MOODY'S ANALYTICS

WEEKLY MARKET OUTLOOK

The Least Inaccurate Forecaster

Moody's Capital Markets Research

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Credit Markets Review and Outlook

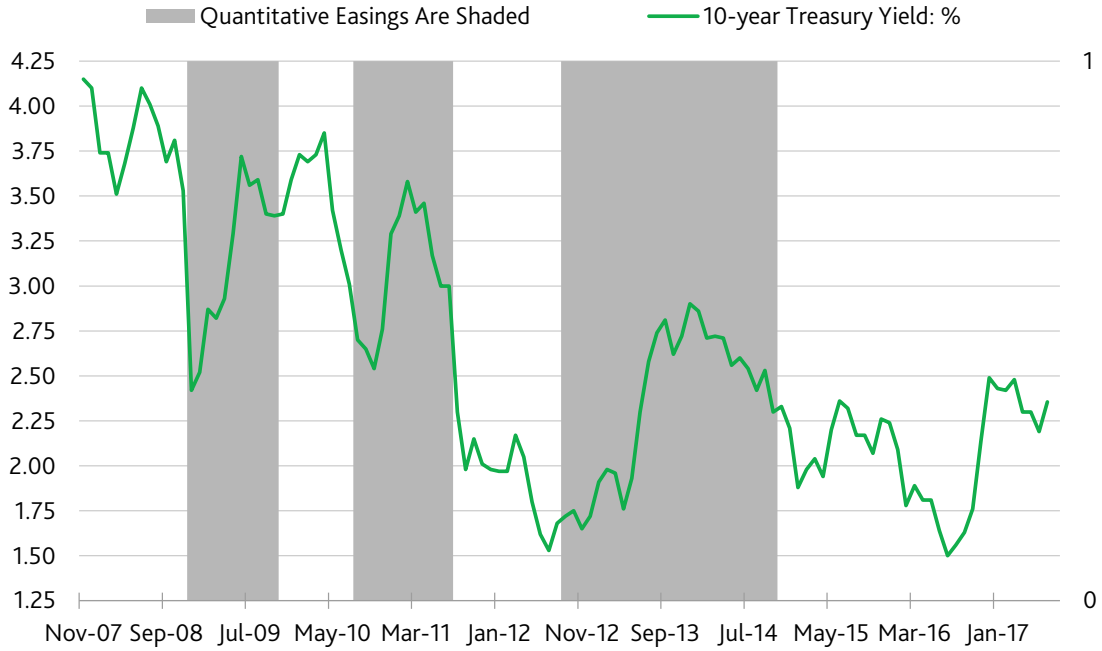
By John Lonski, Chief Economist, Moody's Capital Markets Research, Inc.

The Least Inaccurate Forecaster

The forthcoming passive reduction of the Fed's bond holdings may not be followed by higher Treasury bond yields. So suggests what came after October 2014's end to the third installment of quantitative easing (QE3). In fact, since the October 2014 expiry of QE3, the average 10-year Treasury of 2.07% has been less than its 2.30% average of October 2014, never mind its "taper tantrum" average of 2.71%.

In anticipation of a winding down of QE3, towards the end of June 2013 the 10-year Treasury yield began to climb higher. The mere anticipation of fewer purchases of bonds by the Fed drove the 10-year Treasury yield up from its 1.82% average during the 12-months-ended June 2013 to the 2.71% average of the next 12-months-ended June 2014. Within the latter span, the 10-year Treasury yield's month-long average peaked at December 2013's now six-year high of 2.90%. (Figure 1.)

Figure 1: 10-year US Treasury Yield Tended To Rise In Anticipation of An End to Fed Bond Purchases and Then Fall After Such Stimulus Was Removed



Forecasters grossly overestimated the impact of QE3's demise

On balance, professional prognosticators badly overestimated what was to become of Treasury bond yields following the conclusion of QE3. Thus, it would not be surprising if both the market and forecasters now overestimate the likely path of benchmark interest rates once the Fed allows its bond holdings to gradually shrink via the partial reinvestment of maturing securities.

In response to the winding down of QE3, October 2014's Blue Chip consensus survey projected a 2.7% average for Q4-2014's 10-year Treasury yield that would be followed by a 3.2% average for yearlong 2015, including a 3.5% average for 2015's final quarter. The lowest 10 projections — the bottom quintile — of the consensus's roughly 50 forecasts projected a 2.5% 10-year Treasury yield for Q4-2014 followed by a 2.8% average for 2015 that included a 3.0% average for Q4-2015.

Much to the contrary of the consensus view, but less so for the expectations of the bottom quintile, the 10-year Treasury yield actually posted unexpectedly low averages of 2.28% for Q4-2014, 2.14% for yearlong 2015, and 2.19% for Q4-2015.

In part, the consensus outlook for 2015's 10-year Treasury yield proved to be far too high because of an overestimation of 2015's annual growth rates for real and nominal GDP. Yearlong 2015's actual 2.6%

increase by real GDP was slower than the 3.1% projected by the consensus, while the accompanying 3.7% rise by nominal GDP showed an even deeper shortfall compared to the expected 5.0%.

Though the bottom quintile was spot on with a real GDP growth forecast of 2.6%, its predicted 4.3% increase by nominal GDP was a bit too high. The latter miss brings attention to how the bottom quintile was not immune to the tendency to overestimate price inflation.

The recent Blue Chip consensus outlook for 2018 calls for gains of 2.4% by real GDP and 4.4% by nominal GDP. In turn, the consensus expects the 10-year Treasury yield to average 3.0% for the entirety of 2018, including a 3.2% average for Q4-2018. Thus, the consensus expects a 9.5-year old economic recovery to be lively enough to lift the 10-year Treasury yield up by roughly 85 bp from its latest 2.35%.

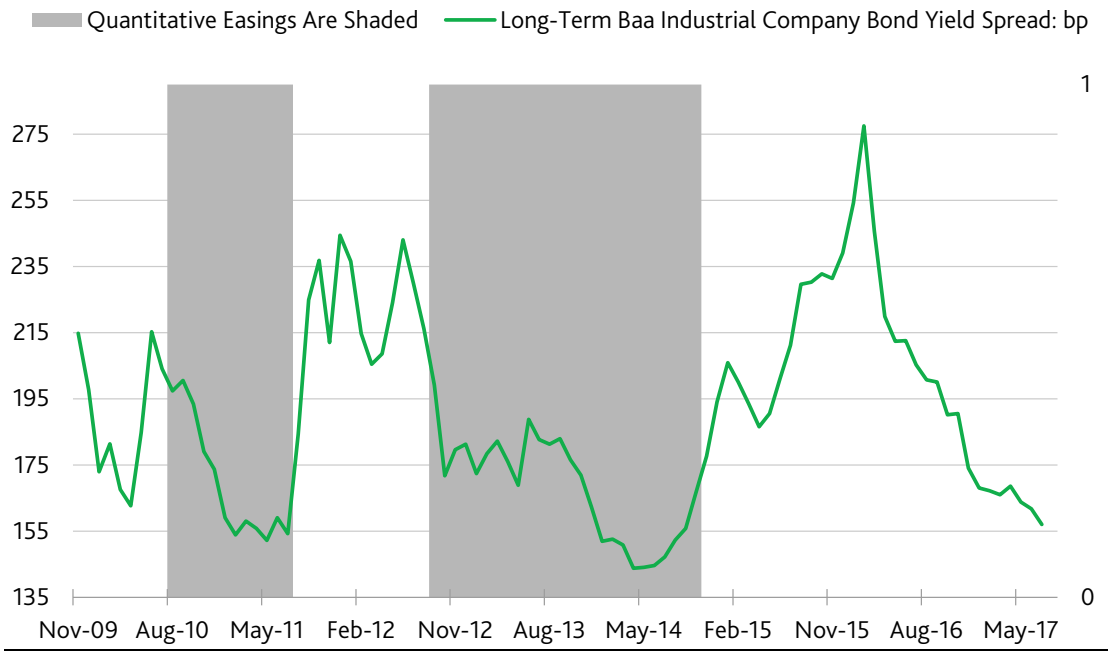
However, if the 10-year Treasury yield jumps up by 85 bp without a sufficient acceleration of business activity, equity prices will tumble, corporate bond yield spreads will swell, and recession risk will rise materially. In turn, the 10-year Treasury yield would eventually undergo a correction and sink well under 3%. Treasury bond yields cannot be divorced from the underlying pace of business activity indefinitely.

