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STATEMENT OF THE PROBLEM

OBJECTIVES

HYPOTHESIS (ES)

RESEARCH METHODOLOGY

RESULTS & DISCUSSION

FINDINGS

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A STUDY ON THE FINANCIAL PERFORMANCE OF CREDIT RATING AGENCIES IN INDIA

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ABSTRACT

Rating is an important component for individual investors for their security and assurance of returns on bond instruments. The Ratings are assigned by Credit Rating Agencies showing the credit worthiness of issuer companies. It is only an advice but not a recommendation. But most of the bonds are rated on the basis of financial soundness of issuer companies. In this context, it was felt to study the financial performance of credit rating agencies for a period of 15 years. In the present study, Credit Rating and Information Services of India Limited (CRISIL), Investment Information and Credit Rating Agency of India Limited (ICRA), Credit analysis and Research limited (CARE), Fitch Ratings, Brickwork Ratings India Private Limited financial indicators such as Revenue, Profit Before Tax, Earnings per Share, Net worth, Dividend, Market Capitalization, Number of Employees and Revenue per employee are focused. The result of analysis by use of hypothesis study and application of ANOVA revealed that there is significant difference between dividend payout ratio, Earnings per share and Profit before tax of CRISIL, ICRA and CARE, Fitch, Brickwork Ratings. It is the rating component which is for any investor to take decisions to invest in debt instruments which is assigned by rating agencies.

KEYWORDS

CRISIL, rating, revenue, global financial crisis.

INTRODUCTION

The role of credit rating agencies can be traced back to 1987, where the Indian financial markets were under developed in terms of regulation and credit rating. The then regulations had least control over the credit rating agencies which were few in number and primarily on the first credit rating. The latter two decades witnessed a steady growth of credit rating agencies in terms of ratings, grading and other services. The number of instruments rated in all grew more than 100 times. The escalating growth of rating agencies was focused by SEBI to restructure the regulatory framework for ensuring the rating assignments and quality service to the issuers. The period 2001- 2015 studied to be pre and post global financial crisis and implement stringent regulations for the vibrant development of credit rating agencies. During this period SEBI has been taking measures to regulate the activities and disclosures of credit rating agencies.

A **credit rating agency** is a company that assigns **credit ratings**, which rate a debtor's ability to pay back debt by making timely interest payments and the likelihood of default. Credit Rating Agencies gained significance after the introduction of the New Economic Policy (1991). Credit Rating was made mandatory in India for instruments like Commercial Papers, Debentures with a maturity period of 18 months and Non-financial Companies Fixed Deposits. After March 1998, Credit Rating has become compulsory for all debt instruments. Before the formation of Credit Rating Agencies, Merchant Bankers and Brokers were the only source of information regarding the risk of a particular issue. The Credit Rating Agencies reduced the task of merchant bankers to a great extent.

REVIEW OF LITERATURE

Tabrez Ahmed (2009) analyzed that whether the credit rating agencies downgrade companies promptly enough, leading to suggestions rather than rely on Credit Rating Agencies (CRA) ratings in financial regulation, financial regulators should instead require banks, broker dealers and insurance firms to use credit spread when calculating the risk in their portfolio.

Jaydev M et al (2010) found the significant part of the variation in the credit spreads of different rating categories by proof of default probability and recovery rate. The relation between credit spreads and important credit risk factors are to be consistent with that of the structural models. It justified the introduction of poll based spreads in the emerging market which could be an encouraging step in the development of the bond and credit derivative market.

Avinash D Persaud (2010) analyzed the differences between rating agencies analysis that rating agencies do not have the business model of analysts who bag multimillion dollar bonuses. But ratings are as much at the heart of the current rate and relocate model of banking as analysts' recommendations were made to the dotcom. Banks were looking more like traders and some traders were looking more like banks. It was stressed that one fall of the sub-prime crisis has been the anger towards credit rating agencies and calls for regulation.

