
Financial Institutions Rating Methodology

Financial Institutions

Call for comments

Scope welcomes market participants' comments on its proposed methodology.
Please send your comments by 4 September 2025 to consultation@scoperatings.com.

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Table of contents

1. Scope of application	3
1.1 Rating framework	3
1.1.1 The issuer rating	3
1.1.2 Long-term debt ratings and correlation with issuer rating	3
1.1.3 Short-term ratings and correlation with long-term ratings	4
1.1.4 Local and foreign currency debt ratings	4
1.1.5 Regulatory action leading to non-payment of debt is a sector-specific consideration for regulated issuers	4
1.1.6 Issuers benefiting from a guarantee and/or government-related entity (GRE) status	4
1.1.7 Issuers benefitting from being part of a group	4
2. Key components	5
2.1 Analytical process	5
2.1.1 Step 1: Initial mapping and adjusted anchor assessment	5
2.1.2 Step 2: Determination of standalone credit assessment	5
2.1.3 Step 3: Integration of external support, if applicable	6
3. Information/Data sources	6
4. The issuer rating	7
4.1 Operating environment	7
4.1.1 Country-level operating environment (CLOE) assessment	7
4.2 Business model	13
4.3 Initial mapping	15
4.4 Long-term sustainability	15
4.5 Earnings capacity and risk exposures	16
4.6 Financial viability management	18
4.7 Additional factors	20
4.8 Standalone rating	20
4.9 External support	20
4.9.1 Guarantees and rating equalisation	20
4.9.2 Parent support	21
4.9.3 State or government support	26
4.9.4 Group rating approach	26
4.9.5 Assessing the creditworthiness of the source of support	26
5. Ratings on debt instruments	27
6. Other considerations	29
6.1 Bank holding companies/non-operating holding companies	29
6.2 Branches issuing debt	29
6.3 Low issuer ratings	29
6.4 Banks under regulatory intervention	29
6.5 Impact of coupon cancellation on AT1 ratings: no automatic downgrade	29
6.6 Impact of write-down or conversion on capital securities ratings	29
6.7 Key limits and uncertainties of this methodology	30

Summary

This proposed methodology update:

- introduces a framework for the assessment of country-specific operating environments based on a mix of qualitative and quantitative sub-factors
- introduces two qualitative scorecards for the assessment of parental support for i) assessing the degree of a subsidiary's integration into a banking group (and hence the choice between a top-down or bottom-up rating approach); and ii) the parent company's expected willingness to support the subsidiary, which is a key driver in downward notching in a top-down approach and upward notching in a bottom-up approach
- simplifies our long-term sustainability assessment, which can now only result in one of three outcomes: Positive, Neutral or Negative

The update also includes editorial changes and clarifications that do not alter the content of the methodology.

1. Scope of application

This rating methodology explains our approach to assigning credit ratings to financial institutions globally, including banks and a broad range of non-banking financial institutions. These include listed and unlisted credit institutions such as savings banks and cooperative groups; government-owned banks, retail and commercial banks, investment banks, specialised lenders, diversified credit institutions; other providers of financial services like mortgage institutions; non-bank lending institutions such as building societies, microfinance companies, leasing and factoring companies; and lending captives of car and other manufacturing companies. It is not intended to assign credit ratings to insurance companies, investment funds or asset management companies. For financial institutions that conform to our definition of a government-related entity, this methodology should be read in conjunction with our [Government-Related Rating Entities Methodology](#).

The methodology is based on a transparent step-by-step approach. The first step, combining credit views on a financial institution's operating environment, business model and long-term sustainability, leads to the determination of an adjusted anchor assessment. We then refine this anchor with a compare-and-contrast analysis of financial performance, specifically earnings capacity and risk exposures, financial viability management, and additional factors when applicable. The third and final step of the analysis addresses external support, whenever applicable.

1.1 Rating framework

1.1.1 The issuer rating

Issuer ratings assigned on our long-term credit rating scale (see [Credit Rating Definitions](#)) are forward-looking opinions on the relative creditworthiness of an issuer's ability and willingness to repay its financial obligations.

1.1.2 Long-term debt ratings and correlation with issuer rating

We rate each class of long-term debt based on: i) the issuer's credit strength as reflected by the issuer rating; and ii) the specific terms and conditions of the debt instrument itself. Consequently, long-term debt ratings are assigned as follows (see section 5 for more details):

- Higher than the issuer rating: certain classes of financial obligations benefitting from additional protection because they are secured by collateral and/or because of our expectation that they would otherwise be shielded from losses, even in a gone concern scenario. For example, this would be the case for covered bonds (see our Covered Bonds Rating Methodology) or preferred bank deposits.
- Same as the issuer rating: for categories of senior unsecured debt, depending on their seniority, as well as the regulatory and legal framework. For example, in the case of banks subject to resolution, preferred senior unsecured debt (or equivalents) would be rated at the same level as the issuer rating.
- Lower than the issuer rating: for capital instruments, subordinated debt and for categories of senior unsecured debt, depending on the ranking in the capital structure, debt-specific features as well as the regulatory and legal framework. For example, in the case of banks subject to resolution regimes, non-preferred senior unsecured debt, or structurally subordinated senior debt issued at the holding level, would be rated at least one notch below the issuer rating.

1.1.3 Short-term ratings and correlation with long-term ratings

Short-term issuer and debt ratings are derived from long-term issuer ratings. The assessment is further informed by a review of an issuer's funding and liquidity profile – including the potential impact of changes in market sentiment and access to central bank funding in case of market disruptions. For institutions benefitting from access to central bank funding, we assign the highest possible short-term rating given the range indicated by the long-term rating, unless our analysis highlights specific weaknesses in the issuer's funding and liquidity profile. The correlation between short-term and long-term ratings is detailed in our [Credit Rating Definitions](#).

1.1.4 Local and foreign currency debt ratings

Unless otherwise specified, our issuer and debt ratings apply equally to liabilities in local and foreign currency.

For issuers located in countries assessed by Scope with a sovereign credit quality of BB+ and below (non-investment grade), we may assign both local and foreign currency ratings.

For issuers located in non-investment grade countries, transfer and convertibility risks could play a greater role in determining our local and foreign currency ratings compared to issuers located in investment-grade countries. Our local and foreign currency ratings may differ if we consider that there is a higher risk that debt denominated in non-domestic currencies will not be reimbursed. This rating differential would capture the risk that an issuer may be prevented from honouring its debt obligation in full and on time due to government-imposed restrictions on foreign-currency payments, leading to a higher risk of default on foreign-currency liabilities.

Conversely, we view transfer and convertibility risks as negligible in investment-grade countries and in the euro area. As a result, in these countries, there is no difference between local and foreign currency issuer and debt ratings.

Any rating differential between local and foreign currency ratings reflects our view of the likelihood of the government imposing capital controls, including restrictions on sourcing foreign currency or transfers of foreign currency to investors. In this case, we will typically cap foreign currency ratings at the level of the foreign currency rating of the sovereign in which the issuer is domiciled.

Conversely, if the issuer has earmarked adequate foreign currency reserves to repay outstanding foreign currency debt and these resources are sufficiently protected from capital controls (for example via accounts or assets outside the country of residence), we will not apply such a cap.

1.1.5 Regulatory action leading to non-payment of debt is a sector-specific consideration for regulated issuers

Because banks and some other financial institutions are regulated entities, investors may face the risk that issuers are either unable to or are prevented from meeting their financial commitments due to regulatory intervention. This can be in the form of: i) early supervisory intervention, e.g. to prevent payments on capital securities; ii) resolution-related debt bail-ins that affect liabilities eligible for bail-in; or iii) insolvency proceedings. Credit ratings must therefore assess the extent to which credit fundamentals and other factors evaluated in the rating process influence the likelihood of such an event, along with events that are common to other industry sectors.

1.1.6 Issuers benefitting from a guarantee and/or government-related entity (GRE) status

Our Financial Institutions Rating Methodology describes how we assign ratings based on the analysis of standalone credit factors and applicable external support factors. In general, we do not perform a standalone analysis on financial institutions that benefit from an effective guarantee (see 4.9.1) or are assessed as being government-related entities. In such cases, we opt for a top-down approach as defined under our [Government-Related Rating Entities methodology](#).

1.1.7 Issuers benefitting from being part of a group

Financial institutions can have complex corporate structures. We consider the operational and legal/structural features of the underlying corporate structure on a case-by-case basis to determine the appropriate analytical perimeter. This is the starting point to determine whether a financial institution is analysed under a consolidated group approach, or alternatively on a standalone basis.

The identification of a group is not limited to a specific legal entity owning or controlling others but can also include a mutual or cooperative structure. For instance, there may be legal, contractual, regulatory, or governance considerations that indicate that the entities collectively form the equivalent of a group. Furthermore, the notion of a consolidated group for the purpose of this analysis does not necessarily coincide with accounting-specific consolidation.

If we deem that the primary driver of credit strength is the expectation of support under exceptional circumstances, we may apply a top-down rating approach as defined in section 4.9 of this methodology.

2. Key components

The key components for the assignment of an issuer rating are:

- Operating environment assessment
- Business model assessment
- Long-term sustainability assessment
- Earnings capacity and risk exposure assessment
- Financial viability management assessment
- Additional factors assessment (if applicable)
- External support assessment (if applicable)

2.1 Analytical process

To begin our analysis, we examine the range of data and information available, on both the macro and micro levels.

As indicated in sections 1.1.6 and 1.1.7, steps 1 and 2 may not be needed when we rate an issuer using a top-down approach (i.e., eligible government-related entities, members of a cohesive group or subsidiaries).

2.1.1 Step 1: Initial mapping and adjusted anchor assessment

We arrive at an initial mapping based on a combined assessment of an issuer's operating environment and business model.

