



LET'S TALK ABOUT...

FINANCIAL LEXICON EDITED BY THE SWISS ASSOCIATION OF ASSET MANAGERS

Rating Agencies

Rating agencies evaluate the financial conditions of private and public institutions that issue financial instruments aimed at investors, and deliver the related grade statements.

There are many of them around the world but the most renowned and influential are Standard & Poor's Corporation and Moody's Investors Service Inc., headquartered in New York City and Fitch Rating Inc., which has main offices both in New York and London.

They apply standardized methods and consider several factors, then stating a rating which however varying in terms of label details, ranges from the top financial reliability and safety, the prestigious AAA grade, down through the various B and C levels until the ill-famed D mark, which states the issuer's default, that is its inability to face obligations in full and at due time, so not complying with the original terms.

The importance of these agencies is considerable in influencing the markets and the strategies of the issuers themselves, as current events show in relation to a possible Greece's default.

A downgrading normally causes increased borrowing costs for the issuer and, as a more harsher consequence, securities which become rated below certain levels may not be held in the portfolio of certain institutional investors, such as pensions funds, insurance companies and so on.

For private issuers, such as banks and corporations, the basic criteria which agencies review and assess are their financial status (which is essentially evaluated through ratios), their histories and the environments in which they operate. In evaluating governmental issuers (sovereign) the matter is some more complex, because more qualitative and less predictable factors are to be taken into account, as well as political and social related issues. It may be fundamental, as a matter of instance, not only the actual ability to repay debts, but also the political willingness to do so. The assigned rating is the result of a committee vote, where the specialist members, aside from their seniority, have equal weight in determining the final result. The agencies also issue outlooks about the issuer's perspectives and monitor "critical" issuers which are included in special watching lists. - *GLT*

The views expressed are not necessarily those of the Swiss Association of Asset Managers