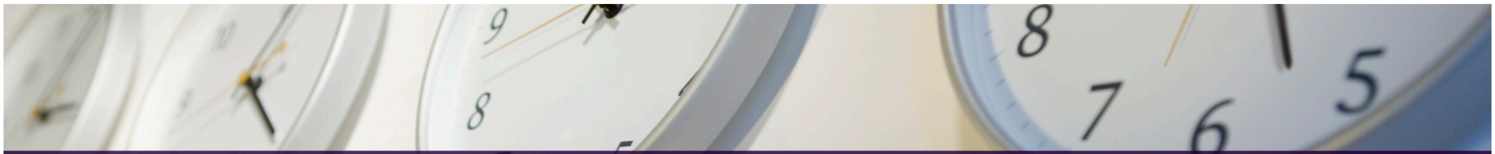

Credit Outlook

2 September 2021

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Hurricane Ida will temporarily boost oil and gas companies' margins, but have no lasting effect on refiners

Originally published on 31 August 2021

On 29 August, Hurricane Ida struck Louisiana south of New Orleans. Hurricane Ida's shutdown of US refining capacity will increase refiners' profit margins temporarily and reduce inventory levels for US refined products, but we expect a limited effect overall for the large diversified refiners from the storm's damage along Louisiana's Gulf Coast. Gulf Coast facilities were still assessing the conditions of their facilities the day after the storm. We expect only limited property damage to most refining facilities, not requiring extended downtime for rebuilding or repairing plant assets, some of which were hit by storms just last year.

However, severe storm damage to the surrounding areas will cause outages at various midstream logistics assets and utilities. The storm's dislocation of the local workforce also risks significantly disrupting refining operations and delaying their return to normal operations.

Hurricane Ida hit the US Gulf Coast south of New Orleans as a Category 4 storm, featuring 150 mile-per-hour sustained winds, heavy rain and a storm surge—and east of where the Category 4 Hurricane Laura struck in August 2020, and Category 2 Hurricane Delta in October. As in those storms, wind damage and flooding from Hurricane Ida will significantly disrupt the local oil and gas industry, though the exact scope of the damage and facility downtime remains unclear. Much of southeastern Louisiana was without power a day after the storm. Ida did not significantly affect refineries in the Port Arthur, Texas area. US Gulf Coast refineries represent about half of US refining capacity, and much of its petrochemical capacity.

