



FY 2015-16

# CRISIL Ratings Round-up



Debt downgraded in 2015-16 at an all-time high of Rs 3.8 trillion  
Firms rated higher by CRISIL continue to witness low-intensity rating actions



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## Executive summary

Debt of firms<sup>1</sup> downgraded by CRISIL in 2015-16 has risen to an all-time high of Rs 3.8 trillion, underscoring credit quality pressures continue to mount for India Inc. More than half of this debt belonged to firms in the metal sector, which were hit by falling realisation and high debt. And the second-biggest chunk of about a quarter belonged to the infrastructure sector.

In the second half of 2015-16, the debt-weighted credit ratio – or the quantum of debt of firms upgraded versus downgraded – stood at 0.2, the lowest in the last three years. Also, the credit ratio – or rating upgrades to downgrades – stood at 0.76.

Debt under stress at infrastructure and metal-linked firms is at a record level because there hasn't been any meaningful deleveraging of balance sheets, and metal prices continue to be low. On the other hand, sectors with strong domestic consumption linkages such as auto ancillaries, or with inelastic export demand such as pharmaceuticals, had relatively robust credit quality metrics.

Almost half of the upgrades were driven by business-related factors such as high operating efficiency. This was reflected in the median RoCE<sup>2</sup> of upgraded firms, which stood at 16% or twice that of downgraded firms. Downgraded firms, meanwhile, were hobbled by high indebtedness and stretched liquidity. The median debt/EBITDA of downgraded firms was 4.6 times, or twice that of the upgraded ones.

The intensity of CRISIL's rating actions in category 'CRISIL A' and above continued to be low. During the second half of 2015-16, there were 99 rating actions by CRISIL in these categories of which nearly 95% were one-notch<sup>3</sup> changes. The few multi-notch downgrades were because of the sharp deterioration in the external environment. Overall, CRISIL's portfolio was remarkably stable despite the choppy waters. The two multi-notch rating upgrades were because of a revision in CRISIL's criteria for factoring in parent or group support.

CRISIL does not expect a sharp improvement in credit quality in the near term. Indebted firms in the investment and metal-linked sectors will continue to face considerable headwinds, while consumption-linked firms with low leverage will see some uptick in credit quality.

And the debt-weighted credit ratio will continue to languish below 1, which is expected to reflect in likely increase in weak assets of banks. The ratio can turnaround only if there is substantial deleveraging of stressed balance sheets through sale of non-core assets, or a sharp reversal in metal prices.

A broad-based improvement in credit quality will depend on pick-up in investment demand, favourable monsoon and the government's ability to continue to push reforms.

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<sup>1</sup> Excluding financial sector players

<sup>2</sup> RoCE = Return on capital employed, EBITDA = Earnings before interest, tax, depreciation and amortisation

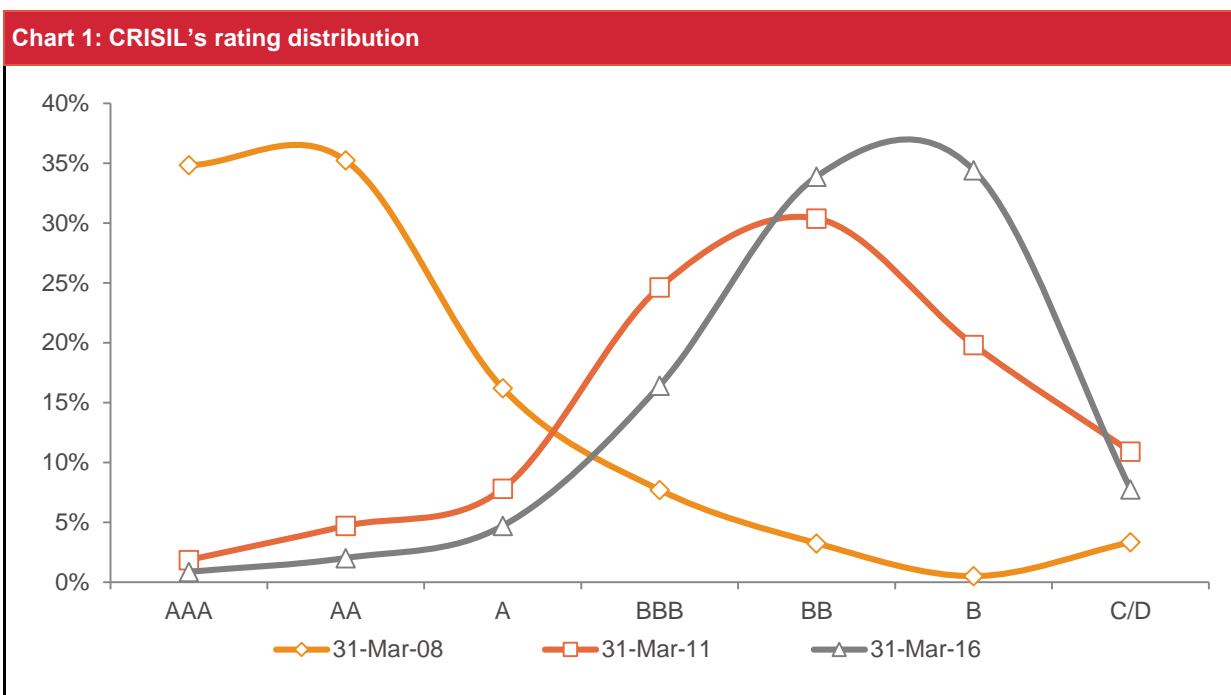
<sup>3</sup> Excludes ratings placed on 'Rating Watch'. This is used to convey to investors that the rating is being monitored for certain critical events and that additional information is awaited. This helps reduce the possibility of any surprise for the investors.

## About CRISIL's Ratings Round-Up

CRISIL's Ratings Round-Up is a semi-annual publication that analyses CRISIL's rating actions and traces linkages between the actions and the underlying economic trends and business factors. A credit rating is an opinion on the likelihood of timely debt repayment. Therefore, an analysis of rating actions in a large and diverse portfolio of rated firms is an apt indicator of economic prospects. This edition analyses CRISIL's rating actions in the six months ended March 31, 2016.

## CRISIL's portfolio of outstanding ratings has stabilised

CRISIL's portfolio of outstanding ratings has stabilised – ratings on 14,252 firms were outstanding as on March 31, 2016. More than three-fourths of them are rated 'CRISIL BB' or lower. The median rating has remained at 'CRISIL BB' in the four-and-a-half years ended March 31, 2016 -- down from 'CRISIL AA' on March 31, 2008 (*Chart 1*).



