Fiscal Policy Research Institute

FPRI's Research for the ASEAN+3 Research Group Draft Report

The International Discussions on the Credit Rating Agencies and Enhancing Infrastructure to Strengthen the Regional Credit Rating Capacity in the ASEAN+3 Region

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1. Introduction

The evolution of local currency bond markets over the last decade has been one of the success stories of the Asian capital market. Growth in the ASEAN+3 local currency bond markets has been impressive. Outstanding issue volumes have risen by more than 300% since 2000, with government bonds having attracted considerable inflow from overseas investors. Nevertheless, much needs to be done from a regulatory, infrastructural and informational standpoint if Asia is to realise the potential of its fixed income markets by promoting increased growth, diversity and liquidity in its local currency bond markets. Regarding this, much also needs to be done if Asia is to develop dynamic cross-border investment among institutions and private investors, enhancing infrastructure within the region.

Credit ratings are a necessary accompaniment to bond issues. Most regulatory authorities require a credit rating for a bond issue while investment policies of some specific funds are dependent on credit rating limits. Therefore, the implicit corresponding requirement is that credit ratings should be subject to appropriate regulation since they provide investment information of public interest and for public use. The credit rating landscape post 2008 global financial crisis is characterised by regulatory reforms at the national and regional levels such as the revision of IOSCO's Code of Conduct Fundamentals, G-20 Declaration on Strengthening the Financial System that includes an oversight regime for Credit Rating Agencies (CRAs) whose ratings are used for regulatory purposes, U.S. SEC regulation amendments, and EU registration and regulation of CRAs. In Asia, the fragmented nature of regional credit rating market, however, means that any regulatory oversight that has been introduced is confined to the national authorities concerned. The increasing role of global regulatory changes and the continuing involvement of Global Credit Rating Agencies (GCRAs) with growing influence in domestic markets, therefore, become important factors to be considered in the development of regional CRA markets.

This study discusses the present conditions of credit rating markets in ASEAN+3 region in addition to those in European and Latin America regions, and provides a perspective on the relative positions of domestic credit rating agencies (DCRAs) on the path towards regional harmonization.[1] These conditions provide an indication of the potential benefits of an accelerated rating harmonization

[1] *Generally defined as "convergence of various practices and rating principles across borders" in order to achieve a degree of comparability across rating agencies in terms of rating methodology, rating criteria, definitions, benchmarks and overall rating process (Imai,2004).*

process and the establishment of a regional credit rating system, in addition to how well DCRAs will be able to participate under such arrangement. A brief overview of credit rating system in the EU, Latin America and the Caribbean is given in the next section, followed by an overview of DCRAs in the ASEAN+3 region in Section 3 where the role of ACRAA in supporting regional DCRAs development is also discussed. Section 4 contains a more detailed description of DCRAs in major ASEAN markets.[2] Sections 5 to 7 present DCRAs' characteristics that are essential for their credibility and market acceptance in the context of regional credit rating harmonization and development of a regional credit rating system. Section 8 concludes with a discussion on how the regional credit rating system can be developed, principally through a Regional Credit Rating Agency (RCRA), in order to gain investors' acceptance and participation in the regional bond market development.

2. CRA Market Conditions in other Regions

2.1 European Union CRA Regulation

The 2008 global financial crisis and the subsequent Euro crisis brought about a wave of regulatory changes in the European region. The European System of Financial Supervision created in 2009 consists of European Systemic Risk Board (ESRB) and three European supervisory authorities – the European Securities and Market Authority (ESMA) based in Paris, the European Banking Authority (EBA) based in London, and the European Insurance and Occupational Pensions Authority (EIOPA) based in Frankfurt. In 2009, the European Parliament and the Council of the European agree to formulate specific rules for CRAs operating in the EU with principal to protect investors and assure the stability of the financial market. The Regulation on CRA was adopted (Regulation No. 1060/2009) and was amended by the Regulation No. 513/2011. The combined regulations are now referred as the 'CRA Regulation'.

Following the introduction of CRA Regulation, the European Securities and Markets Authority (ESMA) was established as an independent EU authority. Founded on December 2009, ESMA is exclusively responsible for registration and supervision of the credit rating agencies (CRAs) in European Union. ESMA started its CRA supervisory competence on 1 July 2011. Starting with 5 registered CRAs at that time, there are now 32 registered and 2 certified CRAs form 13 countries

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[2] *Indonesia, Malaysia, The Philippines and Thailand*

inside and outside the EU as of March 2013 (Table 1). ESMA requires all registered and certified CRAs to provide historical rating information and statistics such as rating activities, default ratios and transition matrix to its central credit rating information repository (CEREP). CEREP is responsible for publishing rating activity and performance statistics of the CRAs by calculating aggregate statistics of both quantitative and qualitative data and disclose them on its website which is open to anyone and can be used for commercial purposes.

Table 1: ESMA Registered and Certified CRAs

	Name of CRA	Country of residence	Status	Effective date
1	Euler Hermes Rating GmbH	Germany	Registered	16-Nov-10
2	Japan Credit Rating Agency Ltd	Japan	Certified	6-Jan-11
3	Feri EuroRating Services AG	Germany	Registered	14-Apr-11
4	Bulgarian Credit Rating Agency AD	Bulgaria	Registered	6-Apr-11
5	Creditreform Rating AG	Germany	Registered	18-May-11
6	Scope Credit Rating GmbH (formerly PSR Rating GmbH)	Germany	Registered	24-May-11
7	ICAP Group SA	Greece	Registered	7-Jul-11
8	GBB-Rating Gesellschaft für Bonitätsbeurteilung mbH	Germany	Registered	28-Jul-11
9	ASSEKURATA	Germany	Registered	18-Aug-11
10	Assekuranz Rating-Agentur GmbH	Germany	Registered	18-Aug-11
11	Companhia Portuguesa de Rating, S.A. (CPR)	Portugal	Registered	26-Aug-11
12	AM Best Europe-Rating Services Ltd. (AMBERS)	UK	Registered	8-Sep-11
13	DBRS Ratings Limited	UK	Registered	31-Oct-11
14	Fitch France S.A.S.	France	Registered	31-Oct-11
15	Fitch Deutschland GmbH	Germany	Registered	31-Oct-11
16	Fitch Italia S.p.A.	Italy	Registered	31-Oct-11
17	Fitch Polska S.A.	Poland	Registered	31-Oct-11
18	Fitch Ratings España S.A.U.	Spain	Registered	31-Oct-11
19	Fitch Ratings Limited	UK	Registered	31-Oct-11
20	Fitch Ratings CIS Limited	UK	Registered	31-Oct-11
21	Moody's Investors Service Cyprus Ltd	Cyprus	Registered	31-Oct-11
22	Moody's France S.A.S.	France	Registered	31-Oct-11
23	Moody's Deutschland GmbH	Germany	Registered	31-Oct-11
24	Moody's Italia S.r.l.	Italy	Registered	31-Oct-11
25	Moody's Investors Service España S.A.	Spain	Registered	31-Oct-11
26	Moody's Investors Service Ltd	UK	Registered	31-Oct-11
27	Standard & Poor's Credit Market Services France S.A.S.	France	Registered	31-Oct-11
28	Standard & Poor's Credit Market Services Italy S.r.l.	Italy	Registered	31-Oct-11
29	Standard & Poor's Credit Market Services Europe Limited	UK	Registered	31-Oct-11
30	CRIF S.p.A.	Italy	Registered	22-Dec-11
31	Capital Intelligence (Cyprus) Ltd	Cyprus	Registered	8-May-12
32	European Rating Agency, a.s.	Slovakia	Registered	30-Jul-12
33	Axesor SA	Spain	Registered	1-Oct-12
34	CERVED Group S.p.A.	Italy	Registered	20-Dec-12
35	Kroll Bond Rating Agency	USA	Certified	20-Mar-13

Source: ESMA

In November 2011 after two years of operation, ESMA evaluated registered CRAs performance by sending out a formal request for information regarding rating actions for three different classes (banks, sovereigns and covered bonds). Based on the information obtained from the CRAs, ESMA suggested that further formalization and disclosure of CRAs methodologies, policies and procedure including internal control is required and that CRAs should monitor the adequacy of resources in terms of number of employees and expertise, within the context of market development and their impact on the organization, according to its view on CRAs activities in the areas subject to the examination as follows (ESMA, 2012).

2.1.1 CRAs Internal Processes

The new regulatory framework requires CRAs to increase the level of formalization of their activities, to follow more rigorous policies and procedures and to clearly allocate detailed roles and responsibility of the staffs. This includes 1) proper recording of the rating committee discussion to verify internally, as required by Article 8(2) of the CRA Regulation, that "thorough analysis of all the information that is available to it and that is relevant to its analysis according to its rating methodologies" has been made, and 2) consistent application of CRAs' rating methodologies (rigorous, systematic and continuous) as required by Article 8(3) of the CRA Regulation. As a result of the review, ESMA suggested that CRAs use a more rigorous and formalized approach to the organization and recording of core internal processes mainly in the activity of the Rating Committees and decision making within key internal meetings in order to improve control mechanism.

2.1.2 Transparency and Accuracy

According to Article 11.2 of the Regulation (EC) No 513/2011 on Credit Rating Agencies, ESMA has set up a Central Repository (CEREP) for publishing the rating activity statistics and rating performance statistics of CRAs. This is in response to market participants' indication that historical performance data presented by CRAs has not always been completed and that CRAs differ in their approach to collect and present data. CEREP creation is also in accordance with regulatory requirement to enhance transparency and to contribute to the protection of investor by providing information on the past performance of CRAs and about credit rating issued in the past (ESMA 2011). The role of CEREP is therefore to centrally collect data on credit rating issued by CRAs that are registered in compliance with the EU Regulation, on credit ratings that are endorsed by a registered credit ratings agency, and on credit ratings issued by CRAs that have been certified in compliance with the EU Regulation. In addition, CEREP will collect credit ratings issued in a third country by CRAs not certified or registered but belonging to the same group as a registered CRA on voluntary basis. CRAs are responsible for the accuracy and completeness of the data sent but subject to CEREP examination and request for correction and resubmission.

CEREP collects two types of raw data from the CRAs: (1) Rating data for corporate, sovereign or public finance, and structured finance rating, and (2) qualitative data such as explanation of the concept and definitions used by CRAs. Upon receiving data from CRAs, CEREP calculates performance and statistics for predefined periods of time in a harmonized manner and discloses them for public access through the CEREP's website. CEREP does not disclose any individual ratings information to the public but published only aggregated statistics that help promoting transparency and reducing the cost of information for both market participants and regulators.

2.1.3 Analytical Resource

CRA Regulation requires the CRAs allocate sufficient number of employees with appropriate knowledge and experience to its credit rating activities. Recital n. 31 of Regulation No 1060/2009 requires that CRAs should ensure that adequate human resources are allocated to the issuing, monitoring, and updating of credit ratings. In addition, point A(8) of Annex I of CRA Regulation requires that CRAs employ appropriate resources to ensure continuity and regularity in the performance of its credit rating activities. Based on its finding, ESMA suggests that CRAs monitor the adequacy of resources in terms of number of employees and expertise, within the context of market development and their impact on the organization.

2.1.4 Governance and Control functions

The overall framework of the CRA Regulation relies on sound presence of internal control functions – auditing, compliance and internal review function – and focus on their accountability and independence. According to ESMA, CRAs should ensure that their internal control function comply with the CRA Regulation by continuously monitor the adequacy of resources (number of employees and expertise), and make sure that the relevant control functions effectively contribute to consistent credit rating methodologies. CRA Regulation assigned specific duties to the Independent Directors to enhance oversight of the rating process. ESMA expects the Independent Directors to continue developing their role and involvement in CRAs' activities especially in the internal control function.

