MOODY'S ANALYTICS

WEEKLY MARKET OUTLOOK
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What a Difference a Year Makes

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Throughout the pandemic, corporate credit markets have remained surprisingly calm despite significant and risky debt exposures. As U.S. public borrowing as a source of demand for goods and services has increased for decades, corporate borrowing has followed suit.

Since the end of the 2007-2009 recession, household debt as a share of GDP fell by 20%, while federal debt rose by more than 50%, followed by a 16% jump in corporate debt. Households have rightsized their liabilities compared with the mortgage bubble years, but firms have levered up, often to buy back shares at low interest rates.

While the Treasury's creditworthiness causes few immediate liquidity concerns, the same is less obvious for corporations, which are at the whim of private revenue streams, at least some of which dried up in 2020. Further, inflated corporate debt already had analysts concerned prior to the pandemic. To much attention, the leveraged loan market had more than doubled from about $500 billion in 2010 to more than $1.2 trillion by the end of 2019. Adding the U.S. corporate junk bond market, the sector entered the 2020 downturn with around $3 trillion in debt of questionable quality and leveraged loan issuance was strong in 2020 and remains above that seen pre-pandemic this year.

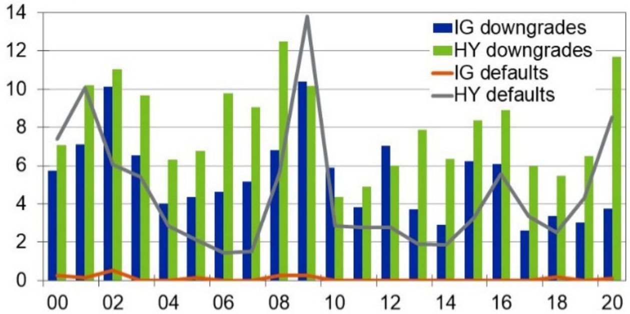
The difference between 2020 and 2008

As the U.S. went into its COVID-19-related lockdown last March, corporations drew down credit lines to meet payments, eroding credit quality. About half of Moody's-rated corporate bonds entered the crisis in junk status, and the second quarter of 2020 saw the most corporate downgrades on record. Yet, while total 2020 industrial downgrades rose to the levels of the 2008 financial crisis, BAA corporate interest spreads widened by only 180 basis points, compared with 450 basis points in 2008.

Moody's Analytics and Moody's Investors Service maintain separate and independent economic forecasts. This publication uses the forecasts of Moody's Analytics. Moody's Analytics markets and distributes all Moody's Capital Markets Research materials. Moody's Analytics does not provide investment advisory services or products. For further detail, please see the last page.

Firm Defaults Fall Short of Downgrades

1-yr corporate downgrades and 1-yr corporate defaults, %

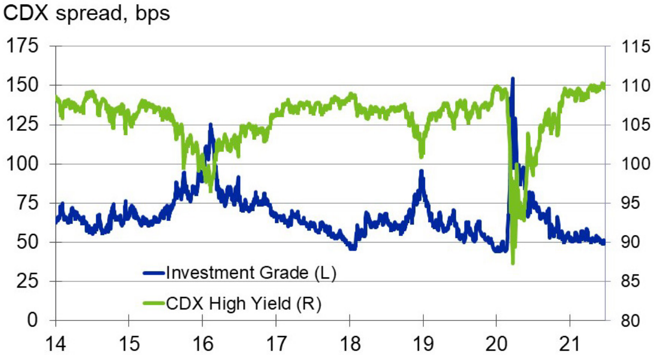


Sources: MIS, Moody's Analytics

Markets took downgrades in stride because of key differences between the last two recessions: There were few financial sector downgrades in 2020, as it remained in good health and the Federal Reserve aggressively eased monetary policy and restarted its emergency credit facilities.

Perceptions of Credit Risk Remain Low

CDX spread, bps

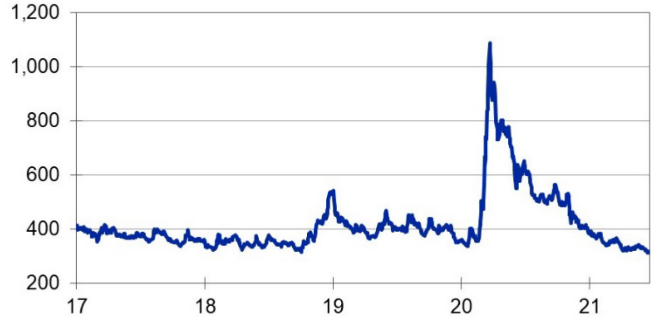


Sources: Markit, Bloomberg LP, Moody's Analytics

What a difference a year makes. Rating changes for U.S. corporate and financial institutions have been mostly favorable. By a count of actions, the share of favorable rating changes is near 60%, the highest since 2013. Market perceptions of credit risk, proxied by the CDX spread, remain low for both investment grade and high yield. This coupled with declining defaults and low market volatility are keeping high-yield corporate bond spreads tight.

Spreads Haven't Budged

High-yield OA spread, bps



Sources: ICE BofA, Moody's Analytics

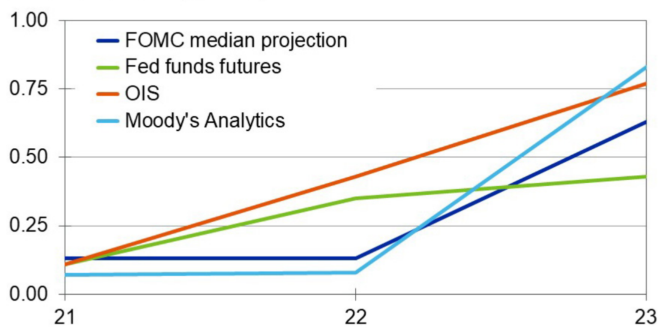
Though corporate bond issuance is lagging behind last year's torrid pace, investment-grade and high-yield issuance are both on track to post more issuance this year than that seen in the few years prior to the pandemic.

Hawkish Fed boosts leverage loans

The Federal Reserve's dot plot implied that the majority of participants believe the appropriate path for the target range for the fed funds rate is for an earlier liftoff and two rate hikes in 2023. The Fed's move puts them closer to our baseline and market expectations. The hawkish shift initially rattled the bond market, as it was a larger hawkish shift in the dot plot, but it has provided a boost to the leverage loan market.

Fed Moves Closer to Our Baseline

Fed funds rate at yr's end, %



Sources: Federal Reserve, Bloomberg LP, Moody's Analytics

Over the past week, leveraged loan demand remains strong and companies are rushing to reprice their borrowings as the Fed turned more hawkish, implying rates could rise earlier than previously thought. Leveraged loans are typically priced with floating interest rates. The number of leveraged loans that were repriced was significantly higher this month than in each of the prior two months, and it will continue to climb. Leveraged loan issuance for M&A deals also increased from May to June, but repricing has been busier.

The leveraged loan market should continue to do well because of the risk that rates could rise sometime in 2023. Also, the acceleration in realized inflation is another positive for the leveraged loan market. Leveraged loans have been used as alternatives to traditional inflation hedges—gold, TIPS and natural resources. As inflation accelerates, corporate real debt burdens lessen. In other words, more inflation means debtors can pay back the dollars they owe their creditors in money that has a lower real value. This is beneficial for highly indebted companies.

