

Long-term interaction between corporate credit ratings and the stock market

István Bakos

Supervisor: Xin Zhao, Ph.D.

World Headquarters, Morgan Stanley & Co. LLC, New York

Abstract

In this thesis, we discuss the interaction between credit ratings and the stock market. More specifically, corporate credit ratings are taken as an example to conduct the empirical analysis. The research has two interesting achievements.

First, we provide a brief overview of the credit rating history of all the rated S&P 500 companies between January 1990 and December 2015 in order to examine the long-term interaction between the corporate ratings of S&P 500 companies and the S&P 500 Index. The historical data shows consistent interaction between the issued corporate credit ratings and the stock market performance of S&P 500 Index during the period from January 2006 and December 2013.

Second, a rating prediction model using the empirical results is also introduced. The developed model predicts the corporate rating of a selected S&P 500 company based on its corporate rating history and the performance of S&P 500 Index. This model has several potential uses. It could be extended to private sectors, which do not have publicly available ratings. Besides, the rating prediction model can be used to benchmark the public corporate ratings and provides more updated information about the creditworthiness of S&P 500 companies.