



ICRA-ASSIGNED SECURITISATION RATINGS: TRANSITION STUDY

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Summary

This paper studies the transition made by all ICRA-assigned securitisation¹ ratings—viz. ratings of Asset-Backed Securities (ABS), Mortgage-Backed Securities (MBS) and Corporate Loan Sell-Offs (LSO)—that were either live as in April 2000 or were assigned thereafter. The primary objective of this study has been to gauge the stability of ICRA-assigned securitisation ratings, for which purpose, the one-year transition of all such ratings, since 2000-01, was analysed. The analysis presented here also seeks to provide insights into the factors that led to the rating revisions made over the period of study.

Overall, the analysis brings out the high stability that is a feature of the securitisation ratings assigned by ICRA. While none of the ICRA-assigned MBS ratings have been downgraded till date, in 2008-09, some ABS ratings were downgraded with the pools concerned reporting higher-than-expected delinquency in the backdrop of a difficult operating environment, tighter liquidity conditions and lengthening of the post-default recovery process. In the case of LSO ratings, the rating downgrades that happened in 2008-09 were restricted to borrowers from certain sectors, such as real estate.

¹ Including bilateral placements (commonly termed 'Direct Assignment' transactions)

1 COVERAGE OF THE STUDY

This paper analyses the one-year transition made by ICRA-assigned ratings for ABS, MBS and LSO transactions. The one-year transition in a given financial year considers transactions that were live both at the beginning and at the end of that financial year. Ratings assigned or withdrawn during a financial year have been *excluded* in the transition for that financial year. For transactions involving multiple rated tranches, each tranche has been accounted for separately in this analysis. Rated second-loss facilities as well as liquidity facilities have also been included in the analysis. Private ratings and credit opinions *do not form* a part of this transition study. Similarly, this note does not cover guaranteed debt (partly or fully guaranteed), escrow-backed debt, and such other structured debt. The analysis addresses *inter-category* rating transitions only.

There has been no transition in medium-term securitisation ratings till March 2009. As on March 2009, there were eight medium-term ratings outstanding on securitised instruments.

There has been no transition in short-term ABS ratings till March 2009. However for LSO, 33 short-term ratings (pertaining to three corporate entities) were downgraded till March 2009. As in March 2009, there were eight short-term ABS ratings and 63 short-term LSO ratings outstanding.

2 TRANSITION ANALYSIS

2.1 Upgrades and Downgrades

The ABS and MBS market in India is heavily skewed towards LAAA ratings. There is hardly any investor appetite for instruments rated below LAAA. Hence, rating upgrades are rare (in fact, a rating upgrade can happen only for a transaction that has been downgraded earlier).

Till March 2009, there was no rating upgrade in any ICRA-rated ABS, MBS or LSO transaction².

Table 1: Rating downgrades and average extent of downgrade in ABS and LSO³ ratings since 2004-05

Financial Year (FY)	ABS		LSO	
	No. of downgrades	Average notching down of rating in an FY	No. of downgrades	Average notching down of rating in an FY
2004-05	0	NA	0	NA
2005-06	0	NA	0	NA
2006-07	0	NA	0	NA
2007-08	4	1.0	2	1.0
2008-09	24	2.5	8	3.0

NA: Not Applicable

In *Table 1*, the number of downgrades in a financial year includes multiple downgrades for a single instrument. The average notching down denotes the average number of notches by which a rating has been downgraded during a financial year.

The financial years 2007-08 and 2008-09 reported a progressively increasing number of downgrades. Also, the extent of downgrades was more severe in 2008-09—a reflection of the difficult economic conditions prevailing that year.

² Post-March 2009, there have been some rating upgrades in ABS paper; however the period considered for this paper is end of 2008-09.

³ There has been no downgrade in MBS ratings till March 2009.

2.2 ABS Downgrades Concentrated among CV and Auto Pools Rated in 2006-07

Figure 1: ABS rating downgrades in 2008-09 by asset class

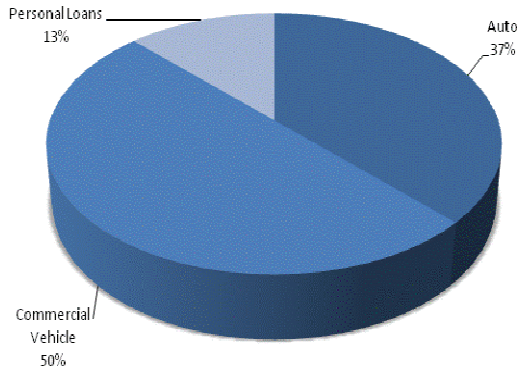
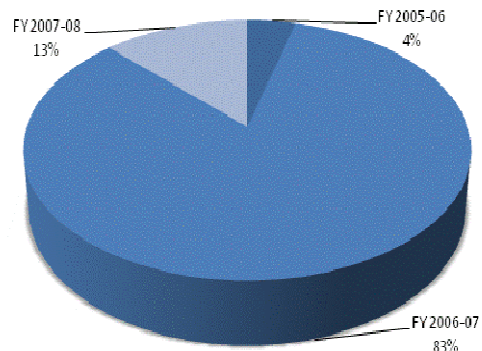


Figure 2: ABS rating downgrades in 2008-09 by rating vintage



Of the 397 tranches of ABS rated by ICRA till March 2009, eighteen were downgraded from their original rating level. The ICRA-rated ABS transactions that have suffered a downgrade have largely been those that were rated in 2006-07, a period characterised by increase of competition in the retail loan business and relaxation of lending norms by some players. While the weakening of credit quality in the second half (H2) of 2008-09 was largely systemic—with the extent varying across players—it was only in specific transactions, that rating actions had to be taken. The ratings assigned in 2007-08 have performed better than those assigned in 2006-07 owing to the stricter lending policy adopted for the overall underlying portfolio, the tighter pool selection criteria used by the Originators concerned, and the relatively larger credit enhancement cover provided.

