MOODY'S ANALYTICS

Weekly Market Outlook will not publish next week due to the July 4 holiday.

WEEKLY MARKET OUTLOOK

Moody's Analytics Research

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Below-Trend Spreads Bank on Profits Growth, Lower Rates and Healthy Equities

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.

Below-Trend Spreads Bank on Profits Growth, Lower Rates and Healthy Equities

Sequential declines by the Bureau of Economic Analysis' quarterly estimate of nonfinancial-corporate profits from current production, or core pretax profits, often reveal little about the current or future states of the business and credit cycles. For example, despite first quarter 2014's 6.1% quarterly drop by nonfinancial-corporate core profits, real GDP advanced by 5.0% annualized, on average, during 2014's second and third quarters, a composite high-yield bond spread narrowed from the 381 basis points of the first to the 344 bp of 2014's second quarter, and the U.S. high-yield default rate fell from year-end 2013's 2.1% to July 2014's current recovery low of 1.6%.

When attempting to discern recurring trends pertaining to business activity and corporate credit from core profits, the moving yearlong average of core profits provides the most reliable insights.

Each recession since 1982 was preceded by a peaking of core pretax profits' moving yearlong average. For now, the good news for the business cycle is that the core pretax profits of nonfinancial corporations have yet to peak.

Prior to the July 1990 start of the 1990-1991 recession, the moving yearlong average of nonfinancial-corporate core profits crested in March 1989; prior to the March 2001 start of the 2001 recession, the yearlong average of core profits topped off in December 1997; and prior to the December 2007 start to the Great Recession, yearlong core profits peaked in December 2006.

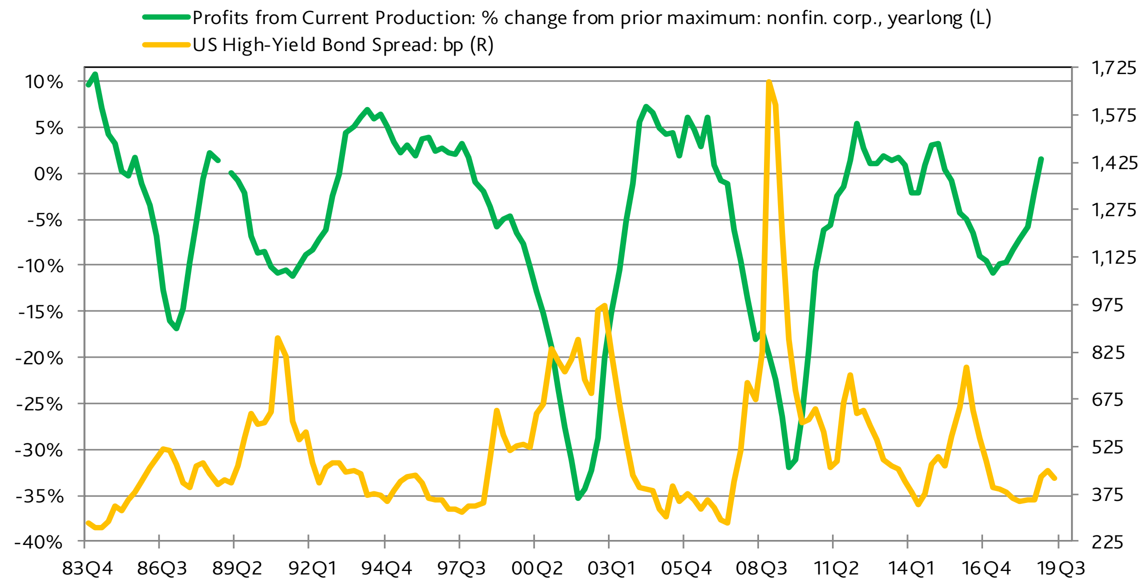
Not all meaningful declines by nonfinancial-corporate core profits' moving yearlong average led to recessions. In 1985-1987, core profits' yearlong average bottomed in March 1987 at a deep 16.9% under September 1985's then record high and a recession failed to materialize. More recently, core profits' yearlong average troughed in March 2017 at 10.9% under June 2015's erstwhile zenith and the business cycle upturn continues to this very day.

When Profits Contract, High-Yield Spreads Expand

Since late 1983, the five peak-to-trough declines of 5% or deeper by the yearlong estimate of nonfinancial-corporate core profits overlapped 49 quarters and were joined by a 644 bp average and 594 bp median for a composite high-yield bond spread. For the sample's remaining 94 quarters, the high-yield bond spread generated an average of 452 bp and a median of 413 bp. The entire sample's 143 quarters produced a 518 bp average and a 462 bp median for the high-yield bond spread.

Credit Markets Review and Outlook

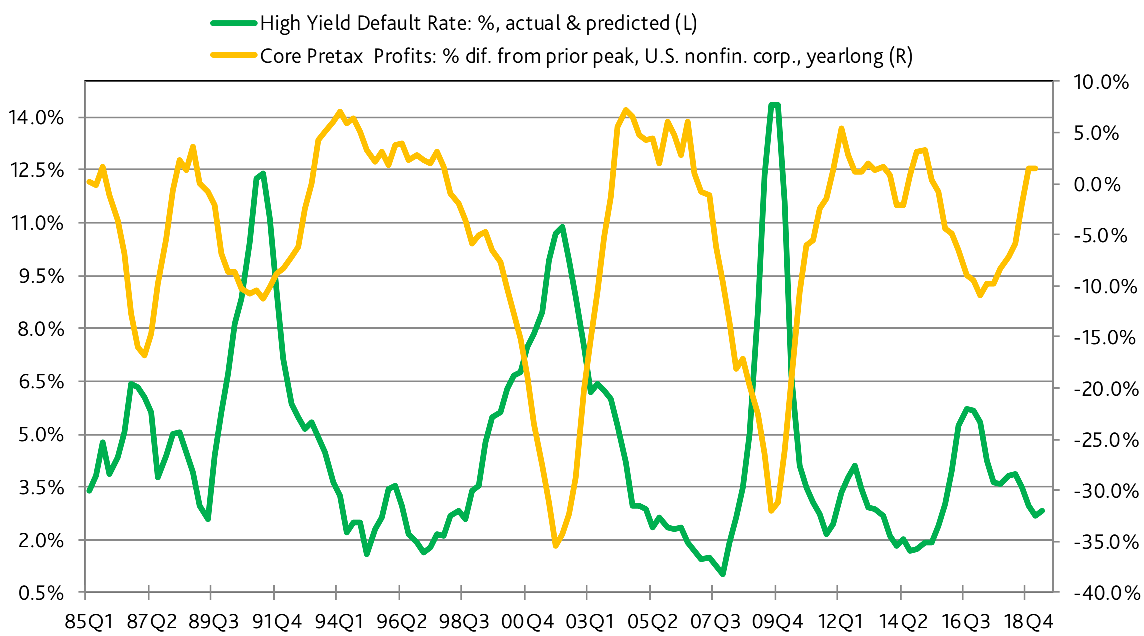
Figure 1: Expectations of New Highs for Profits Now Rein In the High-Yield Bond Spread
sources: BEA, Moody's Analytics



New Record Highs for Profits Are Joined by Relatively Low Default Rates

In addition, the five peak-to-trough declines of 5% or deeper by the yearlong estimate of nonfinancial-corporate core profits prompted pronounced upturns by the default rate. Following these five episodes, the default rate's peaks averaged 9.8%, wherein the median peak was 10.7%. By contrast, for the 53 quarters since 1984 showing a new record high for nonfinancial-corporate core profits, the calendar-quarter default produced an average of 2.9% and a median of 2.7%. Since core profits' yearlong average began to top its previous highs following September 2018, the default rate has averaged 2.8%.

Figure 2: Deeper Than 5% Drops by Core Profits from Prior High Led to a Greater than 5% Default Rates
sources: Moody's Investors Service, BEA, Moody's Analytics



High-Yield Rating Changes May Be Warning of Impending Top for Profits

The U.S. high-yield credit rating revisions of 2019's first half will show the number of downgrades doubling upgrades notwithstanding June 2019's likely setting of a new yearlong high for nonfinancial-corporate core profits. Not since March 1989 have high-yield downgrades doubled upgrades despite the setting of a new yearlong high for core profits.

However, immediately thereafter core profits began an extended descent. Thus, if high-yield downgrades continue to double upgrades, yearlong core profits may commence another declining trend that leads to the fourth recession since 1982.

The U.S.' speculative-grade credit rating changes show downgrades leading upgrades by a 1.50:1 margin for a sample that starts with 1986's first quarter and ends with 2019's second quarter. However, the high-yield downgrade per upgrade ratio drops to 1.07:1 for those observations coinciding with a new record high for the yearlong estimate of nonfinancial-corporate core pretax profits. For those observations showing yearlong profits below the then record high, the high-yield downgrade per upgrade ratio jumps up to 1.80:1.

