

Policy on Default Recognition

[Issued in August 2023]

1. Background

CARE Ratings Nepal Limited's (CARE Ratings) ratings are an opinion on the relative ability and willingness of an issuer to repay debt (including interest and other obligations) in a timely manner. CARE Ratings follows a concept of 'one-day-one rupee' delay for default recognition in respect of all debt instruments from market (Bonds, Debentures, Commercial Papers etc.). CARE Ratings' default recognition policy in respect of ratings for instruments with a pre-determined repayment schedule, 'one-day-one-rupee' delay is considered, whereas for facilities with no pre-determined repayment schedule, a 30 day 'grace period' is considered.

This document explains in detail the instrument-wise definition of default followed by CARE Ratings, and the criteria for treatment of defaults while assigning initial ratings and review of outstanding ratings.

2. Instrument-wise definition of default followed by CARE Ratings

Facilities	Definition of Default
<i>Fund-based facilities & Facilities with pre-defined repayment schedule #</i>	
Term Loan	A delay of more than 30 days even of 1 rupee (of principal or interest) from the scheduled repayment date.
Working Capital Term Loan	
Working Capital Demand Loan (WCDL)	
Debentures/Bonds	A delay of 1 day even of 1 rupee (of principal or interest) from the scheduled repayment date.
Certificate of Deposits (CD)/ Fixed Deposits (FD)	
Commercial Paper	
Packing Credit (pre-shipment credit)	Overdue/unpaid for more than 30 days.
Buyer's Credit	Continuously overdrawn for more than 30 days.
Bill Purchase/ Bill discounting/ Foreign bill discounting /Negotiation (BP/BD/FBP/FBDN)	Overdue/unpaid for more than 30 days.
<i>Fund-based facilities & No Pre-Defined Repayment Schedule</i>	
Cash Credit	Continuously overdrawn for more than 30 days.
Overdraft	Continuously overdrawn for more than 30 days.
<i>Non fund-based facilities</i>	
Letter of credit (LC)	Overdue for more than 30 days from the day of devolvement.
Bank Guarantee (BG) (Performance/ Financial)	Amount remaining unpaid from 30 days from invocation of the facility
Other Scenarios	
When rated instrument is rescheduled.	Non-servicing of the debt (principal as well as interest) as per the existing repayment terms in anticipation of a favourable response from the banks of accepting their restructuring application/ proposal shall be considered as a default.

Facilities	Definition of Default
	Rescheduling of the debt instrument by the lenders prior to the due date of payment will not be treated as default, unless the same is done to avoid default or bankruptcy. OR Rescheduling of the debt instrument allowed by central bank as a policy without additional provisioning and categorization as Non-Performing Assets will not be treated as a default.
When instrument is backed by a guarantee is in default	CARE Ratings rates instruments backed by the guarantor on the strength of the guarantor in case the entire debt is backed by a guarantee. The recognition of a default on such instrument is based on the guarantor becoming aware of the obligation to pay on invocation and his ability to make the payment within the payment within the stipulated time once the guarantee is invoked. Hence, post invocation of the guarantee by the trustee/banker/investor, failure by the guarantor in servicing the debt obligation (principal as well as interest) of issuer within the stipulated time shall be construed as default
Curing Period	90 Days – for Default to Speculative Grade Generally, 365 Days [@] for Default to Investment Grade

#If the sanctioned terms allow grace period for payment after due date, CARE Ratings also considers the due date considering the grace period

@ CARE Ratings may deviate from the stipulated curing period for upgrading rating to investment grade in certain situations (after 90 days), where it believes that the underlying credit profile of the entity has altered significantly following specific events like change in ownership and significant infusion of long-term funds or certain forms of refinancing which lead to complete replacement of the facilities/instruments in default.

3. Treatment of default in Initial Ratings

In case of **initial ratings**, a rating of 'CARE-NP D' is assigned in case of ongoing delays in debt repayment of the rated instrument. In case of instances of past delays in repayment of any debt instrument, the following four dimensions of delay are analysed:

- the extent of delay (number of days of delay),
- frequency of delay (number of times the delay occurred in the past one year),
- severity of delay (amount not paid vis-à-vis amount due) and
- status of an ongoing delay (facility in default).

A non-default rating would not be assigned if the curing period post an earlier default on any instrument of similar seniority has not lapsed. For subordinate instruments and structured instruments, curing period will apply on instrument level.

Rating Action

- In case of (d) above, a rating of 'CARE-NP D' is assigned if the delay is in respect of the rated instrument.

- In other cases, the rating would take into account the extent, frequency and severity of the delay as also how recent the delay has occurred. A default free track record of 90 days is required to assign ratings in the speculative grade other than CARE-NP D [i.e. from CARE-NP BB+ to CARE-NP C- (long term rating) and CARE-NP A4+ or CARE-NP A4 (short term rating)], and generally a default free track record of 365 days is required to assign an investment grade rating.

4. Treatment of default in review of outstanding ratings

Whenever CARE Ratings becomes aware of any missed payment, the rating is brought down to 'CARE-NP D' and in case the delay has been cured, the rating can be moved within the sub-investment category based on extent, frequency, severity and the date of occurrence of delay. A default free track record of 90 days is required to move an instrument/facility's rating from CARE-NP D to other ratings in the speculative grade and generally a default free track record of 365 days is required to move an instrument/facility's rating from CARE-NP D to investment grade.

5. Treatment of default in case of hybrid instrument ratings

The terms of the hybrid instrument may allow deferment of principal and / or interest payment in case of invocations of certain pre agreed clauses. Any delay in payment of interest/principal (as the case may be) following the invocation of the lock-in clause, is considered an event of default as per CARE Ratings' definition of default and as such, these instruments may exhibit a somewhat sharper migration of the rating compared with conventional subordinated debt instruments.

6. Treatment of default in case of technical delay / dispute

CARE Ratings examines the reasons for default from the rated entity, duly corroborated by the investor / lender. If as per CARE Ratings' assessment, the delay was not caused by liquidity stress at the issuer level but due to some technical problem, then default is not recognised. However, based on the assessment, severity and frequency of such incidences, the credit rating of the issuer may be reviewed.

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About Us:

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