

WEEKLY MARKET OUTLOOK

Moody's Analytics Research

Weekly Market Outlook Contributors:

John Lonski
1.212.553.7144
john.lonski@moody.com

Yukyung Choi
1.212.553.0906
yukyung.choi@moody.com

Moody's Analytics/Asia-Pacific:

Katrina Ell
+61.2.9270.8144
katrina.ell@moody.com

Moody's Analytics/Europe:

Barbara Teixeira Araujo
+420.224.106.438
barbara.teixeiraaraujo@moody.com

Moody's Analytics/U.S.:

Ryan Sweet
1.610.235.5000
ryan.sweet@moody.com

Michael Ferlez
1.610.235.5162
michael.ferlez@moody.com

Editor

Reid Kanaley
reid.kanaley@moody.com

The Fed Cured 1998's Yield Curve Inversion

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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: During 2019's first five months, bond issuance by U.S. companies grew by 9.6% annually for investment-grade and fell by 4.5% for high-yield.

Credit Spreads	Investment Grade: We see year-end 2019's average investment grade bond spread above its recent 134 basis points. High Yield: Compared with a recent 470 bp, the high-yield spread may approximate 485 bp by year-end 2019.
Defaults	US HY default rate: Moody's Investors Service's Default Report has the U.S.' trailing 12-month high-yield default rate dropping from April 2019's actual 2.7% to a baseline estimate of 1.5% for April 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 rise by 0.1% for IG to \$1.277 trillion, while high-yield supply grows by 14.9% to \$319 billion. A significant drop by 2019's high-yield bond offerings would suggest the presence of a recession.

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Ratings Round-Up

U.S. Downgrades Include Tenneco, Penny

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Market Data

Credit spreads, CDS movers, issuance.

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Moody's Capital Markets Research *recent publications*

Links to commentaries on: Inversions, unmasking danger, divining markets, upside risks, rating changes, high leverage, revenues and profits, Fed moves, riskier outlook, high-yield, defaults, confidence vs. skepticism, stabilization, buybacks, volatility, monetary policy.

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

Credit Markets Review and Outlook

Credit Markets Review and Outlook

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

The Fed Cured 1998's Yield Curve Inversion

The implied probability of a fed funds rate cut at the Federal Open Market Committee's July 31 meeting recently soared to 72% mostly in response to Jerome Powell's apparent willingness to heed the recessionary warning of a possibly persistently inverted yield curve.

The containment of inflation expectations provides the FOMC with the ability to respond quickly to a persistent inversion of the Treasury yield curve. The Fed's quick cutting of interest rates in response to the yield curve inversion of the summer and autumn of 1998 prevented a recession. By contrast, the Fed's slow response to the inverted yield curves of 1989, 2000, and 2006-2007 facilitated the arrival of recessions.

Fed policymakers cannot help but wonder if inflation is falling short of its target despite an ultra-low unemployment rate of 3.6%, perish the thought of what might occur to inflation expectations in a soft or declining economy. Few recent developments are more damaging to corporate credit quality than the widespread incidence of significantly lower-than-expected prices for materials and final products. An extreme example would be the considerable harm done to the credit standing of households, businesses, and financial institutions by the severe home price deflation of 2007-2009.

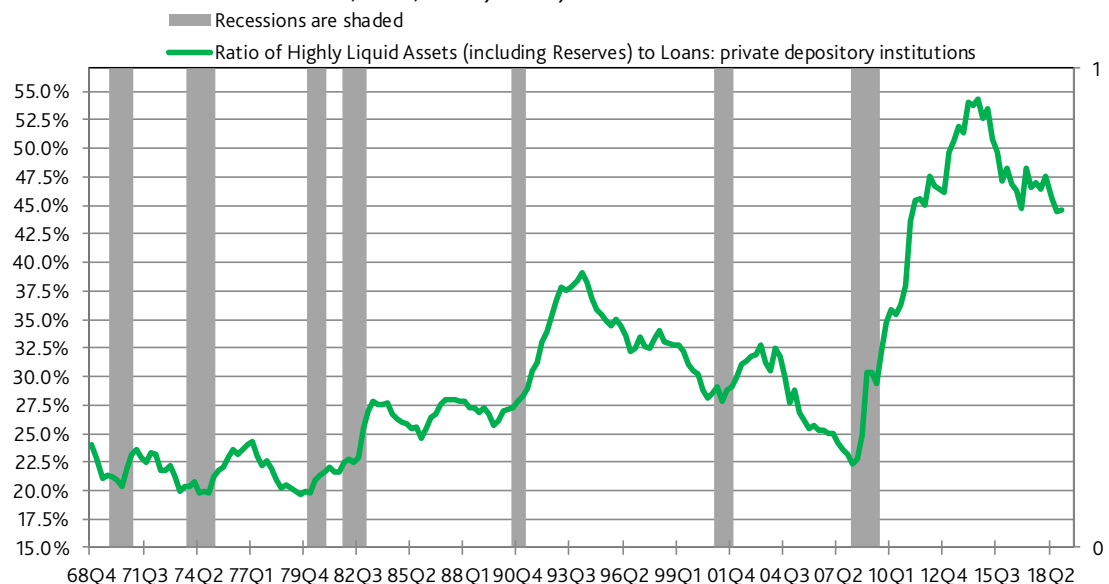
Deeper Capitalization May Prevent Next Credit Crunch from Mutating Into a Financial Crisis

However, mostly because of enhanced capitalization, today's financial system is better able to absorb the next wave of credit losses. For example, the sum of the reserves and highly liquid financial assets of U.S. private depository institutions now equals 45% of the sum of the loans, corporate bonds, and municipal bonds held by such institutions. Prior the start of the Great Recession, the ratio was a much lower 23%.

Figure 1: Banking System Is Better Able to Withstand Credit-Related Losses

Loans include bank-held municipal, corporate and foreign bonds

sources: Federal Reserve, NBER, Moody's Analytics



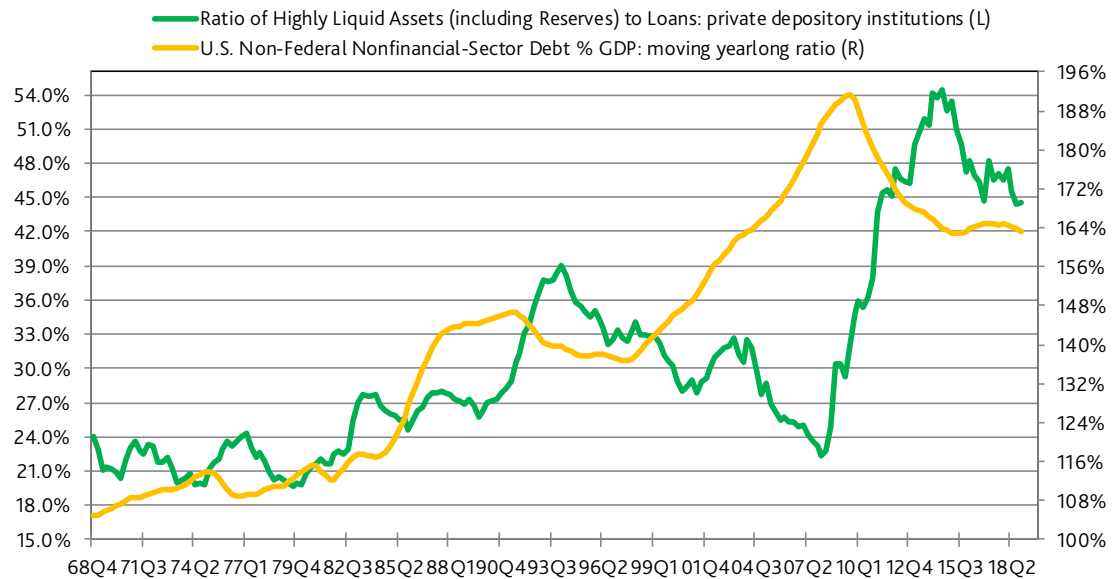
During the 10-years-ended 2007, the loan and non-Treasury bond assets held by banks advanced by 8.6% annualized, on average. At the same time, the reserves and liquid financial assets held by banks grew by a much slower 4.7% annually. In turn, the ratio of reserves plus highly liquid assets to loans plus bonds excluding Treasuries fell from 1997's 33% to 2007's 23%. Meanwhile, the ratio of U.S. non-federal nonfinancial-sector debt to GDP skyrocketed from 1997's 137% to 2007's 183%.

