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NEED FOR UNIFORM RATING SCALES ACROSS ALL RATING AGENCIES

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Abstract

Credit Rating Agencies (CRAs) play an important role in the financial markets and in India, they work along with the regulator in regulating the market. They are mentioned in many statutory regulations of SEBI, IRDA, RBI, NSIC etc. Corporate debt market in India has developed manifold over the last decade and regulators believe that CRAs credit assessment capabilities is a necessary input for obtaining quality rating. Entry of new agencies with good analytical abilities and fair competition will help in the growth of debt market. They are five registered rating agencies in India out of which few agencies hold the major market share. The rating given by the CRAs is on an ordinal scale denoted by a rating symbol. Each rating agencies rate debt instruments with different rating symbols and SEBI achieved standardization of rating symbols for debt instruments (includes mutual fund schemes and structured obligations) alone. There are other ratings that are yet to be standardized. Financial literacy is still in the nascent stage in India and uniform rating scale will help the investor community to better understand the repaying ability of the issuers. Moreover, for fair competition to emerge and for the benefit of all the investors it is important that the rating symbols are standardized. This paper deals with the need for standardization and perspective of the regulators (who influence the ratings market at the international level) regarding standardization of rating scale. It is also important to view the rating symbols of various rating agencies in a comparable scale to infer if there is any difference in their symbols and definition.

Keywords: **IOSCO; SEC; ESMA; Standardization; Competition**
JEL classification: **K22, G21, G22, G24, G28**

INTRODUCTION

Credit ratings are embedded in the countries securities regulation [1] and have far reaching implications in the world economy. Credit Rating agencies are private institutions whose main role is to measure the relative credit risk of the financial instruments. CRAs have gained further influence over the financial markets, through governmental regulations that mandate the use of ratings and through private contract rating requirements. They were subjected to very little regulatory oversight by the government agencies. They failed to provide accurate ratings for the structured instruments which led to the financial crisis in 2008. A broad consensus exists among policy makers and regulators, that the increased competition and transparency between ratings providers is a tool for improving ratings quality [2]. OECD [3] in its hearings on competition and credit rating agencies stated that the credit rating market, a natural oligopoly is controlled by few dominant players with more than 90% of the market and increasing competition will improve the performance of the industry. Competition would be meaningful only when investors are able to compare the ratings given by different agencies.

There is no standardized definition for many terms related to rating agency across the world. For instance, according to Securities Exchange Board of India [4] "rating" means an opinion regarding securities, expressed in the form of standard symbols or in any other standardized manner, assigned by a credit rating agency and used by the issuer of such securities, to comply with a requirement specified by these regulations. International Organization Securities Commission [5] defines “Credit rating” or “rating” as an assessment regarding the creditworthiness of an entity or obligation, expressed using an established and defined ranking system. No common definitions for credit rating exist among IOSCO member countries. For instance European Union CRA Regulation (Regulation (EC) No 1060/2009), in its definition of rating uses the word “opinion” and United States (CRA Reform Act 2006) in its definition of rating uses the word “assessment”.

Regulatory agencies in India use credit rating in various statutory regulations of investments and issuance of debt instruments. SEBI in its circular [6] standardized the rating symbols and definitions. Rating scale used for rating debt instruments and entities were not uniform, until the year 2011 when rating scale for rating long term and short term debt instruments were standardized. There are other rating scales that are not yet standardized. Globally, countries are having varied thoughts regarding standardized rating scales.

RATING SCALES-AN OVERVIEW

According to the credit rating agencies [7], credit rating scales used are ordinal in nature which measures relative credit risk and are indicated by a rating symbol. Credit ratings express risk in relative rank order and they are ordinal measures of credit risk. Thus, from the investor's perspective they should be seen as broadly consistent indicators of relative vulnerability, rather than predictive indicators of actual, cardinal default rates. Obligations that are highly-rated have lower credit risk than lower-rated obligations, but the individual ratings themselves are not intended to be predictive of frequency of default or a percentage expected loss.

Credit ratings provide an opinion on the relative ability (and willingness) of an obligor to meet financial commitments. According to Langohr [8] the characteristics of rating scales as expected by the investors and regulators are (i) ordinal on an alpha-numeric scale, (ii) stable, that is, CRAs aim to rate through the cycle, (iii) consistent and comparable across instruments, maturities, industries and countries and (iv) objective and transparent. Ratings deal with defaults and place an issuer or an instrument on a scale from least likely to default to most likely to default.

