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WEEKLY MARKET OUTLOOK

Low Interest Rates Offset Fiscal Gridlock

Moody's Capital Markets Research

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Credit Markets Review and Outlook *by John Lonski*

Low Interest Rates Offset Fiscal Gridlock.

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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, "The outstandings of high-yield bonds from US companies contracted year-over-year by -3.9% in Q1-2017 and -5.0% in Q2-2017," begin on page 15.

Credit Spreads	Investment Grade: Year-end 2017 spread to exceed its recent 111 bp. High Yield: After recent spread of 372 bp, it may approximate 420 bp by year-end 2017.
Defaults	US HY default rate: Compared to June 2017's 3.8%, Moody's Credit Policy Group forecasts the US trailing 12-month high-yield default rate will average 2.9% during 2018's second quarter.
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 20.0% to $409 billion, which lags 2014's $435 billion record high.

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Ratings Round-Up *by Njundu Sanneh*

US Downgrades Mount Up.

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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: Sov risk, Qatar, equities, debt-to-GDP, energy, bond yields, Philippines, thin spreads, Qatar, toxic tightening, Paris, sales and profits, aging upturn, retail, Korea, lower yields, less risk, doubt VIX, Venezuela.

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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.

Low Interest Rates Offset Fiscal Gridlock

A fundamentally excessive climb by Treasury bond yields is one of the bigger risk factors facing corporate credit. Now that gridlock may persist indefinitely in Washington, the absence of fiscal stimulus requires a continuation of low interest rates.

The demise of healthcare legislation reduces the likelihood of tax reform or increased infrastructure spending becoming law well into 2018, if ever. Nevertheless, the market value of US common stock recently set a new record high, having advanced by more than 10% since year-end 2016.

Low interest rates compensate for lack of fiscal stimulus

Monetary accommodation can substitute for the lack of fiscal stimulus. Markets will not sell-off in response to unfulfilled expectations of fiscal stimulus if interest rates are low enough to assure a pace of expenditures that is capable of growing profits. Remember, during the week prior to Election Day — when Hilary Clinton was heavily favored to capture the Presidency and by doing so preserve gridlock in Washington — the 10-year Treasury yield averaged 1.82%. The 10-year Treasury yield's month-long average subsequently peaked at December 2016's 2.49% in anticipation of a dose of fiscal stimulus that was supposed to stoke both business activity and price inflation.

In response to fading prospects for any fiscal stimulus into the foreseeable future, the 10-year Treasury yield has since receded to 2.24%. In the event, business activity slows and inflation expectations do not rise, the benchmark Treasury yield will move lower.

Diminished worry over a possibly disruptive climb by fed funds and Treasury bond yields has helped to narrow corporate bond yield spreads. For example, the long-term Baa industrial company bond yield spread has narrowed from year-end 2016's 168 bp to a recent 151 bp, while the composite high-yield bond spread has thinned from 424 bp to July 18's 372 bp. In addition, the VIX index would not have dropped from an already exceptionally low December 2016 average of 12.5 points to a recent 10.0 points if equity investors feared an ascent by interest rates that would risk both a slowing by business sales and heightened competition from higher interest rates.

As inferred from market sentiment, any forthcoming rise by interest rates will not be great enough to detract significantly from the relative attractiveness of earnings-sensitive securities. But, if higher interest rates were to prove to too burdensome, worsened business prospects will drive both share prices and Treasury bond yields lower. According to this scenario, Treasury yields will not bottom until share prices recover.

Slide by Treasury yields lowers default risk

In addition to diminished worry over a damaging ascent by interest rates, a benign default outlook and ample liquidity now underpin the constructive outlook for high-yield credit. When the 10-year Treasury yield last peaked at July 7's 2.39%, the average EDF (expected default frequency) metric and the high-yield bond spread formed localized tops at 4.04% and 389 bp, respectively. A subsequent slide by the 10-year Treasury yield to 2.25% prompted a dip by the high yield EDF to 3.87% and a narrowing by the high-yield spread to 372 bp.

Nevertheless, the easing of interest rate worries has been the offshoot of lower than expected retail sales and slower than anticipated consumer price inflation, where high-yield credit quality is likely to soften if sales and prices weaken much further. However, for now, household spending's pace should be sufficient for the purpose of preventing a contraction by profits that otherwise might materially lift default risk. Of special importance is how the latest slide by Treasury bond yields has steadied the outlook for home sales that now lend critical support to US business activity.

The US high-yield default rate has dropped from January 2017's seven-year high of 5.9% to the 3.8% of June. Moody's default research team expects the default rate to further ease to 3.3% for Q4-2017 and then to 3.0% for Q1-2018. However, the latter would still exceed the default rate's 1.85% average of January 2014 through June 2015.

Credit Markets Review and Outlook

In anticipation of a lower default rate, the high-yield bond spread averaged 379 during the 12-months-ended September 2014. The 372 bp high-yield spread of July 19, 2017 implies the market expects the default rate to average 2.5% by the spring of 2018.

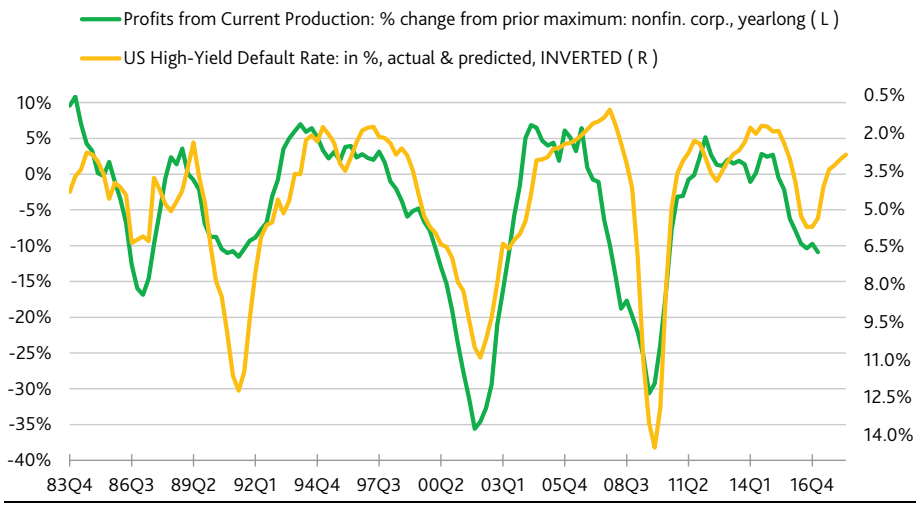
Profits growth suppresses defaults

As long as pretax profits from current production grow, a disruptive ascent by the default rate is likely to be avoided. As of early July, the Blue Chip consensus predicted sufficient annual increases by pretax profits from current production of 3.6% for 2017 and 4.1% for 2018.

The latest climb by the default rate from the January 2014 through June 2015 average of 1.85% to the January 2017 high of 5.9% was closely linked to the -16.1% slump by nonfinancial-corporate pretax operating profits from Q3-2014's record high to Q4-2015's latest bottom. Most of the damage stemmed from the petroleum & coal products industry, where Q3-2014's $53 billion of annualized profits eventually gave way to Q4-2015's -$79 billion of losses. But, even after excluding petroleum and coal, the rest of nonfinancial-corporate profits still fell by a cumulative -7.6% from Q3-2014 to Q4-2015.

From a macro perspective, corporate credit is binary. Since 1982, material contractions by pretax profits from current production have always been accompanied by above-average bond yield spreads and a rising default rate. More specifically, there have been five incidents since 1982 where the moving yearlong average of nonfinancial-corporate profits from current production sank at least -5% under its record high. In each of the five incidents, the default rate's quarter-long average climbed above 5%. (Figure 1.)

Figure 1: Each Deeper Than -5% Drop by Profits from Prior Cycle High Was Joined by a Greater Than 5% High-Yield Default Rate (inverted)



Though recessions have always been accompanied by wide spreads and rising default rates, an economic recovery offers no guarantee that a significant climb by the default rate and an attendant swelling of spreads will be avoided. Each of the substantial contractions by profits of 1986, 1998-2000, and 2016 occurred in the context of an economic recovery and each came with a rising default rate and a notable broadening of spreads.

The case of 1998-2000 is of special interest. Despite how the profits of the year-ended March 2000 were a deep -10.4% under their earlier apex and notwithstanding a climb by the average default rate from Q1-1999's 3.5% to Q1-2000's 6.0%, a record-smashing overvaluation of US equities continued unabated.

