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CORPORATE SECTOR | RUSSIA

RESEARCH

THE RUSSIAN DEBT MARKET HAS STOOD ITS GROUND AGAINST NEW RISKS

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- **The rapid stabilization of the domestic political situation after the events of late June 2023 helped minimize the negative impact on the bond market** in terms of both yields of bonds and issuers' plans to place them.
- **Each credit rating notch increase in April to June 2023 led to the risk premium declining by 40 bps on average** — a twofold reduction compared to September 2022.
- **In all rating categories, G-spreads for bonds with durations of up to one and a half years have halved compared to September last year,** while for those with durations of one and a half to three years they have declined by 1.2–1.5 times. There was no significant revaluation of bonds with durations of three to five years, with the exception of high-yield bonds rated BB–B.
- **In the sample of bonds with a lower rating category (BBB), G-spreads increase with duration, while the G-spreads for bonds with high credit rating categories (AAA–AA) on the contrary, decrease as duration increases.** These dynamics are explained by the fact that investors are likely to be more interested in long-term issues, which allow them to receive higher yields due to the current slope of the OFZ curve.

G-SPREADS IN H1 2023

For the purposes of its analysis of the situation in the bond market, ACRA has used a G-spread that is calculated as the difference between the bond yield and the yield for a point on the zero-coupon yield curve for government securities with the same duration. The G-spread shows the credit risk premium of a certain issue, while the widening or narrowing of the spread indicates revaluation by investors of the credit risk of bonds relative to government obligations.

See ACRA's research Will the Debt Market Be Able to Recover Quickly Again? from October 19, 2022 for more information on the first period.

The Agency analyzed the values of G-spreads[1] for two periods during which there were events that could lead to a significant increase in yields in the bond market. The first period was September 2022 when partial mobilization was announced; the second was from April to June 2023, at the end of which the domestic political situation was exacerbated. The analytical sample included issuers and issues with credit ratings assigned by ACRA and/or Expert RA[2].

After a surge in activity in the debt market at the end of 2022, the number and volume of placements have been declining over the past few months.

From January to June 2023, the number of placements and volumes of transactions considerably exceeded the indicators for the same period in 2022. This was anticipated and the result of both a recovery of economic activity of companies in the Russian market and the Bank of Russia lowering of its key rate (following growth of uncertainty amid shocks at the start of 2022). In March and April 2023, 230 corporate bond issues were placed to a total of around RUB 880 bln (during this period in 2022, 19 new corporate bond issues were placed to a total of RUB 13 bln). As of the end of

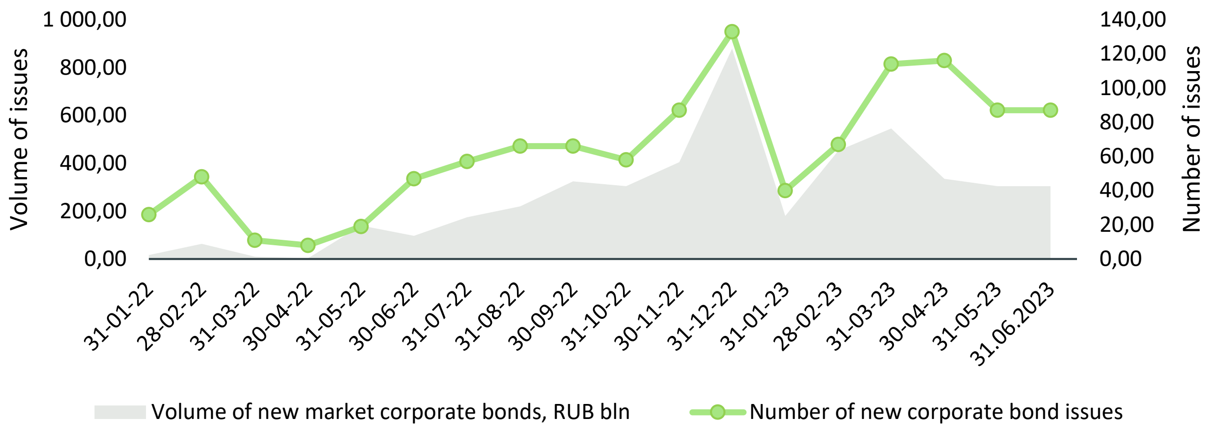
[1] The analysis excludes G-spread outliers.

