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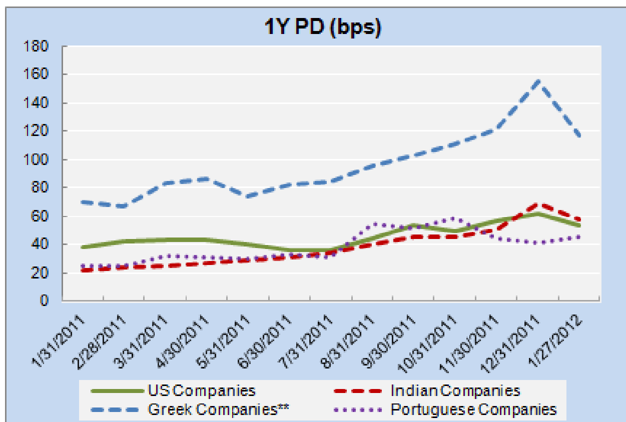
Weekly Credit Brief

Jan 22 – Jan 28 2012

Story of the Week

Fed enhances its pro-growth stance while uncertainty lingers over Greece and Portugal

The US Federal Reserve announced last Wednesday that it expected to maintain the federal funds rate between 0 to 0.25% until late 2014 and indicated further easing of its monetary policy to support the US economy. This indicates a more accommodative stance by the Fed, which may see the timeframe for near-zero interest rates extended from a previous estimate of mid-2013, as it lowered the assessment of the US economy.



The latest Fed's monetary decision has boosted the credit outlook of US companies as it may sustain their low costs of borrowing and ensure ample liquidity in the real economy. However, recent weaker-than-expected home sales statistics and mixed earning reports from US companies attest to the Fed's concern for the economy and point to economic challenges ahead for US companies. The RMI CRI's 1-year probability of default (PD) for all US companies decreased to 53.2bps on January 27 from a high of 61bps in December, but it remained high compared to a low of 35bps last July.

In a similar move, the Reserve Bank of India reduced the cash reserve ratio (CRR) requirements by 50bps to 5.5% as it boosted liquidity supply to support the Indian economy. The credit outlook of Indian companies showed some improvement as the 1-year PD for all Indian companies decreased to 57.4bps on January 27 from a high of 68bps last December.

Meanwhile, negotiations between Greece and its private creditors over a voluntary debt restructuring broke down last Monday, as the two sides hit an impasse over the terms of a debt swap. Private creditors represented by the Institute of International Finance (IIF) proposed a swap of existing Greek bonds into new, longer-dated ones with a minimum coupon of 4%, but this was rejected by Greece and other European governments who were seeking a coupon of no more than 3.5%. A voluntary debt restructuring is important for reducing Greece's debt burden. It is also a pre-condition for Greece to secure a second €130bn bailout by the IMF and the EU, without which Greece would risk a disorderly default on €14.5bn of debts maturing in March.

After the deadlock on Monday, talks continued for the last week and optimism emerged among European officials about an impending agreement. However, Greece still needs to satisfy demands from the IMF, EU and ECB for more aggressive budget reductions before it can receive the second bailout funds. Uncertainty also lingers over the sustainability of Greece's €350bn debt load. After the IMF said that public creditors might need to accept losses on Greek bonds to bring down Greece's debt to a sustainable level, the ECB ruled out extending debt maturities while France and Italy rejected voluntary write-downs. As the debt crisis continued in Greece, the credit outlook of Greek companies remained negative. The RMI CRI's aggregate 1-year PD for all Greek companies** was 116.6bps on January 27 compared to a low of 70bps last January.

Elsewhere in Europe, Portugal's 5-year credit default swap (CDS) rate soared to a record 12.7% last Tuesday, as fears grew that Portugal might follow Greece in seeking a second bailout and voluntary debt writedowns by private creditors. The yield of Portugal's 10-year government bond remained elevated at 13.73%, after its rating was downgraded to 'junk' status by S&P on January 13. Increased woes such as high borrowing cost for Portugal could be detrimental to the credit outlook of Portuguese companies. The 1-year PD for all Portuguese companies increased to 45.1bps on January 27 from a low of 30bps last July.

** Two Greek banks were excluded from this data series: Geniki Bank because of a rights issue on December 8, and T Bank SA as it was forced into liquidation by the Greek central bank on December 17.

