

Amended Draft Mapping of Cerved Rating Agency S.p.A.'s credit assessments under the Standardised Approach

1. Executive summary

1. This report describes the mapping exercise carried out by the Joint Committee of the European Supervisory Authorities (ESAs) to propose an amended 'mapping'¹ report of the credit assessments of Cerved Rating Agency S.p.A. (Cerved), with respect to the version published in November 2015.
2. The methodology applied to produce the mapping remains as specified in Commission Implementing Regulation (EU) 2016/1799 of 7 October 2016 (the Implementing Regulation)² laying down implementing technical standards with regard to the mapping of credit assessments of external credit assessment institutions for credit risk in accordance with Articles 136(1) and 136(3) of Regulation (EU) No 575/2013 of the European Parliament and of the Council (Capital Requirements Regulation – CRR). This Implementing Regulation employs a combination of the provisions laid down in Article 136(2) of the CRR.
3. The information base used to produce this mapping report reflects additional quantitative and qualitative information collected after the production of the mapping report published in November 2015. Cerved has introduced a short-term rating scale.
4. 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 entity³ nor should be understood as a comparison of the rating methodologies of Cerved with those of other ECAs. This mapping should however be interpreted as the correspondence of the rating categories of Cerved with a regulatory scale which has been defined for prudential purposes.

¹ 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).

² OJ L 275, 12.10.2016, p. 3-18

³ 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.

5. As described in Recital 12 of the Implementing Regulation, it is necessary to avoid causing undue material disadvantage on those ECAs which, due to their more recent entrance in the market, present limited quantitative information, with the view to balancing prudential with market concerns. Therefore, the relevance of quantitative factors for deriving the mapping is relaxed. This allows ECAs which present limited quantitative information to enter the market and increases competition. Therefore, the relevance of quantitative factors for deriving the mapping should be relaxed. This allows ECAs which present limited quantitative information to enter the market and increases competition.
6. The resulting mapping tables have been specified in Annex III of the Consultation Paper on the revised draft ITS on the mapping of ECAs' credit assessments under Article 136(1) and (3) of Regulation (EU) No 575/2013. Figure 1 below shows the result for the main ratings scale of Cerved, the corporate long-term rating scale.

Figure 1: Mapping of Cerved's Corporate long-term rating scale

Credit assessment	Credit quality step
A1.1	1
A1.2	1
A1.3	1
A2.1	2
A2.2	2
A3.1	2
B1.1	3
B1.2	3
B2.1	4
B2.2	4
C1.1	5
C1.2	6
C2.1	6

2. Introduction

7. This report describes the mapping exercise carried out by the JC to propose an amended ‘mapping’ report of the credit assessments of Cerved Rating Agency S.p.A. (Cerved), with respect to the version published in November 2015.
8. Cerved is a credit rating agency that has been registered with ESMA on 20 December 2012 and therefore meets the conditions to be an eligible credit assessment institution (ECAI)⁴. Cerved an Italian company resulting from the merger of three pre-existing legal entities (Lince, Cerved BI, Centrale dei Bilanci) carried out in 2009. It provides credit information to Italian financial institutions and non-financial companies; in particular it is specialized in the assessment of creditworthiness of non-financial companies and in the development of credit risk assessment models aimed to support credit decision making processes.
9. The methodology applied to produce the mapping is the one specified in the Commission’s Implementing Regulation (EU) 2016/1799 (‘the Implementing Regulation’) laying down Implementing Technical Standards (ITS) with regard to the mapping of credit assessments of External Credit Assessment Institutions (ECAIs) for credit risk in accordance with Articles 136(1) and (3) of the Regulation (EU) No 575/2013 of the European Parliament and the Council (‘the CRR’). This Implementing Regulation employs a combination of the provisions laid down in Article 136(2) CRR.
10. The information base used to produce this mapping report reflects additional quantitative information collected after the submission of the draft Implementing Technical Standards by the JC to the European Commission. The quantitative information is drawn from data available in the ESMA’s central repository (CEREP⁵) based on the credit rating information submitted by the ECAIs as part of their reporting obligations.
11. Regarding qualitative developments, the qualitative factors specified in the Implementing Regulation remain unchanged (e.g. default definition, time horizon, no material changes introduced to the corporate methodology), while a mapping for the short-term rating scale is provided.
12. The following sections describe the rationale underlying the mapping exercise carried out by the Joint Committee (JC). Section 3 describes the relevant ratings scales of Cerved for the purpose of the mapping. Section 4 contains the methodology applied to derive the mapping of Cerved’s corporate long-term rating scale, whereas Section 5 refers to the mapping of the Short-term rating scale. The mapping tables are shown in Appendix 4 of this document and have been specified in Annex III of the Consultation Paper on the revised draft ITS on the mapping of ECAIs’ credit assessments under Article 136(1) and (3) of Regulation (EU) No 575/2013.

