

## Global Sovereign 2014 Transition and Default Study

**Regional Risks Persist:** The year was characterized by uneven growth in the major advanced economies and persistent weakness among leading emerging markets. Improved growth in the US and the UK stood in marked contrast to faltering expansion in the eurozone and Japan. Geopolitical tensions, structural shortcomings and lower commodity prices weighed on the outlook for EMs.

**Sovereign Upgrades Overtake Downgrades:** For the first time since 2011, sovereign downgrades trailed upgrades, by a margin of 0.8 to 1, compared with 1.3 to 1 in 2013 and 1.9 to 1 in 2012. The share of sovereigns downgraded – 9.4% and upgraded – 11.3% contracted modestly from 2013’s 15.5% and 11.7%, respectively.

**Ratings Outlook Broadly Stable:** Positive and Negative Outlooks became more evenly balanced. Negative Outlooks were concentrated in EM, reflecting the risks posed by falling oil prices and the prospect of higher U.S. interest rates. Conversely, the balance of Outlooks in the eurozone pointed to a mild improvement in credit quality, as crisis-hit sovereigns started to recover and rebalance.

**Ratings Returning to Historical Levels:** Eurozone upgrades included Ireland and Spain, both positive indications for Europe. Saudi

Arabia was the only sovereign to break new ground, its IDR rising from AA- to AA; all other sovereign IDR uplifts entailed countries that had previously been rated at current levels or above.

**Developed/Emerging Rating Trends:** Mixed signals emanated from developed markets (DMs), with both France and Bermuda downgraded. Emerging market (EM) downgrades divided almost evenly between EMEA and LATAM, with each region reflecting economic and political concerns and both testing the lower extremities of the rating scale with Ukraine (‘CCC’) and Venezuela (‘CCC’) respectively.

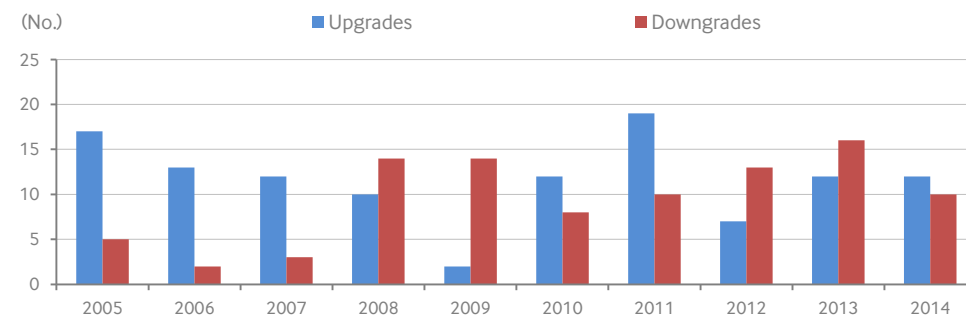
**Recent Rating Convergence:** Sovereign rating convergence between DMs and EMs, evident since the outbreak of the global financial crisis, ceased in 2014 as sovereign creditworthiness in DMs stabilized, whereas EMs encountered a more challenging global economic environment.

**A Single Default in 2014:** Argentina recorded the sole sovereign foreign currency default when it was unable to cure a missed payment. The 2014 long-term foreign currency default rate was 0.94%. Over the long-term (1995–2014), the average annual default rate across Fitch-rated sovereign issuers is 0.69%.

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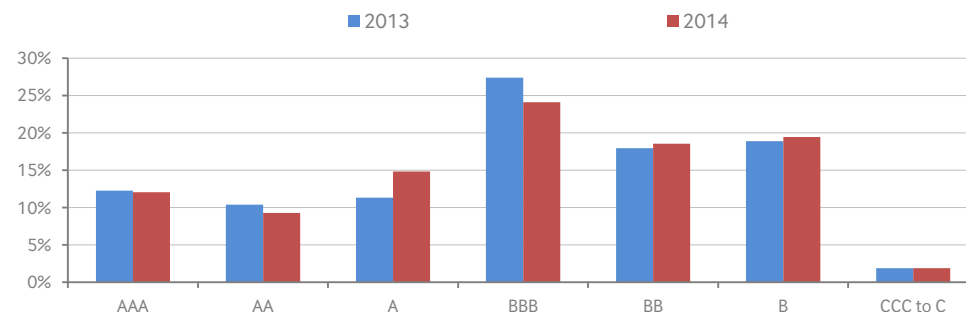
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### Sovereign Historical Rating Activity