Kuljeet Kaur et al (**2010)** found that the level of satisfaction regarding credit rating among the investors on the basis of investors decisions by comparing many instruments of various companies at a time and they rely on credit rating for their investment decision by which they might be familiar with the various rating attributes. The analysis made by them indicates that various rating attributes including credit rating, is the expression of safety, it saves time and energy of investors, it helps the investors in decision making. The rating agencies rate the instruments according to their actual worth and the revision of rating by the rating agencies has positive impact on the satisfaction level of the investors. The negative satisfaction level of investors' includes selection of long term portfolio by the investors and involvement of rating agencies in research. Further it revealed that the proper steps should be taken to make the working of credit rating agencies more accountable.

Shobha Kannan (2010) found that Ratings Agencies plan to step up their due diligence process and strengthen their rating methodology after the recent satyam incident. Rating agencies base their analysis on the audited balance sheet of a company which forms the primary source of information. Rating agencies do not look at the company's primary accounts. As a whole the rating agencies should take additional measures in order to ensure there is no discrepancy in ratings.

Bheemanagauda and Madegowda (2010) evaluated the performance of credit rating agencies in India including CRISIL, ICRA, CARE and FITCH. Secondary data relating to long term debt instruments from time period 2000-08 has been used for the purpose of the study. The analysis of the study brings out that during the given period there is a substantial increase in the rating business in India. During the study period, the maximum percentage of instruments rated is assigned the investment grade rating. As far as rating revisions are concerned the study depicts that the downgrades were more than double the upgrades both in terms of number of instruments and the volume of debt. It was depicted that the ratings were issuer based. So the authors suggested that stringent methods should be adopted to avoid frequent downgrades. It further highlights that among the agencies which maintain the stability of ratings, Fitch India ratings holds the top most position followed by CRISIL, ICRA and CARE in line.

Roopa Kudva (2011) forecasted the lowering the GDP from the earlier estimate in view of the deteriorating global economic scenario and the grim investment climate in India on account of the policy environment. It was also anticipated that the impact of rising interest rates and slowing government expenditure, the declaration in advanced countries has been sharper than expected.

Rajiv Bhuva (2011) compared the credit rating agencies listing during the first half of year during 2008 as its business had yet to get off the ground where Reliance Power had a grade of 4 from CRISIL which indicated that it had above average fundamentals but the shareholders lost 83 per cent on the scrip, on the other hand CRISIL assigned a grade of 1 for poor fundamentals to Bhagawati Banquets and Hotels, delivered 106 percent returns whereas Parabolic Drugs got a Grade of 2 from CARE Ratings and Grade 3 from Brickwork Ratings, this sort of happening becomes the business of credit ratings agencies in India a smaller part of the work they do. Rating levels went up, the correlation between ratings and market implied yields fell, and the ability of ratings to predict default deteriorated.

George Batta and Volkan Maslu (2011) compared credit rating agencies adjustments to company reported earnings with equity analysis. The gap between the adjusted earnings of credit rating agencies and equity analysts is larger when a company's operations and status as going concern is more uncertain. It was predicted that agencies can point to inputs as evidence of their caution in the event of an increase in the credit risk of a highly rated company. The interpretation complements that rating agencies make soft adjustments to their rating models, thereby producing ratings that are more optimistic than ratings that would be predicted by harder inputs like adjusted earnings.

IMPORTANCE OF THE STUDY

Credit Rating Agencies were started to evaluate the risk involved in the instruments. The primary purpose of such rating assignment is to take necessary investment decisions by the prospective investors. On the transition of liberalized economy, the Credit Rating Agencies have been providing various categories of services to educate and bring awareness among investors. In this process the investors can also seek advice from experts who have undergone such investing experience. These agencies have been assisting the investors since last twenty years. The historical realities of Credit Rating Agencies have been under surveillance of regulatory authority. Even after such steps, Credit Rating Agencies could not assess the failure of performances in respect of borrowing companies. The rating agencies could not also deduce the fraudulent practices of WorldCom (2002) and Enron (2001).

STATEMENT OF THE PROBLEM

The credit rating agencies assign the ratings to debt instruments. These ratings are backbones for the investors to decide. The earnings of the investors will be based on their decision to invest. Similarly, the earnings of credit rating agencies have any reflection on the returns in these agencies to the shareholding agencies.

