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Performing the Politics of Creditworthiness: The Uncertainty of Rating European Sovereign Debt

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As Member States struggle to retain the investment grades necessary to allow them to finance their governmental operations at a reasonable cost, credit rating agencies (CRAs) have been blamed for exacerbating a procyclicality which only makes this task more difficult. How CRAs contribute to the constitution of the politics of limits underpinning the European sovereign debt crisis is at the core of this article. As a socio-technical device, sovereign ratings are an 'illocutionary' statement about budgetary health. An artificial fiscal normality is promoted. Subsequently, this austere politics of creditworthiness has 'perlocutionary' effects, which seeks to censure political discretion through normalising risk techniques aligned with the self-systemic, and thereby self-regulating, logic of Anglo-American versions of capitalism. By tracing the performative effects of the European Securities and Markets Authority (ESMA) registration process and the regulatory technical standards (RTS) on CRAs, investors and Member States, how sovereign ratings obtain their authority is revealed. The ensuing antagonistic relationship between the programmatic/ expertise and operational/ politics dimensions of fiscal governance leaves the socio-technical *agencement* vulnerable to misfire and the renegotiation of how the 'political' is established in the economy.

Keywords: credit rating agencies; European Union; risk and uncertainty; sovereign debt crisis; financial governance

Introduction

What actually constitutes the real risk of sovereign debt default? This question has been the focus of much scrutiny during the recent stages of the Europe's sovereign debt crisis. With escalating contagion threatening to engulf the eurozone's larger periphery economies, including Italy and Spain, discussions of the 'rescheduling', 'reprofiling', or 'soft restructuring' of Greek debt are more pronounced around Brussels. Although at first adamantly opposed by the European Central Bank (ECB), after their 21 July 2011 Euro Area Summit, European Union (EU) politician finally admitted what financial markets had long suspected: Greece has little alternative but to restructure its debt obligations. Reiterating their previous warnings, the main three credit rating agencies (CRAs) – Moody's Investor Services, Standard & Poor's (S&P) and Fitch Ratings– announced that Greece's failure to meet its interest or principal payments in a timely fashion or on 'less favourable terms' constitutes

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‘selective’ default (Standard & Poor’s 2011a). Moody’s confirmed that ‘the probability of a distressed exchange, and hence a default, on Greek government bonds is virtually 100%’ (Moody’s Investor Service 2011a).

So widely expected but vehemently denied, the western developed world is now preparing for its first national debt default in sixty years. It is compelling to concede that this blow simply signals the further authoritative ascendance of CRAs and the continued descendence of EU governments. A second Greek bailout package (109 billion euros) may provide beleaguered periphery economies some reprieve from the market onslaught but that can only be temporary as the structural factors underpinning chronic uncompetitiveness and fiscal profligacy remain unsolved. Arguably, the default and battle between the EU and CRAs is a recent occasion for the more pressing puzzle which is ultimately about the politics of limits and the ability of governments to establish the parameters of the political within the economy.

Given their poor track record, how do CRAs exercise such authority over governments and financial markets? Insofar as ratings help constitute a fiscal normality what does this signify for European political economy? How does the new CRA regulatory framework – Regulation (EC) No 1060/2009 (CRA Regulation v1), the (EU) No 513/2011 (CRA Regulation v2) – effect EU attempts to manage the politics of creditworthiness surrounding sovereign debt and instil greater stability in the eurozone? To answer these questions, this article analyses how the act of rating sovereign debt normalises a fictitious bifurcation between the economy and politics through the regenerative dominance of the discourse of (quantitative) risk and its false dichotomy with (qualitative) uncertainty. Sovereign rating ranges rest on a judgement – codified and commercialised as the ‘risk of default’ – about ‘the capacity and willingness’ of governments to raise the necessary resources for the timely servicing of their debt obligations (Moody’s Investor Service 2008:

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4). Probability of payment depends on the tolerability of austerity and the costs of adjustment.

Yet the 'pain' threshold which a constituency can endure fluctuates according to its changing political economy. It escapes prescient quantification as a probability distribution through the utilitarian calculus of risk. Unfortunately, as I argue, CRAs' recursive search for certainty equivalence in the budgetary relations of European governments simply distorts the contingent liabilities involved in the construction of these ratings. This subjects European fiscal politics to an artificial uniformity while invalidating how competing notions of budgetary normality are ascertained and articulated. Misguided EU policies only aggravate these tensions making governments and financial markets more vulnerable to destabilising effects.

Divorcing technoscientific epistemology from its messy politico-economic context, sovereign ratings serve as 'fugitive social facts' (Holmes and Marcus 2005: 237), which grant CRAs exorbitant authority over the politics of creditworthiness. Analogous to Donald Mackenzie's (2005a) 'black boxes', sovereign ratings must be unpacked. This helps us understand how they produce a misleading fiscal normality exogenous of national contexts, which is aligned with a self-systemic, and thereby self-regulating, logic of Anglo-American versions of capitalism. Sovereign credit ratings are the internal forms of governmentality involved in the reiteration, re-establishment and sedimentation (Butler 2010: 149) of this politics of limits underpinning European budgetary relations.

Against this mentality, Member States creditworthiness is assessed and, thus their capability to perform the fundamental functions of 'government' (i.e. provide for their citizens) is hindered. Political discretion becomes increasingly marginalised as normalising mathematical models depoliticise the decision-making process (de Goede 2004; Luhmann 1993). Of course, as Timothy Sinclair (2005: 58-59) reminds us, this adjustment of the diachronic through the synchronic produces explosive effects – illustrated by the

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European debt crisis – as fiscal sovereignty unleashes unsuspecting forces contingent on the 'singular nature of sovereignty' and its vicissitudes (Moody's Investor Service 2008a: 6).

