CHAPTER 7

CONCLUSIONS: FINDINGS, RECOMMENDATIONS AND SUGGESTIONS

7.1 INTRODUCTION

The concluding chapter brings together the vital aspects of the entire research effort in one place. The essentials of all the preceding chapters are reiterated and summarised, and based on such summarisation; recommendations and suggestions are made in this chapter. As highlighted in the methodology section of the first chapter, the thesis is presented in such a way that if one reads in-between the lines of the first and the last chapters, it would be easy to comprehend what lies between the two.

With such ends in view, this chapter is split into six sections. The second section presents a very succinct description of matters such as the researcher’s rationale for the choice of the research topic, the problem statement, the objectives and hypotheses of the study, the nature, scope, importance and limitations of the study, and the chapter scheme. In a way, it gives a concise summary of the first chapter. The third section furnishes the principal findings of the inquiry. Based on the findings, the fourth section gives the recommendations and suggestions. The fifth section provides the scope for further research. And the sixth section concludes the chapter.

7.2 RESEARCH DESIGN: AN OVERVIEW

A succinct summary of the research design is presented here. It includes such matters as: need for the present inquiry or the researcher’s rationale for choosing the present topic for doctoral research; problematics (problem statement); objectives set for the study; hypotheses intended to be tested; methodology adopted by the researcher in
this study; nature, scope and importance of the study; limitations of the study; and the chapter scheme.

7.2.1 Need for the Present Research Inquiry: Researcher’s Rationale

The era of liberalisation, privatisation, marketisation and multinationalisation, inter alia, has brought with it unprecedented changes, challenges and opportunities and also ways and means to face the challenges effectively. Everybody around the globe is affected by this mega process of globalisation. With a view to coping with the new business environment, the organisations have been reengineering their approaches and redesigning their instruments to attract fresh investments. The redesigned/innovated instruments are highly complex in nature and their assessment requires scrupulous expertise. In this context, it is not just vital but critical for CRAs to measure various aspects of the organisation which reflect not just the past performance and present credentials but also the future prospects of the organisation. The review of the theoretical and empirical works on CRAs and their services (Chapter - three) shows that few researchers across the globe have proposed few models, but the fact remains that not all the dimensions of issuers are considered in the models while assigning rating. Not much research has gone into the area of developing a comprehensive model covering all the aspects. The review also highlights that majority of the works in the global context have analysed the impact of rating upgrades and downgrades on stock prices. Few studies have analysed the impact of rating watch and rating outlook, but no concrete view is established with respect to those events. There are hardly any studies in Indian context that have analysed the impact of rating changes on stock prices by categorising the changes - agency wise, industry wise, grade wise and year wise. Studies on the impact of rating watch and rating outlook on stock prices are also not examined. It is pertinent to point out that there is a paucity of systematic research endeavoured in the Indian context.
However, this should not lead us to the hasty conclusion that no work has been done on CRAs and their services in India. A few works are there but they are focused mainly on the performance of CRAs, investors’ perception towards CRAs and a few in the study area with different time periods. The aforesaid gaps in research on the CRAs and their services encouraged the researcher and her research supervisor to take up the present piece of research for doctoral thesis.

7.2.2 Problematics

With a view to identifying and making explicit the various dimensions of the problems implicit in the research topic, the topic is analysed by raising some relevant questions. In other words, the topic is problematised through questions. The questions raised include:

- In these days of hyper competitive markets and complexity in investments; awareness and knowledge about the CRAs and their services is a must for all stakeholders. Are the investors’ aware of all the services offered by CRAs?
- Credit rating being a multivariate function is expected to embrace the entire (both external and internal) perspective of an organisation. Do the CRAs consider such wider aspects when rating an entity or an instrument? In other words, what are the determinants of credit ratings?
- The credit rating being a decisive variable in the investment decision ought to capture accurate data of the organisation. The CRAs heavily rely on the data provided by the issuers. How do CRAs ensure the accuracy of the data provided by issuers?
- Debenture ratings are more prominent in the Indian markets. The CRAs consider firm specific factors such as liquidity ratios, leverage ratios and profitability ratios to be more important in the debenture rating process. Do these financial variables
adequately capture the company’s performance? Do all the CRAs have consistent debt rating methodology?

- Qualitative factors are subjective in nature and difficult to quantify. How do CRAs quantify the qualitative data in the rating process?

- There are studies which lend diametrically diverging evidences to the assertion that “CRAs provide valuable information to the markets”. Do CRAs carry new information in the Indian markets context or do they summarise the publicly available information?

- The current issuer pay model of CRAs leads to conflict of interest. What are CRAs doing to eliminate the inherent conflict of interest between them and the issuers?

