MOODY'S ANALYTICS

Editor's note: The Weekly Market Outlook will not be published Thursday, December 28, due to the holiday week. Next issue: January 4.

WEEKLY MARKET OUTLOOK

Benign Credit Outlook Comes With Blemishes

Moody's Analytics Research

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Credit Markets Review and Outlook *by John Lonski*

Benign Credit Outlook Comes With Blemishes

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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

Full updated stories and key credit market metrics: The percent changes for 2017's US$-priced corporate bond issuance were -23% for Aaa/Aa to $226 billion, +0.2% for single-A to $564 billion, and +29% for Baa to $715 billion. Begins on page 16.

Credit Spreads	Investment Grade: We see year-end 2018's average spread exceeding its recent 104 bp. High Yield: Compared to a recent spread of 365 bp, it may approximate 425 bp by year-end 2018.
Defaults	US HY default rate: Compared to November 2017's 3.4%, Moody's Default and Ratings Analytics team forecasts that the US' trailing 12-month high-yield default rate will average 2.4% during 2018's third 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 6.8% to a new zenith of $1.508 trillion, while US$-priced high-yield bond issuance may increase by 32.7% to $452 billion, surpassing 2014's record $435 billion.

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Ratings Round-Up *by Njundu Sanneh*

Positive Rating Changes on the Rebound

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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: Greece and Spain, dangers in the outlook, high-yield borrowing, Saudi Arabia, defaults, credit/stocks, China, yields/prices, debt/growth, Spain, upside surprise, bulls, less fear, Fed & BoJ, inflation, market triggers, hurricanes, data in sync.

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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.

Benign Credit Outlook Comes With Blemishes

No forecast is free of downside risks. In a manner that is consistent with (1) the recent increase in the incidence of high-yield credit rating downgrades relative to upgrades and (2) a roughly unchanged reading for the average high-yield EDF (expected default frequency) metric since the EDF's month-long average last bottomed in February 2017, Moody's Default Research Group upwardly revised its projected U.S. high-yield default rates for each of the 11 months ended October 2018 by 24 basis points (bp), on average. For example, the projected average default rate for 2018's third quarter was raised from the 2.14% of the November 2017 forecast to 2.40% as of December's projection.

Because the upwardly revised default rates were joined by an improved outlook for corporate earnings, December's set of upwardly revised default rates may not be the first of a series. The upward revision of the projected default rates occurred despite how December's Blue Chip consensus' estimates of pretax operating profits growth topped those of November 2017's survey. More specifically, the projected annual increases by core profits were revised up from 4.1% to 4.8% for 2017 and from 4.8% to 5.4% for 2018.

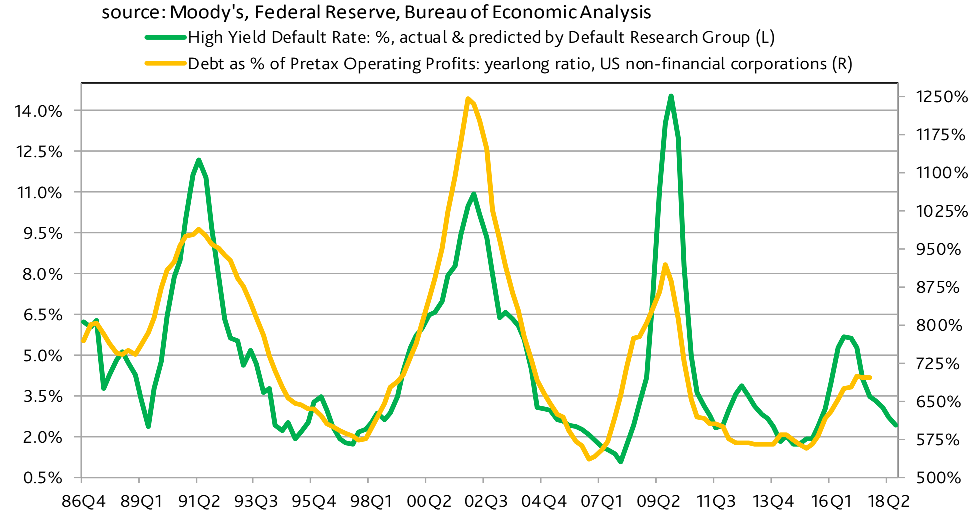
For now, December's upwardly revised default forecasts might be viewed as more closely aligning the default projections with what is suggested by other leading indicators of default such as the ratio of corporate debt to core profits, the high-yield EDF, the high-yield bond spread, net high-yield downgrades, and the number of downgrades to Caa3-or-lower. Only the ultra-low VIX index currently predicts a default rate of 2% or lower.

Getting the high-yield bond spread to remain under its recent 366 bp on a recurring basis will probably require fewer downgrades and more upgrades among high-yield credit rating changes. And it would be helpful if 2018's annual increase by non-financial corporate debt lagged behind pretax operating profits' projected 5.4% climb.

Credit Quality Will Suffer if Leverage Climbs Higher

Markets are fairly confident that nonfinancial-corporate leverage is about to peak and then move lower. Otherwise, how else can one justify expectations of a flat to lower default rate going forward? In terms of moving yearlong observations, the ratio of nonfinancial-corporate debt to pretax operating profits edged up to 696% in Q3-2017. Nevertheless, Moody's Default Research Group expects a decline by the default rate from Q3-2017's 3.5% to 2.4% by Q3-2018.

Figure 1: Realization of Expected Slide by Default Rate May Require Faster Growth by Profits Vis-a-vis Corporate Debt
source: Moody's, Federal Reserve, Bureau of Economic Analysis



Credit Markets Review and Outlook

After the ratio of corporate debt to pretax operating profits last rose to 696% during Q1-2008, the default rate quickly shot up from Q1-2008's 1.7% to Q1-2009's 6.9% as the ratio of debt to operating profits soared to the 831% of Q1-2009.

What happened in 2008-2009 was not without precedent. Prior to 2008, the ratio of corporate debt to operating profits climbed up to 696% during Q2-1999, or when the default rate equaled 4.4%. By Q2-2000, the ratio of debt to core profits had soared to 850% and the default rate reached 6.5%.

Thus, today's seeming indifference to an elevated ratio of debt to operating earnings might be ascribed to expectations of an impending peak for the ratio of debt to core profits. The jumps by nonfinancial-corporate leverage of 2000 and 2008 were largely the consequence of substantial contractions by corporate earnings. Thus, market expectations of a peaking of leverage and a declining default rate over the next 12 months are predicated on a sufficient expansion of pretax operating profits. The failure of profits to grow would lead to a higher, as opposed to lower, default rate by late 2018.

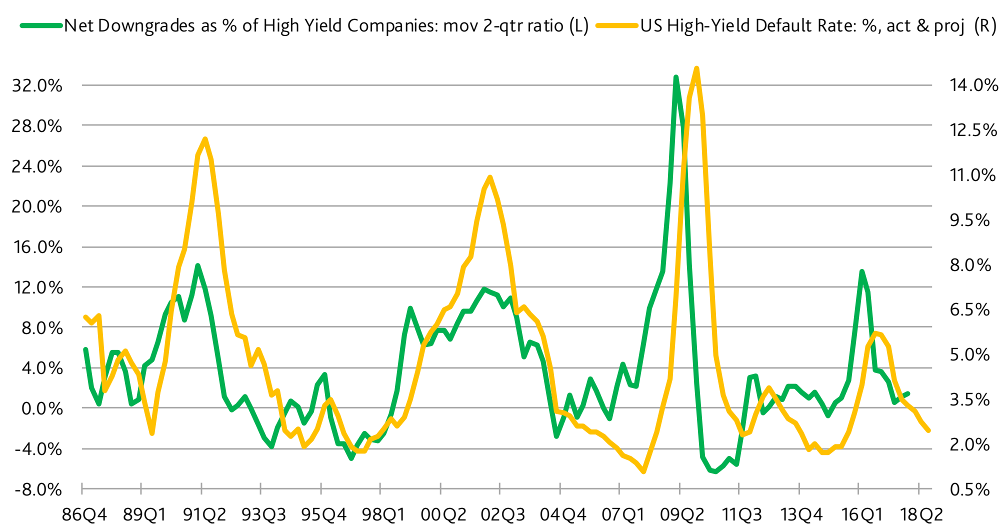
Drop by Net High-Yield Downgrades Would Strengthen Case for a Less-than-3% Default Rate

Though the recent distribution of US corporate credit rating changes does not indicate mounting financial stress, the relative frequency of downgrades to upgrades weighs against a drop by the default rate to 2% or lower. The default rate shows a strong correlation with the ratio of net high-yield downgrades to the number of high-yield issuers from nine-months earlier.

In order to neutralize the inherent volatility of quarter-to-quarter swings in net high-yield downgrades, the ratio is expressed as a moving two-quarter average. Moreover, net high-yield downgrades is simply the number of high-yield downgrades less high-yield upgrades, where the rating changes are tallied according to a methodology that has been employed since 1986.

In a manner that is typical for the business cycle, net high-yield downgrades bottomed early in the current recovery at -6.3% of the number of high-yield issuers in the six-months-ended September 2010. Mostly because of 2015-2016's bout of industrial commodity price deflation, the net high-yield downgrade ratio formed its latest localized peak at the 13.5% of the span-ended Q1-2016.

