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# A STUDY ON CREDIT RATING ON INVESTMENT BANKING IN INDIA

**Dr. A. Fazlunnisa**
*Assistant Professor, Department of Commerce, Texcity Arts and Science College, Madukkarai, Coimbatore.*

## ABSTRACT
*The present Research study on Credit rating on Investment Banking in India is one of the measurement of credit rating system and agencies. A credit rating is an opinion of a particular credit agency regarding the ability and willingness an entity (government, business, or individual) to fulfill its financial obligations in completeness and within the established due dates. A credit rating also signifies the likelihood a debtor will default. It is also representative of the credit risk carried by a debt instrument – whether a loan or a bond issuance. A credit rating is, however, not an assurance or guarantee of a kind of financial performance by a certain instrument of debt or a specific debtor. The research study concluded that in India, the Securities and Exchange Board of India (SEBI) is the primary authority that approves or regulates Credit Rating companies in India and their various functionalities. A good credit rating indicates consumer's higher creditworthiness and lower risk of default for the lender/ investor and can thus help the borrowing entity access loans at low interest rates along with longer repayment tenure. Credit rating involves evaluating the creditworthiness of entities, usually governments and businesses, by Credit Rating Agencies (CRAs), such as CRISIL, ICRA, CARE, etc. A good credit rating indicates higher creditworthiness and a lower risk of default for the lender and thus, may help an entity avail credit more easily and at considerable rates of interest. Credit ratings that are assigned to entities also serve as a benchmark for financial market regulations.*

**KEYWORDS:** *Credit rating, score, agency, approvals or regulates, investment banking*

## INTRODUCTION
A credit rating is an opinion of a particular credit agency regarding the ability and willingness an entity (government, business, or individual) to fulfill its financial obligations in completeness and within the established due dates. A credit rating also signifies the likelihood a debtor will default. It is also representative of the credit risk carried by a debt instrument – whether a loan or a bond issuance. A credit rating is, however, not an assurance or guarantee of a kind of financial performance by a certain instrument of debt or a specific debtor. The opinions provided by a credit agency do not replace those of a financial advisor or portfolio manager. credit agency evaluates the credit rating of a debtor by analyzing the qualitative and quantitative attributes of the entity in question. The information may be sourced from internal information provided by the entity, such as audited financial statements, annual reports, as well as external information such as analyst reports, published news articles, overall industry analysis, and projections. A credit agency is not involved in the transaction of the deal and, therefore, is deemed to provide an independent and impartial opinion of the credit risk carried by a particular entity seeking to raise money through loans or bond issuance. Presently, there are three prominent credit agencies that control 85% of the overall ratings market:

- Moody's Investor Services,
- Standard and Poor's (S&P), and
- Fitch Group.

Each and every agency uses unique, but strikingly similar, rating styles to indicate credit ratings.

### Types of Credit Ratings
Each credit agency uses its own terminology to determine credit ratings. That said, the notations are strikingly similar among the three credit agencies. Ratings are bracketed into two groups: investment grade and speculative grade. Investment grade ratings mean the investment is considered solid by the rating agency, and the issuer is likely to honor the terms of repayment. Such investments are typically less competitively priced in comparison to speculative grade investments. Speculative grade investments are high risk and, therefore, offer higher interest rates to reflect the quality of the investments.

### Users of Credit Ratings
Credit ratings are used by investors, intermediaries such as investment banks, issuers of debt, and businesses and corporations. Both institutional and individual investors use credit ratings to assess the risk related to investing in a specific issuance, ideally in the context of their entire portfolio. Intermediaries such as investment bankers utilize credit ratings to evaluate credit risk and further derive pricing of debt issues. Debt issuers such as corporations, governments, municipalities, etc., use credit ratings as an independent evaluation of their creditworthiness and credit risk associated with their debt issuance. The ratings can, to some extent, provide prospective investors with an idea of the quality of the instrument and what kind of interest rate they should be expecting from it. Businesses and corporations that are looking to evaluate the risk involved

with a certain counterparty transaction also use credit ratings. They can help entities that are looking to participate in partnerships or ventures with other businesses evaluate the viability of the proposition.

**Credit Score**

A credit rating is used to determine an entity's creditworthiness, wherein an entity could be an individual, a business, a corporation or a sovereign country. In case of a loan, the rating is used to establish whether a loan should be rendered in the first place. If the process goes further, it helps in deciding the term of the loan such as dates of repayment, interest rate, etc. In the case of bond issuance, the credit rating indicates the worthiness of the corporation or sovereign country's ability to repay the bond payments in due time. It helps the investor evaluate whether to invest in the bond or not. A credit score, however, is strictly for indicating an individual's personal credit health. It indicates the individual's ability to undertake a certain load and his or her ability to honor the terms and conditions of the loan, including the interest rate and dates of repayment. A credit score for individuals is used by banks, credit card companies, and other lending institutions that serve individuals.