The asset class-wise break-up of ABS downgrades reveals a higher number of downgrades in the commercial vehicle (CV) and auto loan pools as these asset classes comprise the majority of ICRA-rated pools. Among the various asset classes, construction equipment related loans have reported good performance till date, while the credit quality of unsecured personal loans, particularly small ticket personal loans, has been on the weaker side.

Overall, the performance of some of the securitisation ratings has been adversely affected by a combination of factors, including selection filters and the operating environment. The slowdown in demand across sectors, contraction in real income levels, and the increase in collection-related difficulties have also led to a weakening of the credit quality of the rated pools for most Originators.

2.3 Performance of ABS Ratings

Table 2: One-year transition matrix—long-term ABS ratings (2008-09)

	LAAA	LAA	LA	LBBB	NI
LAAA	91.08%	6.37%	2.55%	0.00%	0.00%
LAA	0.00%	25.00%	75.00%	0.00%	0.00%
LA	-	-	-	-	-
LBBB	0.00%	0.00%	0.00%	100.00%	0.00%

NI: Non-investment grade, that is, ratings below LBBB- (viz. LBB+ till LD)
The categories of LAA, LA and LBBB include ratings with suffixes "+" and "-" within the respective categories. Thus, for instance, the category LAA contains three ratings: LAA+, LAA, and LAA-.

Table 3: One-year transition matrix—long-term ABS ratings (2007-08)

	LAAA	LAA	LA	LBBB	NI
LAAA	97.50%	2.50%	0.00%	0.00%	0.00%
LAA	-	-	-	-	-
LA	-	-	-	-	-
LBBB	0.00%	0.00%	0.00%	100.00%	0.00%

Table 4: Average one-year transition matrix—long-term ABS ratings (Since 2003-04)⁴

	LAAA	LAA	LA	LBBB	NI
LAAA	96.28%	2.89%	0.83%	0.00%	0.00%
LAA	0.00%	25.00%	75.00%	0.00%	0.00%
LA	-	-	-	-	-
LBBB	0.00%	0.00%	0.00%	100.00%	0.00%

The key findings of the above analysis are highlighted below -

- The transition analysis for ABS ratings indicates *consistently high stability* of LAAA ratings.
- As discussed earlier, the Indian ABS market is highly LAAA-centric. Thus, there are not enough data points for other rating categories, which makes establishing ordinality in the ratings difficult.
- A seemingly high transition is observed from the LAA category. However, the number of ratings in these categories being very low, any statistical inference drawn from such limited data is likely to be misleading.
- The LBBB category ratings appearing in the tables above are those that have been assigned to the 'Second-Loss Portion' of the credit enhancement. These ratings have also shown a high degree of stability.

2.4 MBS Ratings exhibit High Stability

There were 27 MBS ratings outstanding as in March 2009. So far, there has been no downgrade of any MBS transaction rated by ICRA. The following factors have contributed to the high stability of the MBS ratings:

- The propensity to default on a home loan has remained low for a typical Indian borrower.
- MBS transactions are typically of long tenure (10-25 years for loan against property and 15-20 years for home loans) and many of the rated transactions have not undergone substantial amortisation yet.
- In most transactions, the rise in the interest rates on the underlying loans in the pools has provided greater cash flow cover for the investor payouts.

Note: It is possible that the rating-stability indicated benefits, to an extent, from what is termed as the small-sample bias, given that the number of rated MBS transactions is small (for reasons including low investor appetite for long tenure instruments).

⁴ There were no long-term ABS ratings assigned before this period

2.5 LSO Ratings—Downgrades Restricted to a Few Obligor

Ratings of LSO transactions are reflective of the credit quality of the underlying obligor. In the case of long-term LSO ratings, all the downgrades that happened during the period of study pertained to two underlying obligors. Till March 2009, thirty-three short-term LSO ratings had been downgraded, with all of them pertaining to three underlying obligors, among whom two were from the real estate sector.

2.6 Performance of LSO Ratings

Table 5: One-year transition matrix—long-term LSO ratings (2008-09)

	LAAA	LAA	LA	LBBB	NI
LAAA	100.00%	0.00%	0.00%	0.00%	0.00%
LAA	0.00%	100.00%	0.00%	0.00%	0.00%
LA	0.00%	0.00%	0.00%	66.67%	33.33%
LBBB	-	-	-	-	-

Table 6: One-year transition matrix—long-term LSO ratings (2007-08)

	LAAA	LAA	LA	LBBB	NI
LAAA	100.00%	0.00%	0.00%	0.00%	0.00%
LAA	0.00%	100.00%	0.00%	0.00%	0.00%
LA	-	-	-	-	-
LBBB	-	-	-	-	-

Table 7: Average one-year transition matrix—long-term LSO ratings (since 2003-04)⁵

	LAAA	LAA	LA	LBBB	NI
LAAA	100.00%	0.00%	0.00%	0.00%	0.00%
LAA	0.00%	100.00%	0.00%	0.00%	0.00%
LA	0.00%	0.00%	0.00%	66.67%	33.33%
LBBB	-	-	-	-	-

The key findings of the above analysis are highlighted below -

- The transition analysis for LSO ratings indicates *consistently high stability* of LAAA ratings.
- Most of the rated transactions are in the LAAA or LAA category. Thus, there are not enough data points for other rating categories, which makes establishing ordinality in the ratings difficult.
- A seemingly high transition is observed from the LA category. However, the number of ratings in these categories being very low, any statistical inference drawn from such limited data is likely to be misleading.

⁵There were no long term LSO ratings assigned before this period



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