Corporate credit markets are more sensitive to default risk than inflation. An acceleration in inflation reduces nominal debt and is usually a symptom of stronger GDP growth; both reduce default risk. Therefore, we don't anticipate significant fluctuations in corporate bond spreads because of heightened inflation concerns. On the credit risk front, there has been some improvement over the past week. The CDX high-yield spread risk, a proxy for credit, has narrowed over the past several trading days and is near its recent lows seen earlier this month.

Economic roundup

It's been a busy week of U.S. economic data and, on net, it reduced our high-frequency GDP model's tracking estimate of second-quarter GDP growth by 0.8 of a percentage point to 9.7% at an annualized rate.

Durable goods orders were up 2.3% in May, a touch lighter than our forecast for a 2.9% gain. Orders for April were revised slightly higher and are now shown to have fallen 0.8%, previously 1.3%. The details of May durable goods orders were on the softer side as the bulk of the gain was concentrated in the volatile transportation component. Excluding transportation, orders rose only 0.3%. The key core capital goods orders and shipments fell 0.1% and rose 0.6%, respectively. Durable goods inventories increased 0.7% for the second consecutive month. All told, it's just a single month but there are some signs that businesses investment is cooling after being on a hot streak.

Separately, trade could be a larger drag on second-quarter GDP than we had previously expected. The advance nominal goods deficit widened more than anticipated in May, coming in at $88.1 billion, compared with April's $85.7 billion. Nominal goods exports slipped 0.3%, with another sizable decline in automotive vehicles. Capital goods exports dropped 1.3% while industrial supplies were down 0.9%. Consumer goods exports jumped 5.6%. Separately, nominal goods imports were up 0.8%. The bulk of the gain in goods imports was in foods, feeds and beverages along with industrial supplies. Capital goods imports fell along with automotive vehicles.

Existing-home sales fell in May, but this is good news because the market was too hot. Existing-home sales declined by 0.9% to 5.8 million annualized units. Sales declined the most in the West, falling 4.1%. Moreover, sales declined 1.4% in the Northeast and 0.4% in the South. On the other hand, sales rose 1.6% in the Midwest.

The lack of inventory and declining affordability are likely weighing on existing-home sales. Though sales have fallen recently, they remain higher than that seen pre-pandemic and the demographic tailwind from more millennials entering their first-time homebuyer years will continue to support demand over the next couple of years. Separately, new-home sales also fell in May.

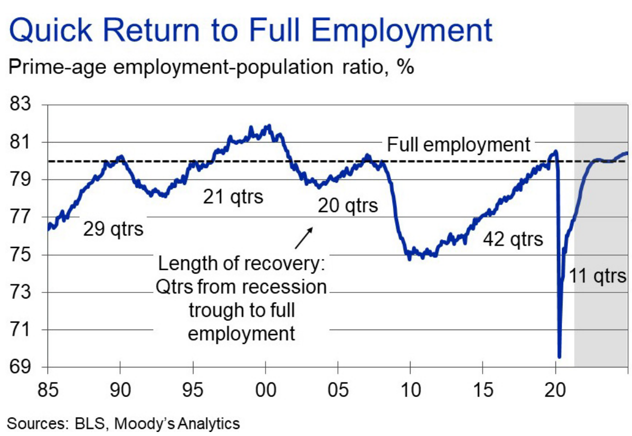
U.S. Economic Recovery Will Be Rapid

BY MARK ZANDI

The economic recovery from last spring's COVID-19-induced recession is in full swing. Real GDP growth is tracking above 10% annualized in the current quarter, and with this gain real GDP will fully recover what it lost in the downturn. If so, it will take six quarters for real GDP to better its fourth-quarter 2019 pre-pandemic peak.

This is substantially faster than the 14 quarters it took for GDP to recover from the financial crisis and Great Recession, although there have been faster recoveries, including the four quarters it took the economy to recover from the recession following the Y2K stock market crash and 9/11.

Nonetheless, it is a notable achievement for the economy to recover so quickly from the stunning more-than-10% decline in real GDP last spring. This is among the steepest declines in the nation's economic history. Moreover, if recovery is defined as the period after a recession until the economy has returned to full employment, then while this recovery will not be the speediest, it will likely outperform most other recoveries. Of course, we won't know this for another year or two, as we expect the economy to be back to full employment by no later than early 2023.



With the pandemic winding down and the recovery winding up, the Federal Reserve is preparing to further reduce the unprecedented support it has provided the economy since the pandemic hit. It began doing so at the end of last year with the wrap-up of its emergency liquidity support to the bond and short-term funding markets. That move hardly created a ripple in financial markets and credit remains ample and cheap.

The Fed's next move will be to provide a rough timeline as to when it will begin reducing its $120 billion in monthly purchases of Treasury and mortgage-backed securities. Federal Reserve Chairman Jay Powell's speech at the annual Jackson Hole conference of central bankers in August would seem to be a good time to announce this tapering of the Fed's quantitative easing program.

We expect Powell to say that tapering will begin at the start of 2022 under the proviso that the economy is well on its way to full employment. It should be. We expect the unemployment rate to be near 4.5% by then and clearly headed back to its 3.5% pre-pandemic low. Our forecast is similar to the median forecast of the members of the Federal Open Market Committee released last week at the end of their monetary policy meeting.

FOMC members also somewhat surprisingly signaled that they expect to begin raising the federal funds rate off the zero lower bound in 2023, and that they would raise the funds rate twice that year. We too expect the Fed to begin raising rates in early 2023, but that ultimately it increases them four times during the year. 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 be moving higher, and that's not something the Fed could shrug off. Of course, there is a lot of script to be written between now and then. We, like policymakers, expect the federal funds rate to eventually settle near 2.5%, but it will take until mid-decade to get there.

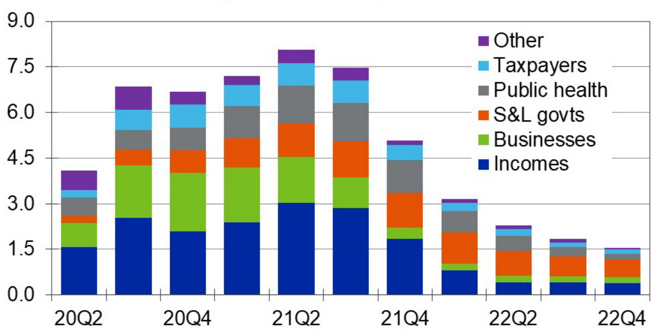
Fiscal policy is also set to become much less supportive to the economy. Unless the Biden administration makes a change in the next few days, the current moratorium on foreclosures and rental evictions will expire at the end of June. If so, many of the approximately 2 million homeowners who are receiving loan accommodations will begin the foreclosure process, and an estimated more than 4 million renters will face potential eviction. While this is well down from the peak in distress last year, when more than 4 million homeowners needed loan accommodations and more than 8 million renters couldn't make their rent payments on time, and delinquent renters and their landlords are just now benefiting from the distribution of $46.5 billion in federal renter assistance, there is bound to be some negative fallout.

