CRISIL

RATINGS ROUNDUP

2002-03

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India's industrial economy has reason to feel optimistic about the next few years according to the CRISIL Ratings Round-Up for 2002-03. For the first time since 1996, upgrades outnumbered downgrades in CRISIL's portfolio of manufacturing companies. Core sectors like steel and key industrial sectors like automobiles led this strong improvement in the manufacturing sector's credit profile. The positive economic impact of the increased investment in the roads sector during the year also contributed to the improvement. Though the current war situation in Iraq has introduced a new uncertainty in the economic environment, it is likely that the continuing investment in the infrastructure sector, especially roads, would provide much needed traction to the Indian industrial economy over the next two years.

The improved credit ratio for CRISIL's long-term ratings in the 12 months ended March 2003 comprised a reduction in the number of downgrades to 19 from 38 in 2001-02 and an increase in the number of upgrades to 14 from 4. This was despite the weakness in the agricultural sector in this year. Therefore, CRISIL expects credit fundamentals to remain strong over the next few years barring another poor monsoon or a global economic downturn following the present Iraq war.

About the CRISIL Ratings Round-Up

The CRISIL Ratings Round-Up is a semi-annual publication that analyses the composition and trajectory of CRISIL's rating actions during a particular period. It also analyses the linkages between these actions and underlying economic trends. This edition analyses CRISIL's rating actions in the financial year 2002-03 and compares them with previous periods. The rating actions are analysed under four broad categories - rating actions, rating stability rates, a trend analysis of credit ratios and their link to macro-economic factors.

Key Conclusions

Credit fundamentals improve, especially in the manufacturing sector

CRISIL's modified credit ratio[1] (MCR) for long-term ratings improved to 0.98 in the current year from 0.85 in FY02. This improvement was most pronounced in the manufacturing sector, which accounted for all the 14 long-term rating upgrades in this year. Moreover, for the first time since 1996, the MCR for the manufacturing sector in FY03 was greater than 1 (meaning more upgrades than downgrades). A revival in core sector industries like steel as well as in other key sectors like automobiles led this strong performance. The increased investment in roads during the year, as part of the ongoing nationwide road development programme, also aided the improved performance.

Improving credit trajectory moving in step with underlying economic fundamentals

(CRISIL's long -term ratings portfolio covers a large number of companies across the manufacturing, financial and infrastructure sectors. In each of these sectors, CRISIL has outstanding ratings on entities across the breadth of these sectors. This makes the credit quality of CRISIL's portfolio a good mirror of systemic credit quality.)

CRISIL's MCR has exhibited a strong correlation with macro-economic indicators such as the growth rates of the index of industrial production (IIP) and gross domestic product (GDP) as well as movements in real interest rates. The improvement in the modified credit ratio in FY03 reflects the improvement in IIP and presages an improved GDP growth rate for FY04. (An independent analysis of macroeconomic fundamentals done by the CRISIL Centre for Economic Research in March 2003 anticipates a GDP growth of about 6.5% in FY04.)

CRISIL's ratings stability maintains improving trend of the past five years - defaults at a new low

The stability of CRISIL's ratings in FY03 was the highest of the last seven years. CRISIL reaffirmed about 81% of all its continuing (non-defaulted) long-term ratings in FY03 against the comparable S&P level of about 74% (based on the global portfolio of ratings on corporate entities) in calendar year 2002. The trend of improving stability of CRISIL ratings over the last four years is validated by a corresponding reduction in the number of defaults in this period. The number of defaults in FY03 at two was the lowest level seen in the last seven years.

