

Enhancing the Risk Management Process

The Client: A Chinese investment management firm

Users: Credit Risk team

One of the responsibilities of the Credit Risk team at this investment manager is to monitor the firm's fixed income portfolio to identify any potential risks and opportunities. These investments are mainly made in U.S. dollar-denominated Chinese assets, and include a number of local government financing vehicle (LGFV) bonds and non-banking financial institution (NBFI) bonds.

Pain Points:

The Credit Risk team is very small and only had access to credit ratings and related publicly-available information to support its analysis. Much of this information is released on an annual basis only, making it difficult to look at changes throughout the year. In addition, the team was unable to tell how the credit ratings were determined and what might cause them to change. A further complication was the absence of financial information for several issuers.

The team's small size and lack of an ongoing monitoring system was becoming very challenging given the heightened importance of risk mitigation at the firm, plus an expanding list of issuers in the fixed income portfolio. The team wanted to enhance its risk management process to get a better handle on the outlook for potential losses and recovery. Priorities included:

- **More detailed and timely information** to support a thorough evaluation of issuers and to provide an early-warning system to readily flag potential problems.
- Insights into **how assessments of creditworthiness** are developed to know which factors are important and could impact risk.
- A tool to help **evaluate the impact of economic conditions and rating actions** on current and potential investments.
- Knowledge about how other firms use **data and tools to manage credit risk**.

The Credit Risk team turned to S&P Global Market Intelligence (“Market Intelligence”) to discuss the company’s ability to meet these needs.

The Solution:

Representatives from Market Intelligence focused the discussion on three components of their offering: (1) RatingsDirect®, (2) Credit Analytics, and (3) the S&P Capital IQ platform.

(1) RatingsDirect

RatingsDirect is the official desktop source for S&P Global Ratings' credit ratings and research, combining ratings and research with comprehensive market data and risk indicators. This component would help the Credit Risk team obtain a view of fixed income markets at the industry, company, and issuer levels. It would also provide a robust workflow solution for efficient credit analysis, as well as an understanding of the rationale behind each rating.

(2) Credit Analytics

Credit Analytics delivers a suite of capabilities to help users ease their workflow when running risk analysis on rated, unrated, public, and private companies. Market and fundamentals-driven models would provide the Credit Risk team quick access to Probabilities of Default (PDs) and quantitative credit scores¹ that broadly align with credit ratings by S&P Global Ratings. Early warning indicators would facilitate easy monitoring of credit deterioration, while contribution and sensitivity analysis would provide insights into the importance of each factor impacting risk. In addition, an expanded PD framework would create proxy PDs based on a combination of industry and geographic factors to provide the needed context if financials were not available for any issuer.

While LGFVs and NBFIs cannot be scored with Credit Analytics, a parental/government support overlay was mentioned as an alternative to gain insights on LGFVs, and diversified banks as an alternative to gain insights on NBFIs.

(3) The S&P Capital IQ Platform

This web-based platform offers a powerful array of financial and macroeconomic data, analytics, and research. The financial data provides over 5,000 individual data items², including industry-specific metrics on 17 industries. Adjustments are made for nonrecurring charges to enhance cross-company comparability and the details are auditable down to the source documents. In addition to having access to these deep and broad data sets, the platform would enable the Credit Risk team to stay on top of developments by creating alerts on recent ratings changes in RatingsDirect and changes in Credit Analytics PDs.

¹ S&P Global Ratings does not contribute to or participate in the creation of credit scores generated by S&P Global Market Intelligence. Lowercase nomenclature is used to distinguish the credit scores generated by the model from the actual S&P Global Ratings credit rating.

² As of March 2020.

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The Market Intelligence representatives took the time to describe how similar firms were using these three components as part of their risk management systems. In addition, a Credit Analytics specialist was available to address detailed questions about the methodology, country risk scores, model performance, and more. A customized credit surveillance template was also discussed that would present an issue versus issuer version of the information, which was important for the Credit Risk team.

Key Benefits:

These three components of the Market Intelligence offering met the needs outlined by the Credit Risk team. In particular, they valued:

1. **The ability to stay current with top stories in RatingsDirect**, sector highlights, and dynamic ratings distribution and credit ratings migration charts—plus credit research in Chinese.
2. **An easy-to-use web-based capability with Credit Analytics** to automate the creation of credit scores and PDs, plus an approach that can be used with limited financial data or internal information on firms that may not be public or rated.
3. **A well-tested methodology behind the Credit Analytics models** with annual recalibrations to help keep the tools highly predictive of default risk, plus technical documentation and white papers that explain the development process, use of data, and overall performance.
4. **The ability to boost productivity with access to extensive data on the S&P Capital IQ platform and via an Excel® plug-in** to perform company and industry research and monitor companies and markets.
5. **Training and on-going support** to help the team understand the range of available capabilities and continue to get the most out of the solutions.

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