## CREDIT RATING AGENCIES IN INDIA

**1. Credit Rating Information Services of India Ltd. (CRISIL)**

Incorporated in 1987, CRISIL Ratings Limited (A subsidiary of CRISIL Limited, an S&P Global company) is a full-service credit rating agency that serves investors, lenders, issuers, and market intermediaries and regulators by covering banks, NBFCs, PSUs, manufacturing companies, financial institutions, state governments, urban local bodies, etc. Credit Rating Information Services of India Limited (CRISIL) evaluates the creditworthiness of commercial entities based on their strengths, market reputation and market share. The credit rating agency helps investors make informed investment decisions by providing credit ratings for companies, organisations and banks. CRISIL generates and provides various ratings services, such as Independent Credit Evaluation, Corporate and financial Sector ratings, Fund Ratings, Recovery Risk Ratings, Expected Loss (EL) Ratings, etc. It also offers services related to Structured Finance and Insurance Hybrids. The rating generated by the agency ranges from AAA to D, where in AAA is the highest or credit worthy and D being the lowest or even defaulted.

**2. Investment Information and Credit Rating Agency of India (ICRA) Ltd.**

ICRA Limited (formerly Investment Information and Credit Rating Agency of India Limited) is an independent and professional investment Information and Credit Rating Agency. Formed in 1991, ICRA offers guidance and information to institutional and individual investors and creditors. It rates rupee-dominated debt instruments issue by commercial banks, NBFCs, PSUs, manufacturing companies and municipalities. The agency uses a transparent rating system to assign comprehensive credit ratings to corporates. It specialises in assigning corporate governance rating, mutual funds rating, structured finance rating, performance rating, etc.

**3. Credit Analysis and Research (CARE) Ltd.**

Established in 1993, Credit Analysis and Research Limited (CARE) is an experienced credit rating agency that covers various market sectors, including infrastructure, manufacturing, and financial sector, including banks and non-financial services. The agency provides ratings to companies related to developing bank debt and capital market instruments that include CPs, corporate bonds and debentures, and structured credit. Its credit ratings can be used by investors to make informed decisions on the basis of credit risk and risk-return expectations. CareEdge Ratings' (CARE Ratings Ltd.) manages and operates its wholly owned subsidiaries, such as CARE Advisory, Research & Training Ltd. and CARE Risk Solutions Pvt Ltd.

**4. Acuite Ratings & Research Ltd.**

The Acuité Ratings & Research Limited (Formerly known as SMERA Ratings Limited) is a SEBI registered and RBI accredited credit rating agency that offers ratings to companies serving structured finance, corporate and financial sectors. Its earlier range of products and services portfolio included Bank Loan Ratings, SME Ratings, Bond Ratings, CP Ratings, etc. However, currently the agency's primary services include Bond & Bank Loan Ratings, Economic Analysis and Financial Research services. Largely, Acuité offers services to largely small-sized private corporates, and public sector organizations like Nuclear Power Corporation, and renowned companies in the financial sector. The agency offers credit rating services to companies serving various sectors, such as banking, telecom, IT & ITes, steel, aviation, oil and gas, retail, etc.

**5. Brickwork Ratings India Private Ltd.**

Brickwork Ratings (BWR) is a SEBI registered and RBI accredited Credit Rating Agency that offers rating services on Bank Loans, Fixed Deposits, Non-convertible debentures (NCD), Commercial Paper, Securitised paper, Security receipts, etc. The agency offers credit ratings for banks, financial institutions, large corporate customers, and state and local governments. BWR offers a wide range of rating services and products related to Capital Market Instruments and Bank Loans for the Corporate, Financial, Infrastructure and Insurance Sectors, PSUs, State Government, Municipal and Urban Local Bodies, etc.

**6. India Ratings and Research Pvt. Ltd.**

In India Ratings and Research (Ind-Ra), a wholly owned subsidiary of the Fitch Group is one of the leading credit rating agencies recognized by SEBI and accredited by RBI. Ind-Ra offers credit rating services to banks, insurance companies, corporate issuers, finance and leasing companies, urban local bodies and managed funds, structured finance and project finance companies. With its Head office is Mumbai, the agency operates from its seven branch offices across India, including Delhi, Chennai, Kolkata, Ahmedabad, Bengaluru, Hyderabad and Pune.

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**7. INFOMERICS Valuation and Rating Private Ltd. Integrated Financial Omnibus Metrics Research of International Corporate Systems**

INFOMERICS Valuation and Rating Private Limited is a SEBI registered and RBI accredited Credit Rating Agency that provides deep analysis and evaluation of creditworthiness and ratings of Banks, NBFCs, Large Corporates and Small and Medium Scale Units (SMUs). INFOMERICS offer credit rating services money market & capital market instruments and borrowing programmes, such as Non-Convertible Debentures, Commercial Papers, Tier I & Tier II Bonds, Perpetual Bonds, Structured Obligations (including Guarantee Backed Debt programme), and Securitisation Transactions. The agency also rates Mutual Funds and Alternative Investment Fund schemes. Its grading services include Corporate Governance rating, and Grading of Construction entities, Engineering & Management institutions, Initial Public Offerings (IPOs), etc.