Looking ahead, the realization of modest profits growth should at least contain the default rate and, thereby, prevent a major reversal of an overvalued high-yield bond market. By itself, overvaluation does not imply impending doom. Instead, overvaluation warns of a more severe correction than otherwise once the market senses that unexpectedly low corporate earnings imperil debt repayment and dividends.

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, July 21: The Federal Reserve will be the focus for the upcoming week. We expect the Federal Open Market Committee to use its July post-meeting statement to guide financial markets' expectations for the beginning of the balance sheet normalization at the September meeting. This will be done via a tweak to the forward guidance about the start of normalization. The statement could change the words "this year" to "relatively soon," consistent with language used by a number of core members of the FOMC. This would strongly signal action could occur in September but would not amount to a pre-commitment to act at the next meeting. The Fed has stressed that monetary policy isn't on a preset course, and with the federal budget and debt-ceiling battles likely to heat up ahead of the September meeting, the central bank should give itself an out.

Despite some speculation that the Fed could make the announcement on its balance sheet at next week's meeting, we put the odds of that at only 25%. Some Fed officials have said that the decision on the balance sheet was more sensitive to growth and labor markets than to inflation. This is a little surprising. We would have thought that financial market conditions would factor more in the decision on the balance sheet. Still, July is unlikely. The signaling channel can be powerful, therefore the Fed will likely not want to surprise markets or potentially risk causing a quick adjustment in long-term interest rates.

Elsewhere in the statement, the changes to the Fed's assessment of the economy's performance shouldn't be too surprising. Its description of the labor market will be more upbeat than in the June meeting, but the key is inflation. The Fed will continue to acknowledge that inflation continues to run below its 2% target, but policymakers probably will add the caveat that the recent deceleration is likely transitory.

The Fed has been right in the past about transitory factors but could double down in the statement by naming the factors, including lower energy prices, increased generic drug competition, changes in cell phone plans, and weakness in physician services prices. Explicitly mentioning some of the transitory factors would likely signal unrattled confidence that inflation will move back toward the Fed's objective.

The Fed will continue to describe the risks to the outlook as roughly balanced. We don't anticipate any dissents.

As for the economic data, second quarter GDP growth likely rose 3% at an annual rate. We will revisit our forecast after durable goods, new- and existing-home sales along with the advance goods deficit. In durable goods, we look for a solid increase in June but nondefense aircraft will provide a big boost. We look for both new- and existing-home sales to have slipped in June.

THURSDAY, JULY 20

Jobless claims (week ending July 15; 8:30 a.m. EDT)

Forecast: 254,000
Initial claims are expected to have risen by 7,000 to 254,000 in the week ended July 15. The trend in initial claims has weakened recently as the four-week moving average is among the highest in a few months. However, new filings are notoriously volatile this time of year because of seasonal adjustment issues surrounding the Fourth of July holiday and the timing of the annual retooling for auto manufacturers. Auto production schedules point toward a sizable decline in production in July, but anecdotes are that layoffs won't be overly severe. Still, there is more uncertainty than usual in the forecast for initial claims.

Philadelphia Fed manufacturing survey (July; 8:30 a.m. EDT)

Forecast: 24.6
The Philadelphia Fed manufacturing survey's general business conditions index is forecast to have fallen from 27.6 in June to 24.6 in July. The details of the June survey point toward weakening in July. The gap between new orders and inventories—a proxy for future production—narrowed from 24 to 20.1 in June. The inventory build appears to have been light in the second quarter, which sets up favorably for both GDP growth and manufacturing production this quarter. July can be a difficult month for auto manufacturing because of the annual plant retooling, but we don't believe this should have a big impact on the Philadelphia Fed survey.

FRIDAY, JULY 21

No major economic releases scheduled.

MONDAY, JULY 24

Business confidence (week ending July 21; 10:00 a.m. EDT)

Forecast: N/A
The four-week moving average in our global business confidence survey fell from 33.2 to 30.5 in the week ended July 14. The dip in business confidence may very well be an outlier, particularly as it occurred at the same time that the stock market hovered around record highs. It also comes after an extended period of remarkably stable sentiment readings; confidence has been unshakable since before last year's U.S. presidential election. The drop is noteworthy nonetheless.

Although business confidence is good (despite last week's dip), it remains well off of its record highs achieved in spring 2015. Moreover, our survey results are not as strong as various other surveys of business and consumer confidence, which 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.

Existing-home sales (June; 10:00 a.m. EDT)

Forecast: 5.58 million annualized units
We look for existing-home sales to have fallen 0.7% in June to 5.58 million annualized units. The housing data have generally softened recently, and we believe existing-home sales will paint a similar picture. For example, pending home sales, which lead existing sales by one to two months, fell 0.8% in May, the third consecutive monthly decline and the fourth in the past five months. Assuming no revisions to prior months, existing-home sales will have averaged 5.59 million annualized units in the second quarter, compared with 5.62 million in the first quarter.

Keep a close eye on inventories. The lack of inventory remains problematic and is cutting into sales, boosting prices and hurting affordability.

TUESDAY, JULY 25

Conference Board consumer confidence (July; 10:00 a.m. EDT)

Forecast: 118
The Conference Board's consumer confidence index is forecast to have fallen from 118.9 in June to 118 in July. Fundamentals remain supportive for sentiment in July, including the labor market, low gasoline prices, and increases in equity prices. High-frequency measures of sentiment, including the Bloomberg consumer comfort index, slipped in the first half of July. We are penciling in a modest decline as some of the post-U.S. presidential election bounce fades.

WEDNESDAY, JULY 26

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

Forecast: 593,000 annualized units (starts)
New-home sales rose 2.9% to 610,000 annualized units in May and revisions to April were favorable.

New-home sales in April are now shown to have been 593,000 annualized units, compared with the 569,000 previously reported. The revisions are a reminder that new-home sales are unreliable from month to month. However, we look for new-home sales to have dipped in June, falling to 593,000 annualized units. We continue to look for sales to trend higher over time.

THURSDAY, JULY 27

Jobless claims (week ending July 22; 8:30 a.m. EDT)

Forecast: 238,000

Initial claims for unemployment insurance benefits are forecast to have risen by 5,000 to 238,000 in the week ending July 22. This would reverse little of the 17,000 cumulative decline in the prior two weeks. Initial claims can be volatile this time of year because of seasonal adjustment issues surrounding the Fourth of July holiday and annual auto plant shutdowns for retooling. This normally occurs in early July, and claims are following a pattern similar to 2015.

Durable goods orders (June; 8:30 a.m. EDT)

Forecast: 3.8% (total)

Forecast: 0.2% (excluding transportation)

Durable goods orders lost 1.1% in May, the largest drop since November, and orders for April were revised downward. Total orders are 5.1% higher than a year earlier. The bulk of the monthly decline stemmed from weaker nondefense aircraft orders, but there was weakness elsewhere. Core capital goods orders lost 0.2%. Orders for April in this segment were revised upward from 0.1% to 0.2%, however.

Total durable goods orders likely bounced back in June, rising 3.8%. We expect nondefense aircraft will provide a big boost, consistent with Boeing orders. Excluding transportation, orders likely increased only 0.2% in June.

FRIDAY, JULY 28

GDP (2017Q2-advance; 8:30 a.m. EDT)

Forecast: 3% at an annual rate; Confidence (3), Risks ☐

Our high-frequency GDP model estimates real GDP growth of 3% at an annual rate in the second quarter, compared with the 1.4% gain in the first three months of the year. We view the risks to our forecast as weighted to the downside.

Real consumer spending likely rose 2.9% at an annual rate in the second quarter and gains should be broad-based. The investment details will be mixed. Real residential investment is expected to have fallen 3.2% at an annual rate in the second quarter following a 12.9% gain in the first three months of the year. Nonresidential investment is expected to rise 6.7% at an annual rate in the second quarter, weaker than the 10.4% gain in the first quarter. Equipment spending will eke out a small gain in the second quarter. Inventories will be a small drag on GDP while net exports will provide a modest boost.

The high-frequency GDP model has been doing a reasonably good job in predicting the advance estimate of GDP, with an average absolute error of 0.5 percentage point since the second half of 2014. However, our confidence is lower for the second estimate because these data will incorporate the annual benchmark revisions.

Data from the first quarter of 2014 to the first quarter of 2017 will be subject to revision. The revisions will be primarily because of the incorporation of updated source data rather than methodological changes. Based on the new source data, revisions to GDP should be small, but the composition of growth could shift a little. Revisions to GDP growth in the first quarter can throw off our second quarter estimate, particularly for inventories and net exports.