[2] Data on issuers and issues with ACRA and Expert RA credit ratings under the national scale were used in order to cover the market more widely. ACRA's ratings were used if an issuer or issue had credit ratings from both agencies.

Credit ratings were combined using the following categories to demonstrate data on graphs: category AAA–AA includes ratings from AAA to AA-, category BBB includes ratings from BBB+ to BBB-, category BB–B includes ratings from BB+ to B-.

June 2023, the volume of new corporate bonds placed was RUB 610 bln (six times higher than in the same period the year before), and the number of new issues increased to 131.

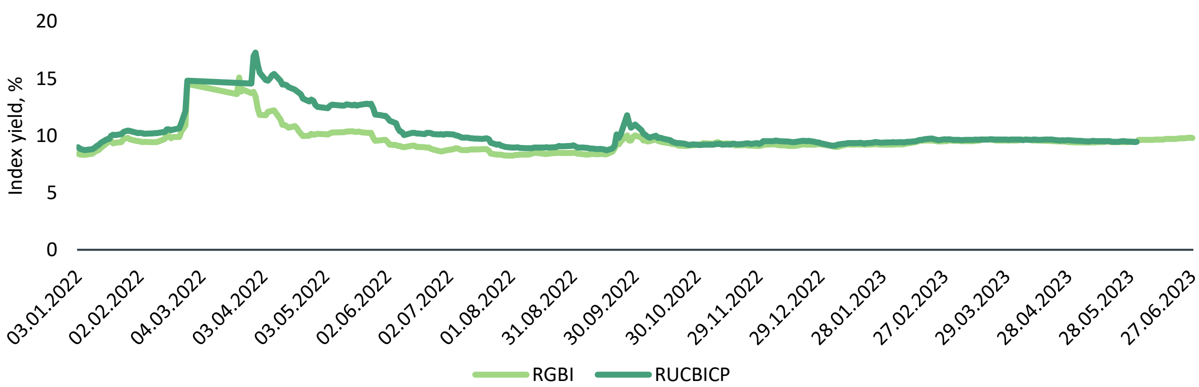
Figure 1. Number and volume of placement of new market issues of corporate bonds



Source: Cbonds

Given the strengthening of inflationary pressure and the possible, in ACRA's opinion, increase of the key rate, over the next few months the Agency does not expect significant growth of activity in the Russian bond market in terms of the number and volume of placements (excluding replacement bonds). At the same time, it is worth noting that the events of June 2023 did not lead to substantial adjustments of issuers' plans to enter the bond market and did not have much impact on their yields.

Figure 2. Indices for corporate (RUCBICP) and government (RGBI) bonds on the Moscow Exchange[3]



