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SOVEREIGN RISK RATINGS FORECASTS FOR 2010 FROM IHS GLOBAL INSIGHT

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Investors are on high alert for sovereign risk ratings in 2010, with concerns highlighted by the recent financial turmoil in Dubai and Greece. Public finances in many countries are under tremendous pressure after government efforts last year to arrest the freefall in the global economy through slashing interest rates, while weaker tax revenues and higher public spending are raising debt burdens.

The greatest challenge in 2010 will be the timing of the withdrawal of these support strategies: exit too soon and the economy could relapse; exit too late and public finances could deteriorate even further. Public finances have deteriorated nearly everywhere, but the situation is more bearable in some countries than in others, with ratings staying in the spotlight.

1 ASIA AND LATIN AMERICA TO LEAD THE POSITIVE SOVEREIGN RISK RATINGS TURNAROUND.

Globally, sovereign ratings finally stopped deteriorating by mid-2009, and a positive turnaround has been led by Asia and the healthier parts of Latin America—notably Brazil, which was upgraded in 2009. These trends will continue into 2010. The West, Eastern Europe, the Commonwealth of Independent States (CIS), and Central America and Caribbean will generally lag due to heavier debt burdens and slower economic recovery. Negative rating actions began to outpace positive actions two years ago at an accelerating pace and hit a peak ratio of 8:1 by first-quarter 2009. Only in third-quarter 2009 did the credit crunch and global recession-induced negative ratings tide finally subside and reverse.

2 EASTERN EUROPE AND CIS RATINGS TO REMAIN DEPRESSED.

Eastern Europe and the CIS have seen the worst ratings falls globally, but the downside risks will abate in 2010 as economic adjustment takes place. Any improvement in ratings will be unlikely in the short-term as most economies in these two regions will need to continue this painful adjustment process to accommodate lower external capital flows and private-sector debt deleveraging. The exception is Poland (see below). The key potential for event risk remains in the Ukraine and the Baltics.

3 NO DEFAULT FOR GREECE OR ANY EUROZONE SOVEREIGN IN 2010.

There will be no sovereign default in the Eurozone in 2010, not even for Greece, which has the weakest Eurozone public finances. Peer group pressure from other Eurozone governments to rectify public finances is generally underestimated, and will necessitate painful fiscal adjustments. But as Greece's economy represents only 3% of the Eurozone's GDP, its problems are relatively small in scale and can be ring-fenced and more easily managed.

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4 OTHERS LIKELY TO FOLLOW IHS GLOBAL INSIGHT'S LEAD IN DOWNGRADING ICELAND TO SPECULATIVE GRADE IN 2010.

Other ratings agencies are likely to follow IHS Global Insight's lead in placing Iceland's sovereign risk in speculative grade. The refusal by Iceland's president to sign a parliament bill to repay the U.K. and Dutch governments for savings in failed Icelandic banks highlights Iceland's continued financial fragility.

5 U.S. AND U.K. SOVEREIGN RATINGS ARE SLIPPING BUT NOT ENOUGH TO TRIGGER NEGATIVE RATING ACTIONS IN 2010.

Among leading Western sovereigns, debt ratios have worsened the most in the U.K. and U.S. where tax revenues had been heavily dependent on property and financial-sector activity—the two sectors worst hit by the credit crunch and recession. Net public debt ratios in these two countries will roughly double to 80–90% of GDP over the credit crunch period. While the triple AAA sovereign ratings of the U.K. and U.S. are slipping, the declines are so far not sufficient to trigger a switch to a negative outlook, let alone an actual rating downgrade. The United Kingdom faces a particular political constraint to its rating involving fiscal policy uncertainty, given that general elections need to take place by early-June 2010.

6 DUBAI SOVEREIGN RISK HAS BEEN OVERSTATED.

Dubai's sovereign risk has been overblown, as neighboring and much wealthier emirate Abu Dhabi was always eventually going to come to Dubai's rescue. Abu Dhabi will continue to support the needs of Dubai's government, but not necessarily the Dubai state's commercial investments. IHS Global Insight has maintained the UAE sovereign risk stable at AA throughout the Dubai crisis, but this is contingent on successful corporate restructuring in Dubai.

7 BRAZIL'S SOVEREIGN RATING COULD RISE AGAIN IN 2010.

Brazil could be upgraded again in 2010. Of the leading Emerging Nations—the so-called BRICS (Brazil, Russia, China, and India)—Brazil is the most likely to be upgraded, if not in 2010, then 2011. New oil-sector development could well propel Brazil into "Net Creditor Nation Status" over the medium term and higher up the investment rating rungs. Turkey has also survived the credit crunch relatively well and could receive a further upgrade in 2010.

8 POLAND'S RATING PROMISING FOR NEXT UPGRADE IN EASTERN EUROPE.

Poland could well receive a positive rating action in 2010. Poland was the only sizeable country in the European Union to avoid recession in 2009. Its currency depreciation and moves by the new Western-oriented government to steer fiscal and other policy towards the requirements for Eurozone entry puts it in a good position for an upgrade in 2010.

9 UGANDA AND GHANA RATINGS EDGING UP.

In Africa, Uganda and Ghana may be in line for upgrades in 2010. In both cases this will be due to new oil finds, but a contributing factor for Ghana will be its relatively robust democratic system.

10 ENERGY EXPORTERS UNLIKELY TO BENEFIT RATINGS IN 2010 DESPITE CASH BOOSTS.

Larger established oil producers are unlikely to see upgrades despite likely improvements in oil prices due to the recovery in the global economy, as sovereign balance sheets in many of these countries—including Russia, Venezuela, and major Middle East states—have been tapped heavily to support growth in 2008 and 2009.

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