Performance of Credit Rating Agencies In India-A Perceptional Study Of Credit Rating Agencies

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Abstract

Credit rating agencies in India have evolved as a prominent force in developing the financial markets and creating awareness among the investors over years. Serving as information intermediaries between the issuers and investors, the rating agencies are in the process of developing new methods for performance measurement and are transiting into new areas. During its long existence of a decade, the ratings industry has evolved greatly and has been playing a pivotal role in the Indian markets. The increasing significance of credit rating services could be discerned from their past performance. There has been a tremendous expansion of their operations thereby exerting significant impact on the industrial capitalization both in quantitative and qualitative terms. Credit Rating is an opinion expressed by an independent professional organization, after making a detailed study of all relative factors2. Such an opinion will be of great assistance to investors in taking decisions regarding the investment. It also helps the issuers of debt instruments to price their issues correctly and to reach out to new investors. Regulators like Reserve Bank of India (RBI) and Securities and Exchange Board of India (SEBI) often use credit rating to determine the eligibility criteria for some instruments. For example, the RBI has stipulated a minimum credit rating by an approved agency for the issue of commercial papers. In general, credit rating is expected to improve quality consciousness in the market and establish, over a period of time, a more meaningful relationship between the quality of debt and yield from it. Credit rating is also a valuable input in establishing business relationships of various types.

KEY WORDS: *Credit Rating, Information Intermediaries, Financial Markets, Credit worthiness, Industrial Capitalisation, Investment Decisions, Debt Instruments, Pricing Issues*

1. INTRODUCTION

Credit rating services, in terms of a credit rating, reflect the opinion of credit rating agencies on the credit worthiness of a particular company as regard to a security, or an obligation or the likelihood that debt will be repaid. The credit rating agencies play a crucial role in enabling the investors to differentiate among debt instruments on the basis of their underlying credit quality. The credit rating services provide an additional channel for mobilizing funds and ensuring improvements in productivity of investments through relative ranking symbols.

Credit rating agencies in India have evolved as a prominent force in developing the financial markets and creating awareness among the investors over years. Serving as information intermediaries between the issuers and investors, the rating agencies are in the process of developing new methods for performance measurement and are transiting into new areas. During its long existence of a decade, the ratings industry has evolved greatly and has been playing a pivotal role in the Indian markets.

2. THE NEED FOR CREDIT RATING

Credit Rating is an opinion expressed by an independent professional organization, after making a detailed study of all relative factors. Such an opinion will be of great assistance to investors in taking decisions regarding the investment. It also helps the issuers of debt instruments to price their issues correctly and to reach out to new investors. Regulators like Reserve Bank of India (RBI) and Securities and Exchange Board of India (SEBI) often use credit rating to determine the eligibility criteria for some instruments. For example, the RBI has stipulated a minimum credit rating by an approved agency for the issue of commercial papers.

In general, credit rating is expected to improve quality consciousness in the market and establish, over a period of time, a more meaningful relationship between the quality of debt and yield from it. Credit rating is also a valuable input in establishing business relationships of various types.

One of the fundamental economic problems faced by developing countries is the difficulty in mobilizing funds to increase the investment. This makes an access to national and international capital markets which are apparently important resources for obtaining funds to raise the level and accelerate the pace of investment and growth. In order to gain access, developing countries must first obtain a favorable rating of their creditworthiness by one or more credit rating agencies. A strong credit rating will play a major role by determining the cost and availability of credit flows.

The rating process of credit rating agencies and their justification and sagacious analysis regarding the consistency in rating of different companies of same sector or divers sectors interested me immensely and the factors have apparently become need for the present study.

3. OBJECTIVES OF THE STUDY

1. To study the need for Credit rating services in India.

2. To ascertain the perceptions of the credit rating agencies (Crisil, Care and Icra) about their own performance assessment.

3. To offer suitable suggestions for the balanced growth of credit rating agencies in the light of the findings.

4. DATA & METHODOLOGY

The study is based on both primary and secondary data. The primary and secondary data for studying the operational and financial performance of the agencies are collected from the records and annual reports through websites from internet. The data relating to other performance aspects, rating methodology and its relevant perceptional concepts are collected through the structured questionnaire.