Read More:

FOMC statement from January 24-25 meeting (Reuters)
January rally interrupted as buyers pull back (Reuters)
Fed sets path for three years of low rates (FT)
Eurozone finance ministers reject Greek debt offer (Telegraph)
Greek Creditors Still Seek Deal After Bond Swap Rejected (CNBC)
WRAPUP 2-EU, IMF press Greece on reforms, Rehn upbeat on debt deal (Reuters)
WRAPUP 3-Greek PM sees quick debt swap deal, end-game in sight (Reuters)
ECB split on how to handle any Greek bond losses (Reuters)
Portuguese Bondholders Fret over Cut (WSJ)

Date	Economy	Title	Summary
Jan 26, 2012	Japan	Japan's stricken nuclear operator set for $13 billion bailout	The Japanese government is planning to inject 1tn yen ($12.8bn) into Tokyo Electric Power Co (Tepco) after the company's management reversed their initial opposition to such aid that would effectively nationalize the company. The capital infusion would lead to the state-backed Nuclear Damage Liability Facilitation Fund taking a two-third share in Tepco, and should help to alleviate the company's financial stress at a time when it is suffering heavy losses and is seeking at least 1tn yen in new loans. Additional financing support is also likely from Japanese banks such as Mitsubishi, Mizuho and Sumitomo as they are expected to protect their large exposures to Tepco. Tepco is currently working on a business plan with the state-backed fund, in which the company is estimated to return to profit in fiscal 2013. According to the plan, Tepco will resume bond issuance in four of five years and will issue equity subsequently. The prospect of a bailout and banks' continued willingness to lend provided uplift to Tepco's credit outlook. The 1-year PD of Tepco eased to 729.5bps on January 27, from a 799.1bps in last December. However, this is still high as Tepco's PD was considerably lower at 3.4bps in last February, the month before its nuclear plants were struck by the earthquake and tsunami. **Read more:** Japan's stricken nuclear operator set for $13 billion bailout (Reuters)
Jan 23, 2012	Europe	EU's Barnier Says Will Stick to Bank Capital Plan	Concerned with the negative impacts of Basel III on bank lending to the real economy, France and Germany are urging a relaxation of the global bank capital rules. The finance ministers of these two countries are calling for a number of elements within the Basel III guidelines to be loosened, including extending the mandatory deadline for leverage ratio disclosure by three years, and providing special treatment for banks that own insurance companies. Despite France and Germany's call, Michel Barnier, European Commissioner in charge of financial regulation said the implementation of the Basel III Accords in Europe would continue as planned. Michel Barnier planned to publish a draft law to wind up troubled multinational banks in crisis, with measures such as imposing losses on bank bond holders. This law could take 1 to 2 years to be approved. **Read more:** UPDATE 1-EU's Barnier says will stick to bank capital plan (Reuters) Germany and France seek relaxation of bank capital rules: report (Reuters)
Jan 23, 2012	Hong Kong	HK banks bolstered by liquidity return	Last year's intensifying fears about a credit crunch in Hong Kong showed signs of easing this January, as savers increased deposits in Hong Kong and US dollars and slowed purchases of Renminbi. Hong Kong saw huge growth of Renminbi deposits last year as savers withdrew Hong Kong and US dollars to take bullish bets on the Renminbi's appreciation. Smaller deposits in Hong Kong and US dollars, combined with the impacts of the European debt crisis, had contributed to tightened

			liquidity in the city that saw mortgage rates tripling to 3% since one year ago. Banks seldom lend out in Renminbi because borrowers prefer US dollar loans to Renminbi loans due to the lower rates, and swapping renminbi into dollars is expensive. Growth of Renminbi deposits is losing momentum as the pace of the currency's appreciation is increasingly being questioned with China's slowing economy, dwindling current account surplus and slowing foreign exchange reserves. The expansion of Hong Kong and US dollar deposit base could boost the ability of banks to lend to Hong Kong firms and increase liquidity in the Hong Kong economy. The 1-year PD of Hong Kong firms retreated to 49.4bps on January 27, from a high of 51.6bps in last December. **Read more:** HK banks bolstered by liquidity return (FT)
Jan 25, 2012	Australia	ASIC welcomes international endorsement of Australia's regulatory regime on credit rating agencies	Australia has become the second country after Japan to receive endorsement by the European Securities and Markets Authority (ESMA) for the domestic regulatory regime on credit rating agencies (CRAs). The ESMA reached such decision after careful assessment of Australia's CRA regulatory framework, which has been strengthened by the Australian Securities and Investments Commission (ASIC) since January 2010. The removal of licensing exemptions for certain CRAs and the requirement that all CRAs should hold an Australian financial service license were among measures taken by ASIC to reinforce Australia's CRA regulatory framework. According to the ASIC chairman, due to the regulatory changes in place, Australia's CRA regulation is now aligned with the International Organization of Securities Commissions (IOSCO) principles and with regulations in major markets such as the United States, Europe and Japan. ESMA's backing of ASIC's credit rating agency regulation will allow Australian companies to use their Australian-issued credit ratings when they issue debts in the European Union. **Read more:** ASIC welcomes international endorsement of Australia's regulatory regime on credit rating agencies (ASIC)