For the investors to compare the ratings given by different rating agencies it is important that all the rating agencies follow harmonized rating scale [9]. This could help market participants to compare the ratings given by different CRAs. If each rating grade had the same interpretation (e.g. AAA or the equivalent highest scale across CRAs always meant 1 in 1000 chance of default) then market participants would have an objective way of comparing the rating given by one agency with the other. This would increase the ability of market participants to identify the quality of CRAs, which could expedite the process newer CRAs need to go through in earning reputation in the market.

LITERATURE REVIEW

There is dearth of research studies among academicians regarding uniform rating scales though there are many reports by the regulatory agencies. After the financial crisis 2008, the regulators all over the world conducted various studies and published reports regarding standardization of various processes, procedures and disclosure practices. The issue of standardizing credit ratings symbols first arose in the SEC Concept Release [10] regarding Rating Agencies and the use of credit ratings under the Federal Securities Laws. In the year 2011, Securities Exchange Commission (SEC) made a study on standardization of credit ratings. Pros and cons for CRAs to use comparable symbol sets were studied so their ratings may be used in conjunction with other CRAs.

Subsequently SEC [11] made a study on credit rating standardization to find the feasibility and desirability of standardizing credit ratings terminology, so that all credit rating agencies issue credit ratings using identical terms. On account of that, several market participants including rating agencies and investment institutions felt that standardization would not lead to higher levels of accountability, transparency, and competition in the credit rating industry. European Commission's [12], study on the state of credit rating market identifies potential measures that could improve competition such as a harmonized credit rating scale across CRAs, developing a track record score, making amendments to the European Central Bank's selection of approved CRAs, and issuers appointing CRAs by competitive tender.

The hearing conducted by OECD [9] discusses the role of CRAs in the financial crisis and the need to reform in the credit rating market. Existing regulation in USA and Europe post financial crisis have been discussed. There is convergence in regulation of CRAs by ESMA and SEC. The credit rating market is a natural oligopoly, with three Credit Rating Agencies (CRAs) accounting for more than 90% of the market. Various regulatory reforms and initiatives taken up by the regulators are essentially of US parentage. In the Circular by SEBI rating symbols and their definitions were standardized, in pursuant of the recommendation made by the securitization advisory committee of SEBI. Following this all the rating agencies registered with SEBI standardized their rating symbols and definition.

FSF Report [13] state that currently many CRAs do not publish verifiable and easily comparable historical performance data regarding their ratings, asserting that the comparability of rating performance would promote competition by allowing investors to assess the accuracy of the CRAs using past ratings. Disclosure of past ratings by the CRAs in a more systematic way to improve the comparability of their track records was recommended.

Reserve Bank of India on Development of corporate debt market of India by Khan [14] traces the development, issue and challenges of corporate debt market. Majority of investment in corporate bonds are made by banks and institutions including Foreign Institutional Investors (FIIs) with very little or negligible part played by retail investors. Corporate debt can provide an excellent long term investment avenue for retail investor who lacks knowledge and understanding of this important asset class. Efforts are on to enable wider participation in the market and create scope for market making.

IOSCO [15] in its review of code of implementation of the IOSCO code of conduct for credit rating agencies finds that Provision 3.5(b) calls for CRAs to differentiate ratings of structured finance products from those of corporate bonds, preferably through a different rating symbology. None of the three largest CRAs in USA have adopted a different symbology, though all three indicate in their ratings releases that the security being rated is a structured product. NISM [1] in its Assessment of Long Term Performance of Credit Rating Agencies in India states that for the benefit of the public, it is necessary to display the various rating symbols of various CRAs on a common website (say of regulators), on a comparable scale. Rating scale uniformity required across CRAs and Rating scales, brought under comparable bands, need to be hosted on the websites of SEBI, RBI, IRDA and PFRDA and also on the sites of investors' associations.

NABARD [16] on Status of Microfinance in India report about existing MFI model i.e., NGO-MFIs, for-profit MFIs, Self Help Groups. Measurement of progress of microfinance across India are through Savings amount, disbursement of bank loans and NPAs. It also put forth issues faced by MFIs like Lack of global standards in rating of the MFIs. Sharma [17] study on issues and implications regarding rating of Microfinance institutions. It introduces a system for rating MFIs by credible rating agencies across the country to enable MFIs access to various funds. NABARD's scheme for financial assistance to banks for rating of MFIs, various rating and certification systems contribute to critical success factors are put forward in this report.

