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CAPITAL MARKETS RESEARCH

MOODY'S ANALYTICS

# WEEKLY MARKET OUTLOOK

Moody's Analytics Research

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# Resurgent COVID-19 Threatens Corporate Credit's Improved Trend

## Credit Markets Review and Outlook *by John Lonski*

Resurgent COVID-19 Threatens Corporate Credit's Improved Trend

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| | |
|---|---|
| Credit Spreads | Investment Grade: Year-end 2020's average investment grade bond spread may be above its recent 118 basis points. High Yield: The high-yield spread may be close to its recent 525 bp by year-end 2020. |
| Defaults | US HY default rate: According to Moody's Investors Service, the U.S.' trailing 12-month high-yield default rate jumped from September 2019's 3.4% to September 2020's 8.5% and may average 9.8% during 2020's final quarter. |
| Issuance | For 2019's offerings of US$-denominated corporate bonds, IG bond issuance rose 2.6% to \$1.309 trillion, while high-yield bond issuance surged by 55.8% to \$432 billion.<br>In 2020, US\$-denominated corporate bond issuance is expected to soar higher by 49.4% for IG to a record 1.956 trillion, while high-yield supply may rise 21.9% to a record-high \$531 billion. |

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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 Capital Markets Economist, Moody's Capital Markets Research

# Resurgent COVID-19 Threatens Corporate Credit's Improved Trend

COVID-19 will determine the near-term fate of the U.S. and world economies in 2021. If resurgent coronavirus infections prompt another broad shutdown of businesses, US real GDP will again contract sequentially. At the other extreme, a vaccine for the virus would significantly enhance 2021's outlook.

Though the pandemic remains a major threat, the consensus view of 49 economists contributing to early November's Blue-Chip survey has 2021's U.S. real GDP growing by 4.0% annually after shrinking by an expected 3.7% in 2020. The consensus growth outlook for 2021 is between the 2.9% rise predicted by the lowest 10 forecasts and 5.0% advance projected by the 10 highest forecasts. Thus, even the lowest projections are consistent with an economic recovery for 2021.

However, a recovery in the context of tangible COVID-19 risks requires sufficient financial assistance for those households, businesses and public-sector entities most adversely affected by the virus.

### Where the Jobs Aren't Tells Us Where Help Is Needed

October's jobs report and the continued slide by the weekly estimates for first-time applications for and the number receiving state jobless benefits suggest that $2.3 trillion of additional fiscal stimulus might be overkill. Nevertheless, fiscal relief is needed in hard-hit occupations. The following may offer insight regarding where help is most needed.

Since payrolls generally peaked in February 2020, the deepest loss of jobs has been in restaurants and bars, where payrolls shrank by 2.1 million or 16%. The next biggest loss was the 1.0 million jobs cut from public-sector education that approximates 9% of that category's February tally.

The other big job losers from February through October include entertainment and recreation (down 732,000, or 29%), lodging (down 656,000, or 31%), manufacturing (down 621,000, or 5%), private education (down 376,000, or 9%) and commercial airlines (down 125,000, or 24%).

The rare instances of payrolls growth since February include the 124,000 new federal government jobs (up 5%), building materials stores (up 94,000 jobs or 7%), and food stores (up 55,000 or 2%).

### Upgrades Top Downgrades Thus Far in 2020's Final Quarter

The distribution of U.S. company credit rating revisions is greatly improved compared to what transpired in 2020's first half. Credit rating upgrades have outnumbered downgrades thus far during 2020's final quarter. Debt refinancings, infusions of equity capital, mergers and acquisitions, as well as improved outlooks for operating earnings have abetted the stabilization of corporate credit quality.

A preliminary count of U.S. high-yield credit rating changes shows 36 upgrades and 25 downgrades, while the rating revisions of U.S. investment-grade issuers include two downgrades and five upgrades. In terms of net downgrades, high-yield is at -11 and investment-grade is at -3.

After averaging 51 per quarter during calendar-year 2019, the arrival of the COVID-19 recession would then drive U.S. net high-yield downgrades up to the 194 of 2020's first quarter and the record-high 368 of the second quarter. By 2020's third quarter, U.S. net high-yield downgrades had plunged to 29. If the current trend holds, the net high-yield downgrades of 2020's final quarter may post their first negative score since the -7 of 2018's final quarter.

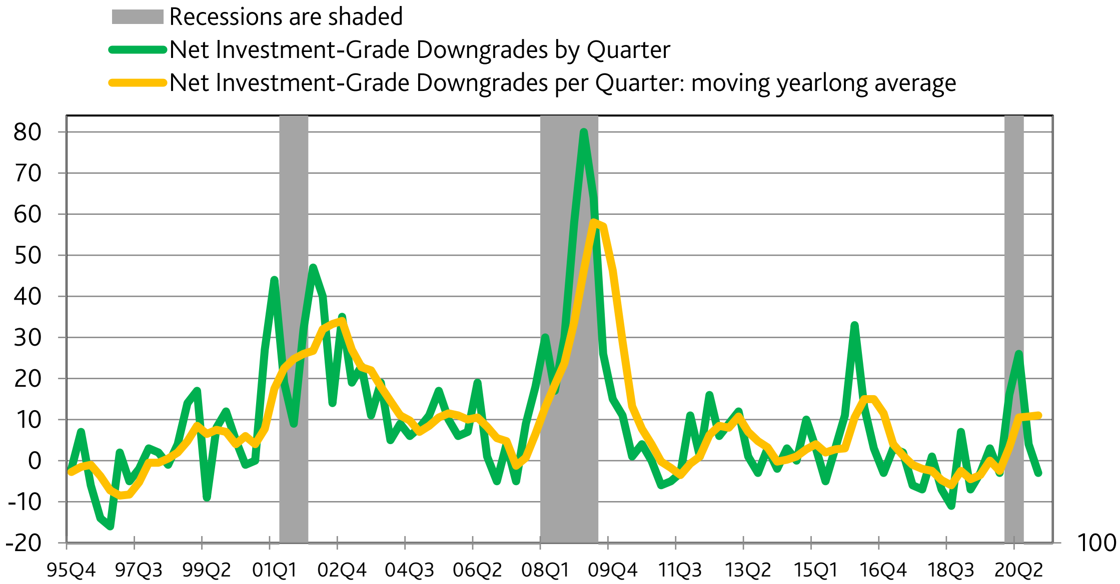
Net U.S. investment-grade downgrades averaged -1 per quarter during calendar-year 2019. The COVID-19 recession then drove U.S. net investment-grade downgrades up to the 21 of 2020's first quarter and the 26 of the second quarter. The latter was the highest such count for any quarter since the 33 of 2016's first quarter.

By 2020's third quarter, U.S. net investment-grade downgrades had dropped to 7. If the current trend holds, the net high-yield downgrades of 2020's final quarter may post their first negative score since the -10 of 2019's second quarter.

The Fed's unprecedented support of investment-grade corporate bonds has helped to rein-in the net downgrades of U.S. investment-grade corporations. The moving yearlong average of net investment-grade downgrades per quarter may have already peaked at the 11 of 2020's third quarter, which is less than its three previous major peaks of 15 for 2016's third quarter, 58 for 2009's second quarter, and 34 for 2002's final quarter. Regarding the latter, the moving yearlong average number of net investment-grade downgrades per quarter did not crest until one year after the end of 2001's recession. During calendar-year 2001, the net downgrades of U.S. investment-grade corporations averaged 26 per quarter.

