Are Rating Actions indicative of Corporate Performance?

CRISIL Ratings Roundup - First Half 2001-02

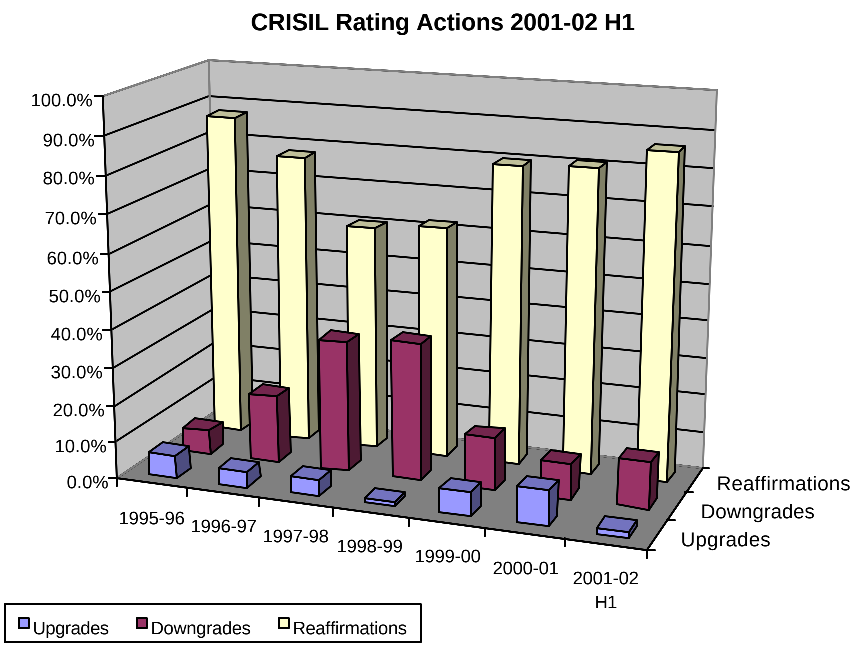
CRISIL has reaffirmed 85.6% of the long-term ratings, upgraded 1.4% ratings and downgraded 13% ratings during the first six months of the current financial year, indicating high stability of CRISIL ratings. The stability of ratings, as indicated by the percentage of rating reaffirmations to the total rating actions, improved to 86% in the first six months compared to 81% stable ratings in 2000-01. The credit ratio, the ratio of upgrades to downgrades, has declined to 0.11 in the first six months of current financial year compared to 1.0 during the last year. CRISIL rating actions exhibited strong correlation with macroeconomic parameters in the past and the sharp decline in Credit Ratio is indicative of the economic slowdown. The decline in Credit Ratio correlates with the macro economic trends such as low IIP growth rate, the meager equity mobilization by the corporates in the first six months and the downward revision of GDP growth rate forecast.

CRISIL's Long-term Rating distribution continued the trend of polarization of ratings i.e., reduction in A/BBB ratings and increase in AAA/AA ratings and speculative grade ratings in the first six months. The high servicing costs of the Fixed Deposit and the corporates' ability to negotiate loans at finer rates from the banking system, have resulted in the number of corporates moving away from Fixed deposit market, which reflected in the reduction in number of outstanding FD ratings.

The excess liquidity in banking system has increased investors' appetite for lower investment grade ratings during the current financial year. For the first time, CRISIL's 'AA' and 'A' ratings accounted for almost equal amount of debt compared to CRISIL's 'AAA' ratings. Also, the softer interest rate regime has resulted in the corporates' preference for low cost short-term debt and Commercial Paper programme to fund working capital needs. The new short-term debt rated by CRISIL has increased by 110% in the first six months of 2001-02 over the corresponding period last year.

<u>CRISIL ratings continued to exhibit high stability</u>

CRISIL long-term rating actions reveal that 118 ratings were reaffirmed, while 2 ratings were upgraded and 18 ratings were downgraded during the first six months of the current financial year. Reaffirmed ratings accounted for 86% of the total rating actions confirming improved stability of CRISIL ratings during the first six months of current financial year, compared to 81% of stable ratings in 2000-01. CRISIL's long-term rating actions revealed a decline in the Credit Ratio, the ratio of upgrades to downgrades. The credit ratio declined to 0.11 in the first six months of current financial year from 1.0 during 2000-01. While the 18 downgrades in the first six months of the current year were in line with the past two year's trend, the number of upgrades were far lower compared to the last year. The list of upgrades and downgrades are enclosed in Appendix I.



