FITCH

SOVEREIGN RATINGS

RATING METHODOLOGY

Fitch's rating of sovereign nations

Sovereign borrowers usually enjoy the very highest credit standing for obligations in their own currency. If they retain the right to print their own money, the question of default is largely an academic one. The risk instead is that a country may service its debt through excessive money creation, effectively eroding the value of its obligations through inflation. When a sovereign nation borrows in a foreign currency, however, there is a more serious risk of outright default since the sovereign borrower cannot print the means of servicing the debt. The task of the credit rating agency is to assess the sovereign's ability and willingness to generate the foreign exchange necessary to meet its obligations.

This assessment is important not merely for the sovereign government, but for other issuers in the country - banks, corporates and public sector entities. The sovereign rating forms a ceiling above which it is not possible for other borrowers resident in the country to rise. This ceiling reflects both the theory and practice of international borrowing. A sovereign government has the legal power to apply foreign exchange controls to its residents, effectively monopolising the foreign currency earnings of all the entities in its territory. Non-government issuers and their investors therefore face a transfer risk - the risk that local currency will not be convertible into the foreign currency that they need to service foreign currency debt - which makes them at least as high a risk as the sovereign.

This risk was apparent during the eighties, when many sovereign countries that were forced to reschedule their foreign currency debt also took responsibility for negotiating the rescheduling of their private sector's foreign currency debt simply because they were rationing foreign exchange. (These considerations are why we examine not merely the Government's outstanding foreign currency obligations when we determine a country's indebtedness, but also the obligations incurred by the private sector.) The sovereign rating is therefore important even if the government itself does not want access to the world financial markets: it sets the parameters within which the private sector can operate.

Sovereign default and the globalisation of the world economy

The financial community has rightly travelled a long way since Walter Wriston, then the head of Citibank, was able to declare that countries do not go bankrupt because they always own more than they owe. Countries have failed to pay both interest and principal not merely during the debt crisis that began in August 1982 but in repeated historical episodes before that date: the US state of Mississippi has continued to have outstanding obligations in default since the early part of the nineteenth century. Indeed, some have argued that there is a forty-fifty year cycle of creditworthiness, followed by over borrowing, and culminating in default.

Nevertheless, the considerable attempts that many of the debtor countries caught up in the 1982 crisis have made to redeem their reputations shows that most Governments remain extremely reluctant to dishonour their debts. Indeed, it is arguable that the costs of default are increasing. This is not because the penalties have become greater - it is not generally possible to seize the assets of sovereigns in the case of default - but because the globalisation of production, trade and finance increases the advantages of pursuing a liberal economic strategy and raises the opportunity costs of pursuing an autarkic one.

There is an important political factor which also diminishes the likelihood of default. The conspicuous failure of world communism removes any plausible alternative to the capitalist mode of development. With the collapse of the Soviet Union and the increasing liberalisation of China, there is no longer a source of power, prestige and capital that could succour a country deciding to break with world financial markets.

To describe this new world of diminished ideological conflict as one where history has ended - Francis Fukuyama's contention - is nevertheless hyperbole. The forces of nationalism are rising. Islamic fundamentalism is a threat in several Middle Eastern states. But the world has entered a period in which there is more international consensus about the broad policies that are required for prosperity than has existed for several generations. To that extent, the world is beginning to look more as it did before the First World War and the rise of world communism. Coincidentally, the pre-first world war period was also a time of enormous international capital flows by the standards of the post-war period.

Fitch's risk model

Though the dangers of politically inspired default have shrunk, it is unlikely that the history of default has ended. Accidents and misadventure will continue to occur, even though they are more likely to be inspired by economic factors than political ones. Fitch's rating methodology for sovereign borrowers draws on the modern instances of default and near-default to establish a range of key leading indicators of distress, and these are incorporated in a risk model which gives a percentage score to sovereign borrowers. This is then converted into the long term ratings with which our investors are familiar. There is a separate short term risk model that analyses the prospects of timely repayment within the next year, and which highlights the importance of liquidity factors.

It is important, though, that investors realise the limitations of this exercise, which is necessarily far less certain than our ability to analyse either bank or corporate risks of default. The essential problem is that the world of sovereign borrowers is far smaller than the world of large banks or corporations, and that the number of instances of default in the modern period when we have reasonable national accounts is tinier still. We are committed to the exploitation of all means of analysis - whether the use of regression analysis or of neural networks - to improve our risk model. But even the most sophisticated econometrics is unable to find certainty amid such a relative lack of examples and data.

