MOODY'S ANALYTICS

WEEKLY MARKET OUTLOOK

Moody's Analytics Research

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Richly Valued Equities Offset Record High Ratio of Corporate Debt to GDP

Click here for *Moody's Credit Outlook*, our sister publication containing Moody's rating agency analysis of recent news events, summaries of recent rating changes, and summaries of recent research.

Credit Markets Review and Outlook

By John Lonski, Chief Economist, Moody's Capital Markets Research, Inc.

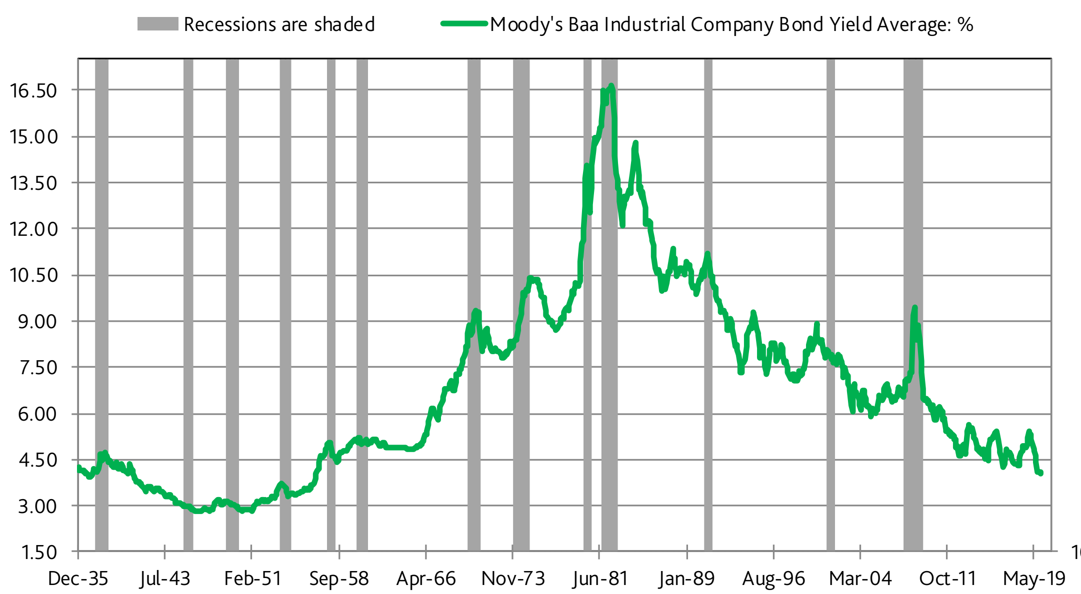
Richly Valued Equities Offset Record High Ratio of Corporate Debt to GDP

Following Jerome Powell's testimony of December 11, Moody's long-term Baa industrial company bond yield fell to 3.98%, which was its lowest close since the 3.95% of August 28, 2019. However, December 11's long-term Baa industrial's 175 basis point yield spread was much thinner than the 198 bp spread of August 28.

Since the end of July 2019, the long-term Baa industrial yield has averaged 4.11%, which represents the lowest extended stretch for this medium-grade benchmark since 1956. It was in August 1956 that the Baa industrial yield last recorded a month-long average of less than 4%. The latter was at the end of a long string, wherein the month-long average of the Baa industrial yield remained under 4% for each month beginning with October 1940.

Better yet, within this span, or beginning with July 1949 and ending with April 1951, each of the Baa industrial yield's month-long averages was less than 3%, or 2.89%, on average. If the forthcoming unprecedented aging of both the population and the workforce of the U.S. sufficiently suppresses business activity, inflation expectations, and corporate earnings growth, the Baa industrial yield might yet stage another prolonged stay under 4%.

Figure 1: Moody's Long-Term Baa Industrial Company Bond Yield's December 2019 Average May Be Lowest since 1956
sources: NBER, Moody's Analytics



The market value of the U.S. equity market almost never conforms to its estimated fair value. The U.S. equity market seems to be always under- or over-valued, where the needle today points toward over-valuation, though not to the extremes experienced during 1998-2000.

The credit ratings of U.S. companies can also be at odds with what otherwise might be inferred from the market value of U.S. corporate bonds and equities. The equity market matters considerably when assessing the likelihood of default and the creditors' expected recovery in the event of default. For one thing, the market's valuation of equity capital greatly influences the value of the collateral backing outstanding debt.

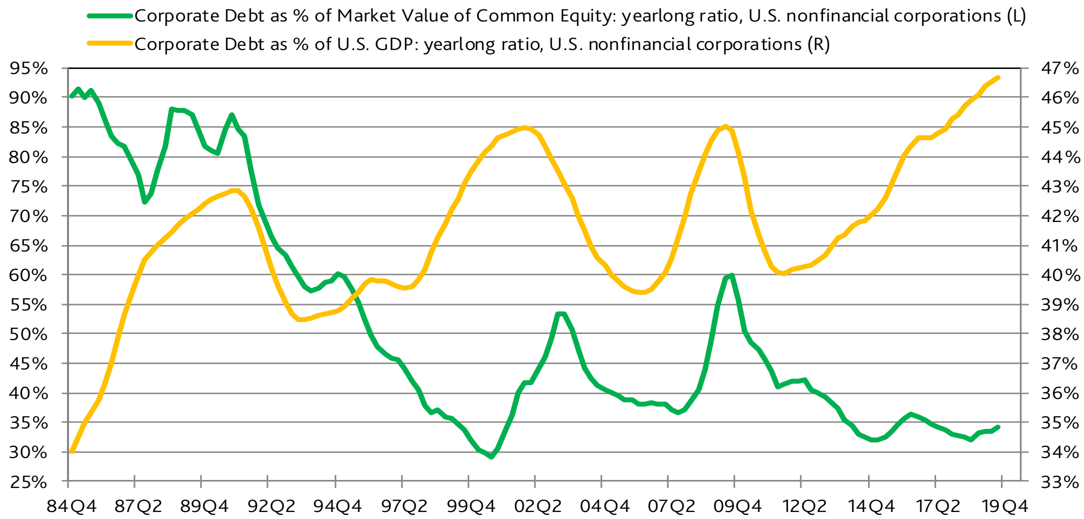
Credit Markets Review and Outlook

Should the need arise, a healthy equity market facilitates the retirement of outstanding debt with either new equity capital or funds secured via the sale of business assets.

In addition, a well-functioning equity market also makes it easier for financially strong companies to acquire (or rescue) financially weak businesses. Hence, over time, credit rating upgrades are more likely than downgrades when high-yield businesses are party to mergers, acquisitions and divestitures.

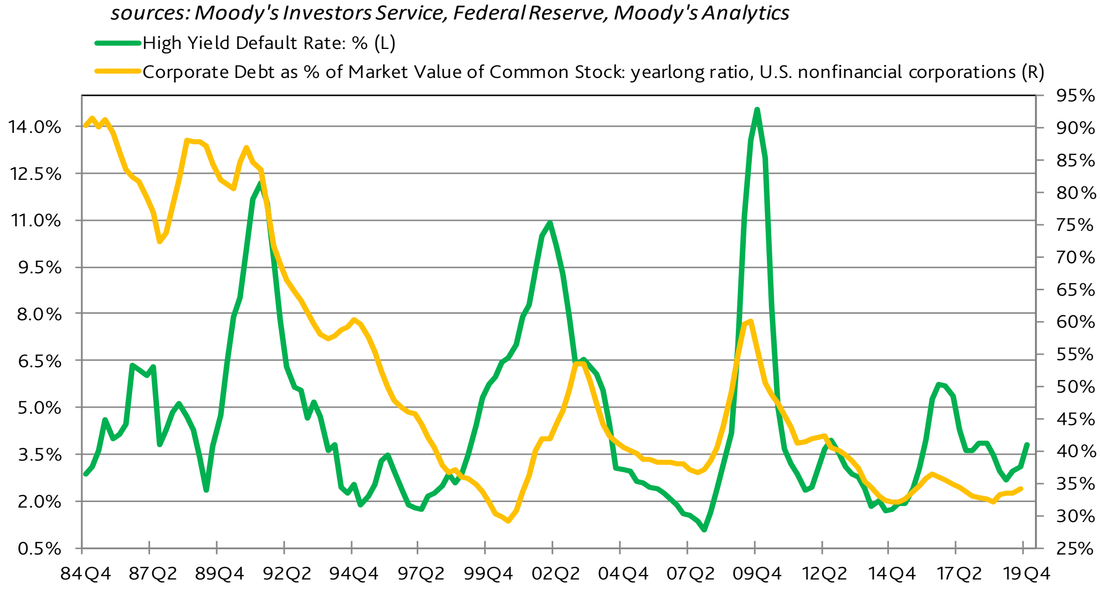
Recent concerns surrounding the adverse default implications of a record high ratio of nonfinancial-corporate debt to GDP overlook not only how historically low corporate borrowing costs make historically high leverage more manageable, they also tend to ignore the downward pressure put on defaults by today's ample systemic liquidity. A now-healthy equity market is but one manifestation of ample systemic liquidity.