We further hone the initial mapping by analysing the long-term sustainability of the issuer's business in the context of a changing operating environment. This analysis is based on environmental, social and governance (ESG) considerations and given the anticipated transformational impacts of technology on the financial sector, how an issuer copes with digitalisation.

The adjusted anchor assessment is the end point of step 1 and is a notch-specific assessment.

2.1.2 Step 2: Determination of standalone credit assessment

We refine our adjusted anchor assessment by reviewing the issuer's financial performance:

- Earnings capacity and risk exposures: we assess the risk profile of the issuer, in particular asset quality, and the level of risk protection provided by the issuer's ability to generate adequate risk-adjusted returns that build buffers, from provisions to capital.
- Financial viability management: we assess to what extent an issuer operates at a sufficient distance from regulatory minimum requirements, or industry benchmarks, which are also de facto binding constraints for non- or less regulated entities, and therefore manage the risk of regulatory failure, or the equivalent market perception.
- Additional factors that are not necessarily already captured in the above steps. Temporary considerations that weigh positively or negatively on the issuer's creditworthiness could also be captured in this step.

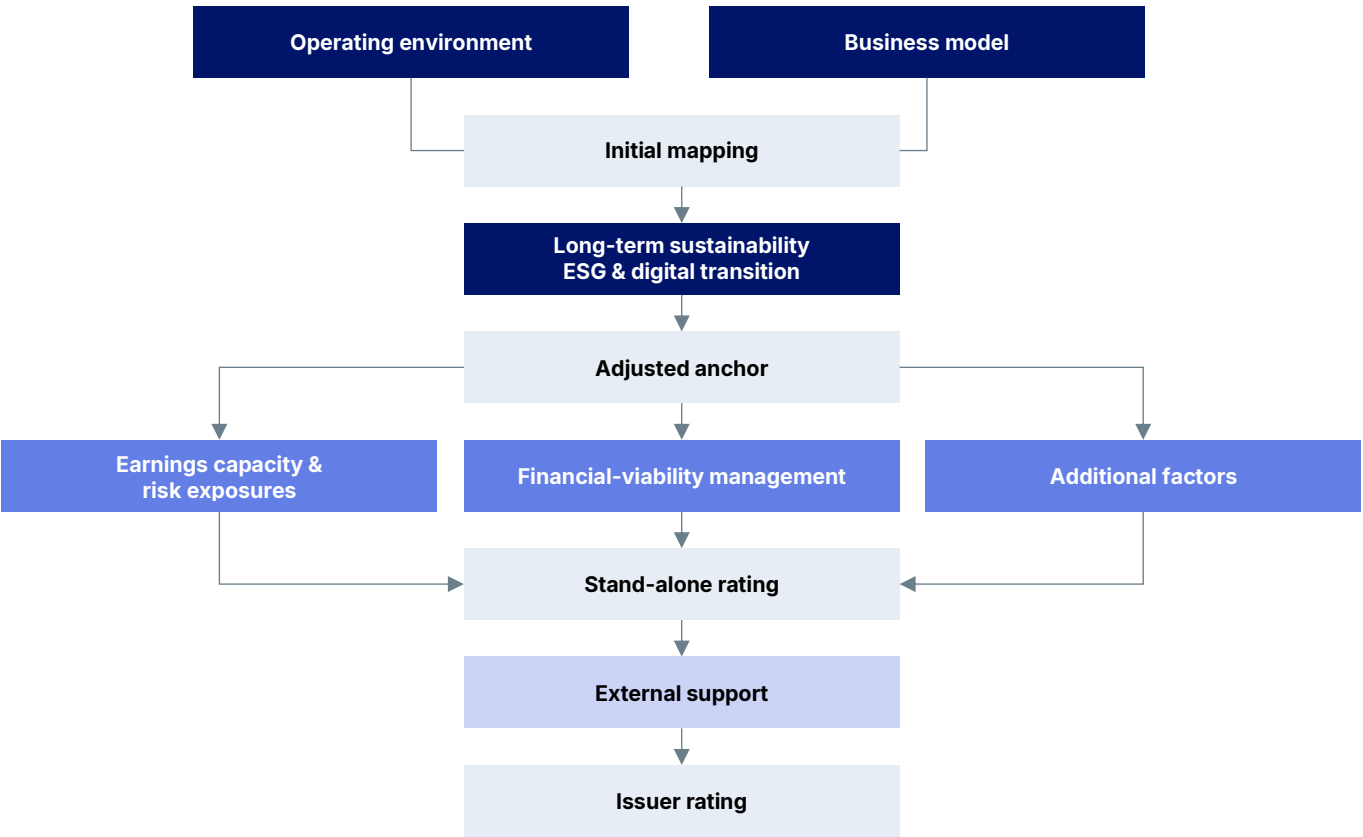
Our analysis of earnings capacity and risk exposures and financial viability management is not based on pre-defined ratios, or pre-determined thresholds. The relevant indicators are assessed at individual bank level but are intended to be similar for peers operating in the same jurisdiction.

We incorporate elements of comparative analysis throughout our assessment. This reflects our belief that compare-and-contrast analysis and the identification of outliers can significantly add to our ability to spot potential credit problems early on.

2.1.3 Step 3: Integration of external support, if applicable

If appropriate, we complement our review of the issuer’s standalone credit assessment with a review of potential external support. The above-mentioned steps are detailed in the following sections.

Figure 1: Methodology outline and analytical framework



3. Information/Data sources

Key assumptions for this methodology are informed by discussions with external parties — such as issuers, institutional owners, regulators and governments — and Scope’s analysis of financial and nonfinancial information, such as issuer financial statements and annual reports; bond documentation; and financial market, industry and economic data and history.

We perform our credit analysis using qualitative and quantitative information, mostly from the public domain. In advanced economies, regulatory initiatives have contributed to a significant improvement in the quality, depth, and degree of standardisation of public disclosures on financial and non-financial information. Assessing the adequacy and completeness of the information available for the rating process is a prerequisite. We will consider limitations observed in available information, such as partial or delayed publication or limited access to audited accounts.

We primarily use audited annual statements, which we may supplement with other public or non-public information (when available).

4. The issuer rating

4.1 Operating environment

In this first stage, we assess whether the environment in which the issuer operates is supportive of banking and/or other financial activities or is in itself a source of risk to the performance of financial activities. We identify the relevant operating environments by identifying the spread of its geographic activities based on the banks disclosed split by assets, credit exposures or loans or alternatively the geographic split of revenues. The combination of country assessments will be determined by the rating committee also taking into account forward looking views based the issuers strategic plans.

This process involves four steps:

- 1. Identification of key countries of operation.** The starting point of our analysis is to identify the main markets in which the issuer operates, within or beyond the bank's country of domicile, in order to capture the national or international characteristics of the issuer's operating environment.
- 2. Country-level operating environment (CLOE) assessment(s).** For each country where the rated issuer has material operations, we will assess how supportive the environment is for banking operations. For details on the derivation of CLOE assessments, see section 4.1.1.
- 3. Adjustment for non-bank financial institutions.** Non-bank lending institutions are typically subject to less stringent regulation and supervision and may have no access to central bank liquidity support. When rating non-bank lending institutions, we assess the extent to which this translates into heightened risk across the sector. In such cases, the operating environment assessment may differentiate between banks and non-bank financial institutions.
- 4. Issuer-level operating environment (ILOE) assessment.** This assessment is based on the relevant CLOEs and any adjustment derived under step 3 above. For issuers with material business activities across several jurisdictions, the assessment will reflect a blended view of the different CLOE assessments.

We summarise our view on the riskiness of an issuer's operating environment by assigning one of five qualifiers, further refined through a high or low modifier to a 10-degree scale ranging from Very supportive (high) to Very constraining (low). This assessment interacts with our business model assessment in determining the initial mapping of the rating (see section 4.3).

4.1.1 Country-level operating environment (CLOE) assessment

For each country where the rated issuer's operations are large enough to affect its credit profile, we will assign and maintain an operating environment assessment at the country level (CLOE). CLOEs are assigned on a 10-degree scale ranging from Very supportive (high) to Very constraining (low) based on the weighted score of each pillar (Figure 2), which is assessed on a scale of 1-100, as well as additional analytical considerations not captured in the scoring tool. Our framework to produce CLOE assessments incorporates several quantitative and qualitative considerations which entail a degree of expert judgement.

Figure 2: Country-level operating environment assessment framework

Assessment pillar	Weight	Sub-pillar	Weight	Approach	Variable	Qualitative considerations
Economic Strength Score (ESS)	50%	Economic prosperity	75%	Quantitative	GDP per capita	
		Size of the economy	25%	Quantitative	Nominal GDP	
Banking Sector Performance Score (BSPS)	25%	Profitability	33%	Quantitative	ROE	
		Capitalisation	33%	Quantitative	Tier 1 capital	
		Asset quality	33%	Quantitative	NPL ratio	
Structural Features Score (SFS)	25%	Regulatory oversight	30%	Qualitative		Regulation, supervision, resolution
		Operational support	40%	Qualitative		Deposit protection, state bail-out, lending of last resort, strength of domestic currency
		Financial stability risks	30%	Qualitative		Crisis history, sovereign-bank nexus, banking sector fragmentation
Indicative outcome	100%					
Additional considerations	+3/-3 qualifiers				Qualitative	
CLOE						

Economic Strength Score (ESS)

An important pillar of our CLOE assessment pertains to the underlying strength of the domestic economy. In our analysis, we focus on structural, long-term economic dynamics rather than short-term shifts in GDP, interest rates or cyclical indicators. As key metrics¹, we look at GDP per capita and nominal GDP as measures for the prosperity and size of the domestic economy. Short-term shifts in GDP growth are unlikely to drive our CLOEs.

