

RATINGS

Credibility Is Everything

When Thailand's bond market was in its infancy a few years ago, foreign analysts considered it little more than a gambling den. With no objective way to judge the quality of new issues, investing often seemed more like gaming. Those days are changing. In Thailand and throughout Asia, growing along with the need to raise capital by issuing bonds (see story page 48), are agencies that will judge the danger of default.

None too soon. Investors must have a way of knowing the risk they are taking, says Greg Neumann, who heads the Hong Kong office of U.S. investment house Scudder, Stevens & Clark. After all, bonds are decidedly less sexy than stocks — and if they go bad, they become not so much unglamorous as notorious. A ratings agency should be able to warn investors away from real risks, or at least alert them to demand a higher return, says Neumann.

That was the theory behind the establishment two years ago of the Thai Rating and Information Services (TRIS) by the Bank of Thailand, the Thai Ministry of Finance and a wide range of private investors. No single partner in TRIS is permitted to own more than 5% — to ensure that assessments are not manipulated. Investment analysts stress that bond ratings must be based solely on one question: how likely is the issuer to repay?

Even the industry big boys, such as Moody's Investors Services and Standard & Poor's, are systematically evaluated both for their success in predicting default and for their independence from outside influence. The two companies' ratings methods differ in detail, but they are essentially similar. The four highest Standard & Poor's ratings, in decreasing order, are AAA, AA, A and BBB. These are "investment

grade," and the likelihood is good that bonds carrying these assessments will be repaid. BB bonds and below are "junk bonds." In general, the lower a bond is graded, the higher the interest rate it must carry to attract an investor and, therefore, the greater the cost of borrowing for the issuing entity. One Moody's official says: "The pressure from issuers for higher ratings must always be in delicate balance with the agencies' need to retain credibility among investors."

New ratings companies tend to tackle the smaller issues — below \$200 million, says one expert — that the established companies are not interested in. But even with these issues, credibility is everything. TRIS is currently fighting a \$500,000 wrongful dismissal suit from a top ex-officer who claims she was sacked for refusing to upgrade her rating of a real-estate company's debt. A recent government investigation found, in general, that the company's methods were sound.

Rating Agency Malaysia (RAM) is well on its way to being accepted as a decisive player in that nation's burgeoning bond market. The company has rated 223 bond offerings

worth almost \$12 billion since it opened in 1990. Last year, it earned close to \$4.8 million in fees, 50% more than in 1993. Revenues like that could attract competition, and RAM's chief executive officer, Chellapah Rajandram, welcomes the prospect: "It would take the monopolistic tag away from RAM." The Malaysian company and London's International Credit Rating Agency provide technical help to Indonesia's 18-month-old Pefindo agency, which has so far issued four BBB bond ratings — equivalent to Standard & Poor's risk rating for Indonesia.

Still, Malaysian Finance Minister Anwar Ibrahim recently told bond traders and analysts in Hong Kong that "it is not easy to understand" why ratings agencies downgrade bonds of low-debt Asian countries in comparison with those from Western countries with budget deficits. Good question. •



Chellapah Rajandram

RAM's Rajandram welcomes rivals