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RM1b wipeout due to downgrades

Players accuse MARC of being 'trigger happy' in downgrading water bonds

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PETALING JAYA: The value of Selangor water bonds has tumbled by RM1bil since last week's downgrades on seven sets of these bonds, with the exception of Viable Chips (M) Sdn Bhd's bank-guaranteed (BG) BaIDS by Malaysian Rating Corp Bhd (MARC).

According to Bond Pricing Agency, data from April 5 (the day the downgrades were announced) to April 6 indicated that as much as RM1.05bil had been wiped off the market value of these bonds, which now mostly carry single, double or triple 'B' ratings instead of the previous single, double or triple 'A' ratings.

Financial institutions holding the bonds will likely suffer a temporary hit when they mark-to-market the losses, which will be reflected in their profit and loss accounts.

However, this can be reversed if the bonds do not default, which according to an industry player, would occur when the equity portion of this financing was wiped off.

"At the moment, the equity holders of the bonds – Syarikat Bekalan Air Selangor Sdn Bhd (Syabas), Syarikat Pengeluar Air Sungai Selangor Sdn Bhd (Splash) and Puncak group – have the money to top up.

"Only when they cannot top up with the equity portion, can we call it a default," said one of the industry players, noting that at the same time, the Selangor government has a RM9bil bid for the water assets while Gamuda Holdings Bhd had offered RM10bil.

"Either way, the bondholders are covered," he said.

In its downgrades of about RM7bil worth of water bonds, MARC had referred to their "increasingly challenged liquidity positions" arising from the unresolved deadlock in talks between the Selangor and Federal governments as well as water concessionaires on the restructuring of water assets in the state.

In their protest of the downgrades, industry players claimed that MARC appeared to be "trigger happy" especially when there were already ongoing restructuring talks and that the rating agency should differentiate between debt and equity (as a default occurs only when equity is gone).

Moreover, they said the downgrades could make investors more cautious of infrastructure financing in the bonds and loans markets.

MARC chief executive officer Mohd Razlan Mohamed rebutted, saying: "We are protecting investors by informing them of the credit and political risks. Since last year, we have placed these bonds on negative watch and warned that we would downgrade if there was no progress in the talks.

"The impact of a bond valuation as a result of a rating agency's rating action is independent from a credit evaluation. We are rating only the debt portion and not the possibility of equity upside; hence, they should also not be confused.

"These investors should also carry out a thorough credit analysis and not expect bonds to carry explicit and implicit government support," said Razlan.

> TURN TO B3

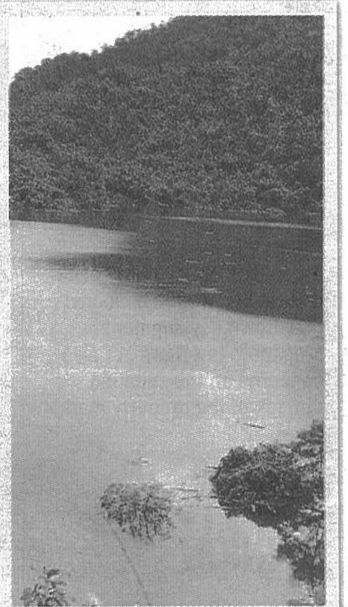
Drop in market value of water-related bonds

(RM mil) *April 5-6, 2011*

Bonds	Market value impact
SYABAS (15 issues)	–487.64
Puncak Niaga Conventional (2 issues)	–118.92
RHSB Conventional *(RUN Holdings Sdn Bhd) (1 issue)	–5.32
Puncak Niaga Islamic (6 issues)	–123.74
Splash (12 issues)	–31.33
Viable Chips (2 issues)	–19.26
Titisan Modal (10 issues)	–266.71
	–1.05bil

Market Impact Value:
Price change multiply by amount outstanding

Source: Bond Pricing Agency



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Banks can withstand bonds impact

> FROM B1

RAM Ratings deputy chief executive officer Foo Su Yin said: "A bond is classified as held-for-trading (HFT), available-for-sale (AFS) or held-to-maturity (HTM) in a bank's books.

"Depending on how a bond is classified, a change in market value has different impact on a bank's financials. A decline in the value of a bond will result in unrealised marked-to-market losses which will either be reflected in the bank's income statement if it is a HFT security, or taken out of the bank's AFS reserves in its shareholders' funds if it is an AFS security. In the event the bond is classified as HTM, there could be impairment charges that the bank has to bear in its income statement.

"The Malaysian banking industry's overall risk-weighted capital adequacy ratio (RWCAR) and total assets stood at 14.3% and RM1.58 trillion respectively as at end-February 2011.

"Even if we were to assume that in the unlikely event that all the water-related bonds outstanding in the industry of RM7.5bil (as at end-March 2011) are held by banks, they only account for 0.5% of the banking industry's total assets.

"On a worst case scenario, if all the bonds were to be fully provided for, we estimate that the industry's RWCAR would decline to 13.6% (based on February 2011 numbers) which is still considered healthy.

"This shows that the banking industry, as a whole, is in a strong position to withstand any potential impact stemming from the water-related bonds," said Foo.