Risk Rating Methodology for Companies *holding*

Concept	First and Last Name – Position	Signature	Date of signature
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1. Objective

To describe the methods and criteria for risk rating *holding* companies or corporate groups. This methodology can be supplemented with risk rating methodologies for short-, medium-, and long-term debt instruments, preferred shares, and issuers, as well as risk rating methodologies for financial institutions, insurance companies, investment funds, and other industries that provide support for understanding the viability of the *holding company*'s cash flows.

2. Scope

This methodology applies to *holding* companies or corporate groups whose long-term objective is to generate capital by investing in assets with the expectation that they will appreciate in value, in addition to managing and eventually selling certain assets or reinvesting in new projects. Furthermore, a *holding* company seeks to operate in more than one industry, whether locally, regionally, or globally; therefore, even if it currently operates in a single sector, its intention to diversify into additional sectors in the future and the extent to which its operating expenses depend on the dividends it receives are taken into account. The rating may apply to a specific issuance or reflect the company's financial strength.

In addition, companies with an exclusive stake in *joint ventures* or with shared control are considered part of *the holding company* or corporate group, provided that the holding company has access to their cash flow or provides financial support in stress scenarios.

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3. Definitions

Issuer
The company that issues securities. *E.g.: issuer*
Solvency / Financial Strength The ability to meet contracted debts; and by extension, public recognition of a person's or company's respectability in business. It also applies to governments regarding the payment of their external debt. *E.g.: credit strength*
Security
A document evidencing the ownership of a right in a company (stock, bond) or against a debtor (government debt, treasury bills, check). It may be a registered security or a bearer security. *E.g.: instrument, security, issue, money market instrument* (short-term security) **Investment portfolio**
Holding of securities intended to generate income from dividends and interest, rather than capital gains. *E.g.: investment portfolio*
Dividend An active dividend is the amount of money that, when a company distributes profits—after increasing reserves, providing for amortization, and paying taxes—corresponds to each share. // Passive dividend: each of the partial amounts that the holder of a share or bond agrees to pay, at the issuer's request, until the total committed amount is paid out. *E.g.: dividend*
Double leverage
This occurs when a debt is issued by the *holding company* and the proceeds are invested in a subsidiary as *equity*. In this way, the *holding company* injects capital into the subsidiary, allowing it to increase its leverage. Therefore, since the *holding company*'s capital level has not changed, through double leverage, the *holding company* is more exposed to the subsidiary. *E.g.: double leverage*

4. Basic Conditions

In general, a *holding* company's rating reflects the risk profile it assumes as a result of its investments in each company and industry, taking into account each business model, the *holding company*'s strategic approach to each position, the country risk of the markets where it operates, the fundamental risk of the assets generating cash flows (liquidity, credit, and diversification), and its financial performance. A *holding* company's financial performance depends on its ability to successfully execute profitable investments with moderate levels of leverage and stable sources of funding, guided by the prudent establishment of risk policies (risk appetite).

A *holding* company typically has no, or only limited, operations in the businesses in which it holds stakes; therefore, such companies are expected to be diversified without a significant strategic *core business*. Their primary business consists of maximizing their investment portfolio and periodically rotating their assets in order to realize capital gains and accumulate those funds for new investments. In fact, the *holding company* is considered financially independent from the companies in its portfolio, to the extent that it can finance or guarantee them and prevent contagion in the event of a specific default.

5. Specific Conditions

Given the business model of a *holding* company, taking on debt to finance equity stakes in

certain sectors, the holding company assumes the risk of servicing the debt primarily with dividends or management fees from the companies in the portfolio, as opposed to what a corporation does with cash flows. These dividends received by the portfolio companies are discretionary and subordinate to the other commitments established by them to maintain the course of their operations. Another risk assumed by a *holding* company is the inherent mismatch between its assets and liabilities, since they do not generate abundant cash flow and require the company's ability to refinance debt or, as a last resort, the liquidation of some of the operations, subject to market liquidity.

When a *holding* company has a presence in other markets, the following factors are considered: the risk the company assumes in transferring or repatriating its dividends, the liquidity level of the home market, tax regulations, and the level of investor protection, evaluated on a consolidated basis with respect to the markets where it operates.

The liquidity of the assets comprising the portfolio is a key factor in assessing the fundamental risk of the investment portfolio, since the *holding* company's ability to sell its positions quickly at reasonable prices serves as a last-resort tool for servicing its debt. On the other hand, greater portfolio diversity—whether by asset, industry, or region—allows the *holding* company to generate dividends that are not heavily correlated with a single line of business. Additionally, the credit quality of each portfolio participant is relevant to the assessment of fundamental risk, as the *holding* company may lose value since a stake is always subordinate to other obligations.

