MOODY'S
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WEEKLY MARKET OUTLOOK

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High-Yield Might Yet Be Challenged by a Worsened Business Outlook

Credit Markets Review and Outlook *by John Lonski*

High-Yield Might Yet Be Challenged by a Worsened Business Outlook

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The Week Ahead

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

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The Long View

Full updated stories and key credit market metrics: The U.S. high-yield credit rating changes of 2019-to-date show downgrades doubling the number of upgrades.

Credit Spreads	Investment Grade: We see year-end 2019's average investment grade bond spread above its recent 127 basis points. High Yield: Compared to a recent 430 bp, the high-yield spread may approximate 500 bp by year-end 2019.
Defaults	US HY default rate: Moody's Investors Service forecasts that the U.S.' trailing 12-month high-yield default rate will dip from January 2019's 2.6% to 2.4% by January 2020.
Issuance	For 2018's US$-denominated corporate bonds, IG bond issuance sank by 15.4% to $1.276 trillion, while high-yield bond issuance plummeted by 38.8% to $277 billion for high-yield bond issuance's worst calendar year since 2011's 274 billion. In 2019, US$-denominated corporate bond issuance is expected to dip by 0.9% for IG to $1.265 trillion, while high-yield supply grows by 10.5% to $307 billion. A significant drop by 2019's high-yield bond offerings would suggest the presence of a recession.

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Credit spreads, CDS movers, issuance.

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Moody's Capital Markets Research *recent publications*

Links to commentaries on: Confidence vs. skepticism, Fed pause, default rates, high-yield bonds, stabilization, growth and leverage, buybacks, volatility, Fed policy, yields, profits, corporate borrowing, U.S. investors, eerie similarities, base metals prices, trade war.

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Click here for *Moody's Credit Outlook*, our sister publication containing Moody's rating agency analysis of recent news events, summaries of recent rating changes, and summaries of recent research.

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Credit Markets Review and Outlook

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

High-Yield Might Yet Be Challenged by a Worsened Business Outlook

High-yield bonds have led the credit market in terms of total return thus far in 2019. After soaring from 6.32% at the end of September 2018 to 8.06% by year-end 2018, a composite speculative-grade bond yield has subsequently dropped to February 20's 6.79%.

In turn, the total return from high-yield bonds went from the -2.3% of the three-months-ended December 2018 to the 5.7% of 2019-to-date. Among 2019-to-date's other total returns were the 2.65% of investment-grade corporate bonds that included a 3% return for Baa-grade corporates.

The year-to-date drop by the composite speculative-grade bond yield helped to narrow the accompanying high-yield bond spread from the 553 basis points of year-end 2018 to a recent 430 basis points.

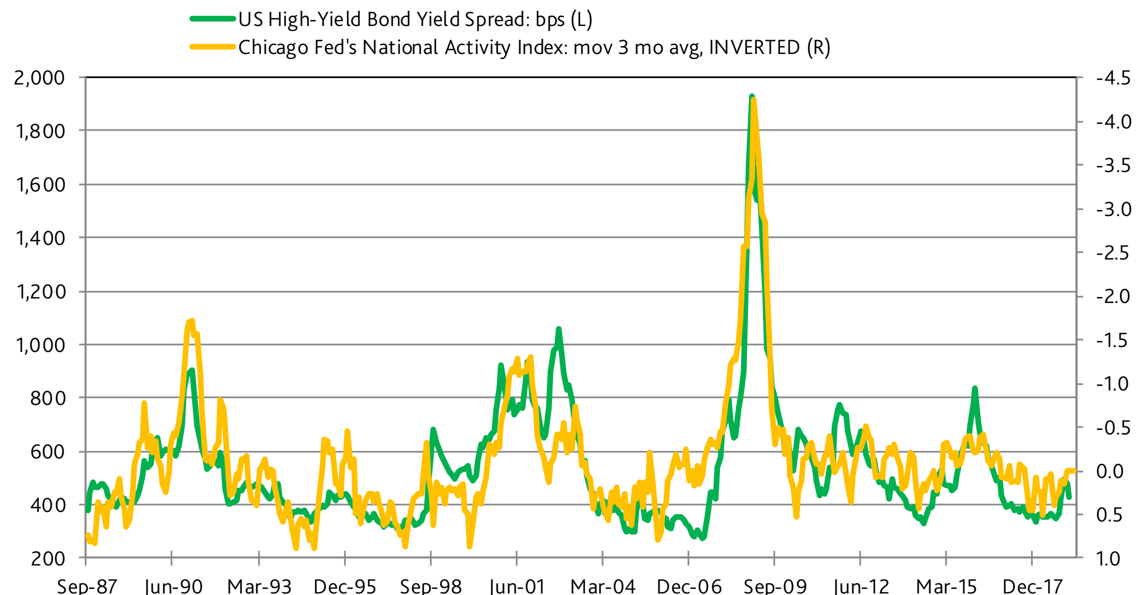
The valuation of high-yield bonds currently receives support from expectations of corporate earnings growth into 2020 and a related benign outlook for defaults. Though S&P 500 earnings per share are likely to dip year over year in 2019's first quarter, this metric is expected to post yearly beginning with the second quarter and well into 2020.

In terms of monthly observations, the high-yield bond spread reveals relatively strong correlations of -0.83 with the moving-three-month average of the Chicago Fed's national activity index, 0.81 with the VIX, -0.79 with the three-month percent change of private-sector payrolls, 0.76 with the median expected default frequency metric of high-yield issuers, and 0.74 with the average expected default frequency metric of high-yield issuers.

National Activity Index Gives Direction to High-Yield Spreads

Among all possible macroeconomic indicators, the high-yield bond spread exhibits its strongest correlation with the 80-variable national activity index. The NAI's latest three-month average of 0.16 points favors a 463-basis point midpoint for the high-yield bond spread.

Figure 1: Chicago Fed's 85-variable National Activity Index Favors a 463 bp Midpoint for High-Yield Bond Spread
sources: Chicago Federal Reserve Bank, Moody's Analytics



Both the long-term average and median of the NAI equal 0.0 by design. When business activity proceeds at an above-trend pace, the NAI is greater than zero.

The record high for the NAI's moving three-month average was set in April 1978, or when the 0.61% average monthly increase by payrolls equates to 925,000 new jobs per month given the size of today's payroll employment. Also, 1978's second quarter was home to a scintillating 16.4% annualized quarterly surge by real GDP. Thus, it may be of no surprise that the spread over Treasuries for Moody's long-term Baa industrial company bond yield average was merely 78 basis points in April 1978, which was much thinner than its recent 206 basis points.

The high-yield bond spread tends to be thinner; the faster is the growth of private-sector payrolls over a three-month span. The 0.55% increase by private-sector payrolls during the three-months-ended January 2019 has been historically associated with a 458-basis point midpoint for the high-yield bond spread.

Latest National Activity Index Implies Inflation Risks Are Well Contained

Moreover, 1978's unsustainably rapid economic growth set the stage for persistently rapid price inflation. The NAI's 0.99 point average of 1977-1978 gave rise to the breakneck consumer price inflation of 1979-1981.

According to the Chicago Fed, recurring increases by consumer price inflation have been associated with a greater than 0.70-point moving three-month average for the NAI. This metric last briefly exceeded 0.70 point in December 2005 and January 2006. Moreover, the NAI's six-month average last reached 0.70 point in January 1995, while the NAI's moving 12-month average has not posted a score of at least 0.70 point since December 1984. Thus, the NAI's 0.16-point average of 2018's final quarter favors the near-term containment of price inflation.

