



Weekly Credit Brief

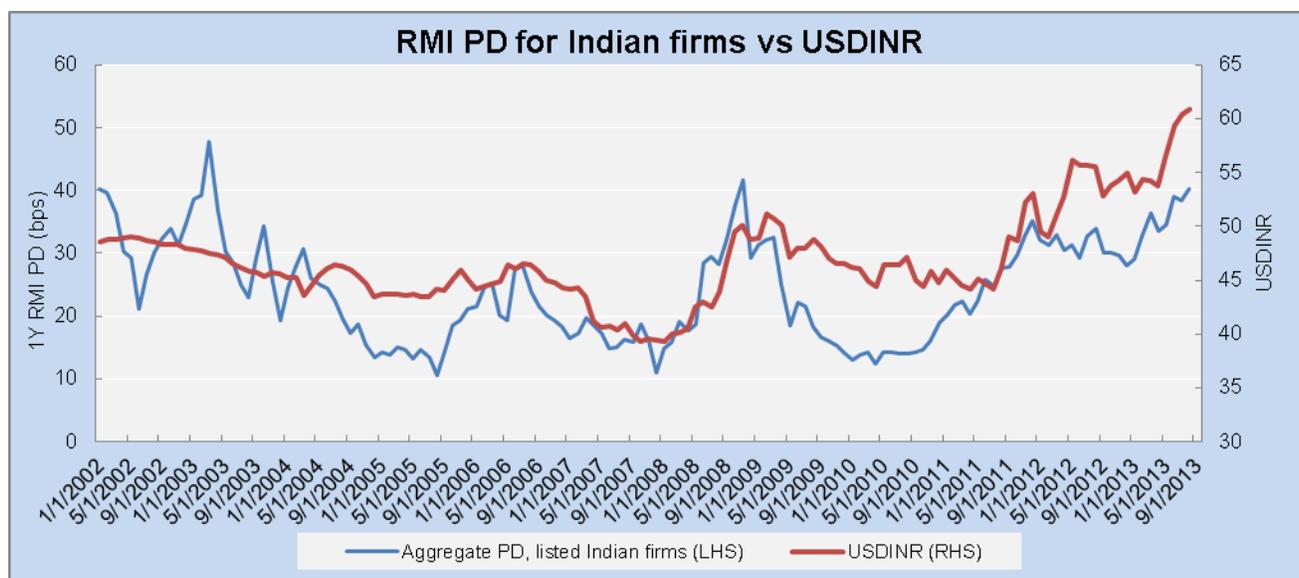
Jul 30 - Aug 05 2013

Story of the Week

Indian rupee falls to record low against US dollar

The INR declined to an all-time low of over 61 INR per USD in the first week of August, despite steps taken by the Reserve Bank of India (RBI) and the government to support the INR. At the same time, the aggregate 1-year RMI probability of default for Indian firms (RMI PD) has risen sharply. The latest RMI PD of 40.2bps shows that Indian companies are facing their highest default risk since the 2008 financial downturn.

India's central bank is believed to have sold USD and bought INR on August 3 to prevent the INR from declining further. On the same day, RBI governor Duwuri Subbarao said that the central bank does not have a timeframe for rolling back liquidity tightening measures imposed to address exchange rate volatility. Instead, the measures will be in place until volatility in the USDINR market is controlled. Last month, the RBI raised the short term interest rates and lowered the amounts banks can borrow or lend to strengthen the INR.



The table below displays the sectors with the highest and lowest correlations with the USDINR between 2002 and 2013. The sectoral PDs of banks and construction firms exhibited the highest positive correlation with the USDINR while the PDs of private equity and oil and gas firms were negatively correlated with the currency pair. The credit profiles of Indian lenders may have deteriorated following a lower INR. Based on recent earnings results by India's largest banks, the amount of non-performing loans have increased in Q2. Non state banks such as Kotak Mahindra Bank, HDFC Bank and ICICI Bank have reported more bad loans, and have raised their provisions sharply. (A positive correlation of +1 implies a perfect linear relationship between the appreciation of the sectoral PD and the depreciation of the INR, i.e., the sectoral PD increases as the INR depreciates against the USD.)

Industry groups with the highest correlation	PD correlation coefficient with USDINR between 2002 and 2013	Industry groups with the lowest correlation	PD correlation coefficient with USDINR between 2002 and 2013
Banks	0.32	Environmental Control	-0.03
Engineering & Construction	0.30	Healthcare-Services	-0.04
Insurance	0.27	Office/Business Equipment	-0.04
Retail	0.26	Oil & Gas Services	-0.09
Food	0.25	Private Equity	-0.10

Moody's had also echoed the negative sentiment for Indian banks. On July 22, the CRA said that the RBI's measures to bolster the INR are credit negative for Indian banks because rising market rates will negatively affect economic growth and place downward pressure on the banks' asset quality and earnings. The risk of tight money market liquidity in India may persist, which would eventually have a material negative effect on bank funding.

Other Indian credit rating agencies such as India Ratings however are more optimistic about the falling INR. The CRA said that as many as 225 of the 290 corporate bond ratings it currently maintains are unlikely to be impacted if the INR falls to 65 against the USD. On June 12, Fitch Ratings surprised market participants after the CRA upgraded India's sovereign outlook to 'stable' from 'negative'. Fitch affirmed their outlook after the Indian government tried to contain the fiscal deficit and revive economic growth. In April 2013, Indian government officials requested Fitch and Standards and Poor's to upgrade their credit outlook for its sovereign bonds, after the country tried to reduce the fiscal deficit and bolster investor confidence.

