

## WEEKLY MARKET OUTLOOK

### Moody's Analytics Research

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## Operating Leverage May Help to Narrow Yield Spreads in 2021

### [Credit Markets Review and Outlook](#) by *John Lonski*

Operating Leverage May Help to Narrow Yield Spreads in 2021

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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: A broader equity market rally will help to enhance corporate credit quality.

Credit Spreads	<a href="#">Investment Grade</a> : Year-end 2020's average investment grade bond spread may exceed its recent 116 basis points. <a href="#">High Yield</a> : The high-yield spread may be wider than its recent 461 bp by year-end 2020.
Defaults	<a href="#">US HY default rate</a> : According to Moody's Investors Service, the U.S.' trailing 12-month high-yield default rate jumped from October 2019's 3.8% to October 2020's 8.3% and may average 10.3% during 2021's first quarter.
Issuance	<a href="#">For 2019's</a> offerings of US\$-denominated corporate bonds, IG bond issuance rose 2.6% to \$1.309 trillion, while high-yield bond issuance surged by 55.8% to \$432 billion. <a href="#">In 2020</a> , US\$-denominated corporate bond issuance is expected to soar higher by 52% for IG to a record 1.996 trillion, while high-yield supply may rise 24% to a record-high \$537 billion.

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### [Ratings Round-Up](#)

Latest U.S. Changes Follow Familiar Pattern of Upgrades to Downgrades

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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: Resurgent virus, split Congress, profits, misery, issuance boom, default rate, volatility, credit quality, unprecedented stimulus, bond yields, record savings rates, demographic change, high tech, complacency, Fed intervention, speculation, risk, credit stress, rate cuts, optimism, coronavirus, corporate credit, spreads, leverage, VIX.

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## Credit Markets Review and Outlook

## Credit Markets Review and Outlook

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

## Operating Leverage May Help to Narrow Yield Spreads in 2021

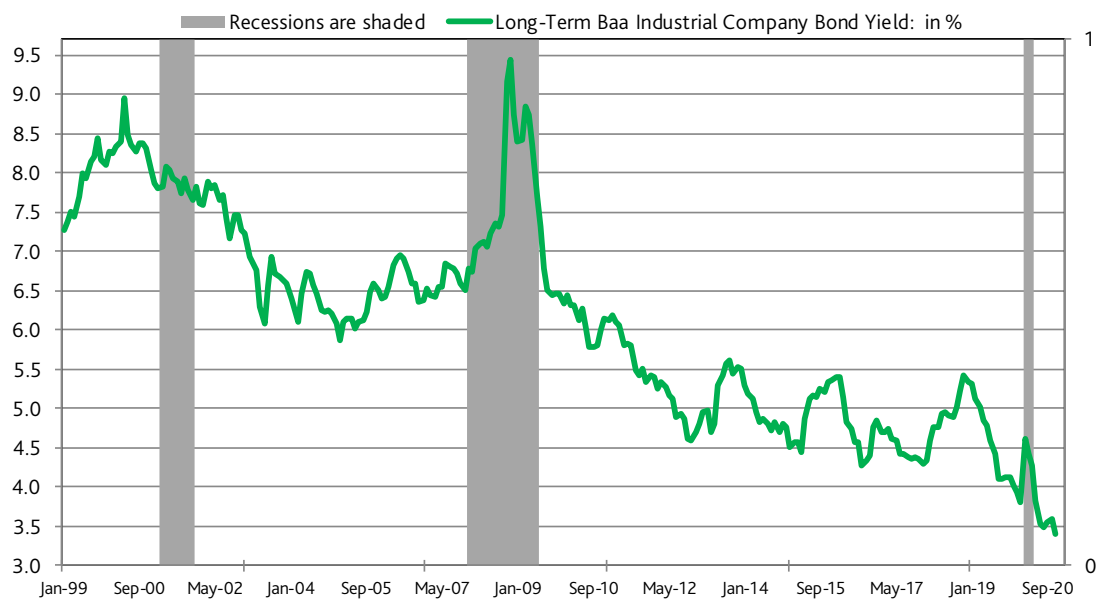
Corporate credit has largely recovered from the terrible slump prompted by COVID-19. In general, corporate bond yield spreads are now the narrowest since February 2020. Corporate bond yields also now reside near historical lows. For example, November 18's 3.37% long-term Baa industrial company bond yield was barely above August 6's 65-year low of 3.33%, while the accompanying 177 basis-point spread over the 30-year Treasury yield was the thinnest since mid-February 2020.

Prior to COVID-19 and since 2016, the lowest moving 12-month averages for the yield and spread of Moody's Analytics long-term Baa industrials were the 4.46% and 157 bp, respectively, of the span-ended March 2018. If, as expected, profits growth becomes well established in 2021, a 20 bp narrowing by the long-term Baa industrials spread seems likely.

However, such spread narrowing may be more than offset by higher benchmark Treasury bond yields later in 2021. In turn, after soaring higher by a prospective 52% annually in 2020 to a record high \$1.996 trillion, 2021's issuance of US\$-denominated investment-grade corporate bonds may shrink by 20% to \$1.600 trillion. However, the latter would still top 2017's erstwhile record-high of \$1.509 trillion.

**Figure 1: Still Low Long-Term Baa Industrial Company Bond Yield May Limit Downside for 2021's Investment-Grade Bond Issuance**

sources: NBER, Moody's Analytics

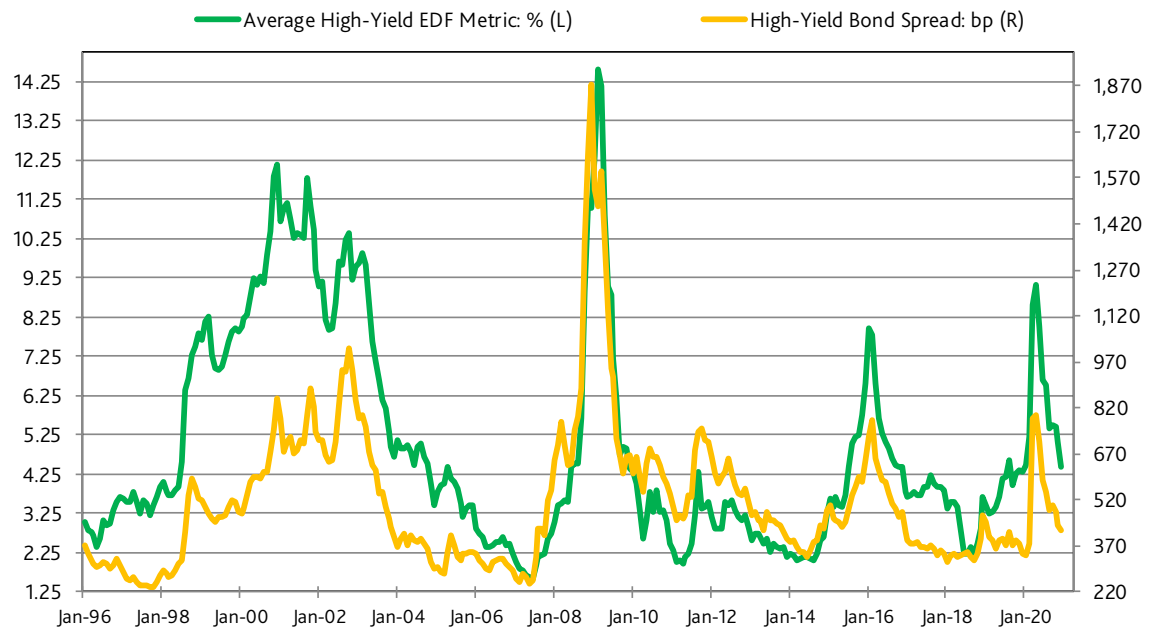


## Thinner High-Yield Bond Spread Likely in 2021

Though Bloomberg/Barclays recent speculative-grade bond yield of 4.80% was up from November 9's record-low 4.56%, November 18's high-yield bond spread of 417 bp was less than each of its prior month-long averages going back to February 2020's 377 bp. Granted that November 18's 4.42% average high-yield expected default frequency metric for U.S./Canadian high-yield issuers was the lowest since the 4.40% of January 17, 2020, or when COVID-19 fears first moved U.S. financial markets, the high-yield EDF is not yet low enough to warrant a high-yield bond spread as thin as 417 bp. Nevertheless, a high-yield bond spread that may now be too thin would be more worrisome if the high-yield EDF had been in a rising trend.