Credit Markets Review and Outlook

The drastically different directions taken by these two ratios contributed to the credit crisis of 2008-2009. As leverage was soaring for households and businesses, the financial system steadily became less capable of absorbing the substantial credit losses that often follow a prolonged episode of aggressive leveraging. The next credit crunch should be more manageable according to both the much deeper capitalization of the financial system and 2018's lower 163% ratio of non-federal nonfinancial-sector debt to GDP.

Figure 2: Financial System's Capitalization Weakened When Ratio of Non-Federal Debt to GDP Soared During 10-years-ended 2007

sources: Federal Reserve, BEA, Moody's Analytics



A July Rate Cut May Extend a Now Record Long Upturn

As of June 6, the 2.38% targeted midpoint for the federal funds rate was 28 basis points above the 2.10% 10-year Treasury yield. If the federal funds rate exceeds June's average for the 10-year Treasury yield by 20 basis points or more, the target range for the federal funds rate will probably be reduced at the July 31, 2019 meeting of the FOMC. As inferred from the CME Group's FedWatch Tool, the futures market recently assigned an implied probability of 71% to a fed funds rate cut at the FOMC's July 31 meeting. Moreover, the futures market also assigned implied odds of 92% to a lower-than-2.38% fed funds midpoint following the FOMC's September 18 meeting and an 87% likelihood of a lower than 2.13% fed funds midpoint after the FOMC's December 11, 2019 meeting. It should be added that the futures market recently gave implied odds of 55% to fed funds' midpoint ending 2019 no higher than 1.88%. Nevertheless, these implied probabilities can change radically with a jarring abruptness.

In terms of May's averages, the 2.39% 10-year Treasury yield essentially matched the accompanying midpoint of 2.375% for the federal funds rate's target range. As noted earlier, the fed funds rate recently exceeded the 10-year Treasury yield by 28 bp. Since the end of 1985, there have been 42 months where the federal funds rate topped the average 10-year Treasury yield's month-long average by at least 10 bp. Recessions occurred within the next 24 months following 39, or 93%, of the 42 months.

However, recessions often were slow to arrive. On average, recessions arrived 16 months after the first month in which fed funds exceeded the 10-year Treasury yield by at least 10 bp. By the way, the sixteenth month following June 2019 is October 2020, which is immediately prior to 2020's Presidential election.

Only once did a recession not occur within 24 months of a meaningful and extended inversion of the Treasury yield curve. The exception pertained to the inverted yield curve from the late summer and early autumn of 1998. Though the 5.25% average fed funds rate of August-October 1998 was 36 bp above the 10-year Treasury yield's 4.89% average, the next recession did not arrive until March 2001.

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The recessionary warning of 1998's meaningful inversion of the Treasury yield curve was overruled by the quickness with which the Fed cured an inverted yield curve with rate cuts. Immediately after August 1998's 16 bp inversion, fed funds was cut from 5.50% to 5.25% in September 1998. And in immediate response to the yield curve inversions of September 1998 and October 1998, fed funds was lowered to 5.00% in October 1998 and to 4.75% by November 1998.

Business Activity Began to Ease Prior to May's Heightened Trade Tensions

Though April's 3.6% unemployment rate was historically low, it overstated both the underlying pace of business activity and inflation risks. The Chicago Fed's national activity index provides a radically different sounding of U.S. business activity compared to the unemployment rate.

According to the Chicago Fed, the NAI is a weighted average of [85 existing monthly indicators](#) of national economic activity that include not only employment data, but other monthly readings on production, income, personal consumption, housing, business sales, new orders, and inventories. An NAI that is positive, or greater than 0.0 corresponds to above-trend growth, while a negative, or less than 0.0, NAI indicates below-trend growth. The NAI's entire sample average will always equal 0.0, which corresponds to the trend rate of growth for the U.S. economy.

The NAI's -0.32-point average for the three-months-ended April 2019 was well under its 0.12-point median since the three-month average's starting point of May 1967. As a point of reference, the NAI's moving three-month average ranges from a January 2009 low of -4.26 to an April 1978 high of 2.07.

In April, the NAI supplied a much different assessment of business activity compared to the unemployment rate. For example, 483, or 77.4%, of the NAI's moving three-months averages since May 1967 outperformed April 2019's three-month average. By contrast, only 17, or 2.7%, of the 624 monthly unemployment rates beginning with May 1967 were less than (or superior to) April 2019's 3.6% jobless rate.

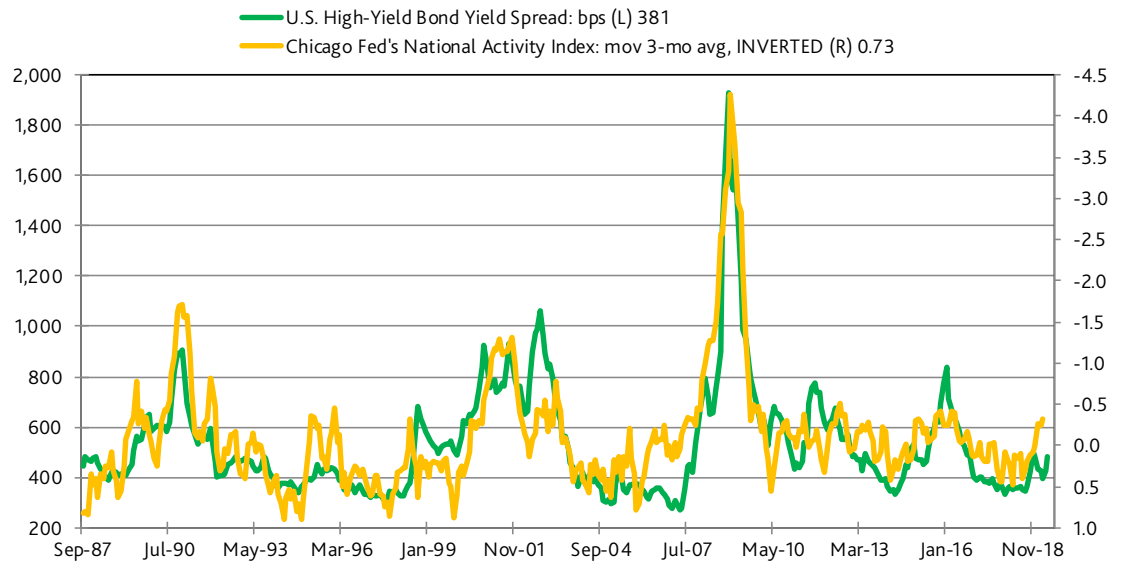
It may be worth recalling that when the unemployment rate averaged only 3.9% during 2000's final quarter, the NAI averaged a disturbingly low -0.55 points. Fourth-quarter 2000's very weak NAI may help to explain why the annual rate of core PCE price index inflation was merely 1.8% despite an ultra-low jobless rate. As it turned out, the exceptionally low NAI performed better at warning of the March 2001 start to the next recession than did the then extraordinarily low unemployment rate.