- Given the critical role of SEBI recognized CRAs and their services, what is the perception of investors’ towards CRAs performance and is there any influence of demographic factors of investors towards performance of CRAs measured in terms of timeliness, accuracy, methodology, transparency and CRAs orientation towards investors?

### 7.2.3 Objectives of the Study

The objectives set for the study, to a great extent, are based on and derived from the researcher’s rationale (Section 7.2) and the problematics (Section 7.2). They are:

1. To make a relatively comprehensive review of the research works those have gone into the present area of research so far.

2. To identify and compare the services offered by SEBI recognized CRAs with special reference to rating and grading services.

3. To identify and compare the determinants of credit ratings of SEBI recognised CRAs.
4. To understand the regulatory framework of SEBI recognised CRAs.

5. Given the absence of a comprehensive model of CRAs, it is intended to build a simple theoretical credit rating model for the use of Indian CRAs.

6. To assess the debt rating methodology (both within the grade and across the grade) of SEBI recognised CRAs.

7. To examine the cross sectional variation in stock prices owing to the debt rating changes (of the SEBI recognized CRAs).

8. To study the awareness levels of investors towards CRAs and their services.

9. To study the influence of demographic factors on the investors perception towards performance of CRAs

**7.2.4 Hypotheses**

Hypotheses proposed to be tested and subsequently got tested in the thesis are given below. Some of them are tested theoretically, and some, empirically.

1. The rating determinants are identical for all the SEBI recognised CRAs.

2. Debt rating methodology adopted by CRAs is consistent both within the rating grade and across the rating grade.

3. Debt rating changes (both upgrades and downgrades) have an impact on the stock prices of the securities concerned.

4. Debt rating changes (both upgrades and downgrades) of different CRAs have an impact on the stock prices of the securities concerned.

5. The respondent investors are aware of the SEBI recognised CRAs, their services offered, instruments rated and their functioning.

6. There is a positive association between the demographic factors of investors towards CRAs performance.
7.2.5 Research Methodology

The methodology adopted is quite in keeping with the problematics and the objectives set for the study. The researcher has gathered the information and the data required for the study from both secondary as well as primary sources

i. The secondary sources include: the various publications of the rating agencies, rating agencies websites, SEBI reports, RBI Bulletins, databases such as Ace equity analyser, ThomsonReuters financial database, Prowess, money control.com, BSE, research papers, working papers, articles, annual reports and doctoral theses.

ii. The Primary sources include: the questionnaire-based interview method. In this regard, the researcher developed questionnaire and collected by personally administering questionnaires/schedules to the individual investors through stock broking firms located in Ballari, Hosapete and Bengaluru such as Karvy securities, Religare securities, Geogit securities, Anandrathi, Kotak Securities, Angel broking firm, HDFC securities etc. The data was also collected from individual rating agencies. The first questionnaire entitled “Credit Rating Agency Profile” (Annexure 1) was used to gather data pertaining to individual CRA and the second one entitled “Individual Investors’ awareness and perception towards credit rating services in India” (Annexure 2) was used to capture the investors’ awareness and perceptions towards CRAs.

iii. The information and data so gathered have been used in the core chapters of the thesis.

iv. Both aggregative and disaggregative methods have been used in analyzing and interpreting the data and findings; because, often what holds good at aggregate level may not hold good at disaggregate level. More than that, many a time, the aggregates conceal the differences with-in the aggregates.
7.2.6 Nature, Scope and Importance of the study

i. As the title of the thesis suggests, it is an investigation into diverse facets of credit rating services both theoretical and empirical. It is an in-depth inquiry into the comparative analysis of CRAs services, determinants, rating methodology, influence of debt rating changes on security prices, investors’ awareness and perception towards performance of CRAs. Even though the title does not indicate anything about its users (investors), the study of users constitutes an integral part of the present research inquiry.

ii. The study focuses on the four major and well established SEBI recognised CRAs in India (CRISIL, ICRA, CARE and INDIA RATINGS). Due to non availability of data and its recent presence, Brickwork Ratings agency (BWR) and Informerics Valuation and rating Pvt Ltd is not included in the study and SMERA being a niche agency which caters to small and medium enterprises only is not considered for the study. Both primary as well as secondary data has been used for the study.

Temporally, by and large, the investigation is conducted for different time periods. The consistency of the debenture rating methodology of four CRAs has been assessed during the period 2008-09 to 2015-16. The impact of rating changes on the security prices concerned is analysed for the period 2001 to 2015. As far as the data pertaining to investors’ perception, the researcher went personally to the stock broking houses and met most of the investors and collected the required data.

iii. Credit ratings are particularly useful for investors when they face an array of investment opportunities. Therefore, considering the usefulness of credit ratings and its importance to investor’s community, it is necessary to study different aspects of credit rating. Also, the review of the theoretical and empirical studies
made in the third chapter highlight that despite the increasing importance of credit rating agencies as information providers and gate keepers, the research relating to credit rating in the Indian context has been limited. So, the present study is a modest attempt to evaluate different facets pertaining to rating agencies and to know the investors’ awareness and perception regarding the performance of CRAs.