High-Yield Spreads Shrug Off Elevated Downgrade per Upgrade Ratio

Despite how the moving two-quarter ratio of high-yield downgrades per upgrade rose from the 1.67:1 of the span-ended March 2019 to the prospective 2.13:1 of the span-ended June 2019, the high-yield bond spread narrowed from a first-quarter 2019 average of 448 bp to the 424 bp of the almost finished second quarter. By contrast, when the high-yield downgrade per upgrade ratio rose from the 1.27:1 of the six-months-ended September 2015 to the 2.23:1 of the six-months-ended December 2015, the high-yield bond spread widened from third-quarter 2015's 558 bp to the 648 bp of 2015's final quarter.

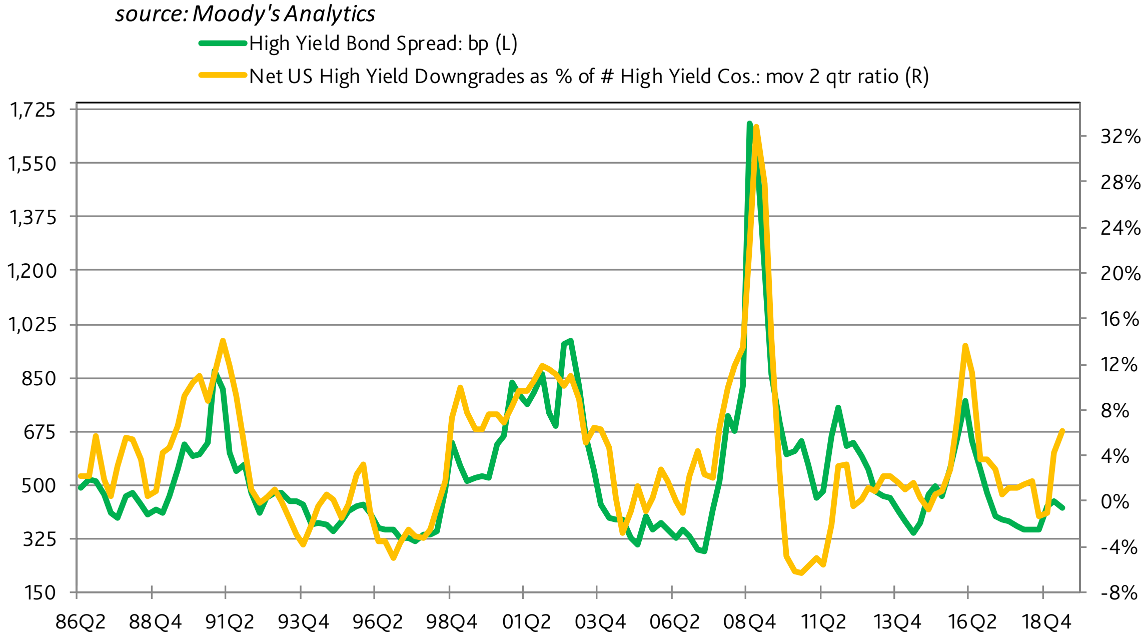
Apparently, the market implicitly expects that new record highs for core profits and lower benchmark interest rates will extend the possible beginnings of a declining trend for the still elevated ratio of high-yield downgrades per upgrade. Reason for hope can be gleaned from the drop by calendar-quarter version of the high-yield downgrade per upgrade ratio from the 2.27:1 of 2019's first quarter to the 2.02:1 of the second-quarter-to-date.

Nevertheless, as inferred from the historical record, the latest two-quarter ratio of high-yield downgrades per upgrade favors a 565 bp midpoint for the high-yield bond spread, which is much wider than the 430 bp of June 26, 2019.

Another way of explaining the high-yield bond spread in terms of credit rating changes employs the moving two-quarter ratio of net high-yield downgrades as a percent of the number of high-yield issuers. This methodology now predicts a 600 bp midpoint for the high-yield spread.

Figure 3: High-Yield Bond Market Senses Only a Brief Stay by a Now Well Above-Trend Net High-Yield Downgrade Ratio

source: Moody's Analytics



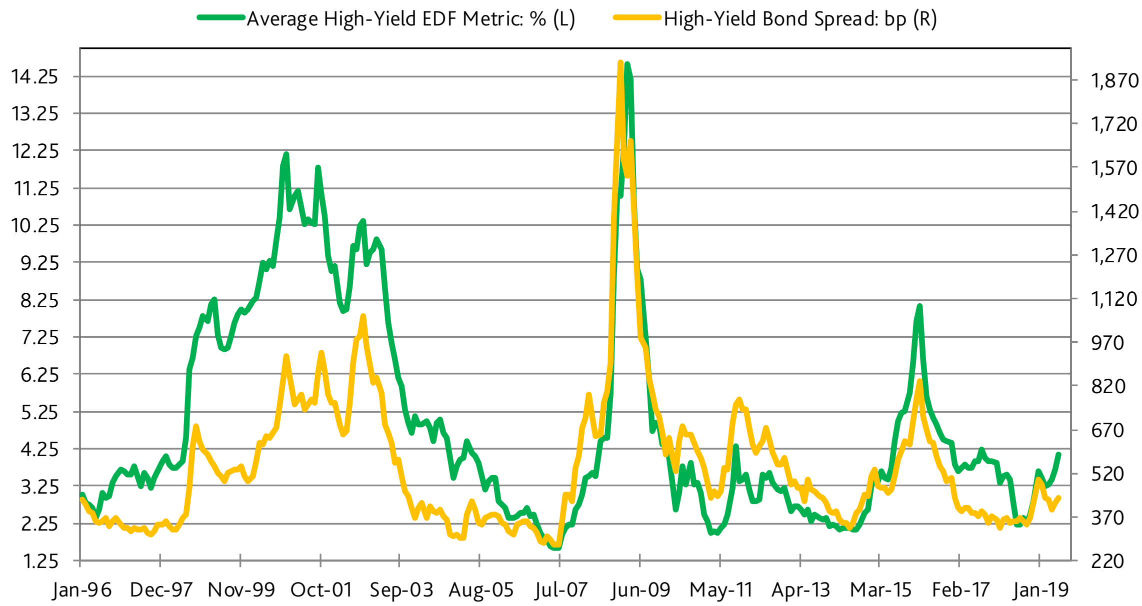
High-Yield EDF Metric Favors Wider Spreads

Other predictors also warn of a wider spread over Treasuries for the composite speculative-grade bond yield. For any issuer, the expected default frequency metric will be greater the lower is the market value of a borrower's net worth and the higher is the volatility of the market value of the borrower's business assets.

On a daily basis, Moody's Analytics calculates an average and median EDF for publicly held high-yield issuers. June 26's average high-yield EDF of 4.19% exceeded each of its prior month-long averages going back to the 4.25% of August 2017. When the high-yield EDF's calendar-year average rose from 2014's 2.81% to 2016's 5.43%, the high-yield bond spread's annual average widened from 392 bp to 611 bp, respectively. And when the high-yield EDF subsequently eased to a 2018 average of 2.90%, the high-yield spread's annual average narrowed to 373 bp.

As inferred from the statistical record, the latest high-yield EDF and its three-month increase favor 500 bp midpoint for the high-yield bond spread. This prediction is not without recent support. When the moving 12-month average of the high-yield EDF last rose to 4.19% as of the span ended November 2015, the high-yield bond spread's accompanying average equaled 525 bp.

Figure 4: Highest Average High-Yield EDF Metric since August 2017 and Its Three-Month Jump Favor a 500 bp Midpoint for High-Yield Bond Spread
source: Moody's Analytics



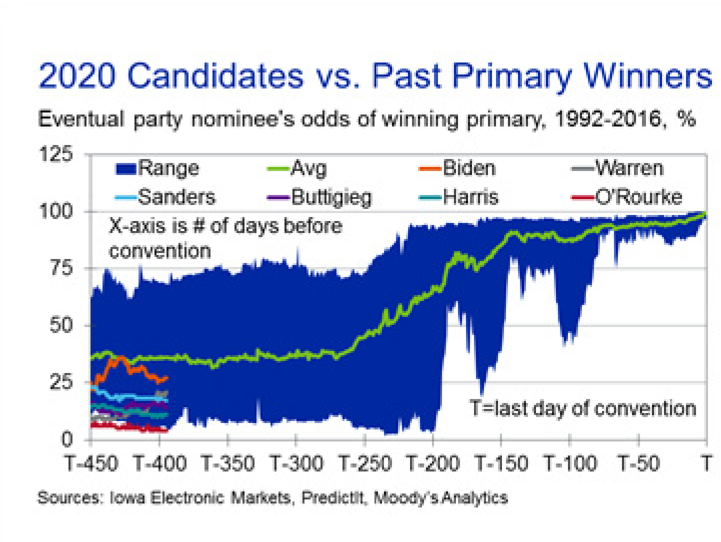
The Week Ahead – U.S., Europe, Asia-Pacific

THE U.S.
By Bernard Yaros, Moody's Analytics

Do U.S. Primary Election Debates Matter?