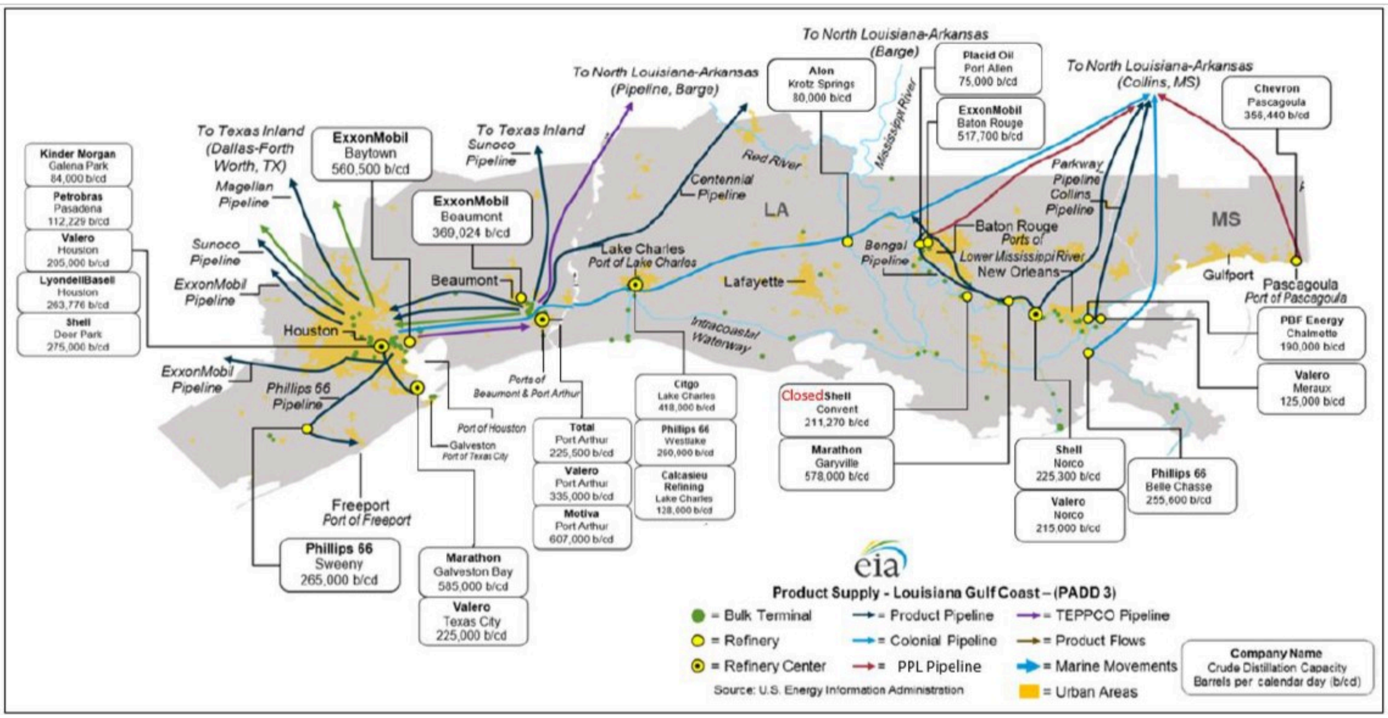
As a precautionary measure before Hurricane Ida struck, refiners shut in about 2.3 million barrels per day of capacity, or 13% of US capacity, and many facilities in Louisiana shut down as the local population evacuated. Oil and gas producers also shut in an estimated 96% of oil production and 94% of natural gas production in the US Gulf of Mexico offshore area, according to the US Bureau of Safety and Environmental Enforcement, while ports closed and operators curtailed certain midstream services. Colonial Pipeline (A3 stable), a major shipper of refined products from the US Gulf Coast to East Coast markets, shut down the Houston-to-North Carolina portion of its network before the storm.

The refining shut-ins will increase utilization rates for the facilities still operating, giving their margins a temporary boost. Refining utilization rates were above 90% in August 2021 for both the US and PADD 3—the Gulf Coast region—compared to above 95% for both August 2018 and 2019, before the coronavirus pandemic. At such utilization rates, the PADD 3 region has less excess capacity today than before Hurricane Laura in August 2020, when utilization was about 82%.

The duration of the improvement in margins depends on how quickly operations return to normal. With PADD 3 inventories of gasoline, distillate fuel oil and crude oil close to their five-year averages today, we do not expect near-term shortages or large ongoing increases in refined product prices. The disruption from Hurricane Ida will reduce inventory levels, and a drawdown will temporarily support higher industry margins, especially if certain regions experience some supply shortages from disruptions to midstream logistics. Crack spreads rose before the hurricane, and New York harbor gasoline, diesel and fuel oil spot prices were up over 5% the day after the weekend storm.

Hurricane Ida's impact on particular refining companies will be limited, since most operate in multiple regions, with few facilities in the area that the storm actually hit. Refiners generally will have adequate liquidity to weather the disruptions to their operations. Large refiners such as Phillips 66 (A3 negative), Marathon Petroleum (Baa2 stable) and Valero Energy (Baa2 negative) have refineries in the area, but the loss of volumes accounts for only a minority of their overall capacity (see Exhibit 1).

Petroleum supply chain includes numerous refining facilities along the Louisiana Gulf Coast



Source: US Department of Energy

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Hurricane Ida unlikely to hurt chemical companies' credit quality, but will boost certain commodity prices

Originally published on 31 August 2021

On 29 August, Hurricane Ida, a dangerous Category 4 storm, hit the Louisiana Gulf Coast, but is not likely to have a credit-negative effect on the US chemical industry. The storm made landfall southwest of New Orleans in an area critical to the US petrochemical industry before heading inland passing east of Baton Rouge. Areas to the east of the storm typically sustain more weather related damage. Since the storm struck on the eastern edge of the Gulf Coast petrochemical production zone, we expect some effect on commodity prices depending on the length of power outages. Facilities' operating rates and inventories continue to recover from a series of disruptive events, including the global outbreak of COVID-19, the impact of Hurricane Laura in August 2020, and the impact of winter storm Uri in February 2021. If the frequency of hurricanes increases, we would begin to incorporate expectations for outages into our forecasts rather than treat them as extraordinary events.