As inferred from the still subpar growth rates of business sales and pretax operating profits, July 2017's bottom quintile is likely to again be more accurate than the consensus regarding projections for 2018. The bottom quintile's latest forecasts for yearlong 2018 are 2.0% for real GDP growth, 3.9% for nominal GDP growth, and 2.5% for the 10-year Treasury yield, where the latter includes a 2.7% yield for Q4-2018.

Corporate bond yield spreads widened during the exit and aftermath of QE2 and QE3

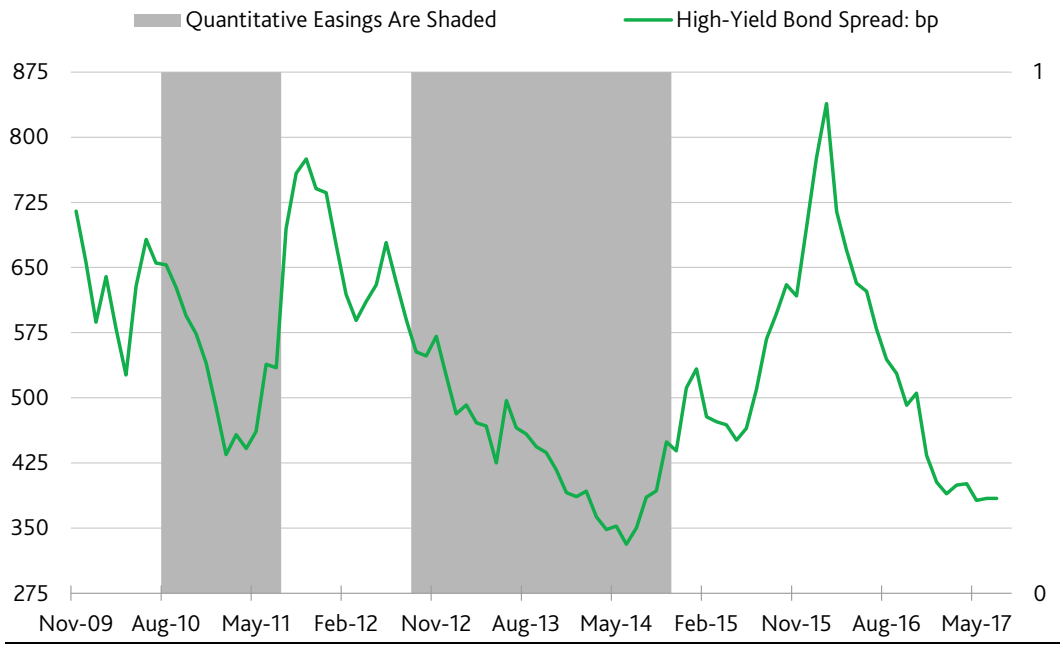
The approaching end of quantitative easing and its immediate aftermath have not been kind to the spreads of Baa-rated and high-yield corporate bonds. Since July 2010, long-term Baa industrial company bonds showed medians of 170 bp during months corresponding to QE2 and QE3 and 207 bp otherwise. (Figure 2.)

Figure 2: Long-Term Baa Bond Yield Spread Has Widened Near the End of and During the Immediate Aftermath of Quantitative Easing



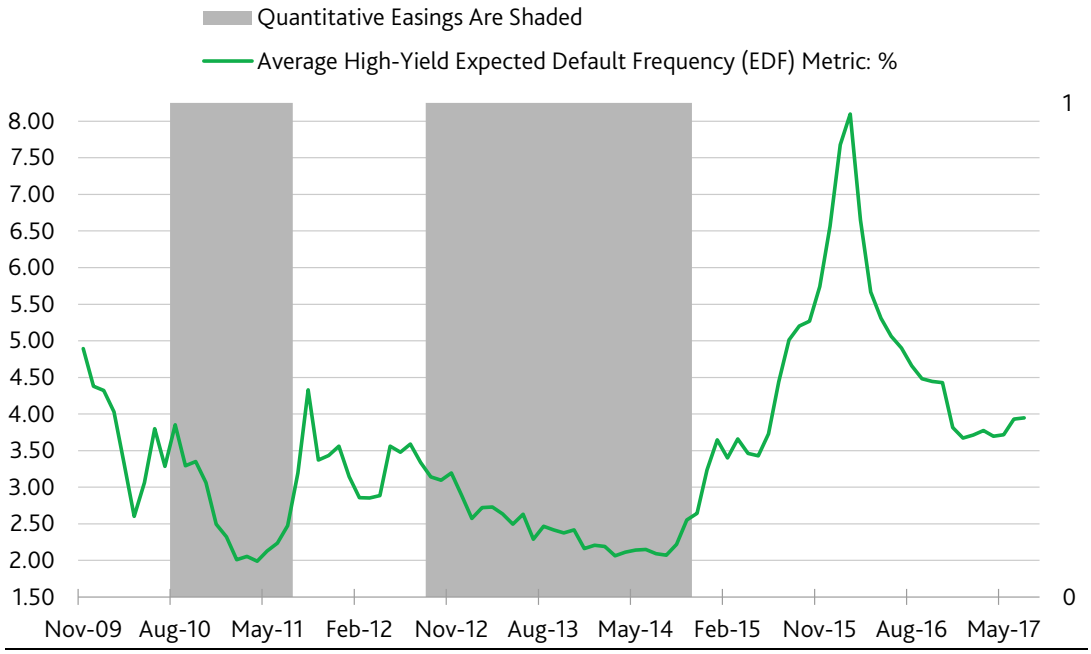
A composite high-yield bond spread shows a surprisingly high correlation of 0.93 with the Baa industrial company spread since 1989. For high-yield bonds, the difference in spreads widened from the 460 bp of the months overlapping QE2 and QE3 to the 584 bp for all other months since July 2010. (Figure 3.)

Figure 3: High-Yield Bond Spreads Widened Towards the End of and Following QE2 and QE3



The average expected default frequency (EDF) metric of US/Canadian high-yield issuers quantifies market-wide default risk on a daily basis. The average high-yield EDF shows statistically meaningful correlations of 0.63 with the Baa industrial spread and 0.75 with the high-yield spread. The behavior of the Baa and high-yield bond spreads since July 2010 is consistent with the increase by the average high-yield EDF (expected default frequency) metric from its 2.5% average amid quantitative easing and 4.2% otherwise. (Figure 4.)

