MOODY'S ANALYTICS

WEEKLY MARKET OUTLOOK

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One Small Step for Fed

The post-meeting statement from the Federal Open Market Committee strengthens our view that the central bank will provide some additional clarity about its tapering plans in September, but the taper itself won't start until early next year. Some Fed officials have been pushing for an earlier start to gradual reductions on the $120 billion in monthly asset purchases, which may be why some changes to the statement around tapering occurred.

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The statement noted the economy's progress toward the Fed's goals of maximum employment and price stability and said the FOMC will continue to assess progress in its coming meetings. Other changes to the statement were minor, and it continued to describe inflation as transitory. Fed Chairman Jerome Powell has recently shifted to describing inflation as temporary, a less wonky term.

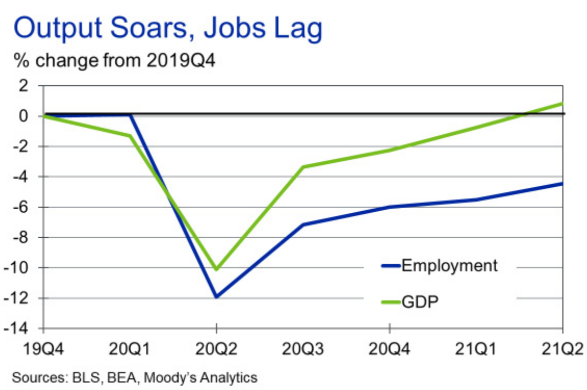
Reaction in the bond market was muted, but there was some movement in Eurodollar yields. They are now pricing in 4 basis points in additional tightening in the fed funds rate over the next three years. This isn't an enormous adjustment, but it is interesting that the bond market read the statement differently.

The Fed did announce the creation of a pair of standing repo facilities to support the implementation of monetary policy and smooth functioning in financial markets. A domestic facility will accept Treasuries and mortgage-backed securities. Primary dealers have access to the facility, but the Fed said that it will be expanded over time to include additional depository institutions. A foreign repo facility used during the pandemic is now permanent. It strengthens the Fed's ability to be the lender of last resort in the repo market. A standing repo facility had been discussed since early 2019.

The initial maximum operation size of the domestic facility will be $500 billion, and the minimum bid rate for repos under the facility will be set at 0.25%, which is the top end of the target range for the fed funds. Odds are this is where the rate will remain, so that usage is extremely low, if any at all, during good times. When there are bouts of market stress, the standing facility will be tapped, helping to limit the disruptions and allowing the repo market to function.

Disappointments keep rolling in

The U.S. economic data continue to come in weaker than expected as growth has likely peaked this cycle. U.S. GDP growth remained strong at 6.5% in the second quarter, sufficient to push GDP above its pre-pandemic level. However, the growth in the second quarter was weaker than our below consensus forecast of 7.6% at an annualized rate. The mix of growth was stronger than the top-line growth rate would suggest, though it weakened. Final sales, which exclude the impact on GDP from inventories, rose 7.7% after rising 9.1% in the first quarter.



On the other hand, consumer confidence was an outlier as it come in better than expected. The Conference Board Consumer Confidence Index rose from a revised 128.9 in May (previously 129.1) to 129.1 in June, better than either we or the consensus anticipated. Consumers' assessment of the present situation increased from 159.6 to 160.3, while expectations were little changed.

The labor market differential—the difference between those saying jobs are plentiful versus hard to get—is very strong and has widened for seven consecutive months. The difference between those expecting incomes to increase minus those anticipating a decline improved from 11.6 in June to 12 in July.

The Conference Board measure of sentiment has basically fully recovered from the recession. However, measures of consumer confidence have diverged, with the University of Michigan's consumer sentiment index dropping recently.

There are two potential reasons for the Conference Board index outperforming other measures of consumer confidence currently. The first is its sensitivity to labor markets. Despite the still-high unemployment rate, job openings are plentiful, and consumers are recognizing this. The quit rate, or the share of workers quitting their jobs voluntarily, has soared above pre-pandemic levels to a record high.

Despite recovery in the Conference Board survey, the immediate implications for consumer spending are small, since other factors are more important, particularly real disposable income.

To highlight this, we created a fairly simple model of real consumer spending growth. In the model, consumer spending growth, or real personal expenditures, is a function of growth in real disposable income; household net worth; a lag of leverage, defined as household debt as a share of disposable income; and a lag of consumer confidence.

Focusing on sentiment, the recent gains in the Conference Board index would raise year-over-year growth in real consumer spending this quarter by 0.09 of a percentage point. We re-estimated the model and swapped out the Conference Board index with the Michigan index, and this points toward a much smaller boost to real consumer spending, at 0.02 percentage point. Overall, happy consumers reduce some of the downside risk to consumer spending this quarter, particularly from the Delta variant.

TOP OF MIND

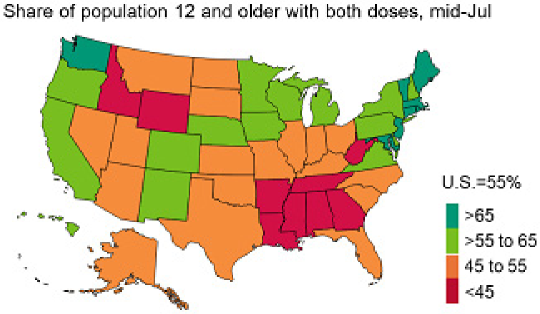
Delta-Variant Fears Remain a Risk

BY MARK ZANDI

The Delta variant of the COVID-19 virus is an emerging threat to our optimistic economic outlook. We have not revised our baseline economic forecast, which expects real GDP growth of close to 7% this year and 5% in 2022, but the variant demands attention as infections, hospitalizations and deaths are on the rise again. The variant is potentially particularly problematic in the South and Mountain West where vaccination rates are low. Adding to the economic concern is that these parts of the country have been largely leading the economic recovery from the pandemic recession. Many states in this part of the country have also decided to end supplemental unemployment insurance benefits before the September expiration, making their economies even more vulnerable.

Delta Poses a Threat

Share of population 12 and older with both doses, mid-Jul



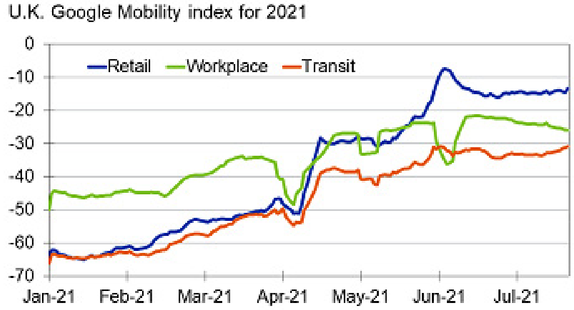
Sources: CDC, Moody's Analytics

The variant will do meaningful economic damage if it causes people to resume sheltering in place and forces schools to remain online when the school year starts in a few weeks. It could also exacerbate problems with global supply chains, which are proving difficult to unscramble, and delay when people go back to work. We've been expecting that many of the record number of open job position would be filled in the next few months as those staying home to take care of children, elderly parents, or sick family members and friends would be able to take a job. Others fearful of getting sick at work would feel safer and return. But the return to work could now be delayed.

