

## **FAQs on Credit Rating**

### **What is a credit rating and what does it convey?**

Credit rating is a qualitative & quantitative assessment of the probability of default on payment of interest and principal on a debt instrument. It is not a recommendation to buy, sell or hold a debt instrument. Credit Rating only provides an additional input to the investor and the investor is required to make his own independent and objective analysis before arriving at an investment decision.

### **How does a credit rating agency differ from a credit bureau?**

A credit rating agency provides an opinion relating to future debt repayments by borrowers. A credit bureau provides information on past debt repayments by borrowers.

### **How is a rating denoted?**

Rating is denoted by a simple alpha-numeric symbol, for e.g. AAA, AA+, A-, etc. For a complete list of ratings symbols and their definitions refer to India Ratings website [www.indiaratings.co.in](http://www.indiaratings.co.in)

### **Whether the issuer company is rated or the instrument?**

The rating is assigned to a security or an instrument. Ind-Ra also assigns issuer rating.

### **How is credit rating done?**

Ratings are based on a comprehensive evaluation of the strengths and weaknesses of the company fundamentals including financials along with an in-depth study of the industry as well as macro-economic, regulatory and political environment.

### **What do the various rating symbols mean?**

Each rating symbol is an alpha-numeric representation of degree of repayment risk associated with debt instruments. For a complete list of ratings definitions and their symbols refer to India Ratings website.

### **Are rating symbols the same across all types of debt instruments?**

No. Rating symbols may vary depending on the type of debt instrument and the tenure i.e. long term or short term. For a complete list of ratings definitions and their symbols refer to India Ratings website.

### **What do the “+” and “-” sign indicate in a rating?**

Plus and minus symbols are used to indicate finer distinctions within a rating category. The minus symbol associated with ratings has no negative connotations. In fact, ratings in a higher rating category such as ‘AA-’ are stronger than ratings in a lower rating category such as ‘A+’. For a complete list of ratings definitions and their symbols refer to India Ratings website.

### **What are investment and speculative grade ratings?**

An investment grade rating signifies the rating agency's belief that the rated instrument is likely to meet its payment obligations. In the Indian context, debt instruments rated 'BBB-' and above are classified as investment grade ratings.

Instruments that are rated 'BB+' and below are classified as speculative grade category ratings in which case the ability to meet the payment obligations is considered to be "speculative". Instruments rated in the speculative grade are considered to carry materially higher risk and a higher probability of default compared to instruments rated in the investment grade.

### **What difference will a rating make to my borrowing costs?**

A credit rating does not guarantee lower borrowing costs. Investors and lenders are free to set lending margins at any level that makes commercial sense. Additionally, at low levels of rating, the capital costs applied may be the same whether or not a borrower is rated, or may in fact be higher (for example, if a borrower has both a small exposure and a very low rating). However, to the general benefit of higher-rated entities, implementation of Basel II in India is expected to make the bank system in general more discriminating in its allocation of capital, and more risk-sensitive in assigning lending margins.

### **Who regulates rating agencies?**

Credit rating agencies are regulated by Securities and Exchanges Board of India (SEBI). The SEBI (Credit Rating Agencies) Regulations, 1999 govern the credit rating agencies and provide for eligibility criteria for registration of credit rating agencies, monitoring and review of ratings, requirements for a proper rating process, avoidance of conflict of interest and inspection of rating agencies by SEBI, amongst other things.

### **Does SEBI have a role in the rating exercise?**

SEBI does not play any role in the assessment made by a credit rating agency. The rating is intended to be an independent, unbiased and professional opinion of a credit rating agency.

### **Is rating a one-time exercise?**

No. To protect the interest of investors, SEBI has mandated that every credit rating agency shall, during the lifetime of the securities rated by it, continuously monitor the rating of such securities and carry out periodic reviews of all published ratings.

### **What is the validity period of a credit rating?**

A rating is expected to remain valid until the rated debt obligation is fully paid or the rating is withdrawn and is subjected to a periodic review to ascertain the validity of the same.

### **Why do ratings change?**

Rating is an opinion based on information available at a point in time with the rating agency and expectations made on the basis of such information by the agency. However, information and expectations can change significantly over time, thereby affecting the future repayment abilities and thus, requiring the rating to be altered.

### **What does a rating downgrade indicate?**

Rating is monitored throughout the life of the instrument. A downgrade in the rating indicates that the risk of default of the instrument is higher than what was earlier predicted.

### **From where can the credit ratings of instruments be obtained?**

Credit ratings assigned by India Ratings to various instruments are made available on its website and through press releases. To subscribe to such press releases you can refer to India Ratings website. The same are also available in the prospectus or the offer document of the issuer company and in media advertisements.

### **What are the common factors that are taken into account while awarding the credit rating?**

India Ratings has a set of criteria for assigning the ratings (To read rating criteria of India Ratings refer to India Ratings website). Examples of some factors that may be taken into consideration for credit rating are Issuer Company's operational efficiency, level of technological development, financials, competence and effectiveness of management, past record of debt servicing, etc.