Figure 2: Low Ratio of Corporate Debt to Market Value of Equity Differs Radically from Record High Ratio of Corporate Debt to GDP
sources: Moody's Investors Service, Federal Reserve, BEA, Moody's Analytics



Nevertheless, the ratio of corporate debt to the market value of equity is not one of the better macro-financial indicators of default. For example, the high-yield default rate soared from the 1.7% of 1997's second quarter to the 7.9% of 2000's first quarter notwithstanding a deep drop by the moving yearlong average ratio of nonfinancial-corporate debt to the category's market value of common stock from 44.1% to 33.7%, respectively.

Figure 3: Healthy Equity Market Now Helps to Rein In the Default Rate
sources: Moody's Investors Service, Federal Reserve, Moody's Analytics



Credit Markets Review and Outlook

The gross overvaluation of equities from 1998 to 2000 was of little help to the default rate mostly because the span's equity rally was narrowly focused among blue-chip, telecommunications and high-technology firms. Put simply, 1998-2000's explosive equity rally lacked breadth.

Unlike the 28% cumulative advance by the S&P 500 from 1998's second quarter to 2000's first quarter, Value-Line's Geometric stock price index revealed a far different 15% cumulative decline. Whereas the S&P 500 weights its share prices by a company's market capitalization, the Value Line index attempts to assign an equal weight to each of its share prices.

Moreover, the VIX averaged an atypically elevated 25.8 points during July 1998 through March 2000, which well exceeded its 21.4-point average of the contiguous 21-months-ended June 1998.

As shown by how the Value Line index recently was 9% under its cycle high of August 28, 2018, while the S&P 500 has been setting new record highs, not all shares have benefited equally from the current equity rally. And, though the Value Line index was up by 13.9% since the end of 2018, the S&P 500 posted a much greater increase of 25.3%.

However, not only was VIX's 15.0-point average of the latest five-day span well under its 25.8-point average of July 1998 through March 2000, it also fell short of its 15.6-point median since the year-end 2003.

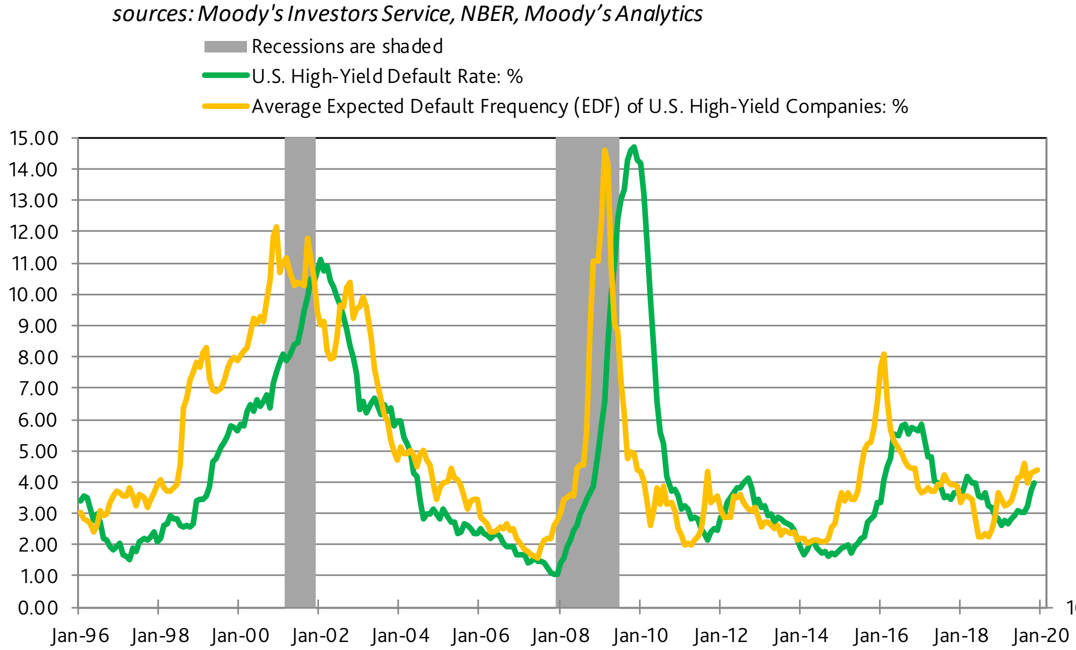
If the current equity rally loses more breadth and if the VIX were to trend higher, then medium- to speculative-grade corporate credits would receive less support from any continuation of the bull market in equities.

EDFs Employ the Linkage Between the Market Value of Net Worth and Default Risk

According to Moody's expected default frequency metric, the probability of an issuer defaulting on outstanding debt obligations will be greater (i) the lower is the market value of net worth and (ii) the more volatile is the market value of the issuer's business assets. All else the same, if an issuer's market value, or share price, rises, the company's EDF, or probability of default, will decline.

December-to-date's 4.38% average for the EDF metrics of U.S./Canadian high-yield issuers is up by roughly 0.7 of a percentage from a year earlier and, thus, signals a material year-over-year increase by 2020's average high-yield default rate. November 2019's U.S. high-yield default rate of 3.9% exceeded its 3.0% average of January-October 2019 and was the highest since May 2018's 4.0%. Nevertheless, the latest average high-yield EDF signals only a limited upside for the default rate in 2020.

Figure 4: Latest High-Yield EDF Signals a Flat to Slightly Higher Speculative-Grade Default Rate
sources: Moody's Investors Service, NBER, Moody's Analytics



Bond-Implied Ratings of Baa3 Industrial Companies Worsen Since Year-End 2018

Prior to the current upturn, the outstandings of Baa-grade U.S. industrial-company bonds had never approached the $2.032 trillion of 2019's third quarter, wherein $751 billion were rated Baa1, $783 billion were graded Baa2, and $498 billion were assigned the lowest investment-grade rating of Baa3.

Because of the current magnitude of outstanding Baa-grade bonds, many fret over a possible flood of fallen-angel downgrades in response to the next recession. Though 2019's credit rating revisions of Baa credits did not supply any cause for alarm, December 11's bond-market implied ratings for Baa3 issuers deteriorated from their readings of year-end 2018.

For a sample of issuers that supplied both bond implied ratings and EDF implied ratings, the average difference between the bond implied rating and the actual Baa3 rating sank from year-end 2018's 0.25 notches to December 11's -0.24 notches. In other words, the average bond implied rating of Baa3 industrial-company issuers went from being between Baa3 and Baa2 at the end of 2018 to between Baa3 and Ba1 on December 11.

All bond implied ratings less than Baa3 are equivalent to high-yield, or speculative-grade, ratings. Thus, it is noteworthy that the percent of the Baa3 category's bond implied ratings that were less than Baa3 increased from year-end 2018's 21.1% to December 11's 36.5%. At the other extreme, the percent of the group's bond implied ratings that were above Baa3 sank from year-end 2018's 42.3% to December 11's 25.7%.