Source: Fitch

### Sovereign Ratings Distribution by Major Rating Category<sup>a</sup>



<sup>a</sup>Year-end ratings. Source: Fitch

### Sovereign Average Cumulative Default Rates: 1995-2014

%	1 Year	2 Year	3 Year	4 Year	5 Year
Investment Grade	-	0.21	0.46	0.74	0.94
Speculative Grade	1.88	3.31	4.17	4.97	5.44
All Sovereigns	0.69	1.35	1.81	2.28	2.56

Source: Fitch

**Emerging Markets Relapse:** EMs bore the brunt of negative actions in 2014. Fitch put Russia's ratings on Negative Outlook in March and downgraded Ukraine to 'CCC' as political and economic turmoil mounted in February. South Africa was put on Negative Outlook in June, while protracted economic and fiscal weakness drove Croatia's rating down one notch to 'BB' in August and Serbia's to 'B+' in January. Elsewhere, in Latin America, Argentina defaulted, while Venezuela sustained multiple downgrades to 'CCC' amid rising political uncertainty and falling oil prices. Guatemala and Aruba were also downgraded. Upgrades included Latvia, Lithuania, Rwanda, Saudi Arabia and Vietnam.

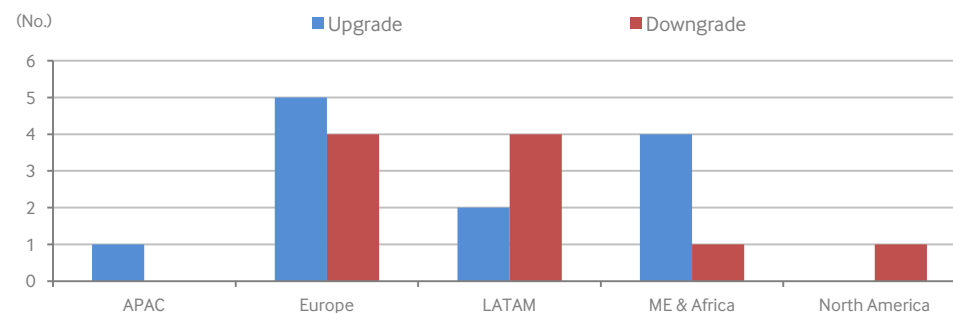
**Developed Markets' Comeback:** Upgrades and positive rating actions in 2014 were concentrated in DMs. Fitch removed the U.S. from Rating Watch Negative in March following a one-year suspension of the ceiling on federal debt. Positive rating actions were dominated by the eurozone periphery. Greece, Spain and Ireland – three of the worst affected eurozone peripherals – were upgraded on the back of improved economic and fiscal performance. Additionally, Cyprus's Outlook was revised to Stable from Negative and Portugal's to Positive. Nonetheless, these countries' ratings remained below their pre-crisis levels. Additionally France sustained a one notch downgrade in December and Belgium's Outlook was revised to Negative in November.

### Sovereign One-Year Transition Matrix: 2014

%	AAA	AA	A	BBB	BB	B	CCC to C	D	WD
AAA	100.00	-	-	-	-	-	-	-	-
AA	-	90.91	9.09	-	-	-	-	-	-
A	-	-	100.00	-	-	-	-	-	-
BBB	-	-	10.34	89.66	-	-	-	-	-
BB	-	-	-	-	94.74	5.26	-	-	-
B	-	-	-	-	5.00	85.00	10.00	-	-
CCC to C	-	-	-	-	-	50.00	-	50.00	-

