



August 2012

CRISIL Insights



Translating Global Scale Ratings on to
CRISIL's Scale



About CRISIL Insights

For over two decades, CRISIL has helped shape the evolution of the debt markets in India, and has added value to market participants in a variety of ways.

'CRISIL Insights' is a knowledge sharing endeavour from CRISIL to

1. Share our analytical insights and thought leadership perspectives: CRISIL continues to focus on developing a strong understanding of the Indian economy, corporate sector, and financial landscape. The knowledge and insights gained in this process are constantly shared with issuers and investors on relevant topics that impact the credit markets.
2. Generate awareness about the rigour followed in our ratings process: As the country's leading ratings agency, CRISIL has always set standards in analytical rigour, disclosures, and best practices in the industry. CRISIL tries to generate familiarity of the market participants with the same.
3. Enhance transparency of our analytical methodology and criteria: To develop confidence of the debt market participants, CRISIL constantly endeavours to highlight the analytical methodology and criteria used in its ratings process.

CRISIL Ratings hopes that you find this research valuable, insightful, and useful. Your comments and queries regarding the issues discussed here are welcome.

Analytical Contacts:

Somasekhar Vemuri

Director – CRISIL Ratings

Email: somasekhar.vemuri@crisil.com

Chetan Rao

Associate Director – CRISIL Ratings

Email: chetan.rao@crisil.com

Executive Summary

CRISIL, whilst assigning ratings on subsidiaries, assesses the credit linkage of the subsidiary with its parent. As a result, the credit rating of the parent is a critical input in the assessment. In the event that the parent is a foreign company, its rating may be on a global rating scale and CRISIL factors in the rating assigned by Standard & Poor's (S&P) to the parent company. CRISIL maps the parent's ratings, which are on the global rating scale, onto CRISIL's own rating scale in order to assess the parent's credit profile. Though the rating symbols used by S&P and CRISIL appear to be similar, they do not mean or represent similar credit quality. While S&P, an international rating agency, assigns ratings to instruments on a global scale, CRISIL assigns ratings on the national scale. This inter-scale comparison or 'translation' between global and national scale ratings, may be made in one of three ways: sovereign ceiling, direct credit assessment, and the first-principles approach. CRISIL's methodology is based on the first-principles approach, where comparison of financial ratios are used together with comparison of default and transition rates, to determine the broad mapping of the global scale ratings to CRISIL's rating scale.

Scope

This article elucidates the meaning of, and need for, an inter-scale comparison between global scale ratings and ratings on the national scale. It outlines each of the three methods that rating agencies adopt to map global scale ratings on to the national scale. The article also describes CRISIL's approach in translating global scale ratings. CRISIL's translation criteria should be applied only while factoring in the credit linkage between the foreign parent and Indian subsidiary, and not to rate a global entity on CRISIL's rating scale.

Understanding 'translation'

In an increasingly globalised investment environment, investors seek clarity on how credit ratings by global rating agencies may be translated into ratings on the domestic scale. CRISIL ratings are not directly comparable with S&P ratings, even though the rating scales appear to be similar—while S&P's ratings are assigned based on an assessment of the issuer in relation to other issuers globally, CRISIL's ratings benchmark the issuer against other domestic issuers.

CRISIL's assessment of the credit quality of instruments that carry an element of foreign credit risk involves 'translation': in other words, the foreign company's ratings on the global rating scale are mapped on to CRISIL's own rating scale. This is backed by CRISIL's extensive in-house research efforts and a rating history of more than 25 years.

With the opening up of the financial markets, multinationals have steadily increased their presence in India, thereby enhancing the need for such translation. CRISIL's ratings of these entities are influenced, to varying degrees, by the credit quality of their parents, as indicated by their outstanding credit ratings from S&P. CRISIL uses these global-scale ratings in its analytical framework while rating the debt issued by the related Indian entities. CRISIL, in its ratings, factors in credit uplift due to parent support, or an explicit guarantee by the parent; or notch-down on account of a weaker parent. If the parent provides an explicit guarantee for the rated debt, which is supported by an appropriate and enforceable payment structure, CRISIL's rating depends solely on its assessment of the credit quality of the guarantor, as reflected in the translated rating. In instances where there is no explicit guarantee, CRISIL takes a view on the standalone rating of the Indian entity, and the translated rating of the foreign parent, and assesses the relationship between the two from a credit perspective. These factors determine the extent to which the Indian entity's standalone rating will be notched up or down, based on the credit linkage with its parent. In both instances, the foreign company's credit quality is assessed after translating its rating on the global scale onto CRISIL's scale.