There are some small methodological changes. The BEA will improve its allocation of industry-based retail sales to consumer goods consumption and alter the deflator used to estimate fixed investment in pre-packaged software. The issue of residual seasonality won't be addressed until the benchmark revisions in 2018.

Employment cost index (2017Q2; 8:30 a.m. EDT)

Forecast: 0.7%

The employment cost index is forecast to have risen 0.7% (not annualized) in the second quarter following a 0.8% gain in the first three months of the year. Though measures of labor costs have been sending some mixed messages, they are generally moving higher. This isn't too surprising, as the labor market has tightened. Our forecast would leave the ECI up 2.5% on a year-ago basis, compared with the 2.4% gain in the first quarter and better than the 2.3% in the second quarter of 2016. Overall, we expect the second quarter ECI to keep alive the debate about whether the economy is at full employment as wage growth should be even stronger.

University of Michigan Survey (July-final; 10:00 a.m. EDT)

Forecast: 93.1

The University of Michigan's consumer confidence index is expected to come in at 93.1 in July, according to the final survey. This would be on par with the preliminary survey but below June's 95.1. Stock prices are a positive for the Michigan survey, but gasoline prices were likely neutral in the second half of the month. The key will be inflation expectations. In the preliminary survey, both short- and long-run inflation expectations inched higher but remained depressed.

EUROPE

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

Summary, July 21: Next week will bring the preliminary estimate of second quarter GDP figures for the U.K. and France. We are rather downbeat about Britain's economic momentum, and we expect growth there to only have matched the first quarter's meagre 0.2% pace. Manufacturing production is set to have failed to offset the consumer-led slowdown in the services sector, notably as foreign demand disappointed despite the pound's sharp depreciation; industrial production decreased by 0.1% q/q in May following a mere 0.2% rise in April, putting factory growth down by a sharp 1.8% since the start of the year. Manufacturing was primarily behind this disappointment, as output in the industry fell by 0.2% m/m, fully offsetting a diametrically opposed gain in April. Prospects for June are not much brighter, and industrial production should have fallen by around 0.4% q/q at the second quarter. Construction should also have disappointed, as construction output fell sharply in April and May, putting the sector on track to shave around 0.09 percentage point off growth in the three months to June.

What's more, U.K. consumption likely remained extremely weak despite the recent pickup in retail sales, also depressing production in consumer-faced services firms. Car sales have plunged sharply in April and May, and leading surveys such as Visa's consumer spending index and the BoE's Agents' Summary of Business Conditions pointing to falling turnover in services firms. This means that household consumption should have slowed even further from its 0.4% q/q increase in the first quarter, likely to only 0.2%. That's why we still think that GDP will grow by only 0.2% q/q in the second quarter, as all sectors appear to have lost considerable momentum.

In France, the story is much rosier, and we expect investment to have rebounded from a subdued first quarter. Industrial output is expected to have increased by around 1% q/q in the three months to June assuming that production at the end of quarter mean-reverted slightly from May's 1.9% m/m jump. All sectors should have performed strongly, though a boom in transport equipment and food production likely powered the rebound. This is consistent with the recent stellar survey data, and with the jump in INSEE's new orders-to-inventories ratio, which is one of the most accurate leading indicators for industrial production in the country. Similarly, construction is also expected to have rebounded despite the fact construction output contracted slightly in May, as the decline was not enough to fully offset April's 3.5% m/m jump. We expect a further rise in June on the back of the month's warmer-than-average temperatures, and this should put construction up by 1.5% q/q in the June quarter.

French consumer spending is also expected to rise following no growth in the first quarter, meaning that domestic demand will likely have contributed strongly to second quarter growth. Retail sales data for France have surprised on the upside in April and May, and so did consumption in services; we are also expecting good news for June. Further, net trade should have contributed, reversing partially the 0.6-percentage point drag it had on first quarter GDP, though inventories should also have mean-reverted from a strong first quarter boom and offset some of net trade's support. We are penciling that GDP will have increased by 0.5% q/q in the three months to June, matching the growth rate for the first quarter.

THURSDAY, JULY 20

U.K.: Retail Sales (June; 9:30 a.m. BST)

U.K. retail sales should have mean-reverted in June following the 1.1% slump in May. We expect them to increase by 0.4% m/m, pushing the yearly rate of growth in sales up to 2.6%, from 0.9% previously. Leading indicators released in recent weeks were relatively upbeat, suggesting a broad-based recovery in spending over the month mainly on the back of warmer-than-average weather. Data from the Confederation of Business Industry showed that the balance of reported sales increased to +12 in June from +2 in May, though it still remained below its +18 average for the past three years. Similarly, the BDO survey showed that sales in value on the high street rose by 1.3% y/y, while the British Retail Consortium's survey indicated that like-for-like retail sales values increased by 1.2% y/y in June, from a decrease of 0.4% in May, while total sales were up by 2%.

The details should reveal that both food and nonfood sales improved, notably sales of clothing. But June's improvement should only be a blip; retail sales are set to remain poor as higher inflation combined with limited wage growth erodes real wages and consumers' purchasing power throughout the year, curbing households' will to spend.

Euro Zone: Monetary Policy (July; 12:45 p.m. BST)

We expect that the ECB may drop its quantitative easing bias with regard to size next week, meaning that it won't increase the monthly purchases in the future. Meanwhile, the bank will likely leave open the option to extend asset purchases beyond 2017. Because core euro zone inflation might not accelerate in line with the ECB's forecasts, we believe the central bankers should proceed with caution. After changing its forward guidance in July, the ECB will likely announce its plans to taper asset purchases in September but continue its bond-buying program until at least June 2018. We don't expect the bank to start raising the deposit rate back into positive territory before the second quarter of 2018, when it terminates its purchases.

FRIDAY, JULY 21

Spain: Foreign Trade (May; 9:30 a.m. BST)

We expect Spain's trade deficit to improve to €0.9 billion on the back of a strong export performance and to a larger extent, slowing imports. The gap should narrow further by the end of the year as we do not foresee a rebound in imports any time soon, while competitiveness gains and robust external demand will propel exports. We caution, however, that the medium-term outlook is still clouded by concerns over protectionist trade policies which may emerge in the U.S., and the details of the trade agreement with the U.K. Trade barriers could slow the expansion of exports and cement the trade deficit over the medium term.

MONDAY, JULY 24

No major indicators are scheduled for release.

TUESDAY, JULY 25

France: Job Seekers (June; 7:00 a.m. BST)

France's job market is making progress despite a few speed bumps, and we expect the number of job seekers fell to 3.47 million in June after a poor showing in May. 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. Large year-over-year declines in youth unemployment are also encouraging. 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 labour market reforms, such as a revamp of hiring and firing legislation.

WEDNESDAY, JULY 26

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

We expect retail sales accelerated to 3% y/y in June, completing the second quarter at 2.5%. This still lags behind the retail performance of last year, which sat at 3.6% y/y on average, but marks a recuperation from the disappointing first quarter at 0.7% y/y. We project retail sales to accelerate somewhat, but to advance more slowly than what Spain's economic growth would dictate, since consumers' will to spend is still constrained by sluggish pay gains. Nevertheless, the 3-percentage point improvement in retail trade compared with the first quarter gives us reason to believe that the short- and medium-term prospects are solid.

U.K.: GDP Production Breakdown (Q2; 9:30 a.m. BST)

We expect U.K. GDP to have increased by only 0.2% q/q in the second quarter, matching the first quarter's meagre results. In yearly terms, GDP should have grown 1.7%, slowing from a 2% increase in the first quarter. The service sector likely powered the expansion again, but we expect it contributed far less than in the previous quarter, mainly because of a further slowdown in output growth of consumer-faced services firms. Car sales plunged sharply in April and May, and leading surveys such as Visa's consumer spending index and the BoE's Agents' Summary of Business Conditions are all pointing to falling turnover in services firms.

Industrial production and construction, by contrast, should have been a drag, shaving together 1.5 percentage points off second quarter growth. Industrial production decreased by 0.1% q/q in May following a mere 0.2% rise in April, putting factory growth down by a sharp 1.8% since the start of the year. The primary cause of this disappointment was manufacturing, where output fell by 0.2% m/m in May, fully offsetting April's gain. Prospects for June are not much brighter, and industrial production should have fallen by around 0.4% q/q in the second quarter. Construction should also have disappointed, as output fell sharply in April and May, putting the sector on track to shave around 0.09 percentage point off growth in the three months to June.

