



Ministry of Finance of the Czech Republic  
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## Corporate Bond Scorecard

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Inexperienced, conservative investor



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## Ministry of Finance warns



A bond as a form of investment **is not always best for small investors**, who do not have the **experience in investing or higher financial literacy related to the same form of investment, the best and safest**. More and more small investors, in the search for better returns on investment, misjudge alternatives and eventually lose their money.

## Purpose of the document



The purpose of this document is **to provide investors**, who are not experienced in such a kind of investment, **a simple and fast tool for initial evaluation of bonds**. We point out that this applies only to initial evaluation of issuance of issuer. During more careful and complex evaluation of issuance of issuer more factors come into place. For the purposes of this document, **several factors are simplified for better understanding**. Some other factors are mentioned in the additional section.

## Bond scorecards



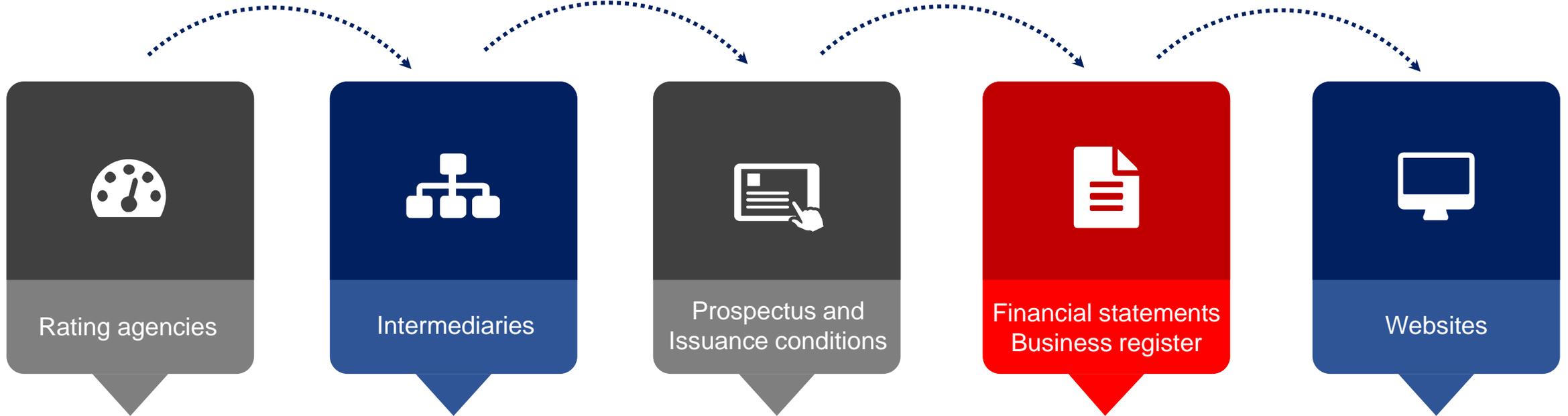
We divide the bond scorecards into two branches: **Scorecard with ratings and scorecard without ratings**. In these branches, we assume that investors are planning to **hold the bond until reaching maturity**. Hence, the liquidity and investment horizon do not play a crucial role and we mention them in the additional section. The rating of some of the reputable firms, mostly **Moody's, S&P or Fitch plays a crucial role when choosing a bond**. When a firm **does not have a rating** and investors do not know the firm really well and **do not consider themselves as experienced investors, we do not recommend to invest in the bond**. This fact even could not be reversed by existence of prospectus from Czech National Bank, which on the one hand indicates that a certain firm has fulfilled all the formal requirements, but on the other hand does not check the financial health of the firm. Later on, in the document we publish both scorecards – scorecard with ratings and more risky **scorecard without ratings for those, who would like to invest despite these warnings**. Last but not least, we publish examples of how the scorecards could be used.

## Information sources



In this document we also publish information sources, which should be freely available on the internet. **In these sources investors should then find needed information for an initial evaluation of the issuance and issuer**.