Source: Moscow Exchange

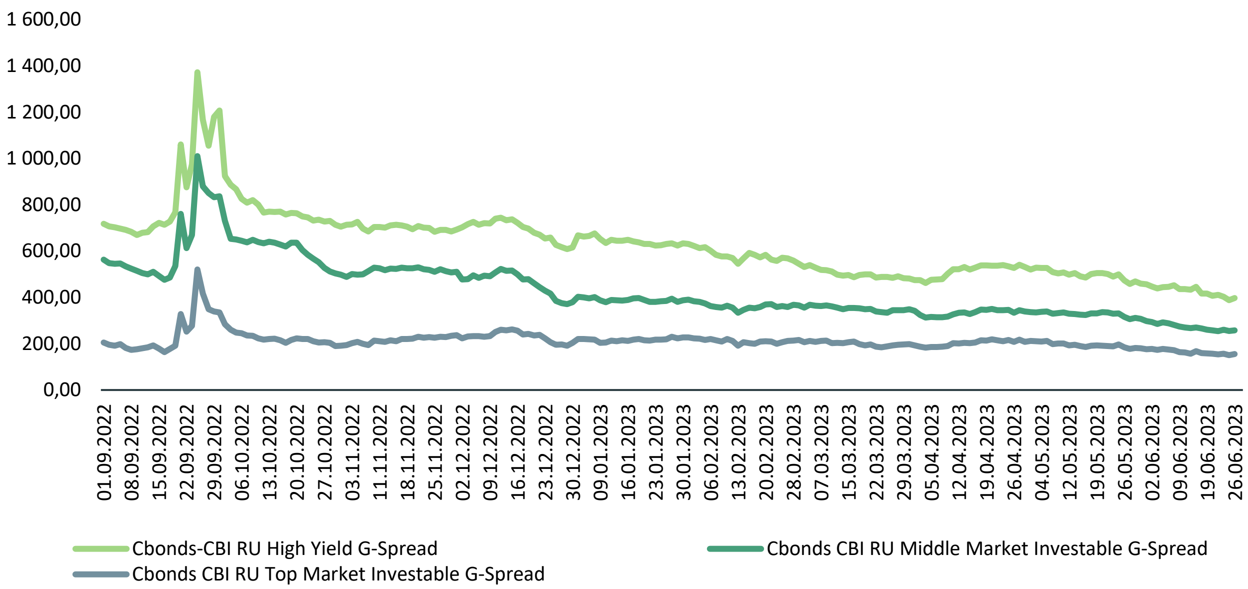
After the peak values of G-spreads recorded in September 2022, the yield indices[4] for bonds with high credit quality (Top Market Investable), bonds of the middle market (Middle Market Investable), and high-yield corporate bonds (High Yield) have stabilized at the achieved levels since the beginning of the year. Over the past three months, risk premiums for bonds of the highest quality issuers averaged 188.6 bps (-57 bps vs. September 2022), the G-spread of bonds of the middle market was 313 bps (-311 bps vs. September 2022), and the average risk premium of high-yield bonds was

[3] The calculation base of the Moscow Exchange Corporate Bond Index (RUCBICP) includes the most liquid bonds of Russian borrowers admitted to trading on the Moscow Exchange with durations of more than a year.
The calculation base of the Moscow Exchange Government Bond Index (RGBI) includes the most liquid federal loan bonds with durations of more than a year.

[4] The Cbonds CBI RU Top Market Investable reflects the market of liquid Russian corporate bonds with credit ratings ranging from A to AAA (inclusive).
The Cbonds CBI RU Middle Market Investable reflects the middle market of liquid Russian corporate bonds, which includes securities of issuers with credit qualities from BB+ to A+ (inclusive).
The Cbonds-CBI RU High Yield Index reflects the Russian market of high-yield corporate bonds.

484 bps (-370 bps vs. the average for September 2022). The exacerbation of the domestic political situation at the end of June this year did not lead to a significant reassessment of yields: on June 23 and 26, the average G-spread on bonds with high credit ratings amounted to 153 bps, in the middle bond market it was 256 bps, and for highly profitable bonds it was 393 bps (which is lower than the average values of these indices for June by 11, 16, and 35 bps, respectively). It seems that these dynamics were due to the rapid stabilization of the domestic political situation, which became more complicated over the weekend.

Figure 3. Dynamics of G-spreads by categories of issuers



Source: Cbonds

The current G-spreads for bonds of non-financial companies by rating categories and duration categories compared to September 2022 are given in *Fig. 4*.