Figure 2: Net High Yield Downgrades Sense the Default Rate May Not Break Under 3% Until 2018's Final Quarter
source: Moody's Analytics



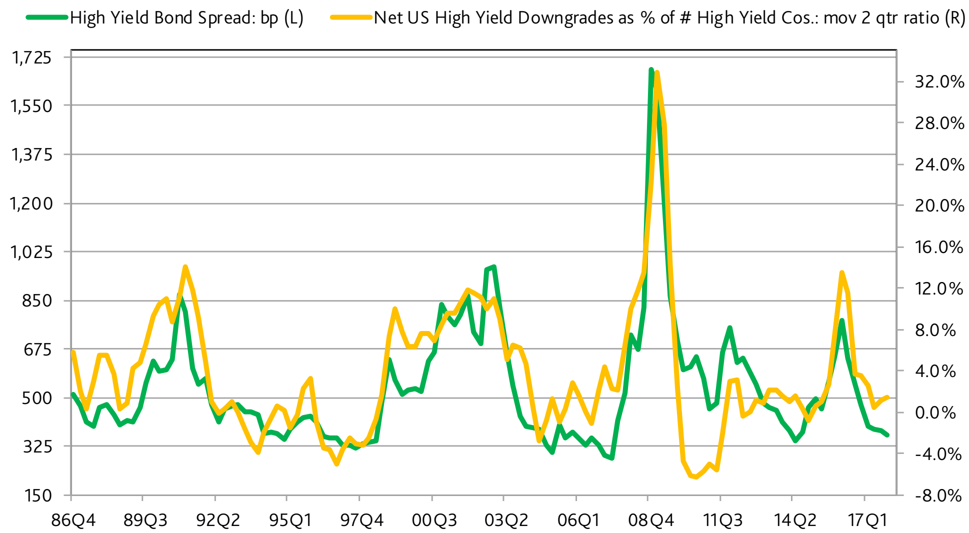
In response to 2015-2016's jump by net high-yield downgrades, the high-yield default rate climbed up from Q4-2014's current cycle low of 1.7% to Q3-2016's latest high of 5.7%. Soon thereafter, the net high-yield downgrade ratio eased to Q2-2017's 0.5%. In turn, the default rate declined to Q4-2017's prospective 3.3%.

Credit Markets Review and Outlook

However, because net downgrades have subsequently edged up to Q4-2017's 1.5% of the number of high-yield issuers, the case favoring a less than 3% default rate by 2018's third quarter has been weakened. The realization of a 2.4% average default during Q3-2018 may require a quick end to second-half 2017's rise by net high-yield downgrades.

Not only is the net high-yield downgrade ratio a useful leading indicator of the default rate, it is also a helpful coincident indicator of the high-yield bond spread. The net high-yield downgrade ratio now favors a 419 bp midpoint for a composite high-yield bond spread, which exceeds the recent actual high-yield spread of 365 bp. This difference of opinion implies that the high-yield spread predicts a lower default rate than do net high-yield downgrades.

Figure 3: High-Yield Bond Spread Now Prices In More High-Yield Upgrades than Downgrades
source: Moody's Analytics



Moreover, net high-yield downgrades favored a wider than actual high-yield spread in each of the six quarters ended Q3-2017, where this difference averaged 66 bp. Nevertheless, the current gap pales in comparison to what happened in 2007's first half, or when the 400 bp midpoint suggested by net high-yield downgrades was far above the actual high-yield spread average of 287 bp.

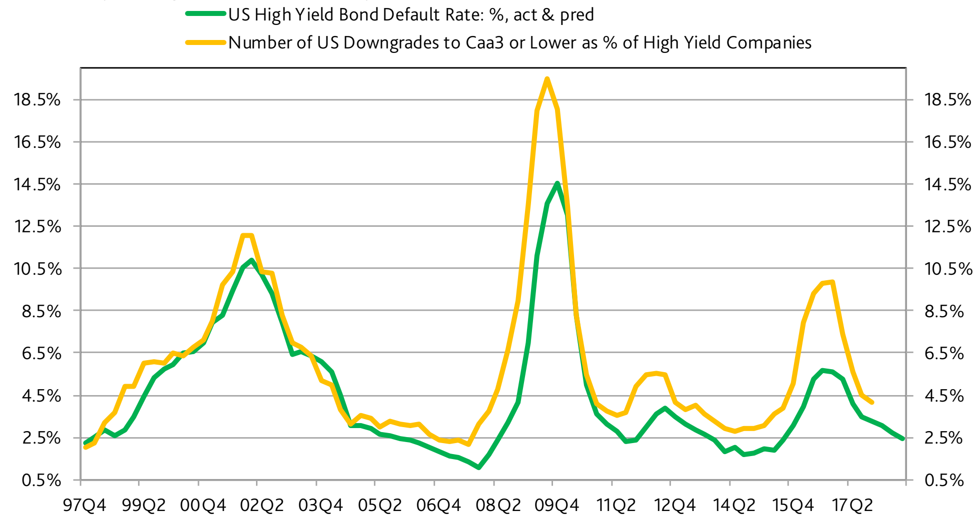
Downgrades to "Caa3 or Lower" Climb Higher in Q4-2017

It's very much worth keeping an eye on high-yield credit rating changes, especially downgrades to the lowest rungs of the high-yield ratings' ladder, or Caa3 or lower. Because the lowest high-yield credit ratings often accompany defaults, the relative incidence of downgrades to "Caa3 or lower" shows a very high correlation with the default rate.

More specifically, the moving yearlong ratio of the number of credit rating downgrades to "Caa3-or-lower" to the number of high-yield issuers shows a very high correlation of 0.92 with the percent of high-yield issuers defaulting during the past year, where the latter is commonly referred to as the high-yield default rate.

Figure 4: Downgrades to "Caa3-or-Lower" Show a Very High Coincident Correlation of 0.92 with High-Yield Default Rate

yearlong ratios; source: Moody's



When yearlong count of downgrades to "Caa3-or-lower" set a record high of 283 for the span-ended Q3-2009, the default rate peaked immediately thereafter at Q4-2009's 14.5%. The yearlong sum of downgrades to "Caa3-or-less" then entered into an uneven slide before bottoming at the 43 of the span-ended Q2-2014. By the third and final quarters of 2014, the high yield default rate troughed at 1.7%.

However, an ensuing bout of industrial-commodity price deflation drove the yearlong number of downgrades to "Caa3-or-lower" to its latest localized high of 185 for the span-ended Q3-2016, which coincided with a localized peak of 5.7% for the default rate. In quick response to an easing of the number of downgrades to "Caa3-or-lower" to the likely 77 for the year-ended 2017, the default rate fell to Q4-2017's preliminary estimate of 3.3%.

Nevertheless, a further slide by the moving yearlong count of downgrades to "Caa3-or-lower" is in doubt mostly because the quarter-long tally of such downgrades recently jumped up from Q3-2017's 14 (the lowest since Q1-2015's 12) to Q4-2017's 25. For now, the latest thinning of Caa-grade bond spreads suggests that the market believes the latest increase in default-prone downgrades will be short-lived. For example, during the past three months (or since mid-September 2017), the 7 bp narrowing of a widely followed high-yield bond spread included a deeper 43 bp thinning by the spread for Caa-rated bonds. Moreover, as of the end of November 2017, Moody's median yield spreads showed a 93 bp year-to-year plunge by the Caa spread to 509 bp, which was much deeper than the accompanying 55 bp drop by the overall median spread for high-yield bonds to 310 bp.

Tax Reform May Prove Costly for Caa-Rated Issuers

Making the recent narrowing by Caa spreads all the more remarkable is how recent tax reform legislation weighs most heavily on Caa-rated issuers. According to Moody's Investors Services, the combined benefits of a lower corporate income tax rate and the full and immediate deductibility of capital spending will exceed the costs of less than full deductibility of business interest expense "for all but a handful of U.S. investment-grade nonfinancial companies".

However, the loss of the full deductibility of interest expense leaves an estimated 26% of U.S. high-yield issuers worse off despite both a lower corporate income tax rate and the more favorable tax treatment of capital expenditures. In addition, the share of high-yield companies that are worse off soars as the high-yield credit rating moves lower.

For example, the percent of issuers made worse off jumps from 7% at the Ba rating to 27% for B2-rated issuers and, then, to 50% for B3-grade issuers. Finally, more than 75% of issuers rated Caa1 or lower will be worse off because of the loss of the full deductibility of interest expense. The high-yield market must be careful not to underestimate the risks now implicit to any unexpected broad-based contraction of operating profits.

The Week Ahead – US, Europe, Asia-Pacific

THE US

By Ryan Sweet of Moody's Analytics

Tax reality sets in

The sweeping changes to the tax code passed by the Trump administration and Republican Congress will significantly impact the near-term economic outlook. The $1.5 trillion, 10-year tax cut will juice up growth through the remainder of this decade but will result in meaningfully weaker growth at the start of the next decade. Longer run, the tax cuts will add little to the economy but will add significantly to the government's deficits and debt load.

The deficit-financed tax cuts will act like fiscal stimulus, temporarily pumping up growth. Based on simulations of the Moody's Analytics macro model, which is similar to models used by the Federal Reserve, Congressional Budget Office, and the Joint Committee on Taxation—the official budget scorer of tax legislation—the tax legislation will lift real GDP growth by 0.4 percentage point in 2018 and 0.2 percentage point in 2019. Without tax cuts, the economy was set to grow by 2.5% per annum through the remainder of the decade, but with the cuts, growth will be 2.9% per annum. The problem is that the economy is arguably already operating beyond full employment. The unemployment rate is just higher than 4%, well below most estimates of the full-employment unemployment rate, including our own estimate of 4.5%.

The underemployment rate at 8%—a broader measure of slack in the job market—is also signaling a fully employed economy. Even without tax cuts, unemployment was set to fall below 4%, but with them it could fall into the low-3% range. The only other time unemployment has been as low was during the Korean War in the early 1950s. Although wage and price pressures have been largely dormant, this won't last, and the Federal Reserve will have little choice but to normalize monetary policy more aggressively. Fed policymakers are anticipating three 0.25-point rate hikes in 2018 and about the same in 2019, but they likely haven't fully incorporated the implications of the tax cuts into their thinking. Four rate hikes each year now seem more likely.

Long-term interest rates should also increase because of the more aggressive Fed and investor expectations of larger future budget deficits. This so-called crowding-out effect is evident in the Moody's Analytics model, as for every 1-percentage point increase in the nation's publicly traded debt-to-GDP ratio, 10-year Treasury yields increase in the model by an estimated 4 basis points. Given that tax legislation adds 5 percentage points to the debt-to-GDP ratio, 10-year yields rise by 20 basis points, all else being equal.

