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# Mapping of EuroRating credit assessments under the Standardised Approach

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## 1. Executive summary

1. This report describes the mapping exercise carried out by the Joint Committee to determine the ‘mapping’<sup>1</sup> of the credit assessments of EuroRating Sp. z o.o. (EuroRating).
2. The methodology applied to produce the mapping is the one specified in the Implementing Technical Standards on the mapping of ECAIs’ credit assessments under Article 136(1) and (3) of Regulation (EU) No 575/2013 (Capital Requirements Regulation – CRR). These ITS employ a combination of the provisions laid down in Article 136(2) of Regulation (EU) No 575/2013.
3. The mapping neither constitutes the one which ESMA shall report on in accordance with Article 21(4b) of Regulation (EC) No 1060/2009 (Credit Rating Agencies Regulation - CRA) with the objective of allowing investors to easily compare all credit ratings that exist with regard to a specific rated entity<sup>2</sup> nor should be understood as a comparison of the rating methodologies of EuroRating with those of other ECAIs. This mapping should however be interpreted as the correspondence of the rating categories of EuroRating with a regulatory scale which has been defined for prudential purposes. This implies that an appropriate degree of prudence may have been applied wherever not sufficient evidence has been found with regard to the degree of risk underlying the credit assessments.
4. As described in Recital 12 of the Implementing Technical Standards on the mapping of ECAIs’ credit assessments under Article 136(1) and (3) of Regulation (EU) No 575/2013, in order to avoid causing undue material disadvantage on those ECAIs which, due to their more recent entrance in the market, present limited quantitative information, with the view to balancing prudential with market concerns, two mappings apply for these ECAIs, with the first mapping for a limited period of three years. Both mappings should take into account quantitative and qualitative factors. Compared to the second mapping, the quantitative factors for deriving the first mapping should be relaxed. This solution would allow ECAIs which present limited

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<sup>1</sup> According to Article 136(1), the ‘mapping’ is the correspondence between the credit assessments of and ECAI and the credit quality steps set out in Regulation (EU) No 575/2013 (Capital Requirements Regulation – CRR).

<sup>2</sup> In this regard please consider [http://www.esma.europa.eu/system/files/esma\\_\\_2015-1473\\_report\\_on\\_the\\_possibility\\_of\\_establishing\\_one\\_or\\_more\\_mapping....pdf](http://www.esma.europa.eu/system/files/esma__2015-1473_report_on_the_possibility_of_establishing_one_or_more_mapping....pdf).

quantitative information to enter the market and would positively stimulate them to collect a sufficient number of quantitative information.

5. In accordance with the previous paragraph for a subset of ECAIs two mappings are applicable, one applicable until 31.12.2018 and one applicable from 01.01.2019. EuroRating belongs to the subset of ECAIs that are provided two mappings. Updates to the mapping should be made whenever this becomes necessary, including in relation to the mapping to be applied after the three years, to reflect quantitative information collected during the three year-period. Nevertheless, in the absence of such a review, for the ECAIs that are provided two mappings the one applicable from 01.01.2019 shall operate after the three years phase-in period.
6. The resulting mapping tables have been specified in Annex III of the Implementing Technical Standards on the mapping of ECAIs' credit assessments under Article 136(1) and (3) of Regulation (EU) No 575/2013. Figure 1 below shows the result for the EuroRating ratings scale, the Global long-term rating scale, displaying the mapping applicable until 31.12.2018 and the one applicable starting from 01.01.2019.

Figure 1: Mapping of EuroRating's Global long-term rating scale

Credit assessment	Credit quality step	
	Applicable until 31.12.2018	Applicable from 01.01.2019
AAA	1	2
AA	1	2
A	2	2
BBB	3	3
BB	4	5
B	5	6
CCC	6	6
CC	6	6
C	6	6
D	6	6