Without many instances of successful and unsuccessful debt service, it is impossible to be sure those particular indicators will pick up future problems. This difficulty, which is inherent in the economic analysis of any phenomena for which only small samples exist, is confirmed by our study of past instances of default. Defaults have engulfed countries with relatively low as well as high debts, relatively good as well as poor foreign exchange earning capacity, relatively long-established as well as more recent political institutions.

So the rating of sovereigns depends more on the art of political economy than on the science of econometrics. It depends on the careful judgement of experienced analysts about the durability of policy and the values of policy-makers as much as on a hard-nosed assessment of the prospects for a nation's export potential. It follows that it is more difficult to establish with precision the probability of sovereign default than, say, the probability of a default by other issuers in their local currency. The assessment of sovereign risk inevitably requires more judgement because we have fewer examples of success and failure.

The co-operative rating process

These difficulties of analysis make the cooperative nature of our rating process all the more important. Although we reserve the right to issue ratings at the request of our investors, Fitch has never seen the rating process as confrontational, and our method of rating sovereigns draws heavily on this tradition. Once a sovereign issuer has agreed to a rating, we send a questionnaire to the relevant officials asking for information that is not necessarily in the public domain about indebtedness and the sovereign's view of its debt servicing ability. This questionnaire is largely standardised, but includes sections specifically tailored to the sovereign in question where there are factors that make its economic and political circumstances unusual and special.

The answers to this questionnaire form the basis of the rating interviews conducted by at least two analysts in the country concerned over a period of up to a week. During our visit, we will seek to establish the debt burden of the country and its ability to service it. We also consider other external liabilities of the economy, such as foreign holdings of direct and portfolio investment, as these may also lead to requirements for foreign exchange that can impose a stress on the economy. However, the stock of these obligations can be sharply reduced in value by falls in domestic asset markets or in the country's currency so that debt remains our chief focus.

We review the orthodox indicators such as the ratios for debt to exports and debt to Gross Domestic Product, providing a measure of the current and prospective ability to service debt. We look at debt service and interest payments relative to exports; the fiscal balance and the growth of the monetary aggregates; the size and nature of the official foreign exchange reserves and so on.

We also examine the growth and the level of living standards, both as a measure of economic dynamism and as an indicator of a country's ability to make sacrifices should the need arise. High incomes give countries a cushion in times of adversity, enabling a compression of demand, cut in the import bill and a rapid generation of foreign exchange. The distribution of income can also be important both as an indicator of the ability to make sacrifices and of social tensions. A full list of the indicators we examine and the documentation we require is available on request.

Assessment of policy

This process also involves relatively conventional economic exercises, drawing particularly on the experience of the International Monetary Fund over many years, to assess the trends of gross national savings and investment and their implications for the current account of the balance of payments. Interviews with policy makers are particularly essential to a correct understanding of fiscal and monetary policy, which we have found to be the best leading indicator of the current account and debt problems.

Where appropriate, the fiscal balance is assessed after adjusting the domestic stock of debt for any erosion by inflation. We also look at the cyclically-adjusted deficit, separating the structural and cyclical components of the Public Sector Borrowing Requirement. The key question addressed by our examination of fiscal policy is whether there is a realistic path for the public sector deficit compatible with the country's economic development. This will usually involve an eventual stabilisation of the ratio of Public Sector Debt to Gross Domestic Product unless there is clear evidence of an equivalent build-up of public sector assets earning reasonable rates of return.

We reward policy coherence highly. An impressive defence by policy-makers of the appropriateness of policy to the realities of the country's economic situation is always reassuring, while any evidence that policymakers are failing to recognise or tackle problems is a source of worry. In the worst case, countries are marked down where there is clear evidence of policy initiatives that have been announced but never implemented.

Our assessment of the thrust of policy is not limited merely to financial indicators: a reduction in inflation and the current account deficit at the cost of soaring unemployment would not score as highly as policy that was clearly tackling the requirements of internal balance as well as external balance and financial stabilisation. Four key indicators must be considered together: growth, inflation, external balance and the level of unemployment. Thus our concern is not merely with stabilisation policy but also with the Government's attempts to improve the structural characteristics of the economy.

