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WEEKLY MARKET OUTLOOK

Low Bond Yields Extend an Aging Upturn

Moody's Capital Markets Research

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Credit Markets Review and Outlook *by John Lonski*

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The Week Ahead

We preview economic reports and forecasts from the US, UK/Europe, and Asia/Pacific regions.

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The Long View

Check our chart here for forecast summaries of key credit market metrics. Full updated stories, "During January-May 2017, medium-grade issues supplied 56% of investment-grade bond offerings — close to its 55% share of the last five years," begin on page 16.

Credit Spreads	Investment Grade: Year-end 2017 spread to exceed its recent 119 bp. High Yield: After recent spread of 385 bp, it may approximate 425 bp by year-end 2017.
Defaults	US HY default rate: Compared to May 2017's 3.9%, Moody's Credit Policy Group forecasts the US trailing 12-month high-yield default rate to average 2.7% during the three-months-ended May 2018.
Issuance	In 2016, US$-IG bond issuance grew by 5.6% to a record $1.412 trillion, while US$-priced high-yield bond issuance fell by -3.5% to $341 billion. For 2017, US$-denominated IG bond issuance may rise by 2.8% to a new zenith of $1.451 trillion, while US$-priced high-yield bond issuance may increase by 17.3% to $400 billion, which lags 2014's $435 billion record high.

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Ratings Round-Up *by Njundu Sanneh*

A Much Better Week in the US.

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Market Data

Credit spreads, CDS movers, issuance.

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Moody's Capital Markets Research *recent publications*

Links to commentaries on: Philippines, thin, Qatar, toxic, Paris, mediocre, capital, retail, Korea, yields, less, doubt, Venezuela, inflation, CCAR, global, Treasury yield, France.

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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.

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Credit Markets Review and Outlook

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

Low Bond Yields Extend an Aging Upturn

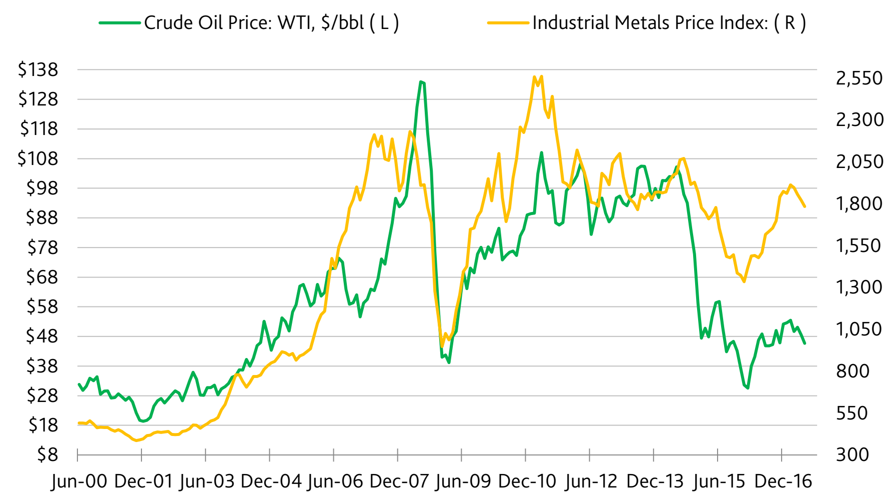
A renewed drop by the price of crude oil has grabbed the market's attention. June 2017's average price of WTI crude oil is on track to fall by nearly -6.5% annually. In turn, the annual rate of PCE price index inflation may eventually slow from April's 1.7%, or when the price of crude oil was up by 24.3% from a year earlier.

Though PCE price index inflation is likely to remain under the Fed's 2% target, it would be premature to dismiss the possibility of a 1.375% midpoint for fed funds by the end of 2017. Recently, the futures market implicitly assigned odds of less than 50% to fed funds finishing 2017 at something greater than its current 1.125% midpoint.

Lately, industrial commodity prices have been hinting of a mild and non-inflationary rate of global economic growth, which explains why the 10-year Treasury yield has eased from a March 2017 average of 2.48% to the 2.18% of June-to-date. Compared to their respective averages of yearlong 2011 (or when the 10-year Treasury yield averaged 2.79%), the June-to-date averages were down by -52% for the price of crude oil and off by -21% for Moody's industrial metals price index.

Though June-to-date's average for the industrial metals price index topped its June 2016 average by 18.3%, the same June-to-date average trailed its 31-month high of February 2017 by -6.7%. Flat to lower industrial commodity prices would practically rule out a lasting stay by the 10-year Treasury yield at 2.5% or higher. (Figure 1.)

Figure 1: Compared to 2011's Yearlong Averages, June-to-Date's Industrial Metals Price Index Was Off by -21%, while Price of Crude Oil Was Down by -52%



Unduly low VIX index explains why high-yield spread is too thin

On balance, the equity and corporate bond markets have largely withstood recent hints of slower business activity and lower industrial commodity prices. Though up from its recent lows, the VIX index remained under an extraordinarily low 11 points.

Meanwhile, despite a rise by the average EDF (expected default frequency) metric of high-yield issuers from January 2017's 3.69% to the 3.92% of June-to-date, the high-yield bond spread managed to narrow from 403 bp to 381 bp, respectively. The antithetical narrowing of spreads amid a rising risk of default stemmed from a drop by the VIX index from a January 2017 average of 11.6 points to the 10.5 of June-to-date.

The high-yield bond spread can be explained via a regression model that utilizes the following explanatory variables: (i) the median high-yield EDF, (ii) the VIX index, and (iii) the Chicago Fed's national activity index. The model's sample commences in 1990 and generates a convincing adjusted R-square

statistic of 0.87. The June-to-date averages of the explanatory variables are consistent with a 409 bp midpoint for the high-yield bond spread, which exceeds its actual average of 381 bp.

However, the mere removal of the VIX index from the set of explanatory variables drives the high-yield spread's predicted midpoint for June-to-date up to 491 bp. In this abbreviated version of the spread's explanatory model, the adjusted R-square eased, but to a still highly significant 0.81. Thus, once the VIX index normalizes, the high-yield bond spread is likely to quickly break well above 400 bp.

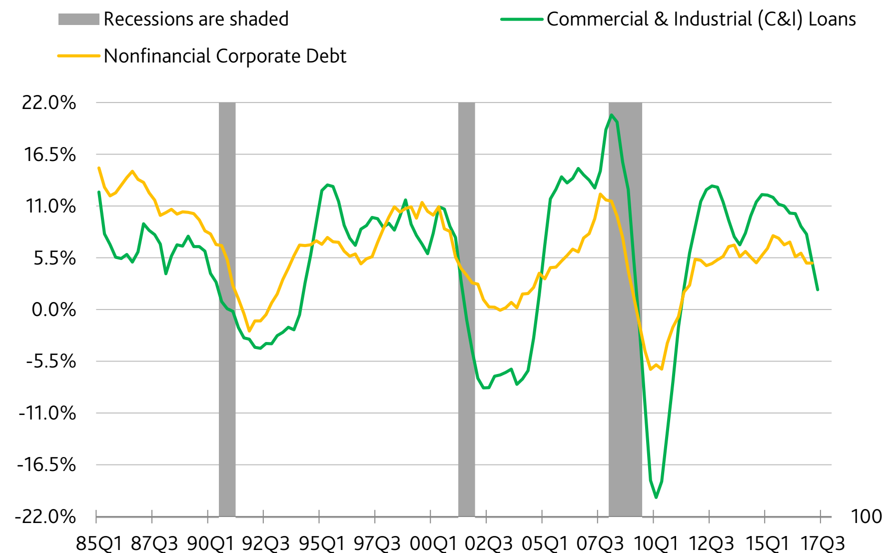
Corporate debt to follow marked slowing of outstanding C&I loans

An overvalued, yet seemingly confident, equity market, atypically narrow high-yield spreads, and a declining default rate underpin a plentiful supply of financial liquidity. In turn, US$-denominated borrowing by corporations has been brisk. Yearlong 2017 is likely to show annual increases of 2.8% for investment-grade bond issuance (to prospective record $1.451 trillion), 17.3% for high-yield bond offerings (to nearly $400 billion), and 32.5% for new bank loan programs from high-yield issuers (to $686 billion). Yearlong 2017's prospective $1.086 trillion grand total of high-yield gross borrowing would be a record high.

Nevertheless, the year-to-year growth rate for bank-held commercial and industrial (C&I) loans slowed dramatically from May 2016's 10.4% advance to the 2.0% rise of May 2017. The deceleration by C&I loans outstanding signals a further slowing by the yearly growth rate of US nonfinancial corporate debt.

After easing from Q2-2015's current cycle high of 7.8% to Q1-2017's 4.9%, the yearly increase of nonfinancial corporate debt is expected to ease to roughly 4.5% by 2017's second quarter. However, the latter is still faster than early June's Blue Chip consensus forecast of a 3.6% annual gain for yearlong 2017's pretax profits from current production. (Figure 2.)

Figure 2: April-May-2017's 2.3% Rise by Outstandings of C&I Loans Portends a 4.5% increase for Q2-2017's Nonfinancial Corporate Debt *yy % changes*



A further deceleration by nonfinancial-corporate debt may be in order, especially when in view of how Q1-2017's -5.6% year-to-year drop by nonfinancial-corporate operating profits was worse than the comparably measured +3.7% yearly increase posted by the broadest estimate of operating profits.

Expectations of higher interest rates prompt a lengthening of maturities

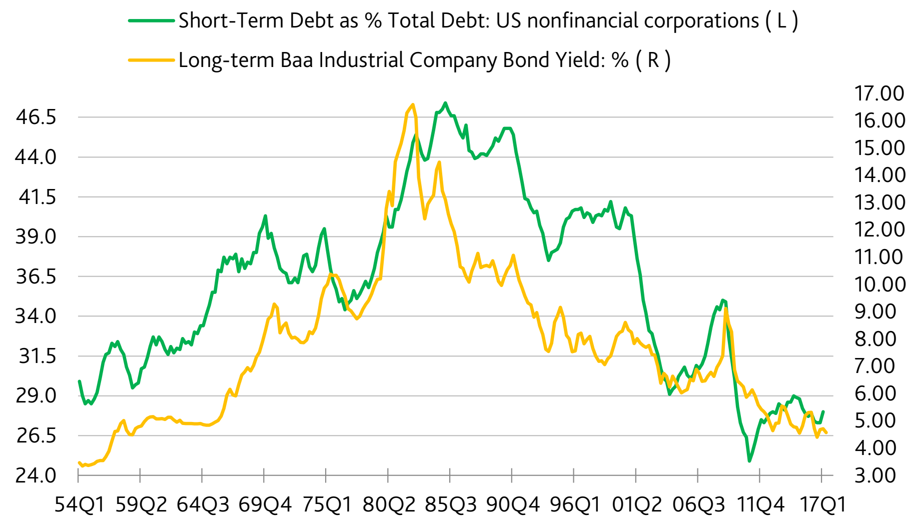
The slowdown by C&I loans owes something to the refinancing of shorter-term debt, such as bank loans, with longer-term fixed rate bonds. Expectations of significantly higher short- and long-term borrowing costs will prompt the refinancing of short-term debt with long-term bonds.

