



Coface, a new player in corporate solicited ratings

The rating industry

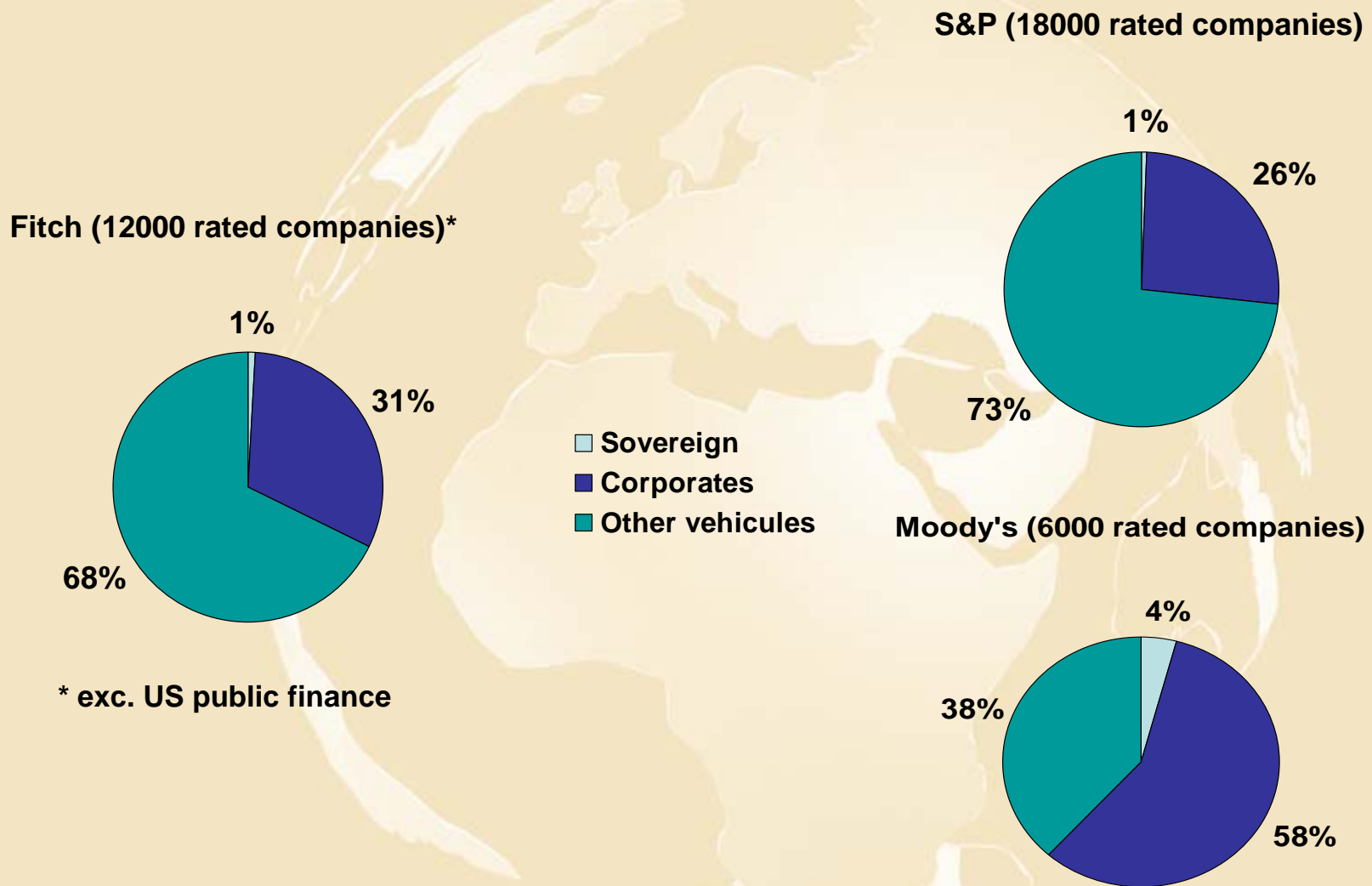
- Rating is a business model which makes sense in a market economy when customers/investors have neither time nor expertise to analyze the quality of a product/service: for taste (Michelin guide, Parker...) or for probability of default of corporates (rating agencies).
- Rating originated and mostly developed in the US, for good reasons:
 - the size of US capital markets,
 - the importance in the US of disintermediation of corporate finance in general, and of bonding market in particular.