The 2020 presidential election cycle is underway, and the first Democratic debates this week will be an opportunity for the frontrunners to distinguish themselves on policy, experience and temperament, and for lesser-known candidates to raise their national profiles. Despite what the polls may indicate, the 2020 Democratic presidential nomination is up for grabs, and this is the message political betting markets are conveying.

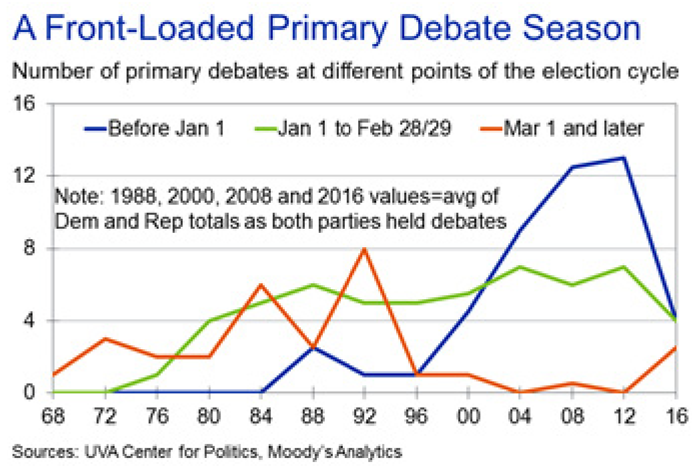
Moody's Analytics compiled historical data from the Iowa Electronic Markets, which have let participants bet on the outcome of primary elections going back to the 1992 Democratic nomination contest. At this point in past election cycles, IEM participants ascribed odds as high as 68% and as low as 6% for the eventual party nominee to win the primary.



The probabilities of winning the 2020 Democratic nomination that prediction markets are currently assigning to former Vice President Joe Biden, Senator Elizabeth Warren, Senator Bernie Sanders, and other leading contenders are within that historical range. Most important, the average candidate who eventually won their party's primary boasted higher odds of winning at this point than even Biden, though he is leading in the polls by a wide margin.

Political betting markets such as the IEM have accurately predicted the outcome of past political contests, so it is worth paying attention to the signals they are sending, even at such an early stage. Right now, the takeaway is that the scoreboard for the 2020 Democratic nomination will be anything but static in the next months as candidates continue to barnstorm across the country, hone their policy proposals, and attract increasing media scrutiny.

Whether this week's debates and subsequent ones will affect the scoreboard is a fair question to ask. After all, primary election debates have not only become more frequent but have also tended to be held earlier and earlier in the election cycle.

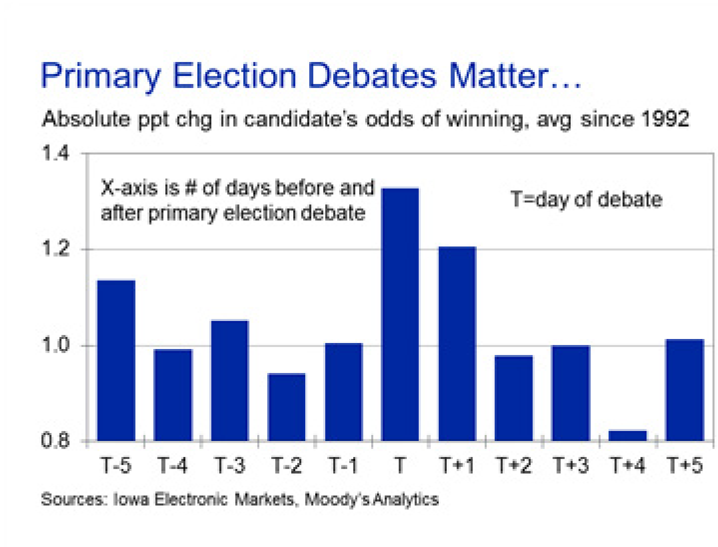


To answer this timely question ahead of this week's debates, Moody's Analytics conducted an event-study analysis, using historical IEM data to determine whether past candidates' odds of winning changed more on the day of a debate than in the days before and after. The IEM operate on a 24-hour basis, so the closing price (equal to a candidate's likelihood of winning the primaries) on the day of a debate should have already priced in their debate performance.

This analysis involved more than 70 debates and over 35 primary election candidates since 1992. We excluded debates occurring between the Iowa Caucus and Super Tuesday. During that time, IEM participants begin to factor in the results from early primary states, making it difficult to isolate the impact of a debate. We also did not look at debates after Super Tuesday by which time the eventual outcome of the primaries is largely anticipated.

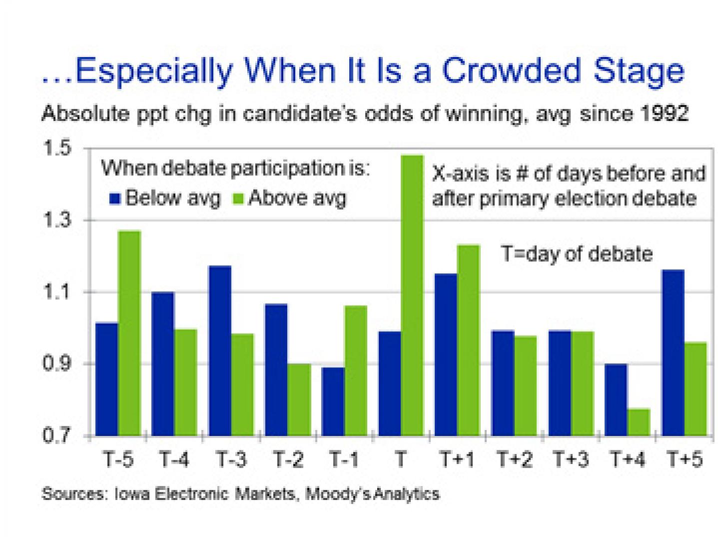
Our event study revealed that primary election debates do have a noticeable impact. The absolute change in a candidate's probability of winning is, on average, greater on the day of a debate than in the days before and after. Though primary election debates are not major televised events compared with general election debates, many of the viewers who do tune in have yet to settle on a candidate and can be swayed by a candidate's debate performance. In contrast, the majority of viewers of a general election debate will have already divided themselves into their respective partisan camps, with little chance for a change in heart.

Sometimes, there is a smoking gun behind the extreme movements we observe in a candidate's probability of winning on the day of a primary election debate. Former Texas Governor Rick Perry's odds of winning the 2012 primaries dropped significantly during the debate on November 9, 2011, when he famously named two of the three federal agencies he wanted to eliminate but then forgot the third. In other cases, a smoking gun is difficult to locate. The late Senator John McCain's probability of winning the 2007 nomination declined notably during a debate on June 5, 2007. Yet, his deteriorating odds of winning seemed less to do with the debate itself than with incoming polls at the time showing former Senator Fred Thompson eclipsing him.



We also asked ourselves whether a crowded debate stage makes it tougher for viewers to separate candidates from each other and to pick a favorite, which we thought would dampen debate-day movement in candidates' odds of winning the primaries. This question is especially relevant to this week's two debates, which will each feature 10 Democratic candidates on stage.

In the historical sample of debates we looked at, the average number of participants in a debate was just under seven. We therefore compared the average absolute change in candidates' odds of winning during debates with less than seven participants versus those with seven or more participants. Our a priori was wrong. We found more extreme movement in candidates' odds of winning when the debate had a higher than average number of participants.



This was surprising at first blush. However, when the field of primary candidates is less crowded, IEM participants seem to quickly settle on a potential winner and to deviate little from that bet over the course of the debate season. Even though former Senator and NBA star Bill Bradley was the only one to share the stage with former Vice President Al Gore throughout the 2000 primary election debates, he was unable to sway IEM participants, who continued to overwhelmingly favor Gore as the eventual nominee. Similarly, throughout the early 2004 Democratic primary debates, which featured a below-average number of debate participants, the IEM were fixated on former Vermont Governor Howard Dean. It wasn't until after the Iowa Caucus that Senator John Kerry's odds began to rise.

Primary election debates have an impact, but at times they can even mark turning points in a campaign. Perry's odds of winning the 2012 nomination tumbled after a debate on September 22, 2011, when he defended a Texas policy for illegal immigrants that alienated the Republican base. By the time his disastrous gaffe occurred more than a month later, the door had all but closed on his bid for the nomination. Former House Speaker Newt Gingrich's odds of winning declined notably in a debate on December 15, 2011, as he came under repeated attack from the other contenders, questioning his conservative credentials and the money he received as a consultant to Freddie Mac. His polling numbers didn't recover until his upset victory in South Carolina a month later.