When the NAI is less than zero, business activity is below trend. The record low for the NAI's three-month average is the -4.25 points of the span ended January 2009, or when the high-yield bond spread averaged 1,732 basis points.

Low VIX Favors Thinner High-Yield Bond Spread

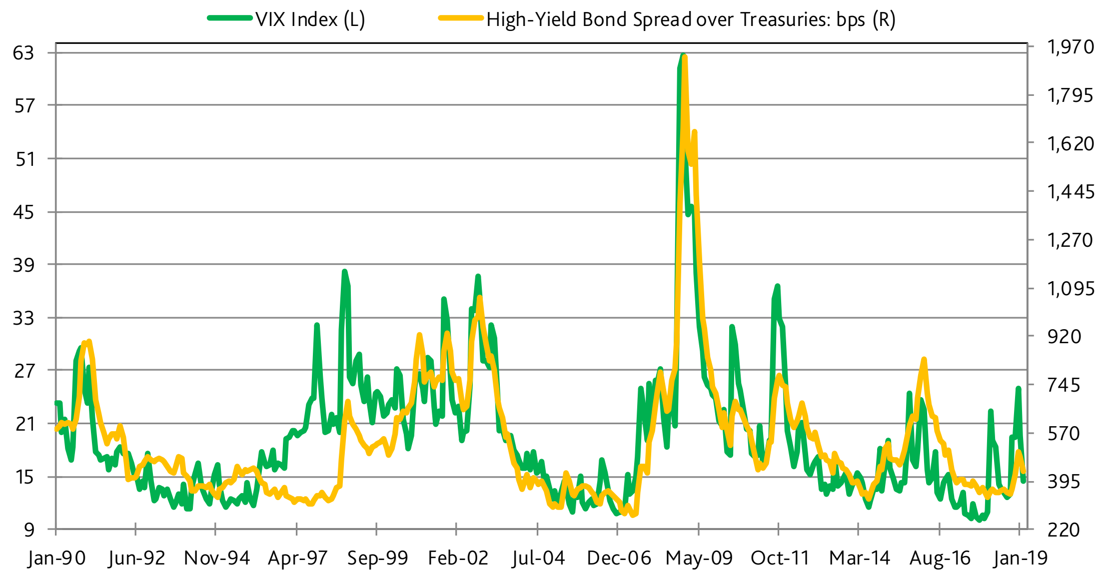
The strong correlation between the VIX and the high-yield bond spread underscores the importance of the U.S. equity market to corporate credit. All else the same, the risk of default should decline as the equity market assigns a greater and more stable value to the corporate assets and earnings streams backing corporate debt.

A healthy equity market enhances systemic liquidity. Financially stressed companies can more easily raise cash via the divestment of assets when the VIX is low and price-to-earnings multiples are high.

The recent VIX of 14.3 points was well under its long-term median of 17.5 points. For a sample that commences in January 1990, the accompanying long-term median of the high-yield bond spread is 472 basis points. A recent 14.3-point VIX favors a 416-basis point midpoint for the high-yield bond spread.

Figure 2: Both the High-Yield Bond Spread and the VIX Are Less than Their Post-1989 Medians of 472 bps and 17.5 points, Respectively

sources: CBOE, Moody's Analytics



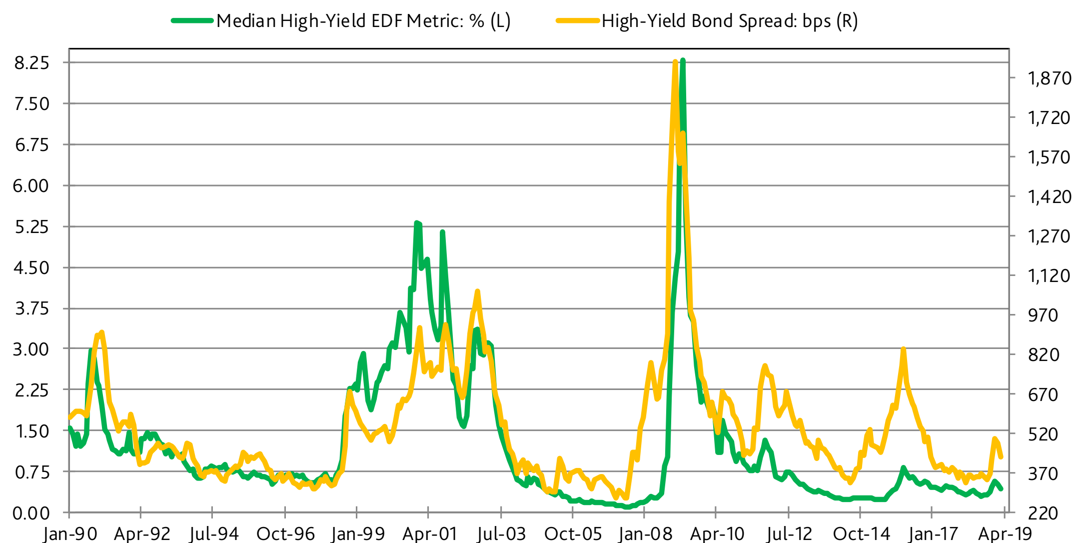
Median EDF Favors a Thinner High-Yield Spread Compared With Average EDF

The expected default frequency metric will be lower, the greater is the market value of a company's net worth, and the lower is the volatility of the market value of a company's business assets. Like high-yield spreads, the EDF is a forward-looking indicator of defaults.

If default risks are high due to the difficulties facing one or several industries, the median EDF may offer a better measure of the underlying credit risks of high-yield issuers. February-to-date's 0.43% median for the high-yield EDF is less than its long-term median of 0.73%. The combination of the 0.43% median EDF and its slight dip of the last three months favors a 430-basis point midpoint for the high-yield bond spread.

Figure 3: Recent Median High-Yield EDF Metric and Its Three-Month Difference Are Consistent with a 430 bp Midpoint for the High-Yield Bond Spread

source: Moody's Analytics

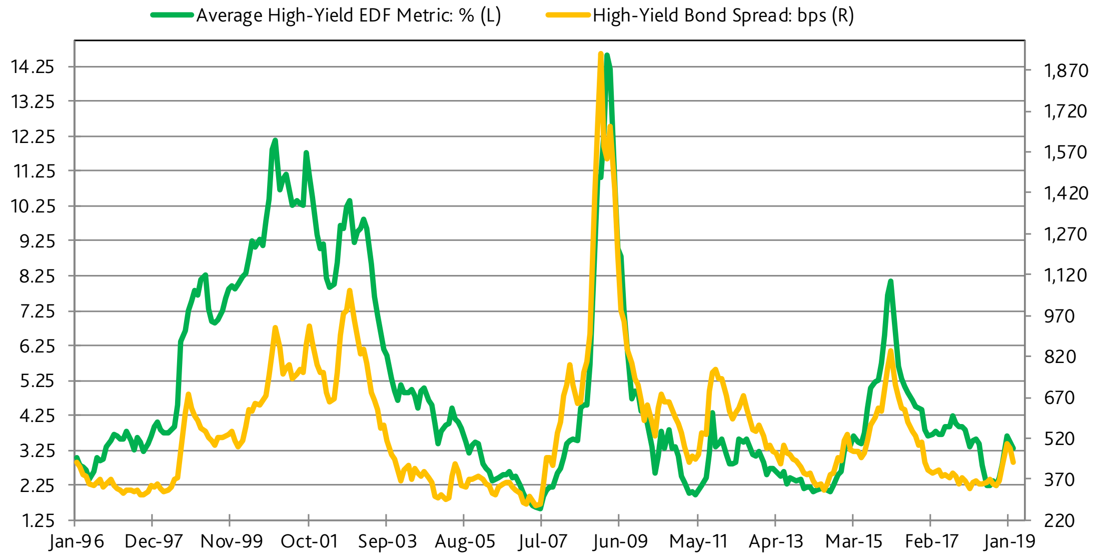


Credit Markets Review and Outlook

Though February-to-date's average high-yield EDF of 3.3% is well under 3.8% long-term median, the fact that it is up from its reading of three months earlier helps to explain why the average EDF now favors a somewhat wider 461-basis point midpoint for the high-yield bond spread.