What has gone wrong with ratings

- An oligopoly, bringing “value for money” issues,
 - the big 3: S&P (3Bn TO, 1,4Bn Op. Result), Moody’s (2,3Bn TO, 1,1Bn Op. Result), Fitch (0,6Bn TO, 0,2Bn Op. Result);
 - other small players (DBRS, JRI, JCR,...), each representing less than 0.5% of the market.

- A hazardous diversification of the industry,
 - from rating financial instruments backed by entities (corporates or public entities), and which can followed statistically over time,
 - to financial instruments backed by no institutions:
 - ratings applied to packages of any kind of loans,
 - with slicing on very poor statistical basis,
 - and no control on UW quality.
 - a symbol of this diversification:
 - only 3 consensual AAA US corporates: Automatic Data Processing/Exxon Mobil, General Electric, Johnson & Johnson,
 - but 5.000 AAA US financial vehicles.

The diversification of the rating industry



Open debate concerning rating agencies (1)

The recent crisis was made possible by the mountain of « false money » (toxic AAA or investment grade financial instruments) created by banks with the support of rating agencies. Main responsibility is with American regulators who authorized regulated investors to invest in any instrument, as long as it was rated by “recognized rating agencies”.

This brought a number of proposals:

- SEC proposes,
 - to introduce a different scale for corporates and for financial vehicles,
 - to improve transparency by disclosure of methods and statistic data, and minimize conflicts of interest.
- French Government,
 - requests a European registration of credit rating agencies,
 - is in favor of a better distinction between consulting and rating.
- French AMF proposes
 - a reform of the code of conduct of the rating agencies,
 - a registration and a worldwide organisation of credit rating agencies.

Open debate concerning rating agencies (2)

- **European Commission**
 - thinks that the IOSCO code (rating agencies code of conduct) is useless and not enforceable,
 - says a regulatory solution to fix governance rules is necessary.

"I hope we can also craft these measures in a way that will encourage entry to the (rating) market by new players, working perhaps on a different business model."

Charlie McCreevy (European Commissioner for Internal Market and Services - Inaugural Global Financial Services Centre Conference Dublin, 16th June 2008)

Open debate concerning rating agencies (3)

- Europe new and strong position is good news
- For the time being, Europe has not really supported newcomers
 - European regulation recognizes “internationally recognised rating agencies”, but without any European recognition process, it is just another way of saying “existing Big 3” (one recent example: “Communication Notice on State Aid in the form of guarantees”)
 - Basle 2 rating (with the recognition of the status of “External Credit Assessment Institution”) seems to be a missed opportunity:
 - Big 3 are automatically agreed in all EU
 - others have to dialogue with each and everyone of the 27 national regulatory authorities (Coface is still only recognized in France)
- Coface is ready to participate in this debate

Coface scope vis-à-vis the different ratings

There are 5 very different rating categories.

Regulated entities (banks, insurance)

- Potential ambiguity between regulatory authorities “implicit” rating and agencies: a non profit mission?

- Not in Coface scope

States (sovereign ratings)

- Potential ambiguity with Coface role in its public mission

- Not in Coface scope
(Coface country @rating measures average corporates ratings in a country)

Corporates

- Core field for ratings

- Coface core scope,
 - already with unsolicited rating
 - now with solicited ratings

“vanilla” financial products

- Portfolios of corporate loans: risk is linked with corporate rating, but complexity is underestimated

- Coface scope, with original business model (rating + risk sharing)

“sophisticated” financial products

- Portfolios of anything else: no room for public rating, investors should make their own due diligence (or banks should keep it in their assets)

- Not in Coface scope

Coface progressive development on ratings

Which ratings?

Before 2000,

- Internal scores on 50mns corporates
- based on public and proprietary information

Since 2000,

unsolicited public @rating score + reports on 50mns corporates

Before 2008,

Internal full rating + info, discussed with management, on 17.000 corporates

NEW in 2008, solicited rating + report, for 3rd parties

To whom?

Internal use
CONFIDENTIAL

Any customer
NON
CONFIDENTIAL

Internal use to underwrite sensitive risks
CONFIDENTIAL

Any customer
- for its own confidential use
- restricted to its stakeholders
- or for public use
CONFIDENTIAL
OR NOT

Our approach: a strict control of confidential data; a transparency on ratings, as a way to improve their quality.