The empirical findings derived there from, it is hoped, would be of immense use to various stakeholders such as regulators, issuers, investors and government.

7.2.7 Limitations of the Study

Notwithstanding the importance that the thesis claims in terms of its contribution to the theory and usefulness of CRAs and their services, it does have some limitations. But for the limitations mentioned below, the work’s significance would have been more than what it is now.

- Having identified the need for a simple theoretical credit rating model for the use of all stakeholders through a relatively comprehensive survey of the literature (theoretical and empirical) on CRAs and their services (chapter 3), a simple theoretical model of CRAs is developed. In it the influence of each factor in determining the credit rating and the precise weight to be considered for each industry is not identified.
  - But the researcher knows that theory building is not an easy task. It is only a humble attempt. As such, the researcher does not claim either finality or infallibility for the simple theoretical credit rating model developed by her (chapter 3).
• The researcher could not include any qualitative variables to study the consistency of debt rating methodology both within and across the grade.
  o Further only four rating grades ‘AAA’, ‘AA’, ‘A’ and ‘BBB’ are considered to study the consistency of CRAs debt rating methodology. The researcher could not take up other rating grades such as ‘BB’, ‘B’, ‘C’ and ‘D’ owing to the non-availability of data for that exercise.

• The assertion that ratings carry information to the security markets is analysed, interpreted and tested using debt rating change (both upgrades and downgrades) of four SEBI recognized CRAs during 2001 and 2015.
  o The researcher could not undertake this exercise for all other financial instruments such as bank loans, equity, commercial papers, and certificates of deposits. The researcher was also not able to study the impact of rating outlook and rating watch on stock prices. The researcher could not undertake such an exercise owing to the non-availability of accurate and reliable data and information required for that exercise. This, indeed, is a limitation.

• In spite of these limitations, the work claims its importance by adding something meaningful to the existing knowledge of CRAs and their services apart from adding some useful dimensions to research methodology and research reporting.

**7.2.8 Chapter Scheme**

In all there are seven chapters in the thesis. The first chapter, which is introductory in nature, among other things, acquaints us with what is proposed to be done, why it is proposed to be done, and how it is proposed to be done. The second chapter entitled Profiles of the CRAs throws light on various aspects of SEBI recognised CRAs. The profiles include details on the year of establishment, rating services offered, rating
methodology adopted, rating symbols, shareholders information, and promoter’s information, apart from providing the regulatory framework of CRAs. The next four chapters are core chapters of the thesis. A relatively comprehensive survey of literature – theoretical and empirical – pertaining to CRAs and their services in general, and Indian CRAs, in particular, is undertaken in the third chapter. While doing so an attempt is also made to develop a simple theoretical credit rating model for the use of Indian CRAs. The fourth chapter attempts to study the debt rating methodology of CRAs using financial ratios. The fifth chapter is devoted to study the impact of debt rating changes on stock prices. The sixth chapter is designed to capture the investors’ levels of awareness and perception towards the performance of SEBI recognized CRAs. The seventh chapter, being the last chapter, concludes the study by providing an integrated summary of all the principal findings, and based on the findings, it makes some recommendations and suggestion as curative measures to the SEBI recognised CRAs and to regulatory body SEBI, which can be applied to CRAs somewhere else with some context-specific modifications. The thesis also carries some suggestions for further research.

### 7.3 A SUMMARY OF THE PRINCIPAL FINDINGS

This research work has provided us with an opportunity to study and understand diverse facets of CRAs and their services. The study has helped us to gain an insight into the functioning of CRAs. This section intends to provide a brief account of the principal findings of the study.

#### 7.3.1 Profile of CRAs

- The CRAs in India is the brain child of CRISIL. CRAs in India got established in the light of the successful experiences drawn from the Global CRAs of USA. Indian CRAs are either promoted or have strategic tie-ups with Global CRAs (CRISIL’s largest shareholder is SandP; ICRAs largest shareholder is Moody’s;
India Ratings is a subsidiary of Fitch). Though Indian CRAs are not as robust as global CRAs in their operations and research domains, the alliance with Global CRAs have certainly helped the SEBI recognised CRAs to gain enormous knowledge and add value in the rating methodology.

- Of the seven CRAs recognised by SEBI, four CRAs (CRISIL, CARE, INDIA RATINGS and SMERA) have their head office in Mumbai; one in Bengaluru (BRICKWORKS); one in Gurgaon (ICRA) and one in New Delhi (INFOMERICS).