OBJECTIVES OF THE STUDY

The following are the objectives of the study,
1) Need for the uniform rating scale and comparison of revised rating scales with earlier rating scales for all the registered rating agencies in India.
2) Difference of rating scales and definitions among non-standardized rating scales used for rating entity or instrument given by different rating agencies in India.
3) Global perspective on uniform rating scales for specific instruments across all rating agencies.

RESEARCH METHODOLOGY

This is an exploratory research based on secondary data. Data's are collected from the official reports regarding regulation published and available in the regulatory (national and international) web sites and rating agency web sites. For reviewing the earlier literature, various journals, reports, discussion papers, thesis report of various institutes were referred.

Data for the rating scales of various debt instruments were got from the five registered rating agency websites. Data regarding earlier rating scale were got from a thesis report, SEBI report on standardization of rating scale and rating agency website. Reports were taken from Indian and International regulatory agency websites viz. SEBI, RBI, SEC, European Commission, ESMA and CRISIL. The idea of having standardized rating scales for rating instruments is in discussion level among certain regulators including IOSCO (International Organization of Securities Commission) and ESMA (European Securities and Markets Authority). Discussion reports and final reports of varied themes were taken from these regulators website. However SEC have considered and rejected the view of having standardized rating scales. The concept letter and study reports were taken from the regulator's website. This paper compares the revised rating scale and earlier rating scale for long term and short term debt instruments of various rating agencies. This paper also compares instruments with non-standardized rating scales across rating agencies in India following standardization of rating scales. From various discussion and study reports of international regulatory agencies this paper studies and analyses the view of international agencies, regulators regarding the standardized rating scales. This study analyzed the data descriptively.

ANAYSIS AND DISCUSSION

Need for Uniform Rating Scales

Financial crisis in the year 2008 affected economies of many countries deeply [18]. Collateralized debt obligations with an initial triple-A rating backed by subprime asset-backed securities have, however, defaulted. Following the real estate bubble the ratings given to exotic financial products including structured financial instruments fell several notches from AAA to D. CRA competition and the lack of transparency in structured finance transactions, combined to undermine the integrity of the credit rating process for these products. Lack of competition and oligopolistic market structure for credit rating agencies were one of the reason for rating inflation. The quest for market shares is viewed as a reason for a lack of commonality in the rating symbols.

This led to rethinking and development of regulatory norms for the credit rating agencies in many countries. Though regulatory reforms are not uniform, registration and certain disclosures norms are common in all countries. Many of the rules within these and other regulatory regimes are not uniform, nor are the CRAs operating within them. Indeed, the global CRA industry is highly varied. For the IOSCO code to continue to have relevance as a fundamental harmonizing platform, it needs to maintain a set of principles and provisions that reflects the unique nature of ratings and accommodates CRAs of all shapes and sizes.

Governmental regulations increase reliance on ratings by, among other things, setting a permissible minimum rating for certain investments. In India they are used in many investment regulations and Basel III. Globally many countries are working towards standardizing credit rating terminology across asset classes, so that named ratings correspond to a standard range of default probabilities and expected losses. Many regulators including IOSCO are proposing the introduction of harmonized rating scale to be used by all CRAs. The uniform rating scale would establish comparable metrics for all existing rating scales. Such metrics would contribute to the transparency, interoperability, and comparability of the rating process and could enhance competition in the sector.

Standardization of Rating Symbols

The rating agencies were following rating symbols and definitions that were not standardized. The Corporate Bonds and Securitization Advisory Committee of SEBI recommended that the rating symbols and their definitions should be standardized in observance that registered rating agencies were following different rating symbols and definitions. SEBI issued circular (CIR/MIRSD/4/2011) to all the registered rating agencies in India [19] to use common rating symbols and definitions.

Common rating symbols and definitions meet the following objectives:
(i) for easy understanding of the rating symbols and their meanings by the investors, and
(ii) to achieve high standards of integrity and fairness in ratings.

In consultation with the CRAs and considering the international practices, standardized symbols and their definitions have been devised by SEBI for the following. Standardized rating symbols and their definitions have been included in the circular, 2011.
a) Long term debt instruments;
b) Short term debt instruments;
c) Long term structured finance instruments;
d) Short term structured finance instruments;
e) Long term mutual fund schemes; and
f) Short term mutual fund schemes.