Figure 4: Recent Average High-Yield EDF Metric and Its Three-Month Difference Favor a 461 bp Midpoint for the High-Yield Bond Spread

source: Moody's Analytics



Claims of a Strong Economy May Be Hyperbole

In some respects, the minutes of the January 29-30 FOMC meeting seemed dated. For one thing, the FOMC may have inadvertently exaggerated the strength of fourth-quarter 2018's household spending.

Much to the contrary, December 2018's seasonally adjusted retail sales sank by 1.2% from November's pace, while, before seasonal adjustment, the year-over-year increase of retail sales dropped from the lively 5.4% of July-November 2018 to December's dull 1.4%.

In response to December's lousy retail sales report, the Atlanta Fed's GDPNow estimate for the annualized quarterly increase of fourth-quarter 2018's real consumer spending was slashed from 3.7% at the time of the January 29-30 FOMC meeting to the latest 2.6%, or after unexpectedly weak news on December's retail sales was released on February 14. The downgraded outlook for real consumer spending helps to explain why the GDPNow projection for the annualized sequential growth for fourth-quarter 2018's U.S. real GDP was cut from the 2.8% of January 18 to a now measly 1.4%.

Early indications hint of an uninspiring pace of first-quarter 2019's real consumer spending. For example, January 2019's unit sales of cars and light trucks in the U.S. fell by 5.1% from December 2018's pace on a seasonally adjusted basis to 16.6 million annualized units. January's monthly drop was the deepest since the 8.1% plunge of May 2011, while January's seasonally adjusted annualized sales pace was the lowest since the 16.4 million units of August 2017.

The FOMC's January 2019 minutes also mentioned December's strong showing by manufacturing output. Nevertheless, after growing by 0.8% monthly in December 2018, manufacturing output contracted by 0.9% monthly in January 2019.

Elsewhere, housing activity may remain hobbled by untenably high home prices. As recently as the span ended January 25, the moving four-week average of the Mortgage Bankers Association's index of mortgage applications for the purchase of a home set a record high for the current recovery. However, less than four weeks later, February 15's four-week moving average for homebuyer mortgage applications was 8.5% under January 25's high.

In summary, the flatness of early 2019's business activity preserves the possibility of yet lower Treasury bond yields. It's for good reason that the futures market assigns merely a 5% likelihood to fed funds ending 2019 above their current 2.375% midpoint.

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

THE U.S.

By Ryan Sweet, Moody's Analytics

Roger, Roger. What's Our Vector, Victor?

The normalization of the Federal Reserve's balance sheet goes from autopilot to emergency landing. The minutes from the January meeting of the Federal Open Market Committee showed that almost all participants thought it would be desirable to announce, before too long, a plan to stop reducing the Fed's asset holdings later this year. Balance sheet aside, the minutes echoed Fed Chairman Jerome Powell's view that patience in regard to future changes to the fed funds rate range would "allow time for a clearer picture of the international trade policy situation and the state of the global economy to emerge."

The Fed's shift lends downside risk to our forecast for the 10-year Treasury yield to end this year at 3.36% and finish near 3.5% in 2020. Baked into the forecast is that solid nominal GDP growth pushes long-term rates higher, but this isn't a slam dunk. Long-term Treasury yields have less correlation to GDP growth than is generally believed. Since 1960, the 10-year yield has normally remained below year-over-year nominal GDP growth, except for the late 1970s and 1980s, when inflation was high. Since 2010, the 10-year yield has been 1.5 percentage points below nominal GDP growth. If this relationship continues to hold, this is a fairly sizable hurdle to higher long-term rates over the next couple of years.

Also, since 1990, the 10-year Treasury yield has generally peaked around the terminal fed funds rate. This implies limited upside for the 10-year Treasury yield this year. With this tightening cycle on pause for now, there is limited upside for long-term interest rates.

The Fed's balance sheet also could limit the rise in long-term rates. The minutes reiterated that the Fed still intends to hold primarily Treasury securities in the long run. Therefore, it would be appropriate once asset redemptions end to reinvest most, if not all, principal payments received from agency mortgage-backed securities in Treasury securities. In other words, the Fed will be a net purchaser of Treasuries.

To assess the impact of a lower 10-year Treasury yield on the economy, we ran a simulation of our U.S. macro modeling, assuming the 10-year Treasury yield remains around 2.68% this year. This would add 0.1 to 0.2 percentage point to GDP growth this year, relative to the baseline.

We will revisit our assumptions for the Fed's balance sheet, but the minutes suggest that the runoff will end sooner than we anticipated. Our initial thoughts are that the Fed will announce in March that the runoff in the balance sheet will end in the fourth quarter of this year. The balance sheet could decline to $3.7 trillion, compared with the $3 trillion to $3.5 trillion we previously anticipated.

Other changes seem to be brewing. A few participants expressed concerns that in the current environment of increased uncertainty, the policy rate projections (the dot plot) don't accurately convey the FOMC's policy outlook. The Fed needs to kill the dot plot. The dot plot was introduced in late 2011 when the Fed was considering how to prepare markets for the shift it hoped to make away from the unprecedented array of monetary support measures it had put in place after the financial crisis.

The objective for the dot plot was to give markets a look into the Fed's thinking beyond any immediate meeting. Given the shift toward more data dependence, the usefulness of the dot plot has run its course. It will be difficult to provide any significant clarity or direction on the path of interest rates beyond one or two meetings. Continuing to provide the dot plot, which is often misunderstood, would convey the Fed has an a priori view of where rates are headed. It also signals that the Fed still plans to turn policy restrictive in 2020, fanning market concerns that the Fed's plan is to hike until something

breaks. On the contrary, the interest rate projections are not set in stone and are likely causing the Fed more problems than they are worth.

In January, the Fed said that it is sticking with its current monetary policy framework and that the fed funds rate remains its primary tool. This likely remains an open debate and changes are possible. The fed funds market is a shell of its former self. Trading volumes in the fed funds market have fallen and the Federal Home Loan Banks are the only significant lenders remaining, but the borrower base is dominated by non-U.S. institutions seeking to arbitrage the interest on excess reserves.

The effective fed funds rate barely moves each day and is somewhat disconnected from other overnight interest rates, including the secured overnight financing rate. Unless there is legislation that allows the Fed to pay IOER—interest rate on excess reserves—to the GSEs, it seems unlikely that fed funds trading volumes will recover in an environment where bank reserves are permanently ample. Banks may turn to the fed funds market only if they face a temporary overdraft in their intraday clearing account at the Fed or can earn an IOER spread. However, the IOER spread is fairly thin now.