- SMERA is the country’s first and the only dedicated rating agency that focuses on MSME sector. BRICKWORKS and INFOMERICS rating agencies are nascent in the ratings venture.

- INFOMERICS which has close to twenty five years of experience in financial service is newly registered CRA under SEBI to provide rating service.

- The four major SEBI recognised CRAs (CRISIL, ICRA, CARE and INDIA RATINGS) are engaged in providing other ancillary services such as Information and Advisory Services; BPO/KPO Services; Risk Solutions and Information Technology Solutions, apart from Rating and Grading Services.

- The financial performance of the four major CRAs show that their earnings have increased every year owing to the range of ancillary services providing by them.

- The ratings stability and transition rate of four major CRAs for a period of 10 years (2006 to 2016) show that the ‘AAA’ rating grade has the highest stability and has moved down by only one notch that is to ‘AA’ rating grade with an exception in India Ratings. The ‘C’ rating category showed the lowest stability and eventually was downgraded to Default grade. This highlights that the rating methodology is lenient and issuer friendly. The CRAs may have provided higher
initial ratings to appease the issuer and subsequently downgraded the instrument or issuer when deterioration was apparent.

- BRICKWORKS, SMERA and INFOMERICS rating agency’s major focus is on Rating/Grading and Research Services and do not provide other ancillary services.
- It is also learnt that all the seven SEBI recognised CRAs rate Long Term, Medium Term and Short Term Instruments; Insurance Companies’ ability to pay claims; Issuers; SSI/MFIs/MSME and Bank Loan Ratings. Further, Corporate Governance Ratings; Structured Products Rating; Rating of State Government/U Urban Local Bodies; Mutual Fund/IPO grading and Real Estate/Developer Grading is offered by all CRAs except SMERA. In addition to these, CRISIL, ICRA and CARE also grade the Maritime Training Institutions/Courses. CRISIL, ICRA, BRICKWORKS and INFOMERICS also undertake Grading of Healthcare Institutions. While, BRICKWORKS rating agency has pioneered in providing ITI/NGO and Tourism grading.
- All the CRAs have standardised their rating symbols for rating the Long, Medium and Short Term Instruments, Issuers, Structured Products and Mutual Funds Grading. Whereas, the CRAs rating/grading symbols vary for Microfinance Institutions, Maritime Training Institute, Health Care Institutions and Corporate Governance. The way the prefix and scales are used also vary.
- All the CRAs portray the rating process and determinants used in the rating process, but the exact weight attached to each determinant is kept confidential. The quantitative model of credit rating process is not revealed.
- All the CRAs predominantly assess Business risk, Industry risk, Financial risk, and Management risk to arrive at a rating. CRISIL and CARE in addition to the above analyse the Project risk too. Group structure is also considered by CRISIL
and INDIA Ratings CRA. It is also observed that the determinants considered by CRAs are not by and large forward looking and market based.

- The accuracy of ratings is measured by the number of defaults and the rating sustainability of CRAs. It is observed that CRISIL, India Ratings and BRICKWORKS rating agency had lesser default rates; and ICRA had more default rates. In terms of rating sustainability, India Ratings has the highest rating stability for AAA, AA and A rating grades. Whereas, CRISIL has the highest stability for BBB rating grade.

- The CRAs currently follow the issuer pay model and the fee collected from issuer is not disclosed by ICRA, BRICKWORKS, SMERA AND INFOMERICS rating agencies. It is also found that the CRAs reserve the right to modify the fee structure for bulk deals and complex instruments.

- As per the circular dated September 2017 by SEBI, all the CRAs disclose both the accepted and unaccepted ratings on their website. The ratings that are unaccepted by issuer carries an asterisk (*) indicating that the issuer has not cooperated with the CRAs and the rating is based on the best available information.

- It is also found that the amendment made by SEBI on the CRAs disclosure practice aims to increase the transparency in CRAs. The CRAs are required to upload the list of defaulted issuers and instruments on their website; the movement of each credit rating; the movement of credit rating from investment grade to speculative grade and the movement of credit rating that has changed more than one notch. Unfortunately, the disclosure pattern is not consistent.

- SEBI has restricted the threshold on cross-holding in CRAs to ten per cent to eliminate conflict of interest.
The Indian CRAs undertake only solicited ratings and unsolicited ratings are not practiced by SEBI recognised CRAs.

7.3.2 Outcomes of the Review of Theoretical and Empirical Works

- Major works carried out in India and abroad covering different aspects of credit rating (determinants of rating, impact of rating on stock prices, default prediction models, investors’ perception towards CRAs) are reviewed, highlighting the contribution of various researchers. The review shows that most of the studies have been extensively evaluated for developed markets (the USA) for the obvious reason that these CRAs have been in operation there for more than one century. However, works in emerging markets like India are limited.