The record shows how businesses often correctly assumed that exceptionally high corporate bond yields would not persist. In response to this view, businesses often temporarily increased their reliance on variable-rate, short-term debt. For example, in response to 1984's exceptionally high yearlong average of 13.84% for Moody's long-term Baa industrial company bond yield, short-term debt comprised an atypically high 46.6% of outstanding nonfinancial corporate debt. During the recovery of 1991-2000,

the long-term Baa industrial yield had eased to 8.23%, on average. In turn, short-term-debt's share of total corporate debt eased to 40.2%.

The trend toward lower corporate bond yields and lower ratios of short-term debt to total debt continues. After averaging 6.68% during 2002-2007's upturn, the Baa bond yield dropped to its 5.30% average of the current recovery. In response, short-term debt has dropped from 31.2% to 27.7% of nonfinancial-corporate debt, on average. (Figure 3.)

Figure 3: Lowest Long-term Baa Industrial Company Bond Yield since Mid-1950s Explains Low Ratio of Short-Term Debt to Nonfinancial Corporate Debt
source: Moody's Analytics, Federal Reserve Financial Accounts

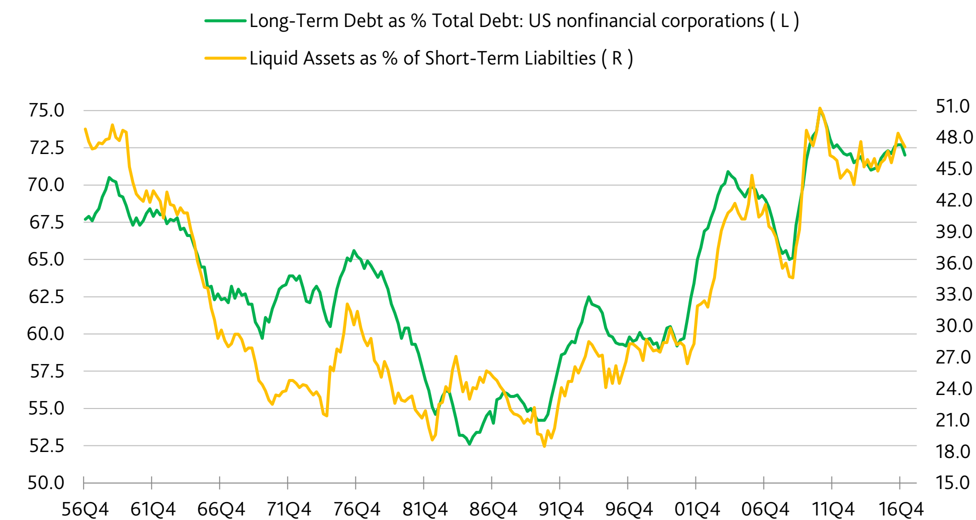


Longer maturities enhance credit quality

The lengthening of debt maturities is good for credit quality. Liquidity and financial flexibility benefit as a credit market obligation's term to maturity is lengthened.

The "quick ratio," or the ratio of liquid financial assets to short-term liabilities, offers insight regarding how well a business can cope with unexpected financial stress. For example, sufficient liquidity allows a company to retire maturing debt amid a widespread credit crunch that otherwise would render the refinancing of maturing debt as very costly if not impossible. Because of a lengthening of debt maturities that has been facilitated by exceptionally low bond yields, the "quick ratio" has risen from its 40% average of the five-years-ended 2007 to Q1-2017's 47%. Back when the long-term Baa bond yield averaged 13.84% in 1984, the "quick ratio" averaged only 25%. (Figure 4.)

Figure 4: An Extended Stay by Low Bond Yields Extends Maturities And Leaves Businesses Better Able to Withstand a Credit Crunch *source: Moody's Analytics, Federal Reserve Financial Accounts*



Credit Markets Review and Outlook

M&A's widening lead over profits reflects an aging upturn

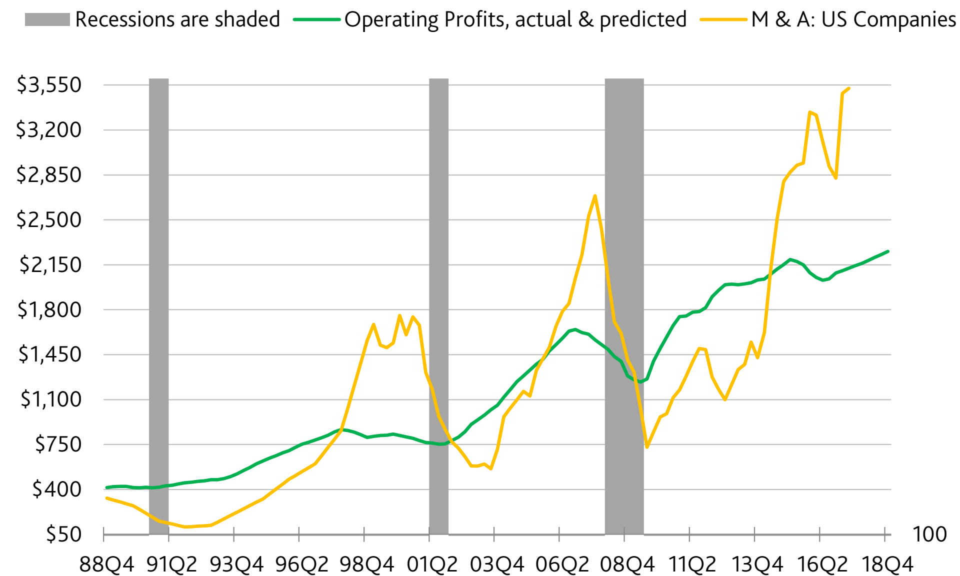
The aforementioned lackluster showing by broad measures of pretax operating profits stems from the relatively slow growth of corporate revenues relative to employment costs.

The growth of corporate gross value added (GVA), or the value of the final products supplied by corporations, has not been lively enough to improve the outlook for business spending on capital equipment and staff. The first-quarter of 2017 showed lackluster year-to-year increases of 3.0% for total corporate GVA and merely 2.2% for nonfinancial-corporate GVA. Both metrics have yet to break free from a pronounced deceleration. For example, the average annualized growth rate of total corporate GVA slowed from the 5.1% of the five-years-ended March 2015 to the 2.7% of the two-years-ended March 2017. On a comparably measured basis, nonfinancial-corporate GVA decelerated from 5.0% to 2.3%, respectively.

A typical late-cycle softening of the outlook for organic revenues drives the latest upturn by mergers, acquisitions and divestures involving US-domiciled businesses to a new record high. The ample amounts of financial capital stemming from comparatively low corporate borrowing costs and an upbeat equity market have facilitated M&A's robust response to diminished prospects for organic revenues.

However, M&A's latest surge comes with a warning. When M&A previously soared above pretax operating profits in 2007 and 1999-2000, a business cycle downturn was fast approaching. Thus, concerns about the adequacy of organic revenue that currently drive M&A also suggest that the upturn's momentum may be waning. (Figure 5.)

Figure 5: Dull Prospects for Revenues and Operating Profits Boost M&A ... M&A Tends to Surge In the Latter Stage of a Business Cycle Upturn: *$ billions*



The Week Ahead – US, Europe, Asia-Pacific

THE US

From Moody's Analytics - Economy.com and the Moody's Capital Markets Research Group
(Updates are made on Mondays.)

Summary, June 23: The Fed has hinted that the normalization of its balance sheet will be announced in September, earlier than our December call. The signal was fairly strong and something that we couldn't ignore, therefore we are changing our forecast from December to September. Though it will be announced in September, the process won't begin until October. This has implications for the next rate hike and our subjective odds of a rate hike have changed as we put the odds of an increase at 10% for September, 15% for November and 50% for December. This puts the cumulative odds of another rate hike this year at 75%. The odds of September are low, because the Fed will avoid double tightening by keeping changes in its balance sheet and interest rate policies separate.

Consistent with the Fed's communication, we expect the central bank to announce a schedule of caps on the maturing Treasuries and mortgage-backed securities of $6 billion and $4 billion, respectively, in September. The monthly caps will increase every three months until they reach their fully phased-in levels. For Treasury securities, the cap will increase in $6 billion increments over 12 months until it reaches $30 billion per month. For mortgage-backed securities, the cap will increase in $4 billion increments over 12 months until it reaches $20 billion per month. The fully phased-in caps will remain in place until the committee judges the Fed is holding no more securities than is necessary to conduct monetary policy, which we put at close to $3 trillion. This process will take three years to complete.

The changes relative to our earlier projections are minor, with the balance sheet shrinking sooner than we expected and suggesting that the balance sheet will hit its equilibrium level in late 2020 rather than in 2021 as we previously thought. The decline in the balance sheet will be $30 billion this year and $420 billion in 2018.

The incoming data will highlight the Fed's struggle to hit its inflation target. We expect the core PCE deflator to have risen 0.1% in May, lowering year-over-year growth from 1.5% to 1.4%. This could give some of the Fed reason to pause with regards to hiking rates. Elsewhere, we look for a modest decline in durable goods orders and the Conference Board Consumer confidence index. First quarter GDP growth will likely be revised higher, thanks to stronger growth in consumer spending.

