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The impact of Ratings on the stability of financial markets

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As I begin my presentation

Some of you might be thinking

LOOK WHO IS SAYING

**THESE RATING AGENCIES WERE
SOLEY RESPONSIBLE FOR THE
FINANCIAL CRISIS**



I ACCEPT THE BLAME

HOWEVER

**YOU NEED TO ASK AN HONEST
QUESTION TO YOURSELF**

**WERE THE RATING AGENCIES
ONLY TO BE BLAMED**



PARTICIPANTS OF THE CRISIS

- **Politicians**
- **Regulators**
- **Mortgage Companies**
- **Investment Banks**
- **Rating Agencies**
- **Insurance Agencies**
- **Mortgage Buyers**
- **Investors**



LOT OF MYTHS CORRECTED

‘ Good times will remain forever. The theory of cyclicity is now a matter of past and with financial engineering we can continue to enjoy the good times’

‘Even if there is a some sort of financial crisis, our region would not be impacted. The reasons for growth in our economies are far different than other markets’



LESSONS LEARNT FROM CRISIS

The most important perhaps is that growth especially at a supernatural speed, should not be accepted.

Stakeholders must ensure that the economies grow but at a pace which is sustainable and during this phase of growth, they should not close their eyes on supervisory aspects.

The age old saying has come back to surface ‘ Bad decisions are taken in good times’



HOWEVER THERE ARE STILL LOTS OF POSITIVES

The fundamentals of our economies are still very much present and strong

Most of the analyst believe that 2010 would be a year of stabilization, followed by a recovery

Optimist believe that recovery would be at a much faster pace than other markets



WHAT IS OUR JOB NOW

To ensure that we are ready for the next phase of growth

We must take steps now to ensure that this time the growth is on a strong foundation and the one which is sustainable in long run.



WHAT CAN RATING AGENCIES DO



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Rating Agencies Role

- **Introduction**
- **Surveillance**
- **History**



Introduction

Lingkaran Trans Kota Holding

Lingkaran Trans Kota Holding Sukuk

Rated AA2



Surveillance

All the rated entities and issues are constantly under surveillance

Any public or private news are incorporated into rating decisions

This significantly reduces the chances of any negative surprises and anxiety in the market



History

Rating Agencies maintain a complete history of the rated entities and issues. This history is publicly available

This provides a snapshot view of the history of the entity / issue clearly telling investors at which point in time the entity / issue has done good or bad



History

This history significantly helps the investors in doing their own forecasts about the particular issue / entity or entities of similar nature



Does the role of rating agencies finish here

NO

Rating Agencies can help improve the way of doing business through its governance ratings



PILLARS OF CORPORATE GOVERNANCE

- **Ownership Profile**
- **Effectiveness of Board Structure**
- **Management Structure & Processes**
- **Efficiency of organizational units**
- **Transparency & Disclosure**



FAILURES DUE TO POOR CORPORATE GOVERNANCE

Too much power is centered on one individual without proper oversight... **e.g. Enron,**

Board fails to ensure controls are robust or question the unusual or the unrealistic ... **e.g. Barings**

Poor disclosure and transparency becomes commonplace ... **e.g. WorldCom**

Shareholder rights are mistreated... **e.g. Parmalat et al**



WHY THE REGION GENERALLY IS INDIFFERENT TO CORPORATE GOVERNANCE



Hawkamah Institute of Corporate Governance in UAE

One major reason there hasn't been better corporate governance take-up from private businesses is that the region has yet to be hit by a cataclysm on the scale of the Enron collapse or the Asian economic crisis.



**UNFORTUNATELY WE HAVE
BEEN HIT BY SOME NOW**

THE AHAB CASE



THE AHAB CASE

TIBC was a bank whose chairman and executive directors never appeared at board meetings (although the minutes carried their signatures anyway).

Source : The Economist, Zawya



THE AHAB CASE

The investigators found little evidence that any of the Saudi borrowers in TIBC \$ 2.2 billion loan-book were genuine.

Source : The Economist, Zawya



THE AHAB CASE

They note that Deloitte, which Ahab appointed as a consultant, made 'drive-by' visits to the borrowers' addresses, discovering that 'the premises were not occupied by the borrowers or used for trade purposes.'

Source : The Economist, Zawya



RATING AGENCIES WITH A AN
UNDERSTANDING OF SHARIA
DYNAMICS CAN ALSO HELP TO
IMPROVE THE SHARIA
GOVERNANCE MECHANISM



CONCLUSION

While some of the rating agencies were a part of problem, the rating industry has still lot to offer during the financial restructuring phase

Ratings can help not only through their credit ratings but equally important through their governance ratings.



THE FINAL MESSAGE

DO

PUNISH THE PLAYERS

DO NOT

PUNISH THE INDUSTRY



Thank You

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