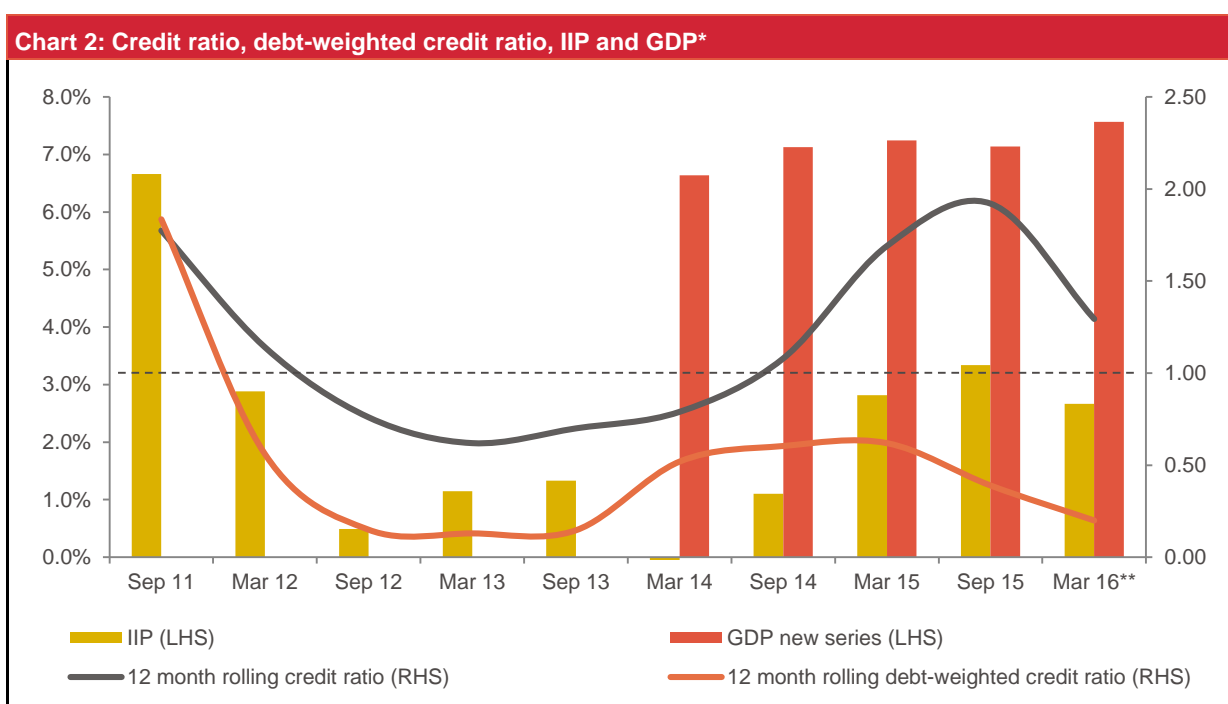
Source: CRISIL



## Credit quality pressures mount – debt-weighted credit ratio slips further

CRISIL's debt-weighted credit ratio, which reflects trends in credit quality of corporate India, slipped further to 0.20 in the second half of 2015-16 from 0.27 in the first half, driven by macro-economic headwinds. In the second half, despite steady growth in GDP, the Index of Industrial Production indicated a slowdown. This, combined with global factors such as sluggish demand, deceleration in China and depressed commodities adversely impacted credit quality. The credit ratio, which stood at 0.76 in the second half compared with 2.13 in the first half, and anaemic debt-weighted credit ratio, are reflective of the systemic stress.

The decline in credit quality metrics (*Chart 2*) shows up even on a 12-month rolling basis, which typically normalises seasonality in rating actions. Both the credit ratio and the debt-weighted credit ratio have declined for the 12 months ended March 31, 2016, compared with a similar timeframe that ended September 30, 2015.



Source: CRISIL

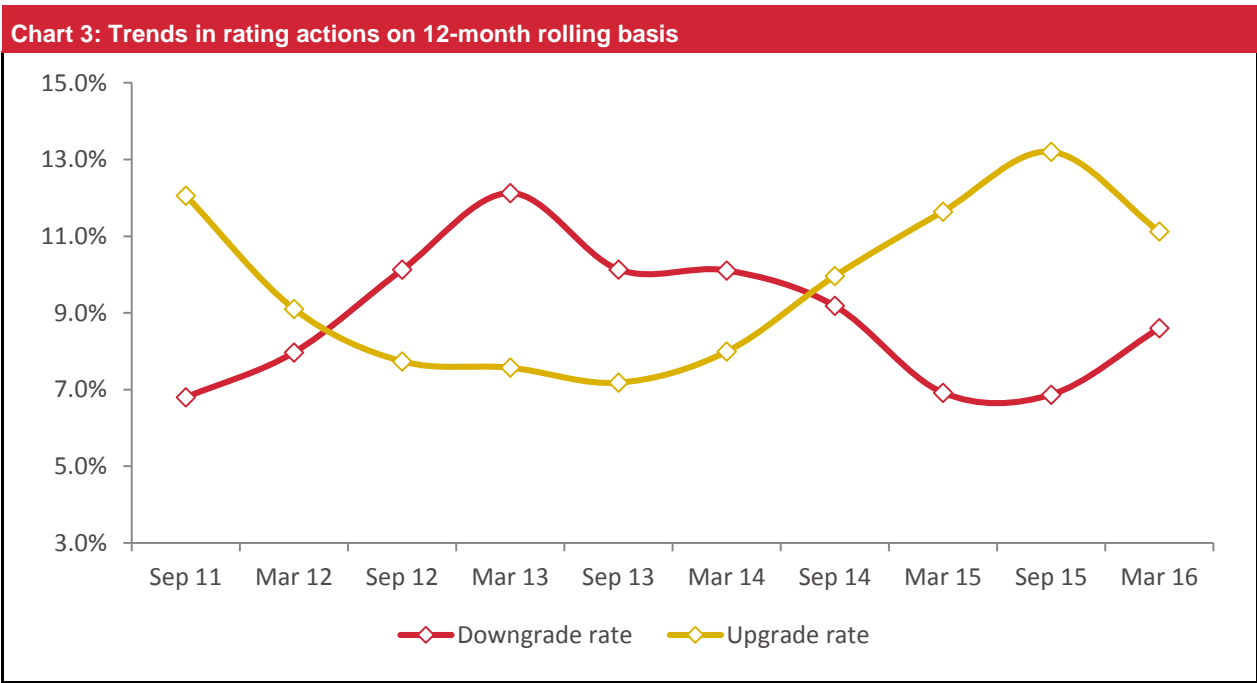
\* GDP and IIP growth numbers are on 12 month rolling basis

\*\*GDP numbers for the 12 months ended March 2016 are based on CRISIL's estimates, and for IIP are based on Apr 2015 to January 2016 period

### Downgrade rate surges, upgrade rate plummets in the second half

CRISIL upgraded ratings on 1,521 firms and downgraded 1,177 firms during 2015-16. In the second half of the year, the numbers stood at 575 and 755, respectively. The upgrade rate has fallen sharply to 11.1% for the 12 months ended March 31, 2016, after touching a high of 13.2% in a similar timeframe ended September 30, 2015. On the other hand, the downgrade rate accelerated from 6.9% in the 12 months ended September 30, 2015, to 8.6% in a similar timeframe ended March 31, 2016 on subdued demand and the commodity complex meltdown. More than a third of the downgrades were to default category, and most of the firms defaulting were from 'CRISIL BB' or lower rating categories.