## Credit Markets Review and Outlook

**Figure 2: High-Yield Bond Spread Expects Declining Trend for High-Yield EDF Metric**  
 month-long averages; sources: Bloomberg/Barclays, Moody's Analytics



During 2017-2019, the moving 12-month average of the Bloomberg/Barclays high-yield bond spread bottomed at the 340 bp of the span-ended September 2018. Thus, if a positive outlook for profits growth is sustained in 2021, the high-yield bond spread might well narrow by 50 to 70 bp in 2021, which ought to be enough to more than offset a likely increase in benchmark Treasury yields.

In turn, after advancing by a likely 24% annually in 2020 to a record high \$537 billion, 2021's US\$-denominated high-yield bond issuance may ease by only 7%, to \$500 billion, which would still top 2017's former calendar-year zenith of \$453 billion. In addition to possibly lower speculative-grade bond yields, the refinancing of a still substantial amount of high-yield loans will help to power 2021's high-yield bond issuance.

After 2020's prospective 23% decline to \$402 billion, newly rated loans from high-yield issuers may grow by 19% in 2021 to \$480 billion. However, the latter would still fall noticeably short of its \$579 billion annual average of the five-years-ended 2019.

#### In 2021, Real GDP May Grow by 4% for First Time in 20 Years

A November 19 front-page article in the Wall Street Journal claimed that a 95% effective vaccine to prevent COVID-19 may be ready for distribution by the end of the year provided that federal regulators approve. If a COVID-19 vaccine is widely distributed by early 2021, U.S. real GDP growth of between 4% and 5% in 2021 seems doable. The consensus, or average, estimate of early November's Blue-Chip survey has 2021's real GDP expanding by 4%, where the average growth rate of the lowest 10 forecasts was 2.9% and the average of the highest 10 forecasts was 5.0%.

Calendar-year 2000's 4.1% was the last time real GDP grew by at least 4.0% annually. Nevertheless, despite 1998-2000's very rapid 4.5% average annual increase by real GDP, the then Lehman Brother's high-yield bond spread averaged a well-above average 496 bp during the span. The wide spread was largely the offshoot of a climb by the U.S. high-yield default rate from an April 1997 low of 1.5% to 7.5% by December 2000.

Thus, an extended stay by faster than 4% real GDP growth offers no assurance of below-average readings for the default rate and high-yield bond spreads. Nevertheless, when real GDP growth recovered from 1991's 0.1% dip with a 4.0% advance by 1994, the high-yield default rate would fall from a June 1991 high of 12.3% to 1.6% by March 1995. The combination of faster economic growth and a declining default rate

## Credit Markets Review and Outlook

helped to narrow a composite high-yield bond spread from a January 1991 high of 904 bp to November 1994's 338 bp.

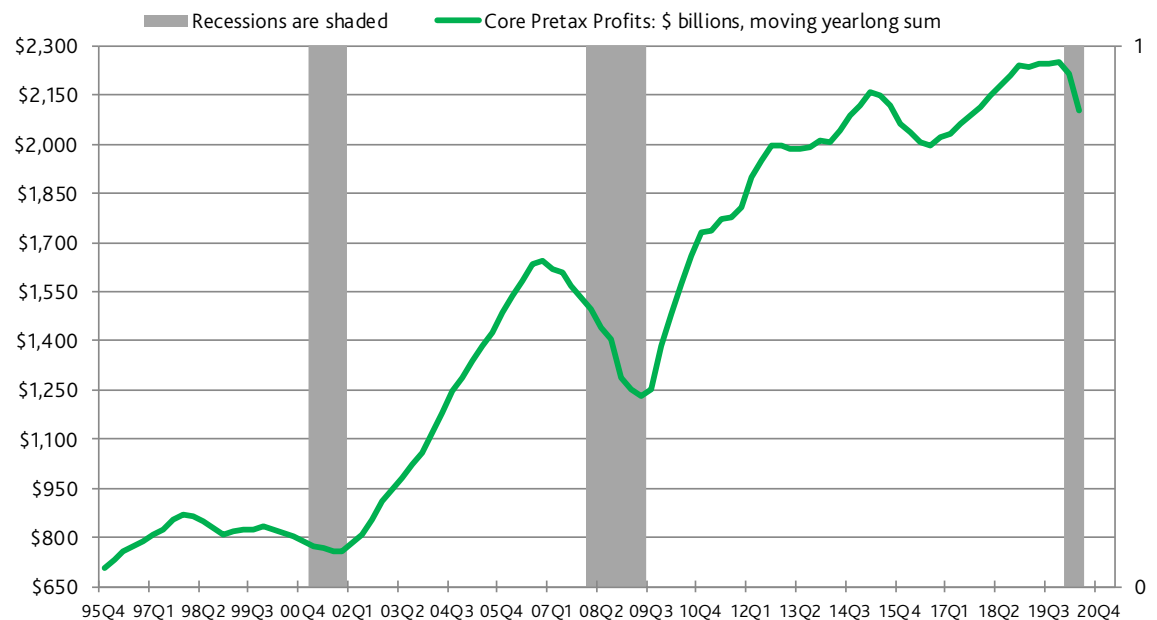
Immediately thereafter, an interest-rate induced slowing of growth to 1995's 2.7% rise temporarily lifted the default rate and widened spreads. However, a remedial cutting of fed funds helped to re-energize business activity by enough to fuel a 4.4% annual increase by 1997's real GDP which facilitated a drop by the default rate to April 1997's 1.5%. Also, the composite speculative-grade bond yield spread's month-long average would bottom at September 1997's 310 bp.

### 1990s Showed Profits Growth to be More Important than Real GDP Growth

Though real GDP's 3.0% average annualized rise of the seven years ended 1997 was much slower than the 4.5% of the three-years-ended 2000, core pretax profits' 11.0% average annualized advance of the seven-years-ended 1997 was much faster than the metrics' 3.3% average annual contraction of the three-years-ended 2000. (Core pretax profits are also known as pretax profits from current production and are from the U.S. government's National Income Product Accounts.) Thus, profits may matter more than GDP growth if companies are left with less income with which to pay off debt and fund dividends?

**Figure 3: Typical Post-Recession Recovery by Profits Will Enhance Corporate Credit Quality**

*sources: BEA, NBER, Moody's Analytics*



### Operating Leverage May Enhance 2021's Corporate Credit Quality

Thus, a positive 2021 outlook for corporate credit requires favorable prospects for corporate profits. According to FactSet, the consensus view of equity analysts has the earnings per share of the S&P 500's member companies more than recovering from 2020's prospective 14.5% contraction with an anticipated 22.1% expansion in 2021. The expected recovery by S&P 500 EPS follows from a projected rebound by S&P 500 revenues from 2020's 2.0% decline to a 7.8% increase in 2021.

By contrast, the average of 27 forecasts submitted to early November's Blue-Chip Economic Indicators calls for only a 5.7% annual increase by 2021's core pretax profits following 2020's expected drop of 10.8%. Here, the bottom 10 forecasts predict an average annual decline of 4.0% for core pretax profits, while the top 10 predictions have profits expanding by 15.1%, on average.

However, some of the forecasts on profits submitted to Blue Chip are patently inconsistent with adjacent views on business activity. One projection calling for a 9.1% drop by 2021's profits also predicts scintillating annual growth rates of 5.5% for real GDP, 7.8% for nominal GDP, and 6.4% for industrial production. To the contrary, the latter's forecasts on economic activity and production favor a climb by rates of resource utilization—from a low base no less—that ordinarily supply a much faster rate of core profits growth vis-a-

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vis nominal GDP growth. At the other extreme, another projection has profits soaring higher by 25.5% in 2021 notwithstanding accompanying subpar growth rate predictions of 2.0% for real GDP and 2.9% for nominal GDP.

Because of 2020's low rates of resource utilization, any material percent increase by 2021's business sales is likely to provide a textbook example of "operating leverage." When operating leverage takes hold, profits grow at a rate that is a multiple of the rate of growth for business sales.