The upcoming week is fairly quiet on the data front. The Conference Board's Consumer Confidence index for December will be released. This measure of sentiment remains very strong, noticeably outperforming the University of Michigan survey. The gap is large but not rare at this point of the business cycle as the Conference Board survey is more sensitive to labor market conditions. Elsewhere, pending-home sales will try and extend the recent string of strong housing data. The advance goods deficit and inventory will feed into our estimate of fourth quarter GDP, which is currently tracking 2.6% at an annualized rate.

	Key indicators	Units	Moody's Analytics	Consensus	Last
Tues @ 10:00 a.m.	Moody's Analytics Business Confidence for 12/22/17	index, 4-wk MA			38.2
Wed @ 10:00 a.m.	Conference Board Consumer Confidence for December	index		128.0	129.5
Wed @ 10:00 a.m.	Pending Home Sales for November	% change		-0.8	3.5
Thur @ 8:30 a.m.	Advanced goods deficit for November	$ bil		-67.5	-68.3
Thur @ 8:30 a.m.	Jobless Claims for 12/23/17	ths			245

EUROPE

By Barbara Teixeira Araujo and Europe staff of Moody's Analytics in London and Prague

Russia's situation remains fragile

This preview covers both the week between Christmas and New Year and the first week of January. The period will be light on economic data as many businesses close for the holidays.

Next Friday will bring GDP figures for Russia. We expect the country's GDP grew 1.8% y/y in the third quarter, slowing from 2.5% in the previous stanza and below the Ministry of Economic Development's early estimates of 2.2%. Investment, which boosted GDP growth in the first half of the year, likely slowed as the low base effect from early 2016 faded; investment actually declined by 1.4% y/y in the first half of last year but then roared back in the third quarter. Instead, we expect consumer spending supported growth the most in the three months to September. We already know that retail sales gained 2% y/y in the third quarter, but services spending likely surged as well. Consumption is being propelled by a pickup in real wage growth, which accelerated to a three-year high in October after earnings hit rock bottom amid the oil crisis in 2015. Meanwhile, the contribution of net exports to growth disappointed yet again.

Russia's situation is still fragile. We doubt that growth can pick up significant momentum next year without much-needed structural reforms, but those are unlikely to come at this point in the election cycle. This means that net exports will continue to languish as oil revenues remain subdued given OPEC's recent renewal of output cuts, and as the EU's sanctions were prolonged by another year. Further, a large swath of industries may suffer now that inflation recently dropped to a record low. Although the ongoing practice of freezing nominal wage growth helped companies reduce real costs of production amid double-digit inflation, subdued price growth diminishes such gains. This may prove painful to businesses in the short term, eroding investment.

Germany will dominate the headlines in the week following New Year. We expect unemployment figures to again confirm that the country's labour market is on a roll, and even if we forecast that joblessness remained steady at 5.6% in December, we would not be surprised if the rate fell to a record low of 5.5%. That's because November's sharp drop in claims pushed the trend lower, and even a small decline in December would manage to further reduce the unemployment rate. And given that vacancies also rose in the middle of the fourth quarter, a further tightening of the labour market is likely. This will in turn push up the country's wage growth, which was already reading at a strong 4.6% y/y in the third quarter, more than doubling the average 1.6% recorded for the euro area as a whole. In all, Germany's current economic momentum is impressive, and we are running out of superlatives to describe the strength of the euro zone's biggest economy.

Preliminary CPI figures for the euro zone will likely show that inflation is cooling slightly in the closing month of the year, to 1.3% from a reading of 1.5% in November. The dip will mainly be due to base effects, since oil prices rose by around 18% m/m between November and December last year; this should push energy inflation down substantially, though the increase in oil prices since September means that energy price growth will remain above zero in the next few months. Elsewhere, food inflation should accelerate slightly, and so should services inflation. We expect nonenergy goods inflation to remain unchanged, though we still expect it to heat up throughout 2018, in line with the currency area's economic recovery.

We will release our forecasts for upcoming economic data on Tuesday.

	Key indicators	Units	Moody's Analytics	Last
Tues @ 1:30 p.m.	Russia: Business Confidence for December		-8.0	-4.0
Wed @ 8:05 a.m.	Spain: Retail Sales for November	% change	0.6	-1.1
Wed @ 5:00 p.m.	France: Job Seekers for November	ths, SA	3.47	3.48
Thur @ 7:05 a.m.	U.K.: Nationwide Housing Price Index for December	% change yr ago	2.1	2.5
Fri @ 7:30 a.m.	Russia: GDP for Q3	% change yr ago	1.8	2.5
Fri @ 9:00 a.m.	Euro Zone: Monetary Aggregates for November	% change yr ago	4.9	5.0
Wed @ 9:00 a.m.	Germany: Unemployment for December	%	5.6	5.6
Thur @ 8:00 a.m.	Germany: Lending by Banks for November	% change yr ago	4.2	4.4
Thur @ 9:00 a.m.	Italy: Consumer Price Index for December	% change yr ago	1.2	1.1
Fri @ 8:00 a.m.	Germany: Retail Sales for November	% change	0.9	-1.2
Fri @ 10:00 a.m.	Euro Zone: Producer Price Index for November	% change yr ago	2.4	2.5
Fri @ 10:00 a.m.	Euro Zone: Preliminary Consumer Price Index for December	% change	1.3	1.5

FRIDAY, DECEMBER 22

France: GDP (Q3; 6:30 a.m. GMT)

Final GDP data are expected to confirm that the French economy grew by 0.5% q/q in the three months to September, slowing slightly from a upwardly revised 0.6% gain in the previous stanza. The year-on-year rate is expected to have shot up to 2.2%, from 1.8% previously, its strongest since 2011. Domestic demand should have contributed the most to growth, as household consumption and investment surged. Consumer spending is set to have accelerated to 0.5% q/q, from 0.3% in the second quarter, on the back of a 1.6% rise in energy consumption—particularly as September's below-average temperatures boosted demand for heating—and of a jump in sales of clothing, since annual sales started later this year than last year, boosting July's sales volumes. But services spending is also expected to have ramped up to 0.4% q/q, from 0.2% in the second quarter. Investment also expanded, by 0.8% q/q and building on an already-strong 1% increase in the previous stanza. Investment in manufacturing rose 0.8% q/q, from a 0.5% rise in the second quarter, but this gain was offset by slowdowns in construction and services capital expenditures.

Foreign trade by contrast likely dragged, which was expected following the second quarter's jump. That's because imports likely surged by 2.5% q/q in the third quarter, following a mere 0.2% increase in the second, on the back of a replenishing of inventories. Stock-building and imports are strongly correlated in France, especially in the transport sector, and the story in the third quarter is that after sales of aeronautic equipment soared in the second quarter, companies rushed to replenish their stocks in the third. As a result, inventories also skyrocketed and offset the plunge in net trade. Exports, meanwhile, decelerated to only 0.7% q/q, though this was expected following the 2.3% jump in the three months to June. In all, net trade is expected to have shaved 0.6 percentage point off the GDP headline.

France: Household Consumption Survey (November; 7:45 a.m. GMT)

French household expenditures on goods likely rose by 2% m/m in November, fully reversing October's 1.9% plunge and pushing the yearly rate back to 1%, from a 0.6% contraction previously. This would still be below the past year average at 1.1%, but we think that a further rebound will come in December. Sales have been unusually volatile lately, but we caution that this is mostly on the back of one-off factors. For instance, while October's unseasonably mild weather depressed energy consumption, November's temperatures turned sharply lower, raising demand for heating. Similarly, we expect that clothing sales rebounded following weakness in October, notably as the colder weather should have boosted consumers' interest in retailers' new winter lines. Elsewhere, we are penciling in mean reversions in most other subsectors of retailing following the broad-based weakness in October, though the standout should be a soar in the sale of household goods. We note that Black Friday sales were probably not included in the retail sales figures for November, and the different countries' indexes are normally compiled around the second or third week of the month.

Spain: Foreign Trade (November; 9:30 a.m. GMT)

We expect the Spanish trade deficit deteriorated to €2.9 billion in October because of weaker export performance over the month. Amid the bitter row between Catalonia and the Spanish government, more than 3,000 companies left Catalonia and relocated to other regions. The political uncertainty may have weighed on exports, although it is hard to say by how much. But we do not think the political situation will hurt trade; we expect exports to bounce back and hover around €24 billion, given the sector has managed to stay competitive. Accounting for seasonal and calendar effects, Spain's unit labour cost decreased by 0.1% y/y in the third quarter, down from a moderate 0.5% in the previous quarter, which should keep labour-intensive exports cost competitive.

ASIA-PACIFIC

By Katrina Ell and the Asia-Pacific staff of Moody's Analytics in Sydney

Japan's CPI unlikely to have changed after October's mild rise

A barrage of eye-catching economic data will be released in the final week of 2017. Japan's CPI was likely unchanged in November, after a mild rise to 0.8% y/y in October. Higher energy costs may be starting to affect core inflation, although the longer-term effects remain unclear. The BoJ is still not expected to meet its 2% inflation target in the foreseeable future. The November employment report will likely show annual employment growth remained upbeat. But the tightening labour market hasn't led to stronger wage growth.

South Korea's monthly foreign trade data are closely watched because the country is amongst the first major economies to release monthly data. Tech exports are expected to keep leading the gains, driving a healthy surplus. In November, semiconductor exports were up an impressive 65.2% y/y following a 69.6% surge in the prior month. South Korean manufacturing likely rebounded in November after national holidays reduced October production. Annual growth, however, will be moderated by a high base year.

Chinese manufacturing sentiment likely weakened slightly in December but remains comfortably in expansionary territory, according to the official manufacturing PMI. Chinese manufacturing is performing well through the peak holiday season thanks to both upbeat global tech demand and domestic demand for automobiles and other goods. In the November survey, new orders and new export orders gathered pace from an already-high level, a testament to strong manufacturing momentum.

Australian exporters are again reaping the benefits of a mining investment boom, this time with liquefied natural gas. Australia is in the final stretch of a A$200 billion LNG construction boom. Australia has recently become the world's second largest exporter of LNG. Once the remaining two projects of eight are finalized, Australia could topple Qatar as the biggest. Looking at the November data, we expect the trade surplus widened.