Credit quality deteriorated in the metal and investment-linked sectors, which remain beset by low capacity utilisation (and inventory pile-up), fall in realisation and high leverage. Moreover, the decline in upgrade rate was due to further delay in the investment cycle and sluggishness in global demand, which together will prolong the agony for exporters. However, interest rate cuts and steady private consumption supported an uptick in the credit quality of consumer-facing firms.



Source: CRISIL



## Most rating actions in high rating categories continue to be of low intensity

The expectation of investors from the higher rating categories ('A' and above) is high stability rates – i.e., rating actions should be gradual and wherever possible, outlook-driven. Sharp rating actions are undesirable because they leave investors in the lurch and they are unable to manage their exposure. CRISIL's portfolio of 1,031 firms in these categories witnessed 99 rating actions – 39 upgrades and 60 downgrades. All but six<sup>4</sup> were of low intensity, where the rating change was just one notch. Only two firms in CRISIL A and above rating categories were upgraded by two notches -- primarily due to CRISIL revising its criteria for factoring parent or group support.

Four firms were downgraded by more than one notch:

- One because of the steep fall in steel prices
- Another -- an agro-chemicals manufacturer – by two notches because of information risk. The management had become non-cooperative which meant limited access to information that impacts credit quality. So CRISIL took a rating view based on publicly available information
- Two banks through negative outlook due to severe asset quality pressures

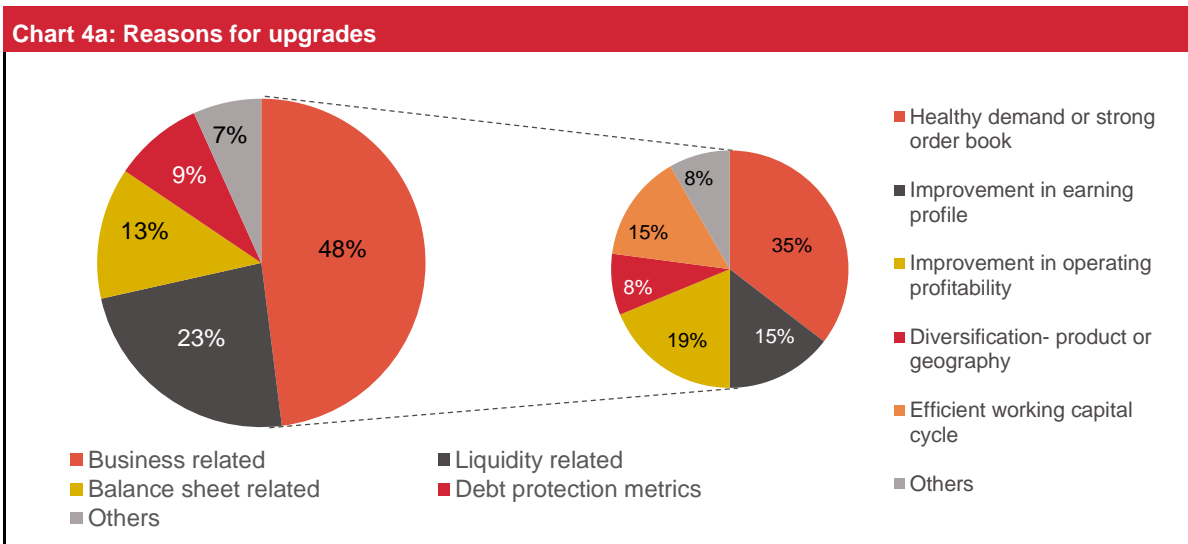
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<sup>4</sup> Excludes ratings placed on 'Rating Watch'. This is used to convey to investors that the rating is being monitored for certain critical events and that additional information is awaited. This helps reduce the possibility of any surprise for the investors.

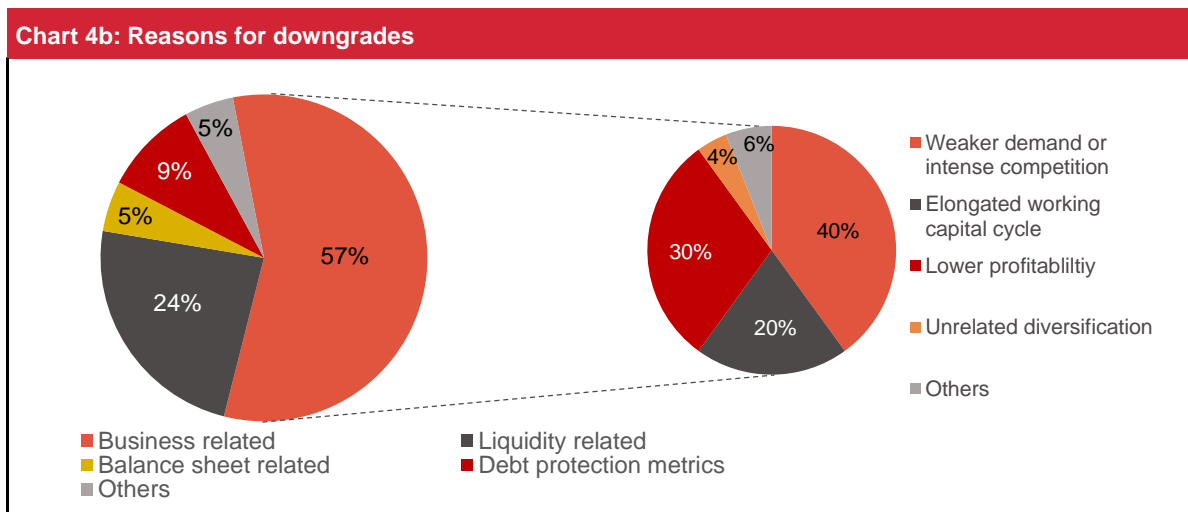


## Operating efficiency and liquidity drove upgrades, sluggish demand spurred downgrades

An analysis of CRISIL’s rating actions for the second half of 2015-16 shows that 45% of the upgrades were driven by improvement in the financial risk profile -- such as better debt protection metrics, higher cash accrual and improved liquidity. Business-related factors such as more orders, improved operating margin and efficient working capital management were responsible for about half of the upgrades (*Chart 4a*). More than two-thirds of the companies upgraded for business reasons belonged to consumption-linked sectors such as agricultural products, textiles and automotive retail.