GDP per capita is a widely used indicator to proxy the prosperity and living standard of countries. It is correlated with several economic and socioeconomic variables, including the level of household and corporate income, financial wealth, the education and literacy rate, human development, governance, banking penetration and capital markets development. Economies with a higher GDP per capita have more predictable and less volatile business trends and cycles, an environment which supports the asset quality and performance of financial institutions.

Based on the following calibration table, we assign a prosperity score as shown in **Figure 3** below.

Figure 3: Prosperity, scoring bands

GDP per capita in USD (current prices) - thresholds and assigned scores		
Minimum	Maximum	Score
0	<1,000	5
1,000	<2,000	10
2,000	<4,000	15
4,000	<6,000	20
6,000	<8,000	25
8,000	<10,000	30
10,000	<13,000	35
13,000	<16,000	40
16,000	<19,000	45
19,000	<22,000	50
22,000	<25,000	55
25,000	<29,000	60
29,000	<33,000	65
33,000	<37,000	70
37,000	<41,000	75
41,000	<45,000	80
45,000	<50,000	85
50,000	<55,000	90
55,000	<60,000	95
60,000	∞	100

Nominal GDP accounts for economic diversity and the ability to absorb, adapt and recover from shocks such as recessions, financial crises and external disruptions.

Based on the following calibration table, we assign a size score as shown in **Figure 4**.

¹ Historical data is typically sourced from the IMF but can also come from data sources that we deem reliable such as national central banks or statistical institutes.

Figure 4: Size of the economy, scoring bands

GDP in USD bn – thresholds and assigned scores		
Minimum threshold	Maximum threshold	Score
0	<5	5
5	<10	10
10	<15	15
15	<20	20
20	<30	25
30	<40	30
40	<50	35
50	<60	40
60	<80	45
80	<100	50
100	<150	55
150	<200	60
200	<400	65
400	<800	70
800	<1,200	75
1,200	<1,600	80
1,600	<2,200	85
2,200	<3,000	90
3,000	<4,000	95
4,000	∞	100

Banking Sector Performance Score (BSPS)

We assess the soundness of the financial industry in terms of i) its profitability, as measured by the return on equity; ii) capitalisation, as measured by the Tier 1 capital ratio; and iii) asset quality, as measured by the gross NPL ratio. We adjust historical data² to produce through-the-cycle assessments. We ensure our assessments remain relatively stable through the cycle by using long-term (10-year) averages that are adjusted upwards or downwards based on the medium-term (five-year) trend. Short-term shifts in sector performance are unlikely to drive our CLOEs.

The trend adjustment kicks in when the five-year average is more than 50% higher/lower than the 10-year average for each of the used metrics – resulting in an adjustment to the base score of +/- 12.5 points.

We give each sub-assessment a score from 1 to 100, which is used to calculate the overall BSPS.

Profitability. Banking systems that display attractive profitability metrics are less prone to financial instability, given their relative ability to generate capital organically and to attract fresh capital at times of stress. We assess base profitability based on the calibration table in **Figure 5**.

² Historical data is typically sourced from the IMF but can also come from data sources that we deem reliable such as national central banks or statistical institutes.

Figure 5: Profitability, scoring bands

Return on equity - thresholds and assigned scores		
Minimum	Maximum	Score
$-\infty$	<0%	0
0%	<5%	25
5%	<10%	50
10%	<20%	75
20%	∞	100

Capitalisation. A banking system's level of capitalisation offers insight on its ability to absorb unexpected shocks. Structurally high levels of capital indicate conservative prudential regulations, including a proactive use of regulatory buffers above the Basel minimum levels.

We assign a base capitalisation sub-assessment based on the following calibration table.

Figure 6: Capitalisation, scoring bands

Tier 1 capital ratio - thresholds and assigned scores		
Minimum	Maximum	Score
0%	<8%	0
8%	<10%	25
10%	<13%	50
13%	<18%	75
18%	∞	100

Asset quality. A structurally high level of NPLs in an economy can reflect structural factors such as a loan book mix skewed to the riskiest customer segments, ineffective NPL resolution frameworks or a supervisory approach that encourages forbearance and late resolution. Structurally high NPLs at system level make the banking sector as a whole vulnerable to shorter-term changes in economic conditions, including in collateral values. Moreover, they can indicate partially unresolved legacy issues. Finally, high levels of NPLs can lock up capital that could otherwise be deployed for new lending growth.

We assess banking sector asset quality based on the following calibration table.

Figure 7: Asset quality, scoring bands

Gross NPL ratio - thresholds and assigned scores		
Minimum	Maximum	Score
0%	<1%	100
1%	<3%	75
3%	<5%	50
5%	<10%	25
10%	<100%	0

Structural Features Score (SFS)

Under this heading, we assess softer factors that support a bank's operating environment, which include:

- **Regulatory oversight**, including the quality and robustness of bank regulations and the credibility of the supervisory and the resolution framework. We look favourably at jurisdictions that have closely aligned to global regulatory standards (Basel 3), have implemented a robust operational resolution regime, and display a strong, dynamic and independent prudential supervision.
- **Operational support**, including the availability of a credible lending of last resort facility, deposit protections, the status of the domestic currency, and the possibility for state-sponsored bailout (bailouts are unlikely in most developed markets with established resolution

regimes). We look favourably at banking systems benefitting from a liquidity backstop by well-funded institutions, including central banks. This is even more the case when the central bank can create a currency that is broadly accepted in global markets. Strong deposit protection, including broad depositor preferences and well-funded deposit guarantee schemes, are also positive features.

- **Financial stability risks**, informed by sector fragmentation, which in our view can lead to aggressive price and risk competition, a crisis history and an assessment of stability risks stemming from the high interconnectedness between bank and sovereign risks.

We use a qualitative scorecard assessment using 10 sub-factors qualitatively scored as constraining (0), neutral (1) or supportive (2). The resulting overall score is then rebased to a range of 0 to 100 to match the scale of the ESS and BSPS.

Figure 8: Structural Features Score, scorecard

Regulatory oversight	Quality of banking regulation
	Strength of prudential supervisory framework
	Implementation of resolution regime
Operational support	Deposit protection
	Expectation of state support
	Effectiveness of lending of last resort
	Reserve currency adjustment
Financial stability risks	Concentration of the banking industry
	Exposure to sovereign risk
	Credit performance record

Indicative CLOE assessment and additional considerations

The combination of the ESS, BSPS and SFS results in an indicative CLOE assessment. The weighted score is transformed into an indicative CLOE qualifier by applying the following correspondence table

Figure 9: Indicative CLOE assessments

Overall Score and indicative CLOE assessments		
Minimum	Maximum	Indicative CLOE
0	<15	Very constraining low
15	<25	Very constraining high
25	<35	Constraining low
35	<45	Constraining high
45	<55	Moderately supportive low
55	<65	Moderately supportive high
65	<75	Supportive low
75	<85	Supportive high
85	<95	Very supportive low
95	100	Very supportive high

The assigned CLOE assessment could reflect considerations that are not captured by the framework described above but are still relevant for the credit risk of rated financial institutions in the country. For example, the indicative CLOE be adjusted upwards or downwards by up to three qualifiers for:

- **High geopolitical risk.** CLOE assessments can be adjusted to reflect heightened geopolitical risks not yet reflected in economic and banking sector data.

- **Asset price vulnerability.** Expectations of a severe correction in key asset prices such as for real estate or equity could lead to a downward adjustment.
- **Private sector credit dynamics.** Excessively fast growth in private sector credit, especially when combined with high indebtedness, can be negative for the assessment.
- **Funding imbalances.** Systemic funding vulnerabilities, for example, due to a high reliance on external or short-term funding, can heighten the risk of capital flight.
- **Currency volatility.** A volatile currency can lead to a more cautious approach to the CLOE assessment. This will especially be the case when a significant proportion of domestic lending is denominated in foreign currency, as currency volatility can have an outsized impact on asset quality and bank capital.
- **Forward-looking adjustments.** Scope's analysts could deem the historical data underlying the BSPS to not reflect expected through-the-cycle performance, for example, when the data series includes exceptionally strong or weak periods that are unlikely to recur.

Loose correlation with sovereign ratings. Our operating environment assessment is de-linked from our view on a sovereign's debt-servicing capacity, though it does include several common considerations that produce some correlation with sovereign assessments. The size and wealth of the domestic economy, for example, are common factors underpinning both our sovereign ratings and our CLOE assessments.

4.2 Business model

Our business model assessment examines the ability of an issuer's business to consistently deliver stable and solid risk-adjusted performance.

Our assessment starts with a review of the issuer's business lines across geographies. Many large banking groups are universal in nature and their business model consists of a specific mix of different business lines, which can often be clustered into three categories: retail and commercial banking, wholesale and investment banking, and wealth and asset management. Alongside universal banks, more specialised business models exist, such as private banks, specialised lenders (mortgages, consumer, leasing etc.), specialised trading and/or investment banks.

The key drivers of our business model assessment include:

- **The issuer's market position and pricing power.** Dominance in a product segment in a market tends to correlate with higher pricing power. To assess an issuer's market position and pricing power, we analyse its size and market shares in its main countries of operations.
- **The degree of geographic and product diversification.** Revenue diversification is generally positive for a business model. Diversification, especially in lowly correlated markets or product segments, supports the resilience of financial performance against idiosyncratic shocks.

When relevant, we also consider additional factors, including, for example:

- **The overall risk-adjusted return profile of the business mix.** Some activities are inherently riskier than others due to the specific focus on certain products or client segments. We may adjust our business model assessment to reflect the risk return profile of the issuer's business model.
- **Volatile performance.** Highly volatile key performance indicators (KPIs) typically point to riskier business models. Similarly, activities that are structurally unable to generate enough revenue to cover their overall cost typically weigh down our business model assessment.
- **Implementation of medium-term strategy.** To ensure our business model assessments are forward-looking, we review the issuer's strategic direction and recent corporate activity (such as M&A, divestments) and adjust our business model assessment to incorporate its likely impact on the business model, when we expect this to be material. As well as the clarity and coherence of the strategy, we consider the execution record.
- **Niche players.** For issuers with a marked geographic or product focus, we would consider not only their overall market position, but also the positioning in a specified niche, if we consider this to be more representative of the actual competitive position and pricing power. The stability of an issuer's franchise, including its customer base, effectiveness of distribution and strong brand recognition can also inform our business model assessment.
- **Strategic partnerships.** For issuers that benefit from group membership, strategic alliances or strategic support from shareholders, we will reflect the increased ability to service clients coming from such associations.