## 2. Introduction

7. This report describes the mapping exercise carried out by the Joint Committee (JC) to determine the 'mapping' of the credit assessments of EuroRating Sp. z o.o. (EuroRating).
8. EuroRating is a credit rating agency that has been registered with ESMA on 7 May 2014 and therefore meets the conditions to be an eligible credit assessment institution (ECAI)<sup>3</sup>.
9. The methodology applied to produce the mapping is the one specified in the Implementing Technical Standards on the mapping of ECAIs' credit assessments under Article 136(1) and (3) of Regulation (EU) No 575/2013 (Capital Requirements Regulation – CRR). These ITS employ a combination of the provisions laid down in Article 136(2) of Regulation (EU) No 575/2013. The information base used to produce the mapping is the same that has been employed when performing the first mapping proposal which was disclosed during the consultation period to these ITS. At that time, as EuroRating did not yet submit information to ESMA Central Repository (CEREP<sup>4</sup>), the main source of information was the credit rating agency itself. On the one hand, the quantitative and qualitative information provided by EuroRating has been used to obtain an overview of the main characteristics of this ECAI. On the other hand, information regarding the types of credit ratings produced and the definition of the applicable rating scales has also been taken into account.
10. The following sections describe the rationale underlying the mapping exercise carried out by the Joint Committee (JC) to determine the mappings for both the applicable time periods. With respect to the quantitative requirements used to perform the mappings, in case of ECAIs for which limited quantitative information is available the same methodology has been applied across the two applicable time periods, although with two different levels of prudence. Section 3 describes the relevant ratings scales of EuroRating for the purpose of the mapping. Section 4 contains the methodology applied to derive the mapping of EuroRating Global long-term rating scale. The mapping table is shown in Appendix 4 of this document and have been specified in Annex III of the Implementing Technical Standards on the mapping of ECAIs' credit assessments under Article 136(1) and (3) of Regulation (EU) No 575/2013.

## 3. EuroRating credit ratings and rating scales

11. EuroRating produces one type of credit ratings - **Long-term issue/issuer credit ratings** - that may be used by institutions for the calculation of risk weights under the Standardised Approach (SA)<sup>5</sup>. This rating is shown in Column 2 of Figure 2 in Appendix 1.

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<sup>3</sup> It is important to note that the mapping does not contain any assessment of the registration process of EuroRating carried out by ESMA.

<sup>4</sup> CEREP is the central repository owned by ESMA to which all registered/certified CRAs have to report their credit assessments. <http://cerrep.esma.europa.eu/cerep-web/>.

<sup>5</sup> As explained in recital 4 ITS, Article 4(1) CRA allows the use of the credit assessments for the determination of the risk-weighted exposure amounts as specified in Article 113(1) CRR as long as they meet the definition of credit rating in Article 3(1)(a) CRA.

12. The ratings assigned by the EuroRating credit rating agency represent an overall estimate of the risk of losses (that is to say, the ultimate loss of part or all of the sums owed, together with any interest payable) on the part of creditors regarding the entity in question in the event of default. The ratings given by EuroRating therefore represent a combination of the estimated probability of default (PD) on the part of the entity in question and an estimate of the ultimate losses likely to be incurred by its creditors if it should actually default (Loss Given Default - LGD).
13. EuroRating assigns this credit rating to the **Global long-term rating scale** as illustrated in column 3 of Figure 2 in Appendix 1. Therefore, a specific mapping has been prepared for this rating type. The specification of the Global long-term rating scale is described in Figure 3 of Appendix 1.
14. The mapping of the Global long-term rating scale is explained in Section 4 and it has been derived in accordance with the quantitative factors, qualitative factors and benchmarks specified in the ITS.

## 4. Mapping of EuroRating's Global long-term rating scale

15. The mapping of the Global long-term rating scale has consisted of two differentiated stages where the quantitative and qualitative factors were considered. In addition, the benchmarks specified in Article 136(2) CRR have been taken into account.
16. In the first stage, the quantitative factors referred to in Article 1 of the ITS have been taken into account to differentiate between the levels of risk of each rating category. The *long run default rate* of a rating category has been calculated in accordance with Article 6 of the ITS, as the number of credit ratings cannot be considered to be sufficient.
17. In a second stage, the qualitative factors proposed in Article 7 of the ITS have been considered to challenge the result of the previous stage, especially in those ratings categories where less default data have been available.

### 4.1. Initial mapping based on the quantitative factors

#### 4.1.1. Calculation of the short-run and long-run default rates

18. EuroRating has started issuing ratings since 2007. However, the number of ratings issued by the agency cannot be considered sufficient for the calculation of the short and long run default rates specified in the Articles 3 – 5 of the ITS. Therefore, the allocation of the CQS has been made in accordance with Article 6 of the ITS, as shown in Figure 4 and Figure 5 of Appendix 3. In these cases, the long run default rate benchmark associated with the equivalent category in the international rating scale is a key qualitative factor that has been used for the mapping proposal.

19. For D rating category, no calculation of default rates has been made since it already reflects a 'default' situation.

20. The default definition applied by EuroRating, described in Appendix 2, has been used for the calculation of default rates.

#### 4.1.2. Mapping proposal based on the long run default rate

21. As illustrated in the second column of Figure 6 and Figure 7 in Appendix 4, the assignment of the rating categories to credit quality steps has been initially made in accordance with Article 6 of the ITS. Therefore, the numbers of defaulted and non-defaulted rated items have been used together with the equivalent rating category of the international rating scale.