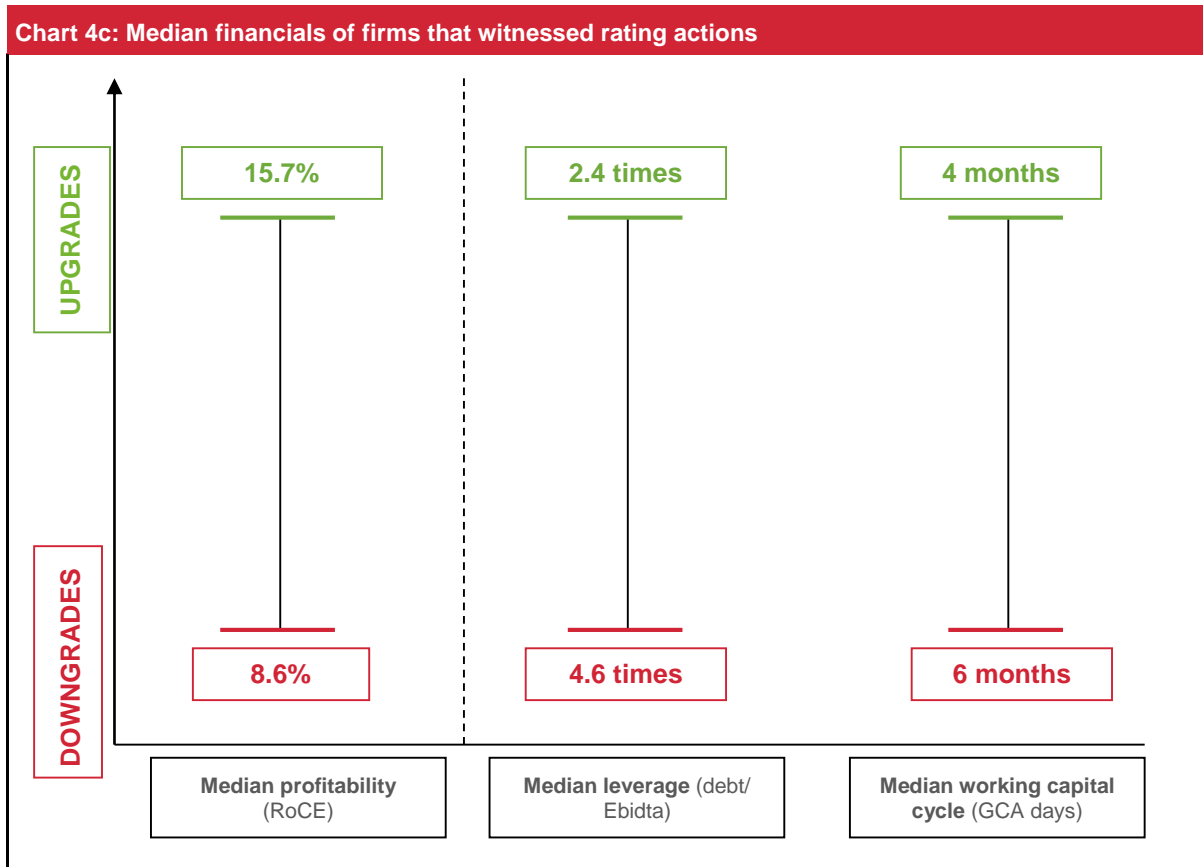


By contrast, subdued demand, intense competition and diminishing profitability accounted for 40% of the downgrades (*Chart 4b*). Another 40% of the downgrades were attributable to deteriorating financial performance including weak liquidity, lower cash accrual and high leverage. Steel, electric utilities and industrial machinery were the major infrastructure-linked sectors witnessing downgrades due to business reasons such as weak demand and lower profitability.





In the second half of 2015-16, firms upgraded had a distinctly better profile compared with those downgraded. Upgraded firms, in general, had higher profitability, lower indebtedness and managed their working capital prudently. This is illustrated by wide gap between median of these parameters for upgraded firms and downgraded firms (*Chart 4c*).



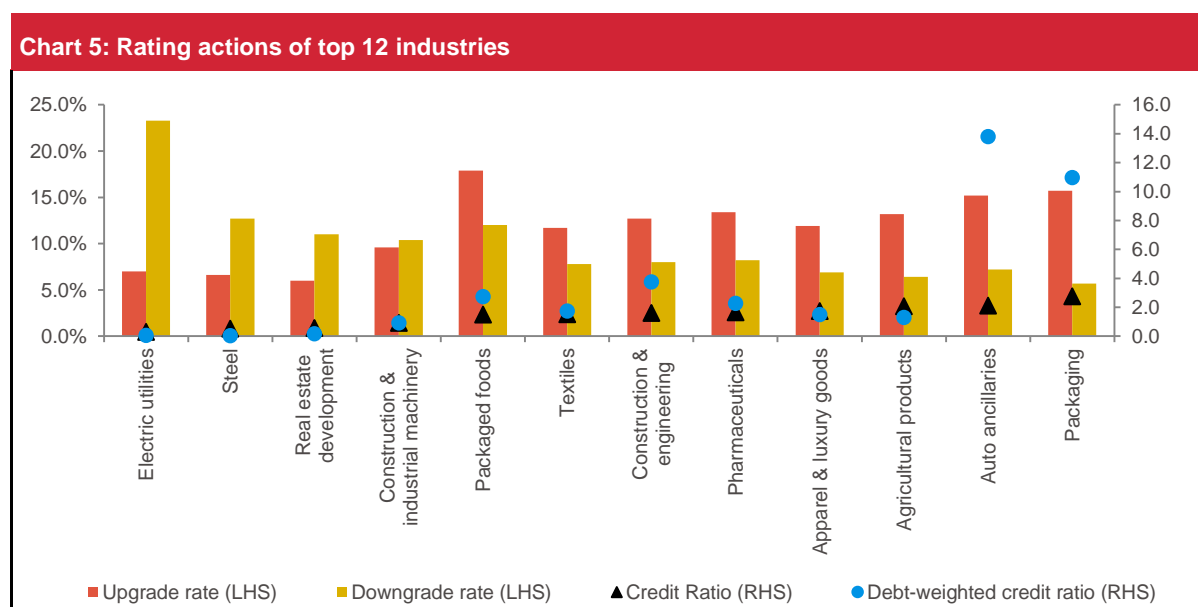
Source: CRISIL

## Debt in the books of downgraded firms peak

CRISIL-rated firms which witnessed downgrades during 2015-16 had cumulative debt of Rs 3.8 trillion. That's the most debt downgraded since CRISIL began ratings in 1987 – and way above the Rs 3.3 trillion seen in 2012-13, the previous peak.

