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Transforming Big Data into Smart Data

Weekly Credit Brief

May 20 - May 26 2014

**Story of the week**

**Gazprom strengthens after Russia-China gas deal**
By Wang Yunjiao

The 1-year RMI probability of default (RMI PD) for Gazprom decreased to 6.2bps from 13.1bps after the Russian energy giant inked a 30-year gas deal worth USD400bn with China on May 21, 2014. The current PD level is just shy of its post global financial crisis low of 3bps, seen in April 2011. The drop in the RMI PD can be largely attributed to an increase in DTD–currently at 4.98 versus 3.28 at the end of last month. DTD is a volatility-adjusted leverage measure, and changes in the measure are a significant determinant of RMI PDs. Numbers close to or below zero suggest a higher possibility of insolvency. An increase in stock price to 144.57 currently, from 128.77 at the end of April has also increased its relative size and aided the decline in PD.

Gazprom, the top holder of natural gas reserve, currently caters to approximately 14% of the global gas demand. The company has been making steady progress in the expanding global market during the recent decade, lifting its European market share from 22% in 2003 to a record 30% in 2013. The company's financial performance remains healthy: its natural gas sale is increasing; the company sees continued profitability for consecutive years. The default risk associated with Gazprom is significantly lower compared to the industry, as evident from a 30-to-40bps gap between the two RMI PD graphs over the most recent year.

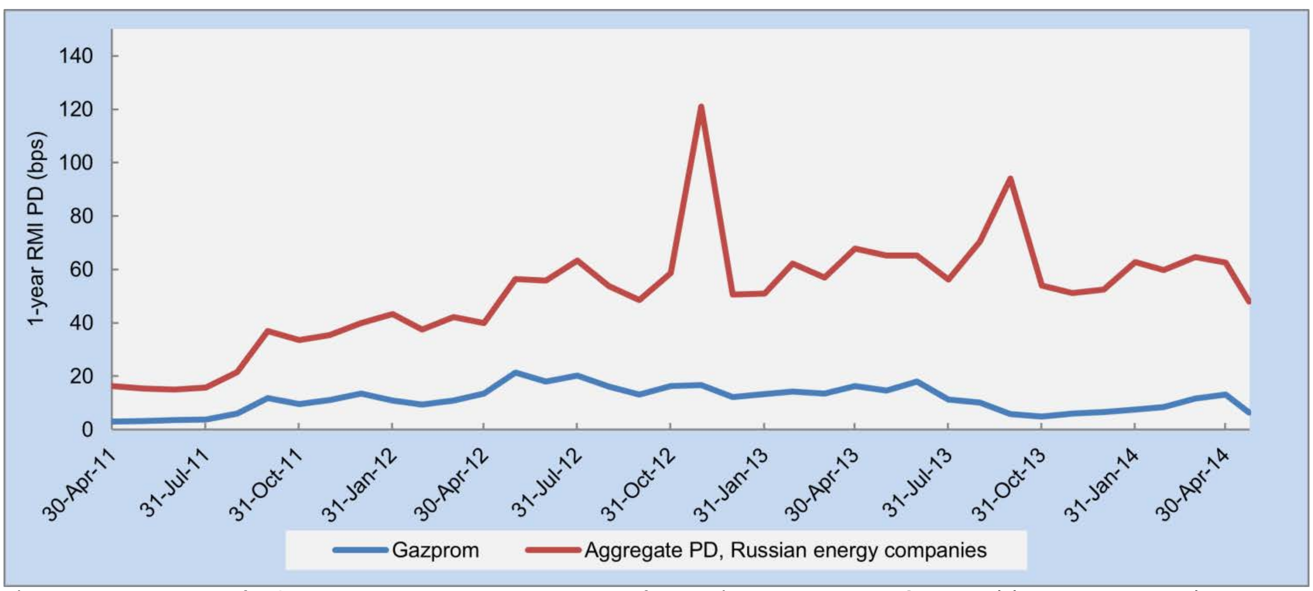

Figure 1: 1-year RMI PD for Gazprom vs 1-year aggregate RMI PD for Russia's energy sector. *Source: Risk Management Institute*

Considering that Gazprom now derives 64% of its revenues from Europe, its financial performance can be threatened by Russia's role in the crisis in Ukraine, which is a transit country of the company's gas delivery route to Europe. Its profitability can be eroded if the EU finds alternative gas suppliers, amid speculation that Gazprom would be added into the sanction list imposed by the US and EU. Against such a political backdrop, the deal between Russia and China acts as a powerful hedge. It also opens up a new promising market for Gazprom with ample opportunities: a more diversified export market, production growth in the foreseeable future, large-scale development of two natural gas reserves in East Siberia as well as another probable gas deal with China via the Western pipeline in due course.