What is revealing is how this predication on the hegemonic discourse of risk actually fails to secure organisational integrity; instead precipitating volatility and breakdown. Tensions flare and crisis looms as this artificial fiscal normality imposes unbearable socio-political costs on the populations of heterogeneous economies. As it ruptures, it engenders an antagonistic relationship between the programmatic (expertise/risk) and operational (politics/uncertainty) dimensions of fiscal governance. What constitutes as the 'political' in the economy becomes revealed and renegotiated. Technical practices become susceptible to (re)politicisation – albeit temporarily. Now the ECB will accept Greek defaulted bonds as collateral and a partial ban on short-selling of financial stocks was introduced by France, Italy, Spain, and Belgium

Research from both the 'social studies of finance' (Callon 1998; Knorr Cetina and Preda 2005; Langley 2008; MacKenzie 2006) and 'governmentality' (Dean 1999; O'Malley 2004; de Goede 2005; Aitken 2007) fields provide a number of promising intellectual points of departure in the analysis of this politics of creditworthiness. One of the most pivotal to our understanding of CRAs is the discursive constitution of the infrastructure of referentiality underpinning finance. Meaning and materiality must be studied together. Unfortunately, lacking the necessary analytical tools, conventional international political economy (IPE) neglects how ratings act as a socio-technical device to modulate the discursive construction and representation of (European) sovereign debt as a problem of government.

This article seeks to problematise this force of performativity by tracing the effects of sovereign ratings and the corresponding EU regulatory response in the constitution of three subjects of government involved in the European debt crisis; namely CRAs, investors, and Member States. Mapping how these

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calculative practices enable particular subjectivities and stabilisations in the European political economy provides an enhanced understanding of how authority is practiced in devising an infrastructure of referentiality according to which fiscal profligacy is assessed and corrective measures proposed (e.g. default). By challenging the prior ontological status of agency and interests, I suggest how financial discourse, as a 'technology of thought', shapes their very actualisation (Miller and Rose 1990: 5).

In order to demonstrate the exigency of this enterprise, the article focuses on how the category of performativity enhances our grasp of the problematic. Sovereign ratings, as a discursive practice, have 'illocutionary' effects (Austin 1962; Callon 1998; MacKenzie 2006). Through their description of budgetary positions, they communicate notions of proper fiscal conduct which inform the constitution of the politics of limits. Deconstruction exposes how, framed as binary opposites, the dialectical relationship between risk and uncertainty is distorted; thereby embedding risk as the dominant modality informing this performance.

Subsequently, these austere politics of creditworthiness have 'perlocutionary' effects on the broader EU assemblage which dictate how fiscal sovereignty is exercised. Lacking a 'felicitous set of circumstances' (Butler 2010: 151) anchored in the realities of budgetary sovereignty, reconstruction of the lineages where this inscription takes place highlights the contestation and instability implicit in organising fiscal relations in accordance with a mentality promoting the strict censure of political discretion (government through uncertainty) through normalising quantitative techniques.

To demonstrate this position, the first part of the article documents serious inconsistencies in the analytics of ratings which amplify the asymmetric authority exercised by CRAs. As the dominant mentality of rule, risk recodes the place of the state in the economic discourse. Sovereign ratings are implicated in this performativity. The second part argues how their authoritative capacity is reinforced by a misguided EU regulatory response.

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Arguably, the EU is sabotaging its own core ambitions – minimising an overreliance on external ratings and injecting competition into the ratings space – through the European Securities and Markets Authority (ESMA) registration process and flawed supervisory mechanics. Here I trace how these performative practices have self-validating/self-generative effects on CRAs, constitutive effects on investors, and unintended (prohibitive) consequences for beleaguered national governments. Together this matrix normalises a volatile stabilisation based on a politics of limits which privileges the discourse of risk over the government through uncertainty by entrenching a false quantitative/qualitative dichotomy in the determination of creditworthiness. Crisis shocks the EU as the authoritative capacity of perlocution to instil the separation between the economy and politics diminishes as fiscal sovereignty reasserts itself.

Uncertainty of Rating Sovereign Debt

Underpinning the practice of ratings is the discourse of risk which attempts to aggregate contingent fiscal relations into a calculable measure of variance around an expected value (Beck 1992; Bernstein 1998; Friedman and Savage 1948; Hardy 1923). Adherence to a predictive positivism claims to align sovereign ratings with the infallibility of a rationalist-empirical epistemology and methodology. A fictitious dichotomy between (quantitative) risk and (qualitative) uncertainty is promoted; whereby the former is perceived as a tangible phenomenon tractable to rational choice modelling and equilibrating outcomes but uncertainty cannot be assigned a definite numerical probability (Reddy 1996; Short 1992).

A strict binary opposition, however, between risk and uncertainty should be avoided. Their relationship, as Pat O'Malley (2000) contends, is not one of mutual exclusion but contestable and heteromorphic. Determining the actual displacement of one by the other, in a painstaking attempt to unearth their supposed ontological properties, distracts from the more interesting

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governmental puzzle; namely how the modalities of risk and uncertainty help constitute the problem of sovereign debt. Instead, O'Malley (2004: 174) invites us to consider the '*redistribution and reshaping*' of these calculative techniques (original italics). This reveals egregious inconsistencies in how uncertainty is appropriated for the purposes of fiscal governance.

On the one hand, uncertainty is denounced if synonymous with government spending. Here risk's performative properties help frame the European sovereign debt debate by making EU fiscal relations intelligible according to a specific Anglo-American market mentality that prizes austerity and low budget deficits. Binding concessions are thought to prevent governments from compromising stable prices, which help protect the value of assets (Roy, Denzau and Willet 2007). Expansionary fiscal policies threaten this disinflationary objective of monetarism (Friedman 1962).

From 9.1 per cent in 2010 to a projected 5.9 per cent in 2011, the Portuguese public budget deficit may be inching down but, according to Moody's (2011b,) not fast enough to satisfy its 2013 Excessive Deficit Procedure (EDP) target of 3 per cent. Irrespective of its consolidation programme, Greece faces 'medium-term solvency challenges' as 'its stock of debt will still be well in excess of 100% of GDP for many years' (Moody's Investor Services 2011a). In short, 'political imperatives only compromise economic fundamentals, impeding the efficient operation of the market mechanism' (Hay 2007: 56). Policy discretion is a liability to be mitigated.

On the other hand, uncertainty is embraced by market participants for its entrepreneurial spirit (Keynes 1921/1979; Knight 1921/1964; Peters 1987). By targeting the latent creative capacity of individuals as self-regulating subjects, free-market virtues are extolled and uncertainty is perceived as a profitable opportunity to be exploited. Most evident in the construction of sovereign ratings is a 'diagnostic' form of uncertainty which 'implies the presence of expert judgment' (O'Malley 2004: 24).

