RATING AGENCIES & THEIR ROLE IN THE CAPITAL MARKET SPACE
Presentation by ICRA

An Associate of Moody’s Investors Service
Scheme of Presentation

- Introduction to ICRA
- Role of Credit Rating Agencies, Rating Process and Approach
About ICRA

- ICRA commenced rating services in 1991
- Services Offered
  - Credit Ratings
  - Grading Services
- Covers all major Sectors
  - Manufacturing companies covering the entire gamut of Indian industry Oil & Gas, Power, Telecom, Textiles, Steel, Cement, Pharmaceuticals, Paper, Fertilizer, Auto and auto ancillaries, Chemicals, Sugar, Tea, Paper, Hotel, Construction, Real Estate, Gems & Jewellery etc.
  - Financial sector covering banks, financial institutions, Insurance, NBFC, primary dealers, housing finance companies, brokerage houses etc
  - Project Finance including infrastructure
  - Structured finance including asset backed securities (Auto, CV), Mortgage backed securities (Housing loans - fixed and floating rate), Collateralised debt obligation, Partial guarantee, Future flow transaction etc
- ICRA has done 4500+ assignments, covering 2000+ companies in various sectors such as entire manufacturing, financial, project finance including infrastructure and structured finance
ICRA's Shareholding Pattern

- Moody’s holds around 29%, Moody’s provides high-value technical services, access to global research base
- Listed Since 2007, Around 32% held by Indian Banks and Insurance companies, SBI being the largest at 10%; around 22% held by Indian Public
Role of CRA

- Credit information intermediary
- Independent fundamental credit analysis
- Combine finance and sector experience
- Cash flow focused
- Not an auditor
Role of Credit Ratings

• Credit Ratings allow investors to take an informed decision. Establishes Risk to Reward environment

• Enables issuers to tap broader investor base

• Development of Bond Market to facilitate channelizing long term funds to sectors such as infrastructure
What is an ICRA rating?

• An ICRA rating is an independent opinion on the future ability and willingness of an issuer to make timely payments on its financial commitments.
• It is normally assigned to a specific debt instrument.
Rating Process

- Request from issuers
- Evaluation by a team of analysts
- Independent rating committee
- Acceptance/Non acceptance
- Request for a review
- Surveillance of accepted ratings
- Credit watch
Rating Approach

- Prospective
  - Tenure specific
- Focus on
  - Downside
  - Stability - Sustainability - Predictability
- Qualitative & Quantitative
- Interactive & Use of Judgement
Analytical Basics

MANAGEMENT

Influences

BUSINESS RISK

Determines

FINANCIAL RISK
Business Risk Assessment

• Industry characteristics and outlook
  – Growth prospects
  – Competitive intensity
  – Regulatory risks
  – Capital intensity

• Issuers competitive position
  – Operating efficiency
  – Market strengths

• Scale and risks of new projects
Financial Risk Assessment

• Existing financial position
  – Trends in margins and RoCE
  – Leveraging
  – Liquidity position

• Currency and interest rate risks

• Financial flexibility
  – Undrawn limits
  – Liquid investments
  – Group strength
Management Evaluation

• Plans and strategies
  – Risk appetite
  – Approach to growth

• Group companies
  – Performance
  – Transactions

• Corporate Governance concerns
The analysis is complemented with Future Cash Flow Adequacy

- Estimates over 3-5 years
- Simulations for range of scenarios
- Key drivers
  - growth
  - selling prices
  - input costs
  - capital requirements - Fixed & WC
  - currency values
Putting it all together

Operating Revenues
less Operating Costs
less working capital adjustments
= Cash from operations
less interest
less dividend
less normal capex
= free cash flows
less debt repayments
= Net retained Cash flows
less project capex
plus external funding
= net surplus/deficit

Business Volumes
- Industry growth
- Market share
Realisations
- Industry Structure
- Price Cycle

Raw Materials Prices
Location
Operating Efficiencies

Competitive situation
Nature of operations
Management Control

Level & Maturity of debt
Currency exposures
Contingent Liabilities

Scale
Construction/implementation/
marketing risk
Financing plan & Status

Liquid investments
Group Support
Bankers/Investors support
Thank you

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