### **How can an investor know if any credit rating assigned has been changed or updated?**

India Ratings continuously monitors the ratings assigned to a particular instrument. In case of any changes in the ratings so assigned, India Ratings discloses the same through press releases and on its websites.

### **Does a credit rating assure repayment?**

A credit rating is not an assurance of repayment of obligations under the rated instrument. Rather, it is an opinion on the relative degree of risk associated with such repayment.

### **Who pays for a credit rating?**

The Issuer who wants to get rated pays towards the remuneration of fees for credit rating.

### **If the issuer pays for the rating, how does a credit rating agency maintain its independence?**

Although the issuer pays for the rating, the investor uses it. Like any other product or service, the 'value' of the rating depends entirely on the perceptions of the investor. Investor perceptions are based on the credibility of the past ratings assigned by each rating agency. In addition credit rating agencies are also expected to follow Code of Ethics and Business Conduct which are available on the rating agency's website.

### **How are rating agencies evaluated?**

Though there is no formal method of evaluating a rating agency, the international best practice is to refer the transition and default study of the agency. This gives the investor an indication of the stability and reliability of the ratings given by the agency. To access the T&D study of India Ratings refer to India Ratings website.

### **How much time does it take for the rating process to be over?**

Credit Rating is an exhaustive exercise which typically takes about 3-4 weeks to complete from the date of receipt of the adequate information to carry out the process.

### **What is Outlook/Watch?**

Rating Outlooks indicate the direction in which a rating is likely to move over a one to two year period. They reflect financial or other trends that have not yet reached the level that would trigger a rating action, but which may do so if such trends continue. The majority of Outlooks are generally Stable, which is consistent with the historical migration experience of ratings over a one to two year period. Positive or Negative rating Outlooks do not imply that a rating change is inevitable and, similarly, ratings with Stable Outlooks can be raised or lowered without a prior revision to the Outlook, if circumstances warrant such an action.

Rating Watches indicate that there is a heightened probability of a rating change and the likely direction of such a change. These are designated as Positive, indicating a potential upgrade, Negative, for a potential downgrade, or Evolving if ratings may be raised, lowered or affirmed. However, ratings that are not on Rating Watch can be raised or lowered without being placed on Rating Watch first, if circumstances warrant such an action. A Rating Watch is typically event-driven and, as such, it is generally resolved over a relatively short period. The event driving the Watch may be either anticipated or have already occurred, but in both cases, the exact rating implications remain undetermined.

### **What are provisional ratings?**

Where a rating is prefixed as [Provisional], it indicates that a full rating has been assigned based upon the agency's expectations regarding final documentation or certain steps pending, typically based upon a review of the final draft documentation provided by the issuer. If such final documentation is received or steps pending are executed as expected, the provisional rating will typically be converted to a final rating.

Provisional ratings are not conditional upon receipt of further analytical information. By the time a provisional rating is assigned to a transaction, no change is anticipated to that opinion other than in exceptional circumstances. While provisional ratings typically convert to final ratings within a short time, determined by timing of transaction closure, in the period between assignment of a provisional rating and a final rating, provisional ratings may be raised, lowered or placed on Rating Watch or withdrawn, as with final ratings.

### **What are Structured Obligation (SO) and Credit Enhancement (CE) ratings?**

Based on certain characteristics, an instrument can be assigned Structured Obligation (SO) ratings. A suffix in the form of '(SO)' indicates a credit enhancement and a structured payment mechanism and is typically assigned to instruments from the ratings of securitized debt and asset backed transactions where the credit enhancement/structure around cash flows leads to rated instrument being bankruptcy remote of the issuer/originator. 'CE' (Credit Enhancement) is suffixed to rating of instruments having explicit credit enhancement and are not securitized debt and asset backed transactions i.e. All ratings where the credit enhancement is external (or from third party), but the rated instrument is not bankruptcy remote of the issuer/ originator.

### **What happens when issuers stop cooperating?**

In case an issuers who stops cooperating or does not share information to carry out a rating, India Ratings will try to carry out the process on the basis of best available information in the public domain. Such ratings will be marked with a suffix "ISSUER NOT COOPERATING\*". This will be followed by an asterisk mark. The asterisk mark shall be explained and shall read as 'Issuer did not cooperate; based on best available information'. India Ratings will communicate such ratings through its usual communication channels such as press release, website, etc. In line with regulatory requirement, investment grade ratings in Issuer Not Cooperating status, outstanding for more than six months with Ind-Ra, will necessarily be downgraded to the non-investment grade, while maintaining the Issuer Not Cooperating status. This action will be taken regardless of whether the issuer is cooperating or not cooperating with any other CRA.

### **Can the issuer appeal if he not satisfied with the rating outcome?**

If the issuer is not satisfied with the rating outcome, an appeal on the decision can be constituted as per the provisions laid out in the rating process manual available on the website of India Ratings.

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