**Figure 1: COVID-19 Driven Upturn by Net Investment-Grade Downgrades Has Been Tame Compared to Prior Recessions**

*U.S. issuers ex utilities; sources: Moody's Investors Service, Moody's Analytics*



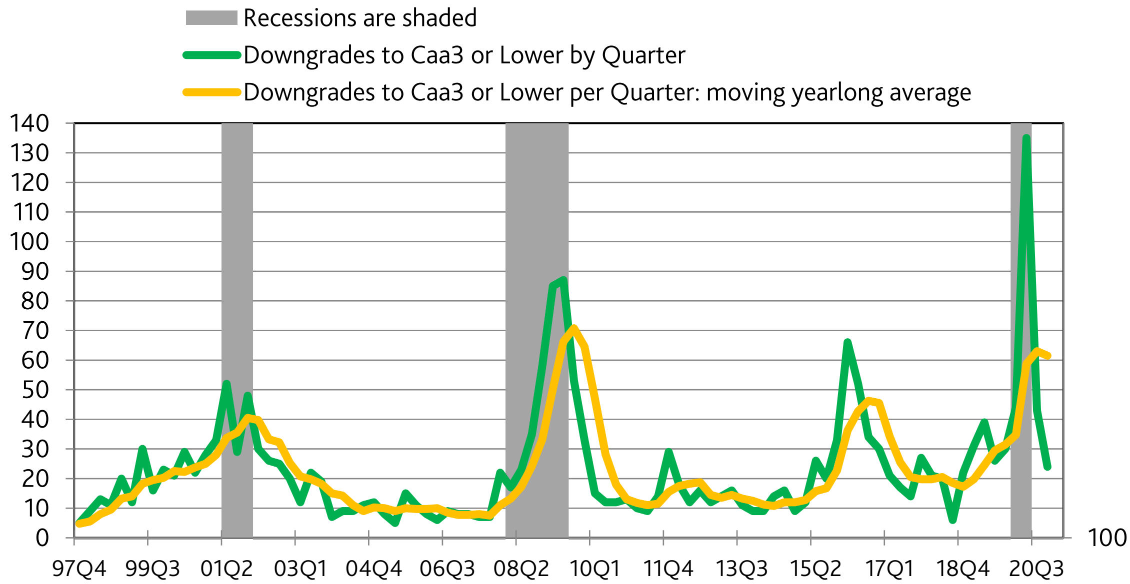

One way of assessing the risks implicit to high-yield rating downgrades involves counting the number of downgrades to Caa3 or lower. The direction taken by the moving yearlong average of the number of these downgrades offers insight regarding where the high-yield default rate is headed. In order to facilitate comparisons with the quarterly tallies, the number of downgrades to Caa3 or lower per quarter over a yearlong span is employed.

Following yearlong 2019's average of 32 downgrades per quarter, the number of U.S. company credit rating downgrades to Caa3 or lower rose to 44 in 2020's first quarter and then skyrocketed to a record-high 135 in the second quarter.

However, a partial recovery by business sales, ample systemic liquidity, and an equity market rally quickly pared the number of downgrades to Caa3 or lower to 43 during 2020's third quarter. For the fourth quarter to date, there have been only six downgrades to Caa3 or lower, which barely exceeds the accompanying five upgrades from ratings that were no greater than Caa3.

**Figure 2: Number of Downgrades to Caa3-or-Lower Drops from Q2-2020's Record High... Yearlong AverageFalls Short of Q3-2009's Apex**

*U.S. issuers; sources: NBER, Moody's Investors Service, Moody's Analytics*




For now, it appears as though the moving yearlong average number of downgrades to Caa3 or lower peaked at the 63 of 2020's third quarter. The latter falls short of the record-high 71 per quarter of 2009's third quarter. And that may be yet another reason to expect a topping off of the U.S. high-yield default rate at something significantly less than November 2009's post-Depression high of 14.7%.

After dipping from August 2020's 10.5-year high of 8.8% to October's 8.3%, the baseline estimate found in October 2020's "Monthly Default Report" of Moody's Investors Service has the U.S. high-yield default rate cresting at March 2021's 10.4% and then easing to 8.2% on average during July-October 2021. When weighted by the dollar amount of debt outstanding debt, the U.S. high-yield default rate dipped from August 2020's latest high of 6.6% to October's 6.45%.

### Speculative-grade Bond Yield Rises from November 9's Record Low

Hints of success at developing a COVID-19 vaccine prompted a breathtaking rally by high-yield bonds that slashed Bloomberg/Barclays speculative-grade bond yield by 46 basis points on Monday, November 9 to a record low 4.56%. However, the spec-grade bond yield quickly rose to 4.73% on November 10. Nevertheless, the latter was still under its pre-2020 nadir of 4.83% from June 2014.

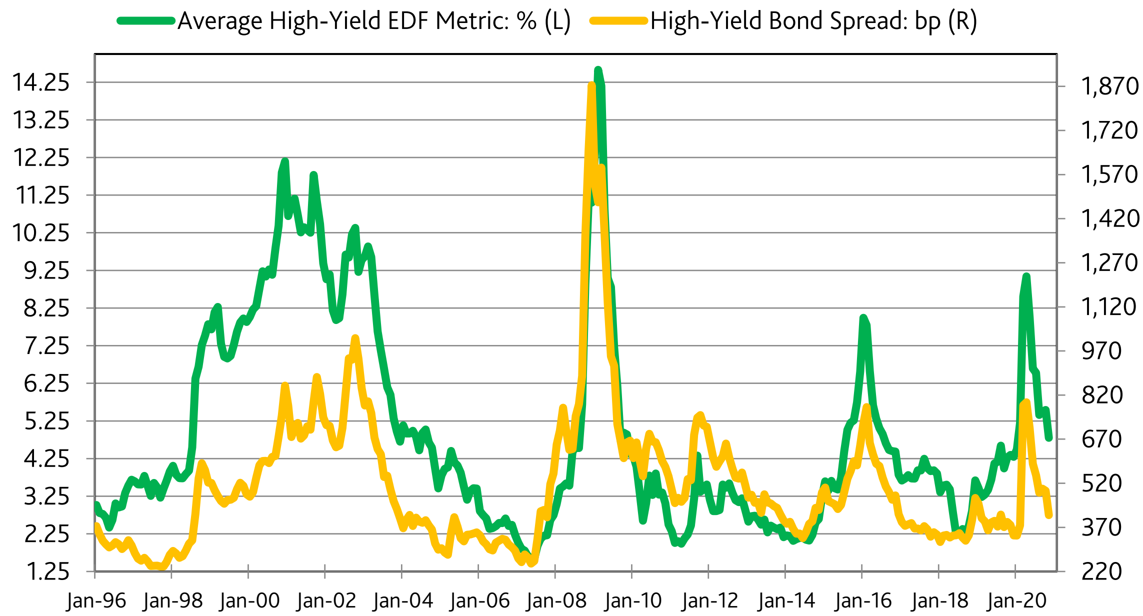
Despite the -11 net high-yield downgrades of the fourth quarter to date, November 10's high-yield bond spread appears to be too low given the still considerable risk of a jarring loss of business sales to resurgent COVID-19.

The sudden descent by the spec-grade bond yield narrowed the high-yield bond spread to 412 bp as of November 10 for its narrowest band since late February 2020. During January-February 2020, the high-yield bond spread averaged 359 bp.