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

The German Ifo Business Climate Index likely retreated slightly to 114.8 at the start of the third quarter after hitting a record high of 115.1 in June. The sharp appreciation of the euro during July has likely weighed on business confidence somewhat. The euro appreciated to $1.162, which is the highest since early 2015. The strengthening currency will likely weigh on German exports outside of the euro area. But despite the downtick, confidence in the German economy remains high thanks to the strong performance in the second quarter. The Markit manufacturing PMI jumped to a 74-month high of 59.6 in June, though the overall composite PMI retreated somewhat because of a slowdown in the service sector. Even so, the average reading for the second quarter was the highest in six years, reaching 56.8, pointing to economic growth of 2% y/y.

THURSDAY, JULY 27

Spain: Unemployment (Q2; 8:30 a.m. BST)

We expect the unemployment rate was at 18.4% in the second quarter, slightly down from 18.8% in the first quarter because of a strong tourist season and robust performance of the export sector. Spain entered the fourth year of stellar economic growth, and this expansion has caused the labour market to tighten. While the outlook is still upbeat, we see that the labour-intense phase of the recovery might be nearing its end as the growth becomes more broad-based. The falling unemployment rate will therefore likely moderate from next year. We caution that the bulk of the unemployed are without a job for the long term, implying that their re-employment requires active labour programmes. We believe that structural unemployment will stay higher for longer, meaning that the medium-term unemployment rate will linger around 15% to 16%. Nevertheless, there are encouraging signs of renewed interest in expatriate workers in the country, which will likely prop up the employment statistics.

Russia: House Prices (Q2; 10:00 p.m. BST)

Russian house prices will begin rising in 2017. Prices dropped precipitously when oil prices plummeted and sanctions over Ukraine took the wind out of the economy. The broader economy is improving, with two consecutive quarters of GDP growth. Both retail sales and household consumption are rebounding, indicating that consumers are beginning to spend again. The Central Bank of Russia has also dropped interest rates three times this year, which should spur increased borrowing. With balance sheets improving, incomes rising, and rates falling, homebuyers should increase demand for housing, allowing prices to rise. We expect house prices to increase a modest 0.3% in the second quarter.

FRIDAY, JULY 28

France: GDP (Q2; 6:30 a.m. BST)

The French economy likely grew 0.5% q/q in the three months to March, matching the rate for the previous quarter. We expect investment to have rebounded from a subdued first quarter. Industrial output is expected to have increased by around 1% q/q in the three months to June assuming that production at the end of quarter mean-reverted slightly from May's 1.9% m/m jump, while construction is also expected to have increased despite the fact construction output contracted slightly in May, as the decline was not enough to fully offset April's 3.5% m/m jump. We expect a further rise in June on the back of the month's warmer-than-average temperatures, and this should put construction up by 1.5% q/q in the June quarter.

Consumer spending is also expected to rise following no growth in the first quarter, meaning that domestic demand will likely have contributed strongly to second quarter growth. Retail sales data for France have surprised on the upside in April and May, and so did consumption in services; we are expecting similarly good news for June. What's more, net trade should also have contributed, reversing partially from the 0.6-percentage point drag it represented to first quarter GDP, though inventories should also have mean-reverted from a strong boom in the first quarter and offset some of net trade's support.

ASIA-PACIFIC

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

Japan's inflation is going nowhere quickly

It's likely to be the same old story for Japan's June data dump. Core CPI was likely unchanged at 0.4% y/y in June. Underlying inflation has improved in 2017 but remains below the central bank's 2% target. Higher oil prices and a lower currency have boosted inflation this year. But price pressures from the

domestic economy remain elusive. Workers' nominal household expenditure likely rose again in annual terms. But the increase stems mostly from base effects rather than improved underlying momentum in spending habits. And as prices begin to rise, real income could fall further.

Japan's unemployment rate likely fell in June after a surprise increase to 3.1% in May. The jobs-to-application ratio remains elevated, which suggests that labour demand is outstripping labour supply. This trend will likely persist for the remainder of 2017 as the economy expands, but the population is shrinking because of aging.

Asia's bellwethers, South Korea and Taiwan, are due to release preliminary June quarter GDP data. South Korean GDP growth likely cooled as exports didn't maintain their burly first quarter pace. Consumption likely improved a little towards the end of the quarter thanks to soaring sentiment in anticipation of newly elected President Moon Jae-in's generous spending program.

Taiwan's GDP growth also softened. Renewed weakness in domestic demand helped cool headline growth as private consumption remains the economy's laggard. The sustained upswing in the global tech cycle is keeping Taiwan's exports and manufacturing upbeat. Forward indicators suggest demand will remain buoyant at least through the third quarter, good news for Taiwan's economy because of its large exposure to the global electronics trade.

THURSDAY, JULY 20

Japan – Foreign Trade – June

Time: 9:50 a.m. AEST (Wednesday, 11:50 p.m. GMT)
Forecast: ¥200 billion
Japan's monthly trade surplus likely increased from ¥134 billion in May. We look for a ¥200 billion surplus for June, as exports are expected to rise but the increase in imports will likely slow. Commodity prices, albeit higher than the previous year, have fallen in recent months and this will ease the import bill. Export growth remains strong thanks to improved global demand and the yen's depreciation earlier this year, which is boosting export values and Japan's overall external competitiveness.

Australia – Employment Situation – June

Time: 11:30 a.m. AEST (1:30 a.m. GMT)
Forecast: 5.7% Unemployed
Australia's June unemployment rate will be steady at 5.7%. Labour market conditions appear to have picked up in recent months. Job growth has accelerated and a larger share of the new jobs have been full time. If this trend continues it bodes well for lowering the underemployment rate. Underemployment, which is at a record high, is a persistent issue for the Australian economy, dragging on wage growth and consumer spending.

Indonesia – Monetary Policy – July

Time: Unknown
Forecast: 4.75%
Bank Indonesia will keep the policy rate on hold at 4.75% at its July policy meeting. The central bank is comfortable on the sidelines, as inflation is expected to remain within the 3%-to-5% target range. Moreover, policymakers have delayed a third planned administrative price hike until after Ramadan festivities to ensure inflation stays well anchored. We expect the policy rate to remain on hold through 2017, before gradual normalization begins around mid-2018.

Japan – Monetary Policy – July

Time: Unknown
Forecast: ¥80 trillion
The Bank of Japan is set to keep its policy levers unchanged at the July monetary policy meeting. Yield curve control will target the 10-year government bond yield at 0%, while a negative interest rate of 0.1% will continue for excess reserves. Moreover, we expect the BoJ to maintain its asset purchases at a

target rate of ¥80 trillion per month even though the central bank slowed its pace of asset purchases in the last few months. Inflation remains below the central bank's 2% target, but the BoJ is out of policy options to spur growth. Overall, the central bank is unlikely to change its levers in 2017, with an official slowdown in asset purchases likely in 2018.

FRIDAY, JULY 21

No major economic indicators are scheduled for release.

MONDAY, JULY 24

Taiwan – Domestic Trade – June

Time: 6:00 p.m. AEST (8:00 a.m. GMT)
Forecast: 1%
Taiwan's domestic trade is increasing at a modest pace. Robust employment conditions are helping matters, although households are refraining from big-ticket purchases such as motor vehicles and household goods. Improved manufacturing and export conditions are taking longer than usual to filter through to consumers; industrial production and domestic trade are historically tightly correlated. Domestic spending likely expanded 1% y/y in June, after a similar increase in May.

Taiwan – Industrial Production – June

Time: 6:00 p.m. AEST (8:00 a.m. GMT)
Forecast: 2%
Taiwan's industrial production likely accelerated further in June after a soft gain in May. Relatively subdued domestic demand is crimping energy and construction, but manufacturing is growing as firms make components for new products. Exports are rising, and this is likely to boost Taiwan's economy for the remainder of the year. Taiwan's industrial output likely rose 2% y/y in June after a 0.8% increase in May.

TUESDAY, JULY 25

South Korea – Consumer Sentiment Index – July

Time: 7:00 a.m. AEST (Monday, 9:00 p.m. GMT)
Forecast: 108
South Korean consumer sentiment likely cooled to 108 from its lofty heights in June. The index last month reached its highest level in more than five years at 111.1, from 108 in May. Households are feeling more upbeat thanks to newly elected President Moon Jae-in and his proposed generous welfare and employment spending. It is hoped that households will remain festive and loosen their purse strings a little, as consumption has been a laggard.

