Weekly Credit Brief

Dec 04 - Dec 10 2012

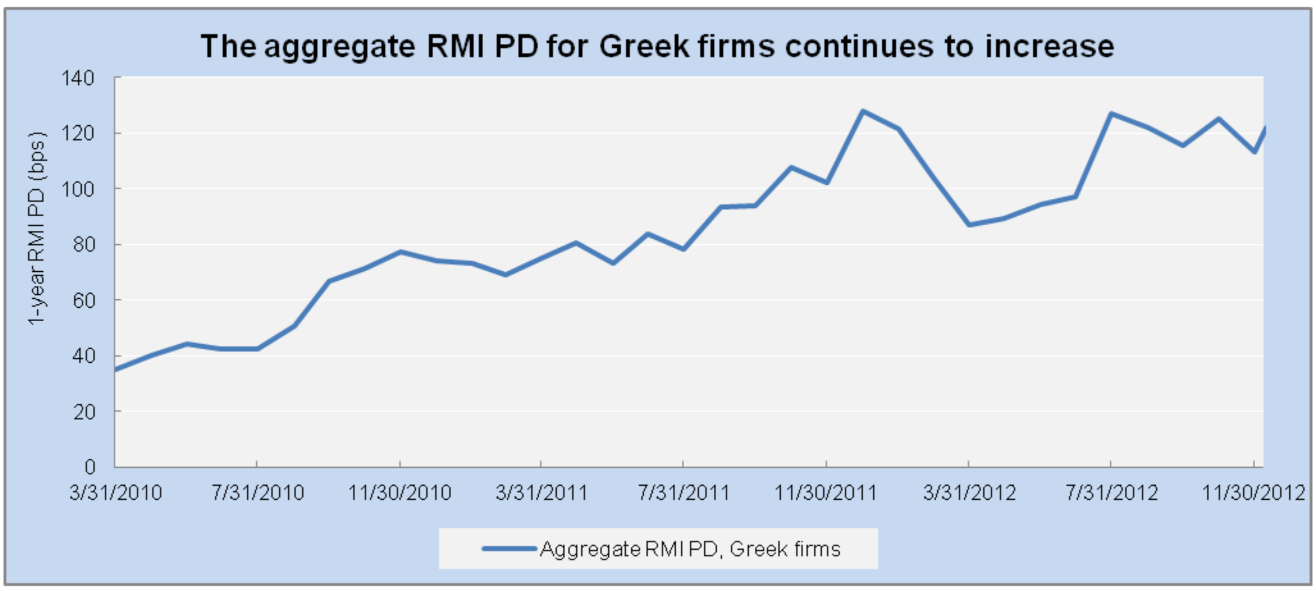
Story of the Week

Lack of success in Greece's effort to buy back bonds a credit negative for the country's firms

By Dexter Tan

A lack of success in Greece's latest attempt to buy back bonds from private investors continues the uncertainty faced by Greek firms. This is consistent with the 1-year aggregate RMI probability of default (RMI PD) for Greek companies, with the aggregate RMI PD increasing nearly 9bps over the seven days till December 10.

The buyback is the latest effort by Greece to lower the government's debt to GDP ratio, which is a prerequisite to secure more funding from the IMF and the eurozone. The country has not received additional funding since June, although most observers expect a decision from both parties to extend funding by December 13. We have previously noted the uncertainties surrounding the Greek economy and highlighted the possibility of the country leaving the eurozone. Moving forward, the credit outlook for Greek companies remains unnervingly fragile and likely to deteriorate further.



Sector analysis: The aggregate RMI PD tracks a total of 230 Greek firms, most of which operate in the industrial (32%) and consumer cyclical (19%) sectors. A breakdown of sectoral median RMI PDs reveals that industrials, technology and communications possess the highest default risk. A number of industrial firms focused in the shipbuilding and construction business had been affected by falling freight rates and a lack of construction demand within the Greek economy. Meanwhile, decreasing capital outlays and weakening consumer discretionary spending has led to lower bottom lines in the technology and communications sectors. Moreover, 35 out of the 230 (15.2%) companies have a RMI PD of more than 100bps while 14 (6.1%) of them have a RMI PD of more than 200bps, both indicating a high likelihood of default for the firms.