	Key indicators	Units	Moody's Analytics	Last
Tues @ 10:30 a.m.	Japan Consumer price index for November	% change yr ago	0.8	0.8
Tues @ 10:30 a.m.	Japan Unemployment rate for November	%	2.8	2.8
Tues @ 10:30 a.m.	Japan Household expenditures survey for November	% change yr ago	-0.2	2.6
Tues @ 11:00 p.m.	Singapore Industrial production for November	% change yr ago	8.3	14.6
Wed @ 8:00 a.m.	South Korea Consumer sentiment index for December	Index	110.2	112.3
Wed @ 4:00 p.m.	Japan Housing starts for November	% change yr ago	-1.3	-4.8
Thurs @ 10:00 a.m.	South Korea Industrial production for November	% change yr ago	2.1	-5.9
Thurs @ 10:00 a.m.	South Korea Retail sales for November	% change	0.7	-2.9
Thurs @ 10:50 a.m.	Japan Retail sales for November	% change yr ago	0.6	-0.2
Thurs @ 7:30 p.m.	Hong Kong Foreign trade for November	HK$ bil	-40	-44
Fri @ Unknown	Thailand Industrial production for November	% change yr ago	3.0	-0.1
Fri @ 10:00 a.m.	South Korea Consumer price index for December	% change yr ago	1.9	1.3
Fri @ 6:30 p.m.	Thailand Private consumption for November	% change yr ago	1.9	1.4
Fri @ 6:30 p.m.	Thailand Foreign trade for November	US$ bil	2.7	1.6
Sun @ 12:00 p.m.	China Official manufacturing PMI	Index	51.7	51.8
Mon @ Unknown	South Korea Foreign trade for December	US$ bil	8.2	7.8
Fri @ 11:30 a.m.	Australia Foreign trade for November	A$ mil	650	105
Fri @ 11:30 a.m.	Taiwan Consumer price index for December	% change yr ago	0.5	0.3
Fri @ 3:00 p.m.	Malaysia Foreign trade for November	MYR bil	8.3	10.5

FRIDAY, DECEMBER 22

Taiwan – Domestic Trade – November

Time: 7:00 p.m. AEDT (8:00 a.m. GMT)
Forecast: 3.5%

Taiwan retail sales likely grew 3.5% in November, up from 3.2% in October. Retail sales have improved noticeably in recent months, coinciding with the sustained upswing in consumer confidence. Consumer confidence surged to a 29-month high in November, as a booming stock market, public service wage increases next year and plans for new labour laws boosted confidence. Upbeat consumer confidence and a modestly improving labour market should support retail sales in coming months.

Taiwan – Industrial Production – November

Time: 7:00 p.m. AEDT (8:00 a.m. GMT)
Forecast: 3%

Taiwan industrial production likely grew 3% y/y in November, after ticking up 2.8% in the prior month. Firm demand for semiconductors and other tech products should support manufacturing output into 2018, particularly with economic conditions abroad expected to remain favourable. Still, downside risks include a slowing mainland Chinese economy and souring cross-straits relations that could undermine supply chains. Power supply issues will also need watching, especially in light of a recent power outage and the government's commitment to phase out all nuclear power plants by 2025.

TUESDAY, DECEMBER 26

Japan – Consumer Price Index – November

Time: 10:30 a.m. AEDT (Monday, 11:30 p.m. GMT)
Forecast: 0.8%

Consumer price inflation in Japan was likely unchanged in November, after a mild rise to 0.8% y/y in October. Higher energy costs may be starting to affect core inflation, although the longer-term effects remain unclear. The BoJ is not expected to meet its 2% inflation target in the foreseeable future. Domestic demand has been weak in the final two quarters of the year, and we expect consumption to remain moribund in 2018. Despite inflation not hitting the BoJ's target, we expect the central bank will begin lowering its pace of asset purchases by the end of 2018.

Japan – Employment Situation – November

Time: 10:30 a.m. AEDT (Monday, 11:30 p.m. GMT)
Forecast: 2.8% Unemployed

We expect Japan's unemployment rate remained at 2.8% in November. Employment is expected to grow on a year-ago basis, although wage growth is unlikely to rise. The number of unemployed is expected to remain steady. In recent months, job growth has come from regular employees, and this trend is expected to continue. Overall, this supports our view that Japan's labour market is tightening. However, despite these increases, wage growth remains a laggard, and recent forward indicators suggest it's not likely to rise over the coming months.

Japan – Household Expenditures Survey – November

Time: 10:30 a.m. AEDT (Monday, 11:30 p.m. GMT)
Forecast: -0.2%

Japanese workers' household expenditure surprised on the upside and rose 2.6% y/y in October, but that's unlikely to have been repeated in November, with a drop of -0.2% forecast. Household expenditure data have been choppy of late, and it's difficult to gauge a credible trend. We still think consumers' balance sheets will remain under pressure given that wage growth has been low this year and prices have risen on the back of higher energy costs.

Singapore – Industrial Production – November

Time: 11:00 a.m. AEDT (12:00 a.m. GMT)
Forecast: 8.3%

Singapore industrial production likely rose 8.3% y/y in November, after a 14.6% increase in October. Although industrial production has cooled since August, production is increasing at a healthy pace, having risen for 15 consecutive months thanks to the upturn in global demand. Production of products such as semiconductors and electronics has been especially strong, helping to propel GDP growth to 5.2% y/y in the September quarter, its fastest pace since the fourth quarter of 2013. However, although manufacturing should continue to benefit from favourable external conditions, a high base from a year earlier is likely to inhibit growth in coming months.

WEDNESDAY, DECEMBER 27

South Korea – Consumer Sentiment Index – December

Time: 8:00 a.m. AEDT (Tuesday, 9:00 p.m. GMT)
Forecast: 110.2

The Bank of Korea's consumer confidence index likely slipped to 110.2 in December, as North Korea tensions have escalated following two months of relative calm. Consumer sentiment rose 3.1 points to 112.3 in November, its strongest reading in almost seven years. Improved economic conditions and President Moon Jae-in's policies, including a pledge to create 810,000 public sector jobs during his five-year term, are lifting sentiment. However, tensions on the Korean peninsula appear to have ticked up a notch in December following the North's latest missile test. That likely dimmed sentiment in December.

Japan – Housing Starts – November

Time: 4:00 p.m. AEDT (5:00 a.m. GMT)
Forecast: -1.3%

Japan's housing activity continues to dive. Housing starts fell sharply by 4.8% y/y in October, and we expect a further 1.3% decrease in November. The broad-based decline is likely across all major categories, with owner-occupied and houses built for sale falling; these are the two major categories of housing starts. After a tailwind from negative interest rates and various tax concessions to owners in 2016, housing starts are dropping on a year-ago basis. Japan's ageing population means that there will be ample housing supply over the coming years that keeps prices subdued. Further increases in housing starts are unlikely next year.

THURSDAY, DECEMBER 28

South Korea – Industrial Production – November

Time: 10:00 a.m. AEDT (Wednesday, 11:00 p.m. GMT)
Forecast: 2.1%

South Korean industrial production likely ticked up 2.1% y/y in November, after dipping 5.9% in the prior month. Industrial production weakened markedly in October, as national holidays reduced production during the month. A backlog of production will likely result in a production rebound in November, albeit modestly as a high base from a year earlier will likely cap the gains. That would be consistent with the modest improvement in export growth during the month. Exports were up 9.7% y/y, after slowing to 7.1% in October. Semiconductor exports surged, up 65.2% y/y following a 69.6% gain in the prior month. Meanwhile, mobile phone exports were up 24.8% y/y and exports of computers increased 18.4%.

South Korea – Retail Sales – November
Time: 10:00 a.m. AEDT (Wednesday, 11:00 p.m. GMT)
Forecast: 0.7%

South Korean retail sales likely edged up 0.7% m/m in November, after dipping 2.9% in the prior month. A gradually improving labour market and Moon's stimulus measures should support firmer retail spending in coming months. However, following two months of relative calm, tensions on the Korean peninsula have ramped up again after the latest North Korea missile test. Should those tensions escalate, consumer confidence is likely to dim, posing a downside to retail sales. The Bank of Korea's consumer sentiment index increased to 112.3 in November, thanks to an improvement in sentiment about living standards and a big lift in sentiment regarding domestic economic conditions.

Japan – Retail Sales – November
Time: 10:50 a.m. AEDT (Wednesday, 11:50 p.m. GMT)
Forecast: 0.6%

Japan's retail sales unexpectedly slipped in October following strong gains throughout the year. Retail sales fell 0.2% y/y, but we expect them to rebound to 0.6% y/y for November. Base effects from low spending last year means that sales will likely rise this year. But tepid wage growth weighs on demand for big-ticket items, and that's unlikely to change. Despite our expectations of an increase in November, year-ago increases have petered out. Overall, consumption growth has slowed, as evidenced by private consumption declining in the September quarter. We expect consumption likely subtracted from growth again in the December quarter.

Hong Kong – Foreign Trade – November
Time: 7:30 p.m. AEDT (8:30 a.m. GMT)
Forecast: -HK$40 billion

Trade activity through Hong Kong's port remains healthy, although exports and imports increased more slowly in October. That was mostly due to seasonal factors such as the Golden Week in the mainland. Hence a recovery in trade activity is expected. Manufacturers in China continue to see higher export orders and have been increasing their own tech component imports ahead of the holiday season. Hong Kong's trade deficit likely narrowed to HK$40 billion in November from a HK$44 billion deficit in October.

FRIDAY, DECEMBER 29

Thailand – Industrial Production – November
Time: Unknown
Forecast: 3%

Industrial production likely increased 3% y/y in November, after slipping 0.1% in the prior month. October's slowdown reflected a 1.3% y/y fall in food and beverage production, as well as declines in textiles and furniture and jewellery production. Textiles production fell for a fifth consecutive month, while production of electronic devices fell 0.7% y/y, a 20-month low. Despite the slowdown in October, favourable external conditions should support industrial production into 2018. Industrial production should also get a boost from government-led infrastructure projects, which are expected to ramp up in 2018.