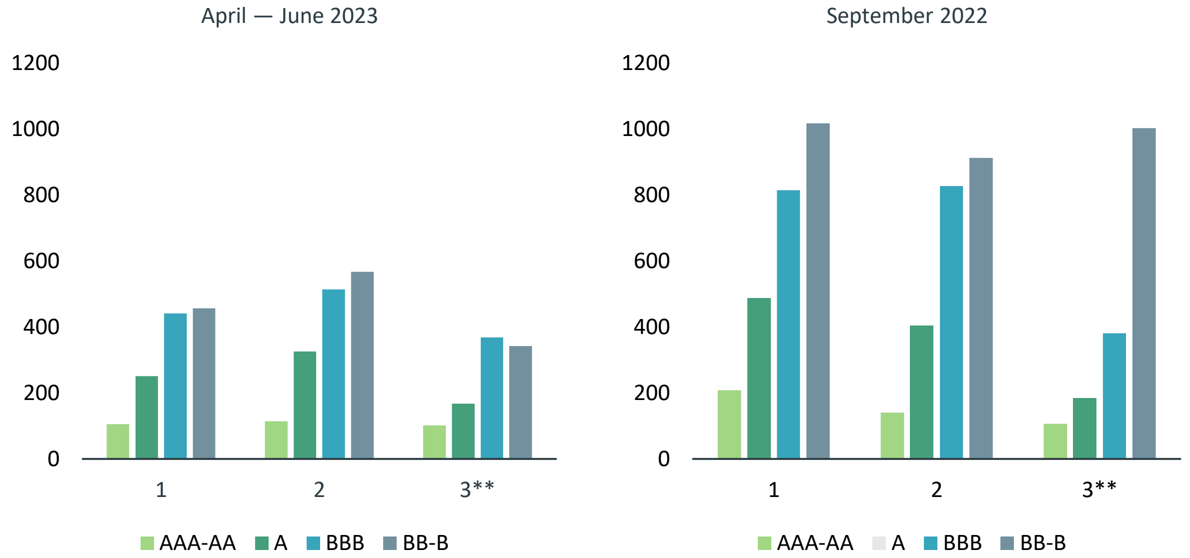
The risk premiums in the rating categories AAA–AA stabilized at 100–115 bps for all duration categories over the past three months. The values of G-spreads of these rating categories for bonds with durations of less than one and a half years have halved (from 209 bps in September 2022 to the current 106 bps), while in the second and third duration categories, the decrease in spreads is not so significant — by 25 bps and 4 bps, respectively. At the same time, in contrast to September last year, in April–June this year, risk premiums for bonds with durations of one and a half to three years turned out to be higher than for issues with durations of less than one and a half years.

A similar picture was seen in rating category A: G-spreads for bonds with durations from one and a half years to five years fell by 48 bps on average, while risk premiums fell by almost half — from 488 bps in September to the current 250 bps for bonds with durations of up to one and a half years.

In the BBB rating category, credit risk premiums for bonds with durations of up to three years declined on average by 345 bps compared to September 2022.

The most significant decline in risk spreads took place for bonds rated BB–B, where G- spreads changed by 520 bps on average. In September 2022, the risk premium for them ranged from 900 to 1,000 bps, and has now declined to 350–550 bps depending on duration.

Figure 4. G-spreads for bonds of non-financial companies in April–June 2023 and September 2022 broken down by rating category and duration category*



* Duration category: 1 — less than one and a half years, 2 — less than three years, 3 — less than five years.
** Duration category 3 includes a limited number of observations for all rating categories except AAA–AA.
Sources: Cbonds, ACRA

In September 2022, each credit rating notch increase corresponded to an average decrease in the risk premium by 85 bps, while in April–June 2023, it resulted in a decrease in the credit spread by an average of 40 bps. As shown in *Fig. 5*, the revaluation of risk premiums was observed mainly for issues rated BBB–B and A, and G-spreads on them have not exceeded 1,000 bps over the past three months. Issuers with very high credit quality (AAA–AA) have shown no significant change in the dependence of risk premiums on the credit rating.