However, the durability of a high-yield bond spread that is less than its long-term median of 463 bp is very much in doubt. One indicator of default risk says the high-yield bond spread is likely to widen to a band that exceeds its long-term median.

Though Moody's Analytics' average expected default frequency metric for U.S./Canadian high-yield issuers has plummeted from a March 18, 2020 high of 10.6% to November 11's 4.8%, the latter EDF still exceeds its long-term median of 3.9%. As inferred from the historical record, the high-yield EDF favors a 480 bp midpoint for the high-yield bond spread. Still, it is worth noting that during the last extended stay of more high-yield upgrades than downgrades, the high-yield bond spread averaged 370 bp during 2018's second half. Moreover, the average high-yield EDF favors a less than 6% midpoint for the high-yield default rate of August 2021.

**Figure 3: Average High-Yield EDF Metric Warns of a Wider High-Yield Bond Spread**
*month-long averages; sources: Bloomberg/Barclays, Moody's Analytics*



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

THE U.S.
By Mark Zandi, Chief Economist, Moody's Analytics

## When the Election Is in the Rearview

It is now clear that Joe Biden will be the nation's 46th president. With some of the script still unwritten, odds are high that Republicans will continue to control the Senate and Democrats the House, though with thinner majorities. There will be a divided government.

And our election model got it right—almost. The model of the Electoral College based on a range of political and economic variables had Biden winning with 279 electoral votes. By Thursday, the Associated Press had his total at 290, with few states yet to be called. We also expected the Senate to remain Republican and the House Democratic. Econometric analysis beat the polling hands down, at least in this election.

Stock prices have risen strongly on the election results, and long-term Treasury yields are down. The reaction in financial markets to the election is telling us a lot about what investors think it all means for the economy. Most immediately, investors appear to be betting that the election results will be settled reasonably soon. Worries that vote counts would be seriously contested and ultimately dragged all the way to the Supreme Court weeks from now appear overdone. The race was close, but not close enough for President Trump to credibly argue that cheating changed the outcome. Besides, there is no evidence of cheating.

Stock investors also appear cheered by the prospects for a divided government that will make fundamental changes to economic policy more difficult. Getting any major legislation into law won't be easy. Remember President Obama's second term? It seemed he was constantly doing political battle with a recalcitrant Republican Senate. Not much economic policy of consequence got done. There is a chance that Biden's long-standing relationship with Senate leader Mitch McConnell, who also led the Senate when Obama was president, may result in more compromise this go-around. But with the country still extraordinarily divided, that is less than likely.

Shareholders are particularly wary of Biden's proposal to increase taxes on corporations—he has proposed raising the top marginal rate from 21% to 28%—which would mean less cash to make dividend payments and to buy back shares. They are also no fans of Biden's proposal to raise capital gains taxes, and have been doing some handwringing over Biden's desire to increase the federal minimum wage. It is hard to see any of this happening now.

Bond investors have pushed down long-term interest rates—10-year Treasury yields fell 10 basis points on Election Day. This signals that investors believe economic growth will be slower because of the divided government, at least compared with the policy and resulting growth that would have come with a Democratic sweep, which, given the polling, investors had been discounting just prior to the election.

They would be right. We expect a President Biden and split Congress to come to terms on another fiscal rescue package on the other side of the presidential inauguration early next year, but it will be on the smaller side. Prior to the election, lawmakers were coalescing around a $2 trillion fiscal package that never came to fruition. Senate Republicans balked at the cost and at helping out hard-pressed state and local governments. These same Republicans will push back even more on a President Biden, resulting in a package closer to half the size, and with little for state and local governments. Lawmakers might agree to a fiscal package in the next few weeks during the lame duck, although such a move would likely require clearer evidence that the economy threatens to stall out with the intensifying pandemic. Friday's jobs numbers for October indicate the recovery is slowing but not enough to pressure lawmakers to come up with additional help for the economy.

Even more consequential for growth are dashed prospects for additional fiscal support to jump-start the economy once the pandemic is over. A Democratic sweep of government would have held good odds for support including many of Biden's proposals for more investment in infrastructure, housing and education, and spending on healthcare, child and elder care. During the campaign, Biden had proposed more than $7 trillion in additional government investment and spending over the next decade. This would have been a boon to growth, but not much of it is likely to happen with a split government.

However, there are things a President Biden will do without Congress via executive orders. President Trump used executive orders aggressively to ramp up his tariff wars with China and other big trading partners, severely restrict foreign immigration, both legal and undocumented, and significantly scale back regulations, especially on the fossil fuel and utility industries.

Given Trump's muscular use of executive orders, Biden will be empowered to do the same—to flip Trump's orders on their head. He would quickly end Trump's tariffs on our allies, and while he would continue to confront China—like Trump, he feels China doesn't trade fairly—he wouldn't do so with higher tariffs. Not that he will lower the existing tariffs on China without some concessions from the Chinese. Moreover, he would work through the World Trade Organization and team up with our allies to put collective pressure on the Chinese to change their behavior. Biden has also talked about re-engaging on the Trans-Pacific Partnership—the free-trade deal between the U.S. and other Pacific Rim nations that excludes China, because it doesn't abide by the rules—although re-engagement would ultimately require legislation.

On immigration, Biden has said he would quickly reset things to where they were pre-Trump. In the quarter century prior to Trump, close to 1 million foreign immigrants came to the U.S. each year. That number was cut approximately in half during Trump's presidency. It won't take long for a Biden administration to restore immigration. Biden will also reinstate the "dreamer" program, which allows those brought to the U.S. illegally as children to stay in the country.

Given Biden's strongly expressed views on the threats posed by climate change, he is sure to quickly re-engage on the Paris Climate Agreement and resurrect strict regulations on the fossil fuel industry. Drilling, and fracking, on federal lands will largely end, and there will be a recommitment to fuel economy standards for vehicles. Regulation of the financial system will also be strengthened under the Biden administration, particularly with regard to consumer protections and creditors in the non-bank or shadow system. Privatization of Fannie Mae and Freddie Mac, which their regulator the FHFA has been aggressively pursuing, also appears meaningfully less likely.

While hard to quantify, the economy will benefit from Biden's respect for the independence of the Federal Reserve to conduct monetary policy. President Trump often railed against the Fed and Chairman Jay Powell as the Fed was working to normalize interest rates. Trump also actively worked to stack the Fed with his cronies. Biden as president is sure to re-establish the core principal that an independent central bank is necessary for a well-functioning market economy. However, Biden has weighed in on the Fed, saying that it should consider the large existing racial wealth gaps when setting monetary and regulatory policies. Moreover, with no prodding from the Biden administration, but with its tacit approval, the Fed also seems likely to focus more on the risks climate change poses to the financial system, something like central banks in Europe and Asia are already doing.

Biden has already begun planning to dramatically shift the federal government's response to the pandemic. He has rightly made the point that as long as the virus is raging the economy will struggle. He will not leave it to states and localities and the patchwork response that has failed to contain the virus. This will unlikely mean widespread business shutdowns like in March and April, but it will likely mean more consistent and stricter mask-wearing and social-distancing rules across the country. The result will be a stronger economy as infections, hospitalizations and deaths moderate.

