MOODY'S ANALYTICS

WEEKLY MARKET OUTLOOK

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Full updated stories and key credit market metrics: The Blue Chip consensus projection for 2020's core pretax profits has improved from a June bottom of -20.1% to September's -13.4%.

Credit Spreads	Investment Grade: We see the year-end 2020's average investment grade bond spread may resemble its recent 139 basis points. High Yield: The high-yield spread may approximate its recent 530 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 July 2019's 3.1% to July 2020's 8.4% and may average 11.4% during 2020's final quarter.
Issuance	For 2019's offerings of US$-denominated corporate bonds, IG bond issuance rose by 2.6% to \$1.309 trillion, while high-yield bond issuance surged by 55.8% to \$432 billion. In 2020, US\$-denominated corporate bond issuance is expected to soar higher by 50.8% for IG to \$1.975 trillion, while high-yield supply may rise 20.4% to \$521 billion.

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Moody's Capital Markets Research *recent publications*

Links to commentaries on: Unprecedented stimulus, bond yields, record savings rates, demographic change, high tech, complacency, Fed intervention, speculation, default risk, credit stress, rate cuts, optimism, coronavirus, corporate credit, spreads, leverage, VIX.

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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 Economist, Moody's Capital Markets Research, Inc.

Corporate Credit Mostly Unfazed by Equity Volatility

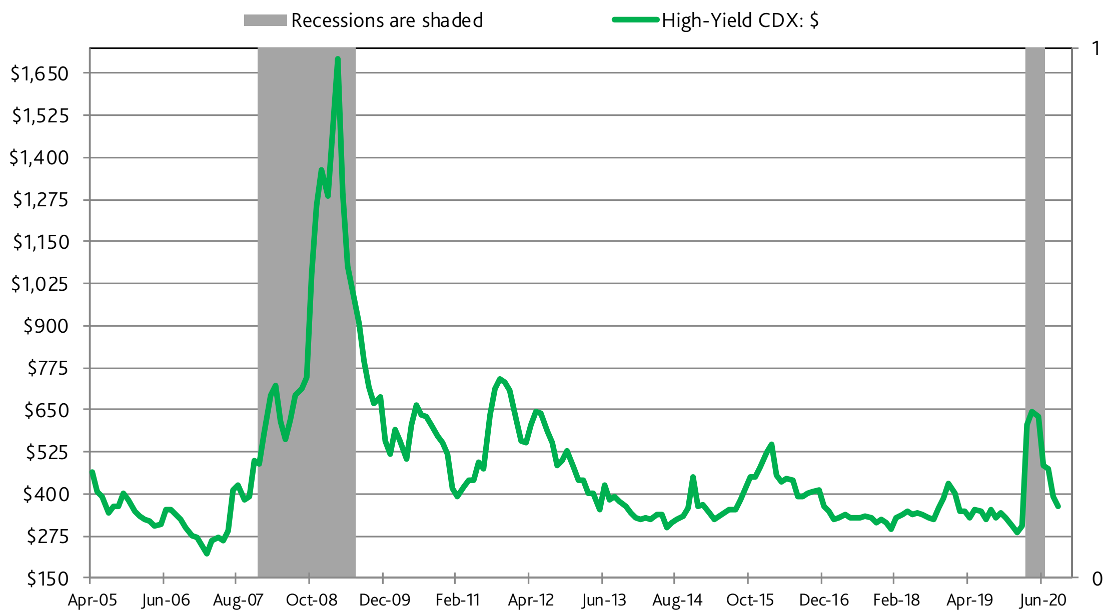
The U.S. is now in high-season politically. Going forward, both business activity and financial markets will be influenced by the perceived outcome of November 3's presidential and Congressional elections. In all likelihood, recent equity market volatility has stemmed from the risk of a substantially different U.S. tax and regulatory framework.

Markets will not remain indifferent to the negative stock-price implications of possibly higher rates of taxation on capital gains and corporate earnings, as well as the heightened regulation of business and potential anti-trust actions against the high-tech giants. Worry over a potential increase in the capital-gains tax rate may help to explain the heavy selling of shares that have posted substantial price appreciation over the recent past.

During the U.S. equity market's 7.1% drop from September 2's new record high to September 8, the deepest percent declines by stock prices applied to those shares showing the biggest capital gains over the recent past. For example, the five tech giants showed a median share price plunge of 11.3% since September 2, which was more severe than the estimated 6% drop by the U.S. equity market excluding the high-tech giants. Among the shallower September 2 to September 8 declines by specialized stock price indices were the setbacks of 2.15% for the KBW bank stock price index, 2.45% for the Dow Jones Utilities, 3.2% for the Dow Jones Transports, and 5.5% for the Russell 2000.

Most do not buy corporate bonds for potential capital gains. In part that may help to explain why the high-yield bond market did not reflect the high-anxiety implicit to September 8's 31.5-point close for the VIX. Granted that the high-yield CDX index, or the cost of insuring $10,000 of high-yield CDX debt, rose from September 2's $350 to September 8's $384, the latter was still less than its $394 month-long average of August 2020. On September 9, the high-yield CDX closed at $371, where the latter is low enough to suggest that the COVID-19 recession has expired.

Figure 1: A Recent High-Yield CDX Contract of Less than $400 Suggests the COVID-19 Recession Is Over
sources: Markit, NBER, Moody's Analytics



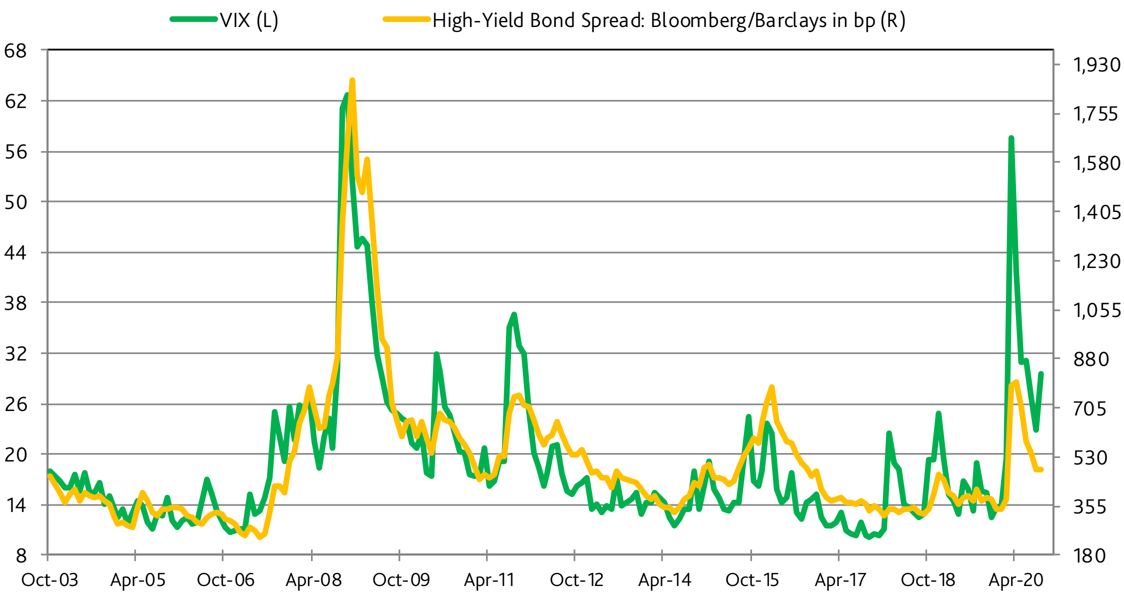
Once Again, High-Yield Questions a Sharply Higher VIX

In response to heightened equity market volatility, a composite high-yield bond spread widened from the 517 basis points of the five trading days ended September 2 to a 535 bp average thereafter. However, widening of the high-yield bond spread is less than what might be inferred from the comparably measured jump by the VIX from 25.3 points to 31.1 points.

Ordinarily a rise by the VIX of 5.8 points is accompanied by a 59 bp widening of the high-yield bond spread. However, the latest widening of the high-yield bond spread was a much thinner 18 bp. Apparently, the recent jump in equity market volatility is mostly for reasons that extend beyond any possible diminution of pretax profits.

