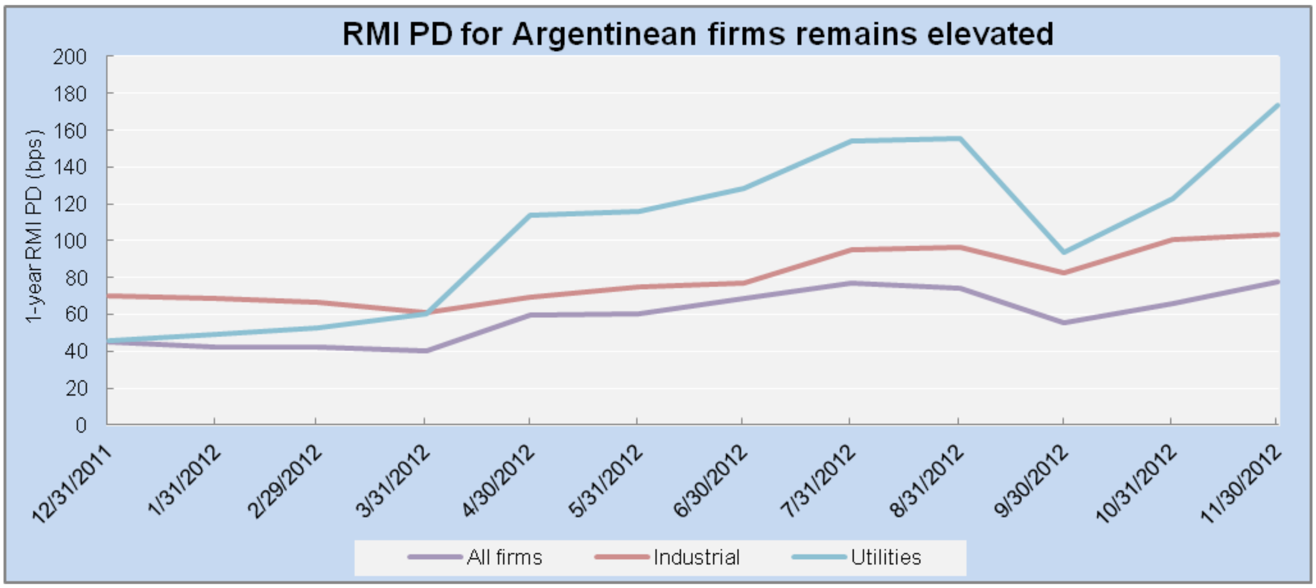
NUS National University of Singapore | RMI Advancing Risk Management for Singapore and Beyond
Weekly Credit Brief
Nov 27 - Dec 03 2012

Story of the Week

The credit outlook for Argentinean firms worsens

The 1-year aggregate RMI probability of default (RMI PD) for Argentinean firms has increased to levels unseen since June 2009. Economic woes along with the possibility of a sovereign default weigh on the credit outlook for domestic firms. Increasing interest rates in interbank markets and volatility in domestic capital markets suggest that corporate financing may have become increasingly difficult. The 90 day ARS deposit rate rose to 15.66% on December 3, from around 12% in mid-2012. The Merval Argentina Index has fallen nearly 20% since the beginning of 2012.

