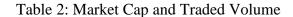


This metadata can be used to sort the news articles in the manner the user wants and get the required score.

The advantage of using only financial news is the realization that financial reporters have limited

Sentiment Score and Returns

One might argue that the raw returns do not specifically suggest whether news-based trading can generate alpha (excess return). Our research has shown that news-based algorithm can help you develop alpha-generating strategies. On a different set of companies and different time period, our proprietary algorithm is used to evaluate whether one can generate alpha using news-based trading strategy. The results (Table 3) are quite encouraging.



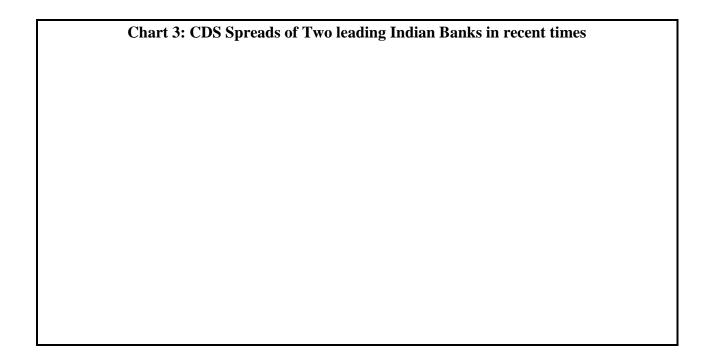
Market cap is in millions of and traded volume is in millions of shares in June 2012 in NSE. Data support by Ms. Priyanka Dasgupta, Assistant Manager, Finance Lab

Partha Ray, Ph.D., is Professor, Economics, Indian Institute of Management Calcutta (IIM-C). Prior to joining IIM-C, Prof. Ray, a career central banker, was the adviser to Executive Director, International Monetary Fund, Washington D.C. during 2007-2011.

Credit Default Swaps (CDS) (equivalently as "CDS spread") "is a bilateral, off-balance sheet agreement between two counterparties in which one party offers the other party protection against a credit event" (like default) in return for a premium payment. Thus, an increase in CDS spread of any entity (like corporate, Sovereign or bank) is indicative of its receding credit worthiness. Of late the CDS spreads of Indian commercial banks are showing some signs of nervousness. Are these in anyway fore-runner of some bad news in the days to come?

Interestingly, the CDS spreads of these banks shot up despite the small or non-existent exposit of Indian banks to the sub-prime toxic assets, originated in the U.S mortgage market.	ure

In such a situation how does the future look like? On a point-to-point basis, over the last one year (i.e., July 2012 over July 2011), the CDS spreads of both the banks have gone up substantially (Chart 3). There are reasons to believe that apart from mildly deteriorating asset quality and global uncertainty, domestic macroeconomic situation could have played a responsible role behind such a phenomenon.



What does it mean for the banking sector and the economy? In any such situation, banks will need capital to tide over any eventual stress. So far, Indian banks at an aggregative level are well-capitalized with capital to Risk weighted Assets Ratio (CRAR) of the banking system at 14.1 per cent as at end March 2012. Notwithstanding such aggregate CRAR, three implications for the Indian banking may be noted. *First*, there are elements of divergence across the banks in the distribution of CRAR; e.g., while the CRAR of the new private banks exceeds 16 per cent, that of the public sector banks is slightly less than 14 per cent. *Second*, it may be noted that the growth of NPAs at 43.9 per cent as at end March 2012 far outpaced credit growth of 16.3 per cent. *Third*, in the flip side, of course, there are reports that CDS spreads for Bank of China and China Development Bank have also surged recently and that they are rising at much faster rates than the rest of Asia excluding Japan.³

But against a perception of weak domestic economy along with heightened global uncertainty, it could be difficult to acquire capital for low credit-worthy banks. As of now it is

Given the Indian legal system's unusual delay in giving appropriate relief to enforce the contract of debt with regard to payment of periodic interest, enforcing collaterals against the debt, bankruptcy, etc. poses serious challenges to attract right kind of investors in the corporate debt market. Corporate Debt Restructuring (CDR) scheme introduced by RBI to bypass the unusual legal delays in judicial system has not been very successful. The insolvency regime is spread over several pieces of legislation and among different course and regulatory bodies and this poses serious challenges and does not sound to be cost effective. Given the regulatory framework at present, serious structural changes and suitable legal reforms are needed to provide a strong legal basis to the Indian debt market. Creating better market infrastructure like technology platforms, clearing corporations, etc. are going to help to some extent but legal framework will address issues from a long term prospective and help creating a robust market place.

Market Liquidity and Depth

Current estimated size of the Corporate debt market in terms of outstanding issuance is about `9.0lakh crores while Government issuance outstanding is about `31.0lakh crores. The corporate bond market has been wary of the large government borrowing program crowding out the corporate bond market and a new SEBI law on rollover of limits limiting FII participation. The government has set the cumulative debt investment limit in corporate bonds (including Infra Bonds) for FIIs at US\$45 billion and at US\$15 billion in government securities. However, there are certain changes to the FII investment rules with regard to limits reuse and this may affect the participation of FIIs in the market.

Most of the issuers of the corporate bonds are typically Public Sector Units – predominantly owned and controlled by Government. These entities find it easier to sell their bonds as they are also perceived as sovereign entities with tacit and perceived guarantee on such borrowings. This provides an immense comfort to the investors with respect to possible bankruptcy that may require higher provisioning. Investing in these entities is a workaround to avoid legal impediments. Major bonds issuances in India are done through private placement route. The private placement route requires little disclosures as the market is confined to qualified institutional investors and cheaper vis-à-vis public issuances. The private placement document is generally a brief document that gives brief details of the issue and the company issuing the bond. The issuers prefer this route as it is far cheaper in terms of cost vis-à-vis public issue. Unlike a prospectus for public issuances, private placement does not require any statutory disclosure. Since bonds are privately placed with institutional investors, the secondary market liquidity is limited as most of the investors generally hold the bonds till maturity as they have already assumed the risk and the bonds are held in the mark to market category of investment (Held for Trading).

During 2011-12, 252 companies raised funds through 2363 bond issuances. The issuance statistics shows that most of the issuances are up to 3 years of maturity (61%). With regard to the rating structure of the issues, the investment grade securities were dominant in the market and higher grade A-class securities (A, AA and AAA) accounted for 84% of the number of

issuances. The issuers do not prefer issuing lower grade securities as the market does not have appetite to absorb these securities. The moot point is the efficient valuation of the lower grade securities in the market.

The absence of varied class of instruments also does not augur well for the market. Bonds with floating rate coupons linked to benchmark rates, embedded options, convertibility clauses, etc. are not very popular in the market. Bank bonds are most preferred by investors as they are considered almost lie sovereign securities as the incidence of bank failures are very rare in India. Hence Bank bonds demand premia for investment. Trading in corporate bonds concentrated in AAA rated bonds which accounts for 89% (81% of deals – multiple deals in same bond) and 99% of the total deals were in the first 3 A group rated securities (A, AA and AAA). Issuers and investors concentrate only on high rated securities and hence market almost non-existent for lower rated bonds in India.

Need of the Day