WEDNESDAY, JULY 26

New Zealand – Foreign Trade – June

Time: 8:45 a.m. AEST (Tuesday, 10:45 p.m. GMT)
Forecast: NZ$550 million
New Zealand's monthly trade surplus likely widened to NZ$550 million in June, from the NZ$103 million surplus in May. Higher world prices for milk powder are lifting exporter receipts. Dairy exports were up an impressive 35.4% y/y in May, unchanged from April's pace, and a similar gain is expected in June. Higher prices are the main contributor to the gain in dairy, as volumes are not as buoyant. Despite the slow start to the 2016-2017 season, dairy values for May 2017 were almost 10% ahead of those at the same time last year.

Australia – Consumer Price Index – 2017Q2

Time: 11:30 a.m. AEST (1:30 a.m. GMT)

Forecast: 0.5%
Australian headline consumer price inflation was likely flat at 0.5% q/q in the June quarter. Tradables inflation was likely a positive for price growth, as the Australian dollar depreciated in the three months to June. Offsetting this will be slower rises in healthcare and education costs, which jumped in the opening quarter of 2017 because of scheduled price rises. The Reserve Bank of Australia's preferred measure of inflation will remain below its 2% to 3% target band. Demand-side pressures on inflation remain weak because of the constraint that low wage growth is placing on consumption.

Singapore – Industrial Production – June
Time: 3:00 p.m. AEST (5:00 a.m. GMT)
Forecast: 5.4%
Singapore's industrial production growth likely nudged up to 5.4% y/y in June from 5% in May. The city-state's manufacturing has benefited from the uptick in global demand in the first half of 2017. June Purchasing Manufacturers' Index data suggest that this trend will persist; output expanded at a faster clip in the month, driven by higher new orders and new export orders. Electronics will be the main contributor to production growth, but biomedicals should also start to contribute positively as high base effects start to fade.

THURSDAY, JULY 27

South Korea – GDP – 2017Q2
Time: 9:00 a.m. AEST (Wednesday, 11:00 p.m. GMT)
Forecast: 0.6%
South Korean GDP growth likely cooled to 0.6% q/q in the June quarter, according to preliminary estimates, weaker than the previous 1.1% gain. Consumption likely improved a little towards the end of the quarter thanks to soaring sentiment in anticipation of the president's generous spending program. Consumption remains the laggard on account of high household debt and a struggling labour market. Exports didn't maintain their burly first quarter pace as a blip in tech demand and slower Chinese demand hurt shipments.

Hong Kong – Foreign Trade – June
Time: 6:30 p.m. AEST (8:30 a.m. GMT)
Forecast: -HKD45 billion
Trade activity through Hong Kong's port has slowed after a burst of activity in the first quarter, but it remains healthy. Imports and exports are growing as global demand for electronics expands and as the mainland's economy remains robust. The monthly deficit likely rose to HKD45 billion in June from HKD34.1 billion in May, in line with historical cycles.

FRIDAY, JULY 28

South Korea – Industrial Production – June
Time: 9:00 a.m. AEST (Thursday, 11:00 p.m. GMT)
Forecast: 1.3%
Korea's industrial production likely improved in June to 1.3% from the disappointing 0.1% y/y expansion in May. Tech manufacturing likely strengthened as other tech bellwethers in the region report stronger production and exports in anticipation of product launches later in the year. This should provide a broader lift to manufacturing in Korea.

South Korea – Retail Sales – June
Time: 9:00 a.m. AEST (Thursday, 11:00 p.m. GMT)
Forecast: 0.5%
Korea retail trade likely ticked up a notch to 0.5% in June after the 0.9% m/m fall in May. Consumer confidence has surged since Moon's election, suggesting households will open their wallets a little more freely through the September quarter in anticipation of reaping the benefits of anticipated higher

welfare and employment spending. High household debt, in part fuelled by the central bank's record low interest rates, will prevent a strong rebound in consumption.

Japan – Consumer Price Index – June

Time: 9:30 a.m. AEST (Thursday, 11:30 p.m. GMT)
Forecast: 0.4%
Japan's core CPI was likely unchanged at 0.4% y/y in June. Underlying inflation has improved in 2017 but remains below the central bank's 2% target. Higher oil prices and a lower currency have boosted inflation this year, but price pressures from the domestic economy remain elusive. Until wages increase meaningfully, inflation is unlikely to reach the Bank of Japan's 2% target.

Japan – Employment Situation – June

Time: 9:30 a.m. AEST (Thursday, 11:30 p.m. GMT)
Forecast: 3% Unemployed
Japan's unemployment rate likely fell to 3% in June after a surprise increase to 3.1% in May. The jobs-to-application ratio remains elevated, which suggests that labour demand is outstripping labour supply. This trend will likely persist for the remainder of 2017 as the economy is expanding, but the population is shrinking. The gap between the full-time and temporary workforce means that wage growth will likely remain elusive.

Japan – Household Expenditures Survey – June

Time: 9:30 a.m. AEST (Thursday, 11:30 p.m. GMT)
Forecast: 1.7%
Japan's nominal workers' household expenditure likely increased 1.7% in June after a 2.8% jump in May. The rise stems mostly from base effects rather than improved underlying momentum in spending habits. As prices begin to rise, real income could fall further. Without a sustained pickup in wages, households are unlikely to open their purse strings in the coming months.

Japan – Retail Sales – June

Time: 9:50 a.m. AEST (Thursday, 11:50 p.m. GMT)
Forecast: 1.6%
Retail spending likely decelerated to 1.6% in June after a 2% y/y rise in May. The uptick in retail fuel costs has been a primary driver of overall retail sales in the past few months. However, with energy prices ebbing in recent weeks, the cost of retail fuel will likely decrease. Although car sales rose strongly in May, overall spending on big-ticket items such as household appliances is falling.

Singapore – Employment – 2017Q2

Time: 12:30 p.m. AEST (2:30 a.m. GMT)
Forecast: 2.1% Unemployed
We look for Singapore's unemployment rate to have fallen to 2.1% in the June quarter after sitting at 2.3% in the three months to March. Preliminary GDP estimates show that Singapore's economy performed reasonably well in the second quarter, expanding 2.5% y/y. This was driven by improvements in all three major subsectors of the economy—manufacturing, construction and services. The strength of manufacturing and rebound in construction, in particular, should revive employment in these sectors.

Taiwan – GDP – 2017Q2

Time: 6:00 p.m. AEST (8:00 a.m. GMT)
Forecast: 2.4%
Taiwan likely grew 2.4% y/y in the June quarter, according to preliminary estimates, softer than the March quarter's 2.6% gain. Renewed softness in domestic demand helped cool headline growth; private consumption remains the economy's laggard. The sustained upswing in the global tech cycle is keeping Taiwan's exports and manufacturing upbeat. Forward-indicators suggest demand will remain buoyant at least through the third quarter, good news for Taiwan's economy given its large exposure to the global electronics trade.

The Long View

The US: The outstandings of high-yield bonds from US companies contracted year-over-year by -3.9% in Q1-2017 and -5.0% in Q2-2017

By John Lonski, Chief Economist, Moody's Capital Markets Research Group,
July 20, 2017

CREDIT SPREADS

As measured by Moody's long-term average corporate bond yield, the recent investment grade corporate bond yield spread of 111 bp is under 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 372 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 June's 3.8%. Moody's credit policy group expects a 3.0% 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

Yearlong 2016's 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

Second-quarter 2017's worldwide offerings of corporate bonds showed an annual percent decline of -6.7% for IG and an increase of +7.5% for high-yield, wherein US$-denominated offerings fell by -6.2% for IG and grew by +4.9% for high yield.

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 0.5% annually for IG and may advance by 21.8% 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
July 20, 2017

Eurozone

The euro zone's short-term outlook is brightening now that political risks have eased and Italy's government injected billions of euros to help heal ailing banks. Businesses have shaken off some of the uncertainty regarding the U.K.'s departure from the EU, while financial markets have seen investment inflow surge and volatility decline to a multiyear low. Despite moderating threats, it would be unwise to think that the euro zone economy can expand enough in the next years to narrow the gap with U.S. growth. Labour market slack, tepid wage growth, and tightening monetary conditions could still send the euro zone economy off the rails. The erratic behavior of U.S. President Trump may also harm trade between two economies and torpedo the export-driven rebound in the euro zone, particularly in Germany. A turn towards greater protectionism in the U.S. may worsen the euro zone's trade balance with the world's largest economy, though this is not yet visible from the latest figures.