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Yet, whereas deployed by governments, uncertainty is considered toxic and corrosive, its (discreet) appropriation by CRAs – and the corporate sector more broadly – is condoned; even celebrated as being alert to local dynamics. Such asymmetry fuels an ensuing antagonism, which may be conceptualised as a dialectic between expertise and politics. It pits the two competing logics of legitimacy (in the eyes of financial markets) and accountability (to citizens) against each other; thereby constraining policy choices. Rash downgrades to the debt of beleaguered Member States only intensify this tension between the programmatic and operational elements of fiscal governance. This inconsistency is reflected in the current debt crisis as governments are denied their traditional countercyclical role.

Speculation in the bond markets – often triggered by the coercive tactics of CRAs (Kerwer 2005: 461) – escalates the onslaught against vulnerable governments, such as Greece or Portugal, while averting attention away from the actual composition of those ratings. As panic spreads, markets are too rattled to probe the accuracy of these downgrades. Moreover, as I posit, ratings have performative effects that normalise adherence to their conclusions. Their resonance is only amplified by a quantitative/qualitative distortion in the analytics of ratings.

Judging Sovereigns

Although CRAs claim not to design ratings as a probabilistically quantifiable frequency denoting the credit event of default or expected loss, but rather ordinal rankings of credit risk, key (qualitative) political determinants, such as the stability and legitimacy of political institutions or the transparency of policy decisions (Standard & Poor's 2008: 2), are framed in absolute risk terms. This makes them more tractable to the rational choice scenarios and stress tests implicit in CRA propriety models. For example, the one-to-six scale employed by S&P attempts the quantitative capture of the nine analytical categories it monitors. S&P admits that these 'analytical variables are interrelated and the

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weights are not fixed, either across sovereigns or across time' (Standard & Poor's 2008: 2). If so, then the ratios that produce the comparative fiscal normality against which peers are assessed are artificially static and, therefore erroneous outside of the strict confines of their underlying assumptions. The 'special' status of sovereigns (Moody's Investor Service 2008a: 5) necessitates more discretionary forms of assessment that are sensitive to the 'constantly mutating formation' of 'contingent social arrangements' (Barry and Slater 2005: 14); namely the government through uncertainty.

Before analysing debt dynamics, CRAs first focus on the 'resilience' of a country and its shock-absorbing capacity. Can it manage economic and political stress 'without having to impose an intolerable economic sacrifice on its population' (Moody's Investor Service 2008a: 6)? Yet how can the permissible threshold in Greece be synchronically standardised – in comparison with any other political economy – to produce that narrow rating range? Qualitative (informal) judgement is paramount in assessing the unique and contingent character of fiscal politics. Where uncertainty prevails, Moody's concedes that it will 'normally assign a rating based on its *perception* of the most likely outcome' rather than 'assign a rating based simply on a probability weighting of the outcomes' (added italics) (Moody's Investor Services 2002: 5). But lacking a systematic 'formula for combining these scores to arrive at a ratings decision' (Standard & Poor's 1992: 15), it is primarily through the 'continuous effort to make the analysis more quantitative' (Moody's Investor Service 2008a: 6) that ratings command and sustain their authority. Defendable risk calculus serves as their legitimising force.

If sovereign ratings, in large part, are subjective estimations susceptible to serious inconsistencies and bias (Johnson *et al* 1990), what justifies the scope and salience of these 'opinions'? Sinclair (2005: 65-66) refers to the historical institutionalisation of norms and rules surrounding creditworthiness, or the 'embedded knowledge network', which grants CRAs their leverage over global capital markets. Arguably, this is constituted through the performative

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effects of ratings, which create the conditions that serve to validate this epistemic framework and, thus their utility and reputation for impartiality. Performativity combines this relationship between action and authority.

Unfortunately, the discretionary construction of ratings is muted through the 'objectifying cloak of economic and financial analysis' (Sinclair 2005: 34) which purports to translate more uncertain (political) events into statistical regularities. But the deliberate discounting of uncertainty-based practices in favour of a defendable calculus of risk obscures how the CRA's own contingent liabilities factor into the production of their 'judgements'. Individual rating agencies have their own institutional protocols and corporate identities that influence the various stages of rating design. Without any serious consideration of their discursive constitution, and compounded by an unhindered deference to exogenous quantitative analysis, this amounts to the misrepresentation of uncertainties as risks.

To reduce fiscal complexities, however, to static risk calculations is to neglect what Callon (1998: 36-37) labels as 'framing' and 'disentangling'. Markets are continually (re)negotiated. Without the potential to 'exclude things' and 'leave certain costs or claims out of the calculations, and deny responsibility for certain consequences', markets would not work (Mitchell 2007: 244). Uncertainty helps render sovereign debt intelligible as a problem of government as it discriminates amongst various factor inputs in the production of ratings. Together with risk, they act to unite dispersed fiscal sites across the spatial-temporal terrain of the EU. By arranging relationships according to inclusive/exclusive categories, uncertainty acts as a 'boundary object' immanent in strategies of control implicit in sovereign ratings. Subsequently, ratings produce an inside/outside effect which excludes certain governments from the privileges afforded by a higher credit grade; that is access to capital markets.

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Performativity of Ratings

The notion of an *a priori* and exogenous ontological reality, called the market economy, which simply exists to be described, has been skilfully refuted by a variety of scholars (Maurer 2002; Miller 2001; Porter 2005; Clark, Thrift and Tickell 2004). In his widely acclaimed contribution to the performativity literature, *The Laws of Markets*, Michel Callon (1998: 23) argues that economic theories and formulas 'do not merely record a reality independent of themselves; they contribute powerfully to shaping, simply be measuring it, the reality that they measure'. Referring to Deleuze and Guattari's (1987) notion of *agencement,* Callon (2007: 320-21) argues that economic formulas perform the worlds they suppose into existence. That is until failure/crisis brings about adjustment and alteration.

Applying the central thrust of this argument to the measurement practice of ratings offers insights into the politics of limits surrounding the European sovereign debt crisis. Consonant with the proposition that '"the economy"...only becomes singular and monolithic by virtue of the convergence of certain kinds of processes and practices that produce the "effect" of the knowable and unified economy' (Butler 2010: 147), as a quantitative technology, ratings make qualitative statements about the degree of a sovereign's creditworthiness. These help condition the discursive constitution of its subsequent fiscal realities. Of interest from the point of view of the debt crisis, is how fragile these stabilisations are when the forces of fiscal sovereignty are unleashed.