With the election outcome sticking to our expectations, the fiscal policy assumptions underlying our baseline (most likely) outlook, and thus our projections for the economy's performance, are unchanged. We expect real GDP to decline 3.6% this year, and increase 4.1% in 2021 and 3.7% per annum over Biden's first term. With this growth, the economy would make its way back to full employment—a mid-4% unemployment rate—by late 2023. Of course, there are many other assumptions that underpin this outlook, most importantly that the COVID-19 pandemic will largely wind down by this time next year, one way or another.

This election has been a painful experience, but it will soon be behind us. Few of us will be completely happy with the outcome, but simply having a clear political path forward will go a long way to shoring up frayed psyches and the struggling economy.

## Next Week

Retail sales for October will be telling. Sales have seen a stunning recovery from the severe, if brief, recession that decimated the economy in the spring, but support from fiscal programs and the shift in spending from services to goods has seemed set to fade. The housing market also has been strong, and fresh indicators to watch in the coming week include the NAHB housing market index, new residential construction (which had dipped slightly in September), existing-home sales (which in September reached their highest level since May 2006), and MBA mortgage applications. We also will get new data on import and export prices, industrial production, business inventories, the New York State manufacturing, and the Census Bureau's quarterly services survey.

## EUROPE

By Ross Cioffi of Moody's Analytics

### Euro Zone Consumer Prices Likely to Slide for October

Final estimates for October CPI inflation in Italy, the U.K. and the euro zone are due next week and will lead the economic news. We expect Italian consumer prices declined 0.3% y/y in October, this would be an improvement on the 0.6% decline in September. Prices fell by less in October as core inflation and unprocessed food prices strengthened. Even energy prices fell by less during the month, but these were still the main factor behind the negative inflation rate. We expect a similar dynamic in the rest of the euro zone, where consumer prices likely slid 0.3% y/y in October, as they did in September. According to the preliminary release, year-on-year energy prices decreased further during the month. Moreover, although the decline in core industrial goods prices softened from September, services inflation slowed for yet another month.

Meanwhile U.K. inflation likely firmed to 0.8% y/y in October from 0.5% in September, even as the third quarter rebound in the economy came to an end. The outlook from now on is tilted to the downside as demand is set to fall again during the winter and spring with the second wave of COVID-19 infections. Indeed, for this reason we already expect a decrease in retail sales in October. We foresee U.K. retail sales sliding 0.6% from September, a month that saw a solid 1.5% increase. This would leave retail sales still well above last year's level, but the trend will be pointing downhill as job losses pick up and consumer sentiment darkens.

Finally, news from Russia won't paint as bright a picture for October. We expect industrial production contracted 6% y/y in October, worsening on September's 5% decline. This will likely come as demand for oil faltered in Europe, Russia's main export market, while the second wave of COVID-19 mounted in the Continent. Unemployment also is expected to worsen to 6.6% from 6.3% in September as demand remains weak in the domestic economy. A second wave of infections mounted rapidly over the course of October in Russia as well, but the country is holding off on imposing another country-wide lockdown. Targeted measures will still sting, as will the increase in precautionary savings of firms and households, which we think will show through continued year-on-year declines in retail sales during the month.

| | Key indicators | Units | Moody's Analytics | Last |
|---|---|---|---|---|
| Mon @ 11:00 a.m. | Italy: Consumer Price Index for October | % change yr ago | -0.3 | -0.6 |
| Tues @ 6:00 p.m. | Russia: Industrial Production for October | % change yr ago | -6.0 | -5.0 |
| Wed @ 9:00 a.m. | U.K.: Consumer Price Index for October | % change yr ago | 0.8 | 0.5 |
| Wed @ 12:00 p.m. | Euro Zone: Consumer Price Index for October | % change yr ago | -0.3 | -0.3 |
| Fri @ 9:00 a.m. | U.K.: Retail Sales for October | % change | -0.6 | 1.5 |
| Fri @ 6:00 p.m. | Russia: Retail Sales for October | % change yr ago | -2.6 | -3.0 |
| Fri @ 6:00 p.m. | Russia: Unemployment for October | % | 6.6 | 6.3 |

## Asia-Pacific

By Xiao Chun Xu and Shahana Mukherjee of Moody's Analytics

## Japan GDP Rebounds after Second-Quarter Drop

Japan's GDP is likely to have rebounded slightly in the September quarter, having risen by 3% on a quarterly basis, following a 7.9% decline in the June quarter. The COVID-19 pandemic triggered an unprecedented shock to Japan's economy in the prior quarter as domestic restrictions eroded household sentiment and undermined consumer spending, while the hit to overseas demand battered Japanese exporters and deepened the downturn.

Even though economic activity has resumed since restrictions were eased in May, a slow revival in the overseas demand for durables has weighed heavily on Japan's external position, while subdued confidence in the wake of the domestic second wave of the virus held back household spending through the September quarter, giving rise to further deterioration in the labour market. Soft aggregate demand conditions and a weaker labour market are expected to have weighed on the third quarter rebound, even though a sizeable fiscal spend is likely to have offset some of this decline.

Thailand's GDP is likely to have contracted by a narrower margin in yearly terms in the September quarter, following a 12.2% decline in the prior quarter. The second-quarter downturn was led by a sharp collapse in exports (down 28%) and private consumption (down 6.7%). The settling of the domestic coronavirus outbreak has supported the revival in domestic spending since July; however, the significant weakness in overseas demand and the prolonged pause in tourism is expected to have weighed heavily through the September quarter, giving rise to another quarter of contraction.

Australia's unemployment rate is likely to have risen to 7% in October, from 6.9% in September. Despite most of Australia being in recovery and income support provided through the fiscal stimulus package, the pickup in spending has been weak and uneven. Moreover, the Victoria-centred restrictions have amplified the downturn in prospects since August. Even though these restrictions were eased in recent weeks, the October reading is expected to reflect the strain from the curbs, with services-oriented industries likely to see the sharpest declines.

| | Key indicators | Units | Moody's Analytics | Confidence | Risk | Last |
|---|---|---|---|---|---|---|
| Mon @ 10:50 a.m. | Japan GDP for Q3 | % change | 3.0 | 3 | ↓ | -7.90 |
| Mon @ 1:00 p.m. | China Industrial Production for October | % change yr ago | 6.3 | 3 | ↓ | 6.9 |
| Mon @ 1:00 p.m. | China Retail Sales for October | % change yr ago | 4.0 | 3 | ↓ | 3.3 |
| Mon @ 1:00 p.m. | Indonesia Foreign Trade for October | US$bil | 2.1 | 3 | ↓ | 2.4 |
| Mon @ 1:30 p.m. | Thailand GDP for Q3 | % change yr ago | -6.0 | 3 | ↓ | -12.2 |
| Tues @ 11:30 a.m. | Singapore Foreign Trade for October | % change yr ago | 3.5 | 2 | ↓ | 5.9 |
| Wed @ 10:50 a.m. | Japan Foreign Trade for October | ¥bil | 120 | 3 | ↓ | 675 |
| Thur @ 11:30 a.m. | Australia Unemployment for October | % | 7.0 | 3 | ↑ | 6.9 |
| Fri @ 10:30 a.m. | Japan Core CPI for October | % change yr ago | -0.3 | 3 | ← | -0.3 |

# The Long View

## A possible return of widespread shutdowns would widen spreads and increase corporations' demand for cash.

By John Lonski, Chief Capital Markets Economist, Moody's Capital Markets Research
November 12, 2020

### CREDIT SPREADS

As measured by Moody's long-term average corporate bond yield, the recent investment grade corporate bond yield spread of 118 basis points resembled its 116 basis-point median of the 30 years ended 2019. This spread may be no wider than 135 bp by year-end 2020.

