Rating's Transition & Default Study FY 2018

About Brickwork Ratings

Brickwork Ratings, a credit rating agency founded by bankers, former regulators, and credit rating professionals, is a SEBI registered credit rating agency with its corporate office in Bengaluru. It is also accredited by RBI and empaneled by NSIC for carrying out bank loan, SME rating, NCD, Commercial paper and MSME rating respectively. It has a country wide presence through its branches in Ahmedabad, Chandigarh, Chennai, Hyderabad, Kolkata, Mumbai and New Delhi along with representatives across more than fifty cities.

About this Publication

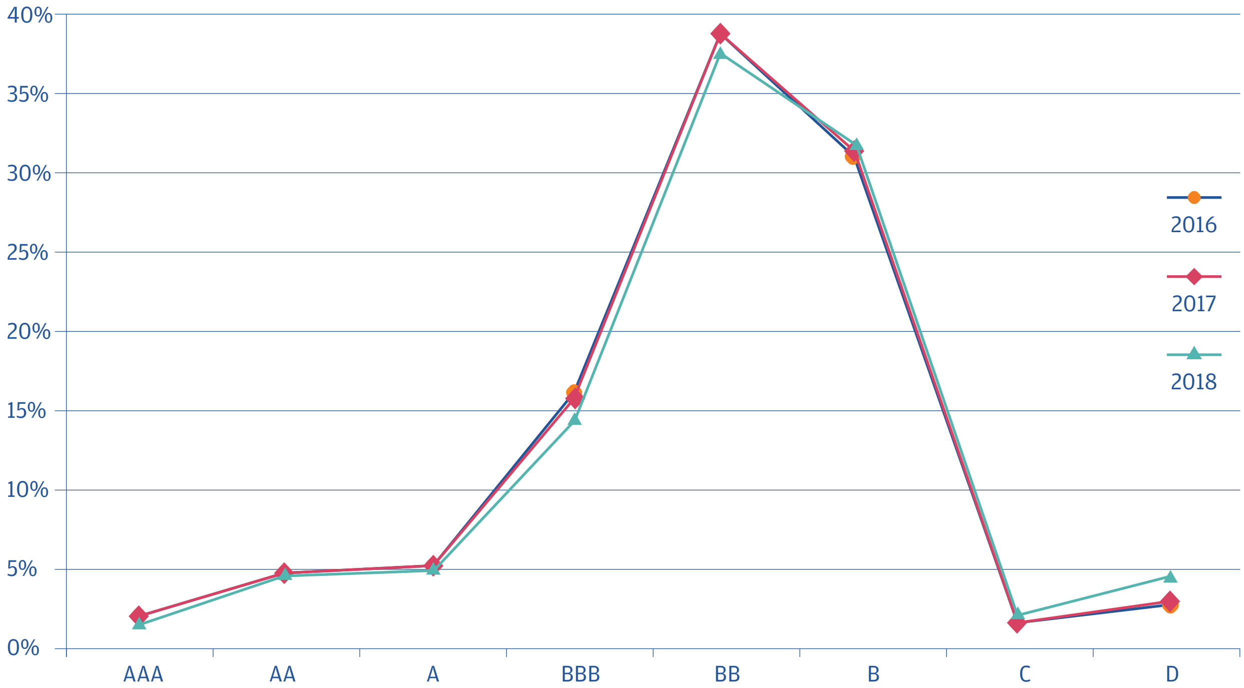
The transition and default study report is an annual publication of Brickwork Ratings. Brickwork considers analytical excellence, integrity and transparency as its core values in its operations. The report seeks to provide an insight into the rating performance of all ratings assigned by Brickwork Ratings to the investing community and the public at large. All rating rationales are also available on the website of Brickwork Ratings **www.brickworkratings.com**

Executive Summary

The total number of long term ratings assigned by Brickwork Ratings that were outstanding as of 31st March 2018 exceeded over 7500 ratings. The ratings distribution continues to have a median of BB which was the case for FY 17 too. The non-investment grade population of Brickwork Ratings contributes to around 76% of the total rated population for FY18.