Our examination of structural policies is also a component in the analysis of the long-run growth rate of the economy. We take into account the growth rate of the population; the age distribution of the population; the scale of differences in productivity levels between different sectors of the economy, particularly agriculture and industry; the degree of urbanisation of the economy; and the effectiveness of the educational system both in providing a high proportion of the population with secondary and university education and in assuring a reasonable quality.

In our review of policy, we also assess the competence of the country's administrative machinery; the skill of policy managers in dealing with external debt in a manner that demonstrates understanding of the nature of world markets and the desirability of an orderly and regular amortisation schedule; and the past experience of the authorities in dealing with any liquidity crises that may have arisen. We also assess the prospects for the country concerned retaining the market access which will allow it to refinance maturing debt.

Analysing the tradeable sectors

Our analysts conduct a cross-check on the outlook for the current account which is implied by the development of national savings and investment by examining in detail the prospects for the country's tradeable sectors. This includes a review of the evidence on price and non-price competitiveness; market share; geographical diversity of markets; and sectoral diversity of exports as between primary products and manufactures. Evidence of a strongly growing, diversified and competitive tradeable sector, able to hold its own or even expand its share of buoyant markets, is particularly impressive. This is the key to foreign exchange earning capacity.

We also determine the openness of the economy to international influences and innovations. An open trade policy will tend to go hand in hand with competitive industries, since companies protected behind high tariff barriers will tend to be inefficient. And where those protected industries are competitive, they will often prefer selling into the home market because higher prices make the home market more profitable than the exploitation of overseas markets. In the long run, tariffs or quotas without a clear timetable of reduction and removal may therefore impede a country's ability to earn foreign exchange.

Openness to investment - the treatment of foreign direct investment and the repatriation of profits and dividends - is also a positive factor in our assessment of the country's growth potential and hence its capacity to service debt. Other factors are the productivity trend not only in the tradeable sectors (like manufacturing) but also in services, since this will help to determine the efficiency with which business can be conducted throughout the economy.

The level of investment as a share of Gross Domestic Product is an important indicator of economic health and vitality, and we attempt to assess in particular the extent to which investment is being made in activities which can earn or save foreign exchange. In the long run, the counterpart to the build-up of debt ought to be a build-up of capacity to service that debt by earning foreign currency. We also use our expertise in the rating of banks to assess the sophistication and efficiency of financial intermediation, since this is a key source of the efficient allocation of national resources.

Can the sovereign withstand economic shocks?

In addition to the establishment of a base case for the sovereign's economic and financial outlook, our analysts examine how the country might react if faced with certain international economic shocks. This sensitivity or stress analysis is designed to give us a clear idea of the robustness of the economy and of policy in the face of the unexpected.

The scenarios may change depending on the particular structure of the economy: an oil producer has relatively few problems faced with a doubling of world oil prices for example, but may find a halving more problematic. However, the standard scenarios include world recession, high world real interest rates, and a commodity price collapse. The exploration of these scenarios enables us to assess the appropriateness of different levels of debt for different economies: a highly flexible economy that has proved able to adjust quickly to changes in its international environment may be able to carry significantly higher debt relative to exports and Gross Domestic Product than others.

In assessing a country's reaction to shocks and its potential flexibility, it is particularly important to examine its labour market institutions and the extent to which there is some form of social safety net. Labour market inflexibility, caused by a fragmented and militant trade union movement, might increase the country's need for foreign capital inflows to meet any emerging deficit on the current account. It might also cause rising social tensions or an increasing public expenditure burden as unemployment rose.

The assessment of political risk

In this new world of global finance, it is appropriate that the disproportionate share of our analysis should fall on economic rather than political factors. Nevertheless, political risk has not been abolished by the self-destruction of communism.

There is an internal and an external dimension to the remaining political risks. Internally, the first question is whether the political settlement - whether a liberal democracy or a military government - is durable and stable. We do not seek to impose value judgments based on western preconceptions, but to judge a regime on the basis of its own country's history and traditions. We examine whether its leaders are able to mobilise support amongst the population even for unpopular measures. Are they able to communicate their concerns, and do important groups in society understand the Government's overall problems and objectives? We also examine the existence of political and social tensions whether their source is economic, social, ethnic or religious.