Good liquidity and healthy cash balances and relatively high commodity prices across the sector will limit impact on producers' credit quality—and by extension, ratings and outlooks. A few producers had large facilities directly in the path of the storm. But Cornerstone Chemical (CSTN Merger Sub, Inc., B3 negative), the largest US producer of acrylonitrile. had its sole facility near the center of the storm. Dow Chemical (Baa2 stable) had two crackers in Louisiana close to the path of Ida, one in Plaquemine and one in St. Charles. Both Exxon (Baton Rouge) and Shell (Norco) have refineries and petrochemical plants in the path of the storm as well. Chemours' (Ba3 negative) largest facility is in Delisle, Mississippi, 25 miles from the Louisiana border, which may also incur a longer outage due to the lack of power or logistics.

Some commodity markets remain very tight today. We expect that hurricane-related disruptions will drive up spot prices for those that already had tight supply/demand balances before the storm, including key resins such as polyethylene (PE), polypropylene (PP) and polyvinyl chloride (PVC). If some assets remain idle or come back online slowly, other PE, PP and PVC producers will benefit from a disruption-driven increase in commodity prices, just as Hurricane Harvey benefiting Louisiana-based chlor-alkali producers when it disrupted production in Texas in 2017. We expect any further increase in prices to be relatively short-lived, based on the small number of facilities whose operations are at risk of disruption. We still expect these plastic prices to decline in the fourth quarter, unless there is another hurricane that take out more capacity either in Texas or further west in Louisiana. The impact on acrylonitrile may last longer if Cornerstone doesn't get its power back in the next two weeks. We predicted similar temporary price spikes right after Hurricane Laura landed in western Louisiana in August 2020, a time of COVID-related chemical facility idlings. Hurricane Harvey inflicted widespread damage across a larger swath of the petrochemical heartland when it landed closer to Houston in 2017.