In a Democratic primary field as large as the current one, the race is going to be unpredictable, and if the past is any indication, the coming debates are poised to add to that unpredictability. A strong debate performance this week could provide momentum for a candidate to build on over the next months. Conversely, a poor debate performance could spell the end for a candidate months before voters cast their first ballots next year.

Looking ahead

The key data next week include June employment, the ISM manufacturing and nonmanufacturing surveys, trade deficit factory orders, vehicle sales and jobless claims.

We will publish our forecasts for next week's data on Monday on Economy.com.

EUROPE
By Barbara Teixeira Araujo of Moody's Analytics

Euro Area Unemployment Likely Remains Low and Steady

One of the main pieces of news in the week ahead will be the release of May unemployment figures for most euro zone countries and the currency area itself. We expect them to show that unemployment remained steady across most major economies, and our forecast for the euro zone aggregate is that it held at 7.6%, following two consecutive months of decline. This is the lowest reading since August 2008. The main story there is that the euro zone's job market remains robust despite the recent drop in confidence and growth numbers across the currency bloc. Such a scenario is not unexpected. The labor market is normally a lagging indicator of activity, which means employment gains often remain solid even as GDP growth eases. The bad news: we are not expecting this pace to be sustained for long. We remain of the view that employment gains will slow in coming months, as firms become increasingly insecure about the currency area's future economy prospects and reduce hiring. Joblessness should nonetheless fall a bit further this year. We expect it will finish 2019 at 7.5%, though risks tilt toward an even lower reading.

Across countries, we expect that the main upside will continue to come from France and Spain, as the economic momentum in both economies remains solid on the back of a continued increase in domestic demand. Germany's situation is more fragile. Growth there has slowed sharply during the second quarter, dragged lower by a plunge in overall sentiment and by a further decline in external demand. Advanced figures from the country's statistical office showed that unemployment rose in June for the first time since 2013. While methodology changes may have explained some of the increase, there is no denying that the German labour market is on a downward trend following several years of extremely strong results. Vacancies and claimant count figures all attest to that. Elsewhere, we expect that Italy's unemployment numbers will remain volatile, though we see the underlying momentum in that country's labour market as being rather weak. Italy's economy has been struggling for several years, hit by prolonged political uncertainty and a deterioration in financial conditions.

Across the Channel, there won't be much on the data front for the U.K. All eyes there will remain on the Conservative leadership contest. After a first stage of voting, the 160,000 paying Tory party members now get to choose between the two remaining candidates on a postal ballot over the next few weeks. First is the hard-liner Boris Johnson—the firm favorite for the position. Second is Jeremy Hunt, the Foreign Secretary. Hunt initially voted Remain but has since repented, and now is fully in favor of leaving the EU. He is nonetheless much less open than Johnson to the idea of exiting without a deal and favors a renegotiation with the economic bloc. The winner is expected to be announced on July 23.

If Boris Johnson wins, as we expect, the chances of a no-deal Brexit will soar, but ironically so will the chances of Brexit being cancelled. That's because it is possible that a Boris Johnson premiership will be the shortest in history. Given Johnson's extreme views and his preference for a no-deal exit, we wouldn't be surprised if the opposition decided to call a no-confidence vote on his government. If Johnson lost a no-confidence vote, there would be 14 days for someone to try to form a new government that commanded majority. If no government is formed (which is our base case, given the current divisions in parliament), new elections would be held. Recent polls all but suggest that a Labour-led coalition would be the most likely outcome of the elections, which would open the way for a much softer Brexit or for the holding of a new referendum.

	Key indicators	Units	Moody's Analytics	Last
Mon @ 9:00 a.m.	Germany: Unemployment for June	%	5.0	5.0
Mon @ 9:00 a.m.	Italy: Unemployment for May	%	10.3	10.2
Mon @ 10:00 a.m.	Euro Zone: Unemployment for May	%	7.6	7.6
Tues @ 7:00 a.m.	Germany: Retail Sales for May	% change	0.4	-2.0
Tues @ 2:00 p.m.	Russia: GDP for Q1	% change yr ago	0.5	2.7
Thur @ 10:00 a.m.	Euro Zone: Retail Sales for May	% change	0.0	-0.4
Fri @ 7:00 a.m.	Spain: Industrial Production for May	% change	-0.5	1.8
Fri @ 2:00 p.m.	Russia: Consumer Price Index for June	% change	5.5	0.3

ASIA-PACIFIC

By Katrina Ell of Moody's Analytics

Business Sentiment in Japan a Casualty of the Trade War

Japan's June quarter Tankan survey is expected to remain down in the dumps. The index for large manufacturers fell by 7 points to 12 in the March quarter and is expected to stay there in the June quarter. Sentiment deteriorated sharply early in 2019 and has remained weak since, with the U.S.-China trade war a key drag, adding to uncertainty and causing firms to delay capital investment and slow hiring intentions. In the March quarter there was a broad-based slowdown across industries, with machinery, electrical machinery and nonferrous metals leading the rout. Sales and profit forecasts were revised down heavily, confirming that the export slump has weighed on business sentiment. Deterioration in business sentiment since the escalation of the trade war has largely been a global phenomenon, with other major global players including China, Germany and the U.S. seeing marked weakness in business sentiment.

South Korea's foreign trade data for June will be closely watched, given it is Asia's first major economy to release the monthly print and is a bellwether for the region. Exports are forecast to remain in contraction territory in June after the 9.4% y/y slide in May. Korea's semiconductor exports have been hit hard by the cyclical decline in the global tech cycle, with an added hit coming from the trade war. Increases in tariffs on imports to the U.S. from China, as well as retaliatory tariffs on imports to China from the U.S., which took effect around late May, will be a further drag on South Korea's manufactured goods.

The Week Ahead

The Reserve Bank of Australia is expected to keep the cash rate steady at 1.25% in July, following the 25-basis point reduction in June. The June rate cut was motivated by a desire to reduce spare capacity in the economy, achieving "more assured progress" towards the 2%-to-3% inflation target and faster progress in reducing the unemployment rate. The RBA believes that the natural rate of unemployment is around 4.5%, which is lower than its prior estimate of around 5%. With this in mind, it is using cash rate reductions to spur further labour market tightening to reduce the unemployment rate, which has started to creep higher, in a bid to bolster stubbornly subdued wage growth and unlock a sustained improvement in consumption. Our baseline is for a cumulative 50 basis points worth of reductions this year, but odds of a cumulative 75 basis points stand at 40%.

	Key indicators	Units	Confidence	Risk	Moody's Analytics	Last
Mon @ 9:50 a.m.	Japan Tankan survey for Q2	Index	3	↑	12	12
Mon @ 3:00 p.m.	Japan Consumer confidence index for June	Index	3	←	40.8	39.4
Mon @ Unknown	South Korea Foreign trade for June	US$ bil	2	↓	2.9	2.3
Tues @ 9:00 a.m.	South Korea Consumer price index for June	% change yr ago	3	←	0.7	0.7
Tues @ 2:30 p.m.	Australia Monetary policy for July	%	4	←	1.25	1.25
Wed @ 11:30 a.m.	Australia Foreign trade for May	A$ bil	2	←	4.3	4.9
Thurs @ 11:30 a.m.	Australia Retail sales for May	% change	3	←	0.3	-0.1
Thurs @ 2:00 p.m.	Malaysia Foreign trade for May	MYR bil	2	↓	9.8	10.9

The Long View

Oil & gas figured in 19% and retailing entered into 12% of the high-yield downgrades of the second-quarter-to-date.

By John Lonski, Chief Economist, Moody's Capital Markets Research Group
June 27, 2019

CREDIT SPREADS

As measured by Moody's long-term average corporate bond yield, the recent investment grade corporate bond yield spread of 124 basis points resembles its 122-point mean of the two previous economic recoveries. This spread may be no wider than 140 bp by year-end 2019.

The recent high-yield bond spread of 430 bp is thinner than what is suggested by both the accompanying long-term Baa industrial company bond yield spread of 192 bp and the recent VIX of 15.9 points.

DEFAULTS

May 2019's U.S. high-yield default rate of 2.9% was less than the 4.0% of May 2018. Moody's Investors Service now expects the default rate will average 2.9% during 2020's first quarter.

US CORPORATE BOND ISSUANCE

Yearlong 2017's US$-denominated bond issuance rose by 6.8% annually for IG, to $1.508 trillion and soared by 33.0% to $453 billion for high yield. Across broad rating categories, 2017's newly rated bank loan programs from high-yield issuers sank by 26.2% to $72 billion for Baa, advanced by 50.6% to $319 billion for Ba, soared by 56.0% to $293 billion for programs graded single B, and increased by 28.1% to $25.5 billion for new loans rated Caa.