Thus, the FactSet consensus predictions for 2021 of 7.8% revenue growth and 22.1% EPS growth make perfect sense from the perspective of operating leverage. By contrast, according to the 27 prognosticators supplying Blue-Chip with a profits forecast, the 5.7% average projection for core pretax profits growth exactly matched the group's average projection of 5.7% growth for 2021's nominal GDP. Thus, the Blue-Chip profits forecast dismisses the possibility of operating leverage, which often emerges during the early stages of a business cycle upturn, especially if productive resources are significantly underutilized. In all likelihood, 2021's growth rate for core pretax profits may at least double the rate of nominal GDP growth.

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

### THE U.S.

By Bernard Yaros of Moody's Analytics

### The 2020 Election: No Big Surprises

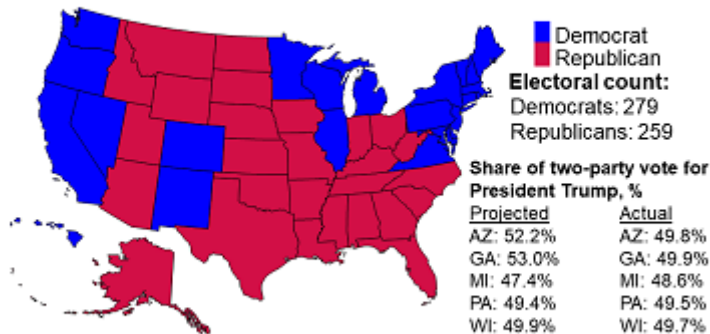
Former Vice President Joe Biden is the president-elect, Democrats will retain the House majority, and Republicans are favored to control the Senate. These are all outcomes that Moody's Analytics [had expected](#). Therefore, no election-induced changes to the U.S. economic outlook were warranted in November.

#### Why we got it right

The Moody's Analytics U.S. election models correctly predicted the 2020 presidential outcome. Our final model update, based on the October vintage of the U.S. baseline forecast, showed Biden eking out a nail-biter with 279 electoral votes to President Trump's 259. Though Biden has won 306 electoral votes, this was still a close race from the perspective of the Electoral College, since it came down to the slimmest of margins in a few must-win states. Arguably, the three most important states were Michigan, Pennsylvania and Wisconsin. Our projection of Trump's share of the two-party vote in the three "blue wall" states turned out to be close to the mark. We were off by only a tenth of a point in Pennsylvania, two-tenths of a point in Wisconsin, and just over a point in Michigan.

### Election Models Predicted a Nail-Biter

Oct 2020 forecast assuming typical nonincumbent turnout



Source: Moody's Analytics

This was not an easy election to forecast. Historically, it is tough to dislodge an incumbent. Our models automatically give the incumbent a 2-percentage point advantage in their projected share of the two-party vote across states. The economy does matter, though, and has overridden the benefit of incumbency. In the past century, all but one incumbent who ran for re-election within two years of a recession lost.

## Recessions Have Doomed Incumbents

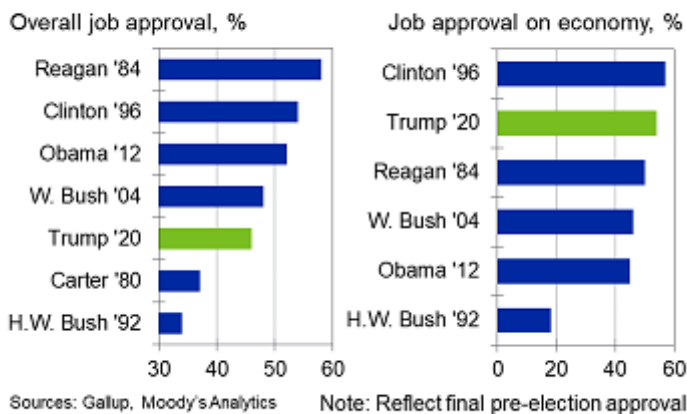
Elections in which incumbent ran within two yrs of a recession

Election Yr	Incumbent	Recession	Unemp. rate, %, ann. avg	Outcome
1912	William Taft	Jan 1910 to Jan 1912	5.2	Loss
1924	Calvin Coolidge	May 1923 to Jul 1924	5.5	Win
1932	Herbert Hoover	Aug 1929 to Mar 1933	23.6	Loss
1976	Gerald Ford	Nov 1973 to Mar 1975	7.7	Loss
1980	Jimmy Carter	Jan 1980 to Jul 1980	7.2	Loss
1992	George H.W. Bush	Jul 1990 to Mar 1991	7.5	Loss
2020	Donald Trump	Mar to Apr 2020	8.2	Loss

Sources: BLS, Census Bureau, NBER, Moody's Analytics

Trump, however, is not your average incumbent. Though he has had the lowest average approval of any president since FDR, his approval has been the most stable. Despite the pandemic, recession, and racial justice protests this year, Trump entered Election Day with a higher approval rating than Jimmy Carter and George H.W. Bush, who were the last two incumbents to lose re-election in the shadow of a recession. Though Trump's approval has shown remarkable stability due to steadfast Republican support, it has never breached the 50% mark, so he entered Election Day with a lower approval than Ronald Reagan, Bill Clinton and Barack Obama, who all won re-election handily. Therefore, Trump's approval rating, which was included in our models, was already telegraphing that while the president's path to re-election was tricky, he would not get wiped out like Carter or H.W. Bush.

## Not an Easy Election to Forecast



Further complicating our election forecast was the pandemic. This was not your average recession. Trump entered Election Day with the second-highest approval on the economy of any incumbent since Reagan. There are two potential explanations. First, the pandemic was an exogenous shock. It did not occur endogenously to the economy like the U.S. housing bubble. Therefore, Trump was not necessarily blamed for the crisis. Second, the pandemic has had such an uneven impact on the economic variables used by our models. Though the jobless rate paints a dark picture, personal income remains above precrisis levels, the stock market has roared back after its March lows, and

## The Week Ahead

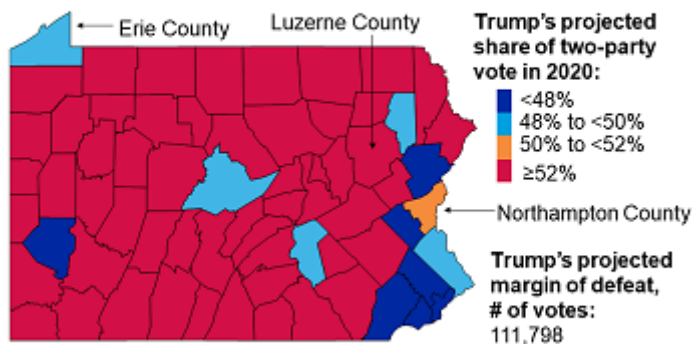
house prices have defied gravity. Had our models relied on just one of these economic variables, they would have either projected a Biden blowout or a comfortable Trump win. However, by including all these variables and their contradictory signals, our models pointed to a tight race that slightly favored Biden.

### Predicting the Keystone State

This was the first election cycle in which Moody's Analytics took its state-level methodology for forecasting presidential elections down to the county level for a few major battleground states. By and large, our county-level model performed well, and especially so in Pennsylvania, where we accurately predicted the winner in all but one of the state's 67 counties.

## Biden Leads by 68,300 Votes & Counting

How PA counties were forecast to vote under avg nonincumbent turnout



Source: Moody's Analytics

Note: Results reflect Sep 2020 forecast

Our model correctly projected that Erie County would flip from Trump to Biden. Erie, which is considered to be a bellwether for the state, is one of three counties that voted for Obama in 2012 but then voted for Trump in 2016. The other two Obama-Trump counties were Luzerne and Northampton County. While our model got Luzerne right, it did err on Northampton. Biden is eking out a narrow win in Northampton, whereas our model had projected a slim margin of victory there for Trump.

The county-level model for Pennsylvania features two economic variables: the unemployment rate and income per household. While we never expected Biden to pull off any big upsets in Trump country other than flipping Erie back into the Democratic column, our model still projected that Biden would whittle away at some of Trump's support, even in solidly red counties, because of the economic fallout of the pandemic. That assumption turned out to be correct. Biden ate into Trump's 2016 margins in heavily red areas outside Pittsburgh, Lancaster, and the Philadelphia region. However, one thing our Pennsylvania model did miss was Trump's outperformance in Philadelphia County. Even though Trump got walloped in Philadelphia County by 63 points, that was a 4-point improvement from his 2016 result. This likely owes to Trump's electoral gains among nonwhite voters this year.