Given their procedural dimension, ratings share a certain affinity with the 'illocutionary' performativity discussed by J.L. Austin (1962). Variable and contested, these utterances communicate a range of judgements denoting degrees of budgetary prudence or profligacy. In turn, they help modulate the market parameters within which political governments are normalised to operate. But ratings are not simply a linguistic process. Formulations of social facticity are derived from techniques of truth production, which include

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‘methods of observation, techniques of registration, procedures of investigation and research, apparatuses of control’ (Foucault 1980: 102). Representations demarcating the limits of debt financing, and thus fiscal possibility, reflect ‘a circulating operation of power that constitutes agents and their interests’ (de Goede 2005: 10). Tracing these effects in the formation of three subjectivities implicated in the debt crisis illuminates this process.

Fiscal sovereignty cannot be readily captured through the utilitarian calculus of risk. Callon (2010: 164) is correct to assert that the success of illocutionary performativity is only temporary because its capacity ‘to make inactive and invisible [its] overflowing and misfires’ for an extended period of time is dubious. In the European context, however, it is not that ratings actually precipitate the ‘converse’ of what they describe to alter political economy ‘in such a way that [their] empirical accuracy...is undermined’ or what MacKenzie (2006: 19) labels as ‘counterperformativity’. Budgetary politics is replete with numerous exigencies that can randomly sabotage the programmatic ambitions of its surveillance as well as refute the accuracy and reliability of ratings. Such is the case because rather than uniform and statistically probable, the EU assemblage is composed of:

> complex ensembles of discontinuous elements and forces bound by heteromorphic relations...irreducible to a fundamental essence, and that are composed of multiple and varying dimensions...implying lines of continuous variation that can never be homogenised into a linear process of change or transformation. (Dean 1996: 55-56)

To discuss this process in totalising or monolithic terms is to neglect the implicit contingency and ‘unusually heterogeneous arrangement of elements’ found in European political economy (Barry 2002: 143).

Nevertheless, the discourse of risk has the depoliticising effect of naturalising the separation of the economic from the political by treating the latter as an unproblematic and exogenous reality whose properties may be unearthed with the correct quantitative tools. Ratings are the internal forms of governmentality that help engender this bifurcation. They assume their

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authority by aligning social forces in congruence with a coherent and transposable notion of fiscal normality; against which creditworthiness may be assessed. Their expertise allows CRAs to mediate this representational process and designate conditions of budgetary abnormality. How this alterity is assessed through a specific configuration and deployment of risk and uncertainty-centred techniques is at the heart of this article.

Whether such as prior ontological realm actually exists is of secondary significance because it is 'performed' through the alignment of interests and subjectivities. Once fiscal variance is codified and commercialised as a calculation, ratings exert 'isomorphic pressure' (Leicht and Jenkins 1998: 1325) through the standardisation of budgetary normality as a numerical figure, 'whose strength consists in its machine-like, engineering quality' (Hutter and Power 2005: 7). Such purported accuracy makes risk discourse difficult to resist for market participants and policy-makers alike as it promises to enhance the precision of surveillance at a low cost. With a calculus of probabilities at their disposal, even EU officials increasingly understand fiscal profligacy as a problem rooted in the language, ideas and methods of commercial risk management (European Commission 1993; CESR 2010; ECB 201; ESME 2008). So much so that risk has begun to displace other forms of understanding EU fiscal governance, such as through the lens of national economic security or in terms of socio-economic classes (Walters and Haahr 2005).

Control as calculation is revealed and institutionalised through these discursive practices of identification and prioritisation implicit in ratings. Drawing on Gilles Deleuze's (1995) discussion of the post-disciplinary logics of 'control', ratings have the effect of *modulating* budgetary conduct. Whereas discipline entails both individualisation and normalisation, regimes of control regulate deviance rather than reform the actor. Ostensibly, this aggravates the relationship between CRAs and EU governments because it fails to induce the internalisation of self-regulation among Member States to conform to the

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prescribed fiscal normality. Although compliance is not an objective of CRAs, the act rating a government's propensity towards fiscal failure exerts (exogenous) performative pressures of convergence. Control of conduct varies with the degree to which risk's representation of a budgetary normality compels officials to acquiesce to market demands. Authority is exercised through constant surveillance in this struggle for representation. Since European governments are unlikely to repudiate completely global credit markets, harsh austerity is expected until a breaking point; at which constituencies mobilise their governments to cushion the crisis.

By deconstructing the EU regulatory response, we are in a better position to discern how its effects help bolster this performative capacity of ratings. As a governmental category, the perceived uniformity of risk is disturbed to expose the alterity underpinning fiscal relations, the conditions facilitating their constitution and their translation into ratings. Technical and depoliticised enclosures open up to 'test the limitations and the exploration of excluded possibilities' (Ashley and Walker 1990: 263).

Reconstruction of these lineages reveals incompatibilities between the programmatic and the operational dimensions of budgetary governance, which precipitate a backlash whereby the politics of resilience attempts to reclaim its lost fiscal sovereignty. Fraught with perils and vulnerable to breakdown, the perlocutionary performativity – 'performation' for Callon (2007: 330) – of the politics of limits underpinning European sovereign debt become susceptible to displacement as the terms of the political in the economy are renegotiated. Encompassing a 'fact/value ambiguity that has always been present in the idea of the normal' (Hacking 1990: 168), the EU becomes a terrain where competing visions of fiscal normality are performed.

EU Regulatory Response

As escalating market turmoil fuels intense antagonisms between the European officials and CRAs, a reasonable expectation is for the EU to

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impose severe restrictions on their conduct. A series of rash downgrades, including the relegation of Portuguese debt to junk status (Ba2 from Baa1 by Moody's), have evoked an all too familiar reaction from Brussels. José Manuel Barroso, Commission president, reprimanded Moody's for being guilty of 'mistakes and exaggerations'. This harsh sentiment was echoed by Wolfgang Schäuble, the German finance minister, who was dumbfounded by the timing of the announcement, asserting that Europe must 'break the oligopoly of the ratings agencies' (Europe lashes out over downgrades 2011). Not surprisingly, this rhetoric has not reassured jittery markets. More troubling is the fear of contagion. Bloomberg (Randow 2011) reports that credit default swap (CDS) spreads – a popular measure of creditworthiness – estimate a 27 per cent chance that Italy will fail to meet its debt obligations within the a five year period while forecasting a 31 per cent probability of a Spanish default.