Rating actions - salient features

- Downgrades outnumber upgrades in CRISIL's long-term ratings' portfolio (14 upgrades and 19 downgrades) yet again in FY03[2].
- The 19 downgrades comprised two from the 'AAA' category (by one notch), eight from the 'AA' category (seven by one notch and one by two notches) and eight from the 'A' category. Of the eight ratings downgraded from the 'A' category, five remained in the investment grade.
- The 14 upgrades comprised two upgrades from 'D', one from 'C', seven upgrades from 'AA' category and three from the 'A' category.
- Interestingly, the speculative grade saw three upgrades against one downgrade. However, while only one of these three upgraded ratings transitioned to the investment grade (DCW Ltd. from C to BBB), as many as three investment grade ratings transitioned into the speculative grade in FY03 (BPL Ltd., Max India Ltd. and Videocon International Ltd.).
- Of the 33 ratings changes in FY03, 22 were by one notch indicating a low intensity of rating changes.
- Two ratings (Lupin Ltd and Kalyani Steels Ltd.) were upgraded from 'D' and an equal number were downgraded to 'D'; BPL Ltd. and Orient Paper and Industries Ltd.

Stability of CRISIL ratings continues to improve as defaults reduce to a new low

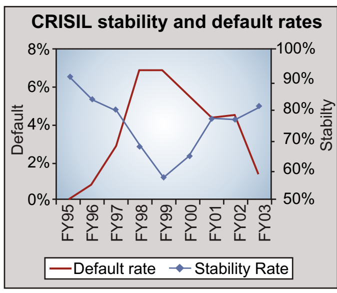
In FY03, within CRISIL's long-term ratings portfolio, there were 228 rating actions on continuing ratings (ratings that were outstanding throughout the

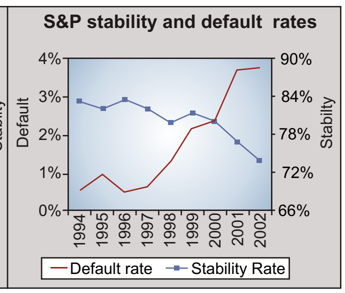
[1] The modified credit ratio (the ratio of [upgrades + reaffirmations] to [downgrades + reaffirmations]) is a good indicator of the performance of CRISIL's portfolio. Given the breadth of CRISIL's portfolio, it is also an effective indicator of systemic credit fundamentals. The modified credit ratio is superior to the conventional credit ratio (upgrades/downgrades) as it tends to be less volatile than the conventional credit ratio in periods when the number of upgrades and downgrades is much smaller than the number of reaffirmations.

[2] The downgrade of BOB Housing Finance, which was first rated during this year, is not included in the computation of credit ratios, as they are based on entities rated as at 31 March, 2002.

year). This comprised 14 upgrades, 18 downgrades and 196 reaffirmations. That translates to a reaffirmation level of about 86% of all rating actions, up from 82% in 2001-02. (If the continuing defaulted ratings in FY03 are excluded from the set of reaffirmed ratings, the reaffirmation level was about 81% as compared to 77% in the previous year). The list of CRISIL's upgrades and downgrades in FY03 is enclosed.

The steady improvement in the stability of CRISIL's long-term ratings is validated by a corresponding fall in the number of defaults on outstanding ratings. In fact, the movement of CRISIL's stability rates has exhibited a near-perfect inverse correlation with the number of defaults, as a percentage of outstanding ratings, over the last eight years. Thus, the new high scaled by CRISIL's stability rates in FY03 was matched by a steep reduction in defaults. Only two of CRISIL's long-term ratings in 2002-03 defaulted, against eight in the previous year - the lowest level since 1995-96.[3] This inverse correlation between stability rates and defaults is also seen in S&P's portfolio as seen below.





The stability of CRISIL's long-term ratings has steadily improved over the last four years and is now comparable to S&P's[4]. This was after a five-year period of rather high rating activity in CRISIL's portfolio caused by the bunching up of the post-1997 industrial slowdown and the structural difficulties faced by India's once booming non-banking finance companies. This caused a very large number of downgrades in the 1996-2000 period. The stability rates in CRISIL's portfolio in FY03 were the highest of any in the last seven years.