The Credit Ratings Behavior Ratio (CRBR) is an indication of the rating action trend and is defined as (Rating Upgrades / Rating Downgrades). For the current year the CRBR for the total rated population stood at 0.37 overall. Modified Credit Ratings Behavior Ratio (MCRBR) which is (Rating Upgrades + Ratings Reaffirmed)/(Rating Downgrades +Ratings Reaffirmed) for the total rated population stood at 0.88 overall.

Ratings Distribution



The rating distribution as on March 2018 has shifted slightly to the right compared to that of March 2017, with nearly 76% of the total ratings assigned falling in the non-investment category. The median of the rating distribution continues to remain in the BB rating category as on March 2018.

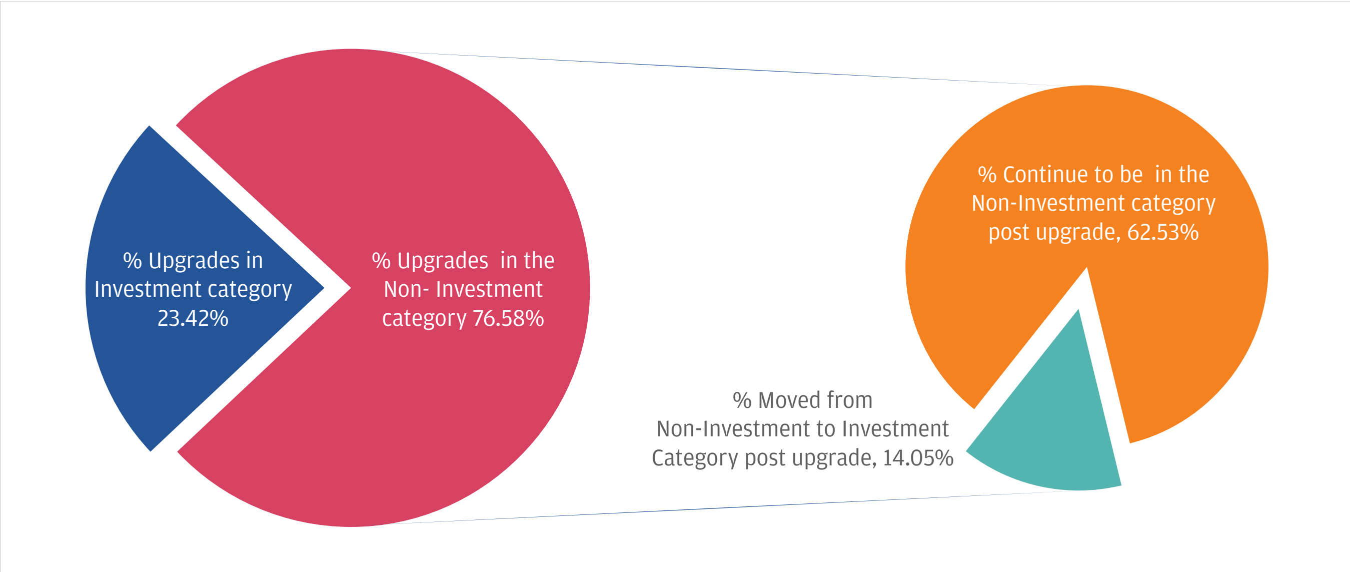
Credit Ratings Behavior ratio & Modified Credit Ratings Behavior ratio

CRBR for the total rated population for the period 2017-18 stood at 0.37. CRBR When broken down further in to investment and non - investment category stood at 0.59 and 0.33 respectively. The MCRBR defined as (Rating upgrades+ Ratings Reaffirmed)/(Rating Downgrades + Ratings Reaffirmed) for the total rating population stood at 0.88 overall, out of which MCRBR for the investment and non-investment category stood at 0.95 and 0.86 respectively.

Information risk (non-receipt of adequate information) & non receipt of no default statements on a timely basis, as per the latest regulatory guidelines are few of the major reasons for downgrading of ratings. The other reasons for downgrading of ratings of various companies are substantial decline in financial performance, delay in timely servicing of debt obligations, negative feedback from the lender etc. Despite the adversities some companies have been able to improve their performance or maintain at the existing levels, such companies have been considered for upgrades.