Since the end of 2009, there have been six distinctive jumps by the VIX which were not accompanied by a commensurate widening of the high-yield bond spread. Following each of the six episodes, the VIX receded and the high-yield bond spread either stabilized or narrowed. The muted response by the high-yield bond spread to a substantially higher VIX correctly viewed the sudden surge in equity market volatility as not signaling a long-lived worsening of the outlook for corporate earnings.

Figure 2: September 2020 May Be the Sixth Incident since 2009 Where the High-Yield Bond Spread Outperformed Equities At Assessing Underlying Financial Conditions
sources: CBOE, Bloomberg, Barclays Capital, Moody's Analytics



Net High-Yield Downgrades Remain Under Destabilizing Readings of March-May 2020

For any time span, the net downgrades of U.S.-based high-yield issuers equal the number of downgrades less the number of upgrades.

At the start of 2020, U.S. net high-yield downgrades jumped up from January's -1 (meaning that upgrades eclipsed downgrades by a single rating change) to February's 19. Thereafter, COVID-19 triggered widespread shutdowns that drove U.S. net high-yield downgrades up to 176 in March, a record-high 219 in April, and 100 in May.

Since then, U.S. net high-yield downgrades dropped to June's 46, July's 0, and the 15 of August. Thus far in September, net high-yield downgrades equal -1.

The month-long averages of the Bloomberg/Barclays high-yield bond spread have mostly followed the direction taken by net high-yield downgrades.

After rising from January 2020's 342 bp to February's 377 bp, the high-yield bond spread ballooned to 785 bp in March and to April's current cycle high of 796 bp. Subsequently, the high-yield bond spread narrowed to May's 708 bp, June's 586 bp, July's 547 bp, and the 488 bp of August.

Note how the high-yield bond spread narrowed from July to August despite the rise in net high-yield downgrades from July's 0 to August's 15. Thus far in September, the spread has averaged 483 bp. The high-yield bond spread has yet to mimic the increased worry implicit to the recent jump by the VIX above 30 points. Moreover, the VIX has since declined to 28.6 points as of mid-day September 10.

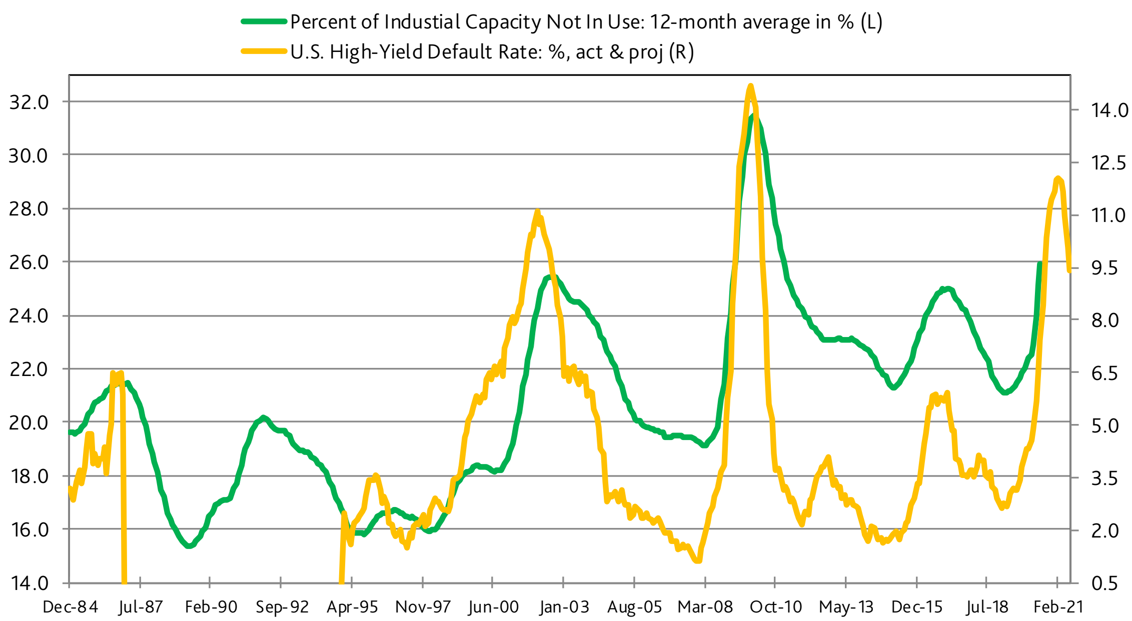
Rising Rate of Industrial Capacity Utilization Portends a Declining Default Rate

For corporate credit quality, the next worthwhile economic release arrives on Tuesday, September 15 in the form of the August estimate for industrial production. The early Bloomberg consensus foresees a monthly increase of 1.2%. However, a very upbeat reading on August manufacturing from the ISM hints of a upside surprise for industrial production. a rising rate of capacity utilization implies that operating leverage now takes hold, which is shorthand for the faster growth of operating profits vis-a-vis revenues. The scope for operating leverage is greater the lower is the starting point for the rate of capacity utilization.

After bottoming at April 2020's record low 64.2%, the percent of industrial capacity in use, or the capacity utilization rate quickly recovered to July's 70.6%. A continuation of the climb by the industrial capacity utilization rate would favor the start of a declining trend for the U.S. high-yield default rate by early 2021.

The default rate often moves in the direction taken by the percent of industrial capacity not in use. When the moving 12-month average for the percent of U.S. production capacity not in use sank from December 2009's record high of 31.5% to a January 2015 bottom of 21.3%, the U.S. high-yield default rate dropped from November 2009's post-Depression high of 14.7% to September 2014's cycle bottom of 1.6%.

Figure 3: Forecasts of a Lower Default Rate Implicitly Assume the Fuller Utilization of Production Capabilities
sources: Moody's Investors Service, Federal Reserve, Moody's Analytics



Employment-Income Growth Underpins Household Spending's Revival

Recent gains by retail sales are consistent with a recovery by business sales. On Wednesday, September 16 arrives the August report on retail sales. The Bloomberg consensus has retail sales growing by 1.2%, or by 1.1% after excluding the sales of auto dealerships and gasoline stations.

Only six months separated retail sales' record highs of January 2020 and July 2020. By contrast, retail sales fared much worse during the Great Recession. After peaking in June 2008, 33 months passed before retail sales established a new record-high in March 2011.

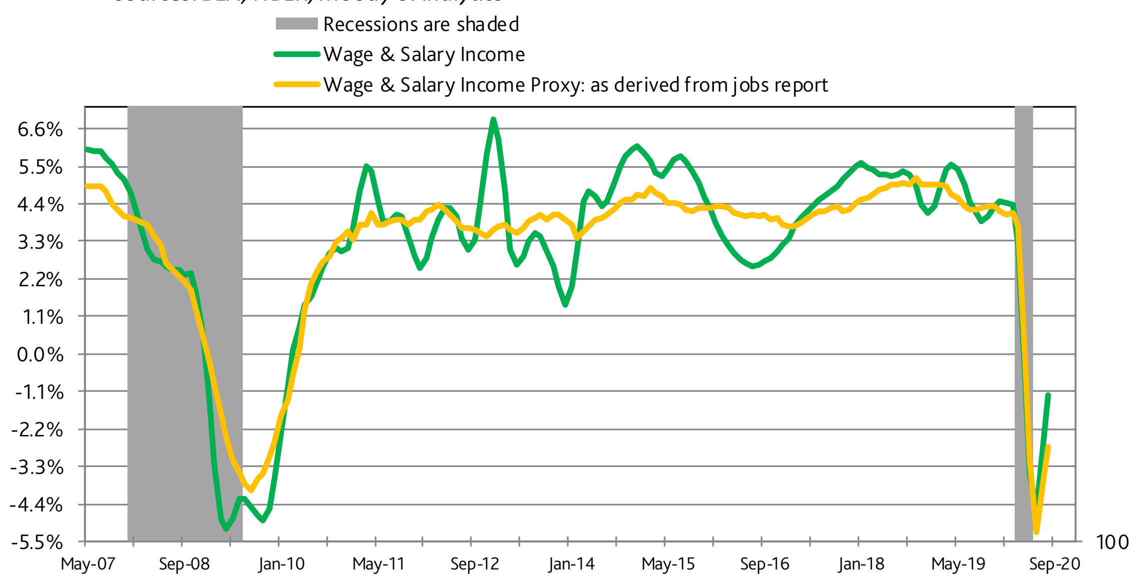
Retail sales excluding gas station sales may more than recover from their 21% annualized contraction from the first to the second quarter of 2020 with a faster than 60% annualized sequential surge for the third quarter.

