The Association of Corporate Treasurers

Comments in response to
Criteria Report, Exposure Draft on
FitchRatings – Proposed Revision to Short-Term Rating Scales
October 2006

November 2006

The Association of Corporate Treasurers (ACT)

Established in the UK in 1979, The Association of Corporate Treasurers is a centre of excellence for professionals in treasury, including risk and corporate finance, operating in the international marketplace. It has over 3,600 members from both the corporate and financial sectors, mainly in the UK, its membership working in companies of all sizes.

The ACT has 1,500 students in more than 40 countries. Its examinations are recognised by both practitioners and bankers as the global standard setters for treasury education and it is the leading provider of professional treasury education. The ACT promotes study and best practice in finance and treasury management. It represents the interests of non-financial sector corporations in financial markets to governments, regulators, standards setters and trade bodies.

General

The ACT welcomes the opportunity to comment on this matter. Contact details are provided at the end of this document.

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Overview

We are pleased to have an opportunity to respond to your paper "Proposed Revision to Short – Term Rating Scales". Our comments reflect the considerations of an issuer, although the issuer view must itself take account of the investor perspective and the overall functioning of the market.

In summary, our understanding is that the proposal involves assigning separate short-term issuer and instrument ratings formalising the incorporation of recovery given default considerations within short-term ratings of instruments.

Response to specific questions

For ease of reference we have responded directly to the questions you have raised with additional comment where appropriate.

- *Do you use short-term ratings primarily for counterparty use (issuer rating) or for instrument analysis (instrument ratings)?* Issuers of short-term debt instruments would have an expectation that investors are concerned with both elements but it is difficult to be prescriptive as to investors' specific motivations. The paper also highlights certain circumstances when there will be a formal divergence in issue ratings - e.g. bank deposits – where investor behaviour would be expected to favour the more positive rating.

- *Do you agree that investment grade short-term ratings should be based on 'sustainable liquidity' and that non-investment grade ratings should be based on 'actual expected liquidity' over the following 13 months?* Our view would be that greater significance should be given to 'sustainable liquidity' in most circumstances. However given the time-scale of a short-term rating, we would query the relevance of the distinction between 'sustainable' and 'actual expected' liquidity.

- *Should short-term instrument ratings just reflect default and liquidity risk <u>or</u> should they take the 'expected loss approach' and include an element of recovery given default?* This will depend on investor preference but our view would be that if issue specific ratings are to convey any additional information as compared to the issuer rating then they should incorporate the effects of recovery.

- *Should Fitch's short-term investment grade ratings be available for issuers who are non-investment grade long term?* There is no clear reason why non-investment grade issuers should be denied a notching up into an investment grade short-term rating if that instrument has demonstrable liquidity or exceptional recovery prospects from asset backing or other sources.

- *Is there scope for a new short-term rating level of F4 for strongly liquid non-investment grade names?* This will depend on investor demand for the instruments issued by these issuers, however we believe that making this sort of subtle distinction would be confusing to the market and not helpful.

Our conclusion would be that extending the use of Issuer Default Ratings and clarifying that issue specific rating incorporate a weighting for recovery given default expectations serve a useful purpose of supplying the market with additional information in a manner that is already well understood for long term ratings.

Contacts: John Grout, Policy and Technical Director (020 7213 0712; jgrout@treasurers.org) Martin O'Donovan, Assistant Director, Policy and Technical (020 7213 0715; modonovan@treasurers.org) Peter Matza, Policy and Technical Officer (020 7213 2033; pmatza@treasurers.org)	The Association of Corporate Treasurers Ocean House 10/12 Little Trinity Lane London EC4V 2DJ Telephone: 020 7213 9728 Fax: 020 7248 2591 Website: http://www.treasurers.org