The expiration of various emergency unemployment insurance benefits in early September, including the controversial $300 in weekly supplemental unemployment insurance that about half the states are winding down early, and the termination of the current moratorium on federal student loan payments at the end of September, will also sting; as will the expiration of various other smaller temporary tax credits and government support at the end of the year.

The economic benefit of the close to $5 trillion in federal government support provided since the pandemic struck, including the $1.7 trillion CARES Act passed last March and the $1.9 trillion American Rescue Plan this March, is also peaking. More than $4 trillion of the federal funds have already been disbursed, with the peak in outlays, equal to about 7.5% of GDP, occurring this quarter and next. By the fourth quarter of this year, outlays will fall to less than 5% of GDP and if lawmakers provide no additional support it will fall to 1.5% of GDP in 2022. Fiscal policy will swing from significantly shoring up economic growth to weighing on it by this time next year.

Fiscal Support Is Peaking

% of real GDP due to government support of...



Source: Moody's Analytics

This will happen despite our expectation that the Biden administration and Congress will come to terms on another fiscal package later this year through the budget reconciliation process that allows for legislative passage without Republican support. The package will include many of the policies proposed in Biden's American Jobs Plan, which includes mostly infrastructure spending, and American Family Plan, which includes spending on various social programs.

Biden's proposals cost some $4.5 trillion over the 10-year budget horizon, and Democratic lawmakers are now bandying about a $6 trillion price tag, but we anticipate something closer to $2.5 trillion when all is said and done. To pay for this, which will occur over a 15-year horizon, taxes on multinational corporations and well-to-do individuals will go up. While a sizable fiscal package, it is mostly about supporting long-term productivity and labor force growth, and not providing a near-term boost to the economy. Indeed, given the timing of the tax increases and when the infrastructure and other spending get into the economy, the package doesn't provide a meaningful economic boost until mid-decade.

Financial markets are just starting to adjust to the reality that monetary and fiscal policy will no longer be the same strong and reliable tailwind to growth and could soon become a headwind. The stock market sold off in the wake of last week's FOMC meeting, and the selling intensified as trading ended the week. The market seems especially sensitive to the Fed. It hit bottom late last March just as the Fed was slashing the federal funds rate to the zero lower bound. Since then, it has been more or less straight up for the stock market, as the value of all publicly traded stocks as measured by the Wilshire 5000 has almost doubled to nearly $44 trillion.

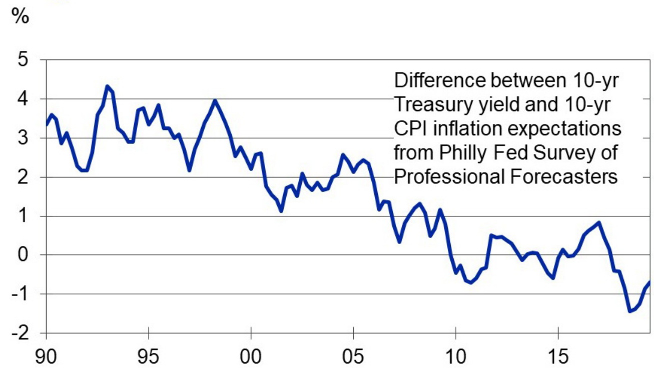
The market has become meaningfully overvalued—price-to-earnings multiples are outside of most historical bounds—and bordering on speculative. The explosive popularity of GameStop and other meme stocks, the Archegos Capital kerfuffle, and the proliferation of SPACs or so-called blank-check companies are symptomatic of the froth in the market. We expect the stock market to more or less trade sideways for the foreseeable future as it digests the shift in monetary and fiscal policy, but given the overvaluation/speculation, odds are uncomfortably high it will suffer a more severe correction. While it is difficult to construct scenarios in which a decline in stock prices, even a severe and sustained selloff, could undermine the current recovery, there are scenarios in which it would materially change the contours of the recovery.

Unlike stock investors, fixed-income investors appear nonplussed by the developing shift in monetary and fiscal policy. Ten-year Treasury yields rose with the Fed's hawkish FOMC meeting, but immediately fell back when stock investors sold and put the cash they raised into Treasuries. The 10-year Treasury yield is hovering near 1.5%, up about a percentage point from its pandemic low last summer, but about where it has been for the past three months.

The bond market also appears overvalued, as real Treasury yields—the difference between Treasury yields and inflation expectations—are firmly negative. It is hard to square this given the strongly held expectation that the economy will quickly return to full employment.

Possible explanations include strong foreign demand, although capital flows to the U.S. haven't been particularly strong, the Fed's quantitative easing program, and other technical factors related to the amount of Treasury bond issuance associated with the federal government's massive budget deficit. If so, then once Fed Chairman Powell makes clear the Fed's intentions regarding QE and the technical factors sort themselves out, Treasury yields are headed higher. We expect 10-year Treasury yields to approach 2% by the end of this year, 2.5% by year's end 2022, and to eventually settle near 3.5% by mid-decade. However, like the stock market, the bond market looks vulnerable to a significant correction, with yields rising much more and much more quickly.

Negative Real Rates?



Sources: Federal Reserve, Philly Fed, Moody's Analytics

This is all a bit mind-numbing, but the upshot is that with the economic recovery in full swing, monetary and fiscal policy can no longer be as accommodative, and stock, bond and other asset markets must recalibrate. We expect this adjustment to be largely graceful, but it wouldn't be too surprising if there were a stumble or two along the way, and there is a not-inconsequential risk that there could be an uncomfortably hard fall.

The Week Ahead in the Global Economy

U.S.

The U.S. economic calendar remains busy next week. Among the key data is the June employment report. Nonfarm employment rose 559,000 in May, and has risen by an average of 541,000 over the past three months. We will finalize our forecast for June employment after the ADP National Employment Report and ISM manufacturing survey are released. We will pay close attention to measures of labor supply to see if there has been any improvement. Odds are that a significant easing in will likely not occur until the end of this summer, when the new school year begins. Childcare issues are a significant weight on the supply of labor.

Aside from employment, the May trade deficit will be released along with the Conference Board's consumer confidence index, the June ISM manufacturing survey, and pending-home sales, which should provide further evidence that housing demand has softened.

Europe

Next week's European releases will give a glimpse of this summer's recovery. We are expecting consumer spending to begin its rebound in May, as France's household consumption of goods likely increased 3.5% month over month, after dropping by 8.3%, and German retail sales likely jumped 3.5%, after a 5.5% tumble. Lockdowns eased considerably halfway through the month, spurring a first wave of consumer spending. Larger gains, however, will come in June.

Easing lockdowns, meanwhile, will have allowed the unemployment rate to tick down in the euro zone this May to 7.9% from 8%. That said, employment gains will be mitigated by workers returning to the labor force after temporarily dropping out during the pandemic. As they won't be reabsorbed immediately, the unemployment rate will fall only gradually.

Business and consumer sentiment in the euro zone, as measured by the European Commission's Economic Sentiment Index, will rise to 115 in June from 114.5 in May. Reopening will charge sentiment among service providers and retailers. However, as we enter the post-lockdown period, future expectations will be moderated. Finally, we are expecting euro zone CPI inflation to have increased to 2.1% year over year in June. Base effects in the energy component have likely already peaked, but now that the economy is reopening, we should see some more recovery in the core basket of prices.