The recent high-yield bond spread of 462 bp is thinner than what is suggested by the accompanying long-term Baa industrial company bond yield spread of 177 bp and the recent VIX of 26.3 points. The latter has been historically associated with a 715-bp midpoint for a composite high-yield bond spread.

### DEFAULTS

October 2020's U.S. high-yield default rate of 8.3% was up from October 2019's 3.8% and may average 10.3% during 2021's first quarter.

### US CORPORATE BOND ISSUANCE

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.

Fourth-quarter 2019's worldwide offerings of corporate bonds revealed annual advances of 15.3% for IG and 329% for high-yield, wherein US$-denominated offerings dipped by 0.8% for IG and surged higher by 330% for high yield.

First-quarter 2020's worldwide offerings of corporate bonds revealed annual advances of 17.7% for IG and 26.5% for high-yield, wherein US$-denominated offerings increased 43.7% for IG and grew 21.4% for high yield.

Second-quarter 2020's worldwide offerings of corporate bonds revealed annual surges of 69% for IG and 31% for high-yield, wherein US$-denominated offerings increased 142% for IG and grew 45% for high yield.

Third-quarter 2020's worldwide offerings of corporate bonds revealed an annual decline of 6% for IG and an annual advance of 44% for high-yield, wherein US$-denominated offerings increased 12% for IG and soared upward 56% for high yield.

For 2019, worldwide corporate bond offerings grew by 5.4% annually (to $2.447 trillion) for IG and advanced by 49.2% for high yield (to $561 billion). The projected annual percent increases for 2020's worldwide corporate bond offerings are a 15.5% for IG and 16.0% for high yield.

### US ECONOMIC OUTLOOK

Unacceptably high unemployment and other low rates of resource utilization will rein in Treasury bond yields. As long as the global economy operates below trend, 1.00% will serve as the upper bound for the 10-year Treasury yield. Until COVID-19 risks fade substantially and election year risks recede, wider credit spreads are possible.

# Europe

By Anna Zabrodzka and Ross Cioffi of Moody's Analytics
November 12, 2020

## UNITED KINGDOM

As expected, the U.K. economy recovered strongly in the third quarter, though at a slightly weaker pace than we forecast. All GDP components rebounded following sharp contractions in the first half of the year. Those industries most affected by the spring lockdowns such as tourism, healthcare and education have made tangible improvements.

But despite strong quarterly gains, the level of output is still significantly below pre-pandemic levels. Moreover, the monthly GDP data showed that the rate of increase continued to lose momentum, with growth slowing to 1% m/m from 2.1% in August.

The second wave of the pandemic, which gained ground throughout October, forced the U.K. government to reintroduce stricter lockdown measures following the easing which took place over the summer. As the number of new infections soared above the spring peak, worries about healthcare system failure resulted in renewed restrictions on social gatherings and in closures of restaurants, among other measures. This will again impact the accommodation and food service sector, which is still not over the impact of the previous wave of lockdowns.

We thus expect the country's output to contract again at the end of this year, albeit much less so than in the spring. So far, the lockdown is lighter than previously, with schools and factories remaining open. We pencil in a 1.6% q/q drop in the three months to December, which will push GDP down more than 10% in year-ago terms.

Because of the renewed economic difficulties, both the government and the Bank of England have ramped up their stimulus. The government extended the furlough scheme until the end of March, after it was supposed to finish it in October this year. Meanwhile, the central bank expanded its bond-purchasing programme during its November monetary policy meeting while holding the main policy rate unchanged at 0.1%.

We expect that the second wave of the pandemic will be contained by the end of this year, allowing for the gradual reopening of the economy at the start of 2021 and resulting in a small rebound in first-quarter GDP.

## EURO ZONE

On Tuesday the European Parliament and Council reached a final deal on the EU's next Multiannual Financial Framework—the bloc's seven-year budget. The budget will now total €1.074 trillion, after the Parliament convinced the Council to bolster spending on EU health, research, education, digital and green programs. Part of the agreement was a Parliament-devised outline for the Own Resources Decision. This is the document that adds 'own resources' (or revenue streams) necessary for funding the EU's future expenses such as the €750 billion that will be borrowed on markets to pay for the region's recovery fund.

The road map indicates that the European Commission will propose a plastics tax in 2021, an emissions trading system and digital tax by 2023, and a financial transactions tax and new common corporate tax by 2026. Agreement between the European Parliament and Council on an MFF, and the road map for new own resources, were necessary to pass the Council's 'Next Generation EU' recovery plan announced over the summer.

Now the Council and the European Parliament need to officially adopt the MFF, and national governments need to ratify the new 'own resources'. Only after this can we be certain that the EU's recovery fund will be operational next year. The biggest obstacle remains opposition from Hungary and Poland on legislation that would condition EU funds on rule of law. The two have threatened to veto the MFF, which requires unanimity if this regulation gets passed. The rule-of-law condition needs only a qualified majority in the Council to be passed, however, which it will have.

It looks like the EU will vote on the rule-of-law regulation in the next weeks, before the final drafts of the MFF and ORD are voted on. The hope is that with the regulation passed, Poland and Hungary will lose their leverage and would only be doing themselves great harm by using their veto. Our assumption is that the MFF, the ORD, and the recovery fund are passed. But we can't say we are fully confident either country will relent. Either way, Tuesday's agreement took a big step towards mobilizing the region's necessary recovery funds.

## Asia Pacific

By Xiao Chun Xu and Shahana Mukherjee of Moody's Analytics
November 12, 2020

### CHINA

China's trade recovery continues to strengthen in its post-COVID-19 phase. The latest statistics showed that China's export growth accelerated in October, having risen 11.4% in yearly terms, following a 9.9% increase in the prior month, as overseas demand revived from the historical lows induced by the coronavirus shutdowns. Domestic conditions remain largely positive for China, characterised by a strong rebound in production, while retail spending is catching up, and the labour market continues to stabilise. However, the downside risks from escalating global infections persist, with fears that the resurgence of COVID-19 cases in Europe and the U.S. may disrupt the recovery momentum in the months ahead.

Another major risk is the possibility of waning demand for the major drivers of export growth, namely computer equipment and medical PPE. Despite recent gains, the high dependence on these categories is a risk to the sustainability of China's rebound in external demand. In October, these categories weakened, though it is unknown whether the weakening was induced by weaker foreign demand or by the disruption to supply due to the Golden Week holidays.

Industrial commodity shipments such as rare earths, aluminium products, steel and petroleum, and auto parts continue to disappoint. Near-term prospects for Asia's supply chain are also concerning, especially for the auto industry as year-to-date shipments of autos and auto spare parts were down 8.5% and 10.7%, respectively. The resurgence of cases in western economies increases the risk of a more prolonged recovery in these industries.

Under a Biden administration, there is a higher likelihood of less volatile U.S. China trade relations, which may eventually lead to lower bilateral tariffs and potentially, a freer flow of capital and goods between the two economic giants in the medium term. That said, the conflict over the past few years can also have a longer-term bearing on China's role in the Asia supply chain, with a non-negligible possibility of more diversification in manufacturing dependence away from China.