South Korea – Consumer Price Index – December

Time: 10:00 a.m. AEDT (11:00 p.m. GMT)
Forecast: 1.9%

South Korean consumer prices likely increased 1.9% y/y in December. Consumer price inflation has eased since August and fell to a 15-month low of 1.3% in November, as lower food prices kept a lid on inflation. Even as inflation has slipped below the Bank of Korea's 2% inflation target, the central bank raised its key policy rate 25 basis points at its November policy meeting, the first rate hike since 2011. Although underlying inflation pressures remain subdued, the strong GDP reading in the September quarter likely prompted the central bank to raise rates earlier than expected.

Thailand – Private Consumption – November

Time: 6:30 p.m. AEDT (7:30 a.m. GMT)
Forecast: 1.9%

Private consumption likely grew 1.9% y/y in November, after growth slowed to a three-month low of 1.4% y/y in October. Although consumption of durables and services remained firm in October, the decline of semidurables purchases and a slowdown in nondurables consumption weighed on overall consumption growth. Thai consumers have had relatively little to cheer about this year. Although economic activity has firmed and consumer confidence has perked up, little if any wage growth is inhibiting consumer spending. Meanwhile, elevated household debt is also likely to be inhibiting spending.

Thailand – Foreign Trade – November

Time: 6:30 p.m. AEDT (7:30 a.m. GMT)
Forecast: US$2.7 billion

Thailand's trade surplus likely increased to US$2.7 billion in November, after falling to US$1.6 billion in the prior month. Imports grew a firm 16.6% y/y in October, as imports of raw materials and intermediate goods surged 21.9%, up from a 7.5% gain in September. Meanwhile, exports rose at a solid pace, up 13.4% y/y in October, the third consecutive month of double-digit gains. We expect external demand to remain firm into 2018. Although the firm baht has had a limited impact on exports to date, it remains a downside risk to the outlook.

SUNDAY, DECEMBER 31

China – Manufacturing PMI – December

Time: 12:00 p.m. AEDT (1:00 a.m. GMT)
Forecast: 51.7

Chinese manufacturing sentiment likely weakened slightly in December to 51.7, from 51.8 in November. Chinese manufacturing is performing well through the peak holiday season, thanks to both upbeat global tech demand and domestic demand for automobiles and other goods. In the November survey, new orders and new export orders gathered pace from an already-high level, a testament to strong manufacturing momentum.

The Week Ahead

MONDAY, JANUARY 1

South Korea – Foreign Trade – December

Time: Unknown
Forecast: US$8.2 billion

South Korea's foreign trade surplus likely ticked up to US$8.2 billion in December after rising to US$7.8 billion in November. Export growth picked up to 9.7% y/y in November, with tech exports leading the gains. Semiconductor exports were up 65.2% y/y following a 69.6% surge in the prior month. However, automobile exports were relatively soft, up just 3.4% y/y. Currently, soaring prices for DRAM, or dynamic random-access memory, caused by supply shortages are helping to push up South Korea's exports. However, DRAM prices could fall next year and undermine export growth.

FRIDAY, JANUARY 5

Australia – Foreign Trade – November

Time: 11:30 a.m. AEDT (12:30 a.m. GMT)
Forecast: A$650 million

Australia's monthly trade surplus likely widened to A$650 million in November, from a A$105 million surplus in October. The small trade surplus in October was caused by falls in hard commodity exports. Iron ore endured hefty falls in values and volumes over October. November iron ore values likely improved, reflecting the higher spot price, which increased by 22% from its late-October slump to US$71.51 per metric tonne in early December. Usually the lag is short between the spot price and being incorporated into export contracts. A longer-term support to merchandise exports is higher production capacity coming on line from liquefied natural gas. Australia is in the final stretch of a A$200 billion LNG construction boom. Once the remaining two projects of eight are finalized, Australia could topple Qatar as the world's biggest LNG exporter. Australia has recently become the world's second largest exporter of LNG.

Taiwan – Consumer Price Index – December

Time: 11:30 a.m. AEDT (12:30 a.m. GMT)
Forecast: 0.5%

Taiwan's consumer prices were subdued in the final month of 2017. We expect CPI rose 0.5% y/y in December, from a 0.3% rise in November. Food prices have been the main drag on the CPI in the fourth stanza. Core inflation is higher and likely remained steady at 1.6% y/y in December for a second straight month. Underlying price pressures show signs of building, consistent with firmer economic activity. The central bank will keep its monetary policy settings unchanged at its December policy meeting. The benchmark policy rate has been at 1.375% since July 2016.

Malaysia – Foreign Trade – November

Time: 3:00 p.m. AEDT (4:00 a.m. GMT)
Forecast: MYR8.3 billion

Malaysia's monthly trade surplus likely maintained its seesaw pattern in November. The surplus likely narrowed to MYR8.3 billion, after widening to MYR10.5 billion in October. The bright spot on the export ledger will remain electrical and electronics products. Tech manufacturing has enjoyed stellar conditions in 2017 amid strong offshore demand. We expect the tech cycle has passed its peak and expect cooler conditions through 2018.

The Long View

The US: The percent changes for 2017's US$-priced corporate bond issuance were -23% for Aaa/Aa to $226 billion, +0.2% for single-A to $564 billion, and +29% for Baa to $715 billion.

By John Lonski, Chief Economist, Moody's Capital Markets Research Group,
December 21, 2017

CREDIT SPREADS

As measured by Moody's long-term average corporate bond yield, the recent investment grade corporate bond yield spread of 104 bp is far under its 122-point mean of the two previous economic recoveries. This spread is more likely to be wider, as opposed to narrower, a year from now.

The recent high-yield bond spread of 365 bp is less than what is inferred from the spread's macroeconomic drivers and the high-yield EDF metric. The adverse implications for liquidity of possibly significantly higher interest rates merit consideration.

DEFAULTS

After setting its current cycle high at January 2017's 5.8%, the US high-yield default rate has since eased to the 3.4% of November. Moody's Default and Ratings Analytics team expects the default rate will average 2.4% in Q3-2018. 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.

Second-quarter 2017's worldwide offerings of corporate bonds showed an annual percent decline of -6.3% for IG and an increase of +8.3% for high-yield, wherein US$-denominated offerings fell by -6.4% for IG and grew by +5.8% for high yield.

Third-quarter 2017's worldwide offerings of corporate bonds showed an annual percent decline of -1.6% for IG and an increase of +6.6% for high-yield, wherein US$-denominated offerings dipped by -0.7% for IG and grew by +4.3% 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 3.9% annually for IG and may advance by 41.2% for high yield. The worldwide corporate bond offerings of 2018 are expected to show annual increases of 2.5% for IG and 6.0% 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 consensus expects that the mid-point for the federal funds rate should finish 2018 at 2.125%. 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 2.5% 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 Kristopher Cramer of Moody's Analytics
December 21, 2017

Netherlands

The Dutch economy is in fine fettle, continuing its longest economic expansion since the recession in 2008. Although real GDP slightly missed the mark in the first quarter, the economy has picked up on cue with output expanding by 3.8% year over year in the second quarter and 3.3% in the third. Overall, we expect the Dutch economy to end this year well, with 2017's annualized GDP reaching 3.1% before slowing to 1.9% in 2018.

Exports continue to propel the economy. Being a major economic hub and home to Rotterdam—one of Europe's busiest ports—the Netherlands benefits significantly from global and European trade. A key reason for the surge over the last few years is the machinery and transportation equipment industry, which accounts for more than a quarter of all Dutch exports. The industry has benefited from low oil prices and firming global demand. We expect robust domestic demand and increased trade volumes to continue, which will boost productivity, investment and incomes. Business confidence and manufacturing exports have also improved: Manufacturer surveys suggest new orders and production will grow, indicating higher output prior to the end of the year.

But although output is expanding rapidly, the U.K.'s vote to leave the European Union clouds the future of Dutch exports. Despite the EU and Britain reaching an agreement that covers the main divorce issues—including financial obligations to the EU, the border between Northern Ireland and the Republic of Ireland, and citizens' rights—trade has not yet been resolved. The U.K. will have to negotiate a free trade agreement similar to the one Canada has with the region. However, time is not on its side. The Comprehensive Economic and Trade Agreement took seven years to negotiate, whereas the U.K. is set to leave in March 2019. The Netherlands will be among the hardest-hit European countries if the U.K. exits without an agreement, since Britain accounts for about a tenth of Dutch exports.

The Netherlands' job market is tightening quickly. The national unemployment rate, at 4.5% in October, shed more than a full percentage point since last October and remains well below the euro zone average. The number of unemployed fell by 18,000 following a 4,000 decrease in September, while the labor force added about 7,000 workers over the last two months, suggesting that the broader economy is on solid footing. As a result, a tighter job market is boosting workers' bargaining power, supporting a bump in pay. Wages and salaries increased by 6.9% in the third quarter of this year; over the next year, the market will tighten even further. As the labor supply dwindles, incomes will continue to grow more quickly, while employment gains will gradually decelerate as the country reaches full employment.

The Netherlands' real estate market is booming. The house price index reached 100.79 in the third quarter, surpassing 100 for the first time since 2010. On a year-ago basis, prices increased by 7.5% in the September quarter with existing-home prices in Amsterdam, the Dutch capital, rising by 13.4% in the second stanza. Even with surging prices, the Dutch housing market still has more room to grow, since prices remain at 5% below their precession peak. However, low supply is becoming a concern in the capital. Rabobank estimates that only about 55,000 houses a year are being built, but 70,000 are needed to satisfy current demand. Municipalities cannot issue permits fast enough, resulting in a backlog in the new housing construction pipeline. The supply shortage is a scar from the financial crisis, when too few houses were built.

With the British exit looming, Dutch politicians are seizing on the potential exodus to attract banks and businesses afraid to lose access to the EU market when Britain leaves the bloc in 2019. Amsterdam has strong connections to the rest of Europe and a good supply of office space, recently attracting companies such as Netflix and Uber. Recently, the Royal Bank of Scotland announced it was in discussions with the Dutch central bank to use Amsterdam as its EU trading base once the U.K. bids farewell.