Given the deepening of this crisis, rather than excising references to ratings, the EU is, in fact, doing the opposite. Mandatory registration with the European Securities and Markets Authority merely serves to promote and institutionalise their status while ceding further sovereign authority to Moody's, S&P and Fitch. While CRA Regulation v1and v2 are indicative of the EU's determination to address some of the more egregious elements of ratings, erroneous assertions and inadequate mechanics threaten to undermine the EU's capacity to manage effectively its sovereign debt woes. Two are particularly problematic.

Not least of these is the misguided belief that it is possible to reduce the overreliance on (dubious) external ratings by giving them the EU's blessing. By officially sanctioning the current practice, without correcting the fallacious analytics of ratings, arguably, the EU enhances the legitimacy what is a form of outsourced due diligence. Ratings, *per se,* are not problematic. If fact, their marginal utility is debateable as sophisticated market participants (e.g. PIMCO) perform their own comprehensive analyses (Partnoy 2002; Schwarcz 2002). Failure to conduct proper internal risk assessments often

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precipitates a crisis. Outsourced due diligence may represent value of simplicity but accuracy suffers. Readily adopted scores generated by opaque proprietary models is one thing. Even more precarious, however, is the embeddedness of ratings in regulatory and contractual architecture, which only intensifies their spill-over effects (ECB 2011; IMF 2010).

Neither does this redress another grave problem identified by the European Commission (European Commission 2010a) in its 5 November 2010 consultation paper on CRAs; namely the lack of competition in the ratings space and the (intangible) barriers to entry. No doubt, the issuance of ratings is highly concentrated. According to the US Securities and Exchange Commission (SEC 2009), in 2009, Moody's, S&P and Fitch accounted for a staggering 97 per cent of all outstanding ratings across all categories. Current EU measures will not disturb the oligopolistic authority exercised by the big three CRAs but rather reinforce it. Compounded by deficient regulatory technical standards (RTS) devised to monitor compliance, the EU response is fraught with contradictory effects which can jeopardise its own ambitions and eurozone stability. Once these questionable practices are identified, it will be possible to elucidate their performative effects on the range of subjectivities implicated in the debt crisis.

Special Status Registration

First, in accordance with the CRA Regulation v2 (6), ESMA is empowered with the 'exclusive responsibility for the registration and supervision of credit rating agencies in the Union' beginning in the second half of 2011. Transparency is the driving force behind this initiative (CRA Regulation v2). Similar to the 'Nationally Recognized Statistical Rating Organizations' (NRSRO) designation in the United States (Pollock 2005; White 2002), certification is intended to identify whose ratings are appropriate for regulatory purposes in the EU. Centralised supervision at the pan-European level can help enforce CRA compliance with EU regulatory provisions. Key stipulations

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include prohibiting CRAs from providing advisory services or from rating financial instruments without the sufficient quality information upon which to ground their opinions (CRA Regulation v2). Quality is of the utmost importance so the disclosure of models, methodologies and key assumptions used in ratings is also mandated. Unfortunately, devoid of the appropriate supervisory methods to ascertain how uncertainty is deployed in the construction of ratings, I posit that the EU's capacity to monitor and manage CRAs is greatly circumscribed.

On the surface, enhanced disclosure and registration appear like credible policy initiatives that promise to correct some of the failures in financial supervision exposed by both the credit and sovereign debt crises. Until now, CRAs have operated with a fair degree of autonomy from regulatory interference (Sinclair 2005). Lax governance, however, is a principal factor that the Commission (2009) believes contributed to the excessive risk-taking, poor internal controls and an overall failure of governance – hallmarks of a self-regulating financial order gone astray – in many of these institutions. Upon closer examination, however, serious deficiencies in the EU's response come to light.

Unintended Consequences for Member States

Unintended consequences derived from ESMA registration can have inhibiting effects on Member States. Investment-grade ratings help to facilitate the business of government. They grant national officials access to liquid capital markets through which they can fund their respective programmes (e.g. social spending, military) (Kerwer 2005). More favourable ratings translate into lower costs of borrowing. Conversely, those credit channels demand a higher premium or dry up with consecutive downgrades; thereby inhibiting the fundamental roles of 'government'. This 'certification' performance indicates which securities satisfy regulatory capital requirements, such as ECB eligibility as collateral for money market operations, or the private contractual criteria of

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investment funds, banks or other financial institutions. In other words, ratings confirm government compliance with regulatory standards by functioning as 'gatekeepers' (Partnoy 2006). They continuously generate and validate representations of appropriate fiscal conduct. Simultaneously, this 'logic of appropriateness' anchored in risk discourse confronts and overlaps a 'logic of consequences', which together produce the growing leverage of 'reputational capital' (MacLeod 2007: 246). Official registration enhances the legitimacy of their decisions and thus the authoritative capacity of CRAs.

An analysis of the US managerial approach to CRAs – widely emulated by the EU – reveals the potential adverse externalities involved in granting rating agencies special status. Recent legislation – relatively speaking given that the genealogy of ratings can be traced back to the 1860s – in the US (Rating Agency Reform Act of 2006) has introduced criteria detailing what the NRSRO designation actually entails.[1] Prior to 2006, however, certification by the SEC was quite informal, which only erected barriers to entry (Sinclair 2010: 103). Frank Partnoy (1999) cynically equates such recognition to bestowing CRAs with 'regulatory licences'.

In addition to issuing credit statements, once ratings are incorporated into regulation, this scheme encourages CRAs to sell the 'valuable property rights associated with compliance with that regulation' (Partnoy 1999: 684). Issuers of debt covet that high investment grade and the privileges which it affords; whereas a sullied reputation of what Otmar Issing (2008) refers to as a 'fiscal sinner' is eschewed. Of course, as recent events demonstrate, who is in fact deserving of such recognition is highly controversial. Framed through uncertainty, sovereign ratings possess a rather ambiguous threshold for verification. Extremely lucrative, Partnoy (1999: 623-24) argues that this business:

> has had dramatic effect, not only causing a decline in the informational value of credit ratings but also creating incentives for the agencies to provide inaccurate ratings and for market participants to pay for regulatory entitlements stemming from the agencies' ratings, instead of paying for the informational content of the ratings. The result is

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> a bewildering array of dysfunctional financial behavior as well as substantial financial market distortion and inefficiency.