2.1.5 Disclosure of methodologies and presentation of rating

In order for the users of credit ratings to make informed decisions, CRA Regulation requires credit rating agencies to disclose their rating criteria and methodology in a transparent manner. According to Section E, point 1.5 of Annex I of the CRA Regulation, a credit rating agency should disclose "the methodologies, and descriptions of models and key rating assumptions such as mathematical or correlation assumptions used in its credit rating activities as well as their material change." Recital n. 25 also specifies that "The level of detail concerning the disclosure of information concerning models should be such as to give adequate information to the users of credit ratings in order to perform their own due diligence when assessing whether to rely or not on those credit ratings."

Section D(2)(b) of Annex I of the CRA Regulation further requires that for each rating "the principal methodology or version of methodology that was used in determining the rating is clearly indicated, with a reference to its comprehensive description; where the credit rating is based on more than one methodology, or where reference only to the principal methodology might cause investor to overlook other important aspects of the credit rating, including any significant adjustments and deviations, the credit rating agency shall explain this fact in the credit rating and indicate how the different methodologies or these other aspects are taken into account in the credit rating."

2.2 CRAs in Latin America

In Latin America, there is no single regional regulator that is responsible for CRAs registration and supervision. Credit rating agencies are required to register with the Securities and Exchange Commision (SEC) in their own country under its regulation. In a recent survey, there are mainly 13 credit rating agencies in the Latin America region (Table 2). Peru ranks first with respect to the number of CRAs, totalling 4, followed by Ecuador (2), Columbia (2), Chile (2), Uruguay (1), Mexico (1), and Costa Rica (1). Most of these are GCRA affiliates (Fitch, Moody's or Standard & Poors). Some local CRA operate in several countries. Pacific Credit Rating, Inc. for example, has branches in Bolivia, Ecuador, El Salvador, Guatemala, Panama and Peru. HR Ratings in Mexico is also registered in the United States as a

Nationally Recognized Statistical Rating Organization (NRSRO) and thus has a global presence.

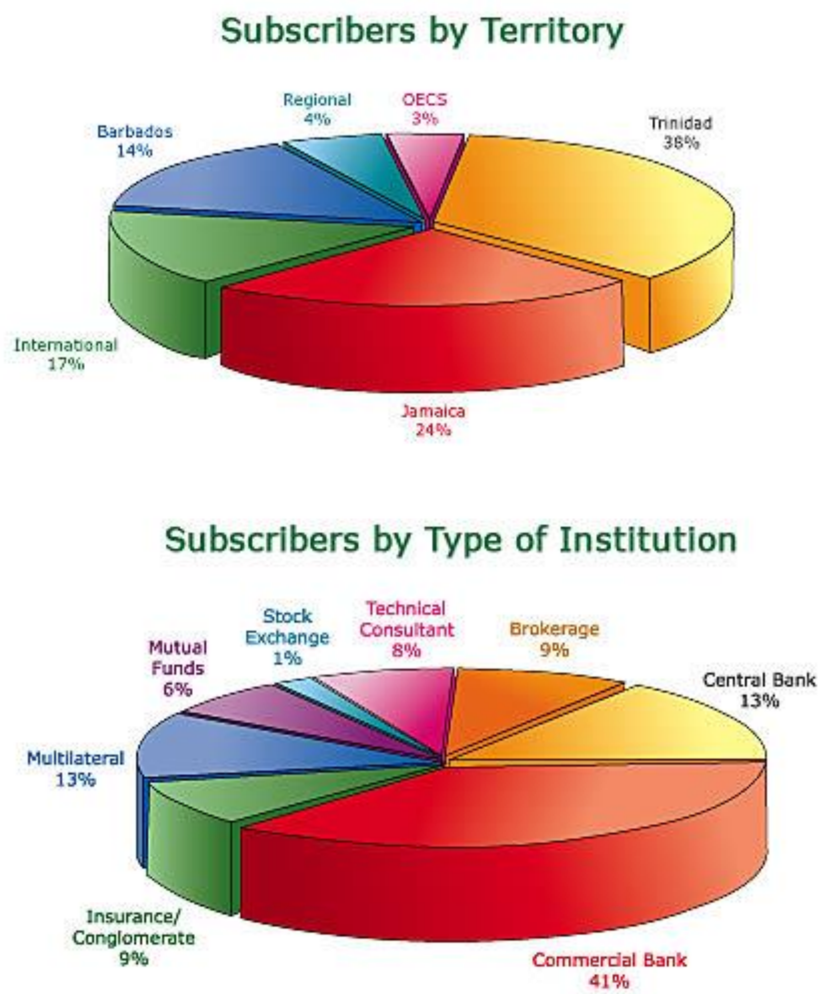
Table 2: CRAs in Latin America

CRAs in Latin America	Description
1. Pacific Credit Rating	Pacific Credit Rating - or PCR - began in Peru but now serves a number of Latin American countries. Branches in PCR Bolivia, PCR Ecuador, PCR El Salvador, PCR Guatemala, PCR Panama, PCR Peru.
2. Apoyo & Asociados Internacionales S.A.C. [Support & Associates International SAC]	Apoyo is based in Peru and is an associate of Fitch Ratings. Services include local ratings for instruments and sovereign risk ratings.
3. Bank Watch Ratings	Bank Watch Ratings is based in Ecuador and is an affiliate of Fitch Ratings.
4. BRC Investor Services S.A.	BRC is based in Columbia and is an affiliate of Moody's Investor Service.
5. Calificadora de Riesgo	Calificadora de Riesgo are based in Uruguay and provide accurate risk assessment for investors.
6. Humphry's	Humphry's is based in Chile and was established in 1988.
7. Classy Asociados S.A. Clasificadora de Riesgo	Class & Asociados is based in Peru.
8. Duff & Phelps de Colombia, S.A., S.C.V	DCR Colombia is a Fitch associate.
9. Ecuability, SA	Ecuability SA is based in Ecuador.
10. Equilibrium Clasificadora de Riesgo	Equilibrium is based in Peru and is an affiliate of Moody's.
11. Feller Rate Clasificadora de Riesgo	Feller Rate is based in Chile and is a strategic affiliate of Standard & Poor's.
12. HR Ratings de Mexico, S.A. de C.V	HR Ratings are based in Mexico and have a large base in international support. It aims to provide transparency on the Mexican financial market.
13. Sociedad Calificadora de Riesgo Centroamericana, S.A. (SCRiesgo)	SCRiesgo are based in Costa Rica and provides risk rating for companies and projects in the region.

2.3 The Caribbean Region

In the Caribbean region, Caribbean Information and Credit Rating Services Limited (CariCRIS) was established as the world's first regional credit rating agency in 2004 as a result of cooperation among 19 members from 23 economies in the Caribbean region in order to support the development of regional capital markets. CariCRIS formation was supported by feasibility studies that indicated the benefits of having a collective regional debt market with substantial economic size, cross-border financing and progressive regulatory regime. CRISIL Limited, India acted as the technical consultant during its formation. CariCRIS has a diversified shareholding structure which limits the influence of individual shareholders or shareholder blocks, meaning that its ownership would not coincide with any single market. The Board of Directors includes representatives from multilateral and regulatory institutions. The Rating Committee is totally independent from shareholders and the Board of Directors.

Figure 1 : CariCRIS Subscribers



Source: CariCRIS

CariCRIS offers national and regional scale (foreign and local currency) ratings to fill in the gap left by GCRAs' global scale that are typically capped by sovereign ratings. Since sovereign ratings of the Caribbean are comparatively low at BBB or below, the non-sovereign counterparts are inevitably compressed towards the lower end of the global scale leaving little variations for investors to differentiate risks at the regional level. Thus CariCRIS's role is to facilitate investors' risk identification and diversification, and act as a regional credit rating agency that provides transparent, independent, and unbiased risk assessments thereby enhancing credibility, acceptability and investors' access. The development of CariCRIS also supports regulatory authorities in increasing investor protection and market discipline and assists local authorities in infrastructure policy formulation and financial sector regulation. CariCRIS's services include credit ratings to debt issued by sovereigns, private and public companies, banks and financial institutions, private credit assessment, and risk management and training. However its revenue from rating income and other services (USD 0.7 million, as of March 2012) is still below total operating expenses (USD 1.0 million).

3. Asia's Local CRAs

The development of ASEAN+3 early domestic credit rating agencies (DCRAs) in Japan and Korea during 1980s, followed by those in emerging markets (such as Indonesia, Malaysia and Thailand) during the early 1990s, has preceded respective countries bond market development. The past decade also saw rapid growth of Asian bond market with local currency (LCY) bond outstanding for ASEAN+3[3] in 2011 of USD 18.4 trillion (around USD 15 trillion in sovereign bonds and USD 3 trillion in corporate bonds; Table 3)[4] growing more than three-fold over 15-year period from USD 5 billion in 1996. In terms of regional distribution, Japan's share of the market was 70% of the total value followed by China 18%, Korea 7% and ASEAN-6 (Indonesia, Malaysia, Philippines, Singapore, Thailand and Vietnam) 5%.

China with five currently accredited CRAs that are Association of Credit Rating Agencies in Asia (ACRAA) members, in particular, saw the amount of its government bond outstanding rising over 16-fold and corporate bond rising 300-fold since 2000. As of June 2012, the amount of LCY bonds outstanding was USD 3.5 trillion (USD 2.6 trillion government and USD 0.9 trillion corporate). In 2008, around 13% of corporate bonds were rated by the CRAs. In Japan, two out of three

[3] Excluding Cambodia, Lao PDR, Myanmar and Brunei

[4] USD 5.7 trillion excluding Japan; USD 3.8 trillion in government bonds and USD 1.9 trillion in corporate bonds
Source: AsianBondsOnline

Table 3: Local Currency Bond Outstanding (USD Billions)

Size of LCY Bond Market in USD Billions				
	2000		2011	
Market	**Government**	**Corporate**	**Government**	**Corporate**
Japan	3,499	1,053	11,556	1,152
Korea	122	233	510	719
China	199	3	2,540	852
Hong Kong	14	47	91	78
Indonesia	51	2	93	16
Malaysia	36	33	158	106
Philippines	21	0	67	10
Singapore	25	20	118	71
Thailand	26	5	182	43
Vietnam	0	0	15	2
Total	3,993	1,396	15,331	3,049

Source: AsiaBondsOnline

DCRAs were registered NRSROs and thus have global reach and expertise (Japan Credit Rating Agency, Ltd. – JCR, and Rating and Investment Information, Inc. – R&I[5]). The other agency was Mikuni & Co., Ltd. with extensive reach on Japanese firms and operating under an investor–pay model.[6] Larger DCRAs in one country inside or outside the ASEAN+3 region often provide technical assistance to the more recent DCRAs in other countries. Korea's Seoul Credit Rating & Information, Inc. (SCI), for instance, has a technical cooperation with JCR since 2000. Among the other three established DCRAs in Korea, only National Information and Credit Evaluation, Inc. (NICE) is owned locally and has cooperation with Dagong of China and R&I of Japan. The others, Korea Investor Services, Inc. (KIS) and Korea Ratings Corporations (KR), belong to Moody's and Fitch respectively.[7] Table 4 gives a listing of these Plus Three DCRAs.