Amsterdam will have become the new home of the EU's Medicines Agency by the time the U.K. leaves, bringing a significant number of jobs with it. EMA's new headquarters has yet to be built, but Amsterdam has proposed a 19-floor office, which should support the construction sector. But while financial firms are attracted to the metropolitan area, investment banks have been less interested because of the country's cap on bonuses for workers in financial services. More financial services moving in would spark employment in this sector, which has steadily declined since 2005 in the wake of the struggling insurance industry.

Fragile coalition

The re-election of Mark Rutte's conservative-liberal VVD party in March removed key political risks to financial markets and calmed investors. Almost seven months after the election, Rutte and the VVD have formed a new four-party coalition—the longest time to form a new government in modern Dutch history. The VVD joined with the pro-EU CDA and D66 parties, each with 19 seats in parliament, as well as the Christian Union. The new coalition will hold 76 out of 150 seats, but the new government has a difficult road ahead: While the VVD, CDA and D66 parties are pro-EU, the Christian Union had previously campaigned for a north-south breakup of the single-currency union.

ASIA PACIFIC

By Katrina Ell of Moody's Analytics
December 21, 2017

This year kept us on our toes. There wasn't one particular trend or event in 2017 that dominated, but rather a multitude of often unrelated issues brought ructions, upswings, and persistent downside risks to the 2018 outlook.

Upswing in global tech cycle

The sustained upswing in the global tech cycle took us by surprise and was a welcome development given the significant lift it provided to manufacturers and exporters across the region. Tech exporters such as Japan, South Korea, Taiwan and Malaysia enjoyed lofty gains in their tech sectors that provided a sizeable spillover to the broader economy.

South Korea's export performance is a good barometer of the global tech cycle, given its outsize exposure. South Korea represents around 6% of global electronics production. During 2017, annual export growth averaged an impressive 14% y/y.

Taiwan is a relatively small, export-oriented economy at the whim of global demand and of tech in particular. Taiwan's export-oriented sectors have done swimmingly through 2017. Despite government efforts over the years to shift manufacturing into higher-value-added segments, electronics remain the bulk of Taiwan's manufacturing. Electronics represent around 20% of Taiwan's GDP and about half of all exports.

Benefits to Malaysia from the upswing in global tech demand were clear; third quarter GDP growth reached a three-year high at 6.2% y/y. Exports rose an impressive 12% y/y in the third stanza. Malaysia isn't historically known for its tech sector but its integrated circuit sector accounts for around 30% of exports and a sizeable share of manufacturing.

China's Congress

All eyes were on China's 19th Communist Party Congress mid-October, to watch closely for clues on policy priorities and who will be the next set of leaders. At the once-every-five-year event, President Xi Jinping consolidated his power and cemented himself as China's leader for a generation rather than a decade. With no successor announced, Xi will likely remain at the helm beyond 2022. His name and ideologies have been included in the Communist Party constitution during his reign, putting him alongside Communist China founder Mao Zedong. Xi filled the seven-member Politburo Standing Committee and 25-member Politburo with long-term loyalists.

At the outset of the congress it was assumed that reforms would play a more important role. But that appears to be a secondary priority to elevating China's position on the international stage and filling the void left as other global powers turn inward. During his opening address, Xi described China as a "great power" or "strong power" 26 times. This is a significant shift from past leaders, who tended to downplay China's global influence, characterizing China as a more timorous player offshore.

The Belt and Road Initiative is an important vehicle for China to expand its reach offshore and is arguably Xi's signature international policy. Closer ties to China in the form of increased investment and development assistance could tie some countries in the region to China. For example the Philippines under President Rodrigo Duterte has already swung away from the U.S. towards China, with China committing billions of dollars of investment in the Philippines, mostly for infrastructure development. It is a similar situation in less-developed ASEAN countries such as Cambodia, Laos and Myanmar.

The bottom line is that a multitude of developing economies require significant infrastructure development, and China is responding with billions in investment. For instance in 2016, ASEAN won approximately US$30 billion in Chinese investment/contracts. Although this a boost for growth, it undermines ASEAN's bargaining power geopolitically, such as on the South China Sea.

Another takeaway from the congress was that the Communist Party will play a more prominent role in economic activity. The party has supposedly gained the credibility to do this via its far-reaching anti-graft campaign that has coincidentally purged Xi rivals.

Beyond the bravado, Xi has his work cut out for him. Steering the economy through a transition away from exports and manufacturing, the traditional backbone of the economy, towards greater consumption is no mean feat. This is to occur while managing the pockets of worryingly high debt, chronic overcapacity in some state-owned enterprises, an aging population, and slowing GDP growth. Being a greater influence internationally means China can't turn a blind eye to issues such as North Korean antagonism as it has in the past.

North Korea posed elevated downside risks

International abhorrence with North Korea escalated over 2017 as the rogue nation has increased the frequency of its weapons testing. North Korea has long been a reprobate given its unrelenting desire to build a nuclear weapons program and maintain a dictatorship, led by the unpredictable Kim Jong-un. The risk that North Korea poses to global peace is higher than in the past. Increasingly severe sanctions have not been enough to dissuade North Korea from defiance of United Nations resolutions, which the state has developed a sophisticated network to circumvent.

The economic implications of North Korea's actions remain minimal. It's presumed that South Korean households would be amongst the most sensitive to the escalated tensions, but consumer confidence remains comfortably optimistic. The Bank of Korea's consumer sentiment index has averaged 110.2 in the past six months to November, comfortably above the neutral 100. Elsewhere, Japanese households appear preoccupied with local politics following the comfortable victory of incumbent Shinzo Abe at the general elections in October, with consumer sentiment hovering around a four-year high.

The toughest economic sanctions on North Korea to date were imposed by the U.N. Security Council in the third quarter. The sanctions approved on 5 August and 11 September involved the most far-reaching and adverse economic consequences ever inflicted upon the rogue state. This includes banning critical North Korean exports, including textiles, coal, iron ore and seafood, from reaching all trading partners. Anecdotes suggest China is adhering to these sanctions like never before.

China is an important ingredient to disrupting the status quo in North Korea given it is the state's largest trading partner. Estimates suggest China accounts for around 80% of North Korea's trade and 90% of foreign direct investment. It is significant that China is now exerting pressure on Pyongyang. The North Korean regime is not infinitely adaptable and while it has found a multitude of ways to circumvent sanctions, a complete Chinese shutdown of trade would likely bring the rogue state to its knees. China has so far steered clear of this route and has instead chosen to exert influence but keep reduced trade routes functioning.

Increased geopolitical risk does not automatically translate to weaker or more volatile financial markets. Though financial markets have been jittery following specific military tests from the North and harsh rhetoric from the international community, there has not been a more medium-term impact. A measure of Kospi 200 volatility has been relatively calm in general this year, compared with its five-year average, despite temporary spikes.

Return to frugality in Japan

Japan has enjoyed a stellar run through 2017. The economy has had seven consecutive quarters of uninterrupted growth, its longest run since early 2001. A positive output gap emerged late in 2016 and has stuck around through 2017. Prior to this, Japan's output gap has mostly been negative since the asset price bubble burst in the early 1990s, except for a few short periods. This reflects the economy's perennial battle with deflation and dismal economic growth. We forecast Japan's GDP growth will hit 1.5% in 2017, above potential, which we estimate is around 1%.

The year started out promising for Japanese consumption, which emerged as the main economic driver but soon faded. Exports returned as the economy's backbone by the second half, since meaningful improvements in wage growth couldn't be sustained. A sustainable recovery in private consumption is critical to turning the economy's fate around, and we are not there yet. Solid exports and export-oriented manufacturing helped by the global tech upswing and strong offshore demand for autos, alongside a weak yen, have mostly offset a recurrence of weakness in domestic demand in the second half.

India has had it rough

India's economy is rarely correlated with regional economic cycles, and this year was no different. While much of region was expanding around potential, India struggled. The ill effects of 2016's demonetization, which caused sentiment to fall and disrupt activity, hurt 2017's economic performance.

An added drag was from the introduction of the convoluted goods and services tax on 1 July. Unlike the GST in other countries, where a single tax rate is applied to all goods and services, India's GST has four tax rates: 5%, 12%, 18% and 28%. Which products fall into which broad categories is confusing, making it harder for businesses to appropriately implement the tax and for authorities to police it. 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%.

Below-average rainfall during the monsoon season didn't help matters and could add to inflation in 2018. Ultimately the level of pass-through to consumer prices will determine the monetary policy path. However, on balance, 2018 is looking healthier for India as the disruption from demonetisation and the GST introduction fade.

Bitcoin regulation

Bitcoin mania erupted in 2017. Interest in cryptocurrencies, in particular bitcoin coincided with incredible price gains, concentrated in the second half. This is more a global event, but the response from Asia's regulators is worth mentioning. We think that the ultimate fate of bitcoin will rest on regulators' response to the cryptocurrency, which in theory operates outside of any central control.

While bitcoin was by far the world's best-performing currency in 2017, its relatively extreme volatility in recent history cannot be overlooked. Over the past four years, it has been either the best- or the worst-performing currency against the greenback.

Bitcoin could pose serious threats to financial stability if not properly regulated, given the influx of investors into the asset class in 2017. It's a risk that households and other local investors could keep piling into this speculative asset, potentially driving the price even higher over a short period of time and bringing significant risks to financial stability. Regulation is a sensible path given the increasing exposure of investors to bitcoin.

Japan began officially recognizing bitcoin as a legal form of payment on 1 April, but China has gone down the opposite path. Beijing has never seemed a fan of bitcoin, and its actions through September have cemented this view. Bitcoin prices slumped by 13% in mid-September after one of the largest exchanges in China, BTCChina, announced it was closing its operations by 30 September in response to action from Chinese authorities. Chinese regulators have banned firms from raising money through initial coin offerings, referring to them as unauthorized fund-raising tools. The effect of local Chinese regulation on the bitcoin price confirms that national regulators still have the power to influence currency prices and trading volumes, even when a financial intermediary is not required.