Figure 4: Since October 2009, High-Yield EDF Averaged 2.5% Amid Quantitative Easing and 4.2% Otherwise



Compared to the average EDF, the median high-yield EDF metric is better insulated from biases stemming from the influence of just several troubled industries. In order to insulate overall default risk from the excessive influence of several industries, the median high-yield EDF metric still increased from a 0.40% median amid QE2 and QE3 to 0.55% otherwise.

Credit Markets Review and Outlook

Systemic liquidity may become less plentiful as the Fed withdraws stimulus

Perhaps an abundance of financial liquidity explains why both estimated default risk and medium- to lower-grade yield spreads were significantly lower when QE2 and QE3 were in effect. The greater median 1.9% monthly increase by the market value of US common stock amid quantitative easing versus 1.1% for all other months since July 2010 complements the view that QE2 and QE3 enhanced systemic liquidity significantly. In a manner that is consistent with the improved price performance by equities when the Fed enlarges its balance sheet, the VIX index's median rises from 15.3 points under QE2 and QE3 to 15.9 points otherwise.

Fundamentals ultimately determine the correct price for bonds

The Treasury bond market currently engages in a classic example of "price search", where the market attempts to ascertain the likely range for benchmark Treasury yields once the Fed begins to passively shrink its bond holdings. The current pricing activity of Treasury bonds resembles that of the "taper tantrum", when Treasury yields temporarily soared in anticipation of a tapering of the QE3 episode of Fed bond buying.

Earnings-sensitive financial markets fear an upturn by Treasury yields that exceeds what is warranted by fundamentals. The recent climb by the 10-year Treasury yield occurred despite recent slowdowns by consumer price inflation both with and excluding food and energy prices, as well as expectations of only a modest pace for consumer spending. The Fed's beige book for June specifically cited a softening of consumer spending, especially for autos.

Because of the seemingly intractable impediments to both tax reform and increased infrastructure spending, a fundamentally excessive climb by interest rates must be avoided. Currently, growth in home sales compensates for a contraction by unit sales of cars and light trucks. Prospects would worsen if home sales and auto sales were to shrink simultaneously.

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 14: Financial markets interpreted Fed Chair Janet Yellen's testimony before Congress as dovish and investors may be focused on her comment that because the neutral rate is low by historical standards, the federal funds rate would not have to rise much higher to get to a neutral policy stance. In other words, monetary policy is still accommodative, but it will become neutral after a few more rate hikes. We don't believe Yellen is signaling that the tightening cycle is nearing an end. Rather, the path of the fed funds rate will be determined by changes in the equilibrium rate, which should rise as some of the headwinds that have depressed it over the past several years lift.

The marked decline in the neutral federal funds rate may be partially attributable to a range of persistent economic headwinds that have weighed on aggregate demand. These include tighter underwriting standards and limited access to credit for some borrowers, household deleveraging, contractionary fiscal policy, weak growth abroad coupled with a significant dollar appreciation, slower productivity and labor force growth, and elevated economic uncertainty. Although many of these headwinds have declined noticeably over the past few years, some have remained significant. As they abate, the neutral federal funds rate should gradually rise over time.

A higher neutral fed funds rate would require additional rate hikes, supporting our interpretation of Yellen's comments Wednesday that nothing has changed in her expected path of the fed funds rate and that the Fed will continue to raise interest rates. We are sticking with our forecast of an announcement on the balance sheet in September followed by a rate hike in December.

The upcoming week is fairly light on the economic data front. We look for the first two regional manufacturing surveys to weaken modestly in July. These surveys will provide guidance on how non-auto manufacturing is doing early this quarter. Auto manufacturing will struggle in July as production schedules point toward a large decline in production because of auto retooling. The housing data will look a little better, since we expect homebuilder confidence to have edged higher in July. We look for housing starts to have rebounded in June after falling sharply in May.

FRIDAY, JULY 14

CPI (June; 8:30 a.m. EDT)

Forecast: 0% (headline) Forecast: 0.2% (core)
The consumer price index is forecast to have been unchanged in June following a 0.1% decline in May and a 0.2% increase in April. The Fed can shrug off a poor month of inflation, but a trend is beginning to emerge. The CPI will have been unchanged, on average, over the past three months and up 0.1% per month since the beginning of the year.

Oil and gasoline prices fell in June and we believe this will be a drag on the headline CPI. Food prices have firmed recently and we look for a trend-like 0.2% gain in June. The core CPI, which excludes food and energy, is expected to have risen 0.2% in June. Within core, we anticipate trend-like gains in rents. New-vehicle prices were likely unchanged while used-car prices inched higher. Medical care prices have been running soft, but we look for a modest gain in June.

Year-over-year growth in the headline CPI will have decelerated from 2.5% in January to 1.7% in June. This is a notable. Through May, a good chunk of the deceleration was in year-over-year transportation. Also, communication prices have been a drag. Telephone services prices have fallen sharply because of new cellular deals. This drag on core inflation won't be persistent. Medical care prices have also been less supportive and may be attributed to new generic drug launches.

Not all of the drags will lift quickly. For example, rents and owner equivalent rent growth could moderate and would be an issue, since rent has provided an outside contribution to year-over-year

growth in the CPI. Rents are a sizable and sticky component of the CPI. Considering the rental vacancy rate has likely bottomed and additional supply will hit the rental market, rent growth may weaken.

There have been temporary supports to inflation. For example, tobacco and smoking product prices were up 4.2% between March and April, the largest gain since 2009. Prices were little changed in May. Tobacco prices were boosted by the increase in taxes in California—a onetime lift. But tobacco and smoking products have added several basis points to year-over-year growth in the CPI.

We expect the core CPI to have risen 1.8% on a year-ago basis in June.

Retail sales (June; 8:30 a.m. EDT)

Forecast: 0.1% (total)
Forecast: 0.2% (ex autos)
We look for nominal retail sales to have risen 0.1% in June, reversing some of May's 0.3% decline. Unit vehicle sales fell 0.9% in June and this, coupled with aggressive discounting, is expected to hurt nominal spending at automobile and other motor vehicle dealers. Autos are forecast to shave 0.1 percentage point off total retail sales growth in June. We look for better results in the other main categories, save for gasoline. Control retail sales, or total excluding autos, gasoline, building materials and restaurants, are expected to have risen 0.3% in June. Control retail sales were soft in May and we believe some modest payback is due. Retail gasoline prices fell in June, which we expect to shave 0.1 percentage point off total retail sales growth.

June retail sales will help us assess the trajectory of consumer spending heading into the third quarter. Control retail sales were up 2.3% annualized over the prior three months in May, noticeably weaker than that seen at the beginning of the year.

Industrial production (June; 9:15 a.m. EDT)

Forecast: 0.2% (total)
Industrial production was unchanged in May but we anticipate a slight improvement in June. In May, manufacturing output dropped 0.4% following a 1.1% gain in April and a 0.8% decline in March. Manufacturing will remain bumpy over the next few months; there are anecdotes that domestic manufacturers are lengthening the annual retooling process. We believe the retooling will be a bigger issue for manufacturing production in July. For June, the ISM manufacturing survey and hours worked from the employment report showed varying strength. Away from manufacturing, mining production likely increased in June as the sector still benefited from past gains in energy prices. Meanwhile, utilities should be an enormous factor in June, as weather was near seasonal norms. All told, we look for industrial production to have risen 0.2% in June.

