



SEBI Registered
RBI Accredited
NSIC Empanelled

Rating Criteria for Consolidation of Companies

In addition to its own business, a Company may opt to conduct similar/related/diverse businesses through separate legal entities such as a subsidiary, a Special Purpose Vehicle (SPV) or associate/ group company. Intra group transactions may have a direct impact on the financial performance and loan repayment ability of the Company that is being rated. A rating of a subsidiary or an affiliate that is controlled by a dominant shareholder, involves an examination of the parent company's credit quality, which could enhance or detract from the subsidiary or affiliate's stand-alone rating. If parental linkages are weak, the issuer is likely to be rated more on a stand-alone basis. BWR also examines the parent's willingness and/or ability to support the subsidiary in exigencies. The extent of integration between the rated entity and the related entity is analysed based on the equity stake held, commonality of management, stated or documented support, economic/strategic importance of the related entity to the parent entity, common logo/name and fungibility of cash flows.

In analyzing the credit risk profile of a company that has direct or indirect controlling interest in another entity, BWR considers the financials of the company and its related entity on a consolidated basis, where available. Consolidation of accounts gives a better picture of the group's financial health, capital structure, liquidity, net worth, and leverage levels. Consolidated assessment of Financials helps in assessing the liabilities that the rated company needs to honor in the case of exigencies in a related entity.

BWR's Approach to Consolidation:

- a) **Business Risk and Management Risk of the Group:** The Business and Management risks of the group are assessed on the basis of the rating criteria used by BWR for analyzing the specific businesses. Based on such evaluation, the credit risk profile of the rated company is arrived at.
- b) **Assessment of Group's Key Financial Parameters and Financial Risk:** Group liabilities, net sales, profitability, interest cover and debt servicing ability are assessed when the audited statements of consolidated financial position are provided by the company. This in turn helps in understanding Group's financial position. While consolidating, all off-setting reciprocal pairs such as assets and liabilities, revenues and costs, and investment and equity accounts, which appear in the financial statements of the related entities are cancelled. The purpose is to net off or nullify all intra-group transactions. In the balance sheet, investments in related entities are netted off from the group's net worth, and borrowings within the group are netted off from advances/investments. BWR also nets off all intra Group sales, that is those sales which are not made to the third parties, but are made within the Group entities. BWR adopts best practices for this purpose.

- c) **Consolidation Approach for Subsidiaries that do not operate in the same sector as the parent:** BWR factors the potential impact of cash flow support to the unconsolidated subsidiary while arriving at the rating, which may either be notched up or down appropriately.
- d) **Others:** When the rated company does not have any major shareholding in group companies, there could still be transactions between them, which may have cash-flow implications for both the entities. There could be commonality of management and the Company may be performing specific work for the related Group entity - such as raw material sourcing, branding, production, customer sourcing and marketing activities for the product. BWR relies on the companies to provide consolidated accounts in such cases. Whereas, in cases where group companies hold substantial equity in but have no management control over other entities, the possibility and extent of cash flow transactions between the two entities may be assessed.

Disclaimer:

It must be clearly understood that a Rating opinion is based on various factors/aspects which includes application of certain Rating criteria. The particular criteria applied depends on a number of factors, inter alia, sector/Industry, historical performance, cyclical trends, prevailing economic condition, group support etc. Rating opinions factor many assumptions and the application of any particular criteria or a set of criteria may be full or partial depending upon peculiarity of each case. Application of any Rating criteria should not therefore be considered as rendering finality or completeness to a Rating assessment. A reference to criteria needs to be perceived in broad terms, only as an aid to a rating decision.