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Ms Ingrid Bonde
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Committee of European Securities Regulators
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Via email: rgarcia@cesr.eu

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Consultation on the Role of Credit Rating Agencies in Structured Finance

Dear Ms Bonde,

we would like to take the opportunity to make some remarks to the discussed role of the rating agencies in the so-called subprime crisis.

Founded in 1987, Feri Rating & Research AG (Feri), with approximately 1,000 customers worldwide, focused on Germany, France and the United Kingdom, is a leading European rating agency specialized in ratings of investment markets and investment products. We are one of the largest commercial economic research and forecasting institutes in Europe. The key feature of Feri's rating procedures is a comprehensive approach with independent analysis and detailed, quantitative market forecasts. In contrast to the big players in the rating markets, Feri is not engaged in the credit rating business. We focus instead mainly on selected rating market niches.

Feri prepares market ratings for industries, countries, capital markets and real estate markets based on deep economic analyses and forecasts. In addition to our global industry analysis, Feri also produces real estate market reports. Our analysis of real estate markets throughout the world are used by our customers to understand property, portfolio, and indirect real estate (open-end and closed-end real estate funds) investment markets.

In the field of investment products, Feri rates investment funds in selected European countries, close-end funds for institutional investors, as well as for retail business, corporations and asset managers. In addition, Feri produces market studies of investment markets. These reports provide an overview of opinions and expected behavior of different kinds of investors.



With more than 60 employees, Feri is based in Bad Homburg, Germany, near Frankfurt, and has additional offices in London, Paris, and New York.

1. General

It is long understood that rating agencies play an important role in financial markets, as their organizations collect expert knowledge about market participants, their products and instruments, financial relations and their evaluation. Without independent assessments of rating agencies, trust and stability in the financial markets would even be more in danger. The current crisis is proof of this. Rating agencies are an indispensable part of modern capital markets and an essential element of the global financial system. This is true not only for the markets of structured finance, but increasingly also for the special market niches Feri is engaged in.

The current crisis demonstrates that the role of rating agencies must be strengthened. Reinvigoration of the rating system must be accompanied with measures to assure that rating markets function well. Governmental and supervisory institutions have vital interest in designing a proper framework for the rating industry.

2. Current Problems of the Rating Market

The current structure of the rating market could not prevent the current crisis. Transparency of rating processes and methodologies, monitoring of rating performance, CRA staff resourcing, and handling of conflicts of interest are key areas to be covered when reviewing the positive and negative aspects of the current self-regulatory regime, compared with a possible, formal, regulatory regime. Nevertheless, we believe that more attention must be drawn to some basic features of the rating market as it currently exist:

a) Lack of transparency

Ratings were developed and used to increase market transparency. They are a key factor in the decision-making process of investors, shedding light on the opportunities and risks involved in investments. In addition, ratings must allow lenders to identify credit risks in their financing activities. Transparency, public accessibility and insights into the rating results do not meet these standards today.

b) Duopolistic market structure

Dominating roughly 75 % of the global market for ratings of corporations, governments, financial institutions and structured finance, the current duopolistic structure carries with itself all the classic malfunctions known from any textbook regarding the abuse of monopoly status in any market.

c) Lack of research integration

Rating methods are based on more or less extensive research. It is our observation that risks related to a market in its entirety, are not adequately measured by looking only at individual securitizations. The



systematic risk from excess valuations and bubbles cannot be captured without an extensive research of the macroeconomic environment.

d) US bias

Currently, the rating systems of the big players represent more or less the US style of financial markets. They do not adequately reflect European attitudes to financial markets. Rating markets in the USA and in Europe do not function in the same way. Even within Europe, product features and behavior patterns are different. This holds true also for individual financial products. This nature of European financial markets must be addressed.

3. Possible Amendments

We believe that significant improvements of rating services can be achieved only by structural changes. First steps for the reinforcement of ratings in the financial markets could be the following:

- a) Rating agencies must be obligated to ensure transparency by publishing their fee structure, rating philosophy and methodologies, and how they derive their ratings from facts. Disclosure must be on such a level that meaningful scientific discussions on all relevant issues is possible.
- b) At the same time, the influence of investors must be strengthened to ensure that they better understand rating procedures and measures.
- c) Analysis and research, which the ratings are based on, must have a higher importance for the investor, in order to give him a better understanding of the rating results.
- d) Barriers to market entry are too high for any potential new player. Mechanisms for recognizing rating agencies must be enforced by a European approval procedure. This issue cannot be left to the US, as their recognition criteria are very much domestic (see the Credit Rating Agency Reform Act of 2006), and fail to meet European requirements and norms.
- e) In contrast to the segment of structured finance, oligopolistic structures must be avoided in other rating market niches. Competition allows young European agencies to develop a rating style meeting European needs. Thus, regulations by a supervisory authority on these markets must guarantee quality, but avoid high market barriers.

We are looking forward to providing you with further details on demand.

Yours sincerely,

Feri Rating & Rating AG

A handwritten signature in black ink, appearing to read "Dr. E. Weiß", with a large checkmark at the end.

Dr. Eberhard Weiß
Managing Board