Asia-Pacific

China's manufacturing sentiment likely improved in June, after dipping in May. The official manufacturing PMI is forecast to hit 51.4 in June, from 51 in May, its lowest reading since February. Improved demand from major trading partners likely lifted orders in June, while elevated commodity prices kept upward pressure on input prices, which surged to 72.8 in May, up from April's 66.9 reading. Supply-chain disruptions are also adding to supplier delivery times, a situation not expected to ease until late in 2021.

Japan's Tankan survey for large manufacturers likely improved to 11 in the second stanza, from 5 in the first quarter. The prior reading was the first time the headline had been positive since the September quarter of 2019 and marked the third straight quarterly improvement. Improved global demand thanks to rising exports from the U.S. and China are contributing to the expected further improvement. Nonmanufacturing is improving at a slower pace, reflecting sluggish domestic demand, despite the pending Olympics.

Geopolitical Calendar

Date	Country	Event	Economic Importance	Financial Market Risk
16-Jul	Japan	BOJ Monetary Policy meeting	Medium	Medium
23-Jul to 8-Aug	Japan	Summer Olympics, Tokyo	Medium	Low
5-Sep	Hong Kong	Legislative Council elections	Low	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

Spreads Haven’t Budged

BY RYAN SWEET

CREDIT SPREADS

Moody's long-term average corporate bond yield is 94 basis points, down 1 basis point from this time last week. This is below its high over the past 12 months of 139 basis points among the lowest over the past year. This spread may be no wider than 115 bp by year-end 2021.

The long-term investment grade corporate bond yield is 130 basis points, 1 basis point wider than that seen last week. It remains well below its recent high of 222 basis points.

The recent composite high-yield option adjusted bond spread of 315 bp approximates what is suggested by the accompanying long-term Baa industrial company bond yield spread and is in line with the recent VIX of 15.7. The VIX has dropped over the past week and remains below its historical average of 19.

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.

April and May corporate bond issuance came in a little lighter than expected. U.S. dollar-denominated corporate bond issuance has moderated, not surprising as issuance typically is slow this time of year.

In the week ended Wednesday, weekly dollar-denominated investment-grade issuance rose $24.72 billion, bringing the year-to-date total to $875.6 billion. High-yield issuance rose $12.8 billion in the latest week, bringing the year-to-date total to $367.9 billion.

U.S. ECONOMIC OUTLOOK

The Moody's Analytics June baseline now looks for real GDP to rise 6.9% this year, compared with the 6.8% in our May baseline. We have been consistently revising our forecast higher for GDP this year because of changes to our fiscal policy assumptions, but the adjustment in June is modest compared with prior forecast revisions. The June baseline incorporates the government's second estimate of first-quarter GDP, but the top-line number was unrevised, still rising 6.4% at an annualized rate.

We raised our forecast for GDP growth in 2022 from 4.8% to 5%. Risks to the forecast are weighted to the upside because of the lack of inventory build this year. The global semiconductor shortage bit into inventories during the first quarter and will likely continue to do so through the remainder of this year. Inventories lend a downside risk to our forecast for GDP this year but are an upside for 2022 and 2023.

There is the potential that supply issues become a big problem, particularly for autos. Auto industrial production is trailing sales. Therefore, inventories could continue to decline. We didn't alter our forecast for the change in private inventories over the next few years, but this may need to be revisited, since lean inventories need to be replenished, and that could add more to GDP growth next year than we expect.

The June baseline forecast has average monthly job growth this year of 510,000, in line with the May baseline. Similarly, there were no significant revisions to average monthly job growth next year, which will be 327,000.

The unemployment rate is expected to average 4.5% in the fourth quarter of this year, the same as in the May baseline. A 3.5% unemployment rate and an 80% prime-age employment-to-population ratio are consistent with an economy at full employment. We don't have the prime-age employment-to-population ratio in our model but we do a back-of-the-envelope estimate based on the other labor market variables we forecast.

There weren't any changes to our assumptions about monetary policy. We still expect the Fed to announce its tapering plans in September and a $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.

The Fed will aim for inflation to exceed its 2% objective. How large of an overshoot is allowed before a rate liftoff will also be important in gauging the pace of tightening. If the Fed allows a larger overshoot, then the pace of tightening will likely be similar to a traditional tightening cycle, 25 basis points per quarter, because inflation should continue to accelerate even after the first rate hike. If the Fed doesn't allow too much of an overshoot, then the tightening cycle will be less aggressive. The first hike for the target range for the fed funds rate occurs in early 2023 and the pace of tightening is expected to be similar to historical norms.

There were no significant changes to the forecast for the 10-year U.S. Treasury yield. The forecast is for the 10-year Treasury yield to end this year just north of 2% and near 2.4% next year.

U.K. Trade Deals Heavy on Symbolism, Light on Impact

BY KATRINA PIRNER

The announcement of a new U.K. trade deal with Australia occurred with much fanfare, conveniently sidestepping its negligible impact on U.K. GDP. If the government is serious about promoting a 'Global Britain', then its loftier goals such as membership in the Comprehensive and Progressive Agreement for Trans-Pacific Partnership or a free trade deal with the U.S. are what truly matter.

Rollover agreements maintain status quo

The U.K.'s departure from the European Union limited its access to not only the single market but also markets in more than 70 countries with whom the EU had free trade deals. Undaunted, the conservative government has brandished the moniker of a 'Global Britain' that is open for business and keen to strike trade deals both near and far. It has set itself the ambitious target of securing free trade agreements with countries that cover 80% of U.K. trade by 2022.

In just over six months, the U.K. has signed more than 60 trade agreements. At first glance, the number and speediness of these agreements seems impressive. However, most of these deals were simply rollovers from previous agreements struck by the EU.

For example, the government was keen to promote its trade agreement with Japan as the first deal it had signed as an independent trading nation. The optics of this deal mattered as Japan is one of the largest economies in the world, though it accounted for just 2% of U.K. trade in 2019. Built on the EU-Japan Economic Partnership, the government emphasised that its deal went further, providing additional benefits to British businesses and consumers.

In truth, the bespoke nature of the deal was limited to particular clauses. Some notable advantages included an increase in quotas for U.K. malt producers as well as a data localisation clause which should benefit financial services. Also, the principle of nondiscriminatory treatment of digital products, which was absent from the EU's agreement with Japan, provides a leg up to e-commerce businesses. Lastly, rules of origin were liberalised so that U.K. manufacturers of goods such as textiles, biscuits and pet food could access preferential tariffs despite sourcing inputs or ingredients from other markets.

However, the U.K. couldn't secure its own independent quotas for certain agricultural goods that under the EU deal are exported with lower tariffs. Instead, the U.K. is allocated any leftover quotas that go unused by the EU.

Australian FTA doesn't live up to hype

The Australian free trade agreement is the first the U.K. has signed where the EU didn't have a deal already in place. While symbolic, the economic impact of the trade deal is negligible. Tariffs will be lifted on goods exports over a 15-year period, boosting U.K. GDP by 0.01% to 0.02%. Based on 2018 GDP, the increase to GDP would be equivalent to a maximum amount of £500 million. While British consumers should save around £34 million a year, this amounts to less than a pound per person each year.