Prior to November 3, we projected Biden would win the Keystone State by about 112,000 votes. The president-elect is currently leading in Pennsylvania by more than 68,000 votes. However, thousands of absentee and provisional ballots have yet to be counted. Given that these ballots will break heavily for Biden, the president-elect's lead will likely expand closer to 100,000 votes. If that is the case, then our county election model will have done a very good job in predicting the outcome in the all-important state of Pennsylvania.

## The Week Ahead

**AZ, GA reveal model blind spots**

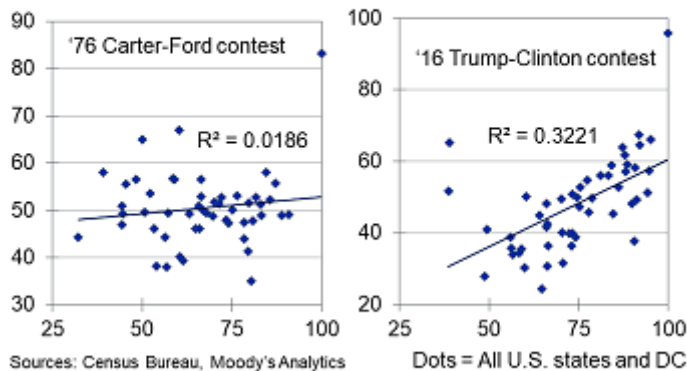
Our election models were not perfect, though. Biden won Arizona and Georgia, which our models did not foresee. One of the most crucial variables in our models is state fixed effects, which control for the share of the two-party vote that the incumbent president's party received in the prior election. These fixed effects capture state-specific idiosyncrasies such as the demographic composition of the electorate that will cause a state to vote a certain way. However, our state fixed effects will miss any major demographic change that occurs within four years of the last election. This is what seems to have happened with Arizona and Georgia.

There are many reasons why Arizona turned blue, such as a rising Latino population, which broke for Biden, and backlash against Trump's treatment of the late John McCain. However, since 2016, net migration into the Grand Canyon state has surged to a decade-long high, and it is the composition of in-migrants that has mattered the most. California, Illinois and Washington are contributing to more than half of net migration into Arizona. This influx of Democratic-leaning in-migrants is changing the contours of Arizona's electorate.

In Georgia, it is a slightly different story. Increasing racial diversity, which is progressing at a faster than average rate, along with Gen Z's outsize share of the population helps explain Biden's win in the Peach State. However, urbanization played a fundamental role. The Atlanta metro area, which broke heavily for Biden, made up only 40% of the state's population 50 years ago. It now makes up close to 60%, which matters because of the growing urban-rural divide in U.S. politics. Looking ahead to 2024, any model improvement will entail the inclusion of new variables that better capture urbanization and other demographic trends in real time.

**Urban-Rural Divide Grows in U.S. Politics**

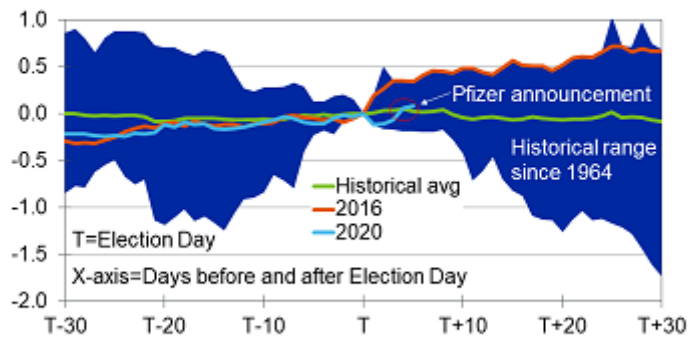
X-axis=% of pop in urban areas; Y-axis=Dem share of two-party vote, %



The post-election narrative in 2020 is much different than in 2016. To contrast the two, we performed an event study in which we looked at the 10-year U.S. Treasury yield in the days immediately before and after a presidential election. Since the 1964 Johnson-Goldwater contest, yields have, on average, risen by less than a basis point in the day immediately following an election. However, the two most extreme post-election movements in yields have occurred in 2016 and 2020.

## Yields Slump as Stimulus Prospects Fade

U.S. 10-yr Treasury yield, change relative to Election Day, ppt



Sources: Federal Reserve, Moody's Analytics

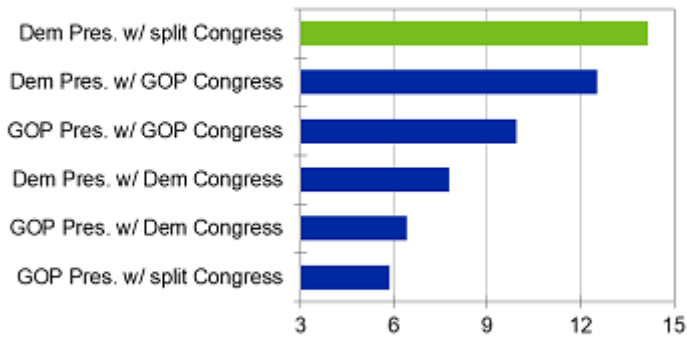
In 2016, the 10-year yield surged by 19 basis points after Trump's surprise win. This was the largest increase ever in the day after an election. At the time, the bond market was betting that Trump would get reflationary policies such as tax cuts, a military spending buildup, and an infrastructure package through a Republican-held Congress. Moreover, protectionist policies under Trump were expected to boost inflation.

In contrast, the 10-year yield plunged by 12 basis points after November 3, 2020. This was the largest decline ever after an election. Prior to November 3, the polls suggested that Democrats were poised to sweep the White House and Congress, which would have allowed Biden to enact an ambitious array of spending policies on everything from infrastructure to education. Moreover, a Democratic sweep would have all but guaranteed a multitrillion-dollar pandemic relief package à la the HEROES Act. Yet, with Republicans now favored to retain the Senate, this "reflation trade" was gutted.

Though investors have marked down their expectations for fiscal stimulus under Biden, stocks have rallied since the election. Historically, stocks have performed the best under divided government—specifically when Democrats control the White House while Congress is split. Investors seem to prefer divided government because policy gridlock will prevent the most contentious policies of either party from ever getting passed. In today's context, investors are rooting for gridlock in which a Republican Senate keeps Biden from imposing higher taxes on corporations and capital gains and expanding government healthcare, which would weigh on healthcare stocks. At the same time, markets are also looking forward to greater trade certainty under the new administration.

## Stocks Like Divided Government

S&P 500, avg annual % change by political outcome since 1945



Sources: Standard & Poor's, Moody's Analytics

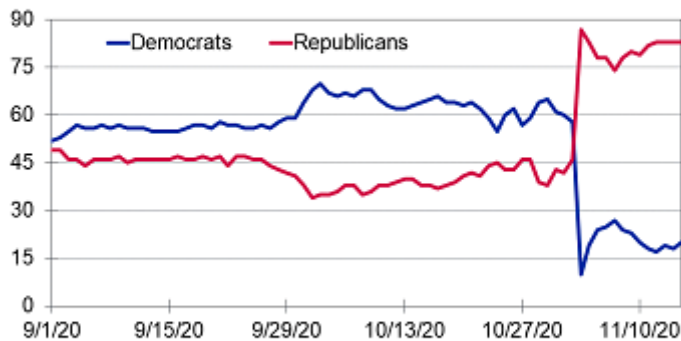
The baseline forecast for federal fiscal conditions assumes Biden and a divided Congress will pass a \$1.5 trillion rescue package in February. Thus, we project the deficit will remain elevated at 14.8% of GDP in fiscal 2021. This compares with an 8.6% deficit-to-GDP ratio as forecast by the Congressional Budget Office, which assumes current policy.

### Risks

The 2020 election is not over, and there is still some script left to be written. If Democrats win both runoff elections for Georgia's two Senate seats, they would control the Senate, which would force us to pencil in a larger COVID-19 rescue package, as well as sweeping changes to federal tax and spending policies.