It should be added that the final quarter of 2000 was accompanied by very wide yield spreads over comparably-dated Treasuries of 260 basis points for Moody's long-term Baa industrial company bond yield average and 837 bp for a composite speculative-grade bond yield. Recently, the spreads were 209 bp for the Baa industrials and 470 bp for high-yield.

The record shows that the moving three-month average of the NAI explains the high-yield bond spread better than any other available macroeconomic metric. The correlation between the high-yield bond spread's month-long average and the NAI's moving three-month average is a rather strong 0.83. Right now, the NAI warns of a possibly wider than 550 bp high-yield bond spread.

Credit Markets Review and Outlook

Figure 3: Chicago Fed's 85-variable National Activity Index (INVERTED)
Favors a Wider than 550 bp Midpoint for High-Yield Bond Spread
 sources: Chicago Federal Reserve Bank, Moody's Analytics



A deceleration by business sales was under way well before May's intensification of trade-related stress. The year-over-year increase for the moving three-month average of core business revenues (which excludes sales of identifiable energy products) eased from July 2018's nearly seven-year high of 5.6% to April 2019's prospective 2.5%.

However, after probably sinking by 0.5% monthly in April, core business sales may post a lively rebound in May partly because of surprisingly brisk auto sales. May's unit sales of light motor vehicles in the U.S. advanced by 5.5% from April. March 2019's 5.7% monthly surge by unit auto sales was joined by an outsized 0.8% monthly jump by core business sales.

Nevertheless, if core business revenues grow by less than 2% yearly during 2019's second half, a very destructive annual contraction by core pretax profits could arrive by 2019's final quarter.

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

THE U.S.

By Ryan Sweet, Moody's Analytics

Road to Recession Paved by Tariffs

The tensions between the U.S. and its trading partners were already weighing on financial markets, business confidence and the U.S. economy, and now things could deteriorate further. President Trump has announced plans to impose a 5% tariff on all goods imported from Mexico, effective June 10.

The initial tariff on Mexican imports appears small compared with those imposed on others, including China. However, the U.S. imported \$350 billion in goods from Mexico last year and the supply chains with the U.S. and Mexico are more intertwined than those between the U.S. and China. Therefore, the spillover effects on the U.S. economy would be more significant than the 5% tariff would otherwise suggest. The U.S. auto supply chain will likely feel the brunt of this. If the initial tariff is implemented, it would be approximately a \$17.5 billion tax on U.S. businesses and consumers.

The Trump administration's continued use of tariffs as a policy lever could cause us to adjust our subjective odds around our trade war scenarios. The worst-case scenario is that Trump engages in an all-out trade war, following through on most of what he has threatened to do. This scenario didn't include the potential for the latest tariffs on Mexico, making economic costs of this dark scenario even darker.

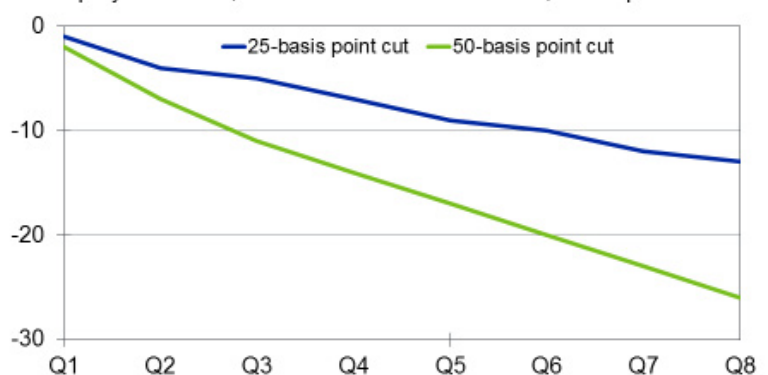
The escalation of the trade tensions, worries about the U.S. and global economies, and negative long-term rates in other developed countries are pushing the 10-year Treasury yield lower and causing a harder inversion in the yield curve. There have been other instances when the 10-year yield fell sharply during this expansion, including in 2016, when the 10-year fell below 1.5%. The weakness in the economy in 2015 and 2016 was concentrated in manufacturing, and we could repeat that now.

The recent manufacturing data have been rough. Durable goods orders fell 2.1% in April. Orders and shipments of nondefense capital goods excluding aircraft, or core capital goods shipments, were soft in April.

The housing market has shown some response to the drop in mortgage rates and consumer spending appears to be emerging some from its funk in the first quarter. The strength of the economy is most visible in the labor market. Trend job growth is strong and initial claims for unemployment insurance benefits are very low.

Fed Could Help

Unemployment rate, deviation from the baseline, basis points



Source: Moody's Analytics

Still, the case for the Federal Reserve to cut interest rates later this year is building. The Fed reacts systematically to a changing forecast, and the escalation in trade tensions between the U.S. and China and now Mexico could weigh on business

The Week Ahead

sentiment, disrupt the supply chain, and reduce manufacturing output and business investment. Also, the spillover effects on financial markets lend some downside risk to the Fed's outlook, which called for an orderly deceleration in the economy this year and next. A prudent risk management approach would suggest a cut is more likely as the risks to the forecast for growth are heavily weighted to the downside. It doesn't appear that the Fed is on board with this yet.

We now put the odds of a fed rate cut by the end of the third quarter at 30%, compared with the 5% odds of a rate hike. We have the odds of a rate cut in the fourth quarter at 40% and the probability of a hike then at 10%. These odds put the expected value of the fed funds rate at 2.26% at the end of this year—representing a single rate cut.

If an insurance cut is needed, it would probably be 25 basis points. A larger cut would likely destabilize financial markets, because it would likely be interpreted as meaning the central bank knows something others don't about the state of the economy and could be seen as the Fed panicking. To assess the impact of an insurance rate cut we ran a couple of simulations through our U.S. macro model. In the first simulation, we lowered the path of the fed funds rate by 25 basis points. This lowered the unemployment rate by 7 basis points after four quarters and 13 basis points after eight quarters. The impact on GDP is fairly modest, boosting year-over-year growth by 0.1 percentage point after four quarters. The implications for inflation were not significant. Next we assumed a 50-basis point insurance cut, which lowered the unemployment rate by 14 basis points after four quarters and 26 basis points after eight quarters. GDP growth is also boosted by 0.2 and 0.3 percentage point, respectively.

Q1 and Q2 GDP tracking update

The new data on the Quarterly Services Survey lowered our tracking estimate for first quarter GDP growth from 3.1% to 3% at an annualized rate. New data on international trade, vehicle sales, construction spending and factory orders have boosted our high-frequency GDP model's estimate of second quarter GDP growth from 1.2% to 1.5% at an annualized rate.

Looking ahead

The economic calendar is full. The key data will be consumer prices, producer prices, jobless claims, retail sales and industrial production.

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

EUROPE

By Barbara Teixeira Araujo of Moody's Analytics

Subdued Growth Expected in U.K. Monthly GDP

The U.K.'s monthly GDP growth for April is in the spotlight next week. We are expecting a rather subdued 0.1% q/q increase, which will disappoint following March's diametrically-opposed contraction. Adding to that, risks are clearly tilted toward a no-growth reading. But such a result shouldn't take markets off guard. We already expected a sharp mean-reversion in manufacturing output and exports, after firms in the U.K. and abroad rushed to stockpile finished goods before the initial Brexit deadline in March. Accordingly, we are penciling in a sharp 1.5% m/m contraction in manufacturing production, following a cumulative 2.3% rise over the previous three months. But there are two considerations to be made regarding our forecasts. On the upside, the first postponement of the Brexit deadline to April 12 likely boosted stockpiling at the start of the month as well, which could result in a less pronounced increase. On the downside, anecdotal and survey evidence suggest that the decline over the month could be even sharper than expected as factories brought forward planned summer shutdowns to April to prevent no-deal Brexit disruptions while firms were in full-scale production mode.