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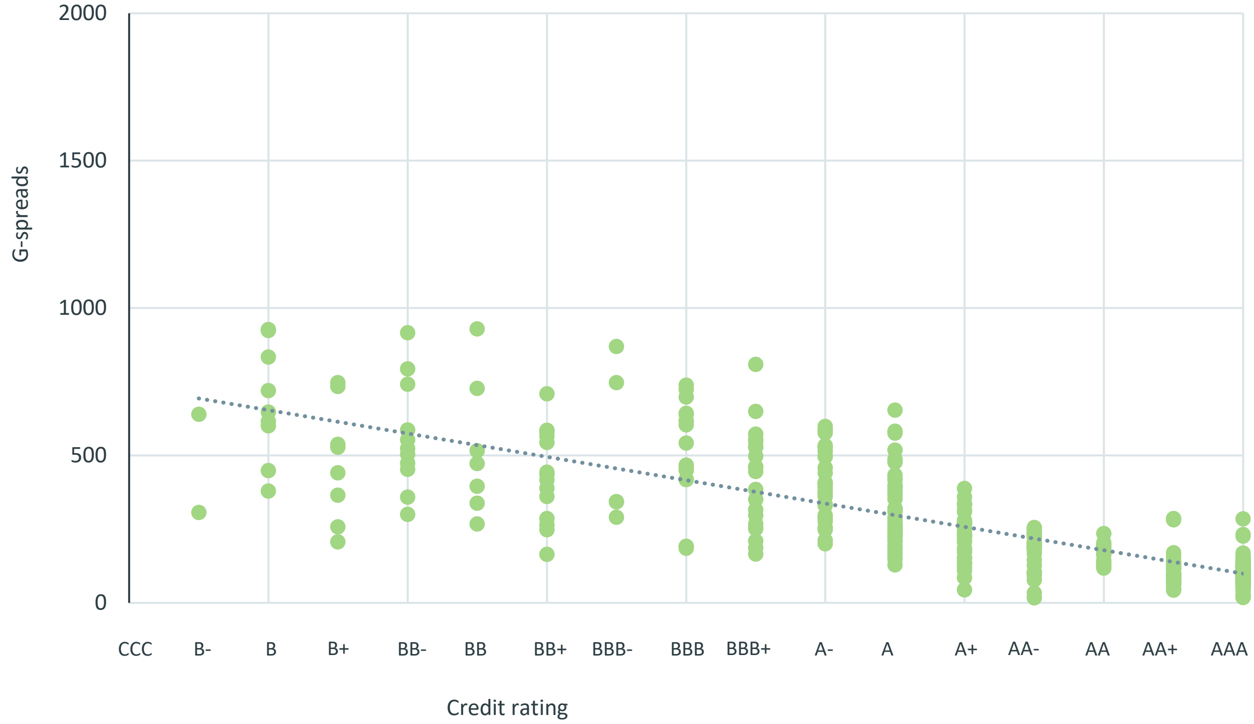
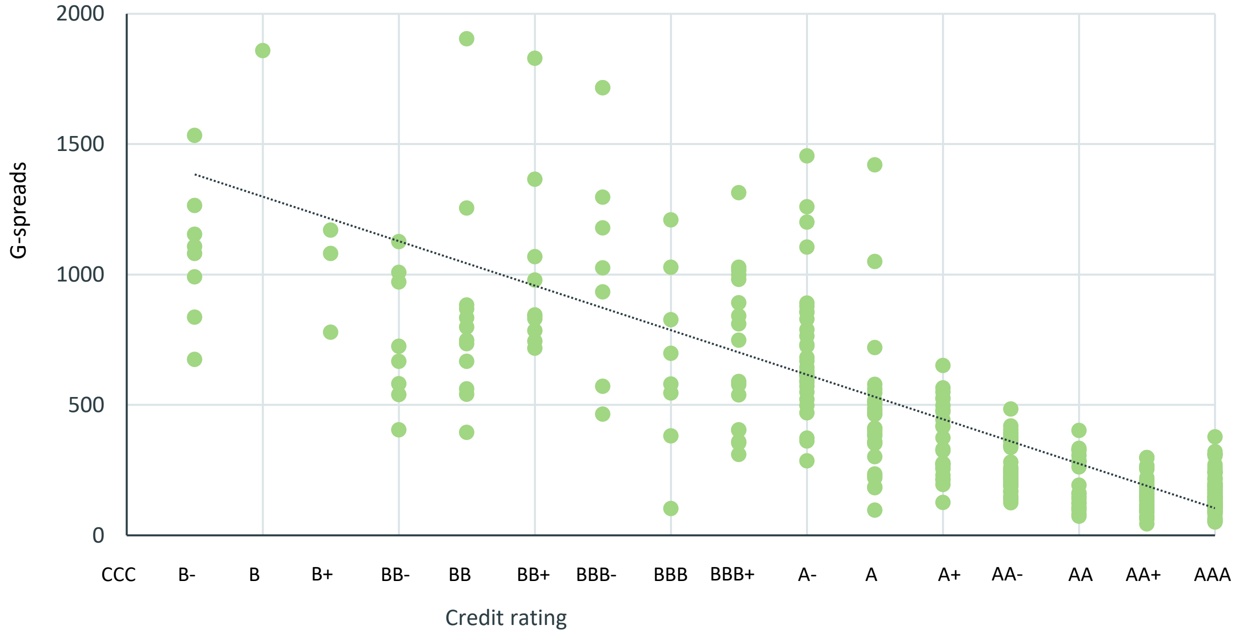
Figure 5. Relation of G-spreads and credit ratings for bonds*