China's exports have risen during a period when the yuan appreciated because of the rising current account balance and relative attractiveness of Chinese assets. We do not expect that a strong yuan will be a major detriment to exports, since the rises have been modest to this point and Chinese authorities will likely intervene to prevent a surge. In October they removed reserve requirements on shorting the yuan, as a sign that they would seek to manage the currency float.

The outlook for China remains largely positive. China's domestic economy is steadily rebounding, with production leading the charge, while consumers become more willing to spend and travel. However, rising COVID-19 cases in Europe and the U.S. threaten to derail external demand through early 2021.

# Ratings Round-Up

## Europe Downgrades Continue to Outnumber Upgrades

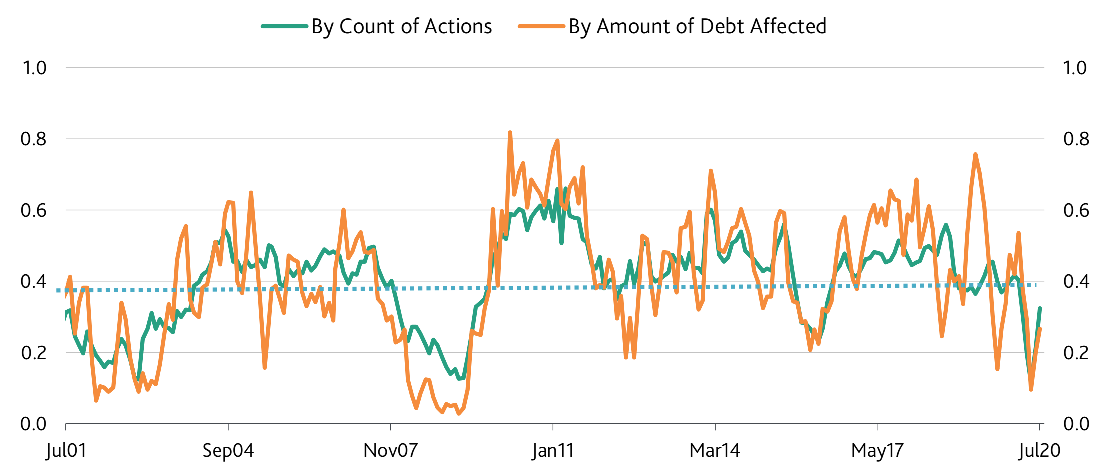
By Michael Ferlez

U.S. credit rating changes were credit positive last period, continuing the positive trend in rating change activity over the past several weeks. For the period ended November 10, upgrades accounted for 73% of total changes and 98% of total affected debt. Upgrades were concentrated in building materials, business services and the specialty industries, while downgrades were confined to consumer industries and oil services—two industries that have been hit hard by the pandemic. The largest change by amount of debt affected was to Albertsons Companies Inc., which saw its corporate family rating and probability of default rating upgraded to Ba3 and Ba3-PD. Additionally, the food and grocery company also saw its senior unsecured notes upgraded to B1 from B2. In the rating action, Moody's Investors Service noted that Albertsons has posted a strong performance during the pandemic with record sales and EBITDA in the first half of 2020 and has meaningfully improved its credit metrics after reducing debt through free cash flow.

European rating change activity was predominately credit negative for the week ended November 10. Downgrades outnumbered upgrades seven to one and accounted for all the reported debt affected in the period. The most notable change last week was made to ENGIE SA. Moody's Investors Service downgraded ENGIE's issuer rating and senior unsecured ratings to Baa1 from A3, reflecting Moody's expectation that ENGIE's weak credit metrics would not recover to levels consistent with the A3 rating. The downgrade affected $35 billion in company debt.

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 |
|---|---|---|---|---|---|---|---|---|
| 11/4/20 | EQUINOX HOLDINGS, INC. | Industrial | SrSec/BCF/LTCFR/PDR | | D | Caa3 | Ca | SG |
| 11/4/20 | LESLIE'S POOLMART, INC. | Industrial | SrSec/BCF/LTCFR/PDR | | U | B2 | B1 | SG |
| 11/4/20 | POLARIS INTERMEDIATE CORP. -MPH ACQUISITION HOLDINGS LLC | Industrial | SrSec/BCF | | U | B1 | Ba3 | SG |
| 11/5/20 | L3HARRIS TECHNOLOGIES, INC. | Industrial | SrUnsec/CP | 6,776 | U | Baa3 | Baa2 | IG |
| 11/6/20 | PETSMART, INC. | Industrial | SrSec/SrUnsec/BCF | 3,900 | U | B2 | B1 | SG |
| 11/6/20 | ALBERTSONS COMPANIES, INC. | Industrial | SrUnsec/LTCFR/PDR | 8,962 | U | B2 | B1 | SG |
| 11/9/20 | MARTIN MARIETTA MATERIALS, INC. | Industrial | SrUnsec | 2,655 | U | Baa3 | Baa2 | IG |
| 11/9/20 | VULCAN MATERIALS COMPANY | Industrial | SrUnsec/BCF | 3,356 | U | Baa3 | Baa2 | IG |
| 11/9/20 | SPRING EDUCATION GROUP, INC. | Industrial | SrSec/BCF | | D | B2 | B3 | SG |
| 11/9/20 | VT TOPCO, INC. | Industrial | SrSec/BCF/LTCFR/PDR | | U | Caa3 | Caa2 | SG |
| 11/10/20 | BASIC ENERGY SERVICES, INC. | Industrial | SrSec/LTCFR/PDR | 600 | D | Caa2 | Ca | SG |

*Source: Moody's*

FIGURE 4
### Rating Changes: Corporate & Financial Institutions – Europe

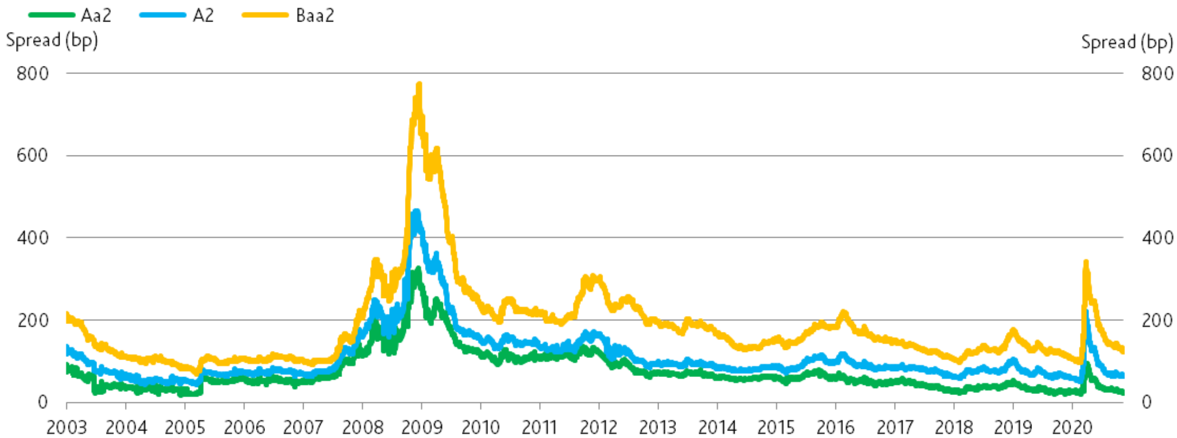
| Date | Company | Sector | Rating | Amount ($ Million) | Up/ Down | Old LTD Rating | New LTD Rating | IG/SG | Country |
|---|---|---|---|---|---|---|---|---|---|
| 11/4/20 | CORIO N.V. | Industrial | SrUnsec | 506 | D | A3 | Baa1 | IG | NETHERLANDS |
| 11/5/20 | CATLUXE ACQUISITION S.A.R.L. | Industrial | SrSec/BCF/LTCFR/PDR | | D | B3 | Caa1 | SG | LUXEMBOURG |
| 11/9/20 | ENGIE SA | Utility | SrUnsec/LTIR /JrSub/MTN | 34,971 | D | A3 | Baa1 | IG | FRANCE |
| 11/9/20 | ISS A/S-ISS GLOBAL A/S | Industrial | SrUnsec/LTIR/MTN | 3,087 | D | Baa2 | Baa3 | IG | DENMARK |
| 11/9/20 | IGNITION TOPCO BV | Industrial | SrSec/BCF/LTCFR/PDR | | D | B2 | B3 | SG | NETHERLANDS |
| 11/10/20 | SAS AB | Industrial | LTCFR/Sub/PDR | 141 | U | Caa2 | B3 | SG | SWEDEN |
| 11/10/20 | GATEGROUP HOLDING AG | Industrial | LTCFR/PDR | | D | B3 | Caa2 | SG | SWITZERLAND |
| 11/10/20 | BAHIA DE LAS ISLETAS, S.L. | Industrial | SrSec/LTCFR/PDR | 1,382 | D | Caa2 | Ca | SG | SPAIN |