## Information sources



- Ratings from firms as Moody's, S&P or Fitch
- Assessing firm's ability to meet its obligations

- Intermediary as one of the first indicators of quality of bonds
- Established financial institutions under the supervision of the Czech National Bank are preferable

- Prospectus from the Czech National Bank is easily traceable in the prospectus register
- Issuance conditions then state the level of interest, bond maturity etc.
- Eventually business plan

- Financial statements (balance sheet, profit and loss account and cashflow statement) can be easily traceable in the business register justice.cz together with basic information about the firm

- A well-designed company website and regular release of news entails transparency
- Websites and internet research may serve as a good source of information as well



## Scorecard WITH ratings

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## Scorecard with existing ratings



Scorecard with existing ratings assumes the presumption that **some of the renowned companies have already assessed the company's ability to meet its obligations**. Renowned companies and links to their available ratings can be found in the list of sources of information.

Rating	Yes		No	
<b>Existence of rating (S&amp;P, Moody's, Fitch)</b>	See the value of rating ↓		Continue to scorecard without rating →	
<b>Value of rating</b>				
<b>Scale of rating (Moody's)</b>	Aaa, Aa1, Aa2, Aa3	A1, A2, A3	Baa1, Baa2, Baa3	Ba1, Ba2, Ba3, B1, B2, B3, Caa, Ca, C, D
<b>Scale of rating (S&amp;P a Fitch)</b>	AAA, AA+, AA, AA-	A+, A, A-	BBB+, BBB, BBB-	BB+, BB, BB-, B+, B, B-, CCC, CC, C, D
<b>Evaluation of scorecard</b>	●	●	●	●
<b>Evaluation and recommendation</b>	Safe investment with a very low risk, but at a lower interest rate. High probability of coupon gains payments and repayment of nominal value.	Still safe investment with a slight vulnerability to unfavorable conditions. High probability of coupon payments and nominal value repayment.	Medium-safe to speculative investment. The company is likely to be able to meet its obligations, but there is a higher risk.	Very speculative investment. Issuers' deterioration of conditions and therefore inability to repay its obligations is expected. Only for very dynamic investors



## Scorecard **WITHOUT** ratings

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## Scorecard with absent ratings



Scorecard with absent ratings should be used **when there is no access to the rating**. This is likely to be corporate bonds of small and medium-sized businesses. If the investor is **not considered an experienced investor, we recommend not to invest in these bonds**.

Prospectus approved by Czech National Bank	Yes		No	
Existence of prospectus	1 point		0 points	
Financial statements	Balance sheet, Profit and loss statement	Cashflow statement		Annual report and future outlook
Publishing of financial statements (min. of 3 years). Multi-choice. If not published – 0 points	0,5 points	0,5 points		0,5 points
History of the corporation	> 10 years	5 – 10 years	1 – 5 years	< 1 year
No. of years of existence of the corporation	1,5 points	1 point	0,5 points	0 points
Owner of the corporation	Government		Other	
Government as higher security	2 points		0 points	
Intermediary	Established financial institution under the supervision of the Czech National Bank		Other	
Bond distribution typology	1 point		0 points	

Continuation of the scorecard on the next page

## Continuation – Scorecard with absent ratings

Size of the corporation	> 24	24 - 8	8 – 3,2	3,2 – 0,8	0,8 – 0,4	< 0,4
Size according to revenues (in CZK bn.)	3 points	2 points	1,5 points	1 point	0,5 points	0 points
EBITDA/Revenues (EBITDA margin)	> 45 %	45 – 25 %	25 – 18 %	18 – 10 %	10 – 5 %	< 5 %
<ul style="list-style-type: none"> <li>• EBITDA/Revenues</li> <li>• Available in profit and loss statement</li> <li>• EBITDA = Earnings before interest and taxes (EBIT) + depreciation and amortization (E.)</li> <li>• Revenues = Rows (I.), (II.) and (III.)</li> </ul>	<b>In the field of financial statements and ratios check at least 3 consecutive years</b>					
	3 points	2 points	1,5 points	1 point	0,5 points	0 points
Debt/EBITDA	< 1,5		1,5 – 2	2 - 3		> 3
<ul style="list-style-type: none"> <li>• Available in profit and loss statement</li> <li>• Debt (Usually liabilities in the statement (B.))</li> <li>• EBITDA = Earnings before interest and taxes (EBIT) + depreciation and amortization (E.)</li> </ul>	2 points		1 point	0,5 points		0 points
EBITDA/Interest (Interest coverage ratio)	> 15		15 - 10	10 – 6		< 6
<ul style="list-style-type: none"> <li>• Available in profit and loss statement</li> <li>• EBITDA = Earnings before interest and taxes (EBIT) + depreciation and amortization (E.)</li> <li>• Interest expense (N.)</li> </ul>	2 points		1 point	0,5 points		0 points