First-quarter 2018's worldwide offerings of corporate bonds incurred year-over-year setbacks of 6.3% for IG and 18.6% for high-yield, wherein US$-denominated offerings posted sank by 14.4% for IG and 20.8% for high yield.

Second-quarter 2018's worldwide offerings of corporate bonds eked out an annual increase of 2.8% for IG, but incurred an annual plunge of 20.4% for high-yield, wherein US$-denominated offerings rose by 1.6% for IG and plummeted by 28.1% for high yield.

Third-quarter 2018's worldwide offerings of corporate bonds showed year-over-year setbacks of 6.0% for IG and 38.7 % for high-yield, wherein US$-denominated offerings plunged by 24.4% for IG and by 37.5% for high yield.

Fourth-quarter 2018's worldwide offerings of corporate bonds incurred annual setbacks of 23.4% for IG and 75.5% for high-yield, wherein US$-denominated offerings plunged by 26.1% for IG and by 74.1% for high yield.

First-quarter 2019's worldwide offerings of corporate bonds revealed annual setbacks of 0.5% for IG and 3.6% for high-yield, wherein US$-denominated offerings fell by 2.3% for IG and grew by 7.1% for high yield.

During yearlong 2017, worldwide corporate bond offerings increased by 4.1% annually (to $2.501 trillion) for IG and advanced by 41.5% for high yield (to $603 billion).

For 2018, worldwide corporate bond offerings sank by 7.2% annually (to $2.322 trillion) for IG and plummeted by 37.6% for high yield (to $376 billion). The projected annual percent increases for 2019's worldwide corporate bond offerings are 2.6% for IG and 15.5% for high yield. When stated in U.S. dollars, issuers based outside the U.S. supplied 60% of the investment-grade and 61% of the high-yield bond offerings of 2019's first quarter.

The Long View

US ECONOMIC OUTLOOK

As inferred from the CME Group's FedWatch Tool, the futures market recently assigned an implied probability of 100% to a cutting of the federal funds rate at the July 31, 2019 meeting of the Federal Open Market Committee. In view of the 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 3% 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.

EUROPE

By Barbara Teixeira Araujo of Moody's Analytics
June 27, 2019

EURO ZONE

Thursday was full on the data front, but what stole the spotlight was the sharp decline in the European Commission's gauge of euro zone economic sentiment. It read at only 103.3 in June, down from 105.2 in May and the weakest reading in almost three years. Across sectors, the main drag on the headline was yet another plunge in industrial confidence, to -5.6 from -2.9 in May. June marked the fifth consecutive month that sentiment in the sector has read below zero, after it averaged 6 over 2017 and 2018.

This result is disappointing, but it does chime in with our view that euro zone manufacturers will struggle this year on the back of a trade war-related slowdown in world trade and of a drop in overall confidence in future prospects. Germany is a case in point given the openness of its economy; we were not surprised to see that industrial sentiment tumbled by more than four points to -9.5 in June, a six-year low. But industrial confidence fell everywhere else as well, and it is reading in negative territory across all four major euro zone economies and in the U.K.

We hope that consumers will save the day this year and help keep the euro zone economy afloat, so we weren't pleased to see that consumer confidence also declined over the month to -7.2 from -6.5 in May. This compares with an average of -5 for 2018. At least the high-frequency hard data have been better, in line with the recent pickup in wage growth and strong employment gains. Across countries, the standout was France. Consumer confidence in the country has increased for seven straight months, with retail sales data confirming that French households have freely opened their wallets lately. On the downside, consumer confidence in Italy sank to a 22-month low in June, as the economic situation in the country remains challenging.

UNITED KINGDOM

The big news on Tuesday was that the British CBI's monthly retail sales balance plunged to -47 in June, its worst reading in a decade, from -27 in May. This came against the market consensus and our expectation of a significant rebound following a weather-depressed May, suggesting that Britain's economy may be running a lot colder than we thought. We had hoped that U.K. consumers would again open their wallets at the end of the second quarter—in line with the continued pickup in real wage growth and the strong labour market—and continue to help offset weakness in the manufacturing sector.

We caution that June's drop should be taken with a pinch of salt. The CBI balance is derived from retailers comparing sales with volumes recorded for the same month a year ago, and June 2018 was a one-off month for the retailing sector. There was a heatwave, which boosted consumption of summer clothes and furniture, as well as of foods and drinks, but more important was the start of the 2018 men's soccer World Cup. Consumption of snacks and alcoholic drinks skyrocketed during that period, and so did sales in bars and restaurants.

Given that most of the decisive World Cup games took place in July 2018, we expect that the CBI sales balance will remain unsustainably depressed this July as well. Base effects are favourable for a marked rebound in August, but the bad news is that even accounting for the volatility, there is no denying that the underlying conditions for U.K. High Street retailers are challenging. Competition is fierce, while the recent depreciation of the pound should only further squeeze their margins. Our guess is that retailers will find it hard to pass all the increase in import prices through to consumers.

The good news for the retail sector is that the fundamentals for consumers remain solid. Nominal wage growth has gained impressive momentum over the past year and is set to remain above 3% y/y over the rest of 2019. Also, labour market gains remain strong, with the unemployment rate reading at a 44-year low in April. Unless there is a Brexit catastrophe in coming months, we don't see why consumers would become more cautious and increase their savings instead of spending.

ASIA PACIFIC

By Katrina Ell of Moody's Analytics
June 27, 2019

U.S.-CHINA TRADE WAR

The world will be watching the expected watershed moment at the G-20 summit on Friday and Saturday when Presidents Donald Trump and Xi Jinping are confirmed to meet. The trade dispute between the U.S. and China could take meaningful steps towards a truce or head down a darker path. Trump's threat to impose tariffs on a further US$300 billion Chinese goods imports is looming large.

China has shown its retaliatory tariff and nontariff measures carry ferocity. At this point of the trade war, the stakes are high. A good and probable outcome is that cooler heads prevail with some sort of truce being reached at the Osaka, Japan, summit, including an agreement to roll back the existing tariffs over time.

A common question is who is hurt more by the trade war. To answer, the dispute must be looked at in context. Beijing was already in a tough spot prior to the escalation of the trade war, managing intentionally slower domestic demand with a deleveraging campaign to ultimately deliver more sustainable growth. This remains a worthy endeavor given that China's debt was 254% of GDP in 2018, up from 143% of GDP in 2008, according to the Bank for International Settlements.

Since the trade war was deepened, Beijing has had to shift priorities such that stabilizing domestic demand has become the priority, as manufacturers and exporters have taken a noticeable hit and the existing downtrend in global demand has steepened. Stabilising China's economy has proven more difficult than anticipated, particularly as Beijing has avoided the barrage of stimulus of prior downturns. China's economy is in a more vulnerable position compared with the U.S., which is not managing such hefty risks. Indeed, the Federal Reserve has only recently started considering interest rate cuts.

Central banks in Asia have overwhelmingly boarded the easing bandwagon this year. India, Australia, New Zealand and the Philippines have already cut key policy rates and all have flagged a high likelihood of further easing, often as soon as the third quarter.

The profound global influence of this trade dispute between the world's two largest economies was clear at the numerous central bank meetings in Asia the past two weeks. The common theme from central banks in Japan, Thailand, the Philippines, Indonesia, New Zealand and Taiwan was the hefty downside risks to global growth and the rising need for monetary stimulus, with the trade war the key unknown, even though they all held fire in June.

JAPAN

The Bank of Japan kept monetary policy settings steady, as expected. The most important takeaway from its meeting was the BoJ signaling that it is ready and willing to up the stimulus, if necessary. Governor Haruhiko Kuroda said that the bank could combine bigger asset purchases with interest rate cuts, if the downside risks to global growth materialized and further hurt Japan's already weakened economy. This was an important development, as the market consensus was that the BoJ had largely run out of firepower to shore up the economy if conditions deteriorate further.

Whispers that the BoJ will need to up the ante have been growing for some time, given that the 2% inflation target is unlikely to be hit in the foreseeable future. But this is not a straightforward, win-win endeavour. The BoJ released its monetary policy minutes from April this week, with one member noting that further interest rate cuts could cause more harm than good.

This references the distortion negative rates are having on financial markets and profitability of financial institutions, particularly regional banks, which are already struggling with the side effects of an aging population. The April policy meeting was significant because the BoJ pledged to keep current settings in place at least until the spring of 2020.

Japan's important export sector is struggling and has been a key source of concern for the BoJ. Exports fell for a sixth straight month in May, with particular weakness in semiconductors and auto parts bound for China. Headline exports fell by 7.8% y/y in May, from April's 2.4% decline. The slowdown in exports was likely exacerbated by the 10-day holiday in Japan due to the enthronement of the new emperor.