To determine whether to downgrade our economic outlook, we are monitoring various real-time economic data including Google Mobility, the number of travelers going through TSA checkpoints, OpenTable restaurant bookings, Homebase hours worked, initial claims for unemployment insurance, and the number of people going to movie theaters. So far, we've not seen meaningful weakening in these indicators nationally. However, our Back-to-Normal Index, which is a compilation of a range of government and third-party statistics measuring where current economic activity is compared to pre-pandemic, has notably weakened in recent weeks in Florida, one of the states hit hardest by the variant. Moreover, the United Kingdom, where infections have been rising strongly since early June, may be something of an early warning for the United States. Mobility in the U.K. has gone sideways at retailers, workplaces and transit stations in recent weeks, and purchasing managers say that the British policy of requiring those that have come in contact with someone sick with the variant to self-quarantine is disrupting businesses, particularly in the transportation and leisure and hospitality industries.

U.K. Mobility Goes Sideways

U.K. Google Mobility index for 2021



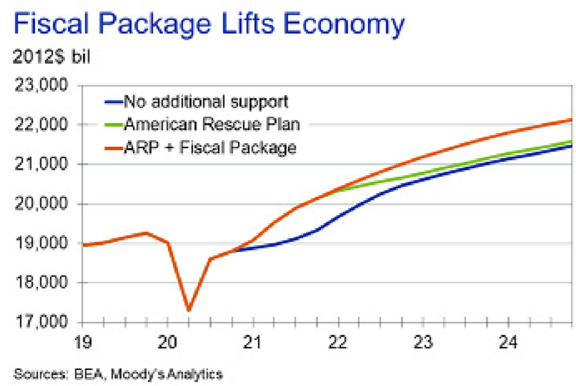
Sources: Google, Moody's Analytics

The recent volatility in the stock market and sharp decline in long-term bond yields signal that investors are starting to discount the possibility that the Delta variant will harm the economic recovery. Investors don't appear to think this is the most likely scenario, but even if they attach a small probability to that happening it will be tough on financial markets given how overvalued they are. Investors may also be contemplating more remote, but even darker, scenarios. As long as the pandemic is still raging, and it is in much of the world, odds will remain uncomfortably high that there will be other variants that are highly contagious, virulent, and allude our vaccines.

Putting aside these dark scenarios, it remains highly unlikely that the Delta variant would short-circuit the economic recovery. That would require shutting down businesses again, and the bar for that is very high. The healthcare system would have to be overwhelmed. Moreover, concerns over the economic fallout from the variant may prompt the Federal Reserve, the Biden administration, and Congress to keep their foot flat on the monetary and fiscal policy accelerator for longer. We thought the Fed might soon signal when it would begin tapering its quantitative easing, but that probably won't happen until it is obvious the variant is receding. Lawmakers may also feel added pressure to further extend the supports the federal government has been providing to pandemic-stricken renters and homeowners. As it stands, the CDC's rental eviction moratorium and FHFA's foreclosure moratorium expire at the end this month, and the payment forbearance on government-backed mortgages and student loans ends in September. As of the end of June, we estimate that 6.4 million renters, not quite 15% of all renters, were delinquent on their rent payments. This is approximately double the typical percentage of renters that are unable to pay their rent on time. And as of mid-July, some 1.75 million homeowners, equal to 3.5% of those with mortgages, are receiving forbearance, according to the Mortgage Bankers Association.

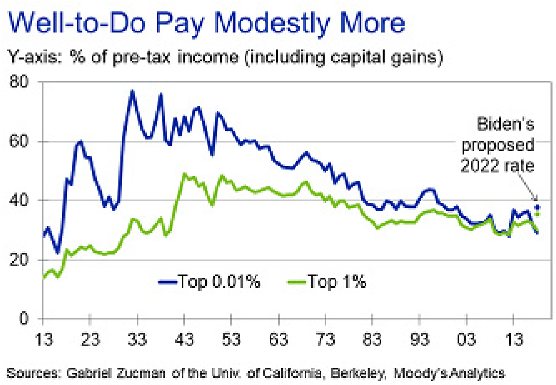
Federal lawmakers are also debating another massive round of fiscal support for the economy. It calls for nearly $600 billion in additional infrastructure spending and $3.5 trillion in investments in social programs over the next decade. This legislation is designed to lift the economy's longer-term growth and to ensure the benefits of the stronger growth go to lower- and middle-income households, but the Delta variant is a reminder that the pandemic is unlikely to go away easily, and the fiscal support provided in the legislation beginning later next year could be a big help.

Given its size and complexity, it is not surprising that the fiscal legislation is receiving significant pushback. Some worry that the proposed policy changes are too expansive given the fiscal support already provided during the pandemic. The concern is that even more spending would exacerbate the uncomfortably high inflation already evident as the economy reopens. The economy could even overheat if the Federal Reserve is forced to respond by tightening monetary policy quickly. This concern cannot be dismissed, but it is overdone. With unemployment still high at nearly 6% and labor force participation well below where it was pre-pandemic, the economy has considerable slack. Even with all the fiscal support already in train, this legislation would be just enough to provide the added boost needed to lift the economy all the way back to full employment by early 2023. Moreover, much of the additional fiscal support being considered is designed to raise the economy's longer-term growth and ease inflationary pressures. For example, the plan calls for additional spending on new rental housing supply for lower-income households. This is critical to rein in rent growth and housing costs. High prescription drug costs are also addressed. Finally, the legislation reduces the financial burden of inflation for lower- and middle-income Americans by helping them with the cost of childcare, eldercare, education, healthcare and housing for these income groups.



Others are concerned that tax increases in the plan will have serious negative economic consequences. To be sure, all else being equal, higher taxes will weigh on economic growth, but the impact on the economy from the higher proposed taxes will be small. In part, the tax increases being considered on high-income and wealthy households would be the first meaningful tax hike on individuals since the early 1990s. And from a historical perspective they are, on net, modest. Effective tax rates will remain close to historical norms. The proposed tax increases for multinational corporations, similarly, only partially roll back the large tax cuts they received with the Tax Cut and Jobs Act in 2018. Moreover, there is little evidence to date that the TCJA led to a meaningful sustained increase in business investment, hiring or wages, or prompted businesses to shift production to the U.S. from overseas as intended. This suggests that partially undoing those tax cuts will not meaningfully hurt the economy.

The most serious concern with the legislation given its size and complexity is around execution. Successfully organizing all the massive moving parts in the legislation would be difficult even for the best-managed private companies. Scaling up existing government programs as envisaged in the legislation is one thing, but standing up new programs and tax policy is another. It is difficult to believe this won't result in significant delays in implementation and unintended consequences. This is especially the case for much of the new policy addressing climate change, such as the proposed carbon border adjustment tax.



On paper, the legislation is largely paid for and does not add meaningfully to the nation's deficits and debt. But there is a risk that spending and tax credits in the plan that are slated to ultimately expire will not—ending any government program is politically vexing. Tougher tax enforcement also might not raise as much additional revenue as anticipated. The result would be larger federal budget deficits and debt. Running large deficits made a lot of sense during the pandemic, so those hit hard can manage through, limiting the broader economic and fiscal fallout. It also makes sense as the pandemic winds down, to get the economy back to full employment quickly. But once the economy has returned to full employment, focusing on our long-term fiscal problems becomes critical.

