International Regions and Municipalities

Ratings on local authorities and regional governments outside Germany

Overview

The LB-Rating module International Regions and Municipalities is designed for assessing local authorities and regional governments outside Germany. A differentiated modelling approach reflects the structural differences between the regional and municipal level. The rating algorithm is based on a scorecard approach, which combines quantitative and qualitative factors. In particular, it takes into account the credit standing of the central government. The system produces a rating grade that corresponds to the one-year probability of default (PD).

Annual validations of International Regions and Municipalities started in 2005. The module was first approved for the IRB Approach in early 2007.

Scope of Application

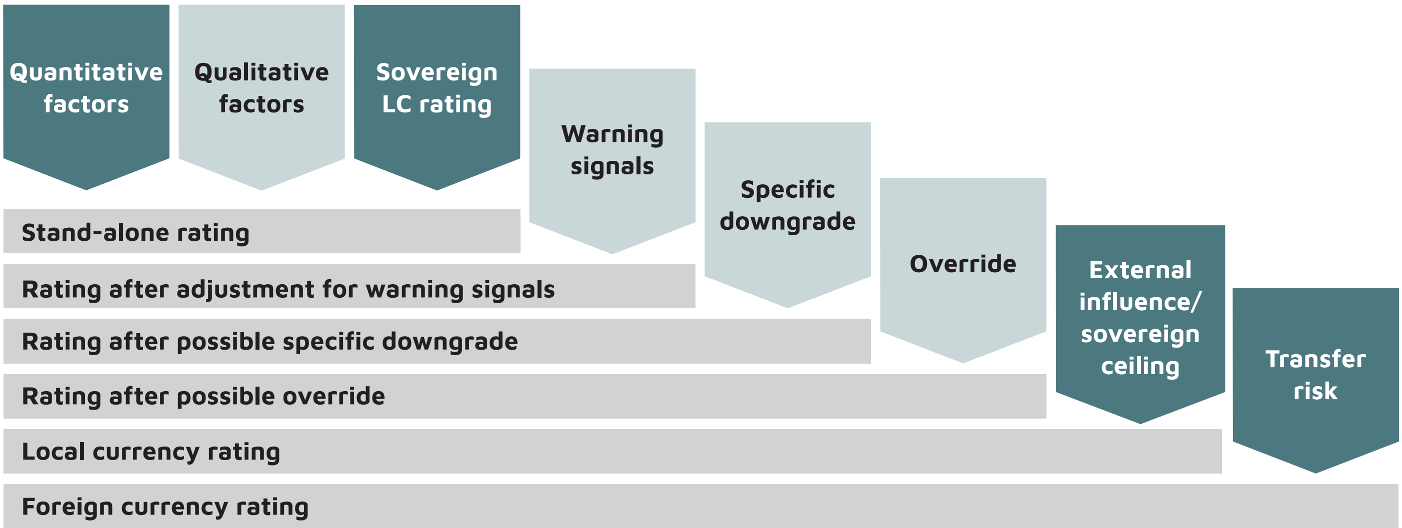
The scope of application of the International Regions and Municipalities module covers local authorities and regional governments outside Germany. These are defined as administrative units below the sovereign level that have governmental responsibilities and are entitled to non-earmarked taxes and duties. The module may also be used for assessing special-purpose districts, such as school districts in the USA, if they are mainly funded by transfer payments from local and regional governments enjoying the above tax privileges or if they cover a substantial part of their budget by levying own taxes.

Limitations

Government-related enterprises (GREs), i.e. companies that are majority-owned by the state and have a public interest mission should be rated with the Corporates module.

RSU RATING

Rating Process



Dark arrow: mainly data-based
Bright arrow: mainly human judgement

Quantitative and Qualitative Factors, Sovereign Rating

The quantitative factors are based on budget and structural metrics. In addition, analysts are required to evaluate a number of qualitative factors. The sovereign local currency rating is also taken into account as it reflects the substantial influence of the political, legal and economic environment on a sub-sovereign entity ‘s creditworthiness.

Warning Signals, Specific Downgrade and Overrides

If certain budget figures reach critical values or the central government takes detrimental measures, this can be taken into account as a warning signal. Further, a specific downgrade can be applied for risks arising from pension and contingent liabilities. If there are any other exceptional circumstances that have not been sufficiently covered otherwise, analysts can override the rating and change it manually.

External Influence and Sovereign Ceiling

A guarantee scheme is considered to apply if the central government or a superior entity are effectively required by law or contract to prevent the borrower from defaulting. If there is no legal requirement but support is still likely to be provided in a critical situation, this can also be recognised in the rating system. Given the substantial dependence on the central government, the final rating may be capped at what is referred to as the sovereign ceiling.

Transfer Risk

In addition, the risk of restrictions on foreign currency transfers is taken into account. This risk must be considered when a loan is not denominated in the obligor’s domestic currency.

RSU GmbH & Co. KG
Karlstraße 35 | 80333 München | Germany
Tel. 0049 89 442340-0
infos@rsu.one | www.rsu.one