⁴ It is to be noted that the mapping does not contain any assessment of the registration process of Cerved carried out by ESMA.

⁵ <https://cerp.esma.europa.eu/cerp-web/>

3. Cerved credit ratings and rating scales

13. Cerved produces a **long-term and a short-term ratings**, which may be used by institutions for the calculation of risk weights under the Standardised Approach (SA)⁶, as shown in column 2 of Figure 2 in Appendix 1.
14. Cerved assigns these credit ratings to the **corporate long-term and short-term rating scales** as illustrated in column 3 of Figure 2 in Appendix 1. Therefore, a specific mapping has been prepared for these rating scales. The specification of Corporate long-term and short-term rating scales are shown in Figure 3.

4. Mapping of Cerved's Corporate long-term rating scale

15. The mapping of the Corporate long-term rating scale has consisted of two differentiated stages where the quantitative and qualitative factors as well as 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. More specifically the *long run default rate* of a rating category has been calculated in accordance in 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 has been available

4.1 Initial mapping based on the quantitative factors

4.1.1 Calculation of the long-run default rates

18. The number of credit ratings for rating categories A1.1, A1.2, A1.3 and A2.1 of the long-term credit rating scale cannot be considered to be sufficient for the calculation of the short run and long run default rates specified in Articles 3 – 5 of the Implementing Regulation. Therefore the allocation to the CQS has been made in accordance with Article 6 of the Implementing Regulation, as shown in Figure 6 of Appendix 3.
19. For the remaining categories the number of ratings cannot be considered sufficient for the calculation of the short and long run default rates specified in Articles 3 – 5 of the ITS. Therefore also in this case the allocation of the CQS has been made in accordance with Article 6 of the ITS, by considering the number of defaulted and not defaulted items. However in this case the size

⁶ 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.

of the pools is too large⁷ to be evaluated by a small pool methodology. In this situation Article 6 is applied by considering the number of defaulted and not defaulted items through the computation of short run default rates and a proxy for the long run default rate⁸ (see Figure 6 in Appendix 3). Thus the computed proxy of the long run default rate is considered as a first indicator to perform the allocation to each CQS, together with the prior expectation of the equivalent rating category of the international rating scale. However in this case the result needs to be confirmed by the qualitative factors given that only a proxy of the long run default rate has been achieved

4.1.2 Mapping proposal based on the long run default rate

20. As illustrated in the second column of Figure 10 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 prior expectation of the equivalent rating category of the international rating scale. The results are specified in Figures 6, 7, 8 and 9 of Appendix 4.

- **A1.1/A1.2/A1.3/A2.1:** the number of rated items is equal or larger than the respective minimum required number of observed items given the number of defaulted items in the rating category, with the exception of A1.2. A robustness check has been performed as the current data pool is relatively small considering the introduction of a new rating scale in 2014. A proxy reconciliation can be done for rating category A1.2, resulting in a longer time-series. When analyzing the extended sample, the analysis is inconclusive. This, coupled with Cerved meeting all the qualitative factor definitions, and considering its meaning and relative position, leads to maintaining the current allocation. Thus the credit quality steps associated with the A1.1, A1.2, A1.3 and A2.1 rating categories in the international rating scale (CQS 1, CQS 1, CQS 1 and CQS 2, respectively) can be assigned.
- **A2.2 to C2.1:** The proxy long run default rates are considered as a first indicator to perform the allocation to each CQS, together with the prior expectation of the equivalent rating category of the international rating scale. In accordance with these factors A2.2, A3.1, B1.1, B1.2, B2.1, B2.2, C1.1, C1.2 and C2.1 can be assigned respectively with CQS 2, CQS 2, CQS 3, CQS 4, CS 4, CQS 5, CQS 5, CQS 6 and CQS 6.