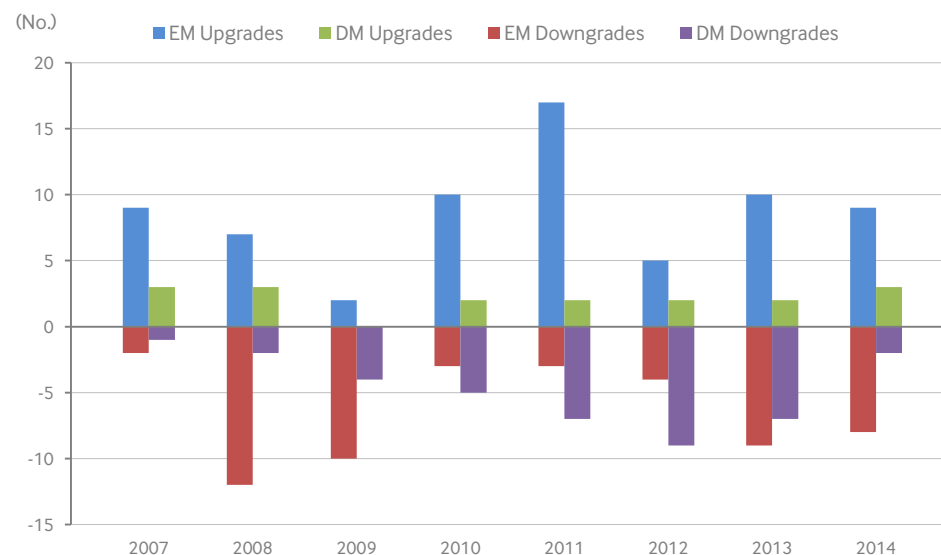
Source: Fitch

### Sovereign Rating Activity by Region: 2014



Source: Fitch

### Sovereign Developed and Emerging Market Historical Rating Activity



Source: Fitch

## Fitch-Rated Sovereign IDR Defaults: 1995-2014

**Russian Federation (1998):** Fitch dates sovereign default to August 1998. Although this was when the Russian Federation defaulted on its local-currency (LC) debt, it began to incur arrears on foreign-currency (FC) debt owed to the Paris Club official bilateral creditors very quickly afterwards. Defaults on FC debt instruments held by private creditors occurred in 1999, although payments on Russian Federation Eurobonds were maintained and honored.

**Indonesia (1998):** Paris and London Club rescheduling operations in June 1998; further rescheduling in 2000 and 2002. Indonesia maintained payments on the single Fitch-rated sovereign bond outstanding at the time.

**Argentina (2001):** Defaulted on more than USD80 billion of sovereign foreign-currency bonds in December 2001, most of which were held by nonresidents. Debt default partially cured in 2005, but some holdout investors remained, constraining the rating to 'RD' until July 2010.

**Moldova (2002):** USD75 million Eurobond restructured in 2002, followed by a Paris Club deal.

**Uruguay (2003):** DDE in March 2003 affecting more than USD5 billion of sovereign FC debt, mostly held by nonresidents.

**Dominican Republic (2005):** Distressed debt exchange (DDE) in 2005 affected more than USD1.1 billion of eligible foreign-currency-denominated bond debt.

**Ecuador (2008):** Missed coupon payment on its 2012 global bonds followed by an announcement that the government would selectively default on all global bonds. The rating was lowered to 'RD' in December 2008.

**Jamaica (2010):** A DDE in February 2010 affected the country's domestic debt, which included FC-denominated instruments to which Fitch's FC rating applied.

**Greece (2012):** A DDE in March 2012 affecting approximately EUR199bn of Greek and foreign-law government bonds resulted in each EUR100 face value amount of Greek government bonds being exchanged for new bonds with a face value of EUR31.5, EUR15 of one- to two-year EFSF ('AAA') notes, and short-term EFSF notes to cover accrued, unpaid interest. Bondholders also received a notional EUR31.5 of Greek GDP-linked securities. The implied net present value loss relative to the original terms and conditions of the bonds implied by the exchange was estimated to be approximately 74%.

**Jamaica (2013):** A DDE in February 2013 included JMD860 billion in both FC and LC domestic debt, resulting in both FC and LC IDR downgrades to RD. The DDE announced by the government included the extension of maturities and a reduction in coupons for the affected debt instruments. The debt exchange was one of the pre-conditions for Jamaica to sign a new IMF agreement totaling nearly USD750 million.

**Cyprus (2013):** A DDE in June 2013 comprised an exchange of domestic government bonds, which resulted in a downgrade of the LC IDR to RD. The exchange constituted domestic bonds with a total nominal value of EUR1 billion, due to expire within the EU-IMF program period (2013 to the first quarter of 2016). These bonds were replaced by new bonds with the same coupon rates but with the maturity dates of the new securities extended beyond the original program period. As foreign Cypriot bonds were unaffected, the FC IDR was unchanged.

