Commodity Processing and Trading Companies

Rating Navigator Companion

Special Report

Navigator for Corporates is a graphical peer comparator that forms part of a series of similar tools used by Ind-Ra.

Information on the formal rating criteria that underlie Ind-Ra's corporate ratings can be found in Ind-Ra's Corporate Rating Methodology Master Criteria, dated 20 April 2020

Sector Navigators provide guidance for applying the concepts of the Corporate Rating Criteria to the issuers in the sector the Navigator covers. This Navigator Companion Report provides an additional description of the key rating factors for companies that are assessed using the Commodity Trading and Processing Navigator.

Rating horizon is defined as a period ranging between 5-10 years and remains independent of the tenure of debt obligations.

Analysts

Khushbu Lakhotia
+91 33 4030 2508
khushbu.lakhotia@indiaratings.co.in

Krishan Binani
+91 22 4035 6162
Krishan.binani@indiaratings.co.in

Sectors and Subsectors: This report presents the key peer-comparator elements observed or expected for companies that process and trade physical commodities. These companies refer to traders of commodities spanning from metals and oil to agricultural products. It excludes entities that wholly conduct speculative trading activities, but includes those that have invested down in the value chain and sell higher-value processed commodities such as edible oil or biodiesel.

Key Factors: The Sector Risk Profile defines and groups companies operating in the sector into a "natural rating territory" based on India Ratings and Research's (Ind-Ra) view of the inherent risk profile of the industry. Each company's overall risk profile generally does not stray away too far from this rating range. After assessing the management and corporate governance, the navigator examines four sector-specific factors for given rating levels. Finally, three financial profile factors help capture financial attributes commensurate with particular rating categories.

Sector Risk Profile

Rating Range: The risk profile of the commodity processing and trading sector ranges up to the 'BBB' rating category, reflecting the inherent cyclicality and volatility of the commodity markets where both lower volumes and volatility in prices are the key risk factors that can drag down profitability in absolute terms.

Company-specific traits indicate ratings potentially up to mid 'A' rating category, according to the categorisation of scale of operations, geographic and commodity diversification, risk management policies and asset ownership factors.

Sector-Specific Key Factors

Operational Scale: Key factors to assess relative scale include continuity of commodity supplies, supply chain and logistics infrastructure, and funds flow generation.

Diversification: This factor indicates an issuer's ability to withstand the operating earnings and cash flow volatility linked to inherently variable commodity markets. A broad geographic footprint and breadth of the commodity basket can mitigate this business risk.

Risk Management: This key factor evaluates the risk appetite and risk management systems of commodity processors.

Regulatory Risks: Regulatory risks are relevant as many commodities including cotton, jute, etc. are impacted by government regulations that increase the volatility and uncertainty associated of earnings.

Financial Profile Key Factors

Profitability: The analysis focuses on the stability of earnings and cash flows from the issuer's major business lines. Sustainable operating cash flow supports the issuer's ability to service debt and finance its operations and capital expansion without reliance on external funding.

Financial Structure and Flexibility: These factors use an array of predominantly cash-based metrics to measure the level of capitalisation of an issuer and other flexibility measures such as liquidity and exposure to foreign-exchange movements.

The financial profile factors, in this case, are measured up to the 'A' rating category. Ind-Ra's analysis includes measures adjusted for readily marketable inventories (RMI), to factor in the debt availed to fund these commodity purchases.

Limitations

This report outlines the indicative factors observed or extrapolated for rated issuers. Ratio levels refer to the mid-point of a through-the-cycle range, and actual observations are likely to vary from these. Certain sub-sectors may contain a small number of observations overall, or at any given rating category. Where no observations exist, guidelines for a category are extrapolated based on Ind-Ra's judgment. The relative importance of factors will vary substantially over time both for a given issuer and between issuers, based on the significance agreed upon by the rating committee. The factors give a high-level overview and are neither exhaustive in scope nor uniformly applicable. Additional factors will influence ratings particularly where group relationships constrain or enhance a rating level.