## Odds Favor GOP Holding on to Senate

Probability that a major party will control the Senate, %



Sources: PredictIt, Moody's Analytics

However, prediction markets are assigning only a 20% probability to this scenario, and we concur that odds are low that Democrats will control the Senate, when all is said and done. As a result, the baseline forecast does not assume a Democratic Senate majority next year.

### Next Week

The holiday-shortened week in the U.S. will nevertheless see a slate of economic data releases including the Bureau of Economic Analysis' second estimate of third quarter GDP plus the PCE deflator, advance

## The Week Ahead

durable goods and international trade in goods numbers, personal income, and personal spending results, all for October. The latest Philadelphia Fed's nonmanufacturing survey and the Richmond Fed's manufacturing survey are due, along with the Chicago Fed National Activity Index. And in the robust housing sector, October new-home sales, the FHFA's purchase-only house price index, and the S&P CoreLogic Case-Shiller Home Price indexes will arrive.

## EUROPE

By Ross Cioffi of Moody's Analytics

### Consumer Spending Drives German Rebound for Q3

Third quarter GDP for Germany and France will headline the economic news in the week to come. We already have a clear idea of what the releases have in store thanks to preliminary estimates already published. In both cases, real output exceeded our expectations. We expect Germany's third quarter GDP to have increased 8.2% q/q following the 9.7% decline in the second. In France, GDP likely jumped 18.2% after a 13.8% decrease. The French flash estimate offered details that reflect our own understanding of the dynamics in Germany, too. Consumer spending drove the third quarter rebound and investments recovered quicker than expected. With trade flowing again, all countries in the euro zone benefitted. Unfortunately, with the rising COVID-19 infections the GDP outlook in both countries is dark. Our November baseline forecasts a 1.8% q/q decline in fourth quarter euro zone output.

We expect the seasonally adjusted number of French job seekers in October to have remained at September's level of 3.6 million. The labor market had been improving over the third quarter, but things will get worse in the fourth quarter as firms are forced to shut down again under lockdown orders and a lack of demand. National fiscal policies are helping to keep unemployment from surging and October was a transition month, so some of the effects of the second wave won't be felt until November.

Likewise, we think household consumption of goods in France slid 1% m/m in October. This comes after a steeper 5.1% decline in September. With consumer confidence reversing during the month we aren't too optimistic for private spending. For the same reason we see Spanish retail sales sliding 0.5% m/m in October, adding to September's 0.3% decline. Finally, the euro zone business and consumer sentiment survey for November likely came in with a reading of 85.8, down from 90.9 in October, which was unchanged from September. The October survey did not cover the periods when euro zone countries began tightening social distancing measures again, so we think there will be a large fall in November to reflect the change. Specifically, consumer, retail, and services subindexes should add the heaviest weights on the index.

	Key indicators	Units	Moody's Analytics	Last
Tues @ 9:00 a.m.	Germany: GDP for Q3	% change	8.2	-9.7
Wed @ 1:00 p.m.	France: Job Seekers for October	mil, SA	3.6	3.6
Fri @ 9:45 a.m.	France: Household Consumption Survey for October	% change	-0.6	-5.1
Fri @ 9:45 a.m.	France: GDP for Q3	% change	18.2	-13.8
Fri @ 10:00 a.m.	Spain: Retail Sales for October	% change	-0.5	-0.3
Fri @ 12:00 p.m.	Euro Zone: Business and Consumer Sentiment for November	index	85.8	90.9

## Asia-Pacific

By Shahana Mukherjee of Moody's Analytics

### Bank of Korea Likely to Keep Policy Rate on Hold at 0.5%

Next week's economic calendar is light, with the Bank of Korea's monetary policy decision the highlight. We expect the central bank to keep the key policy rate unchanged at the record low 0.5% at its November meeting. South Korea's economy rebounded with a strong 1.9% expansion in the September quarter, aided by the government's fiscal measures and an improving trade position. However, the scope for sustaining this recovery will be challenged by the recent escalation in domestic COVID-19 caseloads, which have resulted in the reimposition of stricter social distancing rules in the greater Seoul area.

The recovery in exports, too, is expected to moderate over the December quarter, as the renewed restrictions across large parts of Europe and the U.S. disrupt global consumption. However, having delivered rate cuts worth 75 basis points in response to the COVID-19 shock, the Bank of Korea is likely to adopt a wait-and-see approach for now as consumer spending gradually picks up, with concerns regarding rising household debt levels likely to discourage a lower interest rate through the rest of 2020.

Singapore's industrial output is likely to have grown by 4% in yearly terms in October, following a 24.2% increase in September. Singapore's industrial activity has rebounded since August, driven by the surge in global demand for biomedical products and electronics. However, sustaining this pickup will be difficult in the face of the global COVID-19 resurgence. We expect a weaker showing in nonelectronics goods exports to have weighed on the revival in industrial activity in October.

	Key indicators	Units	Moody's Analytics Confidence	Risk	Last
Tues @ 8:00 a.m.	South Korea Consumer Sentiment for November	Index	83	4	91.6
Thur @ 12:00 p.m.	South Korea Monetary Policy for November	%	0.5	4	0.5
Thur @ 4:00 p.m.	Singapore Industrial Production for October	% change yr ago	4	3	24.2

## The Long View

### A broader equity market rally will help to enhance corporate credit quality.

By John Lonski, Chief Capital Markets Economist, Moody's Capital Markets Research  
November 19, 2020

#### CREDIT SPREADS

As measured by Moody's long-term average corporate bond yield, the recent investment grade corporate bond yield spread of 116 basis points resembled its 116 basis-point median of the 30 years ended 2019. This spread may be no wider than 125 bp by year-end 2020.

The recent high-yield bond spread of 461 bp is thinner than what is suggested by the accompanying long-term Baa industrial company bond yield spread of 177 bp and the recent VIX of 22.8 points. The latter has been historically associated with a 645-bp midpoint for a composite high-yield bond spread.

#### DEFAULTS

October 2020's U.S. high-yield default rate of 8.3% was up from October 2019's 3.8% and may average 10.3% during 2021's first quarter.

#### US CORPORATE BOND ISSUANCE

Third-quarter 2019's worldwide offerings of corporate bonds revealed annual advances of 15.2% for IG and 56.8% for high-yield, wherein US\$-denominated offerings soared higher by 36.8% for IG and 81.3% for high yield.

Fourth-quarter 2019's worldwide offerings of corporate bonds revealed annual advances of 15.3% for IG and 329% for high-yield, wherein US\$-denominated offerings dipped by 0.8% for IG and surged higher by 330% for high yield.

First-quarter 2020's worldwide offerings of corporate bonds revealed annual advances of 17.7% for IG and 26.5% for high-yield, wherein US\$-denominated offerings increased 43.7% for IG and grew 21.4% for high yield.

Second-quarter 2020's worldwide offerings of corporate bonds revealed annual surges of 69% for IG and 31% 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.

For 2019, worldwide corporate bond offerings grew by 5.4% annually (to \$2.447 trillion) for IG and advanced by 49.2% for high yield (to \$561 billion). The projected annual percent increases for 2020's worldwide corporate bond offerings are a 17.5% for IG and 18.8% for high yield.

#### US ECONOMIC OUTLOOK

Unacceptably high unemployment and other low rates of resource utilization will rein in Treasury bond yields. As long as the global economy operates below trend, 1.00% will serve as the upper bound for the 10-year Treasury yield. Until COVID-19 risks fade substantially and election year risks recede, wider credit spreads are possible.

## The Long View

## Europe

By Ross Cioffi of Moody's Analytics  
November 19, 2020

### TURKEY

The new governor of the Central Bank of the Republic of [Turkey](#) increased the key policy rate—the benchmark one-week repo rate—by 475 basis points to 15% at Thursday's meeting. The late liquidity window rate was also raised, to 19.5% from 14.75%. The rate hike meets market expectations that the CBRT needed to act forcefully to get inflation and inflation expectations under control.

With such a strong rate increase, inflation pressures should soften and demand for the Turkish lira should strengthen, thereby helping the external balance. The lira already started to rally following the announcement of the new governor on 6 November, with the currency appreciating about 8.7% against the dollar since then. Markets will take the rate decision as proof of a more credible and independent monetary policy in Turkey.

