



# RAEX Europe

## Introductory presentation

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# Agenda

- About RAEX
- What is credit rating and CRA?
- How CRAs are regulated: EU vs. Russia
- Case study: sovereign risks in the CIS region



# About RAEX

# RAEX-group

- International group of independent rating agencies:
  - ✓ **RAEX-Moscow (since 1997)**, registered by the Russian Central Bank, one of the two national rating agencies in Russia, the oldest and the largest CRA in Russia
  - ✓ **RAEX-Kazakhstan (since 2008)**, the agency recognized according to the local regulatory standards, located in Almaty
  - ✓ **RAEX-Europe (since 2013)**, the European rating agency located in Frankfurt am Main

# RAEX-Europe: who are we?

- Active since **2013 in Frankfurt am Main**;
- **Registered** as a credit rating agency by the European Securities and Market Authority (ESMA) on the 1<sup>st</sup> of December 2015;
- **Official status** of “External credit assessment institution”;
- Advanced multinational **rating service team** with diverse academic and professional background;
- Reputable **advisory board**, stringent **compliance** procedures and experienced **review function**.

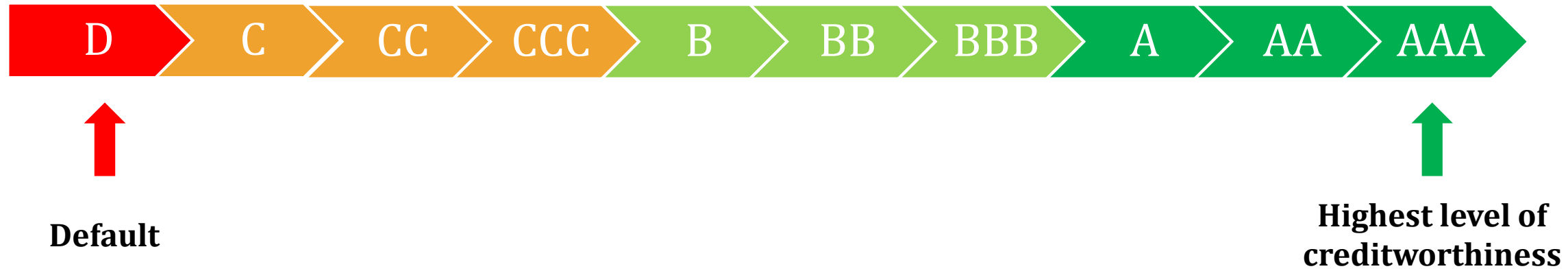
# RAEX-Europe: what are we doing?

- Assigning **credit ratings** to:
  - ✓ Sovereign issuers;
  - ✓ Sub-sovereign issuers (regions);
  - ✓ Banks;
  - ✓ Insurance companies;
  - ✓ Non-financial companies.
- Assigning non-credit ratings: **ESG ratings** (environmental, social and governance);
- **Business-conferences** and **presentations** in Frankfurt am Main.

# What is credit rating and CRA?

# What is a credit rating?

- Credit rating of an entity represents the opinion of the Rating Agency on its ability to fulfill its financial obligations **in full** amount and in a **timely manner**.
- Typical **rating scale**:





# Who issues credit ratings?

- Credit rating agency (CRA) is a legal entity which issues **credit ratings** on a **professional basis**\*;
- Most developed financial markets (e.g. US and EU) CRAs are **subject to a strict supervision**;
- CRAs **must have**: approved methodologies; “Chinese wall” separation between analytical and sales units; stringent compliance practices; team of highly-qualified analysts; independent review function; etc.

\* CRA 1 (Regulation (EC) No 1060/2009 of the European Parliament and of the Council of 16 September 2009 on credit rating agencies)

# Why do entities need a credit rating?

## Debt issuance

- Company can reduce the cost of funding and raise more funds when issuing debt

## Loans from banks

- Presence of credit rating can improve conditions for the bank loan

## Listing on stock /bond exchange

- Rating can help to attract more investors
- Issuers are required to be rated in order to be listed on some stock exchanges

## Market entry

- Entities must have a credit rating in order to operate in some markets (i.e. public funds' transaction in the case of banks)

# Why do entities need a credit rating?

## Investor relations

- Credit rating is an independent professional assessment of a company's financial stance

## Counterparty assessment

- Credit rating enhances transparency whereby preventing counterparty credit risk realizations

## Compliance with legal requirements

- For regulated markets, such as banks, credit ratings are used for regulatory purposes (credit quality steps)

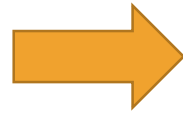
## PR

- All ratings are published in media and professional databases, hence can improve entity's public image
- Public credit rating underpins the entity's reliability for customers and counterparties

# How credit ratings are assigned?



Signing rating agreement with rated entity or related party.