We summarise our view on the issuer's business model by assigning one of five qualifiers, further refined through a high or low modifier to a ten-degree scale ranging from Very resilient (high) to Narrow (low) (**Figure 10**).

Figure 10: Business model assessment

Qualifiers	Typical characteristics (see Figure 11 for mapping with operating environment assessment)
Very resilient	Issuers with very strong and well-rounded business franchises, typically with a high degree of effective, well executed business and geographic diversification with adequate pricing power in several core markets and products. Leadership in domestic retail and commercial banking is often the anchor for the business model. KPIs are expected to remain very resilient and display very limited volatility even in stressed environments.
Resilient	Issuers in this category typically display a strong market position in their domestic retail and commercial market, where they may also be an important player in investment banking, insurance and wealth management. The domestic franchise is often complemented by some degree of international diversification. KPIs are expected to remain resilient and display low volatility through the business cycle.
Consistent	Issuers with a certain degree of revenue and earnings predictability, as is the case for most domestic retail and commercial banks. Regional franchises with strong local market positions or that focus on very low-risk customers or business lines can also be included in this category. Specialised lenders with well-established franchises or a high degree of geographic diversification can also be included in this category. KPIs are expected to display manageable volatility through the business cycle or in more stressed economic environments.
Focused	Issuers that operate on a small local scale and/or focus on a limited product range, making them more vulnerable to changes in the operating environment. This category also includes issuers with challenged franchises, and business models in need of reshaping. KPIs may display significant weaknesses or volatility through the business cycle or in more stressed economic environments.
Narrow	Business models with very high revenue volatility or a restricted revenue base, such as monoliners operating locally and lenders specialised in highly cyclical sectors or products with limited pricing power. A lack of business or geographic diversification limits the assessment.

4.3 Initial mapping

The combination of our operating environment and business model assessments provides the starting point for our rating process. Based on our qualitative assessment of these two factors, we arrive at an initial mapping assessment of the issuer (**Figure 11**).

Figure 11: Initial mapping table

			Operating environment assessment									
			Very Supportive		Supportive		Moderately Supportive		Constraining		Very Constraining	
			High	Low	High	Low	High	Low	High	Low	High	Low
Business model assessment	Very resilient	High	a	a	a	a	a	a-	bbb+	bbb	bbb-	bb+
		Low	a	a	a	a	a-	bbb+	bbb	bbb-	bb+	bb
	Resilient	High	a	a	a	a-	bbb+	bbb	bbb-	bb+	bb	bb-
		Low	a	a	a-	bbb+	bbb	bbb-	bb+	bb	bb-	b+
	Consistent	High	a	a-	bbb+	bbb	bbb-	bb+	bb	bb-	b+	b
		Low	a-	bbb+	bbb	bbb-	bb+	bb	bb-	b+	b	b-
	Focused	High	bbb+	bbb	bbb-	bb+	bb	bb-	b+	b	b-	b-
		Low	bbb	bbb-	bb+	bb	bb-	b+	b	b-	b-	b-
	Narrow	High	bbb-	bb+	bb	bb-	b+	b	b-	b-	b-	b-
		Low	bb+	bb	bb-	b+	b	b-	b-	b-	b-	b-

4.4 Long-term sustainability

From the initial mapping, we refine our view of the long-term sustainability of the business profile through an assessment of relevant environmental, social and governance (ESG) factors, with a specific focus on an issuer's preparedness for digital transition (D) – which we refer to as long-term sustainability (ESG-D).

Focus on ESG-D as source of credit risk. ESG-D encompasses a broad spectrum of topics. Our assessment, however, focuses on how ESG-D factors may impact an issuer's creditworthiness. Our approach takes into account the absolute level of sophistication of the issuer as well as the relative level of sophistication of the market(s) in which it operates. We aim to capture the extent to which proactive management of sustainability-related issues, including proper disclosures, reflects good risk management practices and provides a competitive edge in the market where the issuer operates, and therefore justifies a rating uplift. We also flag exceptionally weak ESG-D profiles, which we believe add to the risk profile of the issuer, justifying a downwards adjustment of the rating.

Materiality of ESG-D. To date, digitalisation and governance factors remain most relevant in the credit risk assessment of financial institutions. However, the importance of environmental and social factors is growing. Public and investor confidence are critical for financial institutions. Numerous ESG factors influence this perception, particularly those related to environment and social. These include an issuer's relationships with its various stakeholders, its management of human capital (e.g. employee welfare, skill development, diversity), its impact on the environment, and its role in environmental stewardship (i.e. support for sustainable growth and investment).

Our assessment of sustainability-related risks and opportunities is centred around the following elements:

Governance. We identify aspects of governance that may lead to higher credit risk, such as complexity in a group's ownership or corporate structure, a lack of independence among the board of directors, excessive power of (and reliance on) a key executive, or evidence of deficiencies in internal risk control and management. We also consider whether an issuer's business model is particularly exposed to litigation risk and the issuer's record on business conduct. Examples include incidents of product mis-selling, benchmark manipulation and money laundering. Misconduct can be a source of reputational and legal risk on top of regulatory fines. Remedial measures often involve direct costs and legal risks can represent a significant loss contingency.

Established financial institutions would in most cases display strong governance structures – at least on paper. Supervisory guidance, stock market governance codes and investor expectations have led to some convergence in the governance arrangements of larger institutions. As such, governance is unlikely to be a positive differentiating factor. Governance failures, on the other hand, are likely to drive credit differentiation. Small, unlisted or unregulated institutions are more likely to have weaker governance arrangements, partly due to a lower level of investor and supervisory scrutiny.

Digitalisation. To remain competitive, financial institutions need to make sufficient investments in their IT infrastructure, not only in client-facing functions but also in middle and back offices. We determine to what extent managing the digital transition is at the heart of strategic initiatives, or is a key component of the business model itself, whether a strong digital presence can be considered protective of established issuers, or whether digital transformation is shaping the competitive dynamic in the market the issuer operates in. Failure

to keep up with evolving technologies and trends may not result in immediate losses but may jeopardise the business franchise in the long term. With financial services becoming increasingly digital, cyber risks are also becoming more prominent. This is no longer only an operational issue as failures in IT security, with respect to the loss of customer data, can lead to significant reputational damage and ultimately customer losses – affecting the longer-term sustainability of the business.

Environment. Our focus is on how an issuer addresses environmental issues from a risk management perspective, i.e. its efforts to identify risks and manage them. This is particularly the case when regulators have set expectations in this area. We look for evidence that an issuer is more exposed than peers to climate change risk, either in its credit portfolio or because of the nature of its business activities. A presence in multiple geographies typically constitutes a challenge given the heterogeneity of market and supervisory expectations, at least until a global standard emerges.

We also evaluate the availability and quality of disclosures on these risks and consider how an issuer is supporting sustainable growth and investment as this may be relevant for its stakeholders and represent a strategic business opportunity.

Social. Related factors impacting creditworthiness are often tilted to the downside and linked to governance issues. Issuers in the financial services industry can be large employers with sizeable customer bases. The social repercussions of management actions may alter an issuer's reputation and constrain future growth prospects or the quality of its business franchise. Aggressive pricing, high remuneration policies or workforce adjustments tend to create more publicity than actions supporting social objectives. Governance models where customers have a significant influence on decision making tend to be more exposed to social risks.

Data limitations. We acknowledge the current constraints to peer comparisons, such as the level of industry disclosures, the ongoing development of standards, and the varying relevance of sustainability-related issues across geographies from a credit perspective. We also recognise that perceptions and expectations regarding ESG-D may vary across regions.

We expect the availability and quality of information to improve gradually and markedly as there is increasing demand from both supervisors and investors for ESG-related disclosures, transparency, and risk assessments. As supervisory expectations are further codified, financial institutions that cannot meet them face potential regulatory consequences and additional costs. In our assessment, we look for signs that management is aware of these expectations and is taking steps to meet them.

If needed, ESG-D factors may be further reflected in other steps of the rating process. Exceptionally strong (unlikely) or weak (more likely) ESG-D profiles, which warrant additional credit differentiation, could be reflected as additional factors (see Section 4.7).

Factoring long-term sustainability into the rating process

We summarise our view on an issuer's long-term sustainability by assigning one of three qualifiers (**Figure 12**). Based on the qualifier, the adjusted anchor assessment will benefit from a one-notch uplift, be unchanged, or be lowered by up to two notches.

Figure 12: Long-term sustainability assessment modifier

Qualifiers	Typical characteristics	Rating approach
Positive	The issuer is effectively and proactively managing sustainability-related considerations and stands out as a frontrunner in at least one sustainability theme that enhances its credit standing.	+1 notch
Neutral	The issuer is embracing changes in the ESG-D area, in line with peers. Progress made may be tangible but does not warrant further credit differentiation.	0
Negative	The issuer's management of material sustainability considerations displays significant shortcomings, which need to be addressed in the short term to catch up with evolving industry standards or market perception.	-1 or -2 notches

We then further refine our adjusted anchor assessment by analysing an issuer's financial profile, including earnings capacity, risk exposures and financial viability management.