Even the still struggling commercial airline industry shows signs of improvement. As reported by Bloomberg, though still down by 56% from a year earlier, early September's count of people passing through airport security portals was the highest since mid-March 2020.

The August employment report hinted of another sizable monthly percent increase by wage and salary income, which adds fuel to consumer spending's recovery. The monthly increase by an employment-income proxy rose from July 2020's 1.1% to 1.7% for August. At the same time the year-to-year decline by estimated employment income narrowed from July's 2.7% to the 1.9% of August. The yearly decline by the employment-income proxy bottomed at April 2020's 7.0%, or when wage and salary income's yearly decline by wage and salary income also bottomed at 7.0%.

In conjunction with the Great Recession, the employment-income proxy fell from a year earlier for 15 consecutive months. It is conceivable that the string of yearly declines by the employment-income proxy may last no more than six straight months implying that this barometer of worker income may post a yearly increase as early as October 2020.

Figure 4: Wage and Salary Income May Show Faster Recovery from 2020 Recession Compared to 2008-2009 Recession
yy % change of moving 3-month average
sources: BEA, NBER, Moody's Analytics



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

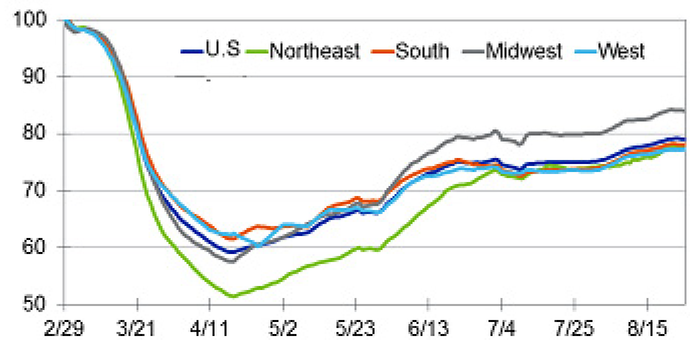
THE U.S.
By Mark Zandi of Moody's Analytics

The Weight of Expiring Federal Fiscal Support

The August jobs numbers were somewhat stronger than anticipated but did not meaningfully change our near-term economic outlook. We continue to expect employment to be down by approximately 10 million jobs from its pre-pandemic peak at year's end. As of August, employment was off by 11.5 million jobs. Unemployment is expected to end the year at close to 9%, up from 8.4% in August, as labor force participation continues to recover.

The economy is struggling to gain traction. The Back-to-Normal Index we've constructed with CNN Business—a compilation of a wide range of economic statistics from government and private sources—has only edged higher since mid-June and remains below 80%. This means the economy is operating at more than 20% below its pre-pandemic level. The Midwest, which had been leading the national economy, is suffering from intensifying COVID-19 infections, setting that economy back. There is a clear connection between the virus and the economy's performance, suggesting that the economy will remain far from normal until the pandemic is over.

Midwest Has Been Leading the Way Back
Back-to-Normal Index, Mar 1, 2020=200



Sources: CNN, Moody's Analytics

Complicating any recovery is the difficulty schools are having. With so many schools across the country forced to go online rather than reopen classrooms, parents are scrambling to figure out how to juggle kids at home and their own jobs. For single-parent households this is especially problematic and may significantly interfere with parents' ability to work. There are about 2.6 million single-parent households with children 5 to 12 years old, ages that require significant supervision but likely without alternative childcare arrangements. An additional 13 million households with children in this age group have more than one adult living in the household but still have to figure things out.

Households With Children by Age			
Thousands			
	Total	Single Adult	Multiple Adults
Total	128,579	42,319	86,260
No Children Under 18	90,516	36,477	54,039
Age 0 to <1	1,272	88	1,184
Age 1 to <2	1,745	146	1,599
Age 2 to <3	1,944	178	1,766
Age 3 to <4	2,062	289	1,774
Age 4 to <5	2,239	312	1,927
Age 5 to <6	2,151	297	1,853
Age 6 to <7	2,077	341	1,735
Age 7 to <8	2,207	366	1,841
Age 8 to <9	2,256	376	1,880
Age 9 to <10	2,327	405	1,922
Age 10 to <11	2,144	405	1,739
Age 11 to <12	2,408	427	1,982
Age 12 to <13	2,281	393	1,888
Age 13 to <14	2,406	414	1,992
Age 14 to <15	2,282	392	1,889
Age 15 to <16	2,322	391	1,931
Age 16 to <17	2,221	373	1,849
Age 17 to <18	1,720	250	1,470
Age 5 to <12	15,569	2,617	12,952
Share of Total Households, %	12.1	6.2	15.0
Sources: March 2019 Current Population Survey, Moody's Analytics			

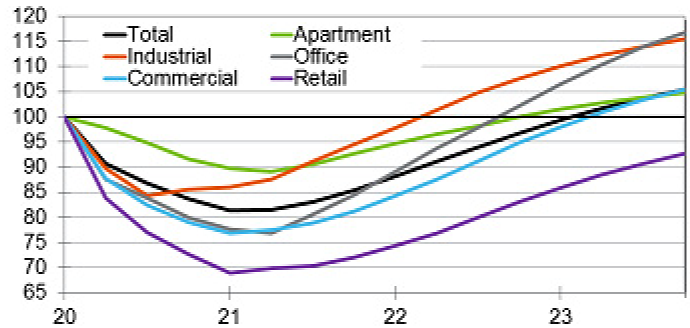
Fallout from the expiration of federal fiscal support will also weigh more and more heavily on the economy. At the peak of the support in April, the government provided aid totaling $1.2 trillion, equal to almost 6% of pre-pandemic GDP. By August, the support was gone. The Trump administration and Congress continue to negotiate another fiscal rescue package, but the odds of passage appear to be fading. Lawmakers could include the package in a continuing resolution that they must pass to keep the government operating after September, but such an inclusion now appears to be a 50-50 proposition. We continue to assume in our forecast that lawmakers will agree to a $1.5 trillion package of aid to state and local governments, more supplemental unemployment insurance, another round of stimulus checks, and additional funds for small businesses through the Paycheck Protection Program. Without this support, the economy would likely contract again, with unemployment ending the year back above 10%.

The economy needs the help, even if it were able to avoid backsliding without additional federal aid. We estimate that approximately 40 million Americans, one-fourth of the nation's workforce, are either unemployed, working fewer hours than they would like, out of the workforce altogether but wanting a job if they could find a suitable one, or have suffered a recent pay cut. Of these, 24 million people, equal to more than one-sixth of the workforce, are in this financial plight because of the pandemic. And of them, more than 5 million will have a tough time getting back to work even after the pandemic is over, because their previous job is not coming back. This is either because the firm they worked for didn't survive or has had to fundamentally change its business model and labor force to make it through the pandemic. This situation is widespread among brick-and-mortar retailers, businesses in the travel and transportation industries, and global manufacturers.

Commercial real estate is being forced to quickly absorb all these structural changes. Demand for retail space was slumping prior to the pandemic as online retailers cut into sales of brick-and-mortar retailers, but the pandemic has pushed this change into hyper-drive. Malls are especially hard-hit given the long list of retailers, including Neiman Marcus, J.C. Penney and J. Crew, that have filed for bankruptcy. Downtowns in cities across the country are pummeled by the rash of failing mom-and-pop retailers. We expect retail property prices, as measured by the Moody's Analytics repeat sales price index, to eventually fall by as much as 30% from their pre-pandemic peaks.