[5] *R&I withdrew its NRSRO registration in November 2011 but remained registered with Japan Financial Services Agency since September 2010.*

[6] *Yamori, N., & Nishigaki, N. (2006). Credit Ratings in the Japanese Bond Market. Japanese Fixed Income Markets: Money, Bond and Interest Rate Derivatives, pp. 257-281.*

[7] *An evaluation of relative performance among these Korean DCRAs is provided in Ferri, G., Kang T.S., Lacitignola P.,& Lee, J.Y. (2009). Foreign Ownership and the Credibility of National Rating Agencies: Evidence from Korea. Paper presented at the Conference on Credit Ratings, Credit Rating Agencies, and their Development in Asia, Asian Development Bank Institute, Tokyo, 1-2 July.*

Table 4: Domestic CRAs in Plus Three countries

Country		ACRAA Members	Name	Acronym	Year of est.	Shareholding Structure
China	1	✓	China Chengxin Int. Credit Rating Co., Ltd	CCXI	1992	Joint venture between China Chengxin Credit Management (51%) and Moody's (49%)
	2		China Chengxin Rating Co., Ltd		2012	Fully owned by China Chengxin Credit Management
	3	✓	China Lianhe Credit Rating Co., Ltd.	Lianhe	2000	Joint venture between Lianhe Credit Information Service (51%) and Fitch Ratings (49%)
	4	✓	Dagong Global Credit Rating Co., Ltd.	Dagong	1994	Fully domestically-owned
	5	✓	Shanghai Brilliance Credit Rating & Investors Service Co., Ltd.	SBCR	1992	Fully domestically-owned
	6		Pengyuan Credit Rating Co., Ltd.	Pengyuan	1993	Fully domestically-owned
Japan	1	✓	Japan Credit Rating Agency, Ltd.	JCR	1985	Fully domestically-owned by local financial institutions
	2		Rating and Investment Information, Inc.	R&I	1998 through merger of Nippon Investor Service, NIS and Japan Bonds Research Institute, JBRI (est. 1985)	Fully domestically-owned by local financial institutions (NIKKEI Group as its majority shareholder)
	3		Mikuni & Co., Ltd.	Mikuni	1975	
Korea	1	✓	Korea Investors Service, Inc.	KIS	1985	Moody's (50% + 1 share) KIS Info (50% - 1 share)
	2	✓	Korea Ratings Corporation	KR	1983	Fitch Ratings (73.55%)
	3	✓	National Information & Credit Evaluation, Inc.	NICE	1987	Vanda Pte, Ltd 14.93% KTB Asset Management 14.57% Employee Stock Ownership 9.83% Tokyo Shoko Research 6.88% Woori Bank 6.83% Hana Bank 4.56% National Agricultural Cooperative 2.99% Shinhan Bank 2.78% Others 36.63%
	4	✓	Seoul Credit Rating& Information, Inc.	SCI	1992	SP Partners (19.19%)

Source: Bank of China (Hong Kong) (2011), originally Wind Information, E Fund Management (HK) Co., Limited; Yamori N., Nishigaki N., Asai Y. (2006); Ferri, G., Kang T.S., Lacitignola P.,& Lee, J.Y. (2009); Company websites

Table 5: Domestic CRAs in major ASEAN markets

Country		ACRAA Members	Name	Acronym	Year of est.	Analysts	Types of Rating	Others Services	Number of Rated Entities
Indonesia	1	✓	PT Pemeringkat Efek Indonesia	P.T. Pefindo	1993	Corporate Rating Division (6) Municipal Rating Division (2) Financial Institutions Rating Division (5) Equity and Index Valuation Division (3)	Corporate and debt instrument ratings	Mutual Fund Services, Pefindo25 equity index, equity valuation, industry report, economic updates, credit information relating to debt capital markets	436 solicited ratings (as of October 2012)
	2	✓	PT ICRA Indonesia	ICRA Indonesia	1991	2	Corporates, banks and financial institutions, claim paying abilities and debt instruments including ABS	Research	8 companies (as of October 2012)
	3		PT Moody's Indonesia (formerly PT Kasnic Credit Rating Indonesia)	Moody's Indonesia	1997	12	Banks, insurers, securities companies, mutual funds, Islamic debt, corporate bonds, RMBS, ABS, asset-backed commercial paper, future flow transactions, CDOs, CLOs, CMBS, municipal bonds and medium-term notes.	Research	43
Malaysia	1	✓	Malaysian Rating Corporation Berhad	MARC	1995	Board of Commissioners (6) Rating Committee Members (8) Syariah Advisory Panel (4) Rating Team (4)	Corporate debt, issuer, structured finance, Islamic capital market instruments, financial institution, corporate credit, insurer financial strength, Islamic financial institution governance, sovereign issuer credit	Research and training	683 ratings (cumulative, as of December 2012): 400 corporate debt; 60 project finance; 168 structured finance; 1 sovereign debt; 2 sovereign credit strength; 23 financial institution ratings; 6 issuer ratings; 15 corporate credit ratings; and 8 insurer financial strength ratings
	2	✓	RAM Rating Services Berhad	RAM	1990	49 (as of 2011)	Local and foreign corporates, financial institutions and insurers, government-linked and other public-financed entities, project finance, sukuk, structured finance, including ringgit-denominated foreign issues	Consultancy, training, research, credit information	860 (1,919 cumulative ratings, as of January 2013)

Country		ACRAA Members	Name	Acronym	Year of est.	Analysts	Types of Rating	Others Services	Number of Rated Entities
Philippines	1	✓	Philippine Rating Services Corporation	PhilRatings	1985	8	Corporate, Banks, Financial Institutions, Government Institutions, Local Government Units, Insurance Companies	Research	39 (as of October 2012)
	2		Credit Rating and Investor Services Philippines, Inc.	CRISP	2008	5	Bond issuers and debt instruments in real estates, food and beverage, and energy sectors, Local governement financing	Investment Risk Assessment Training Industry Research	4
Thailand	1	✓	TRIS Rating Co., Ltd	TRIS Rating	Found in July 1993, Splited into TRIS Rating in June 2002	Research&Development 4 Staffs CRA 15 Analysts 4 Head 4 Support Staffs	TRIS Rating: 1. Credit Rating Services (Company rating, Issue rating, Short-term securities, Structured finance, Hybrid securities, Local government, Government-related entities) 2. Information Services	TRIS: 1. Performance Evaluation Consulting 2. Enterprise Risk Management Consulting 3. Performance Improvement Consulting 4. Good Corporate Governance and Corporate Social Responsibility Consulting 5. Internal Audit and Quality Assessment Report (QAR) Consulting 6. Survey and Business Research Service	102 (as of November 2012): 1 structured finance, 30 financial institutions, 66 corporates, 5 government related entities

Source: Company websites and reports

Within ASEAN, where LCY bond market saw a four-fold increase in both corporate and government segments since 2000, there are still relatively few DCRAs present. Major markets are Malaysia, Thailand and Singapore with two, one and no DCRAs respectively. Vietnam which has a corporate bond market also largely relies on global CRAs. Vietnamnet Credit Rating Centre (VCRC) was established in June 2005 but discontinued its operation in after less than one year due to small credit rating market and lack of accurate information from banks and government agencies. Table 5 provides information on ASEAN CRAs' businesses. Like some of the Plus Three DCRAs, many of these ASEAN DCRAs maintain relationship with the GCRAs either through shareholding or technical service agreements. RAM Rating Services Berhad (RAM) has interestingly embarked on a transition towards becoming a GCRA in its own right by recently providing ratings based on its Global and ASEAN rating scales.[8] The following subsections review DCRAs in ASEAN market in more details and attempt to assess their characteristics in order to ascertain their ability to serve growing local markets relative to the GCRAs. In particular, possible advantages of regional harmonization and the establishment of a Regional Credit Rating Agency (RCRA) are examined. These subsections are divided according to the characteristics identified in the Asian Bankers Association study since 2000 (ABA, 2000) as being critical for the credibility of DCRAs in gaining investors acceptance within any framework towards harmonization of credit rating practices.[9] The study together with subsequent studies by the ADB[10] led to the publication of ADB Handbook on International Best Practices in Credit Rating (ADB, 2008) for which the current ACRAA Code of Conduct (ACRAA, 2011) is based on.

ACRAA was established in 2001 with the help of the ADB to represents 15 DCRAs in Asia and began its operation on 1 January 2002. Current membership has increased to 30 and spread across 13 Asian countries.[11] Its objectives focus on promotion of 1) exchanges of ideas, experiences, information, knowledge and skills to enhance DCRAs capabilities and provision of reliable market information; 2) adoption of best practices and common standards to ensure high quality and

[8] *RAM (2013b). RAM takes major step to become global rating agency. RAM Press Release, 21 January 2013. And RAM (2013a). Credit FAQs: Global and ASEAN Ratings Explained. RAM Criteria & Methodology, January 2013.*

[9] *Namely, Independence, Transparency, Accuracy and consistency of ratings, Quality of analysis, and Timeliness and effectiveness of rating actions. These characteristics are referred to in the IOSCO Code of Conduct Fundamentals for Credit Rating Agencies (IOSCO, 2008).*

[10] *Including a follow up study in 2004, ADB. (2004). Development of Regional Standards for Asian Credit Rating Agencies: Progress & Changes. Asian Development Bank.*

[11] *The 13 ACRAA member countries are Bangladesh; India; Indonesia; Japan; Kazakhstan; Korea; Malaysia; Pakistan; People's Republic of China; Philippines; Sri Lanka; Taipei, China; and Thailand.*

comparability of credit ratings; 3) the development of Asia's bond markets and cross-border investment throughout the region. Thus ACRAA objectives are consistent with the credibility enhancing characteristics of DCRAs that will be discussed in the subsequent subsections. The correspondence between ACRAA Code of Conduct and these characteristics is given in Annex 1. In addition, to the extent that some elements of the Code of Conduct (which are based on the articles of IOSCO code) are consistent with laws and regulations by each country's regulatory authorities, the implementing guidelines become a binding commitment from member DCRAs in the respective country. In Japan, for example, a recent IMF's assessment (IMF, 2012) found that all CRAs whose ratings are used for regulatory purposes are registered with Japan Financial Services Agency (FSA) and subject to periodic reporting and inspections in line with IOSCO's principle.[12]

ACRAA's objectives are pursued through joint training workshops, best practices dialogues, as well as conferences with regulatory authorities and participation in various activities. As an action program for ACRAA, *'Rating Harmonization'* is the effort to make the credit ratings of all member DCRAs comparable as a basis for investment decisions. ACRAA has three committees under the *'Capacity Building Initiative'* , namely, Training Committee, Best Practice Committee, and Regulatory Relationship Committee that work under two main objectives: for joint training workshops and for best practices dialogues. Research studies commissioned by the committees point to the necessity of having high standards of corporate governance, accounting policies and practices, transparency in disclosures and adequacy of regulatory oversight (Choudhury, 2004) that subsequently feature in ACRAA Code of Conduct for DCRAs. The harmonization challenge is for the DCRAs in different stages of development, rating methodologies[13], national market conditions, accounting standards and regulatory frameworks to work together for market integration and regional development interest as a whole.

[12] *CRA recognition criteria include six elements: Objectivity, Independence, International Access/Transparency, Disclosure, Resources and Credibility. Japan FSA, for example, has taken administrative action against Standard and Poor's as a result of violations related to its credit rating announcement, monitoring and information disclosure, by requiring the company to submit periodic reports on preventive measures (FSA, 2012).*
[13] *Some of which are derived from those of different GCRAs, principally, Moody's, Standard and Poor's, and Fitch.*

3.1 ASEAN DCRAs

This section provides background profiles of the major ASEAN DCRAs listed in Table 5. Further details concerning their credibility enhancing characteristics in relation to those of the Plus Three DCRAs are also discussed in the subsequent sections.

Indonesia

3.1.1 PT. PEFINDO (PT Pemeringkat Efek Indonesia)

Incorporated on December the 21st, 1993, PT Pemeringkat Efek Indonesia, or PT. PEFINDO in short, was the first credit rating agency in Indonesia that was established through the initiative of BAPEPAM (Indonesia's Capital Market Supervisory Board) and Bank Indonesia (the Central Bank) under the requirement that all commercial papers held or traded by banks need to have credit ratings. PEFINDO was structured as a private limited liability company owned by institutional shareholders. At the date of establishment, joint owners were 99 financial institutions with major shareholders (above 5%) as follow:

Figure 2 : PEFINDO's initial shareholding structure

SHAREHOLDERS	% of ownership
Dana Pensiun Bank Indonesia	25.56%
Bursa Efek Jakarta	18.00%
Dana Pensiun Pertamina	10.34%
Taspen	6.00%
Danareksa Sekuritas	5.10%

Source: PT. PEFINDO Credit Rating Indonesia Ltd.

As of 2011, PEFINDO shareholders comprised of domestic financial institutions, major pension funds, banks, insurers, Indonesia Stock Exchange (IDX) and securities companies, and two state-owned banks (see Table 6). Despite its purely domestic outlook in terms of the company's shareholding structure, PEFINDO has, from its early days, received technical support from the Standard & Poor's Corporation (S&P). For instance, PEFINDO rating process was adopted from S&P established methodologies. PEFINDO's directors and analysts also attended periodical trainings, workshops and courses organized by S&P. Apart from having S&P as its affiliate, PEFINDO is also a member of ACRAA and actively involves with ACRAA activities.