While no investment grade rating got downgraded to default category during the first six months, four speculative category rated entities were downgraded to default category.

Even among the downgrades, only two ratings were downgraded from investment grade category to speculative grade category, while 11 downgrades were within investment grade and 5 within speculative grade. This re-establishes the fact that CRISIL investment grade ratings exhibit high degree of stability.

Sector-wise rating actions:

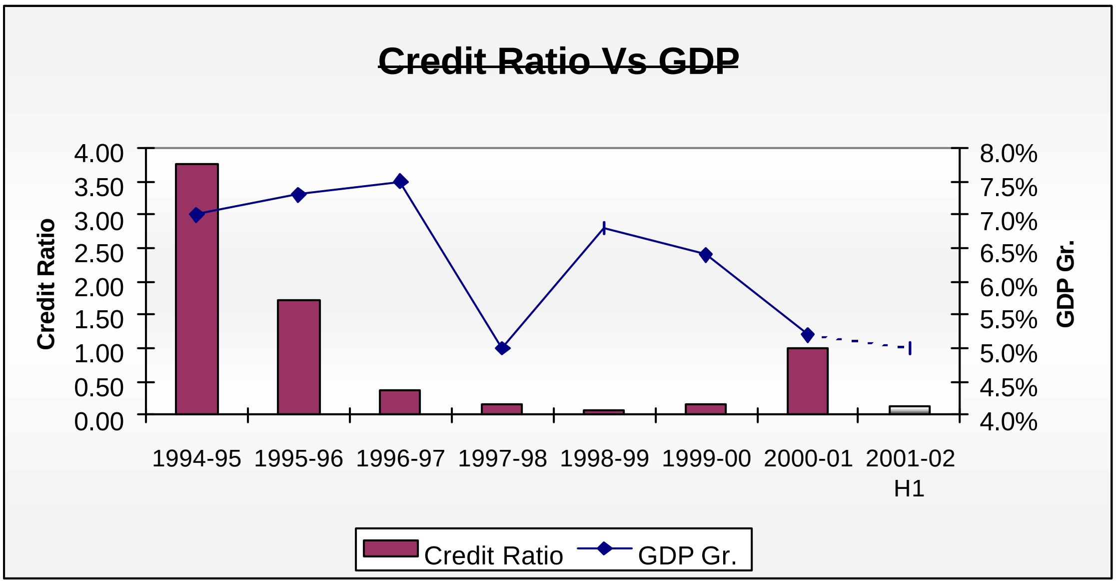
As per the Long-term ratings portfolio of CRISIL, manufacturing entities constitute around 77% of the total portfolio of ratings. However, rating upgrades/downgrades in the first half were mainly limited to the manufacturing sector as 85% of upgrades and downgrades were from the manufacturing sector, while only 15% were from finance and infrastructure sector.

<u>Decline in Credit Ratio - an indicator of economic slowdown:</u>

CRISIL rating actions as depicted by Credit ratio, the ratio of upgrades to downgrades, exhibit strong correlation with macroeconomic indicators such as Gross Domestic Product (GDP) growth rate, Index of Industrial Production (IIP) growth rate and equity mobilized by Indian corporates.