			Bond Implied Rating (BIR)			
Date	Actual Rating	Number of Issuers Having Both an Implied EDF and BIR	Average Difference between Implied and Actual Rating: in notches	% of Issuers Whose Implied Rating Is Less Than Actual Rating	% of Issuers Whose Implied Rating Is Speculative-Grade	% of Issuers Whose Implied Rating Is Above Actual Rating
		1	*2*	*3*	*3a*	*4*
end of 2018	**Baa1**	59	0.27	23.7%	1.7%	40.7%
end of 2018	**Baa2**	80	0.40	16.3%	1.3%	41.3%
end of 2018	**Baa3**	71	0.25	21.1%	21.1%	42.3%
12/11/2019	**Baa1**	60	0.05	36.7%	1.7%	36.7%
12/11/2019	**Baa2**	92	0.08	29.4%	12.0%	43.5%
12/11/2019	**Baa3**	74	-0.24	36.5%	36.5%	25.7%

Firmer EDF-Implied Ratings Highlight Current Importance of Well-Functioning Equity Market

Unlike the bond implied ratings that are derived from an analysis of corporate bond yield spreads, the EDF implied ratings are derived from the market value of an issuer's net worth and the volatility of the market value of an issuer's business assets. When comparing year-end 2018 with December 11, the EDF implied ratings of Baa3 industrial-company issuers provided a different story than that of bond-implied ratings. For starters, the average gap between the EDF implied and actual Baa3 ratings edged up from year-end 2018's 0.70 notches to December 11's 0.78 notches, meaning that the EDF implied rating inched closer to Baa2.

However, the EDF implied ratings were more broadly distributed than were the bond implied ratings. For example, though the percent of the Baa3 industrials EDF implied ratings that were equivalent to high-yield ratings rose from year-end 2018's already worrisome 43.7% to December 11's 45.9%, the share of the EDF implied ratings that exceeded Baa3 jumped up from 39.4% to the same 45.9% respectively. The now relatively firmer EDF-implied ratings of the Baa3 industrials warn of how important a healthy equity market has been in preventing a broad-based deterioration of corporate credit quality.

			Implied EDF Rating				
Date	Actual Rating	Number of Issuers Having Both an Implied EDF and BIR	Average Difference between Implied and Actual Rating: in notches	% of Issuers Whose Implied Rating Is Less Than Actual Rating	% of Issuers Whose Implied Rating Is Speculative-Grade	% of Issuers Whose Implied Rating Is Above Actual Rating
		1	*2*	*3*	*3a*	*4*
end of 2018	**Baa1**	59	1.12	33.9%	18.6%	57.6%
end of 2018	**Baa2**	80	1.05	45.0%	28.8%	48.8%
end of 2018	**Baa3**	71	0.70	43.7%	43.7%	39.4%
12/11/2019	**Baa1**	60	1.88	33.3%	20.0%	65.0%
12/11/2019	**Baa2**	92	1.74	30.4%	7.6%	52.2%
12/11/2019	**Baa3**	74	0.78	45.9%	45.9%	45.9%

The Week Ahead – U.S., Europe, Asia-Pacific

THE U.S.
By Ryan Sweet of Moody's Analytics

Fed Ready for an Extended Pause

The Fed is sending a strong signal that if everything goes according to its plan, rates are on hold in 2020. Rate hikes won't be on the table soon, since inflation would have to show signs of consistently running ahead of the Fed's 2% objective before the debate around tightening monetary policy can start.

Inflation and inflation expectations will carry more weight going forward. While survey-based measures of longer-term inflation expectations were generally little changed, some measures of households' inflation expectations had moved down to historically low levels. Market-based measures of inflation compensation remained low, with some longer-term measures being at or near multiyear lows. Still, the takeaway from the Fed's new dot plot is that policymakers plan on keeping monetary policy accommodative, suggesting that they are not going to be proactive in addressing potential inflation, but rather reactive. This may be a good approach and reduces the odds of a policy error.

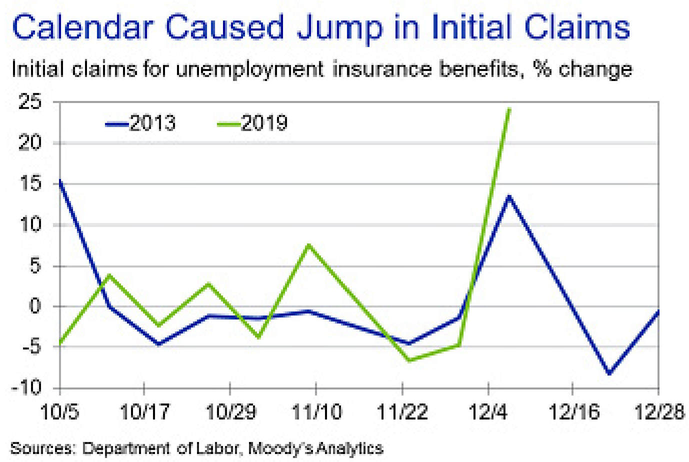
During his presser, Powell noted that the relationship between labor market slack and inflation has been weak. One reason Fed officials are comfortable being reactive is that the slope of the Phillips curve is flat. The Phillips curve refers to a negative (or inverse) relationship between unemployment and inflation in an economy—when unemployment is high, inflation tends to be low, and vice versa. However, this relationship can change, but there is little evidence that this relationship will change quickly. For now, the Fed has a buffer to allow the unemployment rate to remain below its estimate of NAIRU and not worry about inflation. Though Powell noted that the relationship between slack and inflation has weakened, it is also possible that slack isn't being correctly measured by looking at the unemployment rate.

Powell was grilled on the issues in the repo market. He was noncommittal, but the Fed could be forced to implement a standing repo facility. The facility would enable banks to swap Treasury holdings for cash, allowing these banks to reduce cash reserve holdings and instead hold Treasuries in the knowledge that Treasuries can be swapped for cash at any time to meet liquidity/capital requirements. It would be a complement to the Fed's current expansion of its balance sheet, but this increase in the balance sheet isn't quantitative easing. The Fed began buying $60 billion in Treasury bills.

Following the December meeting we have updated our subjective odds for the path of the fed funds rate through next year. Odds heavily favor the Fed keeping the fed funds rate unchanged. We have reduced the odds of a rate cut to less than 20% at each meeting. That said, our baseline forecast includes a 25-basis point rate cut in June. This may be removed, but it would be premature to do that right now. The reasoning is that the decision on U.S. tariffs scheduled to go into effect on December 15 hasn't been made, and Brexit is scheduled for January.

Turning to the economic data, initial claims for unemployment insurance benefits caught many by surprising. Claims provide a timely assessment of the labor market and broader economy, but they are not perfect. New filings can be volatile, particularly around holidays, and that is why we put more emphasis on the four-week moving average rather than the week-to-week fluctuations. Keeping this in mind, the recent increase in initial claims should not raise a red flag. It has more to do with Thanksgiving and issues surrounding the seasonal adjustment than actual problems in the labor market.

Initial claims jumped by 49,000 to 252,000 in the week ended December 7, more than our well-above-consensus forecast. Claims are now above their break-even level—that consistent with no monthly job growth. However, the recent surge in initial claims is misleading. One reason we expected a noticeable increase in new filings in the week ended December 7 is because of the calendar configuration. The last time the calendar was configured similarly to this year was in 2013, and new filings are following a similar pattern around Thanksgiving, which fell on November 28 in both years.



Claims jumped in the same week in 2013. Therefore, we anticipate that new filings will continue to follow a similar pattern as in 2013 over the next few weeks. If this holds, initial claims will remain elevated this week before declining. We are in that awkward period each year when initial claims are less useful because of the timing of various holidays. There will be more noise than signal in initial claims through the rest of this year and early 2020.

Next week

Looking ahead to next week, we will get housing start, industrial production, existing-home sales, personal income and spending along with revisions to third quarter GDP.

We will publish our forecasts for next week's data Monday on Economic View.

EUROPE
By Barbara Teixeira Araujo of Moody's Analytics

Questions Remain After UK Vote

The week before Christmas will bring loads of economic releases for Europe. In the U.K., we will get the third-quarter GDP final estimate, as well as the monthly retail sales, unemployment and CPI reports. We expect them all to confirm the story that the momentum in the U.K. economy remains fragile, but that consumers remain crucial in keeping the economy afloat. That's because unemployment is still very low, and wages are rising fast, while inflation has taken a breather on the back of base effects in oil prices. Accordingly, we expect that the data next week will show that CPI inflation fell further below the bank's 2% target in November, depressed by a further decline in motor fuels inflation. The bad news for consumers is that this trend should start changing course from December or January—provided that the price of the Brent barrel remains steady at around $64—while underlying inflation pressures will continue to gradually pick up pace, in line with the wage gains.