Submission of questionnaire and supporting information by the entity.



Analysis of information:

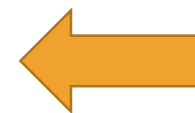
- Processing of information
- Rating interview
- Expert assessment



Discussion of results in the Rating Committee and voting.



Coordination with the entity. Report is sent to the client indicating the main factors affecting the rating.



Disclosure. The entity has two alternatives:

1. Accept the rating and agree on its disclosure.



2. Sign Non-Disclosure Agreement and keep the rating non-public.

# How CRAs are regulated: EU vs. Russia

# European Union

- **Reasons:** In the period leading up to the financial crisis in 2008, CRAs failed to properly appreciate the risks of some complex financial instruments. In addition, certain European countries were faced with abrupt bond sell-offs following downgrades of their credit ratings by big CRA;
- **Response:** EC made proposals to strengthen the regulatory and supervisory framework for CRAs in the EU, which were meant to restore market confidence and increase investor protection;
- **Key steps:**
  - ✓ **2009:** regulatory framework for CRAs and regulatory oversight regime on national level (for example, BaFin for Germany);
  - ✓ **2011:** creation of the European Securities and Markets Authority (ESMA), which supervised CRAs registered in the EU;
  - ✓ **2013:** improvement of regulation in relation to sovereign debt credit ratings.

# Russia

- **Reasons:**

- ✓ **Internal:** Transferring of supervision of the whole financial market from various government bodies to the Central Bank of Russia (“mega regulator” concept);
- ✓ **External:** The downgrade of the sovereign credit rating of Russia following the sanctions in 2014 by three largest CRAs led to a downgrade of a large amount of credit ratings of Russian companies. This affected the regulated financial markets within the country.

- **Response:** the CBR initiated the rating industry reform in order to avoid influence of foreign CRA’s decisions on Russian financial markets, increase industry standards and improve transparency of CRAs

- **Key steps:**

- ✓ **2015:** Federal law №222-FZ (The framework regulation of CRAs) and additional regulations
- ✓ **2016:** Improvement of requirements for CRAs; Registration of two CRAs in Russia
- ✓ **2017:** Coordination of all regulations related to credit ratings; end of transition period.