1 – Corporate solicited ratings

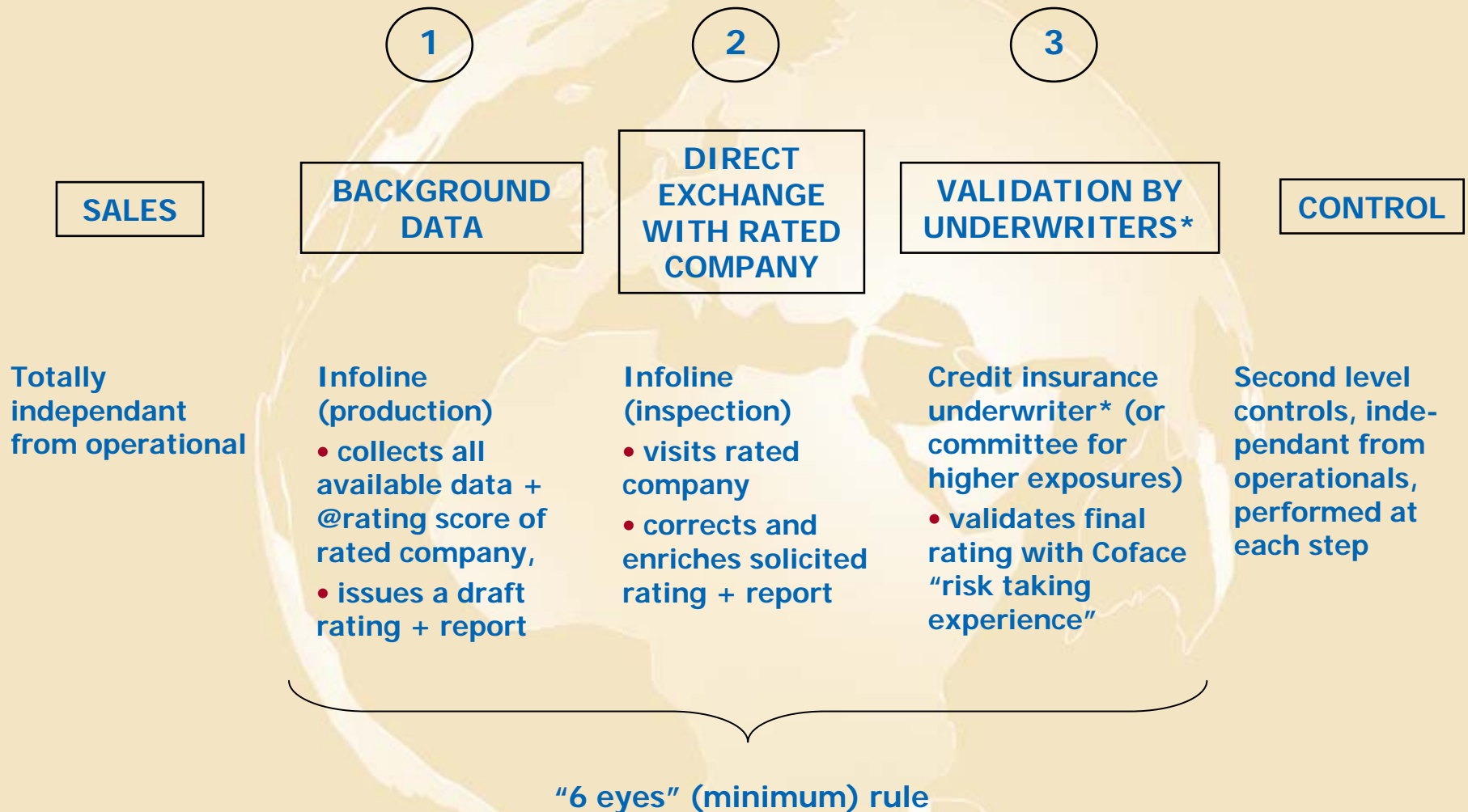
Product description and key advantages

- A corporate solicited rating.
- Rating can be self initiated by the rated company, or initiated by a stakeholder of the rated company (with full knowledge and agreement of the rated company). In both cases, the rated company is in full control of confidentiality.
- Rating is based on an “in depth” management interview on the premises of the rated company.
- Rating is presented as a letter (AA, BBB...), equivalent to other ratings, and with the same statistical equivalent.
- Rating is topped off with an analysis report, which can be customized for the specific needs of a stakeholder.
- Rating is available within a short time, with reasonable management time invested and a reasonable fee: 4.000€ for a simple medium size corporate (1 country, no subsidiaries); fee can be paid by rated company OR by interested stakeholder.