##### Mapping Tables applicable until 31.12.2018:

- **AAA/AA/A/BBB/BB/B:** the number of rated items in each of these categories is equal or larger than the respective minimum required number of observed items given the number of defaulted items in the rating category. Thus the credit quality steps associated with the AAA/AA, A, BBB, BB, B rating categories in the international rating scale (CQS 1, CQS 2, CQS 3, CQS 4 and CQS 5 respectively) can be assigned.
- **CCC-C:** since the CQS associated with the equivalent rating category of the international rating scale is 6, the proposed mapping for these rating categories is also CQS 6.

##### Mapping Tables applicable starting from 01.01.2019:

- **AAA/AA/BB/B:** the number of rated items in these categories is below the minimum required number of observed items so that the credit quality step associated with the AAA/AA, BB and B rating categories in the international rating scale (CQS 1, CQS 4 and CQS 5 respectively) cannot be assigned. Therefore, the proposed credit quality steps for these rating categories are CQS 2, CQS 5 and CQS 6 respectively.
- **A/BBB:** the number of rated items in each of these categories is equal or larger than the respective minimum required number of observed items given the number of defaulted items in the rating category. Thus the credit quality steps associated with the A and BBB rating categories in the international rating scale (CQS 2 and CQS 3 respectively) can be assigned.
- **CCC-C:** since the CQS associated with the equivalent rating category of the international rating scale is 6, the proposed mapping for these rating categories is also CQS 6.

#### 4.2. Final mapping after review of the qualitative factors

22. The qualitative factors specified in Article 7 of the ITS have been used to challenge the mapping proposed by the default rate calculation. Qualitative factors acquire more

importance in the rating categories where quantitative evidence is not sufficient to test the default behavior<sup>6</sup>, as is the case for all rating categories of the Global long-term rating scale.

23. The **definition of default** applied by EuroRating and used for the calculation of the quantitative factors has been analysed:

- The types of default events considered are shown in Appendix 2 and are consistent with letter (a), (b), (c) and (d) of the benchmark definition specified in Article 4(4) of the ITS.
- Bankruptcy-related events represent 23% of the total defaults recorded by Eurorating.

Therefore, no specific adjustment has been proposed based on this factor.

24. Regarding the **meaning and relative position of the credit assessments**, they are aligned with the mapping proposal resulting from the quantitative factors in case of the Mapping Tables applicable until 31.12.2018. However, the absence of sufficient quantitative evidence does not allow a significant use of this factor to modify the proposed mappings, thus no specific adjustment has been proposed based on this factor for the Mapping Tables applicable starting from 01.01.2019. In the case of the D rating category, its meaning is consistent with the one of CQS 6 stated in Annex II ITS.

25. Regarding the **time horizon** reflected by the rating category, EuroRating's rating methodology focuses on the long-term. The stability of the rated items however cannot be confirmed due to lack of data over a 3-year time horizon.

26. Finally, it should be highlighted the use of the long run default rate benchmark associated with the equivalent category in the international rating scale as the **estimate of the long run default rate** for the calculation of the quantitative factor of all rating categories under Article 6 of the ITS..

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<sup>6</sup> The default behavior of a rating category is considered to be properly tested if the quantitative factors for that rating category are calculated under Articles 3 – 5 of the ITS.

## Appendix 1: Credit ratings and rating scales

Figure 2: EuroRating's relevant credit ratings and rating scales

SA exposure classes	Name of credit rating	Credit rating scale
<b>Long-term ratings</b>		
Institutions	Long-term issuer rating	Global long-term rating scale
	Long-term issue rating	Global long-term rating scale
Corporates	Long-term issuer rating	Global long-term rating scale
	Long-term issue rating	Global long-term rating scale
Covered bonds	Long-term issue rating	Global long-term rating scale

Source: EuroRating

Figure 3: Global long-term rating scale

Credit assessment	Meaning of the credit assessment
AAA	Negligible credit risk. Highest level of financial credibility. Rating assigned exclusively where an entity has extremely strong capacity to meet financial commitments.
AA	Very low credit risk. Very high level of financial credibility. Very strong capacity to meet commitments. Low susceptibility to adverse economic conditions.
A	Low credit risk. High financial credibility and capacity to meet commitments. Average resistance to long-term unfavourable economic financial conditions.
BBB	Average credit risk. Good financial credibility and adequate capacity to meet commitments in the long term. Increased susceptibility to long-term adverse economic conditions.
BB	Increased credit risk. Relatively low financial credibility. Adequate capacity to meet commitments under average or favourable economic conditions. High or average likelihood of recovering debts in the event of default.
B	High credit risk. Capable of meeting commitments only under favourable external conditions. Average or low likelihood of recovering debts in the event of default.
CCC	Very high credit risk. Very low capacity to meet commitments even under favourable economic conditions. Low or very low likelihood of recovering debts in the event of default.
CC	
C	
D	Extremely high credit risk. Total absence of capacity to meet commitments. Without additional external support, the likelihood of recovering debts is very low or close to zero.