## Credit News

### PBOC cuts corporate yield spread most since crisis

**May 26.** China's central bank's decision to ease monetary policy to revive bond issuance has caused China's corporate borrowing costs to fall the most since the global financial crisis. The spread between AAA rated companies and the sovereign yields has narrowed down to 126bps from 186bps on March 31. These lower costs of funding have encouraged more than CNY1tn of debt offerings since March 31. (Bloomberg)

### Fitch upgrades Greece's credit rating to "B"

**May 22**. Fitch Ratings has upgraded Greece's long-term foreign and local currency Issuer Default Ratings (IDRs) to 'B' from 'B-'. The outlook for both categories remained as stable. The country's senior unsecured foreign and local currency bonds have also been upgraded to 'B' from 'B-'. Greece achieved a primary surplus in the general government account in 2013 - a key target of the EU-IMF programme and an over-performance relative to its budget plan. Fitch forecasts the adjusted primary surplus will rise further in 2014 to 1.4% of GDP. The rating agency also stated that near-term sovereign liquidity risk has fallen, although it remains contingent on Greece staying on track with its programme. (Reuters)

### Moody's cuts outlook for China's property industry to negative

**May 21**. Moody's cut its outlook for China's property industry, signalling slower growth of residential property sales and weakening liquidity over the next 12 months. The negative outlook is caused by the tighter onshore liquidity, higher mortgage rates, possibility of further easing of property prices and slower GDP growth in China. However, Moody's believed that the credit quality for most of the rated developers would remain unchanged because of their good liquidity and access to funding. Besides, since housing price started to cool down in the late of 2013, China' s central bank has demanded the commercial banks to grant more home loans and set mortgage rates at reasonable levels in order to avoid the abrupt correction which would bring risks to banking systems and economy. (Reuters)

**China allows local governments to sell CNY 109.2bn of bonds in 2014** (WSJ)

**Portugal's borrowing costs rise at EUR 1Bn bill auction** (Bloomberg)

## Regulatory Updates

### EU financial transaction tax plans turn to derivatives

**May 23.** The European Union is formalizing a transaction tax by deciding which derivative contracts to tax and how the rule can be expanded in future. Documents prepared for the May 28 working group meeting showed that Greece has proposed several plans to finalize the tax law. One plan would be to insert a review clause which would allow other products to be included in the tax, and the other requires the European Commission to offer a new proposal for any expansion. There has been little progress on the tax initiative so far as participants from 11 interested EU nations could not agree on the definition and scope of the proposed law. Countries outside the 11 member nations such as the UK and Sweden have also voiced concern, saying they will be affected by the transaction tax implementation even if they do not plan to participate in the tax plan. (Bloomberg)

**Finra trade-surveillance system to be revised**

**May 21**. The Financial Industry Regulatory Authority (FINRA) is revising a trade-surveillance system which enables smaller brokers that do not use clearing firms to have more flexibility to send trade and commission data to Finra with the help CARDS (Comprehensive Automated Risk Data System). This system would allow Finra to automate its analysis of suspicious activity by brokers. There have been complaints that the system will increase data security risk and compliance costs. In response to the complaints, Finra said that it would not require brokers to submit information that could possibly be used to identify an individual account owner.(Bloomberg)

**India's central bank eases rules for loans to exporters**

**May 21.** The Reserve Bank of India now allows exporters with a good track record of three years to obtain long-term loans for a maximum term of 10 years, as compared to the 1-year loan term before. Exporters will have to report to the central bank if their loan amount exceeds USD100mn. Besides, the interest rate charged by banks should not go beyond 200bps above LIBOR. (Reuters)

**US lawmaker fears some bank regulator standards too vague** (Reuters)

**ECB launches public consultation on supervisory fees** (ECB)

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