Weekly Credit Brief

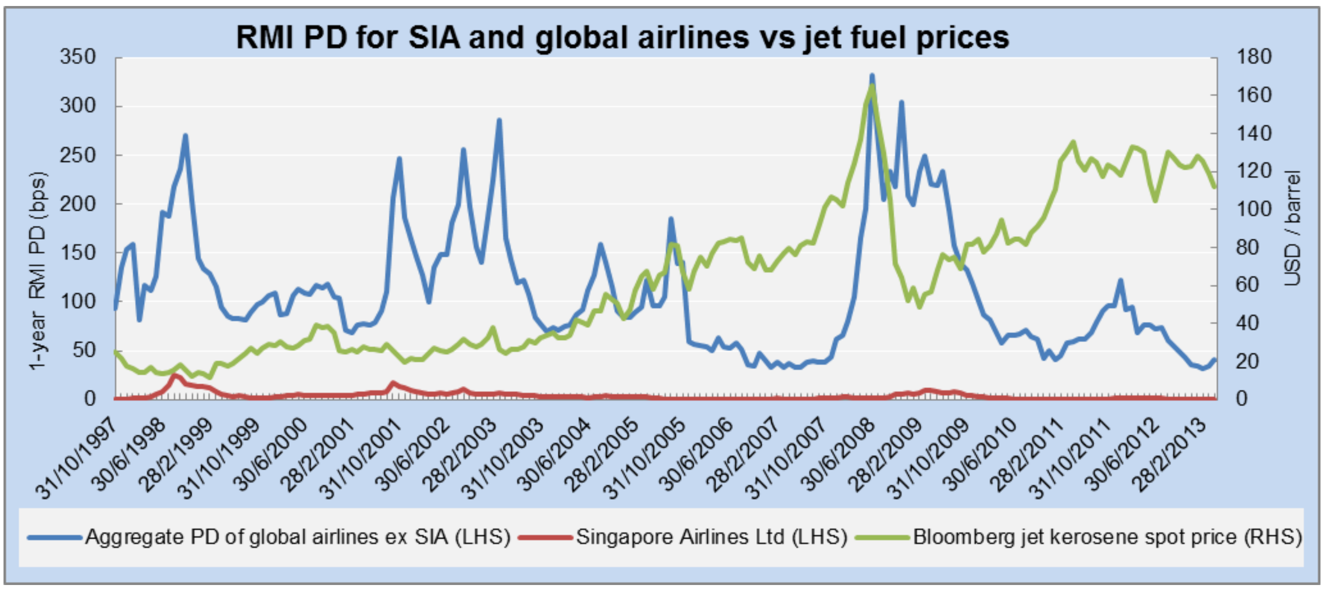
May 14 - May 20 2013

Story of the Week

Singapore Airlines stands out with low default risk

The chart below highlights the 1-year RMI probability of default (RMI PD) for Singapore Airlines (SIA) against the 1-year aggregate RMI PD of global airlines. Last week, SIA reported a 12.8% YoY increase in earnings for its March fiscal year ending 2013. Full year net income rose to SGD 379mn from SGD 336mn a year ago. With a near zero RMI PD of 0.03bps, the carrier is well positioned for any potential slowdown in passenger or freight demand. Based on the latest default parameters calibrated on May 9, a low 3 month SIBOR (Singapore Interbank Offered Rate) rate averaging 0.37% during May and large cash to total asset ratio largely accounted for the firm's low default risk.

The company has been conservative in expending its cash and increasing its level of debt. The latest earnings report showed the carrier held SGD 5bn of cash on its balance sheet bringing its cash and current ratios to 0.98 and 1.35 respectively. Its ratio of debt to EBITDA (earnings before interest, taxes, depreciation and amortization) has remained around 0.54 for the last six quarters. Despite reporting higher profits, the company said passenger yields will probably remain under pressure as forward passenger traffic for the next few months is nearly at the same levels from a year earlier. The airline cited the uncertain global economic outlook and weak demand in Europe and the United States as reasons for the less optimistic forecast. Still, SIA is adding more planes to its fleet and upgrading its business class cabins as competition for the Southeast Asian market heats up.