4.2 Final mapping after review of the qualitative factors

21. 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

⁷ If the total number of rated items over a 5 years period is larger than 10 times the number representing the inverse of the long run default rate benchmark associated with the equivalent rating category in the international rating scale, but at the same time this pool of ratings does not satisfy Article 3 ITS, then this pool of ratings is considered to be too large for the application of a small pool methodology.

⁸ It has to be noted that in this situation the proxy LRDR is formally not a LRDR, the latter needs indeed to be computed over at least 10 short run default rates. We are here abusing of the LRDR naming.

rating categories where quantitative evidence is not sufficient to test the default behavior⁹, as it is the case for all rating categories of Cerved's Corporate long-term rating scale.

22. The qualitative factors remain unchanged with respect to the mapping report published in November 2015. No amendments are proposed based on qualitative factors.

5. Mapping of Cerved's corporate short-term rating scale

23. Figure 4 presents the description of the short-term rating scale. Given that the default information referred to these rating categories cannot be comparable with the 3-year time horizon that characterises the benchmarks established in the Implementing Regulation, the internal relationship established by Cerved between these two rating scales (please see figure 5) will be used to derive the mapping of the short-term credit rating scale. This is in line with Article 13 of the Implementing Regulation and should ensure the consistency of the mappings proposed for Cerved.

- **S-1.** Superior capacity to meet short term financial commitments. Very low credit risk. It is internally mapped to rating categories A1.1 to A1.3, which are associated to CQS 1. Therefore the proposed mapping is CQS 1.
- **S-2.** Strong capacity to meet short term financial commitment. Low credit risk. It is mapped to the long-term scale rating categories A2.1 to A3.1, which are associated to CQS2. Therefore the proposed mapping is CQS2.
- **S-3.** Adequate capacity to meet short term financial commitment. Moderate credit risk. It is mapped to the long-term scale rating categories B1.1 and B1.2, which are associated to CQS3. Therefore the proposed mapping is CQS3.
- **V-1.** Vulnerable with weak capacity to meet short term financial commitments. Substantial credit risk. However, adverse economic conditions may impair its ability. It is mapped to the long-term scale rating categories B2.1 and B2.2. The most frequent CQS is 4, which is therefore the proposed mapping.
- **R-1.** Difficulty to meet short term financial commitments. High credit risk. It is internally mapped to rating categories C1.1, C1.2 and C2.1. The most frequent CQS is 6. Since the risk weights assigned to CQS 4 to 6 are all equal to 150% according to Article 131 CRR, the mapping proposed is CQS 4.

⁹ 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 ITS.



Appendix 1: Credit ratings and rating scales

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

SA exposure classes	Name of credit rating	Credit rating scale
Long-term ratings		
Corporates	Long-term issuer rating	Corporate long-term rating scale
Short-term ratings		
Corporates	Short-term issuer rating	Corporate short-term rating scale

Source: Cerved

Figure 3: Corporate long-term rating scale

Credit assessment	Meaning of the credit assessment
A1.1	Large company, with an excellent business and financial profile. Extremely strong capacity to meet financial commitments. Minimal credit risk.
A1.2	Large / medium-sized company, with excellent business and financial profile. Very strong capacity to meet financial commitments. Very low credit risk.
A1.3	Very good business and financial risk profile. Very good capacity to meet financial commitments. Very low credit risk.
A2.1	Very good fundamentals and high capacity to meet financial commitments. Low credit risk.
A2.2	Very good fundamentals and good capacity to meet financial commitments. Low credit risk.
A3.1	Good fundamentals and good capacity to meet financial commitments. Low credit risk.
B1.1	Adequate capacity to meet financial commitments. Potentially vulnerable to serious and unexpected changes in business, financial and economic conditions. Moderate credit risk.
B1.2	Adequate capacity to meet financial commitments. Vulnerable to serious and unexpected changes in business, financial and economic conditions. Moderate credit risk.
B2.1	Overall good fundamentals. Vulnerable to unexpected changes in business, financial and economic conditions. Credit risk is below average.
B2.2	Evidence of weaknesses in business and / or financial profile. Vulnerable to changes in business, financial and economic conditions. Credit risk is substantial but not far from the average.
C1.1	Serious weaknesses in business and / or financial profile. The company could not meet financial commitments. High credit risk.

