FSB Approves First Credit Rating Agencies

The Financial Services Board is pleased to announce that the first credit rating agencies to apply for registration under the Credit Rating Services Act ("the Act") have had their applications approved.

The agencies are Global Credit Rating Co. (Pty) Ltd and Fitch Southern Africa (Pty) Ltd.

The agencies made application in terms of the legislative requirements and these were reviewed before being approved by the Registrar of Credit Rating Agencies.

Applications for registration have also been received from Standard and Poor's and Moody's Investors Service and these will be processed early in 2014. They will be permitted to continue to provide credit ratings until their applications are finalised.

An important requirement of the Act is that for a credit rating agency to be able to continue issuing ratings in South Africa, it is obliged to seek regulatory approval of its application for registration by 17 December 2013. To this end, the Credit Rating Services department of the Financial Services Board has instituted all the steps necessary to assist with the registration process, including engaging and accommodating the agencies with their documentation and information requirements.

The Act was introduced in South Africa in response to the shortcomings identified during the financial crisis, where the G-20 group of nations committed to creating a globally-consistent regulatory framework for the credit rating industry. As a member and signatory of the G-20, South Africa passed and promulgated the Act which came into force on 14 January 2013. This Act ensures that registered credit rating agencies will work within the regulatory requirements of South Africa which are in line with international standards.

The object of the legislation is to foster responsible and accountable credit rating agencies, protecting the integrity, transparency and reliability of the credit rating process and published ratings and help reduce systemic risk in financial markets.

As at end October 2013, over 600 credit ratings were published by the various agencies operating in the Republic. It is recognised that rating agencies can increase the systemic risk of financial markets through unanticipated and abrupt rating action. Such ratings crises have the potential to lead to large market disruptions and have knock-on effects on a number of systemically important market participants.

Despite the vulnerabilities associated with rating actions, some comfort is obtained from the fact that a number of the entities are multi rated (especially in the banking sector) and should one CRA decide to withdraw from the market, investors and users of these ratings will have a fall-back position with regards to a credit rating.

As demonstrated during the financial crisis, reliance on external ratings to the exclusion of internal credit assessments can be a cause of herding behaviour and of abrupt sell-offs of securities when they are downgraded (“cliff effects”). These effects can amplify procyclicality and cause systemic disruption. The FSB will be working with users of credit ratings to reduce reliance on credit ratings and have investors be required to institute alternative internal credit assessment capability.

Given the different reporting templates used by the agencies the FSB will be working towards having a credit rating repository and information highway in place. This project is expected to synchronise reporting and enable the department to review the postings and ensure a proper account of credit ratings in the market.

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