Externally, the key risk for sovereign borrowers is war or the imminence of war, as the defaults of Russia in 1917 or Japan in 1941 show. For most countries, war risks are thankfully negligible. But there are some sovereign borrowers who recognise the existence of a grave external threat by spending a substantial share of national income on defence. For others, some measure of the potential threat can be gauged from the military spending of neighbours. In assessing the overall risk, we take into account the policies of neighbours and the attitudes of great powers towards any potential conflict. If, though, we conclude that there is an imminent risk of a damaging local conflict, this factor will tend to override every other element in our analysis. However sound the economic and liquidity ratios may be, war risk is enough on its own sharply to reduce a country's credit rating.

Our perception of the risks involved in a particular sovereign is improved markedly by a network of international ties even if they do not formally involve guarantees of mutual support in either a military or economic sense. Membership of the Bretton Woods institutions; of the Organisation for Economic Cooperation and Development; of the North American Free Trade Agreement all help in this respect. Where there are closer understandings about support - for example, the credit lines in the European exchange rate mechanism or a healthy relationship with the International Monetary Fund - a country will be marked up accordingly.

The short term rating

We will normally assign a short-term rating at the same time as a rating for long and medium term obligations. A country with a relatively low long term rating, reflecting a high debt or a weak debt servicing capacity, may nevertheless enjoy a high short term rating if it has proved itself able to manage its liquidity needs successfully in the past.

A key factor in the assignment of the short term rating is the country's official holdings of foreign exchange reserves compared with its imports. However, a number of adjustments must be made to put this comparison into context. If the country's export earnings are particularly volatile, a higher ratio is required. Similarly, the existence of a high level of overseas investment of a short term nature - for example, bank deposits - would increase the need for reserves. However, the availability of credit lines is also taken into account.

In assessing the country's short term rating, we require evidence not merely of the level of the foreign exchange reserves but of their currency composition and of their maturities.

Assignment of ratings

Once the rating visit is complete, a detailed report is drafted and despatched to the sovereign authorities for factual comment. The sovereign report includes extensive comparisons between the rated country and its peer group for many of the indicators previously discussed. The report is subsequently submitted to the Sovereign rating committee, usually chaired by the Managing Director or another senior member of the Sovereign Group. The rating committee will consist of the lead analysts who will make the rating recommendation, senior sovereign analysts and credit analysts from the Financial Institutions or Corporate Groups when relevant. The outcome of the rating committee is then made public as soon as reasonably possible, via a press release and notification on the financial newswires, while the supporting sovereign report is made available to subscribing investors on the Fitch Ratings website, www.fitchratings.com.

APPENDIX I

Checklist of Sovereign Rating Criteria

This checklist is intended as an indication of the subject areas covered in our rating interviews, and as a review of the documentation that will normally be required. In many developing countries, not all of the series will be available but there may be indications from other sources. Some topics will not be appropriate. As our rating process is forward looking, our data requirements are generally for at least five historical years and two forecast years, one of which will usually be the year in which the review is taking place. Officials should highlight where national statistical definitions differ from the United Nations recommended system of national accounts.

i. Demographic, educational and structural factors

a) growth rate of the population
b) age distribution and dependency ratio
c) urban population as a percentage of the total
d) details of significant ethnic, religious and language minorities
e) numbers and percentage of eligible population attending secondary school and higher education
f) any measures of educational output, particularly if internationally benchmarked
g) living standards as measured by Gross Domestic Product per head, consumers' spending per head and both measures at purchasing power parity
h) distribution of income, wealth and land-holding
i) standard of infrastructure in transport and telecommunications together with principal plans
j) infant mortality, life expectancy and development of health services
k) natural resource endowment including proven reserves of minerals and fuels

ii. Labour market analysis

a) size, historical development and projection of total labour force
b) employment as a percentage of labour force; female and male breakdown; part and full time split
c) employment by sector, percentages of total, and changes over time
d) unemployment by sex, age, region, former occupation and duration (more than six months and more than one year)
e) the development of pay settlements and earnings growth; level of nominal hourly wages in the public and private sector
f) the average and marginal tax wedge between gross hourly wage cost to the employer and gross hourly wage paid to the employee
g) any incomes policy affecting the growth of pay, social security and so forth
h) the degree of trade union density and days lost through industrial action
i) description of the key influences on wage determination

