

# EMPERICAL STUDY ON FUNCTIONING OF CREDIT RATING AGENCIES IN INDIA

\*Pavneet Kaur

\*Assistant Professor, Guru Nanak Khalsa College for Women, Ludhiana.

## ABSTRACT

Credit rating agencies (CRAs) plays a crucial role in financial markets for lenders, investors and issuers in reducing information asymmetry between different parties. Credit rating helps us to know about the credit capability of individuals in a country. When all the investors are positively rated, then there will be an increase in new start-ups. Gradually income of the country increases, Employment opportunities expands and Poverty ranks less. When there is development in all the sectors then the GDP increases and country develops. Analytical research as well as descriptive type of research is used for the study. Secondary as well as primary data has been gathered for the study. Banks helps in knowing the investment status of the country. The credit rating has been a long established part of the financial mechanism abroad. Credit rating agency means a body corporate engaged in the business of rating of securities. Thus, services of Credit rating agencies to the investors play a major role in evaluating risk and return of the investment in taking the decisions. It is very much essential to understand the credit rating agencies methodology process and rating symbols adopted and overall services. This paper emphasizes on functioning of all the rating agencies, methodology, process, symbols and services of CRISIL (Credit rating information service Ltd.), ICRA (Investment information and credit rating agencies), CARE (Credit Analysis and Research Limited), and Fitch India Ltd. The rating agencies in India need to evolve their own methodologies, process, and symbols within the context of macro-economic environment. The sources for the data are through the websites of the rating agencies, journals, newspapers and banks.

**Keywords:** Credit rating, Credit rating agencies (CRA), Process, functioning, Methodology.

## INTRODUCTION

### Credit Rating

Credit rating refers to knowing the credit assess ability of customers that means knowing the credit repayment history of the customer. All the customers who would like to seek loan facilities use credit rating.

### Credit Rating Agencies

Credit rating constitutes an opinion of a rating agency that evaluates the basic credit strength of any customer and his capability to fully and on time meet his debt commitments. Credit Rating specifies the credit praiseworthiness of the borrowers and the possibility of the borrowers will pay back the interest and principal on payable dates.

### Origin of Credit Rating Agencies

The journey of Credit Rating Agency started from 1841 by Lewis Tappan in New York City. Robert Dun, who published its first ratings guide in 1859, then gained it. Another early agency, John Bradstreet, started in 1849 and published a ratings guide in 1857. Credit rating agencies took birth in the United States in the early

1900s, when ratings began to be practical to securities, exclusively those related to the railroad bond market. In the United States, the construction of wide-ranging railroad systems had led to the enlargement of corporate bond issues to finance them, and consequently a bond market several times superior than in other countries. Following the 1907 financial crisis, demand started increasing for the autonomous market information, in particular for independent analyses of bond creditworthiness. In 1909, financial analyst John Moody issued a publication focused solely on railroad bonds. His ratings are the first one to be published extensively in an easy to get to format, and in fact, his company was the first one to charge subscription fees to investors.

Credit Rating Agencies are thus essentially the corporations with specialized functions namely, assessment of the likelihood of the timely payments by an issuer on a financial obligation. In India, the rating activities started with the incorporation of the Credit Rating Information Services of India Ltd. (**CRISIL**) in 1987, which commenced its operations of rating of companies in 1987-1988 and was promoted by Industrial Credit and Investment Corporation of India Ltd. (ICICI) and Unit Trust of India (UTI). The second rating agency Investment Information and Credit rating Agency of India Ltd. (**ICRA**) was incorporated in 1991 and was jointly sponsored by Industrial Finance Corporation of India (IFCI) and other financial institutions and banks. The other rating agency, Credit Analysis and Research Ltd. (**CARE**), incorporated in April 1993, is a credit rating information and advisory services company promoted by Industrial Development Bank of India (IDBI) jointly with Canara Bank, Unit Trust of India (UTI), private sector banks and financial services companies. Another rating agency **ONICRA** Credit Rating Agency of India Ltd., which was incorporated in 1993, is recognized as the pioneer of the concept of individual credit rating in India. Further Duff and Phelps Credit Rating (India) Private Ltd. (**DCR**) was established in 1996, which is presently known as Fitch Ratings India Private Ltd. One more rating agency SME Rating Agency of India Limited (**SMERA**), which was a joint venture of SIDBI, Dun & Bradstreet Information Services (D&B), Credit Information Bureau of India Limited (**CIBIL**), and 11 other leading banks in the country, was established in 2005. A new rating agency, Brickwork Ratings (BWR) that is based in Bangalore was incorporated in 2007. Besides CRISIL (Standard & Poor), ICRA (Moody's), CARE and Fitch, **Brickwork** Ratings is the fifth Credit Rating Agency to be recognized by SEBI.