April — June 2023



After September 21, 2022



* For the purposes of representativeness, bond issues with durations of up to three years were used in calculations; only national scale credit ratings are shown on the chart.

Sources: Cbonds, ACRA

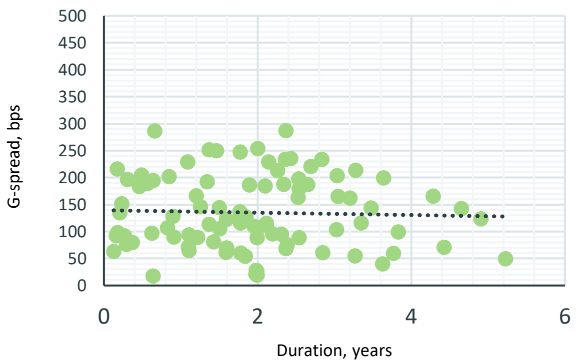
G-SPREAD DYNAMICS FOR BONDS OF ISSUERS IN THE AAA–AA RATING CATEGORIES

For the AAA–AA rating categories, credit risk premiums on bonds with durations of less than five years declined, on average, by 28% (by 50 bps) compared to September 2022

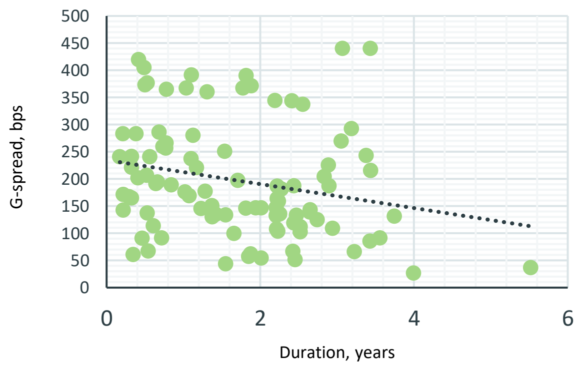
A third of the issues from the sample of bonds reviewed by ACRA belong to the AAA–AA rating categories. A significant portion of the sample includes state-owned companies from a wide range of industries — electric power (generation and grids), oil and gas industry, telecommunications, transport, chemical industry, mechanical engineering, etc. Bonds of issuers in the AAA–AA rating categories have a range of durations of up to five years (long-term bonds of non-financial companies have historically been issued by issuers of these rating categories, which are characterized by base low spreads) and are fairly evenly distributed among them.

