Moody’s Downgrades US Sovereign Credit Rating

Rating Lowered from ‘Aaa’ to ‘Aa1’, Outlook Maintained at ‘Stable’

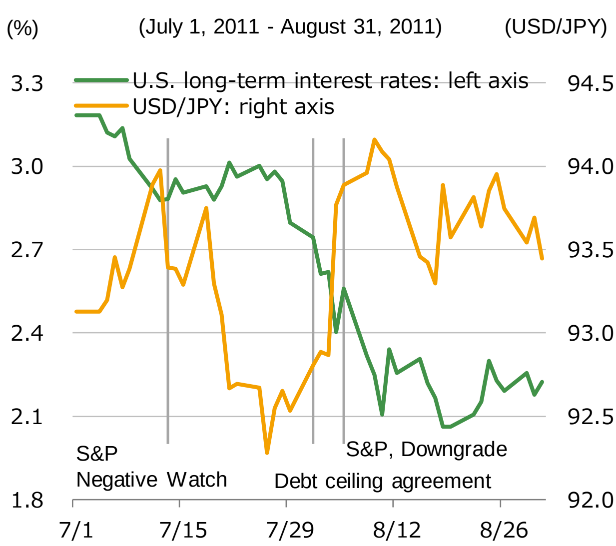
May 19, 2025

Compared to the 2011 downgrade, the direct impact on financial markets appears to be limited.

On May 16 (local time), Moody’s Ratings downgraded the long-term sovereign credit rating of the US by one notch, from the highest tier of “Aaa” to “Aa1,” while maintaining a “Stable” outlook. The rating agency cited the persistent failure of successive administrations and Congress to implement credible fiscal consolidation measures to reverse the trajectory of large fiscal deficits and rising interest burdens. Moody’s further noted that the current fiscal proposals under consideration fall short of delivering substantial multi-year reductions in mandatory spending and the federal deficit. In response, Treasury Secretary Bessent dismissed the downgrade as a “lagging indicator.” Notably, other major credit rating agencies had already taken similar actions: S&P Global Ratings downgraded the US in 2011, and Fitch Ratings followed suit in 2023. While the timing of Moody’s move was somewhat unexpected, it largely aligns with prior actions and does not represent a significant deviation.

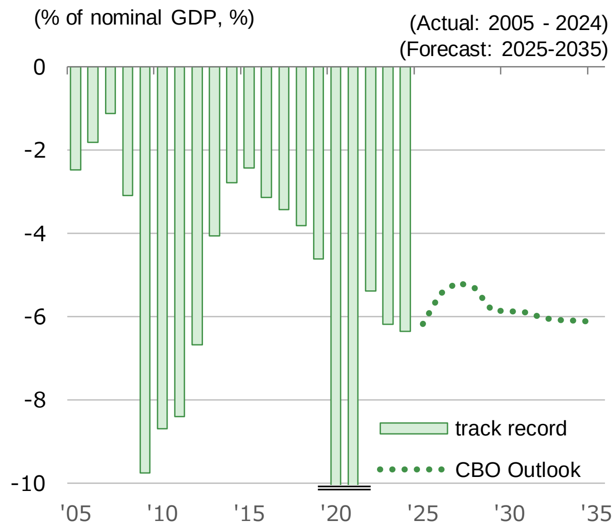
Following the downgrade announcement, the US Dollar depreciated, and Treasury yields rose. However, the overall market impact appears to be limited compared to the 2011 downgrade, which was dubbed the “US Treasury Shock.” There are two primary reasons for this muted reaction: First, the 2011 downgrade marked the loss of the top-tier rating for the first time since 1941, making it a highly symbolic and psychologically significant event. Second, from the perspective of market liquidity and scale, credit ratings do not necessarily have a linear correlation with interest rates. Given the depth and liquidity of the US Treasury market, Treasuries are expected to retain their status as benchmark securities. While concerns over erratic fiscal policy under the Trump administration have fueled some lingering skepticism toward the US Dollar and Treasuries, the current downgrade is unlikely to trigger widespread divestment of US government bonds or materially undermine the Dollar’s role as the global reserve currency.

Bond and currency markets at the time of the 2011 S&P downgrade



Source: Bloomberg; Complied by Daiwa Asset Management

US budget deficit



Source: CBO; Complied by Daiwa Asset Management

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