The Barbados Economics Society

Response to Barbados' recent Credit Rating Upgrade

Sentiments of the BES President, Mr. Shane Lowe

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Summary

On November 16th, 2018, Standard and Poor's (S&P) upgraded its rating on Barbados' local currency debt from 'SD' (Selective Default) to 'B-'. Although this action represents a positive development for the country, reflecting improved capacity to service newly-exchanged debt at lower interest rates and longer maturities, it is not surprising as, in their previous rating action, S&P indicated that they could increase the government's rating to "…the 'CCC' or low 'B' categories." A rating of 'B-' is on par with the level last seen in early-2017 and is one notch lower than Jamaica's 'B' rated long-term, local currency debt rating. However, this rating for Barbados remains several notches below investment grade and thus our debt will still be characterized as 'speculative-grade' or 'junk'.

Nonetheless, as long as the government remains on track with the targets set under the BERT programme, the rating itself will not likely influence the government's interest costs or capacity to obtain local financing in the near-term given the IMF's projections that the government will not borrow from private, domestic creditors over the next four years. The Central Bank of Barbados' recent decision to reduce the securities reserve requirement for commercial banks from 20.0% of domestic deposits to 17.5% of domestic deposits supports this. In fact, a need to borrow substantial amounts from private, domestic creditors over the next four years may imply that the government has fallen off track

The Barbadian economy's local currency debt was upgraded from 'SD' (Selective Default) to 'B-' by the regulatory agency, Standard and Poor's.

with its programme altogether. At no time over the life of the IMF-financed BERT programme is this desirable.

Of utmost importance in the medium-term is the rating on Barbados' foreign currency debts. This rating will likely remain at default until negotiations with external creditors are completed. The pace of future rating upgrades on foreign currency debt will determine how quickly the Government of Barbados can regain access to international capital markets should the need arise once the 4-year financing programme with the IMF ends. However, as evidenced in Jamaica, the pace of restoring the credit rating to investment grade status (BBB- or higher) even after substantial debt reduction and multiple, consecutive years of large primary surpluses can be very slow. Further, empirical research (see for example Catão and Mano, 2017) suggests that investors charge countries that default on their external debt a higher interest rate premium (a so-called "default premium") than those that do not. Similarly, the extent of losses incurred by investors may also determine the size of the premium paid by countries that default and the length of time they are excluded from international, commercial borrowing (Cruces and Trebesch, 2013). Cruces and Trebesch (2013) suggest that "the size of haircuts is a significant predictor of spreads for up to seven years after a restructuring..." (Cruces and Trebesch, 2013) while Catão and Mano (2017) suggest that the default premium "…accounts for between 30% and 60% of the market spread within five years after settlement with creditors…" (Catão and Mano, 2017). Thus, notwithstanding any future improvements in the credit rating, the IMF's latest Staff Report issued on October 4th, 2018 suggests that the Government of Barbados will likely preclude itself from borrowing on the global capital market for at least the next 4 years as investors' perceptions about the government's willingness and ability to stay current on its new debt obligations will likely slowly improve.

Bibliography

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