OBJECTIVE

To assess the financial performance of credit rating agencies in the pre and post global financial crisis.

HYPOTHESES

The hypotheses developed and tested are as follows.

1. There is no significant relationship between Dividend Payout Ratio of CRISIL, ICRA and CARE Rating Agencies.
2. There is no significant difference between Earnings Per Share of CRISIL, ICRA, CARE and BRICKWORK RATINGS.
3. There is no significant difference between Profit Before Taxation of CRISIL,ICRA and CARE Rating Agencies.
4. There is no significant difference between Ratios of Revenue of CRISIL,ICRA and CARE Rating Agencies.

RESEARCH METHODOLOGY

The study covers four credit rating agencies. The data used for the present study includes secondary data which was collected from official websites of Credit Rating Agencies. The financial information provided by various credit rating agencies is taken for the present study through financial analysis techniques. The other dimension of financial performance was by use of single factor ANOVA.

DATA COLLECTION

Data has been collected from annual reports of all the credit rating agencies and reports submitted to SEBI.

CREDIT RATING AGENCIES – AN OVERVIEW

Credit Rating, as a whole, is playing a very important role in the debt market. Credit Rating agencies have also made a good attempt in the equity primary market by offering the grading service to Initial Public Offering (IPO). In the light of their prominence, an attempt is made to evaluate the performance of rating services of Credit Rating Agencies in India as a whole. The relevant statistics are collected pertaining to the number of long term debt instruments rated, their amount, grades assigned for a period of 15 years from 2000 to 2015 from the publications of SEBI, RBI and Annual Reports of CRISIL, CARE, ICRA, Fitch, Brickworks and Onicra Agencies. Based on this information the ratings assigned for long term corporate debt securities are either equal to or more than one year are presented. The financial performance indicators under taken for the present study are the Revenue, Profit before Depreciation and Tax (PBDT), Profit before Tax (PBT), Earnings per Share (EPS), Net worth, Dividend, Market Capitalization and Revenue per Employee for all the credit rating agencies.

TABLE 1: FINANCIAL PERFORMANCE OF CRISIL (Rs. In Lakhs)

Financial Performance Indicator	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015
Revenue	4033	5154	6929	7186	7426	9173	15865	27088	40389	46445	63915	52871	97800	78279	90336	127707
PBDT	2216	1787	3614	3523	3303	3890	6046	10481	18696	20422	26918	26924	29421	41192	33131	41217
PBT	1923	1338	2862	2802	2684	3341	5391	9147	17512	19034	24897	24756	27029	38870	30738	37605
EPS	20.83	15.59	21.09	28.83	28.67	34.20	35.00	35.00	35.00	22.25	29.1	31.4	39.91	30.37	30.20	33.0
Net worth	5939	6537	7104	8246	9497	11011	16298	26821	35751	43381	36250	36521	45446	60884	72738	84835
Dividend (%)	55	55	65	100	100	125	150	250	250	250	250	275	300	300	400	142
Market Capitalization	24800	7440	19639	15834	31153	43785	120410	266314	17732	32115	42540	63000	76070	84840	81000	130834
Number of employees	202	252	243	239	246	389	814	1521	1668	1627	1817	2121	2466	3424	3313	3883
Revenue per employee	19.97	20.45	28.05	30.07	21.46	23.58	15.57	19.27	23.25	24.31	24.93	25.92	29.99	34.00	34.00	37.00

Source: CRISIL Annual Reports.

Table 1 presents the financial performance indicator with various elements viz., Revenue, Profit before Depreciation and Tax, Profit before Tax, Earnings per Share, Dividend percentage, market capitalization, number of employees and revenue per employee for a period of 15 years. It is observed that the revenue is consistently showing an increasing trend throughout the period of study. Profit before Depreciation and Taxation is fluctuating in 2 years in all the fifteen years which means that the depreciation has not affected the profitability for the remaining 13 years. This indicates the agency is showing an efficient financial performance. Similarly, the profit before tax is also showing an improved performance.