iii. Structure of output and trade

a) Nominal and real Gross Domestic Product, Gross National Product
b) composition of GDP by sector (agriculture, construction, manufacturing, extraction, other)
c) implied productivity differences given by ii, c and iii, b now and five and ten years ago.
d) the ratio of oil consumption to GDP
e) share of imports and exports in GDP and trend over time
f) exports and imports by commodity type; highlighting any category worth more than 5 per cent of the total
g) exports and imports by geographical area

iv. Dynamism of the private sector

a) rate of business creation and failure and its trend
b) self employment and its trend
c) percentage of total economy in marketed sectors and in private sector
d) business sector fixed capital formation as a percentage of GDP, and annual changes
e) rate of return on capital employed in the business sector and trend
f) estimate of the capital stock and trend in the business sector
g) framework for ensuring competition and lack of concentration
h) business research and development expenditure and any indicators of patenting activity, particularly in the United States
i) estimate of the size of the publicly owned marketed sector and any plans for privatisation with expected proceeds
j) description of the method of privatisation

v. Balance of supply and demand

a) aggregate supply as a percentage of GDP, detailing imports of goods and non-factor services
b) aggregate demand as a percentage of GDP, including exports of goods and non-factor services
c) gross domestic expenditure as a percentage of GDP, including consumption, gross fixed capital formation, stockbuilding
d) external balance on goods and non-factor services as a percentage of GDP
e) gross domestic savings as a percentage of GDP
f) annual percentage changes in consumer spending, government spending (current and capital); Gross Fixed Capital Formation; exports and imports of goods and non-factor services
g) breakdown of gross domestic saving into personal, business and public sector as percentage of GDP
h) breakdown of gross domestic investment between public and private as a percentage of GDP

vi. Balance of payments

a) description and analysis of the level and growth of the export of goods and services for aggregates and for categories; a similar analysis for imports of goods and services
b) the split between convertible and non-convertible currencies where this is appropriate
c) the merchandise trade balance
d) levels and growth rates of exports and imports of services, looking both at aggregates and at important receipt and payments categories.
e) the services balance split by major categories including shipping and other transportation; investment income and tourism
f) private and official transfers
g) export and import unit values as indices, and the terms of trade
h) current account balance in local currency, dollars and as a percentage of GDP
i) long term capital flows broken down by creditor and debtor, equity or other type
j) short term capital flows (debt with a maturity of one year or less) split as above
k) analysis of comparative advantage in trade with an estimate of the development of exports relative to the country's existing markets (ie world markets weighted by the composition of the country's exports) and of the trend of imports as a percentage of domestic demand
l) estimates (or ranges of estimates) of the income and price elasticities of imports and exports
m) estimate of residents' lending and other investment overseas
n) any evidence of underinvoicing of exports or overinvoicing of imports
o) errors and omissions
p) reserve movements

vii. Analysis of medium-term growth constraints

a) the best estimate of the Non-Accelerating Inflation Rate of Unemployment (NAIRU) or natural rate, or of the maximum growth of employment without inflationary pressure
b) the best estimate of the trend of GDP growth, measured from cyclical peak to peak and cyclical trough to trough
c) any other indicators of output potential or spare capacity, such as independent surveys
d) the size of the output gap, ie the difference between GDP and potential GDP
e) the calculation of the warranted rate of GDP growth if the current account of the balance of payments is to be kept in line with long-term capital inflows (see balance of payments analysis)
g) assessment of the growth trend and whether it is improving or deteriorating

viii. Macroeconomic policy

a) the objectives and setting of monetary policy; the commitment to achieving and maintaining price stability; and any independence given to the central bank
b) the trend of inflation indicators, including the consumer price index, GDP deflator, any measures of intermediate prices, public sector charges and details of any direct price controls

c) description of recent pressures on the currency, objectives for exchange rate policy, and the resolution of any conflicts between exchange rate objectives and any commitment to domestic price stability
d) interest rate rates at the short and long end of the maturity range, including real short and long interest rates (deflated by the change in the consumer price index).
e) exchange rate trends, including indices of the effective exchange rate weighted by principal trading partners' currencies and of the real effective exchange rate computed using relative unit labour costs or other competitiveness measures
f) monetary growth trends including those for narrow and broad money and domestic credit expansion, with estimates of velocity trends
g) the setting of fiscal policy and its short and long run objectives, examining the Public Sector Borrowing Requirement as a percentage of GDP; the path of net public sector debt as a percentage of GDP; the net asset position of the public sector
h) estimates of revenue buoyancy by major source; split of revenues according to direct and indirect tax or charge
i) taxes and social security charges as a percentage of GDP, and incidence by social group
j) trends in public spending, including all major elements of spending including interest payments and an estimate of any cyclicality for welfare spending or other categories
k) sources of financing of the PSBR between monetary and non-monetary financing, domestic and foreign financing
l) breakdown of the PSBR and stock of national debt by borrower (general government, central government, local authorities, public enterprises) in nominal terms and as percentage of GDP.