But credit quality pressures were not uniform across sectors. These were harsh for sectors facing commodity headwinds or demand pressure, and mild for those with domestic consumption linkages or inelastic export demand (*Chart 5*).

This is illustrated in the chart below:



Source: CRISIL

Downgrades of firms in the metal sector were on the back of steep fall in realisation due to sluggish global demand. Competition, especially from imports, added to their woes. The metals sector contributed more than half of the downgraded debt.

A quarter of the downgraded debt resided in the books of infrastructure linked firms. These firms were plagued by weak investment demand, which led to inadequate capacity utilisation. Due to high levels of indebtedness in these firms, their financial risk profile was adversely impacted.

In the real estate sector, for every one upgrades, there were two downgrades in 2015-16. A chunk of the downgrades were attributable to poor demand of the last three years. Delays in approvals and other bottlenecks, along with inventory pile-up, exacerbated the woes of realtors.

On the other hand, sectors with strong domestic consumption linkages such as auto ancillaries had relatively robust credit quality metrics. That's because of better operating efficiencies and increase in sales on the back of new launches and a pick-up in the medium and heavy commercial vehicles segment. Operating profitability of OEMs improved as input costs plunged, while higher sales volume in some segments led to healthy cash generation.

## Systemic credit growth inches up, seen staying course in 2016-17

While the Reserve Bank of India (RBI) has reduced its policy rate by 125 basis points (bps) since January 2015, base rates of banks fell only 60 bps. And mounting asset quality pressure, especially at public sector banks, spawned lending caution. Nonetheless, lower interest rates did lead to slightly better credit growth of 11.3% as on March 18, 2016. While corporate loan off-take remained sluggish, credit demand from the retail and service sectors improved.

Money raised through commercial papers surged 55% year-on-year in February as better-rated corporates accessed the bond and money markets.

CRISIL believes bank credit growth, expected to be 11-12% in 2015-16, will rise to 12-14% in 2016-17 for three reasons. First is that the Union Budget was non-inflationary, which gives the RBI the elbow room to further cut its policy rate. Second, monetary transmission will improve going forward because of the adoption of the 'marginal cost of lending rate' methodology by banks to calculate their base rate. Third, consumption and public investment-driven would boost lending to the retail, public sector and small-scale enterprises segments.

**Table 1: Trends in industrial activity and fund mobilisation**

Quarter ended	Sep-13	Dec-13	Mar-14	Jun-14	Sep-14	Dec-14	Mar-15	Jun-15	Sep-15	Dec-15	Mar-16
Bank credit growth (%)	17.8	14.5	14.6	13.1	10.6	10.5	10.2	9.3	9.6	11.1	11.3*
Repo rate (%)	7.50	7.75	8.00	8.00	8.00	8.00	7.50	7.25	6.75	6.75	6.75
Credit spreads (%) #	0.9	0.5	0.6	0.4	0.4	0.4	0.4	0.5	0.4	0.4	0.6@
ECB mobilised (USD billion)	9.4	8.7	9.6	6.5	4.2	6.9	7.5	6.3	5.5	8.3	1.4@@
Equity mobilised (Rs billion)	120.1	249.1	400.3	210.5	143.2	117.5	193.0	312.3	165.6	624.6	103.8@
IIP growth (% YoY)	1.9	-0.8	-0.4	4.6	1.3	2.0	3.3	3.3	4.8	1.6	NA
GDP growth (% YoY)^	7.7	6.0	6.7	7.5	8.3	6.6	6.7	7.6	7.7	7.3	7.7^^

\*Updated as on March 18, 2016

#AAA spread over 10 year G-Sec

@ Updated in February 2016

@@ Updated in January 2016

^ As per new GDP series

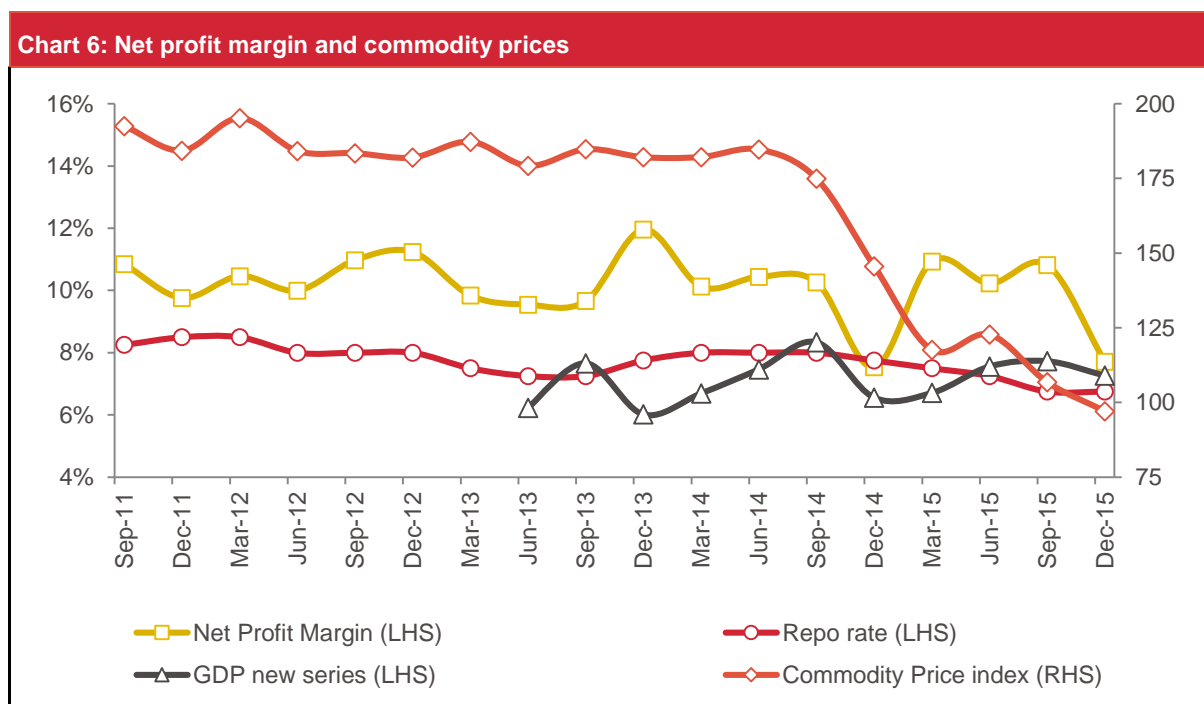
^^ As per CRISIL's estimates

Source: CRISIL

## Corporate profitability in doldrums

CRISIL's analysis of the financial performance of 407<sup>5</sup> firms in the S&P CNX 500 index shows net profit margin (NPM) fell sharply to 7.7% in the third quarter of 2015-16 because of the aforementioned issues at investment and commodity-linked firms. Also, commodity-linked firms faced inventory losses in the third quarter, which impacted profitability.