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

Forecast: 94.7
The University of Michigan's consumer sentiment index is forecast to have slipped from 95.1 in June to 94.7 in July, according to the preliminary report. There is a clear bias for the preliminary estimate to decline in July, but we expect lower gasoline prices to limit the slide. The Michigan survey is sensitive to gasoline prices, and they continue to buck their normal seasonal pattern and consumers likely have noticed. The labor market is another positive, but it would provide a bigger boost if wage growth was accelerating. We expect the stock market to be a slight drag on sentiment. High-frequency measures of consumer confidence, including the weekly Bloomberg survey, also support a decline in the Michigan survey in early July. The key detail will be long-term inflation expectations, which remain low and there is the risk that they Fed could anchor them there.

MONDAY, JULY 17

Empire State manfuacturing survey (July; 8:30 a.m. EDT)

Forecast: 15.3
We look for the Empire State manufacturing survey's general business conditions index to have fallen from 19.8 in June to 15.3 in July. The index has been bouncing around recently, but there are signs that manufacturing conditions are holding up reasonably well as the euro zone economy is showing signs of improving and the appreciation in the U.S. trade-weighted dollar has moderated. This should provide support to the Empire State index. The annual auto retooling occurs in July and can affect

manufacturing data, since the magnitude of the shutdowns can vary from year to year. We don't believe retooling should affect the Empire State index, as motor vehicle and parts manufacturing is almost nonexistent in New York.

Business confidence (week ending July 14; 10:00 a.m. EDT)

Forecast: N/A

Global business confidence is strong and remarkably stable, as it has been since before last year's U.S. presidential election. Responses to all nine questions in the survey are upbeat. Sentiment is consistent with buoyant global financial markets that have exhibited extraordinarily low volatility in recent months, and with a global economy that is expanding above its potential.

While business confidence is very good, it remains well off its record highs achieved in spring 2015. Moreover, our survey results are not as strong as various other surveys of business and consumer confidence that have strengthened sharply since the presidential election. According to a recent New York Federal Reserve study, sentiment surveys that depend on canvassing new respondents each time are probably somewhat biased as those happy with the election results are more likely to respond. The four-week moving average in our weekly business confidence survey rose from 32.8 to 33.2 in the week ended July 7.

TUESDAY, JULY 18

Import prices (June; 8:30 a.m. EDT)

Forecast: -0.3

We expect import prices to have fallen 0.3% in June, matching the drop in May. This would be the third decline in the past four months. Energy prices are expected to be a weight as global crude oil prices fell between May and June. Food prices likely didn't provide any significant support to total import prices in June. Nonfuel import prices have weakened recently, and we look for this to have extended into June, rising only 0.1%. Nonfuel import prices, which matter for core consumer prices, should get a little support as the drag from past appreciation in the U.S. dollar is fading.

WEDNESDAY, JULY 19

Housing starts (June; 8:30 a.m. EDT)

Forecast: 1.163 million annualized units (starts)
Forecast: 1.209 million annualized units (permits)

There isn't any reason to be alarmed by the drop in housing starts and permits in May. This may seem like an overly optimistic assessment, but starts and permits are extremely unreliable from month to month and the trend in the important single-family segment remains favorable.

Housing starts fell 5.5% in May to 1.092 million annualized units, weaker than our well below-consensus forecast of 1.189 million. Single-family starts dropped 3.9% while multifamily fell 9.7%, their fifth consecutive monthly decline. The recent slide in permits isn't as troubling as it may appear. Single-family permits fell 1.9% in May, their third consecutive monthly decline. This could reflect payback for the boost the unseasonably warm weather provided in the fourth quarter of 2016 and early this year. Multifamily permits dropped 10.4% in May. Still, the trend in the level of multifamily permits has been relatively flat since mid-2016. We are not overly optimistic about the near-term prospects for multifamily construction.

We look for total housing starts to have risen from 1.092 million annualized units in May to 1.163 million in June. Permits are forecast to have risen from 1.168 million annualized units in May to 1.209 million 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.

EUROPE

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

Summary, July 14: The week ahead will bring June inflation numbers for the U.K. and the euro zone. In the currency area, we expect inflation to have stepped back slightly to 1.3%, from 1.4% in May, mainly due to energy inflation plummeting in most major countries on the back of declining oil prices and fading base effects. Energy inflation pushed headline inflation sharply up in the first quarter, to a peak of 2% in February, but the story will be different in the second half of the year; already in Germany, energy inflation was reading at -0.1% in June, with a further decline expected in July, while in France it slumped by a sharper 1.1%. If Brent prices remain stuck at around their current value of $47 or $48, energy inflation should remain relatively flat throughout the rest of the year before starting to fall again in December.

But the economy's pickup means that core prices are starting to strengthen, even if with a lag. Core inflation jumped to a cyclical high of 1.6% in June in Germany, mainly due to a jump in services inflation. Granted, some of the rise could be attributed to the fact that the timing of the Pentecost holiday likely boosted prices of hotels and restaurants over the month, but the late holidays weren't the only culprit. Rent inflation is rising too, peaking at a high of 1.8% in June, and so are prices for core goods. Similarly, in France, the decline in prices of core manufactured goods slowed to only 0.3%, from 0.7% in May, as clothing inflation spiked ahead of summer sales. The story isn't any different in Spain or Italy; although the inflation headline slowed sharply in Spain to 1.5%, from 1.9% in May, and in Italy to 1.2%, from 1.4%, the core rate in both countries picked up to 1.2% from 1%, and to 1% from 0.8%, respectively. This is consistent with the pickup in euro zone producer prices, and with the recovery-led building of domestic price pressures.

The pace of the core rate's increase will nonetheless be slow, and core inflation is expected to remain below the ECB's 2% target for a prolonged period. That's why we expect the bank to maintain its refinancing rate at 0% at Thursday's monetary policy meeting. We expect repo rates will stay at the lower bound until at least the beginning of 2019, though in between the bank will start tapering its bond-buying programme, and likely raise its deposit rate from the current -0.4%. Our forecast is that

the ECB will announce in September a reduction in the pace of bond purchases, to likely €40 billion a month from the current €60 billion, and that quantitative easing will run until at least summer 2018.

Across the Channel, the story is completely different. Inflation pressures have built rapidly in the U.K. following last June's exit vote, mainly because the pound's plunge has automatically raised prices of imported goods for British consumers. Headline inflation peaked at 2.9% in May, its highest in four years, while core inflation rose to 2.6%, its strongest since November 2012. We expect that inflation remained steady in June at 2.9%, but that it will continue to pick up during the second half of the year as retailers continue to pass on higher import prices through to consumers. Both food and core goods inflation, such as clothing and household goods, are set to be the main drivers of the headline, but transport prices should also rebound following an Easter-related correction in May. By contrast, we expect energy inflation should slow somewhat.