ix. Trade and foreign investment policy

a) the principal measures taken to control imports (quotas, tariffs, non-tariff barriers) by sector
b) average tariff applied to manufactures weighted by category and any estimate of the overall degree of effective protection
c) description of the agricultural import regime, including variable levies etc
d) export subsidies including loans available at below market rates and any other export promotional measures
e) policy towards trade liberalisation with a timetable for removal of any measures
f) policy towards foreign investment including any prohibited sectors or regions and limits on foreign ownership
g) controls on repatriation of interest, profits, dividends and proceeds from disinvestment
h) any positive or negative difference in the tax or legal regime applied to foreign investors, including portfolio investors
i) stock of foreign investment by type (equity, foreign direct, debt), source country and by sector of investment

x. Banking and finance

a) analysis of bank lending by type of institution and sectoral destination

b) recent and projected borrowing requirements of private and state owned corporations
c) description of credit policies, detailing open market operations, reserve requirements, credit controls, interest rate regulations and rediscount facilities
d) description of the principal features of the banking system and its prudential regulation, including the level of non-performing assets
e) assessment of the domestic capital markets, including liquidity and scope, taking market capitalisation as a percentage of GDP for both equity and debt markets

xi. External assets

a) central bank foreign exchange reserves detailing gold, currency composition and maturity of instruments.
b) ratio of reserves to imports (expressed in months) and trend over time
c) foreign assets of the banking system
d) public sector external assets such as loans and export credits
e) non-bank private sector assets detailing bonds, shares and foreign direct investment

xii. External liabilities

a) description of the authorities' debt strategy
b) legal restrictions on government and other borrowing (domestic and international) and interest rate swaps and other off-balance sheet obligations
c) description of how central government monitors other state sector borrowings
d) breakdown of external debt by borrower (private, public, financial, non-financial)
e) breakdown of external debt by creditor (multilateral, bilateral, banks, bonds, suppliers' credits)
f) net external debt (debt less stock of foreign assets; reserves, commercial bank assets, private sector loans).
g) net external liabilities (net debt plus net stock of direct and portfolio investment and government loans abroad)
h) amortisation schedule and currency composition of gross debt
i) proportion of debt at floating interest rates; average terms of such debt as a spread over LIBOR
j) record of recent foreign currency fixed interest rate bond issues, their coupon, price, maturity and launch spread over the equivalent bond of the currency's government
j) external debt as a percentage of exports of goods and services and of GDP; debt service as a percentage of exports of goods and services; interest payments as a percentage of exports of goods and services
k) net interest and net investment payments

xiii. Politics and the state

a) description of the constitution and the relationship of the principal institutions including the courts

b) description of political parties, bases of support, share of the vote, and stability of support
c) election timetable for all levels of government
d) degree of consensus on macro and microeconomic policy of main parties
e) durability of the policy directions on which the Government is embarked
f) method of leadership succession
g) rationale for the sequence of any economic reforms, particularly financial reforms
h) size, growth and importance of the armed forces
i) description of principal alternative policies put forward by parties or important social groups
j) description of the legal framework for private property and contract settlement
k) description of the effectiveness of tax collection system
l) brief curriculum vitae of the principal permanent economic policy-makers

xiv. International position

a) foreign policy objectives and strategy
b) membership of international, multinational and supranational organisations including any regional trading blocs
c) relationship with the International Monetary Fund as shown by recent Article IV reports
d) relations with neighbouring countries
e) assessment of any external and internal security threats
f) relations with the European Union, USA and Japan

APPENDIX II

International Credit Ratings

The following ratings scales apply to foreign currency and local currency ratings. A short-term rating has a time horizon of less than 12 months for most obligations, or up to three years for US public finance securities, and thus places greater emphasis on the liquidity necessary to meet financial commitments in a timely manner.