Over the past three months, G-spreads for securities issued by companies with high credit ratings ranged from 50 bps to 250 bps (in September, risk spreads above 300 bps were noted in about 16% of observations). The observed reduction in spreads was not so significant compared to lower rating categories. Thus, G-spreads for bonds with durations of up to one and a half years decreased by an average of 99 bps, those on bonds with durations of one and a half to five years — by an average of 25–30 bps. In comparison with September 2022, a reduction in risk premiums is more clearly observed as duration increases, which can be explained by a very strong slope of the zero-coupon yield curve, and investors are ready to buy securities with lower spreads at the long end of the yield curve in order to fix high absolute rates.

Figure 6. G-spreads for bonds of issuers in the AAA–AA rating categories in April–June 2023 and September 2022



a) April–June 2023



b) September 2022

Sources: Cbonds, ACRA

G-SPREAD DYNAMICS FOR BONDS OF ISSUERS IN THE A RATING CATEGORY

For the A rating category, credit risk premiums declined by 1.5 times (122 bps) on average compared to September 2022.

In the non-financial sector, bond issuers in the A credit rating category are mainly represented by companies from the housing construction, metals, IT and food industries. In this rating category, the range of bond durations is mainly limited to three years. At the same time, G-spreads are fairly evenly distributed by duration (100 to 400 bps for durations of less than a year, 100 to 600 bps for durations of one to three years), and in comparison with September 2022, there are no values that stand out from the general sample.

Similar to the AAA–AA rating categories, the main revaluation of risks occurred in the short- and medium-term ends of the yield curve. Spreads for bonds with durations of up to one and a half years decreased, on average, by 245 bps in April—June 2023 compared to September 2022, for bonds with durations of one and a half to three years — by 102 bps, and for bonds with durations of three to five years — by 20 bps.

Figure 7. G-spreads for bonds of issuers in the A rating category in April–June 2023 and September 2022

a) April–June 2023

b) September 2022

Sources: Cbonds, ACRA

G-SPREAD DYNAMICS FOR BONDS OF ISSUERS IN THE BBB RATING CATEGORY

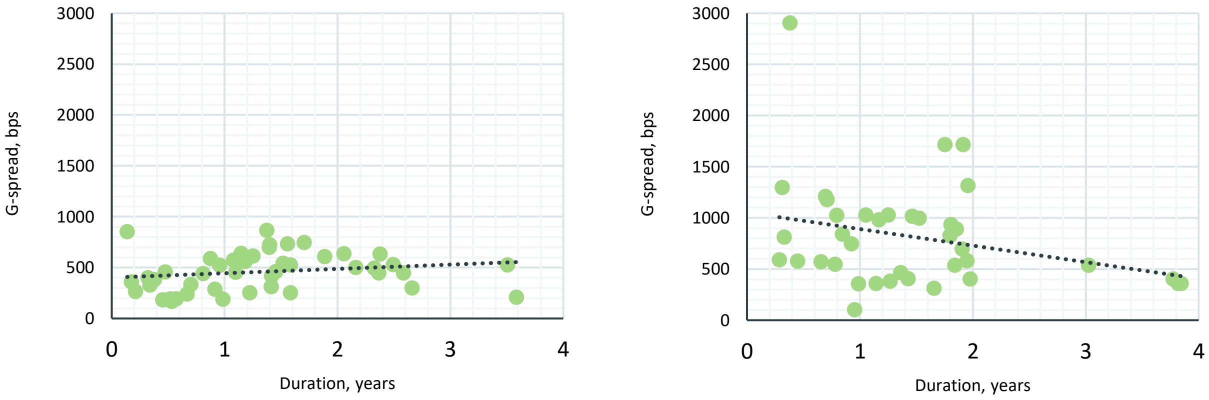
For the BBB rating category, credit risk premiums declined by 1.6 times (260 bps) on average compared to September 2022.

