How Sensitive is Corporate Debt to Swings in Commodity Prices? †

Pablo Donders a Mauricio Jara b and Rodrigo Wagner c, d

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a Metlife. Formerly graduate student at University of Chile. Diagonal Paraguay 257. Santiago. Chile. pdonders@fen.uchile.cl
b School of Economics and Business. Admin Dept. U. of Chile. Diagonal Paraguay 257. Santiago. Chile. mjarab@fen.uchile.cl
c School of Economics and Business. University of Chile. Diagonal Paraguay 257. Santiago. Chile.
Center for International Development, Harvard. Cambridge, MA. (Associate Researcher)
d Corresponding Author. Email Rodrigo_Wagner(at)post.harvard.edu

Highlights
• Commodity producing corporations have trillions of dollars in outstanding debt.
• We explore how exogenous commodity price changes impact the bonds of these firms.
• A 10% change in price impacts yields by 0.15%. Much stronger in price drops.
• Hedging derivatives significantly moderate bond sensitivity to commodities
• Results matter for stress tests in sectors and countries exposed to commodities.

Abstract

Commodity producing corporations have trillions of dollars in outstanding debt. Thus, the recent fall in commodity prices raised concerns about sustainability and systemic risks. Using a global sample (2003-2015) we measure how corporate bonds react to the underlying commodity price. On average a 10% change in the commodity moves yields-to-maturity by only 15 basis points. This is just a tenth of the sensitivity of stocks returns. Nonetheless, bond sensitivity to commodities is significantly stronger for smaller, leveraged and less profitable firms. Also for short maturity bonds. The type of commodity price change matters too. Sensitivity to price drops is at least five times stronger than to increases. Transitory price changes matter for shorter maturities and leveraged firms. In contrast, longer maturities react more to permanent commodity variations. When firms use hedging derivatives, bonds are less sensitive to all price variations. Hedging mitigates the amplification of commodity shocks, as in Shiller (2008). In conclusion, while debt finance deteriorated with the commodity bust, it hardly dried-up.

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