Commercial RE Markets Hit Hard

Moody's CPPI by property type, 2020Q1=100

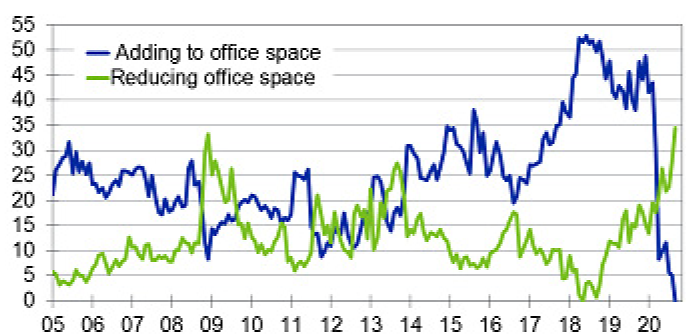


Sources: REIS, Moody's Analytics

Work from home was a developing trend that the pandemic has also accelerated, empowered by Zoom and similar communication platforms that were coming into their own just prior to the pandemic. WFH will moderate once the virus has run its course and offices reopen in earnest, but there is no going back, and demand for office space will be diminished. This is especially true of downtowns in large urban areas as more workers unnerved by the pandemic will want to live in less densely populated areas with shorter commutes. Businesses are working through the issues involved with allowing their employees to be more footloose. For example, should someone who worked in New York City but moves to Tampa still be paid NYC wages? Once such issues are resolved, WFH will become even more entrenched. This is evident in the collapse in the number of businesses responding to the Moody's Analytics business survey that say they are adding to their office space. Just prior to the pandemic, a record number of respondents said they were adding space, but in the past two weeks, no one has. Even during the worst of the financial crisis, about 10% of respondents were adding space. Our property price index for office space is expected to eventually decline nearly 20% from its pre-pandemic peak.

Commercial RE Demand Collapses

% of respondents to business survey that say they are...



Source: Moody's Analytics

For a long time to come, business travel also will not be what it was. Businesses have figured out that they can be as effective and productive without employees traveling as much. And though tourism is expected to revive, it could take time as the pandemic lingers, safety remains a concern, and governments are slow to allow foreign travel. The upshot is that hotels will find it difficult to fill their rooms and convention centers their venues. We don't have a price index for hotels, but price declines on par with the 30% peak-to-trough slide in retail-space prices seem likely.

High-end apartments and condos in big urban centers are also at risk. People are likely to want more space post-pandemic, and with WFH there is no reason they need to pay such high rents to live close to their jobs. Demand for luxury units will also be impaired as demand from wealthy foreigners is slow to revive. The converse of this is strong demand for single-family homes in suburban, exurban, and second and vacation home markets. Powering this demand are record low mortgage rates—fixed rates are hovering around 3%—and ample mortgage credit, particularly for higher-income households. Our property price index for apartments is projected to eventually decline by almost 10% from its pre-pandemic peak.

Commercial real estate's travails show why the economic recovery from the pandemic will be a slog. Even when the pandemic is over—which could take time given how difficult it will be to distribute an effective vaccine that is widely adopted across the globe—there will be a lot to adjust to. Much depends on policymakers. It is encouraging that this recovery should not be as long or as painful as the one after the financial crisis. That recovery was undermined by the collapse of the financial system, which required a government bailout and that financial institutions substantially build up their capital and liquidity. We've been spared this in the pandemic in part because of the reforms imposed on the system after the financial crisis, but more importantly because of the effective firewall the Fed quickly erected between the chaos in the economy and financial markets. It's adoption of zero interest rates, a ramp-up of quantitative easing, and the standing-up of a range of credit facilities have helped stock and bond markets fully rebound and for credit and capital to remain cheap and ample.

While the Fed has effectively used during the pandemic what it learned in the financial crisis, it is unclear whether lawmakers will do the same. A key lesson from the financial crisis was that Congress and the Obama administration pivoted much too quickly from providing fiscal stimulus to imposing fiscal restraint. When this switch occurred in mid-2010, the unemployment rate wasn't much different than it is today. And because of the fiscal restraint, it took much of the remainder of the decade for the economy to return to full employment. Hopefully, this Congress and the Trump administration won't make the same mistake. We will find out in the next few weeks.

EUROPE

By Ross Cioffi of Moody's Analytics

Euro Zone CPI Likely Fall for August

Final estimates of August consumer prices for the euro zone are due next week along with indicators for the U.K. and Russian economies. We'll also see the British unemployment rate for July and retail sales for August, while for Russia we'll get August industrial production, retail sales and the unemployment rate. The Russian Central Bank will also meet for its September policy meeting.

Initial CPI estimates for the euro zone show a 0.2% y/y decline in August. The fall in prices came as a surprise as the consensus expected some price growth. The main story from the preliminary release was that services inflation fell to its lowest on record. This came in line with our forecast and with the fact that overall demand has dropped sharply because of the COVID-19 crisis. This trend will continue in coming months as the drop in employment and incomes, the rise in precautionary savings, and the value-added tax cuts in some countries add to the downward pressure. We'll see similar dynamics on the country level, which is why we expect Italian consumer prices to slip 0.5% y/y, French prices to inch up by only 0.2% after a 0.8% increase in July, and U.K. prices to grow at only 0.4% after rising 1% in July.

We expect the U.K. unemployment rate to have risen to 4.3% in the three months to July from 3.9% in the three months to June. The high-frequency data have been pessimistic. Claimant count statistics from last month's release showed that the number of job seekers rose in July compared with June, while the July PMI's employment index registered one of the steepest drops since the 2008-09 financial crisis, falling to 35.4 from 41.5 in June. Since government stimulus measures like the Job Retention Scheme began winding down in August, we expect consumers to begin retrenching. As a result, the recovery in retail sales will lose steam. We expect sales grew by only 0.9% y/y in August, after jumping 3.6% in July.

In Russia, the upward revision to second quarter GDP to a decline of 8% (from a preliminary estimate of -8.5%), has us slightly more positive about August's indicators. The economy has a long way to go before recovering, which is why we see retail sales remaining 1.5% below year-ago levels. Likewise, we see the unemployment rate holding steady in August at 6.3%. The downside is mostly for industry, where OPEC+ limitations and persistently low oil prices are weighing on the country's oil producers. We expect industrial production was 6% below year-ago levels, still an improvement on the 8% y/y decrease in July.

Finally, we expect the Russian Central Bank to cut its policy one-week repo rate 25 basis points to 4%. The bank has lowered rates at the past four meetings. With the most recent CPI estimate of 3.6% y/y in August, inflation is still undershooting the bank's target of 4%.

	Key indicators	Units	Moody's Analytics	Last
Mon @ 10:00 a.m.	Euro Zone: Industrial Production for July	% change	3.5	9.1
Tues @ 7:45 a.m.	France: Consumer Price Index for August	% change yr ago	0.2	0.8
Tues @ 9:00 a.m.	Italy: Consumer Price Index for August	% change yr ago	-0.5	-0.4
Tues @ 9:30 a.m.	U.K.: Unemployment for July	%	4.3	3.9
Tues @ 1:00 p.m.	Russia: Industrial Production for August	% change yr ago	-6.0	-8.0
Wed @ 9:30 a.m.	U.K.: Consumer Price Index for August	% change yr ago	0.4	1.0
Wed @ 10:00 a.m.	Euro Zone: External Trade for July	€ bil	25.0	21.2
Thur @ 10:00 a.m.	Euro Zone: Consumer Price Index for August	% change yr ago	-0.2	0.4
Fri @ 9:30 a.m.	U.K.: Retail Sales for August	% change yr ago	0.9	3.6
Fri @ 11:30 a.m.	Russia: Monetary Policy for September	%	4.0	4.3
Fri @ 2:00 p.m.	Russia: Retail Sales for August	% change yr ago	-1.5	-2.6
Fri @ 2:00 p.m.	Russia: Unemployment for August	%	6.3	6.3

ASIA-PACIFIC

By Shahana Mukherjee of Moody's Analytics

New Zealand's Q2 GDP Will Show Effects of the Pandemic

We expect New Zealand's GDP to have contracted by 12% on a quarterly basis through the June quarter, following a 1.6% decline in the prior quarter. The slowdown in March resulted from a sharp decline in gross fixed capital spending, which fell by 6.8% in yearly terms, even though a decline in exports and domestic consumption also weighed on the aggregate. The June quarter, however, will reflect the full effects of the containment measures, resulting in a sharp contraction, with a decline in exports and domestic consumption driving the downturn.