Business sentiment among Japanese manufacturers has deteriorated with the trade war escalating, and this is denting capital investment plans and hiring intentions. At this point, odds are high that the government will delay the planned sales tax hike from 8% to 10% in October, potentially marking the third time it has been delayed.

INDONESIA

Bank Indonesia expectedly kept the seven-day reverse repo rate at 6% at its June policy meeting. But the likelihood of near-term easing of the policy rate is high, with BI indicating in June it is looking for the right opportunity to begin reversing the 175 basis points' worth of hikes delivered in 2018.

Expectations that the Federal Reserve would continue with policy normalization led emerging market assets to fall out of favour last year. Indonesia was amongst the worst affected in Asia by capital outflows. This year is a different story, with Fed normalisation off the cards and odds of near-term easing high. This is a game changer for Indonesia and has allowed BI to pencil in reductions to its key policy rates.

It is all about timing for BI when it comes to delivering rate cuts, particularly given its preoccupation with keeping the external position relatively stable, a difficult endeavor given that the trade deficit has widened, straining the government's ability to narrow the current account deficit as a proportion of GDP. On the upside, Indonesia's rupiah has been relatively stable this year, although there have been times of downward pressure.

Bank Indonesia reduced reserve requirement ratios across the board in June to help lift credit growth and broader growth momentum. It was likely testing the waters before delivering a cut to the key policy rate, which is likely in the September quarter.

PHILIPPINES

Bangko Sentral ng Pilipinas surprised markets and kept the policy rate on hold at 4.5% in June. The central bank opted for a "prudent pause" to assess the impact of June's 25-basis point rate reduction, alongside phased reductions in reserve requirement ratios for banks.

Another driver for BSP holding steady was the modest uptick in inflation to 3.2% y/y in May, from 3% in April, which was a 16-month low. The bank is treading carefully given its mandate to maintain price stability, a sensitive issue since CPI growth peaked at 6.7% y/y in the third quarter of 2018. Odds for another 25-basis point reduction in the third quarter are high, particularly given inflation is likely to remain within the BSP's 2%-to-4% target this year.

TAIWAN

Taiwan's central bank expectedly kept the discount rate at 1.375% in June and is one of the few in Asia that will likely keep the policy rate on hold through 2019. But likely central bank inaction is not a sign that Taiwan is immune to slower global demand and the risks posed by the U.S.-China trade dispute. Taiwan's economic growth is closely hitched to China, given it is a key manufacturing hub for many Taiwanese-owned firms and an important source of demand.

Taiwan's biggest export earner is tech and it has been in a cyclical downswing for over a year. Anecdotal evidence suggests that tech supply chains throughout the region have been particularly disrupted by the trade dispute and reordering of supply chains. The central bank downwardly revised GDP growth to 2.06% for 2019, from 2.13% previously. Like other central banks in the region, it noted that trade war developments were the critical input to the outlook.

THAILAND

Meanwhile, the Bank of Thailand kept the policy rate at 1.75% in June. The monetary policy committee reduced its GDP forecast for 2019 to 3.3%, from 3.8%. The CPI forecast held at 1% for 2019. The committee said future movements would depend on the data and offshore developments, notably trade tensions. We expect a 25-basis point reduction in the second half of 2019.

Ratings Round-Up

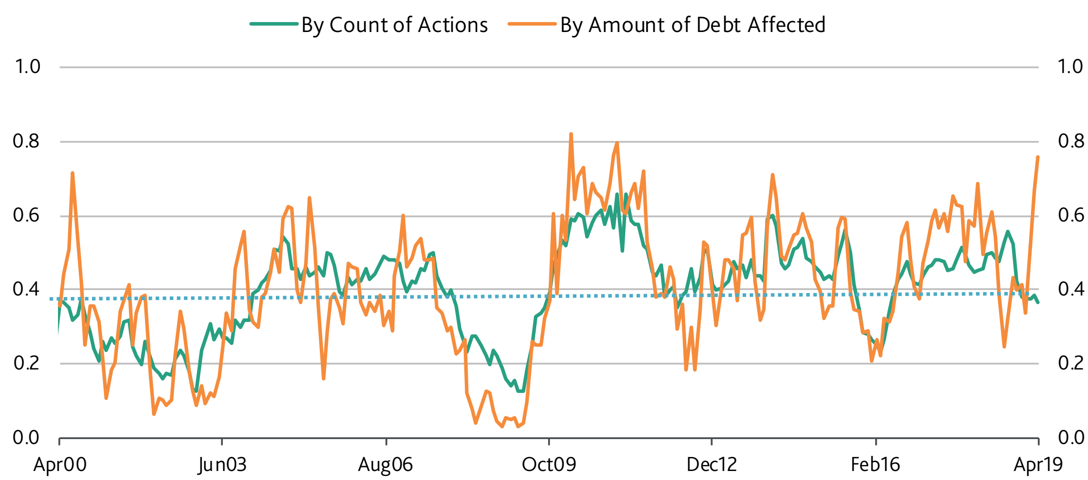
U.S. Upgrades Represent Bulk of Affected Debt

By Michael Ferlez

U.S. rating change activity remained subpar for the period ending June 25. Positive rating changes accounted for 44% of total changes, a slight increase from the previous week. Rating activity remain heavily concentrated in the industrial sector. Despite being outnumbered, upgrades represented the bulk of affected debt. Upgrades were headlined by Talen Energy Supply LLC and Kennedy-Wilson Inc. Talen Energy Supply saw its senior unsecured credit rating upgraded one-notch to B3 reflecting the guarantee of $240 million of previously unguaranteed senior unsecured notes. Meanwhile, Kennedy-Wilson saw its credit rating raised to B1 from B2 reflecting the firm's successful integration of Kennedy Wilson Europe Real Estate plc in addition to the increased scale and meaningfully larger earnings and reduced geographical and asset concentrations. In keeping with recent trends, downgrades were concentrated among smaller firms with speculative credit ratings. With one exception, all the downgrades were to industrial firms spread across a variety of industries.

In Europe, rating change activity was broadly negative following the downgrade of Turkey's sovereign credit rating from Ba3 to B1. For the week ended June 25, Moody's Investors Service downgraded the credit rating of twelve Turkish firms. The most notable downgrade were made to Koc Holdings A.S and Turkiye Sise ve Cam Fabrikalari A.S. The downgrades reflected Moody's Investors Service view of an increased risk of a balance of payments crisis in Turkey, which raises the risk of a government default. On the positive side, U.K grocery market Tesco Plc saw its senior unsecured credit rating upgraded one-notch to Baa3. The upgrade reflects improvements in the firm's operating profit and Moody's expectation of continued profit growth, cash generation, and debt reduction. The upgrade affected $6.1 billion in outstanding debt.

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

Ratings Round-Up

FIGURE 3
Rating Changes: Corporate & Financial Institutions – US

Date	Company	Sector	Rating	Amount ($ Million)	Up/ Down	Old LTD Rating	New LTD Rating	IG/ SG
6/19/19	ALLIANCE HEALTHCARE SERVICES, INC.	Industrial	SrSec/BCF /LTCFR/PDR		D	Ba3	B2	SG
6/19/19	TALEN ENERGY SUPPLY, LLC	Utility	SrUnsec	1,250	U	Caa1	B3	SG
6/19/19	LPL HOLDINGS II -LPL HOLDINGS, INC.	Financial	SrUnsec/SrSec /BCF/LTCFR	900	U	B2	B1	SG
6/19/19	GENWORTH FINANCIAL INC-GENWORTH LIFE AND ANNUITY INSURANCE COMPANY	Financial	IFSR		D	Ba3	B1	SG
6/19/19	KENNEDY-WILSON HOLDINGS, INC.-KENNEDY-WILSON, INC.	Industrial	SrUnsec /LTCFR	1,150	U	B2	B1	SG
6/19/19	FOUNDATION BUILDING MATERIALS, INC-FOUNDATION BUILDING MATERIALS HOLDING COMPANY LLC	Industrial	SrSec/BCF /LTCFR/PDR		U	B3	B2	SG
6/19/19	ENCAPSYS, LLC	Industrial	SrSec/BCF		D	B1	B2	SG
6/19/19	LEGACY RESERVES INC. -LEGACY RESERVES LP	Industrial	SrUnsec /LTCFR/PDR	349	D	Ca	C	SG
6/20/19	HECLA MINING COMPANY	Industrial	SrUnsec /LTCFR/PDR	500	D	B3	Caa2	SG
6/20/19	NN, INC.	Industrial	SrSec/BCF		D	B2	B3	SG
6/21/19	MACOM TECHNOLOGY SOLUTION HOLDINGS, INC.	Industrial	SrSec/BCF /LTCFR/PDR		D	B2	B3	SG
6/21/19	ALTA MESA HOLDINGS, LP	Industrial	SrUnsec /LTCFR/PDR	500	D	Caa2	Ca	SG
6/21/19	ASCENA RETAIL GROUP, INC.	Industrial	SrSec/BCF /LTCFR/PDR		D	B1	B3	SG
6/21/19	DYNAMIC PRECISION GROUP, INC.-TURBOCOMBUSTOR TECHNOLOGY, INC.	Industrial	SrSec/BCF /LTCFR/PDR		U	Caa1	B3	SG
6/24/19	CASELLA WASTE SYSTEMS, INC.	Industrial	LTCFR/PDR		U	B1	Ba3	SG
6/24/19	VERINT SYSTEMS INC.	Industrial	SrSec/BCF /LTCFR/PDR		U	Ba2	Ba1	SG
6/24/19	PAREXEL INTERNATIONAL CORP.	Industrial	SrUnsec/SrSec /BCF/LTCFR	770	D	Caa1	Caa2	SG
6/24/19	BOYNE USA, INC.	Industrial	SrSec /LTCFR/PDR	400	U	B2	B1	SG