### EURO ZONE

[Euro zone](#) construction output fell by 2.9% m/m in September, ending the recovery that started in May. September's slump reverses much of the 3.9% m/m increase in August. Construction output rose by 12.5% q/q over the third quarter following an 11.6% plunge in the second. But after two previous quarters of declines, construction was still 2.9% lower in yearly terms between July and September.

The main drag on September's production came from buildings projects, which were down 3.2% m/m after gaining 4.1% in August. Civil engineering projects fell by just 0.4% m/m after a 1.5% increase previously. Government spending will keep civil engineering projects from weighing too heavily on construction output, but private demand for new buildings will lag in the final months of this year and heading into the next. Consumer and business sentiment has recently soured, erasing the gains made over the summer.

On the country level, yearly construction output remains in the doldrums in France and Spain. French construction was down 8.1% y/y, while Spain's declined by 7.2% in September. By contrast, output was up 0.3% y/y in Germany and 5.1% in Italy.

New passenger car registrations dropped 7.8% year over year across the EU in October, to a total of 953,615. The decline comes after a 3.1% y/y rise in September, which was the first time the number of registrations increased this year. On a country level, new registrations were down in all EU economies except for Ireland and Romania. Registrations plunged by 21% in Spain, by 9.5% in France, by 3.6% in Germany, and by just 0.2% in Italy.

Car registrations can fluctuate wildly, and even before the pandemic registrations were looking weak, down 7.5% in January and 7.4% y/y in February. But there is no question about the reason behind October's swing into negative territory. The second wave of COVID-19 reversed the gains made this summer in consumer confidence, pushing households back into precautionary savings mode.

The release darkens the immediate outlook for the auto sector, which directly contributes 8.5% of total manufacturing employment in the EU. The highest share of employment in the auto industry is in Slovakia, at 15.8%; in Germany, the largest economy in the EU, the industry contributes about 11.8% of all manufacturing jobs. Low demand for cars will translate into low industrial production, but the good news is that car demand hasn't taken as much of a hit outside of the European market. We should also bear in mind that the EU-wide figure does not say what's happening in the market for used cars, which we suspect has performed better this year than that for new cars. We expect households looking to secure themselves a 'safer' mode of transport than public transit will opt for a used car, given the economic outlook.

We're reading Wednesday's report as yet another sign that consumers—the force that drove the third-quarter recovery—have been retrenching this fall. The October registration data come on the heels of a further decline in retail sales in September, and after the European Commission's consumer confidence indicator fell to -15.5, its lowest reading since last May's -18.8. Wednesday's consumer price release for the euro area also reflects persistently low demand among core goods and services. Prices in the core basket grew just 0.2% y/y in October, while the headline HICP fell by 0.3%.

## The Long View

## Asia Pacific

By Shahana Mukherjee of Moody's Analytics  
November 19, 2020

### JAPAN

Japan's economy returned to growth in the September quarter, as seasonally adjusted GDP increased by a notable 5% on a quarterly basis after a historic 8.2% plunge in the prior quarter. The stronger than expected rebound was anchored by a revival in private consumption and exports, which rose by 4.7% and 7%, respectively, on a quarterly basis, even though an extended decline in non-residential investment eroded the net gain. The latest reading translated into an annualized rebound of 21.4% in September, providing some solace that the economy is gradually emerging from the throes of the COVID-19 crisis.

The September quarter's performance was particularly noteworthy because it marked the first increase in output in four quarters, as domestic conditions gradually revived following the dual shocks from the consumption tax hike and the pandemic. But the reading should also be evaluated in context. The most promising aspect was the revival in private consumption, which accounts for more than 50% of national output, as it contributed 2.5 percentage points to the net 5% increase. While the recent improvement in overseas sales also helped, a stronger external position (which added 2.9 percentage points to the quarterly gain) resulted not from higher net sales, but from a sharp decline in imports. A significantly weaker investment position also remained a big concern, as it shaved 1 percentage point from the net gain.

Despite the impressive September rebound, the downside risks to Japan's recovery are intensifying. Chief among these is the accelerating trend in domestic COVID-19 cases, which will weigh on confidence and is likely to cause households to retreat once again. With daily caseloads exceeding 1,000 through most of November, Japan's third wave may well prove to be stronger and more prolonged as winter approaches and may necessitate the reimposition of strict social distancing rules. With household spending still below pre-pandemic levels, the implications of widening restrictions on a fragile labour market, with unemployment at nearly 25% above levels a year ago, will be dire.

Compounding these challenges is the resurgence of cases in Europe and the U.S., which has led to the reimposition of lockdowns or widening state-level restrictions. Even though these measures are more targeted and of limited duration this time, they will induce another setback in global consumption, with stronger implications for Japan's durable goods exports. With a high probability of these restrictions being extended through the rest of 2020, there's an elevated risk that Japan's manufacturing industries are set for another shock to income in the months ahead.

The need for additional fiscal stimulus can therefore not be overstated, and while the Suga government is likely to pass another package in the weeks ahead, the composition of the new support will be key. Spending oriented towards attracting private investment, as intended by the government, will not yield substantial gains amid the current uncertainty. Instead, the situation necessitates additional direct income support, especially as household incomes come under pressure from deteriorating prospects.

Eventually, the extent of the December-quarter slowdown will depend on the severity of the domestic outbreak and the duration of renewed international lockdowns. We expect Japan's economy to contract by 5.5% in 2020, but another nationwide emergency, or, a delay in providing the right mix of fiscal support, may well lead to a deeper decline in 2020 and a slower revival through the first half of 2021.

## Ratings Round-Up

## Ratings Round-Up

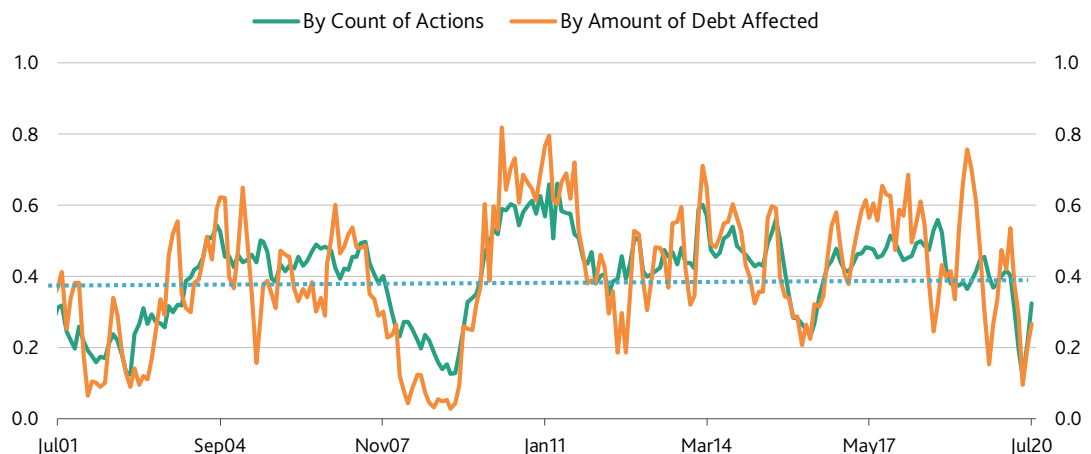
Latest U.S. Changes Follow Familiar Pattern of Upgrades to Downgrades

By Steven Shields

U.S. corporate credit performance was mixed for the period ended November 17, with downgrades accounting for half of the rating changes but 82% of the affected debt. Upgrades were concentrated in homebuilding and consumer staples, while downgrades were concentrated in energy and commercial real estate—a common theme since the onset of the COVID-19 pandemic. The most notable downgrade was made to Pfizer Inc. with Moody's downgrading its senior unsecured long-term ratings to A2 from A1. The downgrade reflects the credit-negative aspects of Pfizer's separation of its Upjohn business, including a significant contraction in free cash flow and reduced diversity. Moody's Investors Service also downgraded Peabody Energy Corp.'s corporate family rating to Caa1 from B3 and senior secured debt ratings to Caa1 from B3. The downgrade was driven primarily by the company's eroding liquidity and increased likelihood of a debt restructuring. Gulfport Energy Corp.'s credit ratings were withdrawn by Moody's Investors Service after Gulfport's filed for joint prearranged chapter 11 plan of reorganization. Lennar Corp. and PulteGroup Inc.'s senior unsecured notes were both upgraded to Baa3 from Ba1. Despite the pandemic, demand for homes recovered relatively rapidly and steadily since bottoming in the second quarter. Moody's expects conditions to remain stable over the next 12 months as underlying housing fundamentals remain favorable.