Continuation of the scorecard on the next page

## Continuation – Scorecard with absent ratings

Evaluation of scorecard	● 17 – 13 points	● 12,5 - 10 points	● 9,5 - 7 points	● 6,5 – 0 points
<b>Evaluation and recommendation</b>	<p>Safe investment with a very low risk, but at a lower interest rate. High probability of coupon gains payments and repayment of nominal value.</p>	<p>Still safe investment with a slight vulnerability to unfavorable conditions. High probability of coupon payments and nominal value repayment.</p>	<p>Medium-safe to speculative investment. The company is likely to be able to meet its obligations, but there is a higher risk.</p>	<p>Very speculative investment. Issuers' deterioration of conditions and therefore inability to repay its obligations is expected. Only for very dynamic investors.</p>



## Additional section – other factors to consider

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## Additional section – other factors to consider

Securing	Description
<b>Securing can play a crucial role when choosing a bond</b>	As far as securing is concerned, it can take different forms. Often the bond is secured by the bill of exchange of the business owner. But it can also be a real estate, etc. It is important to estimate the quality of the securing. In the case of a highly leveraged issuer, we consider securing as important.
Investment horizon	Description
<b>Investment horizon influencing the level of coupon and risk</b>	In general, the longer the period in which the investor is willing to hold the bond, the greater the coupon yield. In addition, if the investor does not plan to hold the bond until its maturity, there is a higher risk of volatility over a longer maturity of the bond. Changes in interest rates have a direct impact on the price of bonds and can therefore result in either income or loss.
Liquidity	Description
<b>Higher liquidity represents easier sale and lower transaction costs</b>	Liquidity generally indicates the ability and possibility to convert a certain asset into cash. From an investor point of view and the issuance of bonds, we will be interested in whether the issue is traded on the stock exchange. On the stock exchange, mostly large issuances of reputed companies are traded, so the sale of the bond will be easier and its transaction costs lower.
Coupon	Description
<b>Coupon also as a risk indicator</b>	Usually, but not in every case, the higher the coupon, the higher the risk. Also, in the case of a fixed coupon, the longer the maturity with this coupon, the greater the risk for the investor. A variable coupon can serve as an alternative.

## Additional section – other factors to consider

Planned debt	Description
<b>Certain ratio of debt to equity better for investors</b>	For investors, active debt policy will be more favourable. This involves maintaining a certain ratio of debt to equity (debt-to-equity ratio).
Purpose of issuance	Description
<b>Why the company wants money</b>	The investor should also be interested in the purpose of the issue. The reason why the corporation actually needs the money. This also makes it possible to better assess the likelihood that the investor will get his money back. The seniority of the bonds and the willingness of the bank to lend money also play a role here.
Industry	Description
<b>Diverse industries entail different risks</b>	The industry, in which the company operates is also one of the factors that have a direct impact on the risk of the bond. The table below breaks down the industries by rating agencies and also lists the individual risks associated with them according to company Coface.
Risk	Industry
<b>Low</b>	Pharmaceutical industry
<b>Medium</b>	Agricultural and food-processing industry, automotive industry, chemical industry, energy industry, information and communication technology, metal industry, paper industry, services, clothing industry, forest-based industry
<b>High</b>	Construction industry, transportation



## Example of issuance of the corporate bond **WITHOUT** ratings

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## Example of issuance of bonds of ABC, s.r.o.



