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Rating Methodology for Group Companies of Corporate Group

1. Scope of this Methodology and its Relations with Other Methodologies

This rating methodology is applied to group companies of domestic groups with business corporations as core companies and such groups with financial corporations as core companies. However, for financial institutions and the like under the prudential regulation, the "Rating Methodology for Financial Groups' Holding Companies and Group Companies" shall be applied preferentially. Regarding group companies with the overseas business corporations and financial corporations as the core companies, this rating methodology shall be applied mutatis mutandis after making necessary adjustments based on the legal and accounting systems of the location of those companies.

2. Long-term Issuer Rating of Group Companies

(1) Main Components of Rating Methodology

There are two methods for assigning a long-term issuer rating to a group company of a corporate group: top-down approach, which uses the corporate group's creditworthiness as a starting point and takes into account the degree of likelihood of future group support; and bottom-up approach, which uses the group company's stand-alone creditworthiness assessment as a starting point and adds the degree of likelihood of group support to this. In principle, JCR adopts the top-down approach for rating of group companies. The term "group companies" as used in this rating methodology refers to subsidiaries, affiliates, and other companies, which JCR considers belong to a specific corporate group from various perspectives, such as capital, personnel, and business relationships.

JCR mainly takes into account the following factors to determine a long-term issuer rating for the group company of the corporate group.

- Likelihood of support by the corporate group for the group company
  - ・Degree of Control and Involvement of Corporate Group in Group Company
  - ・Degree of Managerial Importance in Corporate Group
- Stand-alone Creditworthiness of Group Company (Stand-alone Assessment)
- Creditworthiness of Corporate Group

(2) Support by the corporate group to the group company

Support by the corporate group to the group company is judged comprehensively based on an evaluations from two axes: degree of control and involvement evaluation and degree of managerial importance evaluation. The key point of the top-down approach is recognition of a probability that the corporate group will provide remedial support, based on reasonable grounds, when the creditworthiness of the group company declines. In addition, it is usually assumed that the corporate group will often provide strategic support such as additional investments and loans to the group company, or further enhancement of ties between the corporate group and the group company, for the realization of the group strategy and sustainable growth. JCR will judge support of the corporate group from the perspectives of both remedial and strategic supports.

(i) Degree of Control and Involvement of Corporate Group in Group Company

The evaluation of control and involvement is based on (i) ratio of voting rights held by the corporate group in the group company, (ii) degree of involvement of the corporate group in the decision-making process of the group company, (iii) status of dispatch of directors and others, and (iv) status of establishment and utilization of group CMS and credit lines or integrity of management control. The higher the ratio of voting rights, the greater the degree of control and involvement of the corporate group, but if the ratio is not 100%, JCR considers the effective controlling power of the corporate group, taking into account the composition of other shareholders.

With regard to listed subsidiaries, they are positioned as leading companies in the corporate group, and their sharing of strategies and business ties are relatively strong. On the other hand, the perspective of ensuring independence is becoming increasingly important amid the increasing demand for more sophisticated group governance, and the degree of control and involvement by a company is highly constrained. Furthermore, for companies that are fifty-fifty joint ventures, the positioning and importance in the two corporate groups in terms of business strategy are not consistent. For these companies, JCR will make a comprehensive judgment of the degree of control and involvement by carefully examining how the group company joined the group or how it was established, current status of governance, and changes in positioning in the two groups.

(ii) Degree of Managerial Importance in the Corporate Group

The degree of managerial importance is evaluated from the perspectives of (i) degree of strategic importance (whether the business segment to which the group company belongs is important for the corporate group's long-term vision and medium-term management plan) and (ii) degree of functional importance (whether the group company performs important functions in forming the value chain and group infrastructure for business operations). The more important a group company is in the corporate group, the closer the creditworthiness of the group company becomes to that of the corporate group.

(3) Stand-alone Creditworthiness of Group Company (Stand-alone Assessment)

The stand-alone creditworthiness of a group company refers to the creditworthiness of the group company on its own, based on the evaluation of its business and financial bases that have been formed through its relationship with the corporate group (formed by the core company). JCR does not assume a fully independent company with no consideration of ties to the group in terms of people, goods, money, and business. The target of long-term issuer rating is unambiguously the group company. Assuming that the group creditworthiness declines and support cannot be obtained from the parent company and others, or that the group company leaves the corporate group, JCR will evaluate the creditworthiness of the group company alone.

(4) Creditworthiness of Corporate Group

With regard to the creditworthiness of a group company, JCR will evaluate the creditworthiness of the corporate group to which the group company belongs in order to determine the base point for notching down when the top-down approach is applied. With regard to the creditworthiness of a corporate group, JCR basically analyzes the consolidated business and financial bases of the corporate group, but adjustments may be made to the consolidated data in accordance with the actual condition of the group. The creditworthiness of a corporate group can be regarded as the underlying strength that supports its group companies. No matter how strong the degree of control and involvement or managerial importance, if the creditworthiness of the corporate group is low, it will have a negative impact on the degree of likelihood of group support.

(5) Consideration of Approach to be Applied

Through (2) through (4) above, JCR evaluates the likelihood of support by the corporate group to the group company to determine whether the top-down approach can be applied. If possible, JCR determines the rating of the group company by applying notching (difference in creditworthiness between the group and the group company) according to the likelihood of support.

However, during the evaluation process, it may be determined that the top-down approach should not be applied even if a company falls under the category of group companies. For example, the top-down approach may not be applied in cases where the core company is an investment fund and the like, and the group company is a net investment target, and it is therefore easily assumed that the group company will be replaced in the future, even if the ratio of voting rights is sufficiently high.

If it is recognized that the degree of likelihood of remedial or strategic support by the corporate group will change in the future due to a change in management policy or strategy of the corporate group or a change in the investment ratio, JCR will flexibly review whether the top-down approach should be applied.

If the stand-alone assessment exceeds the top-down approach assessment, JCR gives priority to the stand-alone assessment for the rating of the group company. Even in such cases, in principle, the rating level of the group company shall not exceed the group creditworthiness. However, if the influence of the corporate group is judged to be limited due to the fact that the group company is listed on a stock exchange or other factors, the creditworthiness of the group company may exceed that of the corporate group to a certain degree.

For companies that do not fall under the category of group companies or whose importance to the corporate group is not considered at a high degree, stand-alone assessment is the general rule. However, even for such companies, the creditworthiness of the corporate group may be reflected if the likelihood of remedial or strategic support by the corporate group is recognized to more than a certain degree.

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