European rating change activity was predominately credit negative in the period. Downgrades outnumbered upgrades three to one and accounted for all the reported debt affected. The largest change in terms of debt affected last week was made to Heathrow Finance PLC with Moody's Investors Service downgrading Heathrow's corporate family rating to Baa2 from Ba1 and its senior secured debt ratings to B1 from Ba3. The downgrade reflects the persistently difficult operating environment for Heathrow airport as evidenced by the weaker than anticipated pace of passenger demand recovery due to travel restrictions and quarantine measures in 2020, and Moody's expectation that the breadth and severity of the coronavirus outbreak will lead to slower than previously anticipated traffic recovery.

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

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

FIGURE 3

## Rating Changes: Corporate &amp; Financial Institutions – US

Date	Company	Sector	Rating	Amount (\$ Million)	Up/ Down	Old LTD Rating	New LTD Rating	IG/SG
11/12/20	SERVICE PROPERTIES TRUST	Industrial	SrUnsec/LTCFR /SrSub/JrSub/PS	6,100	D	Ba1	Ba2	SG
11/12/20	PEABODY ENERGY CORPORATION	Industrial	SrSec/BCF/LTCFR/PDR	1,000	D	B3	Caa1	SG
11/12/20	MAVERICK, INC. -IRB HOLDING CORPORATION	Industrial	SrSec/SrUnsec /BCF/LTCFR/PDR	1,235	U	B3	B2	SG
11/16/20	LENNAR CORPORATION	Industrial	SrUnsec	6,220	U	Ba1	Baa3	SG
11/16/20	PULTEGROUP, INC.	Industrial	SrUnsec	2,723	U	Ba1	Baa3	SG
11/16/20	PFIZER INC.	Industrial	SrUnsec/BCF/LTIR	40,506	D	A1	A2	IG
11/17/20	TUPPERWARE BRANDS CORPORATION	Industrial	SrUnsec/LTCFR/PDR	600	U	Ca	Caa3	SG
11/17/20	GULFPORT ENERGY CORPORATION	Industrial	PDR		D	Ca	D	SG

Source: Moody's

FIGURE 4

## Rating Changes: Corporate &amp; Financial Institutions – Europe

Date	Company	Sector	Rating	Amount (\$ Million)	Up/ Down	Old LTD Rating	New LTD Rating	IG/SG	Country
11/11/20	HEATHROW FINANCE PLC	Industrial	SrSec/LTCFR/PDR	1,481	D	Ba3	B1	SG	UNITED KINGDOM
11/11/20	BIRMINGHAM AIRPORT HOLDINGS LIMITED-BIRMINGHAM AIRPORT (FINANCE) PLC	Industrial	SrUnsec	626	D	Baa2	Baa3	IG	UNITED KINGDOM
11/13/20	PIOLIN II S.A.R.L	Industrial	SrSec/BCF/LTCFR/PDR		D	B3	Caa1	SG	SPAIN
11/16/20	BOPARAN HOLDINGS LIMITED	Industrial	LTCFR/PDR		U	Caa1	B3	SG	UNITED KINGDOM

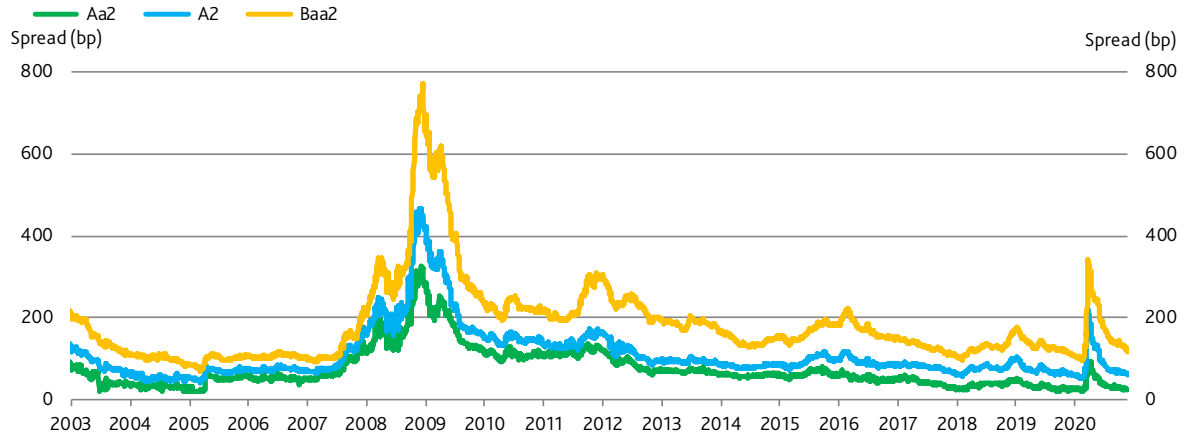
Source: Moody's

Market Data

Market Data

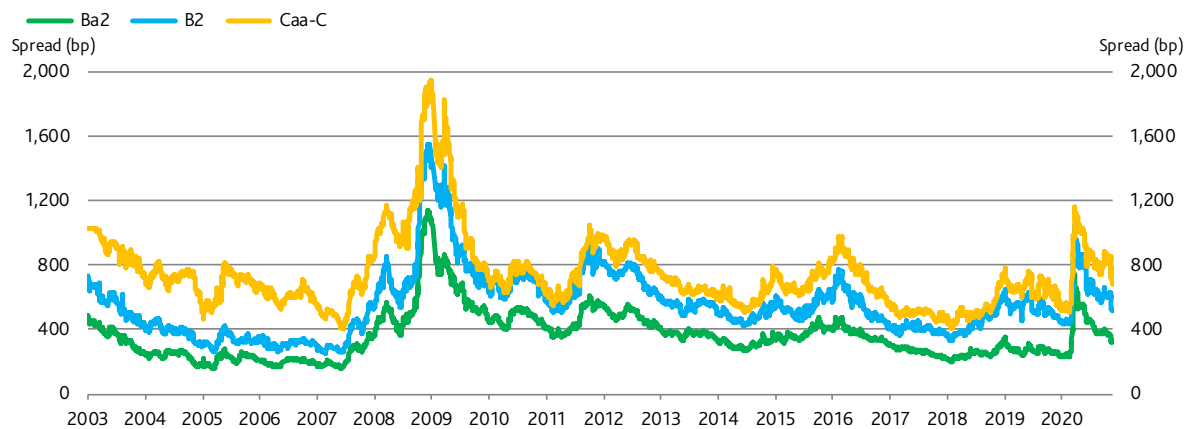
Spreads

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 (November 12, 2020 – November 18, 2020)

CDS Implied Rating Rises		CDS Implied Ratings		
Issuer		Nov. 18	Nov. 12	Senior Ratings
McDonald's Corporation		Aaa	Aa1	Baa1
Boeing Company (The)		Ba3	B1	Baa2
PepsiCo, Inc.		Aa2	Aa3	A1
Walt Disney Company (The) (Old)		Aaa	Aa1	A2
General Motors Company		Baa3	Ba1	Baa3
United Airlines, Inc.		Caa2	Caa3	Ba3
Delta Air Lines, Inc.		Caa1	Caa2	Baa3
Carnival Corporation		Caa2	Caa3	B2
Nissan Motor Acceptance Corporation		B2	B3	Baa3
Conagra Brands, Inc.		Aa2	Aa3	Baa3

CDS Implied Rating Declines		CDS Implied Ratings		
Issuer		Nov. 18	Nov. 12	Senior Ratings
Mack-Cali Realty, L.P.		Caa3	Ba1	B1
Danaher Corporation		A3	Aa3	Baa1
CVS Health		A3	A2	Baa2
American Express Credit Corporation		Aa2	Aa1	A2
Intel Corporation		A2	A1	A1
Merck & Co., Inc.		Aa3	Aa2	A1
Charles Schwab Corporation (The)		A3	A2	A2
Abbott Laboratories		Baa1	A3	A3
National Rural Utilities Coop. Finance Corp.		Aa3	Aa2	A2
ONEOK, Inc.		Ba2	Ba1	Baa3