- An example of issuance **without** rating can be issuance of **ABC, s.r.o.**
- The company was established on **18th December 2006** and is mainly engaged in operating sauna centres
- ABC, s.r.o. issues bonds in order to **expand its business**. The minimum investment is **10,000 CZK** and the yield is **6,25 %**. The maturity of the bond is in **4 years**. For instance, bonds are **offered through various internet servers**

Prospectus from Czech National Bank	Yes		No	
Existence of prospectus	1 point		0 points	
Financial statements	Balance sheet, Profit and loss statement	Cashflow statement		Annual report and future outlook
Publishing of financial statements (min. of 3 years). Multi-choice. If not published – 0 points	0,5 points	0,5 points		0,5 points
History of the corporation	> 10 years	5 – 10 years	1 – 5 years	< 1 year
Number of years of existence of the corporate	1,5 points	1 point	0,5 points	0 points
Owner of the corporation	Government		Other	
Government as higher security	2 points		0 points	
Intermediary	Established financial institution under the supervision of the Czech National Bank		Other	
Bond distribution typology	1 point		0 points	

## Example of issuance of bonds of ABC, s.r.o.

Size of the corporation	> 24	24 - 8	8 – 3,2	3,2 – 0,8	0,8 – 0,4	< 0,4
Size according to revenues (in CZK bln.)	3 points	2 points	1,5 points	1 point	0,5 points	0 points
EBITDA margin	> 45 %	45 – 25 %	25 – 18 %	18 – 10 %	10 – 5 %	< 5 %
<ul style="list-style-type: none"> <li>• EBITDA/Revenues</li> <li>• Available in profit and loss statement</li> <li>• EBITDA = Earnings before interest and taxes (EBIT) + depreciation and amortization (E.)</li> <li>• Revenues = Rows (I.), (II.) and (III.)</li> </ul>	<b>In the field of financial statements and ratios check at least 3 consecutive years</b>					
	3 points	2 points	1,5 points	1 point	0,5 points	0 points
Debt/EBITDA	< 1,5	1,5 – 2	2 - 3	> 3		
<ul style="list-style-type: none"> <li>• Available in profit and loss statement</li> <li>• Debt (Usually liabilities in the statement (B.) EBITDA = Earnings before interest and taxes (EBIT) + depreciation and amortization (E.)</li> </ul>	2 points	1 point	0,5 points	0 points		
Interest coverage ratio EBITDA/interest	> 15	15 - 10	10 – 6	< 6		
<ul style="list-style-type: none"> <li>• Available in profit and loss statement</li> <li>• EBITDA = Earnings before interest and taxes (EBIT) + depreciation and amortization (E.)</li> <li>• Interest expense (N.)</li> </ul>	2 points	1 point	0,5 points	0 points		

## Example of issuance of bonds of ABC, s.r.o



- The score of the company ABC, s.r.o. according to our proposed scorecard with absence of rating is 3
- Therefore, we consider this as a very speculative investment where there could be a deterioration of conditions or even bankruptcy of the issuer
- However, an experienced investor must also consider other factors that we have defined in the additional chapter
- For investments from inexperienced and conservative investors, we strongly discourage investing in these bonds

Evaluation of scorecard	● 17 - 13 points	● 12,5 - 10 points	● 9,5 - 7 points	● 6,5 – 0 points
<b>Evaluation and recommendation</b>	Safe investment with a very low risk, but at a lower interest rate. High probability of coupon gains payments and repayment of nominal value.	Still safe investment with a slight vulnerability to unfavorable conditions. High probability of coupon payments and nominal value repayment.	Medium-safe to speculative investment. The company is likely to be able to meet its obligations, but there is a higher risk.	Very speculative investment. Issuers' deterioration of conditions and therefore inability to repay its obligations is expected. Only for very dynamic investors.



## Example of issuance of the corporate bonds WITH ratings

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## Example of issuance of bonds of XYZ, s.r.o.