Sector Risk Profile

The sector risk profile generally reaches up to the 'BBB' rating category reflecting the cyclicality and seasonality of certain commodities, which can be caused by, among other things, political and economic shocks and episodes of agricultural disease and droughts. This is compounded by the inherent volatility in commodity prices as well as supply and demand dynamics which participants are not in control of, causing substantial swings in the profits and liquidity requirements through economic and commodity cycles.

The relatively high sector risk profile is further underpinned by trading risks. For example, profit concentration on one/two quarters around the harvesting period also adds to a heightened risk profile mainly for smaller, less diversified agricultural commodity processors.

Commodity processors and traders with a worldwide presence can strengthen their sourcing ability, or improve distribution through a presence across the value chain while helping commodity trading volumes and arbitrage opportunities. Also, the companies that trade and process physical commodities through their origination, processing and transportation operations are increasingly important as they satisfy the demands of economic growth and worldwide population growth. In a developing economy such as India, demand for commodities can vary significantly, depending on the trend in industrial output and the nature of the commodity.

Companies that have substantial scale, geographical reach, and demonstrate constant demand would be placed in higher investment grades. Additionally, companies having meaningful processing capacities and commodity diversification, lending greater stability, can attain the highest rating consistent with the overall sector risk profile.

Higher Investment-grade Commodity Processing and Trading Companies

- Substantial trading and processing capacities across regions
- High diversity, lending greater stability in trading volumes
- Fully funded working capital requirements
- Substantial hedging of price risk

Applicable Criteria

Corporate Rating Methodology Master Criteria (April 2020)

Lower Investment Grade/Speculative-grade Commodity Processing and Trading Companies

- Small firms with limited geographic reach and product mix
- Majority of revenues generated through trading activity

Management and Corporate Governance

See Appendix I

Sector-Specific Key Factors

Operational Scale

Operational Scope and Access to Long-Term Supply

While many firms can trade commodities, the ability to provide procurement, trading, storage, processing and transportation of multiple commodities on a large scale globally is present in just a few. These abilities broaden a company's opportunity to capture value through additional processing, local intelligence about commodity logistics and substantially increase its number of potential customers. Meaningful market shares in specific commodities along with a highly diversified product offering are typically associated with high ratings, potentially exceeding the average sector risk profile. Ind-Ra also considers the size of commodity processor and traders, the extent of their logistical capabilities, and their access to uninterrupted commodity supplies.

Infrastructure Ownership and Access

Companies with owned transportation facilities have a better control over delivery timelines than ones reliant on external transport, while owned storage facilities provide the flexibility of scaling up inventory to meet increased orders. However, infrastructure ownership will generally be a positive only for companies with high and stable volumes, as these attributes require substantial capital expenditure.

Operational Structure

Companies having investments in parts of the value chain through subsidiaries/JVs/minority stakes have an added advantage in terms of sourcing or selling their products.

Figure 1

Operational Scale: Sub-Factors

Rating category	Operational scope	Size (annual FFO)	Access to long-term supply	Infrastructure ownership and access	Operational structure
IND A	Ability to procure, trade, store and transport diverse commodities on a global scale or across India along with substantial processing capability	>INR700 million	Reliable access to long-term supply of all relevant commodities through sourcing arrangements	Storage and transportation facilities owned by the company (or subsidiaries)	Presence in value chain through majority of wholly owned subsidiaries
IND BBB	Ability to procure, trade, store and transport commodities in multiple regions in India along with some processing capability or presence in two-three commodities	INR150 million-600 million	Adequate access to input supply with no significant (or only occasional) evidence of disruption/	Long-term contract for storage and transportation facilities	Presence of JVs or significant minority stakes across value chain
IND BB and below	Limited trading ability with majority of revenue derived from a single commodity and location. No/negligible processing ability	Below INR150 million	Frequent supply disruption/volatility	Short-term arrangement	Not present in other parts of the value chain

Source: Ind-Ra

Diversification

Operating earnings and cash flow volatility for commodity processors and traders can be somewhat mitigated by geographic and product-line diversification. Ind-Ra analyses the key geographical markets and the depth and breadth of the portfolio of commodities traded and processed. Special attention is paid to the relationships between commodities, particularly unanticipated correlations and changes in correlations. Ind-Ra seeks to determine if a company is dependent on one or two key products or segments for the bulk of its earnings and to what degree, if any, those earnings are correlated. Strong entities in the sector are often those that achieve strong earnings from multiple sources across geographies.