Credit assessment	Meaning of the credit assessment
C1.2	Very serious weaknesses in business and / or financial profile. The company could not meet financial commitments. Very high credit risk.
C2.1	Very serious problems in economic and / or financial profile. The company could not meet financial commitments even in the short term. Maximum credit risk.

Source: Cerved

Figure 4: Short-term rating scale

Credit assessment	Meaning of the credit assessment
S-1	Superior capacity to meet short term financial commitments. Very low credit risk.
S-2	Strong capacity to meet short term financial commitment. Low credit risk.
S-3	Adequate capacity to meet short term financial commitment. Moderate credit risk
V-1	Vulnerable with weak capacity to meet short term financial commitments. Substantial credit risk.
R-1	Difficulty to meet short term financial commitments. High credit risk.

Source: Cerved

Figure 5 : Internal relationship between Cerved's long-term and short-term rating scales

Long term rating	Short term rating
A1.1	S-1
A1.2	
A1.3	
A2.1	S-2
A2.2	
A3.1	
B1.1	S-3
B1.2	
B2.1	V-1
B2.2	
C1.1	R-1
C1.2	
C2.1	

Source: Cerved

Appendix 2: Definition of default

According to Cerved definition, defaults include events all represented in data filed with public registers. In particular the definition of default that Cerved is going to adopt includes:

- Legal default: bankruptcy other legal proceedings, and debt restructuring stated in the Italian bankruptcy law (recorded by Chambers of Commerce);
- Non-legal default: these events are not considered as legal default by the Italian civil law, however they result in domestic public registers:
 - o relevant material protests on trade bills or cheques, filed in a public electronic register of protests
 - o other prejudicial actions (judicial mortgages, distraint of property), resulting in public register of properties and tax offices registers

Source: Cerved

Appendix 3: Default rates of each rating category

Figure 6: Number of weighted items¹⁰

	A1.1	A1.2	A1.3	A2.1	A2.2	A3.1	B1.1	B1.2	B2.1	B2.2	C1.1	C1.2	C2.1
01JAN2014	8.5	30	66	154.5	743.5	2402.5	3201	3232	3156	2041.5	740.5	398	243
01JUL2014	7.5	36.5	68.5	135.5	613.5	2161.5	2957.5	3154.5	3225.5	1904	840.5	446.5	193
01JAN2015	9	25.5	66.5	142	524.5	1852	2739	3312	3489	1900.5	960	490	166.5
01JUL2015	5.5	26.5	75	132	483	1636	2414	2852	2835	1478.5	775	422	140
01JAN2016	5.5	21	60	112	391	1255	1946.5	2440	2262.5	1135.5	589	330.5	105.5
01JUL2016	5	17	37	92	334.5	1033.5	1782.5	2520.5	2460	1191.5	649	352	97
01JAN2017	3.5	14.5	40.5	95	350.5	1093	1897	2822	3341.5	1676.5	819	407.5	91.5
01JUL2017	4.5	12.5	43.5	95	333	1099	1924.5	2809	3422.5	1719	741.5	351.5	80
01JAN2018	3	10.5	38.5	80.5	292	1094.5	1856	2710.5	3370	1693.5	742	361	87
01JUL2018	3	11	33	79.5	285.5	1075.5	1834.5	2671	3347	1698	716	362.5	75

Source: Joint Committee calculations based on CEREP data.

¹⁰ Withdrawn ratings have been weighted by 50% as indicated in Article 4(3) of the Implementing Regulation.