- CRAs arrive at a particular rating after extensive analysis of both, quantitative factors (financial variables) and qualitative factors (management of the company, age and size of the company, business profile, goodwill, strength of the brands, core competencies) for an entity/instrument. Qualitative factors are subjective in nature and are difficult to quantify for analysis. While on the other hand, quantitative elements prove to be good predictors of ratings which in turn measure the risk; Review highlights that all rating agencies and researchers worldwide assert that financial ratios/variables are an important input into their ratings.

- Most of the studies mentions that Liquidity ratios (current ratio, quick ratio), Solvency ratios (debt equity ratio, interest coverage ratio), Profitability ratio (operating profit margin, return on capital employed, return on net worth, earnings before interest and tax, cash profit margin) are considered to be the most important quantitative factors that go into the determination of a rating. However, the works on rating agencies consistency in debt rating methodology viewed in terms of these variables are very limited in India context.
• Rating analysts super impose subjective judgments over quantitative variables while assigning final ratings. Thus, it gives the impression that qualitative factors play a vital role in bond rating.

• The stock price reactions to the announcement of rating changes are mixed. Here, the information content in credit rating is examined. Few studies in the US have shown that rating updates carry no new information, while a few other studies opine that CRAs deliver valuable information that are not factored in the stock prices as they have access to confidential and inside information. In general, there is substantial evidence in global market that downgraded rating announcements have seen a shrink in the stock prices, while the upgraded rating announcements have not seen any significant changes in the stock prices. Studies on impact of rating changes on stock prices in India have been examined by few researchers. However, there is a need to analyse the impact of debt rating changes on stock prices by categorising the changes agency wise and industry wise.

The aforesaid findings based on the theoretical and empirical studies reviewed in Chapter-three, lend support to the following hypotheses:

1. Debt rating methodology adopted by CRAs is consistent both across the grade and within the grade (Hypothesis No.2)

2. Debt rating changes (both upgrades and downgrades) have an impact on the stock prices of the securities concerned (Hypothesis No.3)

3. Debt rating changes (both upgrades and downgrades) of different CRAs have an impact on the stock prices of the securities concerned (Hypothesis No.4)
7.3.3 Debt Rating Methodology of CRAs

The findings of debt rating methodology within the rating grade are given below:

- It is gratifying to note that the rating methodology of all the four CRAs within the rating grade is found to be fairly consistent in assigning AAA and A rating grade with exception to only net profit margin in case of AAA rating grade and EBIT and GPM in case of A rating grade.

- It is indeed satisfying to record that all the four CRAs while assigning AA Rating grade have similar values of the below mentioned ten financial ratios, namely debt equity ratio, long term debt equity ratio, interest coverage ratio, operating profit ratio, Return on capital employed, Return on net worth, Earnings before interest and tax margin, Gross profit margin and Debt to capital ratio.

- Seven ratios namely Operating profit margin, Return on net worth, Earnings before interest and tax, Gross profit margin, Net profit margin, Long term debt equity ratio, Assets turnover ratio are found to be similar while assigning ‘BBB’ rating grade by four CRAs.

- The Tukey’s HSD (Honest Significance Difference) test shows that consistency of CRAs rating methodology within the rating grade is maximum for ‘AAA’ rated companies and more so in case of CARE agency, followed by ICRA; similarly, the consistency in ‘AA’ rated companies is found more in CRISIL, followed by CARE; consistency in ‘A’ rated companies is more in CARE followed by CRISIL; consistency in ‘BBB’ rated companies is maximum for CARE and ICRA, followed by INDIA RATINGS. Overall, CARE rating agency exhibits more consistency when compared to other CRAs.

- The overall analysis shows that of the fifteen ratios, it is appalling to see that the values of only four ratios namely, current ratio, quick ratio, financial charges
The coverage ratio and debtors turnover ratio are found to be similar while assigning similar rating grades by four CRAs.

The findings of the analysis made across the rating grade are presented below:

- Across the rating grade analysis shows that the four CRAs have used similar values of nine ratios while assigning different rating grades. Nine ratios, namely, current ratio, quick ratio, return on capital employed, return on net worth, long term debt equity ratio, total debt to owners funds, financial charges coverage ratio and debtors turnover ratio are not varying in different rating grades. This shows that CRAs rating methodology is inconsistent in employing these ratios during the study period.

- However, there are some exceptions where, CRAs have different rating assigned based on differing values of a few ratios. ICRA agency has differentiated the rating grades of companies based on six ratios namely Debt equity ratio, operating profit margin, earnings before interest and tax margin, gross profit margin and net profit margin ratios. While, CRISIL has differentiated the rating grade in only one ratio i.e., Interest coverage ratio and CARE agency has differing EBIT margin and Assets turnover ratio values in different rating grades. This shows that ICRA rating agency has comparatively rating consistency.