## OBJECTIVES OF THE STUDY

- To examine and compare the rating symbols of Indian credit rating agencies.
- To analyze the overall services offered by credit rating agencies.
- To study and compare the rating methodology, process of Indian credit rating agencies.

COMPARISON OF RATING SYMBOLS OF CREDIT RATING AGENCIES:

<b>CREDIT RATING SYMBOLS</b>					
CREDIT RATING SYMBOLS OF CRISIL, ICRA and CARE					
Debt Category	Debt Instruments	Rating Symbols			Remarks
		CRISIL	ICRA	CARE	
Long Term Instrument	Debentures Bonds Preference shares	AAA *AA *A  *BBB *BB *B *C  D	LAAA *LAA *LA  *LBBB *LBB *LB *LC  LD	CARE AAA *CARE AA *CARE A *CARE BBB *CARE BB *CARE B *CARE C CARE D	Highest Safety High safety Adequate safety Moderate safety Inadequate safety Risk prone Substantial risk Default
Medium Term Instrument	Fixed deposits	FAAA *FAA *FA  *FB *FC  FD	MAAA *MAA *MA  *MB *MC  MD	CARE AAA *CARE AA *CARE A *CARE BBB *CARE BB *CARE B *CARE C CARE D	Highest Safety High safety Adequate safety Inadequate safety --do-- --do-- Risk prone Default
Short Term instrument	Commercial Paper	*P1 *P2 *P3 *P4 P5	*A1 *A2 *A3 *A4 A5	*PR-1 *PR-2 *PR-3 *PR-4 PR-5	Highest safety High safety Adequate safety Risk prone Default

*Note :* \* The suffix of "+" (plus) or "-" (minus) signs are added with the rating symbols to indicate the comparative positions of the instrument within the group covered by the symbol

SOURCE : Brochures of Various Credit Rating Agencies.