**Argentina (2014):** A missed payment default on discount bonds issued under foreign law after the expiration of the 30-day grace period. The default relates to a dispute between Argentina and certain holdout creditors that did not participate in the 2005 and 2010 exchange offers culminated in the denial of Argentina's cert petition to the U.S. Supreme Court. The U.S. Lower Court ruling was upheld, prohibiting Argentina from making payments to exchanged bond holders unless payments were also made to the plaintiffs in the case.

IDR – Issuer Default Rating, RD – Restricted Default.

# Methodology

All Fitch publicly rated, sovereign long-term foreign-currency International Default Ratings (IDR) from 1995 to the present are included in Fitch’s transition and default statistics, which includes more than 1,587 data points from the past 20 years. Fitch’s continuing data enhancement efforts may result in slightly different statistics than in previously published studies. Therefore, this most recent study supersedes all prior versions.

It is important to observe that the rating transitions outlined in this study represent a distinct historical period and might not represent future rating migration patterns. Transition rates are influenced by a number of factors, including credit enhancement levels, macroeconomic variables, state of the financial markets, size of subsectors and ratings portfolio and credit conditions generally.

Fitch employs a static pool approach in calculating default and transition data. The static pools or, alternatively, cohorts are created by grouping issuer ratings according to the year in which the ratings were active and outstanding at the beginning of the year. For example, issuers with ratings outstanding at the beginning of 1995 constitute the 1995 cohort, with the same true for additional cohorts. Issuers newly rated by Fitch in any given year are included in the following year’s cohort. For example, the performance of ratings initiated in mid-1995 would be followed as part of the 1996 and future cohorts. Ratings withdrawn in midyear are excluded from subsequent cohorts since they are no longer active.

Issuer ratings may reside in multiple static pools, as long as their ratings are outstanding at the beginning and end of the year or multiple-year horizons under observation. For example, the annual performance of an issuer rating initiated in 1994, and therefore outstanding at the beginning of 1995, and withdrawn in 1999 would be included in the 1995, 1996, 1997 and 1998 static pools. The rating’s performance over multiple-year horizons would also be included in the two-year, three-year and four-year transition rates for each of the cohorts noted and included in the five-year transition rates as a transition to withdrawn.

In all, Fitch’s transition and default data contains 20 static pools or cohorts from 1995–2014, allowing for 20 unique one-year transition rates, 19 two-year transition rates, 18 three-year transition rates and so forth.

An examination of the 2014 one-year rating transition data at the major rating categories identifies the movement of ratings both up and down the rating scale (from A to BBB), for example as opposed to the modifier level, which counts each notch change or from A to A–, for example (see the Fitch Sovereign 2014 Transition Rates at the modifier in the Appendix commencing on page 7). The vertical left-hand column identifies ratings outstanding at the beginning of 2014, while the horizontal axis provides information on the migration pattern of those ratings by year end. The table reads from the top left-hand corner, beginning with ‘AAA’ and following the diagonal to the right in order to examine the stability of each consecutive rating category.

## Default Rates

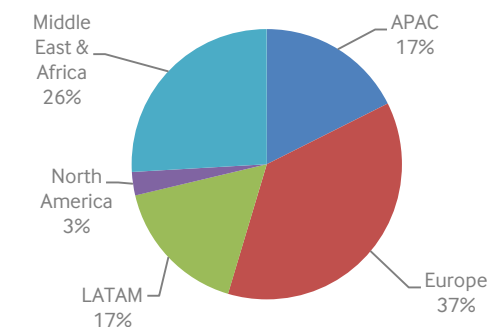
Fitch’s definition of default is available on Fitch’s website, see [Fitch’s ratings definitions](#).

Fitch’s default rates are calculated on an issuer basis, as opposed to dollar amounts. First, defaults are examined by year for each static pool and individual rating category. For example, if 25 issuers defaulted in 2002, and that static pool consisted of 2,000 issuer ratings, the resulting annual default rate for all ratings in 2002 would be 1.3%. If 10 of these defaults consisted of defaults among issuers rated ‘BB’ at the beginning of the year and the ‘BB’ cohort at the beginning of the year totaled 500, the ‘BB’ 2002 default rate would be 2% (10/500).