Therefore, the Fed will continue to debate whether the fed funds rate is the appropriate rate to target. There are possible replacements. Recognizing the narrowness of the fed funds market, the Fed created the overnight bank funding rate in 2016 to provide more clarity on overnight unsecured funding markets. Though the Fed isn't ready to ditch the fed funds rate, change could be coming.

Next week will be busy. Fourth quarter GDP will be released and our current tracking estimate is 1.7% at an annualized rate. Other key data include housing starts, factory orders, ISM manufacturing survey, vehicle sales, construction spending, personal income/spending and the PCE deflator.

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

EUROPE

By Barbara Teixeira Araujo of Moody's Analytics in Prague

Expect Euro Zone Joblessness to Hold Steady at 7.9%

The week ahead highlight will be the preliminary euro zone inflation figures for February. We expect them to show that the area's CPI rose by 1.4% y/y in the middle of the first quarter, a reading similar to January's. The decline in energy inflation is expected to have paused, though risks remain to the downside due to base effects in oil prices. Elsewhere, we expect that food inflation gained some ground after having read below its trend for several months, especially as February's warmer-than-average weather likely put downward pressure on fresh produce prices. Regarding core inflation, we expect that it remained steady at 1.1%. Services inflation is expected to have held steady at 1.6%, following a jump in January, while core goods inflation likely increased slightly to 0.4%, from 0.3%. Due to rounding, though, this won't be enough to lift the core rate to 1.2%.

December euro zone unemployment figures are also on the calendar. We expect that joblessness managed to hold steady at 7.9%, its lowest in over 10 years. Despite the recent easing in confidence and growth figures, our view is that the currency area labour market should continue to perform well in 2019, notably because it is a lagging indicator of the economic momentum. If we don't see some stabilization in the figures soon enough, we will be forced to revise down our employment growth expectations for this year. For now, though, we continue to expect that the unemployment rate will edge lower to 7.6% in the next six to nine months.

In France, final fourth-quarter GDP numbers are set to confirm that the euro area's second-largest country grew by 0.3% q/q in the final quarter of 2018, the same rate as in the previous stanza. Among the area's four major countries, France's performance was second only to Spain, whose GDP rose by a stunning 0.7% q/q at the end of 2018. We expect the figures to confirm that domestic demand slowed,

dragged by an easing in consumer spending and investment, while net trade contributed 0.2 percentage point due to a jump in exports that was larger than the rise in imports. The drag from inventories, meanwhile, is expected to have eased sharply to only 0.1 percentage point, from 0.5 percentage point in the previous quarter. In all, then, the details are expected to have been much less optimistic than the headline, though we are not putting much weigh on the fourth-quarter figures. They were severely impacted by the disruptions caused by the 'yellow vests' protests.

In the U.K., the main focus won't be on the economic data, but on the political front. On Wednesday the British Parliament is likely to discuss a motion on Brexit, and we expect that several amendments will be put on the table. Focus will be on the Cooper amendment—the no-deal amendment—which would likely be selected by the speaker for voting if Prime Minister Theresa May has not convinced Members of Parliament of her Brexit plan. In practice, this amendment would force May to take the no-deal scenario off the table by mid-March if no deal is agreed by then. That's because the amendment would require May to present Parliament with either no-deal plans that would be put to vote, or a plan to extend the negotiations for a set period. Since it is extremely unlikely that Parliament would vote for a no-deal exit, the default option would be for May to go back to the EU with a plan to extend Article 50, thus avoiding a cliff-edge Brexit. It is still not 100% sure that the EU would agree to an extension. EU politicians have recently voiced they have grown tired of the negotiations, and especially of the lack of clarity from the U.K. Parliament. But our view remains that Brussels, when push comes to shove, would not risk plunging the European continent into economic chaos and be responsible for the dire consequences of such a scenario.

Another amendment that is expected to be put to vote is the Kyle-Wilson compromise. It consists of a proposal that Remain-supporting MPs pass May's deal, but on the condition that the deal would then be put to public vote. While this amendment makes sense, as it shares the responsibility of any Brexit outcome between Parliament and British citizens, current evidence suggest that it is unlikely that this compromise will get support from a majority of lawmakers. Last but not least, a new referendum amendment could also be put to vote, though here too we think that there will be no majority for it.

	Key indicators	Units	Moody's Analytics	Last
Mon @ 5:00 p.m.	France: Job Seekers for January	mil, SA	3.42	3.42
Wed @ 10:00 a.m.	Euro Zone: Business and Consumer Sentiment for February	index	105.6	106.2
Thur @ 7:45 a.m.	France: Household Consumption Survey for January	% change	0.4	-1.5
Thur @ 7:45 a.m.	France: GDP for Q4	% change	0.3	0.3
Fri @ 7:00 a.m.	Germany: Retail Sales for January	% change	2.0	-4.3
Fri @ 9:00 a.m.	Italy: Unemployment for January	%	10.5	10.3
Fri @ 10:00 a.m.	Euro Zone: Preliminary Consumer Price Index for February	% change	1.4	1.4
Fri @ 10:00 a.m.	Euro Zone: Unemployment for January	%	7.9	7.9

ASIA-PACIFIC

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

Consumption a Key Driver as India's GDP Keeps Expanding

India's GDP likely expanded 7.2% in the final quarter of 2018, bringing full-year GDP growth to 7.6%, after 6.2% in 2017. Consumption will remain the key fourth quarter growth driver, although distress in the agriculture sector likely slowed consumption growth in the December quarter. The economy muddled through 2018, as various crosswinds continue to hamper investment. The central bank raised interest rates twice in the middle of 2018 on the back of sharp capital outflows. This likely slowed credit growth in the final quarter, while corporate balance sheets still are not conducive to investment

accelerating. Government spending likely supported growth in the final quarter, while the sharp drop in oil prices improved India's current account position. We expect the economy to continue to grow 7.7% in 2019; recent rate cuts will support credit lending, while fiscal support measures to the agriculture sector and more broadly the economy ahead of the April elections will buttress consumption.

Hong Kong's GDP growth likely picked up to 0.5% q/q in the December quarter, after rising just 0.1% in the September quarter. We expect the net exports contribution to fourth quarter GDP growth improved, after a surge in goods imports mostly overwhelmed decent improvement in exports over the quarter. We expect annual GDP growth slowed to 2.4% in the December quarter, its weakest pace in two years, and down from 2.9% in the third stanza and 3.5% in the second. In the third quarter national accounts release the government explicitly mentioned the increasing downside risks from the still-unresolved U.S.-China trade war, a particular concern for Hong Kong given its outsize exposure to foreign demand as a stimulant for GDP growth. The longer the trade war continues, the higher the adverse impacts on global trade flows.

We expect China's official manufacturing PMI rose 0.1 point to 49.6 in February. This will keep it close to its lowest level in three years and in contraction territory. We expect that the new orders subcategory will also remain below the neutral level of 50, a sign of subdued global demand, a consequence of global demand being past its peak for this cycle, with the trade war an added drag. Overall, manufacturing remains in a downturn. Although Beijing has moved to shore up growth in recent months, the slowdown in global demand and disruptions from the trade war are likely to keep manufacturing relatively muted in 2019.

