more reluctant form of extraordinary support and the rating level is more dependent on the standalone credit assessment.

24. By our definition, government ownership refers to direct ownership rather than via pension funds or other entities, which we would consider a strong owner but would view similarly to other diversified fund owners in the absence of a significant public policy role. In cases where the government is both a direct and indirect owner via pension funds or other entities, the

combined ownership may influence our view of government support if all parties are considered long-term investors. In specific instances, we may consider notching for government support in the absence of direct ownership where support may be necessary to preserve an important public service.

25. In the absence of NCR-assigned sovereign, local or regional government ratings, NCR uses its own credit assessments for sovereign and other government entity owners.

Figure 3. Definitions of significance to government

Significance to government	Characteristics
Essential	• Provides goods or services that are irreplaceable or would be provided directly by the government in the absence of the entity. • Supports key economic and social objectives of the government. • Severe political or economic consequences of not providing timely support.
Significant policy role	• Similar to essential entity, though somewhat less likely to receive support, given viable alternatives resulting in no more than short-term interruptions in availability.
Replaceable policy role	• Entity is an independent provider of goods or services that are necessary to achieve government objectives. • Competitive operating environment provides the government and its constituents with satisfactory alternatives.
Strategic interest	• Only a portion of operations are associated with a valuable policy role. • The government is only a minor customer in terms of revenues and strategic direction.
Limited policy role	• Entity provides goods or services in a highly competitive market, limiting incentives for government support. • Unclear or limited policy role.

Figure 4. Definitions of government ownership

Government ownership	Characteristics
Active management and/or wholly owned	• Government-run entity whose operations are fully aligned with government objectives. • Typically a wholly owned government entity, though potential for being majority owned in instances where the government is an active decision-maker. • History of support, investment and government involvement, or explicit government guarantee. • Significant reputational downside of government failure to provide support.
Controlling ownership	• Government owns at least a controlling stake and has a long-term interest in the entity due to policy alignment. • History of influence, support, investment and involvement, with expectations of further support.
Other investment	• Despite having less than a controlling stake, the government has an incentive to provide support to maintain access to goods or services supplied. • Potential for further support is mostly in order to protect the economic value of the investment. • Uncertain long-term government ownership strategy.
No direct ownership	• Government has no direct ownership. • Nevertheless, a rationale for support exists in order to preserve an important public service.

Figure 5. Notching principles for government support

Significance to govt/govt ownership	Active management and/or wholly owned	Controlling ownership	Other investment	No direct ownership
Essential	Aligned with government rating*.	One notch below the government rating*.	Two notches below the government rating*.	Up to two notches above the standalone credit assessment.
Significant policy role	One notch below the government rating*.	One/two notches below the government rating*.	One/two notches above the standalone credit assessment.	Up to one notch above the standalone credit assessment.
Replaceable policy role, or strategic interest	Two notches above the standalone credit assessment.	One/two notches above the standalone credit assessment.	One notch above the standalone credit assessment.	No upward notching.
Limited policy role	Up to one notch above the standalone credit assessment.	Up to one notch above the standalone credit assessment.	Up to one notch above the standalone credit assessment.	No upward notching.

*See paragraph 25.

26. In cases where the principles in Figure 5 allow for more than one alternative to upward notching, NCR considers the perceived likelihood of support and the relative credit quality of the government and the rated entity. In the absence of public statements or historical

precedent for support, or where the standalone credit assessment already takes account of the rated entity's relationship to the government, NCR tends to take a conservative approach to notching.

27. Our assessment of the likelihood of government support also considers potential social aspects. In some cases, the potential negative social impact or moral hazard associated with a government supporting a standalone entity may be significant enough to reduce the government's incentives to provide support.

28. Notching of individual debt instruments for rated entities affected by government-related support follows the principles outlined in NCR's corporate and financial institutions rating methodologies. Rating principles for guaranteed instruments are described in paragraph 50.

RATING PRINCIPLES FOR HOLDING COMPANIES

CORPORATE AND NON-FINANCIAL HOLDING COMPANIES

29. NCR defines corporate and non-financial holding companies as companies with limited operations outside the ownership of stakes in their subsidiaries. In cases where we do not see a holding company as part of a consolidated group structure, but rather as an owner outside the group, holding shares in one or more group parents, we view its credit quality as derivative of its material operating entities, as outlined below.

30. For a holding company to be within the scope of these criteria, its material operating entities must contribute a substantial proportion of the holding company's revenues and profits, with cash flows primarily dependent on dividend payments from operating companies. We expect the investment horizon to be long term, and that, in the case of holding companies owning multiple subsidiaries, their primary focus will be on one company or one industry. Furthermore, we expect the holding company and its operating companies to not be separately listed public companies. In addition, we would expect there to be other linkages between the holding company and its operating entities, typically demonstrated by fulfilling at least one of the characteristics below:

    - The holding company and the operating entities are closely associated, often through a shared name or common reputation.
    - The holding company and the operating entities share management and/or board members.
    - The holding company and the operating company share finance functions.
    - There are other material linkages connecting the holding company and the operating entities, such as internal loans.

31. Investment holding companies, which typically own smaller stakes in companies across many sectors with the aim of buying and selling assets and realising capital gains, are not within the scope of the criteria outlined in this section.

32. The issuer rating of a holding company is typically assessed in line with that of the general credit quality of the group as a whole, including any debt at the holding company. Typically, our assessment of the group's credit quality is based on the standalone credit profiles of its material operating entities.