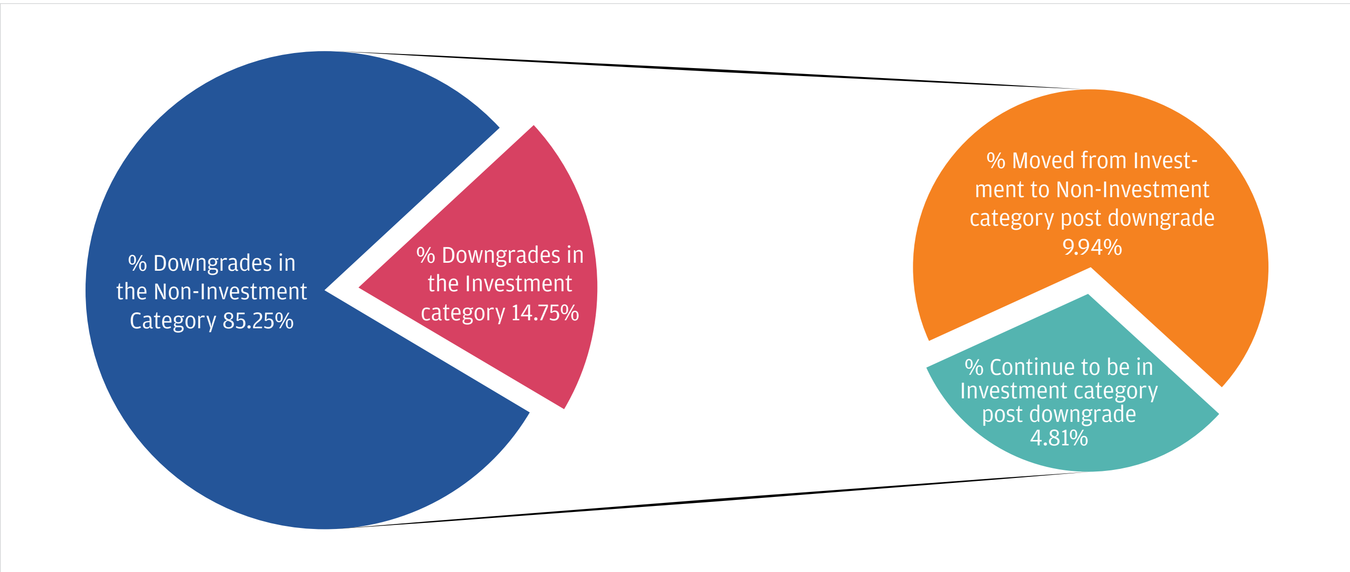
Movement from the investment grade to non-investment grade and vice versa is shown in the charts below

Upgrade Portfolio-FY 18



The upgrade portfolio consists of both investment grade and non-investment grade firms as shown above. Of the upgrades done in the non-investment category, 62.53% of them were upgraded within in the same non-investment category while only 14.05% moved to the investment category (mainly to BBB bucket)

Downgrade Portfolio-FY 18



Of the total downgrades during the year, 85.25 % of the downgrades are in the non-investment category and 14.75% of the downgrades are in the investment category. The low CRBR of BWR is primarily due to downgrades in the non-investment category for reasons explained earlier.

Transition Matrix and Default Study

The transition matrix shows the stability rates as well as the percentage of ratings upgraded or downgraded for each rating scale. The highlighted cells indicate the stability rates which reflect the strength of the rating methodology of Brickwork Ratings.

Transition Matrix for rated instruments excludes structured finance ratings (only 1 structured finance rating has been assigned by BWR to date). The table below indicates weighted average transition of ratings over the latest five years, FY12-FY18 in case of one year transition matrix and FY12-FY18 in case of three year transition matrix.