Higher investment grade-rated entities typically engage in the trading and processing activities of commodities that exhibit strong consumption patterns from a variety of end-users. Ind-Ra seeks to determine how widely dispersed the demand is for a company's products recognising that the demand for certain commodities in specific markets can vary rapidly with changing economic conditions, government policies, evolving preferences, health concerns and inflation.

Figure 2
Diversification: Sub-factors

Rating category	Geographic diversification	Commodity diversification
IND A	National presence	Broadly diversified by commodity
IND BBB	Moderate geographical diversification or strong competitive operating position within its region	Moderate diversification by commodity
IND BB and below	Concentrated in one region	Majorly focused on one commodity/ or two correlated commodities

Source: Ind-Ra

Risk Management

Ind-Ra's assessment of risk management evaluates a firm's risk appetite as well as the adequacy and robustness of its systems that allows management to identify, measure, manage, and monitor risks. The presence and effectiveness of the financial risk policies can be measured through the extent of exposure to price risk, counterparty risk, hedging policy and extent of inventory fluctuation. However, Ind-Ra's rating process does not involve an audit of these risk management systems or practices.

Exposure to Commodity Price Fluctuations

The consistency and extent of hedging of commodity exposure and the instruments used for the purpose will be used to assess the company's commodity hedging mechanism of the company. A company that does back-to-back procurement would not be exposed to price volatility risk and thus the hedging policy sub-factor would not be applicable to it.

Inventory Volatility

Inventory losses may arise due to sharp commodity price movements or speculative inventory holding. Frequent fluctuations in inventory holding levels (except where it corresponds to concluded contractual sales) indicate speculative activities and will be considered as negative for ratings.

Counterparty Risk

The extent of counterparty risk will depend on the credit worthiness of the counterparty and the quantum/period of exposure. The counterparty risk can therefore be assessed as a combination of ratio of sales made by the company on payment basis, credit period offered, bad debts suffered by the company and credit worthiness of the counterparty.

Financial Risk Policy

Key Areas Include:

- Independence and effectiveness of the risk management function
- Whether all risks are managed centrally (including centralised cash management) or can be easily compiled to establish an enterprise-wide view of risk
- The procedures and limits in place, who sets these limits, and the degree to which these procedures and limits are adhered to
- Reporting and frequency of deviations
- Risk management and reporting procedures

Figure 3
Risk Management: Sub-factors

Rating category	Exposure to commodity price fluctuations	Extent of volatility in inventory holding	Counterparty risk	Financial risk policy
IND A	Back-to-back contracts largely insulating the company from both volume and price risk or inventory valuation volatility risk up to 1 day or commodity exposures fully hedged throughout through vanilla derivatives	Consistent inventory holding period during the past five years	Low	Robust risk management policies and sound implementation
IND BBB	High proportion of back-to-back contracts and low inventory valuation volatility risk or consistent and significant hedging through vanilla derivatives with procedures and risk limits in place	Limited volatility in inventory holding period	Moderate	Lack of a documented risk policy
IND BB and below	High exposure to price volatility/ limited/inconsistent hedging or high exposure to complex derivatives	Significant fluctuations in inventory holding period	High	Lack of a documented risk policy and/or inadequate/ inefficient risk management

Source: Ind-Ra

Regulatory Risk

Regulatory risks are relevant as the performance of companies in many commodities is impacted due to government regulations pertaining to pricing as well as quotas, ceiling on inventory holding, etc. These regulations may be applicable for a temporary period or for a long-period with periodic revisions. The possibility of regulatory issues impacting an entity's business would be the key factor in determining the regulatory risk.

Figure 4
Regulatory Risk

Rating category	Regulatory risks
IND A	Low
IND BBB	Moderate
IND BB and below	High

Source: Ind-Ra

Financial Key Factors

The quantitative aspect of Ind-Ra's corporate ratings focuses on an issuer's financial profile and its ability to service its obligations using a combination of internal and external resources.