From an industry point of view, the benefits are similarly underwhelming. For example, Australia is the eighth largest export market for Scotch whisky and distillers will benefit from the removal of 5% tariffs on whisky exports. However, in 2020 exports to Australia amounted to around £113 million, a small slice of the tipple's £3.8 billion export market. Car manufacturers could also benefit from tariff cuts, though the proximity of Japanese and South Korean manufacturers might be hard to compete against.

Much has been made about the impending onslaught of cheap beef into the U.K. market. In 2019 the U.K. imported around 1,766 tonnes of Australian beef and veal, equivalent to 0.6% of all beef and veal imports. Under the deal, quotas will limit the amount of Australian duty-free beef exported to the U.K. for 15 years, with a maximum amount of 170,000 tonnes permitted at year 10. Based on current levels, this would represent 54% of all beef imported by the U.K.

There are a couple of reasons the benefits for British consumers (and risk to farmers) may be less extreme than these eye-catching numbers suggest. According to the U.K.'s Agriculture and Horticulture Development Board, it's possible that increased demand from markets closer to home will eat up a growing share of Australian beef exports. Specifically, it cites the fact that Australian exporters garner higher prices for their beef products in countries like South Korea, Japan and the U.S. Also, Australian beef exports recently dipped because of drought conditions. Such conditions are expected to occur more regularly in the future and could restrict exports.

The U.K. has bigger fish to fry

The Australian free trade agreement is small potatoes, but it could act as a stepping-stone to more ambitious trade deals. The government has emphasised that its trade deals with Japan and Australia should support its application for membership in the Comprehensive and Progressive Agreement for Trans-Pacific Partnership, which it submitted on 1 February 2021.

Britain's trade with the 11 members of the CPTPP grew to £110 billion in 2019 and has expanded 8% a year since 2016. Admittedly, the U.K. already has agreements in place with eight members of the CPTPP and a free trade deal with New Zealand is expected to be signed later this year. This would dent some of the initial economic impact of the deal.

The CPTPP would provide the U.K. the opportunity to consolidate and build on existing trading relationships. For example, it would ensure equivalent treatment of domestic and foreign investors. Around £1 in every £12 of foreign investment in the U.K. comes from a CPTPP country and this could help attract additional capital. British manufacturers would also benefit from rules of origin that cover inputs from any CPTPP country. For those CPTPP countries with whom the U.K. simply rolled over pre-existing trade agreements with the EU, the CPTPP would improve upon areas such as digital services and data flows.

However, at the end of the day, the one trade deal that really matters is with the U.S. In 2019 the U.S. received more than 20% of U.K. exports, compared with 8% in Germany. This makes the U.S. the U.K.'s second largest trading partner after the EU and the U.K.'s largest single country trading partner.

Unfortunately, near-term prospects for a free trade deal between the U.K. and U.S. are dim. In October 2018, the Trump administration initiated free trade agreement negotiations with the U.K. and in 2020 the two countries engaged in five rounds of negotiations. However, a deal would need to be concluded by July 1 under the current Trade Promotion Authority, and President Biden put trade negotiations on the back burner while the pandemic raged. Even if the new negotiations began later this year, sticking points relating to agriculture, pharmaceuticals and financial services could end up scuttling a potential deal.

Given the trivial economic impact of the U.K.-Australia free trade agreement, we won't be updating our growth forecasts for the U.K. economy. Similarly, we aren't incorporating a U.S.-U.K. free trade agreement into our baseline forecasts. However, we do believe the prospect of U.K. membership in the CPTPP is good, which could lead us to upgrade our long-term growth forecasts for the British economy.

Green or Growth Focus for China?

BY CHRISTINA ZHU

China's steady economic recovery was holding up in May. Though the year-over-year growth of industrial production, retail sales, and fixed asset investment continued to ease because of the fading low base effect from the previous year, its two-year average growth was largely stable or improving. Domestic consumption continues to warm up while foreign demand remains robust, putting the production side of the economy under pressure amid increasing supply challenges. Input shortages, surging raw material and labor costs, and shipping disruptions are weighing on the country's manufacturers.

The global economic recovery, driven by a sustained expansion in China and strong rebound in major economies such as the U.S. and U.K. as they emerge from the pandemic fallout and reopen their economies, has been pushing global commodity prices to record highs. China, being a major importer and consumer of a range of industrial commodities, has seen its domestic raw material prices skyrocket.

The surge in energy, metal and chemical materials prices has sent China's purchase price index to a decade high, soaring by 12.5% in May on a year-ago basis, accelerating from 9% in April. On the other hand, China's producer price index, which captures the prices of goods when they are shipped out of factories, jumped by 9% year over year in May, the highest in 13 years. The widening gap between the purchase prices and PPI suggests that not all manufacturers were able to pass on all the input inflation to their customers.

The rising costs are hence cutting into the profit margin of downstream manufacturers, especially the small ones, causing them to delay investment and hiring plans. Some manufactures have even been running at a loss, prompting them to either stop taking in new orders or completely halt production. This makes the surging input prices an increasing concern that threatens to put a brake on China's economic recovery.

The government has been trying to tame the rally by warning against speculation and hoarding. It has also lowered the import duty on a range of raw materials, hoping to boost supply through import. Unfortunately, despite the tax cut, iron ore, coal, plastics, rubber and copper products all recorded significant declines in their import volumes in recent months, which is likely attributed to the rising global prices, skyrocketing freight rate, and shipping delays. The geopolitical tensions with the U.S. and Australia also make imports a less favourable or reliable option. As a result, these cooling measures have temporarily dampened the speculative sentiment in the financial market but didn't resolve the underlying gap between demand and supply.

The government is now looking at ways to boost domestic supply but worries about missing its environmental goals for the year. The state planner aims to reduce energy consumption per dollar GDP by 3% in 2021 to stay on track for the long-term goal of peaking carbon emission by 2030. That would require reductions in the usage of coal and steel production, which would further strain energy supply and production of industrial materials, adding pressure to producer inflation.

The Chinese authority has signalled that it will prioritize growth consolidation this year by toning down on environmental restrictions. The National Development and Reform Commission—the country's top economic planning agency—has limited the initial scope of a national carbon-trading system to around 2,200 firms in the electricity industry, in contrast to 6,000 firms across eight sectors in the original proposal. The government has also lifted restrictions on energy consumption and emissions for some steel producers, and announced the release of batches of metals, including copper, aluminum and zinc, from the state reserve to alleviate the shortages facing manufacturers.

RATINGS ROUND-UP

Improving Commodities Lift Upgrades

BY STEVEN SHIELDS

U.S. corporate credit quality continued to improve during the period ended June 21 with upgrades accounting for more than three-quarters of changes issued by Moody's. Upgrades also accounted for nearly all the affected debt while all rating activity was confined to speculative-grade firms.

The period's most notable upgrade was issued to DCP Midstream, LLC with its senior unsecured debt ratings and corporate family rating upgraded one notch to Ba1 from Ba2. According to the ratings action, the upgrade reflects continued improvement in DCP's credit metrics, improving oil and gas industry fundamentals that will support free cash flow generation and Moody's expectation that the company will further reduce debt.