THURSDAY, JUNE 22

Jobless claims (week ending June 17; 8:30 a.m. EDT)

Forecast: 240,000

We look for initial claims to have risen by 3,000 to 240,000 in the week ending June 17. This would reverse only some of the prior week's 8,000 decline and put new filings closer to their four-week moving average. The incoming data include the June payroll reference week. If our forecast comes to fruition, initial claims will be up only 7,000 between the May and June reference periods. There remains considerable uncertainty in the forecast for initial claims, because they can be thrown off this time of year by the timing of the end of the school year. There is also the potential that the annual auto retooling could occur sooner this year than in the past.

Initial claims in states with intensive auto manufacturing account for the largest share of total initial claims in July. If the shutdowns occur earlier, they could boost new filings in late June. But this would be more noise than signal about the health of the labor market. Because of the shutdowns and upcoming July Fourth holiday, initial claims will be less reliable until August.

FRIDAY, JUNE 23

New-home sales (May; 10:00 a.m. EDT)

Forecast: 588,000 annualized units
New-home sales disappointed in April, falling well short of expectations. Sales dropped 11.4% to 569,000 annualized units, but an upward revision to March eased the sting. Sales in March are now shown to have been 642,000 annualized units (previously 621,000) and the best this cycle. The revisions to March are a reminder that new-home sales are unreliable, since they are subject to large revisions. The trend in new-home sales remains favorable. Sales have averaged 591,000 annualized units over the prior six months, compared with the 592,000 in March and among the best this cycle.

Turning to May, we expect new-home sales to have risen to 588,000 annualized units.

MONDAY, JUNE 26

Durable goods orders (May; 10:00 a.m. EDT)

Forecast: -0.1% (total)
Forecast: 0.2% (ex transportation)
Durable goods orders fell 0.7% in April and some of the weakness was attributable to the volatile aircraft component. Nondefense aircraft orders fell 9.2% following a 15.4% gain in March. Also within transportation, motor vehicle and parts orders rose 0.3%. Excluding transportation, orders fell 0.4% in April. Core capital goods orders were unchanged, while orders slipped 0.1%, but there were downward revisions to March. Turning to May, we expect total durable goods orders to have slipped 0.1%. Excluding transportation, orders likely increased 0.2%.

Business confidence (week ending June 23; 10:00 a.m. EDT)

Forecast: N/A
Global business confidence remains remarkably strong and stable, as it has been since before last year's U.S. presidential election. Responses to all nine questions in the survey are upbeat, with hiring and investment notably strong. Although business confidence is very good, it remains well off its record highs achieved in spring 2015.

Our survey results are also not as strong as various other surveys of business and consumer confidence that have strengthened sharply since the presidential election. According to a recent New York Federal Reserve study, sentiment surveys that depend on canvassing new respondents each time are probably somewhat biased, as those happy with the election results are more likely to respond.
Businesses are increasingly fixated on regulatory and legal issues; about one-half of businesses say these issues are their number one concern. An additional one-fifth of businesses say finding qualified labor is their biggest problem. Concern with the strength of their sales and taxes has receded.
The four-week moving average in our business confidence survey slipped from 36.8 to 36.2 in the week ended Jun 16.

TUESDAY, JUNE 27

Consumer confidence (June; 10:00 a.m. EDT)

Forecast: 116.6
High-frequency measures suggest that the Conference Board Consumer confidence index will decline in June. We look for the index to have dropped from 117.8 in May to 116.6 in June. The strength of the labor market should limit the slide in the index.

WEDNESDAY, JUNE 28

Advance goods deficit (May; 8:30 a.m. EDT)

Forecast: $66.3 billion
The May advance goods deficit is expected to show a modest improvement, coming in at $66.3 billion. We anticipate a modest gain in exports following some weakness in April. Also, gains in imports should have moderated in May. The appreciation in the U.S. dollar has moderated, which should help exports. Also, the global economy is picking up, another support to U.S. exports. Risks to U.S. trade this year remain weighted to the downside given talk of tariffs, a border-adjustment tax, and the renegotiation

of trade deals. These policy actions would affect trade and possibly disrupt U.S. supply chains, which would hurt U.S. manufacturing production.

THURSDAY, JUNE 29

Jobless claims (week ending June 17; 8:30 a.m. EDT)

Forecast: 246,000

We look for initial claims to have risen by 5,000 to 246,000 in the week ended June 24, putting them slightly above their prior four-week moving average of 244,750. There is more uncertainty in the forecast than usual. Annual auto plant retooling usually occurs around early July, but there are suggestions that it could start earlier this year and be extended longer than normal for some domestic manufacturers. This could have implications for initial claims. Initial claims in states with intensive auto manufacturing account for the largest share of total initial claims in July. If the shutdowns occur earlier, they could boost new filings in late June. But this would be more noise than signal about the health of the labor market. Because of the shutdowns and upcoming July Fourth holiday, initial claims will be less reliable until August.

Continuing claims, for the week ending June 17, will be important, since they will be for the household reference week. Continuing claims rose 8,000 in the week ended June 10, their third consecutive weekly gain.

GDP (2017Q1-third estimate; 8:30 a.m. EDT)

Forecast: 1.4% at an annual rate

We anticipate a revision of first quarter GDP growth to 1.4% at an annual rate, better than the 1.2% in the government's second estimate. The final Quarterly Services Survey for the first quarter points toward stronger consumer spending and intellectual property investment growth. There should be a noticeable upward revision to consumer spending, which we look to have risen 1.3% at an annual rate, compared with the 0.6% in the government's second estimate. The upward revision should be concentrated in services, primarily healthcare. The QSS doesn't point to any significant revisions to first quarter intellectual property investment.

Revisions to other components will be mixed. Net exports will be revised lower and were likely neutral for first quarter GDP growth. Net exports added 0.1 of a percentage point to GDP growth in the government's second estimate. New data suggests that the inventory build was $3 billion heavier than previously reported but it will still subtract 1 percentage point from first quarter GDP growth. Growth in real equipment spending will likely be a touch weaker. Meanwhile, revisions to nonresidential structures and residential investment should be small. Similarly, real government spending will be revised to show a smaller decline than previously thought.

FRIDAY, JUNE 30

Personal income and spending (May; 8:30 a.m. EDT)

Forecast: 0.1% (nominal income)
Forecast: 0% (nominal spending)
Forecast: 0.1% (core PCE deflator)

We look for nominal personal income to have risen 0.1% in May following a 0.4% increase in April and 0.2% gain in March. The labor income proxy for all private workers, derived from the already released May employment report, rose 0.2%, but we are penciling a small gain in nominal wages and salaries. We expect nominal wage and salary income to have risen 0.1% in May.

Nominal consumer spending is forecast to have been unchanged in May. Lower gasoline prices will weigh on nominal spending. Autos are expected to be a drag based on already released data on unit and retail sales. Services spending is forecast to have risen a trend-like 0.3% in May, with a small lift coming from utilities.

Data from the May CPI and PPI suggest that the headline PCE deflator fell 0.1%. The core PCE deflator is expected to have risen 0.1%, lowering year-over-year growth from 1.5% in April to 1.4% in May.

University of Michigan confidence (June-final; 10:00 a.m. EDT)

Forecast: 94.2

We expect the University of Michigan's consumer sentiment index to have dropped to 94.2 in June, according to the final report. This would be below the preliminary survey's 94.5 and May's 97.1. The index will remain above that seen prior to the U.S. Presidential election. We believe consumer confidence got ahead of itself following the election. Just as the rise in sentiment following the election didn't justify a change to our spending forecast, the recent decline doesn't warrant a change either. Inflation expectations warrant close watch. Long-term inflation expectations rose in June, according to the preliminary survey but they remain low. Short-run inflation expectations may decline in June or July because of lower gasoline prices and tame food inflation.

EUROPE

By the Dismal (Europe) staff in London and Prague
(Updates are made on Mondays.)

Summary, June 23: The week ahead will shed light on consumer and business sentiment across Europe at the end of the second quarter. The measure for the euro zone is expected to have climbed further above its long-term average in June. The region's economy performed well at the start of the year, which together with high-frequency data suggesting more of the same in the three months to June, has been lifting sentiment. Confidence likely improved in Italy thanks to subsiding political risks. We do expect sentiment to have dipped in Germany, with the Ifo Business Climate Index retreating somewhat in June, but this is a correction after the index hit a record high in May. And a look at the labour market results makes it clear that German businesses remain confident the economy will steadily grow. Germany's seasonally adjusted unemployment rate fell to a record low of 5.7% in May, with the officially registered number of unemployed people dropping further during the month. We expect the jobless rate remained unchanged at 5.7% in June.

Meanwhile, consumer confidence in the U.K. likely retreated at the end of the second quarter. The unexpected loss of the Conservatives majority in the recent parliamentary election only added to the uncertainty caused by exit negotiations, which began on June 19. Overall confidence should remain subdued in 2017, weighed down by the major purchase index, households' sentiment about personal finances, and pessimism about the U.K.'s economic outlook. House prices in the U.K. have been disappointing in recent months, and the annual increase in the Nationwide HPI is expected to have cooled even further to 1.8% in June from 2.1% in the previous month. Excluding February's one-off monthly spike, the Nationwide data show a clear deterioration in price trend, which is corroborated by other gauges of the housing market. Households' living standards are expected to deteriorate further in coming months. The pound's slump should push up consumer prices, and wages are unlikely to follow suit, given our expectations for a weakening labour market. We therefore expect prices to stagnate or barely rise from now on.

The recent slump in oil prices will likely tamp down price pressures in Europe after inflation accelerated strongly at the beginning of this year. In May, the euro zone's annual inflation rate pulled back sharply to 1.4% from 1.9% in the previous month, and we expect it stayed at 1.4% in June. The slowdown has been driven mainly by cooling growth of energy prices. Instability in the Middle East has caused oil prices to fluctuate wildly in recent weeks, and the sharp increase in supply by some non-OPEC countries pushed the Brent crude oil price below $45 this week, which is the lowest level since mid-November 2016.

THURSDAY, JUNE 22

No major releases are scheduled.

FRIDAY, JUNE 23

France: GDP (Q1; 6:45 a.m. BST)

We expect France's GDP grew by 0.4% q/q in the three months to March, a touch lower than the upwardly revised 0.5% increase in the final quarter of 2016 but still higher than the first estimate at 0.3%. A strong pickup in investment likely will be behind the headline, especially in machinery and equipment, but investment in services gathered steam as well. Construction probably lost a little ground. Even so it likely helped lift the headline. A slowdown in consumer spending will have weighed modestly on the headline, likely on the back of the pickup in inflation, but the major drag was a plunge in net trade's contribution to growth. Net trade likely subtracted 0.8 ppt off the top-line number, as imports surged faster than exports. Despite the modest deceleration compared with the fourth quarter, we expect the final GDP numbers for the first quarter to come in relatively solid.