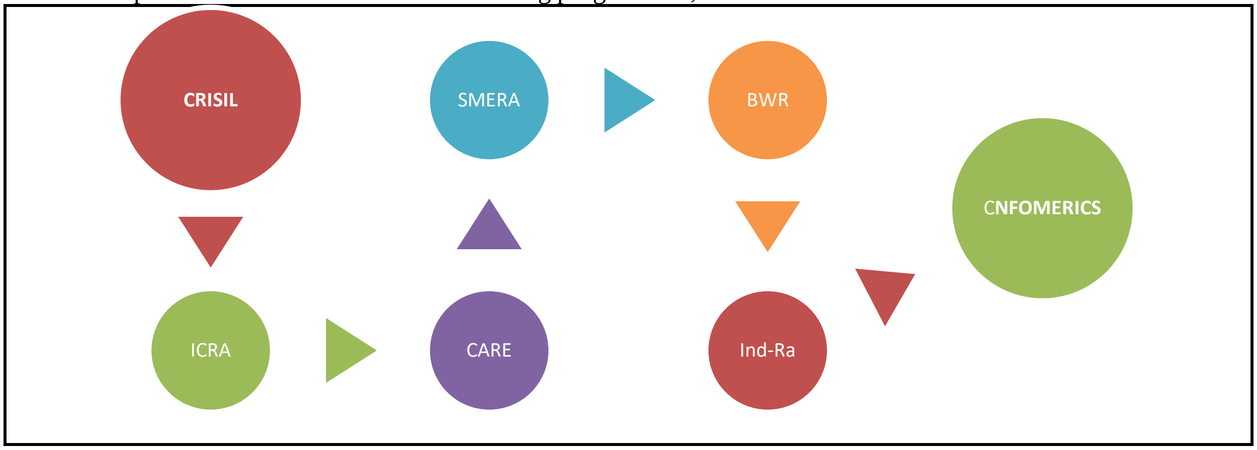


**Figure:*1 Credit rating agencies in India***

## REVIEW OF LITERATURE

**Itay Goldstein, Chong Huang (2020),** Credit Rating Inflation and Firms' Investments, The Journal of Finance, **Volume75, Issue6**, December 2020,Pages 2929-2972. The research study analyze credit rating effects on firm investments in a rational bond financing game that features a feedback loop. The credit rating agency (CRA) inflates the rating, providing a biased but informative signal to creditors. Creditors' response to the rating affects the firm's investment decision and thus its credit quality, which is reflected in the rating. The CRA might reduce ex ante economic efficiency, which results solely from its strategic effect: the CRA assigns more firms high ratings and allows them to gamble for resurrection. We derive empirical predictions on the determinants of rating standards and inflation and discuss policy implications. **Anna Bayona, Oana Peia, Razvan Vlahu (2023), Credit Ratings and Investments, De Nederlandsche Bank Working Paper No. 776,** The research study how inflated credit ratings affect investment decisions in bond markets using experimental coordination games. Theoretical models that feature a feedback effect between capital markets and the real economy suggest that inflated ratings can have both positive and negative real effects. We compare markets with and without a credit rating agency and find that ratings significantly impact investor behaviour and capital allocation to firms. We show that the main mechanism through which these real effects materialize is a shift in investors' beliefs about the behaviour of other investors rather than firms' underlying fundamentals. Our experimental results suggest that the positive impact of inflated ratings is likely to dominate in the presence of feedback effects since ratings act as a strong coordination mechanism resulting in enhanced market outcomes.

## OBJECTIVES OF THE STUDY

1. To study the credit rating system on banking sectors.
2. To study the approvals or regulates credit rating agencies.

## CONCLUSION

The research study concluded that in India, the Securities and Exchange Board of India (SEBI) is the primary authority that approves or regulates Credit Rating companies in India and their various functionalities. A good credit rating indicates consumer's higher creditworthiness and lower risk of default for the lender/ investor and can thus help the borrowing entity access loans at low interest rates along with longer repayment tenure. Credit rating involves evaluating the creditworthiness of entities, usually governments and businesses, by Credit Rating Agencies (CRAs), such as CRISIL, ICRA, CARE, etc. Credit ratings are usually expressed as letter grades. Whereas, credit scores usually help determine the creditworthiness of individuals and are calculated on the basis of the credit history found in the credit report. Credit scores are computed by four major credit bureaus in India including TransUnion CIBIL, Equifax, Experian and CRIF High Mark. Credit score is a 3-digit number ranging between 300 to 900, where a score closer to 900 is generally considered to be a good by lenders. A good credit rating indicates higher creditworthiness and a lower risk of default for the lender and thus, may help an entity avail credit more easily and at considerable rates of interest. Credit ratings that are assigned to entities also serve as a benchmark for financial market regulations.

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