Indeed, next week's labour market report is expected to show that joblessness in the U.K. remained at 3.8% in the three months to October, its lowest since 1974. Granted, the latest leading data have been all suggesting that the momentum in Britain's labour market has already peaked. They show that employment gains have begun to decelerate in recent months, while vacancies are rising. Even so, our view is that the labour market remains robust enough to allow for the unemployment rate to remain unchanged for now. We won't rule out a small increase during the first quarter of 2020, but joblessness is expected to remain historically low throughout next year as well—barring a Brexit disaster or a full-blown recession. This should allow for wages to continue to grow quickly, at a rate above 3% y/y. For the three months to October, we expect that headline pay growth (including bonuses) remained steady at 3.6% y/y, while we expect regular pay growth to have gained pace to 3.7% from 3.6%.

Low unemployment and strong wage growth are supporting household purchasing power, and we were not surprised to see that retail sales have continued to grow at a rate above 3% y/y over recent months. But while the trend in retailing is favorable, November's results will be tricky to analyse. That's because Black Friday sales happened at the very end of the month this year; the bulk of Black Friday-related purchases will only be accounted for in December's report. The Office for National Statistics normally adjusts the figures for seasonal patterns, but they are still struggling with their methodology, especially as this U.S.-imported holiday gains in importance every year. We thus wouldn't be surprised if retail sales underperformed in November, which would normally warrant a sharp rebound in December.

If this barrage of data wasn't enough, next week will also bring the Bank of England's last monetary policy meeting of 2019. We are not expecting much from the bank on Thursday, though. We think it would be premature for policy makers to act before we know more about how Brexit will play out next month. At the time of writing, the U.K. parliamentary election results were not out, but we expect that the Conservatives won a majority. This would mean parliament should be able to pass Boris Johnson's withdrawal agreement during the first half of January and that Brexit should finally happen by January 31. This would lift confidence in the short term, giving a boost to growth, especially to investment, and making a rate cut by the MPC unlikely in the first half of 2020. But risks will remain. The U.K. will still need to negotiate a comprehensive free trade agreement with the EU in less than a year, which looks like a very bold feat. Depending on the size of the Tory majority, hardline Brexiteers could make life miserable for Boris Johnson; trade negotiations could become fractious. If that is the case, we expect that firms and households will fear a no-deal Brexit by the end of the transition period on December 31, 2020, which will make them postpone major financial decisions. If growth falters further as a result, the MPC could be convinced to follow the dovish footsteps of the Fed or the ECB and lower rates. As of now, though, we do not have in our baseline any rate cuts next year.

	Key indicators	Units	Moody's Analytics	Last
Mon @ 10:00 a.m.	Italy: Consumer Price Index for November	% change yr ago	0.4	0.2
Mon @ 2:00 p.m.	Russia: Industrial Production for November	% change yr ago	2.5	2.6
Tues @ 9:30 a.m.	U.K.: Unemployment for October	%	3.8	3.8
Tues @ 10:00 a.m.	Euro Zone: External Trade for October	bil euro	17.1	18.7
Wed @ 9:30 a.m.	U.K.: Consumer Price Index for November	% change yr ago	1.4	1.5
Wed @ 10:00 a.m.	Euro Zone: Consumer Price Index for November	% change yr ago	1.0	0.7
Wed @ 2:00 p.m.	Russia: Retail Sales for November	% change yr ago	1.8	1.6
Wed @ 2:00 p.m.	Russia: Unemployment for November	%	4.6	4.6
Thur @ 9:30 a.m.	U.K.: Retail Sales for November	% change yr ago	3.2	3.1
Thur @ 12:00 p.m.	U.K.: Monetary Policy and Minutes for December	%	0.75	0.75
Fri @ 8:45 a.m.	France: Household Consumption Survey for November	% change	-0.1	0.2
Fri @ 9:30 a.m.	U.K.: GDP for Q3	% change	0.3	-0.2

ASIA-PACIFIC

By Katrina Ell of Moody's Analytics

China Likely to Show November Improvement

China's November activity data dump will likely show improvement after a generally disappointing October. We expect China's fixed asset investment, industrial production and retail trade all recorded modest acceleration in annual terms in November. Industrial production has been particularly weak, while fixed asset investment slowed for a fourth straight month in October. Delving into the detail of fixed asset investment, government investment is making up for private investment. On the industrial production front, several manufacturing industries weakened in October, including textiles, chemicals and machinery, while auto manufacturers recorded a sharp increase in production of 4.9% y/y in October, up from 0.5% in September.

Central banks in Japan, Indonesia and Thailand will hold their final meetings for 2019. All are expected to keep their policy rates on hold. Japan's government announced a stimulus package of around US$120 billion, which includes infrastructure spending, earlier in December. This maneuver by the government takes the pressure off the Bank of Japan from needing to act. The onus has shifted from monetary policy back to fiscal policy. But we don't have concrete dates on implementation, so our baseline remains the same, that Japan will fall into a technical recession after forecast contractions in GDP in the December quarter and the March quarter next year.

Elsewhere, Bank Indonesia will pause again in December, after leaving the seven-day repurchase rate at 5% in November following the cumulative 100 basis points of reductions in the past four months. However, in November, the central bank reduced banks' reserve requirement ratio by 50 basis points, marking the first cut since June. Bank Indonesia has a difficult balancing act trying to bolster domestic demand while maintaining external stability, with a particular focus on the rupiah. The reserve requirement ratio cut is a way to bolster domestic liquidity, without potentially pressuring capital outflows the same way a benchmark interest rate reduction does.

New Zealand's GDP growth likely rose by 0.5% q/q in the September quarter, unchanged from the expansion in the June quarter. Services are expected to again drive the bulk of the growth of the quarterly expansion. Merchandise exports will be a drag on quarterly growth, with shipments down by around 2%. Imports are forecast to rise by around 1% q/q, translating to net exports being a drag over the quarter. Annual GDP growth is forecast to improve to 2.3% in the September quarter, from 2.1% in the June quarter.

	Key indicators	Units	Confidence	Risk	Moody's Analytics	Last
Mon @ 1:00 p.m.	China Fixed asset investment for November	% change yr ago YTD	3		5.4	5.2
Mon @ 1:00 p.m.	China Industrial production for November	% change yr ago	3		5.2	4.7
Mon @ 1:00 p.m.	China Retail sales for November	% change yr ago	3		7.4	7.2
Mon @ 3:00 p.m.	Indonesia Foreign trade for November	US$ bil	2		0.09	0.16
Mon @ 11:00 p.m.	India Foreign trade for November	US$ bil	2		-9.8	-11.0
Tues @ Unknown	Singapore Nonoil domestic exports for November	% change yr ago	3		-9.8	-12.3
Wed @ 10:50 a.m.	Japan Foreign trade for November	¥ bil	2		-37.8	-34.7
Wed @ 6:00 p.m.	Thailand Monetary policy for December	%	3		1.25	1.25
Wed @ Unknown	Indonesia Monetary policy for December	%	3		5.0	5.0
Thurs @ 8:45 a.m.	New Zealand GDP for Q3	% change	3		0.5	0.5
Thurs @ 11:30 a.m.	Australia Unemployment rate for November	%	3		5.3	5.3
Thurs @ Unknown	Japan Monetary policy for December	¥ tril	3		80	80
Fri @ 10:30 a.m.	Japan Consumer price index for November	% change yr ago	2		0.7	0.4

The Long View

Third-quarter 2019's outstandings of U.S. nonfinancial corporate debt edged above $10 trillion for the first time ever.

By John Lonski, Chief Economist, Moody's Capital Markets Research Group
December 12, 2019

CREDIT SPREADS

As measured by Moody's long-term average corporate bond yield, the recent investment grade corporate bond yield spread of 112 basis points was less than its 122-point mean of the two previous economic recoveries. This spread may be no wider than 115 bp by year-end 2019.

The recent high-yield bond spread of 410 bp is thinner than what is suggested by the accompanying long-term Baa industrial company bond yield spread of 175 bp, but wider than what might be inferred from the recent below-trend VIX of 13.8 points.

DEFAULTS

November 2019's U.S. high-yield default rate of 3.9% may average 3.9% during 2020's first quarter, according to Moody's Investors Service.

US CORPORATE BOND ISSUANCE

Third-quarter 2018's worldwide offerings of corporate bonds showed year-over-year setbacks of 6.0% for IG and 38.7 % for high-yield, wherein US$-denominated offerings plunged by 24.4% for IG and by 37.5% for high yield.