MONDAY, JUNE 26

France: Job Seekers (May; 5:00 p.m. BST)

France's job market is modestly improving and we expect the number of job seekers fell to 3.46 million in May after a solid showing in April. Annual numbers should maintain their downward trend as several reforms in 2015 and 2016 begin to bear fruit, including a tax credit and several measures to reduce labour costs. The labour market seems poised for a better year thanks to overall improvement in the economy and rising business and consumer confidence. Additionally, President Emmanuel Macron's party, En Marche, has secured an absolute majority in France's National Assembly, giving it the political power to advance its labor market reforms such as a revamp of hiring and firing legislation.

TUESDAY, JUNE 27

Italy: Consumer and Business Confidence (June 10:00 a.m. BST)

Italy's business confidence likely remained strong in June, in line with other high-frequency indicators. Although expansion in manufacturing and services eased in May, business activity remains buoyant. The strengthening euro zone and the U.S. economy will boost Italy's exports, while ultra-loose monetary and fiscal policy will also remain supportive this year. Subsiding political risks and progress in the banking sector should also boost the economy. Nevertheless, a reevaluation of credit risk in the course of monetary policy normalization, higher "hidden" unemployment, and a strengthening euro could drag on Italy's economy and undermine the recovery.

Germany: Ifo Business Climate Index (June; 11:00 a.m. BST)

The German Ifo Business Climate Index likely dipped in June after reaching a record high in May. The index is forecast to have reached 114.2, down from 114.6 in the previous month. Businesses are increasingly optimistic about the current situation thanks to Germany's robust results in the first quarter and start of the second. The seasonally adjusted unemployment rate fell to a record low of 5.7% in May. The number of unemployed declined by about 9,000 following a 15,000 decrease in the prior month. However, the near-term outlook likely darkened from the previous month. Worries over increased U.S. protectionism hurting global trade, and the upcoming Brexit negotiations in light of the recent spate of terrorist attacks across Europe likely soured sentiment. The ZEW indicator of economic sentiment for Germany slid to 18.6 in June from 20.6 in May.

WEDNESDAY, JUNE 28

Spain: Retail Sales (May; 8:05 a.m. BST)

The retail sector likely showed signs of strain in May. We expect retail sales contracted 0.4% over the month. Sales already slowed to 0.9% y/y until April this year, down from the average of 3.6% in 2016. Retail trade confidence cooled sharply in May compared with last year's average, with businesses expecting sales to edge lower. Sluggish domestic demand will hold back the retail sector's performance. We expect real wage growth will remain subdued and keep a further rebound in demand at bay.

Germany: Unemployment (June; 9:00 a.m. BST)

Germany's seasonally adjusted unemployment rate likely remained at 5.7% in June for a second consecutive month after it fell to this record low in May. German businesses remain confident in the country's future expansion, increasing their labour force, despite the uncertainties and geopolitical tensions. Details of the latest Markit manufacturing PMI showed that new work continued to surge, with the pace of increase among the fastest in the last six years. The weak euro has been supporting exports, which should also drive up demand for German products and in turn translate into higher employment. However, the unemployment rate is likely bottoming out and could start climbing later this year because of the vast inflow of refugees during the second half of 2015, some of whom will be entering the German labour force.

THURSDAY, JUNE 29

Euro Zone: Business and Consumer Sentiment (June; 7:05 a.m. BST)

The euro zone's economic confidence indicator likely improved to 109.5 in June following a marginal dip in the previous month. Despite the drop in May, confidence remained well above the long-run average of 100 and slightly below the 10-year high in April. Following the strong first quarter, with year-ago growth the strongest since mid-2015, the outlook for the second quarter is bright. The composite PMI registered the fastest output expansion in six years in May, with economic activity gaining momentum in France and Germany. Although confidence has rallied after a trough in August last year, significant risks persist. The U.K.'s divorce from the EU adds to market jitters, while Italy's troubled banking sector also poses a significant risk to financial stability. A new immigration wave and continued tensions with Russia could also resurface. On the brighter side, the resolution of election-related uncertainty in France and the Netherlands will likely buoy sentiment.

FRIDAY, JUNE 30

Germany: Retail Sales (May; 8:00 a.m. BST)

German retail sales likely recovered in May following a marginal decrease in the previous month. Sales are expected to have increased by 0.6% m/m from April, when they fell by 0.2%. In year-ago terms, they likely continued to rise at a relatively stable rate close to 2%. Although the Markit retail PMI retreated slightly in May to 55 from 56.2 in the previous month, it continued to suggest strong growth of retail sales. Consumption expenditure supported the country's expansion during the start of this year and will likely do so in the coming quarters. However, conservative German households will probably not increase their spending significantly in coming months because the outlook remains uncertain and because inflation is heating up. Although Germany's annual national measure of inflation decelerated to 1.6% in May, seasonally adjusted, from 2.1% in April, it was still strong and will likely accelerate in the coming months.

Euro Zone: Preliminary Consumer Price Index (June; 10:00 a.m. BST)

The euro zone's annual harmonized inflation likely remained unchanged at 1.4% in June from a month earlier. Softer oil price growth and the base effect likely weighed on the headline figure. Core inflation, meanwhile, remained subdued because of tepid wage growth. Softening inflation pressure is in line with the PMI for manufacturing and services in May, which showed input costs beginning to ease. This could also drive down selling prices in coming months. After the temporary effect of lower energy prices disappears, however, inflation should pick up again. But we don't expect the headline reading to climb above the ECB's target of close to but below 2%. Although below-target inflation doesn't bode well for the central bank, slowing core inflation is more worrying and may delay the

normalization of monetary policy. While we don't expect the ECB to change its forward guidance during the summer months, we do predict it will turn slightly hawkish later this year.

ASIA-PACIFIC

By Katrina Ell and the Asia-Pacific economics team of Moody's Analytics

Japan's economic momentum likely remained firm in May

The positive momentum in the Japanese economy likely continued in May. The economy grew 0.3% y/y in the March quarter, and the May data dump will likely confirm that in the June quarter the economy is set for its sixth consecutive expansion. May retail sales are expected to rise after strong gains the prior month. The uptick is related mostly to base effects, as retail sales were falling sharply this time last year. But in 2017, the improved global environment and an uptick in retail fuel costs are driving overall retail spending. However, demand for big-ticket items remains uneven because of poor wage growth prospects.

A lack of wage growth is keeping Japanese household balance sheets tamed. Workers' household expenditures remain lacklustre. This trend is unlikely to improve meaningfully, because consumers are still pessimistic about their prospects. Surprisingly, a tight labour market isn't leading to higher wages yet. Labour demand is outstripping labour supply, although this also reflects Japan's poor demographics because the workforce is set to decline. This is why the jobless rate is expected to remain at multidecade lows over the coming year. A reason for Japan's recent rise has been the uptick in the global tech cycle. This has been part of the reason production has strengthened. Automakers are also releasing new car models, which will buttress production over the coming months.

Elsewhere, foreign trade data out of Asia will largely be positive. Export growth from Hong Kong remains firm on the back of rising global trade. Trade from the port city is a good proxy for the global trade environment. We expect growing consumption in China to keep demand for New Zealand dairy firm. Agriculture exports are a major export commodity from New Zealand, and these usually benefit from stronger Chinese demand.

THURSDAY, JUNE 22

New Zealand – Monetary Policy – June

Time: 7:00 a.m. AEST (Wednesday 9:00 p.m. GMT)
Forecast: 1.75%
The Reserve Bank of New Zealand will keep the policy rate steady at 1.75% at its June policy meeting. The central bank is comfortable on the sidelines, keeping rates in accommodative territory. Inflation is slowly creeping higher, but low base effects from oil prices will soon fade and take a little pressure off. Domestic demand is going well thanks to strong population growth fuelled by record-high net migration and a tourism boom. The central bank has been clear that policy settings are likely to stay on hold for an extended period in an effort to keep downward pressure on the currency. We expect the central bank will stay on hold for the next year.

FRIDAY, JUNE 23

Singapore – Industrial Production – May

Time: 3:00 p.m. AEST (5:00 a.m. GMT)

Forecast: 8%

We look for Singapore's May industrial production growth to accelerate to 8% y/y, compared with April's 6.7% result. Electronics have been the main positive for the city-state's manufacturing sector in recent months as global tech demand has improved. In May, we look for a rebound in output from the volatile biomedical segment, which was the main drag in April. Transport engineering output will fall again as demand for new oil rigs remains muted.

Taiwan – Domestic Trade – May

Time: 6:00 p.m. AEST (8:00 a.m. GMT)

Forecast: 0.6%

Taiwan's domestic trade likely ticked up a whisker in May from April's mediocre 0.4% y/y gain. Fuel spending is lifting the headline as higher global oil prices filter through to consumers. Improved manufacturing and export conditions are taking longer than usual to filter through to consumers, and industrial production and domestic trade historically are tightly correlated. Softness in wage growth is contributing to soft domestic trade as households keep their purse strings tight.

Taiwan – Industrial Production – May

Time: 6:00 p.m. AEST (8:00 a.m. GMT)

Forecast: 3.7%

Taiwan's industrial production likely accelerated in May after a surprise 0.6% y/y drop in April. A fall in gas and electricity production drove the sharp drop as manufacturing cooled only slightly. Looking through the monthly volatility in utility production, we expect industrial production to cool over 2017, as the global tech cycle appears to have peaked and this tends to drive Taiwan's industrial production given its heavy exposure to electronics and components.

MONDAY, JUNE 26

Hong Kong – Foreign Trade – May

Time: 6:30 p.m. AEST (8:30 a.m. GMT)

Forecast: -HK$28.4 billion

Trade activity through Hong Kong's port is growing strongly. Broad-based export growth indicates that global trade is strengthening. Commodity shipments are being driven by China's investment recovery, which is boosting both values and volumes of shipments. Global tech demand is also driving tech component shipments through Hong Kong, although signs of a slowdown are emerging. The monthly deficit likely narrowed to HK$28.4 billion in May, from HK$34.1 billion in April.