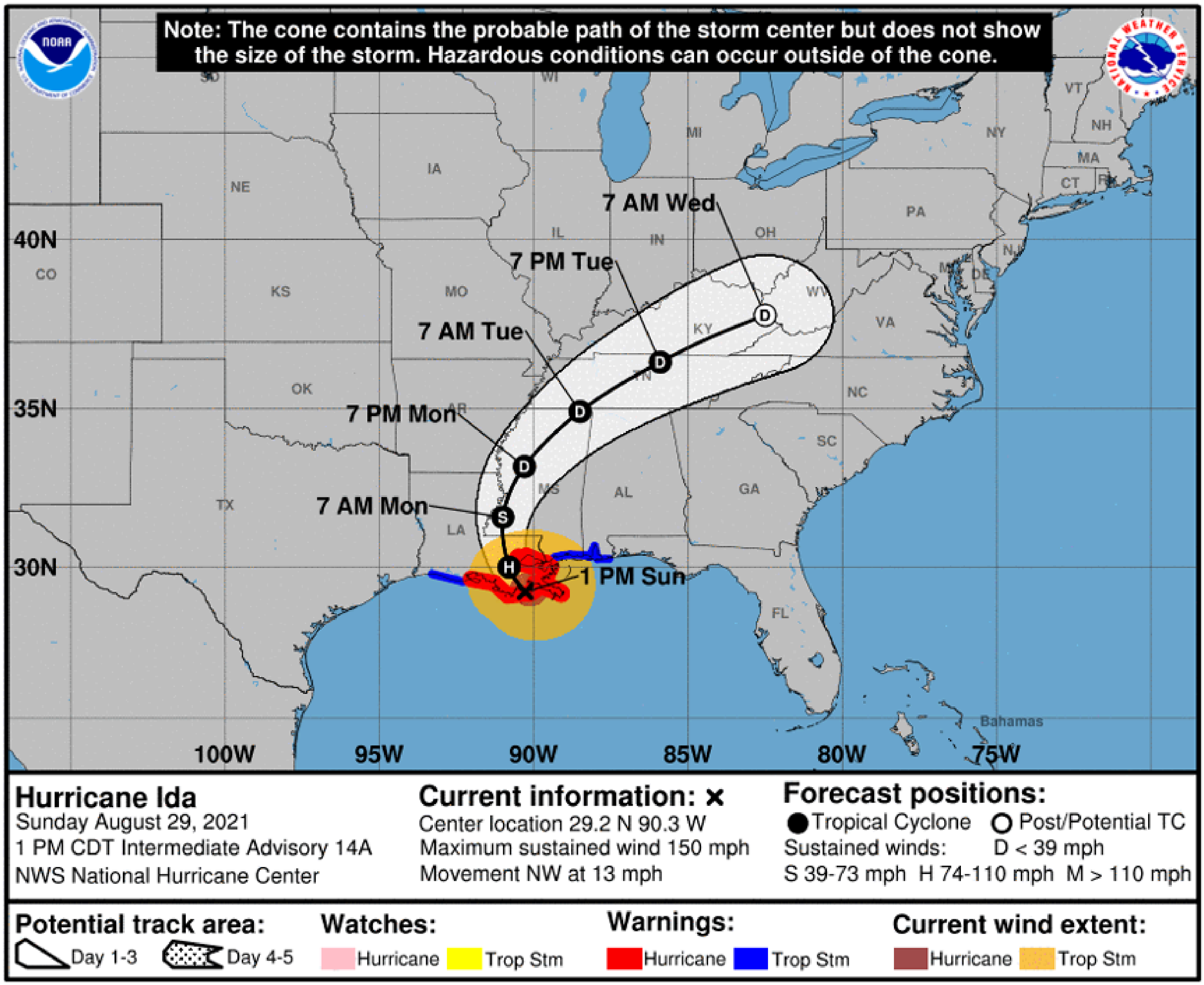
Other chemical producers who idled facilities prior to the arrival of Hurricane Ida, including BASF (A3 stable) and NOVA Chemicals (Ba2 stable), which were west of the storm, should be back on-line quickly like Nutrien. By contrast, Cornerstone operates a single complex along the Mississippi River west of New Orleans that produces acrylonitrile, melamine, and sulfuric acid. Cornerstone has had a number of outages over the past decade with operational issues at its own units, on-site customer units, and power outages. While the facility sits high enough above the river to avoid damage from most weather events, indirect risks such as logistics and access to power even more significant.

Major storms pose an increasing risk for companies whose chemicals production is concentrated along the US Gulf Coast. Climate change has increased the yearly number of weather events on the Gulf Coast. So far we have not experienced two consecutive years where hurricanes have significantly curtailed production. If companies experience more frequent outages, it would increase their credit risk, especially smaller companies, but generally improve margins for the rest of the industry as the supply/demand balance tightens.

Hurricanes on the US Gulf Coast highlight both chemicals producers' exposure to ESG risks and their ability to mitigate these risks. For these companies, hurricanes and tropical storms primarily threaten not property damage but disruptions to logistics, power outages, and flooding that can delay the restart of production for several weeks and even longer.

The petrochemical industry has acted in recent decades to mitigate direct damage from these storms, especially from high winds, but their ability to limit significant disruption-related damages from hurricanes has become an increasingly critical aspect of their credit quality. We capture these risks in the Physical Climate Risk category of our environmental risk classification, and consider commodity chemicals as a high-risk industry in our industry-level heat map. The potential for spills and other post-storm problems fall within the Waste & Pollution category of our environmental risk classification, and the Responsible Production category of our social risk classification. A number of chemicals facilities have recorded discharges during past Gulf Coast hurricanes, including Laura in 2020 and Harvey in 2017.

