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S&P Downgrades Russia's Sovereign Credit Rating to Junk

By The Moscow Times

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People walk past a board showing currency exchange rates in Moscow on Monday.

Ratings agency S&P has cut Russia's sovereign credit rating to junk status, bringing it below investment grade for the first time in a decade.

Warning of difficult times ahead for Russia's economy, S&P said Monday that it had cut the rating from BBB- to BB+ and that Russia's economic growth prospects, hit by low oil prices and Western sanctions over the Ukraine crisis, had worsened.

The ruble weakened to 68.65 against the dollar , more than 6 percent lower than the previous close on the Moscow Exchange, and the cost of insuring Russian sovereign debt for five years rose, in a sign of investors' concern.

"The downgrade throws into stark relief the severity of Russia's financial and economic crisis," said Nicholas Spiro, managing director at Spiro Sovereign Strategy in London.

"It's going to make it more difficult for large corporates and banks to refinance themselves, at a time when ratings agencies clearly have doubts about the macroeconomic and external environment for Russia."

The decision could not only harm Russia's image among investors but push up its borrowing costs, as many mainstream investment and pension funds have rules preventing them from buying anything not classed as investment grade.

Other rating agencies could follow suit by downgrading Russian sovereign debt to what some consider junk territory, and there could eventually be a political impact on President Vladimir Putin if the economic crisis keeps worsening.

But Finance Minister Anton Siluanov played down the situation.

"The decision taken shows the excessive pessimism of the agency. It fails to consider a series of factors which characterize the strong side of the Russian economy: the accumulation of large international reserves, including in the sovereign funds," he said.

He said capital markets had factored in the downgrade and it should have no "serious additional effects" on them.

S&P had warned, in late December, that it could deprive Russia of its investment-grade credit rating as soon as mid-January, following a rapid deterioration of the country's monetary flexibility and a weakening economy.

More Sanctions?

Russia's economy is expected to slide into recession this year as low oil prices depress export revenues, and the sanctions over Ukraine cut some of its biggest companies off from Western funding.

Putin, whose popularity rests partly on bringing financial wellbeing to many Russians, said shortly before the downgrade that his government was close to announcing details of an anti-crisis plan to maintain social stability and protect growth.

But S&P said in a statement it saw growth flatlining for four years, projecting about 0.5 percent annually in 2015-2018, below the 2.4 percent of the previous four years.

French Finance Minister Michel Sapin said the downgrade showed sanctions were taking a toll and urged Moscow to use this as an opportunity to change tack on Ukraine.

"Sanctions were taken because Russia has an attitude towards Ukraine which we consider unacceptable," Sapin told reporters after a meeting of euro-zone finance ministers in Brussels.

The Central Bank said last month Russia's economy may shrink 4.5-4.7 percent in 2015 and 0.9-1.1 percent in 2016, if oil averages $60 a barrel. If oil was at an average of $40 a barrel, the economy could shrink by 5 percent over the course of 2015, according to the Ministry of Economic Development.

"I guess if you were thinking of buying Russia risk, again, last week, you have now got your answer. Too early," said Standard Bank analyst Tim Ash after the downgrade.

The U.S. and the European Union have threatened to impose more sanctions following new violence in Ukraine though Putin blames it on Kiev.

In addition, capital flight soared last year and rising inflation is likely to compound pressures on the ruble.

Russia's international reserves, managed by the Central Bank, have collapsed since early last year, falling to their lowest level since early 2009 as Russia has been forced to spend heavily to defend the ruble.

The ruble fell about 40 percent against the U.S. dollar last year and has continued its decline this year.

"In a sense there is nothing new here. Russia's economic vulnerabilities have been clear for all to see over the past year, and a downgrade — or at least the problems that S&P cited — are surely now priced into the market," said Neil Shearing, chief emerging markets economist at Capital Economics.

"However, the loss of investment grade status is symbolic insofar as it underlines Russia's economic decline. The outlook remains grim."

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