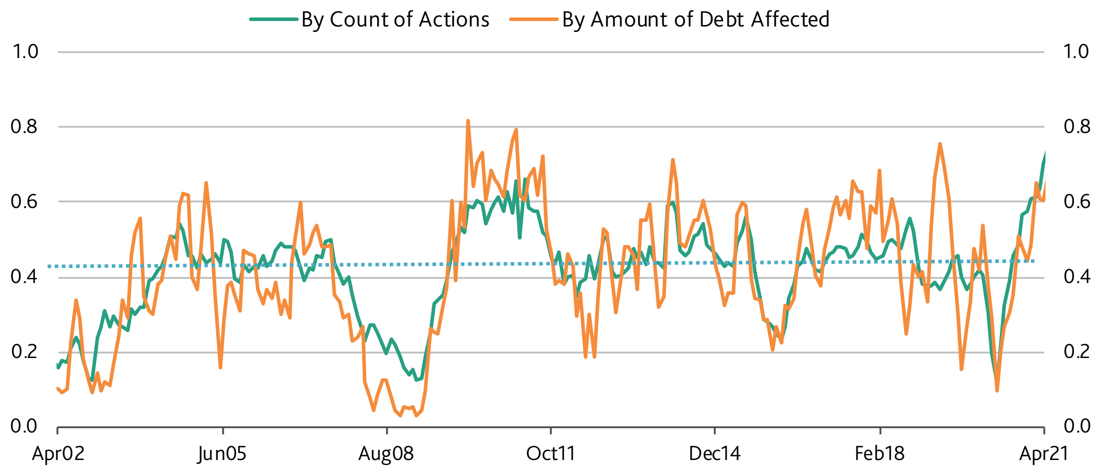
Moody's Investors Service also upgrade Big River Steel's CFR to B1 from B3 and its senior secured debt rating to Ba3 from B1 on June 17. The improved outlook for the U.S. Steel and its subsidiary, Big River Steel, reflects the company's large scale and strong market position as a leading U.S. flat-rolled steel producer, whose footprint is further enhanced by its diversification in Central Europe, as well as our expectation for moderate financial leverage and ample interest coverage in a normalized steel-price environment due to significant debt reduction in 2021.

WESCO Distribution, Inc.'s senior unsecured notes were lifted to B1 from B2 in the period. The new ratings align with Moody's expectations that WECO will continue to realize outlined synergies from the Anixter integration, which will improve operating margin and reduce debt leverage through debt repayment and EBITDA improvement.

Ratings activity was largely positive across Europe with upgrades accounting for half of the ratings issued and approximately 71% of the affected debt. Moody's upgraded Anglian Water (Osprey) Financing plc's senior secured ratings to Ba1 from B1, impacting $1.89 billion of outstanding debt. The rating action follows Anglian Water's announcement on June 17 of a new financing structure, with lower gearing intended to support "solid investment grade credit rating and ensure a sustainable and efficient capital structure in the interest of customers and investors, the environment, and long-term viability."

The largest downgrade in the region was issued to William Hill plc. The downgrade to its senior unsecured notes to B1 from Ba3 was prompted by the completion of Caesars Entertainment Inc.'s acquisition of William Hill on April 22 and the evolving expectations of the impact on William Hill's financial metrics as Caesars finalizes the separation and divestment of William Hill's non-U.S. businesses.

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	Old STD Rating	IG/ SG
6/16/21	OMERS BLUEJAY HOLDINGS, INC-PREMISE HEALTH HOLDING CORP	Industrial	SrSec/BCF/LTCFR/PDR		U	B2	B1		SG
6/17/21	DCP MIDSTREAM, LLC	Industrial	SrUnsec/LTCFR/JrSub/ PDR/PS	6,040	U	Ba2	Ba1		SG
6/17/21	UNITED STATES STEEL CORPORATION-BIG RIVER STEEL LLC	Industrial	SrSec/SrUnsec/LTCFR/ PDR	3,696	U	B1	Ba3		SG
6/17/21	WELLPATH HOLDINGS, INC.	Industrial	SrSec/BCF/LTCFR/PDR		U	B2	B1		SG
6/17/21	WOK HOLDINGS INC.	Industrial	SrSec/BCF/LTCFR/PDR		U	Caa2	Caa1		SG
6/18/21	PRIMARY CARE (ITC) INTERMEDIATE HOLDINGS, LLC AND-CANO HEALTH, LLC	Industrial	SrSec/BCF/LTCFR/PDR		U	B3	B2		SG
6/21/21	CALLON PETROLEUM COMPANY	Industrial	LTCFR/PDR		U	Caa1	B3		SG
6/21/21	WESCO INTERNATIONAL, INC.-WESCO DISTRIBUTION, INC.	Industrial	SrUnsec/LTCFR/PDR	3,175	U	B2	B1		SG
6/21/21	ARDENT HEALTH PARTNERS, LLC-AHP HEALTH PARTNERS, INC.	Industrial	SrUnsec/LTCFR/PDR	475	U	Caa2	Caa1		SG
6/21/21	ALCAMI CORPORATION	Industrial	SrSec/BCF/LTCFR/PDR		U	Caa1	B3		SG
6/21/21	ONE SKY FLIGHT, LLC	Industrial	SrSec/BCF/LTCFR/PDR		U	B3	B2		SG
6/21/21	BCPE ULYSSES INTERMEDIATE, INC.-LBM ACQUISITION, LLC	Industrial	SrSec/BCF		D	B2	B3		SG
6/22/21	EASTERN POWER, LLC	Industrial	SrSec/BCF		D	Ba3	B1		SG
6/22/21	GOPHER RESOURCE, LLC	Industrial	SrSec/BCF/LTCFR/PDR		D	B2	Caa1		SG

Source: Moody's

FIGURE 4

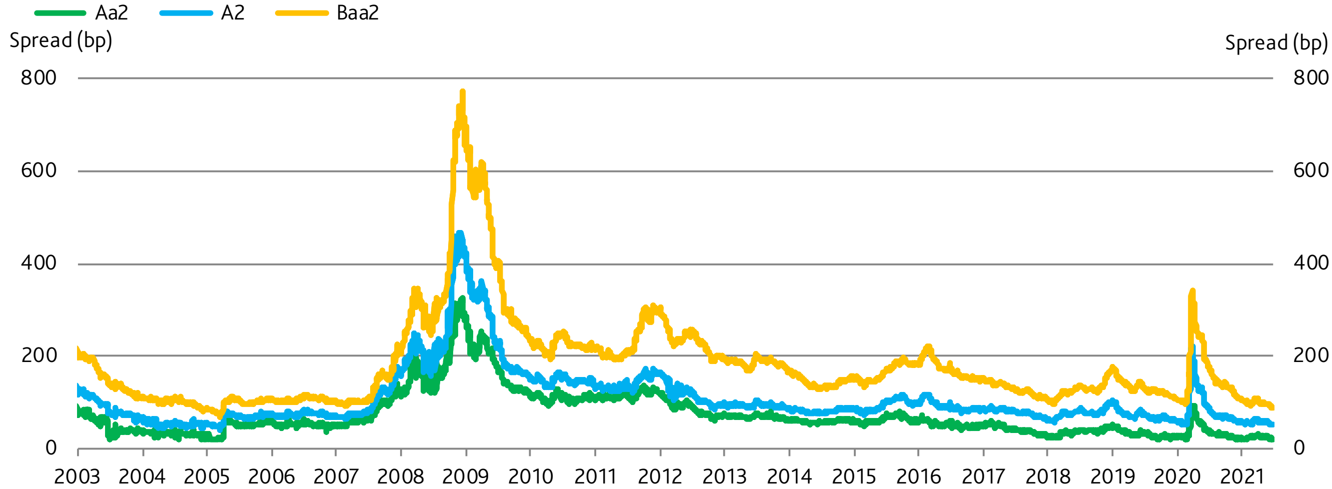
Rating Changes: Corporate & Financial Institutions - Europe