Fourth-quarter 2018's worldwide offerings of corporate bonds incurred annual setbacks of 23.4% for IG and 75.5% for high-yield, wherein US$-denominated offerings plunged by 26.1% for IG and by 74.1% for high yield.

First-quarter 2019's worldwide offerings of corporate bonds revealed annual setbacks of 0.5% for IG and 3.6% for high-yield, wherein US$-denominated offerings fell by 3.0% for IG and grew by 7.1% for high yield.

Second-quarter 2019's worldwide offerings of corporate bonds revealed an annual setback of 2.5% for IG and an annual advance of 17.6% for high-yield, wherein US$-denominated offerings sank by 12.4% for IG and surged by 30.3% for high yield.

Third-quarter 2019's worldwide offerings of corporate bonds revealed annual advances of 15.2% for IG and 56.8% for high-yield, wherein US$-denominated offerings soared higher by 36.8% for IG and 81.3% for high yield.

During yearlong 2017, worldwide corporate bond offerings increased by 4.1% annually (to $2.501 trillion) for IG and advanced by 41.5% for high yield (to $603 billion).

For 2018, worldwide corporate bond offerings sank by 7.2% annually (to $2.322 trillion) for IG and plummeted by 37.6% for high yield (to $376 billion). The projected annual percent increases for 2019's worldwide corporate bond offerings are 5.4% for IG and 45.4% for high yield. When stated in U.S. dollars, issuers based outside the U.S. supplied 60% of the investment-grade and 59% of the high-yield bond offerings of 2019's first 10 months.

US ECONOMIC OUTLOOK

In view of the underutilization of the world's productive resources, low inflation should help to rein in Treasury bond yields. As long as the global economy operates below trend, the 10-year Treasury yield may not remain above 2.00% for long. A fundamentally excessive climb by Treasury bond yields and a pronounced slowing by expenditures in dynamic emerging market countries are among the biggest threats to the adequacy of economic growth and credit spreads.

The Long View

EUROPE

By Barbara Teixeira Araujo of Moody's Analytics
December 12, 2019

UNITED KINGDOM

Markets were on edge before Thursday's U.K. general elections. This vote is one of the most important in the country's history; it is decisive for Brexit and for the future of the British economy. If the Conservatives win the elections with a comfortable majority, it is almost certain that Prime Minister Boris Johnson will manage to pass his Brexit withdrawal deal through Parliament before the current deadline of January 31. This would mean that the U.K. would finally leave the EU almost four years after it voted to do so in a referendum.

While a Brexit in Johnson's terms is not our most optimistic scenario for the economy, in the short term it would nonetheless help remove some of the uncertainty that has been depressing confidence and growth for already so many quarters. The British public seems to agree, and all of the recent polls are showing the Tories continue to have a significant lead over Labour. But history has shown us that election polls can be unreliable in the U.K., and worrying is that the latest YouGov poll of polls showed that the Tories' lead has narrowed to only 28 from 68 over the past days. This means we cannot rule out the Conservatives winning with only a small majority, or a hung Parliament.

A small Tory majority would be a less than ideal outcome for the elections. Although Johnson would likely still manage to pass his withdrawal deal in such a scenario, the lack of a significant majority would make it extraordinarily hard for the prime minister to gather enough support for his policies during the upcoming trade negotiations with the EU. Those are expected to be even harder than the withdrawal negotiations were, especially as Conservative lawmakers each have their own opinion about how close the U.K.'s future relationship with the EU should be. This means uncertainty would persist, while a no-deal Brexit at the end of the year would remain a possibility.

A hung Parliament would be an even worse outcome. If Parliament remains fragmented, then it is uncertain whether Johnson's deal will be ratified, which means that the risk of a no-deal Brexit by January 31 still looms. This would keep the pound low but uncertainty high. In that case, we think that Parliament would vote for another Brexit delay, likely until the end of 2020.

ECB

Thursday was a crucial day for Europe; it was election day in the U.K. and it also brought Christine Lagarde her first monetary policy meeting at the helm of the European Central Bank. At the time of writing, we don't know yet who won in the U.K. We will have a better idea only when the first exit poll is published at 10:00 p.m. GMT or 5:00 p.m. EST. But at least Lagarde kept us busy. Granted, the ECB didn't announce any change to its policy instruments Thursday. But the truth is that we never expected it would do so since Lagarde first needs to establish herself and get the members of the bank's Governing Council fully behind her before contemplating any changes; that is, provided that the currency area's economy doesn't start falling off a cliff, in which case we don't think she would hesitate to follow Draghi's dovish footsteps and lower rates further.

Lagarde's press conference was a hit. She did relatively well for a first conference, skillfully skirting controversial answers. She focused on the upcoming comprehensive strategic review of the central bank's objectives, which is expected to start in January and be completed by the end of 2020. To markets' disappointment, though, she didn't give any details on what the ECB wants to accomplish with this review—will it lower, or maybe raise, its inflation target? Will it make it symmetrical? Also, one issue is that Lagarde might use the excuse of the strategic review to dodge hard questions regarding the effectiveness of the bank's different tools.

Another key point was that Lagarde sounded more optimistic about the euro zone's economic outlook. She repeated several times that, while growth remains subdued and risks are to the downside, there are increasing signs the economy is stabilizing. On the downside, Lagarde admitted that the latest ECB forecast for inflation in 2022—which sees CPI inflation averaging 1.6% y/y over the year—would not be consistent with the ECB's target of inflation close to, but below, 2%. This suggests that, all things staying equal, the central bank would still need to inject more stimulus into the economy to comply with its mandate.

Barring an economic disaster, we are sticking to our outlook of no further rate cuts over the coming year. The ECB needs to see how the additional stimulus translates into the real economy first, as banks now have little margin to further reduce lending rates.

The Long View

UNITED KINGDOM

The pound soared to a seven-month high against the dollar and to a one-month high against the euro on Wednesday, as markets became increasingly optimistic that the Conservatives will win the December 12 general elections with a comfortable majority. The Tories' lead had narrowed over the past few weeks, raising fears that a hung Parliament would result in prolonged uncertainty and further postponements of Article 50, but the latest YouGov poll of polls gave the Conservatives a nine-point lead over the Labour Party. The poll is putting support for the Tories at 42% and for Labour at 33%, which should be enough to give the Conservatives around 359 seats and a majority of 68.

But history has shown us that election polls can be unreliable in the U.K., and chances are that the Conservatives' lead could narrow further over this final week of campaigning as undecided voters make up their minds. Consumer confidence remains depressed, which is usually bad news for the incumbent governing party. We thus cannot rule out the Conservatives winning with only a small majority, or Parliament remaining fragmented.

A small Tory majority would be a less than ideal outcome for the elections. Although Boris Johnson would likely still manage to pass his withdrawal deal in such a scenario, the lack of a significant majority would make it extraordinarily hard for the prime minister to gather enough support for his policies during the upcoming trade negotiations with the EU. Those are expected to be even harder than the withdrawal negotiations were, especially as Conservative lawmakers each have their own opinion about how close the U.K.'s future relationship with the EU should be. Uncertainty would thus persist throughout next year, while a no-deal Brexit at the end of the transition period on December 31 would remain a possibility if no common ground is reached.
A hung Parliament would be an even worse outcome. If Parliament remains fragmented, then it is unsure whether Johnson's deal will be ratified, which means that the risk of a no-deal Brexit by January 31 still looms. This would keep the pound low but uncertainty high. In that case, we think that Parliament would vote for another Brexit delay, likely until the end of 2020.

ASIA PACIFIC

By Shahana Mukherjee of Moody's Analytics
December 12, 2019

INDONESIA

Japan's revised third quarter real GDP growth surprised on the upside, as seasonally adjusted real GDP grew at 0.4% q/q after a preliminary estimate of 0.1%. Private consumption expectedly played an important role in supporting the aggregate, with consumers increasing their purchases ahead of the sales tax increase on 1 October. The pickup in nonresidential investment, however, was surprising. It expanded by 1.8% on a quarterly basis, double the initial estimate and up from 0.2% in the second quarter. While government expenditure growth moderated, exports slumped over the quarter, declining by 0.6%, after a steady second quarter.