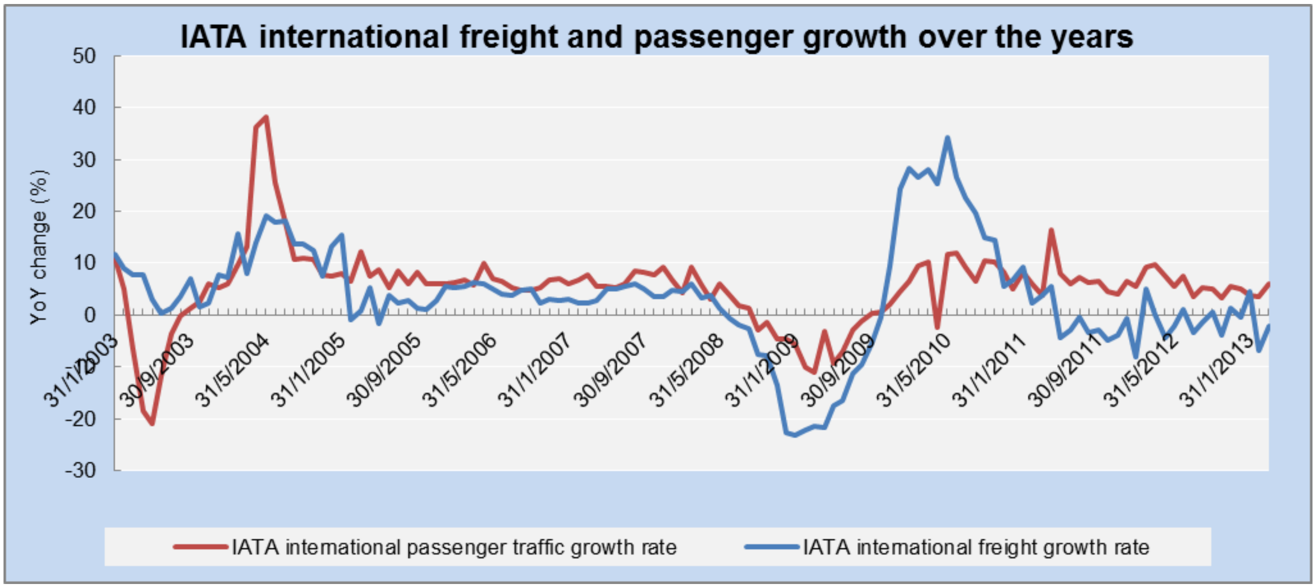


SIA's outlook could be seen as too conservative by many analysts despite a more positive report from the International Air Transport Association (IATA) earlier in the month. According to the association, global airline sector profit is expected to increase to USD 7.5bn in 2013 from USD 4.6bn in 2009. Asia Pacific and West Asia based airlines are also expected to dominate the international passenger market and lead the way in terms of operating margins.

IATA said that the aviation industry has been growing in the last three years despite the economic turmoil around the world. While the North American airline industry consolidates to improve financial strength and capacity utilization, European carriers are busy lobbying for an end to excessive taxation and passenger duties, and Middle Eastern and Asian carriers are capitalizing on both route network growth opportunities and strong passenger demand.

For example, growth in passenger traffic was strongest in the Middle East in March as traffic increased 15.6% YoY, as capacity rose 14.2%, boosting load factor to 79.7%. Middle Eastern carriers have seen an increase in passenger loads over the last 6 months. The airlines account for 13.4% of international air travel, but they have carried about 20% of the increase in worldwide demand between September 2012 and March 2013.

Middle Eastern carriers probably faced a lower impact from rising jet fuel costs, as they spend more on marketing efforts and improving their aircraft fleet to capture more market share in passenger travel. IATA said that the airline industry continues to struggle with increasing fuel costs. Airline spending on jet fuel totaled USD 209bn last year which was USD 33bn higher than in 2011. This year, IATA expects the industry to pay USD 216bn for jet fuel costs. On average, fuel represents 33% of an airline's operating budget. But the impact of fuel costs on the airline's credit risk is not clear as companies tend to hedge their fuel costs through derivatives.