Date	Company	Sector	Rating	Amount ($ Million)	Up/ Down	Old LTD Rating	New LTD Rating	New LGD	IG/SG	Country
6/16/2021	ALBEA GROUP S.A.S.-ALBEA BEAUTY HOLDINGS S.A R.L.	Industrial	SrSec/BCF/LTCFR/PDR		D	B2	B3		SG	FRANCE
6/17/2021	WILLIAM HILL PLC	Industrial	SrUnsec/LTCFR/PDR	966.42	D	Ba3	B1		SG	UNITED KINGDOM
6/17/2021	OSPREY ACQUISITIONS LIMITED-ANGLIAN WATER (OSPREY) FINANCING PLC	Utility	SrSec/LTCFR/Sub	1,890.51	U	B1	Ba1		SG	UNITED KINGDOM
6/22/2021	SOVCOMFLOT PAO-SCF CAPITAL DESIGNATED ACTIVITY COMPANY	Industrial	SrUnsec	498.43	U	Ba2	Baa3		SG	IRELAND

Source: Moody's

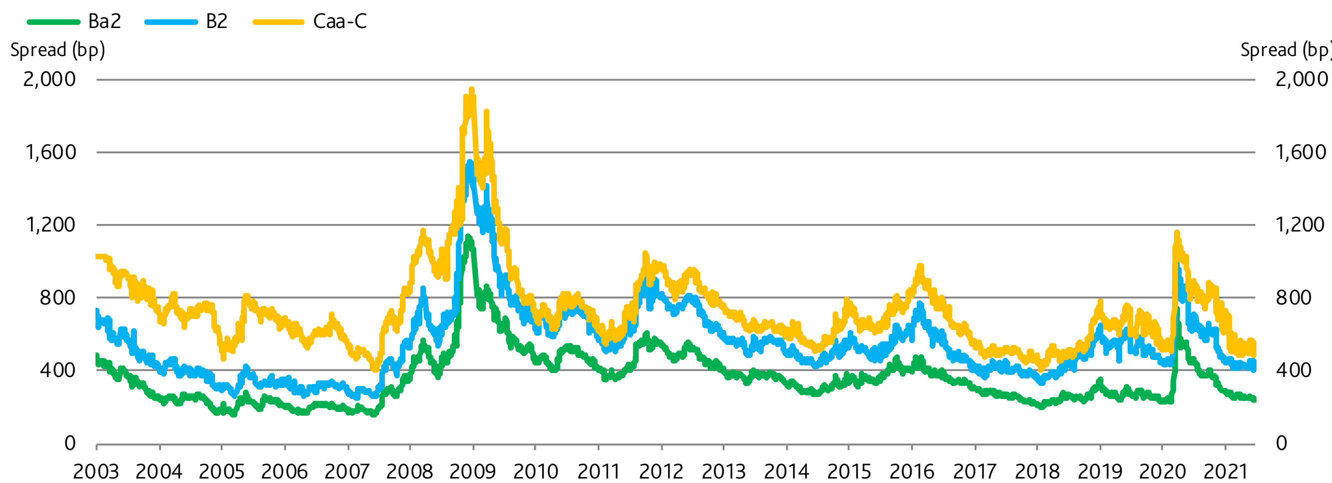
MARKET DATA

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 (June 16, 2021 – June 23, 2021)

CDS Implied Rating Rises	CDS Implied Ratings		
Issuer	Jun. 23	Jun. 16	Senior Ratings
Walmart Inc.	Aa3	A1	Aa2
FedEx Corporation	A3	Baa1	Baa2
Williams Companies, Inc. (The)	Baa2	Baa3	Baa2
Lockheed Martin Corporation	Aa3	A1	A3
Cargill, Incorporated	A3	Baa1	A2
Abbott Laboratories	A3	Baa1	A2
Kroger Co. (The)	Baa1	Baa2	Baa1
ONEOK, Inc.	Baa3	Ba1	Baa3
Archer-Daniels-Midland Company	A2	A3	A2
CenterPoint Energy, Inc.	Baa1	Baa2	Baa2

CDS Implied Rating Declines	CDS Implied Ratings		
Issuer	Jun. 23	Jun. 16	Senior Ratings
Citigroup Inc.	Baa2	Baa1	A3
Bank of America Corporation	Baa1	A3	A2
AT&T Inc.	Baa3	Baa2	Baa2
Comcast Corporation	Baa1	A3	A3
Oracle Corporation	A2	A1	Baa2
John Deere Capital Corporation	A3	A2	A2
Citibank, N.A.	Baa3	Baa2	Aa3
General Motors Company	Ba1	Baa3	Baa3
Philip Morris International Inc.	A2	A1	A2
United Airlines, Inc.	Caa1	B3	Ba3

CDS Spread Increases		CDS Spreads		
Issuer	Senior Ratings	Jun. 23	Jun. 16	Spread Diff
Staples, Inc.	Caa1	834	792	42
Nabors Industries, Inc.	Caa2	676	651	25
Avis Budget Car Rental, LLC	B3	263	242	22
United Airlines, Inc.	Ba3	363	347	16
K. Hovnanian Enterprises, Inc.	Caa3	664	650	14
RPM International Inc.	Baa3	74	61	13
Embarq Corporation	Ba2	312	299	13
Lumen Technologies, Inc.	B2	297	285	12
Carnival Corporation	B2	332	321	12
CSC Holdings, LLC	B3	256	246	11

CDS Spread Decreases		CDS Spreads		
Issuer	Senior Ratings	Jun. 23	Jun. 16	Spread Diff
Talen Energy Supply, LLC	B3	1,447	1,678	-231
L Brands, Inc.	Ba3	136	159	-23
Nordstrom, Inc.	Baa3	221	236	-15
The Terminix Company, LLC	B1	208	221	-14
Macy's Retail Holdings, LLC	B1	315	328	-13
Corning Incorporated	Baa1	75	88	-12
American Airlines Group Inc.	Caa1	590	601	-12
Marathon Oil Corporation	Baa3	117	128	-11
Kohl's Corporation	Baa2	132	144	-11
Dillard's, Inc.	Baa3	119	130	-11

Source: Moody's, CMA

CDS Movers

Figure 4. CDS Movers - Europe (June 16, 2021 – June 23, 2021)