	Key indicators	Units	Confidence	Risk	Moody's Analytics	Last
Tues @ 8:00 a.m.	South Korea Consumer sentiment survey for February	Index	3	↑	97.0	97.5
Wed @ 7:30 p.m.	Hong Kong GDP for Q4	% change	3	↓	0.5	0.1
Thurs @ 10:50 a.m.	Japan Retail sales for January	% change yr ago	3	←	0.9	1.3
Thurs @ 10:50 a.m.	Japan Industrial production for January	% change	2	↑	0.1	-0.1
Thurs @ 11:00 a.m.	South Korea Retail sales for January	% change	3	←	0.5	0.8
Thurs @ 11:00 a.m.	China Official manufacturing PMI for February	Index	3	←	49.6	49.5
Thurs @ 6:30 p.m.	Thailand Foreign trade for January	US$ bil	2	↓	0.9	2.5
Thurs @ 11:00 p.m.	India GDP for Q4	% change yr ago	3	↓	7.2	7.1
Thurs @ Unknown	South Korea Monetary policy for February	%	4	←	1.75	1.75
Fri @ 10:30 a.m.	Japan Unemployment rate for January	%	4	←	2.4	2.4
Fri @ 10:50 a.m.	Japan Machinery orders for January	% change	2	↓	0.5	-0.1
Fri @ 4:00 p.m.	Japan Consumer confidence survey for February	Index	3	←	41.6	41.9
Fri @ Unknown	South Korea Foreign trade for February	US$ bil	2	←	0.5	1.3

The Long View

The U.S. high-yield credit rating changes of 2019-to-date show downgrades doubling the number of upgrades.

By John Lonski, Chief Economist, Moody's Capital Markets Research Group
February 21, 2019

CREDIT SPREADS

As measured by Moody's long-term average corporate bond yield, the recent investment grade corporate bond yield spread of 127 basis points exceeded 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 that what is suggested by the accompanying long-term Baa industrial company bond yield spread of 206 bp but is somewhat wider than what is suggested by an accompanying VIX of 14.3 points.

DEFAULTS

January 2019's U.S. high-yield default rate of 2.6% was less than the 3.6% of January 2018. Moody's Investors Service now expects the default rate will average 2.4% during 2019's fourth 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.

Fourth-quarter 2017 revealed year-over-year advances for worldwide offerings of corporate bonds of 17.6% for IG and 77.5% for high-yield, wherein US$-denominated offerings posted increases of 21.0% for IG and 56.7% for high yield.

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.

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 changes for 2019's worldwide corporate bond offerings are -0.5 % for IG and +4.4% for high yield.

US ECONOMIC OUTLOOK

As inferred from the CME Group's FedWatch Tool, the futures market recently assigned an implied probability of merely 5% to at least one Fed rate hike in 2019. 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
February 21, 2019

EURO ZONE

The euro zone flash PMI figures released Thursday came in mixed. While we welcomed a rise in the area's composite index to 51.4 in February from 51 in January, the downside was that the sectoral details showed activity in the manufacturing sector contracted over the month for the first time since mid-2013. Accordingly, the manufacturing PMI slid to 49.2 from 50.5 in January.

That new orders in manufacturing dropped the most in almost six years only added to the grim picture for factory growth, as it suggested that the downturn in the industry will only intensify over the coming months. Domestic and external new orders each fell more sharply than in January, confirming our fears that the deterioration is not only due to the recent slowdown in the global economy (especially in China), but that the momentum at home is fading as well. True, we still expect some rebound in industrial production in the first quarter of this year following a 1.4% q/q decline in the fourth stanza of 2018, but all indicators suggest that the rise will be minimal.

Elsewhere, that services activity has strengthened brought at least a little cheer. In the spotlight was that employment growth in the sector accelerated further in February, corroborating our view that the labour market will continue to perform relatively well this year, even if we do expect an increase in the unemployment rate. For the time being, the tight labour market should continue to be translated into higher wage gains, which, combined with an easing in inflation pressures should boost households' purchasing power and will to spend.

Across the area's two major economies, the weakness in manufacturing was concentrated mainly in Germany, where firms reported lower orders from the auto sector (following the change of the EU emissions regulation on September 1) and a drop in demand from Asia linked to the ongoing trade tensions. Given that Germany is an export-driven economy, it is no wonder that its manufacturing sector is suffering more than that of France. Accordingly, France's manufacturing PMI rose to 51.4 in February from 51.2 in January, and that's despite reports of lingering disruption caused by the 'yellow vests' protests.

Overall, we maintain that the direction of travel is to the downside. Any rebound in services inflation—in line with the tight labour market—is unlikely to be enough to offset lower core goods, electricity and motor fuels inflation. For the BoE, this means that softer headline and core inflation pressures combined with lower growth will allow the Monetary Policy Committee to stay put for as long as there is still no clarity on what the U.K.-EU future relationship will look like. The BoE wouldn't want to kick the economy when it's down, and the lower inflation pressures will give it justification to stick to its wait-and-see strategy.

ASIA PACIFIC

By Katrina Ell of Moody's Analytics
February 21, 2019

CHINA

China's monthly trade surplus narrowed to US$39.2 billion in January, following December's US$57.1 billion. Exports surprisingly accelerated to 9.1% y/y, from a 4.4% drop in December; seasonality related to the timing of Lunar New Year is likely behind the unexpected annual acceleration. The holiday began on 4 February this year, while it occurred in mid-February in 2018.

The first two months of the calendar year are notoriously difficult for getting a clear look at China's underlying economic performance. With this in mind, we expect to see a deceleration in annual export growth in February due to the weeklong celebrations, but the slump may not be as severe as in 2018 because of some

of the slowdown being captured in January. This is because production and broader business activity generally slow up to two weeks before the start of the celebration as workers return home. Imports fell by 1.5% y/y in January, after a 7.6% drop in December.

Trade war impacts

A clear sign of the U.S.-China trade war is in Chinese imports of U.S. goods, which dropped by 41% y/y in January, the fastest annual drop on record. The Lunar New Year cannot be blamed for this deep fall, as Chinese imports of U.S. goods were down by 36% in December and 25% in November. Tariffs on U.S. soybean imports likely contributed to this slump, since winter is usually the peak import season from the U.S. Under normal trade conditions, soybeans account for around 60% of China's U.S. agriculture imports. Instead, China has been sourcing soybeans elsewhere, including Brazil. In the six months to December, Brazilian soybean exports to China increased 70% on a volume basis and almost 80% by value. In late January, China pledged to purchase an additional 5 million tonnes of U.S. soybeans per day, which should improve imports of U.S. goods from February.

We expect 2019 will be challenging on the export front. The trade war is exacerbating already cooling external demand. Global trade had been driven by the synchronized upturn in growth among the world's major economies from around mid-2016. But with this upturn fizzling in 2018, exports and manufacturing have subsequently weakened, with the disruptions caused by the trade war adding to the slowdown. Reflecting this, China's official manufacturing PMI remains in contraction territory, with new export orders in decline in its January reading for the eighth consecutive month.

Tame inflation

Consumer price inflation cooled further in China to 1.7% y/y in January, the weakest reading since January 2018 and down from 1.9% in December. The main culprit of the slowdown was weaker food prices, with growth slipping to its slowest in five months. Nonfood price inflation held steady at 1.7%. An important driver of weak food prices is pork, where prices were down by 3.2% y/y. Risks of an outbreak from African swine flu prompted farms to increase slaughtering, which weighed on domestic pork prices since November, normally the peak consumption season, according to the Ministry of Agriculture and Rural Affairs.