The exact motivation behind Chinese regulators' bid to quell cryptocurrency trading is unclear. A sensible explanation is that bitcoin trading in China has boomed and investors and speculators have driven the price significantly higher over a short time, so regulators are trying to manage the potential financial risks, given households' rising exposure to this market. Another possibility is that bitcoin by its nature is out of the purview of Chinese authorities, undesirable for an economy that is so tightly regulated; unfettered access to the internet is still unachievable.

The Korean financial regulator is moving toward controlling transactions of decentralized virtual currencies, including bitcoin. Early December, the Korean government established a taskforce to investigate methods of regulating and trading cryptocurrencies, a major shift from its earlier stance that it had no plans to regulate the market. It has reportedly considered investor-protection mechanisms and trading bans on financial institutions, minors and foreigners.

Similarly, Bank Indonesia on 7 December prohibited cryptocurrencies from being used for payments. Deputy Governor Sugeng noted: "virtual currencies have a weak foundation are highly volatile [and may] pose negative impacts on our economy."

Ratings Round-Up

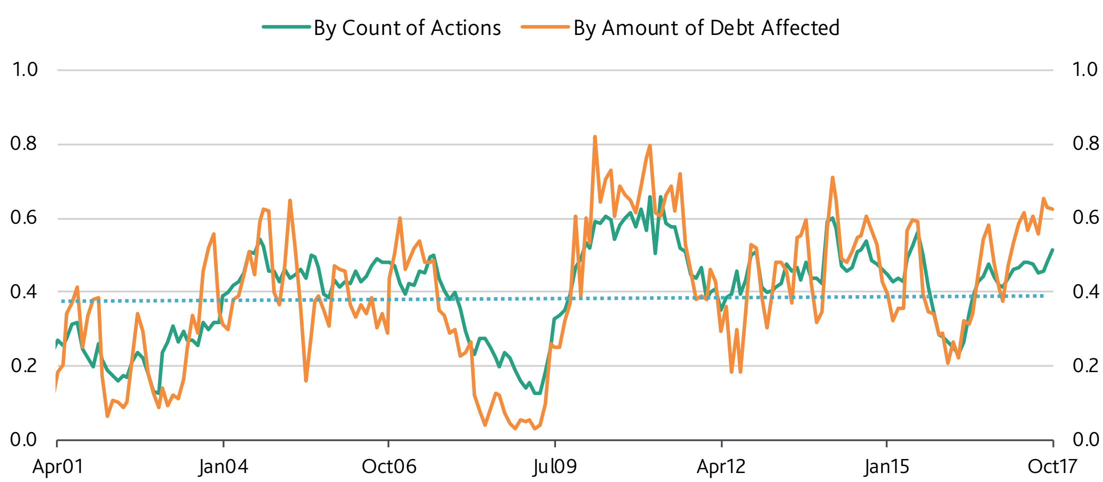
By Njundu Sanneh

Positive Rating Changes on the Rebound

The weekly rating changes for the past week numbered 20 with the spoils divided evenly between the U.S. and Europe. Positive rating changes after have slowly climbed from the low numbers they registered over the past several weeks and are on par with in count with downgrades. The US contribution rate for positive rating changes was 60% compared to 33% and 29% in the weeks prior. Some of the noteworthy names driving positive rating changes in the US include US subsidiaries of the German automotive parts company ZF Friedrichshafen AG, 99 Cents Only Stores, and NCI building systems, Inc. On the downgrade side we have DDR Corp., Tom Shoes and Charlotte Ruse Holdings Inc. In Europe financial company rating revisions were at the fore with four Polish banks and another two from Azerbaijan. Financial companies accounted for a total of seven out of the total 10 rating changes. The improved contribution rate in the positive rating changes over the past several weeks is more in line with the strong corporate credit market with speculative grade spreads in favorable territory.

FIGURE 1

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



* Trailing 3-month average

Source: Moody's

Ratings Round-Up

FIGURE 2

Rating Key

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

FIGURE 3

Rating Changes: Corporate & Financial Institutions – US

Date	Company	Sector	Rating	Amount ($ Million)	Up/ Down	Old LTD Rating	New LTD Rating	IG/ SG
12/13/17	BANCO SANTANDER S.A. (SPAIN) - Banco Santander Puerto Rico	Financial	SrUnsec/LTD	700	U	Baa2	Baa1	IG
12/14/17	DEALER TIRE, LLC	Industrial	SrSec/BCF/LTCFR/PDR		U	B2	B1	SG
12/14/17	TOMS SHOES, LLC	Industrial	SrSec/BCF/LTCFR		D	Caa2	Caa3	SG
12/14/17	TRIBE BUYER LLC	Industrial	SrSec/BCF		D	B1	B2	SG
12/15/17	CHARLOTTE RUSSE HOLDING INC. - Charlotte Russe, Inc.	Industrial	LTCFR/PDR		D	Caa1	Ca	SG
12/15/17	DDR CORP.	Financial	SrUnsec/Sub/MTN/PS	3,282	D	Baa2	Baa3	IG
12/15/17	IBERDROLA S.A.	Industrial	LTIR/SrSec	130	U	Baa1	A3	IG
12/19/17	99 CENTS ONLY STORES LLC	Industrial	PDR	250	U	Ca	Caa1	SG
12/19/17	NCI BUILDING SYSTEMS, INC.	Industrial	SrUnsec/srSec/BCF/LTCFr/PDR	250	U	B3	B1	SG
12/19/17	ZF FRIEDRICHSHAFEN AG	Industrial	SrUnsec	5,466	U	Ba1	Baa3	SG

Source: Moody's

FIGURE 4

Rating Changes: Corporate & Financial Institutions – Europe

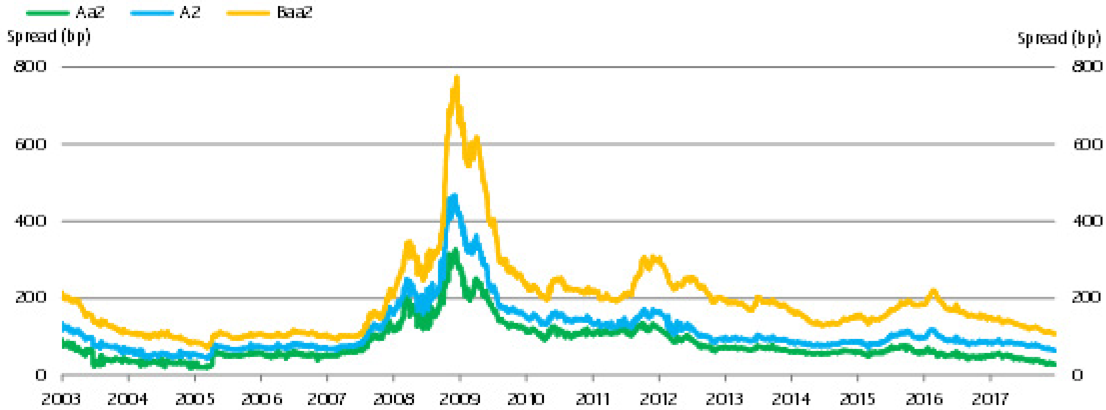
Date	Company	Sector	Rating	Amount ($ Million)	Up/ Down	Old LTD Rating	New LTD Rating	Old STD Rating	New STD Rating	IG/ SG	Country
12/19/17	JOINT STOCK COMMERCIAL BANK RESPUBLIKA	Financial	LTD		D	B3	Caa1			SG	AZERBAIJAN
12/19/17	OJSC BANK OF BAKU	Financial	LTD	225	D	Caa1	Caa3			SG	AZERBAIJAN
12/13/17	SOCIETE DES AUTOROUTES PARIS-RHIN-RHONE - APRR	Industrial	SrUnsec/MTN	1,235	U	Baa2	Baa1			IG	FRANCE
12/18/17	EXPRO HOLDINGS UK 3 LIMITED	Industrial	SrSec/BCF/LTCFR/PDR		D	Caa1	C				LUXEMBOURG
12/14/17	GETIN NOBLE BANK S.A.	Financial	LTD		D	Ba2	Ba3			SG	POLAND
12/19/17	BANCO COMERCIAL PORTUGUES, S.A. - Bank Millennium S.A.	Financial	SLTD		U	Ba1	Baa3	NP	P-3	SG	POLAND
12/19/17	BNP PARIBAS - Bank BGZ BNP Paribas S.A.	Financial	LTD		U	Baa2	Baa1			IG	POLAND
12/19/17	COMMERZBANK AG - mBank S.A.	Financial	LTD		U	Baa2	Baa1			IG	POLAND
12/15/17	TURKIYE HALK BANKASI A.S.	Financial	SrUnsec/LTD/Sub	2,750	D	Ba1	Ba2			SG	TURKEY
12/18/17	BRIGHTHOUSE GROUP PLC	Industrial	SrSec/PDR	293	D	Caa2	Ca			SG	UNITED KINGDOM

Source: Moody's

Market Data

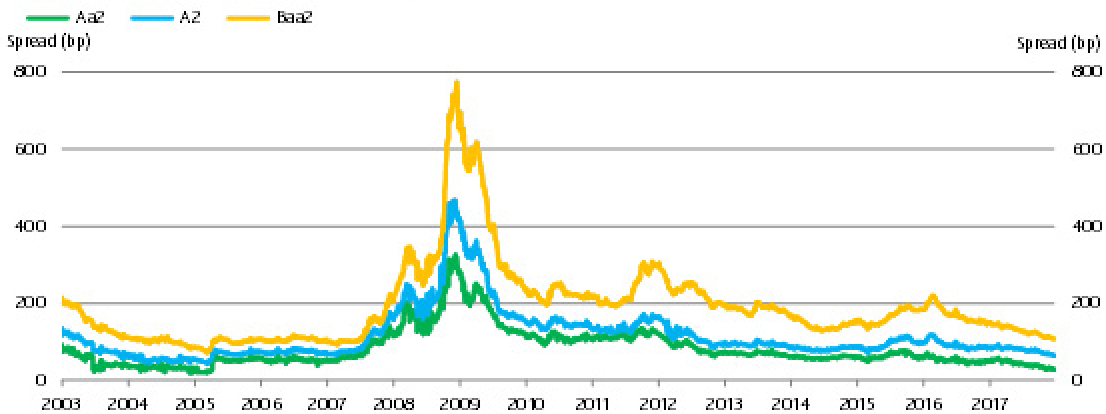
Spreads

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



Source: Moody's

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


Source: Moody's

Market Data

CDS Movers

Figure 3. CDS Movers - US (December 13, 2017 – December 20, 2017)

