



JOINT COMMITTEE OF THE EUROPEAN
SUPERVISORY AUTHORITIES

Consultation Paper

Draft ITS On the mapping of ECAs' credit assessments under Article 136(1) and (3) CRR

Public hearing

London, 4 April 2014

General remarks

- Regulatory mapping (*recital 6 draft ITS*)
 - The mapping should be interpreted as the correspondence of the rating categories of an ECAI with a regulatory scale which has been defined for prudential purposes.
 - ➔ Subparagraph 1, Art. 136(1): “...*Those determinations shall be objective and consistent.*”
Empirical evidence-based approach
 - It does not provide an equivalence of rating categories across ECAIs
- Alignment of CRR and CRA terminology (*recitals 1, 2 and 7 draft ITS*)
 - Only CRA-compliant “credit ratings” are mapped
 - Mappings are provided for each “rating scale” of the ECAI
- Existing framework (*recital 4 draft ITS*)
 - Annex 2 of the ‘Basel II: International Convergence of Capital Measurement and Capital Standards: A Revised Framework - Comprehensive Version’
 - Part 3 of the ‘Revised Guidelines on the recognition of External Credit Assessment Institutions’

Steps of the mapping exercise

1. Quantitative framework

1. Calculation of quantitative factors (*Art. 1 to 7 draft ITS*)
 1. *Centralised calculation (CEREP)*
 2. *Long run and short run default rates*
2. Comparison of quantitative factors with benchmark values (*Annex I draft ITS*)

Initial mapping proposal

2. Qualitative framework

1. Assessment of qualitative factors (*Art. 8 to 14 draft ITS*)
2. Comparison of qualitative factors with reference values (*Annex II draft ITS*)
 1. *Meaning and relative position*
 2. *Time horizon*
 3. *Default definition*

Review of the initial mapping proposal

Quantitative factors

1. Sufficient number of credit ratings is available (*Chapter 1, Section 1 draft ITS*)
 1. Own rated items (*Articles 2 to 4 draft ITS*)
 2. Other items (*Article 5 and 6 draft ITS*)
 1. Externally rated items
 2. Scored items

2. Sufficient number of credit ratings is NOT available (*Chapter 1, Section 2 draft ITS*)
 1. Own rated items (*Article 7 draft ITS*)
 1. Internal estimate of long run default rate by ECAI
 2. Empirical evidence of rated items, even if scarce
 3. Degree of prudence

Benchmark values

1. Long run default rate benchmark (*Part 1, Annex 1 draft ITS*)
 1. Role: assessment of the level of risk and consequently of the corresponding RW
 2. Draft ITS provides intervals (Basel II and CEBS texts only contained point values)
 1. Large number of ECAs (currently 25)
 2. Increase the objectivity and consistency of the results

2. Short run default rate benchmark (*Part 2, Annex 1 draft ITS*)
 1. Role: early warning system
 1. The breach should be **material**
 2. The breach should be **systematic**
 3. The breach should **not** be **exogenous** (avoid pro-cyclicality)

Qualitative factors

1. Definition of default (*Article 9 draft ITS*)
 - Focus on bankruptcy events
 - Reference stemming from data of international ECAIs used by Basel text
2. Time horizon (*Article 10 draft ITS*)
 - Only relevant when quantitative data is not available
 - PIT high/low ratings are more likely to be downgraded/upgraded
3. Meaning and relative position (*Article 11 draft ITS*)
 - Applicable to near-to-default rating categories
 - Applicable when sufficient default data for the adjacent rating category
4. Creditworthiness of items (*Article 12 draft ITS*)
5. Internal estimate of the long run default rate (*Article 13 draft ITS*)
 - In practice, equivalence with international rating scale will be used
6. Internal mapping between rating scales (*Article 14 draft ITS*)
 - Very useful to indirectly derive the mapping of 'secondary' rating scales

Summary

1. Regulatory mapping

1. Focus on risk from the perspective of banking regulation (CRR)
2. Framework already established (Basel and CEBS)

2. Importance of the consistency of the results

3. Empirical evidence-based approach

1. Incentives to provide as much information as possible
2. Incentives to establish internal validation procedures