Pork prices likely will pick up by the second half of 2019 because farmers currently are unwilling to restock their herds due to the swine flu threat. According to the agriculture ministry, the number of breeding sows dropped more than 5% in January for a third straight month, signalling fewer available pigs and eventually higher demand. While the exact weights of China's CPI basket are not known, pork is a staple of the Chinese diet, and past swings in pork prices have clearly influenced the headline.

CPI growth was 2.1% last year, comfortably beneath Beijing's 3% target. That target remains in place for 2019, and like in 2018, it is unlikely to be threatened this year. Inflation is not a primary concern for policymakers, but it enables Beijing to keep the light firmly green for release of further piecemeal stimulus measures in 2019 to shore up domestic demand amid a less supportive global environment and uncertain trade policy.

Producer price weakness

Producer prices in China edged up just 0.1% y/y in January, the weakest reading since August 2016 and down from a 0.9% rise in the prior month. The weakness was driven by a drop in raw materials prices, which fell 1.6% y/y after rising 0.8% in the month prior. This resulted in prices for production materials slipping 0.1% y/y, after a 1% lift in December. Producer price inflation has decelerated for seven consecutive months, adding to other signs of cooling industrial activity amid weakening global demand.

There is a strong correlation between consumer and producer prices in China. However, weak producer prices do not always feed through to the CPI because of the large weight of heavy industries in the PPI. Instead, an important implication of the slowdown in producer price inflation is its impact on industrial profit growth, which tends to track trends in producer prices. Indeed, industrial profit growth has slowed noticeably in recent months, and could begin to undermine investment at a time of already slowing economic growth, adding to Beijing's existing impetus to step up easing.

The Long View

(Measured) stimulus is rolling in

Evidence of stimulus is materializing in China. Total social financing—a broad measure of credit and liquidity—improved to 10.4% y/y in January, from the record low 9.8% in December. New bank loans reached a record high CNY3.23 trillion in January, comfortably above the CNY2.9 trillion new bank loans in January 2018, the prior record high. But liquidity conditions remain relatively tight, a symptom of Beijing's wary approach to releasing stimulus while keeping important deleveraging efforts from losing momentum.

In what must be a pleasing development for policymakers, demand for credit to the corporate sector blossomed in January. Corporate loans increased to CNY2.58 trillion, up from December's CNY473 billion. But comparing with December data can be misleading given that banks front-load loans early in a calendar year. More telling is that corporate loans accounted for 80% of new loans in January, higher than December's 44% share. The corporate sector, particularly small to medium-size businesses, have been a particular target for stimulus. But it is a difficult balancing act, as stimulus to smaller firms cannot be extended with significant vigour given there are concerns about debt serviceability, particularly with slowing domestic demand.

Ratings Round-Up

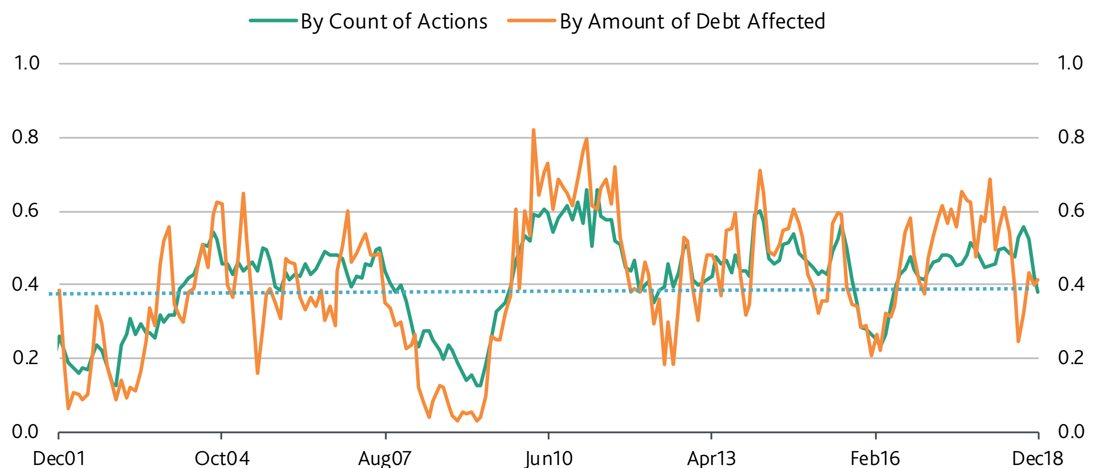
U.S. Rating Activity Weakens

By Michael Ferlez

U.S. rating activity weakened over the week ending February 19. All 10 of the week's rating changes were downgrades. Notable downgrades include Washington Prime Group Inc., Stillwater Mining Company, and Jones Energy Holdings. Washington Prime Group Inc. had its senior unsecured credit rating cut one notch to Ba2 from Baa3. The downgrade changes the classification of the firm's senior unsecured debt from investment- to speculative-grade. The decline in the number of positive credit actions in recent months is indicative of the recent volatility in financial markets. From October to January, the spread between Baa corporate bonds and the 10-year Treasury increased 49 basis points. Rising borrowing costs and greater uncertainty over global growth pose a serious downside risk to corporate credit quality.

European rating change activity remained strong last week, with upgrades accounting for three of the five changes. The recent upgrade of Russia's sovereign credit rating remained a positive tailwind for rating activity last week, with two more Russian firms receiving rating upgrades. Rounding out the list of upgrades was Hapag-Lloyd AG, which had its senior unsecured credit rating raised to B3 from Caa1. On the downgrade side, Nostrum Oil & Gas PLC's senior unsecured credit rating was downgraded to B2 from B3, reflecting the expectation that the company's financial metrics would weaken in 2019.

FIGURE 1
Rating Changes - US Corporate & Financial Institutions: Favorable as % of Total Actions



* Trailing 3-month average
Source: Moody's

FIGURE 2

Rating Key

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

FIGURE 3

Rating Changes: Corporate & Financial Institutions – US

Date	Company	Sector	Rating	Amount ($ Million)	Up/ Down	Old LTD Rating	New LTD Rating	IG/ SG
2/14/19	NEUSTAR, INC	Industrial	SrSec/BCF /LTCFR/PDR		D	Ba3	B1	SG
2/14/19	ANNA HOLDINGS, INC. -ACOSTA, INC.	Industrial	SrUnsec/SrSec /BCF/LTCFR/PDR	800	D	Caa3	Ca	SG
2/14/19	VIP CINEMA HOLDINGS, INC.	Industrial	SrSec/BCF /LTCFR/PDR		D	Caa1	Caa2	SG
2/15/19	STEARNS HOLDINGS, LLC	Financial	SrSec/LTCFR	190	D	B2	Caa1	SG
2/15/19	JONES ENERGY, INC. -JONES ENERGY HOLDINGS, LLC	Industrial	SrSec/SrUnsec /LTCFR/PDR	1,009	D	B2	Caa2	SG
2/15/19	WASHINGTON PRIME GROUP INC.	Industrial	SrUnsec/PS	1,195	D	Baa3	Ba2	IG
2/19/19	IMMUCOR, INC.	Industrial	SrUnsec/SrSec /BCF/LTCFR/PDR	390	D	Caa2	Caa3	SG
2/19/19	ABB/CON-CISE OPTICAL GROUP LLC	Industrial	SrSec/BCF /LTCFR/PDR		D	B2	B3	SG
2/19/19	SIBANYE GOLD LIMITED -STILLWATER MINING COMPANY	Industrial	SrUnsec /LTCFR/PDR	1,050	D	Ba2	Ba3	SG
2/19/19	PAYLESS INC. (NEW)	Industrial	PDR		D	Ca	D	SG