Our optimistic economic outlook has not changed appreciably in recent months, but this outlook has become more uncertain with the emergence of the Delta variant and the intensifying debate in Washington DC over another fiscal package. We are assuming the variant will be largely contained, at least so that it does not meaningfully disrupt economic activity. We also expect federal lawmakers to agree to a fiscal package in the next few months that is in the ballpark of what they are currently debating, albeit somewhat smaller. Some of this may be done through bipartisan legislation, but if that fails, it will be passed into law under budget reconciliation rules that require only Democratic votes. But if the virus and lawmakers don't stick roughly to this script, then neither will the economic outlook.

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The Week Ahead in the Global Economy

U.S.

Its another busy week on the U.S. economic data front. Among the key data scheduled for release include the July employment report, both ISM surveys, construction spending, vehicle sales and the nominal trade deficit. We will release our forecasts early next week. The Fed will be paying close attention to July employment, since a few more strong reports could move the central bank closer to announcing its plans for tapering asset purchases. July employment could be affected by seasonal adjustment issues, particularly around leisure/hospitality and local government education. Separately, the ISM surveys will help assess the breadth of improvement in the economy. The ISM manufacturing survey has been north of 60 for the past few months, and it normally doesn't stay there long. Construction spending and the trade deficit could signal revisions to second-quarter GDP. July vehicle sales will be the first input into our high-frequency GDP model's estimate of third-quarter GDP growth.

Europe

Retail and industrial production will highlight next week's economic releases. We expect to see some rebounds in industrial production following a spotty May, while retail sales will continue to grow as consumers head back to shops following the end of lockdowns. We expect euro zone retail sales to have risen 2% m/m in June following a 4.6% increase in May. Sales like rose 2.8% m/m in Germany and 1% in Italy. Gains were likely focused in out-of-home goods such as clothing and footwear, cosmetics, and transport goods.

Industrial production likely picked up slightly in June. Supply issues will continue to be a downside for European producers. Automakers in particular are exposed to the global bottleneck. In the meantime, production will exhibit some volatility as firms wait on deliveries of inputs. German production likely rose 0.5% m/m in June after May's 0.3% decline. France industrial production likely increased 0.1% m/m while in Spain, output likely rose 1.5 and in Italy output likely increased 0.8%.

Finally, we expect Russia's consumer price inflation to have sped up further in July. Inflation likely picked up to 6.7% y/y during the month from 6.5% in June. Global supply shortages and their effects on commodity and input prices, as well as a weak ruble, have been driving up producer and import prices, which in turn has forced firms to push on cost increases to consumers. The Central Bank of Russia has been consistently responding to inflation pressures and hiked its benchmark policy rate by 100 basis points to 6.5% in July.

Asia-Pacific

The Reserve Bank of Australia's monetary policy decision will be the highlight on the economic calendar. We expect the central bank to keep its interest rate settings steady and the cash rate unchanged at the record low 0.1%. However, the RBA is likely to reverse its decision to taper its bond purchases from September in light of the increasing economic costs posed the domestic outbreaks. The Delta-driven localized outbreaks have triggered significant movement restrictions of varying intensity and duration on some of the populous states, disrupting the recovery momentum and threatening to undo the sizeable progress made toward employment revival

We expect that Australia's seasonally adjusted retail sales decreased 1.8% in monthly terms in June, following a 0.4% increase in May, reflecting the hit to consumer spending caused by shutdowns in Victoria and New South Wales states.

The Reserve Bank of India is expected to keep its benchmark repo rate unchanged at 4%. Daily new cases have been on a declining trend through most of July, allowing state-level restrictions to be eased and consumption to turn the corner after a sharp decline in May. While higher inflation may become a prominent issue over the next couple of quarters, particularly in the event of a suboptimal monsoon season, maintaining low funding costs in the post-restrictions' phase will be critical to support domestic businesses and households. This will be essential as domestic demand may see a slower recovery emerging out of the second wave of COVID-19. The central bank is thus unlikely to deviate much from its current accommodative stance on interest rates and liquidity over the September quarter.

Geopolitical Calendar

Date	Country	Event	Economic Importance	Financial Market Risk
23-Jul to 8-Aug	Japan	Summer Olympics, Tokyo	Medium	Low
5-Sep	Hong Kong	Legislative Council elections	Low	Medium
2-Oct	Brazil	Presidential and congressional elections	High	Medium
22-Oct	Japan	General elections	Medium	Medium
Oct/Nov	ASEAN	ASEAN summit	Low	Low
Nov	Asia-Pacific	Asia-Pacific Economic Cooperation forum	Medium	Low
Nov	G-20	G-20 Summit	Medium	Low
7-Nov	Nicaragua	Presidential, congressional elections	Low	Low
14-Nov	Argentina	Legislative elections	Medium	Low
21-Nov	Chile	Presidential elections	Low	Low
28-Nov	Honduras	Presidential, congressional and municipal elections	Low	Low
29-May	Colombia	Presidential elections	High	Low

Seeking Fed Clarity on Tapering

BY RYAN SWEET

CREDIT SPREADS

Moody's long-term average corporate bond spread is 97 basis points, down 1 bp from this time last week. This is below its high over the past 12 months of 138 bps and not far above its lowest over the past year of 95 bps. This spread may be no wider than 110 bps by year-end 2021. The long-term average industrial corporate bond spread was unchanged over the past week, remaining at 89 bps. This is only modestly above its low over the past 12 months of 86 bps and well below its high of 131 bps.

The long-term investment grade corporate bond spread was 131 basis points, 1 bp tighter than last week. It remains well below its recent high of 194 bps. Its tightest over the past year was 129 bps. Investment-grade industrial corporate bond spreads widened by 8 bps over the past week to 135 bps.

The recent ICE BofA U.S. high-yield option adjusted bond spread of 326 basis points widened by 2 bps. The high-yield option adjusted bond spread approximates what is suggested by the accompanying long-term Baa industrial company bond yield spread and roughly in line with the VIX of 17.5. The VIX has been bouncing around over the past few weeks.

DEFAULTS

The global speculative-grade corporate default rate fell to 4.9% for the trailing 12 months ended in May, returning to where it stood a year earlier and down from 5.6% at the end of April. Among high-yield bond issuers, the U.S. default rate was 2.8% at the end of May when measured on a dollar-volume basis, down from 4.5% at the end of April. The decline reflects the exit of a few large defaults in 2020 from the trailing 12-month window.

According to the Moody's Credit Transition Model, the trailing 12-month global speculative-grade default rate will fall to 1.8% by the end of the year under the MIS baseline scenario and remain little change through May 2022. To derive default-rate forecasts, Moody's CTM uses inputs, including ratings and rating transitions, as well as assumed future paths of high-yield bond spreads and changes in unemployment rates.

In the Moody's Investors Service baseline scenario, the speculative-grade default rate will drop to 1.7% at the end of this year before creeping higher in April and May of next year, touching 1.9%. For Europe, the speculative-grade default rate will steadily decline over the next several months and end 2021 at 1.9%.