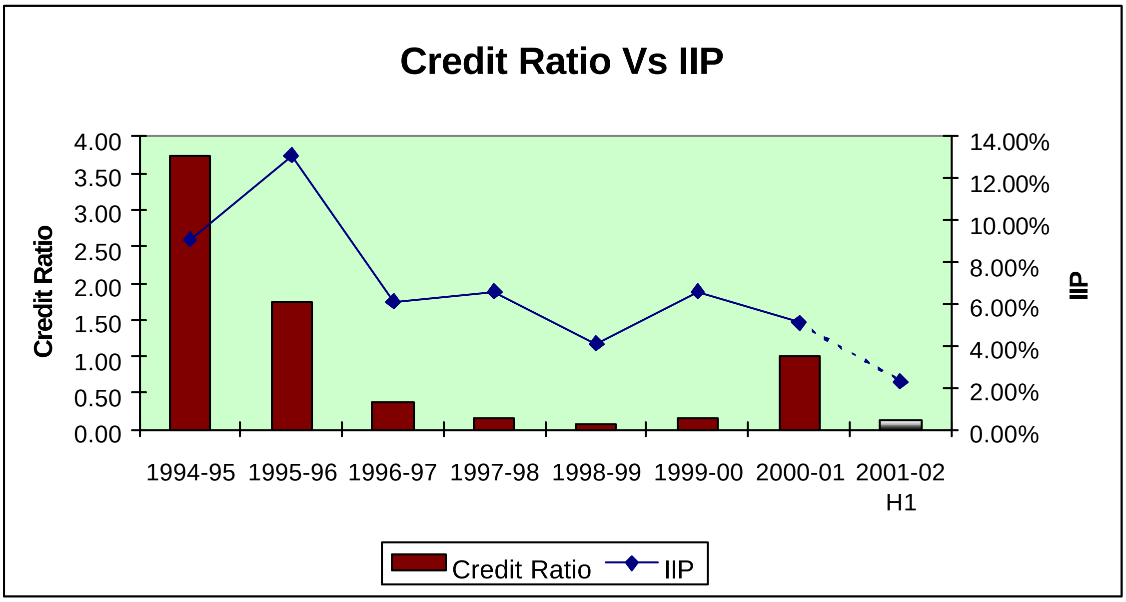
Credit Ratio Vs GDP growth

A strong correlation was observed between GDP growth rate and the Credit Ratio for the previous six years, upto 1999-00. A marginal deviation witnessed in 2000-01 was when the GDP growth rate marginally dipped to 5.2%, but Credit ratio improved to 1.0, the reason was CRISIL's pro-active rating actions in the previous years leading to lower downgrades in 2000-01. During the current year (2001-02) the agricultural growth is expected to be strong due to normal rainfall in 85 percent of the gross cropped area. The weak industrial growth coupled with the after shocks of September 11 events are expected to dampen the GDP growth rate to around 5%, compared to over 6% projected at the year beginning.



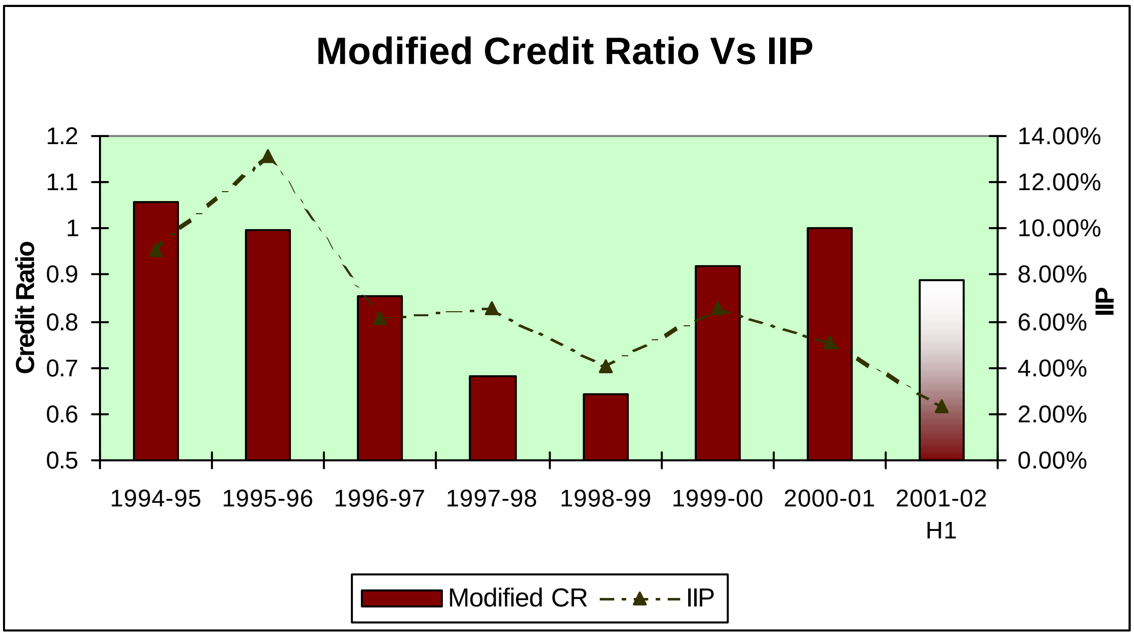
Credit Ratio Vs IIP Growth

The Index of Industrial production (IIP) growth rate was higher at 9.5% and 13% during 1994-95and 1995-96 respectively and in those years the credit ratios were above 1.5 level. Subsequently, the IIP growth rate dropped to around 4 to 6% and the Credit ratio trends also followed a similar trend of remaining within 1.0 or lower levels. The IIP growth rate during April- July 2001 declined to 2.3% compared to a 5.2% in 2000-01, similar to the declining trend in Credit ratio during the first six months of current financial year compared to the last year.



