

Rating Revisions: Q3 FY15

In an attempt to gain insights into the prevailing credit quality of the system, we have analysed here the change in the credit ratings assigned (rating upgrades, downgrades and reaffirmations) to the entities that are rated by CARE Ratings over the last 15 quarters (Q1 FY12 to Q3 FY15). We have also examined the relationship between credit quality and the underlying economic health of the country and based on the extent of correlation between the two seek to gain a forward guidance on the overall economic environment.

We have further segregated our analysis to showcase the changes in credit quality based on the size of the organisation (Large Enterprises and SME¹) as well as industry-wise and thereby pin-point the segments and sectors that have seen an improvement, deterioration or stability in their credit profile.

Modified Credit Ratio (MCR)

CARE's modified credit ratio (MCR) helps measure mobility in ratings. It is defined as the ratio of (upgrades and reaffirmations) to (downgrades and reaffirmations). An increase in MCR denotes an increase in upgrades vis-à-vis downgrades while a decrease in MCR shows the reverse. Therefore, an increase in the MCR implies stable and improving credit quality of the rated entities. An MCR closer to one indicates higher stability in ratings, with larger proportion of reaffirmations.

Given that CARE rates a large and diverse set of entities, the movement of MCR can be regarded as being indicative of the general business and economic environment of the country.

CARE's MCR has witnessed a significant improvement in the current fiscal viz. in the second and third quarter. The MCR increased to a 12 quarter high of 1.25 in the second quarter and although the ratio did witness a moderation in the third quarter (Q3 FY15) to 1.23, it continues to be close to 3 year highs, reflective of the continued improvement in the credit quality of the rated entities.

Exhibit 1 below captures the movement in MCR over the last 15 quarters. The ratio has seen a steady and stable progress since Q2 FY14, with the ratio of over 1 since, indicating the improving stability at the system level.

CARE defines SME (Small and Medium Enterprise) as entities that have a turnover upto Rs. 100 cr and a debt size of Rs. 50 crs

Exhibit 1 : MCR

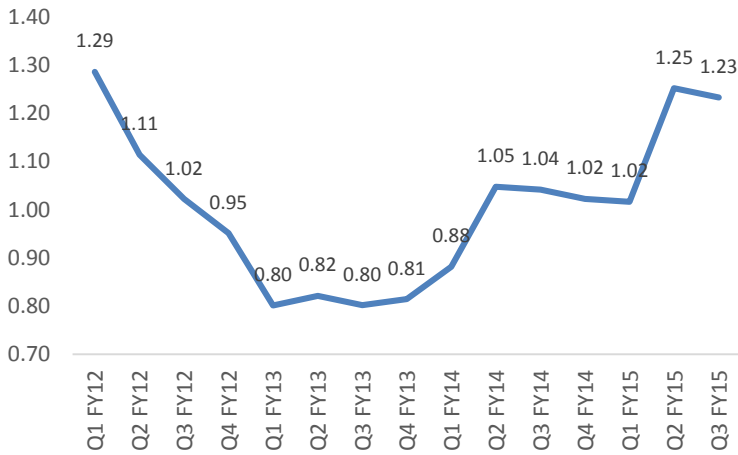


Exhibit 2: MCR - LME and SME



Source : CARE Ratings

Credit Quality – Large Enterprise (LE) and SME

Comparing the movement in MCR of the Large Enterprises and SME segments, it can be seen that the credit quality of the Large enterprises has been superior and steadier, especially since Q1 FY14. The Large enterprises have recorded a MCR of above 1 for the last 6 quarters, reflecting stable and improving credit conditions. The last 2 quarters i.e. Q2 FY15 and Q3 FY15 have seen a sharp improvement in the MCR of the LE segment to 1.29 and 1.20 respectively. Likewise, the SME segment too has been recorded an MCR of above 1 since the last 5 quarters, with the latest quarter gone by seeing the MCR touch a high of 1.31. However, comparing the trend in MCR for both the segments (exhibit 2) it can be seen that the fluctuations in the credit quality of the SME segment has been more pronounced.

There has been a significant increase in the number of upgrades in the LE segment in the ongoing fiscal. In absolute number, 430 entities have seen their ratings being upgraded during Q1 to Q3 FY15, compared to the 343 entities that saw a rating upgrade in the whole of FY14. The comparative figures for upgrades for the SME segment have been 178 in the 3 quarters of FY15 and 174 in FY14.

Trend in Rating Movement

The trend in rating movements in CARE rated entities shows that upgrades have been outnumbering downgrades, since Q2 FY14. Also, a higher number of entities have had their ratings being reaffirmed. In Q3 FY15, 294 entities saw their ratings being upgraded, 106 entities had their ratings downgraded and 703 entities had their ratings being reaffirmed. **There has been a rather sharp increase in the number of upgrades in Q3 FY15.** A year on year comparison shows that the number of entities who have seen their ratings being upgraded has nearly doubled and fewer entities have seen their ratings being downgraded. In Q3FY14, 153 entities recorded a rating upgrade, 120 entities a rating downgrade and 676 entities saw their ratings being reaffirmed.