Hurricane Ida's storm track



Source: National Hurricane Center, National Oceanic and Atmospheric Administration

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Hurricane Ida is credit negative for Entergy, but liquidity and cost recovery support credit quality

Originally published on 30 August 2021

On 29 August, Hurricane Ida made landfall on the Louisana Gulf Coast as a Category 4 storm, severely impacting the service territory of Entergy Louisiana LLC (ELL, Baa1 stable) and Entergy New Orleans, LLC. (ENOL, Ba1 stable), utility subsidiaries of Entergy Corporation (Entergy, Baa2 stable). The hurricane's heavy rain, storm surge and high winds have caused substantial physical damage and widespread power outages in the area. The damages and outages are credit negative for Entergy because of infrastructure repair costs and revenue losses from service outages.

As of Monday, approximately 720,000 ELL and 178,000 ENOL customers were without power, amounting to outages at about one third of Entergy's total electric customers. The storm took out all eight transmission lines that deliver power into Orleans Parish, ENOL's entire service territory, causing the whole city to lose power on Sunday night. In addition, one of the levees failed near neighboring Jefferson Parish, served by ELL, sending over 7.5 feet of floodwaters into the area and knocking out power in several parts of the Parish. Entergy has reported catastrophic damage to its transmission system, citing that it could take several weeks to restore power in some areas. This will heighten the company's social risk related to customer relations and health and safety as power remains out.

In the near term, Entergy faces the possibility of substantial costs related to infrastructure damage, as well as revenue losses stemming from extended service outages. Because of the extensive transmission damage, these costs may be higher than previous storms. For reference, Hurricanes Katrina and Rita that hit the same area in 2005 cost the company over $1.3 billion in restoration of damaged infrastructure. However, we expect Entergy's business fundamentals to remain intact as it recovers from the storm, given the strong precedent for storm cost recovery in Louisiana and New Orleans.

The Louisiana Public Service Commission (LPSC) has a robust track record of allowing utilities to securitize and recover storm costs, including over $2.2 billion for ELL, alone, since 2005. The City Council of New Orleans' (CCNO) regulatory responses have also been helpful in the recovery of major storm costs, such as allowing ENOL to collect revenue for a storm reserve fund and providing for the securitization of storm costs through a discrete charge to customers. We expect Entergy to work closely with regulators and other stakeholders to ensure adequate recovery of Hurricane Ida costs through avenues mentioned previously such as storm reserves, securitization and through customer rates.

In addition, Entergy has access to considerable financial resources with strong capital market access and an adequate liquidity profile (Exhibit 1). These resources should help sustain the company's ability to manage anticipated storm costs. Entergy has access to a $3.5 billion revolving credit facility, expiring in June 2026. As of 30 June 2021, Entergy had about $2.5 billion of available revolver capacity, with $150 million of borrowings under the facility, $6 million in letters of credit and $866 million of commercial paper outstanding. The Entergy credit facility does not contain a material adverse change clause for new borrowings. The company had approximately $687 million of cash on hand at 30 June 2021.

Exhibit 1
Entergy has over $3 billion in liquidity resources available
$ millions

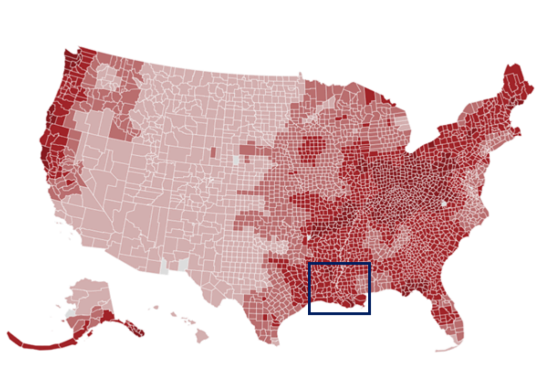
	Entergy Corp	ELL	ENOL
Credit facility total capacity	3,500	350	25
Credit facility capacity available	2,478	350	25
Money pool borrowing limit	N/A	450	150
Money pool borrowing available	N/A	334	73
Cash on hand	687	207	26
Total liquidity resources	**3,165**	**891**	**124**

Data as of 30 June 2021.
Source: Entergy SEC Filings

Entergy's credit metrics have been weak throughout this year and will continue to be challenged by the recovery of previous storm damage costs, which will likely be exacerbated by the most recent hurricane. In 2020, the company incurred roughly $2.4 billion of storm-related costs, leading to a cash flow from operations before working capital (CFO pre-WC) to debt metric around 10% as of the last 12 months that ended 30 June 2021. Although Hurricane Ida damage estimates are yet to be determined, these costs will put additional strain on Entergy's credit metrics in the near term, which have already limited the company's headroom vis-à-vis our expectation that CFO pre-WC to debt will remain above 14% on a sustained basis by 2023. Assuming total storm costs similar to Hurricanes Katrina and Rita of over $1 billion are initially funded mainly with debt, Entergy's credit metrics would be cut about in half at the end of this year.

