CRISIL RATINGS

The Most Reliable Opinion on Risk

RATINGS ROUNDUP

First Half 2004-05

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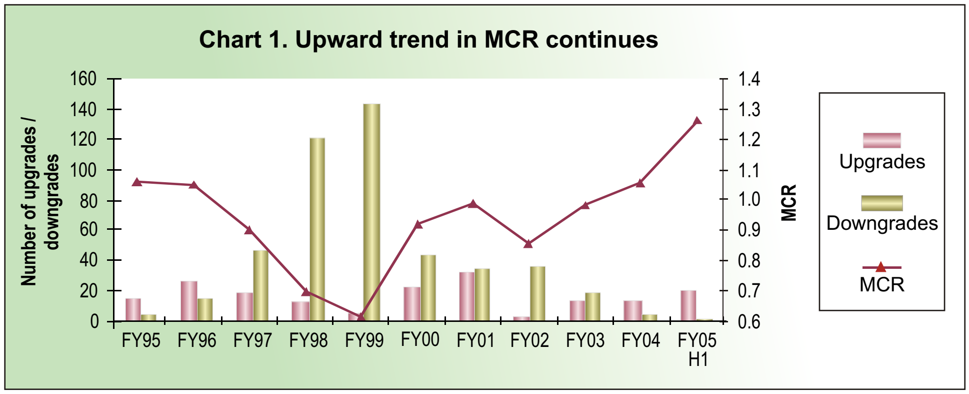
The business outlook for corporate India will continue to improve in H2FY05[1], according to CRISIL's analysis of its rating trends. In the first half of the current year, rating upgrades exceeded downgrades by 25:0 - the highest-ever in CRISIL's history. Notably, CRISIL's rated portfolio did not witness a single default for the first time in ten years, which points robust overall economic growth. The improvement in business fundamentals is in line with the forecast made in the last Ratings Roundup.

While negative agricultural growth will pull down gross domestic product (GDP) numbers, the Index of Industrial Production (IIP) is expected to continue exhibiting strong growth even on last year's high base. Sustained volume growth coupled with efficiency gains will ensure healthy corporate profitability in H2FY05. With limited capacity additions over the last several years, utilisation levels have improved. Given this, the trends in CRISIL's rated portfolio indicate a strong pick-up in planned capital investments. This and higher inflation will keep interest rates firm in the second half of the fiscal.

[1] FY refers to the financial year, April 1 to March 31.

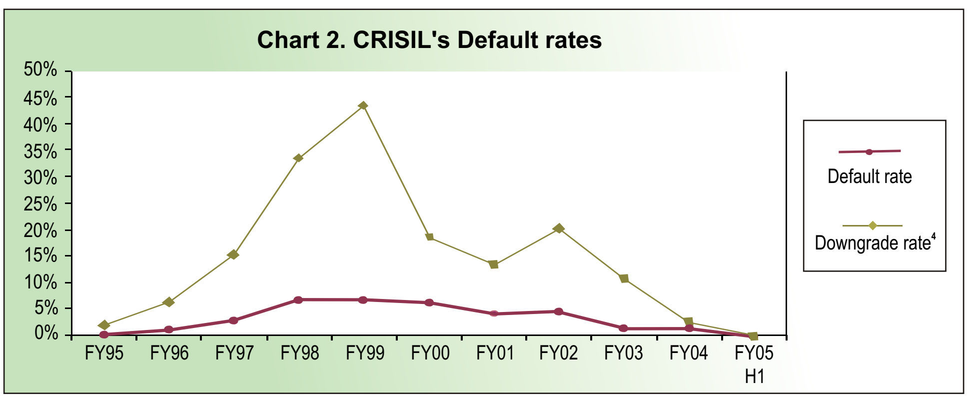
Strengthening credit performance

CRISIL's modified credit ratio (MCR)[2] is an effective indicator of systemic credit quality and a proxy for underlying business fundamentals. As Chart 1 shows, the MCR for long-term ratings reached a new high of 1.28 in H1FY05 (up from 1.05 in FY04) driven by 25 upgrades and no downgrades[3]. Even after excluding the seven upgrades in the financial sector, which were driven by a reassessment of CRISIL's expectation of government support to public sector banks, the MCR would have been healthy at 1.2.