This certification capacity of rating agencies contributes to and, in turn, is bolstered by their pre-eminence. Moody's and S&P, by far, are the most dominant players in the space; Fitch remains a notable, but distant third (White 2002).

Partnoy makes a valid observation. Private entities, rather than regulators, disproportionately control how the substantive advantages of regulation are determined. Applied to Europe, the designation may accelerate the penetration of neoliberal precepts as governments vie for that respected, but elusive, triple-A rating. As the recent spate of downgrades has demonstrated, Member States are increasingly assailable given their profligacy and, in some cases (e.g. Greece), insolvency. Without credible recourse to fend off such attacks, the pressures intensify until default is declared or the necessary reforms to correct this asymmetry are implemented. Hence, the unintended consequences of registration only can exacerbate the crisis.

Constitutive Effects for Investors

Another ominous prospect stems from the constitutive effects of ESMA registration for investors. Arguably, a primary appeal of ratings is as an inexpensive form of outsourced due diligence. Given the uncertainty in calculating the risk of default, investors attempt to minimise such costs while searching for potential arbitrage opportunities (Beunza *et* al; 2006; Partnoy 2006: 78). Irrespective of their actual quality, as regulatory licenses, ratings provide the chance for investors to capitalise on the creditworthiness differentials of Member States. Disparate governments become synchronically connected and comparable as ratings entitle them to varying degrees of accessibility to liquid capital markets. In other words, the institutionalisation of

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ratings equips speculators with an arsenal of tools with which to exploit the relative vulnerability of individual governments. Investors are modulated to accept the authority of ratings as they complement their business ambitions. Registration reinforces the legitimacy of this process.

Self-Generative Effects for Rating Agencies

Yet as tempting as it is to subscribe to the notion that 'revenues flowing to rating agencies are rents from a government-generated monopoly' (Sinclair 2010: 103), and thus the obvious remedy is to abolish this status (Pollock 2005), Sinclair reminds us that it must be carefully considered in relation to how CRAs accumulate their own reputational capital. Herein lies the value-added of performativity. Self-generative effects are visible for rating agencies. Ratings function as self-validating feedback loops (Callon 2007; Hacking 1999). They '"perform" the market by helping to create and sustain the entities [they] postulate' (Guala 2007: 135).

Procyclicality is observed as negative downgrades hinder debt financing, dampen economic growth and thus precipitate further decreases (Lowe 2002). As fiscal positions deteriorate, recessionary pressures grow, which, if persistent, serve to validate the smoothing rule's prescription of additional downgrades implicit in the 'through the cycle' (TTC) rating methodology. TTC approach suffers from a lag as it 'waits to detect whether the degradation is more permanent than temporary and larger than one notch' which tends to 'accentuate the already negative movement in credit quality' (IMF 2010; xiii). Evidence (Haldane *et al* 2000) confirms this procyclicality. Only in less than 25 per cent of cases have Moody's and S&P cut a sovereign rating before the onset of a correction. Most downgrades occur once a crisis has already begun. Procyclicality exhibits is own feedback effects. By that time, however, governments are in damage control mode and the threat of systemic disruption looms.

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Dilution of Competition

Now that the EU has added its stamp of approval, twenty-three CRAs have applied for registration with ESMA – there are ten NRSROs in the US. Not only is this commensurate with promoting an overreliance on external forms of assessment but it serves to dilute the lower tiers of the ratings industry; thereby intensifying the leverage of the big three CRAs in the constitution of authoritative knowledge. In light of the tremendous credibility/intersubjective barriers to entry, all these minor rating agencies, such as ICAP Group SA of Greece or the Bulgarian Credit Rating Agency AD, are no match against goliaths the likes of Moody's (2011c) or S&P (2011b) who, in 2011, rated 112 and 126 sovereigns, respectively. To the contrary, saturation of the lower rungs only crystallises this stark contrast.

At 59 sovereign ratings, but with some stretch of the imagination, Kroll Bond Rating Agency (KBRA) (2011) may be considered as a potential challenger. Most new entrants, however, seem resolved at carving out niche specialisations rather than aspiring to become global full-spectrum rating agencies (Sinclair 2010: 98). For example, Dominion Bond Rating Service Ltd. (DBRS) of Canada focuses on global-corporates and structured finance, while Japan Credit Rating Agency Ltd and Rating and Investment Information Inc. have set their targets primarily on Japan. With the arrival of new CRAs, whatever minimal market share exists will further diminish, thus forcing many smaller firms out of the industry all together while elevating the status of Moody's and S&P. Even if the EU decided to expel Moody's or S&P, what prevents them from issuing ratings from their headquarters in New York?

In 2009, the SEC began a campaign to eliminate references to NRSRO ratings in certain statutes. The Financial Reform Act (Subtitle C of Title IX) seeks to reduce the mechanistic reliance on ratings. A similar position has been advocated by the Financial Stability Board (FSB 2010). Critical of the 'hard wiring' of ratings into laws and market standards, the FSB proposes (broad) principles to expunge ratings where possible and attenuate their

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frequent subscription elsewhere. Hence, it is quite odd that the EU should reverse this trend by institutionalising the very financial instruments that have wreaked havoc with Economic and Monetary Union (EMU). In the end, ESMA registration may only entrench external forms of ascertaining and articulating (sovereign) creditworthiness and solidify the status quo.

Monitoring CRA Compliance

Article 8(3) is the most significant, yet most ambiguous and contested, section of the new regulatory framework. Touted as a unique 'European touch', it stipulates that 'a credit rating agency should use rating methodologies that are rigorous, systematic, continuous and subject to validation based on historical experience, including back-testing' (CRA Regulation v1). Or at least that is the ambition. Such ambitions, however, must be carefully located in a broader assemblage of 'modalities and apparatuses of power' with their own – often conflicting – 'conditions of possibility and regularities' (Rose and Miller 2008: 3). Undoubtedly, ESMA is serious about its supervisory role and ensuring that it has bite as well as bark. Yet it fails to redress how a fallacious analytics of ratings obscures the role of contingent liabilities; thereby invalidating competing notions of fiscal normality in favour of a calculus of risk. Nor is ESMA equipped with the necessary regulatory tools to fulfil its mandate without advocating strategic policy decisions.