Sources:
Singapore air shares slump after wider operating loss (Bloomberg)
Passenger traffic strongest in Middle East (Arab News)
Rising jet fuel costs weigh on global commercial airlines (International Business Times)
Global airline sector profit will grow to USD 7.5bn in 2013 (Global Travel Industry News)

In the News

Indian firms flock to Singapore debt market

May 20. Indian companies are looking to the Singapore debt market for financing, the most recent being Tata Motors five-year bond offering of SGD 350mn. Indian corporations have found it cheaper and faster to raise funds in the Southeast Asian nation, given the large yield-hungry investor base, particularly the significant number of non-resident Indians (NRI). So far this year, six Indian corporations have sold SGD 1.35bn bonds, making up almost 70 per cent of bond sales by non-Singapore issuers. There were 12 SGD denominated bond issues by non-Singapore companies worth USD 1.6bn so far this year. Of these, six valued at USD 1.1bn were by Indian companies. (Business Times)

Indonesia bonds complete worst week since August on fuel subsidy

May 17. Indonesia's sovereign bonds declined this week, resulting in the 10 year yield's highest rise since last August. The rupiah depreciated against the USD on speculation that the government's lack of progress in cutting fuel subsidies will lead to increased outflows from the country. The gasoline price hike that was announced on April 30 has still yet to take place following unresolved issues with the accompanying compensation package for the poor. The decrease in fuel price subsidies is imperative in addressing the nation's current account deficit. (Bloomberg)

Ratings shopping revived in asset-backed rebound

May 15. Bond issuers have started exploiting credit ratings again by seeking firms that will provide high grades on debt backed by assets considered inappropriate by rivals. Borrowers have had the options to shop for the best rating after U.S. regulators doubled the number of companies sanctioned to assess securities since 2006. The Securities and Exchange Commission plans to limit this by creating a board that selects firms which grade asset-backed bonds, than leaving it to the banks. The Federal Reserve's monetary stimulus and pledge to keep interest rates close to zero has led to investors seeking riskier assets, this in turn has staged a comeback for loan and lease linked bonds. Given the increased supply, tightening regulations may limit the freedom to shop for rating by issuers going forward. (Bloomberg)

Spanish banks face fresh hit from bad loans

May 15. Spanish banks are bracing themselves for tighter rules from the Bank of Spain on lenders to write down the value of their EUR 200bn portfolio of restructured loans to the country's troubled companies and households. This move is likely to further reduce the earnings of Spanish banks, and could potentially expose the capital position of weaker lenders. Spanish banks currently treat more than 40% of all restructured loans as performing normally, even though banks have refinanced close to 14% of their total loan book thus far. (Financial Times)

China banks' bad loans rise for sixth quarter as economy slows

May 15. According to the China Banking Regulatory Commission, non-performing loans in China increased for the sixth consecutive quarter to CNY 526.5bn in Q1 this year. This increase comes on the back of slower economic growth and stronger competition among lenders. Banks may see further higher default rates on loans if the economy continues to slow. Non-performing loans ratios in China rose to 0.96% in Q1, from 0.95% in Q4 last year. (Bloomberg)

Creditors agree to supply liquidity to troubled units of STX Group

May 14. South Korean's troubled shipbuilding conglomerate STX group will be given a loan of KRW 300bn by creditors to help the company repay maturing corporate debts and cover operating costs in return for a stringent corporate restructuring. Previously, creditors had injected KRW 600bn won into STX Offshore & Shipbuilding Co. to help repay maturing bonds and operate normally. (Yonhap News)

Fitch upgrades Greece to B- from CCC, citing fiscal progress

May 14. Fitch Ratings upgraded its credit rating for Greece by one notch last Tuesday, citing progress made in cutting the budget deficit and lowered risk of a euro-zone exit. Although Greece's credit rating still remains in junk territory, the upgrade reflects the country's recent progress in implementing structural reforms and other unpopular austerity measures. Greece is expected to hit fiscal targets required under its bailout plan and could qualify for further debt relief soon. (Reuters)

Slovenia's credit rating cut by Fitch as economy sours (Bloomberg)

Turkey bond yields drop to record on Moody's investment grade (Bloomberg)

European banks warned to expect tougher scrutiny (Financial Times)

UAE economic growth surges to 4.4% (Arab News)

Loans portfolio for Saudi banks exceed SAR 1tn mark (Arab News)

Inflation back in India's comfort zone after 3 years (Gulf News)

Islamic banking needs separate regulations and reporting standard (Gulf News)

Tata Steel reveals USD 1.6bn write down (Financial Times)

Debt ceiling: Treasury starts juggling act (CNN Money)

China on track to overtake US in non-financial corporate debt (Financial Times)

China's main money rate hits 2-month low, shrugs off PBOC liquidity drain (Reuters)

Hong Kong to snap up government offer of inflation-linked bonds (South China Morning Post)

Indonesia state-owned companies plan USD 3.6bn bond sale (Jakarta Globe)

Japan GDP Jumps most in year as consumers open wallets (Bloomberg)

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