The sustainability of these credit-protection measures is evaluated over a period of time, using both actual historical numbers but more importantly Ind-Ra's forecasts to determine the strength of an issuer's debt servicing capacity and funding ability. Ind-Ra does not rate based on a temporary phenomenon such as a sharp increase or decrease in volumes or prices. Instead, Ind-Ra would establish a profile beyond such volatility, assuming that the severity of this volatility does not trigger a rating action on the downside, for example, prompting a liquidity event or covenant breaches.

Financial metrics can alleviate only some of the pressures from the Sector Risk Profile and Business Profile characteristics, and do not enable the company to completely insulate itself. Conversely, a company with a strong business profile may be burdened by high leverage, which may exert strong downward pressure on its rating levels.

The Financial Key Factors are

- Profitability, which provides a bridge between the qualitative Business Profile Factors and the mainly quantitative Financial Key Factors, is normally strongly correlated with the attractiveness of the sector and the company's market position in that sector.
- Financial Structure - essentially the level of leverage on the company's balance sheet
- Financial Flexibility includes other important aspects such as Liquidity, FX Exposure and Financial Discipline.

The definition of the credit metrics is included in the *Corporate Rating Methodology* Criteria Report, dated 20 April 2020 and the Special Report *Cash Flow Measures in corporate Analysis* dated 4 April 2016.

Readily Marketable Inventory Adjustments

In addition to evaluating traditional credit measures as discussed in Ind-Ra's *Corporate Rating Methodology,* Ind-Ra evaluates leverage ratios and interest coverage ratios that exclude the debt and interest costs used to finance RMI with reasonable assurance that inventories are protected against price risk. Although hedging allows companies to protect RMI against price risk, there is still basis risk, as spot and future prices may not converge perfectly on the expiration date.

RMI credit varies (typically within a range of 25%-75%) based on the ready marketability of the commodity under consideration. The haircuts are to factor in the pricing and timing of sale; counterparty risk is assessed separately under the risk management function. Any obsolete inventory will be deducted from the inventory before arriving at eligible RMI.

Figure 5 shows a hypothetical example which illustrates the mechanics of the RMI adjustments and which compares the consolidated (or unadjusted) ratios with the equivalent RMI-adjusted metrics. To adjust leverage ratios, the total debt is reduced by the amount used to finance RMI that is protected against price risk. For EBITDAR-to-interest plus rents and FFO fixed charge cover ratios, the gross interest expense on debt incurred to finance RMI is subtracted from the numerator and the denominator, EBITDAR/FFO and total interest expense, respectively. The interest expense for RMI for this calculation is reclassified as an operating expense.

RMI Definition

Headline leverage can be high for commodity companies, yet part of the debt could be incurred to fund inventories that are liquid and readily marketable commodities. Ind-Ra quantifies readily marketable inventory (RMI) and nets a percentage of this against debt to profile the underlying leverage of the group. The remaining debt often funds illiquid investment stakes rather than RMI. Ind-Ra also makes adjustments to income statement figures.

RMI Eligibility

Below is a non-exhaustive list of traits which Ind-Ra considers to regard inventories as RMI:

- ascertainable price via international pricing mechanisms;
- widely availability and liquid markets;
- ability to hedge via forward sales to end-customers or short positions via established commodity exchanges and OTC markets;
- identifiable and appropriately valued in financial accounts;
- stable and/or predictable end-user demand;
- not short-term perishable goods.

