RAPIDRATINGS

SOLUTION BRIEF

Term Probability of Default: Implementing CECL Standards

FASB's new accounting standard, ASU No. 2016-13, commonly referred to as "CECL," will require banks to calculate continual, life-of-loan estimated credit losses on entire commercial & industrial (C&I) portfolios. Although mandatory adoption begins in 2019, this unprecedented change from the longstanding incurred loss model will result in significantly more loan data-collection and analysis than ever before; banks need to begin to develop or enhance models and infrastructure immediately. RapidRatings has developed a series of Term Probabilities of Default (PDs), a key requirement for many banks in estimating forward-looking losses. Our Term PDs run 12 months to 10 years on public and private non-financial companies.

Accurate & Consistent Forward-Looking Model for Term PDs

RapidRatings reveals a company's operating and financial efficiency, along with its near-term resiliency, by carefully examining financial statements alone. It is from these measurements that we extrapolate Term PDs. This quantitative approach deliberately excludes market signals and relies on 22 industry-specific weightings of operating and financial ratios to deliver a clearer picture of a company's health and outlook. The approach is identical for public and private companies, providing an analytical consistency across the C&I portfolio that should be stressed to examiners.

Automated, Continual Reporting on the Entire Portfolio

CECL will require banks to make continual representations on any "significant deterioration" in their loan pools, typically on a quarterly basis. The shift to determining deterioration for all loans rather than impairment for non-performing loans will stress any bank's capabilities. Only an automated, quantitative, Point-in-Time (PIT) ratings system such as RapidRatings' can provide the ability to report on companies underlying the pools and the pools themselves at the frequency, scale, and precision which will be required.

Extensive Reporting & Analytics with Full Audit Trail

In addition to Term PDs for any non-financial company, RapidRatings provides in-depth reports detailing the company's performance and ratings trends, a profile of its liability portfolio, sector and peer comparisons, and due diligence questions about its financial condition. Additionally, pool-based matrices and PD movement alerts provide a quick and easy way to monitor an entire portfolio. This allows banks to be confident they meet the "reasonable and supportable" standard CECL sets and provide an audit trail for examiners.

Business Benefits

- Avoid compiling and parsing large-scale statistics on which to base PD assessments
- Inform methods for underwriting and pricing loans & organizing loan pools
- Meet the CECL equivalent challenge in IFRS 9 -- Stage 2 accounting
- Initiate PD x LGD as the preferred C&I model
- Provide an authoritative second opinion on legacy or newly implemented internal or third party systems

Rapid Ratings International, Inc. | 86 Chambers Street, Suite 701 | New York, NY 10007 | **P** 646 233 4567 | **F** 626 219 7460