S&P Global
Ratings

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Research Update:

Ukraine FC Rating Lowered To 'CCC' On Debt Restructuring Plan; Outlook Negative; 'CCC+/C' LC Ratings Affirmed

April 6, 2023

Overview

- The Ukrainian government has announced a plan to restructure its external debt by midyear 2024.
- We therefore consider it likely that Ukraine will enter a distressed exchange on its external commercial obligations without an unforeseen positive development.
- As a result, we lowered our long-term foreign currency rating on Ukraine to 'CCC' from 'CCC+'.
- At the same time, we affirmed our 'C' short-term foreign currency, 'CCC+/C' local currency, and 'uaBB' national scale ratings on the sovereign. We understand Ukraine's hryvnia-denominated government debt is not in scope for the debt restructuring plan.
- The outlook on the foreign-currency rating is negative and that on the local-currency rating is stable.

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Rating Action

On April 6, 2023, S&P Global Ratings lowered its foreign currency (FC) long-term sovereign credit and issue ratings on Ukraine to 'CCC' from 'CCC+'. The outlook on the long-term sovereign FC rating is negative. At the same time, we affirmed our 'C' short-term FC rating and our 'CCC+/C' local currency (LC) long- and short-term sovereign credit ratings on the sovereign. The outlook on the long-term LC rating is stable. We also affirmed our national scale rating at 'uaBB' and our transfer and convertibility assessment remains 'CCC+'.

As "sovereign ratings" (as defined in EU CRA Regulation 1060/2009 "EU CRA Regulation"), the ratings on Ukraine are subject to certain publication restrictions set out in Art 8a of the EU CRA Regulation, including publication in accordance with a pre-established calendar (see "Calendar Of 2023 EMEA Sovereign, Regional, And Local Government Rating Publication Dates," published Dec. 22, 2023, on RatingsDirect). Under the EU CRA Regulation, deviations from the announced calendar are allowed only in limited circumstances and must be accompanied by a detailed explanation of the reasons for the deviation. In this case, the reason for the deviation is Ukraine's announcement of a government debt restructuring plan. The next scheduled publication on the Ukraine sovereign rating is Sept. 8, 2023.

Outlook

The negative outlook on the FC long-term rating reflects risks to Ukraine's commercial debt service, given the government's debt restructuring plan.

The stable outlook on the LC long-term rating balances increased fiscal pressures against the government's incentives to service hryvnia-denominated debt to avoid distress to domestic banks, which are the primary holders of LC bonds.

Downside scenario

We could lower the FC ratings in the next 12 months if, for instance, we consider it a virtual certainty that commercial debt obligations will be included in the government's debt restructuring. We could lower the LC ratings if we see indications that Ukrainian-hryvnia-denominated obligations could suffer nonpayment or restructuring.

Upside scenario

We could raise the FC rating if commercial debt was excluded from the proposed restructuring, for example, due to significantly improved economic outcomes and a favorable debt sustainability assessment by the IMF.

Upward pressure on the ratings could arise if Ukraine's security environment and medium-term macroeconomic outlook improve.

Rationale

The rating action follows Ukraine's official announcement that it will restructure its foreign currency external debt to restore public debt sustainability, as part of the recently agreed, four-year, $15.6 billon Extended Fund Facility arrangement with the IMF. Ukraine is suffering from significant macroeconomic and fiscal pressures triggered by the ongoing war with Russia. We understand that the parameters and timing of the restructuring have yet to be decided and are contingent on the IMF's assessment of public debt sustainability, which is expected to be updated in early 2024.

Official creditors, including the U.S., U.K., Canada, France, Germany, and Japan (the Group of creditors of Ukraine [CGU]), have agreed to an extension of the deferral of external debt payments until the end of the IMF program in 2027, from the previously agreed period of August 2022 until September 2024.

The CGU also agreed to an additional debt restructuring, which we expect to take place by midyear 2024. This agreement is subject to private external creditors delivering a debt restructuring at least as favorable. However, the potential restructuring will take place more than one year from now and the development of the war in Ukraine remains uncertain. To that end, visibility on the exact scenario for commercial creditors will increase only next year.

That said, bilateral debt represents a small 5% of total government debt. Given our understanding that multilateral and domestic government debt (both in LC and FC) are excluded from the debt restructuring plans, there is, in our view, a relatively high probability that a meaningful debt relief exercise will include Ukraine's commercial external debt outstanding. The latter represents about 20% of total government debt, with another 40% constituting domestic-law bonds (both in LC and FC) and 35% from international financial institutions.

