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Indian developers stand out with enhanced credit profiles

by Wang Chenye

- **NUS-CRI Agg PD for the Indian property developers improved throughout 2023 thanks to improved investor sentiment, improved economic fundamentals, and an influx of private credit**
- **NUS-CRI Forward PD suggests resilience of the Indian developers in the face of the global macroeconomic headwinds due to robust and sustained housing demand and favorable population demographics**

The ongoing infrastructure investment plan of the Indian government has added fuel to the development of the country's property sector, which in combination with rising demand for new homes, is boosting the country's property market. As India overtakes China to become the world's most populous country with a rapidly growing segment of middle-income households, the growing momentum of the Indian property market over the past year (see Figure 1a) is drawing a growing number of investors and creditors set to enter the market and offer improved access to financing for the country's real estate sector. The credit profile of the Indian developers benefits from the strong government support and broadened credit sources, as indicated by the decreasing NUS-CRI Aggregate (median) 1-year Probability of Default (Agg PD) during 2023, falling below the BBB upper bound when referenced to PDiR2.0 bounds[1]. The favorable economic fundamentals, coupled with an inflow of funds redirected from China's property market, are poised to bring about stability in the credit outlook of the Indian property sector. Resultantly, the NUS-CRI Aggregate (median) Forward 1-year Probability of Default (Forward PD[2]) in Figure 1b stabilizes over the next 12 months.

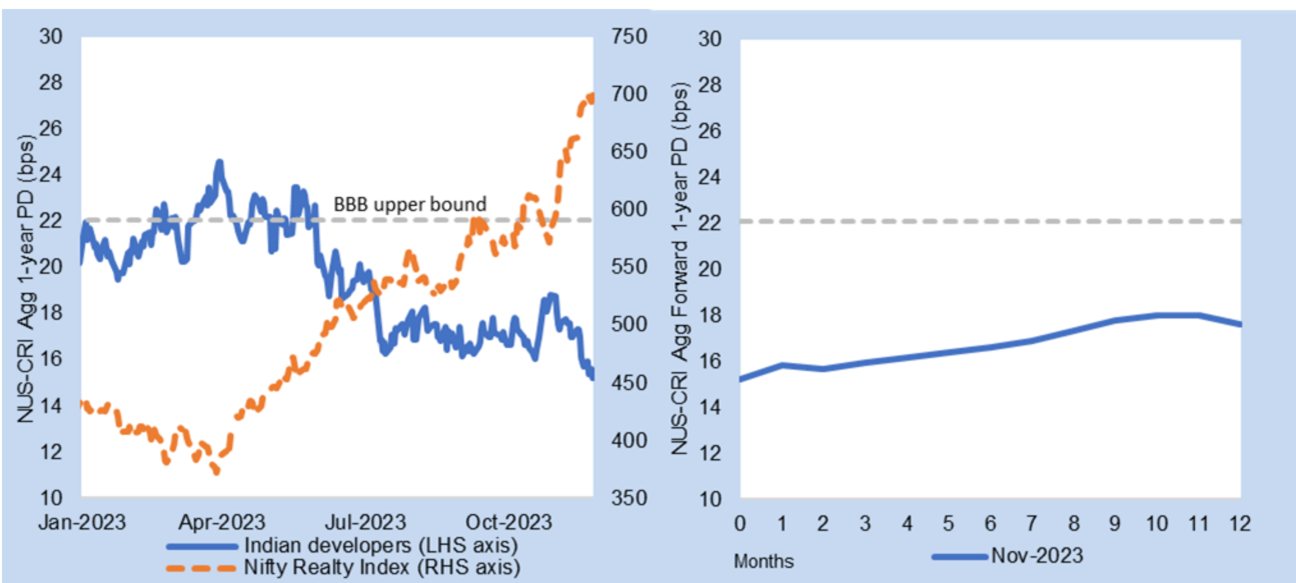

Figure 1a (LHS): NUS-CRI Agg (median) 1-year PD for Indian developers from Jan-2023 to Nov-2023, with reference to PDiR2.0 bounds and the Nifty Realty Index[3]. Figure 1b (RHS): NUS-CRI Forward 1-year PD over the coming 12 months for Indian developers, as of Nov-2023. *Source: NUS-CRI, Bloomberg*

Housing demand in India, particularly for larger homes, experienced an upswing post-pandemic. The increased fiscal spending on infrastructure across the country, encompassing railways, roads, and airports, not only

[1] The Probability of Default implied Rating version 2.0 (PDiR2.0) provides a more familiar interpretation by mapping the NUS-CRI 1-year PDs to the S&P letter grades. The method targets S&P's historical credit rating migration experience exhibited by its global corporate rating pool instead of relying solely on the reported default rates.

[2] The Forward PD estimates the credit risk of a company in a future period, which can be interpreted similar to a forward interest rate. For example, the 6-month Forward 1-year PD is the probability that the firm defaults during the period from 6 months onwards to 18 months, conditional on the firm's survival in the next 6 months.