The said questionnaire is pre-tested among a select sample of Hyderabad localized companies, investors and three rating agencies before its actual administration among the sample companies and investors of concerned agencies.

4.1 Tools of Analysis

In the analysis and interpretation of data, simple statistical measures like percentages are used. Further to examine the extent of performance in totality, Summated Scales (or Likert-type Scales) are used. In addition to this quantitative measures an attempt is also made to furnish the data in a legitimate manner, that is collected through observations and opinion surveys from the respective respondents.

4.2 Sample and Time Period of Study

The three Indian credit rating agencies and their rated companies which are nearly 16 to 18 which have been collected from the official website of credit rating agencies, each from banking, manufacturing, service sectors and financial institutions. Judgment sampling method is used to make the study more appropriate.

The study covers a period of 6 years, commencing from the financial year 2001-02. Almost all the aspects of the study coincide with this study period. It is to be noted hereafter, wherever the study period is mentioned, it simply refers to the period of the 6 years stated.

5. LIMITATIONS

The proposed study is subject to the following limitations.

1. The data collected for the study is confined to a limited time period.

2. The statistical tools are subject to their limitations and bias with regard to their application.

3. The data collected from various sources, inspite of careful attention, is not free from complete bias and errors.

6. ANALYSIS AND FINDINGS

The present is focused on the assessment of overall performance of rating agencies from the agencies point of view. The analysis of the perception of agencies has made it very clear that the role of rating agencies is prominent and worth prospective in India. Broadly the major findings of study are;

PERCEPTION OF THE RATING AGENCIES

To make the study very effective, a scheduled questionnaire has been administered on three credit rating agencies. It is intended to study the objectivity of opinions and differences of the respondents of concerned agencies representing wholly or partly the agency opinion.

1. They gave the meaning of credit rating as the credibility of issuer or borrower to repay or indication of the credit worthiness of the company to repay.

2. The agencies preferred to rate the debt instruments first and other short term instruments next.

3. Credit rating agencies presume their role in India as moderate when compared to other countries.

4. The agencies preferred to rate the specific instrument rather than the company or industry as a whole.

5. The agencies revealed that the validity period of rating of specific instrument would vary from one year to the life of the instrument issued.

6. The credit rating agencies consider that credit rating is important to investors, corporate borrowers and institutions but most of all it is more beneficial to investors.

7. They treat credit rating service would act as an additional information provider, rather than any substitute for the investigation or surety for good performance.

8. The credit rating agencies believe that a good rating would enable a company to raise the funds at lower or cheaper than average or high cost.

9. The credit rating agencies agree that credit rating would forewarn the risks associated with particular securities while rating.

10. The analysis clearly reveals that credit rating agencies would prefer the merchant banker's guidance role to the investors.

11. The agencies expressed that the credit rating agencies would judge the credibility of the issuer, performance of an instrument as well as profitability of a company.

12. The credit rating agencies firmly believed agreed that credit rating would act as a marketing tool in creating the company's image.

13. The credit rating agencies also explained that foreign collaborators would prefer credit rating before investment.

14. The analysis revealed that the all services, i.e., information services, advisory services and research services were equally preferred by investors or borrowers apart from credit rating services.

15. The agencies think that lack of uniformity in rating methodology of different agencies would create a slight confusion to the companies approaching.

16. The credit rating agencies believe that credit rating would improve the investment avenues for a company to a great extent.

17. The time period differs in different Agencies as follows:

1)	CRISIL	-	New Company
	6 – 8 Weeks	-	Exiting
	Company	-	2 – 3 Weeks
2)	ICRA	-	New Company
	3 – 4 Weeks	-	Exiting
	Company	-	3 – 4 Weeks
3)	CARE	-	New Company
	2 – 3 Weeks	-	Exiting
	Company	-	2 – 3 Weeks

18. The credit rating agencies expressed that the basis for grading of the companies among the rating agencies should be acceptability of rating and performance of the instrument rated.

