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# CareEdge Global Transfer and Convertibility Risk Assessment Methodology

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**Note:** This rating methodology is an updated version of the Transfer and Convertibility Risk Assessment Methodology published in October 2025. The update incorporates the consideration that CareEdge Global may differentiate transfer and convertibility risk across various currencies to reflect constraints arising from external factors. This update does not alter the overall framework for T&C risk assessment.

## A. Introduction

The Transfer and Convertibility (T&C) risk assessment reflects CareEdge Global IFSC Limited's (CareEdge Global) opinion on the likelihood that a sovereign government may impose restrictions to access and transfer of foreign currency required by a non-sovereign entity towards meeting its external debt service obligation(s).

T&C risk is an important factor in evaluating cross-border credit risk. The assessment evaluates risks and restrictions associated with availability of foreign currency, controls around convertibility of local currency, and transferability of foreign currency across borders, for debt servicing purposes.

In rare circumstances, constraints on access to foreign currency may also arise from external factors, such as international sanctions imposed by select jurisdictions, force majeure events, etc. In such cases, the ability of a non-sovereign entity (such as a corporate or a financial institution) to access or transfer such specific currencies may be impaired, without impacting access to other currencies. Therefore, if required, CareEdge Global may differentiate T&C risk for different currencies, or set of currencies, to reflect any constraints on their access. Accordingly, where relevant, the T&C assessment may differ for sanctioned and non-sanctioned currencies.

## B. Scope

This methodology is designed to evaluate T&C risk assessment across all sovereigns rated by CareEdge Global.

## C. Approach

CareEdge Global's approach to assessing T&C risk combines quantitative analysis (core pillars assessment) with qualitative judgment (modifiers).

### Core Pillars Assessment

The core pillars assessment is anchored on three pillars (each scored on an 8-point scale) which collectively reflects a sovereign's global standing and its implications for T&C risk:

- a) Financial Openness
- b) External Positions and Linkages
- c) Institutions & Quality of Governance

The blended score is derived using weightage average of these three core pillars. Among them, **External Position & Linkages** pillar carries the highest weight, underscoring its central role in evaluating a country's vulnerability to external shocks. A strong external position indicates that a country is better equipped to manage volatility in capital flows and global financial conditions, thereby reducing the likelihood of imposing capital or foreign exchange controls.