Comparison of Earlier and Revised Rating Scales

Under the revised standardized system, there is no change in the rating symbols and number of grades in the long term debt instruments. Standardization is achieved by adding rating agencies identifier in the prefix. For e.g., AAA rating of CRISIL is denoted as CRISIL AAA. In short term ratings, there is no change in the number of rating grades, a rating symbol has been changed which is denoted by 'A' on a scale of '1' to '4' (i.e. A1, A2, A3 and A4) and Default 'D' has been added.

Table 1 shows the comparison of earlier and revised rating symbol of the major registered rating agencies CRISIL and CARE for long term debt instruments. For rating agency CARE, there is no change in the earlier and revised rating symbol [20-25].

Table 1: Comparison of earlier and revised rating symbol Long Term Debt Instruments.

Earlier Symbol	Revised Symbol CRISIL	Earlier Symbol CARE	Revised Symbol
CRISIL			CARE
AAA	CRISIL AAA	CARE AAA	CARE AAA
AAA	CRISIL AAA	CARE AA	CARE AA
A	CRISIL A	CARE A	CARE A
BBB	CRISIL BBB	CARE BBB	CARE BBB
BB	CRISIL BB	CARE BB	CARE BB
B	CRISIL B	CARE B	CARE B
C	CRISIL C	CARE C	CARE C
D	CRISIL D	CARE D	CARE D
Source: Reports from rating agencies, SEBI and rating agencies website. Note: Compiled by the authors.			

Table 2 shows the comparison of earlier and revised rating symbol of the major registered rating agencies ICRA and India Ratings for long term debt instruments. Revised symbols of rating agencies ICRA and India Ratings differ from the earlier rating symbol.

Table 2: Comparison of earlier and revised rating symbol Long Term Debt Instruments.

Earlier Rating Symbol ICRA	Revised Rating Symbol ICRA	Earlier Rating India Ratings	Revised Rating India Ratings
LAAA	[ICRA] AAA	AAA (ind)	IND AAA
LAA	[ICRA]AA	AA (ind)	IND AAA
LA	[ICRA]A	A (ind)	IND A
LBBB	[ICRA]BBB	BBB (ind)	IND BBB
LBB	[ICRA]BB	BB (ind)	IND BB
LB	[ICRA]B	B (ind)	IND B
LC	[ICRA]C	C (ind)	IND C
LD	[ICRA]D	D (ind)	IND D
Source: Reports from rating agencies, SEBI and rating agencies website. Note: Compiled by the authors.			

Table 3: Comparison of earlier and revised rating symbol short term debt instruments.

Earlier Rating Symbol CRISIL	Revised Rating Symbol CRISIL	Earlier Rating Symbol CARE	Revised Rating Symbol CARE
P1	CRISIL A1	PR1	CARE A1
P2	CRISIL A2	PR2	CARE A2
P3	CRISIL A3	PR3	CARE A3
P4	CRISIL A4	PR4	CARE A4
P5	CRISIL D	PR5	CARE D
Source: Reports from rating agencies, SEBI and rating agencies website. Note: Compiled by the authors.			

Table 4: Comparison of earlier and revised rating symbol Short Term Debt Instruments.

Earlier Rating ICRA	Revised Rating ICRA	Earlier Rating IndiaRatings	Revised Rating IndiaRatings
A1	[ICRA] A1	F1(ind)	IND A1
A2	[ICRA] A2	F2(ind)	IND A2
A3	[ICRA] A3	F3(ind)	IND A3
A4	[ICRA] A4	F4(ind)	IND A4
A5	[ICRA] D	F5(ind)	IND D
Source: Reports from rating agencies, SEBI and rating agencies website. Note: Compiled by the authors.			

Table 3 shows comparison of earlier and revised rating symbol of the major registered rating agencies CRISIL and CARE for short term debt instruments. Table 4 shows comparison of earlier and revised rating symbol of the major registered rating agencies ICRA and India Ratings for short term debt instrument.

It can be found that the number of rating grades is same for both long term and short term debt instruments. Rating symbols and definitions have been changed in both long term and short term. Default (D) was not specified as a grade in short term symbol before standardization.

The rating symbol for mutual fund scheme and structured instruments have unique identifier mfs and SO added to standardized rating symbol prevailing for long term and short term debt instruments. These standardized rating symbols would be beneficial for the investor community and help investors make more informed investment decisions.