- An example of issuance with existence of rating can be company XYZ, s.r.o.
- XYZ, s.r.o. is one of the largest issuers of corporate bonds in the Czech Republic
- Based on S&P rating, XYZ, s.r.o. in 2014 obtained BBB rating with a stable outlook
- In 2018, this rating was affirmed again with a stable outlook

### XYZ, s.r.o.

Issuer Credit Rating					
Rating Type	Rating	Rating Date	Regulatory Identifiers	CreditWatch/ Outlook	CreditWatch/ Outlook Date
Local Currency LT	BBB <a href="#">Regulatory Disclosures</a>	25-Jul-2014	EU	Stable	25-Jul-2014
Foreign Currency LT	BBB <a href="#">Regulatory Disclosures</a>	25-Jul-2014	EU	Stable	25-Jul-2014

[View Ratings Definitions](#)

[Debt Types](#) ▾

### Czech Republic-Based XYZ s.r.o. „BBB“ Rating Affirmed; Outlook Stable

15-Jun-2018 09:27 EDT

XYZ s.r.o. continues to benefit from stable cash flow generation from long-term ship-or pay contracts in the transit business, and from its regulated gas transmission operations in the Czech Republic. However, in the next two to-three years, XYZ s.r.o...

## Example of issuance of bonds of XYZ, s.r.o.



- S&P's rating BBB marks medium-safe to speculative investment. The company will probably be able to meet its obligations, but some risk can not be ruled out.

Rating	Yes		No	
<b>Existence of rating (S&amp;P, Moody's, Fitch)</b>	See the value of rating		Continue to scorecard with absence of rating	
Value of rating				
<b>Scale of rating (Moody's)</b>	Aaa, Aa1, Aa2, Aa3	A1, A2, A3	Baa1, Baa2, Baa3	Ba1, Ba2, Ba3, B1, B2, B3, Caa, Ca, C, D
<b>Scale of rating (S&amp;P a Fitch)</b>	AAA, AA+, AA, AA-	A+, A, A-	BBB+, BBB, BBB-	BB+, BB, BB-, B+, B, B-, CCC, CC, C, D
Evaluation of scorecard				
<b>Evaluation and recommendation</b>	Safe investment with a very low risk, but at a lower interest rate. High probability of coupon gains payments and repayment of nominal value.	Still safe investment with a slight vulnerability to unfavorable conditions. High probability of coupon payments and nominal value repayment.	Medium-safe to speculative investment. The company is likely to be able to meet its obligations, but there is a higher risk.	Very speculative investment. Issuers' deterioration of conditions and therefore inability to repay its obligations is expected. We strongly do not recommend it.



## Information sources and links

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## Information sources and links

Corporate ratings	Links
Moody's, S&P, Fitch Ratings and Czech Credit Bureau websites	<ul style="list-style-type: none"><li>• <a href="https://www.standardandpoors.com/en_US/web/guest/home">https://www.standardandpoors.com/en_US/web/guest/home</a></li><li>• <a href="https://www.moody.com/">https://www.moody.com/</a></li><li>• <a href="https://www.fitchratings.com/site/home">https://www.fitchratings.com/site/home</a></li><li>• <a href="https://www.crif.cz/">https://www.crif.cz/</a></li></ul>
Prospectus from Czech National Bank	Links
Czech National Bank prospectus register	<ul style="list-style-type: none"><li>• <a href="http://oam.cnb.cz/sipresextdad/SIPRESWEB.WEB_PROSPECTUS.START_INPUT_OAM?p_lang=cz">http://oam.cnb.cz/sipresextdad/SIPRESWEB.WEB_PROSPECTUS.START_INPUT_OAM?p_lang=cz</a></li></ul>
Information about corporations	Links
Basic information, financial statements	<ul style="list-style-type: none"><li>• <a href="https://or.justice.cz/ias/ui/rejstrik">https://or.justice.cz/ias/ui/rejstrik</a></li><li>• <a href="https://www.rizikovedluhopisy.cz/">https://www.rizikovedluhopisy.cz/</a></li></ul>