	Upgrades		Downgrades		Rating changes / Number of ratings at beginning of year (%)	
	S & P	CRISIL	S & P	CRISIL	S & P	CRISIL
1994-95	196	15	265	4	16.8	9.5
1995-96	278	26	292	15	18.0	16.7
1996-97	304	18	243	47	16.6	21.1
1997-98	329	14	322	95	18.0	32.5
1998-99	305	10	525	126	20.2	42.6
1999-00	264	13	584	82	18.5	35.4
2000-01	310	30	657	30	19.9	23.3
2001-02	270	4	894	38	23.4	23.5
2002-03	264	14	1093	19[5]	26.3	19.0

Source: S&P Research: Corporate defaults peak in 2002 amid record amounts of defaults and declining credit quality-hazards remain

Gradient of category-wise stability rates maintained

CRISIL's long-term ratings portfolio maintained its intended stability gradient across rating scales with ratings in higher categories being more stable than ratings in lower categories. Note, however, that figures for rating categories below 'BBB' are not very robust due to the presence of very few outstanding ratings in these categories.

Further, as seen in the table below, CRISIL's average stability rates are slightly higher than S&P for the 'AAA" category while S&P stability rates are slightly higher for lower rating categories.

1 Year Stability Rates (%)	CRISIL 2002-03 #	S & P 2002-03	CRISIL 11-year average #	S & P 11-year average	S & P 22-year average
AAA	95.9	90.8	95.4	94.5	93.1
AA	90.8	81.9	86.3	88.3	91.1
A	75.0	88.3	82.8	92.6	91.5
BBB	75.0	87.4	75.5	91.0	89.3
BB	100.0	84.2	59.7	84.9	83.2
B	66.7	76.8	53.8	81.7	82.5
C / CCC	33.3	44.3	58.5	51.7	57.0

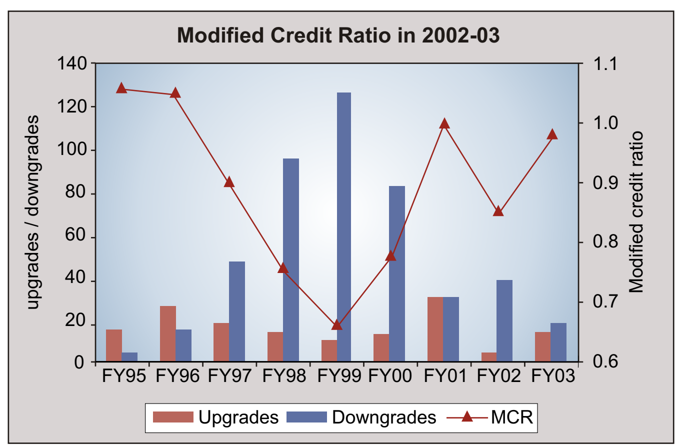
 # To enable consistency with S&P figures, which are on a calendar year basis, CRISIL ratings as on Jan 1 of each year are used to compute stability rates in this table

Source: S&P Research: Corporate defaults peak in 2002 amid record amounts of defaults and declining credit quality - hazards remain

Renewed improvement in CRISIL's modified credit ratio

The trajectory of credit fundamentals, as measured through rating actions, may be seen through two parameters: the credit ratio (ratio of upgrades to downgrades) and the modified credit ratio, defined as the ratio of upgrades plus reaffirmations to downgrades plus reaffirmations. CRISIL favours the use of the latter since it avoids some weaknesses of the simple credit ratio.

CRISIL's modified credit ratio for long-term ratings improved considerably to 0.98 in FY03, from 0.85 in FY02. The improvement in the credit ratio



[3] CRISIL's current stability rates are much better indicators of its rating efficacy than those of 5-6 years ago as the latter did not incorporate the effects of a full business cycle. Increasing polarization of any ratings portfolio tends to have a buoyant effect on stability rates.

[4] For this comparison, stability rates for CRISIL's ratings have been adjusted to eliminate the effect of continuing defaulted ratings. The S&P measures for stability exclude defaulted ratings.

[5] Including 1 downgrade on an entity rated post March 31 2002.

accelerated during the second half of FY03, reaching a level of 1.0, meaning that upgrades equaled downgrades.

