

MATURITIES MATTER

BSRI QUARTERLY UPDATE

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Maturities Matter



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The latest quarterly update of the BlackRock Sovereign Risk Index (BSRI) highlights France, Japan, Indonesia and selected others among the 48 countries we track. Try our [interactive BSRI](#) to view individual country scores, compare two countries and sort rankings by index components.

Our main headlines for the quarter ended 31 March:

- ▶ **France** slid for a third quarter in a row, dropping two spots to 29th place. It was dragged down by an increased external debt burden, a relative worsening of its maturity profile and weakening financial sector health.
- ▶ **Belgium** and **Austria** each fell two spots, also hurt by increased external debt burdens.
- ▶ **Denmark** offered a mirror image of France. It rose to 11th place due to an improved debt term structure and healthier financial sector.
- ▶ **Japan** bounced back to 33rd place on the back of the new government's clear mandate and appetite for change. Other metrics worsened.
- ▶ **Indonesia** fell three spots, the most of any country, to 36th place on across-the-board weakness. The risk of a credit bubble is of particular concern.

Drawing on a pool of financial data, surveys and political insights, the BSRI provides investors with a framework for tracking sovereign credit risk. The index uses more than 30 quantitative measures, complemented by qualitative insights from third-party sources.

The index breaks down the data into four main categories that each count toward a country's final BSRI score and ranking: Fiscal Space (40%), Willingness to Pay (30%), External Finance Position (20%) and Financial Sector Health (10%).

- ▶ Fiscal Space includes metrics such as debt to gross domestic product (GDP), the debt's term structure, tax revenues and dependency ratios.
- ▶ Willingness to Pay measures a government's perceived effectiveness and stability, and factors such as perceived corruption.
- ▶ External Finance Position includes exposure to foreign currency debt and the state of the current account balance.
- ▶ Financial Sector Health gauges the banking system's strength.

For full descriptions, see [Introducing the BlackRock Sovereign Risk Index](#) of June 2011. The BSRI's inputs are updated at irregular intervals, meaning some changes may only reflect the timing of data releases. Small changes in scores can spur big changes in rankings, as many issuers are bunched together in the index. The BSRI is not meant to forecast the creditworthiness of countries.

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The BlackRock Investment Institute leverages the firm's expertise across asset classes, client groups and regions. The Institute's goal is to produce information that makes BlackRock's portfolio managers better investors and helps deliver positive investment results for clients.

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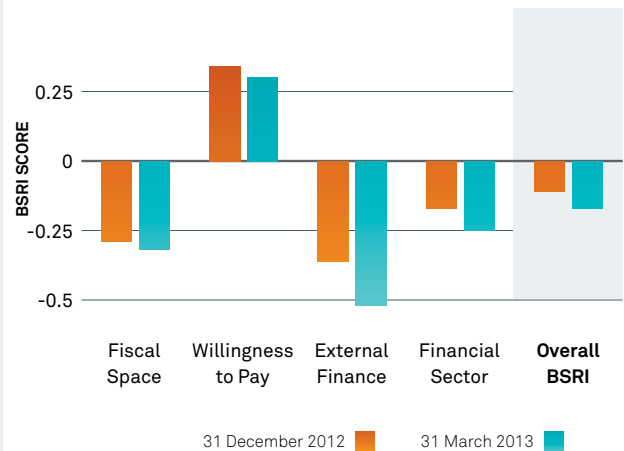
IT'S ALL RELATIVE

France slipped two notches to 29th place, landing in the BSRI's fourth quintile. France's scores declined across the board (see the chart on the right), but two factors in particular stuck out:

- ▶ Worsening external finances
- ▶ Deteriorating financial sector health

France's external debt burden increased. This includes quasi-external debt, or euro-denominated debt that we have designated as external for eurozone countries in proportion to their likely influence on central bank policies. France extended its maturity profile slightly, but made less headway than other countries. This caused France's *relative* external debt profile to worsen. The BSRI is a relative index, so a positive move by one country can hurt another's score. Maturities matter: More debt coming due sooner gives a government less time to decide if and how to restructure debt, retool the economy or implement spending cuts.