FRIDAY, JULY 14

Italy: Foreign Trade (May; 9:00 a.m. BST)

France's industrial production likely rebounded by 0.6% m/m in May following a rather downbeat -0.5% reading in April. A strong mean-reversion in manufacturing output should have provided the main boost to the headline, notably in the transport and machinery sectors. But oil refining and energy production should have also continued to recover from first quarter weakness. The latter was hit by the warmer than average weather denting demand for heating at the start of the year, but temperatures have since normalized. The brightest spot should be construction output, which leading indicators suggest is on a strong upward trend, with production picking up in both the residential and nonresidential sectors. All survey data for May corroborate our optimism, especially the further increase in INSEE's new orders-to-inventories ratio.

MONDAY, JULY 17

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

The euro zone's annual harmonized inflation slowed to 1.3% in June from 1.4% in the previous month, according to the preliminary estimates. Softer oil price growth and the strengthening euro weighed on the headline figure. Although core inflation accelerated to 1.2% from 1% in May, it remained subdued. After the temporary effect of lower energy prices disappears, however, inflation should heat up again. But we don't expect the headline reading to climb above the ECB's target of close to but below 2%. Meanwhile, we see little scope for core inflation to rebound much further and expect it to remain at around 1% in the months to come. Labour market slack limits euro zone wage growth, pushing inflation down.

Russia: Industrial Production (June; 2:30 p.m. BST)

Industrial production's growth will slow in June after a strong May report. Overall growth will be strong coming on the tail of two quarters of modest national economic expansion. After emerging from a two-year contraction in the last quarter of 2016, Russia's first quarter GDP data suggest that the economy is slowly recovering. Stronger oil prices, marginally improving business and consumer confidence, and the resilient labour market have mitigated the risk of capital outflows.

TUESDAY, JULY 18

U.K.: Consumer Price Index (June; 9:30 a.m. BST)

The U.K.'s annual headline CPI should have remained steady at 2.9% in June, a four-year high. Transport inflation should have rebounded following an Easter-related correction in May, but motor fuel inflation should have stepped back as fuel prices fell by around 1% during the month, while energy inflation is also expected to have corrected following the past months' increases in electricity prices by several of the U.K.'s Big Six electricity companies.

Elsewhere, we still expect that higher import prices continued to make their way through to consumer prices over the month, raising the prices of core goods such as clothing, household goods and recreational goods. Food inflation—which normally lags food producer output prices by four months—likely also rose further, in line with the sharp rise in food producer inflation, which hit 5.6% in May.

Survey data corroborate our view: The latest Markit PMI again showed a substantial increase in average purchase prices in manufacturing and services at the start of the second quarter. Output prices also rose quickly, despite slowing somewhat in both sectors. Sellers seem to be passing the higher input prices on to clients much faster than policymakers had anticipated.

WEDNESDAY, JULY 19

Russia: Retail Sales (June; 3:00 p.m. BST)

Russian retail turnover has now climbed higher on a year-ago basis for two consecutive months, with nonfood products entirely driving the gains. The rebound from nonfood products implies that discretionary spending is the key to the rebound, reinforcing the view that the Russian consumer is beginning to strengthen. Household consumption contributed to Russian GDP in the first quarter of 2017 for the first time since 2014. Consumption was one of the last barriers to the economy entering a recovery, but Russia is now growing slowly with consumers contributing. Accelerating improvement in consumption should have led to a 1.2% year-over-year increase in retail turnover in June.

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.

ASIA-PACIFIC

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

China likely grew a respectable 6.9% through the first half of 2017

China's economy accelerated in the first quarter on the back of the buoyant housing market and recovering global economy. This momentum carried into the second quarter. Our tracking model suggests that GDP grew 6.9% in the second quarter, the same as in the first. Activity across Tier 1 housing markets is slowing, which is dampening investment. But manufacturing sentiment is improving as global tech demand remains robust ahead of a likely renewed product cycle later this year.

China's monthly June activity data will show industrial production likely grew 6.3% y/y, down from 6.5% in May. Stronger global tech demand has been boosting electronics production, but improvements have been levelling off. That said, manufacturer sentiment improved in June thanks to reports of better domestic and export-oriented orders. Investment in fixed assets has decelerated in the past few months after a cyclical bounce in February. We expect growth in fixed assets decelerated to 8.4% in the year to June, down from 8.6% in the year to May. The main reason is a renewed decline in mining investment, as commodity supplies have rebounded. Manufacturing investment is growing steadily thanks to strengthening global demand.

Retail spending in China continues to outpace industrial production and overall GDP growth, a sign of rebalancing toward consumption. Retail spending likely grew 10.2% y/y in June after a 10.7% gain in May. Steady employment growth and strong (albeit slowing slightly) wage gains are driving household spending. The main downside in the short term is the cooling housing market in Tier 1 cities, which could crimp spending in related areas.

The Bank of Japan will keep its policy levers unchanged at the July monetary policy meeting. We expect the BoJ to maintain its asset purchases at a target rate of ¥80 trillion per month, despite the BoJ slowing its pace of asset purchases in the last few months. Inflation remains below the central bank's 2% target, but further stimulus is unlikely with the central bank running out of options.

THURSDAY, JULY 13

China – Foreign Trade – June
Time: Unknown
Forecast: US$43 billion
China's trade activity continues to benefit from the global tech cycle and the domestic investment recovery. Purchasing managers' sentiment recovered in June, with manufacturers pointing to a stronger pipeline of export orders. Domestic demand remains robust and is driving strong gains in crude oil, coal and iron ore imports. The trade surplus likely rose to US$43 billion in June from US$40.8 billion in May.

South Korea – Monetary Policy – July

Time: Unknown
Forecast: 1.25%
The Bank of Korea will keep the policy rate unchanged at 1.25% following its July policy meeting. The central bank is in no hurry to raise rates with core inflation only gradually creeping higher amid expectations of improving domestic demand. In May, core inflation held steady at 1.4% y/y, far from the central bank's 2% target for 2017. We expect interest rate normalization will begin from early 2018. It will occur gradually as elevated household debt will put undue pressure on budgets that could have broader adverse consequences with higher debt servicing costs.

FRIDAY, JULY 14

Singapore – GDP - Advanced – 2017Q2

Time: Unknown
Forecast: 3.2%
We look for the advance estimate of Singapore's second quarter GDP figures to show the city-state's economy grew 3.2% y/y, improving on the 2.7% result in the three months to March. The export-oriented economy has benefited in 2017 from the widespread improvement in global demand. This has supported manufacturing and service activity in Singapore. There are also signs of improvement in construction after a long spell of weakness resulting from the persistent falls in house prices. Though construction may not be a positive for the economy in the three months to June, it will cease being a large drag.

India – Wholesale Price Index – June

Time: 4:45 p.m. AEST (6:45 a.m. GMT)
Forecast: 1.8%
India's wholesale prices likely decelerated to 1.8% in June after a 2.2% rise in May. India's disinflation across consumer and wholesale prices means that the odds of rate cuts remain high. Food prices are declining as a result of the good monsoon season last year. Stockpiles also rose after demonetisation, which disrupted food supply chains because vendors were unable to offload their goods.

MONDAY, JULY 17

Indonesia – Foreign Trade – June

Time: Unknown
Forecast: US$780 million
Indonesia's monthly trade surplus likely widened to US$780 million in June, after narrowing significantly to US$470 million in May from US$1.33 billion in April. May's smaller surplus was driven by a surge in consumer imports ahead of festivities in late June to mark the end of Ramadan. Imports should have cooled over June, widening the trade surplus. Export receipts will be crimped by ongoing softness in commodity prices, especially for crude oil.

