SOLEMN DECLARATION – INDIVIDUAL ASSIGNMENT

Solemn declaration by student

73%

Module: Corporate Governance
Module Code: MBAA 811EC
Assignment No.: 1
Assignment due date:09 March 2020

I, ML Kau declare herewith that the assignment which I herewith submit to the North-West University as partial completion of the requirements set for the MBA degree, is my own work.

Signature of student: ML Kau Student number: 35884258

Signed at Germiston, Johannesburg this 06 day of March 2020

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1. Introduction

Credit rating agencies became well known in 1900's in the United States (US). At that time it became very crucial part of the international financial markets operating on an international scale from mid 1970's. Credit Rating Agencies (CRA) are capable of good functioning of financial markets in terms of degreasing lack of equality information between lenders borrowers. Some countries doubted the reliability of CRA, investigation was done as they have seen CRA as a part of crises. The US, European Union (EU) and international companies interrogated the running order of credit rating market and implement regulations to abolish the abnormalities in the market (Bayar 2014:49).

2. What is Credit Rating?

Credit rating is referred to a formal,self supporting opinion of borrower's capability to manage its debt obligations. This is called creditworthiness. John Moody the owner of Moody's credit rating mentioned creditworthiness of a government by retrieving two main characteristics: ability to pay and preparedness to pay.

2.1 Global Leading Credit Rating Agencies

There three main independent rating agencies: Standard and Poor (S&P), Moody Investor Services (Moody's) and Fitch IBCA (Fintch), but are many other rating agencies.

2.1.1 S&P

S&P is the American financial intuition organization. This organization history was discovered back in 1860. Henry Varnum Poor produced a book titled History of Railroads and canals in the US, and his book adhered to everything about financial and operational state of all rail road organization of US.

2.1.2 Moody's

Moody's is the second CRA worldwide. In the year 1900, John Moody produced his assessment called Moody's Manual of Industrial and Miscellaneous Securities and well known John Moody and Company. The publishing provided data associated with stocks and bond of financial organizations, government organizations, manufacturing, mining, utilities and food organizations.

2.1.3 Fintch

This organization was established by John Knowles Finch on the 24th December 1914 in New York City, and it was called Fitch Publishing Company. In December 1997 it was consolidated with London Based IBCA Limited. In the year 2000, obtained Chicago based Duff and Phelps Credit rating Company (Gonderim& Kabul, 2017:113).

3. The role of rating agencies internationally and nationally in the economy

3.1 Role of credit rating agencies in the international economy

Credit ratings areused to assess the financial firmness and determining the level of approach borrowers should be given a loan and financial obligation. Credit rating agencies issue investors with impartial analysis and self supporting evaluation of organizations and countries that publish such securities.

Credit ratings execute the following four functions:

- Prepares independent, special and quality information.
- Pledge substantial, complex, investigate to reduce costs to the users.
- Pay for greater faith to financial representation.
- Development of regulatory framework. (Parbhoo, 2015: 19)

3.2 Role of credit rating agencies in the national economy

From 2018 financial crisis, the role of credit rating agencies has been questioned in South Africa. Credit rating agencies provide gives handy information for investors sovereigns to stay in our country. In the past, the three credit rating agencies played crucial role in South Africa to get entrance to the international capital markets with fair costs. During the high rating times, South Africa has benefited low borrowing costs, but with recent downgrade the borrowing costs are started to rise.

Credit rating agencies investors raised concerns about the current state of the economy growth, weak balance sheets, state owned organizations, escalating government debts including political unreliability and policies including wide current deficiency account of South Africa (MamphoModise, 2016).

4. The regulatory framework within which credit rating function in South Africa

The International Organization of Securities Commission (IOSCO) provided statement of principles concerning activities of CRA in September 2003, followed by Code of Conduct essentials for CRA in December 2004 just a day before global financial disaster.

IOSCO made adjustment to the code of conduct basic essentials for CRA stated the role of CRA in rating of structured finance business and changes. The changes in the amended code are:

- Contemplation regarding the rating of structured securities
- Contemplation regarding self independence of CRA and ignorant of conflicts of interest
- Contemplation about responsibilities of CRA to investors and issuers (Bayar 2014:54).