[3] The Nifty Realty Index comprises a maximum of 10 stocks and is designed to reflect the performance of Indian real estate companies that are primarily engaged in construction of residential and commercial properties.

propels economic development but also improves the livability prospects of numerous areas, thereby driving up the value of land and property. As depicted in Figure 2a, both housing prices and the number of units sold have risen substantially after the COVID-19-induced downturn. While studies indicate that housing prices in India have outpaced the country's GDP growth in recent decades, there remains potential for the real estate market due to favorable demographics to contribute further to the country's growth given its relatively low current contribution to GDP (6%-7%), drawing a parallel to the growth witnessed in China's real estate market and economy prior to the country's deleveraging efforts. As housing prices and transaction volumes continue to rise, the profitability and liquidity of the Indian developers have been improving, thus facilitating their expansion plans, evidenced by the active land acquisitions undertaken by the Indian developers in strategically attractive locations.

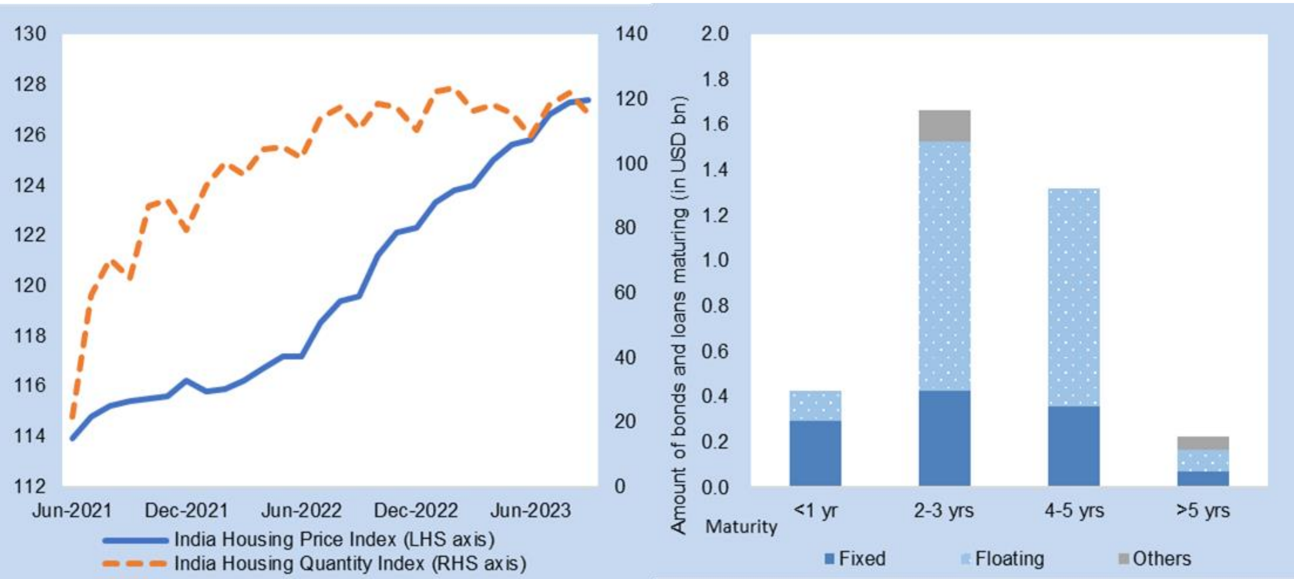

Figure 2a (LHS): Quarterly averages of Indian Housing Price Index and Quantity Index. The "Quantity Index" captures the change in housing units sold over the period 2017–2020, with a baseline value of 100 in Jan-2017. Figure 2b (RHS): Debt maturity distribution of the Indian developers, broken down by coupon types. *Source: SRITNE; Bloomberg*

The sound credit-related fundamentals of Indian developers are underscored by their low levels of indebtedness in the short term. While Indian developers have seen an increase in financial leverage over the past year[4], the leverage level remains lower than that of the Chinese developers[5], whose existing debt surpasses that of Indian developers by over 30 times despite aggressive deleveraging efforts undertaken. As illustrated in Figure 2b, the short-term debt represents a small proportion of the total debt for Indian developers maturing, suggestive of manageable repayment prospects amidst improved liquidity for developers. Additionally, the majority of long-term debts are of the floating-rate variety, reducing refinancing costs as the Reserve Bank of India (RBI) has already paused its rate-hiking campaign and is likely to pivot to a looser stance. Acquiring a boost through improved investor sentiment in the region, Indian developers may be capitalizing on the challenges faced by their Chinese counterparts in the incumbent property market downturn. As Chinese developers experience a record outflow of investment, Indian developers witnessed an inflow of at least USD 2bn in private credit specifically directed towards the real estate sector in India, constituting over half of the total private credit influx in the country in H1 2023. With no substantial debt repayment pressure and an influx of new investments, both the credit profiles and credit outlook of Indian property developers have notably improved.