*Source: Moody's*

# Market Data

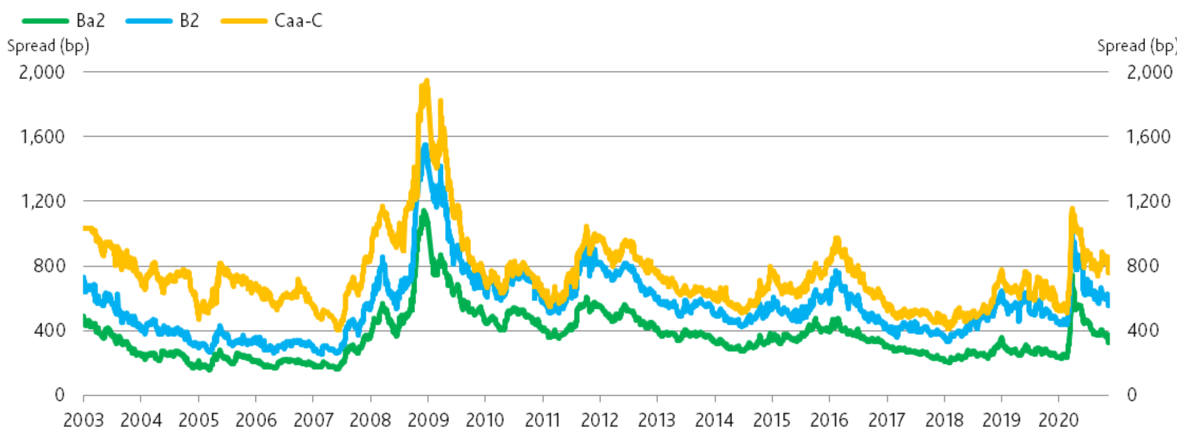
## Spreads

**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 (November 4, 2020 – November 10, 2020)**

| CDS Implied Rating Rises | CDS Implied Ratings | | |
|---|---|---|---|
| Issuer | Nov. 10 | Nov. 4 | Senior Ratings |
| Carnival Corporation | Caa2 | C | B2 |
| Royal Caribbean Cruises Ltd. | Caa3 | C | B2 |
| United Airlines Holdings, Inc. | Caa3 | C | Ba3 |
| CCO Holdings, LLC | Baa3 | Ba1 | B1 |
| United Airlines, Inc. | Caa3 | Ca | Ba3 |
| Delta Air Lines, Inc. | Caa1 | Caa2 | Baa3 |
| PNC Financial Services Group, Inc. | A3 | Baa1 | A3 |
| Calpine Corporation | Ba2 | Ba3 | B2 |
| Dish DBS Corporation | B3 | Caa1 | B2 |
| OneMain Finance Corporation | Ba3 | B1 | Ba3 |

| CDS Implied Rating Declines | CDS Implied Ratings | | |
|---|---|---|---|
| Issuer | Nov. 10 | Nov. 4 | Senior Ratings |
| Toyota Motor Credit Corporation | A1 | Aa1 | A1 |
| Raytheon Technologies Corporation | Aa3 | Aaa | Baa1 |
| Eli Lilly and Company | A1 | Aa1 | A2 |
| Eversource Energy | A1 | Aa1 | Baa1 |
| Danaher Corporation | A2 | Aa2 | Baa1 |
| JPMorgan Chase Bank, N.A. | A1 | Aa2 | Aa2 |
| Apple Inc. | Aa3 | Aa1 | Aa1 |
| Comcast Corporation | Aa3 | Aa1 | A3 |
| John Deere Capital Corporation | A2 | Aa3 | A2 |
| Microsoft Corporation | Aa3 | Aa1 | Aaa |

| CDS Spread Increases | | CDS Spreads | | |
|---|---|---|---|---|
| Issuer | Senior Ratings | Nov. 10 | Nov. 4 | Spread Diff |
| Wendy's International, LLC | Caa2 | 222 | 208 | 14 |
| Exelon Generation Company, LLC | Baa2 | 103 | 100 | 3 |
| NextEra Energy Capital Holdings, Inc. | Baa1 | 56 | 56 | 0 |
| Consolidated Edison, Inc. | Baa2 | 51 | 51 | 0 |
| Cameron International Corporation | Baa1 | 110 | 110 | 0 |
| Philip Morris International Inc. | A2 | 54 | 55 | 0 |
| Raytheon Technologies Corporation | Baa1 | 21 | 22 | 0 |
| Enterprise Products Operating, LLC | Baa1 | 59 | 59 | 0 |
| Waste Management, Inc. | Baa1 | 54 | 54 | 0 |
| DTE Energy Company | Baa2 | 53 | 53 | 0 |

| CDS Spread Decreases | | CDS Spreads | | |
|---|---|---|---|---|
| Issuer | Senior Ratings | Nov. 10 | Nov. 4 | Spread Diff |
| American Airlines Group Inc. | Caa1 | 2,053 | 2,834 | -782 |
| Carnival Corporation | B2 | 594 | 1,054 | -461 |
| Royal Caribbean Cruises Ltd. | B2 | 802 | 1,123 | -321 |
| Staples, Inc. | B3 | 971 | 1,258 | -287 |
| United Airlines Holdings, Inc. | Ba3 | 795 | 1,062 | -267 |
| Macy's Retail Holdings, Inc. | B1 | 923 | 1,184 | -260 |
| United Airlines, Inc. | Ba3 | 678 | 906 | -228 |
| Nabors Industries, Inc. | Caa1 | 3,047 | 3,259 | -211 |
| Talen Energy Supply, LLC | B3 | 1,524 | 1,685 | -161 |
| Nordstrom, Inc. | Baa3 | 486 | 645 | -159 |