Modified Credit Ratio Vs IIP Growth Rate:

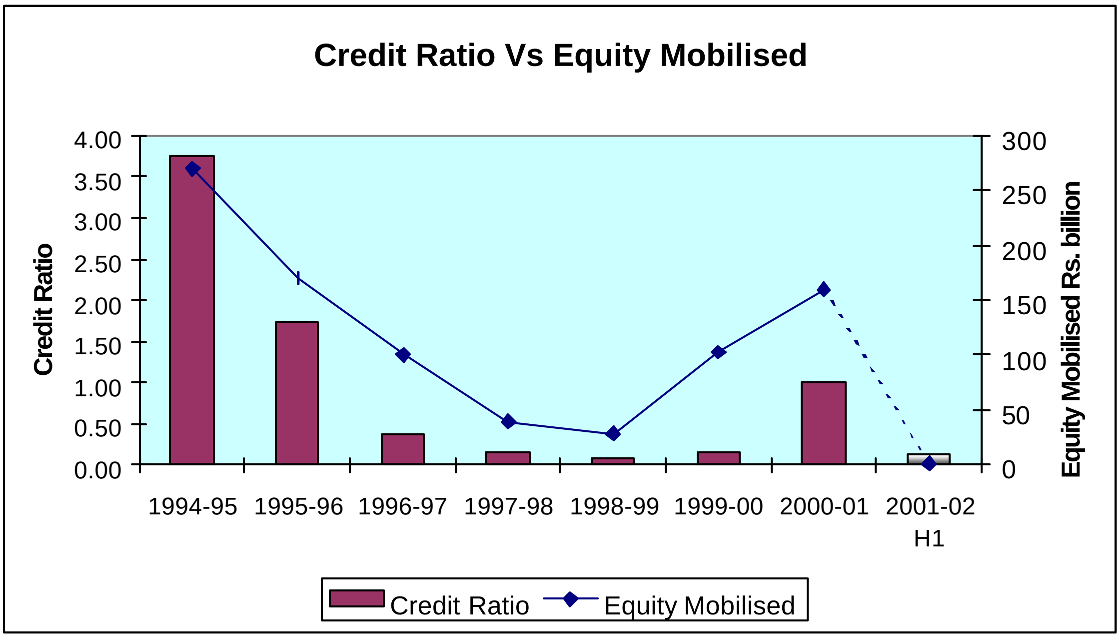
Modified Credit Ratio, defined as the ratio of (upgrades + re-affirmations) to (downgrades + re-affirmations), depicts all rating actions including upgrades, downgrades and re-affirmations. The modified Credit Ratio minimizes the volatility in credit ratio, when small number of upgrades and downgrades occur in the reference period, and the re-affirmations are larger in number. A correlation of modified credit ratio with IIP growth rate is given in the graph below.



As per the above graph, the Modified Credit ratio show higher correlation to the IIP growth rate than the Credit ratio as shown in the previous graph.