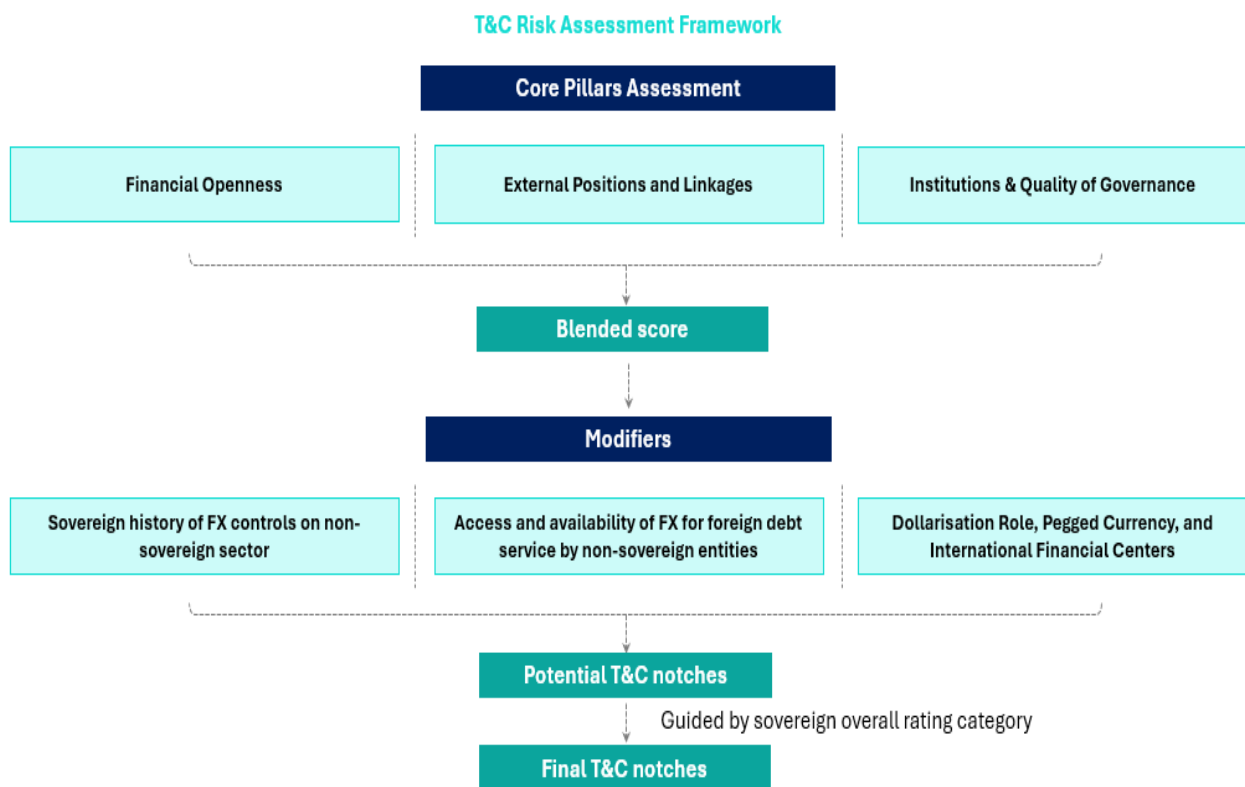
## Modifiers

The blended score is then adjusted using modifiers to incorporate nuanced, non-quantifiable factors such as:

- Sovereign’s history of foreign exchange (FX) controls on non-sovereign entities,
- Recent policy development on foreign exchange management,
- Extent of dollarization in the economy or pegged currency status etc.— which may influence T&C assessment.

These modifiers ensure that the final assessment reflects both structural strengths and evolving policy dynamics.

The final T&C notch(es) is determined based on the abovementioned modified blended score and is also guided by the sovereign’s overall rating category. This ensures consistency and alignment with the broader sovereign credit framework.



## D. Pillars of the T&C Assessment

### 1. Financial Openness:

To assess the financial openness of an economy in terms of its current and capital account transactions, we use the KAOPEN index<sup>1</sup>, also known as the Chinn-Ito Index. The KAOPEN index is constructed using the information on financial restrictions sourced from the International Monetary Fund's Annual Report on Exchange Arrangements and Exchange Restrictions (IMF AREAER). The index factors in four variables i.e. restrictions on current account transactions, restrictions on capital account transactions, existence of multiple exchange rates, and requirements to surrender export proceeds. The index provides score ranges from 0 to 1, where 0 indicates a closed economy and 1 represents an open economy. A higher KAOPEN score implies greater capital account openness, suggesting a lower probability of restrictive capital controls or currency transfer limitations. Conversely, a lower score indicates higher probability of capital restrictions, which may elevate transfer and convertibility risks. Incorporating the KAOPEN index into the T&C assessment strengthens the analysis by providing a quantitative measure of a country's financial openness.

This KAOPEN scores are grouped into classes by CareEdge Global, with each class mapping to a Financial Openness Score (representing a specific level of financial openness).

### 2. External Position & Linkages:

Sound external sector fundamentals are crucial in determining a sovereign's access to foreign funding, trade competitiveness, and external liquidity. In a largely interconnected global landscape, the external sector can become a source of risks emerging from global trade tensions, financial contagion, and geopolitical conflicts. Hence, external indicators such as a comfortable current account position, healthy capital inflows, sustainable external debt, and adequate liquidity become increasingly important cushions to act as offsets.

The External Position & Linkages pillar assesses these factors through three key dimensions:

- **Flow**, which measures the sufficiency of current account receipts and capital inflows to meet external debt servicing requirements. This includes detailed analysis of the current account balance (CAB), foreign direct investment (FDI), and external funding ratio. The CAB and FDI matrix is used to assess the adequacy of stable capital flows to support CAB. Whereas external funding ratio measures the sufficiency of current account receipts and net FDI to meet the immediate obligations i.e. current account payments and external funding required for the current year.
- **Coverage**, which measures the adequacy of foreign currency reserves and current account receipts to meet import needs and debt service requirements, reflecting the sovereign's

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<sup>1</sup> Please refer link: [Chinn, Menzie D. and Hiro Ito. 2006. "What Matters for Financial Development? Capital Controls, Institutions, and Interactions," Journal of Development Economics, Volume 81, Issue 1, Pages 163-192 \(October\).](#)

capacity to absorb external shocks. This includes analysis of the adequacy of foreign currency reserves to meet import payments and the availability of current account receipts to service the external debt.

- **Stock**, which measures the outstanding external debt position and economy's net asset against volatile capital flows. This includes analysis of vulnerability to sudden capital flight, net international investment position, and external debt as a % of GDP.

Secondary factors such as reserve currency status, currency turnover in the foreign exchange market, remittances, and International Financial Center status are also considered to provide a comprehensive and nuanced assessment of external risks.

### 3. Institutions & Quality of Governance:

Institutions are the building blocks of any economy. The strength of institutions and the government's effective policymaking contribute to overall economic stability. In an uncertain world, policy predictability has become increasingly important.

Strong institutions also make an economy less vulnerable to various shocks (economic, financial, and political) as they enable the government to formulate and implement effective policies targeted at mitigating the impact of these shocks.