Australia's unemployment rate is expected to have risen to 7.7% in August, from 7.5% in July. The Australian economy's revival in the post-restrictions phase has been disrupted by the prominent second wave that emerged in the state of Victoria in July. Not only did this renew restrictions through July, but measures also were elevated to the strictest stage (Alert Level 4) in Melbourne in August, which required several businesses to temporarily shut operations. Even though the rest of Australia continues to revive as consumer spending picks up, the severe containment measures in the second-most populous state are expected to weaken the revival in aggregate demand and weigh heavily on labour market outcomes.

Japan's trade position is expected to have remained weak in August. Exports are likely to have contracted by 19% in yearly terms, following a 19.2% decline in July. Even though there are visible signs of easing overseas demand conditions for several Asian economies, Japan's significant reliance on durables such as automotives has prevented a notable pickup. Dovish investor sentiment has also kept imports of machinery largely under check. These factors are likely to have weighed on Japan's position in August, though China's ongoing recovery should partially alleviate some of this strain.

India's exports are expected to have contracted by 8.5% in yearly terms in August, following a 10.5% decline in July. Economic activity has resumed in varying capacities across Indian states since June, following one of the strictest and longest lockdowns in the Asia-Pacific region. Improvement in industrial output, combined with a gradual easing in overseas demand conditions, is likely to have aided the revival in India's exports through August, while a moderate increase in domestic consumption should also have lifted imports up from the sharp 28.4% decline observed in July.

	Key indicators	Units	Moody's Analytics	Confidence	Risk	Last
Mon @ 10:00 p.m.	India CPI for August	% change yr ago	7.0	3	↑	6.93
Tues @ 12:00 p.m.	China Industrial Production for August	% change yr ago	4.6	3	↓	4.8
Tues @ 12:00 p.m.	China Retail Sales for August	% change yr ago	1.0	2	↓	-1.1
Tues @ 12:00 p.m.	China Fixed-Asset Investment for August	% change yr ago	-0.8	3	↓	-1.6
Tues @ 2:00 p.m.	Indonesia Foreign Trade for August	US$ bil	2.7	3	↓	3.3
Tues @ 11:15 p.m.	India Foreign Trade for August	US$ bil	-5.0	3	↓	-4.8
Wed @ 9:50 a.m.	Japan Foreign Trade for August	¥ bil	-32.5	3	↓	-34.83
Thu @ 8:45 a.m.	New Zealand GDP for Q2	%	-12.0			-1.6
Thur @ 10:30 a.m.	Singapore Nonoil Domestic Exports for August	% change yr ago	5.5	3	↓	6.0
Thur @ 11:30 a.m.	Australia Unemployment for August	%	7.7			7.5
Thur @ 1:00 p.m.	Japan Monetary Policy for September	%	-0.1	4	←	-0.1
Fri @ 9:30 a.m.	Japan Core CPI for August	% change yr ago	0.0	3	←	0.0

The Long View

The Blue Chip consensus projection for 2020's core pretax profits has improved from a June bottom of -20.1% to September's -13.4%.

By John Lonski, Chief Economist, Moody's Capital Markets Research Group
September 10, 2020

CREDIT SPREADS

As measured by Moody's long-term average corporate bond yield, the recent investment grade corporate bond yield spread of 139 basis points exceeded 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 530 bp is thinner than what is suggested by the accompanying long-term Baa industrial company bond yield spread of 214 bp and the recent VIX of 29.1 points. The latter has been historically associated with a 782-bp midpoint for the high-yield bond spread.

DEFAULTS

July 2020's U.S. high-yield default rate of 8.4% was up from July 2019's 3.1% and may approximate 12.0%, on average, by 2021's first quarter.

US CORPORATE BOND ISSUANCE

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.

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.

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 12.0% advance for IG and 12.4% 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 wider credit spreads are possible.

EUROPE

By Ross Cioffi Moody's Analytics
September 10, 2020

EURO ZONE

The European Central Bank left monetary policy unchanged in September, and we think it made the right move by keeping policy loose. Although economic activity and financial markets have improved substantially so far in the third quarter, headwinds remain. The recovery is losing momentum as demand stays soft and uncertainty strong.

Bank President Christine Lagarde emphasized that because of softening demand, low wage pressures, nominal euro appreciation, and national policies like the temporary value-added tax cut in Germany, the harmonized consumer prices are forecast to drop in the remaining months of 2020. Regarding the ECB's revised macro outlook, the harmonized consumer price inflation forecast was unchanged from the June forecast at 0.3% for 2020, but it was revised up to 1% from 0.8% for 2021. The rate in 2022 was also left unchanged at 1.3%. The ECB revised up its outlook on core inflation thanks to the effects of stronger stimulus measures across the currency bloc, but weaker energy prices offset the upward pressures on the forecast.

Lagarde reaffirmed that the ECB does not base its policy decisions on the exchange rate, but no one denies that exchange rates are also relevant to inflation. It looks like the euro will stay strong in the coming months, but despite chatter about a strong euro pushing the ECB to loosen, we aren't basing our monetary policy expectations on the exchange rate. Even without a strong euro, inflation expectations will need support, while risks to actual inflation tilt towards disinflation or deflation. For that reason, we see the ECB slightly expanding the Pandemic Emergency Purchase Programme or lowering interest rates on pandemic emergency longer-term refinancing operations and targeted longer-term refinancing operations in December.

UNITED KINGDOM

The U.K.'s newly published Internal Market Bill would break part of the withdrawal agreement that the British government signed with the EU last year. Under the withdrawal agreement, and in order to prevent a hard border in Ireland, Northern Ireland would follow EU customs and standards. Furthermore, an export declaration would be necessary on EU-originating goods entering the rest of the U.K., while duties would have to be paid on goods coming into Northern Ireland that are 'at risk' of moving on to the EU. This so-called Northern Ireland Protocol would remain in place until the EU and U.K. agree on the outstanding issue that necessitates border controls.

Three problems remain unsolved in the protocol. First, the EU and the U.K. haven't agreed on what 'at risk' goods are. Second, they haven't agreed if shipments of goods arriving into the U.K. from both Northern Ireland and the Republic of Ireland would need to be declared. And third, the EU state aid rules apply not only to final producers in Northern Ireland but also to producers of subcomponents in the U.K., an extension that the U.K. resents.

The Internal Market Bill unilaterally resolves these problems by giving the U.K. power to define 'at risk' goods, waive export declarations, and apply state aid requirements only to Northern Irish firms. The government has argued that the bill is a safety net to ensure trade continues within the U.K. should trade negotiations fail. Given the deadlock in the Joint Committee that was assigned to resolve these issues, a safety net isn't fully out of place.

But now that Boris Johnson moved the trade-deal deadline up to October 15, the bill looks more like a move in bad faith against negotiations. Introducing the bill may have been a negotiating tactic, but the U.K. is paying a heavy price; although the bill wouldn't enter law unless trade negotiations fail, the U.K. is being painted as an unreliable trade partner.

A no-deal Brexit would throw off the British recovery, harming trade and investment. Our baseline, however, is that the EU and the U.K. will resolve the remaining issues to the minimal degree necessary to secure a trade deal. Even a light deal would prevent a lot of the damage associated with Brexit, since it would also boost business confidence.