CDS Spread Increases		CDS Spreads		
Issuer	Senior Ratings	Nov. 18	Nov. 12	Spread Diff
Mack-Cali Realty, L.P.	B1	627	114	513
Rite Aid Corporation	Caa3	858	800	58
Avon Products, Inc.	B1	183	164	19
ONEOK, Inc.	Baa3	150	138	12
ONEOK Partners, L.P.	Baa3	132	122	11
Danaher Corporation	Baa1	47	38	9
Iron Mountain Incorporated	Ba3	120	114	7
Kraft Heinz Foods Company	Baa3	90	84	6
Ball Corporation	Ba1	67	61	6
DPL Inc.	Ba1	351	345	6

CDS Spread Decreases		CDS Spreads		
Issuer	Senior Ratings	Nov. 18	Nov. 12	Spread Diff
Nabors Industries, Inc.	Caa1	2,924	3,155	-231
American Airlines Group Inc.	Caa1	2,040	2,246	-205
Macy's Retail Holdings, LLC	B1	864	992	-128
Royal Caribbean Cruises Ltd.	B2	724	845	-121
United Airlines Holdings, Inc.	Ba3	693	794	-101
Carnival Corporation	B2	559	651	-91
Staples, Inc.	B3	933	1,023	-90
Nordstrom, Inc.	Baa3	447	535	-88
United Airlines, Inc.	Ba3	591	678	-87
United States Steel Corporation	Caa2	756	837	-81

Source: Moody's, CMA

## Market Data

Figure 4. CDS Movers - Europe (November 11, 2020 – November 18, 2020)

CDS Implied Rating Rises		CDS Implied Ratings		
Issuer		Nov. 18	Nov. 12	Senior Ratings
Banco Bilbao Vizcaya Argentaria, S.A.		A1	A3	A3
Portugal, Government of		Aa3	A2	Baa3
Lloyds Bank plc		Aa2	A1	A1
Banco Santander S.A. (Spain)		Aa3	A1	A2
HSBC Holdings plc		A2	A3	A2
Svenska Handelsbanken AB		Aa1	Aa2	Aa2
Commerzbank AG		A1	A2	A1
Electricite de France		Aa3	A1	A3
Total SE		Aa3	A1	Aa3
Nationwide Building Society		A1	A2	A1

CDS Implied Rating Declines		CDS Implied Ratings		
Issuer		Nov. 18	Nov. 12	Senior Ratings
ABN AMRO Bank N.V.		Aa1	Aaa	A1
Siemens Aktiengesellschaft		Aa1	Aaa	A1
Thales		A3	A2	A2
Smurfit Kappa Acquisitions		Baa3	Baa2	Ba1
Boparan Finance plc		Caa2	Caa1	Caa1
Italy, Government of		Ba1	Ba1	Baa3
France, Government of		Aaa	Aaa	Aa2
United Kingdom, Government of		Aaa	Aaa	Aa3
Germany, Government of		Aaa	Aaa	Aaa
Spain, Government of		A3	A3	Baa1

CDS Spread Increases		CDS Spreads		
Issuer	Senior Ratings	Nov. 18	Nov. 12	Spread Diff
Boparan Finance plc	Caa1	555	510	45
Koninklijke KPN N.V.	Baa3	107	102	5
Ziggo Secured Finance B.V.	Caa1	224	220	5
Caixa Geral de Depositos, S.A.	Ba1	112	108	4
Virgin Media Finance PLC	B2	258	254	4
Permanent tsb p.l.c.	Baa2	219	215	4
BNP Paribas Fortis SA/NV	A2	33	31	2
Centrica plc	Baa2	91	89	2
Smurfit Kappa Acquisitions	Ba1	68	66	2
3i Group plc	Baa1	96	94	2

CDS Spread Decreases		CDS Spreads		
Issuer	Senior Ratings	Nov. 18	Nov. 12	Spread Diff
Novafives S.A.S.	Caa2	869	959	-90
CMA CGM S.A.	Caa1	541	612	-71
TUI AG	Caa1	816	877	-61
Hammerson Plc	Baa3	393	448	-55
Stena AB	Caa1	601	648	-47
Vue International Bidco plc	Ca	781	823	-42
Jaguar Land Rover Automotive Plc	B1	621	651	-31
Casino Guichard-Perrachon SA	Caa1	725	751	-26
Ineos Group Holdings S.A.	B2	328	354	-26
Rolls-Royce plc	Ba3	306	330	-25

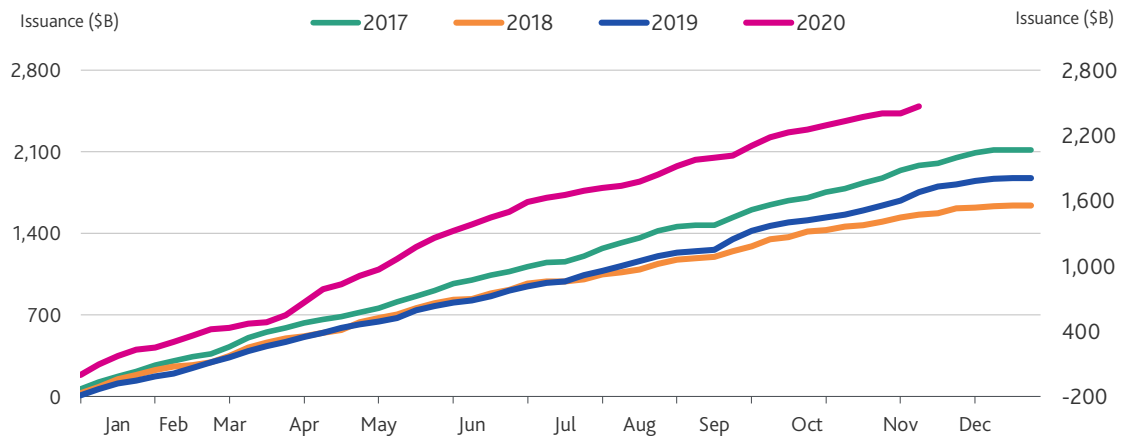
Source: Moody's, CMA

Market Data

Issuance

FIGURE 5

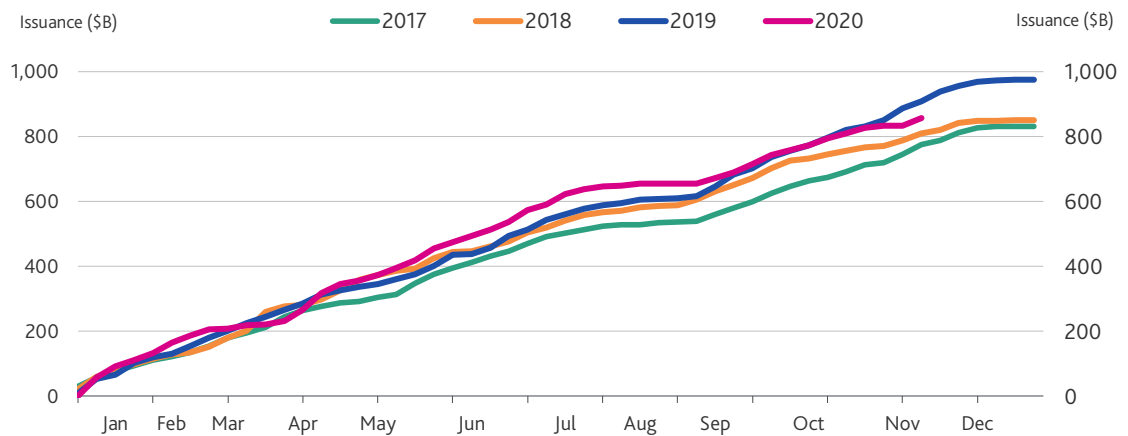
Market Cumulative Issuance - Corporate & Financial Institutions: USD Denominated



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	46.275	16.975	65.127
Year-to-Date	1,897.459	494.621	2,471.048

	Euro Denominated		
	Investment-Grade	High-Yield	Total*
	Amount \$B	Amount \$B	Amount \$B
Weekly	20.624	0.475	23.190
Year-to-Date	715.597	106.656	857.306

\* Difference represents issuance with pending ratings.

Source: Moody's/ Dealogic

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