The latest reading marks a notable pickup in domestic activity prior to the sales tax hike, driven by strong investment and consumption. The lift in consumption was short term and expected. The surprise increase in investment, however, is a positive development since it signals that investors are not overly conservative regarding their near-term spending outlook. While this possibility bodes well for Japan's economy, the October activity data paint a different picture.

Retail sales plunged by 7.1% on a yearly basis in October, driven by sharp declines in sales of machinery and equipment, vehicles, and general merchandise. Household spending plummeted by 11.5% on a monthly basis in October, the fastest decline since April 2014, when consumers retreated following the previous consumption tax hike. Industrial production also suffered, falling by 4.2% on a monthly basis and reversing the previous month's gain. Machinery orders slid by 2.9% over the same period, led by a decline in manufacturing orders. Moreover, the external sector, which has been a persistent source of worry through most of 2019, did little to improve the situation. Exports fell sharply at an annual rate of 9.2% in October, extending September's decline and driven by significant declines in exports to China and the U.S.

Visible deterioration

The Long View

While the current slowdown marks a visible deterioration in consumer and investor sentiment following the transition to a higher sales tax regime and persistent weakness in global conditions, the situation was aggravated by the super typhoon that hit Tokyo in October as well as ongoing trade tensions with South Korea. Moreover, recent developments in the form of punitive tariffs on France, Brazil and Argentina announced by President Donald Trump signal further trade uncertainty, with potentially more severe effects. Such a development will have harsh ramifications for export-reliant economies such as Japan, which is contending with several domestically driven policy challenges.

The current situation will step up the need for policy stimulus. In this regard, the recently approved $122 billion fiscal package will be critical in supporting economic activity over the next two years, especially following the 2020 Tokyo Olympics. Monetary stimulus may also follow, but the Bank of Japan will exercise due caution, considering its limited scope for further monetary accommodation. For now, we expect weak domestic spending and the persistent slump in external demand to weigh heavily on domestic activity, with preliminary estimates suggesting GDP contracted in the December quarter.

Ratings Round-Up

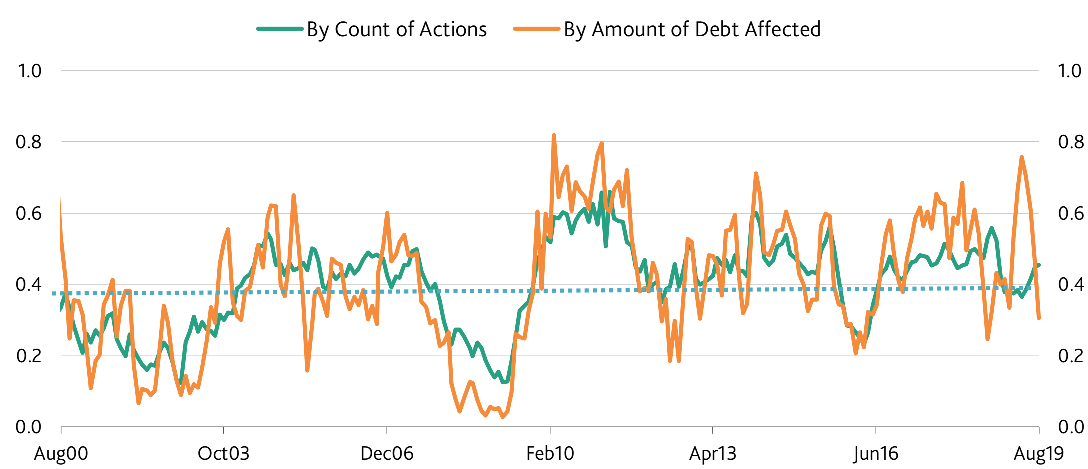
Upgrades Account for Most of Affected Debt in U.S. Changes

By Steven Shields

Fourteen U.S. firms received rating adjustments in the period ended December 9. Despite downgrades outnumbering upgrades 8 to 6, upgrades accounted for most of the debt affected. On December 4, Chesapeake Energy Corp.'s senior unsecured notes were downgraded from Caa2 to Caa3, reflecting its high debt leverage, weak asset coverage, an expected decline in production resulting from a materially reduced capital budget in 2020 and exposure to natural gas price weakness as it continues to attempt to transition to an oil-focused production mix. Meanwhile CHS/Community Health Systems Inc. senior secured notes were downgraded to Caa2 from Caa1, reflecting a higher probability of default occurring over the next 12 to 18 months as it is constrained by weaker liquidity. The change impacted roughly $13.5 billion in debt. Biopharmaceutical company Celgene Inc. received an upgrade on its senior unsecured notes to A3 from Baa2 following the acquisition of Celgene by Bristol-Myers Squibb Co. Over the past year, weekly rating changes have been largely concentrated among smaller, speculative-grade companies. Although these rating actions have been mostly negative, the downgrades are largely the result of idiosyncratic factors and not weakness in the broader U.S. economy.

European rating activity picked up during the period with eleven firms receiving a rating change. The most notable downgrade in terms of debt affected was Danske Bank A/S. The Danish bank senior secured notes were lowered to A3 from A2 following lowered earnings expectations, impacting $23 billion in outstanding debt. Four Irish banks received upgrades following Moody's Investors Service. Irish banking system outlook was revised to stable.

FIGURE 1
Rating Changes - US Corporate & Financial Institutions: Favorable as % of Total Actions



* Trailing 3-month average

Source: Moody's

FIGURE 2

Rating Key

BCF	Bank Credit Facility Rating	MM	Money-Market
CFR	Corporate Family Rating	MTN	MTN Program Rating
CP	Commercial Paper Rating	Notes	Notes
FSR	Bank Financial Strength Rating	PDR	Probability of Default Rating
IFS	Insurance Financial Strength Rating	PS	Preferred Stock Rating
IR	Issuer Rating	SGLR	Speculative-Grade Liquidity Rating
JrSub	Junior Subordinated Rating	SLTD	Short- and Long-Term Deposit Rating
LGD	Loss Given Default Rating	SrSec	Senior Secured Rating
LTCF	Long-Term Corporate Family Rating	SrUnsec	Senior Unsecured Rating
LTD	Long-Term Deposit Rating	SrSub	Senior Subordinated
LTIR	Long-Term Issuer Rating	STD	Short-Term Deposit Rating

FIGURE 3
Rating Changes: Corporate & Financial Institutions – US

Date	Company	Sector	Rating	Amount ($ Million)	Up/ Down	Old LTD Rating	New LTD Rating	IG/ SG
12/4/19	QUAD/GRAPHICS, INC.	Industrial	SrUnsec/SrSec /BCF/LTFR/PDR	243	D	B2	B3	SG
12/4/19	CHESAPEAKE ENERGY CORPORATION	Industrial	SrUnsec	8,287	D	Caa2	Caa3	SG
12/4/19	RENFRO CORPORATION	Industrial	SrSec/BCF /LTCFR/PDR		D	B3	Caa1	SG
12/5/19	COMMUNITY HEALTH SYSTEMS, INC. -CHS/COMMUNITY HEALTH SYSTEMS, INC.	Industrial	SrSec	13,467	D	Caa1	Caa2	SG
12/5/19	LOCKHEED MARTIN CORPORATION	Industrial	SrUnsec	15,213	U	Baa1	A3	IG
12/5/19	CARRIAGE SERVICES, INC.	Industrial	SrUnsec /LTCFR/PDR	400	D	B2	B3	SG
12/5/19	EVERI PAYMENTS INC.	Industrial	SrUnsec/SrSec /BCF/LTFR/PDR	375	U	Caa1	B3	SG
12/5/19	IMAGINE! PRINT SOLUTIONS, LLC	Industrial	SrSec/BCF /LTCFR/PDR		D	B3	Caa3	SG
12/5/19	TAPSTONE ENERGY, LLC	Industrial	SrUnsec /LTCFR/PDR	300	D	Caa2	C	SG
12/6/19	BRISTOL-MYERS SQUIBB COMPANY-CELGENE CORPORATION	Industrial	SrUnsec	19,850	U	Baa2	A3	IG
12/6/19	OWENS CORNING	Industrial	SrUnsec	2,905	U	Ba1	Baa3	SG
12/9/19	RITE AID CORPORATION	Industrial	PDR		U	Caa3	Caa1	SG
12/9/19	TRUIST FINANCIAL CORPORATION -NATIONAL PENN BANCSHARES, INC.	Financial	SrUnsec/LTIR /LTD/Sub/MTN/PS	27,240	D	A2	A3	IG
12/9/19	TRUIST FINANCIAL CORPORATION -SUNTRUST BANK	Financial	SrUnsec /LTIR/STD/LTD /Sub/MTN/PS	17,606	U	Baa1	A2	IG

