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SBP outlines Criteria for recognition of External Credit Assessment Institutions (ECAIs)

The State Bank of Pakistan has outlined the eligibility criteria for recognition of External Credit Assessment Institutions (ECAIs) for the purpose of implementing Basel II in the country.

The criteria, which have been developed after due consultation with various stake holders, will serve as a transparent policy document for evaluating and granting recognized status to ECAIs. This policy document will serve as a benchmark on basis of which the status of recognized ECAIs would be granted.

It may be pointed out that according to the roadmap for the implementation of Basel II in Pakistan issued by the State Bank in March, 2005, banks/DFIs are required to initially adopt Standardized Approach of the New Accord. Under this approach, the capital requirement against credit risk is determined on the basis of risk profile assessed by the External Credit Assessment Institutions (rating agencies) duly recognized by the supervisory authority.

The criteria provide a basis for the evaluation and recognition of the rating agencies that apply to SBP for eligibility for the purpose of Basel II. The Securities and Exchange Commission of Pakistan (SECP) will continue to remain the supervisory / licensing authority for credit rating companies in Pakistan and only those credit rating companies that are duly licensed by SECP under the Credit Rating Companies Rules, 1995, will be eligible to apply to the State Bank for Basel II recognition. The credit rating companies incorporated in Pakistan will also be required to follow the Code of Conduct for Credit Rating Companies issued by SECP.

All rating companies that meet the eligibility criteria and are interested in getting themselves recognized as ECAI for the purpose of Basel II, may apply to the Director, Banking Supervision Department, State Bank of Pakistan, Karachi, Mr. Jameel Ahmed by furnishing the required information / documents.

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The recognition shall mean that the banks can use ECAI's risk assessment rating of their portfolio for the calculation of capital requirement under Basel II.

The eligibility of applicant ECAI shall, interalia, be made on the basis of following:-

- ECAI should have methodology of assigning credit rating that is rigorous, systematic, continuous and subject to validation.
- The ECAI should be independent, free from economic or any external pressures that may influence its credit assessment.

-- The risk assessment of ECAI should be available to both domestic as well as foreign institutions on equivalent terms.

-- In order to promote transparency and enable its stakeholders to make decisions about the appropriateness of its risk assessment methodology, ECAI should disclose enough information. The information at minimum includes, the rating definition, general methodology for arriving at rating, the rating process, time horizon of rating and the surveillance and review procedure.

-- ECAI should demonstrate that it provide access to information that are sufficient to enable its stakeholders to make decision about the appropriateness of risk assessments. The purpose of this disclosure requirement is to promote transparency and bring in market discipline.

-- ECAI should possess sufficient human and technical resources to carry out high quality credit assessment.

-- ECAI must demonstrate that it enjoys credibility in the market where it operates.

In case any recognized ECAI is subsequently found non-compliant with any of the prescribed eligibility conditions or is found non-compliant with any other instructions issued by the Sate Bank from time to time, the State Bank may withdraw its status of recognized ECAI and prohibit banks to use the credit ratings of that ECAI for the calculation of their capital requirement. **(For eligibility criteria and documents details, please visit our website: www.sbp.org.pk)**