However, the topline performance of India Inc (excluding oil marketing companies and financial services firms) seems to have bottomed out and there are incipient signs of broad-based demand recovery. As a result, growth in 2016-17 is expected to be faster. This, along with improved capacity utilisation, softer input prices and lower interest rates, is expected to ease the pressure on corporate profitability. Demand off-take in auto ancillaries, FMCG, pharmaceutical and retail firms will underpin this improvement.



Source: CRISIL

<sup>5</sup> These listed companies have reported results for the quarter ended December 31, 2015, and have remained in the S&P CNX 500 for the past 16 quarters. Three oil marketing companies have been excluded because their reported numbers would have skewed the sample. Companies from the financial sector have also been excluded.



## Exports expected to pick up from a shrunk base

The World Trade Organisation has predicted global trade will grow at 3.9% in calendar 2016, well below the 7% seen during the pre-global financial crisis period. While one reason for this is the commodity complex meltdown, subdued global growth was also behind the trade sluggishness. Barring the United States and the United Arab Emirates, which account for a quarter of India's exports, growth prospects in most other destinations remain fragile. *Table 2* shows growth rates for India's prominent trade partners.

Not surprisingly, exports from India contracted in 2015-16. Merchandise exports, which constitute two-thirds of India's total exports, have been declining since April 2015, cumulatively falling about 18% in the first nine months of 2015-16.

After witnessing a contraction, exports are expected to pick up mildly in 2016-17, as India's trade partners expect mild improvement in their own growth rates. However, downside risks abound. A sharper-than-expected slowdown in China will exaggerate the trade imbalance and hurt metals and commodity-based sectors. And divergent monetary policies across the globe will increase volatility in capital flows and exchange rates.

**Table 2: GDP growth rates**

Countries	2014	2015	2016(P)	2017(P)
Eurozone	0.9	1.5	1.8	1.7
UK	2.9	2.2	2.4	2.2
US	2.4	2.4	2.7	2.6
China	7.3	6.9	6.3	6.1

Source: Standard & Poor's

## Banking sector: Asset quality challenges far from over

In light of the asset quality review (AQR) undertaken by the RBI, more stressed assets were recognised by banks, which increased non-performing assets (NPAs). CRISIL foresees another ~Rs 2.1 lakh crore of corporate stressed assets (from the top 100 exposures of all banks) becoming NPAs by the end of 2016-17.

Regulatory suasion has meant increased recognition of stressed assets by banks. This is narrowing the gap between reported NPAs and weak assets. Given increased slippages, CRISIL expects overall slippages in the banking system to remain high at 4.1% -- or Rs 3.3 lakh crore -- for 2016-17, and gross NPAs to increase to 7.7% -- or Rs 7 lakh crore.

The spike in provisioning will offset profits of public sector banks and will be equal to pre-provisioning profit both in 2015-16 and 2016-17. Provisions as a proportion of total assets will touch a high of 1.6% in 2015-16, and will remain at elevated levels in 2016-17 because of continued high level of slippages, ageing of NPAs and fresh provisioning towards strategic debt restructuring, or SDR, accounts. Further, net interest margin (NIM) will be under pressure due to loss of interest from accounts slipping into NPAs, the impact of implementation of the Ujwal Discom Assurance Yojana – or UDAY -- scheme for discoms leading to lower yields, and implementation of the marginal cost lending rate mechanism. These factors are expected to lower NIM by 10 bps.

These asset quality pressures will manifest in higher capital requirement for public sector banks. Only 10 out of 26 are expected to have some capital cushion over the regulatory minimum by the end of 2016-17, compared with 25 out of 26 at the end of 2014-15. The banking system will require Rs 3.4 lakh crore till 2018-19 with public sector banks requiring the lion's share of Rs 2.6 lakh crore.

**Table 3: Weak assets matrix**

Year ended	Mar-13	Mar-14	Mar-15	Mar-16 (E)	Mar-17 (P)
Gross NPAs (as a percentage of gross advances)	3.3%	3.8%	4.3%	6.8%	7.7%
RSA (as a percentage of gross advances)	5.0%	5.3%	5.7%	4.3%	2.7%
Weak assets <sup>6</sup> (as a percentage of gross advances)	4.3%	5.1%	6.2%	8.5%	8.9%
Gross advances (Rs lakh crore)	59.7	68.7	75.3	81.5	90.9

<sup>6</sup> According to CRISIL's definition, weak assets include reported gross NPAs + 40% of restructured standard assets (excluding those of state power utilities) + 75% of security receipts + 15% of loans structured under 5/25 scheme (as per which banks will be encouraged to extend long term loans to infrastructure sector with flexible structuring to absorb potential adverse contingencies)



## Key reasons for rating action and credit quality outlook for key sectors

Industry	Key reasons for rating action in the second half of 2015-16	Outlook for the medium term
<b>Pharmaceuticals</b>	<p>Upgrades were driven by strong revenue growth, diversity in revenue profile and steady profitability</p> <p>Downgrades were mainly of mid-size players and driven by intense competition and export challenges. Five out of twelve downgrades in this sector were to the default category.</p>	<p>Growth drivers, especially from developed markets, continue to hold. This will help exports to grow steadily. However, increased regulatory scrutiny will be a constraint for some. Emerging markets, despite currency devaluation in the near term, are expected to grow at a steady pace in the medium term, backed by increase in demand for low-cost medicines. On the domestic front, sales growth is expected to remain healthy because of the availability of chronic care drugs and price revision flexibility for products under National List of Essential Medicines. We expect domestic demand to grow at a higher pace of about 13% as against export demand of about 10%.</p> <p>Notwithstanding regulatory and currency headwinds, large makers of formulations are expected to see operating margins of 24-25% because of growth in the US. Increasing R&amp;D expenditure and compliance costs will curb significant improvement in profitability. Small and mid-sized makers of formulations may witness greater improvement on the back of increased product and geographic diversification. For bulk drug manufacturers, pressure on profitability continues due to commoditisation of active pharmaceutical ingredients and competition from China. However, these manufacturers gain from lower raw material prices, and are rationalising their portfolio to target high value, low volume products. This will help them sustain their operating margins.</p>