From these annual default rates, Fitch derives average annual default rates by weighting each cohort’s default rates by the number of ratings outstanding in the given cohort relative to the number of total ratings outstanding for all cohorts. Following the example above, the 2002 ‘BB’ annual default rate of 2% might be followed by a 2003 ‘BB’ annual default rate of 1%. A straight average of these two rates would ignore potential differences in the size of the two cohorts. Rather, weighting the results based on the relative number of ‘BB’ ratings outstanding in 2002 and 2003 gives greater emphasis to the results of the ‘BB’ cohort with the most observations.

The same technique is used to calculate average default rates over multiple-year horizons. For example, the two-year default rate for the 2002 ‘BB’ rating pool would be averaged with the two-year default rate for the 2003 ‘BB’ rating pool by weighting the default rates by the relative size of each pool.

**Sovereign Ratings Distribution by Region: 2014<sup>a</sup>**



<sup>a</sup>Year-end. Source: Fitch

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## Related Research

### Report Data - Excel File



The Fitch 2014 Transition and Default Study data is available in an Excel format. Click [here](#) to download.

### Related reports

[Global Corporate Finance 2014 Transition and Default Study](#) (March 2015)

[Global Structured Finance 2014 Transition and Default Study](#) (March 2015)

[U.S. Public Finance 2014 Transition and Default Study](#) (March 2015)

[International Public Finance 2014 Transition and Default Study](#) (March 2015)

[Fitch Ratings Global Cross-Asset First-Half 2014 Default Update](#) (September 2014)

[Risk Radar](#) (September 2014)

[The Credit Outlook](#) (January 2015)

**Appendix: Sovereign Default Rates**

**Average Cumulative Default Rates: 1995-2014**

%	One-Year	Two-Year	Three-Year	Four-Year	Five-Year	10-Year
AAA	-	-	-	-	-	-
AA+	-	-	-	-	-	-
AA	-	-	-	-	-	-
AA-	-	-	-	-	-	-
A+	-	-	-	-	-	6.25
A	-	-	-	1.52	3.33	7.41
A-	-	-	-	-	-	-
BBB+	-	-	1.96	2.04	2.17	-
BBB	-	-	-	-	-	-
BBB-	-	1.89	3.16	4.82	5.63	11.90
BB+	1.72	2.73	2.94	3.19	3.53	10.20
BB	1.45	2.90	4.41	5.97	6.35	9.52
BB-	-	-	-	-	-	-
B+	-	-	1.20	2.70	3.13	-
B	1.01	3.33	4.88	6.94	6.45	10.71
B-	1.61	6.90	8.93	9.26	9.62	12.50
CCC to C	26.09	28.57	26.32	22.22	27.78	36.36
	-	-	-	-	-	-
Investment Grade	-	0.21	0.46	0.74	0.94	1.78
Speculative Grade	1.88	3.31	4.17	4.97	5.44	8.72
All Sovereigns	0.69	1.35	1.81	2.28	2.56	4.05

Source: Fitch

**10-Year Average of Three-Year Cumulative Default Rates (CDRs)**

%	AAA	AA+	AA	AA-	A+	A	A-	BBB+	BBB	BBB-	BB+	BB	BB-	B+	B	B-
2003 - 2012	-	-	-	-	-	-	-	2.78	-	1.52	-	-	-	1.54	5.48	6.67

Source: Fitch

**Most Recent Three-Year Cumulative Default Rates (CDRs)**

%	AAA	AA+	AA	AA-	A+	A	A-	BBB+	BBB	BBB-	BB+	BB	BB-	B+	B	B-
2012	-	-	-	-	-	-	-	-	-	-	-	-	-	-	10.00	50.00
2011	-	-	-	-	-	-	-	-	-	8.33	-	-	-	-	-	-

