

# The Role of Enterprise Risk Management in S&P Ratings of Non-Financial Companies

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Director

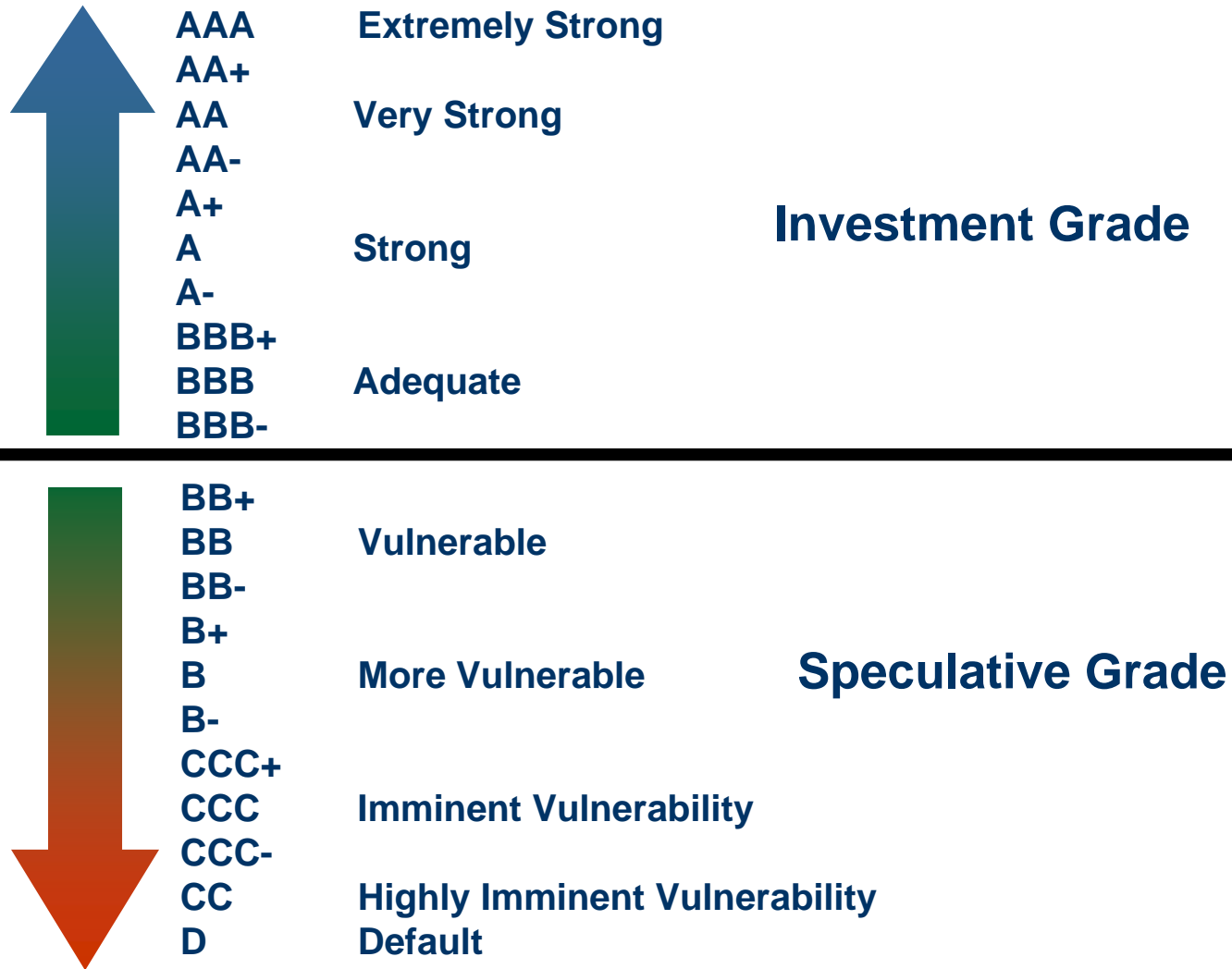
Corporate & Infrastructure Ratings Europe

## **Credit Ratings Provide Investors, Debt Issuers, Traders and Counterparties...**

- An Independent, Objective and Forward Looking Opinion of Creditworthiness***
- A Global Benchmark for Investors to Compare Credit Risk Among Peers***

# Standard & Poor's Credit Ratings Scale

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# S&P Corporate Ratings Methodology

Business	Financial					
	Minimal	Modest	Intermediate	Significant	Aggressive	Highly Leveraged
Excellent	AAA	AA	A	A-	BBB	--
Strong	AA	A	A-	BBB	BB	BB-
Satisfactory	A-	BBB+	BBB	BB+	BB-	B+
Fair	--	BBB-	BB+	BB	BB-	B
Weak	--	--	BB	BB-	B+	B-
Vulnerable	--	--	--	B+	B	CCC+