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Source: EuroRating

## Appendix 2: Definition of default

EuroRating credit rating agency considers a rated entity as defaulted where any of the following type of event has occurred:

- a) a bankruptcy filing or legal receivership that will likely cause a miss or delay in future contractually required debt service payments;
- b) a missed or delayed disbursement of a contractually required interest or principal payment, unless payments are made within a contractually allowed grace period;
- c) a distressed exchange if the offer implies the investor will receive less value than the promise of the original securities;
- d) the rated entity is under a significant form of regulatory supervision owing to its financial situation (this applies only to banks).

Source: EuroRating

## Appendix 3: Default rates of each rating category

Figure 4: Mapping proposal for rating categories with a non-sufficient number of credit ratings, applicable until 31.12.2018

2008h1 - 2011h1	AAA/AA	A	BBB	BB	B	CCC-C
CQS of equivalent international rating category	CQS 1	CQS 2	CQS 3	CQS 4	CQS5	CQS 6
N. observed defaulted items	0	0	0	0	0	0
Minimum N. rated items	0	0	0	0	0	n.a.
Observed N. rated items	0	10	15	0	0	0
<b>Mapping proposal</b>	<b>CQS 1</b>	<b>CQS 2</b>	<b>CQS 3</b>	<b>CQS 4</b>	<b>CQS 5</b>	<b>CQS 6</b>

Source: Joint Committee calculations based on EuroRating data

Figure 5: Mapping proposal for rating categories with a non-sufficient number of credit ratings, applicable starting from 01.01.2019

2008h1 - 2011h1	AAA/AA	A	BBB	BB	B	CCC-C
CQS of equivalent international rating category	CQS 1	CQS 2	CQS 3	CQS 4	CQS5	CQS 6
N. observed defaulted items	0	0	0	0	0	0
Minimum N. rated items	496	0	0	10	5	n.a.
Observed N. rated items	0	10	15	0	0	0
<b>Mapping proposal</b>	<b>CQS2</b>	<b>CQS 2</b>	<b>CQS 3</b>	<b>CQS 5</b>	<b>CQS 6</b>	<b>CQS 6</b>

Source: Joint Committee calculations based on EuroRating data

## Appendix 4: Mappings of each rating scale

Figure 6: Mapping of EuroRating's Global long-term rating scale, applicable until 31.12.2018

Credit assessment	Initial mapping <i>based on LR</i> <i>DR</i> (CQS)	Review <i>based on SR</i> <i>DR</i> (CQS)	Final review <i>based on</i> <i>qualitative</i> <i>factors</i> (CQS)	Main reason for the mapping
AAA	1	n.a.	1	The quantitative factors are representative of the final CQS.
AA	1	n.a.	1	
A	2	n.a.	2	
BBB	3	n.a.	3	The quantitative factors are representative of the final CQS.
BB	4	n.a.	4	The quantitative factors are representative of the final CQS.
B	5	n.a.	5	The quantitative factors are representative of the final CQS.
CCC	6	n.a.	6	The quantitative factors are representative of the final CQS.
CC	6	n.a.	6	
C	6	n.a.	6	
D	6	n.a.	6	The meaning and relative position of the rating category is representative of the final CQS.

Figure 7: Mapping of EuroRating's Global long-term rating scale, applicable starting from 01.01.2019

Credit assessment	Initial mapping based on LR DR (CQS)	Review based on SR DR (CQS)	Final review based on qualitative factors (CQS)	Main reason for the mapping
AAA	2	n.a.	2	The quantitative factors are representative of the final CQS.
AA	2	n.a.	2	
A	2	n.a.	2	
BBB	3	n.a.	3	The quantitative factors are representative of the final CQS.
BB	5	n.a.	5	The quantitative factors are representative of the final CQS.
B	6	n.a.	6	The quantitative factors are representative of the final CQS.
CCC	6	n.a.	6	The quantitative factors are representative of the final CQS.
CC	6	n.a.	6	
C	6	n.a.	6	
D	6	n.a.	6	The meaning and relative position of the rating category is representative of the final CQS.