4.5 Earnings capacity and risk exposures

Earnings, the first line of defence. An issuer's earnings capacity measures its ability to build and preserve economic value over time, as well as to create a sufficient level of risk protection – primarily in the form of credit provisions and equity capital. We view earnings primarily as an element of risk protection, as they are often an issuer's first line of defence against potential losses. Our assessment of an issuer's earnings capacity is a look-through approach of its earnings in light of its unique mix of risk exposures, which could be primarily credit risk, market risk or operational risk. Whereas our review of business models assesses the issuer's capacity to generate predictable and sustainable operating revenue, we focus here on an issuer's ability to generate sufficient income to: i) cover its operating

costs; ii) absorb losses on an ongoing basis including exceptional losses or incremental losses through the cycle; and iii) generate profit above its capital needs to remunerate providers of equity capital.

Credit risk. For most financial institutions – in particular banks – asset quality is a key focus of risk analysis, as credit risk (encompassing both the lending and investment portfolios) is often the primary driver of losses. The quality of underwriting criteria and the permanence of effective protection mechanisms such as insurance or collateral may represent important mitigating factors. We focus on relevant exposures that are more cyclical and are most likely to suffer higher credit losses in a downturn. When problem loans arise, we assess the issuer's capacity to remedy them and its strategic approach to cleaning up the balance sheet.

Other risk exposures. Depending on the business model, market risk, in particular interest rate and foreign exchange risks, can be a relevant source of earnings and capital volatility for financial institutions with significant market activity, or material asset-liability mismatches. In some instances, concentrated exposure to individual risks can constrain an issuer rating. Specialised lenders will often be exposed to specific risks arising from the peculiarities of their business models. Operational risk is especially relevant for issuers with complex operations and for activities structurally carrying low credit or market risk such as, for example, asset management or custody. Legal and litigation risks may be significant in some cases, limiting visibility on future earnings and capital trends. Other risks, inherent to a financial institution's business model, could be considered under this section.

Sovereign risks. For some financial institutions, and in particular those benefiting from effective supra-national support frameworks, such as banks in the euro area, we do not mechanistically link their overall creditworthiness to their respective sovereign. This reflects our view that there is a range of scenarios where banks may go through a sovereign default event without defaulting on their senior obligations.

When our bottom-up analysis indicates the potential for an issuer rating to be higher than the sovereign rating of the country in which the issuer is headquartered, we will systematically review its exposure to domestic sovereign bonds. When this exposure represents a material concentration (i.e. over 25% of Tier 1 capital), we review its risk characteristics and assess whether it impacts our earnings capacity and risk exposure qualifier.

Focus on structural, rather than cyclical drivers. Our ratings provide a medium-to-long term view of an issuer's creditworthiness. This means that a temporary dip in earnings is not in itself a reason to downgrade the issuer rating. Conversely, a one-off boost to profitability would generally not warrant higher ratings. Disregarding temporary earnings spikes or dips should contribute to ratings stability and predictability over time. However, deeper cyclical fluctuations may inevitably indicate material changes in an issuer's financial fundamentals, which will be reflected in the ratings. Our assessments are geared toward future expected trends and developments.

No scorecard approach. Our analysis of earnings capacity and risk exposures does not hinge on the monitoring of a specific ratio, a pre-defined set of ratios, or pre-determined thresholds. The relevant indicators are assessed at individual bank level but are intended to be similar for peers operating in the same jurisdiction. We look at a broad range of measures, depending on the issuer's business model. For example, **Figure 13** illustrates the ratios that are typically reviewed for European banks.

Figure 13: Earnings capacity and risk exposure metrics, European banks

Earnings Capacity	Risk Exposures
Net interest margin	Non-performing loan ratio
Cost/ income ratio	Non-performing loans/ tangible equity and reserves
Pre-provision income/ risk-weighted assets	Coverage ratio
Return on assets	Cost of risk
Return on risk-weighted assets	
Return on equity	

Peer based assessments. Our assessment of earnings capacity reflects the historical record and expected financial performance of the issuer. We look at changes in financial performance using a compare-and-contrast analysis, analysing the issuer's financial ratios relative to peers. As such, our assessment is not based on benchmarks – and we do not use pre-determined fixed thresholds for rating changes.

How we factor earnings capacity and risk exposures into the rating process

We summarise our views on earnings capacity in light of a financial institution's risk exposures by assigning a qualifier based on a five-degree scale ranging from Very supportive to Very constraining (**Figure 14**). A notching grade is attached to each qualifier, leading to an uplift or a lowering of the adjusted anchor from +2 notches to -2 notches.

Figure 14: Earnings capacity and risk exposure modifier

Qualifiers	Typical characteristics	Rating approach
Very supportive	Earnings capacity is highly stable through economic cycles and consistently supports the accumulation of loss absorption buffers. Provisioning and dividend distribution policies are conservative. There is no relevant concentration of risk exposures. Asset quality metrics and loss experience are better than peers. Risks are very low and well-managed, and highly unlikely to lead to losses capable of undermining the issuer's viability.	+2 notches
Supportive	Earnings capacity is stable through economic cycles and provides a strong buffer against losses. Asset quality metrics are relatively better or at least in line with peers. There is no relevant concentration of relatively high-risk exposures. Risks are well managed and are highly unlikely to lead to losses capable of undermining the issuer's viability.	+1 notch
Neutral	Earnings capacity may be variable over economic cycles but is sufficient to cover expected losses. Asset quality is in line with peers. Some risk concentration may exist but is not expected to be high or to generate high losses. Risks are unlikely to generate losses capable of undermining the issuer's viability.	0
Constraining	Earnings capacity is weak. Earnings and loss experience may show high volatility. Concentration risks require monitoring and can weigh on future performance. Asset quality metrics are below peers. Management is addressing risks, but these may still lead to material losses, putting pressure on the issuer's viability.	-1 notch
Very constraining	Earnings capacity is very weak. Earnings and loss experience may show very high volatility. There are material concentration risks. Asset quality metrics are materially poorer than those of peers. Risk management is insufficient to build or rebuild loss absorption buffers, undermining the issuer's viability.	-2 notches

4.6 Financial viability management

Financial resource management a key driver of credit risk. We assess the way an issuer manages its financial resources, including its capital and funding. For banking institutions and other regulated financial institutions, our analysis acknowledges the need for institutions to continuously comply with regulatory requirements and supervisory expectations. For non-regulated issuers, regulatory ratios are typically not available. In these cases, our analysis will focus on measures that are commonly seen as industry benchmarks. For both banks and other financial institutions, we evaluate the stability and diversity of an issuer's funding structure as well as the management of structural mismatches from an asset and liability perspective.

Looking at financial viability through the prism of regulatory metrics. Banking is a regulated business. Compliance with regulatory requirements is a prerequisite for banks to continue operating, often referred to as a 'licence-to-operate risk' or failure risk. With the increased sophistication of regulatory frameworks, maintaining a sufficient distance to regulatory minimums has become a source of complexity for banks, an important driver of their medium-term strategies and a confidence-sensitive issue, attracting both management and investor attention. Maintaining a sufficient distance to minimum regulatory requirements often drives strategy, e.g. capital allocation if capital resources are scarce or regulatory requirements are high. The need to comply with a variety of requirements can also significantly hamper the ability of a bank's management to implement its strategy.

Acknowledging the complexity of financial viability management. A well-defined regulatory regime could be amended at discretion to adapt to changing operating conditions in a pragmatic manner and with little advance notice. We aim to identify requirements that are critical to a bank's viability and, under stressed conditions, scrutinised by market participants, potentially exacerbating default risk. National discretion or regulatory forbearance may ease the challenge of complying with regulatory requirements for some banks, and less so for others. While looser regulatory requirements may facilitate management's ability to execute its medium-term strategy, they could also foster an aggressive risk appetite or insufficient protection against risk, which we would capture in our analysis of key risk exposures. Funding stability is a highly confidence-sensitive issue, and we consider that the analysis of funding adequacy is less easily performed through the prism of regulatory compliance. The reliance, stability and diversity of funding sources are assessed in the context of an institution's business model and the maturity of a country's debt capital market.

No scorecard approach. We do not set prescriptive, pre-defined thresholds above minimum requirements that we consider appropriate for an issuer's business. Our assessment does not hinge on the monitoring of a specific ratio, a pre-defined set of ratios, or pre-determined thresholds. The relevant indicators are assessed at individual issuer level but are intended to be similar for peers operating in the same jurisdiction. For example, **Figure 15** illustrates the ratios that are typically reviewed for European banks.

Figure 15: Financial viability management metrics, European banks

Capital	Funding and liquidity
CET1 ratio	Net stable funding ratio
Tier 1 ratio	Liquidity coverage ratio
Total capital ratio	Loan/deposit ratio
Leverage ratio	
Asset risk intensity	

Quality review. Our assessment incorporates qualitative considerations on the different metrics, including their composition, stability and any imminent risks. For example, we may penalise issuers with very low risk asset intensity, when we consider this is not fully capturing the underlying risks of the balance sheet.

Forward looking view. Our assessment incorporates our expectations on how capital, funding and liquidity metrics will evolve over time. This view is informed by management expectations and guidance, as well as by our expectations around future profitability, asset growth, and upcoming regulatory changes. For example, a bank with very high capital buffers will not receive any rating uplift if we expect such excess capital to only be a temporary feature based on the bank's growth and distribution plans.

Asymmetric approach to capital excesses and deficits. In general, we do not expect excessively large buffers to remain a permanent feature. Consequently, we do not give additional weight to buffers that are significantly above the regulatory minimum. We consider a maximum two-notch uplift to strike a balance between a degree of conservatism and balance sheet optimisation considerations. In contrast, our assessments may penalise by 5 downward notches financial profiles that place an institution's financial or regulatory viability at risk.

Factoring financial viability management into our rating process

We summarise our views on financial viability management by assigning a qualifier based on a six-degree scale ranging from Ample to At risk. A notching grade is attached to each qualifier, leading to an uplift or a lowering of the adjusted anchor assessment from +2 notches to -5 notches (**Figure 16: Financial viability management modifier**Figure 15).

