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Transforming Big Data into Smart Data

Weekly Credit Brief

Apr 15 - Apr 21 2014

Story of the week

Adani Enterprises rides the Modi-wave

As India heads to poll to elect its next government, investors are analyzing economic and business policies proposed by various leading candidates. This election fever has boosted the SENSEX index by over 7% this year. Amidst this rally, Adani Enterprises stands near the very top. Since February 14 this year, the stock price for Adani Enterprises has risen from INR 215/share to INR446/share – an increase of over a 100%. The rise is even more pronounced from September 2013, i.e. a jump of 217%. The improved outlook for the firm is reflected in the RMI PD as well. 1-year RMI PD for Adani Enterprises has seen a steady decline. Adani's RMI PD has come down from a high of 1123bps in September 2013 to a low of 46bps currently. During the same period, distance-to-default, a volatility adjusted leverage measure and an input into our model, has also improved significantly to from 0.36 to 1.56.

Figure 1: One-year RMI PD for Adani Enterprises vs Adani Enterprises share price. *Source: Bloomberg, Risk Management Institute*

India's ongoing general elections and speculations surrounding the same are arguably the primary drivers of the surge in Adani shares. As per opinion-polls, Narendra Modi (Gujarat's Chief Minister and a senior member of the opposition Bharatiya Janta Partly (BJP)) is most likely to be India's next Prime Minister. Based in Gujarat, Adani Enterprises has benefited hugely from Chairman Gautam Adani's reportedly close relationship with Narendra Modi. In addition, the BJP manifesto lists out projects and initiatives where the group has interests. A BJP loss however, is likely to significantly dent investor confidence in the firm and cause upward pressure on the PD.

Adani Ports, 75% of which is owned by Adani Enterprises, could benefit from BJP's promise of connecting all ports through the Sagarmala project. Through Adani Ports, the group has three ports in operation, with plans to commission another three at Mormugao, Visakhapatnam and Kandla over the next few years.

Adani Power, another Adani firm owned 69% by Adani Enterprises has also seen a massive improvement in stock price. Since September last year, the share price has gone up 63%. Moreover, the firm has become

India's largest power producer, overtaking giants Tata Power and Reliance Power.