Typical examples of RMI include:

- gold, silver
- iron ore; non-ferrous metals
- coal
- steel
- cotton

Figure 5

RMI-Adjusted Credit Ratios: Worked Example

Assumptions	(INR million)	Consolidated metrics	(x)
Net sales	80,000	Lease-adjusted total debt/EBITDAR	3.60
EBITDAR	4,000	Lease-adjusted net debt/EBITDAR	2.85
EBITDAR less interest on RMI	3,700	FFO adjusted net leverage.	2.92
FFO	3,000	EBITDAR/gross interest expense+ rents.	4.44
FFO less interest on RMI	2,700	FFO fixed charge cover.	4.33
RMI[a]	6,000		
Lease-adjusted debt	14,400	**RMI-adjusted metrics**	
Cash	3,000	Lease-adjusted gross debt less RMI/EBITDAR less interest on RMI	2.27
Lease-adjusted gross debt less RMI	8,400	Lease-adjusted net debt less RMI/EBITDAR less interest on RMI	1.46
Lease-adjusted net debt less RMI	5,400	Lease-adjusted gross debt less RMI/FFO less interest on RMI plus gross interest paid plus rents	2.33
Gross interest expense/Paid	600	EBITDAR less interest on RMI/gross interest expense plus rents less Interest on RMI	6.17
Rents	300	FFO less Interest on RMI plus gross interest paid plus rents/gross interest paid plus rents less interest on RMI	6.00
Interest rate (%)	5	—	—
Interest on RMI	300	—	—

[a] Eligible inventory
Source: Ind-Ra

Profitability

Ind-Ra prefers to use operating EBITDAR to gross profit (in percent terms) as a measure of a company's underlying profitability. given thin profit margins in the sector. Profit margins, even after adjusting for RMI and the related portion of interest expenses as COGS, are narrow in this sector. Gross profit is a better reflection of operating strength because turnover is subject to inherent commodity price variability.

Ind-Ra also examines the trends in cash flows via fund flow from operations (FFO) and free cash flow (FCF) metrics. FCF, defined as cash flow from operations (CFO) less capital expenditure and dividends, is highly volatile for commodity traders and processors as working-capital needs expand and contract with increases and decreases in commodity prices and volumes processed. The FFO measure serves to provide information, respectively, on cash profits sans the variability resulting from ever-changing working capital requirements. If a firm is at a growth stage, cash flow is constantly reinvested in the business via capex or M&A, resulting in continuing negative FCF. Nonetheless, during non-expansionary periods, Ind-Ra expects the higher-rated firms to be FCF positive.

For companies with positive FCF, Ind-Ra seeks to understand how this excess cash flow may be deployed — whether for acquisitions, share repurchases or equity bonus schemes, debt reduction or held for reinvestment in the business. Higher-rated firms in the industry typically carry excess cash and cash equivalents balances to supplement liquidity. For companies with negative FCF, Ind-Ra enquires how the cash flow deficit might be funded — by new borrowing, an equity issuance or asset sales.

Given the importance of stability of profit generation, a qualitative sub-factor on volatility of profitability has been included as well.

Figure 6

Profitability: Sub-Factors

Rating category	FFO margin	FCF margin	EBITDAR/gross profit (RMI-Adjusted)	Volatility of profitability
IND A	3.0%	1.0%	65%	Lower volatility of profits than industry average.
IND BBB	2.0%	Positive	50%	Volatility of profits in line with industry average.
IND BB and below	1.0%	Negative FCF margin	35%	Higher volatility of profits than industry average.

Source: Ind-Ra

Financial Structure

Ind-Ra bases its analysis on both net and gross leverage ratios, including a mix of FFO-based and EBITDA-based metrics, which are typically close to each other. Gross leverage is a key ratio, as cash can dwindle rapidly when companies are in financial stress, for example due to substantial cash outflows from working capital. However, net leverage is also relevant for companies holding a high level of cash for prudential reasons beyond what is needed for operational purposes.

Asset-light traders normally generate thin margins and raise debt mainly to fund working capital. Hence, the relation of debt to working capital is often used as an auxiliary measure to assess their financial position.

Figure 7

Financial Structure: Sub-Factors

Rating category	RMI, lease adjusted FFO net leverage	RMI, lease adjusted gross debt/EBITDAR	Gross debt/(cash + working capital)	TOL/EBITDA
IND A	2.0x	2.5x	0.5x	4.5x
IND BBB	3.0x	3x	0.75x	5.5x
IND BB and below	4.5x	4.0x	1x	6.5x

Source: Ind-Ra

Financial Flexibility

Financial flexibility allows an issuer to meet its debt service obligations and manage periods of volatility without eroding credit quality.