Exhibit 3: MCR and GDP

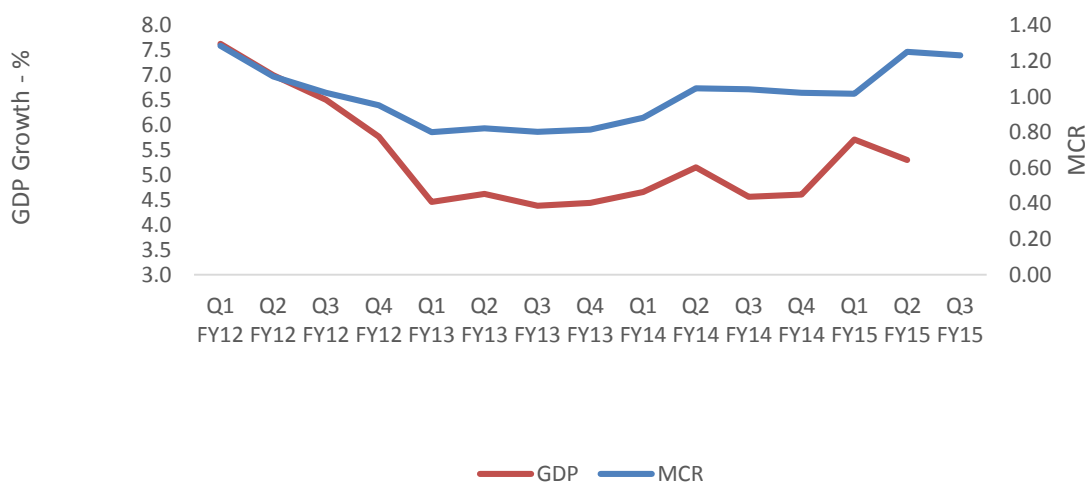


Exhibit 3 highlights the strong correlation (0.71) between the MCR and GDP (FY12 to Q2FY15). The weakness in the MCR in the FY12 and FY13 can be attributed to the weakness in the country’s economy.

Industry wise Rating Action

A comparison of the industry wise MCR across the various years has been given in table 1

Table 1: Industry-wise Movement in MCR

Industry	2011-12	2012-13	2013-14	2014-15 (9 months)
Computer hardware, electronic & optical products	0.83	0.46	1.07	1.25
Leather and related products	1.00	1.00	1.25	1.17
Education	0.97	0.79	1.00	1.29
Printing & reprodn of recorded media	1.00	0.78	1.09	1.83
Paper and paper products	1.13	0.80	1.00	1.68
Manufacture of apparel	1.25	0.71	0.94	1.43
Agriculture, forestry and fishing	1.00	0.91	1.18	1.52
Rubber and plastics Products	1.05	0.76	1.15	1.37
Textiles	0.97	0.85	1.25	1.41
Pharmaceuticals	0.98	0.75	1.00	1.34
Food and food products	1.07	0.86	1.08	1.23
Electricity - Generation	0.98	0.79	0.85	1.23
Beverages	0.78	0.84	1.27	1.06
Transportation and storage	0.86	0.71	0.94	1.16
Construction	0.93	0.75	0.90	1.17
Auto	1.38	0.92	0.97	1.20
Fabricated metal products	1.27	0.86	1.08	1.36
Telecom	1.50	0.39	0.87	1.20
Wholesale and retail trade	1.05	0.87	1.00	1.06
Chemicals and chemical products	1.11	0.94	1.04	1.32
Ceramics	0.94	0.69	0.93	1.47
Electrical Equipment	0.87	0.69	0.93	1.03
Real Estate activities	0.79	0.89	0.96	1.05
Banks	1.16	0.87	0.80	0.97
Iron and Steel	0.90	0.79	0.99	0.99
NBFI	1.23	1.00	1.09	1.09
Cement and related products	1.00	0.82	1.03	1.00
Coke and refined petroleum products	1.43	0.69	1.10	1.17
Crude and Natural Gas extraction	0.67	0.83	0.75	1.00
Electricity -T&D	0.63	0.80	1.00	1.00
Financial Institution	1.00	0.86	0.92	1.00
Mineral Mining	0.70	0.91	1.27	1.13
NBFC	1.00	1.00	1.14	1.26
Water supply; sewerage, waste mgmnt etc.	1.09	0.61	1.38	1.06
Information and communication	0.92	0.80	1.03	1.40
Non Ferrous Metals	0.93	0.73	0.97	1.00
Sugar	0.56	0.82	1.13	1.00
Coal Mining	1.00	0.50	0.71	0.57

There has been a notable improvement in the credit quality across sectors in FY15 as is evident from table 1 above.

- The sectors that have recorded a higher number of upgrades and have seen a noteworthy improvement in their MCR levels above 1 (which indicates stability in credit quality) includes - construction, auto, textiles, pharmaceuticals, agriculture & allied activities, rubber & plastics Products, food products, telecom, paper & paper products, education, apparel manufacture, electricity (generation), wholesale and retail trade, chemicals, ceramics, printing, metal fabrication, electrical equipment, real estate activities, computer hardware, electronic & optical products, transportation & storage, communication, coke & refined petroleum product and crude oil & Natural Gas extraction.
- Sugar, water supply & sewerage, beverages, mineral mining and cement sectors have seen a moderation in their credit quality in FY15. These sectors however, enjoy stable credit quality as indicated by their MCR of 1 or above.
- The coal mining sector has seen a deterioration in credit quality. The MCR for the sector has fallen from 0.71 in FY14 to 0.57 in the current fiscal.

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