The euro zone grew 0.6% q/q in the first quarter, and high-frequency indicators suggest this buoyant pace likely carried over through the second. Although the area's composite PMI slid to 56.3 in June from a six-year high of 56.8 in May, euro zone businesses enjoyed the best quarter for six years. This is consistent with growth picking up further in the second quarter, to around 0.7%. The impressive momentum stems mainly from a stellar manufacturing performance. The euro zone's manufacturing PMI climbed to a six-year high of 57.4 in June, from 57 in May, with soaring new orders helping push job growth to a 20-year high. The results bode well for the region's factory growth in the second and third quarters, and we see no signs that this remarkable performance will end in coming quarters.

A strengthening labour market may also be encouraging, but only at first sight. Although the euro zone unemployment rate stayed at 9.3% in April, the lowest rate since March 2009, a rising share of part-time jobs and an inactive population were largely behind these developments. If the discouraged population of those unable to find suitable work and underemployed part-time workers were added, the jobless rate would be higher. With a higher true unemployment rate tamping down wage growth, core inflation could continue to surprise on the downside, delaying normalization of the ECB's monetary policy. After no change in forward guidance in July, we expect the ECB will likely announce its

plans to taper asset purchases in September but continue its bond-buying program until at least June 2018. We don't expect the bank to start raising the deposit rate back into positive territory before the second quarter of 2018, when it terminates its purchases.

UK

After a mere 0.2% q/q growth in the first quarter, the U.K. economy's growth likely remained weak in the three months to June. High-frequency data for manufacturing shows the story in the U.K. was even more dire than expected. The country's PMI plunged to a three-month low of 54.3, from 56.3 in May, exceeding the consensus. The dismal reading challenges both markets and the Bank of England's views that the lower pound would have boosted British factory growth and exports by now. According to the survey, they couldn't have been more wrong; the export orders balance again declined over the month, to just 52.6 from 53.4 in May, continuing to read well below the total orders balance at 54.9. To that we add that domestic orders also sagged and that the slowdown was broad-based across the consumer, intermediate and goods sectors, which in turn has dampened growth in all categories of manufacturing firms. We repeatedly argued that the other sectors of Britain's economy could not take the lead, though. The uncertainty surrounding exit negotiations is sure to prevent investment from picking up strongly despite the weaker pound making U.K. assets more profitable for foreigners, while the fact that U.K. exporters raised prices sharply offset most of the competitiveness gains brought by the weaker currency. Leading and hard export data released since the start of the year have all disappointed, and that's despite the pickup in world trade, suggesting that sterling's latest depreciation has done practically nothing.

Rising inflation and worsening labor market will weigh on household spending. Labour market figures added to the gloom of the previous data barrage, as they showed that real wages plunged further into negative territory in the quarter to May. Including bonuses, real pay growth shed 0.7% q/q, as nominal wage growth slowed to only 1.8% from 2.1% previously, and inflation peaked at 2.9% in May. It's true that, excluding bonuses, the drop in real wages was less pronounced, but we caution that this was because of distortions caused by the financial sector; wages deteriorated in all other sectors of the economy. 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. The outlook for wages, meanwhile, is dire. All hiring surveys point to a deterioration in pay settlements, especially for first hires, while anecdotal evidence shows that firms are unwilling to raise wages until they know more about the future relationship between the U.K. and the EU.

This leaves the Bank of England in a delicate position; a rate hike seems now unjustifiable given the repeated letdowns and the broad-based economic weakness. 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 1.2% 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 Syed and the Asia-Pacific Staff of Moody's Analytics
July 20, 2017

The Week Ahead

India's consumer price inflation hit a record low of 1.5% y/y in May, which suggests that rate cuts are just around the corner in India. Food prices have caused the headline CPI to decelerate drastically; for perspective, India's inflation never reached this low even during the Great Recession. Meanwhile, the disinflation trend was broad-based, and wholesale prices also decelerated sharply, to 0.9% y/y in June.

Overall, consumer prices have fallen below the Reserve Bank of India's projections. The central bank expected that CPI would remain around 2% to 3.5% in the first half and 3.5% to 4.5% in the second half of fiscal 2017-2018 (April-March). Since inflation is running below these projection and the upcoming monsoon season looking good, we expect a 25-basis point rate cut in the August monetary policy meeting.

India's Southwest monsoon season, which runs between June to September, dictates agriculture output. A bad monsoon season will cause food prices to rise. Typically, rainfalls around 90% of the long-term average are considered normal. And since food inflation accounts for around half of the CPI basket, interest rate decisions are partially based on monsoon rains. And two poor seasons of below-average rainfalls in 2014 and 2015 were followed by good rainfalls in 2016.

The topsy-turvy nature of India's monsoon season helps explain the food price deflation this year. Generally, crop sowing occurs during the monsoon season so the impact of monsoon rains is felt after six to nine months. Prices of key food items—vegetables, pulses and cereals—were growing by double digits in the first half of 2016 because of poor rainfalls for two years prior. However, rainfall in the 2016 monsoon season was normal, and food prices have since declined sharply. So taking account of unusually high food prices in early 2016, a good monsoon season later in 2016 is causing food prices to decline on a year-ago basis.

The double-digit declines across major food categories should peter out in coming months. But prices could still be declining on a year-ago basis. This will largely depend on the current monsoon season; the Indian meteorological department is forecasting normal monsoon rains for this year. So far, the monsoon has been a mixed bag across India, but overall rainfalls have been around long-term normal levels.

Some downside risks remain. Below-average rainfall in central India is concerning because it's crucial for sowing of pulses, oilseeds and cotton crops. The states of Madhya Pradesh, Maharashtra and Gujrat are crucial to production of these kharif crops. That said, forecasts call for monsoon rains to intensify in these regions over the coming weeks, which will likely see overall rainfall return back to normal levels. Overall, assuming rainfalls are normal this year and food supply is relatively the same as last year, we expect food prices are unlikely to rise sharply in the second half of the year.

In the short term, the Reserve Bank of India's 4% inflation target is under threat from disinflation. If monsoon rains remain normal, and crop sowing is close to last year's level, then food inflation will likely decline. This is our baseline assumption; and the RBI will likely cut rates by 25 basis points in its August monetary policy meeting.

Downside risks to our forecast include less crop area sown, which could add to food inflation over the coming months. Overall, food inflation is a wild card, and without reforms to agriculture and subsidies, food prices will remain volatile and unpredictable.

Ratings Round-Up

By Njundu Sanneh

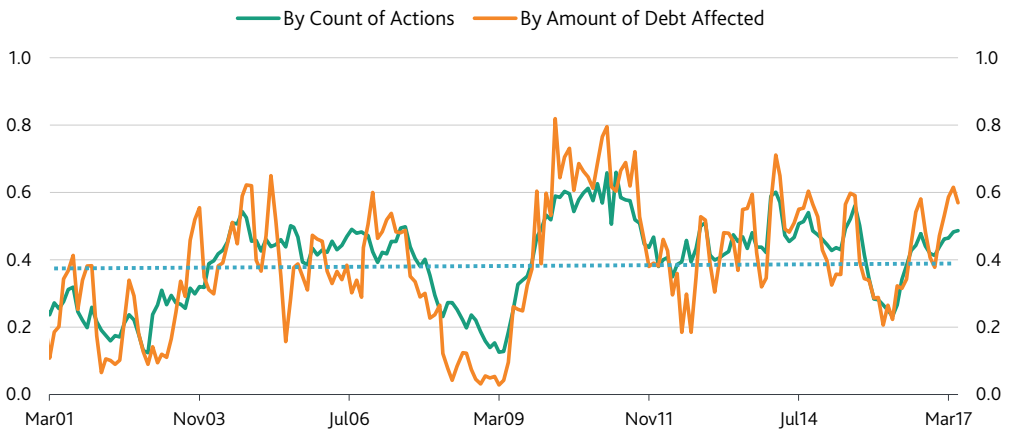
US Downgrades Mount Up

The retail sector continues to add downgrades with two more in the past week. Energy companies are close behind with the downgrade of coal mining company Armstrong Energy, Inc. midstream energy company Semgroup Corporation, and oil and gas project finance outfit HFOTCO LLC, a subsidiary of Buffalo Gulf Coast Terminals LLC. With downgrades in other sectors, such as apparel and forest products – pulp and paper, downgrades were on the ascendancy in the US over the past week, besting upgrades by a ratio of two to one. Upgrades only accounted for five of the fifteen total rating changes with a contribution rate of 31%, well below the 40% long-term average for the metric. Financial companies represent two of the six rating upgrades, with natural products processor American Seafoods Group LLC also adding to the positive rating changes.

