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Upgrade History of China's Sovereign Credit Rating by S&P, Moody's and Fitch Ratings

The Chinese government's refusal to honor repayment of its defaulted sovereign debt first became widely published in June 2001. Since that time, the three primary NRSROs have upgraded China's international sovereign credit rating (i.e., the "long-term foreign currency sovereign credit rating" assigned to China) **ten (10) times**, as follows:

S&P: Assigned initial rating in 1988 and seven (7) subsequent upgrades, five (5) of which occurred post-June 2001:

Assigned "Satisfactory" rating classification (July 1988)

From "Satisfactory" to "BBB" (February 1992)

From "BBB" to "BBB+" (May 1997)

Reclassified from "BBB+" to "BBB" (July 1999)

From "BBB" (affirmed in 2001) to "BBB+" (February 2004)

From "BBB+" to "A-" (July 2005)

From "A-" to "A" (July 2006)

From "A" to "A+" (July 2008)

From "A+" to "AA-" (December 2010)

S&P has maintained an "investment grade" rating for China since 1992, which S&P defines as an issuer not having any defaulted full faith and credit sovereign debt outstanding and unpaid. Note that S&P affirmed China's "investment grade" credit rating the very next day (October 22, 2003) following the Congressional hearing on the ABF, in order to strengthen the sale of China's sovereign bonds and notes registered in the U.S. the same month (October 2003). Compare the published definition of China's prevailing artificial investment grade rating with the definition of the truthful rating of "Selective Default":

http://globalsecuritieswatch.org/Sovereign_Ratings_Definitions_and_Criteria

Moody's: Assigned the first credit rating to China (which China denied seeking: http://www.globalsecuritieswatch.org/China_Denies_Seeking_Sovereign_Credit_Rating) in 1988 and four (4) subsequent upgrades, three (3) of which occurred post-June 2001:

Assigned "A3" rating classification (May 1988)

Reclassified from "A3" to "Baa1" (November 1989)

From "Baa1" to "A3" (September 1993)

From “A3” to “A2” (October 2003)

From “A2” to “A1” (July 2007)

From “A1” to “Aa3” (November 2010)

Fitch Ratings: Assigned initial rating in 1997 and two (2) subsequent upgrades, both of which occurred post-June 2001:

Assigned “A-” rating classification (December 1997)

From "A-" to "A" (September 2006)

From "A" to "A+" (November 2008)

[Above data is current as of July 07, 2012]

The following information is directly pertinent to the periodic upgrades:

United States Department of Justice
Civil Racketeering and Antitrust Complaint:

http://www.globalsecuritieswatch.org/DOJ_Antitrust_Complaint

Supplemental Information:

1. Explicit notification (i.e., constructive notice) was provided to Norman Feit, Senior Counsel to Goldman Sachs for Regulatory Affairs and Compliance, in a letter dated January 2, 2002. This is important because Goldman Sachs served as the credit rating adviser to China in 2003 as regards the sovereign notes and bonds registered in the United States and sold by China in 2003. The 2002 letter included the following enclosure:

http://www.globalsecuritieswatch.org/Sovereign_Rating_Research_Bulletin/China.pdf

2. Explicit notification (i.e., constructive notice) was again provided to the Chief Executive Officers of all three primary NRSROs in a letter dated November 27, 2002:

http://www.globalsecuritieswatch.org/letter_to_Moodys_from_ABF

3. The prevailing artificial ratings assigned to China by the three primary NRSROs were included in the specifications describing the wrongful actions of certain parties in a letter dated April 8, 2004 sent to the Hon. Eliot Spitzer, Attorney General for the State of New York (see pages 11-17):

http://www.globalsecuritieswatch.org/Letter_to_EliotSpitzer_AG_New_York_from_Sovereign_Advisers.pdf

4. Explicit notification (i.e., constructive notice) was provided yet again in a letter dated May 18, 2006, which was sent via certified U.S. mail to the Chief Executive Officers of each of the three primary NRSROs:

http://www.globalsecuritieswatch.org/Letter_from_Sovereign_Advisors_to_Standard_and_Poor's_Corporation

5. Note that S&P upgraded China most recently during July 2006. Also note that both this upgrade, as well as the previous upgrade during July 2005, occurred subsequent to the Financial Times articles on China's defaulted sovereign debt (June 7, 2005), which articles included comments by senior representatives of the credit rating agencies:

http://www.globalsecuritieswatch.org/Financial_Times

On July 31, 2008, the very same day that S&P upgraded China's artificial sovereign ceiling in a bid to profit from the expanded debt issuance capability of Chinese corporations, S&P immediately upgraded the corporate ratings of eight Chinese companies:

http://www.alacrastore.com/storecontent/spcred/662522

A recent investigation by the United States Securities and Exchange Commission found numerous instances of wrongful practices routinely engaged in by S&P, Moody's and Fitch Ratings:

http://www.globalsecuritieswatch.org/SEC_Report_to_Post_on_GSW_Website.pdf

S&P insiders subsequently admitted to orchestrating an artifice responsible for the creation of artificial credit ratings in order to win Wall Street business and profit from increased investor demand for highly, albeit falsely, rated securities:

http://www.pbs.org/now/shows/446/video.html

In response to the wrongful practices of the three primary international credit rating agencies, the United States Congress has introduced concurrent House and Senate resolutions exposing China's artificial sovereign credit rating:

Senate Concurrent Resolution 78:

http://globalsecuritieswatch.org/S.Con.Res.78.pdf

House Resolution 1179:

http://globalsecuritieswatch.org/House_Con_Res_1179.pdf

The Office of the Chief Counsel for the United States Securities and Exchange Commission is in possession of evidence that the actions of S&P, Moody's and Fitch Ratings knowingly exclude and intentionally conceal certain actions of the government of the People's Republic of China including repudiation of China's full faith and credit sovereign debt:

http://www.globalsecuritieswatch.org/SEC_Conference_Brief.pdf

http://www.globalsecuritieswatch.org/Amended_SEC_Complaint.pdf

http://www.globalsecuritieswatch.org/Sovereign_Disclosure_Obligation.pdf

European financial markets regulators are also presently developing regulations intended to halt conflict of interest abuses by S&P, Moody's and Fitch Ratings:

http://www.globalsecuritieswatch.org/EU_Consultation%20_Public_Comment_(Short_Version).pdf

6. EuroWeek Capital Markets magazine published two separate articles related to China's artificial sovereign credit rating (April 2005 and July 2006). The 2006 article contained denials of wrongdoing from S&P, Moody's and Fitch.

7. Moody's most recently upgraded their rating on July 26, 2007 from A2 to A1. Both Standard & Poor's and Fitch Ratings presently maintain a "positive outlook" for China, which indicates an imminent upgrade by both agencies. The higher the rating, the more issuers such as corporations and sovereign governments will pay for the rating in order to issue debt. Moody's freely admits on their website visitor agreement that they may charge issuers upwards of $1 million for a single credit rating! Moody's has also attempted to solicit Chinese corporations to obtain ratings and issue debt globally on the basis of China's pretextual sovereign credit rating:

http://globalsecuritieswatch.org/Moody's-Promotion.pdf

Moody’s is also a joint venture partner with China in establishing local credit rating services in order to boost ratings revenue from expanded debt issuance capabilities of Chinese corporations by virtue of China’s artificial sovereign rating (“sovereign ceiling”):

http://www.globalsecuritieswatch.org/Moody%27s_Announces_Joint_Venture_with_China.pdf

8. In addition to the complaints filed with the SEC and the GAO, a comprehensive description of the wrongful actions of the primary international credit rating agencies as regards China, including an excellent analysis by the Washington Post of the conflicted and self-serving business practices of the international credit rating agencies, is accessible at:

http://www.globalsecuritieswatch.org/Wrongful_Actions_of_the_International_Credit_Ratings_Agencies

9. A narrative describing China's artificial sovereign credit rating is accessible at:

http://www.globalsecuritieswatch.org/Forbes_Article.re.China's_Artificial_Sovereign_Credit_Rating

10. It is revealing to note that China reportedly denied seeking a credit rating in 1988, after which it bought and paid for a rating from S&P which concealed China's defaulted sovereign debt.

http://www.globalsecuritieswatch.org/China_Denies_Seeking_Sovereign_Credit_Rating

As demonstrated by our research into this matter, the prevailing "investment grade" sovereign credit ratings assigned to the communist Chinese government by the three primary NRSROs evidence the application of a reckless standard of care, when compared to their respective published definitions.

Dissimulation of liabilities facing current and future creditors of the Government of China.

By virtue of the successor government doctrine of settled international law, sovereign Chinese Government debt issued prior to 1949 ranks pari passu with contemporary debt such as Chinese Government sovereign bonds quoted in Luxembourg. As a result, present and future holders of contemporary Chinese Government debt are faced with the risk of seeing holders of pre-1949 full faith and credit bonds seeking attachment, as they will undoubtedly do, of payments of interest or capital due to Luxembourg-quoted bondholders absent a proportional payment to pre-1949 bondholders. Such risk is at present dissimulated from holders of contemporary debt as a consequence of China's artificial investment grade rating.

Possible motivation explaining failure of agencies to include information that is relevant according to their rating process.

It is **essential** to understand that by virtue of the 'sovereign ceiling' custom, rating agencies do not normally assign a rating to any one private or public issuer of a given country that is higher than the rating assigned to that country's government. Therefore, if the rating agencies had rated China in 'default', they would have needed to rate any and all Chinese corporate issuers as 'defaults'. As a consequence they would have been deprived of the rating fees from every single Chinese corporate issuer, and not only of the fees for rating the Chinese Government, over the period since post-1949 China re-emerged in western capital markets.

By rating the Chinese Government in default - as rating methodologies clearly show agencies should have done - the agencies would have automatically forfeited the revenue stream from the entire country; this amounts to a revenue shortfall in the billions of dollars for the three leading rating agencies.