**!Before reform: 7 CRAs in Russia (including 3 international); After reform: only 2 national CRAs**

# Example of assessment: sovereign risks in CIS region

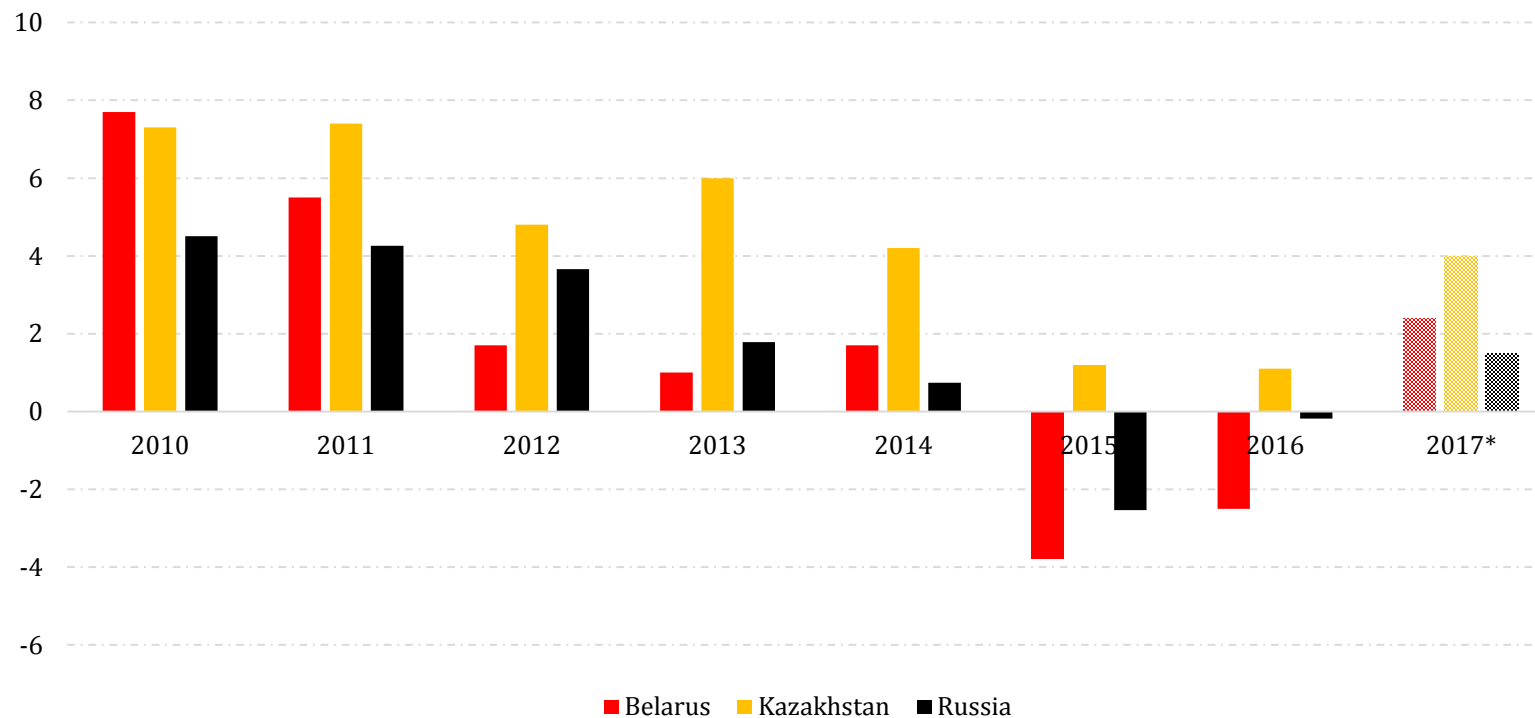


# RAEX-Europe sovereign rating list:

Country	SGC		CCE*		Dynamics	Date
	National currency	Foreign currency	National currency	Foreign currency		
USA	AAA	AAA	AAA	AAA	Confirmed	17.11.2017
Germany	AAA	AAA	AAA	AAA	Confirmed	15.09.2017
China	A+	A+	A+	A+	SGC downgraded/ CCE confirmed	17.11.2017
<b>Russian Federation</b>	<b>BBB-</b>	<b>BBB-</b>	<b>BBB-</b>	<b>BBB-</b>	<b>Confirmed</b>	<b>12.01.2018</b>
<b>Kazakhstan</b>	<b>BBB-</b>	<b>BBB-</b>	<b>BB+</b>	<b>BB+</b>	<b>Confirmed</b>	<b>12.01.2018</b>
Cyprus	BB+	BB+	BB+	BB+	Upgraded	06.10.2017
Armenia	BB-	BB-	B+	B+	Upgraded	26.01.2018
Kyrgyzstan	B	B	B-	B-	Confirmed	19.01.2018
Uzbekistan	B+	B	CCC+	CCC	Confirmed	22.09.2017
<b>Belarus</b>	<b>B</b>	<b>B-</b>	<b>B-</b>	<b>CCC+</b>	<b>SGC confirmed/ CCE upgraded</b>	<b>26.01.2018</b>