No defaults or downgrades

In H1FY05, CRISIL's rated portfolio experienced neither a downgrade nor a default. Notably, as evident from Chart 2, a zero default rate was observed after a gap of 10 years. This clearly underscores the improvement in corporate credit quality.



Credit profile improvement across sectors

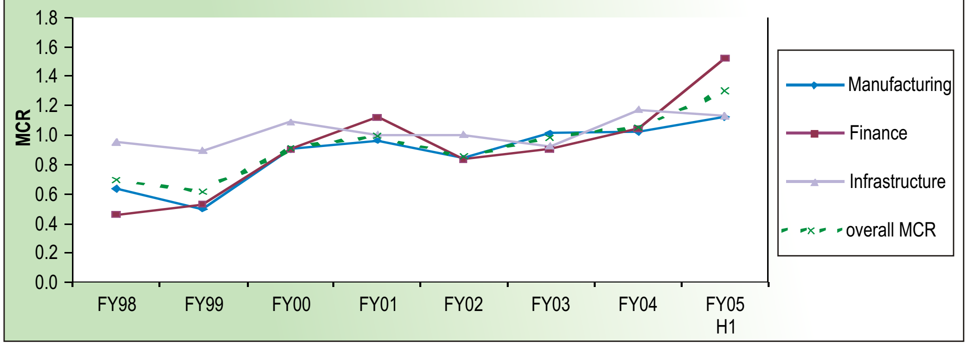
All the three key rating segments - manufacturing, financial services and infrastructure - recorded an MCR of over 1.0, demonstrating that credit profiles improved across the board. Chart 3 compares the MCR across the three sectors over the last few years. The manufacturing and financial services sectors lead the spurt in the MCR with 13 and 10 upgrades respectively.

The financial services segment's MCR increased sharply to 1.53, the highest ever for any sector. Excluding the seven upgrades of public sector banks and their affiliated entities, which were due to a reassessment of likely government support, the MCR would have been 1.16.

[2] MCR is defined as the ratio of upgrades plus reaffirmations to downgrades plus reaffirmations in a given period.
[3] CRISIL's fixed deposit ratings portfolio also experienced more upgrades, taking the MCR to 1.23 in H1FY05 from 1.10 in FY04
[4] The downgrade rate is defined as the number of ratings downgrade divided by the total rating actions in a given period.

Aggressive financial and operational restructuring over the last few years has improved the manufacturing sector's competitiveness across a broad spectrum of industries. This year's upgrade list shows companies from the packaging, plastics, automobiles, pharmaceuticals, fertiliser and other diversified industries. This clearly demonstrates that the improvement in credit profile is broadbased, and is not due to the good performance of a few industries alone.

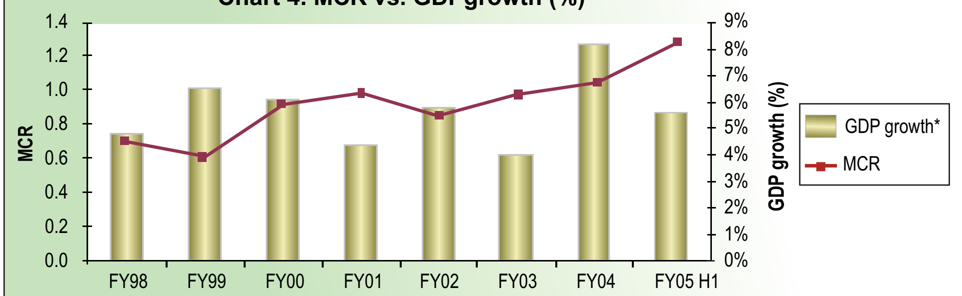
Chart 3. Improvement in MCR across sectors