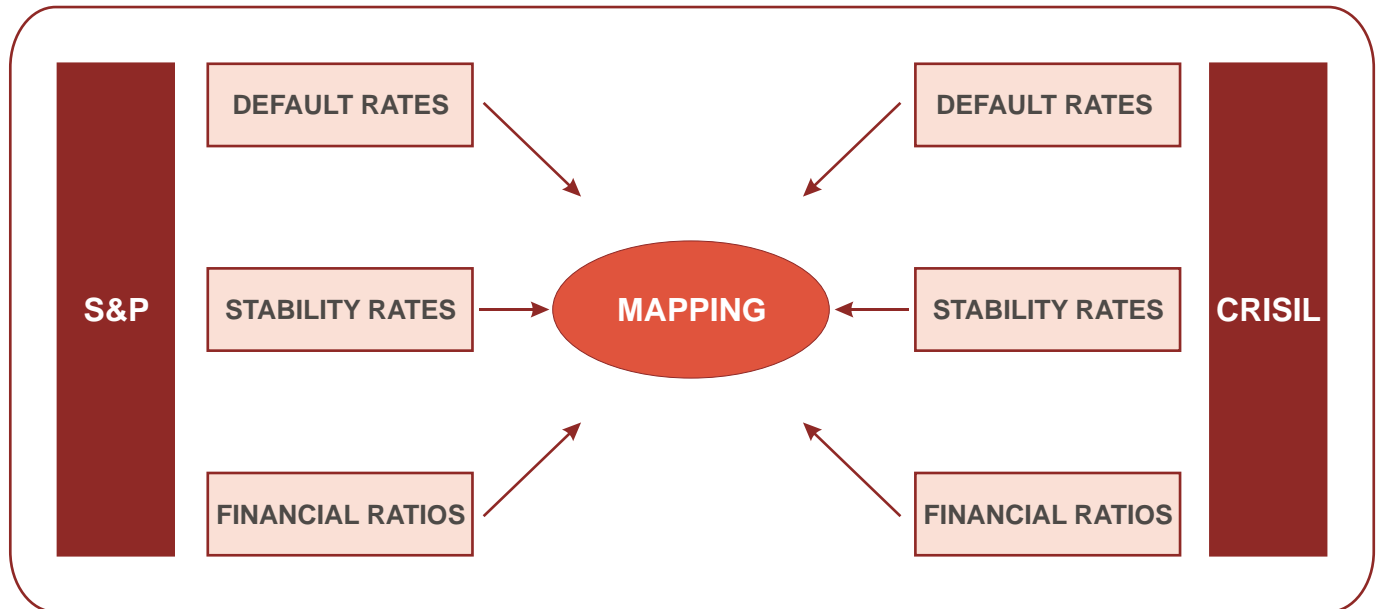
Different approaches used for translation of ratings

An inter-scale comparison between global scale ratings and ratings on the national scale may be made in one of three ways: sovereign ceiling, direct credit assessment and the first principles approach (refer to Box 1 for a detailed description of the three methods).

Box 1: Different methods of Translation of ratings

Sovereign Rating Linkage	Independent Credit Assessment	First Principles Approach
<ul style="list-style-type: none">■ S & P and other major international rating agencies typically have three rating scales - global scale foreign currency ratings, global scale local currency ratings, and national scale ratings - to address the various investor segments.■ The global scale local currency and foreign currency ratings cater to the needs of transnational investors.■ Rating agencies may choose to adopt the concept of sovereign rating linkage while translating global scale ratings onto the national scale, where all global scale ratings that are higher than the rating of the sovereign are assigned 'AAA' (or the equivalent) on the national scale.■ With this benchmark, the global scale ratings that are lower than the rating of the sovereign may be translated to correspondingly lower levels on the national scale.	<ul style="list-style-type: none">■ In such an approach, the foreign company is assessed in the same way a domestic company is, and is assigned a rating on the domestic scale.■ Such an exercise involves an analysis of the industry and business risks of the foreign company. These are placed in the context of local companies in a similar business; the past and expected financial performance of the foreign company, and its comparison with domestic players, with appropriate scaling for size and foreign currency exchange rates; peer group comparison of market position of foreign company, and its domestic contemporaries, and the like.■ While such an exercise may be meaningful in a fully globalised economy (such as Japan or the Western European countries), the sheer difference in size and other structural differences limit its usefulness in the Indian context.	<ul style="list-style-type: none">■ The first principles approach compares the key rating performance indicators (namely, default rates, transition rates and financial ratios) of the two rating scales for translation.■ The ratings are expected to convey a measure of the credit risk (expressed either as default rates or as expected loss)■ Comparing such a uniform measure between the global and national scales provides the most meaningful translation between any two rating scales.

CRISIL's approach to translating global scale ratings



CRISIL's approach to translation is based on the first principles of comparison of default rates, transition rates and financial ratios of CRISIL and S&P, in order to ensure an appropriate mapping of the two rating scales. CRISIL's default and transition rates are based on CRISIL's ratings assigned over nearly 25 years covering multiple credit cycles and is the most comprehensive database on corporate defaults and rating transitions in India.



CRISIL's method of translation

Translation is based on comparisons of:

Historical default rates

Ratings convey a measure of the credit risk (expressed either as default rates or expected loss); comparing such a uniform measure between the global and national scales provides the most meaningful translation between any two rating scales. Ratings by CRISIL and S&P express credit risk in terms of likelihood of default, measured by default rates. CRISIL's method, therefore, uses default rates as a key input in translation.

Historical stability rates

In conjunction with default rates, stability rates also form an important yardstick of a rating agency's performance. While default rates are of interest to all types of investors, some investors, whose investment horizon is less than the maturity of the instrument, are affected by rating transitions as well. Any mapping between two rating scales should also incorporate transition rates/stability rates to capture this element.