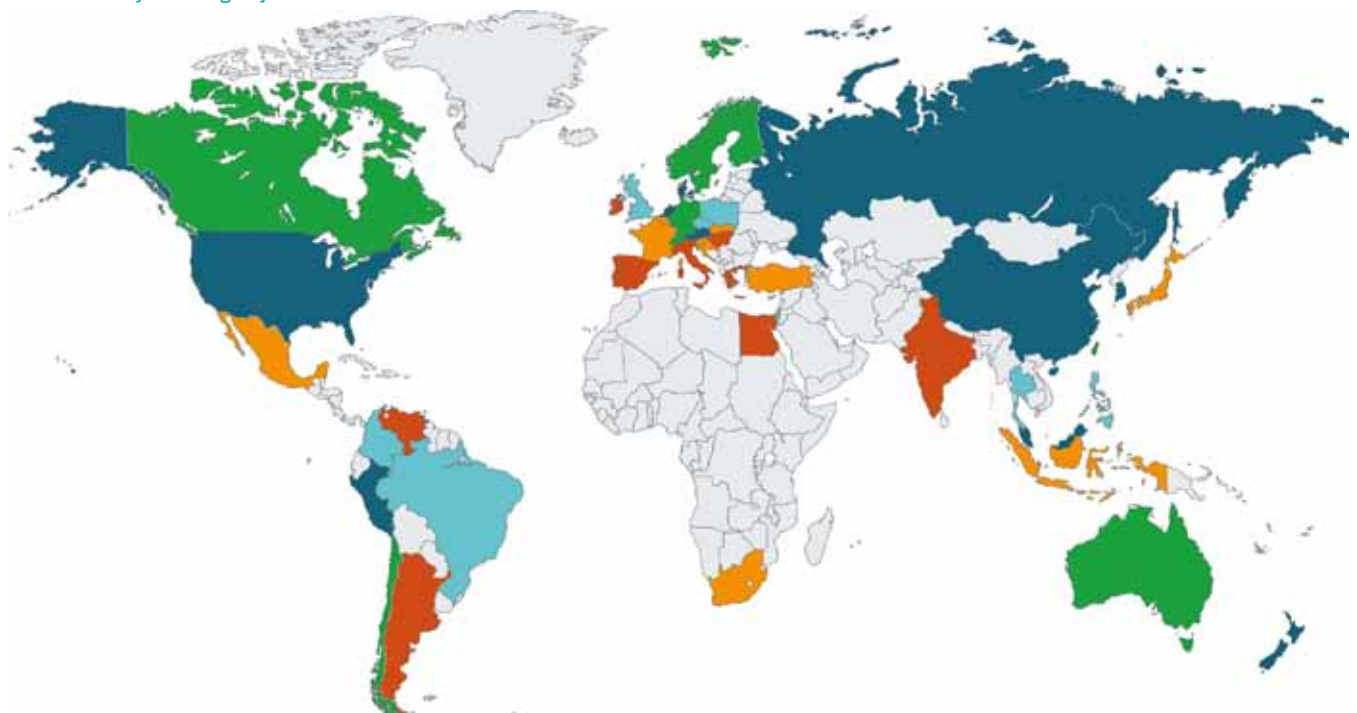
FRANCE: REPUBLIQUE DE DÉTÉRIORATION



Source: BlackRock, March 2013.