Improved MCR indicates positive macro-economic environment

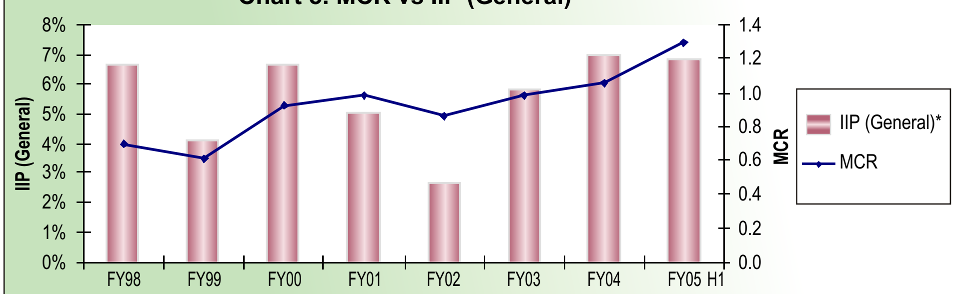
CRISIL's ratings portfolio covers all the key sectors of the economy besides including most of the top players in each segment. Consequently, its rating trends provide an excellent barometer of macro-economic and business outlook. Typically, the MCR is a good lead indicator of GDP growth. While negative agricultural growth will pull down overall GDP growth rate in 2004-05, IIP growth is expected to remain strong despite the high base effect. This is in line with the improving MCR.

Chart 4. MCR vs. GDPgrowth (%)



Source: CRISIL Centre for Economic Research
* GDP growth forecast for 04-05 is for the full year.

Chart 5. MCR vs IIP (General)



Source: CRISIL Centre for Economic Research, CSO
*IIP forecast for 04-05 is for the full year.

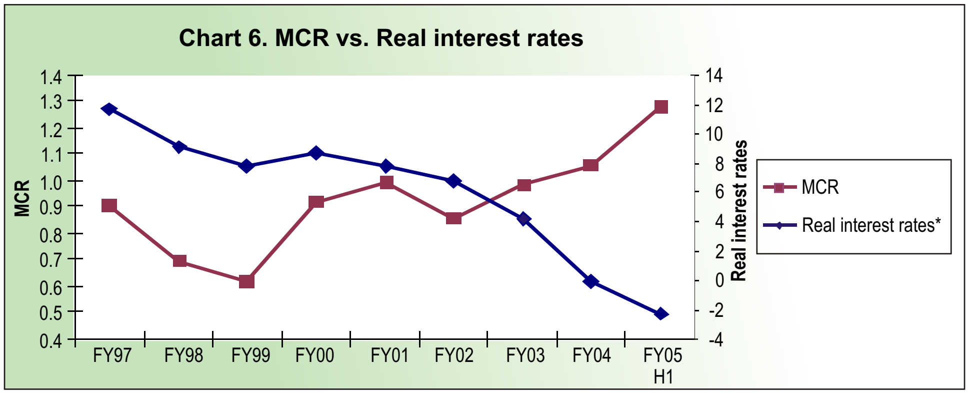
Synopsis of rating actions

In H1FY05, CRISIL's long-term ratings portfolio experienced 25 upgrades and no downgrades. In addition, fixed deposit ratings saw 10 upgrades.

- 20 upgrades pertained to ratings that were already in the high investment grade ('AA-' and above). One company, Tata Power Limited, was upgraded to 'AAA' from 'AA+'
- Manufacturing and financial services sectors led the improvement in overall credit quality with 13 and 10 upgrades respectively
- Eighty percent of the upgrades were by a single notch

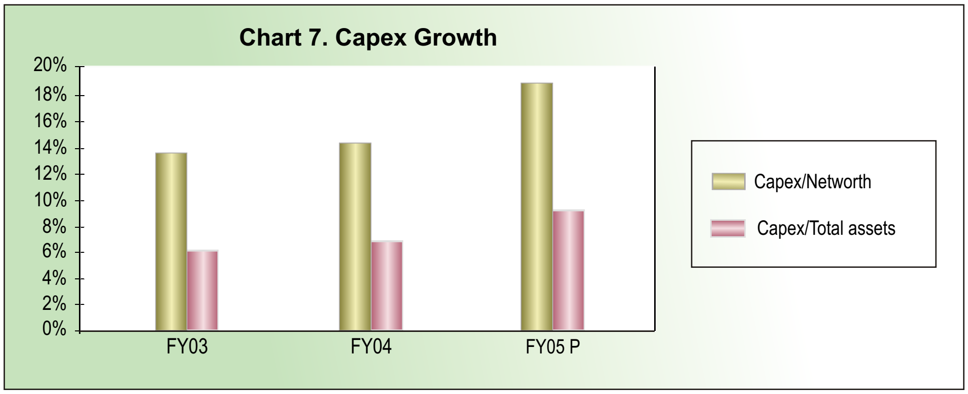
Lower interest rates boost corporate profitability