***Our ratings combine the Business Risk Profile Score and Financial Risk Profile Score***

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Excellent	AAA	AA	A	A-	BBB	--
Strong	AA	A	A-	BBB	BB	BB-
Satisfactory	A-	BBB+	BBB	BB+	BB-	B+
Fair	--	BBB-	BB+	BB	BB-	B
Weak	--	--	BB	BB-	B+	B-
Vulnerable	--	--	--	B+	B	CCC+

**Country Risk**  
**Industry Risk**  
**Competitive Position**  
**Peer Comparisons**  
**Profitability**  
  
 +  
**Management:**  
**Strategic Positioning**  
**Operational Effectiveness**



## *Components of the Business Risk Profile Score*

# S&P Corporate Ratings Methodology

**Cash Flow Adequacy**  
**Liquidity / Short-Term Factors**  
**Capital Structure / Asset Protection**  
**Accounting / Information Risk**

**+**  
**Management:**  
**Financial Management**  
**Governance & Financial Policies**

Financial Business	Minimal	Modest	Intermed.	Significant	Aggressive	Highly Leveraged
Excellent	AAA	AA	A	A-	BBB	--
Strong	AA	A	A-	BBB	BB	BB-
Satisfactory	A-	BBB+	BBB	BB+	BB-	B+
Fair	--	BBB-	BB+	BB	BB-	B
Weak	--	--	BB	BB-	B+	B-
Vulnerable	--	--	--	B+	B	CCC+



***Components of the Financial Risk Profile Score.***

# S&P ERM Review for Non-Financial Corporations: **Discussion Questions\***

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1. What are the company's top risks? How big are they? How often are they likely to occur? How/when is this list updated?
2. What is management doing about each of the top risks it faces?
3. What size operating or cash loss has management and the board agreed is tolerable?
4. Describe the staff responsible for risk management programs and their place in the organization chart. How do you measure the success of risk management activities?
5. How would a loss from a key risk impact incentive compensation of top management and on planning/budgeting?
6. Tell us about discussions about risk management that have taken place at the board level or among top management when making strategic decisions.
7. Give an example of how your company responded to a recent "surprise" in your industry and describe whether the surprise affected your company and others differently.

\* *"Discussion Questions at Management Meetings", on [www.erm.standardandpoors.com](http://www.erm.standardandpoors.com)*

## Credibility

**vs. Company's Stated Objectives, Capabilities & History**

**vs. Our Expectations**

**vs. Industry, Market & Economic Conditions**

**vs. Strategy of Peers**

**vs. Company Culture**

**vs. Shareholder/Stakeholder Expectations**

## Incentives

**Alignment of Compensation with Strategy**

**Consequences of Underperformance (Businesses & Individuals)**

## Culture

**Communication of Plans & Objectives**

**Record of Implementing Policies**

**Understanding Causes of Successes and Failures**

## **Strategy Stability**

**Frequency and Nature of Changes**

**Unanticipated Acquisitions/Divestitures/Restructurings**

**Strategic Fit**

**Diversification**

**Market Share Gains**

**Availability of Excess Cash, Cost Synergies**

**Valuation Considerations**

## **Execution**

**Expertise in Each Key Line of Business**

**Effectiveness of Audit & Control Systems**

**Performance vs. Expectations**

**Organization Structure:**

**Effect on Efficiencies & Achievement of Strategies**

## **Risk Awareness**

**Forecasting Ability**

**Identification of Influencing Factors**

## Sophistication of Financial Standards

**Financial Risk Appetite: Beyond Unadjusted Leverage**

**Interdependencies of Risk**

**Performance vs. Expectations**

**Risk / Reward Tradeoffs**

## Aggressiveness

**Capital Levels & Structure**

**Liquidity Policy: Access to Financing**

**Allocation / Quality of Investments**

**Interaction with Board of Directors**

## **Use of Risk Management Tools**

**Detail and Comprehensiveness of Guidelines**

**Asset / Liability Matching**

**Appropriate Use of Insurance, Hedging**

## **Accounting & Management Information**

**Aggressiveness of Accounting Choices**

**Degree of Adjustment Required**

**Transparency & Responsiveness, especially under stress**

## Governance: Ownership Issues

**Degree of Board Independence**

**Board Activism & Nature of Management Interaction**

## Governance: Management Issues

**Turnover, Concentration**

**Complexity of Organization Structure**

## Governance: Stakeholder Issues

**Quality, Frequency, Consistency of Communications**

**Frequency & Level of Regulatory, Tax or Legal Conflict**



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