Source: Moody's

FIGURE 4
Rating Changes: Corporate & Financial Institutions – Europe

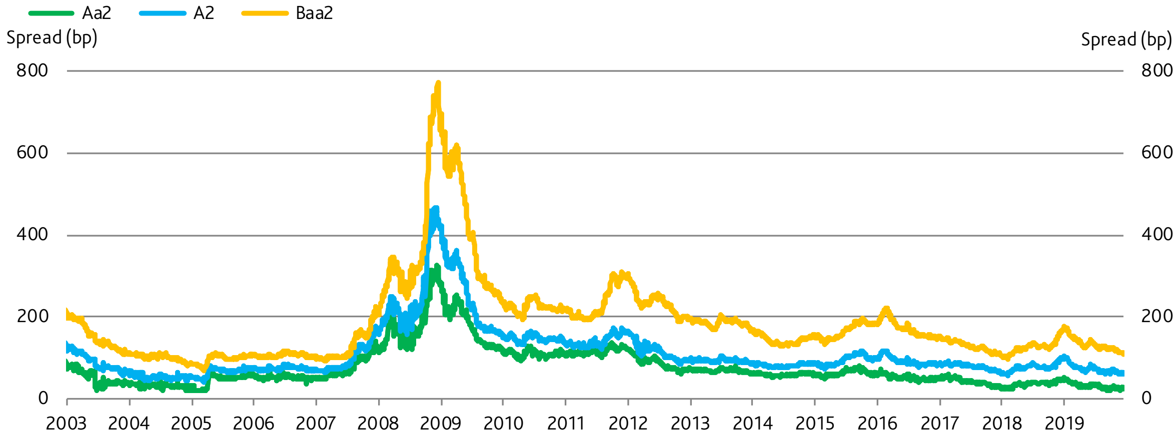
Date	Company	Sector	Rating	Up/ Down	Old LTD Rating	New LTD Rating	IG/ SG	Country
12/4/19	UNICREDIT S.P.A. -YAPI VE KREDI BANKASI A.S.	Financial	Sub/PS	D	Caa1	Caa2	SG	TURKEY
12/4/19	THE ROYAL BANK OF SCOTLAND GROUP PLC -ULSTER BANK IRELAND DAC	Financial	LTIR/LTD	U	Baa2	Baa1	IG	IRELAND
12/4/19	PERMANENT TSB GROUP HOLDINGS PLC	Financial	SrUnsec/LTIR /STD/LTD/MTN	U	Baa3	Baa2	IG	IRELAND
12/4/19	BANK OF IRELAND GROUP PLC	Financial	SrUnsec/LTIR/LTD /Sub/JrSub/MTN/PS	U	Baa3	Baa2	IG	IRELAND
12/4/19	AIB GROUP PLC	Financial	SrUnsec /Sub/MTN/PS	U	Baa3	Baa2	IG	IRELAND
12/5/19	K+S AG	Industrial	SrUnsec /LTCFR/PDR	D	Ba2	Ba3	SG	GERMANY
12/6/19	VALARIS PLC	Industrial	SrUnsec /LTCFR/PDR	D	Caa1	Caa2	SG	UNITED KINGDOM
12/6/19	OFFICINE MACCAFERRI S.P.A.	Industrial	SrUnsec /LTCFR/PDR	D	Caa1	Caa3	SG	ITALY
12/9/19	MALLINCKRODT PLC -MALLINCKRODT INTERNATIONAL FINANCE SA	Industrial	SrUnsec/SrSec /BCF/LTCFR	D	Caa3	Ca	SG	LUXEMBOURG
12/10/19	DANSKE BANK A/S	Financial	SrUnsec/JrSrUnsec /LTIR/MTN/PS/CP	D	A2	A3	IG	DENMARK
12/10/19	PROMONTORIA HOLDING 264 B.V.	Industrial	SrSec /LTCFR/PDR	D	B2	B3	SG	NETHERLANDS

Source: Moody's

Market Data

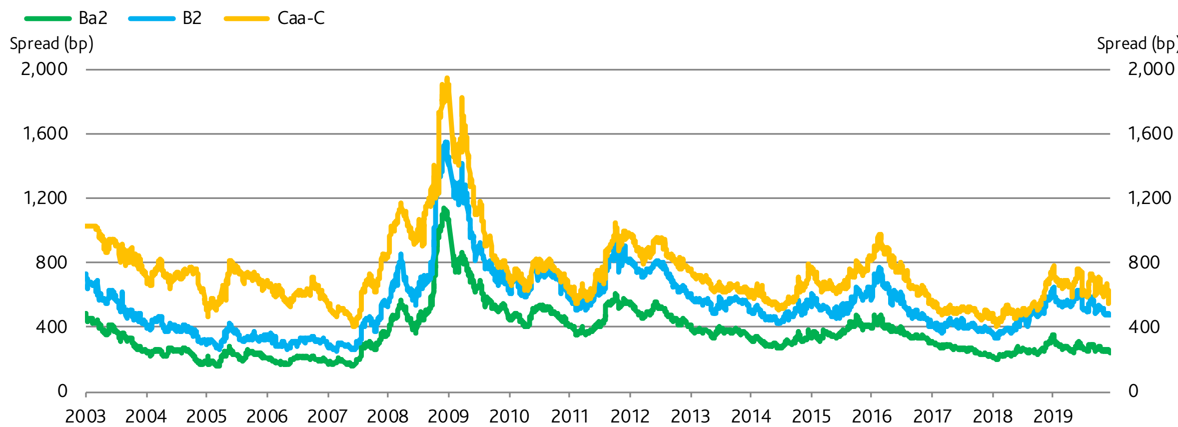
Spreads

Figure 1: 5-Year Median Spreads-Global Data (High Grade)



Source: Moody's

Figure 2: 5-Year Median Spreads-Global Data (High Yield)



Source: Moody's

Market Data

CDS Movers

Figure 3. CDS Movers - US (December 4, 2019 – December 11, 2019)

CDS Implied Rating Rises	CDS Implied Ratings		
Issuer	Dec. 11	Dec. 4	Senior Ratings
Nabors Industries Inc.	Caa2	C	B1
Diamond Offshore Drilling, Inc.	Caa2	Ca	B3
Citigroup Inc.	A2	A3	A3
Bank of America Corporation	A1	A2	A2
Wells Fargo & Company	A1	A2	A2
Morgan Stanley	A3	Baa1	A3
Citibank, N.A.	Baa1	Baa2	Aa3
Caterpillar Financial Services Corporation	A2	A3	A3
Altria Group Inc.	Baa1	Baa2	A3
Consolidated Edison Company of New York, Inc.	A3	Baa1	A3

CDS Implied Rating Declines	CDS Implied Ratings		
Issuer	Dec. 11	Dec. 4	Senior Ratings
Apple Inc.	Aa2	Aa1	Aa1
International Business Machines Corporation	A3	A2	A2
Bristol-Myers Squibb Company	Aa2	Aa1	A2
Coca-Cola Company (The)	Aa3	Aa2	A1
3M Company	Aa3	Aa2	A1
United Technologies Corporation	Aa3	Aa2	Baa1
PepsiCo, Inc.	A2	A1	A1
U.S. Bancorp	Aa2	Aa1	A1
Kraft Heinz Foods Company	Ba1	Baa3	Baa3
NextEra Energy Capital Holdings, Inc.	Baa2	Baa1	Baa1

CDS Spread Increases		CDS Spreads		
Issuer	Senior Ratings	Dec. 11	Dec. 4	Spread Diff
Frontier Communications Corporation	Caa3	7,862	7,506	356
Penney (J.C.) Corporation, Inc.	Caa3	3,198	2,913	285
Chesapeake Energy Corporation	Caa3	2,757	2,623	134
Staples, Inc.	B3	540	467	73
Pitney Bowes Inc.	Ba3	469	403	66
Sprint Communications, Inc.	B3	334	294	40
Pride International, Inc.	Caa2	1,565	1,531	34
Dillard's, Inc.	Baa3	130	112	18
Realogy Group LLC	B3	486	470	16
YRC Worldwide Inc.	Caa1	834	819	15