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Elsewhere in industrial production, we expect that U.K. energy output remained unimpressive as the month's temperatures remained above average (depressing demand for heating). But we are not penciling in an outright decline, since the weather actually cooled off a bit following the extremely warm months of February and March.

The news will be better for the U.K. service sector, if survey figures are anything to go by. Services output declined 0.1% m/m in March, and we are penciling in a 0.2% rise in April. High-frequency data suggest that U.K. consumers are shrugging off Brexit fears and keeping the economy afloat, and this should have boosted retail sales and consumer-faced services spending over the month. Notably, anecdotal evidence from retailers suggests that the Easter week was a boon, as people were driven away from home by the warm weather. Consumers are benefitting from a still-solid labour market, higher wage growth and a decline in inflation pressures, and we expect that this will remain the story for the next two quarters. Risks nonetheless remain, as a no-deal Brexit scenario would cause the economy to collapse and consumers to refrain from spending. However, we expect that car sales declined sharply over the month, in line with the SMMT's registrations data, while output in the professional, scientific and technical activities subsector is similarly expected to have corrected following two months of strong increases.

On the upside, we expect that U.K. construction activity rose sharply over the month, reversing at least partially March's 1.9% m/m decline. We expect that the month's good weather played a major role. Firms have reported that it allowed them to bring forward planned summer construction projects. Still, the outlook for the sector remains grim, hurt by the prolonged Brexit uncertainty.

All in, while we are expecting some rebound in April, our view is that U.K. growth in the three months to June will slow sharply compared to the first quarter of this year. We are penciling in a 0.2% q/q increase, down from 0.5% previously. Manufacturing production is expected to have dragged the most, offsetting continued growth in consumer-faced services spending. In the expenditure breakdown of growth, we expect that exports languished (not only due to a correction in stockpiling, but also because of the slowdown in global growth), and that investment declined, while imports are likely to have increased slightly, and consumer spending likely remained robust. Government spending is a wild card, though.

	Key indicators	Units	Moody's Analytics	Last
Mon @ 9:00 a.m.	Italy: Industrial Production for April	% change	-0.2	-0.9
Mon @ 9:30 a.m.	U.K.: Monthly GDP for April	% change	0.1	-0.1
Tues @ 9:30 a.m.	U.K.: Unemployment for April	%	3.8	3.8
Tues @ 11:00 a.m.	OECD: Composite Leading Indicators for April		98.9	99.0
Tues @ 2:00 p.m.	Russia: Foreign Trade for April	\$ bil	16.1	15.5
Wed @ 8:00 a.m.	Spain: Consumer Price Index for May	% change yr ago	0.8	1.5
Thur @ 7:00 a.m.	Germany: Consumer Price Index for May	% change yr ago	1.4	2.0
Thur @ 10:00 a.m.	Euro zone: Industrial Production for April	% change	0.1	-0.3
Fri @ 7:45 a.m.	France: Consumer Price Index for May	% change yr ago	1.1	1.5
Fri @ 10:00 a.m.	Italy: Consumer Price Index for May	% change yr ago	0.9	1.1
Fri @ 11:30 a.m.	Russia: Monetary Policy for June	%	7.75	7.75

ASIA-PACIFIC

By Katrina Ell of Moody's Analytics

China's May Data Will Likely Show Improvement

China's May data dump will likely show improvement from some pronounced pockets of weakness in April. Fixed asset investment likely improved to 6.3% y/y YTD in May, from April's 6.1% reading. Infrastructure spending has gathered momentum since the second half of 2018 and this is being reflected in a generally steady upturn in fixed investment. Industrial production has been on a relatively wild ride so far in 2019, likely on the back of seasonality from the Lunar New Year. The underlying trend

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has been relatively soft amidst manufacturing weakness offshore alongside only a measured pickup at home. China's retail trade should improve after a surprisingly weak April. The housing market has passed its trough and this should put a floor under retail trade.

China's May exports will be closely watched for any signs of scrabbling before an escalation of U.S. tariffs on Chinese goods exports took effect from 1 June. Imports have struggled with the escalation of the trade war, a consequence of the resulting slump in imports from the U.S., an important market representing almost 10% of China's total merchandise imports.

China's CPI growth is gradually gathering momentum. The main upward contributor is higher food prices including vegetables, fruit and pork. Pork prices rose by 14.4% y/y in April as the impacts of African swine flu hurt supplies of the staple. Nonfood prices cooled to 1.7% y/y in April, after a 1.8% gain in March. Nonfood prices have oscillated around this rate for the past five months.

The second estimate of Japan's March quarter GDP growth will likely be unchanged from the advance estimate, in which GDP expanded 0.5% q/q, following a 0.4% rise in the prior quarter. However, the details were unimpressive. The uptick in GDP came entirely from net exports, which rose on the back of lower commodity price imports, even though overall exports contracted. Consumption and capital expenditure contracted in the first quarter, and domestic demand rose only marginally on the back of an inventory buildup and residential investment. It's difficult to find a silver lining for Japan in the first quarter, except that the preliminary estimate tends to be heavily revised, which could mean that business investment will rise in the final estimate. Fair to say, the economy is beginning to stall.

	Key indicators	Units	Confidence	Risk	Moody's Analytics	Last
Mon @ 9:50 a.m.	Japan GDP for Q1 second estimate	% change	4	←	0.5	0.5
Mon @ Unknown	China foreign trade for May	US\$ bil	2	↓	25.1	13.8
Mon @ Unknown	China Monetary aggregates for May	% change yr ago	3	←	8.6	8.5
Wed @ 9:00 a.m.	South Korea Unemployment rate for May	%	3	←	4.0	4.1
Wed @ 9:50 a.m.	Japan Machinery orders for April	% change	2	↓	-1.5	3.8
Wed @ 11:30 a.m.	China CPI for May	% change yr ago	3	←	2.5	2.5
Wed @ 11:30 a.m.	China PPI for May	% change yr ago	3	←	1.1	0.9
Wed @ 11:00 p.m.	India Industrial production for April	% change yr ago	2	↓	1.1	-0.1
Wed @ 10:00 p.m.	India CPI for May	% change yr ago	3	←	3.0	2.9
Thurs @ 11:30 a.m.	Australia Unemployment rate for May	%	3	←	5.2	5.2
Fri @ 12:00 p.m.	China Fixed asset investment for May	% change yr ago YTD	3	←	6.3	6.1
Fri @ 12:00 p.m.	China Industrial production for May	% change yr ago	2	↑	6.3	5.4
Fri @ 12:00 p.m.	China Retail sales for May	% change yr ago	3	↑	7.9	7.2
Fri @ 2:30 p.m.	Japan Industrial production for April	% change	3	←	-0.2	0.6
Fri @ Unknown	India Foreign trade for May	US\$ bil	2	←	-12.4	-15.3

The Long View

During 2019's first five months, bond issuance by U.S. companies grew by 9.6% annually for investment-grade and fell by 4.5% for high-yield.

By John Lonski, Chief Economist, Moody's Capital Markets Research Group
June 6, 2019

CREDIT SPREADS

As measured by Moody's long-term average corporate bond yield, the recent investment grade corporate bond yield spread of 134 basis points exceeds 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 470 bp is thinner than what is suggested by both the accompanying long-term Baa industrial company bond yield spread of 209 bp and is wider than what is inferred by the recent VIX of 16.0 points.