7.3.4 Impact of Debt Ratings Changes on Security Prices

The findings pertaining to the impact of rating changes (upgrades and downgrades) on stock prices; are briefed here:

- At the aggregate level, it is dismal to note that credit rating changes (both rating upgrades and rating downgrades) did not trigger abnormal returns. The rating changes have not provided any new information/surprise to the market and there is no impact of either rating upgrade or downgrade on security prices. It can be
implicitly understood that the security prices have already factored the changes that have led to credit rating changes. This highlights that CRAs are not proactive in revising the ratings in a timely manner.

- At the disaggregate level, that is, the analysis made across the rating agencies is also quite astonishing, as the credit rating changes (both upgrades and downgrades) of individual agencies have not brought about any major impact on the stock prices. However, it is also found that rating upgrade news announced by ICRA and INDIA RATINGS has yielded positive abnormal returns for many days, while rating downgrade information announced by INDIA RATINGS has provided negative abnormal returns for majority of the days after the announcement of the event. This shows that rating change information by ICRA and INDIA RATINGS helps investors to some extent in decision making.

- Industry wise analysis is also appalling, as the industries under study exhibited negligent changes in stock prices except for rating downgrade announcements of iron and steel product companies.

7.3.5 Investors Awareness and Perception towards Performance of CRAs

The researcher has interviewed 398 investors with a view to capture the awareness and perception levels of investors about CRAs and their performance. The researcher has ascertained the awareness and perceptions of investors by using the questionnaire-based interview method. The responses so secured are tabulated into an Appendix Table (No. 4) and tables (No. 6.10 and 6.16 to 6.21) are derived from it. With a view to lend clarity to the analysis and interpretation of the data pertaining to the responses of select respondent investors, a simple questionnaire consisting of twelve questions on the awareness levels and twenty seven questions on perception was prepared. The findings are given below.
The Investors surveyed are aware of four major SEBI registered CRAs, CRISIL, ICRA, CARE and INDIA RATINGS. Only a small portion of investors are aware of BRICKWORKS, SMERA and ONICRA. Very few investors are aware of INFOMERICS. A great portion of investors are aware that rating agencies prime service is rating and grading of instruments. Not all the investors expressed their awareness about the ancillary services provided by CRAs. Ninety per cent of the investors are aware that CRAs rate debentures/bonds. More than eighty per cent of investors are aware that CRAs rate preference shares, Mutual fund schemes and IPOs. Only a small portion of investors are aware that CRAs undertake grading of Structured Financial Products, Construction Entities, Shipyard, Solar, RESCO, MTI and REIT. It is also found that 57 per cent of the investors are ignorant about the functioning of CRAs.

The analysis shows that the demographic factors such as age, qualification, occupation, and income have an impact on the perception of investors towards CRAs performance. It is found that the perception of investors varies with varying age groups. Young investors are optimistic and elderly investors do not have good opinion about CRAs. It is also observed that there is a strong association between investors’ qualification and their perception towards performance of CRAs. Investors who have a qualification of higher secondary have good opinion about CRAs performance. While, the perception of the investors employed in different sectors and having different incomes are different and have varying opinion on the performance of CRAs. The demographic factors such as gender and marital status have no influence on the perception of investors.
7.4 RECOMMENDATIONS AND SUGGESTIONS

In the present work, the recommendations and suggestions constitute the prescriptive part of the thesis. The recommendations that follow are related to regulations governing CRAs, rating methodology/process of CRAs, the ways and means to increase investor’s awareness towards CRAs and their services; and the suggestions are relating to regulation of CRAs.

7.4.1 Rating Methodology – Related Recommendations

The recommendations of the researcher are based on the qualitative gaps identified through the interaction the researcher had with the rating experts/rating executives, investors and empirical evidences of the core chapters.

The CRAs heavily rely on the information and data (mainly financial statements) provided by the issuers. The CRAs claim that they consider qualitative factors such as (management of the company, age and size of the company, brand, and projects in hand) in the rating methodology, but the precise weight assigned to each factor is not stated. It is also found that the CRAs reveal the processes flow chart and not the actual rating methodology. Their notions are very vague and have no fixed methodology, and qualitative factors many a time outweigh the quantitative factors at a review meeting held between issuer and credit rating analysts. This was discovered by the researcher during her personal interactions with the rating analyst/executives and the rating material provided by CRAs.