A holding company's ability to make profitable investments, execute acquisitions on time, and divest certain holdings on favorable financial terms is critical to its success. This is how the company creates value for its shareholders within the framework of prudently established risk policies.

The leverage ratio includes the debt incurred by the companies in the portfolio, as well as convertible debt instruments and guarantees provided, net of the most liquid assets; this is compared to consolidated equity. Additionally, the diversity and stability of funding sources allow the *holding* company to reduce refinancing risk.

Key Analysis Factors

- Fundamental risk
- Country risk in other markets
- Leverage and funding sources

a. Fundamental risk

Fundamental risk is based on the quality of the assets comprising the portfolio in terms of liquidity, credit, and diversification, as well as the *holding company*'s ability to make investments that help improve its business's risk profile. The liquidity of each asset in the portfolio is related to the speed at which that asset can be liquidated at a reasonable price as a last resort in situations such as the inability to refinance its debt. The *holding company*'s stake in the asset—if it is publicly traded—and the level of dividends it receives are taken into account.

The payment capacity of the companies in the portfolio is assessed to evaluate the risk that the asset will default or reduce its value-generating capacity. In the event of default, the company will lose all its value since the cash flows directed toward the *holding company* are always subordinated to the asset's other obligations. The ability to generate value is assessed in terms of the level and stability of recurring revenue and dividend distributions. Greater capital generation and a continuous flow toward the *holding company* indicate lower capital requirements for the *holding company*.

To assess the asset's ability to pay, the local long-term credit rating assigned by PCR[1]is first considered. Creditworthiness ratings (financial strength) and short-term debt ratings are also taken into account. If international credit ratings (registered with an NRSRO) are available and PCR determines that it can establish equivalencies with that rating agency, the equivalent rating is used. Furthermore, when the entity has international ratings from various

[1] Ratings from other entities that PCR considers reliable (credit rating agencies or other organizations) may be used. At PCR's discretion, these ratings may be adjusted. However, PCR may not accept third-party credit ratings.

Among NRSRO ratings, the one indicating the highest risk is used. Ratings must be no more than 12 months old as of their date of issuance. However, PCR may limit its usefulness

if it is believed or expected that the entity's ability to pay is changing.
Having a diversified portfolio across assets, industries, and geographic locations adds value to the *holding company* and reduces its risk profile. Risk is high when business lines operate within the same industry, and when they operate in different industries, it is vital to identify the geographic areas. Business lines

Business operations across various industries and a global presence enable the holding company to significantly reduce risk.
The *holding company*'s ability to invest in profitable assets, integrate each asset into its business model within the expected timeframe, and divest them under attractive economic conditions are key factors in the *holding* company's success.

b. Country Risk in Other Markets

Country risk analysis is conducted using PCR methodologies for sovereign risk and the methodology for standardizing risk ratings in other markets.

It is important to note that a company's risk fundamentals remain the same regardless of the market to which its cash flows are directed. However, when the *holding company* assumes risk in that company, the company will face various external factors that could affect its own ability to pay and the cash flows generated by it.

c. Leverage, Cash Flow Maturity, and Funding Sources

The holding company's leverage level is a key indicator for determining its financial risk profile through the *loan-to-value* ratio. The appropriate matching of its cash flow and capital structure is also evaluated. The debts included in the analysis are those of all the companies comprising

its portfolio, guarantees granted in favor of subsidiaries, and debt instruments issued through financing vehicles. Cash and the most liquid and readily available investments may be deducted for potential immediate debt repayment; furthermore, convertible instruments and guarantees granted in favor of any portfolio company may be excluded. This also helps ensure that the *holding company* will be able to receive the expected cash flows from its subsidiaries.

When the *holding company* has investment commitments in new projects or agreements with the companies in its portfolio, the strength of those commitments is evaluated, treating them as obligations rather than funds available for debt repayment. Another equally important aspect is the market value of unlisted companies, calculated based on their book value or through a multiple analysis compared to recent transactions.

Additionally, when the *holding company* is highly leveraged, the greater difficulty in liquidating assets to pay off debt is taken into account, thereby increasing its refinancing risk. And if it manages to liquidate an asset, the *holding company* could find itself more leveraged after the transaction or have to liquidate more assets to maintain the same level of leverage.

The level of leverage can be amplified when the *holding company* acquires a new asset or injects capital into a subsidiary through debt, thereby allowing the new portfolio addition or the subsidized subsidiary to increase its own leverage as well—a scheme known as *double leverage*. Thus, since the *holding company* maintains the same level of capital, the immediate effect is that the *holding company* will now support a higher level of assets and will be significantly more exposed to the subsidiary that received the cash. In summary, when capital is double-leveraged, the *holding company* will be exposed to a higher level of unanticipated losses—that is, greater risk. In this regard, the *holding company* must provide information demonstrating the activity among the group's companies.