Table 6: ASEAN DCRAs Shareholding Structure

Country		ACRAA Members	Name	Acronym	Year of est.	Shareholding Structure		
						Public	Private	GCRAs
Indonesia	1	✓	PT Pemeringkat Efek Indonesia	P.T. Pefindo	1993	3.5% State-Owned Banks (2)	96.5% Other domestic institutions: 20% Indonesia Stock Exchange 46.7% Pension Fund (26) 23.1% Securities Companies (56) 6.7% Insurance Companies (7) (as of December 2011)	
	2	✓	PT ICRA Indonesia	ICRA Indonesia	1991			99% owned by ICRA Limited (a subsidiary of Moody's
	3		PT Moody's Indonesia (formerly PT Kasnic Credit Rating Indonesia)	Moody's Indonesia	1997			Moody's Investor Service Inc.
Malaysia	1	✓	Malaysian Rating Corporation Berhad	MARC	1995		Domestically registered major life and general insurance companies, stockbrokers and investment banks (29)	
	2	✓	RAM Rating Services Berhad	RAM	1990		90.2% Domestically registered major banks and financial institutions (28)	4.9% Fitch Ratings Limited 4.9% Standard and Poor's (McGraw-Hill Asian Holdings (Singapore)
Philippines	1	✓	Philippine Rating Services Corporation	PhilRatings	1985		70% Motan Corporation 30% CIBI Foundation	
	2		Credit Rating and Investor Services Philippines, Inc.	CRISP	2008			
Thailand	1	✓	TRIS Rating Co., Ltd	TRIS Rating	Found in July 1993, Splited into TRIS Rating in June 2002	(TRIS Corp.) 13.52% Government Savings Bank 5% Ministry of Finance	76.48% Domestic Financial Institutions: 45.33% Commercial Banks 13.34% Stock Exchange of Thailand 7.81% Finance/Securities Companies 5% Mutual Fund Management Cos 5% Insurance Companies	5% Standard and Poor's (McGraw-Hill Asian Holdings (Singapore) Pte. Ltd.)

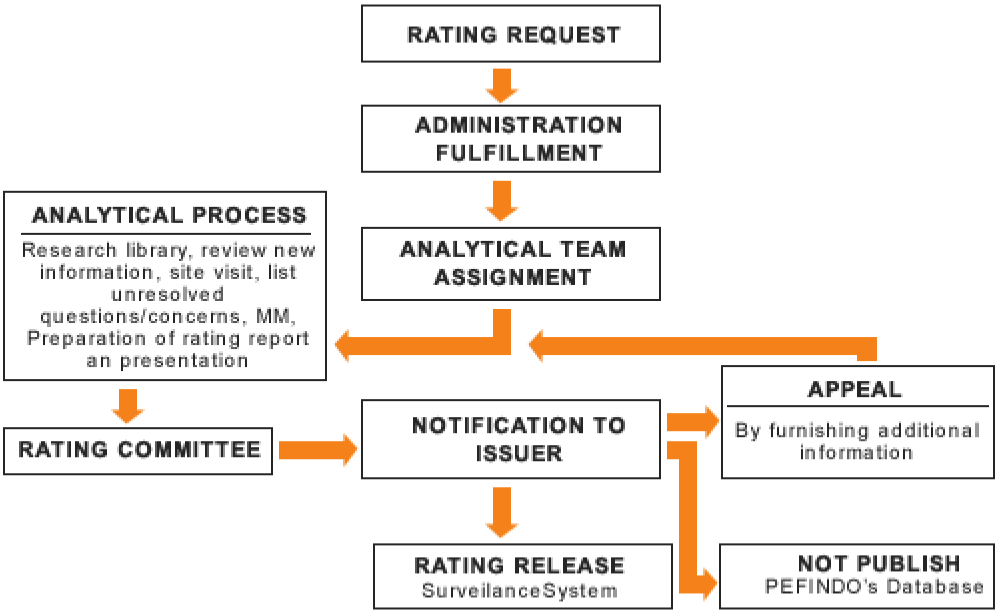
Source: Company websites and reports

Apart from rating services, the company's related businesses include mutual fund services, PEFINDO25 index of small and medium enterprise stocks, corporate governance scoring, industry report and economic updates. Rating is its main focus, for which its rating products could be divided into 2 types: company rating and debt instrument rating. Company rating, also called 'General Obligation' (GO) rating or an issuer rating, reflects the overall credit worthiness of a company, which do not take into account the nature and provisions of the debt security, its standing in bankruptcy proceedings or liquidation, statutory preferences, the creditworthiness of the guarantors, insurers, or other forms of credit enhancement supporting the company. On the other hand, Debt Instrument rating reflects the creditworthiness of an obligor to timely meet its financial commitments. These could be a specific debt bond rating for long-term debt period (more than 5 years), medium term note (MTN) for 1-3 year period, or Commercial Paper (CP) and Promissory Notes (PN) for short-term period (below 1 year).

Since its inception until October 2012, the company has provided solicited ratings for 436 rated entities. For corporate sector, for instance, PEFINDO covers three major risk assessments: industry risks (i.e. cost structure, barriers and competition of the market), business risks (varied depending on Key Factors of Success of the market), and financial risks (i.e. financial policy, capital structure, cash flow protection, financial flexibility). Each risk type is assessed similarly based on the analyses of five key risk factors: 1) the industry's growth and stability 2) revenue and cost structures 3) barrier to entry and competition within the industry 4) regulation and de-regulation, and 5) financial profile of the industry. Nevertheless, there exists a slight distinction between the sets of key analytical factors used for the assessment of corporate business profile which could vary from one firm to another, depending on the so-called Key Success Factors (KSF) of certain industries. In some cases, a rating decision is influenced mostly by financial measures, while in other cases, a company's rating is more influenced by the firm's business profiles and fundamentals. There were no explicit explanations for the proportions of quantitative factors against those of qualitative factors that were integrated into the company's rating methodology, although PEFINDO maintains its commitment that its rating decisions would always reflect the balance of different factors, strengths and weaknesses included.

PEFINDO's typical rating cycle, which lasts for approximately within 30 working days, is illustrated in the diagram below. The process, under an issuer pay model, begins as a response to a formal request from the issuing company. Information request from the company includes 3-5 years of the company's audited financial statements, several detailed questions and operational data as listed in PEFINDO's standard questionnaire depending on the sector, and some other documents such as prospectus, information memo, etc. Following the widely accepted norm, the rated entities possess the right to approve whether the result will be published.

Figure 3 : PEFINDO's initial shareholding structure



Source: PEFINDO website

Assigning ratings specifically within the Indonesian context, PEFINDO ratings are characterized by the utilization of the 'id' prefix as the abbreviation of 'Indonesia'. PEFINDO's rating scale also resembles those of its S&P affiliates, with only one difference on the scale of selective default, idSD rating that ranges between idCCC and idD. This idSD grade would be assigned to a company that has failed to pay one or more of its due financial obligations. Despite the payment failure, this SD rating is to be assigned when PEFINDO believes that the obligor has merely selectively defaulted on some particular issue or class of obligations, yet, would continue to pay on time for its other obligations.

3.1.2 PT ICRA Indonesia (ICRAIndo)

Compared to PEFINDO, ICRA Indonesia is a much younger domestic credit rating agency in Indonesia. Almost two decades after Pefindo incorporation, ICRA Limited, an Indian CRA, with its shares listed on the Bombay Stock Exchange and the National Stock Exchange, decided to have its subsidiaries in the country. Subsequently ICRA Indonesia obtained its operating license from Bapepam-LK - the Capital Market and Financial Institution Supervisory Board on September 14, 2010. As a subsidiary, it is 99 percent owned by ICRA Ltd, with its mother company, in turn, an associate of Moody's investor service. ICRA Ltd. also has Moody's Investor Service as its largest shareholder.

Due to its affiliation, ICRAIndo receives technical know-how from Moody's. This could perhaps most visibly be reflected in its adoption and modification of ICRA Limited's (ICRA Ltd.) Code of Conduct, which is in turn supported by a Technical Services Agreement entailing Moody's provision of high-value technical services, research capabilities as well as access to Moody's global research base to ICRA Ltd. Nevertheless, it is explicitly stated by ICRAIndo that the Code of Conduct has been adjusted to comply with the applicable regulations in Indonesia.

Characterized as a typical DCRA, ICRAIndo's ratings are designed to address the relative credit risks within Indonesia, and not adapted to any rating comparison among instruments across countries. Compared with other DCRAs, ICRAIndo operates in a much smaller manner with merely three members in its Board of Directors and two analysts. Principally through the accumulated experiences of its parent ICRA Ltd., ICRAIndo offers its Indonesian market with services including credit rating, grading and investment information. For its rating services, ICRAIndo offers credit ratings to a wide range of issuers including manufacturing companies, banks and financial institutions, infrastructure sector companies, service companies, municipal bodies, non-banking finance companies, small and medium sector entities, asset backed securities. Nonetheless, given its new position in the Indonesian market, it has only rated 8 companies thus far.

ICRAIndo operates on an issuer-pay model and therefore its rating process starts when an issuer submits the signed agreement. Apart from the information the issuer handed in as rating requirements, ICRAIndo also relies on secondary sources of information provided by its own Research Division. Upon its completion of assessment which normally takes up to 30 working days, the 'Rating Report' is presented to the Rating Committee which is the final authority for ratings assignment before passing on to the top management for acceptance. The report is used only if the issuer finds the rating acceptable.

3.1.3 PT Moody's Indonesia (formerly PT Kasnic Credit Rating Indonesia)

Founded in May 1997, the Jakarta-based PT Moody's Indonesia was formerly recognized as Kasnic Credit Rating Indonesia. Prior to Moody's affiliation accounting for 99% stake, Kasnic Credit Rating Indonesia was previously owned by PT. Kasnic Indotama (70%) and Fitch (30%). Operating as a credit rating agency, its activities involve the provision of ratings and credit opinions on issuers and debt instruments, such as banks, insurers, securities companies, mutual funds, Islamic debt, corporate bonds, residential mortgage-backed securities, asset-backed securities, asset-backed commercial paper, future flow transactions, collateralized debt obligations, collateralized loan obligations, and commercial mortgage-backed securities, as well as municipal bonds and medium-term notes.[14] PT Moody's Indonesia rating methodology is primarily concentrated on financial and operational risks. Unlike other two Indonesian domestic credit rating agencies, PT Moody's Indonesia is not a member of ACRAA.

Malaysia

3.1.4 RAM Rating Services Berhad

RAM Rating Services Berhad was established in November 1990 as the Nation's first credit rating agency of its kind by Bank Negara Malaysia with assistance from CRISIL through trainings of analysts during its inception. RAM is well recognized as world's leading sukuk rating public limited company. RAM is an ACRAA member and owned by domestic financial institutions (90.2%), Fitch ratings (4.9%) and Standard and Poor's (4.9%). As of 2011, RAM operates with the expertise of 49 experienced analysts in total.

