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Credit rating agency sector needs more competition, experts say

An oligopoly of three U.S.-based credit rating agencies has posed threats to financial markets worldwide according to experts, because their extreme power allows them to make manipulative decisions

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The fact that only three credit rating agencies determine the credit ratings of millions of companies, thousands of security exchanges and dozens of countries worldwide is causing "serious problems," according to some experts. Even though there are nearly 80 credit rating agencies worldwide, Standard and Poor's, Moody's and Fitch Ratings are known as the "Big Three" who control nearly 95 percent of the sector.

These three U.S.-based agencies have been criticized by some for what they see as manipulative decisions, along with the extreme power they have gained due to the oligopoly they created in the rating sector. Experts say a more competitive rating sector will provide a more objective and trustworthy service to investors and markets.

Profits affect credit ratings

Companies, public institutions and even states are obliged to apply to these agencies, since they play an important part in various situations such as finding finance with credit rating-efficient conditions, issuing bonds and securities and opening to the public.

With annual prices for obtaining credit ratings starting from $100,000, firms and countries naturally want to work with the credit rating agency that gives them the highest rating. International banks and fund holders also request those asking to borrow money to bring credit ratings from the "Big Three."

A majority of sector representatives in Turkey, including economists, investors and politicians, think it is impossible for the big credit rating agencies that dominate the sector to make objective assessments about the financial positions of those paying money to obtain ratings.

Additionally, the theory that credit ratings, which are crucial in terms of borrowing cost and investments, are based on political reasons rather than economic indicators has caused debates in the sector.

Credit rating agencies should not seek profit

In the U.S., the homeland of the "Big Three," it is notable that Democrat and Republican senators have said, "While credit rating agencies compete with one another to present the best credit ratings to the firms in order to increase their own market values, they have lowered their standards," in a report they jointly submitted to Congress. Former European Central Bank President Jean Claude Trichet and German Finance Minister Wolfgang Schaeuble are among the European politicians who stress that the oligopoly in the rating sector should be broken down.

President Recep Tayyip Erdoğan is a leading voice among those criticizing the ideological approach of the credit rating agencies. Claiming that the country-oriented credit rating system did not work, former Chinese President Hu Jintao also called for "more objective, just and reasonable standards."

Thomas Straubhaar, a director at the Hamburg Institute of International Economics (HWWI), said: "Credit rating agencies whose aims are to maximize their profits should not be allowed to make decisions that bind the third parties as if they were judges."

Bernie Sanders, who is serving as a junior United States Senator from Vermont and ran as the Democratic Party's potential candidate for president of the United States, also thinks credit ratings agencies with strong relations to Wall Street should be restructured. Believing that these agencies should not seek profit, Sanders asserts that some agencies shape their credit ratings in regards to profit.

Agencies triggered the financial crisis

The credit rating agencies' part in the 2007-2008 global crisis proves these criticisms right. According to investigations conducted by the U.S. Congress, Securities and Exchange Commission (SEC) and the U.S. Department of Justice, S&P and Moody's have misled investors for years by giving undeserved, high ratings to derivative products consisting of low-quality mortgage loans in order to increase their profits.

Following this, S&P had to pay $1.5 billion in compensation costs to the U.S. government last year.

The Department of Justice's investigation into Moody's is still under way. The relevant sources foresee that Moody's, which has accepted that it made incorrect ratings, will pay compensation costs to close the investigation as well. Fitch, which is younger and smaller compared to the other two, was not involved in the investigations.

Rating sector needs more competition

Speaking to Anadolu Agency, Mark Calabria, director of Financial Regulation Studies at the

Washington-based Cato Institute, said, "A more competitive rating sector can serve the markets better." Indicating that the rating sector should be audited, Calabria pointed out that companies should be able to work with the rating agencies that they want.