Figure 16: Financial viability management modifier

Qualifiers	Typical characteristics	Rating approach
Ample	We consider that the issuer's management effectively and consistently maintains an ample buffer to relevant regulatory requirements, and we expect it to continue to do so. We expect the issuer's financial viability to prove resilient to tail-risk events.	+2 notches
Comfortable	We consider that the issuer's management effectively maintains a comfortable buffer to relevant regulatory requirements, and we expect it to largely continue to do so. We expect the issuer's financial viability to prove largely resilient to tail-risk events.	+1 notch
Adequate	Financial viability management provides an adequate buffer and, under a base case scenario, should not imminently push any metric close to minimum requirements or jeopardise the issuer's financial viability.	0
Limited	We consider that the issuer's management of its financial resources, intentionally or not, puts pressure on its ability to conduct its medium-term strategy independently and free of regulatory or financial viability considerations.	-1 notch
Stretched	We consider that the issuer's management of its financial resources is too aggressive or that compliance with minimum regulatory requirements is stretched, which hampers management's ability to drive business strategies.	-2 or -3 notches
At risk	We consider that the issuer's compliance with minimum regulatory requirements is too stretched and puts its regulatory and financial viability at risk.	-4 or -5 notches

4.7 Additional factors

This final step captures credit strengths and weaknesses that were not already captured or insufficiently captured earlier in the rating process. We intend to make limited use of this additional step.

This step can reflect transitory situations, such as restructuring measures that have not been fully implemented, events leading to changes in ownership or M&A transactions. The full execution of these strategic moves often entails transition risks, which may temporarily but materially constrain or support an issuer's creditworthiness. By isolating analytical factors under this category, we explicitly signal their material but transitory nature and the possibility that they could eventually be incorporated elsewhere in the rating process.

This step also captures specific business model characteristics and risks relating to non-bank lending institutions and more generally, narrower business models exposed to specific risks and/or with a high dependency on one specific factor, leading to a material concentration risk that may not otherwise be reflected or only be insufficiently captured in other parts of this methodology.

Figure 17: Additional factors

Qualifiers	Typical characteristics	Rating approach
Significant upside factor	We consider that a qualified rating factor, or set of factors, not already captured in the rating process, provides a significant uplift to the issuer's creditworthiness.	+2 notches
Material upside factor	We consider that a qualified rating factor, or set of factors, not already captured in the rating process, provides a material uplift to the issuer's creditworthiness.	+1 notch
Neutral factor	We consider that the previous steps in the rating process adequately reflect the issuer's creditworthiness.	0
Material downside factor	We consider that a qualified rating factor, or set of factors, not already captured in the rating process materially weighs on the issuer's creditworthiness.	-1 notch
Significant downside factor	We consider that a qualified rating factor, or set of factors, not already captured in the rating process, significantly weighs on the issuer's creditworthiness.	-2 notches

4.8 Standalone rating

The standalone rating, resulting from the refinement of the adjusted anchor assessment in step 2, represents the intrinsic credit strength of the issuer, irrespective of any expectation of extraordinary external support.

4.9 External support

We incorporate ongoing operational support (ordinary support) in the standalone analysis. For instance, stable distribution agreements with shareholders could improve our assessment of an issuer's business model; risk-sharing or buyback agreements could boost our assessment of asset quality; and the existence of standby funding commitments could enhance our assessment of financial viability.

Beyond the analysis of these intrinsic rating factors, external support notches can be appropriate if we assess that an issuer is likely to benefit from an external source of support under exceptional circumstances. Our assessment of external support focuses on both the ability and the willingness to support the issuer under exceptional circumstances such as financial distress.

The expectation of the provision of support, assuming the source of this support has the capacity to provide it, depends on:

- The source of support being more creditworthy than the issuer.
- The absence of legal impediments, regulatory limits or other factors that prevent the issuer from receiving support, for instance, in the case of international groups facing transfer or convertibility risks. Such limits make rating uplifts less likely.

4.9.1 Guarantees and rating equalisation

The existence of a legally enforceable guarantee has a major impact on the credit quality of a supported financial institution, typically shifting the primary source of credit strength from the rated entity to the supporting entity.

In cases where the supported financial institution benefits from such guarantees, we equalise the rating of the rated entity to that of the supporting institution.

To equalise ratings at the issuer or debt level we will assess the strength of the guarantee. Guarantees that meet all of the following criteria will always qualify for full rating equalisation:

- i) General: the guarantee covers all liabilities of the rated entity
- ii) Irrevocable: the guarantee cannot be called back by the guarantor
- iii) Unconditional: the guarantee is not subject to any conditions
- iv) Unlimited: the guarantee is not limited in size

In some cases, we could consider rating equalisation when only some of the above criteria are met. The rating committee would make such a determination. This could be the case if some of the conditions are only partially met and Scope considers the scenarios in which the guarantees would not be applicable to be so unlikely as to not affect the credit quality of the rated issuer. Examples are when a size limit exists but is large enough to cover losses under extreme scenarios, or when the condition on a conditional guarantee is already met.

4.9.2 Parent support

Issuer ratings can include parent support, either from a single owner in the case of subsidiaries, or from several owners in the case of joint ventures or other forms of joint ownership. See 4.9.5 for details on how we assess the creditworthiness of the source of support in case of multiple sources of support.

Our approach for incorporating parental support into an issuer's rating involves an assessment of:

- 1. the degree of the subsidiary's integration with the parent
- 2. the willingness of support from the parent
- 3. the ability of the parent to support the subsidiary

















First, we determine whether the primary source of credit risk lies with the rated entity's standalone credit profile or with the parent. This is based on an evaluation of the degree of integration between the rated entity and its parent. This initial assessment, supported by a qualitative scorecard (**SC1**), will allow us to determine if the rating will be assigned under a 'top-down' or 'bottom-up' approach. The application of the **SC1** will provide us an 'integration score' that is calculated as the weighted average of factors that we consider to be drivers of the level of integration (or not) of the credit risk profile between the parent and the issuer.

SC1 - Degree of integration

The assessment of the degree of integration is based on Scorecard 1 (**SC1**) and is the first step to determine how support from the parent should be incorporated as part of the risk profile of the rated entity. Specifically, it will guide our choice to determine whether to consider parental support as the primary source of credit strength (and consequently rate the issuer using a top-down approach) or whether the primary source of credit strength lies with the standalone profile of the issuer (calling for a bottom-up approach).

We assess the degree of integration via four components, as summarised in **Figure 18: Assessment of the subsidiary's integration with the parent - Scorecard 1 (SC1)**.

Figure 18: Assessment of the subsidiary's integration with the parent - Scorecard 1 (SC1)

Scorecard 1: Integration		High	Medium	Limited	N.A.
Resolution Strategy	40%				
Ownership	20%				
Strategic Alignment	20%				
Financial Interdependencies	20%				

Source: Scope Ratings

The integration score, ranging from a minimum of 1 to a maximum 100, is calculated as a weighted average³ of the four components that allow us to assess the strength of the integration relationship between the issuer and the parent. We use a scoring system assigning 'High' (100), 'Medium' (50) and 'Limited' (1). The weighted result of the four assessments determines whether the top-down (integration score of above 66.7) or bottom-up approach (score of below 33.3) is more appropriate. In cases where the integration score is between 33.3 and 66.7 points, both the top-down and bottom-up approaches are possible, and the decision on the analytical approach will be taken based on expert judgement. For entities rated under a top-down approach, a full standalone assessment is not required. However, a degree of financial analysis will be necessary to estimate the parent's willingness to support, such as for example the potential cost of support.

The following analytical components (and weights) determine the integration score:

➤ **Resolution strategy (40%)**

The resolution perimeter and resolution strategy of the parent are key elements to assess the integration with the subsidiary. This analytical component receives the highest weight, reflecting our view of its relevance for the purposes of integration and support considerations.

Assessment	High (100)	Limited (1)
Rationale	The rated entity is included in the resolution perimeter of the parent company.	The rated entity is not included in the resolution perimeter of the parent company.

In cases in which the parent is not a banking group, for which a resolution strategy is not required under the applicable regulatory framework, the assessment will generally be considered as 'not applicable' and will not be part of the weighted components.

➤ **Ownership (20%)**

Ownership is a relevant element of integration and further driver of the expectation of exceptional support. We assess ownership based the percentage of shares owned by the parent in the rated entity.

Assessment	High (100)	Medium (50)	Limited (1)
Rationale	The parent company owns more than 50% of the rated entity	The parent company owns between 20% and 50% of the rated entity	The parent company owns less than 20% of the rated entity

➤ **Strategic alignment (20%)**

We consider that the strategic alignment between the parent and the rated entity is a critical criterion for determining the expectation of exceptional support. Strategic importance can be reflected in the relevance in terms of income generation, product cross-selling, complementary business, strategic fit, among others. Since strategic importance could change over time, depending on changes in the strategic direction taken by the parent, the key element to address strategic alignment in our view comes mostly from the relevance that the parent gives to the development of the business of the rated entity, supporting growth, organically or via M&As.

Assessment	High (100)	Medium (50)	Limited (1)
Rationale	The subsidiary is deemed to be core to the strategy of the parent.	The subsidiary is deemed to have moderate importance to the strategy of the parent.	The subsidiary is considered not to contribute to the strategic goals of the parent

Entities that fulfil a specialised role for the parent (e.g. issuance vehicle, captive operation, payments provider) for which substitutes are available in the market but for which the change is relatively costly, we would generally consider the strategic alignment to be high as they cover and/or provide a key function or business for the parent.