DEFAULTS

April 2019's U.S. high-yield default rate of 2.7% was less than the 4.0% of April 2018. Moody's Investors Service now expects the default rate will average 2.0% 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 1.5% for IG and 11.7% 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 97% to at least one Fed rate cut by the end of 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
June 6, 2019

EURO ZONE

The European Central Bank's June monetary policy meeting was extremely dovish, with the bank unexpectedly changing its forward guidance on rates and announcing a below-expectation pricing for its new TLTRO liquidity operations to be launched in September. That markets had started pricing in a rate cut by next year nonetheless meant that the euro didn't depreciate, but there is no avoiding that bank President Mario Draghi was at his most dovish during the news conference. He made it clear that the Governing Council is ready to adjust all of its policy instruments and to do whatever it takes to ensure that inflation converges to target, while he explicitly said that rate cuts and a relaunching of QE were discussed during the meeting.

Also worth noting is that Draghi declared that a rate hike is not more likely than a rate cut. This means that markets may not be that wrong in pricing in a rate cut by next year, though we think that this would happen only if the economic and financial situation of the euro area deteriorated markedly in coming months. In that regard, Draghi made an unveiled criticism at the Fed, claiming that the bank's new dovish stance is now causing financial conditions in the euro area to tighten and worsening the situation at home.

When asked about the decline in market-based inflation expectations, the ECB's president made it clear that there are still no signs of de-anchoring, and that the probability of deflation is still nil. This means that there is no rush to further loosen monetary policy for now, and that the bank will continue to watch developments closely.

Regarding the TLTRO-III programme, the ECB announced that its interest rate could go as low as -0.3%—which is the deposit rate plus 10 basis points—for banks exceeding their lending benchmark, beating markets' expectations for a -0.2% threshold. And while a deposit rate hike over the next year (as it is still a possibility) could make TLTRO-III more expensive for banks, we think that the ECB would be ready to tweak the programme's terms and conditions so as to keep the cost of lending unchanged. On the contrary, we think that a cut of the deposit rate would be fully transmitted to banks, boosting lending.

Following Thursday's meeting, we have changed our forecast for euro zone monetary policy. We now expect that the central bank will keep rates unchanged until the end of 2020, instead of hiking by summer. The risks to the outlook are tilted heavily to the downside, though, which means that a deposit rate cut is likely down the road if second and third quarter figures disappoint. A relaunching of QE is also a possibility. And we don't think the bank will embark on tiering unless the situation gets pretty ugly.

RETAIL

There is no avoiding that the latest euro zone retail sales figures were disappointing. The currency area's retail sales fell in April and ultimately failed to improve on a no-growth reading in March, with sales down across most subsectors. But the truth is there is no reason for despair. The details were better than the headline, showing that most of the subsectoral declines still failed to reverse strength at the start of the year. We are thus sticking to our upbeat outlook for euro zone consumers this year—in line with the labour market strength and the substantial wage gains—but we will be closely watching the coming months' figures, as trade war jitters and the global slowdown have the scope to make a significant dent in consumers' confidence and will to spend.

The Long View

The details of the report showed that food and nonfood spending fell in April. This is rather disappointing. Extremely good weather and the Easter holidays were expected to boost spending during the second half of the month. But we caution that the main dent in nonfood spending came from internet sales, and a decline there was in the pipeline following three strong months of increases. The story for clothing as well as for the electronics and furniture sector was the same, meaning that April's fall in nonfood spending was not that bad after all. Elsewhere in the nonfood sector, the increase in computer equipment, books and other sales, as well as in pharmaceutical sales, actually beat expectations.

As to food spending, the decline in April fully reversed March's increase. This is disappointing, especially given the good weather conditions. But we are not sounding alarms. April's was the first decline in five months. Last but not least, the marginal increase in fuel sales actually beat our expectation of a decline, since we were expecting that the sharp 9.4% m/m rise in pump prices in April would have dented demand for automotive fuel.

Overall, then, we don't want to read too much into April's dip. Our view is that underlying strength remains, which means that prospects for retail in 2019 are upbeat, even if confidence numbers have deteriorated markedly of late. That's because consumer fundamentals are still solid: Inflation is decelerating on the back of moderating energy inflation, wages are rising, and unemployment remains at record lows. This should warrant continued growth in retail sales in the coming quarters, which should help offset some of the weakness in the industrial sector.

ASIA PACIFIC

By Katrina Ell of Moody's Analytics
June 6, 2019

SOUTHEAST ASIA

The trade war between the U.S. and China has led to a reordering of global supply chains as manufacturers work to circumvent tariffs. More than two-thirds of world trade occurs via global supply chains, according to the World Bank, and the disruption to the status quo from the world's two largest economies lobbying tariffs at each other has been significant.

The trend of Chinese manufacturers moving parts of their operations to Southeast Asia has accelerated since the trade war began. First, these economies are not subject to U.S. tariffs. Second, the structural features of the economies are appealing. Business environments are generally becoming more favourable, and operating costs are lower, especially for labour. For instance, Thailand and Malaysia have seen an increase in auto production in the past year, while Vietnam has seen an increase in rubber, electronics and textiles production. The ASEAN-China trade agreement, which came into force for goods in 2005 and services in 2007, facilitates this transition. The agreement extends beyond eliminating tariffs and seeks to address barriers that are behind the scenes to facilitate the flow of goods and services.

Vietnam is attractive

Prior to the trade war, Vietnam was already closely tied to China. China is a key trading partner and a large source of foreign direct investment. A growing proportion of Vietnam's exports are initially from intermediate goods imports from China. A good snapshot of the role Vietnam has played for China during the trade war comes from foreign trade data. In the March quarter, shipments from Vietnam into the U.S. were up by around 40% on an annual basis, while shipments from China into the U.S. were down by 15% y/y.

Vietnam is attractive due to its relatively low-cost, young, and large working-age population. It has been able to slowly move up the value chain, helped by its increasingly well-educated workforce. The government has been proactive in creating price stability after a history of high inflation and in improving its external position to maintain its attractiveness to offshore firms. Few restrictions on foreign investment and ongoing foreign ownership are noteworthy. While there are caps on foreign investment in local banks, the government can waive caps on a case-by-case basis. Investors can be considered for tax holidays and reductions. Ease of doing business has improved in recent years, according to the World Bank.

Vietnam's relative attractiveness spills over to solid foreign direct investment. As a proportion of GDP, foreign direct investment was at 6% in 2017, the World Bank's latest datapoint.

The Long View

Cambodia's incentives

Cambodia's foreign direct investment as a proportion of GDP has been larger than Vietnam's in recent years, according to the World Bank. Compared with Vietnam, FDI into Cambodia is in lower-value-added manufacturing, with garment manufacturing and agriculture being large recipients. The services industry, including tourism, is a growing market. Sources of FDI are typically from within Asia, including China, Malaysia and Thailand.

Apart from Cambodia's low operating costs, other key incentives for FDI include few restrictions on foreign ownership of companies and tax incentives such as a corporate tax holiday of up to eight years, a 20% corporate tax rate after the incentive period ends, and duty-free imports of capital goods. Cambodia's attractiveness, particularly to China, during the trade war is increased by the U.S.-Cambodia free trade agreement, effective from 2006. The agreement allows favourable terms with the U.S., including having its exports to the U.S. exempt from tariffs.

Asia's export performance is overwhelmingly travelling in a slower lane this year compared with 2018. This is the case for tech exporters Taiwan, Singapore, South Korea and Japan as well as for commodity producers Indonesia and Malaysia.