Table 5: Rating Instruments that follow standardized and non-standardized rating scale.

Standardized Rating scale	Non-standardized rating scale
1. Long Term Debt Instruments	1. Fixed Deposit
2. Short Term Debt Instruments	2. Claims Paying Ability or Insurance
3. Long Term Structured Finance Instruments	3. Corporate Governance rating
4. Short Term Structured Finance Instruments	4. MFI
5. Long Term Debt Mutual Fund Schemes	5. Real Estate
6. Short Term Debt Mutual Fund Schemes	6. Recovery
7. SME	7. Issuer
8. MSE	
9. ITI	
Source: Reports from regulator, rating agencies website. Note: Compiled by the authors.	

Table 5 shows rating instruments that follow standardized and non-standardized rating scale. Long term and short term debt instruments, structured finance instruments and mutual fund schemes, SMEs, MSEs and ITI have standardized rating symbol across rating agencies.

The additional understanding could assist regulators in their oversight. It is beneficial for rating agencies to use comparable symbol sets so their ratings may be used in conjunction with other rating agencies. Investors often use ratings from two or more rating agencies. So an rating agency that chooses a symbol set that doesn't compare with other rating agency might find the audience for its opinions diminished as the investor would have to map the nonstandard symbols to the scales of the dominant rating agencies. Efficient markets do tend to migrate towards common languages and it is likely that over time global standards will emerge for rating industry which will adopt either similar rating scales or provide mapping to the scales of the dominant rating agencies.

Comparison of Rating Scales-Non-Standardized Instruments

From its inception, rating agencies have introduced rating for various instruments/products/Institutes starting from the commercial paper. Apart from serving as information intermediary between the issuers and investors it is also used by regulators in various statutory regulations. The rating agency came into business when corporate bond market was still in the nascent stage. Regulators relied on rating agencies input for the development of bond market.

Developing a vibrant corporate bond market has been an important agenda among the concerned stakeholders, i.e., Government of India , the Reserve Bank of India, the Securities and Exchange Board of India (SEBI), the Insurance Regulatory and Development Authority (IRDA), etc. and in the recent times they have made coordinated efforts to achieve this objective. The share of bonds issued through public issues has therefore increased from 0.86 per cent in 2008-09 to 7.3 per cent in 2011-12. Majority of investment are made by banks and institutions including Foreign Institutional Investors (FIIs) with very little or negligible part played by retail investors.

Corporate debt provides an excellent long term investment avenue for retail investors, who lack knowledge and understanding of this important asset class. In order to counter this, regulators have made an important move by standardizing rating symbols and definitions of major rating instruments. In India, only certain rating instruments are standardized. Table 6 gives the list of rating instruments or entity using standardized and non-standardized rating scale. The rating agencies should seek permission from SEBI to rate each category of instrument separately. The rating scales of debt instruments were standardized and there are host of instruments or entities whose rating grades are not yet standardized.

In this paper we are comparing rating scales of such rating instruments or entities which are not yet standardized by the regulator. The following rating instruments/products/Institutions rating scales are considered for comparison.
1) Company fixed deposits
2) Insurance
3) Corporate governance
4) IPO
5) MFI.

Company Fixed deposits are unsecured loans taken up by company or NBFC and there is no insurance/guarantee in case of default by the company or NBFC. Company Fixed Deposit gives interest at a higher rate than banks. Investors have to rely on rating agencies and fair judgment before investing in company fixed deposit.

Table 6 shows comparison of rating scales of Fixed Deposit rating given by five rating agencies in India. The rating definitions are similar for all the rating agencies. For example Grade B denotes either inadequate safety or high risk. CARE and Brickworks shows finer gradations in the rating category B. Except for CARE and Brickworks other rating agency does not use rating agency name in their rating symbol.

Indian Insurance Sector is growing at substantial rates over the past few years and there is expectation of higher growth in future. India's market share, insurance density and penetration levels in the insurance market have been steadily improving. It has been more than a decade since rating agencies have started giving insurance ratings.

Table 6: Comparison of rating scales of fixed deposit.

CRISIL	ICRA	CARE	India Ratings	BWR LT
FAAA	MAAA	CARE AAA	tAAA	BWR FAAA
FAA	MAA	CARE AA	tAA	BWR FAA
FA	MA	CARE A	tA	BWR FA
		CARE BBB		BWR FBBB
		CARE BB		BWR FBB
FB	MB	CARE B	tB	BWR FB
FC	MC	CARE C	tC	BWR FC
FD	MD	CARE D	tD	BWR FD
Source: Rating agencies website. Note: Compiled by the authors.				