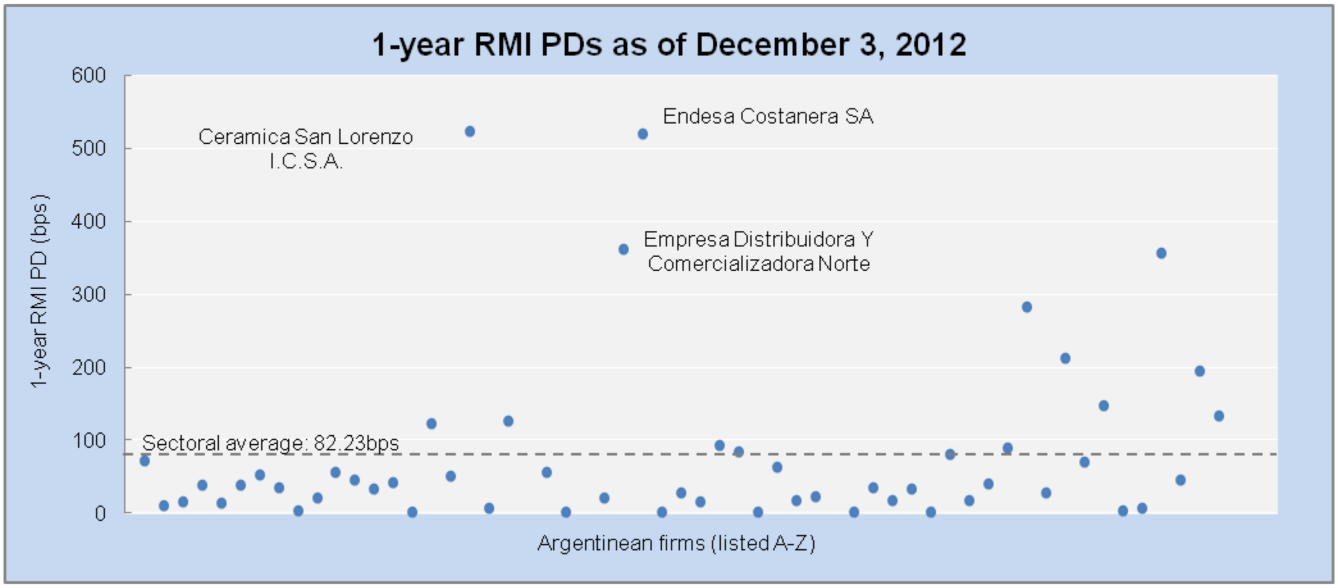


Highest RMI PD in region: The aggregate RMI PD for Argentina is the highest in the Latin American region. The aggregate RMI PD of 80.23bps on December 3 was more than twice the aggregate RMI PD for Brazilian firms (32.08bps) and 3 times the aggregate RMI PD for Chilean companies. Compared to the entire Latin American region, the Argentine aggregate RMI PD is three times higher than the RMI PD average of 29.97bps for Latin America.

Sovereign default & a sluggish economy: The risk of a sovereign default is by far the largest headwind for firms in Argentina. Rising sovereign credit risk directly affects banks via their exposures to government debt. Moreover, a higher chance of a sovereign default makes it harder for Argentine banks to raise USD funding, potentially increasing the cost of domestic corporate borrowing.

A sluggish economy has created earning pressures for Argentinean firms. Industrial production registered declines for six consecutive months between April 2012 and September 2012 while a monthly survey of Argentine household consumer confidence fell to 42.27 in September 2012 from 59.31 a year ago. Lower profits may lead to lower tax revenues, higher sovereign borrowing costs and greater macroeconomic headwinds.

Impact on domestic firms: As displayed in the figure above, utilities and industrials had the highest aggregate RMI PDs on December 3, both of which exceed the average for all Argentinean firms. RMI's PD model currently covers 61 firms in Argentina. On December 3, three of these firms' RMI PDs were at respective historical highs.



High debt levels and negative earnings over the last year weigh upon tile-maker Ceramica San Lorenzo's ability to remain a going concern. Both Endesa Costanera and Empresa Distribuidora Y Comercializadora Norte are utilities with strong links to the Argentine government, which would make them default candidates should the sovereign avoid paying liabilities. Moreover, both the industrial and utilities sectors have come under pressure from rapid depreciation of the ARS against all major currencies, as they have significant foreign currency expenses.

Although the central bank manages the float of the ARS, continuing depreciation of the ARS suggests USD liquidity within the country is drying up. Argentina is in continuing negotiations with its holdout creditors, but prosecutors have urged the US courts to order the country to post a minimum USD 250mn deposit by December 10, increasing the chances of missed coupon payments on international debt.

Sources:
Holdout investors seek deposit from Argentina by December 10 (Reuters)
For Argentina holdout fund, a decade's pursuit may pay off (Reuters)
Don't cry for Argentina, the world's worst sovereign deadbeat (Forbes)

In the News

Cutting UK debt taking longer than hoped: UK Chancellor

Dec 2. UK Chancellor of the Exchequer George Osbourne said it was taking longer than anticipated to fix the country's public finances. A weak economy has made it difficult for the Chancellor to meet budget deficit and debt to GDP targets. A further GBP 11bn of spending cuts may be required in the future. The Chancellor is set to announce the budget for fiscal year beginning April 1, 2013 on December 5. (WSJ)

EU agrees new controls for credit rating agencies, Moody's downgrades bailout funds

Nov 30. The EU agreed on new rules for credit rating agencies (CRAs), which are aimed at reducing reliance on ratings and making it easier for investors to sue CRAs for ratings mistakes. In addition, CRAs will have to schedule dates when they will change sovereign ratings, and will only be able to publish such ratings after close of business in the EU. In related news, Moody's downgraded the credit ratings of the European Stability Mechanism (ESM) and the European Financial Stability Facility (EFSF) to Aa1 from Aaa on November 30, due to Moody's recent downgrade of the French sovereign rating. France is the second largest contributor to the eurozone bailout funds. (Reuters, The Telegraph)

OECD says Euro banks require EUR 400bn in capital, rescued Spanish banks to shrink

Nov 27. The OECD said that large banks in the eurozone need to raise about EUR 400bn in capital to bring their leverage ratios closer to those of their peers. This would allow the banks to meet an OECD recommendation: A minimum 5% ratio of core Tier 1 capital to total assets. This guideline is not part of any regulatory standards. Elsewhere in the eurozone, the restructuring of four Spanish banks was approved by the European Commission, allowing them to receive EUR 37bn in bailout funds. The four banks are expected to reduce their balance sheets by more than 60% by 2017, and concentrate solely on domestic retail banking. (Bloomberg, San Francisco Chronicle)

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