

The Licensing Examination for Securities and Futures Intermediaries

Paper 10 Credit Rating Services

Syllabus

Topic 1: Overview of credit as a financial discipline

- 1 What is Credit?
 - From a legal perspective
 - From an economic perspective
 - From a social perspective
- 2 Credit (debt) as a financial investment
 - Fundamental difference from equity
 - Different types of basic credit products
 - Implicitness of credit in all financial transactions
- 3 Financial asset risk: a function of certainty
 - Credit risk and market risk: similarities and differences
 - Credit quality and risk tolerance
 - Statement of financial position, income statement and cash flow statement
 - Debt capital markets

Topic 2: The credit rating industry

- 1 Credit rating as a relative measure of credit risk
 - Credit ratings as a measure of payment certainty
 - Credit ratings as default risk grading
- 2 How credit ratings respond to the market environment
 - The evolution of key rating distinctions
 - Key developments that drive rating processes and products

- 3 Who makes credit ratings?
 - Credit rating agencies as the neutral provider of credit value
 - The quasi-regulatory role of CRAs
 - The “Majors” and their rating scales
 - Other types of CRAs and credit analytics providers
 - The credit rating agency industry today

Topic 3: The credit rating process

- 1 Elements of the credit rating process
 - Inside the CRA: internal organization of duties and workflow
 - Source material used in the rating analysis
 - What rating agency analysts do
- 2 Quality control issues
 - Independent role of the credit rating agencies
 - Internal sources of quality control
 - External sources of quality control
 - Principles of integrity, transparency, responsibility, good governance in action
- 3 Institutionalizing surveillance, back-testing, reporting and record-keeping
 - Duties of the rating agency as an independent provider of credit quality
 - Surveillance, back-testing, reporting and record-keeping: internal quality controls
 - External regulation on CRA self-evaluation
- 4 Making and changing rating methodology or criteria
- 5 Addressing the needs of users of credit ratings
 - Who are users of credit ratings?
 - Fostering awareness of credit

ratings and their uses

- Explaining the basis of a rating
- Channels of communication
- Speaking to different constituencies
- Inappropriate communications
- Handling complaints

Topic 4: Corporate credit ratings

- 1 Analysing corporation credit quality
 - Balance sheet strength
 - Cash flow position
 - Management capacity and other intangibles
 - Industry-imposed constraints on growth and profitability
 - Covenants
 - Extensions of the corporate paradigm
- 2 Measures of corporate credit strength
 - Key ratios associated with corporate credit strength and ratings behavior
 - Industry-specific benchmarks
 - Case illustrations
- 3 Special topics for bank and financial institution analysis
 - Measures of financial institution health
 - Financial institutions and governments
 - Commercial and policy-oriented financial institutions
- 4 Benchmarking credit quality against aggregate measures
 - Bond default studies
 - Rating transition matrices
 - Option theoretic pricing
- 5 Keeping corporate credit rating freshness
 - Challenges to the going-concern assumption
 - Through-the-cycle versus

Point-in-time ratings

- 6 Rating corporations in emerging economies

Topic 5: Structured finance credit ratings

- 1 Key developments associated with the rise of structured finance
- 2 Defining structured finance and securitization
- 3 Types of transaction structures
- 4 Rating structured securities
 - How the process of rating structured securities differs from that of corporate bonds
 - Methodological differences between agencies
 - Methodological differences for different structural types
- 5 Benchmarking credit quality: structured securities
 - Rating performance
 - Risks to structured transactions performance

Topic 6: Sovereign credit ratings

- 1 Defining sovereign ratings
- 2 Basis of sovereign credit ratings
- 3 Methodological differences between the NRSROs
 - Balance sheet versus income-based approaches
 - Sovereign solvency and access to foreign exchange
 - Sovereign interference
 - The payment system
 - Domestic scale ratings
- 4 Do sovereign ratings work? Evidence from the rating agencies

Appendix A Glossary of key terms and concepts underpinning credit rating products and processes

Appendix B History of rating agencies in the
debt capital markets