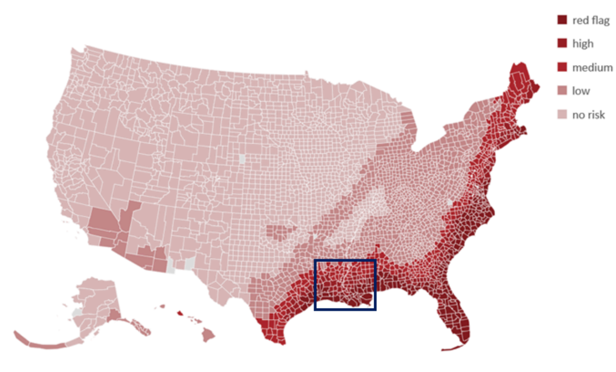
The latest hurricane underscores Entergy's exposure to climate change because of its location and the increasing frequency and magnitude of natural disasters such as flooding and hurricane intensity (Exhibits 2 and 3). Storm costs are continuing to rise, a risk that will persist for Entergy, with ongoing exposure to extreme weather events.

Exhibit 2
Relative projected extreme rainfall and flood stress



This metric is a combination of three projected components (wet days, very wet days, rainfall intensity) with annual changes from 2030-40 vs. 1975-2005 + two historical components (flood frequency and flood severity, on return inundation basis).
Source: 427 (data sourced from CMIP5 models and Fathom)

Exhibit 3
Hurricane risk (historical data)



The indicator reflects the cumulative wind velocity from recorded cyclones over the period 1980-2016.
Source: 427 (data sourced from IBTrACS version 3)

Entergy Corporation is a multistate vertically integrated holding company with five utility subsidiaries and a power generation portfolio, headquartered in New Orleans. The company serves over 3 million utility customers in Arkansas, Louisiana, Mississippi, and Texas. The regulated segment also includes System Energy Resources, Inc. (SERI, first mortgage bonds Baa1 negative), a 1,400-megawatt nuclear unit in Mississippi; together these subsidiaries comprise nearly all operating cash flow and net property plant and equipment. Its largest subsidiary, Entergy Louisiana, is expected to provide nearly 40% of operating company EBITDA in 2021.

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Synaptics' acquisition of DSP Group will enhance internet of things offerings, but increase leverage

Originally published on 31 August 2021

On 30 August, Synaptics, Inc. (Baa2 stable) announced its acquisition of DSP Group, Inc. (DSPG), a credit negative because we expect it to increase financial leverage. Synaptics is offering $22 per share in cash to acquire DSPG for about $580 million in purchase price ($450 million net of DPSG's existing $130 million cash balance). Synaptics said that the acquisition is contingent solely upon approval of DSPG's shareholders and customary closing conditions, with no required regulatory approvals. Closing is expected in late 2021.

Although Synaptics has not stated the exact mix of balance sheet cash and new debt funding for the acquisition, the potential for a large increase in financial leverage is credit negative. Should Synaptics fund the entire purchase price, net of the acquired cash, with $450 million of new debt, we estimate that it would increase financial leverage to over 3x debt to EBITDA (includes DSPG through 30 June 2021, excluding $30 million of anticipated 12 month synergies on a Moody's-adjusted basis) from about 1.6x debt to EBITDA (12 months ended 26 June 2021 on a Moody's-adjusted basis).

Although financial leverage will likely be higher because of the increased debt and DSG's weaker EBITDA margin profile, both companies are cash generative, with Synaptics significantly so. With the added debt, we expect that free cash flow (FCF) to debt will decline to potentially the lower 30% level should Synaptics fund the full net purchase price with new debt, from 70% as of the 12 months that ended 26 June 2021, on a Moody's-adjusted basis . But this would still represent a strong level of FCF. Coupled with management's historically conservative financial policy of prioritizing debt reduction, we anticipate that Synaptics will reduce leverage quickly following closing of the acquisition.