European rating changes inched up to seven in the past week from three the week before. The upgrade column was populated by financials and all the industrial company ratings revisions were downgrades. Print media company Cimpress N.V. and paper and pulp firm Norske Skoginstrier ASA were among the downgraded.

FIGURE 1

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



* Trailing 3-month average

Source: Moody's

FIGURE 2

Rating Key

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

FIGURE 3 Rating Changes: Corporate & Financial Institutions – US

Date	Company	Sector	Rating	Amount ($ Million)	Up/ Down	Old LTD Rating	New LTD Rating	IG/SG
7/12/17	RAYMOND JAMES FINANCIAL, INC.	Financial	SrUnsec/LTIR	1,850	U	Baa2	Baa1	IG
7/13/17	AMERICAN SEAFOODS GROUP LLC	Industrial	LTCFR/PDR		U	B3	B2	SG
7/14/17	AMERICAN ROCK SALT COMPANY LLC	Industrial	LTCFR/PDR		D	B2	B3	SG
7/14/17	CHINOS INTERMEDIATE HOLDINGS A, INC.	Industrial	PDR		U	Caa3	Caa1	SG
7/14/17	CHINOS INTERMEDIATE HOLDINGS A, INC. - J.Crew Group, Inc.	Industrial	SrSec/BCF		D	Caa1	Caa2	SG
7/14/17	EXTRACTION OIL AND GAS, INC.	Industrial	SrUnsec/LTCFR/PDR	550	U	B3	B2	SG
7/17/17	BUFFALO GULF COAST TERMINALS LLC - HFOTCO LLC	Industrial	SrSecBCF		D	Ba2	Ba3	SG
7/17/17	EQUITY RESIDENTIAL	Financial	SrUnsec/Sub/PS	4,633	U	Baa1	A3	SG
7/17/17	OPAL ACQUISITION, INC.	Industrial	SrSec/BCF		D	B2	B3	SG
7/17/17	SEMGROUP CORPORATION	Industrial	SrUnsec/LTCFR/PDR	1,075	D	B2	B3	SG
7/17/17	TOMS SHOES, LLC	Industrial	SrSec/BCF/LTCFR/PDR		D	Caa1	Caa2	SG
7/17/17	VERSO PAPER CORP. - Verso Paper Holding LLC	Industrial	SrSec/BCF/LTCFR/PDR/SGL		D	B2	B3	SG
7/18/17	AES CORPORATION, (THE) - AES Puerto Rico, L.P.	Utility	SrSec		D	B3	Caa1	SG
7/18/17	ARMSTRONG ENERGY, INC.	Industrial	SrSec/LTCFR/PDR	200	D	Caa1	Ca	SG
7/18/17	EYEMART EXPRESS LTD. - Eyemart Express, LLC	Industrial	LTCFR		D	B1	B2	SG
7/18/17	ZEBRA TECHNOLOGIES CORPORATION	Industrial	SrSec/BCF/LGD	1,050	D	Ba2	Ba3	SG

Source: Moody's

FIGURE 4 Rating Changes: Corporate & Financial Institutions – EUROPE

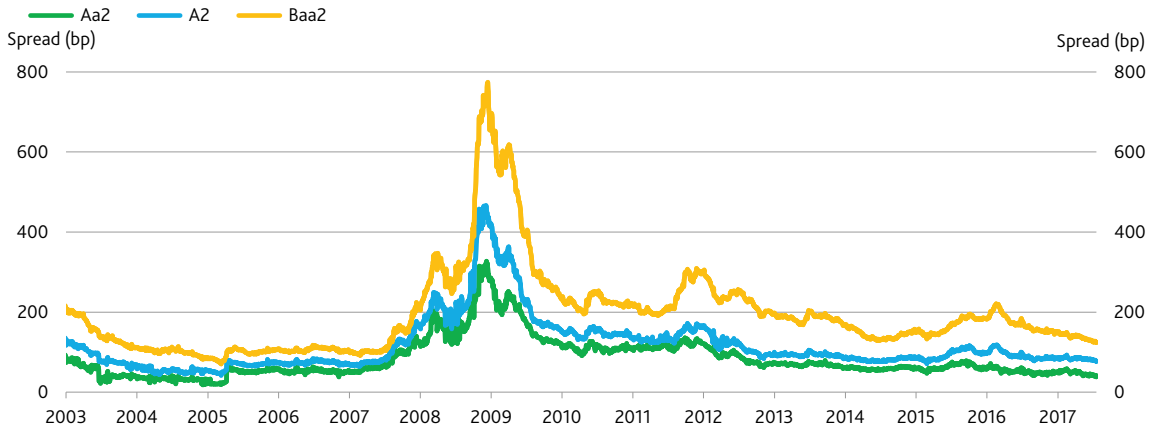
Date	Company	Sector	Rating	Amount ($ Million)	Up/ Down	Old LTD Rating	New LTD Rating	Old STD Rating	New STD Rating	IG/ SG	Country
7/18/17	HYPO TIROL BANK AG	Financial	SrUnsec/SLTD/SrSub/Sub	1,991	U	Baa3	Baa2	P-3	P-2	IG	AUSTRIA
7/12/17	BANCA MONTE DEI PASCHI DI SIENA S.P.A.	Financial	LTD		U	B2	B1			SG	ITALY
7/14/17	BANCA CARIGE S.P.A.	Financial	LTD		U	Caa1	B3			SG	ITALY
7/17/17	CIMPRESS N.V.	Industrial	SrUnsec	275	D	Ba3	B1			SG	NETHERLANDS
7/18/17	NORSKE SKOGINDUSTRIER ASA	Industrial	SrUnsec/PDR	251	D	Caa3	Ca			SG	NORWAY
7/17/17	POWER MACHINES PJSC	Industrial	LTCFR/PDR		D	B1	B2			SG	RUSSIA
7/17/17	CYAN BLUE HOLDCO 2 LIMITED	Industrial	SrSec/BCF/LTCFR/PDR		D	B1	B2			SG	UNITED KINGDOM

Source: Moody's

Market Data

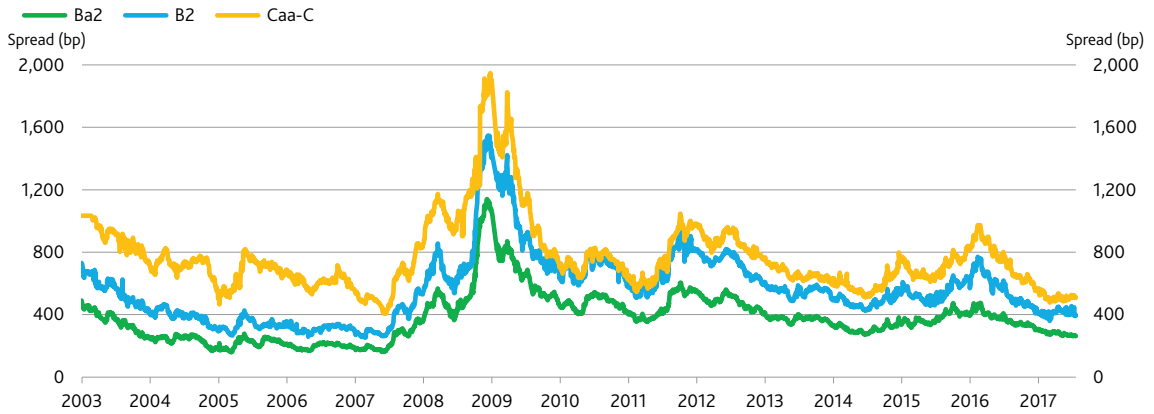
Spreads

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 (July 12, 2017 – July 19, 2017)

CDS Implied Rating Rises	CDS Implied Ratings		
Issuer	Jul. 19	Jul. 12	Senior Ratings
NV Energy Inc.	Baa2	Ba3	Baa2
Apple Inc.	Aa1	A1	Aa1
American Express Credit Corporation	Aa1	A1	A2
Walt Disney Company (The)	Aa1	A1	A2
Amgen Inc.	Aa2	A2	Baa1
Cisco Systems, Inc.	Aa1	A1	A1
Intel Corporation	Aa1	A1	A1
Merck & Co., Inc.	Aa1	A1	A1
United Technologies Corporation	Aa1	A1	A3
Capital One Bank (USA), N.A.	Aa2	A2	Baa1