Source: Fitch

Appendix: Sovereign Transition Matrices

One-Year Transition Matrix: 2014 Cohort

%	AAA	AA+	AA	AA-	A+	A	A-	BBB+	BBB	BBB-	BB+	BB	BB-	B+	B	B-	CCC to C	D	WD
AAA	100.00	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
AA+	-	66.67	33.33	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
AA	-	-	100.00	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
AA-	-	-	25.00	50.00	25.00	-	-	-	-	-	-	-	-	-	-	-	-	-	-
A+	-	-	-	-	100.00	-	-	-	-	-	-	-	-	-	-	-	-	-	-
A	-	-	-	-	-	100.00	-	-	-	-	-	-	-	-	-	-	-	-	-
A-	-	-	-	-	-	-	100.00	-	-	-	-	-	-	-	-	-	-	-	-
BBB+	-	-	-	-	-	-	30.00	70.00	-	-	-	-	-	-	-	-	-	-	-
BBB	-	-	-	-	-	-	-	11.11	77.78	11.11	-	-	-	-	-	-	-	-	-
BBB-	-	-	-	-	-	-	-	-	-	100.00	-	-	-	-	-	-	-	-	-
BB+	-	-	-	-	-	-	-	-	-	-	66.67	33.33	-	-	-	-	-	-	-
BB	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
BB-	-	-	-	-	-	-	-	-	-	-	-	-	92.31	7.69	-	-	-	-	-
B+	-	-	-	-	-	-	-	-	-	-	-	-	14.29	57.14	14.29	-	14.29	-	-
B	-	-	-	-	-	-	-	-	-	-	-	-	-	33.33	66.67	-	-	-	-
B-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	50.00	25.00	25.00	-	-
CCC to C	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	50.00	-	50.00	-

Source: Fitch

Three-Year Transition Matrix: 2012 Cohort

%	AAA	AA+	AA	AA-	A+	A	A-	BBB+	BBB	BBB-	BB+	BB	BB-	B+	B	B-	CCC to C	D	WD
AAA	86.67	6.67	6.67	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
AA+	-	33.33	33.33	-	33.33	-	-	-	-	-	-	-	-	-	-	-	-	-	-
AA	-	-	75.00	-	25.00	-	-	-	-	-	-	-	-	-	-	-	-	-	-
AA-	-	-	33.33	-	-	-	-	66.67	-	-	-	-	-	-	-	-	-	-	-
A+	-	-	-	11.11	66.67	11.11	-	11.11	-	-	-	-	-	-	-	-	-	-	-
A	-	-	-	-	-	66.67	-	33.33	-	-	-	-	-	-	-	-	-	-	-
A-	-	-	-	-	-	-	100.00	-	-	-	-	-	-	-	-	-	-	-	-
BBB+	-	-	-	-	-	50.00	-	50.00	-	-	-	-	-	-	-	-	-	-	-
BBB	-	-	-	-	-	9.09	36.36	36.36	9.09	-	-	-	-	-	-	9.09	-	-	-
BBB-	-	-	-	-	-	8.33	-	8.33	58.33	8.33	8.33	8.33	-	-	-	-	-	-	-
BB+	-	-	-	-	-	-	-	12.50	37.50	37.50	12.50	-	-	-	-	-	-	-	-
BB	-	-	-	-	-	-	-	-	-	-	-	100.00	-	-	-	-	-	-	-
BB-	-	-	-	-	-	-	-	-	-	-	-	-	77.78	11.11	11.11	-	-	-	-
B+	-	-	-	-	-	-	-	-	-	-	-	-	33.33	22.22	33.33	-	11.11	-	-
B	-	-	-	-	-	-	-	-	-	-	-	-	-	40.00	30.00	-	10.00	10.00	10.00
B-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	50.00	-	-	50.00	-
CCC to C	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	100.00