U.S. CORPORATE BOND ISSUANCE

First-quarter 2020's worldwide offerings of corporate bonds revealed annual advances of 14% for IG and 19% for high-yield, wherein US$-denominated offerings increased 45% for IG and grew 12% for high yield.

Second-quarter 2020's worldwide offerings of corporate bonds revealed annual surges of 69% for IG and 32% for high-yield, wherein US$-denominated offerings increased 142% for IG and grew 45% for high yield.

Third-quarter 2020's worldwide offerings of corporate bonds revealed an annual decline of 6% for IG and an annual advance of 44% for high-yield, wherein US$-denominated offerings increased 12% for IG and soared upward 56% for high yield.

Fourth-quarter 2020's worldwide offerings of corporate bonds revealed an annual decline of 3% for IG and an annual advance of 8% for high-yield, wherein US$-denominated offerings increased 16% for IG and 11% for high yield.

First-quarter 2021's worldwide offerings of corporate bonds revealed an annual decline of 4% for IG and an annual advance of 57% for high-yield, wherein US$-denominated offerings sank 9% for IG and advanced 64% for high yield.

Issuance weakened in the second quarter of 2021 as worldwide offerings of corporate bonds revealed a year-over-year decline of 35% for investment grade. High-yield issuance faired noticeably better in the second quarter.

U.S. dollar-denominated investment-grade issuance was $22.5 billion this week, bringing the year-to-date total to $1.012 trillion. High-yield corporate bond issuance has slowed recently, but that's typical this time of year. High-yield issuance was $10.6 billion this week, bringing its year-to-date total to $418.16 billion.

U.S. ECONOMIC OUTLOOK

There was a small downward revision to our GDP forecast for this year, the first in a while. We now look for real GDP to rise 6.7% this year, compared with the 6.9% in the June baseline. We had been consistently revising our forecast higher for GDP this year because of changes to our fiscal policy assumptions, but downward revision in the July baseline is small. Our forecast for GDP growth this year is a hair above the Bloomberg consensus for a 6.6% gain.

We made no adjustments to our forecast for GDP growth in 2022 and 2023. It remains at 5% and 2.3%, respectively. Supply issues could become a big problem, particularly for autos. Auto industrial production is trailing sales, lending downside risk to the forecast for GDP growth this year and early next.

The July forecast has real GDP surpassing its pre-COVID-19 level in the second quarter, the same as in the prior few forecasts. Year-over-year growth peaks in the second quarter for the cycle, now expected to be 12.9%, compared with the 13.2% in the June baseline.

The reason for the downward revision to GDP is a change to our fiscal policy assumptions. Recent political developments have forced us to tweak our federal fiscal assumptions in the July vintage of the baseline forecast. In late June, President Biden struck an infrastructure deal with a bipartisan group of senators to provide $579 billion in new spending over 8 years above the expected baseline funding that Congress regularly renews. The July forecast therefore assumes that lawmakers pass this bipartisan infrastructure bill through regular order and a partisan Build Back Better package through budget reconciliation. The latter would only receive Democratic votes and would cover many other areas of Biden's fiscal agenda that were excluded from the bipartisan deal.

The baseline forecast assumes that this partisan reconciliation bill would include the following other infrastructure investments over the next decade: $300 billion in affordable housing, schools and federal buildings; $300 billion in manufacturing supply chains; and $200 billion in R&D. All told, infrastructure spending under the bipartisan bill and the partisan reconciliation measure would total $1.4 trillion in the July forecast, down slightly from $1.5 trillion in the June vintage. We also reduced our assumption of new social benefits spending from $1 trillion in June to $700 billion in July. If lawmakers pursue these two-track strategy to enacting Biden's Build Back Better proposals, core infrastructure spending, which is arguably the least contentious area of Biden's agenda, would be absent from the partisan reconciliation bill, and its absence could further complicate internal agreement within the Democratic Caucus about which social programs to spend on.

We also made a few tweaks to our Build Back Better assumptions on the tax side. Biden is only assumed to get half of the international tax changes he proposed, given the long and complicated road ahead for a global minimum tax. The tax rate on long-term capital gains for top earners would rise to 28% as Democratic Senator Joe Manchin has suggested, not the 39.6% proposed by the president. Our assumptions surrounding tax credits are unchanged from the prior month, and we still envision $1.1 trillion in expanded tax credits over the next decade.

In sum, the July forecast assumes $3.2 trillion in gross fiscal support via direct spending and tax credits. All but $1 trillion of this amount would be paid for by higher taxes on corporations and well-to-do households over the next decade. However, within 15 years, the assumed Build Back Better agenda would be fully paid for. How gracefully congressional leaders can implement this two-track strategy to enacting the president's fiscal agenda is still uncertain. If the bipartisan infrastructure deal were to falter, the forecast assumes it would instead get included in a partisan reconciliation bill. What matters for the real economy is not necessarily passage, but rather implementation, of the Build Back Better proposals. Whether Congress passes one or two bills to do so, implementation is assumed to occur in early 2022.

There weren't any changes to our assumptions about monetary policy. We still expect the Fed to announce its tapering plans in September and the $15 billion reduction to occur at each Federal Open Market Committee meeting in 2022. The Fed has signaled that it wants tapering to be on autopilot. Once its monthly asset purchases have been reduced from $120 billion to zero, the Fed will reinvest proceeds from maturing assets to ensure its balance sheet doesn't contract, which would be contractionary monetary policy. We still look for the first rate hike in the first quarter of 2023.

Market expectations are for an earlier liftoff than either we or the Federal Open Market Committee anticipate. Markets also have a more gradual tightening cycle than in our baseline. Our more aggressive normalization in rates can't be explained by differences in projections for GDP growth, unemployment or inflation—our forecasts are almost spot-on with the FOMC's newly minted ones. It is difficult to see how policymakers could normalize rates in

2023 as slowly as the FOMC currently projects with the economy expected to be at full employment and inflation firmly above its 2% through-the-business-cycle target. If this were so, inflation expectations would almost surely move higher, and that's not something the Fed could shrug off.

There were no significant changes to the forecast for the 10-year U.S. Treasury yield, but the July baseline was posted before the sudden drop in the 10-year Treasury yield that has occurred this week. Technical factors appear to be pushing rates lower and this should be temporary as current 10-year Treasury yield of 1.3% is well below its economic fair value. We use an ordinary least squares regression to estimate an "economic fair value" of the 10-year Treasury yield. A significant deviation from this estimate would imply that there are other forces that are driving long-term interest rates.

The five variables used in the regression are our estimate of monthly real U.S. GDP, the CPI, the current effective fed funds rate, the Fed's balance sheet as a share of nominal GDP, and a Fed bias measure that was constructed using fed funds futures.

All five variables were statistically significant with the correct sign and explained 63% of the fluctuation in the 10-year Treasury yield. The regression used monthly data. The model's implied "economic fair value" of the 10-year Treasury yield is between 1.6% and 1.65%. We still have the 10-year Treasury yield rising through the rest of the year, ending it near 1.9% but risks are weighted to the downside.