Sources:

[India's central bank intervened to rescue rupee](#) (Fox News)

[No ratings impact seen on most companies if Indian rupee falls to 65 vs USD](#) (Indian Express)

[Fitch returns India to 'stable' outlook, surprising markets](#) (Reuters)

[Finance Ministry pitches for ratings upgrade for economy with Fitch](#) (Indian Express)

[Indian government pitches for rating upgrade with Standard & Poor's](#) (Financial Express)

In the News

RBA cuts rates to record low

Aug 06. The Reserve Bank of Australia cut its key interest rate 25bps to a record low of 2.5%. In a statement accompanying its announcement, the RBA said that the easing of its monetary policy over the last 18 months had provided support to interest-sensitive spending and asset values, but said further action was appropriate to stimulate demand. Bank lending has remained subdued, but recent signs showed increased demand for finance by households. The RBA also said the AUD has remained at a high level despite it depreciating by around 15% since April, and that further depreciation was possible. ([Sydney Morning Herald](#), [Reserve Bank of Australia](#))

Regulator to impose new capital rules on bank holding firms

Aug 05. South Korea's bank holding companies will need to comply with Basel III requirements from December 1, 2013. South Korea's financial watchdog, the Financial Supervisory Service (FSS), imposed Basel III requirements in order to strengthen bank holding companies' financial health in accordance with international standards. Basel III is a regulatory standard on bank liquidity, leverage and capital requirements to promote financial stability in the international financial system. Under new capital rules, a bank is required to set aside a higher amount of capital reserves in common equity, Tier 1 capital and addition capital buffers against liquidity risk. ([Yonhap News](#))

Cautious lending practices at Brazil's private banks bear fruit

Aug 02. Conservative lending practices among Brazil's largest private lenders are showing results as Q2 loan delinquencies declined sharply. The default ratio at Itaú Unibanco Holding SA fell 1 percentage point YoY to 4.2%, the lowest since early 2009. The same measure at Banco Bradesco SA and Banco Santander Brasil SA – Itaú's smaller competitors, dropped significantly as well. The new level of delinquencies appears sustainable and should help private banks improve performance against Brazil's weak credit demand. ([Reuters](#))

DBS faces five-year lag in Indonesia as Danamon bid ends

Aug 01. Following DBS Group Holdings Ltd (DBS)'s failed acquisition of PT Bank Danamon Indonesia, its expansion in Indonesia is seen to be set back by 5 years. The USD 6.5bn acquisition attempt, which began slightly more than a year ago, came unhinged after DBS failed to negotiate around Indonesia's new bank ownership rule that would have restricted its stake to 40%. Despite robust earning profiles, DBS has sought to tap into new and more profitable markets to reduce its dependence on Singapore and Hong Kong, where net interest margins are continually narrowing. With this failed bid, DBS will now pursue its Indonesian expansion organically. ([Bloomberg](#))

Banco Santander Chile issues Chile's first mortgage bond for USD 67mn

Aug 01. Banco Santander Chile, the country's largest mortgage lender, issued the nation's first-ever mortgage covered bonds when it announced the successful placement of USD 67mn worth of 15-year inflation-linked bonds backed by home loans. This is the first issuance in Chile under the new mortgage covered bond rules, created last year by the Central Bank and the SBIF. The Santander Chile must use the funds raised to issue mortgages within 18 months that fit the criteria demanded by the new regulations. The Santander Chile bonds, which were oversubscribed by almost twice the offer amount, yielded 3.39% or 16bps below the bank's similar-maturity senior debt. ([Reuters](#))

Leveraged loans pass 2012 level with record ahead

Aug 01. The amount of US leveraged loans issued so far this year has exceeded the total amount for 2012. Borrowers have borrowed USD 298.4bn from non-bank lenders in 2013 so far, more than the USD 295bn amount seen for the whole of last year. Most of the loans issued this year were used to reduce interest costs and extend existing bond maturities. According to the S&P/LSTA US Leveraged Loan 100 Index, investors in leveraged loans have generated a 3.2% return this year. The 12 month trailing global speculative grade default rate tracked by Moody's meanwhile has fallen to 2.8% at the end of June from 3.2% recorded in the same period last year. ([Bloomberg](#))

Big savers at Bank of Cyprus to take 47.5% of cash in shares

Jul 30. Large depositors at the Bank of Cyprus, Cyprus' largest bank, will be forced to take EUR 8bn in losses as 47.5% of uninsured deposits are to be converted to equity. Legacy depositors in wound-down Popular Bank, will be compensated with 18% of share capital at the Bank of Cyprus. The announcement, made by the Cypriot central bank, will hopefully put an end to uncertainty over the outcome of deposits at the largest bank. 37.5% of deposits exceeding EUR 100,000 at the Bank of Cyprus were converted to equity and an additional 22.5% were held in reserve earlier in the year when Cyprus was bailed out by the troika. ([Reuters](#))

Japan's economic overhaul carries global risks, IMF says ([WSJ](#))

Tokyo vows not to increase debt issuance over two years, but specifics elude ([The Japan Times](#))

Banks mired in profit quagmire ([The Korean Times](#))

Chicago penalty up 25% as rating cut evokes Detroit ([Bloomberg](#))

Potash's USD 20bn market transformed by Uralkali ([Bloomberg](#))

Malaysian stocks fall most in 7 weeks, Ringgit drops on Fitch cut ([Bloomberg](#))

Lacklustre GDP data push Ukraine towards fresh IMF bailout ([FT](#))

IMF to disburse EUR 1.7bn to Greece after loan review ([Bloomberg](#))

Chinese banks' outstanding bad loans reach CNY 539.5bn ([Bloomberg](#))

EBA seeks to reassure on bank risk models ([FT](#))

China money rates slide after strong central bank injection ([Reuters](#))