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Government

A rating agency evaluate the creditworthiness of organisations that issue debt in markets and gives ratings to this entities according to how safe it is to lend money to them. This includes the debts of corporations, nonprofit organisations, and governments, as well as " securitised assets" – which are assets that are bundled together and sold as a security to investors. Rating agencies assign a letter grade to each bond, which represents an opinion as to the likelihood that the organisation will be able to repay both the principal and interest as they become due.

Credit rating agencies are meant to provide global investors with an informed analysis of the risk associated with debt securities. These securities include government bonds, corporate bonds, certificates of deposit (CDs), municipal bonds, preferred stock, and collateralized securities, such as collateralized debt obligations (CDOs) and mortgage-backed securities. The riskiness of investing in these securities is determined by the likelihood that the debt issuer—be it a corporation, bank-created entity, sovereign nation, or local government—will fail to make timely interest payments on the debt. Ratings are made on a descending scale: AAA is the highest, then AA, A, BBB, BB, B, etc. A rating of BB or below is considered a " junk bond," because it is likely to default. Many factors go into the assignment of ratings, including the profitability of the organisation and its total indebtedness. The " Big Three" global credit rating agencies are Standard & Poor's (S), Moody's and the Fitch Ratings.

These are the main three independent rating agencies, the first two of them being American firms and the third one British. Of corse the investors can decide by themselves what to do with their money and in what entities to invest. But the rating agencies Principal-Agent Theory analyzes the relation between principal and agent, the problems that might occur within this relation and the institutions that can help to reduce these problems. An agent, the rating agency in above mentioned case, is a person who is performing an act for another person, called the principal. At the same time, the company, the so-called principle, is a person for whom another person, called the agent, is performing some act. This relation occurs because the agent can fulfill this task potentially better/at a lower cost than the principal itself.

This relation has both advantages and desatvantages, but the aim are the gains from cooperation. Instead of rating agencies and companies that issue debt, there are a lot of others players on the market that have a collaboration based on principal-agent-theory. As examples may serve the company owner and the manager, the investor and the bank, the bank and the borrower, and so on. The principal assigns an agent to act for him because the agent can fulfill this task potentially better/at a lower cost than the principal itself.

The agent has, for example, other skills or talents, better information or contacts. But there can appear some problems. The principal and the agent have different utility functions and the principal must outlay expenses to control the agent. The expenses incurred to control provide the agent with a monopolistic scope of action and the net-benefit of the principle is reduced