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THE LONG VIEW: EUROPE

Sentiment High and Rising

BY ROSS CIOFFI

The euro zone's economic sentiment indicator rose for the sixth time in a row to 119 this month from 117.9 in June, reaching an all-time high. Confidence was driven by the rallying service and industrial sectors. Consumer confidence, on the other hand, lost ground, along with trade, construction and financial services. Employment expectations remained flat while price expectations increased for the fifth month in a row for services, retail trade and construction. Industry was the only exception, but selling price expectations are still at record highs.

The continued improvement in economic sentiment is a positive sign for the outlook. The Delta variant of COVID-19 and ongoing supply bottlenecks have undoubtedly clouded the horizon, but on the whole, European consumers and businesses are keeping their chins up. This implies robust consumption and investments in the third quarter. As the Delta variant outbreak remains much less deadly than previous outbreaks thanks to Europe's vaccination campaign, there is little chance that countries will reimpose full-scale lockdowns. Consumer sentiment should recover some ground as this becomes clearer, although the possibility of a vaccine-resistant COVID-19 variant will continue to haunt many for the next year. Although it is true that supply issues are hitting producers, particularly in semiconductor-dependent sectors, demand remains strong, so there will be strong make-up growth.

Money growth still strong

The past year's massive monetary easing is still showing through the euro zone's money growth figures. The policies taken by the European Central Bank and national governments to confront the COVID-19 pandemic led to large-scale loan and money growth. In June, the M3 money supply was 8.3% above what it was the same month a year earlier. Household loan growth was 4% higher in year-ago terms while loans to companies saw a 1.9% increase. In the context of the pandemic, these high growth rates point to palliative policy measures rather than strong economic growth. On a similar note, growth rates slowing from earlier this year is due to base effects rather than a slowdown in activity. For the time being, the loan growth figures are still a positive sign that monetary policy is supporting the economy. The rapid money growth is not currently driving inflation. Inflation pressures are still being driven by base effects and supply bottlenecks on the production side. Recovering demand this summer will help normalize prices as well, but we still expect inflation to fall tangibly below target next year.

GDP preview from Belgium

Meanwhile, Belgium published its preliminary estimate of second quarter GDP. Belgium is not the most representative of other European economies, but the release was nonetheless a positive sign. Output increased by 1.4% q/q, adding to the 1.1% increase in the first quarter. This brought GDP just 2.5% below what it was in the final quarter of 2019. According to the early estimates, value added increased in all sectors, industry, services and construction. There was no further breakdown, however, of the national accounts.

The euro zone's preliminary estimate of second quarter GDP will be released this Friday. We are expecting output to increase by 1.5% q/q across the bloc after it contracted by 0.3% in the first quarter. Much of the growth will likely have come in May and June, as most of Europe was under lockdown in the first half of the period.

Sweden's preliminary estimate of GDP growth came in just under our expectations, at 0.9% q/q. This added to a 0.8% expansion in the first quarter. There were no further details in the Swedish release either, although we expect that private consumption supported the continued recovery.

U.K. stamp duty phasing out

Household borrowing surged once again as the U.K.'s stamp duty holiday came to an end in June, as many buyers expected this to be their last chance to take advantage of the lower cost. Net mortgage borrowing hit a record high as a result, reaching £17.9 billion in June. This was up from £6.8 billion in May. Now that June has passed, the stamp duty holiday will be gradually phased out. Stamp duty will return to its original rates by 1 October 2021. Demand for housing should ease from its recent frenzied pitch as the year progresses, although borrowing will likely surge one more time leading up to the complete end of the holiday.

Economic Challenges of COVID Keep Coming

BY KATRINA ELL, SHAHANA MUKHERJEE, DAVE CHIA

The COVID-19 situation remains tense in the Asia-Pacific region. Over the past week, several countries responded to stubbornly elevated daily infections by extending or tightening distancing measures. The highly contagious Delta variant is challenging policymakers and threatening our expectation that economic recoveries will gather momentum in the second half of 2021.

Southeast Asia has been hit badly. Daily infections for Indonesia, Thailand and Vietnam remain elevated at record highs, while cases in the Philippines and Malaysia are not far from the peaks reached in the second quarter of 2021. These developments have given way to further markdowns in our current quarter growth forecasts, given economic recoveries are paused. Among the Southeast Asian economies, Indonesia is at the worst end of the spectrum. Moody's Analytics expects Indonesia's economy to grow 4.5% in 2021, a step down from our June baseline forecast of a 5.4% expansion. The likelihood of further downward revisions remains high as the national lockdown saps domestic demand.

Singapore is expected to remain in lockdown until mid-August, but given the outsized importance of exports to its economy, a relative favourable trade outlook will partially offset some of the downside risk to growth in the third quarter. The economy is forecast to grow 5.5% in 2021. In contrast, while the Philippines has eased restrictions over the past month, the likelihood of rising daily infections giving way to reinstated curbs remains high, with the Delta variant becoming prominent.

The situation in other parts of Asia remains worrisome for the most part. In Japan, Tokyo is in the middle of its fourth state of emergency. The Olympics officially began on July 23 with strict movement restrictions imposed on athletes and limited spectators allowed. This has severely limited the lift to retail and hospitality. South Korea is battling a fierce new wave that hit in early July. The government reintroduced tougher restrictions nationwide in mid-July, with the strictest controls in the capital. Retail and recreation will again plunge because of the tightened social restrictions in Greater Seoul. The worsening virus wave also will intensify the strain on the labour market, with services lagging the broader economic expansion because of stricter social distancing measures. The situation is exacerbated by a slowdown in the vaccination pace. With the highly transmissible Delta variant, the new virus wave could be harder to contain, posing a threat to a complete reopening of South Korea's economy.

Asia's slow rate of vaccination is a thorn in the region's economic recovery. Experience in the U.S. and the U.K. shows that a high rate of full vaccination against COVID-19 leads to better health outcomes. As Asia's average rate of full vaccination is low, lockdowns and other restrictive social distancing measures are necessary to protect the vulnerable. Once herd resilience is reached (around 70% of the population) the need for harsh lockdowns is considerably lowered, which will allow domestic demand to sustainably recover.

Central banks face limits

Central banks responded aggressively to the pandemic in the first half of 2020, often unleashing unprecedented support to cushion the blow. But now, even though economies are still struggling, central banks no longer have the same monetary space to support. For example, Bank Indonesia has not changed its seven-day reverse repo rate since February and has little room to manoeuvre as it risks stoking capital outflows and destabilising the already-vulnerable rupiah. The central bank is, however, expected to stand pat for the rest of 2021.

The onus will be on fiscal policy to do the heavy lifting in Southeast Asia. Malaysia, for example, has introduced four significant fiscal stimulus packages this year and may increase its debt ceiling as strict movement restrictions in Kuala Lumpur constrain activity. Indonesia will have significantly larger budget deficit than initially planned this year, with further government support flowing to cushion the fallout from movement restrictions in Bali and Java. On similar lines, the Philippines will likely introduce a further US$3.6 billion stimulus package shortly to keep the government's downwardly revised GDP target for 2021 in the range of 6% to 7% this year. Eventually, however, policy efforts across the region will need to be complemented with an efficiently managed vaccine rollout to mitigate the long-term economic costs inflicted by repeated, debilitating outbreaks.