Long-Term Credit Ratings

Investment Grade

Speculative Grade

AAA ***Highest credit quality***. 'AAA' ratings denote the lowest expectation of credit risk. They are assigned only in case of exceptionally strong capacity for timely payment of financial commitments. This capacity is highly unlikely to be adversely affected by foreseeable events.

AA ***Very high credit quality***. 'AA' ratings denote a very low expectation of credit risk. They indicate very strong capacity for timely payment of financial commitments. This capacity is not significantly vulnerable to foreseeable events.

A ***High credit quality***. 'A' ratings denote a low expectation of credit risk. The capacity for timely payment of financial commitments is considered strong. This capacity may, nevertheless, be more vulnerable to changes in circumstances or in economic conditions than is the case for higher ratings.

BBB ***Good credit quality***. 'BBB' ratings indicate that there is currently a low expectation of credit risk. The capacity for timely payment of financial commitments is considered adequate, but adverse changes in circumstances and in economic conditions are more likely to impair this capacity. This is the lowest investment-grade category.

Short-Term Credit Ratings

F1 ***Highest credit quality***. Indicates the strongest capacity for timely payment of financial commitments; may have an added "+" to denote any exceptionally strong credit feature.

F2 ***Good credit quality***. A satisfactory capacity for timely payment of financial commitments, but the margin of safety is not as great as in the case of the higher ratings.

F3 ***Fair credit quality***. The capacity for timely payment of financial commitments is adequate; however, near-term adverse changes could result in a reduction to non-investment grade.

B ***Speculative***. Minimal capacity for timely payment of financial commitments, plus vulnerability to near-term adverse changes in financial and economic conditions.

C ***High default risk***. Default is a real possibility. Capacity for meeting financial commitments is solely reliant upon a sustained, favourable business and economic environment.

D ***Default***. Denotes actual or imminent payment default.

BB ***Speculative***. 'BB' ratings indicate that there is a possibility of credit risk developing, particularly as the result of adverse economic change over time; however, business or financial alternatives may be available to allow financial commitments to be met. Securities rated in this category are not investment grade.

B ***Highly speculative***. 'B' ratings indicate that significant credit risk is present, but a limited margin of safety remains. Financial commitments are currently being met; however, capacity for continued payment is contingent upon a sustained, favourable business and economic environment.

CCC, CC, C ***High default risk***. Default is a real possibility. Capacity for meeting financial commitments is solely reliant upon sustained, favourable business or economic developments. A 'CC' rating indicates that default of some kind appears probable. 'C' ratings signal imminent default.

DDD, DD, and D ***Default***. The ratings of obligations in this category are based on their prospects for achieving partial or full recovery in a reorganization or liquidation of the obligor. While expected recovery values are hightly speculative and cannot be estimated with any precisions, the following serve as general guidelines. 'DDD' obligations have the highest potential for recovery, around 90%-100% of outstanding amounts and accrued interest. 'DD' indicates potential recoveries in the range of 50%-90% and 'D' the lowest recovery potential, ie. Below 50%.

Entities rated in this category have defaulted on some or all of their obligations. Entities rated 'DDD' have the highest prospect for resumption of performance or continued operation with or without a formal reorganization process. Entities rated 'DD' and 'D' are generally undergoing a formal reorganization or liquidation process; those rated 'DD' are likely to satisfy a higher portion of their outstanding obligations, while entities rated 'D' have a poor prospect of repaying all obligations.

Notes to Long-term and Short-term ratings

"+" or "-" may be appended to a rating to denote relative status within major rating categories. Such suffixes are not added to the 'AAA' long-term rating category, to categories below 'CCC', or to short-term ratings other than 'F1'.

'NR' indicates that FITCH does not rate the issuer or issue in question.

'Withdrawn': A rating is withdrawn when FITCH deems the amount of information available to be inadequate for rating purposes, or when an obligation matures, is called, or refinanced.

RatingAlert: Ratings are placed on RatingAlert to notify investors that there is a reasonable probability of a rating change and the likely direction of such change. These are designated as "Positive", indicating a potential upgrade, "Negative", for a potential downgrade, or "Evolving", if ratings may be raised, lowered or maintained. RatingAlert is typically resolved over a relatively short period.