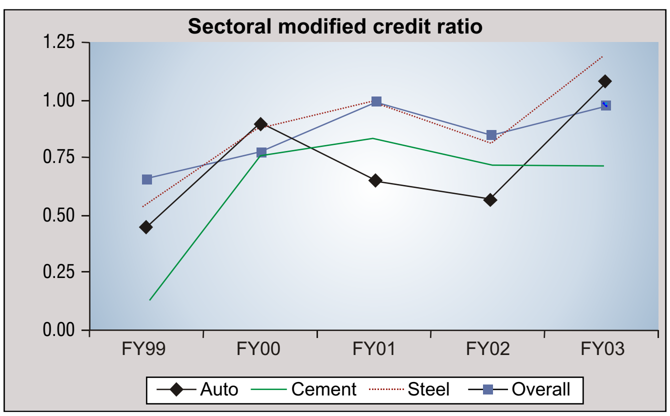
Manufacturing sector sees the strongest credit ratio since 1996 - improvement spread across key sectors

Upgrades outnumbered downgrades in the manufacturing sector for the first time since 1996. In fact, all the upgrades in CRISIL's long-term ratings in this year were in the manufacturing sector. The previous year had 30 downgrades in the manufacturing sector, versus only two upgrades.

Further, the improvement in the credit ratio in FY03 is fairly broad-based across key sectors like steel and automobiles. In fact, the auto sector has registered the strongest credit ratio improvement in FY03. Though the credit ratio for the cement sector did not improve, the sector's performance was supported by better offtake from both the roads and the housing sector. This broad-based improvement augurs well for the sustainability of the improved credit fundamentals seen in FY03.

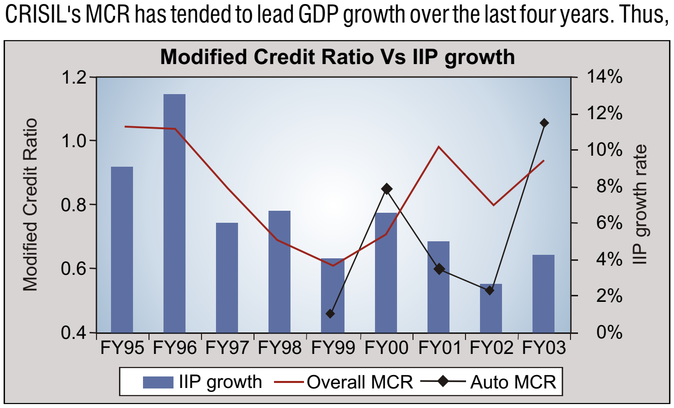
CRISIL's modified credit ratio continues to show a strong correlation with economic trends

Sharp changes in the IIP growth rate have usually coincided with movements in CRISIL's credit ratio. Periods of low and declining IIP growth,



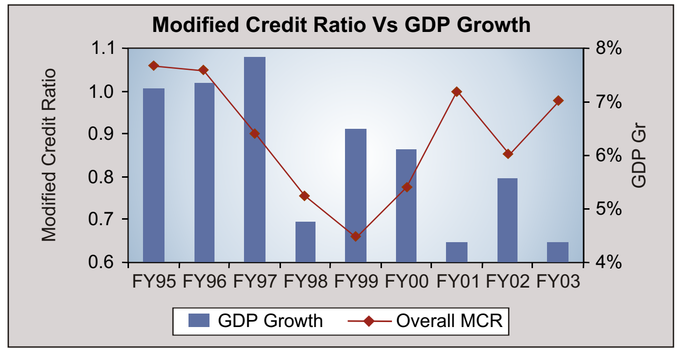
such as those in the late-1990s and between FY99 and FY02, were accompanied by low credit ratios. In keeping with this, the revival of the IIP growth rate in FY03 saw a corresponding improvement in the modified credit ratio to about one. Amongst the sectoral credit ratios, the auto sector displays one of the best correlations with the IIP.