Export strength

As Vietnam has become a relatively more attractive destination for manufacturers in the region, its overall export performance has remained in expansion in annual terms. Although there has been a slowdown compared with last year, exports were up by 7.5% y/y in April.

Vietnam's tech exports have risen on an annual basis, defying the broader global trend of tech demand waning on the back of weaker consumer demand following an upswing that lasted around three years.

Vietnam's attractiveness as an alternate manufacturing destination has a limit. Vietnam's labour costs are rising, although they remain relatively low compared with others, including China, Malaysia and Thailand. Also, the ability for Vietnam to continue absorbing foreign investment is being constrained by rising land costs.

Meanwhile, pressure on Vietnam's infrastructure is rising with increased bottlenecks. This has included increased travel times due to congestion and energy constraints including for electricity. The government cannot keep pace to increase capacity for ports, transport links and power plants.

Fortunes could sour in a tweet

Vietnam has been an attractive alternate destination for manufacturers in China given it is not subject to U.S. tariffs. This could all change in a tweet from President Donald Trump, who has announced other key foreign trade moves on that platform. There is a risk that the U.S. could take action against Vietnam as well. The merchandise trade deficit that the U.S. runs with China has been a particular focus of the Trump administration and the trade deficit with Vietnam has steadily increased, making Vietnam vulnerable to accusations of a one-sided relationship.

There could also be closer scrutiny around the rules of origin, which allow importers to stamp goods as being from a particular country if they are "substantially transformed." In practice this has proven to be problematic. Anecdotes suggest there is much room for standardization and clarity.

Ratings Round-Up

Ratings Round-Up

U.S. Downgrades Include Tenneco, Penny

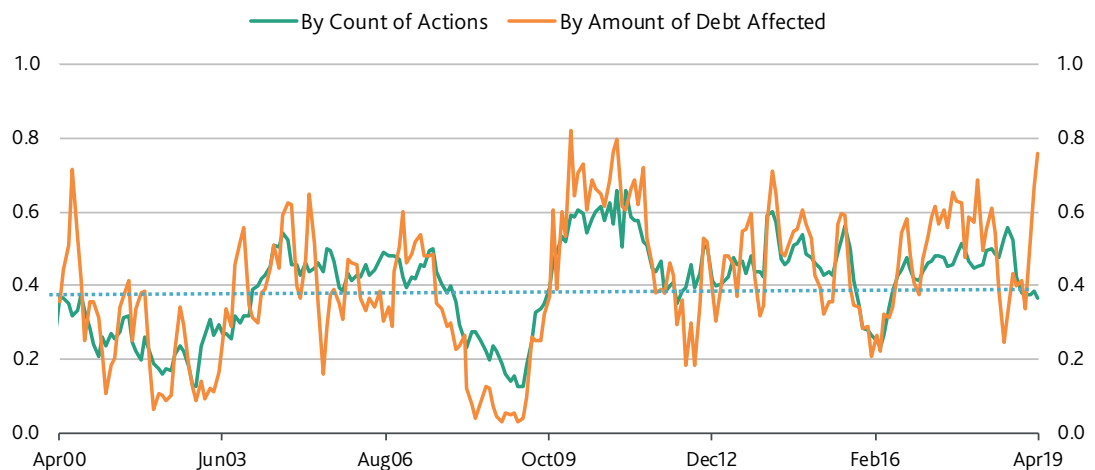
By Michael Ferlez

U.S. rating change activity has returned to recent trend, with downgrades outnumbering upgrades for the week ended June 4. Positive rating changes accounted for 32% of total activity, down from 60% in the previous update. Upgrades were headlined by Avantor Inc. which saw its senior secured debt upgraded three notches to Ba2 from B2. The U.S. life sciences company also saw its corporate family rating raised to B1 from B3 reflecting the firm's improving financial profile and recent debt repayment. The upgrade impacted \$6 billion in outstanding debt. On the downgrade-side, Tenneco Inc. saw its senior secured credit rate cut to Ba3 from Ba2. The downgrade reflects Moody's Investors Service revised expectations that the firm would face a slower pace of deleveraging and lower than expected financial performance over the near-term. The other notable downgrade last week was made to Penny (J.C.) Company Inc. The U.S. retailer saw its senior secured credit rating cut two notches to B3 affecting \$2.8 billion in debt.

In Europe, rating change activity continued to weaken. Upgrades accounted for only 29% of total activity, down from 56% in the prior update. Additionally, downgrades accounted for 93% of affected debt. The most notable downgrade last week was to Engie SA. The French utility saw its senior unsecured credit rating cut to A3 from A2. The downgrade follows a new French Law that among other measures allows the French government to reduce its stake in Engie SA. The downgrade affected \$27.3 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
5/29/19	HALCON RESOURCES CORPORATION	Industrial	SrUnsec /LTCFR/PDR	625	D	Caa1	Caa3	SG
5/29/19	TPC GROUP INC.	Industrial	SrSec /LTCFR/PDR	805	U	B3	B2	SG
5/29/19	DI PURCHASER, INC.	Industrial	SrSec/BCF /LTCFR/PDR		U	Caa3	Caa1	SG
5/30/19	JEFFERIES FINANCIAL GROUP	Financial	SrUnsec	1,000	U	Ba1	Baa3	SG
5/30/19	DXP ENTERPRISES INC	Industrial	SrSec/BCF /LTCFR/PDR		U	B3	B2	SG
5/30/19	CROSBY WORLDWIDE LTD. -CROSBY US ACQUISITION CORP.	Industrial	SrSec/BCF /LTCFR/PDR		U	Caa3	Caa2	SG
5/30/19	OUTERSTUFF LLC	Industrial	SrSec/BCF /LTCFR/PDR		D	B2	B3	SG
5/30/19	TAPSTONE ENERGY, LLC	Industrial	LTCFR/PDR		D	B3	Caa1	SG
5/30/19	PROJECT ACCELERATE PARENT, LLC	Industrial	SrSec/BCF		D	B2	B3	SG
5/30/19	BRAZOS DELAWARE II, LLC	Industrial	SrSec/BCF /LTCFR/PDR		D	B2	B3	SG
5/30/19	BCP RAPTOR II, LLC	Industrial	SrSec/BCF /LTCFR/PDR		D	B2	B3	SG
5/30/19	MAXAR TECHNOLOGIES INC.	Industrial	SrSec/BCF /LTCFR/PDR		D	B1	B2	SG
5/31/19	OGE ENERGY CORP. - OKLAHOMA GAS & ELECTRIC COMPANY	Utility	SrUnsec/BCF /LTIR/CP	2,785	D	A2	A3	IG
5/31/19	PENNEY (J.C.) COMPANY, INC.	Industrial	SrSec/SrUnsec/BCF /LTCFR/PDR/MTN	2,793	D	B1	B3	SG
5/31/19	AVANTOR, INC.	Industrial	SrSec/SrUnsec/BCF /LTCFR /PDR	6,114	U	B2	Ba2	SG
5/31/19	WEST CORPORATION	Industrial	SrUnsec/SrSec/BCF /LTCFR/PDR	1,161	D	B3	Caa1	SG
6/3/19	TENNECO INC.	Industrial	SrSec/SrUnsec /BCF/LTCFR/PDR	3,099	D	Ba2	Ba3	SG
6/3/19	EXELON CORPORATION -ATLANTIC CITY ELECTRIC COMPANY	Utility	LTIR	820	U	Baa2	Baa1	IG
6/3/19	JONAH ENERGY LLC	Industrial	SrUnsec /LTCFR/PDR	600	D	B3	Caa2	SG
6/3/19	MULTI-COLOR CORPORATION	Industrial	LTCFR/PDR		D	Ba3	B3	SG
6/3/19	CLUBCORP HOLDINGS, INC.	Industrial	SrUnsec/SrSec /BCF/LTCFR/PDR	425	D	Caa1	Caa2	SG
6/4/19	COMPUWARE HOLDINGS, LLC-COMPUWARE CORPORATION	Industrial	SrSec/BCF /LTCFR/PDR		D	B1	B2	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
5/29/19	BANCO SANTANDER S.A. (SPAIN) -PSA BANQUE FRANCE	Financial	SrUnsec/LTIR /LTD/MTN	2,229	U	Baa1	A3	IG	FRANCE
5/31/19	CASINO GUICHARD -PERRACHON SA	Industrial	SrUnsec/LTCFR /Sub/PDR/MTN	7,533	D	Ba3	B1	SG	FRANCE
6/3/19	BANCO SANTANDER S.A. (SPAIN)- SANTANDER BANK POLSKA S.A.	Financial	SrUnsec/STD /LTD/MTN	557	U	Baa1	A3	IG	POLAND
6/3/19	COLOUROZ MIDCO	Industrial	SrSec/BCF /LTCFR/PDR		D	B3	Caa1	SG	LUXEMBOURG
6/3/19	ARMACELL HOLDCO LUXEMBOURG S.A R.L. -ARMACELL BIDCO LUXEMBOURG S.A R.L.	Industrial	SrSec/BCF		D	B2	B3	SG	LUXEMBOURG
6/4/19	ENGIE SA	Utility	SrUnsec/STIR/LTIR/ JrSub/MTN/CP	27,300	D	A2	A3	IG	FRANCE
6/4/19	FIRST INVESTMENT BANK AD	Financial	LTD		D	B1	B2	SG	BULGARIA