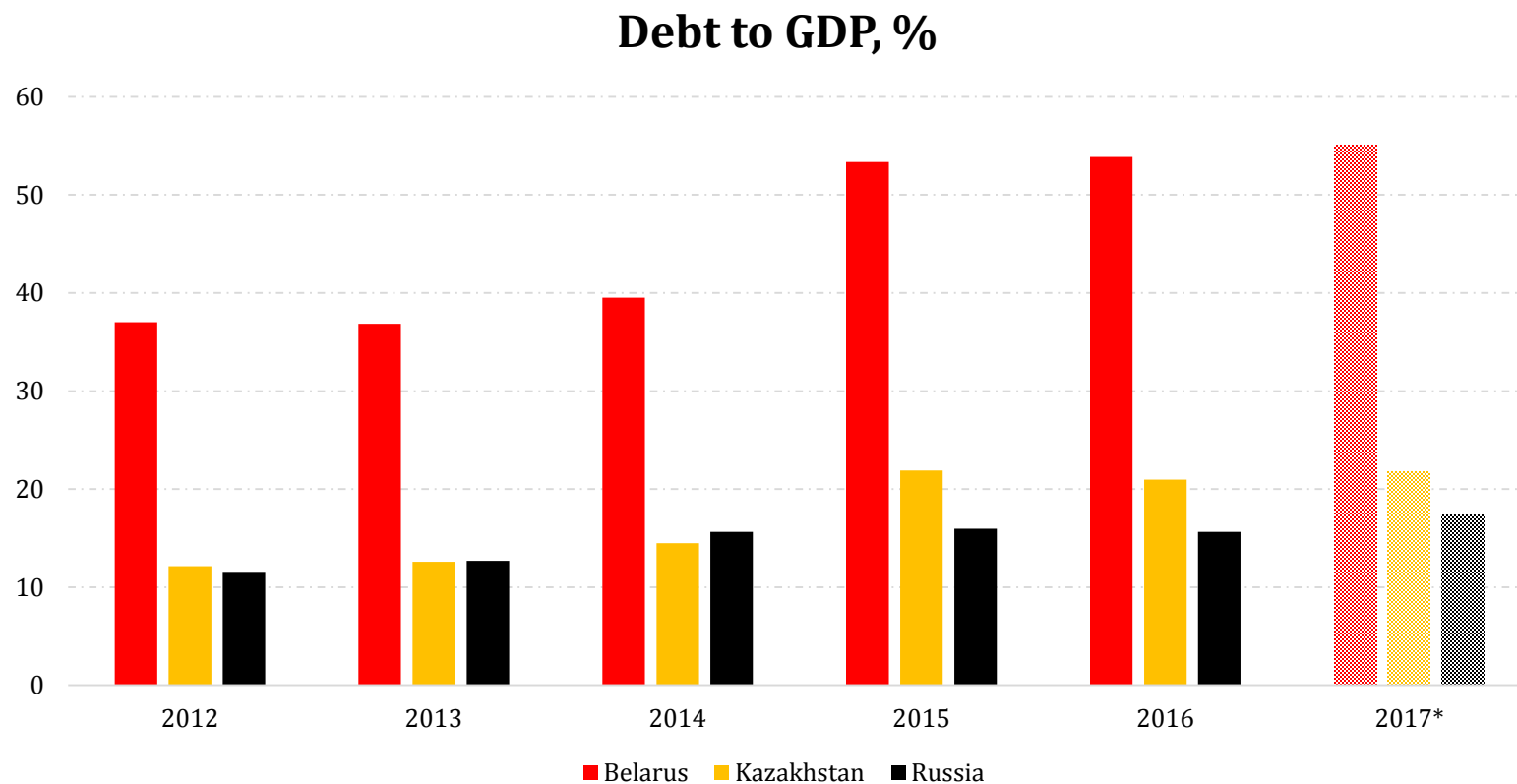
# Economic growth: Russia's economy in comparison with economies of the biggest regional partners showed the lowest growth rate in 2017

