An Analytical Study on Investors Perception towards Credit Rating Agencies

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Abstract- In the capital market including regulators, issuers and investors, Credit rating serves as a valuable input in the decision-making process of different participants. Therefore, in the field of finance it has been attracting the attention of thinkers to study various dynamics of this fast emerging subject. Various studies by different bodies and individuals and thus contributing a lot to explore new insights into the concept of credit rating have been conducted in India as well as in different parts of the world. The area of concern of the studies conducted in the Indian context as well as at the global level and the extent of awareness among the investors, about the concept of credit rating so far has mainly to find out the relevance of credit rating. There are, at present, five Rating Agencies in India which offer services of Rating and assessment agency (ONICRA) is working in India for investment in lieu of reliability, credibility, transparency, clarity and the risk associated with the companies. The present study examined the perception of investors towards the rating of financial instruments for long term investment. For this study total 200 investors were selected from Indore City.

Keywords: Credit Rating, Credibility, Transparency, Risk Involved, Clarity.

I. Introduction

The increasing number of financial instruments and ever the expansion of financial markets has given an opportunity to investors for a large sum of amount in the best companies and in this way they can observed through rating system of the companies. This present environment is very competitive and these companies take money directly from the market. So it provides various options to investors to make a choice of company as there are so many financial avenues and each avenue have a good reputation and goodwill. Now it is need of investors to take help from such credit rating agencies to avoid such fraud cases.

Therefore, investors need a agency that have reliability and credibility so that they can trust them and making their decision for investment. (Singh, 1996). Thus, the main purpose of credit rating is to provide investors the real information about the rating of credit agencies so that they can compare the risk associated with the companies on the comparative basis. The capital market is very open to all the companies who wants to survive and earn good profit through the incorporate the confidence among the investors. (Arora, 2003).
1.1 Characteristics of a Good Credit Rating System

Credit rating system is an effective tool for investors to make a decision about the investment and it regulates the system in likely manner. Hence, there are many elements which is an essential to know what are the characteristics behind this system is as follows-

Credibility: The rating system have the credibility to impart the information to the investors equally without any discrimination. It must have a sense of professionalism and the information has a system of updation. The credit agency have some norms so that the risk would be minimized and through the reviews of this agency the investors can understand the crux of reality. Through the circulation of periodicals, magazines, journals, working papers, the information disseminates among the investors In the words of Wilson (1994), —the credit rating agency have bear the name and year to reflect the authenticity of information (Gurusamy, 2004).

Clarity & Transparency: The information have transparency and no hidden issues are carried out and at the same time the things have a clarity so that it would be understood by the investors. In this way the risk would be minimized because these have a transparent system. If any change is seen it means immediately it should be updated to sustain the transparency. The information should not be contradict.

Disclosure Requirements: The credit rating company needs the essential disclosure from the investors so that these can provide all the required information about the investors.

Need of Educated Investors: For this company needs educated investors as they are capable enough to understand the basic information easily. The main purpose of these companies to impart the information but that should be understood by the investors clearly and for the education is the first and the foremost requirement. If the investors is educated then definitely the rating would reach at higher rank as they know the credibility of the agency.

Soundness: The information given by credit rating agencies must have sound in content of information and there should be criteria that would be fulfilled by investors for incorporating their name in the ratings. The analysis of agencies is perfect and no exaggerations are carried in it.

Thus, the credit rating agencies assessed the ranking of companies depending upon its capital, risk associated, margin of profit, number of shareholders, and assign rank according to their inner worth. The market structure is perfect competitive so there are many players in the market and every player have their own strategy to attract the investors so that they can invest a good amount. There is competition between public and private companies and investors choose those company which offers a good return on their investment. Thus, in this way the companies have assigned the rank on the basis of grades and it would be very easy for investors to observe the best company for investment. These grades are: grades are symbolically represented, viz. A, AA, AAA, etc.) (Jain and Sharma, 2008).

Benefits to Investors:

The investors can weigh the ratings as it adds to the structure and system of trading market for advantages of securities. Credit rating agencies provide various benefits to investors:
Credit rating agency provides the real information and the grades are given in this sense there is an easy for investors to select the best company on the basis of grades. By looking at the grades, investors can assess the risk involved in investment.

With the help of credit rating investors can take quick decisions about the investment in any particular security of the company.

Credit rating reduces the dependence of investors on agents as the portal is enough to provide the whole information and knowledge about the company.

The investors receive the security of their investment.

The highly qualified professional dose the rating analysis after the scanning the whole environment economically and monetarily.

### 1.2 Effects of India’s Demonetization as per Moody’s Rating

Withdraw all INR 500 & 1000 notes by the Government of India affect all sectors of economy with banks the key beneficiary. In the longer term the measures in the near term will pressure GDP growth and revenues of Government of India. There is a need to boost the revenues and translate into higher Government capital expenditure and fiscal consolidation. Corporates those directly exposed to retail sales are influenced by lower sales volume and cash flows. Moody’s concluded that demonetization is beneficial for Indian Government and Banks Moody’s remarked that in short period, definitely demonetization had disrupted economic activity resulting in temporarily weaker consumption and GDP growth.