CRISIL's MCR has tended to lead GDP growth over the last four years. Thus,



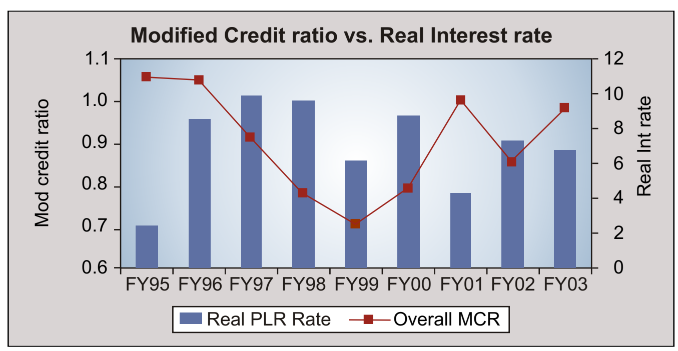
Source: CRISIL Centre for Economic Research, CMIE Review of Indian economy

the strong improvement in MCR in FY01 led the improvement in the GDP growth rate in FY02, with a similar pattern seen in the next year. Therefore, the improvement in credit ratio in FY03 would appear to presage an improvement in GDP growth rate in FY04. An independent analysis of macroeconomic fundamentals done by the CRISIL Centre for Economic Research in March 2003 also predicts an improvement in GDP growth rates in FY04.



Source: CRISIL Centre for Economic Research, CMIE Review of Indian economy

The modified credit ratio tends to display an inverse correlation with interest rates. Real interest rate changes reflect the increasing cost of borrowing for corporates in relation to product prices. The consequent increase in interest outflows immediately affect profitability and interest coverage levels. Thus, high real interest rates between 1995 and 1998 contributed to the decline in credit ratios during that period. The large improvement in the credit ratio in FY03 despite a modest reduction in real interest rates comes from an increase in sub-PLR lending by banks. According to an estimate in the economic survey (2002-03), sub-PLR lending comprises a third of the present bank lending.



Source: Economic Survey 2002-03, Ministry of Finance, GOI, CRISIL Centre for Economic Research

Continuing polarisation in long-term ratings

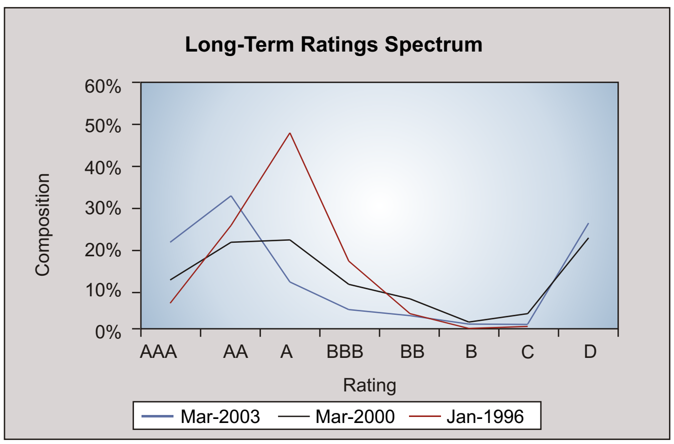
CRISIL's long-term ratings in FY03 continued to exhibit the trend of increasing polarisation that has been seen over the past few years. A comparison of the current portfolio composition with its composition in the beginning of 1996 indicates the extent of this phenomenon. This trend comprises the following components:

- A transition of a large number of erstwhile BBB category and lower ratings to the D category. This was brought about by the underlying process of consolidation in almost all sectors of the industrial sector as the strong companies got stronger and the weak companies were weeded out.

- Non-acceptance of a large number of the ratings assigned in the 'A' or 'BBB' categories by issuers as the above shakeout of sorts made investors reluctant to invest in instruments rated in this category. Thus, the bulk of the new ratings accepted and published over the last few years were in the AA and AAA categories. Of the 37 newly rated entities in the past two years, 27 are rated 'AA' and five are rated 'AAA'.

- A higher rate of withdrawals in the 'A' and 'BBB' rating categories as issuance of new instruments in these categories became difficult even as the old instruments were repaid on schedule. Thus, the withdrawal rate for long-term ratings in the 'A' and 'BBB' categories was 25% in FY03 versus a 10% withdrawal rate for ratings in the 'AA' and 'AAA' categories. This was as compared to the previous year's numbers of 37% for the 'A' and 'BBB' categories and 12% for the 'AA' and 'AAA' categories.