Table 7 compares rating scales of Insurance rating. It shows ICRA and Brickwork does not have a default rating scale, otherwise rating agencies have similar rating scales. Rating agencies CRISIL and India Ratings doesn't use their name identifier in the rating symbol. For e.g. rating agency CARE uses the name identifier CARE along with the rating symbols.

Table 7: Comparison of rating scales of insurance rating.

CRISIL	CARE	ICRA	Brickworks
AAA	CARE AAA(In)	iAAA	BWR AAA efs
AA	CARE AA(In)	iAA	BWR AA efs
A	CARE A(In)	iA	BWR A efs
BBB	CARE BBB(In)	iBBB	BWR BBB efs
BB	CARE BB(In)	iBB	BWR BB efs
B	CARE B(In)	iB	BWR B efs
C	CARE C(In)	iC	BWR C efs
D	CARE D(In)		
Source: Rating agencies website. Note: Compiled by the authors.			

Corporate Governance rating is considered as a yardstick which can be used to measure and monitor the progress on the path of corporate governance. Table 8 compares corporate governance rating followed by different rating agencies. The rating symbols, definition and rating grades are different for all rating agencies. GVC (Governance and Value Creation) ratings has gained acceptance in the Indian market on account of its intrinsic merits as a comprehensive and forward looking measure of governance, and also to create a common language for understanding corporate processes and their effectiveness.

Table 8: Comparison of Rating Scales of Corporate Governance Rating.

CRISIL	**CARE**	**ICRA**	**Brickworks**
CRISIL GVC Level 1	CARE CGV1	CGR1	BWR CG 1
CRISIL GVC Level 2	CARE CGV2	CGR2	BWR CG 2
CRISIL GVC Level 3	CARE CGV3	CGR3	BWR CG 3
CRISIL GVC Level 4	CARE CGV4	CGR4	BWR CG 4
CRISIL GVC Level 5	CARE CGV5	CGR5	BWR CG 5
CRISIL GVC Level 6	CARE CGV6	CGR6	BWR CG 6
CRISIL GVC Level 7			BWR CG 7
CRISIL GVC Level 8			BWR CG 8
Source: Rating agencies website. Note: Compiled by the authors.			

Table 9 shows comparison of IPO rating grades given by various rating agencies. Rating grades and definition are same, though CRISIL and CARE do not follow naming nomenclature. As per SEBI guidelines, all issuers in the primary market filing their draft prospectus or offer document on or after 1 May 2007 must get an IPO Grading from any credit rating agency registered with SEBI.

Table 9: Comparison of IPO rating/grading.

CRISIL	**CARE**	**India Ratings**
05-May	5	Ind-Ra IPO Grade 5
04-May	4	Ind-Ra IPO Grade 4
03-May	3	Ind-Ra IPO Grade 3
02-May	2	Ind-Ra IPO Grade 2
01-May	1	Ind-Ra IPO Grade 1
Source: Rating agencies website. Note: Compiled by the authors.		

This makes obtaining rating from rating agencies mandatory, for the companies seeking funds through primary market via IPO. All the ratings scale which are used in statutory regulations by SEBI or RBI are standardized except IPO grading scale. A Rating Scheme for MSME was introduced in April 2005 in consultation with Industry Association's, Indian Bank's Association (IBA) and Rating Agencies for the MSE sector to help improve their productivity and its contribution to the economy. The

Ministry of Micro, Small and Medium Enterprises (MSME) has revised its guidelines henceforth, on the Performance and Credit Rating Scheme (PCRS) and launched it recently in May 2016. It implemented a uniform rating scale to be followed by all the empaneled rating agencies. i.e. CRISIL, ICRA, SMERA, Brickwork, India Ratings and CARE. Accordingly, it has a rating scale from MSE 1 to MSE 8, indicators to denote financial strength and operating performance. A good rating would enhance their acceptability in the market, enhance public funding and also make access to credit quicker and cheaper, thus help in economizing the cost of credit. Moreover uniform rating would create fair competition among the agencies and investors will be able to compare the ratings given by more than one agency. Micro financing Institutions (MFI) are viewed as a means to bring the disadvantaged populations who does not have access to formal credit into the financial ambit. MFIs play an important role in financial inclusion. Initially MFIs in India has gone through rapid growth, following which it slumped and hit the rock bottom during the Andhra Pradesh crisis. After 2012 Microfinance sector has regained its growth following the Reserve Bank of India (RBI) guidelines for non-banking financial companies-MFIs. Although Indian MFIs rely more on local sources for their funding, Equity and securitizations has been introduced in MFIs recently. The non-uniform rating practices and monitoring mechanism adopted for the microfinance sector prevents investors from investing in the microfinance sector. Most of the MFI find it difficult to find funding through public deposits or securitization of loan receivables because of regulatory restrictions and Lack of transparency in MFI sector.