The DSPG acquisition will expand Synaptics' portfolio of internet of things (IoT) products with complementary products. DSPG's portfolio includes ultra low energy (ULE) products. These chipsets using the ULE wireless standard complement Synaptics' WiFi, bluetooth, and GPS/GNSS product portfolio, extending Synaptics' IoT offering into various in-home communications applications. Also, DSPG's voice over internet protocol technology should enhance Synaptics' video conferencing platform. Moreover, Synaptics reports that there is significant overlap in the customer base, providing a strong basis for cross selling, which should boost revenue growth of the combined company.

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Record household indebtedness is credit negative for Brazil's banks

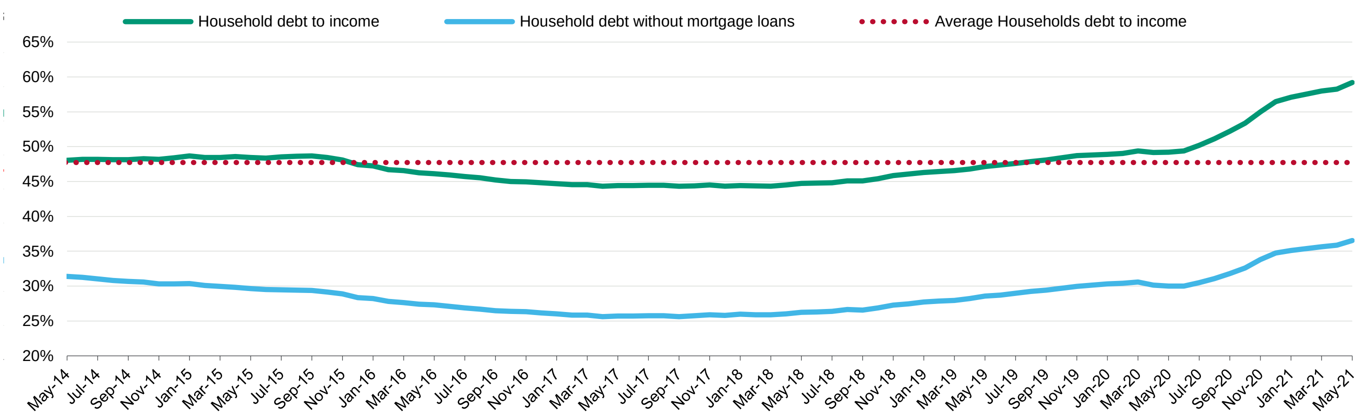
Originally published on 01 September 2021

On 27 August, Brazil's central bank released monthly data showing that households' debt to income ratios had increased to record levels between 2020 and year-to-date in 2021. Because this ratio is a leading indicator for banks' future asset quality, the upward trend is credit negative for Brazilian banks.

Household debt has risen since May 2020 reaching 59.2% as of June 2021, 115 basis points above the average between 2014-21 (see Exhibit 1). However, even with the strong growth in household debt, the portion of monthly salaries dedicated to paying down debt has grown more slowly, which is explained by the lower rates since 2019 that favored repayment capacity. Nonetheless, this conditions may not be sustainable as inflation pressures continues to support a tightening interest rate cycle started in March 2021, from the historic 2% low policy rates to 5.25% reached in August 2021.

Exhibit 1

Asset quality are arising from increasing household debt to income sustained over the past 12 months in Brazil



The household debt/income ratio is the percentage ratio between the balance of debts of families and accumulated income in 12 months, by the wage bill
Source: Central Bank of Brazil

This asset quality risk is more likely to affect Brazil's largest banks, including Banco do Brasil S.A. (Ba2/(P)Ba2 stable, ba2[1]), Banco Bradesco S.A. (Ba2/(P)Ba2 stable, ba2), Itau Unibanco S.A. (Ba2/(P)Ba2 stable, ba2), Banco Santander (Brasil) S.A. (Ba1/(P)Ba1 stable, ba2) and Caixa Economica Federal (Ba2/(P)Ba2 stable, ba3), that together accounted for around 70% of total consumer lending in Brazil as of March 2021. Because they increased their consumer lending exposures by 9.6% over the past six months, these banks are particularly susceptible to rising consumer asset risk.