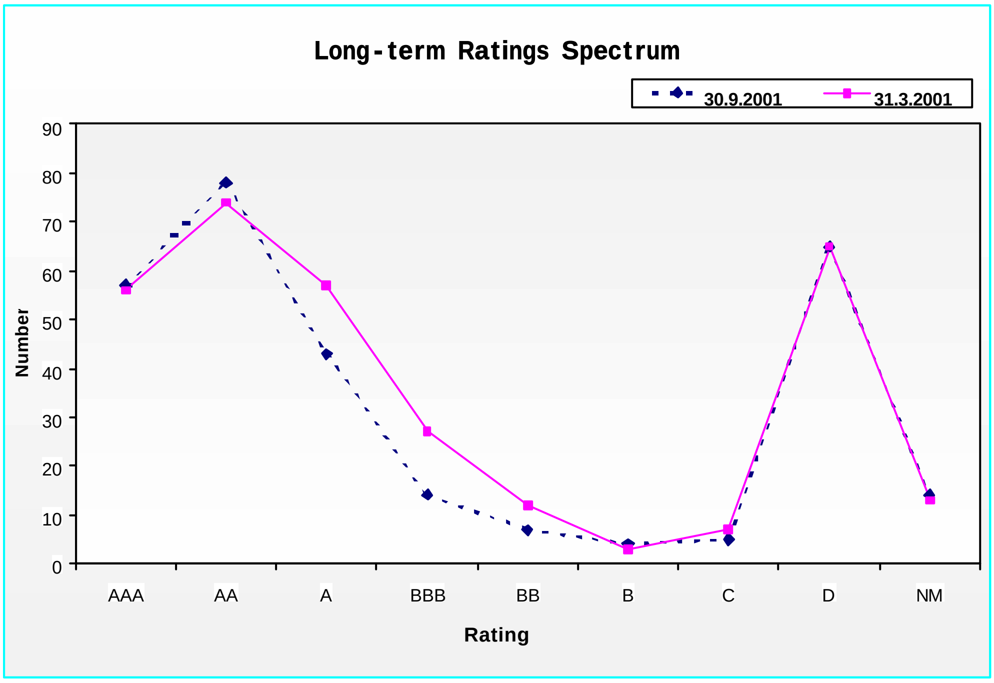
Credit Ratio versus Equity mobilization:

As depicted in the chart overleaf, the equity mobilized by Indian corporates showed a strong correlation for all the previous seven years with the credit ratio, i.e., higher the equity mobilized by corporates, higher the credit ratio and vice versa. The equity mobilized during the first five months (April-August 2001) of current financial year was Rs. 1.2 billion, compared to Rs. 59.1 billion in April-August 2000. This abnormally low equity mobilization correlates with the sharp decline in credit ratio to 0.11.

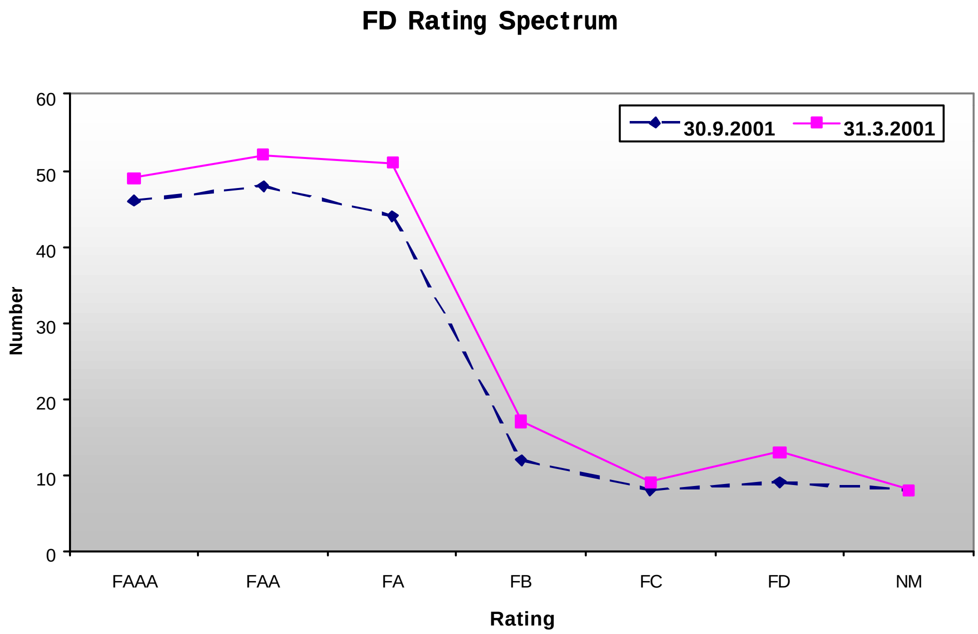


<u>Long-term rating distribution continued the trend of polarization:</u>

The trend of increasing polarisation of ratings towards the ends of the rating scale continued during the first six months of 2001-02 also. The sharp decline in number of A and BBB ratings was observed in the first half, which resulted in sharper edges to the long-term ratings spectrum. While a part of this reduction was on account of upgrades / downgrades to other rating categories, a large part of this reduction was on account of rating withdrawals from these categories. This trend has been observed over the past few years.



