CEE bond technicals: Foreign bondholders and sovereign ratings

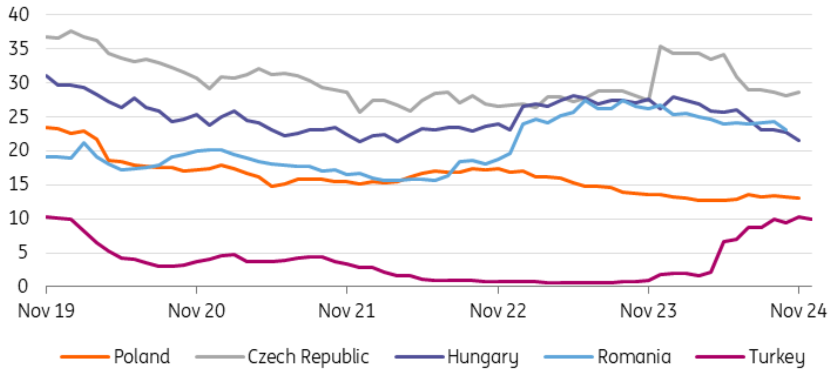
Foreign investors are exiting CEE4 markets and we see unfavourable conditions for this year. Governments have to rely more and more on domestic demand. Turkey should see a continued return of foreign investors to the local market. In terms of sovereign ratings, we are positive on Turkey but negative on Hungary and Romania

Foreign bondholders: Gradual outflow of foreigners and more reliance on domestic demand

If 2023 was a good year for foreign inflows into local currency bond markets in the CEE region, 2024 and especially the second half saw a turn with outflows across the region. No doubt local fiscal issues and a negative global environment are not supportive for the region and we are unlikely to see a different picture this year. Within CEE4, only in the case of Czech government bonds (CZGBs) do we see that foreign inflows can keep pace with domestic demand and if we ignore the methodological one-off in the Czech data, CZGBs is the only market that shows a relative increase in foreign bondholders year-on-year. On the other hand, Romania and Poland saw stable foreign holdings leading to a deterioration in relative terms late last year. Hungary has seen foreign outflows since the middle of last year and has lost the most among CEE peers. We believe that with still-high borrowing needs, heavy issuance and limited room for rate cuts, it will become more and more difficult to attract foreign demand. Governments will have to rely on local demand, which in some cases seems already saturated after last year.

In Turkey, foreign bondholders reached 10% in November and December versus 2% in January 2024. We expect inflows to continue due to the yield level and rate cuts story along with favourable technicals. The weighting of Turkish government bonds (TURKGBs) in the GBI-EM index is gradually increasing from a 0.75% bottom to the current 1.50%. We believe the weighting will continue to increase which should support further inflows into the TURKGBs market.

Foreign bondholders (%)



Source: Macrobond, ING

Sovereign ratings: Positive on Turkey, negative on Hungary and Romania

In the past year we have seen several rating changes in both directions across the region. For this year, we are particularly positive on Turkey, where further normalisation of the policy and economic environment could bring another rating upgrade in the second half of 2025. We are neutral on Poland and the Czech Republic, where we expect relative metrics to stabilise versus peers. We are negative on Hungary and Romania given rating agencies' sensitivity to political uncertainty and deterioration in fiscal metrics.

In Poland (A2/A-/A-), the sovereign rating and outlook seems the most stable in the CEE region and so far there are no indications of any changes. Agencies typically cite the lack of efforts to consolidate public finances as the main risk to the rating. On the other hand, Poland unlocked EU money last year and outperforms peers in GDP growth-stabilising relative metrics. Overall, we thus see the risk of some change in either direction as low for this year.

In the Czech Republic (Aa3/AA-/AA-), Fitch upgraded the outlook from negative to stable in the past year, as have the other agencies, which likely exhausts the scope for any changes. We do not see any changes in the top-rated country in the CEE region this year.

Sovereign rating review calendar

	S&P	Moody's	Fitch
Poland	09-May	21-Mar	14-Mar
	07-Nov	19-Sep	05-Sep
Czechia	28-Mar	24-Jan	14-Feb
	26-Sep	18-Jul	08-Aug
Hungary	11-Apr	30-May	06-Jun
	10-Oct	28-Nov	05-Dec
Romania	24-Jan	14-Mar	21-Feb
	11-Apr	12-Sep	15-Aug
	10-Oct		
Turkey	25-Apr	24-Jan	31-Jan
	17-Oct	25-Jul	25-Jul

Source: rating agencies

In Hungary (Baa2/BBB-/BBB), Moody's downgraded the outlook from stable to negative last November, mainly due to the loss of some EU money, weaker-than-expected growth and limited impact of FDI inflows on the economy. In contrast, Fitch upgraded the outlook to stable from negative in December due to the bullish outlook on the economy in the coming years. For now, we do not see further changes in the near term but risks point to the downside. Another weaker year for the economy along with the political cycle and EU money discussions may lead to further negative moves from the rating agencies in our view.

In Romania (Baa3/BBB-/BBB-), Fitch revised the country's outlook to negative from stable in December last year following a failed fiscal consolidation and political uncertainty resulting from the general and presidential elections. Fitch reaffirmed Romania's abilities to react the quickest to adverse developments in the CEE region. We thus see further ratings reviews by other agencies this year resulting in potential negative outlooks. Romania will have to meet the European Commission consolidation criteria this year to avoid further negative actions by the rating agencies.

In Turkey (B1/BB-/BB-), in the past year we have seen rating improvements from all three major agencies. Moody's upgraded by two notches with a positive outlook in July. S&P upgraded the rating by one notch each time in May and November. Fitch upgraded the rating in two steps in April and September. The agencies' reports mention falling inflation, strengthening lira credibility and reduced FX exposure. We expect the rating upgrades may continue in the second half of this year, in particular with regards to Moody's catching up with S&P and Fitch.

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