India – Foreign Trade – June

Time: Unknown
Forecast: -US$13.9 billion
India's trade deficit likely expanded to US$13.9 billion in June, after a $13.8 billion deficit in May. Exports continue to rise, but imports are rising faster on the back of higher energy costs. Despite the widening trade deficit, policymakers are unlikely to be worried; exports are rising thanks to improved global demand, and the pickup in imports stems from low base effects.

Singapore – Foreign Trade – June

Time: 10:30 a.m. AEST (12:30 a.m. GMT)
Forecast: 3%
We expect Singapore's nonoil domestic export growth to have bounced back to 3% y/y in June after declining 1.2% in May. May's decline in exports was the consequence of anomalies in the data rather than a clear signal of softening demand for Singapore's production. Pharmaceuticals exports, which fell

in May because of high base effects, should have improved in June. Electronics exports will continue to be the main positive for the headline figure.

China – Fixed Asset Investment – June

Time: 12:00 p.m. AEST (2:00 a.m. GMT)
Forecast: 8.4%
Investment in fixed assets has decelerated in the past few months after a cyclical bounce in February. The main reason is a renewed decline in mining investment, as commodity supplies have rebounded. Manufacturing investment is growing steadily thanks to strengthening global demand. However, investment in construction and raw materials is likely to cool as the restrictions on housing start to bite. We expect growth in fixed assets to have decelerated to 8.4% in the year to June, down from 8.6% in the year to May.

China – GDP – 2017Q2

Time: 12:00 p.m. AEST (2:00 a.m. GMT)
Forecast: 6.9%
China's economy accelerated in the first quarter on the back of the buoyant housing market and recovering global economy. This momentum carried into the second quarter. Activity across Tier 1 housing markets is slowing, which is dampening investment. But manufacturing sentiment is improving as global tech demand remains robust ahead of a likely renewed product cycle later this year. Our tracking model suggests that GDP grew 6.9% in the second quarter, the same as in the first.

China – Industrial Production – June

Time: 12:00 p.m. AEST (2:00 a.m. GMT)
Forecast: 6.3%
Stronger global tech demand has been boosting electronics production, but improvements have been levelling off. That said, manufacturer sentiment improved in June thanks to reports of better domestic and export-oriented orders. Tech production is expected to ramp up ahead of new tech devices to be released in the second half of the year, which will offset some of the declines in steel and other heavy industrial products. Industrial production likely grew 6.3% y/y in June, down from 6.5% in May.

China – Retail Sales – June

Time: 12:00 p.m. AEST (2:00 a.m. GMT)
Forecast: 10.2%
Retail spending in China continues to outpace industrial production and overall GDP growth, a sign of rebalancing toward consumption. Steady employment growth and strong (albeit slowing slightly) wage gains are driving household spending. The main downside in the short term is the cooling housing market in Tier 1 cities, which could crimp spending in related areas. Retail spending likely increased 10.2% y/y in June, after a 10.7% gain in May.

TUESDAY, JULY 18

New Zealand – Consumer Price Index – 2017Q2

Time: 8:45 a.m. AEST (Monday, 10:45 p.m. GMT)
Forecast: 0.2%
New Zealand's consumer price growth likely cooled to 0.2% q/q in the June quarter, after jumping 1% in the March quarter. Higher petrol prices alongside the annual rise in the cigarette and tobacco tax drove the uptick. We expect annual inflation cooled to 1.9% after reaching 2.2%, its fastest rate since the third quarter of 2011 (when the goods and services tax was increased from 12.5% to 15%) and at the upper end of the central bank's 1%-to-3% inflation target. Since the March quarter, petrol prices have cooled as have housing-related costs. We expect the Reserve Bank of New Zealand will keep interest rates steady at 1.75% until mid-2018.

WEDNESDAY, JULY 19

No major economic indicators are scheduled for release.

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.

The Long View

The US: Starting with July 1995, the median monthly changes for July US$ bond offerings are -14.7% for investment-grade and -10.6% for high-yield

By John Lonski, Chief Economist, Moody's Capital Markets Research Group,
July 13, 2017

CREDIT SPREADS

As measured by Moody's long-term average corporate bond yield, the recent investment grade corporate bond yield spread of 116 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 388 bp is less than what is inferred from the spread's macroeconomic drivers and the high-yield EDF metric, but is wider than what is implied by an ultra-low VIX index. The implications for liquidity of regulatory changes merit scrutiny. If regulatory change enhances the market making capabilities of banks, corporate bond yield spreads may be thinner than otherwise.

DEFAULTS

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

US CORPORATE BOND ISSUANCE

Yearlon 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 -7.8% for IG and an increase of +7.3% for high-yield, wherein US$-denominated offerings fell by -7.1% for IG and grew by +5.3% 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 2.6% annually for IG and may advance by 22.1% 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 13, 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. Our baseline is that the central bank could drop its quantitative easing bias with regard to size the week of July 17, 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 ECB 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. We don't expect the bank to start raising the deposit rate 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 released on Wednesday added to the gloom of the previous week's 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 Katrina Ell and the Asia-Pacific Staff of Moody's Analytics
July 13, 2017

Indonesia's economic outlook is upbeat thanks to improved economic management that has reduced external vulnerabilities, alongside sustained low interest rates that have fostered buoyant domestic demand. Yet volatile and low commodity prices have hurt exporter receipts, and expected ongoing softness is dampening the outlook. We expect Indonesia to grow 5.5% in 2017 and 5.3% in 2018, moderately stronger than the 5% gain in 2016.

GDP growth hit 5% y/y in the March quarter and is expected to grow a whisker stronger at 5.2% in the June quarter, after rising by 4.9% in December. Government spending contributed little to GDP growth in the opening quarter of 2017. The government contribution should increase over 2017 as infrastructure spending ramps up. The government concluded a successful tax amnesty program on 31 March, raising US$20 billion, which is being used to increase infrastructure and social spending. Finance Minister Sri Mulyani Indrawati announced in April that there would be no more spending cuts in 2017, as revenue collection was on track. Last year GDP growth was crimped by the government's commitment to improve its external position; that included reducing spending to rein in deficits.

Consumption should rebound in coming months, as sentiment has soared to its highest level since 2000. Consumption accounts for 57% of GDP and, thus, is a critical growth driver in the economy. Consumption has been supported by improved job prospects reducing unemployment. The political mood in the capital, Jakarta, has also improved after a religiously charged campaign for governor lifted geopolitical tensions to levels not typically seen in Indonesia, known as a moderate and tolerant multicultural nation. Jakarta accounts for around 20% of the archipelago's economy.

Crude oil prices remain an important driver of Indonesia's export performance even though domestic production has cooled amid government bottlenecks and a lack of infrastructure investment over the years. The correlation coefficient between oil prices and Indonesian exports from 2000 to 2017 was 0.68, where 1 indicates perfect correlation. We also found a causal relationship: Oil prices Granger-cause Indonesian exports with a 95% confidence interval with a lag length of 2. The relationship did not hold in the opposite direction.

This causal relationship confirms that Indonesia's external sector is vulnerable to changes in oil prices. West Texas Intermediate has fallen 18% year to date, suggesting that Indonesian export performance will be limited in the second half as lower global prices filter through.