One Year Transition Rate [FY 2012-FY 2018] Table 1.1

	BWR AAA	BWR AA	BWR A	BWR BBB	BWR BB	BWR B	BWR C	BWR D
BWR AAA	95.41%	4.59%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
BWR AA	0.95%	96.43%	2.14%	0.24%	0.00%	0.00%	0.00%	0.24%
BWR A	0.00%	2.15%	93.86%	1.69%	1.54%	0.15%	0.15%	0.46%
BWR BBB	0.00%	0.00%	2.03%	90.50%	6.19%	0.04%	0.09%	1.15%
BWR BB	0.00%	0.00%	0.00%	2.88%	90.70%	4.47%	0.18%	1.77%
BWR B	0.00%	0.00%	0.00%	0.04%	4.36%	91.19%	2.05%	2.36%
BWR C	0.00%	0.00%	0.00%	0.00%	1.40%	9.81%	82.24%	6.54%

Three Year Transition Rate [FY 2012-FY 2018] Table 1.2

	BWR AAA	BWR AA	BWR A	BWR BBB	BWR BB	BWR B	BWR C	BWR D
BWR AAA	83.62%	15.52%	0.86%	0.00%	0.00%	0.00%	0.00%	0.00%
BWR AA	5.46%	85.79%	7.10%	0.00%	0.00%	0.00%	0.00%	1.64%
BWR A	0.50%	6.44%	79.21%	5.94%	3.47%	0.50%	0.50%	3.47%
BWR BBB	0.00%	0.00%	8.03%	74.93%	11.97%	0.28%	0.00%	4.79%
BWR BB	0.00%	0.00%	0.00%	7.60%	77.91%	9.44%	0.53%	4.51%
BWR B	0.00%	0.00%	0.00%	0.67%	10.94%	79.45%	3.77%	5.17%
BWR C	0.00%	0.00%	0.00%	2.47%	2.47%	20.99%	60.49%	13.58%

AAA stability is less than that of AA because of the small sample size of AAA rated companies. For a small rating population, even one company being downgraded / upgraded can cause a big shift in the stability rate.

BWR Transition and Default Methodology

The Transition Rate is calculated across all rating categories over one and three year time period to evaluate behavior of ratings over different time horizon. BWR has adopted long-term rolling-over weighted average approach to assess CDR (Cumulative Default rate) for arriving at one year CDR and three year CDR of the ratings which are reviewed on an ongoing basis.

- The study tracks long term rating assigned and accepted by the client/issuer and is issuer specific for bank loan ratings which is a major part of rating population of BWR and also for NCD's/Bonds.
- The static pool consists of number of ratings outstanding for each rating category as on the beginning of financial year under study. Default behavior of each rating category is examined over one and three year periods.
- The static pool under study consists of long term ratings in the category of Bank loans, NCDs, Bonds from FY12 to FY18 for 1 YR CDR & from FY12 to FY 18 for 3 YR CDR.

The highlighted cells in Table 1.1 & 1.2 indicate the stability rate across respective rating categories.

Cumulative Default Rates

One year and Three year Cumulative Default rate (CDR): Table 1.3

Rating Category	1-Year CDR	3-Year CDR
AAA or equivalent	0.00%	0.00%
AA or equivalent	0.24%	1.64%
A or equivalent	0.46%	3.47%
BBB or equivalent	1.15%	4.79%
BB or equivalent	1.77%	4.51%
B or equivalent	2.36%	5.17%
C or equivalent	6.54%	13.58%