RATINGS ROUND-UP

U.S. Upgrade Activity Robust

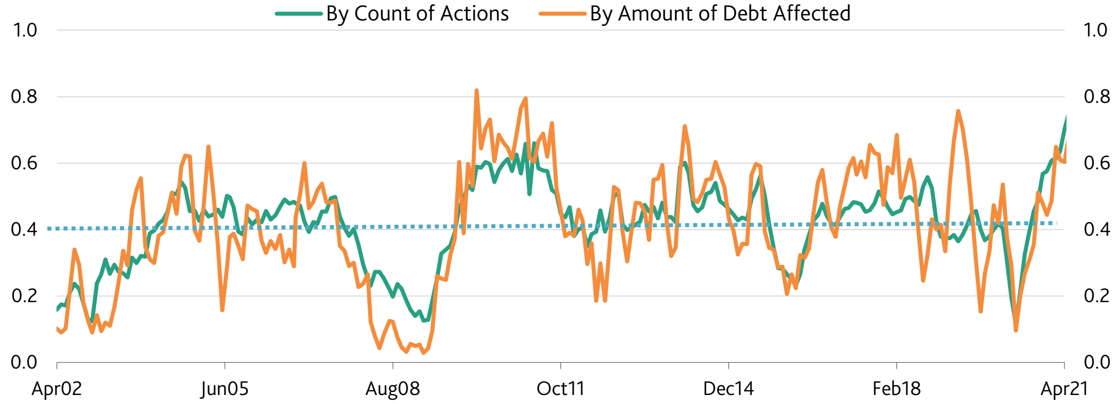
BY MICHAEL FERLEZ

U.S. rating change activity was overwhelmingly positive in the latest period with upgrades accounting for all but one rating change and all the reported debt. Rating changes impacted a variety of different industries, though changes almost exclusively impacted speculative-grade companies. The largest rating change last week in terms of affected debt was EQT Corp. Moody's Investors Service upgraded EQT's Corporate Family Rating and unsecured notes ratings to Ba1, and its probability of default rating to Ba1-PD. In Moody's rating action, Sreedhar Kona, Moody's senior analyst, wrote, "EQT's ratings upgrade reflects the improvement in the company's scale through its primarily equity-funded acquisition of Alta assets and an expected improvement in its debt leverage. EQT's debt leverage should be reduced meaningfully over the long-term from the company's enhanced size; however, the company's absolute debt burden is not likely to be reduced significantly until 2023." Kona added that "EQT's improved capital efficiency, its commodity hedge position and the prospect of further debt reduction contribute to the stable outlook."

U.S. corporate credit quality continues to improve at a robust pace as the economic effects of the pandemic begin to fade. Through the end of the second quarter, upgrades have outnumbered downgrades this year by a ratio of more than two to one.

European rating changes were also credit positive, though activity remained light. Upgrades accounted for 60% of both total changes and affected debt. Geographically, Cyprus and U.K.-based firms received two rating changes, followed by the Netherlands with one. The most notable change in terms of affected debt was Bank of Cyprus Holdings Public Ltd Co. Moody's Investors Service issued several upgrades to the Bank of Cyprus, including upgrading the bank's long-term bank deposit ratings to B1 and its senior unsecured debt ratings to Caa1. The upgrade impacted $1 billion of Bank of Cyprus' debt. Concurrently, Moody's Investors Service also issued several upgrades to Hellenic Bank Public Company Ltd. In the rating action for both firms, Moody's mentions the banks' improved solvency and stronger credit profiles.

FIGURE 1
Rating Changes - US Corporate & Financial Institutions: Favorable as a % 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
7/21/2021	HARTFORD FINANCIAL SERVICES GROUP, INC. (THE)-HARTFORD LIFE & ACCIDENT INSURANCE COMPANY	Financial	IFSR		U	A2	A1	IG
7/21/2021	PACIFIC MUTUAL HOLDING COMPANY-Pacific Life Global Funding II	Financial	SrSec/SrUnsec/MTN/IFSR/SPN		U	A1	Aa3	IG
7/21/2021	BUILDERS FIRSTSOURCE, INC.	Industrial	SrUnsec	1,327.50	U	B1	Ba3	SG
7/21/2021	ASHTON WOODS USA, LLC	Industrial	SrUnsec/LTCFR/PDR	505.00	U	B2	B1	SG
7/21/2021	RADIOLOGY PARTNERS HOLDINGS, LLC-RADIOLOGY PARTNERS, INC.	Industrial	SrSec/BCF/LTCFR/PDR/SrUnsec	1,510.00	U	B3	B2	SG
7/23/2021	EQT CORPORATION	Utility	SrUnsec/LTCFR/PDR/MTN	5,102.82	U	Ba2	Ba1	SG
7/23/2021	WP CITYMD BIDCO LLC	Industrial	LTCFR/PDR/SrSec/BCF		U	B2	B1	SG
7/23/2021	SPECTACLE GARY, LLC-SPECTACLE GARY HOLDINGS, LLC	Industrial	SrSec		U	Caa1	B3	SG
7/26/2021	ATI PHYSICAL THERAPY, INC.-ATI HOLDINGS ACQUISITION, INC.	Industrial	LTCFR/PDR/SrSec/BCF		D	B1	B2	SG
7/26/2021	LATHAM INTERNATIONAL MANUFACTURING CORP.-LATHAM POOL PRODUCTS, INC.	Industrial	LTCFR/PDR/SrSec/BCF		U	B2	B1	SG
7/26/2021	AKUMIN INC.	Industrial	SrSec/SrSec/BCF	475.00	U	B3	B2	SG
7/27/2021	CRESTWOOD HOLDINGS LLC-CRESTWOOD MIDSTREAM PARTNERS LP	Industrial	SrUnsec/LTCFR/PS/PDR	2,600.84	U	B1	Ba3	SG
7/27/2021	SPECTRUM HOLDINGS III CORP.	Industrial	SrSec/BCF/LTCFR/PDR		U	Caa1	B3	SG
7/27/2021	BALLY'S CORPORATION	Industrial	LTCFR/PDR		U	B2	B1	SG

Source: Moody's

FIGURE 4

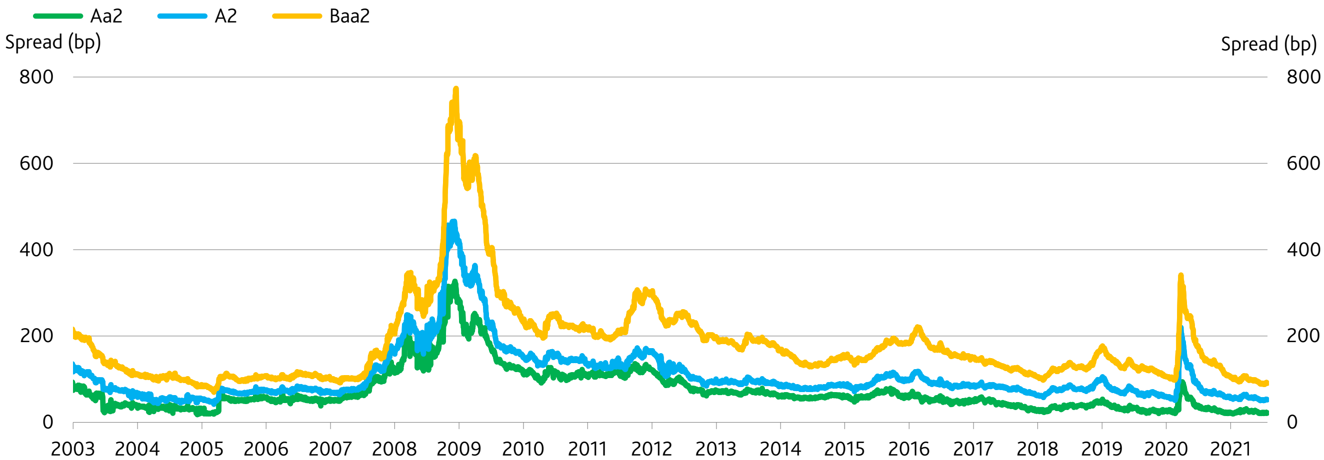
Rating Changes: Corporate & Financial Institutions - Europe