Figure 7: Number of defaults

	A1.1	A1.2	A1.3	A2.1	A2.2	A3.1	B1.1	B1.2	B2.1	B2.2	C1.1	C1.2	C2.1
01JAN2014	0	1	0	0	0	11	34	81	98	83	39	27	79
01JUL2014	0	1	0	0	2	13	33	77	103	93	91	87	79
01JAN2015	0	0	0	0	1	8	35	58	76	98	72	60	49
01JUL2015	0	0	0	0	2	5	24	42	45	62	46	54	39
01JAN2016	0	0	0	0	2	2	13	34	42	41	28	47	30
01JUL2016	0	0	0	0	0	2	10	30	40	29	26	37	21
01JAN2017	0	0	0	0	0	1	12	19	41	49	35	36	16
01JUL2017	0	0	0	0	0	1	6	17	34	49	34	24	23
01JAN2018	0	0	0	0	0	0	2	6	28	23	28	28	28
01JUL2018	0	0	0	0	0	0	0	1	10	13	9	26	15

Source: Joint Committee calculations based on CEREP data.

Figure 8: Mapping proposal for rating categories with a non-sufficient number of credit ratings

	A1.1	A1.2	A1.3	A2.1
CQS of equivalent international rating category	CQS1	CQS 1	CQS1	CQS2
N. observed defaulted items	0	2	0	0
Minimum N. rated items	0	1038	0	0
Observed N. rated items	36	139.5	336	676
Mapping proposal	CQS1	CQS 2	CQS1	CQS2

Source: Joint Committee calculations based on CERE data.

Figure 9: Proxy of the long-run default rate

	A2.2	A3.1	B1.1	B1.2	B2.1	B2.2	C1.1	C1.2	C2.1
CQS of equivalent international rating category	2	2	3	3	4	4	5	6	6
Long-run default rate	0.3%	0.4%	1.0%	1.9%	2.43%	4.5%	7.1%	13.2%	32.5%
Mapping proposal	2	2	3	3	4	4	5	6	6

Source: Joint Committee calculations based on CERE data.

Appendix 4: Mappings of each rating scale

Figure 4: Mapping of Cerved's Corporate long-term rating scale

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
A1.1	1	n.a.	1	The quantitative factors are representative of the final CQS.
A1.2	1	n.a.	1	The quantitative factors are representative of the final CQS.
A1.3	1	n.a.	1	The quantitative factors are representative of the final CQS.
A2.1	2	n.a.	2	The quantitative factors are representative of the final CQS.
A2.2	2	n.a.	2	The meaning and relative position of the rating category and available default experience are representative of the final CQS.
A3.1	2	n.a.	2	The meaning and relative position of the rating category and available default experience are representative of the final CQS.
B1.1	3	n.a.	3	The meaning and relative position of the rating category and available default experience are representative of the final CQS.
B1.2	4	n.a.	3	The meaning and relative position of the rating category and available default experience are representative of the final CQS.

B2.1	4	n.a.	4	The meaning and relative position of the rating category and available default experience are representative of the final CQS.
B2.2	5	n.a.	4	The meaning and relative position of the rating category and available default experience are representative of the final CQS.
C1.1	5	n.a.	5	The meaning and relative position of the rating category and available default experience are representative of the final CQS.
C1.2	6	n.a.	6	The meaning and relative position of the rating category and available default experience are representative of the final CQS.
C2.1	6	n.a.	6	The meaning and relative position of the rating category and available default experience are representative of the final CQS.

Figure 11: Mapping of Cerved's Short-term corporate rating scale

Credit assessment	Corresponding rating category long-term scale	Range of CQS of corresponding Long-term rating scale	Final review <i>based on qualitative factors</i> (CQS)	Main reason for the mapping
S-1	A1.1/A1.2/A1.3	1/1/1	1	The final CQS has been determined based on the most frequent step associated with the corresponding long-term credit rating category.
S-2	A2.1/A2.1/A3.1	2/2/2	2	
S-3	B1.1/B1.2	3/3	3	
V-1	B2.1/B2.2	4/4	4	The final CQS has been determined based on the most frequent step associated with the corresponding long-term credit rating category. The risk weights assigned to CQS 4 to 6 are all 150%, therefore CQS 4.
R-1	C1.1/C1.2/C2.1	5/6/6	4	