CDS Implied Rating Rises	CDS Implied Ratings		
Issuer	Jun. 23	Jun. 16	Senior Ratings
UniCredit Bank AG	Aa2	Aa3	A2
Banco Comercial Portugues, S.A.	Ba2	Ba3	Ba1
Banca Monte dei Paschi di Siena S.p.A.	Ba3	B1	Caa1
Vattenfall AB	Aa3	A1	A3
Deutsche Post AG	Aa2	Aa3	A3
United Utilities PLC	A1	A2	Baa1
Rolls-Royce plc	Ba3	B1	Ba3
VERBUND AG	Aa3	A1	A3
Deutsche Lufthansa Aktiengesellschaft	Ba3	B1	Ba2
Iceland, Government of	Baa1	Baa2	A2

CDS Implied Rating Declines	CDS Implied Ratings		
Issuer	Jun. 23	Jun. 16	Senior Ratings
Safeway Limited	Baa2	A3	Baa2
Rabobank	Aa3	Aa2	Aa3
Banco Bilbao Vizcaya Argentaria, S.A.	A2	A1	A3
ENEL S.p.A.	Baa2	Baa1	Baa1
Sanofi	Aa3	Aa2	A1
British Telecommunications Plc	Baa3	Baa2	Baa2
AstraZeneca PLC	A1	Aa3	A3
Anglo American plc	Ba1	Baa3	Baa2
Vivendi SE	Baa3	Baa2	Baa2
Santander Financial Services plc	Baa2	Baa1	A1

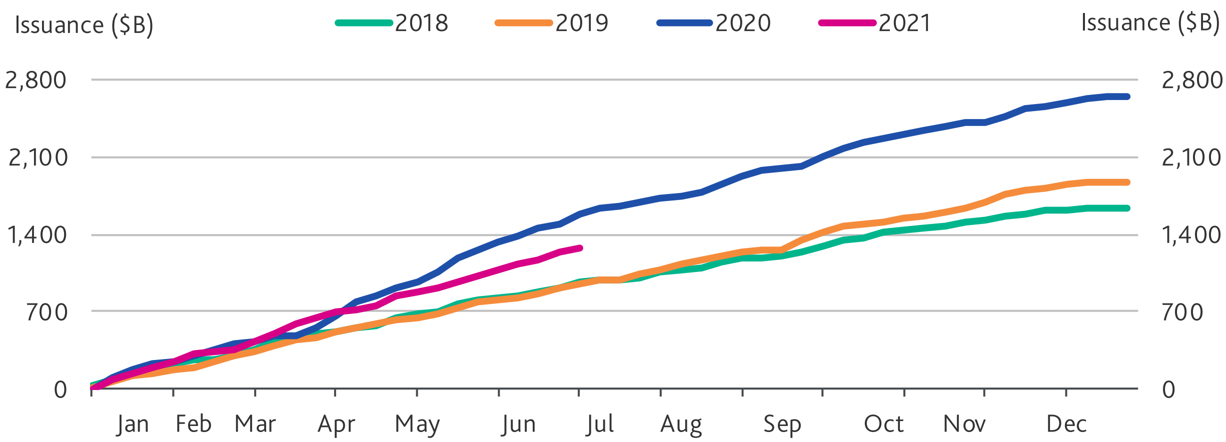
CDS Spread Increases		CDS Spreads		
Issuer	Senior Ratings	Jun. 23	Jun. 16	Spread Diff
Vedanta Resources Limited	Caa1	853	769	84
Wm Morrison Supermarkets plc	Baa2	148	109	39
thyssenkrupp AG	B1	290	274	16
Safeway Limited	Baa2	58	43	15
CECONOMY AG	Ba1	151	137	13
METRO Finance B.V.	Ba1	77	67	10
CMA CGM S.A.	B3	321	314	8
Iceland Bondco plc	Caa2	416	409	7
Telecom Italia S.p.A.	Ba2	154	148	6
British Telecommunications Plc	Baa2	71	65	6

CDS Spread Decreases		CDS Spreads		
Issuer	Senior Ratings	Jun. 23	Jun. 16	Spread Diff
Boparan Finance plc	Caa1	786	832	-46
TUI AG	Caa1	600	614	-14
Casino Guichard-Perrachon SA	Caa1	490	500	-10
Vue International Bidco plc	Ca	579	589	-10
Deutsche Lufthansa Aktiengesellschaft	Ba2	226	234	-8
Banca Monte dei Paschi di Siena S.p.A.	Caa1	229	234	-5
Piraeus Financial Holdings S.A.	Caa3	499	504	-5
Sappi Papier Holding GmbH	Ba2	349	354	-5
Rolls-Royce plc	Ba3	222	227	-4
Hammerson Plc	Baa3	195	199	-4

Source: Moody's, CMA

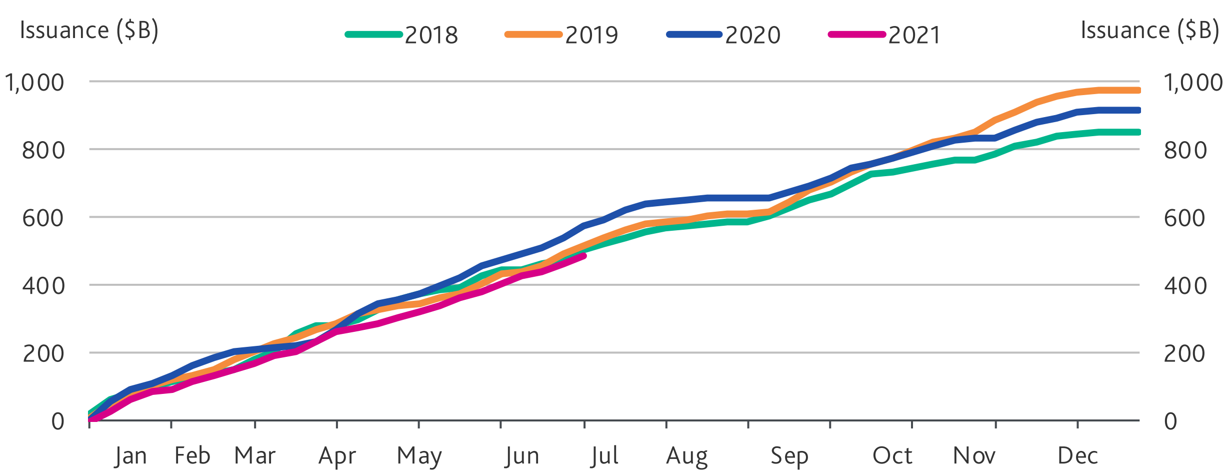
ISSUANCE

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

Figure 7. Issuance: Corporate & Financial Institutions

	USD Denominated		
	Investment-Grade	High-Yield	Total*
	Amount $B	Amount $B	Amount $B
Weekly	24.720	12.800	38.188
Year-to-Date	875.613	367.943	1,274.267

	Euro Denominated		
	Investment-Grade	High-Yield	Total*
	Amount $B	Amount $B	Amount $B
Weekly	17.734	5.663	23.433
Year-to-Date	389.517	85.395	487.514

* Difference represents issuance with pending ratings.

Source: Moody's/ Dealogic

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