Earnings per share are the result of the above effort by the agency. Hence, the proportionate contribution is considerably consistent. Dividend was stagnant during 2007 to 2010 which means the agency was playing safe during and post global financial crisis period. Market capitalization refers to the value of a company traded on the stock market which is determined by multiplying the total number of shares by the present share price. It is better in all the years due to the maintenance of share price.

Revenue per employee is a measure of how efficiently a particular company is utilizing its employees. High revenue per employee is a positive sign that the agency is finding ways to collect more revenue out of each contributor.

TABLE 2: FINANCIAL PERFORMANCE OF ICRA (Rs. In Lakhs)

SNo	Particulars	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	1213	2014	2015
1	Revenue	2760	3220	3665.40	3999.75	4132.51	3860.75	4676.93	6863.	10,143.58	12,794.38	14,184.77	15,909.85	16,486.53	18,018.64	20,617.07
2	PBDT	1260	1430	1495.44	1620.50	1269.65	1891.32	2387.67	3967	5,443.74	7,606.80	7,083.74	7,762.39	7,498.60	8,437.01	9,898.97
3	PBT	1120	1290	1352.09	1483.14	1127.14	1739.06	2223.14	3785.	5,265.95	7,411.24	6,880.51	7,572.75	7,287.86	8,191.81	7,631.12
4	EPS (RS)	9.3	10.4	11.20	12.56	9.20	14.37	18.23	26.66	36.15	50.00	44.91	50.90	60.38	58.73	68.93
5	Net worth	7341.03	7341.03	7341.03	7945.65	8409.29	9237.29	14232.02	15730.	17,941.25	20,959.74	24,234.14	28,291.65	32,236.74	35,565.46	37,698.58
6	Dividend (%)	25	25	30	50	35	40	45	100	120	170	170	200	220	230	240
7	No. of Employees	NA	NA	NA	NA	NA	75	78	107	144	176	216	269	400	421	429
8	Revenue per Employee	NA	NA	NA	NA	NA	51	60	64	0.74	0.73	0.66	0.59	0.41	0.48	0.43

Source: ICRA ratings annual reports,

Note: NA: Not Available

Table 2 presents the data with the slow rate of growth in revenue of ICRA has gained the momentum effectively in post global financial crisis period. This is an indicator that the financial transactions over 5 year period are progressively increasing in a moderate manner. During 2005, the Profit before Depreciation and Tax has fallen compared to the previous years but it has not effected in any other period of study. Net worth of the agency was constant in the first three years of study but speedily it is raised to a remarkable increase. Revenue per employee in not ascertained due to non availability of data from 2001 to 2005. In a later period the revenue per employee has shown a slow fall from 2011 to 2015. Hence, this signifies that number of employees is significantly more over the revenue generated by agency. Therefore, the agency has to take measures to select and train able staff. It may lead to efficient operations.

TABLE 3: FINANCIAL PERFORMANCE OF CARE RATINGS (Rs. In Crores)

S.No	Particulars	2001	2002	2003	2004	2005	2006	2007
1	Total Revenue	322.17	365.54	399.97	413.25	386.14	332.13	397.90
2	PBDT	128.9	135.21	148.31	192.71	173.90	189.13	238.76
3	PBT	111.65	128.90	135.21	148.31	112.71	173.90	222.31
4	EPS	9.31	10.44	11.20	12.56	9.20	14.37	18.23
5	Net worth	672.34	734.1	794.57	840.93	923.73	142.3	142.32
6	Dividends (%)	25	25	30	50	35	40	45

S.No	Particulars	2008	2009	2010	2011	2012	2013	2014	2015
1	Total Revenue	541.93	602.94	609.55	176.63	206.29	227.39	265.12	4844.30
2	PBDT	396.27	544.37	157.15	75.72	72.87	162.4	183.4	2601.77
3	PBT	378.5	526.5	86.32	134.10	149.51	159.88	179.40	2570.9
4	EPS	26.66	30.53	31.82	37.66	39.69	44.7	50.73	50.73
5	Net worth	157.3	179.4	213.5	302.8	285.5	285.3	484	360.6
6	Dividends (%)	NA	40	50	65	100	200	200	280

Source: CARE Annual Reports

* NA: Not Available

Table 3 presents the data relating to CARE Ratings which has better revenue in all the years except 2005 and 2011. It might have occurred due to the shift of rating confidence to other agencies. Similar effect has fallen on Earnings per share and dividend of the agency. Otherwise, the overall financial performance is considered to be satisfactory.