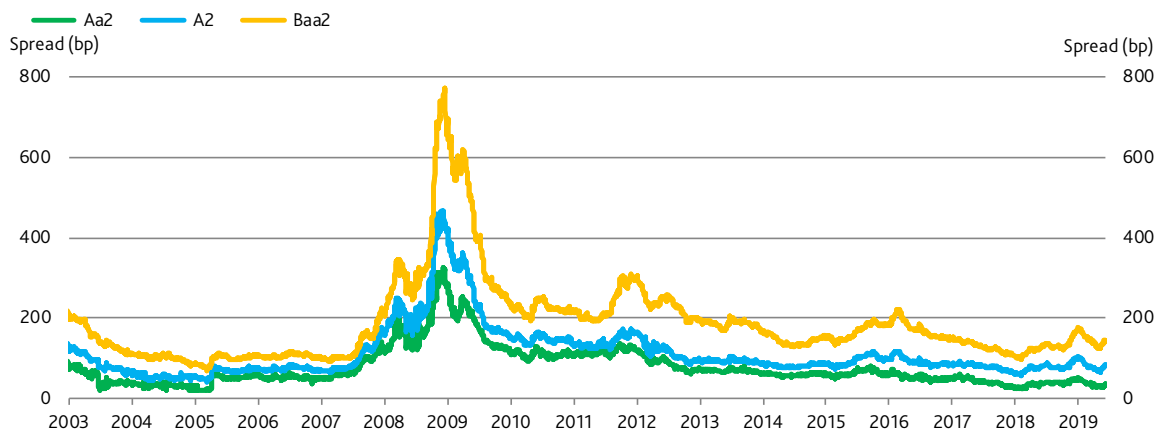
Source: Moody's

Market Data

Market Data

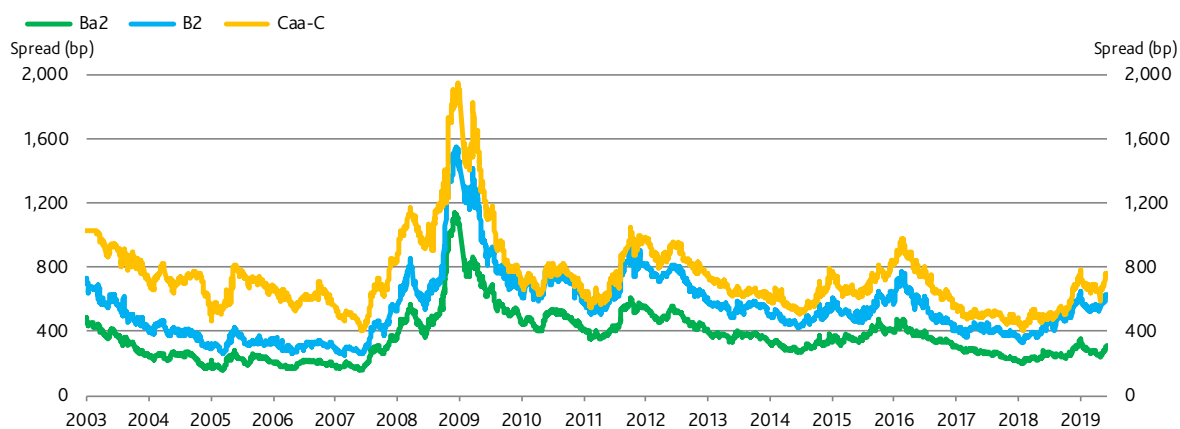
Spreads

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 (May 29, 2019 – June 5, 2019)

CDS Implied Rating Rises		CDS Implied Ratings		
Issuer		Jun. 5	May. 29	Senior Ratings
JPMorgan Chase Bank, N.A.		Aa3	A2	Aa2
JPMorgan Chase & Co.		A2	A3	A2
Comcast Corporation		A2	A3	A3
Citibank, N.A.		Baa2	Baa3	Aa3
CVS Health		Baa2	Baa3	Baa2
McDonald's Corporation		Aa1	Aa2	Baa1
HCA Inc.		Ba1	Ba2	Ba2
Altria Group Inc.		Baa1	Baa2	A3
United Parcel Service, Inc.		A1	A2	A1
Lowe's Companies, Inc.		A2	A3	Baa1

CDS Implied Rating Declines		CDS Implied Ratings		
Issuer		Jun. 5	May. 29	Senior Ratings
Toyota Motor Credit Corporation		A1	Aa2	Aa3
Burlington Resources, Inc.		A1	Aa2	A3
McClatchy Company (The)		Ca	Caa2	Caa2
Oracle Corporation		Aa3	Aa2	A1
United Technologies Corporation		A3	A2	Baa1
Amazon.com, Inc.		Aa3	Aa2	A3
Williams Companies, Inc. (The)		Baa3	Baa2	Baa3
Roche Holdings Inc.		Aa1	Aaa	Aa3
Consolidated Edison Company of New York, Inc.		A3	A2	A3
Kinder Morgan, Inc.		Baa3	Baa2	Baa2

CDS Spread Increases		CDS Spreads		
Issuer	Senior Ratings	Jun. 5	May. 29	Spread Diff
Neiman Marcus Group LTD LLC	Ca	3,056	2,831	225
Chesapeake Energy Corporation	B2	851	762	89
Pitney Bowes Inc.	Ba2	578	494	84
K. Hovnanian Enterprises, Inc.	Caa3	2,144	2,091	53
McClatchy Company (The)	Caa2	977	934	43
Frontier Communications Corporation	Caa1	2,452	2,411	41
United States Steel Corporation	B2	660	628	32
Hertz Corporation (The)	B3	699	670	28
Staples, Inc.	B3	670	647	23
Rite Aid Corporation	Caa2	1,774	1,753	21