With rising inflation, real interest rates have continued to decline. A low real interest rate implies lower borrowing costs for corporates in relation to product prices, which has a positive impact on their profitability. This has partly contributed to the increase in the MCR. Chart 6 shows the relationship between MCR and real interest rates over the last few years.



Capex becoming attractive

Improved capacity utilisation, a positive economic outlook and low real interest rates have made capex attractive. An analysis of over 200 CRISIL-rated companies in the manufacturing and infrastructure sector clearly indicates that corporate India is stepping up its investments in new capacities. As shown in Chart 7, capex to networth ratio is expected to grow to 18.6 percent from 13.7 percent. A strong upsurge in the production index for machinery and capital goods also substantiates the improvement in the investment climate. Moreover, the order-book position of the top 10 capital goods manufacturers in CRISIL's portfolio clearly demonstrates the strong pick-up in planned capex.

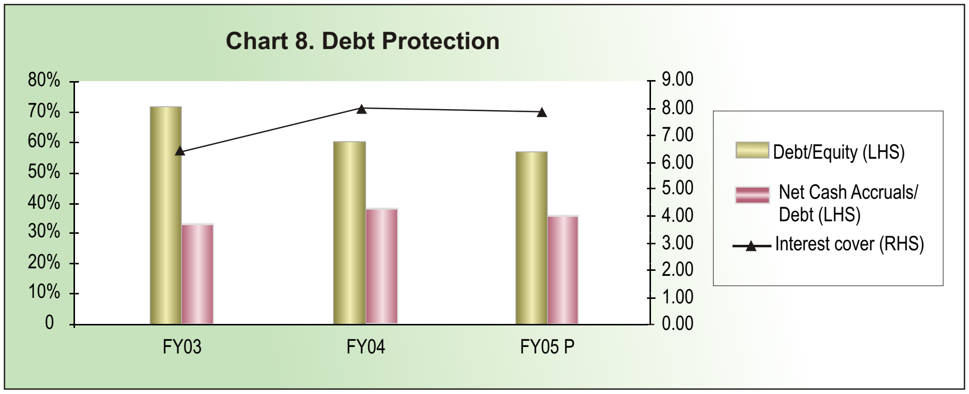


Higher corporate demand for funds should firm up nominal interest rates in the second half. As the oil shock-induced inflationary pressure recedes, real interest rates will turn positive, but will remain low.

Corporate credit profile to remain strong

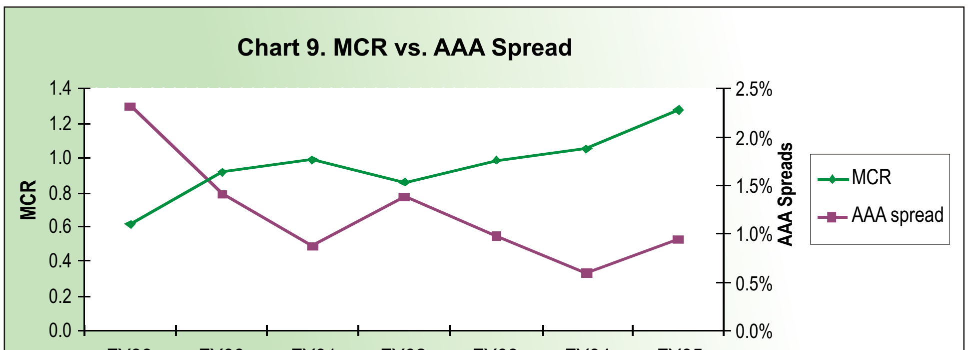
Despite their large capex plans, corporate credit profiles are expected to remain healthy. A significant improvement in balance sheets across the spectrum is enabling companies to take up capex without impairing their credit quality. An analysis of more than 200 rated companies indicates that their key debt protection measures will remain strong in spite of the increase in planned capex. This can be seen in Chart 8 .