As of the end of January 2013, after the introduction of its Global and ASEAN scale ratings, RAM has rated more than 860 companies, accounting for 1,919 bonds and sukuk issues worth close to $261 billion since 1991.[15] It has rated ringgit and sukuk bonds issued by over 20 foreign companies, most of which are from South Korea, Japan, Singapore, Hong Kong, Indonesia, Kazakhstan and Gulf Cooperation Council countries (GCC). Outside the Malaysian territory, RAM

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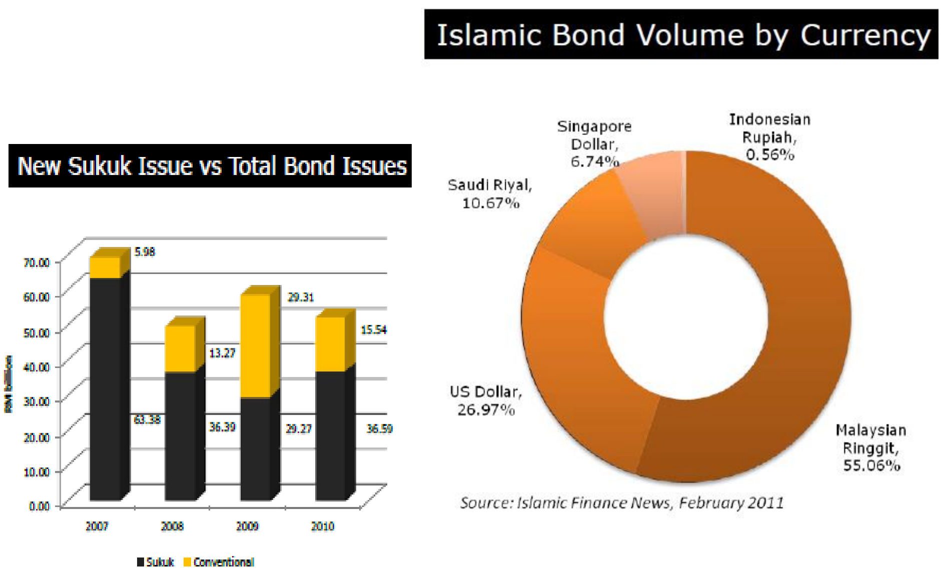
[14] *http://investing.businessweek.com/research/stocks/private/snapshot.asp?privcapId=31208587*

[15] *RAM (2013b). RAM takes major step to become global rating agency. RAM Press Release, 21 January 2013.*

Ratings (Lanka) Limited, another subsidiary of RAM Holdings that was formed in 2005, operates in Sri Lanka and is also an ACRAA member.

Also following the issuer-pay model, RAM provided both solicited and unsolicited ratings. Each rating requires around 4 to 6 weeks from the day of receipt of mandate and/or information until a decision is made by the Rating Committee. Any initial ratings would take up longer time than annual surveillance. Domestically, RAM's clients range from public listed companies, small and mid-sized organizations, financial institutions, large-scale enterprises and conglomerates to government-linked corporations and multinationals. However, on 21 January 2013, RAM Ratings has turned global by debuting its Global and ASEAN rating scales attracting more foreign issuers and investors that aim to compare and measure companies for their relative credit worthiness.[16] The new rating scales are intended to provide an option for domestic companies that wish to expand regionally and globally and give a benchmark and an indication how companies fare in terms of credit standing against their ASEAN or global counterparts. RAM stated that its decision is largely in response to the demand of the ASEAN-region investors and issuers for diversity in opinions. The move was also aimed to promote the Islamic bond market known as sukuk market in Malaysia as well as globally. Apart from its rating activities, RAM also offers other services including consultancy, trainings, research and credit information.

Figure 4 : Islamic Sukuk Market



Source: RAM Rating Services Berhad

[16] *Ibid.*

3.1.5 Malaysian Rating Corporation Berhad (MARC)

Kuala Lumpur-based Malaysian Rating Corporation Berhad (MARC) was incorporated as a public limited liability company in October 1995 prior to its official launch on September 5th 1996. MARC's shareholders comprise of major life and general insurance companies (46.5%), stockbrokers (26%), discount house (2%) and investment banks (25.5%) operating in Malaysia. The company is recognized by Bank Negara Malaysia and Securities Commission as an External Credit Assessment Institution (ECAI) under Basel II and as a bond rating agency regulated under the Guidelines on the Registration of Credit Rating Agencies issued by the Securities Commission on 30 March 2011. In addition to the core credit rating business, it also offers economic and fixed income research reports and training.

As of January 2013, it has rated 860 companies on corporate debts, project finance and structured finance including Islamic capital market instruments, asset-backed securities, as well as financial strength ratings of financial institutions and insurance companies. MARC provides both solicited and unsolicited ratings, the latter of which are public information ratings on a no-fee basis to support ratings on obligations relying on support mechanisms such as bank guarantees, parent company guarantees and state government guarantees. Its corporate rating methodology comprises of business risk analysis, financial risk analysis, consideration of management and other qualitative factors and issue structure and terms, in which detailed information on indicators, ratios, and the analytical focus are identified for each analysis type and for a particular industry category under consideration. MARC requires approximately 7-8 weeks in delivering ratings, and depending on the circumstances, the assigned ratings might be placed on MARCWatch subject to upgrading, affirmation or downgrading. Apart from MARC's established Code of Conduct, the company adheres to many others policies such as whistleblowing, personal investment and trading of securities and analytic firewall policies that, it believes, are for the company, customers as well as investors' best interests.

Thailand

3.1.6 TRIS Rating

Under the promotion of Thailand's Ministry of Finance and the Bank of Thailand, the Industrial Finance Corporation of Thailand acted as the key institution in establishing 'Thai Rating and Information Services Co., Ltd' or 'TRIS' in July 1993 with the purposes to evaluate creditworthiness of debt securities and to assist investors in decision-making. TRIS was then approved as Thailand's first credit rating agency by the Office of the Securities and Exchange Commission (SEC) and started the credit rating business on July 27, 1993.

In June 2002, TRIS Rating Co., Ltd or 'TRIS Rating' was separated from its parent company, 'TRIS', and operated as an independent firm to supervise the credit rating business in comparison to TRIS that oversees the consulting services business. TRIS Rating is wholly owned by TRIS (99.99 percent). A shareholding

Table 7: Domestic Shareholding Structure of 'TRIS', parent company of TRIS Rating [17]

Government Sector:	
Government Savings Bank	13.52%
Ministry of Finance	5.00%
Private Sector:	
Commercial banks**	45.33%
Stock Exchange of Thailand	13.34%
Finance and Securities companies	7.81%
Mutual fund management companies	5.00%
Insurance companies	5.00%
International Agency:	
McGraw-Hill Asian Holdings(Singapore)Pte.Ltd	5.00%

Source: TRIS Rating

structure of TRIS as of March 2012, comprises of 18.52 percent ownership from public sector, 75.48 percent ownership from private sector (commercial banks -- the largest shareholder accounts for 45.33 percent), and 5 percent ownership from the international agency. Standard & Poor's group (S&P) acquired 5 percent stake in TRIS in November 2011. TRIS Rating received technical assistance in credit rating methodology from S&P along with various trainings from ACRAA where TRIS Rating was a co-founding member.

TRIS Rating offers two main services. Its primary business is credit rating services while the other is information services. It only rates local-currency denominated debt instruments but under a variety of types including basic corporate debt instruments (secured and unsecured debentures), structured finance issues (project finance and guarantee debentures), and securitizations.

[17] *Within 45.33 percent of the commercial banks, TMB Bank PLC accounts for 15.30 percent of TRIS Corporation Ltd. (TRIS). TMB Bank PLC is 26 percent owned by Thailand's Ministry of Finance.*

The rating methodology is largely subjective with no exact weighting scales between quantitative and qualitative factors. Nevertheless, TRIS Rating compares company's profile to TRIS Rating's Rating Analysis Methodology Profile (RAMPs) of other companies that have already received ratings. It takes approximately six to eight weeks for the completion of the rating process given that there is sufficient information available.

TRIS Rating uses issuer-pay model as a credit rating model where it provides only solicited rating since the accumulation of essential and sufficient information is the major component in achieving accurate ratings. Rating fees are categorized by types of rating. Fees on company ratings are based on the asset size of the latest reviewed or audited consolidated financial statements while fees on issue ratings are derived from basis points of bond issuance.

Ratings assigned by TRIS Rating cannot be compared with those assigned by international credit rating agencies as TRIS Rating rates local currency bonds under the national scale rating system which does not address either direct sovereign risks of the government or foreign exchange rate risks. In addition, Thai sovereign rating is assigned AAA, the highest rating by TRIS Rating whereas it is rated BBB+ by S&P and BBB by Fitch Ratings.[18] Differences in sovereign rating yield different ceilings of rated issues.

In Thailand, there are two credit rating agencies which are accredited by the SEC, i.e., TRIS Rating and Fitch Ratings (Thailand). However, only TRIS Rating is recognized as a local credit rating agency since Fitch Ratings (Thailand) is an affiliation of Fitch Ratings. Nevertheless, there exists a certain extent of market segmentation among the two credit rating agencies. According to an interview with TRIS Rating, TRIS Rating mainly provides ratings to Thai corporations while Fitch (Thailand) primarily issues ratings to Thai banks.

The Philippines

3.1.7 PhilRating

The 'Philippine Rating Services Corporation' or 'PhilRatings' is the pioneer domestic credit rating agency found in 1985. It is entirely-owned by private sector, i.e., 70 percent owned by Motan Corporation and 30 percent owned by CIBI Foundation. It covers issuer ratings, short-term ratings, and long-term ratings. PhilRatings uses issuer-pay model and conducts solicited rating as well as private

[18] *Source: Thailand Sovereign Rating by Major Rating CRAs; the Public Debt Management Office Thailand. Accessed on November 23, 2012.*

rating for exclusive use by specific parties and entities such as local government units and insurance companies.

The rating methodology encompasses a wide range of quantitative and qualitative factors, however, there exists no exact formulae or specific standard sets of ratios. The rating process carries around four to six weeks after the submission of completed information. Nevertheless, the actual time-frame depends on size and complexity of the issuer or issue. The formal-basis monitoring process requires quarterly updated information. Moreover, it is mandatory to meet with company's management at least once a year as long as there is an outstanding credit rating.

The rating fee is paid upfront and depends on the amount of time and effort needed to complete a credit rating. Issuer ratings fees depend on asset size whereas those of issue ratings rely on the amount to be issued. PhilRatings is regulated by the Philippines Securities and Exchange Commission. It is also a founding member of ACRAA.

3.1.8 CRISP

Credit Rating and Investors Services Philippines Inc. or CRISP was established in 2008. It is not a member of ACRAA. It rates bond issuers and debt instruments covering real estate, food and beverage, as well as energy industries. Types of issues and rated institution are short-term issues, long-term issues, issuer, structured finance, real estate investment trust (REIT), and local government financing. CRISP rating committee and analysts are associated with Asian Institute of Management. Some are former employees of S&P and Moody's. CRISP is also an accredited rating agency regulated by the Philippines Securities and Exchange Commission.

From the above description of DCRAs in major ASEAN markets, there are thus relatively few established DCRAs present in the region. There are also relatively few newcomers in the rating business since the established DCRAs, most of which were formed during the 1980s and 1990s, have gained expertise and position in their respective domestic market. Most of established DCRAs are now members of ACRAA. The next few sections consider CRA characteristics that are essential for gaining further investors' acceptance. Many aspects of these characteristics have been incorporated into the ACRAA Code of Conduct to a certain extent.

3.2 Independence

Independence features in many parts of ACRAA Code of Conduct, notably independence of rating assignment from all sources of compensation and related businesses throughout the rating process and for all its analysts and employees involved (Annex 1). According to the Code of Conduct, the definition of potential conflict of interest can be specific to each DCRA, and it is recommended that DCRAs' Codes of Conduct also apply to their Boards of Directors. In addition, the general code adopted from IOSCO also refers to independence of rating action from potential political or economic effects or otherwise.

Almost all ASEAN DCRAs listed here provide information on the members of their rating committees and boards of directors. Thus market participants can make a certain level of assessment on any potential conflict of interest. DCRA's Code of Conduct can provide some assurance on independence of its analysts. In addition to relevant regulations on credit ratings in Plus Three countries[19], Plus Three DCRAs provide their own Codes of Conduct which contain policies regarding independence and avoidance of conflicts of interest in accordance with their national regulations and IOSCO principles. Most of them are also ACRAA members and thus their Codes are similar and adhere to ACRAA Code of Conduct. China Dagong, for example, is generally devoted to provide independent, objective, fair, transparent, on-time and forward-looking credit information, and has Codes concerning avoidance of conflicts of interest by its employees, rating charges and separation of different businesses (firewall policies), in particular.