In this background, the researcher recommends the following:-

- CRAs should disclose the exact rating methodology and statistical/mathematical tool used to arrive at a particular rating, i.e., state explicitly the qualitative and quantitative determinants and their precise weights used for rating a particular entity/instrument. It is also recommended that all ratings symbols, methodology
and assigned ratings whether accepted or not accepted by issuer are to be hosted on websites of each of the CRAs regulatory platforms such as websites of RBI, SEBI, IRDA and PFRDA.

- The CRAs should indulge themselves in more vigilant and deeper diligence. They have to use both their formal and informal sources to validate the data provided by the issuers. It is a must for CRAs to develop the competence required to carry out due diligence process apart from corroborating the information from the financial statements.

- CRAs should conduct regular workshop and rigorous training for their employees to improve their skills in data gathering from issuer and analysis of the data which is both explicitly stated and implicitly implied in arriving at rating. The rating team should be able to make a thorough inquiry about the firm. The Rating committee decides the rating, it is recommended that the rating committee should involve a minimum of two analysts who were involved in the evaluation process.

- It is recommended that CRAs should make use of multi dimensional constructs such as financial/accounting measures, operational measures, market measures, survival/growth measures, economic value measures on one hand and socio cultural aspects, political, technological, legal aspects on the other hand that captures the comprehensive picture of an organisation/instrument to arrive at a rating (as discussed in detail in chapter 3).

- It is advised that CRAs should proactively monitor the debt obligations and financial health of the issuer/company by keeping a track on the capital structure of the firm, delay or default in interest payment, risk of the projects undertaken, deterioration in liquidity conditions of the issuer. Such changes in the firm should trigger the rating change (upgrade/downgrade) and rating watch.
SEBI should advise CRAs to regularly review ratings upon the occurrence of any corporate event of the issuer/company such as merger, joint venture, amalgamation, acquisition, annual report, dividend announcement, FPOs (Further Public Offering) and such others.

It is strongly recommended that the current issuer pay model needs to be changed to regulator/exchange pay model, which will minimise the conflict of interest between issuers and CRAs.

It is also recommended that the regulator should encourage the CRAs to practice unsolicited rating and CRAs apart from publishing both accepted and unaccepted ratings of issuers, should publish unsolicited ratings too.

CRAs are advised to retain all the internal records which were used to arrive at a particular rating. The logic for any deviation in decision should also be noted. CRAs should have proper internal written procedure documenting the steps required for surveillance.

SEBI should incorporate a provision of making CRAs accountable for the ratings published by them, such as making CRAs liable for any loss caused to investors owing to negligent or fraudulent rating. One way is to monitor the ratings stability and transition rates. It is recommended that SEBI instil a strict regulation to all CRAs to monitor their ratings, the rating grades should exhibit a stability of 99 per cent and above for all rating grades, failing to comply with it, should enable SEBI to provisionally cancel the licence.

SEBI should strictly recommend CRAs to engage only in rating and rating related research activities and hive off all other services offered by CRAs.

Currently the rating symbols are in standard and similar format for long and medium term, short term, issuers, mutual funds and structured products. It is
recommended that SEBI standardise the rating symbols or grades for all the other instruments rated by CRAs such as SME, IPO, MTI, ITI, Corporate Governance and hospital grading. Apart from this, the suffix used (if any) by all CRAs should be identical. This will avoid confusion and obscurity among investor community.

7.4.2 Awareness and Perception – Related Recommendations

Some of them have shown their awareness about the SEBI recognised CRAs, their services, determinants, and their perception relating to performance of CRAs by recording their choice in writing. The following recommendations concerning CRAs are based on and derived from the demands of the changing business environment.

- Investors perceive that CRAs do not update the data on their websites promptly and regularly. Hence, the CRAs are required to put in place measures to anticipate the changes so as to provide relevant and accurate data to the investors regarding the performance of the company through the ratings. CRAs must ensure they communicate with all stakeholders about the updates or changes; they must educate investors regarding their rating methodology and rating symbols used.

- Timeliness of ratings – Rating outlooks and rating watch signal the possibility of a rating change and have a limited life and this should be reviewed and replaced by a rating within a small span of time.

- Usage of Ratings – Most of the investors accept the ratings blindly without inspecting on their own. It is always advised to investors that they not only rely on CRAs data but also work on the fundamentals of the company, their market value, past credentials, present situation and future possibilities; and ratings must serve to be one of the important inputs in the decision making process.

- Disclosure policy - All CRAs must disclose the shareholding pattern to the public to ensure that the relationship of CRAs and any entity that they rate is at an arms
distance. Apart from this the SEBI regulation dated September 2017 mooted
tighter norms for CRAs. Details of the fees collected by CRAs for the current and
all previous rating assignments should be standardised and disclosed on the
website to avoid the menace of rating shopping.