CDS Spread Decreases		CDS Spreads		
Issuer	Senior Ratings	Dec. 11	Dec. 4	Spread Diff
Neiman Marcus Group LTD LLC	Ca	5,629	5,845	-216
McClatchy Company (The)	C	1,851	2,011	-160
Nabors Industries Inc.	B1	655	783	-127
K. Hovnanian Enterprises, Inc.	Caa3	1,268	1,373	-106
Diamond Offshore Drilling, Inc.	B3	646	740	-94
Tenet Healthcare Corporation	Caa1	235	265	-30
United States Steel Corporation	B3	530	561	-30
Apache Corporation	Baa3	174	199	-25
R.R. Donnelley & Sons Company	B3	566	589	-23
Navistar International Corp.	B3	293	311	-18

Source: Moody's, CMA

Market Data

Figure 4. CDS Movers - Europe (December 4, 2019 – December 11, 2019)

CDS Implied Rating Rises	CDS Implied Ratings		
Issuer	Dec. 11	Dec. 4	Senior Ratings
Bankinter, S.A.	A3	Baa2	Baa1
Deutsche Bank AG	Baa2	Baa3	A3
CaixaBank, S.A.	Baa2	Baa3	Baa1
ING Groep N.V.	A1	A2	Baa1
Santander UK plc	A2	A3	Aa3
Greece, Government of	Ba2	Ba3	B1
Bayerische Landesbank	A1	A2	Aa3
Erste Group Bank AG	A2	A3	A2
Landesbank Baden-Wuerttemberg	A2	A3	Aa3
Anheuser-Busch InBev SA/NV	A2	A3	Baa1

CDS Implied Rating Declines	CDS Implied Ratings		
Issuer	Dec. 11	Dec. 4	Senior Ratings
United Kingdom, Government of	Aa1	Aaa	Aa2
BNP Paribas	Aa2	Aa1	Aa3
ENGIE SA	Aa2	Aa1	A3
GlaxoSmithKline plc	Aa1	Aaa	A2
Iberdrola International B.V.	Aa3	Aa2	Baa1
Air Liquide S.A.	Aa2	Aa1	A3
Unilever N.V.	Aa1	Aaa	A1
Bank of Scotland plc	Aa3	Aa2	Aa3
Autoroutes du Sud de la France (ASF)	Aa2	Aa1	A3
Airbus SE	Aa3	Aa2	A2

CDS Spread Increases		CDS Spreads		
Issuer	Senior Ratings	Dec. 11	Dec. 4	Spread Diff
PizzaExpress Financing 1 plc	Ca	4,568	4,378	190
Valaris plc	Caa2	1,442	1,410	32
TUI AG	Ba2	267	258	9
Casino Guichard-Perrachon SA	B3	654	648	6
Jaguar Land Rover Automotive Plc	B1	484	478	6
thyssenkrupp AG	Ba3	210	206	4
Thales	A2	27	24	3
Fiat Chrysler Automobiles N.V.	Ba2	110	108	2
Netherlands, Government of	Aaa	12	11	1
Barclays PLC	Baa3	59	58	1

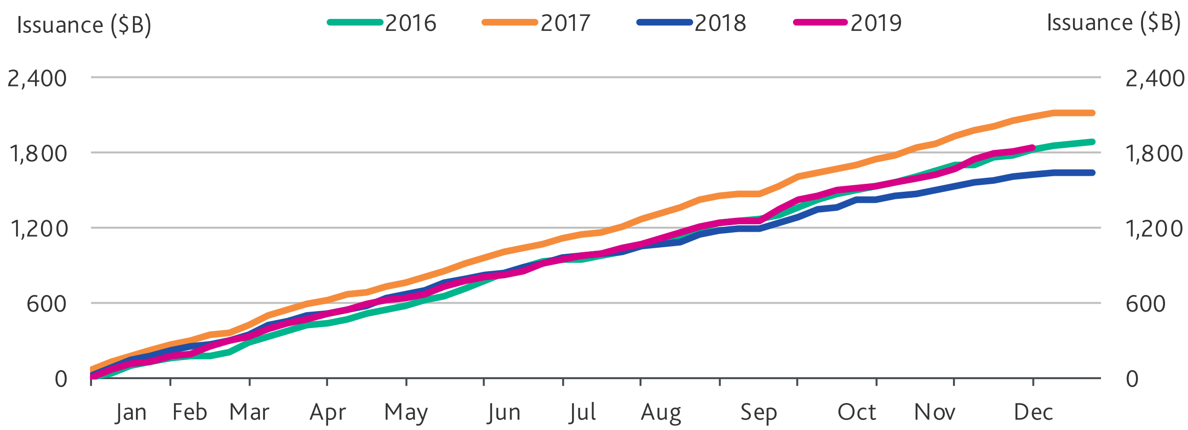
CDS Spread Decreases		CDS Spreads		
Issuer	Senior Ratings	Dec. 11	Dec. 4	Spread Diff
CMA CGM S.A.	Caa1	1,248	1,282	-34
Banca Monte dei Paschi di Siena S.p.A.	Caa1	302	333	-31
Atlantia S.p.A.	Ba1	227	254	-27
Boparan Finance plc	Caa1	1,827	1,853	-25
Sappi Papier Holding GmbH	Ba1	304	324	-20
Novafives S.A.S.	Caa2	688	705	-17
Banco Sabadell, S.A.	Baa3	84	100	-16
Greece, Government of	B1	130	146	-15
Banco Comercial Portugues, S.A.	Ba1	139	153	-15
Altice Finco S.A.	Caa1	254	268	-14

Source: Moody's, CMA

Market Data

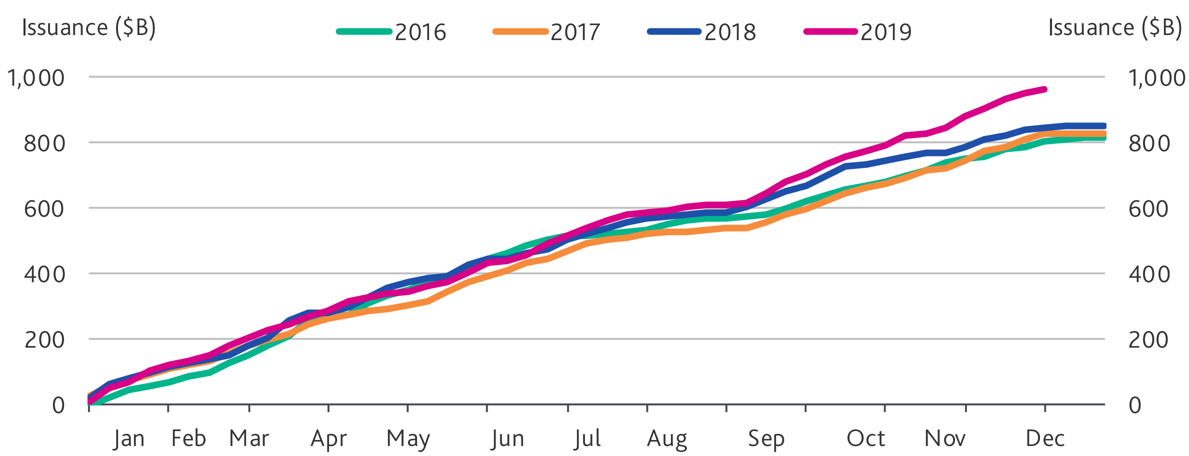
Issuance

Figure 5. Market Cumulative Issuance - Corporate & Financial Institutions: USD Denominated



Source: Moody's / Dealogic

Figure 6. Market Cumulative Issuance - Corporate & Financial Institutions: Euro Denominated



Source: Moody's / Dealogic

Market Data

Figure 7. Issuance: Corporate & Financial Institutions

	USD Denominated		
	Investment-Grade	High-Yield	Total*
	Amount $B	Amount $B	Amount $B
Weekly	17.716	10.024	32.166
Year-to-Date	1,308.797	426.257	1,838.623

	Euro Denominated		
	Investment-Grade	High-Yield	Total*
	Amount $B	Amount $B	Amount $B
Weekly	8.076	1.618	9.989
Year-to-Date	822.279	108.633	962.711

* Difference represents issuance with pending ratings.

Source: Moody's/ Dealogic

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