

Latam Daily: Delay on Fiscal Reform Prompted S&P to Cut Colombia Rating

- Colombia: S&P downgraded Colombia's credit rating from BBB- to BB+, one notch below investment grade; the outlook shifted from "Negative" to "Stable"

COLOMBIA: S&P DOWNGRADED COLOMBIA'S CREDIT RATING FROM BBB- TO BB+, ONE NOTCH BELOW INVESTMENT GRADE; THE OUTLOOK SHIFTED FROM "NEGATIVE" TO "STABLE"

On Wednesday, May 19, S&P decided to cut Colombia's credit rating from BBB-, the bottom threshold of investment grade, to BB+, with the outlook shifted from "Negative" to "Stable" as is typical following a downgrade (table 1). The move was prompted by the withdrawal of the government's initial fiscal reform proposal and its re-negotiation, which is likely to make Colombia's adjustment process more gradual than previously anticipated. Under S&P's estimates, the previous scenario would have led to the stabilization of the debt burden at around 60% of GDP, which, according to S&P, is not consistent with the BBB group. On the other hand, the shift of the outlook to "Stable" was not solely mechanical, but likely also reflected expectations of ongoing economic recovery, the country's response to recent social unrest, and anticipation of eventual agreement on an adjustment package.

The timing of S&P's announcement was somewhat unexpected since it had affirmed Colombia's investment-grade rating and "Negative" outlook on April 22, 2021, after the unveiling of the government's fiscal-reform proposal (see our April 23 [Latam Daily](#)). However, given the political and social opposition that greeted the proposal, and pressures on the government to increase spending, the prospects for an adequate stabilization package had become more complicated in S&P's view.

The credit-rating agency emphasized that a positive revision could follow if Colombia's 2021 growth tracks more strongly than the 6.0% y/y that S&P forecasts for 2021 (table 1, again).

Our take: S&P's move should be read as an emphatic call to the government and stakeholders to reach an agreement on fiscal reform. In the communiqué, Colombia's tradition of solid and prudent economic institutions wasn't emphasized, which in past reviews was noted as a key factor in the maintenance of Colombia's investment-grade rating.

Table 1

Colombia: LT sovereign credit rating profile

Agency	Rating	Outlook	Last revision	Real GDP, y/y change, 2021f
S&P	BB+	Stable	May 19, 2021	6.0%
Fitch	BBB-	Negative	November 6, 2020	4.9%
Moody's	Baa2	Negative	December 3, 2020	5.0%

Sources: Scotiabank Economics, S&P, Fitch, Moody's.

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The S&P announcement may add some volatility to Colombian asset prices, but a downgrade scenario was already partially priced in. The sovereign yield curve is now the steepest it's been since the aftermath of the 2008 global financial crisis, while USDCOP remains significantly off our model-based view of fundamental value owing to recent domestic uncertainty in Colombia.

—Sergio Olarte & Jackeline Piraján

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