Feeble economy: The latest GDP figures show that the Greek economy contracted by 6.9% YoY in Q3, as weak consumer confidence and heightened unemployment weigh on consumer spending and corporate expenditures. As a result of the financial crisis, year-on-year GDP growth has been in negative territory since Q3 2008. Companies facing a highly challenging business environment laid off workers, resulting in record high unemployment of nearly 26% in September. A large number of employees were retrenched in lieu of the punitive austerity measures imposed on institutions together with increased taxes for individuals.

Lackluster revenues and earnings: An examination of the 60 members in the Athens General Stock Exchange Index (which include companies with the largest market capitalization in the economy) highlight falling revenues, earnings and high levels of debt amongst the largest Greek companies. Sales per share fell from EUR 870 in Q3 2008 to EUR 628 in Q3 2012. Operating profit, measured by EBITDA per share dropped from EUR 231 to EUR 77 in Q3 2012. A more disconcerting fact is the level of average current ratios of the firms surveyed, which is at its lowest since Q3 2003. Leverage employed by the firms is also near the highest level on record. The average Debt/equity (D/E) ratio in Q3 for example is four times the D/E ratio four years ago.

Sources:
Greece debt buyback falls short of target (WSJ)
Greece considers reopening debt buyback (WSJ)
Greece downgraded to 'Selective Default' by S&P (CNBC)
Irish, Greek workers seen suffering most in 2013 amid EU slump (Bloomberg)

In the News

The looming crisis of student loan debt

Dec 06. In a report recently released by the Federal Reserve Bank of New York, the 90 day delinquency rate for student loans surpassed the "serious delinquency" rate for credit card debt for the first time on record. The size of the student loan market increased to USD 956bn, exceeding the sizes of the auto loans and credit card markets. Debts issued to students are naturally risky as students do not have an established credit history. Critics say that the lending practices to students are comparable to subprime mortgage lending and call for more reform in this area so that both borrowers and lenders can act with more accountability and transparency. (CNN)

Credit Suisse leaves the Norwegian Krone with nowhere to hide

Dec 06. Investment demand for the Norwegian Krone has increased after Credit Suisse announced on December 3 that institutional clients will receive negative interest income on their deposits held in Swiss francs. The capital inflows into the Norwegian currency adds to the dilemma of regulators at Norway's central bank who have indicated that higher interest rates would be warranted to prevent an overheated labor market and housing bubble in the economy. The country is a large attraction for investors given it has the largest budget surplus of any AAA rated nation and a USD 660bn sovereign wealth fund. (Bloomberg)

UK's credit rating at risk after George Osborne's debt failure

Dec 05. Credit rating agency (CRA) Fitch said that the UK's inability to meet debt reduction targets may lead to a downgrade of the country's AAA credit rating. The Office for Budget Responsibility gave an unfavorable assessment of the country's public finances and said that the UK would not meet the debt target by 2015-16. The Chancellor acknowledged that he would require another year to reduce the nation's debt to GDP ratio, drawing criticism from the Labor party for misrepresenting the financial figures. Early in the year, Moody's and Fitch both placed the country's AAA rating on negative watch.
(The Telegraph, FT)

S&P affirms China ratings on 'exceptional' outlook for growth

Nov 30. Standard & Poor's affirmed China's sovereign ratings at AA-, even though the Chinese economy is expected to expand by 7.7% this year, the country's lowest year-on-year growth rate since 1999. S&P expects GDP per capita growth to average 7.3% in the next two years, down from an average of 10.2% seen in recent years. S&P also interprets Xi Jinping's new presidential appointment as the country's signal toward continued deepening structural and fiscal reforms. (Bloomberg)

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