19. When the agencies were asked how they were rated the response was as follows:

By Companies - Acceptability of Rating

By Investors - Experience

20. As far as the major limitation of rating process is concerned, the agencies stated that credit rating was treated like a surety and a guarantee, but actually it should be only treated as an information provider.

21. The credit rating agencies consider that credit rating charges for companies were affordable to all.

22. The usual complaint the credit rating agencies get from the companies approached was that the claim for that desired rating.

23. The Agencies represented that there was no drawback in the credit rating services.

24. The duty / responsibility of a company to obtain / maintain good rating would be to provide information to companies and keep record of repayment in track.

25. The agencies apparently felt that the underdeveloped debt market was the cause of gap between India and foreign companies.

26. The credit rating agencies denied to develop compulsory rating options for all companies.

27. If a good rated company fails to fulfill its obligation it would indicates the failure of evaluation as well as future uncertainly.

28. The major problem faced by credit rating agencies was lack of information availability on company's part.

7. SUGGESTIONS

1. Credit rating service sector is an emerging professional body in a globalised era, so much attention, care and interest should be taken to provide right and timely information about the agencies to the companies in quest of capitalization.

2. The quality itself is an effective tool of promotion in marketing, though it is suggested that credit rating agencies should also apply any media tool to approach every corner of the business world easily.

3. It is suggested that credit rating service, if reduces the lengthy formalities and could make the simple and sophisticated method to approach, many more companies may come forward to get rated.

4. It is recommended that credit rating agencies should confirm the information and data submitted by the company concerned to be authentic and without misrepresentation.

5. It is advised that inspite of professional and qualitative service of credit rating agencies there should be no room for any malpractice in assigning a rating to a company at any cost.

6. It is suggested that there are many companies such as the medium and small scale sector, which could not afford the rating charges or fees though they are reasonable. If there be any concessions and relaxations on any ground of qualitative performance aspect it would be worth commendable service from the point of view of credit rating agencies as a professional.

7. It is recommended to have rating system for a company or industry as a whole than of any specific financial instrument, as it is more preferable and acceptable to the investor community.

8. It is advised that credit rating agencies should not be in a hurry in rating, as a formality to perform the task in a very little time, but it should be done in a schedule to assess the company for rating.

9. It is informed with earnest request that the credit rating agencies should consider all the factors and risks before rating a company, not only key factors.

10. It is advised that credit rating agencies should act as a mediator, but not as a guarantor or a surety, who could clarify further the doubts in the minds of investor and borrower to develop the debt market in India.

11. It is recommended that credit rating should be easily and conveniently accesible and approachable in the rural India where the industrialists have prospects to flourish by the untapped market business avenues.

12. It is suggested that Government of India, through the direct control of SEBI should enhance the role and responsibility of credit rating agencies and grade them as per the effectiveness and efficiency in their assessment and default.

13. It is also advised that to the corporate investors as well as individual investors, there should be a special grievance machinery to handle and solve smoothly the investment related issues.

8. CONCLUSION

It is evident from the analysis that the role of credit rating agencies is a must for the corporate world as well as investors in making rational decisions pertaining to their investment activities in both equity and debt market. As India is developing much faster in capital market activities, it is worth advisable to the credit rating agencies and industrial sector to take necessary steps to improve the 'slower' debt market in India.

It is observed that there are many companies such as the medium and small scale sector, which could not afford the rating charges or fees though they are reasonable. If sector, which could not afford the rating charges or fees though they are reasonable, if there be any concessions and relaxations on any ground of qualitative performance.

In the global context, the credit rating will help the investors as a marketing tool in finding the best investment avenue. So there is a need to employ credit rating by all corporate firms with the help of agencies to create a perfect investment market in the country. It is also observed that the respondents of credit rating are looking for other value added services besides the normal rating services.

Hence, the rating agencies an expected to collaborate with foreign agencies in rendering the services as expected by the beneficiaries in reaching their targets and objectives. At the end, it can be asserted that the credit rating agencies should play a fair and pervasive role in providing the services and making Indian Financial Markets very perfect in nature.

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