Fund managers, insurers now look beyond rating agencies

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Tighten internal investment analysis and assessment processes after IL&FS crisis

It's a case of once bitten, twice shy for a large number of insurers and fund managers who no longer choose to blindly invest in AAA-rated corporate paper, but delve beyond the numbers into the management profile of the companies they invest in.

After the default by Infrastructure Leasing and Financial Services (IL&FS) last year, insurers, who are big buyers of NBFC paper, no longer blindly trust ratings and have beefed up their internal investment analysis wings. "Earlier, AAA rating was the main criterion for investing in non-convertible debentures, but IL&FS has been a big lesson for us all that we should not depend only on rating agencies. Now, we actively look into companies that we plan to invest in and look beyond the financials into corporate governance and processes and the management team and promoters," said the investment manager of a public sector general insurer.

This was also confirmed by private sector insurers who said that they no longer just rely on rating agencies. "Strong credit evaluation and pricing of credit risk was not properly done in India. AAA corporate was 40-50 basis points over G-Secs," said Anurag Jain, Chief Investment Officer at Canara HSBC OBC Life Insurance. "Our investment committee guided us to build a shadow rating framework, where we would evaluate our own credit evaluation models that are much more stringent than the rating agencies.

"Besides numerical parameters, it also focuses on softer issues such as quality of company, management, auditor comments, group-level exposure and leverage," he said, adding that it has also beefed up the investment team. Ashish Vohra, Executive Director and Chief Executive Officer, Reliance Nippon Life Insurance, said the insurer has tightened its investment analysis and assessment processes. "We are trying to be less dependent on rating agencies," he said. The default by IL&FS took most market participants by surprise as it had enjoyed good ratings – largely of the highest grade – from most rating agencies. Since then, the infrastructure conglomerate has been downgraded to junk status, with debt of more than ₹91,000 crore. The role of rating agencies has also come under the scanner of SEBI.

"No one has seen an event on the scale of IL&FS unfurling in India before, though there have been sporadic one-off events. Most fund managers, including those of pension and retirement funds, mutual funds, and even banks are now being extra cautious of the companies that they invest in and don't just look at the ratings," said an expert who looks after investments of private PF trusts.

Since the IL&FS crisis, issues have also flared up in other NBFCs such as DHFL and a number of housing finance companies.

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