

Sovereign Credit Risk and the Cost of COVID

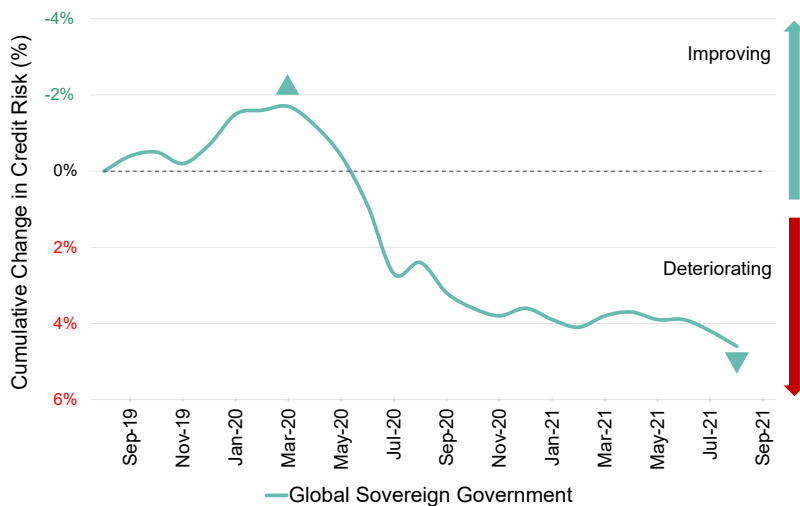
September 2021

The risk of a US Government shutdown is focusing attention on Sovereign credit risk. While various sleights of hand (such as daily changes to bond maturities) are possible, there remains a small but significant risk to US Treasury bond payments in October. A missed payment – even if it is only deferred – would be a major market event. S&P famously downgraded the US to AA+ in 2011 under similar circumstances, and it has never moved it back. Fitch currently have a negative outlook on their AAA rating for the US.

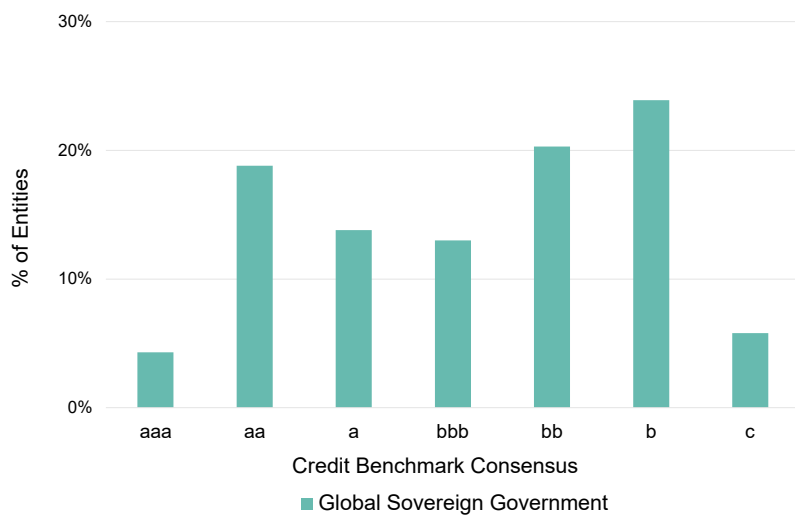
But the broader issue is how Governments around the world handle the cost of COVID.

Figure 1 shows trends in Sovereign credit risk over the past 2 years.

Figure 1: Sovereign Credit Risk trends



Source: Credit Benchmark



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A short, steep decline at the start of the pandemic has been followed by a more gradual but persistent deterioration. Global Sovereign credit risk is now about 6% higher than it was 18 months ago – enough to push some countries into the non-investment grade category. Over the past 12 months, 64 countries have seen some deterioration in their consensus rating.

The Sovereign credit distribution is unusual, compared with the more typical bell-shaped distribution seen in Corporate borrowers. There are two peaks – one in the **aa** category, and one in the **b** category. Less than 15% of the consensus ratings for Sovereigns are in the **bbb** category, compared with more than 25% for Corporates.

Figure 2 shows the current consensus ratings and the S&P equivalents for the G7 and BRICS countries.

Figure 2: G7 and BRICS Sovereign ratings

Country	Consensus	S&P	Notes
Canada	aa+	AAA	One higher risk estimate
France	aa	AA	
Germany	aa+	AAA	
Italy	bbb	BBB	
Japan	aa-	A+	
UK	aa	AA	
USA	aa+	AA+	Fitch: AAA Negative Outlook
Brazil	bb	BB-	
China	a+	A+	
India	bbb-	BBB-	One higher risk estimate
Russia	bbb-	BBB-	One higher risk estimate
South Africa	bb	BB-	bb+ in March 2020

Compared with S&P, two of the consensus ratings are conservative, three are more positive, and the remaining seven are aligned. South Africa is the only country with a full notch consensus downgrade since the start of the pandemic; the other countries show some variation but are broadly stable. However, three countries – Canada, India and Russia – have at least one estimate making up the consensus that is significantly higher risk than the main set of contributions. This lack of agreement may indicate a risk of downgrades in the future.

The consensus dataset includes 122 countries; detailed risk estimates in 21 and 100 categories are now available on Bloomberg (CRDT <GO>).

About Credit Benchmark

Credit Benchmark brings together internal credit risk views from 40+ of the world's leading financial institutions. The contributions are anonymized, aggregated, and published in the form of entity-level consensus ratings and aggregate analytics to provide an independent, real-world perspective of risk. Consensus ratings are available for 60,000 financials, corporate, funds, and sovereign entities globally across emerging and developed markets, and 90% of the entities covered are otherwise unrated.

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