TUESDAY, JUNE 27

South Korea – Consumer Sentiment Index – June

Time: 7:00 a.m. AEST (Monday 9:00 p.m. GMT)

Forecast: 105

The Bank of Korea's consumer sentiment index likely cooled a little in June after surging to 108 in May with the election of President Moon Jae-in, which followed political uncertainty and the impeachment of Park Geun-hye. Moon's plans to increase welfare and employment especially for the young, for whom unemployment is painfully high, has lifted sentiment. Yet, high household debt is a concern, keeping a lid on spending plans.

New Zealand – Foreign Trade – May

Time: 8:45 a.m. AEST (Monday 10:45 p.m. GMT)

Forecast: NZ$220 million

New Zealand's monthly trade balance likely remained in surplus in May after April's NZ$578 million surplus. Merchandise exports are expanding steadily thanks to strong demand for soft commodities, especially diary. Chinese demand has kept dairy prices and volumes buoyant in recent months, and this should continue into the second half of the year. Imports, especially for consumer products, are a good

proxy of domestic demand in New Zealand, which remains robust thanks to strong net migration and tourism spending.

WEDNESDAY, JUNE 28

No major economic indicators are scheduled for release.

THURSDAY, JUNE 29

Japan – Retail Sales – May

Time: 9:50 a.m. AEST (Wednesday 11:50 p.m. GMT)
Forecast: 2.8%
Low base effects and rising fuel prices likely boosted Japan's retail sales in May after their 3.2% rise in April. Though retail sales are increasing on a year-ago basis, the momentum in 2017 has been poor. Spending on big-ticket items is still sporadic because wage growth has remained subdued. A sharp increase in underlying retail activity is unlikely because consumers remain pessimistic about their prospects.

FRIDAY, JUNE 30

Thailand – Industrial Production – May

Time: Unknown
Forecast: 1.2%
Thailand's industrial production growth likely accelerated to 1.2% y/y in May from a 1.7% decline in the prior month. Manufacturing will be supported by improvements in global conditions, which are pushing up demand for electronics products. Food production will also pick up thanks to improved growing conditions. Weak domestic conditions are preventing stronger production growth. Consumer spending is uneven, while private investment has failed to improve since 2014, when the junta government was installed.

South Korea – Industrial Production – May

Time: 9:00 a.m. AEST (Thursday 11:00 p.m. GMT)
Forecast: 4.2%
Korean industrial production likely rose to 4.2% y/y in May, up from 1.7% in April. Manufacturing disappointed in April because of a sharp slowdown in electronics production. We expect tech ticked back up in May, as the slowdown in Chinese tech demand appears to have passed. Manufacturer sentiment surveys show that conditions remain positive in Korea, but demand is mainly driven offshore, as domestic demand is constrained.

South Korea – Retail Sales – May

Time: 9:00 a.m. AEST (Thursday 11:00 p.m. GMT)
Forecast: 0.1%
South Korean retail sales likely remained subdued in May. We expect retail volumes grew just 0.1% m/m, after rising 0.7% in April. The monthly series is notoriously volatile, but looking through the haze, high household debt is keeping consumer spending subdued. Improved jobs growth in recent months has not yet translated to higher spending.

Japan – Consumer Price Index – May

Time: 9:30 a.m. AEST (Thursday 11:30 p.m. GMT)
Forecast: 0.3%
Japan's core consumer prices likely held at 0.3% y/y in May. Underlying inflation remains well below the central bank's 2% target. The recent uptick in prices has been largely driven by higher import costs on the back of the yen's depreciation. Higher global commodity prices than the previous year have also raised import prices. Without wage growth, inflation is unlikely to rise above 1%.

Japan – Employment Situation – May

Time: 9:30 a.m. AEST (Thursday 11:30 p.m. GMT)
Forecast: 2.8% Unemployed
Japan's jobless rate for May is expected to remain at a multidecade low of 2.8%. Labour demand is still high and firms are finding it increasingly difficult to fill positions, as evidenced by the rising jobs-to-applicants ratio. That said, firms still haven't enticed workers with higher pay. There is probably a tipping point when higher wages will need to be paid to keep the workforce growing.

Japan – Household Expenditures Survey – May

Time: 9:30 a.m. AEST (Thursday 11:30 p.m. GMT)
Forecast: 0.4%
Japan's nominal workers' household expenditures likely ticked up in May, after a 2.7% y/y drop in April. However, a modest increase doesn't signal an end to the malaise across household balance sheets. Japanese consumers remain reluctant to spend on big-ticket items because of low wage growth. Recent wage negotiations don't bode favourably for workers. This means overall expenditures are unlikely to shift towards discretionary spending items.

Japan – Industrial Production – May

Time: 9:50 a.m. AEST (Thursday 11:50 p.m. GMT)
Forecast: 0.4%
Industrial production likely cooled in May after a sharp 4% m/m increase in April. Manufacturers benefit from the yen's recent depreciation. The uptick in the global tech cycle has also helped electronics production, and that will likely remain firm as the tech cycle enters the production phase. Auto production remains a bright spot thanks to the release of various new car models.

China – Manufacturing PMI – June

Time: 11:00 a.m. AEST (1:00 a.m. GMT)
Forecast: 51.1
The official manufacturing PMI likely cooled to 51.1 in June, down from 51.2 in May. The slowdown is expected because the Chinese economy has peaked for now. The pullback seems natural because of a soft patch in the global tech cycle and various policy measures that have looked to tighten lending. This should cool manufacturing PMI a little in June.

Japan – Housing Starts – May

Time: 3:00 p.m. AEST (5:00 a.m. GMT)
Forecast: 0.3%
Japan's housing starts likely slowed from the 1.9% y/y increase in April. We expect starts for rental purposes to remain firm, which reflects the construction work for investment properties last year. Low interest rates support the outlook for the housing market, but with a declining population, the need to build more homes has diminished.

Thailand – Private Consumption – May

Time: 5:30 p.m. AEST (7:30 a.m. GMT)
Forecast: 3%
Private consumption growth is expected to have slowed to 3% y/y in May after increasing 3.6% in April. Thai households are faced with persistent uncertainty due to the unresolved political situation. This is hitting consumer confidence and restricting purchases of durable goods. On the positive side, farm incomes have improved in 2017 after struggling in the prior year. However, the susceptibility of agriculture to natural disasters puts the sustainability of this trend in doubt.

Thailand – Foreign Trade – May

Time: 5:30 p.m. AEST (7:30 a.m. GMT)
Forecast: US$2 billion
Thailand’s trade surplus is expected to have widened to US$2 billion in May from US$1.5 billion in April. Export growth has improved significantly over the past six months because of the overall improvement in global conditions. This has been particularly beneficial for electronics. The automobile sector hasn’t had as a large an improvement, though, because of stiff competition from other countries in Southeast Asia.

The Long View

The US: During January-May 2017, medium-grade issues supplied 56% of investment-grade bond offerings — close to its 55% share of the last five years

By John Lonski, Chief Economist, Moody's Capital Markets Research Group,
June 22, 2017

CREDIT SPREADS

As measured by Moody's long-term average corporate bond yield, the recent investment grade corporate bond yield spread of 119 bp hardly differs from its 122-point mean of the two previous economic recoveries. Any narrowing by this spread may be limited by more cash- or debt-funded acquisitions, spin-offs, stock buybacks, and dividends. Subpar growth by business sales and pretax profits will also add to credit risk, as will a rising risk of high-yield defaults.

The recent high-yield bond spread of 385 bp is less than what is inferred from the spread's macroeconomic drivers and the high-yield EDF metric, but is wider than what is implied by an ultra-low VIX index. The implications for liquidity of regulatory changes merit scrutiny. If regulatory change enhances the market making capabilities of banks, corporate bond yield spreads may be thinner than otherwise.

DEFAULTS

After setting its current cycle high at January 2016's 5.9%, the US high-yield default rate has since eased to May's 3.9%. Moody's credit policy group expects a 2.8% average for the default rate of 2018's first quarter. A deeper slide to its 1.85% average of the 18-months-ended June 2015 is unlikely for now.

US CORPORATE BOND ISSUANCE

For 2016, US$-denominated bond issuance rose by 5.5% annually for IG, to $1.411 trillion and dropped by -3.5% to $341 billion for high yield. Across broad rating categories, 2016's newly rated bank loan programs from high-yield issuers advanced by 45% to $98 billion for Baa, rose by 2% to $212 billion for Ba, and soared by 43% to $208 billion for programs graded less than Ba.

Q4-2015's worldwide offerings of corporate bonds showed annual percent declines of -8.7% for IG and -51.4% for high-yield, wherein US$-denominated offerings dipped by +1.3% for IG and plunged by -45.1% for high yield.

Q1-2016's worldwide offerings of corporate bonds showed annual percent declines of -4.9% for IG and -51.4% for high-yield, wherein US$-denominated offerings rose by +1.3% from Q1-2015 for IG, but plunged by -45.1% annually for high yield.

Q2-2016's worldwide offerings of corporate bonds showed an annual increase of +6.3% for IG and an annual drop of -5.2% for high-yield, wherein US$-denominated offerings dipped by -2.2% for IG and sank by -6.3% for high yield.

Third-quarter 2016's worldwide offerings of corporate bonds showed an annual advances of +19.5% for IG and +42.8% for high-yield, wherein US$-denominated offerings soared higher by +34.1% for IG and by +46.4% for high yield.

Fourth-quarter 2016's worldwide offerings of corporate bonds showed annual percent changes of -10.2% for IG and +24.9% for high-yield, wherein US$-denominated offerings fell by -8.5% for IG and advanced by +24.9% for high yield.

First-quarter 2017's worldwide offerings of corporate bonds showed annual percent increases of +7.7% for IG and +110.6% for high-yield, wherein US$-denominated offerings advanced by +17.1% for IG and by +98.3% for high yield.

The Long View

For yearlong 2016, worldwide corporate bond offerings rose by 2.3% annually for IG (to $2.402 trillion) and sank by -7.8% for high yield (to $426 billion). In 2017, worldwide corporate bond offerings may rise by 2.4% annually for IG and may advance by 20.2% for high yield.

The financing of acquisitions and shareholder compensation will stand out among 2016's uses of funds obtained via bond issues and newly-rated bank loan programs. Companies will resort to acquisitions and divestitures in order to better cope with the US's subpar recovery. To the degree companies fear significantly higher bond yields, pre-fundings will rise.