MAPPING SOVEREIGN RISK

BSRI Country Rankings by Quintile



1 Norway	11 Denmark	21 Czech Republic	29 France	39 India
2 Singapore	12 New Zealand	22 Israel	30 Slovakia	40 Hungary
3 Switzerland	13 South Korea	23 United Kingdom	31 Mexico	41 Spain
4 Sweden	14 Netherlands	24 Philippines	32 Belgium	42 Argentina
5 Finland	15 USA	25 Poland	33 Japan	43 Ireland
6 Canada	16 Malaysia	26 Thailand	34 Turkey	44 Italy
7 Taiwan	17 China	27 Colombia	35 South Africa	45 Portugal
8 Australia	18 Peru	28 Brazil	36 Indonesia	46 Venezuela
9 Germany	19 Austria		37 Slovenia	47 Egypt
10 Chile	20 Russia		38 Croatia	48 Greece
Top ten	11-20	21-28	29-38	Bottom ten

Source: BlackRock, March 2013.

Click for
interactive charts



The opinions expressed are as of April 2013 and may change as subsequent conditions vary.

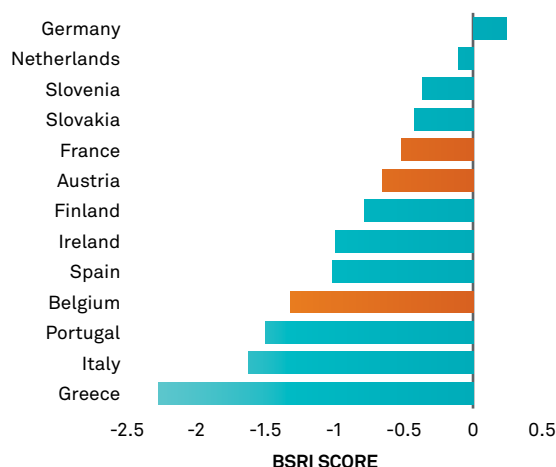
France's Financial Sector Health score also deteriorated. Credit to the private sector as a percentage of GDP has increased over the past three years – whereas it has fallen in other countries (such as the United States). It is far from a credit bubble – but increases the risk of one.

Aside from funding pressures, the Achilles heel of France's banks has been exposure to Europe's southern-tier countries. Banks have cut this exposure but still were owed 348 billion euros as of September 2012, according to a Moody's analysis in March 2013.

Belgium and **Austria** also moved down in the rankings by two spots each, primarily because of increases in their (quasi)-external debt burdens. They are by no means alone in their weak external finance scores. All eurozone countries tracked by the BSRI have negative scores in this area -- except Europe's de-facto paymaster, Germany. See the chart on the right.

EXTERNAL FLAWS

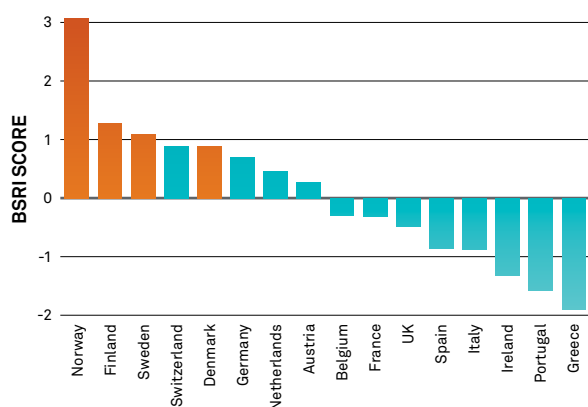
Eurozone's External Finance Scores



Source: BlackRock, March 2013.

NORDIC LIGHTS

Developed Europe's Fiscal Space Scores



Source: BlackRock, March 2013.

DANISH DYNAMITE

Denmark offered a mirror image of France in the quarter. It rose two spots to 11th place due to improved external finance and banking sector scores. The first was driven by a big improvement in Denmark's term structure as bonds maturing in less than two years dropped by about half to less than 5% of GDP. The country's financial sector health also improved, thanks to a decrease in private sector credit as a percentage of GDP.