➤ **Financial interdependencies (20%)**

Financial interdependencies could come in the form of group funding, for instance, available funding lines, centralised funding issuance, and on- and off-balance sheet committed lines. It could also be related to the relevance of revenues/income originated by the rated

³ In cases where a component is assessed as 'Not applicable' the denominator of the weighted average is adjusted by the weight of that component, resulting in higher weights for the remaining assessments.

entity and provided to the parent in the form of dividends or profit-loss transfer agreements, resulting in a strong link between the credit quality of the rated entity and the parent.

























Conversely, specialised financial institutions could not rely on intragroup funding, liquidity or contributions from their parent as they maintain a relative independence or autonomy in their funding policies, due to particularities of their business (different maturity profiles) or due to strict separation policies between the parent and the rated entity.

Assessment	High (100)	Medium (50)	Limited (1)
Rationale	There is a high level of intra-group funding between the parent company and the subsidiary.	There is some level of intra-group funding between the parent and the subsidiary.	The subsidiary is independently funded.

SC2 - Willingness to provide support

The assessment of willingness to provide support is guided by Scorecard 2 (**SC2**), and allows us to determine if the parent is willing to support the rated entity by addressing operational needs (1) on a regular basis based on the characteristics related to the existing operational integration with the parent, governance and parent's track record of support, or (2) on an exceptional basis based on reputational and brand risk, cost of support and cross-border considerations. The overall assessment related to the 'willingness to provide support' is obtained from the highest assessment between the outcomes (High, Medium, Limited) for each analytical pillar.

Figure 19: Assessment of the willingness of the parent to provide exceptional support - Scorecard 2 (SC2)

Scorecard 2: Willingness		High	Medium	Limited	N.A.	
Operational Integration	33%					Control and regular support: -
Governance	33%					
Track record of support	33%					
Reputation and brand risk	33%					Likelihood of exceptional support: -
Cost of support	33%					
Cross border considerations	33%					

Control and regular support

This pillar is assessed by evaluating the parent's relationship with the rated entity in terms of i) operational integration ii) governance; and iii) track record of support. For each analytical component, we assess whether the degree of control and regular support is 'High' (score of 100), 'Medium' (50) or 'Limited' (1). The average of the three assessments determines the indicative classification (High, Medium, or Limited) of this pillar.

➤ Operational integration (33%)

We assess the level of involvement and integration of the parent in critical activities of the rated entity such as risk management, IT Compliance, among others. Common frameworks, policies or shared personnel are elements pointing to a high level of integration.

Assessment	High (100)	Medium (50)	Limited (1)
Rationale	The parent centralises decision-making through the adoption of common policies and procedures and significant sharing of group functions.	The subsidiary has some level of operational independence, though operating frameworks are coordinated at group level	The subsidiary operates independently from the parent company and its policies could be materially different from the parent's.

➤ Governance, key personnel, governing & oversight bodies (33%)

We view governance as a key factor to determine the potential for regular support. Usually, the tighter the control exercised by the parent, the stronger the integration. The composition of the rated entity's board of directors and top management body are indicative of the degree of control. In tightly controlled subsidiaries, management bodies are often entirely comprised of parent company's

employees. Conversely, where the rated entity has an independent top management and board of directors, this indicates a greater degree of autonomy. The greater the power of the parent to influence the rated entity's governance, the stronger the link between the credit quality of both entities.

Assessment	High (100)	Medium (50)	Limited (1)
Rationale	The parent company exercises strict control over the rated entity via tight control of its management and oversight bodies.	The parent company exercises moderate control over the rated entity via some control of its management and oversight bodies.	The parent company has little or no representation in the rated entity's oversight body and executive management.

➤ Parent's track record of support (33%)

We also consider the track record of the parent providing support to subsidiaries. While there is no guarantee of future support, a consistent record of timely and reliable support indicates that the parent company has a propensity to support its subsidiaries.

Assessment	High (100)	Medium (50)	Limited (1)
Rationale	The parent company has promptly and fully supported its subsidiaries as needed through capital or liquidity injections in the past	The track record of support is mixed, with the parent company showing limited willingness to support subsidiaries in the past	In past instances, the parent company did not support its subsidiaries when needed.

Likelihood of exceptional support

This pillar is assessed by analysing the parent's willingness to provide support under exceptional circumstances, in cases where the elements of i) reputation and brand risk; ii) cost of support; and iii) cross-border considerations could be material enough (or not) to trigger extraordinary support. For each analytical component, we assess whether the level is 'High' (score of 100), 'Medium' (50) or 'Limited' (1). The average of the three assessments determines the indicative classification (High, Medium, or Limited) of this pillar.

➤ Reputational risk (33%)

We view reputation and brand risks as critical drivers for determining the willingness to provide support under exceptional circumstances. In this assessment, we look at the reputational consequences of a hypothetical default of the rated entity for the reputation of the parent company.

Assessment	High (100)	Medium (50)	Limited (1)
Rationale	The rated entity operates under the same brand as the parent company. Failure of the rated entity would have severe reputational repercussions for the parent.	The rated entity and parent company operate under separate brands, but these share significant elements. Failure of the rated entity would have moderate reputational repercussions for the parent.	The rated entity and parent company operate under separate brands. Failure of the rated entity would have limited reputational repercussions for the parent.

➤ Cost of support (33%)

We consider the trade-off between a hypothetical default of the rated entity and the hypothetical cost of supporting it. A support/no-support decision would typically consider the size of the capital/liquidity injection needed and its impact on the parent company's own financials. The higher this cost, the lower the willingness of the parent company to provide such support.

We generally proxy the cost of support with the balance sheet size of the rated entity relative to the size of the parent company. The smaller the rated entity, the greater the likelihood that any support need would be seen as affordable and increase the willingness of the parent company to provide it.

Assessment	High (100)	Medium (50)	Limited (1)
Rationale	The rated entity is small relative to the parent company's consolidated resources (less than 10% of total consolidated assets). Cost of support considerations are unlikely to negatively affect a support decision.	The rated entity represents a significant proportion of group assets (between 10% and 30% of total consolidated assets), and cost considerations could affect a support decision from the parent company.	The rated entity is large relative to the parent company's consolidated resources (more than 30% of total consolidated assets). Considerations around the cost of support are likely to weigh significantly on a support decision from the parent company.

➤ **Cross border considerations (33%)**

A parent could have a strong commitment, moral obligation or willingness to support the rated entity, but constraints related to cross-border considerations could limit the ability to do it on a timely manner. Limitations to access domestic currency to cover for upcoming funding maturities, limitations to access foreign currency, regulatory restrictions, among others, could limit the ability of the parent to provide support under exceptional circumstances. This assessment will be closely related to the operating applicable environment of the rated entity.

Assessment	High (100)	Medium (50)	Limited (1)
Rationale	The rated entity operates in the same jurisdiction as the parent, or in different jurisdictions with high expected level of cooperation. Regulatory restrictions could exist but are deemed highly unlikely to affect the ability of the parent company to support the rated entity.	The rated entity operates in a different jurisdiction from the parent, potentially with a low expected level of cooperation. Regulatory restrictions could affect the ability of the parent company to support the rated entity.	The rated entity operates in a different jurisdiction from the parent with a low expected level of cooperation. Regulatory or other cross border restrictions could affect the ability of the parent company to support the rated entity.

Notching-down from the parent company (top-down approach)

When the high degree of integration calls for a top-down approach, we will notch down from the parent company rating based on our assessment of the willingness to provide support, following the guidelines below:

- **High willingness:** 0-1 notches
- **Medium willingness:** 1-2 notches
- **Limited willingness:** 2-3 notches







Notching-up from the standalone rating (bottom-up approach)

When the degree of integration calls for a bottom-up approach, we will add up to three notches to the standalone rating based on the parent's ability and willingness to provide support.

The ability to provide support will be proxied by the rating differential between the parent rating and the rated entity's standalone assessment; the willingness to provide support will result from the application of SC2 above.

Both assessments are then mapped to an indicative credit uplift as indicated in the below **Figure 20**.

Figure 20: Assessment of potential notching uplift

Willingness to support	Potential notching uplift - Rating differential parent vs rated entity		
	≥ 4 notch differential	3 notch differential	≤ 2 notch differential
	 High	 Medium	 Limited
 High	2 - 3	1 - 3	1 - 2*
 Medium	1 - 3	1 - 2	0 - 1*
 Limited	1 - 2	0 - 1	0

* The notching may be capped by the parent's rating.

4.9.3 State or government support

Banks subject to resolution regimes. As resolution regimes have been implemented in various jurisdictions, in particular in Europe and the US, timely external state support for banks in distress (bail-out) has become less likely. We therefore believe that bank ratings cannot be boosted by the blanket expectation of extraordinary state support in those jurisdictions. However, in instances where specific government support is provided, we would assess the extent to which this translates in an improvement of the credit profile of the issuer.

Financial institutions not subject to resolution regimes. Our rating may incorporate the possibility of state support for banks domiciled in jurisdictions without resolution regimes or for issuers not subject to resolution if the systemic importance of those entities indicates a significant likelihood of extraordinary state support. The expectation of state support will be assessed considering the specific characteristics and systemic importance of the issuer, the characteristics of the legal and regulatory framework, including the record of government interventions in the sector, as well as the creditworthiness of the potential source of support.

Government-related entities. Government support will apply for entities qualifying as government-related entities (see our [Government-Related Rating Entities Methodology](#)).

4.9.4 Group rating approach

Some financial groups, for example mutual, cooperative or savings bank groups, have formalised solidarity mechanisms such as joint liability schemes, cross guarantees and/or institutional protection schemes.

Depending on the degree of cohesiveness and organisational structure these groups might produce consolidated or aggregated financial statements that allow for the analysis of the credit strength of the group and the assignment of a rating at group level.

Key indicators for the cohesiveness that inform our rating approach are, for example, regulatory recognition of the Institutional Protection Scheme, Resolution strategy, Supervisory approach to the group.