US ECONOMIC OUTLOOK

The mid-point of the range for fed funds should finish 2017 no greater than 1.375%. In view of the considerable underutilization of the world's productive resources, low inflation should help to rein in Treasury bond yields. As long as the global economy operates below trend, the 10-year Treasury yield may not remain above 2.45% for long. A fundamentally excessive climb by Treasury bond yields and a pronounced slowing by expenditures in dynamic emerging market countries are among the biggest threats to the adequacy of economic growth and credit spreads going forward.

EUROPE

By Tomas Holinka of Moody's Analytics
June 22, 2017

Eurozone

The euro zone recorded its fastest growth rate in two years in the March quarter. The real GDP expanded by 0.6% q/q in the first quarter, stronger than preliminary estimates and the December stanza's 0.5% pace. High-frequency indicators suggest this buoyant pace will persist through the June quarter. The area's composite PMI held steady at 56.8 in May, unchanged from April's six-year high and far above the average of 55.6 recorded in the three months to March. This is consistent with growth picking up further in the second quarter, to around 0.6% to 0.7%. The impressive momentum is being supported mainly by a stellar manufacturing performance. The details brought even better news, showing that booming manufacturing orders are raising work backlogs and lifting job creation to its fastest in over 10 years, as firms expand capacity to meet the rise in demand. Meanwhile, the euro zone's unemployment rate unexpectedly fell to 9.3% in April, from a downwardly revised 9.4% in March and from 10.2% in April 2016, the lowest rate since March 2009. Cyclical labor market improvement combined with strengthening wage growth in some euro area countries will boost household spending, while broad-based improvement in global demand will support euro area exports. Nevertheless, the jobless rate would be higher if discouraged and underemployed part-time workers were added. The falling unemployment rate could thus mislead, and corporations have no reason to increase wages because of still-high labor underutilization. This is restraining wage growth and widening income inequalities.

Ultra-loose monetary policy and mildly stimulative fiscal policy should also support the rebound in investment, which remains below the pre-crisis level as firms expect demand to stay soft. After slightly less restrictive fiscal policy in 2016, government stimulus will likely boost most euro zone economies this year. While fiscal stimulus to GDP will jump in Germany, France and Italy, fiscal policy will subtract from the expansion in Spain, the Netherlands and Portugal, though less so than in 2016. Although the euro zone's outlook remains upbeat, weaker performance in the U.K. may drag on growth. Final data of U.K. GDP show the service sector as the main culprit of the slowdown in the first quarter, though construction and production output also lost some momentum. In the expenditure breakdown, consumer spending pulled back sharply and is the main drag on growth in 2017.

In June monetary policy meeting, the European Central Bank took a small but symbolically important step toward changing its policy stance, taking future rate cuts off the table for now. The ECB noted that

policy rates would remain at present levels for an extended period and well past the horizon of quantitative easing. This is a small change from past forward guidance that said rates would remain at present or lower levels. There remains a bias for extending QE, as the central bank sees this rather than interest rates as their preferred tool to boost inflation. There is plenty of work to be done on the inflation front and we believe the central bank should proceed cautiously as many developed central banks have found it difficult to get inflation to their targets. The ECB didn't make any changes to rates or QE. Our baseline is that the ECB should turn slightly more hawkish later this year, likely announcing its plans for tapering its asset purchases in September but continuing its bond-buying program until at least June 2018. Normalizing the deposit rate should start by the middle of next year, while the repo rate should remain at its current settings at least until the second quarter of 2019.

Results of the French and Dutch elections removed key political risks to financial markets and calmed investors. French president Emmanuel Macron's party, En Marche, has secured an absolute majority in France's National Assembly, giving it the political power to advance its liberal, market- and globalization-friendly reform agenda. The political situation is also brightening in Italy. The Eurosceptic Five Star Movement suffered heavy losses in municipal elections in early June, casting doubt on whether it can win parliamentary elections next year. Furthermore, without agreement on electoral law reform, the odds of snap elections being called this September are worsening. Early elections seem off the table, and Italians will vote next May. This should give former prime minister and ruling party leader Matteo Renzi enough time to consolidate the party and prepare it for the next general election.

U.K.

The U.K. economy's growth likely recovered somewhat in the second quarter following a disappointing start to the year. Accordingly, our high-frequency GDP model has begun tracking second quarter growth at 1.9% in annualized quarterly terms and 0.5% not annualized, an acceleration from a mere 0.2% growth in the first quarter. However, this result does not remove our fears that the U.K. economy is set for a rough ride in 2017. Still, the recovery in industrial survey data in May brings some optimism. The latest U.K. Markit/CIPS manufacturing PMI fell only to 56.7 from three-years high of 57.3 recorded in April, and signaled an improvement in operating conditions. Meanwhile, U.K. consumer confidence unexpectedly rose in May to -5 from -7 in April. We find it hard to understand this optimism since it contrasts sharply with our view that the pound's depreciation, the subsequent soar in inflation, and the slowdown in nominal wages will hurt consumer spending throughout 2017. We expect this to be just a blip, likely related to June's elections. The June elections will likely be seen as a sign that a softer exit could be negotiated if Theresa May were to have a larger majority in government. So in months to come, we expect households to shift focus from politics to the state of their finances. Households' expectations about their future financial situation will likely deteriorate sharply and turn negative by the second half of the year, in line with the decline in real wages. We already see evidence that households are tightening their purse strings: Retail sales figures for the past three months have been weak, and advanced indicators for May suggest that the first quarter's weakness likely carried over into the second.

Rising inflation and worsening labor market will weigh on household spending. Although the unemployment rate fell to a record low 4.6% in the April quarter and employment growth gained 0.4% q/q, wage gains lost further momentum in April; excluding bonuses, they slowed to 1.7% y/y from a downwardly revised 1.8% in the March stanza. This slowdown in pay growth is worrisome, especially in light of the whopping 2.9% jump in inflation reported by the Office for National Statistics in mid-June. That's because higher prices combined with slower pay growth automatically mean households' real wages deteriorate: In monthly terms, real pay plunged by 0.6% y/y in the three months to April, its biggest drop since mid-2014. Given that we expect inflation to average 2.8% this year and peak at 3.1% later this year, household spending—the engine of U.K. growth—should pull back in line with the deterioration in consumers' purchasing power.

Despite the slump in sterling and associated rise in inflation, the weakening British economy is expected to keep the Bank of England on the sidelines. Moody's Analytics expects the Monetary Policy Committee to delay tightening policy until well after the EU exit, gradually raising the main policy rate from mid-2019. Fiscal policy will support the BoE's accommodative monetary policy. The government has abandoned its plan to close the budget deficit by 2020 and has confirmed plans to lower the corporate tax rate from the current rate of 20% to 17% by April 2020 and increase government spending to prop up waning economic activity.

The forthcoming exit negotiations and anxiety about the U.K.'s future at home and abroad should keep sentiment about the general economic outlook for the next year in negative territory, with risks tilted to the downside depending on how negotiations go. Real GDP growth is expected to decelerate from 1.8% in 2016 to around 1.5% in 2017 and 1% in 2018 before gradually strengthening to settle around 1.8%, its new post-exit potential growth rate, around 0.2 percentage point lower than it would have been were the U.K. to stay in the EU.

ASIA PACIFIC

By Faraz Sayed and the Asia-Pacific Staff of Moody's Analytics
June 22, 2017

The Indian economy remains in a cyclical slowdown in mid 2017, and as the Reserve Bank of India Governor Urjit Patel alluded, there is scope to rekindle 'animal spirits'. GDP growth decelerated sharply to 6.1% y/y in the March quarter, down from 7% the quarter prior. The removal of high-valued currency—equivalent to around 86% of total circulation in November—was one reason for the slower growth. However, demonetization exacerbated but did not cause the slide in GDP growth. A sustained slump in investment and exports was the catalyst for the slowdown in mid-2016.

The slowdown has heightened short-term risks to the economy, despite the successful passage of the goods and services reform and robust consumption growth. This is because concerns around investment have intensified; investment declined 2.1% in the March quarter following an abysmal 2016, when it declined 1.9%. Overall, consumption will buttress growth, but GDP growth is still likely to decelerate to 6.8% in 2017, after rising 7.2% in 2016. As the ill effects of demonetisation fade, we expect a moderate recovery, and GDP will likely grow 7.8% in 2018.

Investment has dropped from nearly 40% to 30% as a share of GDP since 2010. The trend is unlikely to improve over the coming year, as both corporate sector and public sector balance sheets are deteriorating. According to some estimates, more than 15% of all credit outstanding in India is nonperforming. Moreover, lending to India's corporate sector fell around 5% y/y in early 2017, a trend that will likely persist for the remainder of the year.

The troubles began with the credit boom at the early part of this decade. Corporate India took on hefty debts to finance investments. But these didn't fully pay off, partly because of supply bottlenecks in India, but also because of overenthusiastic assumptions about returns to investment. As a result, corporate India is struggling to repay these loans. Public sector banks had initially been slow in recognising bad loans, but measures implemented by the RBI are making them more transparent.

As corporate and public balance sheets deteriorate, there's little appetite for more investment. Indian industries are taking advantage of lower interest rates to deleverage; lending rates fell from more than 10% in 2013 to 6.8% more recently.

The recent proposal of the Finance Resolution and Deposit Insurance Bill will make it easier to resolve insolvency in the financial sector. However, piecemeal measures alone are unlikely to solve the issues in the ailing banking sector. Capital injection, or privatisation of the public sector banks, could solve the balance sheet problems.

India's long-awaited goods and services tax looks good to go in July. The GST will eliminate the various taxes and levies across the states and replace them with a single tax system. This will remove the double-counting that currently occurs across states.

For a large economy like India's, teething issues in implementing the GST are expected, so its benefits will not be felt straight away. Unlike other countries with a single GST rate, India's GST will be corralled into four buckets: 5%, 12%, 18% and 28%. This has been a source of confusion for businesses. For instance, renewable energy-based devices attract a 5% tax, but inputs into production such as solar cells and modules are bunched in the higher bucket of 18%. The GST council is expected to revise the various items further in mid-June, but we don't expect large-scale changes to the current system.