33. If a holding company's sole activity is to hold the shares of one operating company, the holding company's issuer rating is generally in line with that of the operating entity.

34. The issuer rating of a holding company could be higher than that of its material operating entities if other assets in the group provide stronger asset-backing or more diversified revenues.

35. Conversely, the issuer rating of a holding company may be lower than that of its material operating entities if we assess it to have a higher risk profile or if debt at the holding company level is substantial.

36. Intermediate holding companies are rated as an associated issuer to their own material operating entities, based on similar considerations as for parent holding companies.

37. Debt instruments issued by a holding company typically only have a residual legal claim on the assets and cash flows of an operating company. The claim in bankruptcy proceedings is therefore subordinate to the debt and other liabilities at the operating company. As a result, we generally view debt issued at the holding company level as structurally subordinate to operating company debt.

38. Where we deem that there is structural subordination with recovery prospects equivalent to those of legally subordinated debt at the operating company level, we make similar notching to holding company debt as to legally subordinated debt at the operating company. To reflect the higher expected loss in the event of default, in most cases we rate senior unsecured debt at the holding company level two notches below the holding company issuer rating for investment grade issuers, and three notches below the holding company issuer rating for non-investment grade issuers. The notching may be reduced to one or two notches in cases where we find structural subordination to be of less significance.

39. If the operating company has issued hybrid instruments, the downward instrument notching of holding company senior unsecured debt may be increased by one notch to reflect the additional structural subordination that arises. This is because holders of hybrid instruments at the operating company have a stronger claim in bankruptcy proceedings than holders of holding company debt, further reducing the recovery prospects of holding company debtholders.

40. In the case of substantial secured debt at the holding company level, which further reduces the recovery prospects for senior unsecured holding company debtholders, we could increase the downward instrument notching by one additional notch.

41. To reflect the fact that loss in the event of default cannot exceed the principal amount of the bond, we typically cap the downward instrument notching of senior unsecured debt to three notches below the holding company issuer rating, even in cases where these criteria result in a sum exceeding three notches.

42. For subordinated instruments, such as hybrid debt, issued at the holding company level, we typically notch down an additional notch compared with senior unsecured debt for both investment grade and non-investment grade issuers.

43. Notching of senior secured debt instruments issued at the holding company level follows the principles outlined in NCR's corporate rating methodology or its other sector methodologies.

44. Unless characterised by the definitions of 'CCC', 'CC', 'C' or 'D' ratings as set out in NCR's *Rating Principles* methodology, issuer and issue ratings on corporate and non-financial holding companies are floored at 'B-' level.

FINANCIAL INSTITUTION HOLDING COMPANIES

45. The issuer ratings of non-operating holding companies of regulated financial institutions are generally notched one notch below the rating on the operating financial institution or group credit assessment to reflect structural subordination and the influence of the regulator over capital distributions and in the resolution and recovery plans of failing financial institutions. Wider notching between the operating entities and the holding company may occur during

periods of stress, when the resolution and recovery methods of a financial institution become clearer.

46. The notching of debt instruments issued by financial institution holding companies is typically one notch lower than the rating on similar instruments of the primary operating entity to reflect structural subordination. The actual notching is dependent on whether the holding company is included in the consolidated capital requirements of the banking group, as well as on the regulator-defined bail-in hierarchy and the terms of the specific debt or capital instruments.

47. Unless characterised by the definitions of 'CCC', 'CC', 'C' or 'D' ratings as set out in NCR's *Rating Principles* methodology, issuer and issue ratings on financial institution holding companies are floored at 'B-' level.

RATING PRINCIPLES FOR SPECIAL-PURPOSE FINANCING ENTITIES

48. Special-purpose financing companies are typically guaranteed by their parent company and have no other activity than acting as a financing entity for their parent. These companies are typically established for legal, tax or regulatory purposes and provide access to funding for the parent or entire group. Due to the specific nature of financing entities, we typically rate these companies in line with the parent company if we deem the guarantee to be adequate.

49. The rating of debt instruments issued by financing entities follows the general guidelines of our methodologies for corporates, financial institutions or other sectors, although the notching is based on the financial obligations of the relevant group and not solely on debt instruments at the financing entity.

RATING PRINCIPLES FOR GUARANTEED DEBT INSTRUMENTS

50. Where the guarantor, or group of guarantors, is of higher credit quality than the debt issuer, NCR aligns issue ratings for instruments with a legally-binding unconditional, irrevocable and timely guarantee.

51. Instruments with an explicit, irrevocable and timely guarantee from a government entity are rated in line with similar instruments issued by the government entity. For unrated guarantors, NCR's credit assessment of the guarantor and instrument notching principles for sovereign or local and regional governments are applied.

52. Instruments with an explicit, irrevocable and timely guarantee from a non-government entity are rated in line with similar instruments issued by the guarantor according to the relevant rating methodology. For unrated guarantors, NCR's credit assessment of the guarantor and instrument notching principles are applied.

53. Where there is a group of guarantors for a specific instrument, the issue rating is typically determined by the average comparable issue rating or NCR credit assessment of the relevant guarantors, unless there is a clear statement of responsibility for the entire obligation by the highest-rated guarantor. Where one or more guarantors have weak creditworthiness or there is a large discrepancy between the creditworthiness of the strongest and weakest guarantor, NCR analyses the impact of the guarantee on a case-by-case basis, including whether the guarantee provides any uplift to the issue rating.

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