Real GDP growth, %



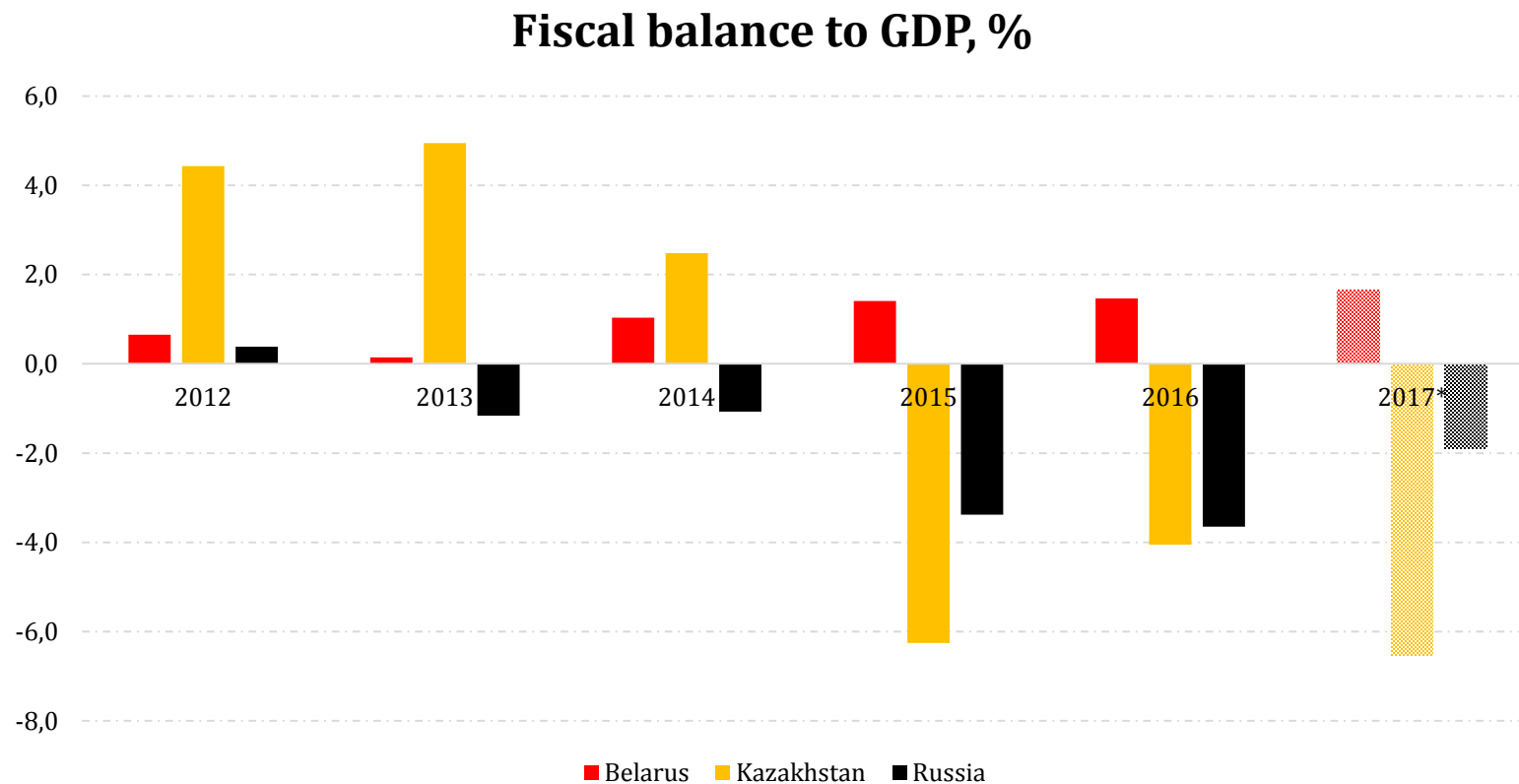
Source: RAEX (Europe) calculations based on data from Belstat, Rosstat, Statistical committee of RK.<sup>18</sup>  
 2017 – preliminary data.