CDS Implied Rating Rises	CDS Implied Ratings		
Issuer	Dec. 20	Dec. 13	Senior Ratings
Monsanto Company	A1	Baa2	A3
21st Century Fox America, Inc	Aa2	A1	Baa1
JPMorgan Chase & Co.	A2	A3	A3
Bank of America Corporation	A2	A3	A3
Bank of America, N.A.	A1	A2	Aa3
Oracle Corporation	A2	A3	A1
Walt Disney Company (The)	A1	A2	A2
General Electric Company	A3	Baa1	A2
Aetna Inc.	A1	A2	Baa2
Chevron Corporation	Aa3	A1	Aa2

CDS Implied Rating Declines	CDS Implied Ratings		
Issuer	Dec. 20	Dec. 13	Senior Ratings
Campbell Soup Company	Baa1	A2	A3
Morgan Stanley	Baa2	Baa1	A3
Verizon Communications Inc.	Baa3	Baa2	Baa1
Coca-Cola Company (The)	Aa2	Aa1	Aa3
PepsiCo, Inc.	A1	Aa3	A1
United Technologies Corporation	A1	Aa3	A3
Abbott Laboratories	Baa1	A3	Baa3
Time Warner Inc.	Baa1	A3	Baa2
U.S. Bancorp	Aa2	Aa1	A1
Medtronic, Inc.	Aa2	Aa1	A3

CDS Spread Increases		CDS Spreads		
Issuer	Senior Ratings	Dec. 20	Dec. 13	Spread Diff
K. Hovnanian Enterprises, Inc.	Caa3	2,789	2,347	442
Frontier Communications Corporation	B3	1,810	1,539	271
MBIA Insurance Corporation	Caa2	1,248	1,117	132
Windstream Services, LLC	B3	2,056	1,996	60
Mattel, Inc.	Ba2	384	335	49
Calpine Corporation	B2	327	304	23
Dish DBS Corporation	Ba3	391	369	22
Chesapeake Energy Corporation	Caa1	729	709	20
NRG Energy, Inc.	B1	206	188	18
Penney (J.C.) Corporation, Inc.	B3	1,206	1,190	17

CDS Spread Decreases		CDS Spreads		
Issuer	Senior Ratings	Dec. 20	Dec. 13	Spread Diff
Nine West Holdings, Inc.	Ca	14,079	15,497	-1,418
Sears Roebuck Acceptance Corp.	Ca	3,292	3,387	-95
Sears Holdings Corp.	Ca	2,928	3,013	-85
Neiman Marcus Group LTD LLC	Caa3	1,384	1,432	-49
Avon Products, Inc.	B3	949	979	-29
DDR Corp.	Baa3	150	178	-28
Tenet Healthcare Corporation	Caa1	582	608	-26
Monsanto Company	A3	35	61	-26
AK Steel Corporation	B3	351	370	-19
Pride International, Inc.	B2	461	480	-19

Source: Moody's CMA

Market Data

Figure 4. CDS Movers - Europe (December 13, 2017 – December 20, 2017)

CDS Implied Rating Rises	CDS Implied Ratings		
Issuer	Dec. 20	Dec. 13	Senior Ratings
Portugal, Government of	Ba1	Ba2	Ba1
CaixaBank, S.A.	Baa2	Baa3	Baa2
ING Groep N.V.	Aa3	A1	Baa1
National Grid Gas Plc	A2	A3	A3
Old Mutual Plc	Aa2	Aa3	Ba1
Italy, Government of	Ba2	Ba2	Baa2
United Kingdom, Government of	Aa1	Aa1	Aa2
Germany, Government of	Aaa	Aaa	Aaa
Spain, Government of	Baa2	Baa2	Baa2
Belgium, Government of	Aaa	Aaa	Aa3

CDS Implied Rating Declines	CDS Implied Ratings		
Issuer	Dec. 20	Dec. 13	Senior Ratings
SEB	A1	Aa2	Aa3
France, Government of	Aa1	Aaa	Aa2
Lloyds Bank Plc	A1	Aa3	Aa3
Nordea Bank AB	Aa2	Aa1	Aa3
Banco Santander S.A. (Spain)	Aa3	Aa2	Baa1
Bayerische Landesbank	Aa3	Aa2	A1
Landesbank Baden-Wuerttemberg	A3	A2	A1
UniCredit Bank AG	Baa2	Baa1	Baa2
ENEL S.p.A.	Baa2	Baa1	Baa2
Raiffeisen Bank International AG	Baa3	Baa2	A3

CDS Spread Increases		CDS Spreads		
Issuer	Senior Ratings	Dec. 20	Dec. 13	Spread Diff
Galapagos Holding S.A.	Caa2	942	912	30
Boparan Finance plc	B3	752	729	23
Unione di Banche Italiane S.p.A.	Baa3	112	97	16
Altice Finco S.A.	B3	412	398	14
PizzaExpress Financing 1 plc	Caa1	796	785	11
CMA CGM S.A.	B3	369	359	10
Stonegate Pub Company Financing plc	Caa1	224	213	10
Novafives S.A.S.	B3	112	106	6
Nordea Bank AB	Aa3	29	24	5
Bayerische Landesbank	A1	32	28	5

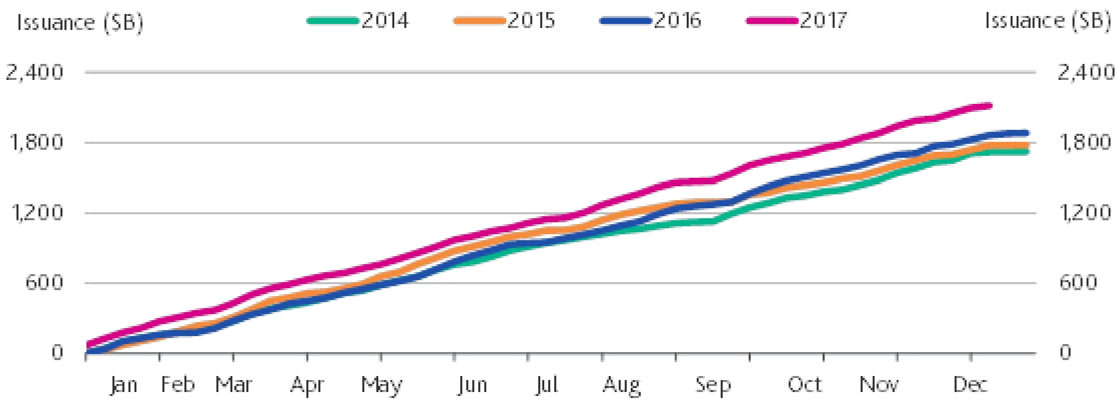
CDS Spread Decreases		CDS Spreads		
Issuer	Senior Ratings	Dec. 20	Dec. 13	Spread Diff
Astaldi S.p.A.	B3	2,570	2,759	-190
Greece, Government of	Caa2	350	379	-29
Ensco plc	B3	471	489	-19
Portugal, Government of	Ba1	92	106	-14
CaixaBank, S.A.	Baa2	57	65	-8
Vedanta Resources plc	B2	401	408	-7
Old Mutual Plc	Ba1	26	33	-7
Fiat Chrysler Automobiles N.V.	B1	155	161	-6
Evraz Group S.A.	B1	245	251	-6
Storebrand ASA	Ba1	183	189	-6

Source: Moody's, CMA

Market Data

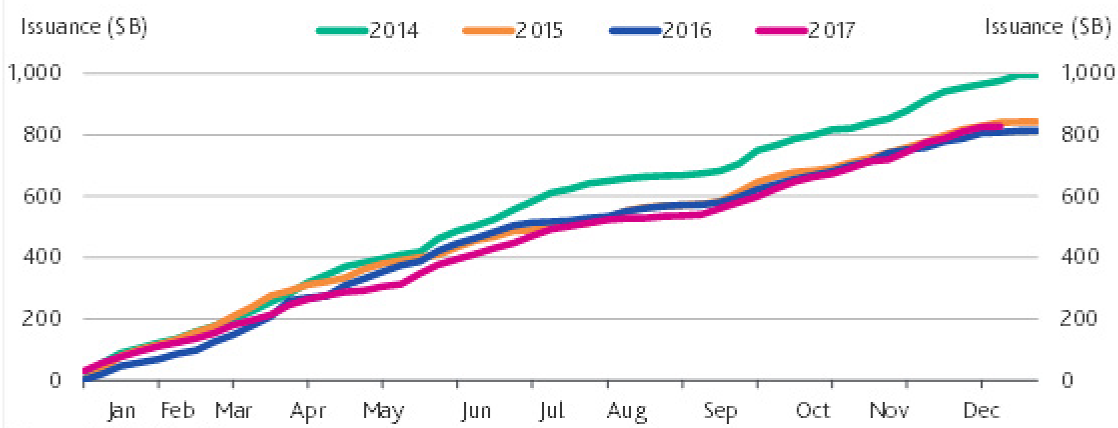
Issuance

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



Source: Moody's / Dealogic

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



Source: Moody's/ Dealogic

Market Data

Figure 7. Issuance: Corporate & Financial Institutions

	USD Denominated		
	Investment-Grade	High-Yield	Total*
	Amount $B	Amount $B	Amount $B
Weekly	10.292	6.180	19.972
Year-to-Date	1,502.553	450.597	2,116.259

	Euro Denominated		
	Investment-Grade	High-Yield	Total*
	Amount $B	Amount $B	Amount $B
Weekly	0.265	1.529	2.276
Year-to-Date	665.649	115.775	827.838

* Difference represents issuance with pending ratings.

Source: Moody's/ Dealogic

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