TABLE 4: FINANCIAL PERFORMANCES OF BRICKWORK RATINGS (Rs. In Crores)

Sr. No	Particulars	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015
1	Total Revenue	703559	565296	532068	558936	553716	593511	656536	635615	556911	606509	670268	723611
2	EBIT	131294	151838	149233	152887	178062	165819	150524	131999	108451	135039	143207	165903
3	EAT	107374	142925	102202	107533	101478	305215	138790	102551	43304	85165	101289	120299
4	EPS	24.00	31.00	36.00	38.00	39.00	85.6	76.60	68.30	53.40	67.70	68.40	81.8
5	ROE	23.3	17.6	10.00	10.00	9.1	22.3	8.4	8.5	2.6	NA	**NA**	4.3
6	Interest Coverage Ratio	5.00	5.00	6.3	4.8	4.8	4.6	6.5	6.4	5.2	NA	**NA**	9.7
7	Debt to Capital Employed	23.2	28.3	27.2	32.0	32.0	21.8	12.1	13.0	14.6	NA	**NA**	14.2

Source: www.brickworkratings.com

Table 4 shows the financial data of Brickwork ratings from 2004 to 2015 as the rating business started after the above rating agencies have established their confidence among investors. The same level of confidence is possessed by Brickwork ratings over a short period by increasing its revenue consistently. The Earning per share has almost more than two fold in 2009 than that of previous year. Return on Equity, Interest coverage ratio, debt to capital employed ratios were not available during 2013, 2014.

RESULT OF THE ANALYSIS

The other dimension of measuring the financial performance of all the credit rating agencies of the present study is made with hypotheses.

Testing Hypotheses - 1

Ho: There is no significant difference between dividend payout ratio of CRISIL, ICRA and CARE

H1: There is significant difference between dividend payout ratio of CRISIL, ICRA and CARE

The analysis of data yielded that there is a significant difference between CRISIL, ICRA and CARE as the calculated value is more than critical value, the null hypothesis is not accepted.

ANOVA OF DIVIDEND PAYOUT RATIO (%)

YEAR	CRISIL	ICRA	CARE
2000	55	NA	NA
2001	55	25	25
2002	65	25	25
2003	100	30	30
2004	100	50	50
2005	125	35	35
2006	150	40	40
2007	250	45	45
2008	250	100	0
2009	250	120	40
2010	250	170	50
2011	275	170	65
2012	300	200	100
2013	300	220	200
2014	400	230	200
2015	142	240	280

ANOVA SINGLE FACTOR
SUMMARY

Groups	*Count*	*Sum*	*Average*	*Variance*
Column 1	15	3012	200.8	10453.89
Column 2	15	1700	113.3333	6995.238
Column 3	15	1185	79	6615

ANOVA

Source of Variation	*SS*	*df*	*MS*	*F*	*P-value*	*F crit*
Between Groups	118322.2	2	59161.09	7.37543	0.001798	3.219942
Within Groups	336897.7	42	8021.375			
Total	455219.9	44				

Testing Hypotheses -2

Ho: There is no significant difference between EPS of CRISIL, ICRA, CARE and Brickwork Ratings
H1: There is significant difference between EPS of CRISIL, ICRA, CARE and Brickwork Ratings
As calculated value is more than critical value, the null hypothesis is not accepted.
The study has an impact on the EPS of three rating agencies has been considerable. Therefore, it is Imperative that the agencies have built the confidence among debt holders.