Source: Moody's

Ratings Round-Up

FIGURE 4

Rating Changes: Corporate & Financial Institutions – Europe

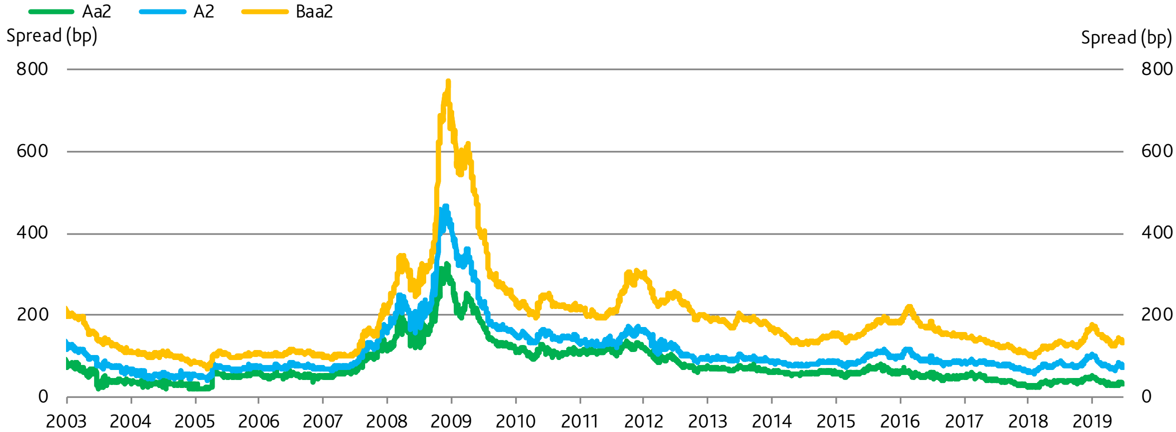
Date	Company	Sector	Rating	Amount ($ Million)	Up/ Down	Old LTD Rating	New LTD Rating	IG/ SG	Country
6/19/19	TURKCELL ILETISIM HIZMETLERI A.S.	Industrial	SrUnsec /LTCFR/PDR	500	D	Ba2	B1	SG	TURKEY
6/19/19	KOC HOLDING A.S.	Industrial	SrUnsec /LTCFR/PDR	2,250	D	Ba2	B1	SG	TURKEY
6/19/19	TURKIYE PETROL RAFINERILERI A.S.	Industrial	SrUnsec /LTCFR/PDR	700	D	Ba2	B1	SG	TURKEY
6/19/19	ORDU YARDIMLASMA KURUMU (OYAK)	Industrial	LTCFR		D	Ba2	B1	SG	TURKEY
6/19/19	EREGLI DEMIR VE CELIK FABRIKALARI T.A.S.	Industrial	LTCFR/PDR		D	Ba3	B1	SG	TURKEY
6/19/19	COCA-COLA ICECEK A.S.	Industrial	SrUnsec /LTCFR/PDR	500	D	Ba2	B1	SG	TURKEY
6/19/19	PSA INTERNATIONAL PTE. LTD.-MERSIN ULUSLARARASI LIMAN ISLETMECILIGI A.S.	Industrial	SrUnsec /LTCFR/PDR	450	D	Ba2	B1	SG	TURKEY
6/19/19	TURKIYE SISE VE CAM FABRIKALARI A.S.	Industrial	SrUnsec /LTCFR/PDR	1,200	D	Ba2	B1	SG	TURKEY
6/19/19	ANADOLU EFES BIRACILIK VE MALT SANAYII ANONIM SIRK	Industrial	SrUnsec /LTCFR/PDR	500	D	Ba2	B1	SG	TURKEY
6/19/19	TURK HAVA YOLLARI ANONIM ORTAKLIGI	Industrial	LTCFR/PDR	425	D	Ba3	B1	SG	TURKEY
6/19/19	APOLLO 5 GMBH	Industrial	SrSec /BCF/LTCFR		U	Caa1	B3	SG	GERMANY
6/19/19	DOGAN SIRKETLER GRUBU HOLDING A.S.	Industrial	LTCFR		D	Ba3	B1	SG	TURKEY
6/19/19	RONESANS GAYRIMENKUL YATIRIM A.S.	Industrial	SrUnsec /LTCFR	300	D	Ba3	B1	SG	TURKEY
6/20/19	LIBERTY BANK JSC	Financial	LTD		U	B1	Ba3	SG	GEORGIA
6/21/19	BANCO BILBAO VIZCAYA ARGENTARIA, S.A.-GARANTIBANK INTERNATIONAL N.V.	Financial	STD/LTD		D	Baa3	Ba1	SG	NETHERLANDS
6/25/19	TESCO PLC	Industrial	SrUnsec /MTN/CP	6,063	U	Ba1	Baa3	SG	UNITED KINGDOM

Source: Moody's

Market Data

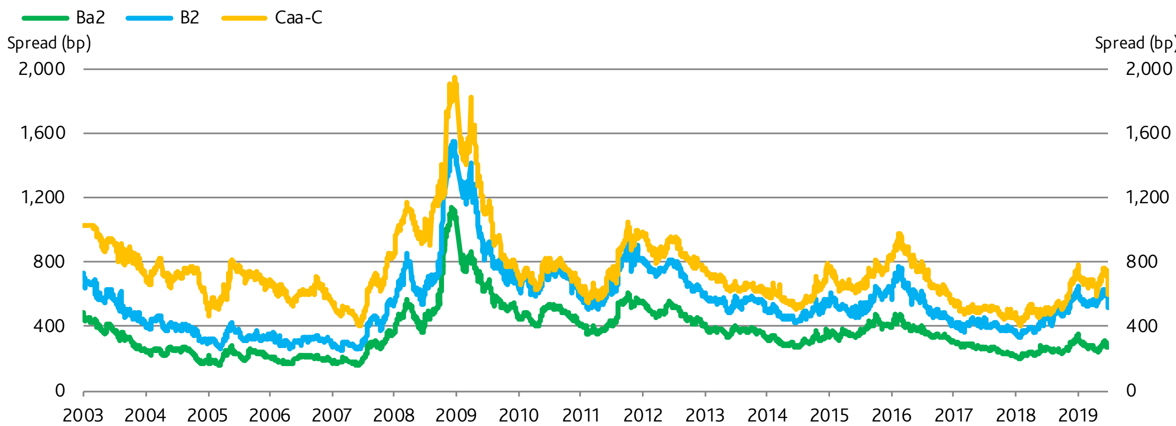
Spreads

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



Source: Moody's

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



Source: Moody's

Market Data

CDS Movers

Figure 3. CDS Movers - US (June 19, 2019 – June 26, 2019)

CDS Implied Rating Rises	CDS Implied Ratings		
Issuer	Jun. 26	Jun. 19	Senior Ratings
Oracle Corporation	Aa2	A1	A1
Amazon.com, Inc.	Aa3	A2	A3
Cisco Systems, Inc.	Aaa	Aa1	A1
Williams Companies, Inc. (The)	Baa2	Baa3	Baa3
Lowe's Companies, Inc.	A1	A2	Baa1
Kinder Morgan, Inc.	Baa2	Baa3	Baa2
Valero Energy Corporation	Baa1	Baa2	Baa2
Sempra Energy	Baa1	Baa2	Baa1
Apache Corporation	Ba1	Ba2	Baa3
Emerson Electric Company	A2	A3	A2

CDS Implied Rating Declines	CDS Implied Ratings		
Issuer	Jun. 26	Jun. 19	Senior Ratings
CVS Health	Baa3	Baa2	Baa2
Bristol-Myers Squibb Company	Aa3	Aa2	A2
PepsiCo, Inc.	A1	Aa3	A1
Enterprise Products Operating, LLC	Baa2	Baa1	Baa1
Altria Group Inc.	Baa2	Baa1	A3
General Electric Company	Ba1	Baa3	Baa1
Kraft Heinz Foods Company	Ba1	Baa3	Baa3
CSC Holdings, LLC	Ba3	Ba2	B3
Consolidated Edison Company of New York, Inc.	A3	A2	A3
CCO Holdings, LLC	Ba2	Ba1	B1