CDS Implied Rating Declines	CDS Implied Ratings		
Issuer	Jul. 19	Jul. 12	Senior Ratings
Frontier Communications Corporation	C	Caa3	B2
K. Hovnanian Enterprises, Inc.	C	Caa3	Caa3
Time Warner Inc.	A3	A2	Baa2
Kraft Heinz Foods Company	Baa2	Baa1	Baa3
First Data Corporation	Ba3	Ba2	B3
United Airlines, Inc.	B3	B2	Baa1
Tyson Foods, Inc.	Baa1	A3	Baa2
Anadarko Petroleum Corporation	Ba3	Ba2	Ba1
Mondelez International, Inc.	Baa1	A3	Baa1
SunTrust Banks, Inc.	Baa3	Baa2	Baa1

CDS Spread Increases		CDS Spreads		
Issuer	Senior Ratings	Jul. 19	Jul. 12	Spread Diff
Nine West Holdings, Inc.	Ca	6,836	6,339	497
K. Hovnanian Enterprises, Inc.	Caa3	1,010	854	156
Frontier Communications Corporation	B2	1,015	921	93
Sears Holdings Corp.	Caa3	3,491	3,414	77
Windstream Services, LLC	B2	884	832	52
Genworth Holdings, Inc.	Ba3	743	694	49
Pride International, Inc.	B1	599	562	36
Neiman Marcus Group LTD LLC	Caa3	1,863	1,829	34
Chesapeake Energy Corporation	Caa2	798	773	25
SunTrust Banks, Inc.	Baa1	88	63	25

CDS Spread Decreases		CDS Spreads		
Issuer	Senior Ratings	Jul. 19	Jul. 12	Spread Diff
NV Energy Inc.	Baa2	60	159	-99
Sears Roebuck Acceptance Corp.	Caa3	3,348	3,429	-81
MBIA Inc.	Ba1	278	346	-68
NRG Energy, Inc.	B1	271	337	-66
Freeport Minerals Corporation	Ba2	324	366	-42
Freeport-McMoRan Inc.	B2	307	347	-39
Hertz Corporation (The)	B3	985	1,013	-27
Meritor, Inc.	B2	208	232	-25
Macy's Retail Holdings, Inc.	Baa3	275	299	-24
Interval Acquisition Corp	Ba3	190	214	-24

Source: Moody's, CMA

Figure 4. CDS Movers - Europe (July 12, 2017 – July 19, 2017)

CDS Implied Rating Rises	CDS Implied Ratings		
Issuer	Jul. 19	Jul. 12	Senior Ratings
Credit Agricole Corporate and Investment Bank	Aa2	A2	A1
Banque Federative du Credit Mutuel	Aa1	A1	Aa3
Swedbank AB	Aa1	A1	Aa3
SEB	Aa2	A2	Aa3
Statoil ASA	Aa1	A1	Aa3
DNB Bank ASA	Aa2	A2	Aa2
Sanofi	Aa1	A1	A1
AstraZeneca PLC	Aa2	A2	A3
AXA	Aa2	A2	A2
UBS AG	Aa1	A1	A1

CDS Implied Rating Declines	CDS Implied Ratings		
Issuer	Jul. 19	Jul. 12	Senior Ratings
Scottish Power UK plc	Baa3	Baa1	Baa1
Evonik Industries AG	Baa1	A2	Baa1
Astaldi S.p.A.	C	Caa3	B3
Barclays Bank PLC	A3	A2	A1
The Royal Bank of Scotland Group plc	Ba1	Baa3	Baa3
The Royal Bank of Scotland plc	Baa1	A3	A3
Standard Chartered PLC	Baa3	Baa2	A2
Royal Bank of Scotland N.V.	A3	A2	A3
RCI Banque	Ba1	Baa3	Baa1
Vodafone Group Plc	Baa2	Baa1	Baa1

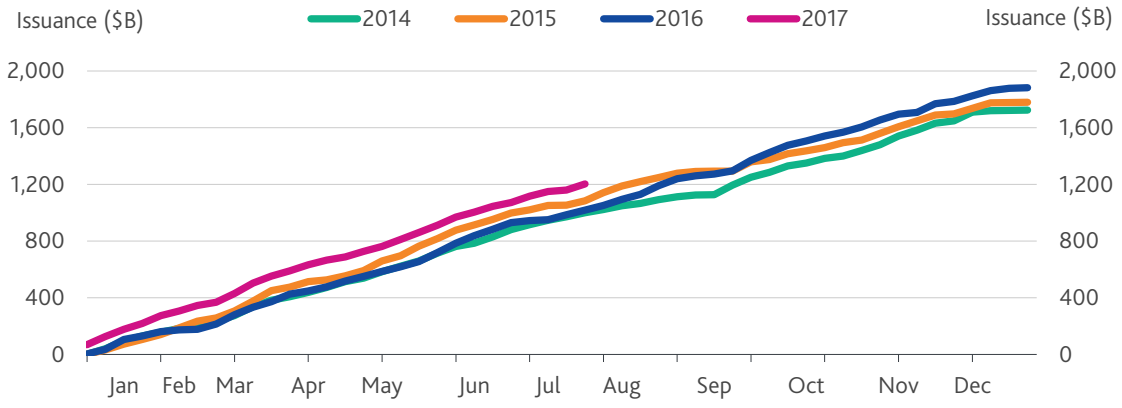
CDS Spread Increases		CDS Spreads		
Issuer	Senior Ratings	Jul. 19	Jul. 12	Spread Diff
Astaldi S.p.A.	B3	920	878	41
Novo Banco, S.A.	Caa2	1,364	1,324	40
Ensco plc	B2	613	575	37
Galapagos Holding S.A.	Caa2	883	847	36
PizzaExpress Financing 1 plc	Caa1	765	732	33
Scottish Power Limited	Baa1	91	63	27
Scottish Power UK plc	Baa1	81	57	25
Care UK Health & Social Care PLC	Caa1	378	356	22
Evonik Industries AG	Baa1	58	37	21
Boparan Finance plc	B2	485	472	14

CDS Spread Decreases		CDS Spreads		
Issuer	Senior Ratings	Jul. 19	Jul. 12	Spread Diff
Norske Skogindustrier ASA	C	23,601	24,455	-854
Eurobank Ergasias S.A.	Caa3	912	1,161	-248
Piraeus Bank S.A.	Caa3	912	1,161	-248
Alpha Bank AE	Caa3	664	845	-181
Matalan Finance plc	Caa2	622	778	-157
Banca Monte dei Paschi di Siena S.p.A.	B3	173	193	-19
Banco Comercial Portugues, S.A.	B1	275	290	-15
Techem GmbH	B1	165	180	-15
Stena AB	B3	680	693	-13
Permanent tsb p.l.c.	B1	189	200	-12

Source: Moody's, CMA

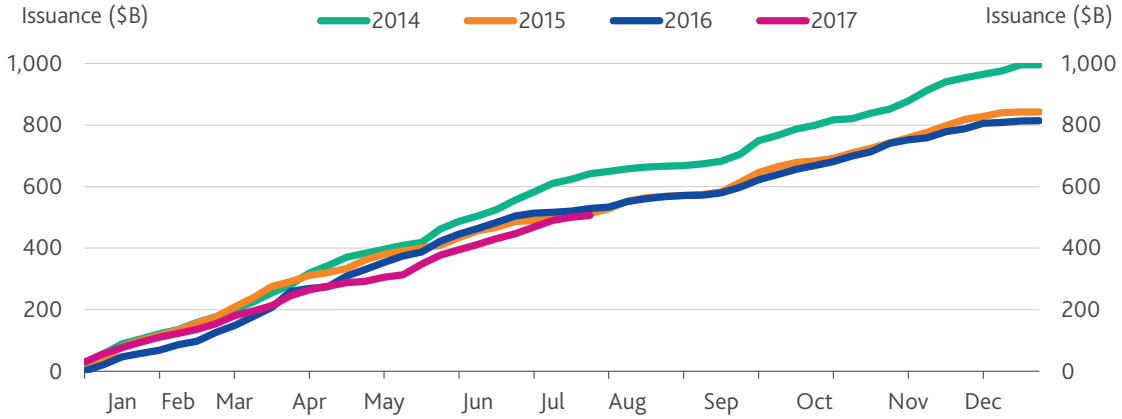
Issuance

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	27.542	7.655	42.812
Year-to-Date	844.266	249.128	1,201.915

	Euro Denominated		
	Investment-Grade	High-Yield	Total*
	Amount $B	Amount $B	Amount $B
Weekly	3.272	0.544	6.560
Year-to-Date	420.236	58.077	506.648

* Difference represents issuance with pending ratings.

Source: Moody's/ Dealogic

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