FINANCIAL TIMES

July 1, 2012 10:03 pm

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Esma probes agencies' views on banks

By Brooke Masters in London

The pan-European markets regulator has launched a probe into the way the big three credit rating agencies evaluate banks to determine if the process is sufficiently rigorous and transparent, its chairman Steven Maijoor told the Financial Times.

The European Securities and Markets Authority has begun inspecting Standard & Poor's, Fitch and Moody's Investors Service and expects to finish by the end of the year.

Credit rating agencies were not regulated in Europe until last year, when the European Union began requiring them to register with Esma. The rating agencies have attracted harsh criticism first for their overly rosy opinions of structured products and banks before the financial crisis and more recently for their mass downgrades of sovereigns and financial institutions amid the eurozone crisis.

"Bank ratings are very important because there is an interaction with sovereign ratings and government bonds," Mr Maijoor said.

Moody's downgraded 15 global banks last month (Nomura and Macquarie had already been downgraded), and S&P took a similar step late last year, downgrading 15 of the top 37 global banks in November after changing its methodology.

Esma, which is less than two years old, has never taken an enforcement action. But rating agencies must be registered and in good standing with the watchdog to operate in Europe, so its concerns cannot be ignored.

Mr Maijoor said the mass downgrades raised "concerns about whether there are sufficient analytical resources" at the rating agencies.

"This is an area where there have been many ratings changes in the past weeks and years. That raises issues of whether there is sufficient resource and expertise to cope with the additional work."

"A bloc rating change cannot be an excuse to spend less time. It is still important that each individual rating gets the same level of attention to detail and analysis," Mr Maijoor said.

He said Esma was not attempting to influence the actual ratings. "This is not rating the ratings. We are not putting restrictions on the methodology. We only ask that their choices make economic sense and be logical."

As a new regulator, Esma is still building its resources. Its credit agencies unit has 14 people and hopes to have 20 by the end of the year. They are charged with supervising 17 rating agencies. Mr Maijoor said the watchdog was taking a risk-based approach and would focus this year on bank ratings at the big three and compliance functions across the board.

S&P, which is owned by McGraw-Hill, said it "looks forward to explaining to Esma, as part of its regular inspection programme, the steps we have taken to maximise the transparency, quality and consistency of our bank ratings".

"Our new criteria provide a clear guide to how we rate banks and what might cause ratings to change, and we are proud of the strong track record of our bank ratings in the region as indicators of default risk," it said.

Fitch and Moody's declined to comment.