On the other hand, when analyzing cash flow, the *holding company*'s cash flow matching is reviewed, considering recurring cash inflows (dividends, management fees, and interest received) and non-discretionary outflows (operating expenses, interest, and taxes). Other productive assets, such as royalties or the sale of movable or immovable property, may be considered as revenue provided that there is sufficient reason to believe they can be liquidated in a timely manner and at a reasonable price.

Furthermore, the evaluation of funding sources and capital structure serves to determine refinancing risk over time (the previous two years, the current year, and the next three years). The diversity of funding sources, the maturity of obligations, and the relationship with creditors are considered. The *holding company*'s debt structure is considered because investment in

Equity is long-term and must be matched with debt; additionally, the expense structure could affect the cash flow available for debt repayment, and differences in accounting policies may result in higher equity rather than cash flow.

Rating Categories

- Short-term (ST) issues [2]

High	CR1+ CR1 CR1- 	Securities with very high certainty of timely payment. Liquidity and debtor protection factors are very good. Risks are negligible (e.g., a 1+ rating would correspond to the highest certainty, other factors excellent, and risk virtually absent).
Good	CR2+ CR2 CR2-	Securities with certainty of timely payment. Liquidity and other aspects of the debtor are solid; however, ongoing funding needs may increase total financing requirements.
Satisfactory	CR3+ CR3 CR3-	Satisfactory liquidity and other protective factors lead to the security being rated as an acceptable investment. Timely payment is expected; however, the risk factors are higher and subject to change.
Does not qualify as an investment	CR4	Securities with characteristics of speculative investments. Liquidity is insufficient to guarantee debt service. Protective factors are subject to a high degree of fluctuation.
Default	CR5	Securities where payment terms have been breached.
	CRE	Refers to securities for which there is insufficient information or the information is not representative. This scale does not allow for an assessment of its risk.

These categorizations may be supplemented, if applicable, by the symbols (+/-) to improve or downgrade, respectively, the rating achieved within categories 1 through 3 inclusive (as an example, the modifier has been described in rating 1). Additionally, local scales will be identified by adding a prefix in accordance with the identification assigned to each market[3] .

[2] In the PCR, a code is established for each rating category used. For Short-Term Issues (ST), it is PCR-MET-P-510.

[3] The nomenclature used corresponds to the international coding based on ISO 3166-1 alpha-2, a two-letter code system.

- Medium- and long-term issues and preferred shares (LP)[4]

Outstanding Rating	CRAAA	Issues with the highest credit quality. Risk factors are virtually nonexistent.
High	CRAA+ CRAA CRAA-	Issues with high credit quality. Protective factors are strong. Risk is modest and may vary occasionally due to economic conditions.
Good	CRA+ CRA CRA -	Issues with good credit quality. The protective factors are adequate; however, during periods of economic downturn, the risks are greater and more variable.
Satisfactory	CRBBB+ CRBBB CRBBB-	Risk protection factors are reasonable and sufficient for an acceptable investment. There is considerable variability in risk during , which could lead to fluctuations in its rating.
Not Investment Grade	CRBB+ CRBB CRBB-	Issues rated below investment grade. It is estimated that their financial flexibility could limit their ability to meet obligations at maturity. The quality of these issues can fluctuate frequently, so they are considered speculative.
	CRB + CRB CRB -	Issues rated below investment grade. There is a higher risk of default. Financial buffers fluctuate widely depending on economic cycles, industry conditions, and the company's management's ability the company to navigate them.
	CRCCC	Issues rated well below investment grade. They are characterized by a high risk of timely payment. Protective factors are scarce, and the risk can be substantial in adverse industry or the company.
	CRDD	Issues where interest and/or principal payments have been missed or where the The issuer has committed other breaches.
	CRDP	Preferred shares with overdue preferred dividends.
	CRE	This category applies to shares for which there is insufficient information or the information is not representative, which does not allow for an opinion to be issued regarding their risk.

These categories may be supplemented, if applicable, with the symbols (+/-) to improve or downgrade, respectively, the rating achieved within the categories AA through B, inclusive. Additionally, local scales will be identified by adding a prefix according to the identification assigned to each market[5] . For Costa Rica, "CR" is used.

[4] The code for medium- and long-term issues and preferred shares (LP) is PCR-MET-P-520.

[5] Based on ISO 3166-1 alpha-2, a two-letter code system.