ASIA PACIFIC

By Shahana Mukherjee of Moody's Analytics
September 10, 2020

JAPAN

The COVID-19 shock to Japan's economy has been severe and was reflected in the June quarter, as real GDP contracted by a significant 7.9% on a quarterly basis in the advance estimate, following a preliminary estimate of a 7.8% contraction and a much narrower 0.6% decline in the prior quarter. The downturn was driven by a significant contraction in exports and domestic private consumption, which fell by 18.5% and 7.9% in yearly terms, respectively. The more severe aggregate decline in the advance estimate, however, reflects a weaker investment position, as nonresidential investment fell by 4.7%, as opposed to an initial estimate of a 1.5% fall. The latest reading translated into an annualized decline of 28.1% in the June quarter. This marked the third consecutive quarter of decline and the sharpest contraction on record, as the economy sank deep into recession.

Japan's economy was yet to recover from the dual shocks of the domestic sales tax hike and the protracted U.S.-China trade war in 2019 when the COVID-19 pandemic impacted the economy. The shocks triggered by the COVID-19 crisis have manifested through various channels. Domestic restrictions, which peaked in April and May with the imposition of the nationwide emergency, weakened household sentiment and undermined consumer spending. The significant hit to overseas demand due to international restrictions jolted Japanese exporters, worsened employment prospects, and deepened the downturn in demand. For the highly trade-reliant economy, the implications of an external demand shock were significant, with the decline in exports totaling 3.1 percentage points of the net 7.9% decline. In comparison, the impact of the decline in household consumption accounted for 4.4 percentage points of the net decline.

Challenging outlook

The near-term outlook for Japan's prospects remains challenging. Even though the shock to global demand bottomed out in June, a revival for Japan's exporting sectors will be more gradual. It is contingent on an improvement in global employment and a turnaround in investor outlook, considering the country's heavy reliance on durables and capital-intensive products such as automotives and general-purpose machinery exports. Moreover, the sustainability of the current global recovery may well be challenged in the months ahead, as the global infections curve continues to rise. The ongoing recovery in China will moderate some of the additional volatility, especially that induced by the COVID-19 resurgence in some European economies. Overall, however, this remains a pertinent downside risk that will ease the pace of rebound expected in the second half of 2020.

Challenges are compounded by the persistence of the domestic health crisis. The second wave in Japan, which peaked between July and August, was stronger than the first one. With daily caseloads still above 400 and Tokyo continuing to experience a large share of this increase, household spending has been severely impacted. It fell by a significant 7.6% in yearly terms in July, after falling 1.2% in June, and its resilience will continue to be tested in the weeks ahead. Given Japan's experience with this crisis, the risks from an intensifying outbreak cannot be overlooked; it could trigger a more serious setback to household spending. Considering the softness in overseas demand for Japanese goods, and the strong second wave that hit Japan in recent months, aggregate demand is likely to have weakened further over the September quarter and amplified the strain on the labour market.

Geopolitical dynamics

Concerns do not end there. Geopolitical dynamics are evolving fast in Asia. While U.S.-China tensions have intensified in recent months, elevating fears of another trade war, the unexpected resignation of Japan's Prime Minister Shinzo Abe has generated some uncertainty regarding the nation's policy trajectory that will be pursued by his successor, following the relatively mixed success of Abenomics. The implications of these changes on decision-making in the near- and medium-term outcomes, which could involve a gradual realignment of regional value supply chains, can prove to be significant for Japan's recovery in the post-COVID-19 environment.

The Long View

Japanese policymakers remain proactive to mitigate the shocks from the COVID-19 crisis. The substantial fiscal stimulus worth nearly 40% of GDP and conducive monetary settings have played an important role in guarding employment prospects, household incomes, and reducing the incidence of bankruptcies. Reviving consumer confidence and household spending will be crucial in the months ahead, and this rests on an effective management of the health crisis. As things stand, Japan's economy will mark another sharp contraction over the September quarter as the effects of the second wave materialize though another decline in domestic consumption and exports. In view of the multiple downside risks, Japan's road to recovery will be slow and protracted.

Ratings Round-Up

U.S. Downgrade Trend Slows

By Steven Shields

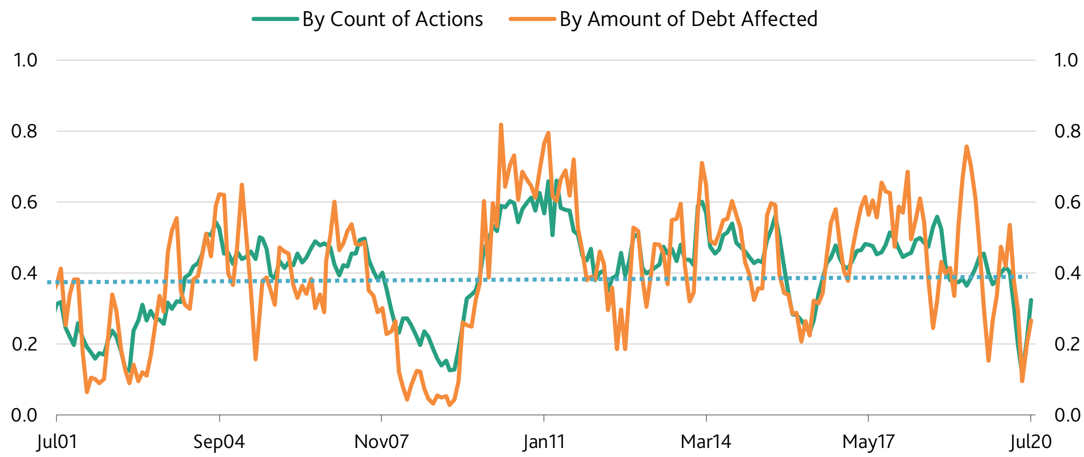
The downward trend in U.S. corporate credit quality slowed in the recent week with upgrades outnumbering downgrades four to three. However, downgrades accounted for the bulk of the affected debt in the period. Summit Midstream Partners LP and Northwest Hardwoods Inc. were the two largest downgrades, with downgrades impacting a combined $1.9 billion in debt. Moody's Investors Service lowered Summit's senior unsecured notes to Caa2 from Caa1. According to the rating action, the downgrade reflects cash flow risk, rising debt refinancing and distressed exchanged risk in the near term as its maturities approach. Meanwhile, Northwest Hardwoods Inc.'s senior secured notes were downgraded to C from Ca following Northwest's missed interest payments on its senior secured notes due 2021. The lower rating also accounts for Moody's revised estimates of recovery values for the note holders. Moody's also changed the company's outlook to stable from negative as the current views of recovery values are now reflected in Northwest's ratings. Qualitytech L.P. was the largest upgrade in the period with the rating on its senior unsecured notes being raised to Ba3 from B1. The upgrade reflects in part the REIT's improved earnings quality resulting from its successful strategic shift to exit non-core cloud and managed services products. The upgrade impacted $400 million in outstanding debt. Since the beginning of the year, Moody's Investors Service has issued 733 credit downgrades to U.S. corporations compared to just 189 upgrades.

European ratings activity was limited to five downgrades and one upgrade in the period. Among the changes, Moody's Investors Service lowered Swissport Group S.A.R.L to C from Ca. The rating action reflects the announcement by the company in August of an agreement between its lenders representing more than 75% of the company's senior secured debt and the company's owner, HNA, on a comprehensive debt restructuring. The proposed restructuring follows a period of significantly depressed cash flows which resulted from the global coronavirus pandemic. On September 7, Moody's Investors Service downgrade British Airways PLC's corporate family rating to Ba2 from Ba1 reflecting the slow pace of passenger demand recovery in Europe since travel restriction and quarantine measures were introduced in the first half of 2020. The airline's outlook remains negative. Moody's also lowered Virgin Media Vendor Financing from B1 to B2, impacting nearly $1.7 billion in outstanding debt. The outlook on all the ratings of Virgin Media Inc. and its subsidiaries has been changed to stable from negative.