Financial ratios

Ratings across different rating agencies may also be directly compared on the basis of the financial ratios of the rated entities. Debt protection ratios like net cash accruals to total debt (NCA/TD) are not influenced by the size or state of the economy, and hence, are comparable across countries.

Mapping of CRISIL and S&P ratings based on each of the three parameters is used to arrive at the final mapping.

According to CRISIL's translation method, a rating on S&P's global scale tends to map to a rating on the CRISIL scale which is roughly 4 to 5 notches higher than the S&P rating. For example a rating of 'A' on S&P's scale would map to either a 'CRISILAAA' or 'CRISILAA+'. A rating of BBB- (India's sovereign rating currently) would map to either a 'CRISILA+' or 'CRISILA'. In order to arrive at the exact mapping level, CRISIL also factors in the outlook of the parent's rating from S&P, the industry/economic scenario, the recent history of S&P's rating actions on the parent, etc.

Any change in the ratings of the parent impacts the guaranteed ratings and parent-linked ratings of Indian subsidiaries. Volatility in global scale ratings, may, therefore, affect the credit quality of Indian companies rated by CRISIL; this is an inevitable fallout of translation between global and national rating scales.

About CRISIL Limited

CRISIL is a global analytical company providing ratings, research, and risk and policy advisory services. We are India's leading ratings agency. We are also the foremost provider of high-end research to the world's largest banks and leading corporations.

About CRISIL Ratings

CRISIL Ratings is India's leading rating agency. We pioneered the concept of credit rating in India in 1987. With a tradition of independence, analytical rigour and innovation, we have a leadership position. We have rated over 50,000 entities, by far the largest number in India. We are a full-service rating agency. We rate the entire range of debt instruments: bank loans, certificates of deposit, commercial paper, non-convertible debentures, bank hybrid capital instruments, asset-backed securities, mortgage-backed securities, perpetual bonds, and partial guarantees. CRISIL sets the standards in every aspect of the credit rating business. We have instituted several innovations in India including rating municipal bonds, partially guaranteed instruments and microfinance institutions. We pioneered a globally unique and affordable rating service for Small and Medium Enterprises (SMEs). This has significantly expanded the market for ratings and is improving SMEs' access to affordable finance. We have an active outreach programme with issuers, investors and regulators to maintain a high level of transparency regarding our rating criteria and to disseminate our analytical insights and knowledge.

CRISIL Privacy Notice

CRISIL respects your privacy. We use your contact information, such as your name, address, and email id, to fulfill your request and service your account and to provide you with additional information from CRISIL and other parts of The McGraw-Hill Companies, Inc. you may find of interest.

For further information, or to let us know your preferences with respect to receiving marketing materials, please visit www.crisil.com/privacy. You can view McGraw-Hill's Customer Privacy Policy at http://www.mcgrawhill.com/site/tools/privacy/privacy_english.

Last updated: April 30, 2012

Disclaimer:

CRISIL has taken due care and caution in preparing this report. Information has been obtained by CRISIL from sources which it considers reliable. However, CRISIL does not guarantee the accuracy, adequacy or completeness of any information and is not responsible for any errors in transmission and especially states that it has no financial liability whatsoever to the subscribers/ users/ transmitters/ distributors of this report. No part of this report may be reproduced in any form or any means without permission of the publisher. Contents may be used by news media with due credit to CRISIL.

Our Offices

Ahmedabad

706, Venus Atlantis
Nr. Reliance Petrol Pump
Prahladnagar, Ahmedabad
Phone: +91 79 4024 4500
Fax: +91 79 2755 9863

Bengaluru

W-101, Sunrise Chambers
22, Ulsoor Road
Bengaluru - 560 042
Phone: +91 80 2558 0899 / +91 80 2559 4802
Fax: +91 80 2559 4801

Chennai

Mezzanine Floor, Thapar House
No. 37, Montieth Road, Egmore
Chennai - 600 008
Phone: +91 44 2854 6205-06 / +91 44 2854 6093
Fax: +91 44 2854 7531

Gurgaon

Plot No. 46, Sector 44,
Opp PF Office, Gurgaon,
Haryana, INDIA
Phone : +91 0124 672 2000

Hyderabad

3rd Floor, Uma Chambers
Plot No. 9 &10, Nagarjuna Hills
(Near Punjagutta Cross Road)
Hyderabad - 500 482
Phone: +91 40 2335 8103 / 05
Fax: +91 40 2335 7507

Kolkata

Horizon, Block 'B', 4th Floor
57 Chowringhee Road
Kolkata - 700 071
Phone: +91 33 2289 1949 / 50
Fax: +91 33 2283 0597

Pune

1187/17, Ghole Road
Shivaji Nagar
Pune - 411 005
Phone: +91 20 4018 1900
Fax: +91 20 4018 1930



CRISIL Limited

CRISIL House, Central Avenue, Hiranandani Business Park,
Powai, Mumbai - 400 076. India
Phone: +91 22 3342 3000 | Fax: +91 22 3342 3001
www.crisil.com