The Act was evaluated in January 9th 2013 and commenced on the 15th April 2013. The Act is divided into the following chapters. Credit Rating ServiceAct 24 of 2012 stipulates that:

Chapter 1: Definitions

Chapter 2: Registration

Chapter 3: Duties of registered CRA

Chapter 4: Endorsement of external credit ratings

Chapter 5: Liability and independence of registered credit rating agencies

Chapter 6: Administration Act

Chapter 7: Enforcement and action and remedies

Chapter 7: Miscellaneous and general provision

Credit Rating Service Act 2012 revealed CRA to civil accountability. It appeared to be an attempt to make CRA's responsible for their neglectful ratings. Some observers have also called for 'independent responsibility' key personnel must be held liable for their negligence, these ideas were opposed by CRA's. Before Credit Rating Service Bill law implemented, lawmakers were prepared to make compromises but at the later stage it appeared that they need to be determined to make CRA more responsible for their actions. Section 2 of Credit Rating Service Act of 2012 stipulates five main objectives namely:

- To warrant responsibility and accountability of credit rating agencies
- Protect the rectitude, image and reliability of credit rating procedure and credit rating
- Enhance investor protection
- Enhance fairness, efficiency and picture of financial markets
- Minimize system risk (Rabinowitz, 2014: 31)

5. The use of code of conduct

The Credit Rating Services Act stipulates that, credit rating agencies mustacquire, issue, stick to code of:

- Acquire the principles that accommodate applicable international code of conduct stipulated by the registrar
- Describe the enforcement of code of conduct

Registered CRA must issue all changes to its code of conduct, also they must issue on a yearly basis any material deviation to the code of conduct prescribed by the registrar in subsection 1 (a) and reasons thereof.

6. The enforcement and mechanism

The Credit Rating Services Act stipulates that the enforcement committee may registrar notwithstanding in addition taking any step the registrar may tale under the Act that violation of the Act to the enforcement or not obey, apply to court

- Restraining persons from going on to commit any act or omissions
- Restraining persons from going on with carrying out such act next time.
- Demanding persons to take such remedial steps as the court of law confider necessary to correct the consequences of the act and exclusions.

Under offices and penalties persons, who don't comply with section 3(2), deceiving false statement of any materials and in the execution inflict by the Act, hand an auditor officer information which is wrong is guilty and may be sentenced to prison for a period not exceeding 10 years or both imprisonment or fine.

They have the right to appeal, that's where the registrar may make decision in terms of this Act. Any persons, who feel that he/she have been aggrieved by the decision made by the registrar, may apply for the appeal in this manner. Persons have the right to appeal in terms of section 26(A) of Financial Service Board Act.

7. Success and failures of mechanism

The evaluation of rating agencies can discourage or encourage the investment. Credit rating agencies are very crucial for investment with respect to the following:

- Most investors use their evaluation to decide whether to invest the money in a certain organizations and nation states
- For example, Regulation 28 of pension Funds, prevent pension funds being invested in junked states. In 2001, the US pension managers bought South African bonds due to good rating (State of Capture & Credit Rating Agencies, 2018:3)

CRA remains crucial, there's no replacement of information they give and make. To alleviate the often-adverse effects of taking this information, they should make it easy for the information to be accessible on the accuracy rating including all factors that impact the ultimate ranking as well as the data on which the rating is based

With the current downgrades to junk in South Africa, the country faces high costs in petrol and other imports (even though exports may benefit from weaker rand), high dent financing costs, decreased business confidence, and withdrawal by institutional investors whose funds may prohibit investments in countries with sub investments ratings. It is very crucial to take into account that 90% of our country's debt is rand dominated, this simply means that in the short to medium term a enfeeble rand should not impact remarkably on the debt to GDP ratio (South African Institute of International Affairs, 2017:6).

Furthermore this affect our country in many ways, for instance, the cost of borrowing is escalating and that makes things harder for South Africans to borrow the money from the banks. International funds will take the money out the country, therefore the capital will leave the money. The rand will be weak, and goods will cost more and lastly the treasury might be forced to increase taxes to draw money into the fiscus, to add on these social grants might be taken away to pay debts (Mlondi Mdluli, 2020)

8. Conclusion

Credit rating is referred to a forma, self-supporting opinion of borrower's capability to manage its debt obligations. Credit rating agencies provide gives handy information for investors sovereigns to stay in our country. In the past, the three credit rating agencies played crucial role in South Africa to get entrance to the international capital markets with fair costs. The International Organization of Securities Commission (IOSCO) provided statement of principles concerning activities of CRA in September 2003, followed by Code of Conduct essentials for CRA in December 2004 just a day before global financial disaster. With the current downgrades to junk in South Africa, the country faces high costs in petrol and other imports (even though exports may benefit from weaker rand), high debt financing costs, decreased business confidence, and withdrawal by institutional investors whose funds may prohibit investments in countries with sub investments ratings. It is very crucial to consider that 90% of our country's debt is rand dominated, this simply means that in the short to medium term a enfeeble rand should not impact remarkably on the debt to GDP ratio. Two Credit rating Agencies have downgraded South Africa due to economic conditions. Our government needs to do something about our economy otherwise we will end up being like Zimbabwe. Africa as a whole struggling and the, market is taken over by Chinese, something needs to be done about them, they want everything for free and they getting away with the murder.

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