The BBB rating category is dominated by issuers from the housing and infrastructure construction industries and companies from a very wide range of industries, which somewhat constrains the analysis of G-spread for these bonds.

The distribution of G-spreads for issues of non-financial companies in the BBB rating category has become more homogeneous over the past few months: the bulk of observations are within the range of 200–800 bps. In addition, more issues with durations of more than two years have appeared in the sample, while in September last year the range of durations was limited to two years, and the risk premiums on securities with durations of less than one and a half years differ by several times (from 103 bps to 2,905 bps). For issues in this rating category, the longer the duration, the higher G-spreads.

G-spreads for BBB bonds with durations of up to one and a half years averaged 448 bps in April—June (almost halved in comparison with the September value), for bonds with a duration of one and a half to three years they averaged about 515 bps, while at the end of September last year the risk-premiums for bonds with durations of up to three years averaged 845–870 bps.

Figure 8. G-spreads for bonds of issuers in the BBB rating category in April–June 2023 and September 2022



a) April–June 2023

b) September 2022

Sources: Cbonds, ACRA

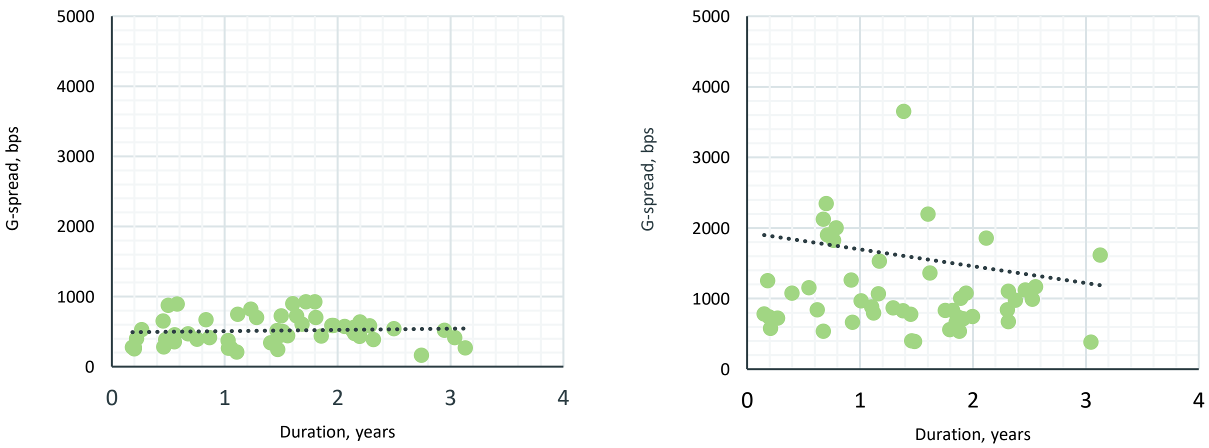
G-SPREAD DYNAMICS FOR BONDS OF ISSUERS IN THE BB–B RATING CATEGORIES

For the BB–B rating categories, credit risk premiums declined by 2.6 times (730 bps) on average compared to September 2022.

The sample of bonds of issuers in the BB–B rating categories consists mainly of issuers belonging to the wholesale trade, housing and infrastructure construction, agriculture and food industry, and mechanical engineering sectors. The duration of these bonds is mainly up to two and a half years.

The range of G-spreads has become narrower: values vary from 200 bps to 1,000 bps (in September last year, G-spreads reached 2,000 bps with individual spikes for bonds with durations of one to three years). Over the past three months, risk premiums have averaged 479 bps for BB–B securities with durations of up to one and a half years, 570 bps for securities with durations of one and a half to three years, and 342 bps for securities with durations of three to five years. These values are almost three times smaller than risk premiums at the end of September last year.

Figure 9. G-spreads for bonds of issuers in the BB–B rating categories in April–June 2023 and September 2022



a) April–June 2023

b) September 2022

Sources: Cbonds, ACRA