The GST will likely add to GDP growth over the long run. India's business environment is set to improve, and foreign direct investment is expected to remain buoyant; India was the 10th largest recipient of foreign direct investment inflows in 2016. A more consistent tax base may help government coffers over the long run, which could create room for infrastructure funding. So far, financial markets have given the tick of approval to India's reform momentum, as evidenced by a sustained rise in the equity index this year.

GST is also unlikely to have a material impact on inflation. In most countries, the GST causes a one-off shift in inflation, which returns to previous rates after the base effects fade. In India, such a jump-off remains improbable; while prices of some goods will rise, the GST will reduce double taxes, which could offset potential price hikes. Thus far, the RBI's projections also suggest the impact of GST will be neutral.

The RBI left the policy repo rate unchanged in early June, though the chorus of calls for rate cuts has risen because inflation decelerated to 2.2% y/y in May. But this is within the 2% to 3.5% band that the RBI projected. The May inflation print alone won't cause the RBI to cut rates, rather, the outlook for rate cuts will depend on the upcoming monsoon season. A good kharif crop harvest boosts food supply and keeps a lid on food inflation, which crucially accounts for nearly half of the consumer price basket.

We forecast a 25-basis point rate cut in the August meeting if the monsoon rains are around the long-term average. Rains more than 90% of the long-term average are considered normal; the Indian Meteorological Department has forecast rains to be around 98% of the long-term average. One piece of supporting evidence for a rate cut is that the real interest rate has trended upwards in 2017. With a concurrent slowdown in GDP growth, a rate cut remains a likely option.

Ratings Round-Up

By Njundu Sanneh

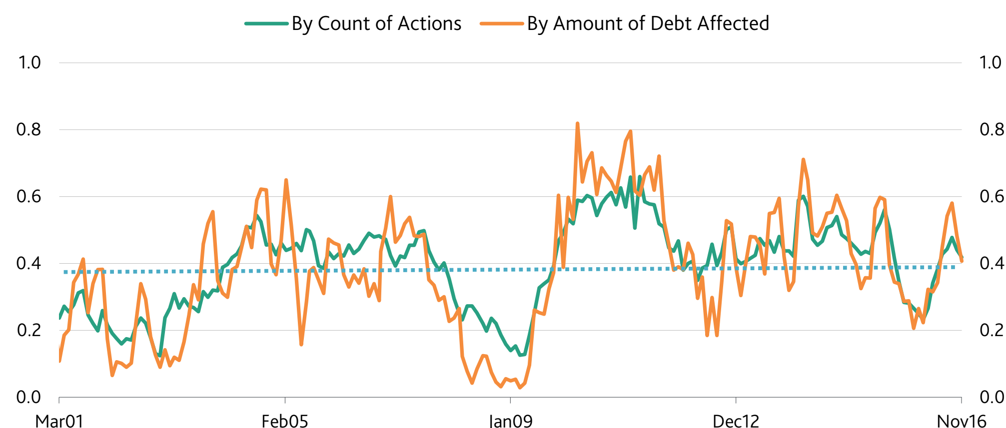
A Much Better Week in the US

Over the past week there were 11 rating revisions apiece for the US and Europe. Speculative grade industrials set the pace in the US, while financials accounted for most of the European list. The contribution of positive rating changes was 45% for Europe and 64% for the US, overturning the pattern in the US which was below 40% for the previous three weeks. The US positive rating changes were anchored by two energy sector upgrades due to changes in capital structure, which has been a major driver of energy company upgrades. Tesoro Corporation and Myria Holdings, Inc. had rating upgrades because of a security fall away and an infusion of equity, respectively. JetBlue Airways Corporation was another noteworthy upgrade with a strengthened balance sheet cited as part of the reason for the positive rating change.

The downgrade of four Azerbaijani banks headlined European rating changes, accounting for four of the seven total downgrades. The devaluation of the Azerbaijani currency amid high dollarization of the bank debts means high borrowing costs, foreign exchange losses, and significantly deteriorated asset quality. Major companies on the rating changes list include Royal Bank of Scotland and Bank of Ireland.

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	Old STD Rating	New STD Rating	IG/SG
6/14/17	CLEAN HARBORS, INC.	Industrial	SrUnsec	1,650	D	Ba2	Ba3			SG
6/15/17	MYRIA HOLDINGS INC.	Industrial	SrSec/LTCFR/PDR	1,750	U	Ba3	Ba1			SG
6/15/17	RECKITT BENCKISER GROUP PLC	Industrial	SrUnsec/LTIR/CP	3,000	D	A1	A3	P-1	P-2	IG
6/15/17	SEMINOLE TRIBE OF FLORIDA	Industrial	SrUnsec/SrSec/BCF	571	U	Ba1	Baa3			SG
6/16/17	CROCKETT COGENERATION, LP	Industrial	SrSec	135	D	Baa3	Ba3			IG
6/16/17	OCWEN FINANCIAL CORPORATION	Financial	SrUnsec/SrSec/LTCFR/BCF	700	D	Caa1	Caa2			SG
6/19/17	FIDELITY NATIONAL INFORMATION SERVICES, INC.	Industrial	SrUnsec	8,950	U	Baa3	Baa2			IG
6/19/17	FIRST QUALITY PRODUCTS, INC. - First Quality Finance Company, Inc.	Industrial	SrUnsec	600	U	B2	B1			SG
6/19/17	JETBLUE AIRWAYS CORP.	Industrial	LTCFR/PDR/SGL		U	Ba3	Ba1	SGL-2	SGL-1	SG
6/20/17	LIQUIDNET HOLDINGS, INC.	Financial	SrSec/BCF/LTCFR		U	B2	B1			SG
6/20/17	TESORO CORPORATION	Industrial	SrUnsec/SGL	2,825	U	Ba2	Ba1	SGL-2	SGL-1	SG

Source: Moody's

FIGURE 4 Rating Changes: Corporate & Financial Institutions – EUROPE

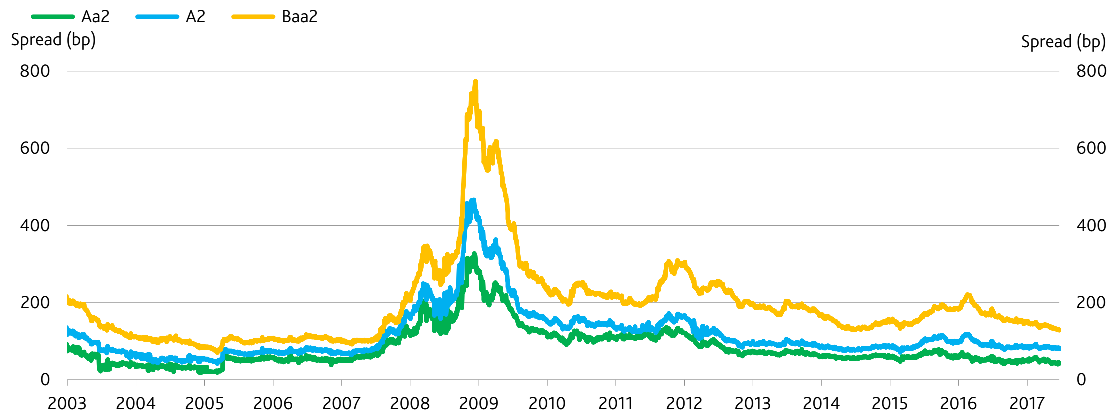
Date	Company	Sector	Rating	Amount ($ Million)	Up/ Down	Old LTD Rating	New LTD Rating	Old STD Rating	New STD Rating	IG/ SG	Country
6/19/17	IMMIGON PORTFOLIOABBAU AG	Financial	SrUnsec/LTIR/LTD/MTN/Sub	1,399	U	B1	Ba1			SG	AUSTRIA
6/14/17	BANK VTB, JSC - VTB Bank (Azerbaijan)	Financial	LTD		D	B2	B3			SG	AZERBAIJAN
6/14/17	JOINT STOCK COMMERCIAL BANK RESPUBLIKA	Financial	LTD		D	B2	B3			SG	AZERBAIJAN
6/14/17	OJSC BANK OF BAKU	Financial	LTD		D	B3	Caa1			SG	AZERBAIJAN
6/14/17	OJSC XALQ BANK	Financial	LTD		D	B2	B3			SG	AZERBAIJAN
6/19/17	CGG SA	Industrial	SrUnsec/SrSec/BCF/LTCFR/PDR	1,596	D	Ca	C			SG	FRANCE
6/14/17	HEIDELBERGER DRUCKMASCHINEN AG	Industrial	SrUnsec/LTCFR/PDR	229	U	Caa1	B3			SG	GERMANY
6/16/17	FTE HOLDING GMBH - FTE Verwaltungs GmbH	Industrial	SrSec/LTCFR./PDR/BCF	294	U	B2	B1			SG	GERMANY
6/16/17	BANK OF IRELAND	Financial	SrUnsecLTIR/LTD/Sub/JrSub/MTN/PS		U	Baa2	Baa1			IG	IRELAND
6/16/17	KLEOPATRA HOLDINGS 1 S.C.A. - Kleopatra Holdings 2 S.C.A	Industrial	LTCFR/PDR	1,750	D	B2	B3			SG	LUXEMBOURG
6/15/17	THE ROYAL BANK OF SCOTLAND GROUP PLC	Financial	SrUnsec/LTIR/SLTD/Sub/MTN/PS/CP	54,898	U	Ba1	Baa3	NP	P-3	SG	NETHERLANDS

Source: Moody's

Market Data

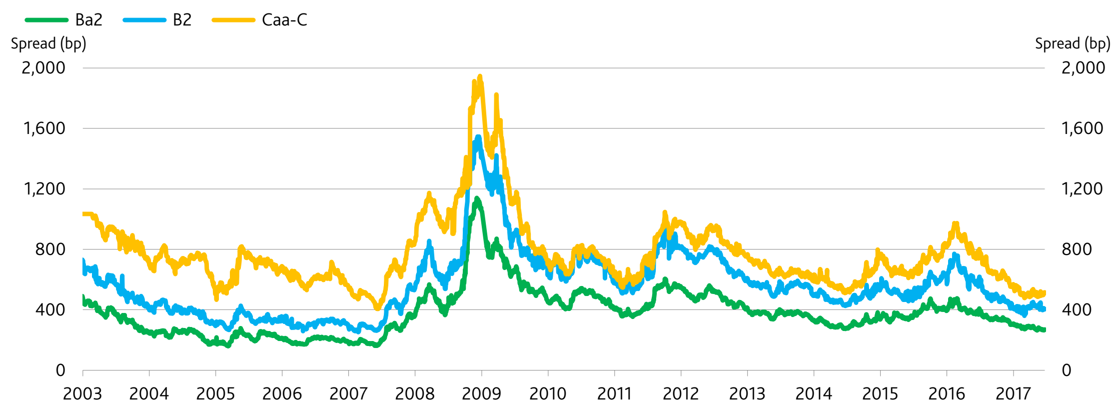
Spreads

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



Source: Moody's

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



Source: Moody's

CDS Movers

Figure 3. CDS Movers - US (June 14, 2017 – June 21, 2017)