The Table 10 compares the MFI rating scale adopted by different rating agencies. The rating grades, symbol and definition for MFI rating are different across the rating agencies. Micro-finance institutions (MFIs) face numerous challenges in finding funds to back their activities. The investors find it difficult to evaluate the MFIs and are not encouraged to invest in them. Although evaluations and assessments are available to MFIs from credible agencies, these tend to be expensive, and lack a common standard that can be applied to the entire industry.

Table 10: Comparison of MFI rating scale.

CRISIL	**CARE**	**ICRA**
mfR1	MFI 1	M1
mfR2	MFI 2+	M2
mfR3	MFI 2	M3
mfR4	MFI 3+	M4
mfR5	MFI 3	M5
mfR6	MFI 4+	
mfR7	MFI 4	
mfR8	MFI 5	

Source: Rating agencies website.
Note: Compiled by the authors.

Most of the evaluations have not been made public, leaving the methodology and/or results unknown to other potentially interested parties. What is required is a credit rating system that takes into account the nuances of the field, and sends a clear signal to the investors and other stakeholders of their sustainability. A common understanding on the reporting, measurement, and evaluation of MFI performance has not been reached given the diversity of the providers. There are agencies like M-CRIL, Microfinance rating including the CRAs listed in the Table 11 which provide variety of rating like Microfinance Institutional Rating, social rating and client protection certifications for MFI sector in India.

The Securitization Advisory Committee of SEBI recommended the standardization of rating symbols and definition for all the rating agencies registered with SEBI through its circular dated June 2011. Following this, SEBI standardized the rating symbol and definition for long term and short term debt instruments. It also uses separate symbols for the mutual fund scheme and structured finance instruments.

They are 9-point scale for short term instruments and 20-point scale for long term instruments. Each scale point has a definition which indicates relative measure of credit risk. This is important decision by SEBI considering SEC and ESMA are yet to move towards standardization of rating symbols.

IOSCO has given code of conduct for the credit rating agencies in a broader level. It is still contemplating on following harmonized rating scales across asset classes. The Rating scales that have been standardized include long term and short term debt instruments that is mandated by the regulators under statutory regulations to obtain rating from registered credit rating agencies. The long term, short term debt instrument for structured obligations and mutual fund schemes have been standardized under regulation of SEBI.

Standardization has been achieved by SEBI using:
1) Uniform rating symbols across all agencies
2) Same number of rating grades standardized across all rating agencies
3) Rating agency identifier on the prefix of the rating symbol.
4) Same rating symbol definition.

Based on this, four criteria are taken to check standardization of non-standardized rating instruments. First criteria include Number of rating grades For example fixed deposit rating of CRISIL is six which are FAAA, FAA, FA, FB, FC and FD. Second criteria are rating symbol.

Third criteria is Rating agency identifier which is prefixed with rating symbol to identify the particular rating agency and fourth criteria is rating definition which is explanation about the rating symbol. For the investor to compare the rating given by one agency with other, it is important that all the agencies follow a uniform rating scale.

Table 11: Comparability of rating scales of all rating agencies.

Instrument or Entity	Rating Grades	Rating Symbols	Agency Name Identifier	Rating Definition
Fixed Deposit	X	X	X	X
Insurance Ratings	X	X	X	√
MFI	X	X	X	X
Recovery Rating	√	X	X	√
Issuer Rating	√	√	X	X
Corporate Governance Rating	X	X	X	X
Real Estate	X	X	X	X
Source: Rating agencies website. Note: compiled by the authors.				

The Table 11 compares rating scales of different rating agencies based on four criteria mentioned in standardization. It shows how far different rating instruments follow rating scales that are comparable. In the Table 11, X denotes the registered rating agency is not uniform in the particular standardization criteria. √ denotes registered rating agencies are uniform in that particular criterion.