Our ratings reflect our view of an issuer's ability and willingness to meet its commercial, nonofficial financial obligations in full and on time. If the commercial debt restructuring takes place in 2024, in light of protracted balance-of-payments and fiscal challenges, we would likely view it as distressed (see "S&P Global Ratings Definitions," published Nov. 10, 2021, and "Ukraine FC Rating Lowered To 'SD' On Approved Debt Restructuring; LC Rating Lowered To 'CCC+' With Negative Outlook," published Aug. 12, 2022, on RatingsDirect).

In our view, the government's ability and medium-term incentives to meet its financial commitments in LC are somewhat higher than those in FC. Hryvnia-denominated debt is primarily held by domestic banks, half of which are state-owned. A default on these LC obligations would amplify banking sector distress, increasing the likelihood that the government would have to provide the banks with financial support, which would limit the benefits of debt relief.

Ukraine's medium-term macroeconomic outlook depends heavily on the duration and evolution of the war. Our base-case assumption is that there will not be a near-term end to hostilities. Given substantial damage to physical and human capital, Ukraine's growth prospects--and its balance-of-payments and fiscal positions--hinge on continued international financial support, access to export routes via the Black Sea, the persistence of war-driven dislocations on the labor market, the restoration of tax mobilization capacity, and reconstruction efforts.

S&P Global Ratings notes a high degree of uncertainty about the extent, outcome, and consequences of the Russia-Ukraine war. Irrespective of the duration of military hostilities, related risks are likely to remain in place for some time. As the situation evolves, we will update our assumptions and estimates accordingly. See our macroeconomic and credit updates here: Russia-Ukraine Macro, Market, & Credit Risks.

Related Criteria

- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021
- General Criteria: Methodology For National And Regional Scale Credit Ratings, June 25, 2018
- Criteria | Governments | Sovereigns: Sovereign Rating Methodology, Dec. 18, 2017
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- General Criteria: Guarantee Criteria, Oct. 21, 2016
- General Criteria: Criteria For Assigning 'CCC+', 'CCC', 'CCC-', And 'CC' Ratings, Oct. 1, 2012
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011
- General Criteria: Methodology: Criteria For Determining Transfer And Convertibility Assessments, May 18, 2009

Related Research

- Ukraine Banking Sector 2023 Outlook: Regulatory Support Is Crucial To Navigate The War, March 20, 2023
- Sovereign Ratings List, March 15, 2023
- Sovereign Ratings History, March 15, 2023
- Sovereign Ratings Score Snapshot, March 2, 2023
- Sovereign Risk Indicators, Dec. 12, 2022. Interactive version available at http://www.spratings.com/sri
- 2021 Annual Global Sovereign Default And Rating Transition Study, May 4, 2022
- S&P Global Ratings Definitions, Nov. 10, 2021

In accordance with our relevant policies and procedures, the Rating Committee was composed of analysts that are qualified to vote in the committee, with sufficient experience to convey the appropriate level of knowledge and understanding of the methodology applicable (see 'Related Criteria And Research'). At the onset of the committee, the chair confirmed that the information provided to the Rating Committee by the primary analyst had been distributed in a timely manner and was sufficient for Committee members to make an informed decision.

After the primary analyst gave opening remarks and explained the recommendation, the Committee discussed key rating factors and critical issues in accordance with the relevant criteria. Qualitative and quantitative risk factors were considered and discussed, looking at track-record and forecasts.

The committee's assessment of the key rating factors is reflected in the Ratings Score Snapshot above.

The chair ensured every voting member was given the opportunity to articulate his/her opinion. The chair or designee reviewed the draft report to ensure consistency with the Committee decision. The views and the decision of the rating committee are summarized in the above rationale and outlook. The weighting of all rating factors is described in the methodology used in this rating action (see 'Related Criteria And Research').

Ratings List

Downgraded

	To	From
Ukraine		
Senior Unsecured	CCC	CCC+
State Road Agency of Ukraine (Ukravtodor)		
Senior Unsecured	CCC	CCC+

Downgraded; Ratings Affirmed

	To	From
Ukraine		
Sovereign Credit Rating		
Foreign Currency	CCC/Negative/C	CCC+/Stable/C
Ratings Affirmed		
Ukraine		
Sovereign Credit Rating		
Local Currency	CCC+/Stable/C	
Ukraine National Scale	uaBB/--/--	
Transfer & Convertibility Assessment	CCC+	
Ukraine		
Senior Unsecured	D	