Industry	Key reasons for rating action in the second half of 2015-16	Outlook for the medium term
<b>Agricultural products</b>	<p>Three-fourths of upgrades could be attributed to business factors such as enhanced sales due to better demand or diversification, increase in operating efficiency and higher profitability.</p> <p>Downgrades were because of subdued demand and lower operating margins.</p>	<p>India's rice exports will remain flat in 2015 at about 10 million tonne due to lower offtake of basmati rice by Iran, coupled with extreme weather events impacting production. Thailand will remain the top rice exporter for the second consecutive year, with India coming second. Based on April-November 2015 export data, India's basmati rice export volume was up 23%. However, realisations were down 18% in dollar terms because of falling paddy prices. In 2015-16, paddy prices continued to be subdued (after beginning to fall drastically in September 2014) due to high inventories. CRISIL expects credit risk profiles of basmati rice exporters to show moderate to high stress. New export permits have been issued by Iran in December 2015 so Indian basmati exporters can expect realisations to stabilise over the medium term.</p>
<b>Textiles</b>	<p>More than two-thirds of upgrades were for business reasons such as revenue growth, higher profitability and better operating efficiency. Upgrades were driven by relatively stable domestic demand. Textile firms upgraded largely belonged to ready-made garments (for which demand has picked up in the UAE and Japan), yarn processing, and man-made fibre sectors.</p> <p>Downgrades were mostly of yarn manufacturers due to lower-than-expected profitability stemming from lower realisations. More than a third of the downgrades were to the default category.</p>	<p>Ready-made garment manufacturers are likely to witness sluggish growth over the medium term. The outlook for exporters will remain muted in the range of 4-5% with moderate recovery in the European Union and low growth in the non-traditional markets. Currency fluctuations and lower export competitiveness (compared with Bangladesh and Vietnam) would result in rangebound profitability.</p> <p>However, an uptick in domestic sales volume is expected, supported by improved economic activity. While realisations are expected to be flat, lower raw material prices will provide cushion to profitability.</p> <p>Demand for cotton yarn is expected to be sluggish, growing just 3-4% in 2016-17 because of muted yarn exports and moderation in derived demand. Hence, consumption will be driven by relatively stable domestic demand. Operating profitability is expected to remain stable with prudent inventory holding policies. Capacity additions by standalone yarn manufacturers would be muted due to sluggish demand and capacity overhang.</p>
<b>Automotive components</b>	<p>Upgrades were majorly on account of better demand from OEMs and global customers, combined with cost optimisation efforts, leading to higher cash accrual. New launches and pick-</p>	<p>Automotive component players are expected to see 8-10% revenue growth in 2016-17 compared with 5-7% in 2015-16. This will be driven by higher offtake from OEMs and steady replacement (after-market) demand, even as exports are expected to</p>



Industry	Key reasons for rating action in the second half of 2015-16	Outlook for the medium term
	<p>up in the commercial vehicles segment and prudent working capital management led to improvement in financial risk profiles, which drove upgrades.</p> <p>Continued weak demand from specific customer segments resulted in profitability pressures and sub-par liquidity, and consequent downgrades in the sector. Downgraded firms had high leverage; the median debt/EBITDA of downgraded firms was 3.9 times as compared to 1.8 times for upgraded firms.</p>	<p>pick up gradually. Sales growth to domestic OEMs will be supported by continued fleet replacement in the medium and heavy commercial vehicle segment and higher offtake in the passenger vehicle and scooters segments as urban consumer sentiment improves and new models are launched. Motorcycle and passenger vehicle sales will also benefit from increased rural incomes and payouts under the Seventh Pay Commission and One-Rank-One-Pension recommendations.</p> <p>Exports will benefit from growth in European passenger and commercial vehicle sales, slower pace of decline in the US truck sales and increasing penetration in south-east Asia. Further, stricter domestic regulations on safety and emission standards would give a fillip to growth rates of players focusing on relevant product categories such as engine components and brake parts in the medium-to-long term. Suppliers to passenger vehicle and two-wheeler OEMs, which are operating at high capacity utilisation rates, will undertake capex towards the second half of 2016-17 to meet the incremental demand. Profitability of component suppliers improved by 50-100 bps in 2015-16, and the improvement is expected to be sustained during 2016-17 as well. Credit metrics are expected at adequate levels in 2015-16, and witness some moderation in 2016-17, with borrowings expected to increase for capex.</p>
<b>Packaged foods</b>	<p>More than three-fourths of upgrades were attributable to business reasons such as better demand, higher profitability, and improvement in operating efficiency.</p> <p>Stretched liquidity and deterioration in financial risk profile led to most of the downgrades.</p>	<p>India's beef exports in 2015-16 are expected to witness degrowth in terms of revenue, in line with CRISIL's expectations. As per the Agricultural and Processed Foods Exports Development Authority, export of buffalo meat during April-December 2015 declined by 10% compared to the corresponding period of 2014. The key reason for the decline in shipment is a sharp fall in the Brazilian currency against the US dollar, which made India's export uncompetitive. India had overtaken Brazil as the largest exporter of beef in the world in 2014. CRISIL expects the revenue of Indian beef exporters to be lower by 8-10% in 2015-16. Their credit risk profiles may be stable depending on their ability to manage working capital cycle through better operating efficiencies and market expansion initiatives.</p>

Industry	Key reasons for rating action in the second half of 2015-16	Outlook for the medium term
Steel	<p>The primary reason for upgrades was prudent working capital management and higher capacity utilisation. Upgrades were mostly of firms with healthy balance sheets stemming from low debt levels.</p> <p>Downgrades resulted from steep fall in realisations due to sluggish global demand leading to lower revenue and profitability. Highly leveraged firms were under greater pressure than smaller ones.</p>	<p>Global steel demand continues to stay tepid on account of slowdown in China. Demand slowdown in China may be prolonged as there is a structural shift from high steel intensity investment driven demand to low steel intensity consumption driven demand. Large overcapacities in China, lower input costs and strong competitive pressures from Russia and China, are expected to keep steel prices low. In this grim scenario, domestic demand may provide some respite. Government impetus on construction, favorable automobile and consumer durable sales are expected to support growth of 4-5% in domestic demand, as against 0.5-1% for global. The government has recently introduced minimum import price (MIP) for 173 steel products out of the total 500 type of steel products, which will protect domestic steel producers from influx of low cost steel imports while the impact on realisations will remain contingent on extent of channel inventory and demand pick up in the near term.</p> <p>Despite supportive domestic demand, and introduction of MIP for steel, the domestic steel players are expected to clock moderate utilization rates. This is on account of bunching up of new capacities, and stiffer competition in export markets. Moderate utilization rates coupled with pricing pressures will keep profitability subdued. Moreover, large steel makers are characterized by elevated debt levels resulting in severe pressure on their debt protection metrics. The impact will be more pronounced for players with mining linkages, as well as small and mid-sized players for whom primary steel acts as a raw material where costs might increase due to imposition of MIP.</p>
Construction	<p>Upgrades were majorly driven by enhanced liquidity, and efficient working capital management. Upgraded firms had median working capital cycle of 5 months against 9 months for downgraded firms. Prudent project tendering led to improvement in business risk profiles and increase in operational efficiencies.</p>	<p>The government is taking steps to ramp up investments in the construction sector. Penning guidelines such as ensuring 80% land acquisition before a project is awarded, premium re-scheduling and ease of exit are expected to once again kindle interest in road sector. While awarding of projects by the National Highways Authority of India increased 45%, execution picked up by 40% between April 2015 and Jan 2016. This momentum is expected to sustain in 2016-17 too. Railways is expected to be another key area where the government will push investment through the creation of freight corridors, adding new lines and electrifying tracks.</p>