More importantly however, DCRAs have to demonstrate their independence from political or business influence since information on such issue as majority shareholding can lead to presumption, correctly or not, about the credibility of their rating actions. Thailand and the Philippines, for example, are affiliated with domestic government, public institutions and/or regulator[20] (Table 6) due to their formation at an early stage of development. Other DCRAs

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[19] *The regulatory agencies in charge of supervising CRAs in Plus Three countries are People's Bank of China (PBOC for issuing regulation), China Securities and Regulatory Commission (CRSC for bond exchange supervision) and National Development and Reform Commission (NDRC for enterprise bonds) in China; Financial Services Commission (FSC), Financial Supervisory Service (FSS) and Korea Financial Investment Association (KOFIA) in Korea; Japan Financial Services Agency (FSA) and Securities Exchange and Surveillance Commission (SESC) under the new IOSCO consistent CRA registration control and inspection system in accordance with the revised Financial Instruments and Exchange Act (FIEA) and Cabinet Office Ordinance in Japan. ADB (2012). ASEAN+3 Bond Market Guide.*

[20] *18.52 percent of TRIS Corp., the parent company of TRIS Rating, is owned by the public sector (13.5 percent Government Savings Bank and 5 percent Ministry of Finance), and 30 percent of PhilRatings belongs to CIBI Foundation, Inc., a private not-for-profit credit information corporation established by the Central Bank of the Philippines, the Securities and Exchange Commission of the Philippines, and the Financial Executives Institute of the Philippines (FINEX).*

Table 8: ASEAN DCRAs Corporate Rating Methodology

Country		ACRAA Members	Acronym	Year of est.	Affiliation	Tech Assit	Rating Duration	Methodology (Corporate)	Data Sources
Indonesia	1	✓	P.T. Pefindo	1993	S&P	S&P	30 days	Risk assessment based on industry risk, business risk and financial risk (corporate sector) including comparative analysis against similar competitors in the same industry and inter-industry analysis	Audited Financial Statements, Financial Projection, Prospectus, Information Memorandum, Annual Reports, business activities and other important information on the companies, Holding companies, Affiliates and Subsidiaris and company's Group in general
	2	✓	ICRA Indonesia	1991	Moody's	Moody's	30 days	Cash flow, business and financial risk analyses including assessment of promoters/management quality and competitive position	Direct business information, company visit, management's plans, outlook, competitive postions, funding policies and research from secondary sources
	3		P.T. Moody's Indonesia	1997	subsidiary of Moody's Indonesia (BVI) Ltd.	subsidiary of Moody's Indonesia (BVI) Ltd.	n/a	Moody's methodology with an emphasis on operational and financial risks	Moody's
Malaysia	1	✓	MARC	1995	none	none	6 weeks	Business and financial risk analyses, management and other qualitative factors, issue structure and terms	Preliminary research, company information, management meetings
	2	✓	RAM	1990	S&P Fitch	CRISIL	4-6 weeks	Industry, business, financial risk analyses and analysis of management quality	Business information on industry, operation and supporting statistics, financial information, principal terms and conditions of the issue, and management meetings on performance, prospects and plans
Philippines	1	✓	PhilRatings	1985			4-6 weeks	Business and financial risk analyses	Business and economic information including management and strategy, financial information and asset quality
	2		CRISP	2008	none	none		Industry, business, financial risk analyses and analysis of management quality	Audited financial statements, feasibility studies, historical and projected market share, management meetings, field visit
Thailand	1	✓	TRIS Rating	1993	S&P	S&P	6-8 weeks	Industry, business, financial risk analyses	Financial statements, site visits, management/audit committee meetings on track-record, teamwork, past successes and failures, vision, creditability and transparency

Source: Company websites and reports

have a largely diversified shareholder base but still concentrated mostly on domestically registered financial institutions which not only can be potential investors in the domestic market but also the issuers of rated securities themselves. Though the proportion of the shareholding held by a particular public or private institution is relatively small, it is still difficult for investors to evaluate the credibility of CRAs' ratings with respect to political independence and independence of ownership, particularly when looking from a regional perspective. In addition, since most DCRAs operate under the issuer-pay model, there is an incentive for DCRAs to give into issuer's rate shopping by awarding higher rating than otherwise in order to gain rating business in some countries where there are intense competition, including from the GCRAs or their affiliates.

Given national differences in rating standards and practices, rating harmonization across the region is thus important for investors' confidence in ratings assessed by the DCRAs. Another possible solution to ensure independence at the regional level is the provision of alternative benchmark ratings, possibly on a regional rating scale[21], by an independent body such as a Regional Credit Rating Agency (RCRA) whose rating standards are recognised regionally and internationally.

3.3 Transparency and Rating methodology

ACRAA Code of Conduct also contains several elements related to DCRAs transparency that reflect their rating process, rating methodology, rating information and potential conflicts of interest (Annex 1). The Code of Conduct requires transparency of the rating process whereby rating policies, procedures, methodologies and criteria are well-defined and published, Rating Committee's discussion is documented and its decisions are subjected to a clearly described review or appeal process. All rating actions and assignments (along with information about DCRA's historical performance data) are disclosed, unsolicited ratings are distinguished, conflicts of interest are defined and published, and rating and non-rating fees are disclosed. DCRA's own Code of Conduct itself, including Code of Ethical Conduct applicable to its employees and board members, should be available publicly along with any changes and description on how these will be implemented and enforced.

Most ASEAN DCRAs listed in Table 5 publish rating process, timeframe and rating methodologies across issue types with varying details. Descriptions of

[21] *So that sovereign and political risks, among other country-specific factors, have been taken into account.*

corporate rating methodologies are broadly similar among DCRAs and involve industry, business and financial risk analyses, and analysis of management quality (Table 8). The data source used by DCRAs include information from meetings with company's managements and/or site visit on competitiveness position, future plans and outlooks, in addition to the examination of audited or non-audited financial statements and information from secondary sources. DCRAs thus have greater access to assess issuer's characteristics and utilize local knowledge and connections. Thailand TRIS Rating, for example, describes its solicited issuer-pay rating process which includes information gathering, analysis, rating committee meeting, rating announcement and monitoring on its official website with specified timeframe. The rating methodologies are classified into different types of rating issues and institutions[22] together with details of each quantitative or qualitative factor under consideration but without exact weighting scale between these factors or exact benchmarks for the quantitative factors.

Despite their similarity in the types of analysis being conducted, the actual rating methodologies used by DCRAs are different and not explicitly stated in all cases. For many DCRAs these are influenced by the ownership of or affiliation with GCRAs with different rating definitions and methodologies (Table 9).

Table 9: DCRAs Affiliation with GCRAs

	S&P	Moody's	Fitch
Ownership	Taiwan: TRC	Korea: KIS Indonesia: ICRA	Korea: KR
Affiliation	Malaysia: RAM (4.9%) Thailand: TRIS (4.9%) Indonesia: Pefindo	China: CCXI (49%) Indonesia: ICRA	China: Lianhe (49%) Malaysia: RAM
Technical Assistance	China: Shanghai Brilliance Indonesia: Pefindo Malaysia: RAM Thailand: TRIS	China: Dagong Global Indonesia: ICRA	Malaysia: RAM
Methodology Similarity	Thailand: TRIS	China: CCXI, Dagong Korea: KIS Indonesia: ICRA	China: Lianhe Korea: KR Malaysia: RAM

Source: Company websites and reports

In order to increase their regional presence, GCRAs have deepened their involvement in the region and transferred technical expertise that in turn improves DCRAs' capacity. Plus three DCRAs also have technical cooperation

[22] *Short term rating, corporate, local government, government related entity, bank, securitization, hybrid securities*

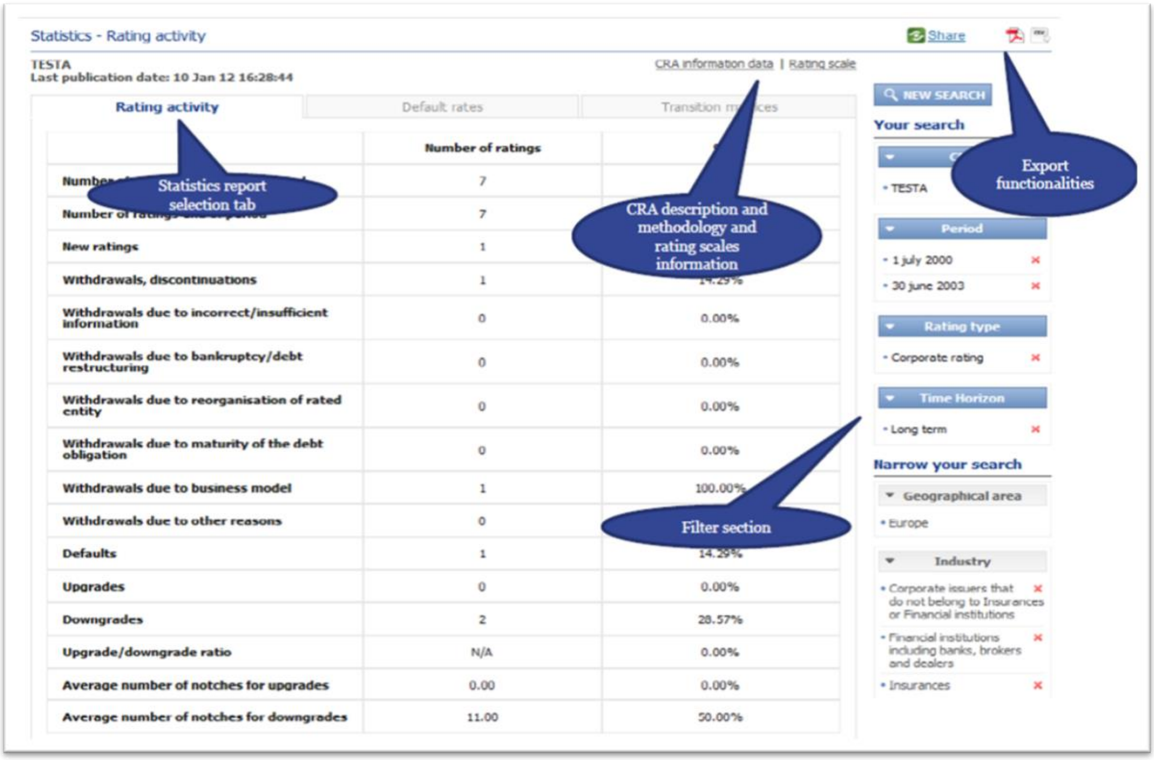
among each other. In Korea, for example, NICE has Japan R&I and China Dagong Rating as partners in credit assessment. Korea SCI is also partnered with Japan JCR (Mitsui, 2009). ASEAN DCRAs are still in the process of gaining their expertise and expanding their rating capabilities in order increase their appeal to wider investor base however. A recent survey of issuers and investors in Malaysia indicated that professional bodies, banks, bond issuers and institutional investors still disagree that DCRAs communicate effectively with investors and issuers on issuer's performance, and that either investors or issuers understand the methodologies employed by the DCRAs (Mat Radzi and McIver, 2012). Thus there is room for improvement on transparency and rating methodology so that information provided by DCRAs becomes meaningful for issuers and investors and increases their confidence and usage of DCRAs' ratings.

In the European Union (EU), the EU Security Market Authority (ESMA) requires registered CRAs whose ratings are used in the EU to provide rating information and statistics such as rating activities, default ratios and transition matrix to its central credit rating information repository (CEREP) which is open to anyone and can be used for commercial purposes. Even though, unlike the EU, there is no supra-national body in ASEAN+3 region to establish uniform region-wide rules and regulations and such regulatory gaps are to be addressed by the ASEAN+3 Bond Market Forum (ADB, 2012), a common CRA registration and reporting system for DCRAs in the region at the standards and contents which are useful for investors' assessment, for example, will help enhance ratings transparency and evaluation at the regional level. A RCRA can take the lead by adopting reporting standards and level of transparency that ensures sufficient understanding and confidence of investors. The Caribbean RCRA, CariCRIS, discussed in Section 2.3 is an example where benchmark ratings are intended to support greater information disclosure, better corporate governance and improved access to publicly available expert analysis (CariCRIS, 2005).