Date	Company	Sector	Rating	Amount ($ Million)	Up/ Down	Old LTD Rating	New LTD Rating	IG/SG	Country
7/21/2021	HELLENIC BANK PUBLIC COMPANY LTD	Financial	LTD		U	B3	B1	SG	CYPRUS
7/21/2021	BANK OF CYPRUS HOLDINGS PUBLIC LIMITED COMPANY	Financial	LTD/SrUnsec/MTN/Sub	999.73	U	Caa2	Caa1	SG	CYPRUS
7/22/2021	BLERIOT MIDCO LIMITED	Industrial	LTCFR/PDR		U	B3	B2	SG	UNITED KINGDOM
7/26/2021	FRIGOGLASS SAIC	Industrial	SrSec/LTCFR/PDR	305.80	D	B3	Caa1	SG	NETHERLANDS
7/26/2021	FERROGLOBE PLC	Industrial	SrUnsec	350.00	D	Caa2	Caa3	SG	UNITED KINGDOM

Source: Moody's

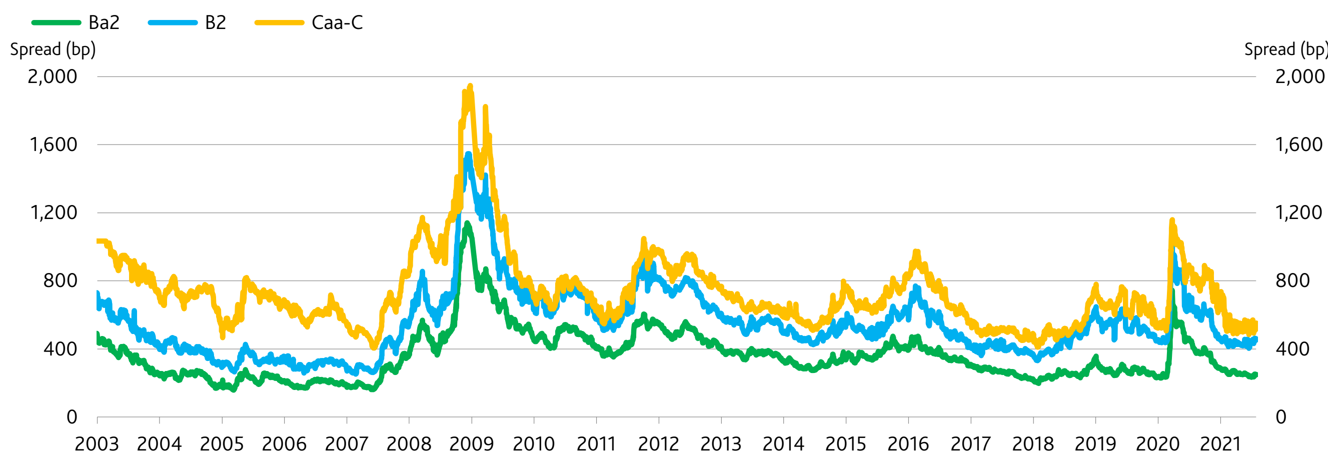
MARKET DATA

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



Source: Moody's

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



Source: Moody's

CDS MOVERS

Figure 3. CDS Movers - US (July 21, 2021 – July 28, 2021)

CDS Implied Rating Rises	CDS Implied Ratings		
Issuer	Jul. 28	Jul. 21	Senior Ratings
Illinois Tool Works Inc.	Aa2	A2	A2
JPMorgan Chase Bank, N.A.	A2	A3	Aa2
Pfizer Inc.	Aa1	Aa2	A2
Intel Corporation	Aa3	A1	A1
Raytheon Technologies Corporation	Aa3	A1	Baa1
NextEra Energy Capital Holdings, Inc.	A2	A3	Baa1
Lowe's Companies, Inc.	Aa2	Aa3	Baa1
Consolidated Edison Company of New York, Inc.	A3	Baa1	Baa1
Dominion Energy, Inc.	Aa3	A1	Baa2
FirstEnergy Corp.	Baa2	Baa3	Ba1

CDS Implied Rating Declines	CDS Implied Ratings		
Issuer	Jul. 28	Jul. 21	Senior Ratings
Eversource Energy	A3	A1	Baa1
Air Products and Chemicals, Inc.	A1	Aa2	A2
PepsiCo, Inc.	A3	A2	A1
General Motors Company	Ba1	Baa3	Baa3
FedEx Corporation	A3	A2	Baa2
Nissan Motor Acceptance Company LLC	Ba2	Ba1	Baa3
Cargill, Incorporated	A3	A2	A2
Abbott Laboratories	Baa1	A3	A2
NRG Energy, Inc.	Ba3	Ba2	Ba2
Welltower Inc.	Baa1	A3	Baa1

CDS Spread Increases		CDS Spreads		
Issuer	Senior Ratings	Jul. 28	Jul. 21	Spread Diff
Talen Energy Supply, LLC	B3	2,722	2,563	160
Staples, Inc.	Caa1	925	860	65
Nabors Industries, Inc.	Caa2	932	884	48
Carnival Corporation	B2	436	411	25
Service Corporation International	Ba3	168	153	15
Rite Aid Corporation	Caa3	872	858	14
American Axle & Manufacturing, Inc.	B2	400	392	8
Macy's Retail Holdings, LLC	B1	333	325	8
RPM International Inc.	Baa3	72	64	8
Unisys Corporation	Caa1	209	201	8

CDS Spread Decreases		CDS Spreads		
Issuer	Senior Ratings	Jul. 28	Jul. 21	Spread Diff
United Airlines, Inc.	Ba3	414	449	-35
United States Cellular Corporation	Ba1	120	154	-34
American Airlines Group Inc.	Caa1	679	713	-34
FirstEnergy Corp.	Ba1	59	83	-24
Avis Budget Car Rental, LLC	B3	287	310	-23
United Airlines Holdings, Inc.	Ba3	409	432	-23
The Terminix Company, LLC	B1	228	250	-22
Qwest Corporation	Ba2	147	166	-19
United States Steel Corporation	B3	325	342	-17
DPL Inc.	Ba1	131	148	-17

Source: Moody's, CMA

CDS Movers

Figure 4. CDS Movers - Europe (July 21, 2021 – July 28, 2021)