Industry	Key reasons for rating action in the second half of 2015-16	Outlook for the medium term
	<p>More than half of the downgrades were driven due to sluggish demand and grim investment scenarios. Also, the debt-weighted credit ratio for the sector was below 1 time.</p>	<p>Investments in irrigation are also expected to grow moderately, primarily due to spends from eastern states, Madhya Pradesh and Gujarat, and also from Andhra Pradesh and Telangana.</p> <p>Under Atal Mission for Rejuvenation and Urban Transformation, urban infrastructure including water supply and sanitation systems, metro rails and smart cities will also provide a fillip.</p> <p>With the investment environment improving, companies have a scope for monetisation of non-core developmental assets thereby creating financial flexibility for future growth.</p>
<b>Real estate</b>	<p>Upgrades were due to demand pick-up in commercial realty on the back of growth in IT/ITES and e commerce.</p> <p>Around half the downgrades were to the default category, which is attributable to liquidity crunch and project-related issues. A large real estate group was downgraded because additional debt contracted weakened its capital structure.</p>	<p>The residential real estate sector has been facing headwinds for the last few years, due to overall slowdown in the domestic economic scenario, coupled with weak demand and bearish consumer sentiments. After 4 years of continued decline, demand is expected to recover marginally in the medium term, driven largely by upcoming infrastructure projects or commercial drivers.</p> <p>Average capital values across the top 10 cities are also expected to remain range-bound in 2016 and 2017. Prices in all cities barring Hyderabad are currently well above their 2008 peaks, so there is very little headroom for any appreciable rise in prices in the next two years in the prevailing macro-economic environment.</p> <p>In commercial real estate sector, vacancy levels have reduced on the back of limited additional supply and increasing absorption over the last couple of years. This trend is expected to continue driven by healthy demand from IT/ITES and growth of e-commerce in the year ahead</p> <p>The Union Budget 2016-17 did provide some positives, especially for the affordable housing segment and clarification on dividend tax for REIT. While affordable housing is expected to have a larger impact in tier II and tier III cities where an average residential unit is priced below Rs 50 lakhs, REIT take off will benefit developers having a sizeable commercial portfolio.</p>
<b>Packaging</b>	<p>More than 70% of the upgrades in the segment are attributable to improvement in business risk profiles – healthy topline or bottomline growth, diversification, and stabilisation of capacity.</p>	<p>Revenues of the Indian packaging industry, estimated to be over \$ 30 billion in 2015-16, are poised to grow at 13-15% annually over the medium term backed by ever-increasing demand from segments such as FMCG, pharmaceuticals, processed foods and beverages, personal healthcare and beauty products. Rising</p>

Industry	Key reasons for rating action in the second half of 2015-16	Outlook for the medium term
	<p>More than half of the downgrades were to the default category mainly on account of weakened liquidity.</p>	<p>disposable incomes, urbanisation, changing tastes and preferences, and favourable demographics will not just keep improving penetration of existing products but will also keep attracting multinationals into pushing new launches.</p> <p>Profitability, particularly in the flexible packaging segment, has benefited and will continue to benefit from low crude oil prices leading to lower raw material costs. For the sector overall, profitability will continue to be supported by increasing capacity utilisation and shorter conversion cycle negating the need to maintain large inventories. This will offer a cushion against volatile raw material prices and optimise working capital requirement.</p>
<p><b>Non-banking financial companies</b></p>	<p>Half of the upgrades were on account of an expected turnaround in the commercial vehicle cycle, resulting in improvement in asset quality.</p> <p>A third of the upgrades were driven by business growth and profitability, while maintaining asset quality.</p> <p>No downgrades were witnessed in the sector.</p>	<p>The performance of retail-financing NBFCs is expected to improve gradually in line with macroeconomic recovery supported by expectation of a normal monsoon. Retail NBFCs' assets under management are estimated to have grown by around 17% in 2015-16 and CRISIL expects 18-20% growth in 2016-17. The commercial vehicle cycle has bottomed out with medium and heavy commercial vehicles segment registering good growth in 2015-16. Growth in other segments such as used-vehicle financing, SME financing, loans against property (LAP), and consumer loans (personal and durables) will continue at a steady clip.</p> <p>Asset quality performance has begun to show signs of stabilisation after deteriorating sharply over the past few years, primarily driven by the vehicle financing segment. However, NBFCs engaged in LAP are seeing headwinds arising from intensifying competition and increased risks in the portfolio. While the overall asset quality is expected to improve gradually, the extent of improvement may not be reflected in reported gross NPAs due to transition to stringent asset classification norms. The overall reported gross NPAs for retail-financing NBFCs are likely to be 4-4.5% as on March 31, 2016, and will increase as NBFCs transition to 120+ days past due (dpd) recognition by March 31, 2017.</p> <p>The profitability of retail financing NBFCs, as reflected by return on managed assets (RoMA) is expected to remain around 1.7-1.9% in 2015-16,</p>



Industry	Key reasons for rating action in the second half of 2015-16	Outlook for the medium term
		<p>supported by higher net interest margins. But this will be offset by elevated credit costs. RoMA is expected to improve slightly in 2016-17 to around 1.8-2% helped by expectation of higher margins from lower borrowing costs. The improvement in RoMA will, however, be offset by increase in provisioning due to tighter NPA recognition norms.</p> <p>NBFCs are augmenting their capital base to support future growth. Larger NBFCs have raised around Rs 35 billion in 2014-15, and Rs 23 billion in the first half of 2015-16. CRISIL believes that the credit risk profiles of NBFCs will remain resilient, supported by healthy capitalisation, which provides a cushion against asset-side risks.</p>

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