Yet oil prices have become a less important driver of financial market movements in Indonesia, a testament to the economy's improved management and resilience. For instance, in the past the rupiah would largely follow oil price movements. Yet the rupiah is up 1.1% against the dollar year to date. It's a similar circumstance for Indonesian stocks, with the Jakarta stock exchange up almost 9% year to date.

Improved financial market resilience is the result of measures fostering narrower current account deficits, higher foreign exchange reserves, and a slower rise in private sector external debt. The current account deficit has narrowed despite the persistence of low commodity prices. Indonesia's current account deficit shrank to 0.8% of GDP in the fourth quarter, its smallest in five years. The country's foreign exchange reserves are hovering around a five-year high. These efforts recently resulted in Indonesia being rated investment-grade by all three major ratings agencies. The upgrade is expected to encourage higher capital inflows. Another boost to capital inflows will come with government easing of foreign ownership restrictions on certain industry sectors in August. This should also help with capital outflow amid tighter U.S. monetary policy.

Indonesia is the world's largest palm oil producer. Palm oil contributed 12% to Indonesia's export revenue last year even as hot and dry conditions related to El Nino hurt supply. Although the near-term outlook has improved with moderate weather expectations, the longer-term outlook has dimmed. Palm oil is a cheap vegetable oil, extensively used in food and cosmetics and as a biofuel. Major

importers are becoming more uncomfortable with the environmental issues caused by palm oil production, including deforestation and greenhouse gas emissions.

In April, the European parliament passed a resolution calling for the European Union to introduce a single certification scheme for palm oil entering the EU market and to phase out unsustainable palm oil imports by 2020. The resolution was approved by 640 votes to 18. This is problematic, as the EU has been one of Indonesia's largest importers, taking in around 15% of Indonesian exports.

The phasing out of electricity subsidies has pushed up inflation in 2017. The government raised electricity tariffs twice this year and delayed a third hike planned for June because it would have coincided with Ramadan, the Muslim fasting month when food prices generally spike. Subsidising electricity costs has long been criticised for drawing resources away from other much-needed priorities such as infrastructure projects.

Inflation reached a 14-month high of 4.3% y/y in June and could have broken through 5% if power costs were raised a third time. Inflation is expected to gradually creep closer toward the upper limit of the central bank's 3% to 5% target range over 2017.

After reducing interest rates six times last year, Bank Indonesia has since kept its benchmark interest rate at 4.75% and will probably maintain that stance through 2017, with gradual normalisation beginning from early 2018.

Ratings Round-Up

By Njundu Sanneh

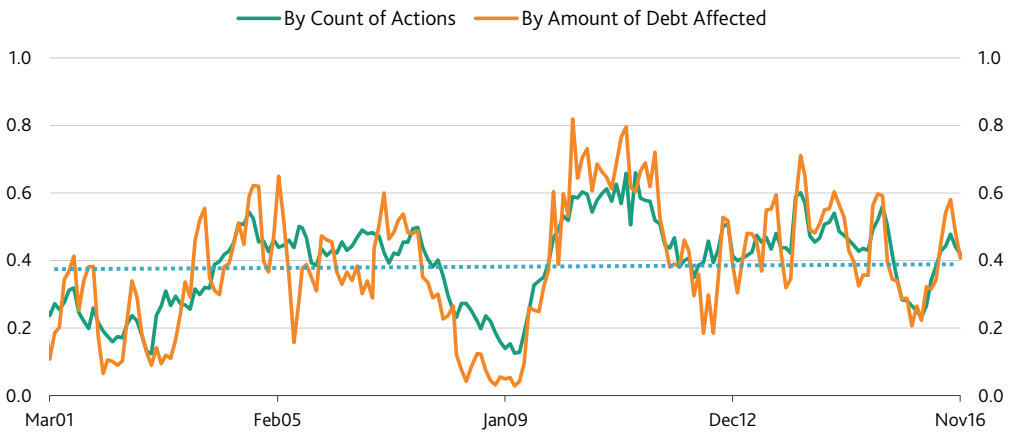
US Rating Changes More Upbeat; Europe Still Quiet

There were 10 rating changes for the US last week, with M&A-related energy company upgrades featured in the list. Baker Hughes's merger with GE Electric, and ONEOK Inc.'s acquisition of the ONEOK Partners unit it did not own, resulted in improvements in the companies' balance sheets with relatively more manageable debts. These energy company upgrades and those of homebuilder Hovnanian and outpatient facility operator Fresenius helped propel the contribution of positive rating changes to 60%, the first time this metric has surpassed the 50% line in over three weeks. The downgrade of True Religion Apparel Inc. ensures that the retail sector continues obstinately in the downgrade column. True Religion's downgrade followed its court filing under the Chapter Eleven bankruptcy code. The company entered into a restructuring support program supported by bulk of its shareholders; this ensures the term loan holders receive 100% of common equity and over a $100 million of first lien notes due in 2022.

Rating revision activity remains timid in Europe for the second week in a row with only three revisions. The financial sector accounts for all three, with two downgrades and one upgrade.

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	Old STD Rating	New STD Rating	IG/SG
7/5/17	BAKER HUGHES, A GE COMPANY, LLC	Industrial	SrUnsec/LTIR	2,800	U	Baa1	A3			IG
7/5/17	CYRUSONE INC. - CyrusOne LP	Financial	SrUnsec/LTCFR	800	U	B1	Ba3			SG
7/5/17	ONEOK, INC.	Industrial	SrUnsec	1,635	U	Ba1	Baa3			SG
7/5/17	ONEOK, INC. - ONEOK Partners, L.P.	Industrial	SrUnsec/CP	5,700	D	Baa2	Baa3	P-2	P-3	SG
7/6/17	TRUE RELIGION APPAREL, INC.	Industrial	SrSec/BCF/PDR		D	Ca	C			SG
7/6/17	WEC ENERGY GROUP, INC.	Utility	SrUnsec/LTIR/PS	5,055	D	A1	A2			IG
7/7/17	CARMIKE CINEMAS, INC.	Industrial	SrSec	460	U	B1	Ba1			SG
7/7/17	FRESENIUS MEDICAL CARE AG & CO. KGAA - Fresenius Medical Care Holdings, Inc.	Industrial	LTIR		U	Ba2	Baa3			SG
7/11/17	HOVNANIAN ENTERPRISES, INC.	Industrial	PDR		U	Caa2	Caa1			SG
7/11/17	MIDCONTINENT COMMUNICATIONS	Industrial	SrSec/BCF		D	Ba1	Ba2			SG