Ratings Round-Up

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

Ratings Round-Up

FIGURE 3

Rating Changes: Corporate & Financial Institutions – US

Date	Company	Sector	Rating	Amount ($ Million)	Up/ Down	Old LTD Rating	New LTD Rating	IG/SG
9/2/20	SUMMIT MIDSTREAM PARTNERS, LP	Industrial	SrUnsec/SrSec/BCF /LTCFR/PDR/PS	994	D	Caa1	Caa2	SG
9/2/20	SAFFRON HOLDCO LLC ('SMART & FINAL HOLDINGS') -SMART & FINAL FUNDING LLC	Industrial	SrSec/BCF /LTCFR/PDR		U	B3	B2	SG
9/3/20	B&G FOODS, INC.	Industrial	SrSec/BCF		U	Ba2	Ba1	SG
9/3/20	PPL HOLDINGS CORP. -PRE-PAID LEGAL SERVICES, INC.	Industrial	SrSec/BCF		D	B1	B2	SG
9/8/20	AIP/HARDWOODS FUNDING, INC. -NORTHWEST HARDWOODS, INC.	Industrial	SrSec/LTCFR /PDR/LGD	870	D	Ca	C	SG
9/8/20	QTS REALTY TRUST, INC. -QUALITYTECH, L.P.	Financial	SrUnsec/LTCFR	400	U	B1	Ba3	SG
9/8/20	SWITCH, LTD.	Industrial	SrSec/BCF/LGD		U	Ba3	Ba1	SG

Source: Moody's

FIGURE 4

Rating Changes: Corporate & Financial Institutions – Europe

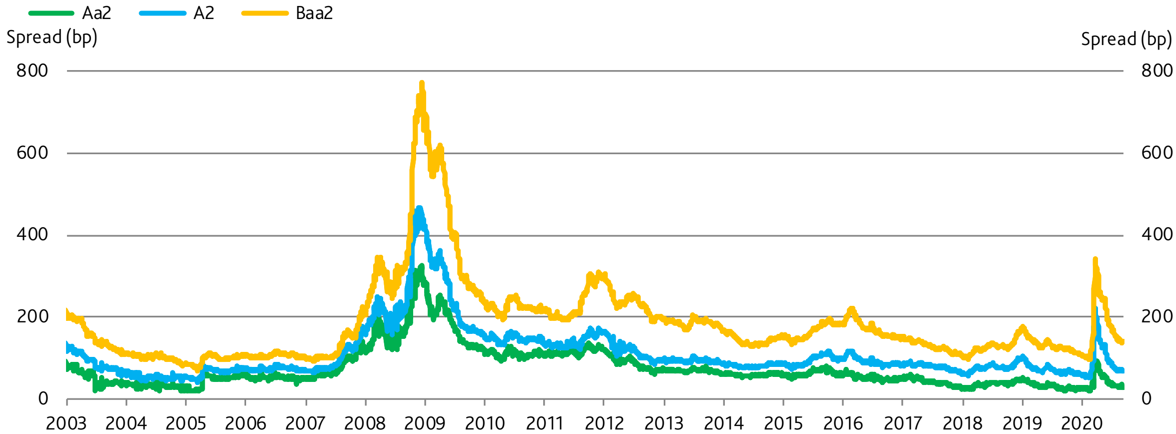
Date	Company	Sector	Rating	Amount ($ Million)	Up/ Down	Old LTD Rating	New LTD Rating	IG/SG	Country
9/2/20	GARRETT MOTION INC.	Industrial	SrUnsec/SrSec /BCF/LTCFR/PDR	413	D	B3	Caa1	SG	LUXEMBOURG
9/3/20	SWISSPORT GROUP S.A R.L.	Industrial	SrSec/SrUnsec /BCF/LTCFR/PDR	2,371	D	Ca	C	SG	LUXEMBOURG
9/7/20	BRITISH AIRWAYS, PLC	Industrial	LTCFR	2,138	D	Ba1	Ba2	SG	UNITED KINGDOM
9/7/20	INTERNATIONAL CONSOLIDATED AIRLINES GROUP, S.A.	Industrial	SrUnsec/LTCFR/PDR	1,180	D	Ba2	B1	SG	SPAIN
9/8/20	RINGKJOBING LANDBOBANK A/S	Financial	LTIR/LTD		U	A2	A1	IG	DENMARK
9/8/20	VMED O2 UK LIMITED-VIRGIN MEDIA VENDOR FINANCING NOTES III DESIGNATED	Industrial	SrSec	1,689	D	B1	B2	SG	IRELAND

Source: Moody's

Market Data

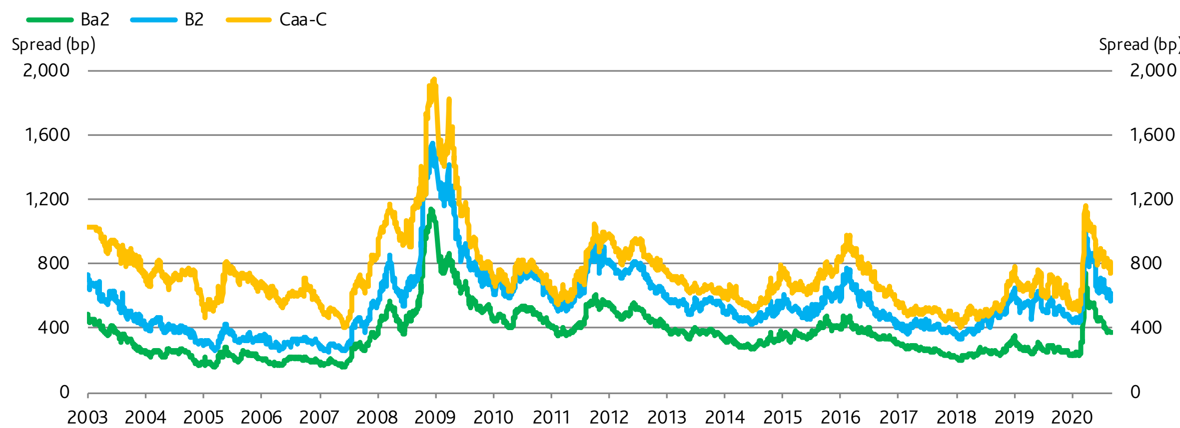
Spreads

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 (September 2, 2020 – September 9, 2020)

CDS Implied Rating Rises	CDS Implied Ratings		
Issuer	Sep. 9	Sep. 2	Senior Ratings
Oracle Corporation	A2	A3	A3
John Deere Capital Corporation	A3	Baa1	A2
Abbott Laboratories	A3	Baa1	A3
Waste Management, Inc.	A3	Baa1	Baa1
FirstEnergy Corp.	A3	Baa1	Baa3
DTE Energy Company	Baa1	Baa2	Baa2
NRG Energy, Inc.	Ba1	Ba2	Ba2
Southwest Airlines Co.	Ba1	Ba2	Baa1
CenterPoint Energy, Inc.	A3	Baa1	Baa2
Expedia Group, Inc.	Ba2	Ba3	Baa3

CDS Implied Rating Declines	CDS Implied Ratings		
Issuer	Sep. 9	Sep. 2	Senior Ratings
Merck & Co., Inc.	A1	Aa2	A1
Comcast Corporation	Aa1	Aaa	A3
McDonald's Corporation	Aa1	Aaa	Baa1
Occidental Petroleum Corporation	Caa1	B3	Ba2
United Parcel Service, Inc.	Aa1	Aaa	A2
Lowe's Companies, Inc.	Aa1	Aaa	Baa1
Cox Communications, Inc.	Aa1	Aaa	Baa2
Dominion Energy, Inc.	Aa3	Aa2	Baa2
Mondelez International, Inc.	Aa2	Aa1	Baa1
Caterpillar Inc.	Aa1	Aaa	A3

CDS Spread Increases		CDS Spreads		
Issuer	Senior Ratings	Sep. 9	Sep. 2	Spread Diff
Nabors Industries, Inc.	B3	4,420	3,864	556
American Airlines Group Inc.	Caa1	2,748	2,621	126
Occidental Petroleum Corporation	Ba2	569	467	101
Talen Energy Supply, LLC	B3	1,287	1,236	51
United States Steel Corporation	Caa2	1,302	1,255	47
Scripps (E.W.) Company (The)	Caa1	259	217	42
UDR, Inc.	Baa1	755	714	40
Apache Corporation	Ba1	273	234	38
Hilton Worldwide Finance, LLC	Ba2	213	176	38
Mattel, Inc.	B3	406	369	37