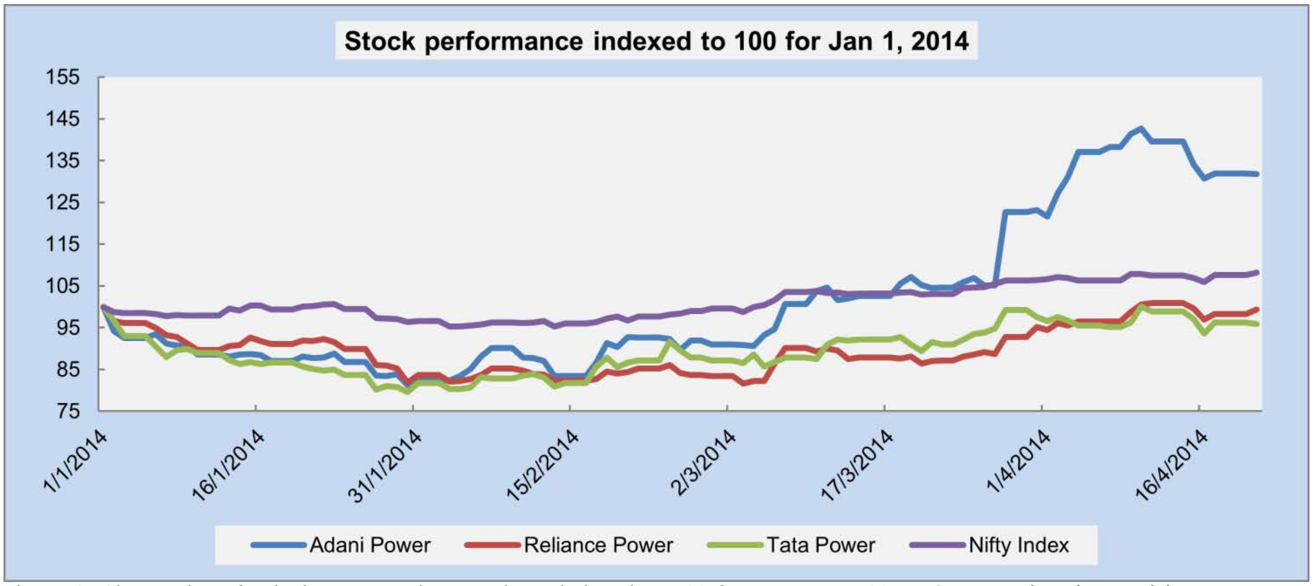

Figure 2: Share price of Adani Power and competitors, indexed to 100 for January 1, 2014. *Source: Bloomberg, Risk Management Institute*

Adani Enterprise's confidence, evident in ambitious expansion projects overseas has also aided the bull run. Adani is developing and operating mines in India, Indonesia and Australia as well as importing and trading coal from many other countries.

Credit News

Chile keeps 4% rate after four rate reductions in six months

Apr 17. Chile's central bank, Banco Central de Chile, kept interest rates unchanged at its policy meeting on Thursday. This decision was largely expected by market participants on back of quickening inflation. In the past six months, the central bank had delivered four reductions, causing the inflation rate to increase with a recent movement from 3.2% in February to 3.5% in March. Additionally, the inflation forecast estimated by policy makers in the quarterly monetary report was corrected upwards from 2.5% to 3%. (Bloomberg)

Junk buyout loans eclipse '07 record in deal making frenzy

Apr 16. The amount of leveraged loans issued to finance acquisitions this year could exceed the record set in 2007 as several US companies use borrowed capital to fund their expansion plans. A low interest rate environment and the issuance of covenant light loans are among some of the factors that explained the increase in leveraged loan activity. Analysts said that lenders have been searching for more opportunities to invest in M&A financings and this further fuel the deal financing trend. The proportion of first lien borrowings to EBITDA in speculative grade US companies has climbed to 4.2 times in Q1 2014, which is near the record high of 4.6 times in Q4 2007.(Bloomberg)

Russian debt and equity sales stall

Apr 15. Russian sovereign bond issuance has fallen significantly by 74% compared to the same period last year. This week, a RUB bond auction did not take place with the Russian Finance Ministry stating that the cancellation is due to "current market conditions". The yield on 10-yr government bonds has significantly increased from 8% at the beginning of 2014 to recent 9.2%. The increasing yield reflects the additional risk of the bond caused by recent political developments. (Financial Times)

Southern Europe's economies are in worse shape than tumbling bond yields suggest (The Economist)

China firm plans USD 1bn distressed asset fund for foreigners (Chicago Tribune)

Italian bonds gain amid sale demand (Bloomberg)

Kuroda inflation focus risking money-market health (Bloomberg)

IMF board signs off on latest Portugal review (Reuters)

US Treasury to sell USD 48bn in bills (Reuters)

Regulatory Updates

Europe's banks prepare for ECB tests with new provisions

Apr 15. Europe's 20 largest lenders have set aside EUR 71.5bn as provisions for loan losses over 2013 a Reuters analysis showed last week. Although the amount of provisions was down 20% compared to 2012 when business was tougher, core tier 1 capital ratios have risen to an average of 11.85% from 10.77% in 2012. The ECB currently requires banks to have a tier 1 capital ratio of 8%. Such actions may substantially reduce the likelihood of European banks failing the upcoming ECB stress tests later this year. (Reuters)

Supervisory framework for measuring and controlling large exposures - final standard

Apr 15. A supervisory framework proposed by the Basel Committee on Banking Supervision for measuring and controlling large exposures will take effect from 1 January, 2019. This framework is designed to ensure a common minimum standard for measuring, aggregating and controlling single name concentration risk across jurisdictions, since inconsistent results have been found under the original standard set out in 1991. With the constraint of the large exposure limits indicated in this framework, a bank's exposure to a single or a group of connected counterparties is set at 25% of the Tier 1 capital. And a tighter limit of 15% is applied to exposures between banks designated as global systemically important banks. (Bank for International Settlements)

EU to approve bank rules before May election slows legislative machine (Reuters)

Yellen says higher capital rules may be needed for big banks (Bloomberg)

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