- Three companies were upgraded by three notches - IDBI Bank (on its merger announcement with IDBI), Tata Finance Limited and Steel Authority of India Limited (on their improved performance)
- One company - Dhampur Sugar Mills Limited - recovered from the default category and was upgraded to BB
- Seven of ten upgrades in fixed deposit ratings belonged to the financial sector all the four upgrades to 'FAAA' were also from financial sector



Credit spreads to retreat

The MCR has historically shown an inverse correlation with credit spreads. This is evident from Chart 9, which shows the relationship between MCR and AAA spreads over the years. In the last few months, however, credit spreads have increased despite the improved MCR. This is largely due to short-term disruptions in the debt market on the back of an inflationary scare. Given the positive outlook on corporate credit profiles, however, CRISIL expects spreads to decline.

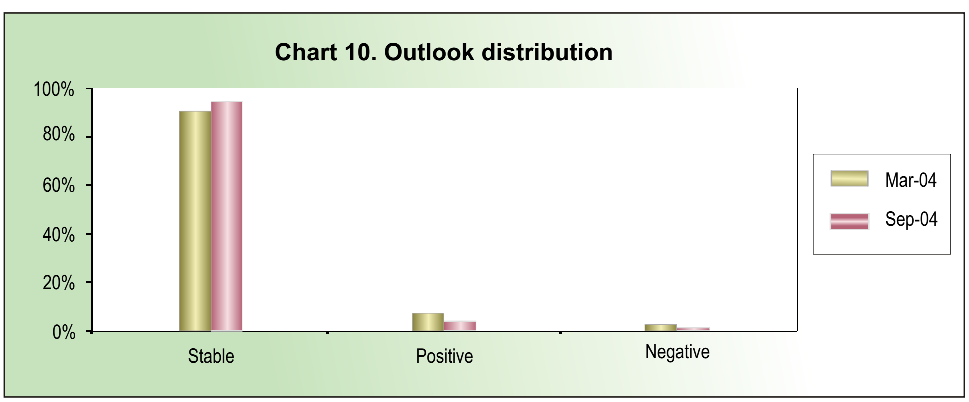


Source: CRISIL Investment and Risk Management Services

Rating Outlooks - early indicators of rating actions

Rating Outlooks, introduced by CRISIL in September 2003, have proved to be good early indicators of the likely direction of ratings, as intended. Fifty per cent of the companies with a positive outlook at the beginning of 2004-05 were upgraded in H1FY05. On the other hand, the upgrade rate for companies with a 'Stable' outlook was only 11 per cent.

As shown in Chart 10, the distribution of outlooks as at September 30, 2004 indicates that the proportion of ratings with a 'Stable' outlook has increased. This and the fact that seven upgrades in H1FY05 were due to CRISIL's reassessment of government support for public sector banks, which is unlikely to recur, indicates that rating changes in the second half will be lower.