CDS Implied Rating Rises	CDS Implied Ratings		
Issuer	Jul. 28	Jul. 21	Senior Ratings
Landesbank Baden-Wuerttemberg	Aa2	Baa1	Aa3
Banca Monte dei Paschi di Siena S.p.A.	Ba2	B1	Caa1
France, Government of	Aaa	Aa1	Aa2
CaixaBank, S.A.	A3	Baa1	Baa1
Orange	Aa2	Aa3	Baa1
Swedbank AB	Aa1	Aa2	Aa3
Deutsche Telekom AG	Aa2	Aa3	Baa1
KBC Bank N.V.	Aa2	Aa3	A1
Iberdrola International B.V.	A2	A3	Baa1
National Grid Electricity Transmission plc	Aa3	A1	Baa1

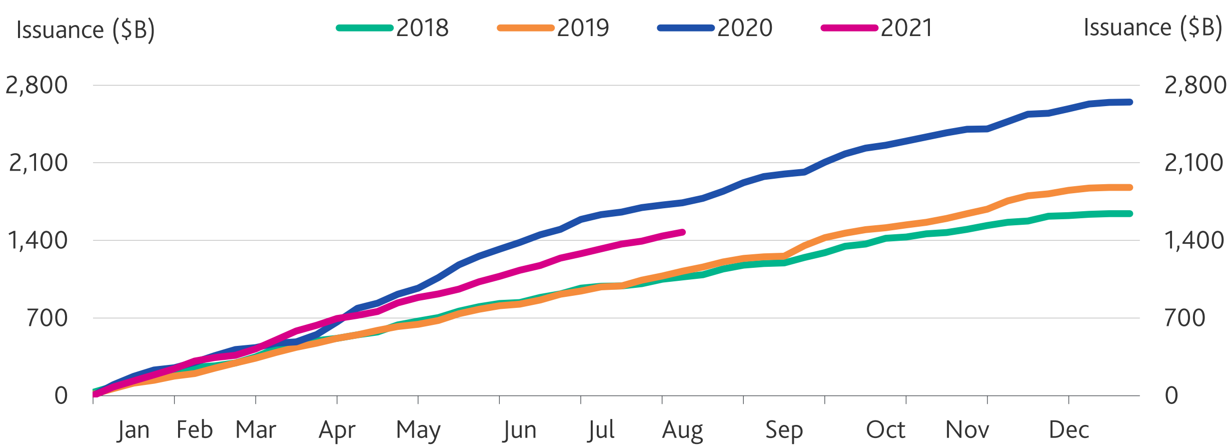
CDS Implied Rating Declines	CDS Implied Ratings		
Issuer	Jul. 28	Jul. 21	Senior Ratings
HSBC Bank plc	A1	Aa2	A1
Deutsche Bank AG	Baa1	A3	A3
HSBC Holdings plc	Baa1	A3	A3
Standard Chartered PLC	Baa2	Baa1	A3
Bankinter, S.A.	Baa2	Baa1	Baa1
RWE AG	Aa3	Aa2	Baa2
Deutsche Post AG	Aa1	Aaa	A3
National Grid plc	Aa3	Aa2	Baa2
3i Group plc	Ba1	Baa3	Baa1
Vue International Bidco plc	Ca	Caa3	Ca

CDS Spread Increases		CDS Spreads		
Issuer	Senior Ratings	Jul. 28	Jul. 21	Spread Diff
Vedanta Resources Limited	Caa1	1,024	938	87
Boparan Finance plc	Caa1	925	885	39
Vue International Bidco plc	Ca	620	583	36
Novafives S.A.S.	Caa2	823	796	28
HSBC Holdings plc	A3	50	44	7
Casino Guichard-Perrachon SA	Caa1	534	528	6
Standard Chartered PLC	A3	53	48	5
Standard Chartered Bank	A1	34	31	3
Telecom Italia S.p.A.	Ba2	163	160	3
HSBC Bank plc	A1	36	33	3

CDS Spread Decreases		CDS Spreads		
Issuer	Senior Ratings	Jul. 28	Jul. 21	Spread Diff
TUI AG	Caa1	712	792	-80
Banca Monte dei Paschi di Siena S.p.A.	Caa1	180	234	-54
Landesbank Baden-Wuerttemberg	Aa3	28	48	-19
thyssenkrupp AG	B1	257	275	-18
Deutsche Lufthansa Aktiengesellschaft	Ba2	254	270	-17
Ineos Group Holdings S.A.	B2	201	218	-17
Avon Products, Inc.	Ba3	213	230	-17
Premier Foods Finance plc	B3	192	207	-16
Hammerson Plc	Baa3	162	176	-14
UPC Holding B.V.	B3	217	226	-10

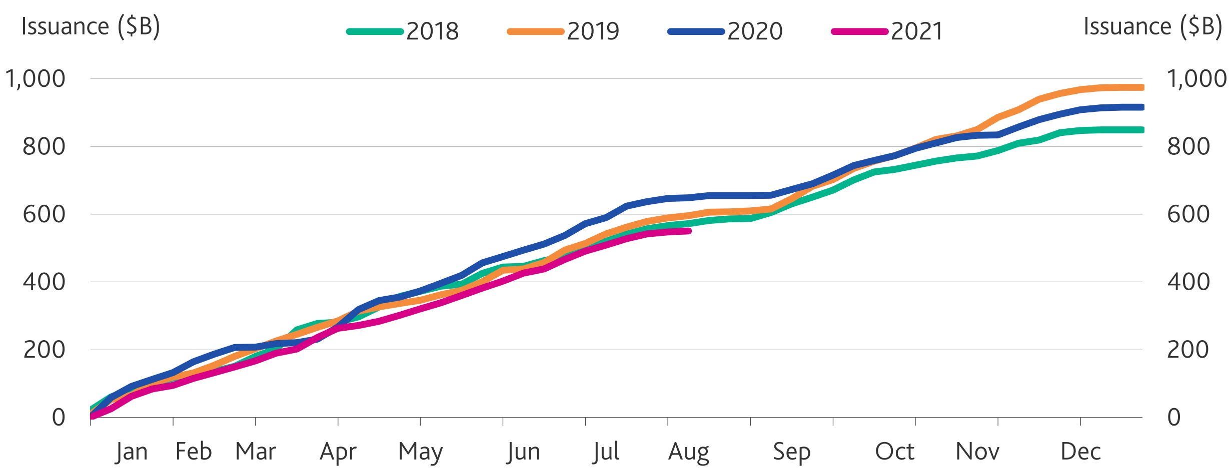
Source: Moody's, CMA

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

ISSUANCE

Figure 7. Issuance: Corporate & Financial Institutions

	USD Denominated		
	Investment-Grade	High-Yield	Total*
	Amount $B	Amount $B	Amount $B
Weekly	22.479	10.637	34.341
Year-to-Date	1,011.566	418.164	1,474.108

	Euro Denominated		
	Investment-Grade	High-Yield	Total*
	Amount $B	Amount $B	Amount $B
Weekly	2.159	0.737	3.467
Year-to-Date	427.570	106.946	550.799

* Difference represents issuance with pending ratings.

Source: Moody's/ Dealogic

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