CDS Spread Decreases		CDS Spreads		
Issuer	Senior Ratings	Jun. 5	May. 29	Spread Diff
Weatherford International, LLC (Delaware)	Ca	5,837	20,279	-14,442
Penney (J.C.) Corporation, Inc.	Caa3	4,649	4,775	-126
Office Depot, Inc.	B3	430	514	-84
Lexmark International, Inc.	Caa3	719	789	-70
AK Steel Corporation	B3	1,056	1,114	-57
Dean Foods Company	Caa2	2,339	2,385	-47
Dish DBS Corporation	B1	531	573	-43
Beazer Homes USA, Inc.	B3	502	537	-35
Interval Acquisition Corp	B1	256	288	-33
Sprint Communications, Inc.	B3	301	322	-21

Source: Moody's, CMA

Market Data

Figure 4. CDS Movers - Europe (May 29, 2019 – June 5, 2019)

CDS Implied Rating Rises		CDS Implied Ratings		
Issuer		Jun. 5	May. 29	Senior Ratings
NatWest Markets N.V.		Aa2	A1	Baa2
Spain, Government of		A2	A3	Baa1
Barclays Bank PLC		Baa1	Baa2	A2
Societe Generale		Aa3	A1	A1
Barclays PLC		Baa3	Ba1	Baa3
BNP Paribas		Aa2	Aa3	Aa3
Lloyds Bank plc		A2	A3	Aa3
Banco Bilbao Vizcaya Argentaria, S.A.		Baa1	Baa2	A3
HSBC Holdings plc		A3	Baa1	A2
Banco Santander S.A. (Spain)		Aa3	A1	A2

CDS Implied Rating Declines		CDS Implied Ratings		
Issuer		Jun. 5	May. 29	Senior Ratings
CMA CGM S.A.		C	Caa2	B3
Nationwide Building Society		Baa1	A3	Aa3
Bankinter, S.A.		Baa1	A3	Baa2
ENEL S.p.A.		Baa3	Baa2	Baa2
Unione di Banche Italiane S.p.A.		Ba3	Ba2	Baa3
Eni S.p.A.		Baa1	A3	Baa1
CNH Industrial N.V.		Ba1	Baa3	Baa3
Deutsche Post AG		Aa2	Aa1	A3
Vivendi SA		A2	A1	Baa2
Swisscom AG		Aa3	Aa2	A2

CDS Spread Increases		CDS Spreads		
Issuer	Senior Ratings	Jun. 5	May. 29	Spread Diff
PizzaExpress Financing 1 plc	Caa2	3,843	3,339	505
CMA CGM S.A.	B3	1,174	864	309
Boparan Finance plc	Caa1	2,703	2,653	50
Casino Guichard-Perrachon SA	B1	626	581	45
Iceland Bondco plc	Caa2	403	379	24
Altice Finco S.A.	Caa1	436	422	14
Matalan Finance plc	Caa1	650	639	11
Stena AB	B3	585	575	10
Bankinter, S.A.	Baa2	62	55	8
Banco Comercial Portugues, S.A.	Ba2	158	150	8

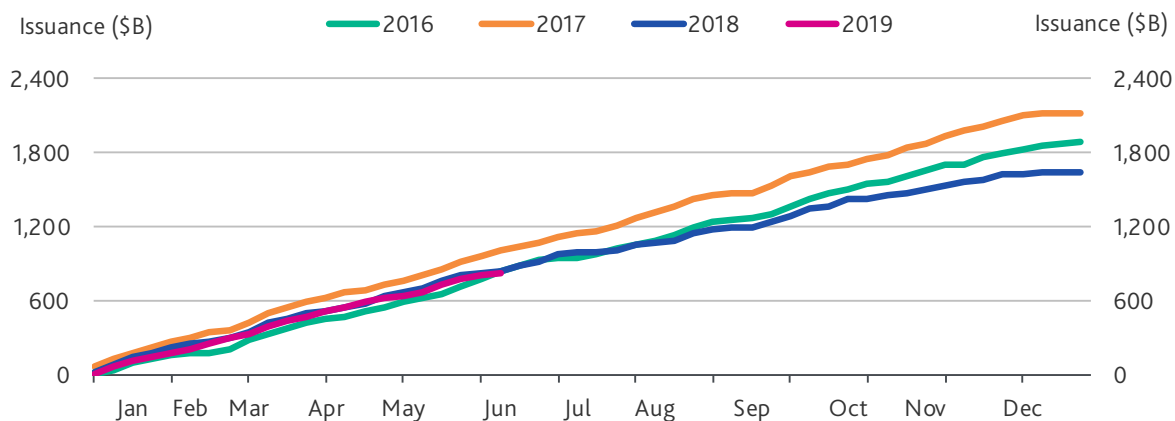
CDS Spread Decreases		CDS Spreads		
Issuer	Senior Ratings	Jun. 5	May. 29	Spread Diff
Galapagos Holding S.A.	Caa3	5,221	8,304	-3,083
Vue International Bidco plc	B3	281	425	-145
Eksportfinans ASA	Baa1	495	529	-35
Virgin Media Finance PLC	B2	136	164	-29
Jaguar Land Rover Automotive Plc	Ba3	563	580	-18
The Royal Bank of Scotland Group plc	Baa2	108	125	-17
Telecom Italia S.p.A.	Ba1	254	271	-17
Barclays PLC	Baa3	106	122	-16
NatWest Markets Plc	Baa2	91	107	-16
Greece, Government of	B1	282	297	-15

Source: Moody's, CMA

Market Data

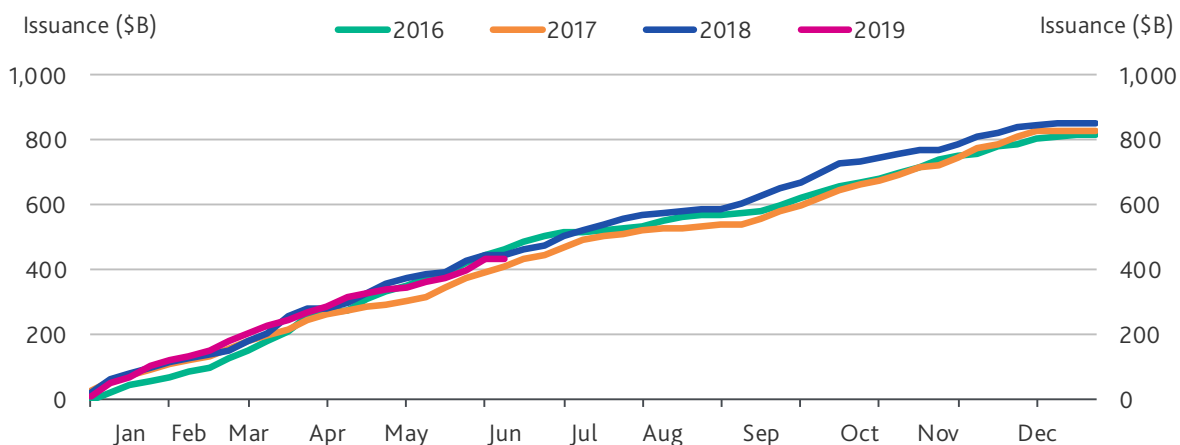
Issuance

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	8.462	2.875	11.969
Year-to-Date	604.191	177.632	817.051

	Euro Denominated		
	Investment-Grade	High-Yield	Total*
	Amount \$B	Amount \$B	Amount \$B
Weekly	3.188	0.000	3.188
Year-to-Date	384.215	41.206	434.879

* Difference represents issuance with pending ratings.

Source: Moody's/ Dealogic

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Editor
Reid Kanaley
reid.kanaley@moody.com

Contact Us

Americas:	1.212.553.4399
Europe:	+44 (0) 20.7772.5588
Asia:	813.5408.4131

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