EPS ANOVA

Financial	CRISIL	ICRA	CARE	BRICKWORK
2000	20.83	NA	6.99	NA
2001	15.59	9.3	9.31	NA
2002	21.09	10.4	10.44	NA
2003	28.83	11.2	11.2	NA
2004	28.67	12.56	12.56	NA
2005	34.2	9.2	9.2	24
2006	35	14.37	14.37	31
2007	35	18.23	18.23	36
2008	35	26.66	26.66	38
2009	22.25	36.15	30.53	39
2010	29.1	50	31.82	85.6
2011	31.4	44.91	37.66	76.6
2012	39.91	50.9	39.69	68.3
2013	30.37	60.38	44.7	53.4
2014	30.2	58.73	50.73	67.7
2015	33	68.93	50.73	68.4

ANOVA: SINGLE FACTOR
SUMMARY

Groups	*Count*	*Sum*	*Average*	*Variance*
Column 1	11	355.43	32.31182	20.4068
Column 2	11	438.46	39.86	411.8053
Column 3	11	354.32	32.21091	200.4577
Column 4	11	588	53.45455	433.9947

ANOVA

Source of Variation	*SS*	*df*	*MS*	*F*	*P-value*	*F crit*
Between Groups	3296.184	3	1098.728	4.120239	0.012272	2.838745
Within Groups	10666.64	40	266.6661			
Total	13962.83	43				

Testing Hypotheses – 3

Ho: There is no significant difference between Profit Before Tax of CRISIL, ICRA and CARE
H1: There is significant difference between Profit Before Tax of CRISIL, ICRA and CARE
As the calculated value is more than critical value, the null hypothesis is not accepted. Therefore, there is a significant difference between CRISIL, ICRA and CARE.

PBT/REVENUE

Financial	CRISIL	ICRA	CARE
2000	47.68	NA	27.95
2001	25.96	40.58	34.66
2002	41.30	40.06	35.26
2003	38.99	36.89	33.81
2004	36.14	37.08	35.89
2005	36.42	27.27	29.19
2006	33.98	45.04	52.36
2007	33.77	47.53	55.87
2008	43.36	55.15	69.84
2009	40.98	51.91	87.32
2010	38.95	57.93	14.16
2011	46.82	48.51	75.92
2012	27.64	47.60	72.48
2013	49.66	44.20	70.31
2014	34.03	45.46	67.67
2015	29.45	37.01	53.07

ANOVA: SINGLE FACTOR
SUMMARY

Groups	*Count*	*Sum*	*Average*	*Variance*
Column 1	15	557.4533	37.16355	45.35257
Column 2	15	141333.2	9422.211	39940418
Column 3	15	64360.81	4290.721	8582340
Column 4	15	662.2407	44.14938	63.12715
Column 5	15	10091.25	672.75	1349199
Column 6	15	5400.87	360.058	399339
Column 7	15	5218.1	347.8733	391572.3
Column 8	15	787.8034	52.52023	448.1553

ANOVA

Source of Variation	*SS*	*Df*	*MS*	*F*	*P-value*	*F crit*
Between Groups	1.18E+09	7	1.69E+08	26.70169	3.23E-21	2.092381
Within Groups	7.09E+08	112	6332928			
Total	1.89E+09	119				

RESULTS AND FINDINGS

The findings of the study show that there is significant difference between dividend payout ratio of CRISIL,ICRA and CARE. The dividend payout ratio of these three agencies has been considerably good because the confidence built by the debenture holders in their ratings is high. The earnings per share of CRISIL, CARE,ICRA and Brickwork Ratings has also not shown any significant difference. This indicates that the commitment of the agency is known through the skill and knowledge employed by its staff. Among the three top credit rating agencies the profits are significantly different.

CONCLUSION

The result of study states that the profits are high in the rating agencies due to their empowered organizational commitment of more number of rating debt instruments. It was also found that there exist positive and significant relationship between the dividend payout ratio and earnings per share in all the three rating agencies. It could be concluded that the influence of various financial indicators has been varying in all the four credit rating agencies.

LIMITATIONS

1. The study is limited to a period of 2001 to 2015.
2. The data available in the secondary source is considered for the present study.
3. The financial indicators are focused from the view of credit rating agencies.

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