CDS Spread Increases		CDS Spreads		
Issuer	Senior Ratings	Jun. 26	Jun. 19	Spread Diff
Neiman Marcus Group LTD LLC	Ca	3,224	3,105	119
Penney (J.C.) Corporation, Inc.	Caa3	4,574	4,501	73
YRC Worldwide Inc.	Caa1	904	831	73
Dean Foods Company	Caa2	2,435	2,372	63
Avon Products, Inc.	B3	339	284	55
Rite Aid Corporation	Caa2	1,720	1,670	50
Weatherford International, LLC (Delaware)	Ca	5,944	5,899	45
Realogy Group LLC	B2	730	689	41
Beazer Homes USA, Inc.	B3	458	428	30
Qwest Corporation	Ba2	212	185	27

CDS Spread Decreases		CDS Spreads		
Issuer	Senior Ratings	Jun. 26	Jun. 19	Spread Diff
Nabors Industries Inc.	B1	553	700	-146
Diamond Offshore Drilling, Inc.	B3	484	546	-61
McClatchy Company (The)	Caa2	1,054	1,097	-43
Univision Communications Inc.	Caa2	367	396	-29
Chesapeake Energy Corporation	B2	807	833	-27
Cablevision Systems Corporation	B3	431	453	-23
Devon Energy Corporation	Ba1	94	115	-21
Hess Corporation	Ba1	120	141	-21
United States Steel Corporation	B2	555	576	-21
Unisys Corporation	B2	322	343	-21

Source: Moody's, CMA

Market Data

Figure 4. CDS Movers - Europe (June 19, 2019 – June 26, 2019)

CDS Implied Rating Rises	CDS Implied Ratings		
Issuer	Jun. 26	Jun. 19	Senior Ratings
ING Groep N.V.	A3	Baa1	Baa1
Swedbank AB	A1	A2	Aa2
Daimler AG	A3	Baa1	A2
Telecom Italia S.p.A.	B1	B2	Ba1
Eni S.p.A.	A3	Baa1	Baa1
Iberdrola International B.V.	Aa3	A1	Baa1
RWE AG	Aa1	Aa2	Baa3
Continental AG	Baa1	Baa2	Baa1
Anglo American plc	Baa3	Ba1	Baa2
Koninklijke Ahold Delhaize N.V.	A1	A2	Baa1

CDS Implied Rating Declines	CDS Implied Ratings		
Issuer	Jun. 26	Jun. 19	Senior Ratings
Italy, Government of	B1	Ba3	Baa3
Spain, Government of	A1	Aa3	Baa1
Dexia Credit Local	Ba2	Ba1	Baa3
Finland, Government of	Baa1	A3	Aa1
Banque Federative du Credit Mutuel	Aa3	Aa2	Aa3
NatWest Markets N.V.	Aa3	Aa2	Baa2
DZ BANK AG	Baa2	Baa1	Aa1
Landesbank Baden-Wuerttemberg	A2	A1	Aa3
DNB Bank ASA	Aa2	Aa1	Aa2
Banco Comercial Portugues, S.A.	Ba3	Ba2	Ba2

CDS Spread Increases		CDS Spreads		
Issuer	Senior Ratings	Jun. 26	Jun. 19	Spread Diff
Boparan Finance plc	Caa1	3,419	2,679	740
CMA CGM S.A.	B3	1,235	1,067	168
Casino Guichard-Perrachon SA	B1	839	741	98
Matalan Finance plc	Caa1	717	646	71
Jaguar Land Rover Automotive Plc	B1	569	535	34
PizzaExpress Financing 1 plc	Caa2	3,357	3,324	33
Eksportfinans ASA	Baa1	524	495	30
METRO Finance B.V.	Ba1	149	132	16
Premier Foods Finance plc	Caa1	180	168	12
Ensco Rowan plc	Caa1	606	598	9

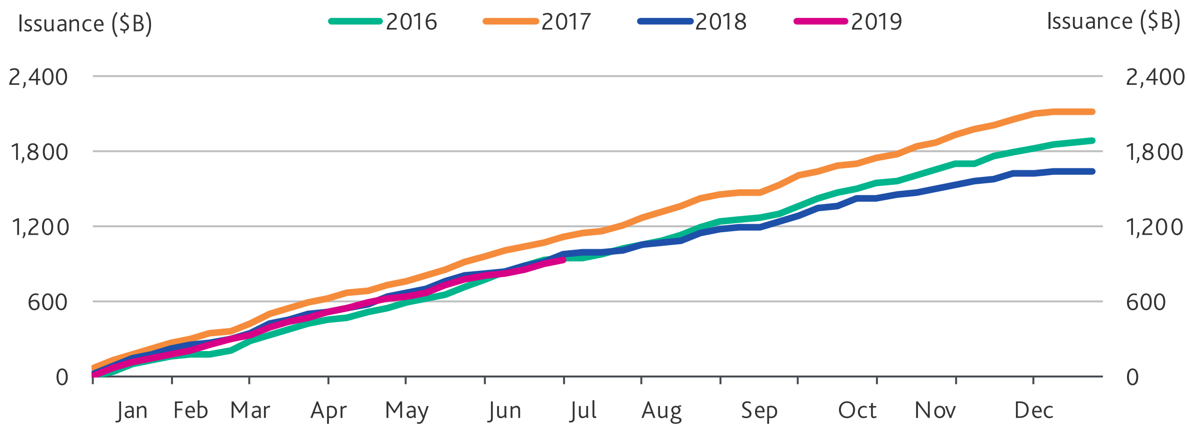
CDS Spread Decreases		CDS Spreads		
Issuer	Senior Ratings	Jun. 26	Jun. 19	Spread Diff
Galapagos Holding S.A.	C	13,247	18,689	-5,442
Novafives S.A.S.	Caa1	438	466	-28
Telecom Italia S.p.A.	Ba1	203	228	-24
Vue International Bidco plc	B3	224	245	-21
thyssenkrupp AG	Ba2	196	208	-12
Anglo American plc	Baa2	94	105	-12
ArcelorMittal	Baa3	160	171	-10
Suedzucker AG	Baa3	100	111	-10
Smurfit Kappa Acquisitions	Ba1	85	94	-9
Stena AB	B3	564	573	-9

Source: Moody's, CMA

Market Data

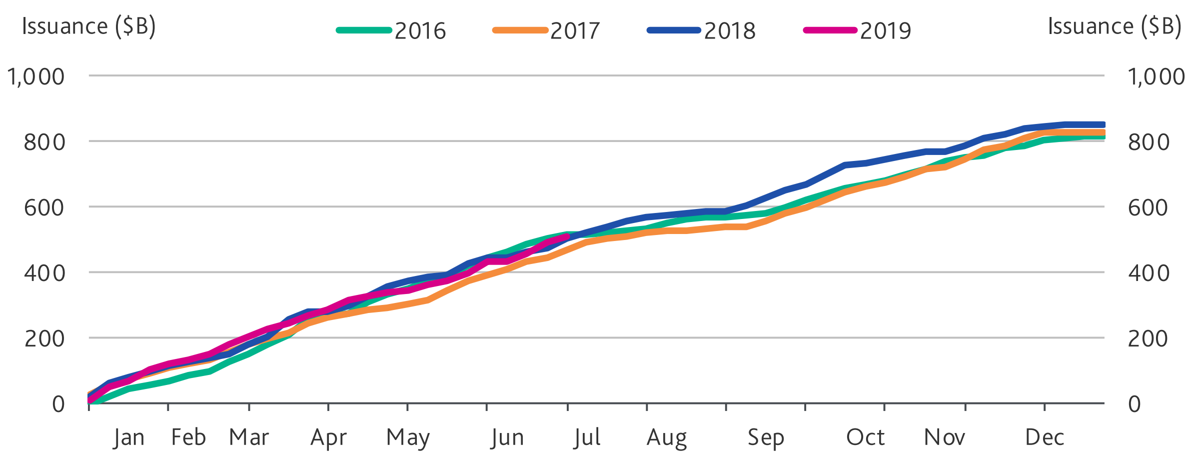
Issuance

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	16.224	11.475	29.754
Year-to-Date	683.811	206.767	932.375

	Euro Denominated		
	Investment-Grade	High-Yield	Total*
	Amount $B	Amount $B	Amount $B
Weekly	17.495	0.448	19.099
Year-to-Date	451.623	46.229	510.166

* Difference represents issuance with pending ratings.

Source: Moody's/ Dealogic

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