APPENDIX I

CRISIL's Long-Term Rating Upgrades in H1 2004-05

Sl. No	Company	Sector	Industry	Rating From	Rating To	Outlook From	Outlook To
1	Ashok Leyland Ltd.	Manufacturing	Automobiles- CV	AA-	AA	Stable	Stable
2	Bank of Baroda	Finance	Banking	AA+	AAA	-	Stable
3	Bharti Cellular Ltd.	Infrastructure	Telecommunication-Services-Equipments /Cable	AA-	AA	Stable	Stable
4	BoB Housing Finance Ltd	Finance	Housing Finance Co.	AA	AA+	Stable	Positive
5	Cadila Healthcare Limited	Manufacturing	Pharmaceuticals	AA	AA+	Stable	Stable
6	Canara Bank	Finance	Banking	AA+	AAA	-	Stable
7	Canbank Factors Ltd	Finance	NBFC	AA	AA+	Stable	Stable
8	Chambal Fertilisers & Chemicals Ltd.	Manufacturing	Fertilizers	A+	AA-	Positive	Stable
9	Dhampur Sugar Mills Ltd., The	Manufacturing	Sugar	D	BB	-	Stable
10	E.I.D. Parry Ltd.	Manufacturing	Sugar	AA-	AA	Stable	Stable
11	Essel Propack Ltd.	Manufacturing	Packaging	AA	AA+	Positive	Stable
12	Finolex Industries Ltd.	Manufacturing	Plastic & Plastic Products	AA	AA+	Stable	Stable
13	IDBI Bank Ltd.	Finance	Banking	A+	AA+	-	Stable
14	Indian Overseas Bank	Finance	Banking	AA	AA+	Stable	Stable
15	LG Electronics India Pvt. Ltd	Manufacturing	Consumer Durable	AA	AA+	Positive	Stable
16	Mahindra and Mahindra Financial Services Ltd.	Finance	Non Banking Finance Company	AA	AA+	Stable	Stable
17	Mahindra and Mahindra Ltd.	Manufacturing	Automobiles- 4 wheelers	AA	AA+	Stable	Stable
18	PNB Housing Finance Ltd	Finance	Housing Finance Co.	AA	AA+	Stable	Stable
19	Steel Authority of India Ltd.	Manufacturing	Steel and Steel products	BBB	A	-	Stable
20	Sterlite Industries (India) Ltd.	Manufacturing	Diversified	AA-	AA	-	-
21	Syndicate Bank	Finance	Banking	AA	AA+	Stable	Stable
22	Tata Chemicals Ltd.	Manufacturing	Diversified	AA	AA+	Positive	Stable
23	Tata Finance Ltd.	Finance	NBFC	BBB	A	Positive	Stable
24	Tata Motors Ltd.	Manufacturing	Automobiles- CV	AA	AA+	Stable	Stable
25	The Tata Power Company Ltd.	Infrastructure	Power	AA+	AAA	Stable	Stable

CRISIL's Fixed Deposit Rating Upgrades H1 2004-05

Sl. No	Company	Sector	Industry	Rating From	Rating To	Outlook From	Outlook To
1	Canbank Factors Ltd	Finance	NBFC	FAA+	FAAA	Stable	Stable
2	Cent Bank Home Finance Ltd	Finance	Housing Finance Company	FAA-	FAA	-	-
3	Chambal Fertilisers & Chem. Ltd.	Manufacturing	Fertilizers	FAA-	FAA	Positive	Stable
4	Dhampur Sugar Mills Ltd., The	Manufacturing	Sugar	FD	FB+	-	Stable
5	Lakshmi General Finance	Finance	NBFC	FAA+	FAAA	Positive	Stable
6	Mahindra and Mahindra Financial Services Ltd.	Finance	Non Banking Finance Company	FAA	FAA+	Stable	Stable
7	PNB Housing Finance Ltd	Finance	Housing Finance Company	FAA+	FAAA	Stable	Stable
8	Steel Authority of India Ltd.	Manufacturing	Steel and Steel products	FA	FA+	-	Stable
9	Sundaram Finance Ltd.	Finance	NBFC	FAA+	FAAA	Positive	Stable
10	Tata Finance Ltd.	Finance	NBFC	FA-	FA+	Positive	Stable

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About the CRISIL Ratings Roundup

The CRISIL Ratings Roundup is a semi-annual publication that analyses CRISIL's rating actions during a particular period and the linkages between these actions and underlying economic trends. To the extent that ratings are an opinion on likelihood of future debt repayments, an analysis of a portfolio of debt-ratings that is statistically representative of the economy can be a useful indicator of economic prospects. This edition analyses CRISIL's rating actions in first-half of 2004-05 and compares them with previous periods. The analysis is organized under three broad categories-rating actions, a trend analysis of credit ratios and their linkages to macro-economic factors.