Financial Discipline

The more conservatively capitalised an issuer, the greater its financial flexibility. In general, a commitment to maintaining debt within a certain range allows an issuer to cope better with the effect of unexpected events. This is reflected in the financial discipline sub-factor.

Liquidity

Other factors that contribute to financial flexibility are the ability to revise plans for capital spending, strong banking relationships, the degree of access to a range of debt and equity markets, committed, long-dated bank lines and the proportion of short-term debt in the capital structure. These issues are incorporated in the liquidity sub-factor. Once liquidity reaches a certain level, it is generally not a source of rating differentiation, hence the identical definition for the 'IND A' and 'IND AA' rating categories.

FFO Fixed Charge Coverage and EBITDAR Gross Interest Coverage

Fixed charge coverage ratios are a central measure of the financial flexibility of an entity, which compares the operational cash-generating ability of an issuer (after tax) to its financing costs. Many factors influence coverage ratios – including general funding costs, the mix of fixed-rate versus floating-rate funding, the use of zero-coupon debt, and so on. For this reason, the coverage ratios should be considered alongside the appropriate leverage ratios.

FX Exposure

Foreign exchange exposure can also impact financial flexibility. Some companies may have a natural currency hedge or an acceptable unhedged exposure in pegged currency regimes, given the type of products they sell and their own cost base. For other companies, there may be a material mismatch between the currency borrowed and the currency in which they have internal cash resources. Where there is a mismatch, Ind-Ra will assess the company's approach and management of that exposure.

Debt-Equity

Debt-equity ratio is often an indicator of an entity's flexibility to borrow from the banking system.

As financial discipline, liquidity and FX exposure are the factors common to all sectors and not specific to commodity processing and trading companies they have been defined for the entire rating scale up to the IND AA rating category and have not been limited to the IND A rating category like the sector-specific factors.

Figure 8

Financial Flexibility: Sub-Factors

Mid-Points	Financial discipline	Liquidity	FFO fixed charge cover (x)	EBITDAR/ (gross interest + rents) (x)	FX exposure	Debt-equity ratio (x)
IND AA	Publicly announced conservative financial policy; Track record of strict compliance	Very comfortable liquidity with no need to use external funding in the next 24 months or more; Well-spread maturity schedule of debt; diversified sources of funding; one-year liquidity ratio above 1.25x	na	na	Negligible unhedged forex exposure	0.3
IND A	Clear commitment to maintain a conservative policy with only modest deviations allowed	Very comfortable liquidity; well-spread debt maturity schedule; diversified sources of funding; one-year liquidity ratio above 1.25x	4.0	3.5	Unhedged forex exposure within 10% of EBITDA	0.6
IND BBB	Financial policies less conservative than peers' but generally applied consistently	One-year liquidity ratio above 1.25x; well-spread maturity schedule of debt but funding may be less diversified	3.0	2.75	Unhedged forex exposure within 20% of EBITDA	1.0
IND BB	Financial policies in place but flexibility in applying it could lead it to temporarily exceed downgrade guidelines	Liquidity ratio around 1.0x; less smooth debt maturity or concentrated funding	2.5	2.25	Unhedged forex exposure within 40% of EBITDA	1.4
IND B	No financial policy or track record of ignoring it; opportunistic behaviour	Liquidity ratio below 1x; Overly reliant on one funding source	na	na	Unhedged forex exposure higher than 40% of EBITDA.	>1.4

Note: Liquidity score is defined as: available cash + undrawn portion of committed facilities + free cash flow (before interest)/debt maturities + interest expense
Source: Ind-Ra