### Rating Symbols

Rating symbols are indicators of the opinion/assessment of credit rating agency regarding superiority of credit or credit quality or grade of the debt obligations or instruments. The rating agencies have standardized rating nomenclatures for long-term ratings, short-term instruments, medium-term ratings, etc. The comparative analysis of the symbols used by various credit rating agencies is shown in Tables given below:

<table>
<thead>
<tr>
<th>CRISIL</th>
<th>ICRA</th>
<th>CARE</th>
<th>Remarks</th>
</tr>
</thead>
<tbody>
<tr>
<td>AAA</td>
<td>LAAA</td>
<td>CAREAAA</td>
<td>Highest Safety</td>
</tr>
<tr>
<td>AA</td>
<td>LAA</td>
<td>CAREAA</td>
<td>High Safety</td>
</tr>
<tr>
<td>A</td>
<td>LA</td>
<td>CAREA</td>
<td>Adequate Safety</td>
</tr>
<tr>
<td>BBB</td>
<td>LBBB</td>
<td>CAREBBB</td>
<td>Moderate Safety</td>
</tr>
<tr>
<td>BB</td>
<td>LBB</td>
<td>CAREBB</td>
<td>Inadequate Safety</td>
</tr>
<tr>
<td>B</td>
<td>LB</td>
<td>CAREB</td>
<td>High Risk</td>
</tr>
<tr>
<td>C</td>
<td>LC</td>
<td>CAREC</td>
<td>Substantial Risk</td>
</tr>
<tr>
<td>D</td>
<td>LD</td>
<td>CARED</td>
<td>Default</td>
</tr>
</tbody>
</table>

**Table 1: Rating Symbols for Long Term Instruments**

From the table 1, it has been evident that all these three rating agencies use similar rating symbols for long term instruments. The long term instruments are divided into two groups; investment group and hypothetical group. The symbols from AAA to A denote the investment group ranges from the highest safety to adequate safety and the second one group is speculative means that symbols from BBB to B presents from moderate safety to high risk.
and the last two C & D based on the speculations of market. Hence, for investment the first three ratings are safe and investors are in comfortable zone.

**Rationale of the Study**

Companies are turning towards the market for their short-term and long-term financial requirements instead of conventional method of looking at the banks and financial institutions. The investors cannot easily compute and compare the associated risk with an array of financial instruments available in the market. Assessment of associated risk, therefore, calls for a scathing expertise. Hence, the assessment and evaluation of risk is carried on in India, as in other parts of the world, by a group of experts who possesses the specialized skills. Credit Rating occupies a significant place in the investment arena as the entire exercise is centred on assessment and grading of financial instrument. However, the importance of Credit Rating cannot be judged by the volume of business the Rating Agencies do but on the quality of Rating and its acceptance by the investors. It helps the investors for moving the depth of CRAs so that they can invests their hard earned money and hope a good returns. So, education is one of the important determinants in understanding the real concept of CRAs.

**LITERATURE REVIEW**

Bhushan, Himashu (2013) pointed out that Credit rating agencies (CRAs) exist to primarily evaluate the creditworthiness of corporate borrowers who directly seek funds from the public without going to a bank. This study seeks to review the developments of CRAs in India, taking into consideration the recent global financial crisis.

Bayar, Yımaz (2014) explained that Credit rating business firstly emerged in the United States in 1900s and became a part of global financial system together with globalization of financial markets as of mid-1970s. The study evaluates that the new rules and regulations on the credit rating agencies will probably do well in increasing transparency and accountability of the credit rating agencies and decreasing over-reliance on credit rating agencies.

De Meijer, Carlo R. W.; Saaf, Michelle H. W.(2015) discussed about the credit crunch that is negatively impacting not only the financial markets, but also the global economy. Although this crisis can (justifiably) be blamed upon all parties involved (deal structures, banks, investors, etc.), a large part of the credit crisis has been blamed on the credit rating agencies (CRAs) that play a vital role in global securities and banking markets.

Rao. D., Sanjeeva, Sudhakar, A. (2017) discussed in their study that Rating is an important component for individual investors for their security and assurance of returns on bond instruments. The Ratings are assigned by Credit Rating Agencies showing the credit worthiness of issuer companies. It is only an advice but not a recommendation. In the present study, Credit Rating and Information Services of India Limited (CRISIL), Investment Information and Credit Rating Agency of India Limited (ICRA), Credit analysis and Research limited (CARE), Fitch Ratings, Brickwork Ratings India Private Limited financial indicators such as Revenue, Profit Before Tax, Earnings per Share, Net worth, Dividend, Market Capitalization, Number of Employees and Revenue per employee are focused. The result revealed that there is significant difference between dividend pay-out ratio, Earnings
per share and Profit before tax of CRISIL, ICRA and CARE, Fitch, Brickwork Ratings. It is the rating component which is for any investor to take decisions to invest in debt instruments which is assigned by rating agencies.

**OBJECTIVES OF THE STUDY**

To study the perception of investors towards CRAs in terms of education for the credibility and reliability.