- CRAs must update the list of defaulted issuers and the rating transition statistics
  on their websites regularly. Apart from this, CRAs must make a wide publicity
  through both electronic media and print media. Though SEBI has mandated all
  CRAs to disclose the defaults on website, it is unfortunately not consistent in all
  CRAs website. It is recommended that all CRAs follow consistent format to
  update the list of defaulted issuers and instruments on their website; movement of
  each credit rating; movement of credit rating from investment grade to speculative
  grade and movement of credit rating that has changed more than one notch.

- Workshops/Seminars must be organized by CRAs to create awareness about their
  rating methodology. It also helps CRAs to update all the stakeholders on the
  recent developments in the domain of credit ratings. In turn, the workshop will
  provide a platform for all stakeholders to discuss the challenges faced by them in
  using the ratings. CRAs can also set up a help desk to make themselves available
  to investors. Through this, investors can get educated on the importance of ratings
  in investment decisions.

### 7.4.3 Suggestions

- The current issuer pay model of CRAs is built upon obvious conflict of interest
  and this also paves way to rating shopping. Recent update made by SEBI on
  shareholding pattern i.e., ten per cent cross shareholding cap for CRAs may
  mitigate concerns regarding conflict of interest, independence of operations. In
  order to completely eliminate the conflicts, the possible alternate model i.e.,
subscriber pay model may be encouraged till the regulator pay model is initiated.

In order to enable the subscriber pay model work, CRAs should price the rating publications at a reasonable amount.

- Currently, The CRAs are not subjected to any kind of civil or criminal liability for malfeasance. CRAs enjoy extensive first amendment free-speech protection. CRAs must be made accountable and liable for their decisions. CRAs free speech protection should be eroded.
- There should be minimum regulatory dependence on credit ratings. They should survive merely on their reputation and not on regulatory dependence. Only NRSRO designated CRAs should operate in the markets.
- External audit of rating operations may be conducted to check if rationale and mandate of the rating systems are efficient.
- The CRAs are entrenched in oligopoly market structure, and barriers to entry are also high. Owing to which, there is reduced competition, which in turn lax the rating standards. Hence, it is suggested that SEBI must foster healthy competition among CRAs.

7.5 SCOPE FOR FURTHER RESEARCH

The following suggestions are made with a view to draw the attention of researchers towards such research gaps, so that some such gaps could be filled in, in course of time.

i. The consistency of CRAs rating methodology can be done for other financial instruments such as bank loans, stocks, IPOs and short term securities. Further, other grades such as ‘BB’, ‘B’, ‘C’ and ‘D’ can be included in the study.

ii. The present study has made use of fifteen key financial ratios to study the consistency of CRAs debenture rating methodology. Qualitative variable may also
be included in future studies to assess the consistency in CRAs rating methodology.

iii. The present study has analysed the impact of rating change on stock prices. The study may also be extended to analyze the impact of rating change on bond prices and yields. Also, the impact of rating watch and rating outlook events can be studied. Firm characteristic wise analysis; Investment grade versus speculative grade analysis can also be performed. Further, the impact of IPO grading, mutual fund grading on the stock prices may be considered for future study.

iv. Research may be conducted in examining the rating agencies ability in forecasting the default before or well in time and suggest the best model that is suitable in Indian context.

v. Studies on split ratings can be made to understand the reasons for split ratings and their impact.

vi. Finally, there is a wide scope for research taking investors from different parts of country and comparing their awareness and perception towards performance of credit rating agencies.
7.6 A FEW CONCLUDING REMARKS

This section is structured in such a way that if one reads in between lines of the first section and the last section, one would be able to comprehend the essence of what lies between the two. The research topic is carefully chosen after duly identifying the various research gaps in the field of CRAs and their services. The present inquiry has made an attempt to understand and analyse the importance and impact of rating services of SEBI recognised CRAs. By being a kind of action research, it has emerged as a descriptive, diagnostic and prescriptive thesis – a thesis which can be used by CRAs in reengineering their approaches.

If one reads the simple model of CRAs developed in the thesis for the use of Indian CRAs, along with the theoretical and empirical review (chapter-3), one will be able to identify the importance of multi dimensional constructs in determining the credit rating.

A detailed discussion on the consistency in the rating methodology of CRAs has been done in the fourth chapter and the impact of rating changes on stock prices are analysed in the fifth chapter. The sixth chapter studies the investors’ awareness and perception towards SEBI recognised CRAs. Based on the findings, the CRAs could redesign their approaches towards providing valuable services to the investors. The thesis offers some useful suggestions to investors, CRAs, regulators and issuers.

The researcher, being fully aware of the limitations of her research, does not claim either exhaustiveness or finality for her work. However, it does add something useful and meaningful to the existing knowledge on CRAs and their services in Indian context.