Appendix I: Management and Corporate Governance

Figure 9

Management and Corporate Governance: Sub-Factors

Category	Management strategy	Governance structure	Group structure	Financial transparency
IND AA	Consistent and robust strategy and very strong track record in implementation	No record of governance failing; strong management team, experienced board with presence of independent directors and functional heads	Transparent group structure; related party transactions, if any, are insignificant and have an economic rationale	High-quality and timely financial reporting
IND A	Coherent strategy and good track record in implementation	Good governance track record; experienced board exercising effective check and balances	Group structure shows some complexity but mitigated by transparent reporting; related party transactions have an economic rationale	Good quality and timely financial reporting
IND BBB	Strategy may include opportunistic/aggressive elements but soundly implemented	Adequate governance track record	Some group complexity; no significant related-party transactions without appropriate economic rationale	Average financial reporting without significant failing
IND BB	Strategy lacks consistency/coherence and/or weakness in implementation	Inadequate governance structure; very high key-man risk	Complex group structure or non-transparent ownership structure; presence of significant related-party transactions	Financial reporting is appropriate but with some failings (e.g., lack of interim or segment analysis)
IND B	Lack of adequate strategic planning and implementation	Poor governance structure; significant instances of governance failing	Highly complex group with large and opaque related-party transactions or opaque ownership structure	Defective financial reporting; aggressive accounting policies

Source: Ind-Ra

Management and Corporate Governance

The company-specific management and corporate governance factor is composed of four sub-factors: Management Strategy, Corporate Governance, Group Structure and Financial Transparency.

Sub-Factors

Management Strategy

Ind-Ra considers management‘s track record in terms of its ability to create a healthy business mix, maintain operating efficiency, and strengthen its market position. Financial performance over time notably provides a useful measure of the management’s ability to execute its operational and financial strategies.

Corporate goals are evaluated centring upon track record and future strategy. Risk tolerance and consistency are important elements in the assessment. The historical mode of financing acquisitions and internal expansion provides insight into management‘s risk tolerance.

Governance Structure, Group Structure and Financial Transparency

The other three sub-factors address different aspects of the general issue of corporate governance. The purpose of addressing governance structure is to assess the w ay effective pow er w ithin an issuer is distributed.

Elements considered are notably the presence of effective controls for ensuring sound policies, an effective and independent board of directors, succession plan, talent bench, management compensation, related-party transactions, integrity of the accounting and audit process and key-man risk.

Corporate governance operates as an asymmetric consideration. Where it is deemed adequate or strong, it typically has little or no impact on the issuer's credit ratings, i.e. it is not an incremental positive in the rating calculus. Where a deficiency, which may diminish lenders' protection, is observed, the consideration may have a negative impact on the rating assigned. Ind-Ra's approach to evaluating corporate governance is described in the Criteria Report *Evaluating Corporate Governance* dated 21 January 2020.

The corporate governance sub-factor focuses on the structural aspects of governance, in particular board of directors' characteristics.

Group structure and financial transparency assess how easy it is for investors to be in a position to assess an issuer's financial condition and fundamental risks. These aspects are somewhat linked to corporate governance as high-quality and timely financial reporting is generally considered by Ind-Ra to be indicative of robust governance. Likewise, publishing inaccurate or misleading accounting statements intentionally is symptomatic of deep flaws in an issuer's governance framework. The public exposure of techniques that subvert the spirit of accepted accounting standards or, worse yet, are designed to mask fraudulent activity can undermine investor confidence.

ALL CREDIT RATINGS ASSIGNED BY INDIA RATINGS ARE SUBJECT TO CERTAIN LIMITATIONS AND DISCLAIMERS. PLEASE READ THESE LIMITATIONS AND DISCLAIMERS BY FOLLOWING THIS LINK: HTTPS://WWW.INDIARATINGS.CO.IN/RATING-DEFINITIONS. IN ADDITION, RATING DEFINITIONS AND THE TERMS OF USE OF SUCH RATINGS ARE AVAILABLE ON THE AGENCY'S PUBLIC WEBSITE WWW.INDIARATINGS.CO.IN. PUBLISHED RATINGS, CRITERIA, AND METHODOLOGIES ARE AVAILABLE FROM THIS SITE AT ALL TIMES. INDIA RATINGS' CODE OF CONDUCT, CONFIDENTIALITY, CONFLICTS OF INTEREST, AFFILIATE FIREWALL, COMPLIANCE, AND OTHER RELEVANT POLICIES AND PROCEDURES ARE ALSO AVAILABLE FROM THE CODE OF CONDUCT SECTION OF THIS SITE.