**HYPOTHESIS OF THE STUDY**

H₀₁: Education wise there is no significant difference in the perception of investors towards credit rating agencies for evaluation of long term financial instruments with respect to credibility and reliability.

**RESEARCH DESIGN**

Research Approach: Descriptive research was used.

Sample Universe: For this study, Indore city is selected as a research area.

Sampling Method: Purposive sampling was used in order to select those investors who have an understanding of CRAs.

Sample Size: 200 Investors

Tools for Data Collection: Self-Structured Questionnaire which was prepared on the basis of previous studies.

Data Analysis: One Way ANOVA was applied on SPSS 20.0

**RESULTS & DISCUSSIONS**

H₀₁: Education wise there is no significant difference in the perception of investors towards credit rating agencies for evaluation of long term financial instruments with respect to credibility and reliability.

<table>
<thead>
<tr>
<th>Dimension</th>
<th>Education</th>
<th>N</th>
<th>Mean</th>
<th>Std. Deviation</th>
<th>F</th>
<th>Sig.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Credibility</td>
<td>Graduate</td>
<td>65</td>
<td>31.25</td>
<td>9.49</td>
<td>5.675</td>
<td>.001</td>
</tr>
<tr>
<td></td>
<td>Postgraduate</td>
<td>75</td>
<td>34.65</td>
<td>7.75</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Professionals</td>
<td>60</td>
<td>39.83</td>
<td>6.22</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Total</td>
<td>200</td>
<td>35.24</td>
<td>8.24</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Reliability</td>
<td>Graduate</td>
<td>264</td>
<td>17.92</td>
<td>4.90</td>
<td>4.348</td>
<td>.008</td>
</tr>
<tr>
<td></td>
<td>Postgraduate</td>
<td>126</td>
<td>18.39</td>
<td>4.48</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Professionals</td>
<td>119</td>
<td>19.17</td>
<td>3.80</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Total</td>
<td>200</td>
<td>18.49</td>
<td>4.45</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Table 2: Age wise Analysis of Variance
From the table on mean of education group, it is disclosed that for the factor of credibility, the mean score 39.83 of professionals is the highest and the lowest mean score is 31.25 for the graduates. It means that professionals have depth understanding of CRAs and they are in view about CRAs a vital tool in measuring the financial performance of companies. The next factor reliability, the professionals have the highest mean 19.17 and the graduates have the lowest mean score that is 17.92 so it is perceived that for the factor of reliability, the professionals have relied on CRAs to examine the performance of companies for long term investment.

For the factor of credibility, education wise there was significant difference found. As P value came out .001 which is less than .05, hence the null hypothesis education wise there is no significant difference in the perception of investors towards credit rating agencies for evaluation of long term financial instruments with respect to credibility was rejected.

For the factor of reliability education wise there was significant difference found. As P value came out .008 which is less than .05, hence the null hypothesis education wise there is no significant difference in the perception of investors towards credit rating agencies for evaluation of long term financial instruments with respect to reliability was rejected.

CONCLUSION

This purpose of this study is to analyse the investors’ perception towards credit rating agencies which includes a thorough analysis of awareness on credit rating agencies, investors’ attitude towards performance of credit rating agencies in terms of credibility and reliability. The findings of this study examined the rating agencies in understanding the investors’ perception, to frame appropriate mechanism for avoidance of fluctuations in the ratings and adopt appropriate strategy to serve stakeholders in the capital market. The researchers made an attempt to analyse the consistency in rating grades and process and may guide the investors by giving clear ideas for their investment decision.

In spite of all the findings and criticisms, Rating services undeniably play a significant role in the enlargement of efficient market and protection of interest of investors, if rating agencies conduct their activities in true spirit. The rating agencies should take paramount care in initial rating as well as in supervision and surveillance. The market regulator should keep always an vigilant eye on the activities of Rating Agencies. Therefore, fostering a reliable and credible rating system in the light of increased complexities in the market is an inevitable necessity of the time. The Researcher is confident that both the parties’ viz., Rating Agencies and the Market Regulator (SEBI) possess the requisite qualities to incorporate the suggestions in their functioning.

Suggestions

On the basis of the findings of present study some suggestions have been given for improvements in future study as follows:

1. Credit rating agencies do not give any hundred percent reliability of their assessment but provide only an indication about the relative risk and capability of various instruments.
2. The only those ratings are disclosed and made public and are accepted by the issuer companies which are accepted by the rating agencies. But the study recommends to the credit rating agencies to publish even those ratings which are not accepted by the given companies.

3. The credit rating agencies should lay more emphasis on quantitative factors apart from qualitative aspects for rating which may not be more reliable and accurate.

4. At least when investment grade instruments default and fail accountability can be fixed on Rating Agencies. Hence, SEBI should encourage setting up of a few more Rating Agencies in India.

5. The competition among Rating Agencies increases the quality of Rating by avoiding oligopoly market as it exists today. However, it is suggested that the Rating Agencies should consider near market movements and indicate positive and negative outlook along with the grading based on fundamentals.

6. The Rating absolutely depends upon the credibility of Rating Agencies. Credibility is the only tool for sustainability.

References