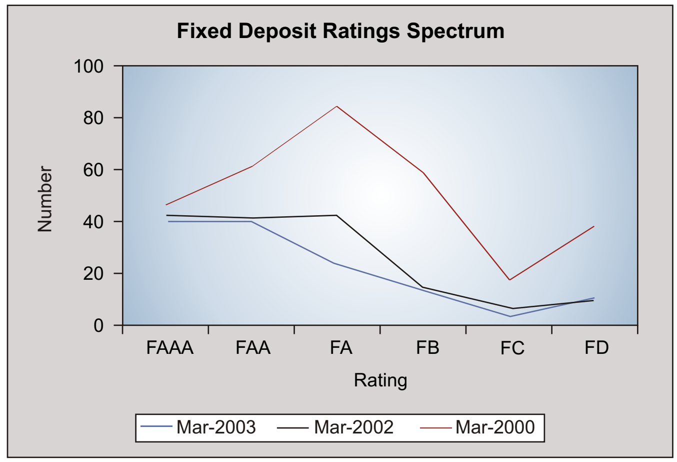
(However, it must be pointed out here that this somewhat blanket rejection of sub-'AA' instruments by investors has caused a pricing anomaly whereby 'A' rated instruments offer better risk adjusted returns than instruments rated in the higher rating categories. A detailed analysis of this phenomenon is presented in the CRISIL article " 'A' rated papers provide higher risk-adjusted yields"[6])



The above trend of polarization has caused the proportion of 'AA' and 'AAA' rated entities in CRISIL's long-term ratings' portfolio at the end of March 2003 to increase to 54% as compared to about 50% a year ago and 33% three years ago. On the other hand the proportion of 'D' ratings has increased to about 26% as at end FY03 from about 22% a year prior to this.

Fixed deposit ratings emulate long-term portfolio even as the instrument continues to lose its appeal

CRISIL's fixed deposit (FD) portfolio, by and large, mirrored the trends in CRISIL's long-term ratings' portfolio discussed above. The FD portfolio also witnessed an improved stability in FY03 with eight upgrades, nine downgrades and 110 reaffirmations. This represents a stability rate of about 87% as compared to the previous year's level of about 84%. Also, the modified credit ratio in FY03 improved to 0.96 over the previous year's level of 0.89 (four upgrades, 20 downgrades and 124 reaffirmations).



FDs have been steadily losing their appeal among issuers. Consequently, CRISIL's FD portfolio has displayed a secular decline in the number of rated entities across all rating categories. A possible cause is the fact that in a falling nominal interest rate scenario, the higher cost of raising FDs for non-bank companies tends to form a larger portion of the total cost of borrowings rendering this instrument less attractive. During the past year, 25 FD ratings were withdrawn while the previous year's number of withdrawals stood at 37. On the other hand, this two-year period saw just seven new FD ratings. (This was against 37 new ratings in CRISIL's long-term ratings portfolio.) Thus, the number of outstanding CRISIL FD ratings fell from 185 as at end FY01 to 153 as at end FY02 and 130 by end Fy03.

[6] *The article was published in the June 2002 issue of CRISIL RatingScan and is available on request from CRISIL*

Changes in CRISIL's long-term ratings portfolio in 2002-03

UPGRADES

Sl No	Company	Industry	Sector	From	To
1	Apollo Tyres Ltd.	Manufacturing	Tyres	A+	AA-
2	Brakes India Ltd	Manufacturing	Auto Ancillaries	AA-	AA
3	DCM Shriram Consolidated Ltd.	Manufacturing	Diversified	A-	A
4	DCW Limited	Manufacturing	Chemicals-Inorganic	C	BBB
5	Eimco Elecon (India) Ltd.	Manufacturing	Engineering	A+	AA-
6	Finolex Industries Ltd.	Manufacturing	Engineering	AA-	AA
7	Gabriel India Ltd.	Manufacturing	Auto Ancillaries	BBB-	BBB+
8	Indian Farmers Fertiliser Co-operative Ltd.	Manufacturing	Fertilisers	AA	AA+
9	Indian Petrochemicals Corporation Ltd.	Manufacturing	Petrochemicals	AA-	AA
10	Kalyani Steels Ltd.	Manufacturing	Steel & Steel products	D	BB
11	Lupin Ltd. (formerly Lupin Laboratories Ltd.)	Manufacturing	Drugs & Pharmaceuticals	D	BB+
12	Paper Products Ltd., The	Manufacturing	Packaging	AA-	AA
13	Tata Engineering & Locomotive Company Ltd.	Manufacturing	Automobiles - 3&4 wheelers	AA-	AA
14	Tata SSL Ltd.	Manufacturing	Steel & Steel products	AA-	AA+