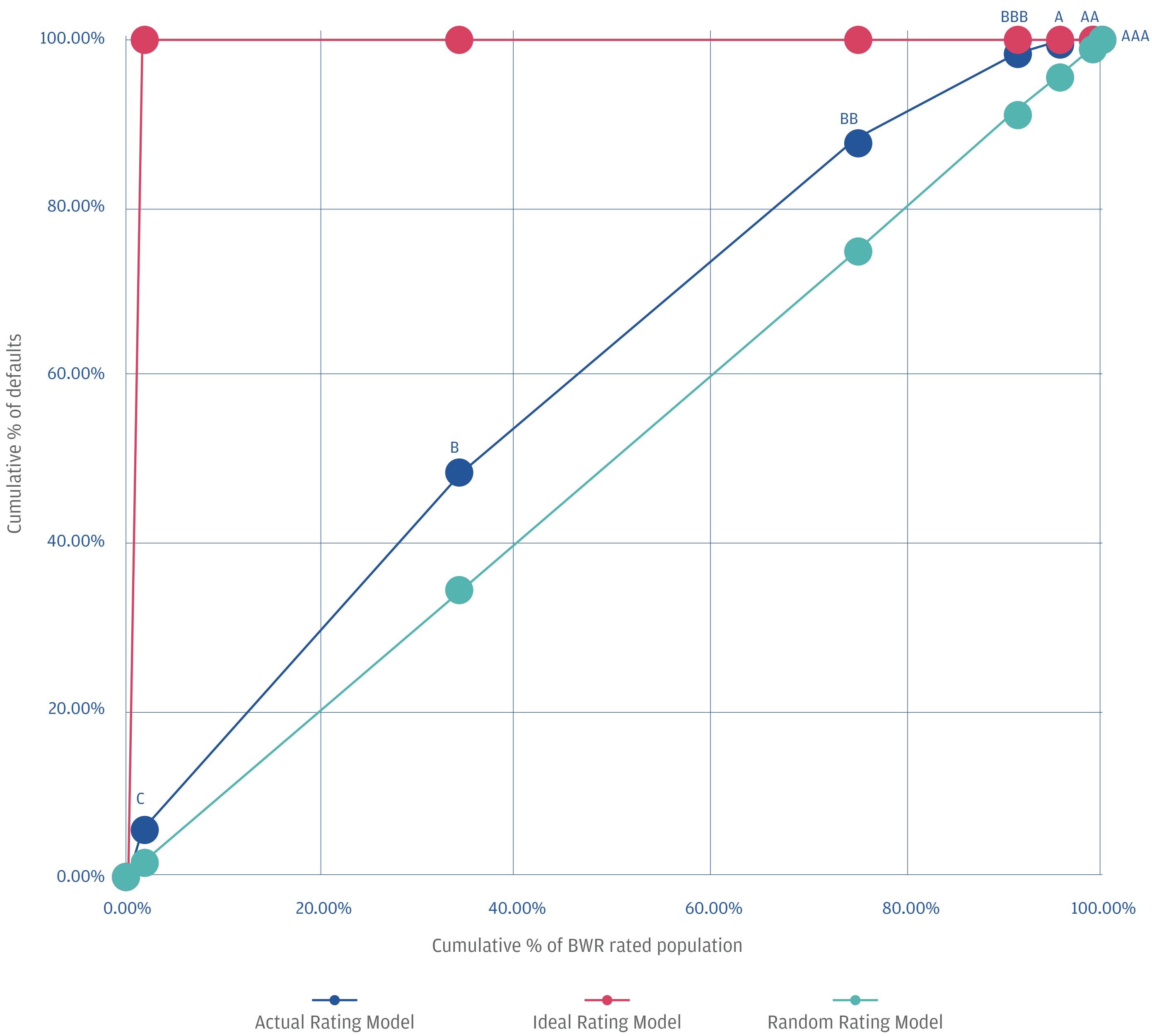
BWR annual default rates are calculated on an issuer basis. One year and three year Cumulative Default rate has been calculated on weighted average basis. Wherein, the default population is weighted with the category population of each year and averaged by total static pool for all the years. Data prior to FY12 is insignificant to be considered for default study as the population was too small, consisting of only bond and NCD ratings of large corporates with hardly any default. BWR started bank loan ratings on a larger scale from FY14 onwards.

Lorenz curve and Gini Coefficient Ratio

Lorenz curve and Gini Coefficient (accuracy ratio) is adopted as a measure to represent the accuracy of the rating exercise by BWR. Following is the Lorenz Curve for the period FY12-FY18

The Lorenz curve (Cumulative Curve) represents the actual scenario vis-à-vis Perfect Scenario. The closer the Lorenz curve is to perfect curve, the better the predictability of ratings. The Gini Coefficient is a ratio which represents the area between the cumulative curve (Lorenz Curve) and random Curve in relation to area between perfect curve and the random curve. This ratio is also called accuracy ratio. If the ratio is nearer to 1, it indicates ratings having better predictive ability, wherein cumulative curve will merge closely with perfect curve. BWR's Gini Coefficient for One year average default for FY 2012-18 was 0.26.

Lorenz Curve : 2012-2018



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