Source: Moody's

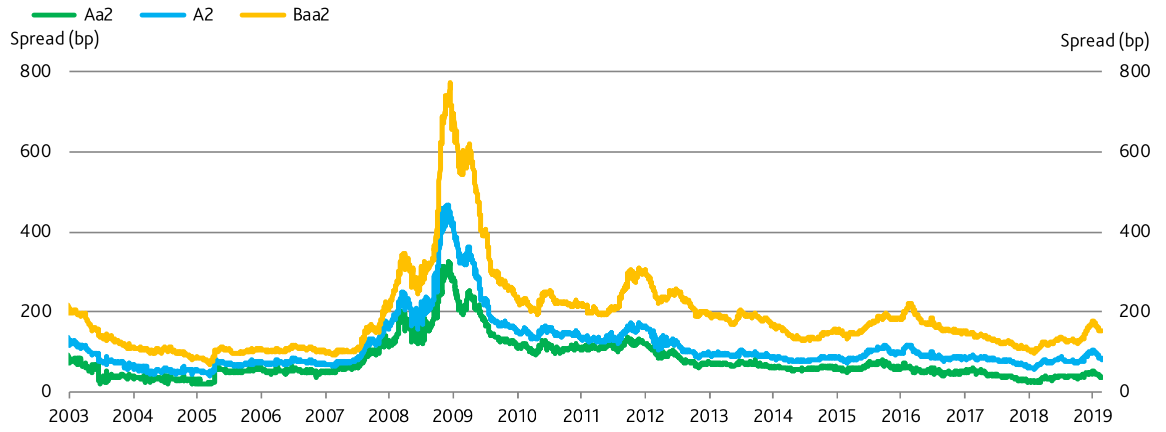
FIGURE 4
Rating Changes: Corporate & Financial Institutions – Europe

Date	Company	Sector	Rating	Amount ($ Million)	Up/ Down	Old LTD Rating	New LTD Rating	IG/SG	Country
2/13/19	TATNEFT PJSC	Industrial	LTIR		U	Baa3	Baa2	IG	RUSSIA
2/13/19	WALES & WEST UTILITIES LIMITED-WALES & WEST UTILITIES FINANCE PLC	Utility	SrSec	321	D	Baa1	Baa2	IG	UNITED KINGDOM
2/13/19	SVYAZINVESTNEFTEKHIM JSC	Industrial	LTCFR/PDR		U	Ba2	Ba1	SG	RUSSIA
2/18/19	NOSTRUM OIL & GAS PLC	Industrial	SrUnsec /LTCFR/PDR	1,125	D	B2	B3	SG	UNITED KINGDOM
2/18/19	HAPAG-LLOYD HOLDING AG-HAPAG-LLOYD AG	Industrial	SrUnsec /LTCFR/PDR	1,014	U	Caa1	B3	SG	GERMANY

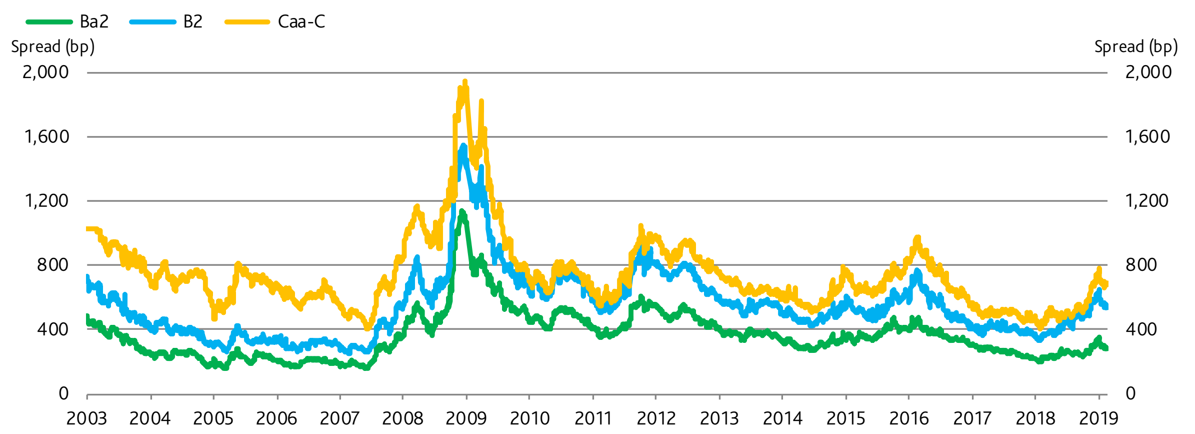
Source: Moody's

Market Data

Spreads



Source: Moody's



Source: Moody's

Market Data

CDS Movers

Figure 3. CDS Movers - US (February 13, 2019 – February 20, 2019)

CDS Implied Rating Rises	CDS Implied Ratings		
Issuer	Feb. 20	Feb. 13	Senior Ratings
International Business Machines Corporation	A2	A3	A1
CenturyLink, Inc.	B3	Caa1	B2
21st Century Fox America, Inc	Aa1	Aa2	Baa1
Kinder Morgan, Inc.	Baa1	Baa2	Baa2
Dish DBS Corporation	Caa2	Caa3	B1
Halliburton Company	Baa1	Baa2	Baa1
McKesson Corporation	Baa2	Baa3	Baa2
Praxair, Inc.	Aa3	A1	A2
Deere & Company	A1	A2	A2
Realogy Group LLC	B3	Caa1	B1

CDS Implied Rating Declines	CDS Implied Ratings		
Issuer	Feb. 20	Feb. 13	Senior Ratings
Newell Brands	B1	Ba2	Baa3
Lubrizol Corporation (The)	A1	Aa2	Aa2
Citigroup Inc.	Baa2	Baa1	Baa1
Goldman Sachs Group, Inc. (The)	Baa3	Baa2	A3
Bank of America Corporation	Baa1	A3	A3
Wells Fargo & Company	Baa1	A3	A2
Citibank, N.A.	Baa3	Baa2	A1
CVS Health	Baa2	Baa1	Baa2
Oracle Corporation	A2	A1	A1
Coca-Cola Company (The)	Aa2	Aa1	A1

CDS Spread Increases		CDS Spreads		
Issuer	Senior Ratings	Feb. 20	Feb. 13	Spread Diff
Windstream Services, LLC	Caa2	7,868	2,467	5,401
Frontier Communications Corporation	Caa1	2,812	2,653	159
Penney (J.C.) Corporation, Inc.	Caa2	3,363	3,245	118
Univision Communications Inc.	Caa2	551	488	63
Newell Brands	Baa3	222	161	61
Mattel, Inc.	B3	359	300	60
Interval Acquisition Corp	B1	266	227	38
R.R. Donnelley & Sons Company	B3	664	645	20
Pactiv Corporation	Caa1	206	188	18
Radian Group Inc.	Ba2	153	139	14