# Debt: Belarus kept being the most indebted country in 2017, lacking sizable FX-reserves



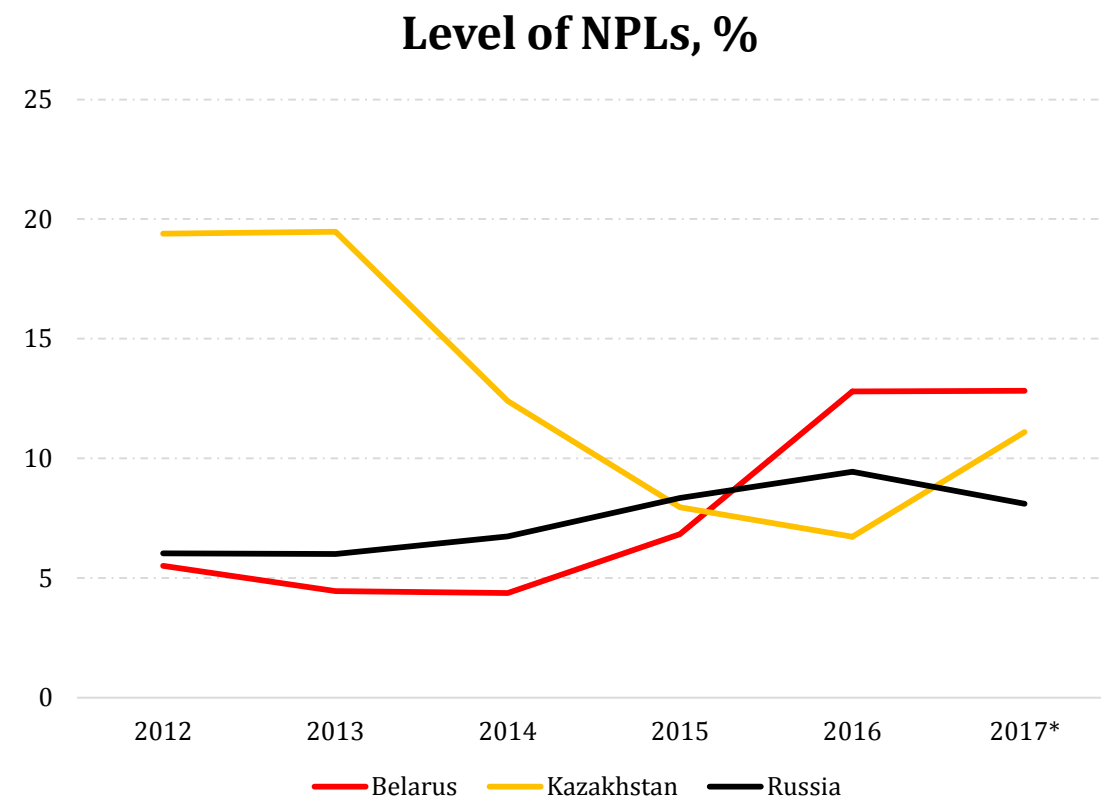
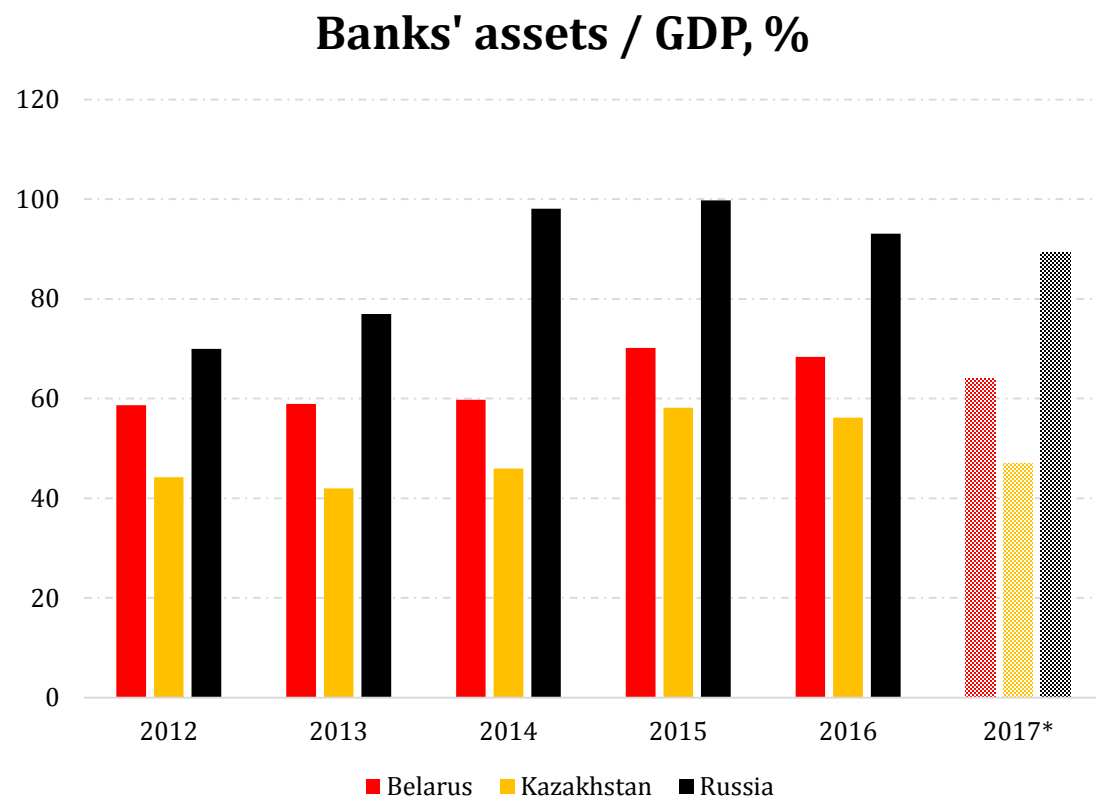
Source: RAEX (Europe) calculations based on data from IMF, WB, Local MFs. 2017 – preliminary data.

**Fiscal position:** Belarus showed a de jure fiscal surplus, which de-facto was distorted by off-balance operations; Kazakhstan increased deficit subsidizing economic growth



Source: RAEX (Europe) calculations based on data from IMF, WB, Local MFs. 2017 – preliminary data

# Banking system: Russian banking system remained moderately stable despite recent incidents, while banking systems of Belarus and Kazakhstan were more fragile



Source: RAEX (Europe) calculations based on data from IMF, WB, Local CBs. 2017 – preliminary data. 21



# Thank you for your attention!

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