A new business model

- Limited fee and management time, with high statistical quality is made possible through a new business model,
 - regarding the production process, with 3 different steps,
 - and regarding the commercial target which is larger than classical ratings.

Production process: Coface 3 steps solicited rating process



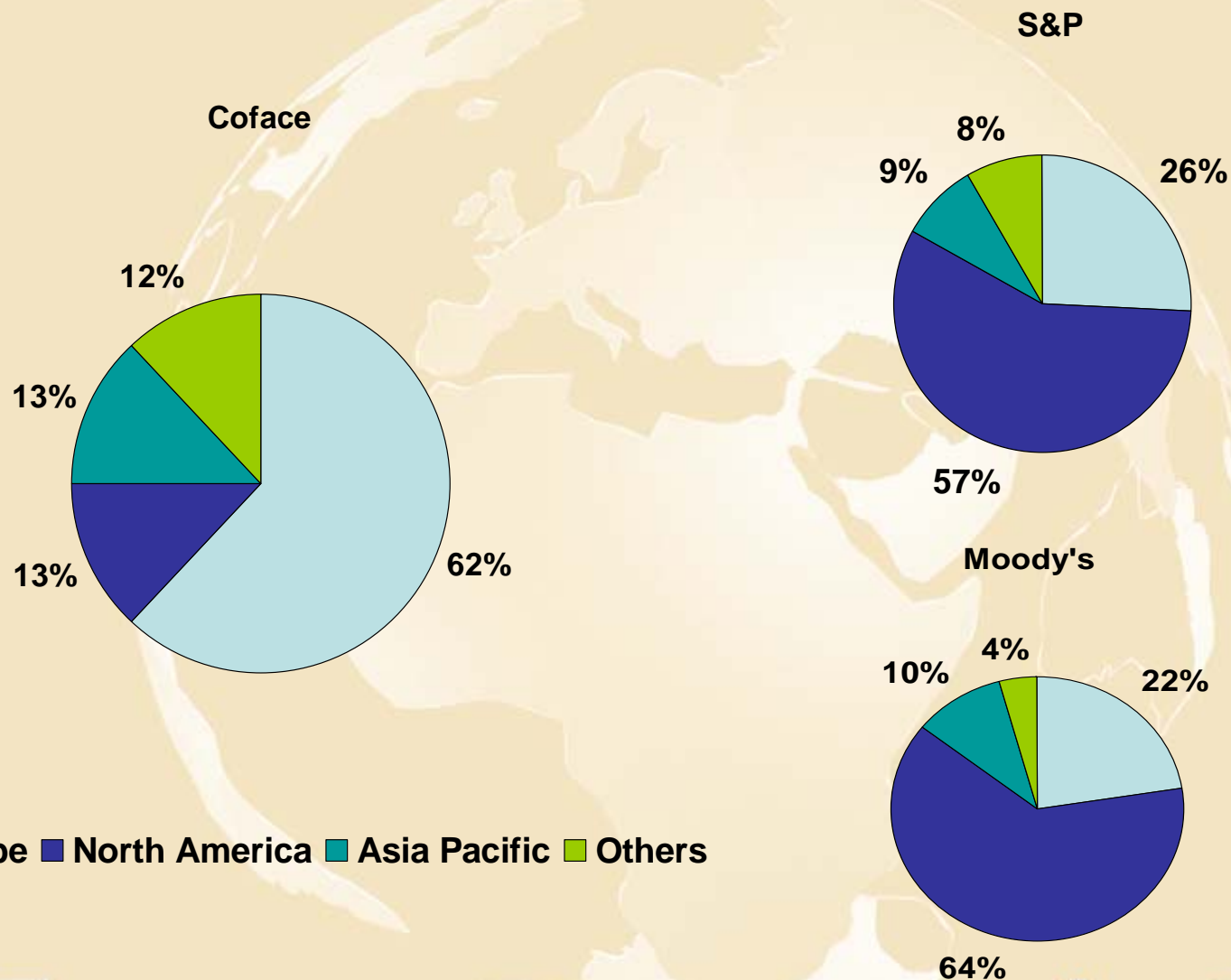
* name of risks subscriber in credit insurance

The strong points of Coface « 3 levels » process (1)

Step 2, direct exchange with rated company, is equivalent to classical rating with a more global expertise.