<u>Fixed Deposit steadily losing to other debt instruments:</u>



Contrary to the past trends of polarization of FD ratings, the Fixed Deposit rating spectrum shifted downwards with decline in rating entities across all rating categories. The Fixed Deposit has been losing its prominence as a debt instrument to mobilize resources directly from public, except in the banking sector. The high servicing costs of Fixed Deposits and the corporates' ability to negotiate loans at finer rates from the banking system together have impacted the number of corporates moving away from Fixed deposit market.

‘AA’ and ‘A’ rated entities gaining prominence:

For the first time, CRISIL’s ‘AA’ and ‘A’ ratings accounted for almost equal amount of debt compared to CRISIL’s ‘AAA’ ratings. During the first six months of current year, ‘AAA’ rated entities mobilized only 55% of total new rated debt, as compared to 93% in the same period last year. The new debt raised by AAA rated entities declined by 26% in 2001-02 H1 compared to the corresponding period last year, while the debt raised by ‘AA’ & ‘A’ rated entities increased significantly by eight times in the 2001-02 H1 over the corresponding period in the last year.

As can be observed from the table below, the new long term debt rated by CRISIL has increased both in terms of number of debt instruments and the debt amount. The new debt instruments have increased from 57 to 59, while debt volume has increased by 26% in the first six months of 2001-02 compared to the same period in 2000-01.

	April-Sept 2001-02		**April - Sept 2000 - 01**	
Rating	Number of Issues	Debt Volumes in Rs. Crores	Number of Issues	Debt Volumes in Rs. Crores
AAA	25	17433	26	23512
AA	30	14117	29	1679
A	4	250	2	20
BBB				
Total	59	31800	57	25211

Trends in CRISIL rated short-term debt instruments:

The softer interest rates and the excess liquidity in the banking system has increased the corporates’ appetite for low cost short-term debt to fund working capital as well as replacement of high cost debt with Commercial Paper Programme. The short-term debt mobilized increased by 110% in the first six months of 2001-02 compared to the corresponding period last year. Still in 2001-02 H1, around 97% of the total short-term debt had very strong rating, with very few takers for lower than P1+ rated short-term debt.

Rating	**April-Sept 2001-02**		**Apr-Sept 2000-01**	
	Number of issues	Debt Volumes in Rs. Crores	Number of Issues	Debt Volumes in Rs. Crores
P1+	39	5878	61	2804
P1	6	202	4	70
P2+	1	10	1	6
P2				
Total	46	6089	66	2880

Appendix I

CRISIL Rating Upgrades / Downgrades in First six months of 2001-02:

	UPGRADES				
Sl No	Company	Industry	Sector	From	To
1	Reliance Petroleum Ltd.	Oil & Refining	Infrastructure	AA	AA+
2	Tata SSL Ltd.	Steel & Steel Products	Manufacturing	A-	AA-
	DOWNGRADES				
Sl No	Company	Industry	Sector	From	To
1	Raasi Fertilizers Ltd.	Fertilisers	Manufacturing	C	D
2	Southern Iron and Steel Co Ltd.	Steel & Steel Products	Manufacturing	C	D
3	Hyderabad Industries Ltd.	Diversified	Manufacturing	BBB-	B
4	Bharat Gears Ltd.	Auto Ancillaries	Manufacturing	BBB+	B
5	Automobile Corporation of Goa Ltd.	Auto Ancillaries	Manufacturing	BB+	C
6	Lok Housing & Construction Ltd.	Builders	Manufacturing	BB	D
7	Indian Organic Chemicals Ltd.	Chemicals-Organic	Manufacturing	B	D
8	Industrial Development Bank Of India	Financial Institutions	Finance	AAA	AA+
9	BPL Ltd.	Consumer Durable	Manufacturing	AA-	A+
10	Xerox Modicorp Ltd	Office Equipment	Manufacturing	AA-	A+
11	National Fertilizers Ltd.	Fertilisers	Manufacturing	AA-	A+
12	La Farge India Ltd	Cement	Manufacturing	AA+	AA
13	Coal India Ltd.	Mining	Infrastructure	AA	AA-
14	Coates of India Ltd.	Miscellaneous	Manufacturing	AA	AA-
15	Purolator India Ltd.	Auto Ancillaries	Manufacturing	A-	BBB+
16	Wockhardt Life Sciences Ltd	Chemicals-Speciality	Manufacturing	A+	A
17	Tata Engineering and Locomotive Company Ltd.	Automobiles - 3&4 wheelers	Manufacturing	AA	AA-
18	Tata Finance Ltd	NBFC	Finance	AA-	A-