CDS Spread Decreases		CDS Spreads		
Issuer	Senior Ratings	Sep. 9	Sep. 2	Spread Diff
Staples, Inc.	B3	1,315	1,454	-139
Macy's Retail Holdings, Inc.	B1	954	998	-44
Nissan Motor Acceptance Corporation	Baa3	388	406	-18
Delta Air Lines, Inc.	Baa3	648	663	-15
Owens Corning	Baa3	71	84	-13
Expedia Group, Inc.	Baa3	191	203	-12
Royal Caribbean Cruises Ltd.	B2	981	989	-8
Avon Products, Inc.	B3	372	380	-8
Univision Communications Inc.	Caa2	313	318	-5
Huntsman International LLC	Baa3	28	33	-5

Source: Moody's, CMA

Market Data

Figure 4. CDS Movers - Europe (September 2, 2020 – September 9, 2020)

CDS Implied Rating Rises	CDS Implied Ratings		
Issuer	Sep. 9	Sep. 2	Senior Ratings
Vedanta Resources Limited	Caa3	C	B3
TUI AG	Caa3	C	Caa1
Spain, Government of	A3	Baa1	Baa1
Intesa Sanpaolo S.p.A.	Baa2	Baa3	Baa1
CaixaBank, S.A.	Baa2	Baa3	Baa1
Bankia, S.A.	Baa3	Ba1	Baa3
UniCredit Bank AG	A3	Baa1	A2
Bayerische Landesbank	Baa1	Baa2	Aa3
Alpha Bank AE	B3	Caa1	Caa1
Landesbank Baden-Wuerttemberg	Baa1	Baa2	Aa3

CDS Implied Rating Declines	CDS Implied Ratings		
Issuer	Sep. 9	Sep. 2	Senior Ratings
Vodafone Group Plc	Baa1	A2	Baa2
Bayer AG	Baa1	A2	Baa1
BNP Paribas	Aa3	Aa2	Aa3
Banco Bilbao Vizcaya Argentaria, S.A.	A2	A1	A3
Credit Agricole Corporate and Investment Bank	Aa2	Aa1	Aa3
Lloyds Bank plc	A1	Aa3	Aa3
Electricite de France	A1	Aa3	A3
NatWest Markets N.V.	Aa2	Aa1	Baa2
Standard Chartered Bank	Aa3	Aa2	A1
HSBC Bank plc	A2	A1	Aa3

CDS Spread Increases		CDS Spreads		
Issuer	Senior Ratings	Sep. 9	Sep. 2	Spread Diff
Iceland Bondco plc	Caa2	632	582	50
Vue International Bidco plc	Caa2	1,076	1,035	41
Jaguar Land Rover Automotive Plc	B1	717	678	39
Rolls-Royce plc	Ba2	418	386	32
thyssenkrupp AG	B1	318	293	25
Ineos Group Holdings S.A.	B2	276	252	24
Marks & Spencer p.l.c.	Ba1	247	226	21
Deutsche Lufthansa Aktiengesellschaft	Ba2	294	275	19
Eksportfinans ASA	Baa1	464	447	18
Fiat Chrysler Automobiles N.V.	Ba2	179	164	15

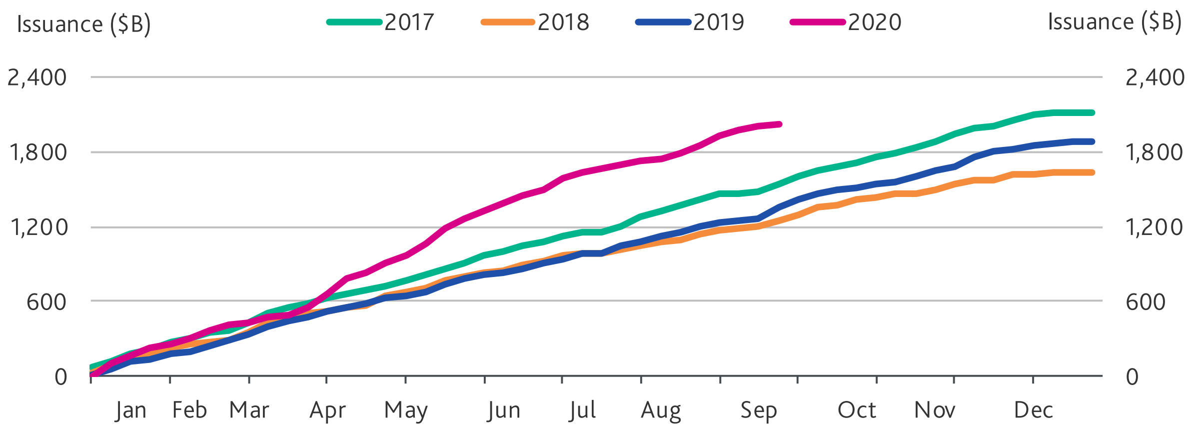
CDS Spread Decreases		CDS Spreads		
Issuer	Senior Ratings	Sep. 9	Sep. 2	Spread Diff
PizzaExpress Financing 1 plc	C	37,620	43,533	-5,913
Selecta Group B.V.	Caa3	2,603	3,688	-1,085
TUI AG	Caa1	885	1,199	-313
Vedanta Resources Limited	B3	960	1,201	-241
CMA CGM S.A.	Caa1	553	587	-34
Bankia, S.A.	Baa3	78	104	-26
Banco Sabadell, S.A.	Baa3	119	139	-21
Casino Guichard-Perrachon SA	Caa1	1,009	1,027	-18
CaixaBank, S.A.	Baa1	68	85	-17
Piraeus Bank S.A.	Caa2	841	857	-16

Source: Moody's, CMA

Market Data

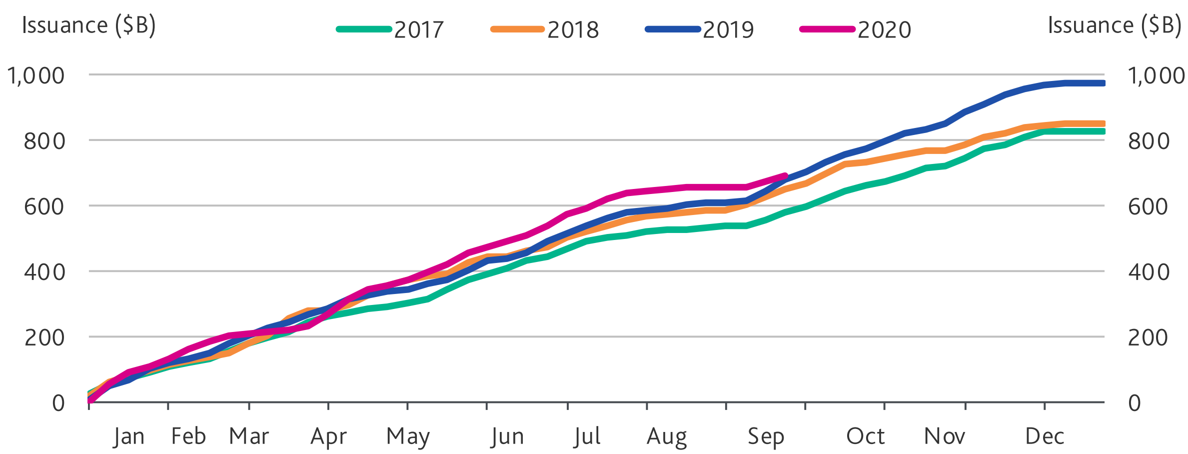
Issuance

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	11.620	4.650	16.978
Year-to-Date	1,565.694	382.859	2,015.448

	Euro Denominated		
	Investment-Grade	High-Yield	Total*
	Amount $B	Amount $B	Amount $B
Weekly	13.708	2.235	16.114
Year-to-Date	585.827	79.681	689.827

* Difference represents issuance with pending ratings.

Source: Moody's/ Dealogic

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