*Source: Moody's, CMA*

## Market Data

**Figure 4. CDS Movers - Europe (November 4, 2020 – November 10, 2020)**

| CDS Implied Rating Rises | CDS Implied Ratings | | |
|---|---|---|---|
| Issuer | Nov. 10 | Nov. 4 | Senior Ratings |
| HSBC Holdings plc | A2 | Baa1 | A2 |
| Vue International Bidco plc | Caa3 | C | Ca |
| Banco Bilbao Vizcaya Argentaria, S.A. | A3 | Baa1 | A3 |
| ING Groep N.V. | A2 | A3 | Baa1 |
| Erste Group Bank AG | A3 | Baa1 | A2 |
| Santander UK plc | Baa2 | Baa3 | A1 |
| Standard Chartered PLC | A2 | A3 | A2 |
| Total SE | A2 | A3 | Aa3 |
| RCI Banque | Ba3 | B1 | Baa2 |
| Anheuser-Busch InBev SA/NV | Baa1 | Baa2 | Baa1 |

| CDS Implied Rating Declines | CDS Implied Ratings | | |
|---|---|---|---|
| Issuer | Nov. 10 | Nov. 4 | Senior Ratings |
| Svenska Handelsbanken AB | A1 | Aa1 | Aa2 |
| Nordea Bank Abp | A1 | Aa1 | Aa3 |
| SEB AB | A2 | Aa2 | Aa2 |
| ENGIE SA | A1 | Aa1 | Baa1 |
| KBC Bank N.V. | A1 | Aa1 | Aa3 |
| France, Government of | Aa2 | Aaa | Aa2 |
| United Kingdom, Government of | Aa2 | Aaa | Aa3 |
| Rabobank | Aa3 | Aa1 | Aa3 |
| Ireland, Government of | Aa2 | Aaa | A2 |
| ABN AMRO Bank N.V. | Aa3 | Aa1 | A1 |

| CDS Spread Increases | | CDS Spreads | | |
|---|---|---|---|---|
| Issuer | Senior Ratings | Nov. 10 | Nov. 4 | Spread Diff |
| Finland, Government of | Aa1 | 13 | 10 | 4 |
| Banco Comercial Portugues, S.A. | Ba1 | 156 | 152 | 3 |
| Austria, Government of | Aa1 | 9 | 9 | 1 |
| Swedish Export Credit Corporation | Aa1 | 12 | 11 | 1 |
| Sweden, Government of | Aaa | 12 | 11 | 1 |
| Caixa Geral de Depositos, S.A. | Ba1 | 119 | 118 | 1 |
| United Kingdom, Government of | Aa3 | 20 | 19 | 0 |
| Germany, Government of | Aaa | 11 | 11 | 0 |
| Belgium, Government of | Aa3 | 13 | 13 | 0 |
| Netherlands, Government of | Aaa | 9 | 9 | 0 |

| CDS Spread Decreases | | CDS Spreads | | |
|---|---|---|---|---|
| Issuer | Senior Ratings | Nov. 10 | Nov. 4 | Spread Diff |
| TUI AG | Caa1 | 872 | 1,541 | -669 |
| Vue International Bidco plc | Ca | 792 | 1,071 | -279 |
| Vedanta Resources Limited | B3 | 1,628 | 1,861 | -233 |
| Casino Guichard-Perrachon SA | Caa1 | 762 | 969 | -207 |
| Novafives S.A.S. | Caa2 | 975 | 1,129 | -154 |
| Piraeus Bank S.A. | Caa2 | 704 | 844 | -140 |
| Jaguar Land Rover Automotive Plc | B1 | 662 | 768 | -106 |
| thyssenkrupp AG | B1 | 313 | 407 | -93 |
| Hammerson Plc | Baa3 | 461 | 542 | -82 |
| Rolls-Royce plc | Ba3 | 316 | 395 | -78 |

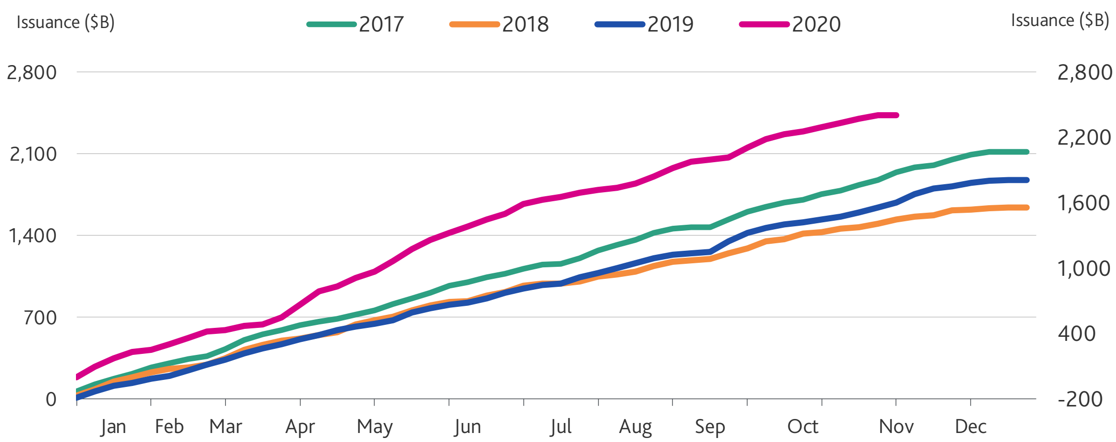
*Source: Moody's, CMA*

## Market Data

# Issuance

FIGURE 5

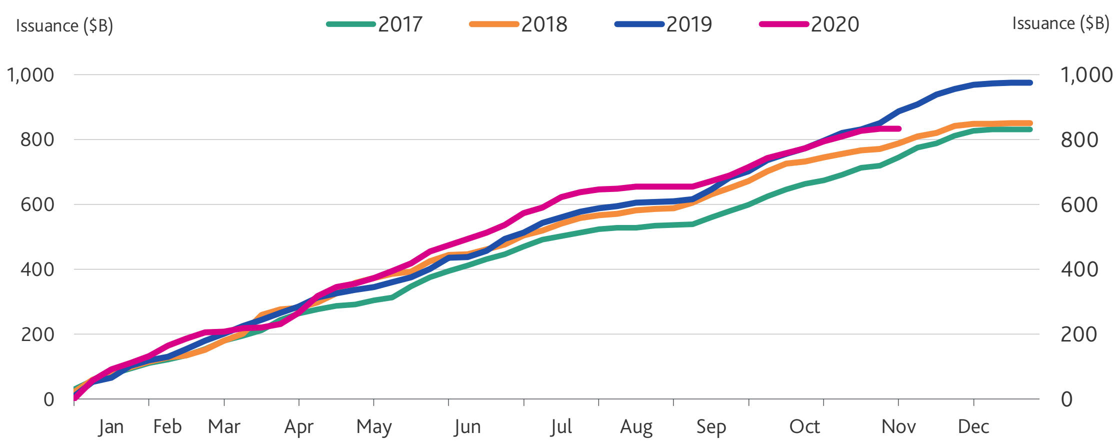
**Market Cumulative Issuance - Corporate & Financial Institutions: USD Denominated**




*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 | 2.503 | 1.725 | 4.685 |
| Year-to-Date | 1,851.184 | 477.646 | 2,405.921 |

| | Euro Denominated | | |
|---|---|---|---|
| | Investment-Grade | High-Yield | Total* |
| | Amount $B | Amount $B | Amount $B |
| Weekly | 1.237 | 0.000 | 1.237 |
| Year-to-Date | 694.973 | 106.181 | 834.116 |

* Difference represents issuance with pending ratings.

*Source: Moody's/ Dealogic*

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