The conflict of interests is therefore much more powerful than in the case of 'structured products' ratings, because assigning a bad rating to a sovereign deprives an agency of the revenue flow **from an entire country**, and not from an isolated structured product arranger.

This had been very clearly pointed out by Mr. Helmut REISEN, head of OECD's research division as early as 1998:

"... Furthermore, the rating agencies derive most of their revenue from those states that use their services; they are therefore reluctant to downgrade their ratings. The fear of displeasing their clients and of witnessing a reduction in the demand for their services and in the associated revenue can lead to some rigidity in downgrading country ratings in times of excessive capital influx."

Sean EGAN, managing director of the independent EGAN JONES rating agency (independent: i.e. paid by investors, not by issuers) clearly sums up the matter:

"*Our ratings are published to inform investors as best we can. The job of Moody's, S&P, or Fitch, is to publish ratings which facilitate the issuance of securities, which is fair enough since issuers account for 80% of their revenue.*"

And in his Washington testimony before the *House Committee on Oversight and Government Reform* on October 22nd 2008 he stated about the **SEC Proposal to Amend NRSRO Regulations** that

"*they proceed from the erroneous premise that the major rating agencies are in the business of providing timely and accurate ratings for the benefit of investors when, in fact, these companies have, for the last 35 years, been in the business of facilitating the issuance of securities for the benefit of corporate issuers and underwriters, i.e., the entities which pay them*".

http://fr.rian.ru/business/20090129/119877069.html

In French; abbreviated translation as follows:

Davos: Russia points a finger at the rating agencies

(...) Russia advocates a change in the business model of rating agencies, declared Arkadi Dvorkovitch, an adviser to the Russian president, in an interview with Vesti television.

"*independent ratings are necessary to allow countries to act in a concerted manner to fight the crisis*" said the expert.

(...)

"*A discussion about the business model of the agencies is necessary*", he said.

"*We must return to the system of agencies paid not by the issuer but by the rating user*".

Jan 27th 2009 speech by C. McCreevy:

http://209.85.229.132/search?q=cache:pLoNJp_5MeEJ:europa.eu/rapid/pressReleasesAction.do%3Freference%3DSPEECH/09/23%26format%3DHTML%26aged%3D0%26language%3DEN%26guiLanguage%3Den+mccreevy+issuer+pay+basel&hl=fr&ct=clnk&cd=3

"The regulation I have proposed for them - including the registration and governance requirements - should go some way towards taming the significant shortcomings of the issuer pays credit rating model. So should the due diligence requirements in the revised CRD proposal. But, to be frank, I believe it is very doubtful whether ratings by **issuer-pay** rating agencies should, in the longer term, be used at all for the purposes of determining risk weightings on rated securities or loans. This I hope will be an issue that will be reviewed within the context of the G20 work."

Moody's upgrades HK and China

HONG KONG, China (Reuters) --International ratings agency Moody's Investors Service upgraded its debt ratings on China and Hong Kong in a move that will further tempt investors to snap up China's upcoming $1 billion bond.

Moody's on Tuesday raised its foreign currency debt rating on China by one notch to A2 from A3, putting China just four notches below the agency's top AAA level.
It raised Hong Kong's foreign currency ratings, which apply to bonds and bank deposits, by two notches to A1 from A3.
The move pushed forwards contracts on the Hong Kong dollar and China's yuan higher, a sign that investors expected these currencies to strengthen in coming months despite the fact that both are pegged to the U.S. dollar.
Moody's said the rating outlook on both Hong Kong and China was stable, meaning it is not likely to shift the new ratings anytime soon.
The move follows an upgrade of China's long-term foreign currency rating outlook by Fitch Ratings on Monday and comes as China kicks off investor presentations for a global bond sale, its first since May 2001, which will also include a 500 million euro bond.

HK ahead of China

Moody's said that although Hong Kong and China were becoming more closely linked, via projects such as the planned bridge linking Hong Kong to Macau and Zhuhai, the former British colony's freer economy and stronger institutional structure justified its higher rating.
"The ratings upgrade is justified because things in Hong Kong are really improving," said Henry Tsoi, senior economist at Hang Seng Bank.
Moody's cited Beijing's policy of keeping its foreign debt, both government and private sector, at a prudent level as a major reason for China's upgrade.
China's economy is growing around eight percent a year with exports leading the charge helped by a flood of foreign investment in its factories.
The surge in foreign investment, growing export revenues and speculative funds betting that China will allow its currency to appreciate in coming months have led to a dramatic rise in the country's foreign exchange reserves.
At the end of August these reserves stood at $364.7 billion, second only to Japan's.
"These factors make even more remote the possibility that the central government would default on its foreign currency bonds," Moody's said in a statement.
"Official foreign exchange reserves that are close to twice the total amount of

external debt make for an exceptionally strong external payments position," it said.
George Leung, China economist at HSBC in Hong Kong, said Moody's move was justified and not really surprising for markets.
"They have cited accumulation of foreign reserves and the strengthening ability to meeting external payments. It is all quite visible in the past year, so it's not surprising and neither exciting for the market because everyone has been well aware of the situation," he said.