International Perspective on Uniform Rating Scales

The three big CRAs i.e., Standard and Poor, Moody's and Fitch dominate the international ratings market. The United States securities regulator SEC in a study on credit rating standardization has concluded that standardization of rating scale is not feasible. It was felt that standardization would not lead to higher levels of accountability, transparency, and competition in the credit rating agency industry and increased transparency would be a more desirable alternative. Although Rating agencies registered with SEC use similar scales and symbols to denote long-term credit ratings, the number of rating scales and the rating symbols, used vary widely among the rating agencies for other types of credit ratings. Standardizing credit rating terminology may facilitate comparing credit ratings across rating agencies and may result in fewer opportunities for manipulating credit rating scales to give the impression of accuracy.

The participants and commenters which involves rating agencies also, states that standardization may not be feasible given the number and uniqueness of rating scales and differences in credit rating methodologies used by credit rating agencies. Standardized credit rating terminology may reduce incentives for credit rating agencies to improve their credit rating methodologies and surveillance procedures.

European Union dint find the need to regulate CRAs until the financial crisis in 2007.

ESMA was formed to perform supervisory role on all the rating agencies operated in European Union. European Commission’s Credit Rating Agency (CRA3) Regulation focused on enhancing competition in the credit rating market, while addressing conflicts of interest and enhancing disclosure on structured finance instruments. They believe that the following would improve ratings competition: developing a track record score for CRAs, making amendments to the European Central Bank’s selection of approved CRAs rating Structured Finance Instruments, and appointing CRAs by means of some form of competitive tender. Another measure that could help in enhancing competition and market participants’ assessment of CRA quality would be a harmonized credit rating scale across CRAs.

Though ESMA suggests that implementing Uniform rating scale will help the stakeholders in understanding the credit quality better, Uniform rating scales have not been implemented for the rating agencies in European Union.

Every rating given by rating agencies for the same instrument have a slightly different meaning and it is not possible to accurately assess the quality of the underlying rating (e.g. if a bond defaults, the CRA could say that that was within the assigned probability of the rating scale).

However, if each rating grade had the same interpretation (e.g. AAA or the equivalent highest scale across CRAs=always meant 1 in 1000 chance of default) then market participants would have an objective way of assessing the quality of the ratings as they would know the relevant parameters. This would increase the ability of market participants to identify the quality of CRAs, which could expedite the process new CRAs need to go by earning reputation in the market.

International Organization of Securities Commission (IOSCO) has laid out broad level code of conduct for credit rating agencies. They raised concerns regarding the lack of a uniform global standard for capital adequacy within the securities sector. This lack of uniform standard might contribute to regulatory arbitrage, competitive inequalities across jurisdictions and a constrained ability to supervise cross-border groups.

In the International forum several proposals were put forward for consideration, including: the establishment of a global rating platform based on a uniform rating scale; initiatives for investors to better understand the role of ratings and make better use of ratings; specific measures to increase transparency and competition; alternative structures to address conflict of interest; and the establishment of domestic and/or public CRAs.

The Table 12 shows that except India all the other countries follow non-standard rating scale for long-term debt instrument. Major countries were in the view that uniform rating scale might improve the competition and ratings quality but have not implemented yet.

Table 12: Countries with standard/non-standard rating scale for debt instruments.

Region	Regulator	Debt Instrument (Standard/Non-standard rating scale)
USA	Securities Exchange Commission	Non-standard
European Union	European Securities and Markets Authority	Non-Standard
India	SEBI	Standard
Brazil	Securities and Exchange Commission of Brazil	Non-standard
Japan	Financial Services Agency	Non-standard
Canada	Canadian Securities Administrators	Non-standard

CONCLUSION

There is no intense study on adopting uniform rating scale for debt instruments across all the rating agencies. The IOSCO suggest that uniform rating scale has many benefits though it does not recommend the usage of it to the member countries. Global standards for rating scales developed by IOSCO would be positive move for the investor community. This would be one of the regulatory reforms that would help enhance the competition and lower the entry barriers for new rating agencies.

The countries with well-developed capital markets are skeptical about implementing standardized rating scale. The rating agencies do not feel to be put up in an advantageous position to implement uniform rating scales. In India the rating scales have been standardized to improve the debt market and to bring more investors for the bond market.

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