Source: Fitch

Appendix: Sovereign Transition Matrices

10-Year Transition Matrix: 2005 Cohort

%	AAA	AA+	AA	AA-	A+	A	A-	BBB+	BBB	BBB-	BB+	BB	BB-	B+	B	B-	CCC to C	D	WD
AAA	75.00	6.25	6.25	-	-	-	6.25	6.25	-	-	-	-	-	-	-	-	-	-	-
AA+	50.00	-	50.00	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
AA	-	-	16.67	-	33.33	-	-	33.33	-	-	16.67	-	-	-	-	-	-	-	-
AA-	-	25.00	25.00	-	-	-	-	25.00	25.00	-	-	-	-	-	-	-	-	-	-
A+	-	-	-	-	50.00	-	-	-	-	-	-	-	-	-	-	50.00	-	-	-
A	-	-	20.00	20.00	20.00	20.00	-	-	-	-	-	-	-	-	-	-	-	20.00	-
A-	-	-	-	-	40.00	10.00	30.00	-	10.00	-	10.00	-	-	-	-	-	-	-	-
BBB+	-	-	-	-	-	-	100.00	-	-	-	-	-	-	-	-	-	-	-	-
BBB	-	-	-	-	-	-	-	25.00	25.00	25.00	-	-	25.00	-	-	-	-	-	-
BBB-	-	-	-	-	-	-	-	33.33	16.67	33.33	-	16.67	-	-	-	-	-	-	-
BB+	-	-	-	BB+	-	-	-	-	25.00	25.00	-	-	25.00	-	25.00	-	-	-	-
BB	-	-	-	-	-	-	-	20.00	20.00	40.00	20.00	-	-	-	-	-	-	-	-
BB-	-	-	-	-	-	-	-	-	25.00	-	-	-	50.00	-	-	-	-	-	25.00
B+	-	-	-	-	-	-	-	-	-	40.00	-	-	-	-	20.00	-	40.00	-	-
B	-	-	-	-	-	-	-	-	-	14.29	-	-	14.29	14.29	28.57	-	-	-	28.57
B-	-	-	-	-	-	-	-	-	-	-	-	-	16.67	-	16.67	-	-	16.67	50.00
CCC to C	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	33.33	66.67

Source: Fitch

Default Rates by Cohort

%	One-Year 2014 Cohort	Three-Year 2012 Cohort	10-Year 2005 Cohort
AAA	-	-	-
AA+	-	-	-
AA	-	-	-
AA-	-	-	-
A+	-	-	-
A	-	-	20.00
A-	-	-	-
BBB+	-	-	-
BBB	-	-	-
BBB-	-	-	-
BB+	-	-	-
BB	-	-	-
BB-	-	-	-
B+	-	-	-
B	-	10.00	-
B-	-	50.00	16.67
CCC to C	50.00	100.00	33.33

Source: Fitch



Appendix: Sovereign Transition Matrices

Average Annual Transition Matrix: 1995-2014

%	AAA	AA+	AA	AA-	A+	A	A-	BBB+	BBB	BBB-	BB+	BB	BB-	B+	B	B-	CCC to C	D	WD
AAA	98.08	1.54	-	0.38	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
AA+	11.43	78.57	7.14	2.86	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
AA	-	9.09	83.84	4.04	2.02	1.01	-	-	-	-	-	-	-	-	-	-	-	-	-
AA-	-	-	13.43	73.13	5.97	-	1.49	1.49	2.99	-	-	-	-	-	-	1.49	-	-	-
A+	-	-	-	8.33	84.72	2.78	1.39	-	-	1.39	1.39	-	-	-	-	-	-	-	-
A	-	-	-	-	14.86	78.38	1.35	4.05	1.35	-	-	-	-	-	-	-	-	-	-
A-	-	-	-	-	-	12.99	79.22	7.79	-	-	-	-	-	-	-	-	-	-	-
BBB+	-	-	-	-	-	3.08	16.92	66.15	9.23	3.08	-	-	-	-	-	-	-	-	1.54
BBB	-	-	-	-	-	-	2.91	17.48	71.84	5.83	0.97	-	0.97	-	-	-	-	-	-
BBB-	-	-	-	-	-	-	-	-	17.24	73.28	7.76	-	-	-	0.86	-	0.86	-	-
BB+	-	-	-	-	-	-	-	-	1.72	18.97	70.69	5.17	1.72	-	-	-	-	-	1.72
BB	-	-	-	-	-	-	-	-	1.45	2.90	20.29	66.67	7.25	-	-	-	-	-	1.45
BB-	-	-	-	-	-	-	-	-	-	-	1.71	7.69	77.78	7.69	3.42	1.71	-	-	-
B+	-	-	-	-	-	-	-	-	-	-	-	1.02	17.35	69.39	7.14	2.04	1.02	-	2.04
B	-	-	-	-	-	-	-	-	-	-	-	-	3.03	15.15	70.71	6.06	3.03	1.01	1.01
B-	-	-	-	-	-	-	-	-	-	-	1.61	-	-	1.61	22.58	59.68	8.06	1.61	4.84
CCC to C	-	-	-	-	-	-	-	-	-	-	-	-	-	-	4.35	21.74	39.13	26.09	8.70

Source: Fitch

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