The assessment of a sovereign's Institutions and Quality of Governance uses Worldwide Governance Indicators (WGI) and considers the following dimensions:

- **Regulatory Quality and Government Effectiveness:** An efficient regulatory system helps the government formulate new rules and improve the existing ones to cater to the intended objective efficiently in a constantly evolving economic and social environment. Good regulatory policies and delivery also aid government effectiveness by improving the quality of public services and enhancing the credibility of the government's commitment toward economic progress.
- **Accountability and Political Stability:** Voice and accountability are important dimensions of governance which empower people by giving them freedom of expression and encouraging their participation in society as responsible citizens. Increased accountability could also contribute to abating corruption and lowering instances of conflict while fostering inclusive development. Political stability forms the foundation of policy predictability and fosters confidence in the economy. It also leads to improved international relations and enhances the ease of doing business. On the other hand, political instability in the form of social conflicts/crimes could undermine competitiveness impacting earning potential. The nature of power and track record of smooth transition in power are equally important aspects that are considered.
- **Rule of Law and Control of Corruption:** The foundation of political stability is the rule of law. It ensures unbiased enforcement of contracts and demonstrates the extent of citizens' respect and confidence in the rules of society. Corruption in the form of the use of

power for personal gains and interests not only erodes the public's confidence in the government's institutions but can also impact the effectiveness of reforms. It could also lead to tax evasion, having implications for the government's revenue generation.

Secondary factors are also considered to assess the potential risk stemming from cross-border tensions, threats of war, etc. For any sovereign, these challenges could undermine the national security having implications on the overall economic performance, eventually straining public finances.

**Note:** The pillars External Positions & Linkages and Institutions & Quality of Governance are assessed as part of the sovereign rating framework. For a more detailed understanding of how these factors are evaluated, please refer to **Sovereign Rating Methodology**.

Therefore, in the context of T&C assessment, countries that demonstrate strength across these three pillars (Financial Openness, External Position & Linkages, Institutions & Quality of Governance) are less likely to impose restrictions on non-sovereign entities for debt servicing. Conversely, countries with weaker performance on these pillars are more likely to place restrictions.

## E. Modifiers

Modifiers may be applied on the blended score to either notch up or notch down, ensuring a more nuanced assessment. It is important to note that the T&C assessment is largely driven by the core pillars with limited adjustment based on modifiers in usual circumstances. Modifiers considers the following key factors:

### 1. Sovereign history of FX controls on non-sovereign sector

It examines the sovereign government's past behaviour regarding foreign exchange restrictions on non-sovereign entities. A consistent track record of imposing foreign exchange controls or capital restrictions indicates a higher risk of future intervention, which can negatively impact debt servicing ability. Conversely, a consistent track record of facilitating non-sovereign access to foreign currency suggests a more supportive environment, reducing T&C risk.

### 2. Access and Availability of FX for Foreign Debt Service by Non-sovereign Entities

This assesses how readily non-sovereign borrowers can access foreign currency to meet their external debt obligations. Limited availability increases the risk of payment disruptions, while reliable FX access enhances confidence in timely debt servicing. Review of central bank policies and the presence of administrative or legal barriers provide more understanding on this factor. Additionally, we assess whether FX reserves are sufficient and whether priority is given to sovereign obligations over non-sovereign entities requirements. Restrictions on capital outflows, delays in FX remittance, or preferential treatment for state-owned enterprises may signal elevated T&C risk, potentially constraining timely debt servicing and impacting the issuer's credit profile.

In certain unusual situations, access to specific foreign currency may also be constrained by factors external to sovereign, such as international sanctions or force majeure events etc. Any such constraints on access to specific foreign currency are also evaluated to appropriately reflect the T&C risk for such currency (or a set of currencies), as applicable, and may represent a material weak link in such assessments.

### **3. Dollarisation Role, Pegged Currency, and International Financial Centers**

While assessing T&C risk, we also assess whether the economy is a dollarized economy which typically lowers convertibility risk. For economies with pegged currency regime, we evaluate likelihood that the peg can be maintained without leading to financial instability or policy reversal. Additionally, we consider the role of International Financial Centers, which generally facilitate global capital flows and are less likely to impose foreign currency restrictions.

## **F. T&C Assessment**

The modified blended score is determined based on the core pillars assessment and modifiers. Modified blended score will lead to the potential T&C notches.

The final T&C notches (ranges from 0 to 4) will be derived based on potential T&C notches and corresponding sovereign rating category.

Thus, after applying the final T&C notches on the sovereign rating, we arrive at the T&C assessment for the sovereign.

[For the previous version, please refer to 'CareEdge Global Transfer and Convertibility Risk Assessment Methodology' issued in [October 2025](#)]

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