- Coface has in each country of presence seasoned specialists used to in-depth discussions with corporate management, following our 17,000 internal full ratings.
- They know the specificities of accounting and of management rules in each country/sector.
- They may have a slight European bias, but no American bias...

A more balanced geographic breakdown of rated corporates



A geographical bias?

The example of the car industry

	2003	2007
Toyota	AAA	AAA
	AAA	AAA
GM	A-/BBB+	B
	BBB	B
Ford	BBB+/BBB	B/B-
	BB-	B+
PSA	A-	BBB+
	A+	A
Renault	BBB	BBB+
	A	A

Rating agencies **Coface**

The strong points of Coface 3 levels process (2)

The 2 other steps of Coface rating process are exclusive.

Step 1, background data

- Coface is n°6 in the world in corporate information, following 50 mn companies.
- We have built exclusive non solicited ratings (@rating family), Basle 2 recognised.
- We get proprietary corporate payment experience from our 3 other lines (credit insurance, factoring and debt collection).
- We can replace and monitor any corporate in its environment: its country, sector, customers, suppliers, competitors...

Step 3, validation by underwriters

- Coface has 250 specialists in corporate risk underwriting, in 30 UW centres across the world, applying uniform standards, and working on a common system;
- They follow € 450 Bn credit exposures, on 2 mn different corporates, in 160 countries;
- they bring in the rating process their "risk culture": a major ingredient lacking in the present system and explaining part of the subprime crisis.

The strong points of Coface 3 levels process (3)

Using its existing process for its internal ratings, Coface is able to propose a rating with a strong statistical stability⁽¹⁾, for only a fraction of the usual cost of rating: both the visible cost (the fee) and in the invisible cost (the management time that rated company must invest in the rating process).

This makes possible to extend the target of such rating to SME's, and to corporates in emerging markets.

(1) in ratings, as in credit insurance, you learn from defaults. Moody's registered 91 defaults on monitored European companies since 1985. Coface registers 91 European defaults per working day.

The use of Coface solicited ratings: to build confidence...

→ In corporate financing

	2007	Ratings
<ul style="list-style-type: none">• bonds• short term negociable instruments	138 Bn 193 Bn	scope for solicited ratings
<ul style="list-style-type: none">• short term banking credit• long term banking credit	173 Bn 626 Bn	scope for Basle 2 ratings
<ul style="list-style-type: none">• B2B financing	656 Bn	<u>new scope</u>

→ In other B2B confidence areas

<ul style="list-style-type: none">• client/supplier relations• outsourcing• licensing• agents(...)	<u>New scope</u> <ul style="list-style-type: none">• a business report is too superficial• a due diligence is too costly and intrusive
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2- PORTFOLIO OF CORPORATE CREDITS RATING

A new business model for portfolio ratings

- Rating diversification has been uncontrolled.
- Can one rate with sufficient statistical quality loan portfolios? We have a major doubt, due to underlying risk, correlation, lack of history, lack of UW control. One should at least use a different “letters” scale.
- In one field, portfolios of trade receivables, we think that a good rating is possible: Coface is used to price (i.e. to rate) and insure portfolios of B2B credit portfolios: this is our core businesses (credit insurance and factoring).
- A suggestion: to ask rating agencies to jointly rate AND insure a small percentage of the rated portfolio.
- The objective: to secure investors that the rating agency will follow the risk through, and would lose more money if it was wrong about its rating, than it would gain on its rating fee.

Coface's objectives in ratings

- To strengthen its leadership in unsolicited rating
- To pursue its registration as a Basle 2 compliant rating agency for both its unsolicited @rating scores, and for its solicited ratings, and solicit its registration for the new process announced by European authorities.
- To take part in open debate in rating, including rating of corporate credit portfolios
- And to become a major player in solicited rating,
 - Tests are launched (beginning of June in Japan, in China, today in France, then in Russia, Turkey and Germany)
 - The full commercial launch is planned in the autumn
 - Coface wishes to become in the end an alternative to capital market financing for big companies; and aims to be the leader for SME's, supplier credits and other B2B confidence areas.