In the face of global economic challenges, India has demonstrated resilience this year, standing out as one of the few economies with the potential to sustain double-digit growth moving forward. This robust economic performance bodes well for the development and value addition in the real estate sector, thereby favoring developers. Additionally, favorable regulation in the form of affordable housing initiatives in India, with investments exceeding USD 2.5bn since 2013, could further propel demand for new housing. These initiatives aim to provide small loans to both buyers and developers engaged in affordable and environmentally sustainable housing projects. This positive trajectory is evident in the stabilization of the Forward PD, as illustrated in Figure 1b, underscoring the favorable conditions that are expected to benefit the real estate landscape in India.

[4] From a sample median of 1.92 to 2.89, data from Bloomberg.
[5] The sample median stabilizes at around 3.5. Data from Bloomberg.

Credit News

Investors pour cash into US corporate debt in bet Fed rates have peaked

Nov 22. Investors are significantly increasing their investments in U.S. corporate bond funds, showing a heightened interest in riskier assets amid expectations of a peak in interest rates. In the month leading up to November 20, over USD 16bn has been invested in these funds, according to EPFR data, marking the largest net inflow since July 2020. This trend is particularly strong in the "junk" bond sector, where USD 11.4bn has been directed towards funds dealing with these high-yield, low-grade bonds. Additionally, USD 5bn has flowed into investment-grade funds, which involve higher-quality corporate debt. These substantial inflows indicate a growing belief among investors that the cooling of inflation may signal an end to the U.S. Federal Reserve's cycle of interest rate hikes. (FT)

Canada's real-estate market stumbles as rate hikes bite

Nov 24. Canada's real estate sector, previously a robust pillar of its economy, is now experiencing significant challenges. Major real estate developers are defaulting on loans, and difficulties in unit sales are leading to the shelving of numerous condominium projects. This downturn, which could negatively impact the Canadian economy for years, affects both single-family homes and condominiums. A key factor in this decline is the Bank of Canada's rapid interest rate hikes, increasing from 0.25% to 5% in just 16 months. These hikes have raised borrowing costs, including mortgages and developer loans, causing financial strain in the real estate market. (WSJ)

Stressed HK developers lure private credit as funding gap looms

Nov 27. Private credit lenders are targeting Hong Kong's property developers as they face a significant financial crunch with USD 23.4 bn in bank loans due next year. This precarious situation has attracted a variety of investors like family offices, private equity firms, and asset managers, including PACM Group Holdings Ltd., who are ready to offer high-risk loans in one of the world's most expensive real estate markets. Hong Kong's real estate market is currently weak, with reduced revenues from office and retail spaces and increasing finance costs. (Bloomberg)

Commercial property's debt burden exceeds pre-2008 level in eurozone, warns ECB

Nov 21. Sharply higher financing costs, in conjunction with falling property values and weaker rental incomes, are hurting the property markets in the Eurozone. Debt of the Eurozone property sector has soared to levels higher than those during the 2008 financial crisis, posing a challenge to the resilience of banks domiciled in the EU. The commercial property sector constitutes up to 10 per cent of all Eurozone bank loans. Increased stress in the property sector is likely to lead to an amplified impact on banks' balance sheets. The average debt of larger European property companies is above 10x their earnings. Contributing to this downturn is the impact of the ECB's tightening campaign that has raised the cost of financing for commercial real estate properties by 2.6 percentage points. The problem is deeply concentrated in Finland, Ireland and Greece, where more than 90 per cent of loans to property developers are at variable rates or mature over the next 24 months. (FT)

China bank-backed dollar bond sales plunge amid default jitters

Nov 27. Chinese borrowers facing financial difficulties are seeing a decline in funding options, as apprehension about defaults affects a market that depends on semi-guarantees from banks. Sales of China dollar-denominated bonds backed by standby letters of credit, which are promises from lenders to cover repayments if issuers fail, have plunged 90% to USD 1.04bn this year, a stark contrast to last year's figures, according to Bloomberg data. This decrease is more significant than the 52% reduction in overall China dollar bond sales, which totalled USD 52.2bn. (Bloomberg)

Country Garden shares, dollar bonds jump on financing aid hopes (Bloomberg)

Germany to suspend borrowing limits for fourth year after debt brake ruling (FT)

Italy's Geico asks banks for funds with debt standstill near end (Bloomberg)

Regulatory Updates

China's central bank pledges to support domestic demand

Nov 27. The People's Bank of China has announced its commitment to combating systemic economic risks and plans to implement vigorous and precise monetary policies to bolster domestic demand. In its recent quarterly policy report, the central bank outlined its strategic financial direction, emphasizing the use of various monetary tools to maintain adequate liquidity. It intends to enhance the effectiveness of its monetary policy transmission and provide stable financial support to the real economy, with a focus on keeping prices stable. (CNA)

Bank of Italy says risks to financial stability have decreased

Nov 25. The Bank of Italy acknowledges that while financial stability risks remain notable, they have lessened due to improvements in the banking sector. The central bank emphasizes that the government should prioritize fiscal responsibility and implement reforms to foster economic growth. Meloni faces the challenge of managing an economy projected to grow only 0.7% this year, coupled with a high debt level, estimated at 140% of the nation's output. (Bloomberg)

European Commission fines Rabobank EUR 26.6mn over bond trading cartel (FT)

Sri Lanka signals pause after four rate cuts as IMF loan awaited (Bloomberg)

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