Source: Moody's

FIGURE 4 Rating Changes: Corporate & Financial Institutions – EUROPE

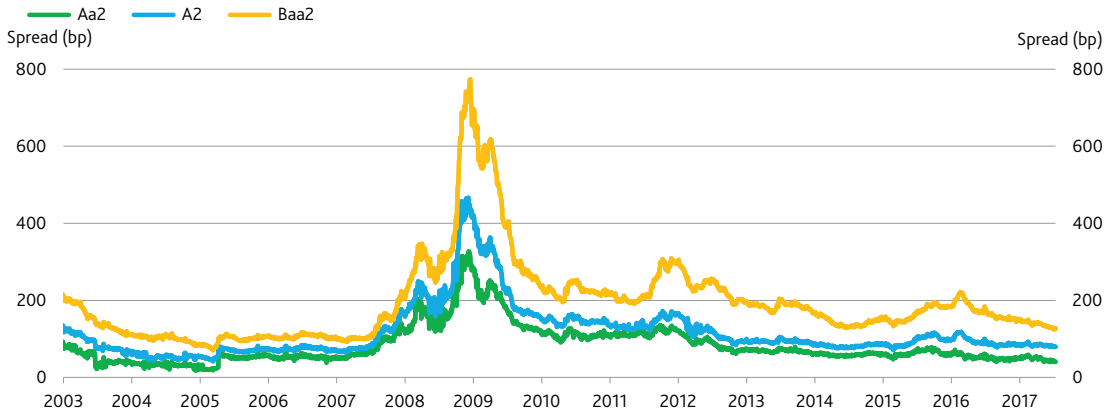
Date	Company	Sector	Rating	Amount ($ Million)	Up/ Down	Old LTD Rating	New LTD Rating	IG/ SG	Country
7/7/17	INTERNATIONAL FINANCIAL CLUB	Financial	LTD		D	B3	Caa1	SG	RUSSIA
7/5/17	UNICAJA BANCO	Financial	LTD		U	Ba3	Ba2	SG	SPAIN
7/10/17	ALLIED WORLD ASSURANCE COMPANY HOLDINGS, AG	Financial	SrUnsec/IFSR/Sub	800	D	A2	A3	IG	SWITZERLAND

Source: Moody's

Market Data

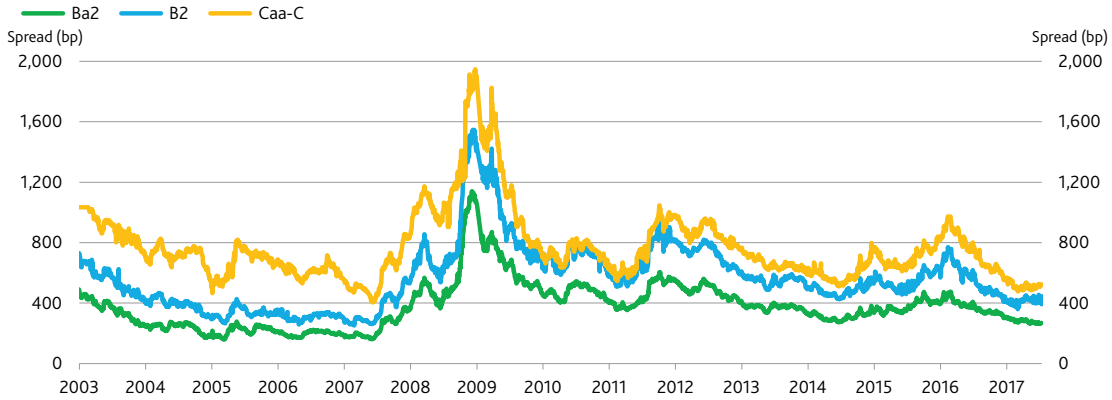
Spreads

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 5, 2017 – July 12, 2017)

CDS Implied Rating Rises	CDS Implied Ratings		
Issuer	Jul. 12	Jul. 5	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. 12	Jul. 5	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. 12	Jul. 5	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. 12	Jul. 5	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 5, 2017 – July 12, 2017)

CDS Implied Rating Rises	CDS Implied Ratings		
Issuer	Jul. 12	Jul. 5	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. 12	Jul. 5	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

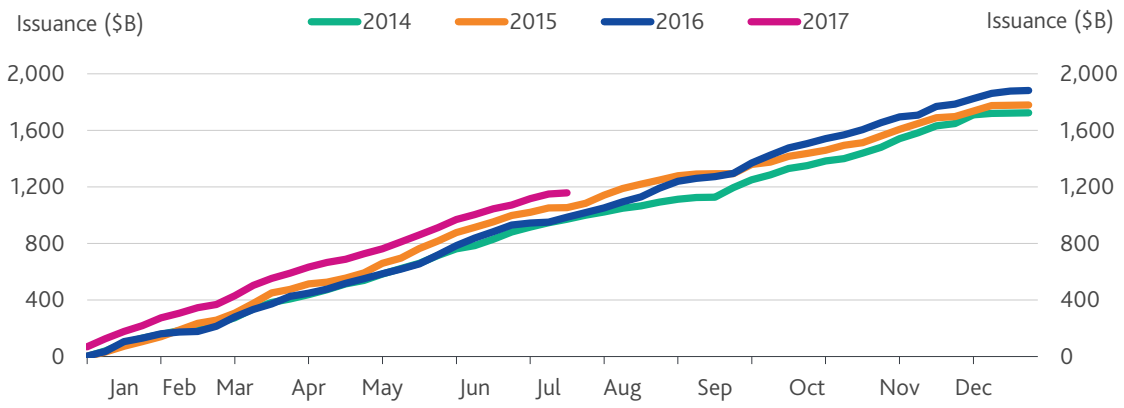
CDS Spread Increases		CDS Spreads		
Issuer	Senior Ratings	Jul. 12	Jul. 5	Spread Diff
Astaldi S.p.A.	B3	920	878	41
Novo Banco, S.A.	Caa2	1,364	1,324	40
Ensco plc	B2	613	575	37
Galapagos Holding S.A.	Caa2	883	847	36
PizzaExpress Financing 1 plc	Caa1	765	732	33
Scottish Power Limited	Baa1	91	63	27
Scottish 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. 12	Jul. 5	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

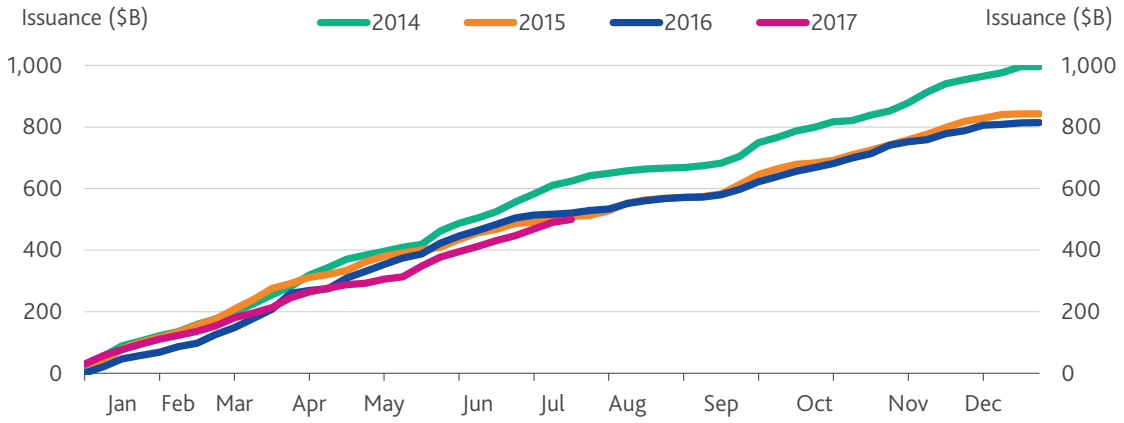
Issuance

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	9.019	0.300	9.910
Year-to-Date	816.668	241.473	1,158.570

	Euro Denominated		
	Investment-Grade	High-Yield	Total*
	Amount $B	Amount $B	Amount $B
Weekly	5.115	3.977	9.674
Year-to-Date	416.953	57.534	499.942

* Difference represents issuance with pending ratings.

Source: Moody's/ Dealogic

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