Despite these improvements, Denmark's external finance and financial sector scores remain challenged. Denmark is trailing other Nordic nations on the key Fiscal Space metric as well. See the chart on the left. Overall, however, Denmark ranks near the top of the BSRI due to its healthy fiscal position (government debt is less than 50% of GDP, for starters).

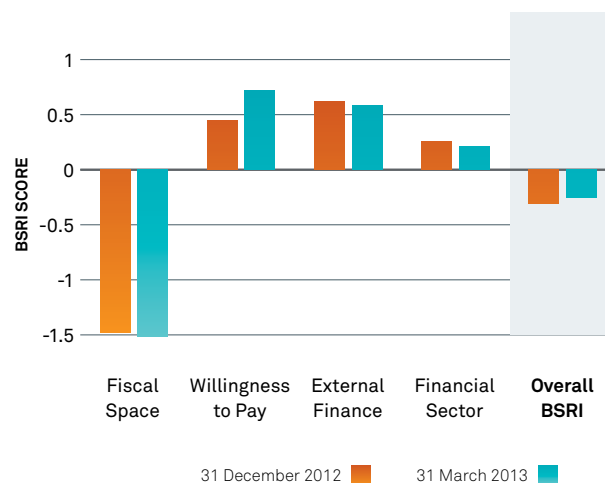
JAPAN FLIPS BACK

Japan swung back to 33rd place, halting a two-quarter slide. The reason was a jump in the country's Willingness to Pay score. See the chart on the right. This was triggered by the landslide election of Prime Minister Abe Shinzo with a clear mandate to rev up the economy through quantitative easing and inflation targeting.

It remains to be seen if "Abenomics" will work. One thing is for sure: Japan's planned \$1 trillion-plus monetary stimulus indicates a radical break with the past -- and could reverberate through global markets.

Japan's other metrics worsened. Its Fiscal Space score edged down as net debt rose to 138% of GDP, from 135%. On the plus side, the country's projected budget deficit decreased to (a still high) 8.9%, from 9.4%.

JAPAN: THE AUDACITY OF HOPE



Source: BlackRock, March 2013.

RUNNING AMOK?

Indonesia sank three spots to 36th place – its lowest ranking since we started the index in 2011. The main driver for the quarterly move was its worsening Financial Sector Health score. Heady credit growth pushed up its loans-to-deposit ratio to 98.1% of GDP, from 92.2%. The country's projected current account deficit increased to 1.95% of GDP, from 1.61%.

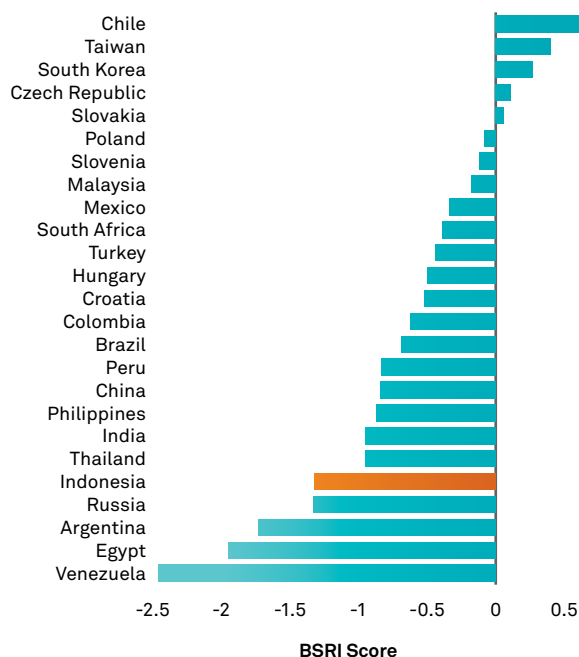
Risk of a credit bubble dominated debate about Indonesia at a March 2013 gathering of leading BlackRock emerging market portfolio managers.

So far, markets have mostly shrugged off any worries. Indonesian equities were the second-best emerging market performer in the first quarter (after the Philippines), up 13.4% in US dollar terms. The total return on Indonesian dollar debt was -3.4% in the period, however.