DOWNGRADES

Sl No	Company	Industry	Sector	From	To
1	Atlas Cycle (Haryana) Ltd (formerly Atlas Cycle Industries Ltd.)	Manufacturing	Cycle & Cycle components	A+	BBB
2	Bank of Baroda	Finance	Bank	AAA	AA+
3	BOB Housing Finance Ltd.	Finance	Housing Finance	AA+	AA
4	BPL Ltd.	Manufacturing	Consumer Durables	A-	D
5	Escorts Ltd	Manufacturing	Automobiles- 3 & 4 Wheelers	A	BBB
6	Excel Industries Ltd.	Manufacturing	Pesticides & Agrochemicals	A+	A
7	Ford Credit Kotak Mahindra Ltd	Finance	NBFC	AA-	A+
8	Housing and Urban Development Corporation Ltd.	Finance	Financial Institution	AA	AA-
9	Kotak Mahindra Primus Ltd	Finance	NBFC	AA	AA-
10	Lafarge India Ltd.	Manufacturing	Cement	AA	AA-
11	Madras Cements Limited	Manufacturing	Cement	AA	AA-
12	Max India Ltd.	Manufacturing	Diversified	A	BB
13	Orient Paper & Industries Ltd.	Manufacturing	Diversified	C	D
14	Perfect Circle India Ltd. (formerly Perfect Circle Victor Ltd.)	Manufacturing	Auto-Ancillaries	A	A-
15	Sterlite Industries (India) Ltd.	Manufacturing	Metals	AA	AA-
16	Takshila Educational Society	Infrastructure	Educational Institution	AA	A+
17	Tata Power Company Ltd.	Infrastructure	Power	AAA	AA+
18	Thirumalai Chemicals Ltd.	Manufacturing	Petrochemicals	A-	BBB+
19	Videocon International Ltd.	Manufacturing	Consumer Durables	A	BB

Appendix I

Changes in CRISIL's Fixed Deposit Ratings portfolio in 2002-03

UPGRADES

Sl No	Company	Industry	Sector	From	To
1	Cent Bank Home Finance Ltd.	Finance	Housing Finance	FA+	FAA-
2	Corpbank Homes Ltd.	Finance	Housing Finance	FA+	FAAA
3	Indian Petrochemicals Corporation Ltd.	Manufacturing	Petrochemicals	FAA	FAA+
4	PNB Housing Finance Ltd.	Finance	Housing Finance	FAA-	FAA+
5	Tamil Nadu Newsprint and Papers Limited	Manufacturing	Paper & Paper Products	FAA	FAA+
6	Venkateshwara Hatcheries Ltd	Manufacturing	Hatcheries	FA	FA+
7	Venky's (India) Ltd.	Manufacturing	Hatcheries	FA+	FAA-
8	Vibank Housing Finance Ltd.	Finance	Housing Finance	FA	FAA

DOWNGRADES

Sl No	Company	Industry	Sector	From	To
1	Amtrex Hitachi Appliances Ltd.	Manufacturing	Airconditioner	FA+	FB+
2	BPL Ltd	Manufacturing	Consumer Durable	FA	FD
3	EIH Ltd.	Manufacturing	Hotels	FAAA	FAA
4	Excel Industries Ltd.	Manufacturing	Pesticides & Agrochemicals	FAA-	FA+
5	Escorts Finance Ltd.	Finance	NBFC	FA-	FB+
6	Housing and Urban Development Corporation Ltd.	Finance	Housing Finance	FAA+	FAA
7	Kotak Mahindra Primus Ltd	Finance	NBFC	FAA+	FAA
8	Madras Cements Ltd.	Manufacturing	Cement	FAA+	FAA
9	Pearl Polymers Ltd.	Manufacturing	Polymer	FB	FC

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