Good governance is dependent on an appropriate set of preventative and corrective practices that can help achieve the programmatic ambitions of an organisation without inhibiting its ability to adapt to the uncertainty of changing circumstances (Power 2007). To apprehend and address the rapidly shifting parameters of global finance and safeguard financial stability, 'it is necessary to identify, at an early stage, trends, potential risks and vulnerabilities stemming from the micro-prudential level, across borders and across sectors' (European Commission 2009: 19). For this purpose, ESMA is labouring to tweak the August 2010 technical standards deployed to assess

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CRA compliance with Article 8(3) (CESR/Ref. 10-945, CESR Guidance) developed by its predecessor, the Committee of European Securities Regulators (CESR). Although a draft was released on 19 September 2011, the formal framework will not be submitted for endorsement until January 2012. It is already clear that substantive similarities exist which threaten its mandate. Principal logics and methods embodied in the antecedent CESR Guidance are being transposed to the new RTS (Anonymous 2011). Unfortunately, these measures are deficient in both their preventative and corrective capacities.

Rigorous

To begin with, the 'rigorousness' of rating methodologies is evaluated. Accuracy relies on uncompromising high standards. Robust precision is desirable but deciphering whether Moody's or S&P demonstrates having 'acquired a clear understanding of *all factors* relevant to the credit rating methodology' (added italics) (CESR Guidance 4A.23) or proving that any information or data is 'from reliable sources and of sufficient quality' (4A.26) is mindboggling; especially when calculating the 'tolerability of debt' encompasses such nebulous notions as the consensus surrounding political succession (S&P 2008: 3) or a regime's 'legitimacy' (Moody's 1991: 165). If Moody's (2008a: 6) itself admits that there are 'no quantitative-based approaches that satisfactorily replace analysts' disciplined judgment on these questions' then how feasible is it for the EU to determine and assess the requisite degree of discretionary conduct involved in rating a sovereign? Not surprisingly, how the quantitative and qualitative parameters are accommodated and synthesised is never revealed by CRAs.

Demanding 'a high level of description of qualitative inputs, including the scope of qualitative judgement' (CESR Guidance 4A.30) presupposes some kind of standardised metric/benchmark, according to which subjective decisions about unique national fiscal positions can be made. Should such a

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formula be readily available or a qualified/competent appraiser exists then what precludes the EU itself from proposing a single method for calculating the risk of default? One definition would assuage the terrible burden of having to discriminate how discretionary judgement is applied by a host of agencies; each with their own proprietary models, corporate culture and institutional identity. As I argue, qualitative elements elude being captured through quantitative techniques. It is difficult to imagine how such opaque procedures can establish methodological rigorousness to yield anything but ambiguous and superficial conclusions.

Insofar as these obscure methods of assessments fail to target adequately the contingent liabilities implicit in the construction of ratings, they enable rating agencies to continue their operations without any substantial interference. Business is as usual if CRAs are only compelled to submit and demonstrate what is essentially already available for public consumption. Unless ESMA defines what these ‘relevant’ or ‘suitable’ qualitative variables are then it will be left to the discretion of the rating agencies themselves to decide what satisfies these requirements. Cooptation of the supervisory analysis is possible as vague criteria and nondescript labels are open for interpretation. Informal judgement, of course, eludes simple regulatory control and sanction.

Systemic and Continuous

Evidence of the ‘systematic’ and ‘continuous’ application of rating methodologies may be slightly more tangible. Consistency can be monitored. Although it is difficult to grasp exactly what of significance in the construction of sovereign ratings will be studied. Irrespective of its acknowledged ‘special’ status by rating agencies, sovereign debt is treated identically to corporate debt – structured finance is a separate category. No specific provisions for sovereigns are included in the regulation. Here again there is a deliberate attempt to deploy ‘pre-defined methodologies’ to rating the fluid and

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contingent character of fiscal relations (CESR Guidance 4B.42). Rather than tailoring context-specific approaches (i.e. differentiated ratings), this sanctions the transposition, and thus enhances the ubiquity, of risk vectors. Seldom problematised but readily applied from one context to another, these techniques may be repeatable but sovereigns are unique. Management through uncertainty cannot be systematically orchestrated because it fails to reproduce itself at regular intervals. An artificial uniformity is promoted which is blind to the nature of budgetary politics.

Continuity and consistency are fundamental to the sedimentation of ratings. Risk's probabilistic (predictive) potential promises some semblance of relative stability in an otherwise constantly changing world of finance. For investors, this provides a platform for their calculations. Asymmetric information and discrepancies in calculating capacities help foster a dependence on external ratings. Subscription, however, to these socio-technical devices subjects investors to exogenous forces.

Here rating agencies 'design and impose modalities of encountering, and consequently sociotechnical algorithms of pricing, that produce asymmetries and guarantee the domination of certain agencies over others' (Callon 2007: 348). External ratings no longer compel investors to use their own 'self-conscious critical faculties' in the assessment of creditworthiness (Holmes and Marcus 2005: 237). Their reiteration and citation impedes the endogenous responsibility of managing one's own uncertainty. Although reducing this overreliance on external forms of assessment is a priority for the EU (European Commission 2010a), the RTS can only heighten this dependence as they work to entrench the validity and utility of risk techniques of investors. Thus, ESMA's administrative apparatus legitimises an infrastructure of referentiality which reinforces the monopolistic authority of Moody's or S&P as principal knowledge entrepreneurs.

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Validation Based on Historical Experience

Ostensibly, the most arduous, if not the most perilous, responsibility for ESMA involves subjecting rating agencies to validation based on actual performance. Is there a comprehensive and integrated framework that 'covers the quality of inputs (including appropriate size of data sample) fed into the system and the reliability of the methods used to process them' which 'allows for a *truly representative* sample...to control the accuracy' of ratings (added italics) (CESR Guidance 4D.65-70)? For this purpose, ESMA concedes that the infrequency of sovereign defaults is highly problematic. Yet it offers no viable alternative apart from mimicking methods that attempt to transform (singular) fiscal uncertainties into (aggregate) pools of risk. Complicit in this misrepresentation of uncertainties as risk, the RTS reaffirms the hegemony of the discourse of risk in assessing fiscal relations. At stake is the stability the EU and financial markets as significant information is distorted or withheld from the market.