3.4 Accuracy and consistency of ratings, quality of analysis and timeliness of rating actions

As mentioned in the beginning section, ASEAN+3 DCRAs are at different stages of development hence the relative rating performance between the more established DCRAs that manage to maintain their relative standing in the respective market and the smaller late comers are likely to differ. The regional market is also fragmented with most ratings done at the national level under an oligopolistic market structure making intra-regional comparison and evaluation of

Figure 5 : ESMA's CEREP Database



Source: ESMA Central Repository (CEREP)

credit ratings difficult. ACRAA's rating harmonization program aims to achieve comparability among DCRAs in terms of rating methodology, rating criteria, definitions, benchmarks and overall rating process that will facilitate cross-border investment. ACRAA Code of Conduct also emphasizes transparency and timeliness of ratings disclosure that include a consistent and uniform default definition, and publication of a default and transition study with annual default rates for each rating category, 3-year average cumulative default rates and 1-year transition rates with guidance on the calculation method (ACRAA, 2011). This is because historical default studies with clear default definition, publication of rating policies, methodologies and practices, and databases for information disclosure and comparison are identified as determinants of credit ratings comparability and demonstrate elements of common standards among DCRAs. As outlined by the ADB (ADB, 2006), rating comparability is seen as a necessary first step in the Asian Bond Market Initiative's (ABMI) agenda to build tools for cross-agency and cross-border comparison of ratings, and compile rating methodologies and databases of all ratings issued by agencies and of regulatory support measures across the regulatory environments of DCRAs.

Table 10: TRIS Average One-Year Corporate Transition Rates (1994 – 2011)

Ratings	No. of Sample	AAA	AA	A	BBB	BB	B	C	D	Cumulative Withdrawals
AAA	14	78.57%	21.43%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	2
AA	81	1.23%	91.36%	6.17%	0.00%	0.00%	0.00%	0.00%	1.23%	7
A	307	0.00%	3.26%	93.81%	2.61%	0.00%	0.00%	0.00%	0.33%	25
BBB	285	0.00%	0.00%	7.02%	87.37%	2.11%	0.70%	0.00%	2.81%	25
BB	14	0.00%	0.00%	0.00%	14.29%	71.43%	0.00%	0.00%	14.29%	8
B	2	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	50.00%	50.00%	-
C	1	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	100.00%	-
Total	**704**									67

Source: TRIS Rating (2012)

Table 11: PEFINDO One-Year Corporate Rating Transition Rate (1996 – 2010)

Ratings	No. of Sample	idAAA	idAA	idA	idBBB	idBB	idB	idCCC	idD	NR
idAAA	18	88.89%	5.56%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	5.56%
idAA	106	3.77%	84.91%	6.60%	0.00%	1.89%	0.00%	0.00%	0.94%	1.89%
idA	383	0.26%	8.88%	82.77%	2.09%	0.78%	0.00%	0.00%	3.39%	1.83%
idBBB	319	0.00%	0.63%	14.11%	66.46%	4.70%	1.25%	1.88%	7.84%	3.13%
idBB	65	0.00%	0.00%	0.00%	20.00%	21.54%	6.15%	4.62%	30.77%	16.92%
idB	23	0.00%	0.00%	0.00%	8.70%	13.04%	34.78%	4.35%	30.43%	8.70%
idCCC	19	0.00%	0.00%	15.79%	47.37%	10.53%	10.53%	5.26%	10.53%	0.00%
Total	**933**									

Source: PEFINDO (2011)

Table 12: S&P Average One-Year Asia Corporate Rating Transition Rates (2000 – 2011)

Ratings	No. of Sample	AAA	AA	A	BBB	BB	B	CCC	CC	C	SD,D,R	Withdrawals
AAA	47	91.39%	6.53%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	2.08%
AA	416	0.69%	92.64%	2.57%	0.00%	0.00%	0.28%	0.00%	0.00%	0.00%	0.00%	3.82%
A	998	0.00%	1.32%	90.74%	1.86%	0.24%	0.34%	0.00%	0.00%	0.00%	0.00%	5.50%
BBB	1143	0.00%	0.00%	3.78%	82.50%	3.43%	0.00%	0.00%	0.00%	0.00%	0.00%	10.29%
BB	821	0.00%	0.00%	0.00%	6.41%	78.58%	4.61%	0.00%	0.13%	0.00%	0.11%	10.17%
B	465	0.00%	0.00%	0.00%	0.00%	8.34%	73.13%	2.17%	0.56%	0.00%	1.94%	13.86%
CCC	61	0.00%	0.00%	0.00%	0.00%	0.00%	16.61%	57.04%	5.56%	0.00%	7.66%	13.14%
CC	18	0.00%	0.00%	0.00%	0.00%	0.00%	12.50%	15.63%	35.42%	0.00%	14.58%	21.88%
SD,D,R	53	0.00%	0.00%	0.00%	0.00%	0.00%	1.39%	5.93%	2.78%	0.00%	29.65%	60.26%
Total	**4022**											

Source: Calculation from CEREP statistics. Retrieved on 5 February 2013.

Table 13: Moody's Average One-Year Asia Corporate Rating Transition Rates (2000 – 2011)

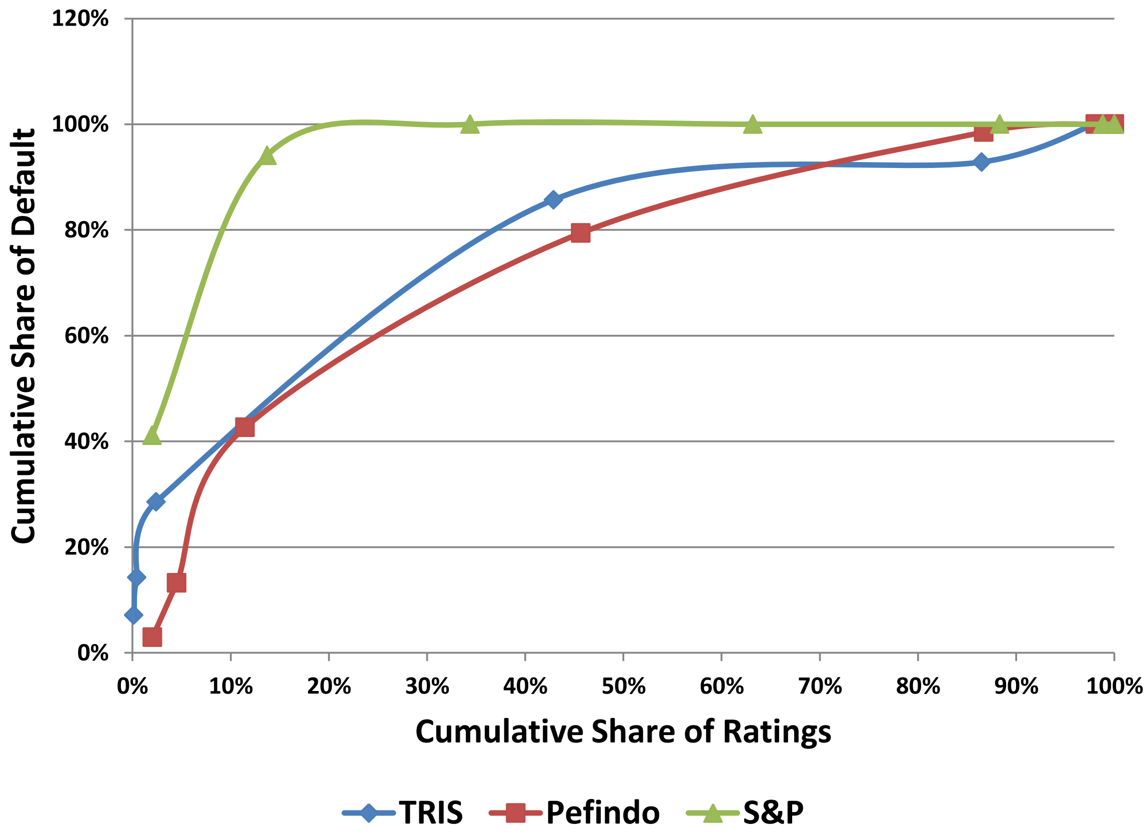
Ratings	No. of Sample	Aaa	Aa	A	Baa	Ba	B	Caa	Ca	C	Default	Withdrawals
Aaa	45	85.24%	8.93%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	5.83%
Aa	364	1.68%	90.70%	5.09%	0.00%	0.00%	0.21%	0.00%	0.00%	0.00%	0.00%	2.32%
A	1036	0.00%	1.50%	87.91%	4.15%	0.13%	0.26%	0.00%	0.00%	0.00%	0.00%	6.04%
Baa	1073	0.00%	0.00%	5.20%	83.70%	1.42%	0.10%	0.08%	0.00%	0.00%	0.10%	9.41%
Ba	391	0.00%	0.00%	0.00%	12.77%	69.20%	5.31%	1.08%	0.67%	0.18%	1.49%	9.31%
B	198	0.00%	0.00%	0.00%	0.33%	10.86%	67.38%	4.68%	1.45%	0.00%	3.71%	11.60%
Caa	30	0.00%	0.00%	0.00%	0.00%	0.00%	15.61%	42.06%	3.70%	0.00%	11.11%	27.51%
Ca	19	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	36.67%	0.00%	0.00%	63.33%
C	2	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	50.00%	0.00%	50.00%
Total	**3158**											

Source: Calculation from CEREP statistics. Retrieved on 5 February 2013.

Most ASEAN DCRAs that are ACRAA members have thus provide historical default studies that allow investors' use of the information in order to evaluate their investment and structure their exposure, in addition to evaluate DCRAs rating performance. Table 10 and 11, for example, show one-year long-term corporate rating transition matrices for Thailand's TRIS (1994-2011) and Indonesia's PEFINDO (1996-2010) respectively that are obtained from their corporate default and rating transition studies. Table 12 and 13 also show similar transition matrices for S&P and Moody's that are obtained by calculating average one-year transition probabilities over the 2000-2011 period from annual transition rates for their long-term corporate ratings in Asia. The annual rating statistics are available at ESMA's CEREP database. Transition rates along the diagonal of the transition matrix indicate the probabilities that issues in the static sample remained in the same rating category throughout the period, whereas off-diagonal entries in a particular row show the likelihood of an upgrade or downgrade from the referenced row rating category to another rating as indicated in the reference column.

If the S&P transition matrix (Table 12) is used as a benchmark for comparison, TRIS's (Table 10) and PEFINDO's (Table 11) ratings are notably more volatile at the BBB category and below, having smaller percentages of ratings on the diagonal entries and much more variability of rating transitions to other categories, in the case of PEFINDO, indicating lower rating performance (i.e. more frequent changes of ratings possibly due to more reactive ratings as opposed to predictive or 'through the cycle' ratings). Although the 'A' and 'BBB' categories for the DCRAs have large numbers of observations (around 300-400 for each rating category cumulatively over the sample period), there are small numbers of sample at the highest and lowest rating grades. TRIS has 18 observations cumulatively for AAA category, 14 for BB and 3 for categories below BB. PEFINDO has 18 observations for the idAAA class, 65 for idBB and 42 for other grades below). S&P's transition matrix contains information from greater number of observations (almost 4000, counted and sum each year from annual information available in the EU CEREP database on a static pool basis) due to greater number of ratings for Asia region as a whole, whereas those of the two ASEAN DCRAs have less number of observations (704 for TRIS and 933 for PEFINDO) due to fragmented nature of the markets.