Copyright © 2020 by Fitch Ratings, Inc., Fitch Ratings, Ltd. and its subsidiaries. 33 Whitehall Street, NY, NY 10004.Telephone: 1-800-753-4824, (212) 908-0500. Fax: (212) 480-4435. Reproduction or retransmission in whole or in part is prohibited except by permission. All rights reserved. In issuing and maintaining its ratings, India Ratings and Research (Ind-Ra) relies on factual information it receives from issuers and underwriters and from other sources Ind-Ra believes to be credible. Ind-Ra conducts a reasonable investigation of the factual information relied upon by it in accordance with its ratings methodology, and obtains reasonable verification of that information from independent sources, to the extent such sources are available for a given security or in a given jurisdiction. The manner of Ind-Ra's factual investigation and the scope of the third-party verification it obtains will vary depending on the nature of the rated security and its issuer, the requirements and practices in the jurisdiction in which the rated security is offered and sold and/or the issuer is located, the availability and nature of relevant public information, access to the management of the issuer and its advisers, the availability of pre-existing third-party verifications such as audit reports, agreed-upon procedures letters, appraisals, actuarial reports, engineering reports, legal opinions and other reports provided by third parties, the availability of independent and competent third-party verification sources with respect to the particular security or in the particular jurisdiction of the issuer, and a variety of other factors. Users of Ind-Ra's ratings should understand that neither an enhanced factual investigation nor any third-party verification can ensure that all of the information Ind-Ra relies on in connection with a rating will be accurate and complete. Ultimately, the issuer and its advisers are responsible for the accuracy of the information they provide to Ind-Ra and to the market in offering documents and other reports. In issuing its ratings Ind-Ra must rely on the work of experts, including independent auditors with respect to financial statements and attorneys with respect to legal and tax matters. Further, ratings are inherently forward-looking and embody assumptions and predictions about future events that by their nature cannot be verified as facts. As a result, despite any verification of current facts, ratings can be affected by future events or conditions that were not anticipated at the time a rating was issued or affirmed.

The information in this report is provided "as is" without any representation or warranty of any kind. An Ind-Ra rating is an opinion as to the creditworthiness of a security. This opinion is based on established criteria and methodologies that Ind-Ra is continuously evaluating and updating. Therefore, ratings are the collective work product of Ind-Ra and no individual, or group of individuals, is solely responsible for a rating. The rating does not address the risk of loss due to risks other than credit risk, unless such risk is specifically mentioned. Ind-Ra is not engaged in the offer or sale of any security. All Ind-Ra reports have shared authorship. Individuals identified in a Ind-Ra report were involved in, but are not solely responsible for, the opinions stated therein. The individuals are named for contact purposes only. A report providing a Ind-Ra rating is neither a prospectus nor a substitute for the information assembled, verified and presented to investors by the issuer and its agents in connection with the sale of the securities. Ratings may be changed or withdrawn at anytime for any reason in the sole discretion of Ind-Ra. Ind-Ra does not provide investment advice of any sort. Ratings are not a recommendation to buy, sell, or hold any security. Ratings do not comment on the adequacy of market price, the suitability of any security for a particular investor, or the tax-exempt nature or taxability of payments made in respect to any security. Ind-Ra receives fees from issuers, insurers, guarantors, other obligors, and underwriters for rating securities. Such fees generally vary from US$1,000 to US$750,000 (or the applicable currency equivalent) per issue. In certain cases, Ind-Ra will rate all or a number of issues issued by a particular issuer, or insured or guaranteed by a particular insurer or guarantor, for a single annual fee. Such fees are expected to vary from US$10,000 to US$1,500,000 (or the applicable currency equivalent). The assignment, publication, or dissemination of a rating by Ind-Ra shall not constitute a consent by Ind-Ra to use its name as an expert in connection with any registration statement filed under the United States securities laws, the Financial Services and Markets Act 2000 of the United Kingdom, or the securities laws of any particular jurisdiction. Due to the relative efficiency of electronic publishing and distribution, Ind-Ra research may be available to electronic subscribers up to three days earlier than to print subscribers.