The main reason for Indonesia's low overall ranking is a weak Willingness to Pay score. The country is not unique in this: just five out of 25 emerging markets tracked by the BSRI have a positive score in this area. See the chart on the right.

TO PAY OR NOT TO PAY

Emerging Markets' Willingness to Pay Scores

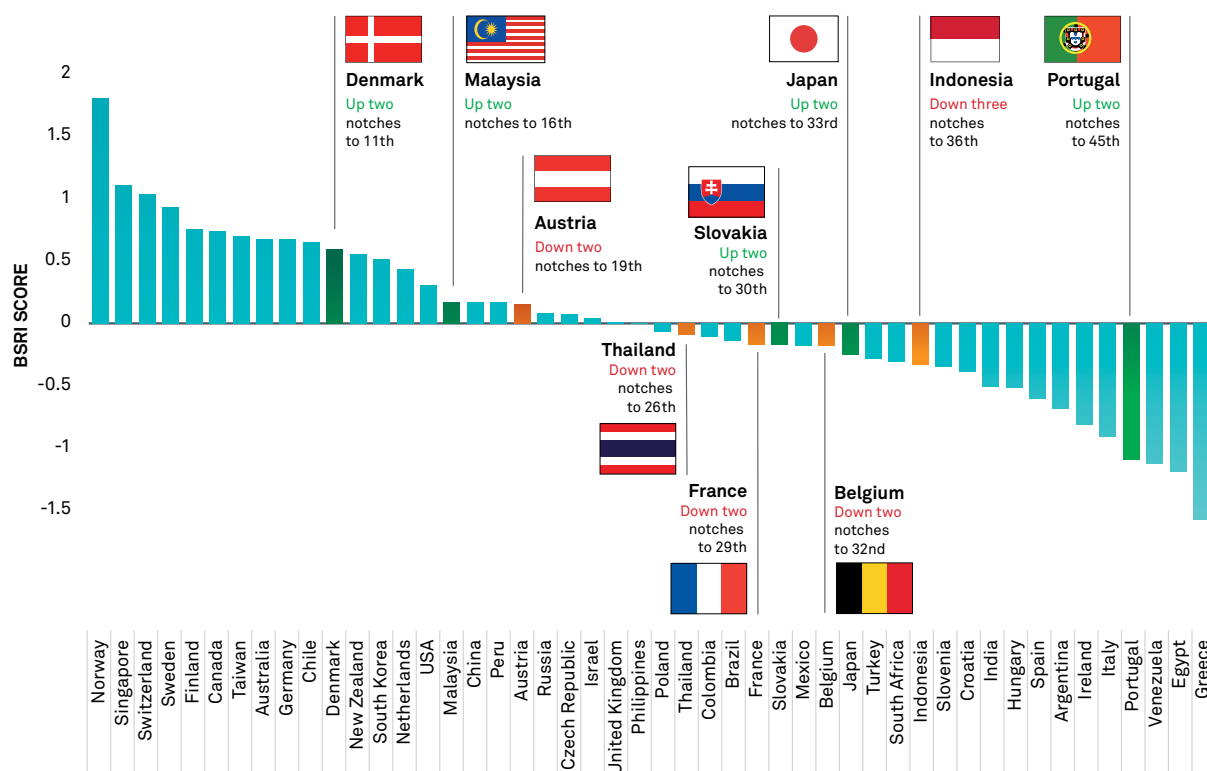


Source: BlackRock, March 2013.

WHO'S UP AND WHO'S DOWN

BlackRock Sovereign Risk Index Rankings, March 2013

Click for
interactive charts



Sources: BlackRock, Bloomberg, IMF, World Bank, central banks, Eurostat, BIS, Consensus Economics, UN, Moody's, Standard and Poor's, Fitch, PRS Group and www.euromoneycountryrisk.com.

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