For assigning issuer ratings to members of such groups, we use the principles of our parental support analysis (4.9.2). We hence distinguish between members of the group that are seen as highly integrated and are rated via a top-down approach and those that are less integrated, leading to the application of the bottom-up approach.

4.9.5 Assessing the creditworthiness of the source of support

To determine whether the source of support is more creditworthy than the issuer, and therefore its ability to provide support, we may rely on different credit assessments, depending on the degree of control the supporting entity has over the issuer. Support may be provided by a single entity or jointly by several entities, which would require an estimate of their average credit strength where appropriate.

Figure 21: Guidelines for assessing the credit strength of parental support

		Rating approach	
		Top-down approach	Bottom-up approach
Ownership stake	50%-100%	Public or private rating by Scope	Public or private rating by Scope
	15%-50%		Credit estimate
	0 - 15%		Not performed

5. Ratings on debt instruments

While the issuer rating does not automatically equate to specific ratings on an individual security, it is the starting point for assigning credit ratings to various classes of liabilities. The ratings on individual securities normally reflect their ranking in the issuer's capital structure, with the most senior unsecured bonds typically rated in line with the issuer rating. Other considerations, such as the expectation of a different treatment of a liability class due to financial stability or political considerations may also inform the final rating, depending on the jurisdiction.

Figure 22: Typical notching structure for classes of bank debt securities

Typical notching structure for classes of bank debt securities	
Senior Secured debt (e.g. covered bonds)	X+1 to X+9
Deposits (preferred)	X+1
Issuer rating	X
Senior unsecured debt	X
Senior unsecured (subordinated) debt	X-1
Subordinated debt	X-2
Tier 2 debt	X-3
Additional Tier 1 debt	X-5

Deposit ratings are either aligned with the issuer rating or are rated one notch above. Specifically, deposits can be rated one notch above the issuer rating if they are considered to be more protected than senior unsecured debt. This is the case in countries with a depositor preference regime.

Senior unsecured debt ratings are aligned with the issuer rating. However, senior unsecured debt is rated one notch below the issuer rating if it is issued as statutorily non preferred, structurally subordinated, or otherwise subordinated to other senior unsecured debt.

Subordinated debt (excluding capital instruments) is rated two notches below the issuer rating.

Banks' capital structures typically also include deeper subordinated debt such as Tier 2 or Additional Tier 1 securities. Our approach to rating these securities reflects their role in strengthening banks' capital positions, including their loss absorption features. The methodology applies solely to Basel III/CRR-CRD compliant capital securities and does not apply to hybrid securities issued before the global financial crisis.

Tier 2 debt is rated three notches below the issuer rating, reflecting its loss absorbing features and junior status in the priority of claims. Tier 2 securities can be written down or converted into equity as part of early regulatory intervention or when an issuer has reached the point of non-viability (PONV). In a resolution bail-in scenario, Tier 2 securities are considered capital securities and rank below subordinated and senior unsecured debt.

When rating specific Tier 2 securities, there may be a further notching beyond the minimum three notches. This would be the case when we see additional risk factors that may be security-specific or issuer-specific. For example, the notching on a Tier 2 security may widen as an issuer's fundamentals deteriorate towards the PONV. Depending on the severity of the capital need and the amount of capital resources available, Tier 2 securities may be converted or written down.

Additional Tier 1 debt (AT1) is rated five notches below the issuer rating, reflecting its loss absorbing features and deeply subordinated status in the priority of claims. Specifically, investors are subject to coupon-cancellation risks in the following situations: i) the issuer lacks available distributable items; ii) the issuer has breached its combined buffer requirement (CBR); and iii) the issuer utilises its discretion not to pay. Further, AT1 securities may be written down or converted into equity when the issuer's common equity Tier 1 capital ratio breaches the specified trigger or when the issuer has reached the PONV.

When rating specific AT1 securities, there may be further notching beyond the minimum five notches. This may be the case when we see additional risk factors. These may be security- or issuer-specific, such as a narrower distance to the maximum distributable amount level compared to peers, the existence of high triggers for write-down, or material earnings volatility due to an issuer's higher risk business model.

Our ratings do not take into account whether AT1 securities will be called by the issuer, or the interest reset rate, although these are important considerations for investors.

Covered bonds are part of the general on-balance sheet funding of a bank, as further confirmed during the great financial crisis, when covered bonds managed to keep many banks afloat. Our rating approach for covered bonds therefore reflects our view that:

- i) The issuer rating is the fundamental anchor point for covered bond analysis.
- ii) The combination of legal and resolution frameworks is the most important element supporting the covered bond rating.
- iii) The cover pool represents a second recourse after a chain of events affecting the issuer. It is limited but provides additional security and stability to the covered bond rating.

The introduction of resolution/bail-in regimes in several markets, e.g. the Bank Recovery and Resolution Directive in the EU, has had significant implications that are reflected in our separate methodology for covered bond ratings. The former base case for covered bond analysis – in which the cover pool becomes the sole source of repayment upon the insolvency of the issuer – has become unlikely in a resolution regime. For more details, see our Covered Bond Rating Methodology⁴.

⁴ Available on www.scooperatings.com.

6. Other considerations

6.1 Bank holding companies/non-operating holding companies

For European financial institutions with a holding company structure, we consider the credit fundamentals of the entire group, i.e. on a consolidated group basis, when assigning an issuer rating to the holding company. This is in line with the regulatory approach followed in Europe and reflects the inherent connection and interdependence among group constituents.

Where the credit risk profile of the holding company is not essentially related to the performance of the consolidated group (e.g. due to material additional leverage or large equity investments), the rating of the holding company could be notched down relative to the group to reflect a potentially higher credit risk.

For debt issued by the various operating and non-operating entities of a group (including the holding company), this will be rated according to their ranking in the creditor hierarchy and within the context of the group's liability structure. For instance, we would typically rate senior debt issued by a holding company one notch below senior debt issued by the main operating bank as the holding company debt has a lower ranking in the context of the group's liability structure.

6.2 Branches issuing debt

We may assign issuer ratings to the local or foreign branches of a financial institution. A key attribute of a branch is that it has no separate legal existence compared to the reference issuer (generally identified as the head office).

A branch located in the same country of operation as the issuer's head office would be rated at the same level. The issuer rating of a foreign branch will be rated lower than the issuer rating of the reference issuer in case of specific country characteristics limiting the ability of the reference issuer to repay its debt obligations via foreign branches in a timely manner. We consider this unlikely for branches in investment-grade countries.

When we consider that there is no such limitation, we will assign debt ratings to debt instruments issued by branches of a financial institution without necessarily assigning an issuer rating to the branch.

6.3 Low issuer ratings

For banks subject to resolution with very low issuer ratings, typically in the B range and below, the likelihood of preferred senior debt (or equivalent) being bailed in would be higher. In these cases, we may notch down all senior unsecured debt ratings from the respective issuer rating to reflect the expectation of heightened bail-in risk for these securities.

6.4 Banks under regulatory intervention

For banks undergoing a resolution process or equivalent regulatory action, we would take a view on the likelihood of a successful intervention returning the bank to the market as a going concern, as well as the credit strength of the resulting institution, which would be captured by a new issuer rating level. Securities not bailed in as part of the process will be notched off the new issuer rating level.

6.5 Impact of coupon cancellation on AT1 ratings: no automatic downgrade

The terms and conditions of AT1 securities allow for coupon payment discretion. Consequently, an issuer who does not pay does not breach any regulatory or contractual obligations and would therefore not be considered in default.

In this scenario, we would evaluate the reasons for the coupon cancellation and assess whether this is a temporary or more permanent change in the issuer's ability to make distributions. If the reason for the coupon cancellation were a one-off event, which does not impair the issuer's future capacity to make payments, we may not change the rating on the AT1 security. More specifically, we will not automatically consider such an event to be a default.

However, if coupon cancellation were due to negative credit developments, such as a permanent deterioration in the issuer's earnings capacity or capital position that is unlikely to be promptly restored, this would lead to a downgrade of the issuer rating and, potentially, a concomitant widening of the notching gap for the AT1 security rating.

6.6 Impact of write-down or conversion on capital securities ratings

The terms of certain capital securities allow for write-down or conversion under certain conditions. In such a scenario, investors would experience a material loss on their principal investment. A write-down is also possible upon regulatory intervention.

If a capital security is converted into equity, we would downgrade to default status and withdraw the credit rating. Similarly, when a capital security is written down permanently, it ceases to exist. We would also downgrade to default status and withdraw the credit rating.

If a capital instrument is written down temporarily, we continue to rate it as it remains outstanding. The rating on the temporarily written-down security would be kept at D. We would then monitor and modify the rating as appropriate – for example, as the likelihood of coupon payment or write-up evolves.

6.7 Key limits and uncertainties of this methodology

This methodology is designed to be applicable to a broad range of financial institutions globally. We believe that the key drivers of credit risk for financial institutions, as described in **Section 2 Key components** are indeed universal. However, information availability and disclosures will inevitably vary across business models and jurisdictions, requiring Scope's analysts to apply judgement in identifying appropriate metrics when analysing individual credits. For example, disclosure heterogeneity limits our ability to quantitatively benchmark issuers on long term sustainability issues, our assessment having to rely on qualitative assessments to a greater extent.

Our aim is to capture all relevant credit drivers in the methodological framework, but we acknowledge the impossibility to foresee any potential source of risk ex-ante. For this reason, **Section 4.7 Additional factors** is designed to capture credit strengths and weaknesses that were not already captured or insufficiently captured earlier in the rating process.

Our ratings incorporate both the historical track record of an issuer and its expected financial performance. However, for some issuers, a long track record of audited financial accounts may not exist. For example, this is typically the case with newly established institutions. In these cases, our analysis will rely more heavily on projections and expectations. For issuers participating in the rating process, our assessments will be informed by management discussions or other confidential information. Neither past results nor management or Scope's analysts' expectations are guarantees of future performance.

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