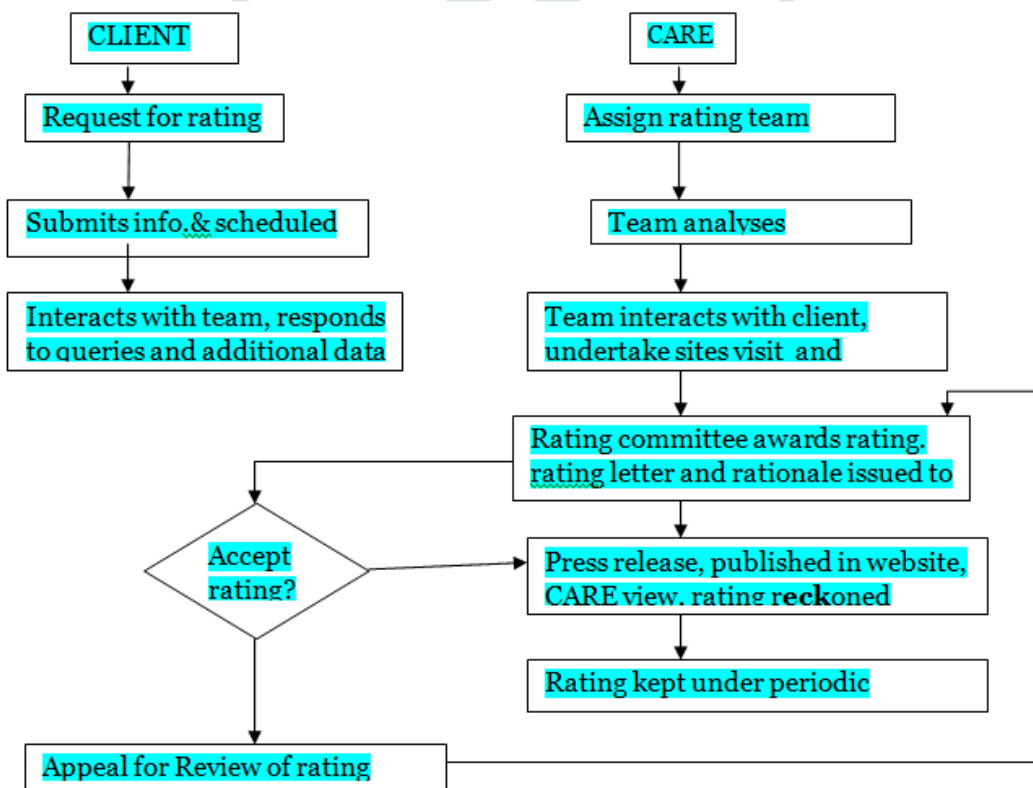
RATING PROCESS OF CREDIT RATING AGENCIES  
CRISIL'S RATING PROCESS



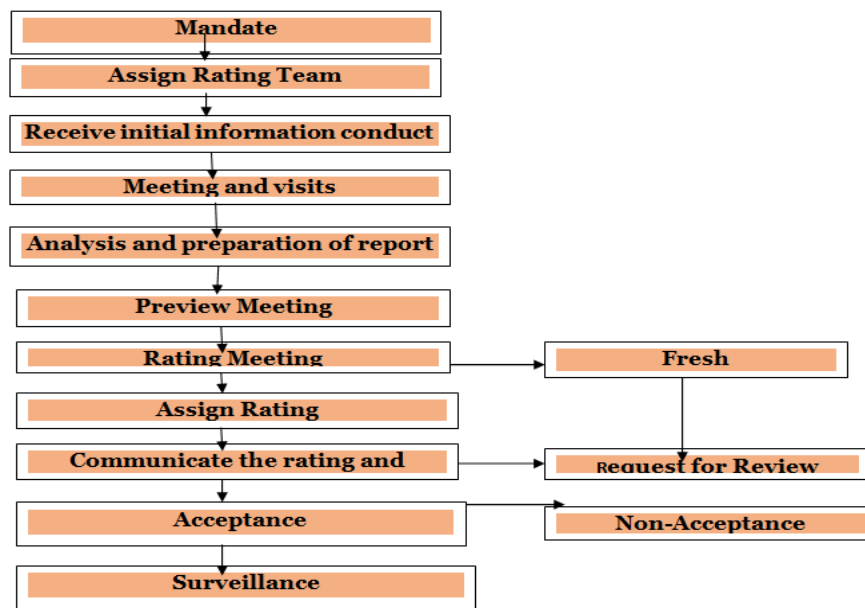
### FITCH RATING PROCESS



### ICRA RATING PROCESS



## CARE RATING PROCESS



## RATING METHODOLOGY

Rating Methodology refers to the use and application of tools in the rating. Rating is undertaken by four different agencies in India, namely, CRISIL, ICRA, CARE and Fitch India, with minor differences in the four, the basic parameters of all of them remain the same. However, presentation of each category has its own value and implication. In addition, it is observed that all rating agencies in India more or less follow similar methodology, which is based on international practice of their counter parts. The methodology encompasses all the key factors for rating assessment and assignment. Rating agencies focused on wide range of factors ranging from macro level factors to micro level factors. The both qualitative as well as quantitative factors are considered by the agencies before assigning any ratings. The common and important factors are considered and analyzed in rating methodology by different rating agencies. These agencies follows typically **CRAMEL** model to evaluate the debt servicing capabilities of banks and institutions. CRAMEL stands for Capital adequacy, Resources, Asset quality, Management quality, Earnings potential and Liquidities.

## CONCLUSION

Indian credit rating agencies have made strategic alliance with reputed international agencies. The rating agencies in India have to evolve their own methodologies, process, and symbols within the context of macro-economic environment. The analyses and assessments provided by various credit rating agencies provide investors with information and insight that facilitates their ability to examine and understand the risks and opportunities associated with various investment environments. It is an undisputed fact that CRAs play a key role in financial markets by helping to reduce the informative asymmetry between lenders and investors, on one side, and issuers on the other side, about the creditworthiness of companies (corporate risk) or countries (sovereign risk). An investment grade rating can put a security, company or country on the global radar, attracting foreign money and boosting a nation's economy. Indeed, for emerging market

economies, the credit rating is key to showing their worthiness of money from foreign investors. Credit rating helps the market regulators in promoting stability and efficiency in the securities market. Ratings make markets more efficient and transparent.

## REFERENCES

- Credit Rating Information Services of India Limited (CRISIL, [www.crisil.com](http://www.crisil.com))
- Investment Information and Credit Rating Agency of India (ICRA, [www.icra.in](http://www.icra.in))
- Credit Analysis & Research Limited (CARE, [www.careratings.com](http://www.careratings.com))
- ONICRA Credit Rating Agency of India Ltd. ([www.onicra.com](http://www.onicra.com))
- V K Sharma and Chandan Sinha, 'The corporate debt market in India'
- M Y Khan, 2005 FINANCIAL SERVICES, 3<sup>rd</sup> edition, Tata McGraw-Hill Publications company Ltd. ISBN NO. 0-07-055885-7