Figure 6 : Cumulative Accuracy Profiles



Source: Calculation based on data from TRIS Ratings (2012), PEFINDO (2011) and CEREP database

Figure 6 shows Cumulative Accuracy Profile (CAP) plots for S&P and the two DCRAs where default information is approximated from their respective transition matrices. The CAP plots show cumulative shares of default (vertical axis) for each rating category from lowest rating to highest rating (horizontal axis). The plot for S&P is closest to an ideal curve where most defaults occur with lowest rating categories. The 'accuracy ratio', ratio of the area between the CAP curve and the 45-degree line to the total area above the 45-degree line, can also be calculated. The calculated ratios for the CRAs are derived here from their corresponding 'average defaulter position', Moody's measure of ordinal rating performance (Moody's, 2011) which shows average shares of ratings above default for defaults that occur in all rating categories. Thus a higher average defaulter position, like the accuracy ratio, indicates better rating performance. The calculated accuracy ratios for S&P, TRIS and PEFINDO are 88.42%, 52.27% and 49.12% respectively and the corresponding average defaulter positions are 94.21%, 76.13%, and 74.56% respectively. In practice, if a RCRA can provide region-wide coverage of benchmark ratings then the information provided by the RCRA can be used to assess the accuracy of its rating relative to those of GCRAs, for example. And subsequently similar comparison for the assessment of DCRAs, given that the numbers of ratings have significantly increased as a result of greater comparability, once the market is harmonized and has a regional scale benchmark to compare against.

Since most ASEAN DCRAs are ACRAA members and thus adhere to the ACRAA Code of Conduct, the harmonization of CRAs regulation or reporting standards is feasible by agreeing on how to adopt the IOSCO codes effectively with a particular emphasis on credibility of CRAs that are based on their independence, transparency and rating comparability. This will help domestic and global investors to better understand credit ratings by DCRAs and enable them to better participate in the regional bond market.

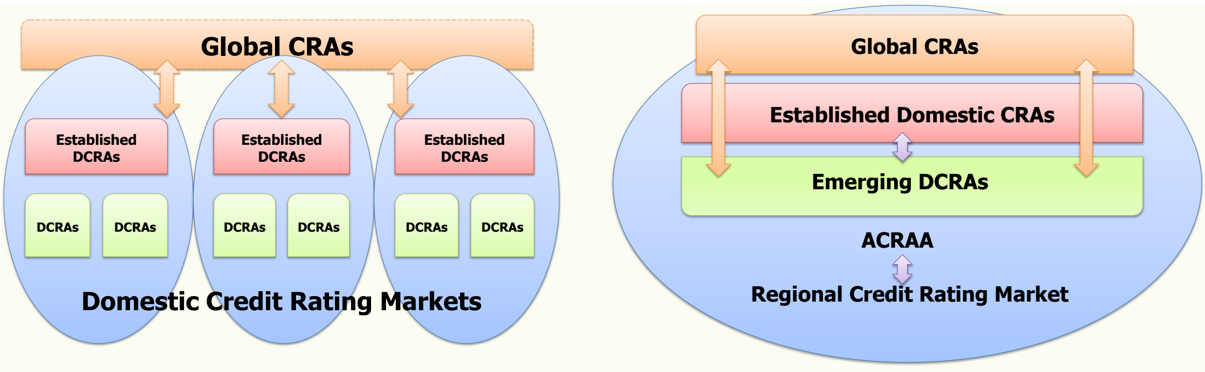
4. Conclusion and Recommendation

Given the present conditions of ASEAN+3 CRAs, there are potential benefits in terms of regional credit market integration and expansion for greater investors' access and investment opportunities through accelerated rating harmonization process and the establishment of a regional credit rating agency (RCRA). The resulting recognition of rating standards and practices as well as alternative regional benchmark ratings under internationally recognized rating standards of an independent RCRA can lead to significant improvement in DCRAs' credibility enhancing characteristics (Independence, Transparency, Accuracy and consistency of ratings, Quality of analysis, and Timeliness and effectiveness of rating actions) necessary for gaining investors' acceptance.

A regionally coherent credit rating market development such as one that follows the establishment of a RCRA will consist of practical measures for implementation such as the utilization of an alternative/common regional scale, a regulatory system for CRAs registration and reporting, support for DCRAs capacity building, and agreement on essential best practice and monitoring. There is currently a gap between services provided, on the one hand, by GCRAs with limited capacity in terms of number of employees and analysts to cover greater number of regional issuance, and on the other hand, services by DCRAs that are limited to their respective country coverage. Thus an independent regional CRA, that leverages on the expertise of GCRAs and greater local reach of DCRAs as well as coordination and facilitation from ACRAA, and financial and technical resources from international organizations under a roadmap for market acceptance would facilitate regional bond market development by improving regional comparability, coverage and market access.

In order to effectively create a regional credit rating system that is able to facilitate cross-country and cross-currency issuances in the context of intra-regional investments as well as outward investment in other regions by local firms, the roles and interests of concerning parties need to be considered. Established DCRAs with specialized local knowledge and reach have the ability to lead local market development in own countries and new markets. GCRAs looking for market expansion, local knowledge and connections can help provide technical support, global expertise and access to international investors. There have been interests among GCRAs for involvement in the region and some established DCRAs notably in the Plus Three countries have their eyes on the regional and global markets. But the initiatives have been from individual CRAs on an individual basis, partly as a result of the fragmented markets and oligopolistic structure that limits profitability potential for new DCRAs as latecomers. An establishment of a RCRA with participation of DCRAs and GCRAs will accelerate the movement towards their more integrated relationship and continue market momentum that already exists in a regionally coherent way that benefits regional market development.

Figure 7 Present and Future Regional Credit Rating Systems



Public institutions, including international organizations and local regulatory authorities, have the role in ensuring that CRAs interests are aligned and the RCRA plays a leading and complementary role in regional and local market development. Consistent with its objectives of enhancing DCRAs' capacity, quality of rating process and rating comparability in order to assist Asian Bond Market development and cross-border investment throughout the region, ACRAA can help coordinate and facilitate the participation of local and global CRAs in establishing the RCRA, possibly through a broad-based shareholding structure. ASEAN+3 members in the more developed markets such as China, Korea, Japan and Singapore can serve as initial funders. Sovereign ratings and other considerations necessary for credit risk adjustment to arrive at a regional rating scale by RCRA such as regulatory risks, transferability and convertibility risks, and parent-subsidiary links, etc., can be endorsed by the more established DCRAs and GCRAs and used effectively as an alternative regional benchmark. The rating and reporting processes and standards established by RCRA also serve as a regional reference for best practices accepted by international investors. Since most DCRAs are ACRAA members thus adhere to the ACRAA Code of Conduct, the harmonization of CRAs regulation or reporting standards is feasible by agreeing on how to adopt the IOSCO codes effectively with a particular emphasis on credibility of CRAs that are based on their independence, transparency and rating comparability. Therefore domestic and global investors who understand RCRA rating standards, methodologies and procedures will also have better understanding of credit ratings by DCRAs and enable them to better participate in the regional bond market development.

Near-term measures to support the establishment of a RCRA include: 1) Gathering interest from potential CRA shareholders/members with initial public sector financial support to build up market reputation and credibility; 2) Arrangement among GCRAs and established DCRAs with capacity to evaluate sovereign risk to provide a common/alternative regional rating scale (as already done individually by GCRAs like S&P and established DCRAs like RAM rating, for example); 3) Market sounding/book building exercise to pool potential issuers and assess investors' demand through the support of shareholder members (DCRAs in local market and GCRAs in international market); and 4) Leverage information required for in-depth rating process from local sources through DCRAs and leverage surveillance capability and technical expertise of international organizations like ADB, AMRO and the IMF.

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Annex I: Correspondence between ACRAA Code of Conduct and DCRAs Credibility Criteria

A summary table on the next page summarizes and classifies ACRAA Code of Conduct into five ideal characteristics for domestic credit rating agencies. Each code of conduct may fall into more than one ideal characteristic depending on the definitions of the characteristics obtained from the Asian Banker Association study on Development of Regional Standards for Asian Credit Rating Agencies (ABA, 2000). These classifications are used as supplementary information under each DCRAs evaluation criterion discussed in the paper.

	ACRAA CODE OF CONDUCT	Independence	Transparency	Accuracy and Consistency of Ratings	Quality of Analysis	Timeliness/ Effectiveness of Rating Actions
I.	**Quality and Integrity of the Rating Process**					
	A. Quality of the Rating Process					
1	Enforce written procedures		√		√	
2	Well-defined and updated credit rating criteria		√		√	√
3	Publishing Rating Criteria		√			
4	Rating committee as the final decision-making body	√				
5	Discussions during the committee open to all DCRA analytical personnel		√			
6	Members with business development responsibilities do not have voting rights in the rating committee	√	√			
7	The rating committee's decisions are subject to a clearly described review or appeal process		√			
	B. Monitoring and Updating					
8	Conduct formal reviews involving meetings with issuers				√	√
9	Conduct periodic surveillance until the rating withdrawal and the publication of surveillance reports				√	√
10	Basic policies, practices, and methodologies used for assignment of ratings are published and freely available in print and on the Web site		√		√	
11	Policy for assigning, revising, suspending, and withdrawing ratings are clearly outlined and made public		√		√	√
	C. Integrity of the Rating Process					
12	The assignment of a rating is derive purely from independent and unbiased views based on the determinants of credit quality and not on any assurance or guarantee given beforehand	√				

	ACRAA CODE OF CONDUCT	Independence	Transparency	Accuracy and Consistency of Ratings	Quality of Analysis	Timeliness/ Effectiveness of Rating Actions
II.	**DCRA's Independence and Avoidance of Conflicts of Interest**					
	A. General					
13	Rating decisions are not influenced by rating fees, any other revenues or business potential from the rated entity, or the consequences of a rating action	√				
14	Compensation of a DCRA's rating analysts is independent of rating fees and the final rating assigned	√				
15	Removal of employees with business development responsibility from the analytical process		√			
16	Adopt a definition of what constitutes a conflict of interest and publish it		√			
17	Disclosure of all ratings assigned		√	√		
18	Separate, operationally and legally, its credit rating business and DCRA analysts from any other businesses of the DCRA, including consulting businesses	√	√			
	B. DCRA Procedures and Policies					
19	Disclose the proportion such non-rating fees constitute against the fees the DCRA receives from the entity for rating services	√	√			
20	Ensure that compensation for analytical personnel is not linked to revenues earned from the ratings that are executed by the analysts concerned		√			
21	Establish policies and procedures for reviewing the past work of analysts that leave the employment of the DCRA		√			

	ACRAA CODE OF CONDUCT	Independence	Transparency	Accuracy and Consistency of Ratings	Quality of Analysis	Timeliness/ Effectiveness of Rating Actions
III.	**DCRA Responsibilities to the Investing Public and Issuers**					
	A. Transparency and Timeliness of Ratings Disclosure					
22	All rating actions are announced promptly, and a list of outstanding ratings made freely available on a DCRA's website			√		√
23	Publicly disclose its policies for distributing ratings, reports, and updates		√	√		
24	Well-defined time lines for completion of each rating assignment					√
25	Publicize the approximate timeline of the rating process to set market expectations					√
26	A consistent and uniform default definition		√	√		
27	A credit rating and the rating report should be current and updated				√	√
28	Publish, at least annually, a default and transition study, along with the methodology used for calculating default rates		√	√	√	
29	A default study should include definition of default, historical data, proxy information such as number of ratings, number of upgrades and downgrades		√	√		√
30	When a DCRA assigns unsolicited ratings, it should distinguish them using some sort of notation		√	√		
	B. Treatment of Confidential Information					
31	All information submitted by a rated entity or an issuer in connection with a credit rating assignment is presumed confidential and shall be kept so at all time		√			
32	The confidentiality requirement must be binding on all company officers, employees and external rating committee members, if any, who have or may have access to such confidential information, and acknowledged in writing		√			

	ACRAA CODE OF CONDUCT	Independence	Transparency	Accuracy and Consistency of Ratings	Quality of Analysis	Timeliness/ Effectiveness of Rating Actions
IV.	**Disclosure of the Code of Conduct and Communication with Market Participants**					
33	Describe generally how it intends to enforce its code of conduct and should disclose on a timely basis any changes to its code of conduct or how it is implemented and enforced		√			
34	Adopt its own code of ethical conduct, applicable to all employees and board members and should be published on the DCRA's web-site		√			
35	Should publish in a prominent position on its home webpage links to (i) the DCRA's code of conduct, (ii) a description of the methodologies it uses, and (iii) information about the DCRA's historical performance data		√	√		