Sovereigns rarely default. Prior to the Greek selective default, in November 2008, Ecuador was negligent on an interest payment of US$ 30.6 million owing on US$ 510 million of global bonds maturing 2012, which it considered as 'illegitimate'. Its second default in a decade, Ecuador eventually was downgraded to Ca by Moody's, who confirmed that 'the government's decision to default was based on ideological and political grounds and is not related to liquidity and solvency issues' (Moody's Investor Service 2008b). Of course, what accurate measurements exist to forecast such shocks? Distressed exchanges also occurred with Belize (2006) and Uruguay (2003). One of the most notable was Argentina's November 2001 announcement that it would fail to pay the coupon on its bonds. Eventually, US$ 82 billion of debt was restructured in 2005.

Now ESMA must devise some elaborate benchmark analysis capable of compensating for this limited population sample while simultaneously accounting for the extreme (political) heterogeneity present in available cases.

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Correlations between fluctuating political economies – especially as diverse as the emerging markets and EMU – are prone to failure. The diverse and factional socio-political elements, which factor into calculating the propensity towards fiscal failure, make arriving at an accurate comparison virtually impossible and improbable. Technical proxies fail to remedy this conundrum as they introduce fictitious assumptions into the design. Absolute default probabilities may not be what CRAs claim to measure but Moody's admits that 'there is an expectation that ratings will, on average, relate to subsequent default frequency' (Moody's Investor Services 2002). Forward-looking evaluations are performed and supplemented with hypothetical stress tests. Probability distributions are integral to this comparison of peers (IMF 2010). But lacking the appropriate sample size to conduct the assessments, these projections are incomplete.

Back testing divorces ratings from the messy world of fiscal politics; which is exactly the accusation levelled against CRAs. Virtual free reign in determining what constitutes as a relevant approximation reinforces the self-generative effects of rating agencies. As opposed to penetrating the hermetic enclosures of CRAs to enhance transparency and reveal ratings errors, this RTS approach is an implicit admission that risk-based techniques alone are insufficient to assess the risk of sovereign default. Nevertheless, it still proposes risk calculus as a solution. A minimal burden of proof coupled with verification techniques that seem daunting to apply serve to immunise rating agencies from any serious scrutiny.

At the same time, technical proxies and aggregating methods that reach beyond Europe effectively reduce diverse political economies to a few common denominators. Tantamount to imposing an artificial uniformity across an even broader section of global political economy, they still fall well short of any reasonable reliability threshold (Desrosieres 1998). In short, EU policy neither prevents nor corrects the tremendous imbalances evident in the ratings space. Its incapability to ameliorate these inadequacies is not simply a

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procedural matter. More significantly, it stems from the regenerative performativity of ratings aligned with a ubiquitous discourse of risk.

Conclusion

Through a variety of significations, a meaning of what constitutes as budgetary normality is inscribed into the European political economy. Progressively, it seeks to eliminate the alterity that exists between Member States. Ratings are an internal form of governmentality aligned with self-systemic disinflationary logics of neoliberalism that induce a fictitious bifurcation between the economy and politics through their performative effects. A false dichotomy between (qualitative) uncertainty and (quantitative) risk helps constitute this politics of limits underpinning the European sovereign debt crisis. Insofar as these stabilisations are produced, their perlocution leaves them vulnerable to breakdown. Once crisis erupts and fiscal sovereignty is excessively threatened, the terms of the political in the economy are revisited.

Through a diagnosis of this relationship between the programmatic and operational dimensions of fiscal governance, two observations are notable. First, by deconstructing how CRAs appropriate the constructs of risk and uncertainty in the design of sovereign ratings, we begin to appreciate how, in spite of the transformative illocutionary potential of ratings, the imaginary quantitative/qualitative binary opposition between risk and uncertainty contributes to their misrepresentation. This distortion permits contingent liabilities to be masked which, in turn, validate a prescriptive (artificial) fiscal normality. Together these instil a false degree of verisimilitude about the nature of fiscal relations and how amenable they are to intervention as they institutionalise a form of dysfunctional information exchange.

Second, reconstruction shows how, based on this (dubious) knowledge, the performation of the politics of limits surrounding sovereign debt is fraught with perils and vulnerable to breakdown. ‘Successful illocution’, Callon posits

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(2010: 164), 'like a successful performation, implies the active presence of appropriate socio-technical *agencements*. As such an adjustment is always fragile and rare, the general rule is a misfire' (original italics). Contestation abounds as the programmatic ambitions and effects of fiscal surveillance clash with national political agendas and aspirations. The inherent heterogeneity of European budgetary relations challenges excessive austerity and crippling adherence to neoliberal precepts. With the ensuing backlash that we are witnessing, this persistent stream of failures swells to disturb the perlocution of the politics of limits. In crisis, the parameters of the permissible become malleable.

Problematising the EU regulatory response demonstrates how it helps engender self-generative effects for CRAs, constitutive effects for investors, and unintended consequences for Member States. Although this matrix may normalise a stabilisation, it is fragile and susceptible to disruption. Misfires occur because 'perlocution implies...the possibility of having an effect, but without any strong notion of probability or any possible version of necessity' (Butler 2010: 151). Government through uncertainty is equipped to deal with fiscal exigencies whereas risk only contributes to and exacerbates them by imposing an artificial uniformity on the European fiscal landscape. Of course, this is not claim that probabilistically quantifiable techniques are without merit. But to recognise the authoritative capacity of ratings is to understand how their construction facilitates their performativity. No matter how much authority ratings may command, ultimately, fiscal temperaments are fluid and too idiosyncratic to be captured in a probability distribution.

Notes:

1. There are ten firms currently registered as NRSROs: A.M. Best Company; DBRS Ltd.; Egan-Jones Rating Company; Fitch; Japan Credit Rating Agency Ltd.; Kroll Bond Rating Agency (f/k/a LACE Financial Corp.); Moody's Investors Service; Rating and Investment Information; Realpoint LLC; Standard & Poor's Ratings Services.

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