CDS Implied Rating Rises	CDS Implied Ratings		
Issuer	Jun. 21	Jun. 14	Senior Ratings
PHH Corporation	B1	B3	B1
Verizon Communications Inc.	Baa2	Baa3	Baa1
Johnson & Johnson	Aa1	Aa2	Aaa
Pfizer Inc.	Aa3	A1	A1
Berkshire Hathaway Inc.	A3	Baa1	Aa2
National Rural Utilities Coop. Finance Corp.	Aa3	A1	A2
Thomson Reuters Corporation	Baa2	Baa3	Baa2
Newell Brands	A2	A3	Baa3
Ball Corporation	Baa3	Ba1	Ba1
NiSource Finance Corporation	A3	Baa1	Baa2

CDS Implied Rating Declines	CDS Implied Ratings		
Issuer	Jun. 21	Jun. 14	Senior Ratings
CA, Inc.	Ba3	Baa2	Baa2
Kroger Co. (The)	Ba1	Baa2	Baa1
Anadarko Petroleum Corporation	B2	Ba3	Ba1
Devon Energy Corporation	B1	Ba2	Ba1
Bank of America Corporation	Baa1	A3	Baa1
CVS Health	Baa1	A3	Baa1
Wal-Mart Stores, Inc.	A2	A1	Aa2
CenturyLink, Inc.	B3	B2	Ba3
Kinder Morgan Energy Partners, L.P.	Ba1	Baa3	Baa3
Kinder Morgan Inc.	Ba2	Ba1	Baa3

CDS Spread Increases		CDS Spreads		
Issuer	Senior Ratings	Jun. 21	Jun. 14	Spread Diff
SUPERVALU Inc.	B3	635	471	164
Chesapeake Energy Corporation	Caa2	849	688	161
Weatherford International, LLC (Delaware)	Caa1	573	422	151
CA, Inc.	Baa2	171	64	108
Nabors Industries Inc.	Ba3	479	372	107
Parker Drilling Company	Caa1	888	811	77
Hertz Corporation (The)	B3	1,117	1,051	66
Windstream Services, LLC	B2	831	768	64
McClatchy Company (The)	Caa2	846	781	64
Diamond Offshore Drilling, Inc.	Ba2	407	346	60

CDS Spread Decreases		CDS Spreads		
Issuer	Senior Ratings	Jun. 21	Jun. 14	Spread Diff
PHH Corporation	B1	186	331	-145
K. Hovnanian Enterprises, Inc.	Caa3	1,011	1,095	-84
Nine West Holdings, Inc.	Ca	5,406	5,451	-45
Sears Roebuck Acceptance Corp.	Caa3	3,365	3,402	-38
Sears Holdings Corp.	Caa3	3,350	3,387	-37
SLM Corporation	Ba2	303	325	-23
Springleaf Finance Corporation	B2	299	319	-20
Advanced Micro Devices, Inc.	Caa1	194	213	-19
HealthSouth Corporation	B1	291	307	-16
Calpine Corporation	B2	421	435	-14

Source: Moody's, CMA

Figure 4. CDS Movers - Europe (June 14, 2017 – June 21, 2017)

CDS Implied Rating Rises	CDS Implied Ratings		
Issuer	Jun. 21	Jun. 14	Senior Ratings
CNH Industrial N.V.	Baa3	Ba2	Ba2
Netherlands, Government of	Aa2	Aa3	Aaa
Dexia Credit Local	Ba2	Ba3	Baa3
HSBC Holdings plc	A3	Baa1	A1
Standard Chartered Bank	Baa1	Baa2	A1
Eurobank Ergasias S.A.	Caa3	Ca	Caa3
Royal Bank of Scotland N.V.	Baa1	Baa2	A3
AstraZeneca PLC	A1	A2	A3
Greece, Government of	Caa1	Caa2	Caa3
Piraeus Bank S.A.	Caa3	Ca	Caa3

CDS Implied Rating Declines	CDS Implied Ratings		
Issuer	Jun. 21	Jun. 14	Senior Ratings
Rabobank	A2	A1	Aa2
Austria, Government of	Aa3	Aa2	Aa1
Nordea Bank AB	A2	A1	Aa3
ING Bank N.V.	A2	A1	A1
ING Groep N.V.	A2	A1	Baa1
Danske Bank A/S	A2	A1	A2
Swedbank AB	A2	A1	Aa3
Total S.A.	A2	A1	A1
Statoil ASA	A1	Aa3	Aa3
Bank of Scotland plc	Baa1	A3	A1

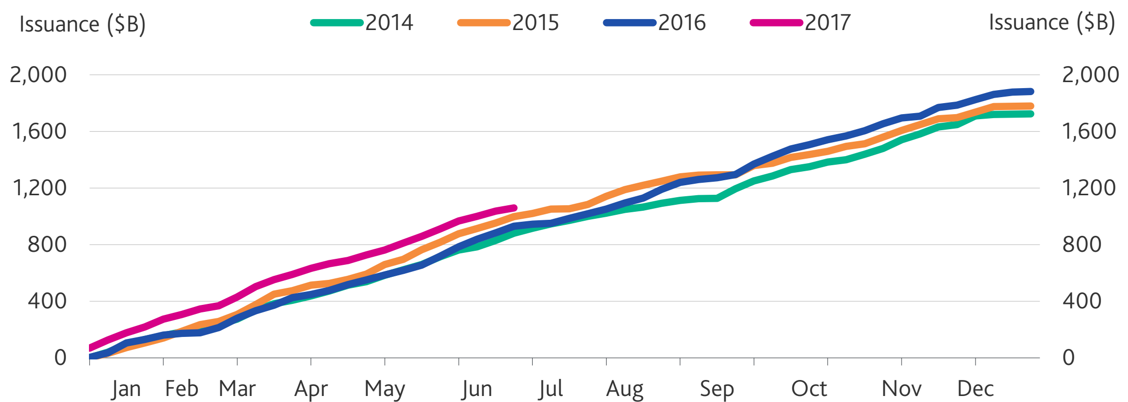
CDS Spread Increases		CDS Spreads		
Issuer	Senior Ratings	Jun. 21	Jun. 14	Spread Diff
Norske Skogindustrier ASA	C	27,300	21,097	6,203
Novo Banco, S.A.	Caa2	1,194	1,101	93
PizzaExpress Financing 1 plc	Caa1	687	628	59
Astaldi S.p.A.	B3	914	859	55
Galapagos Holding S.A.	Caa2	785	739	46
Banca Monte dei Paschi di Siena S.p.A.	B3	312	269	44
Stena AB	B3	671	630	41
Ensco plc	B2	558	518	40
Eksportfinans ASA	Baa3	519	481	39
Evraz Group S.A.	B1	331	294	37

CDS Spread Decreases		CDS Spreads		
Issuer	Senior Ratings	Jun. 21	Jun. 14	Spread Diff
CNH Industrial N.V.	Ba2	79	127	-48
CMA CGM S.A.	B3	499	544	-45
Greece, Government of	Caa3	552	584	-32
Eurobank Ergasias S.A.	Caa3	893	923	-30
Piraeus Bank S.A.	Caa3	893	923	-30
Alpha Bank AE	Ca	650	672	-22
Jaguar Land Rover Automotive Plc	Ba1	127	146	-19
NIBC Bank N.V.	Baa1	170	185	-15
Novafives S.A.S.	B3	314	327	-13
Fiat Chrysler Automobiles N.V.	B1	269	280	-11

Source: Moody's, CMA

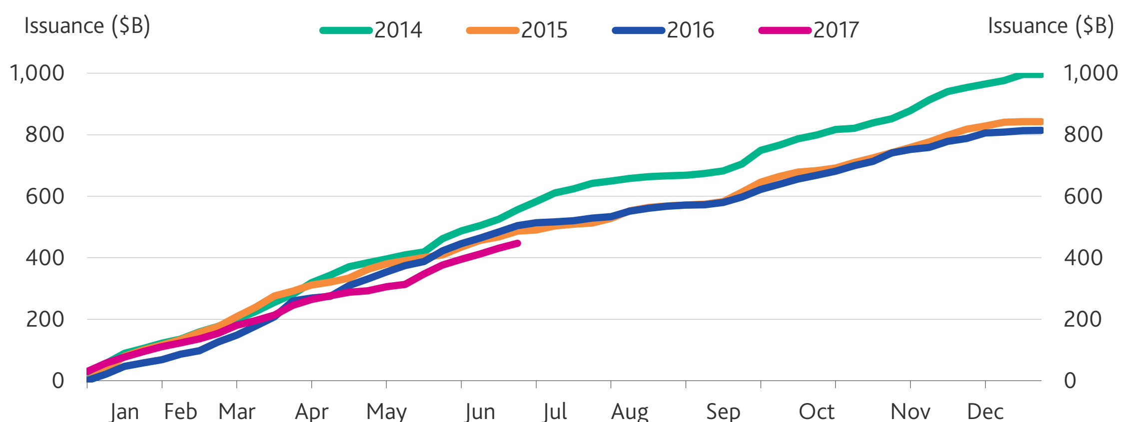
Issuance

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

Figure 7. Issuance: Corporate & Financial Institutions

	USD Denominated		
	Investment-Grade	High-Yield	Total*
	Amount $B	Amount $B	Amount $B
Weekly	14.601	7.290	23.794
Year-to-Date	765.576	218.264	1,059.863

	Euro Denominated		
	Investment-Grade	High-Yield	Total*
	Amount $B	Amount $B	Amount $B
Weekly	10.061	3.636	15.590
Year-to-Date	374.312	49.779	446.639

* Difference represents issuance with pending ratings.

Source: Moody's/ Dealogic

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