CDS Spread Decreases		CDS Spreads		
Issuer	Senior Ratings	Feb. 20	Feb. 13	Spread Diff
K. Hovnanian Enterprises, Inc.	Caa3	3,278	3,482	-205
Weatherford International, LLC (Delaware)	Caa3	1,642	1,769	-126
Talen Energy Supply, LLC	B3	484	591	-106
CenturyLink, Inc.	B2	345	447	-102
Lexmark International, Inc.	Caa3	890	978	-88
Unisys Corporation	B2	322	386	-64
American Axle & Manufacturing, Inc.	B2	292	342	-50
Dish DBS Corporation	B1	594	642	-48
Avon Products, Inc.	B3	546	591	-45
Nabors Industries Inc.	B1	432	463	-31

Source: Moody's, CMA

Market Data

Figure 4. CDS Movers - Europe (February 13, 2019 – February 20, 2019)

CDS Implied Rating Rises	CDS Implied Ratings		
Issuer	Feb. 20	Feb. 13	Senior Ratings
BNP Paribas	A2	A3	Aa3
Banco Bilbao Vizcaya Argentaria, S.A.	Baa1	Baa2	A3
Lloyds Bank plc	A3	Baa1	Aa3
HSBC Holdings plc	Baa1	Baa2	A2
Banco Santander S.A. (Spain)	A3	Baa1	A2
Credit Agricole S.A.	Aa3	A1	A1
Credit Agricole Corporate and Investment Bank	A1	A2	A1
Standard Chartered PLC	Baa2	Baa3	A2
National Grid Gas Plc	A1	A2	A3
Prudential Public Limited Company	A2	A3	A2

CDS Implied Rating Declines	CDS Implied Ratings		
Issuer	Feb. 20	Feb. 13	Senior Ratings
Fortum Oyj	Baa1	A2	Baa2
Ireland, Government of	A1	Aa3	A2
Abbey National Treasury Services plc	Baa3	Baa2	Aa3
Nationwide Building Society	Baa2	Baa1	Aa3
Bayerische Landesbank	Aa3	Aa2	Aa3
Swedbank AB	A1	Aa3	Aa2
Daimler AG	Baa3	Baa2	A2
E.ON SE	Aa2	Aa1	Baa2
Orange	A1	Aa3	Baa1
Landesbank Baden-Wuerttemberg	A1	Aa3	Aa3

CDS Spread Increases		CDS Spreads		
Issuer	Senior Ratings	Feb. 20	Feb. 13	Spread Diff
Galapagos Holding S.A.	Caa3	6,339	6,254	85
Unipol Gruppo S.p.A.	Ba2	227	199	28
Vedanta Resources Limited	B2	476	459	18
Boparan Finance plc	Caa1	1,171	1,154	17
Fortum Oyj	Baa2	62	46	16
EDP - Energias de Portugal, S.A.	Baa3	72	61	11
TUI AG	Ba2	202	195	7
Wm Morrison Supermarkets plc	Baa2	104	99	6
Eksportfinans ASA	Baa3	445	439	6
Italy, Government of	Baa3	211	207	4

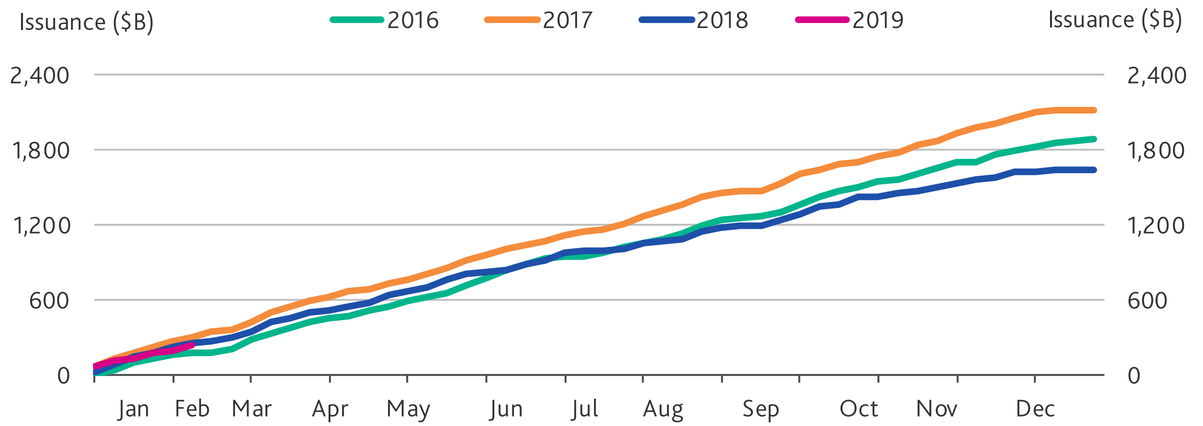
CDS Spread Decreases		CDS Spreads		
Issuer	Senior Ratings	Feb. 20	Feb. 13	Spread Diff
Jaguar Land Rover Automotive Plc	Ba3	661	770	-109
PizzaExpress Financing 1 plc	Caa2	2,154	2,207	-53
Casino Guichard-Perrachon SA	Ba1	437	476	-39
CMA CGM S.A.	B3	658	695	-37
Altice Finco S.A.	Caa1	445	476	-30
Stonegate Pub Company Financing plc	Caa1	279	300	-21
UPC Holding B.V.	B2	105	125	-20
Premier Foods Finance plc	Caa1	233	253	-20
Matalan Finance plc	Caa1	625	644	-19
Telecom Italia S.p.A.	Ba1	285	304	-18

Source: Moody's, CMA

Market Data

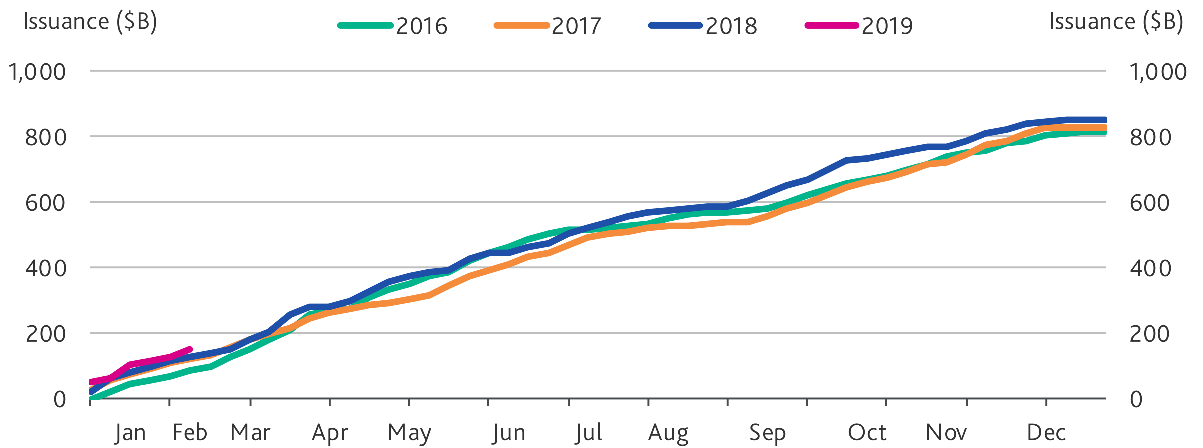
Issuance

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	42.467	3.305	46.411
Year-to-Date	179.478	50.795	240.643

	Euro Denominated		
	Investment-Grade	High-Yield	Total*
	Amount $B	Amount $B	Amount $B
Weekly	17.521	1.695	21.532
Year-to-Date	138.435	8.949	151.656

* Difference represents issuance with pending ratings.

Source: Moody's/ Dealogic

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