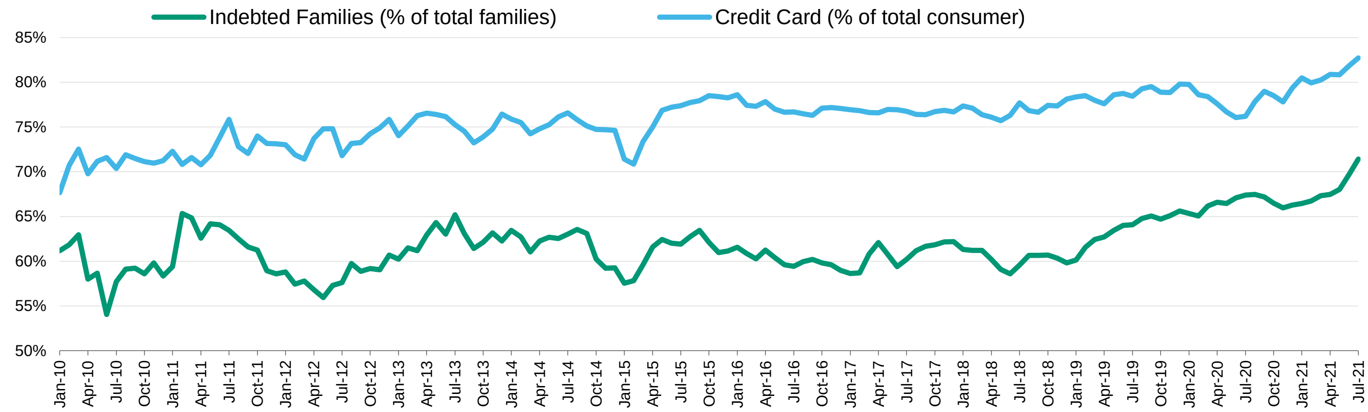
As loan origination grows and banks' risk appetite increases with the economy's recovery, asset quality problems in the systemwide consumer loan portfolio likely will worsen from current low levels. Problem consumer loans bottomed at 4.1% in July 2021, compared to 5.1% in February 2020, before the pandemic. The low delinquencies reflect high household savings and limited consumption during the pandemic, but these factors are likely to change in the coming quarters as individual spending normalizes.

As of July, 71% of Brazilian families had outstanding debt, which was at its highest level on record since 2010. Unsecured loans comprise the majority of household debt, with credit card debt comprising 83% of total consumer loans (see Exhibit 2).

Exhibit 2

Expensive and unsecured consumer loans comprise the majority of household debt

Evolution of credit card loans over total consumer loans and percentage of indebted families



Source: Brazil's National Confederation of Commerce of Goods, Services and Tourism

Brazilian banks built up conservative reserve buffers during the pandemic, representing 6% of total loans as of July 2021, which will partially offset an expected increase in credit losses. Furthermore, families with overdue debts represented 25.6% of total in July 2021, slightly up than 24.7% average between 2017-21. The recent improvements in job markets will also help to reduce unemployment rate that stood at a still high 14.1% as of June, down by 60 basis points compared to March 2021. The consistent increase in wages will also help to reduce inflationary pressures on borrowers' repayment capacity, smoothing these pressures over banks' future asset quality metrics.

Endnotes

1 The bank ratings shown in this report are the bank's deposit rating, senior unsecured debt rating (where available) and Baseline Credit Assessment.

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Russia's easier regulatory requirements for SME loans are credit negative for banks

Originally published on 31 August 2021

On 26 August, the Central Bank of Russia (CBR) announced that it will lower capital requirements and relax underwriting rules for bank loans to small and medium-size enterprises (SMEs). The CBR said the revised regulation aims to increase SME loan affordability for borrowers.

The easier regulations are credit negative for banks because they will incentivise banks to increase SME loans with looser underwriting standards and lead to a deterioration of asset quality when the rapidly augmented SME loan portfolios start seasoning.

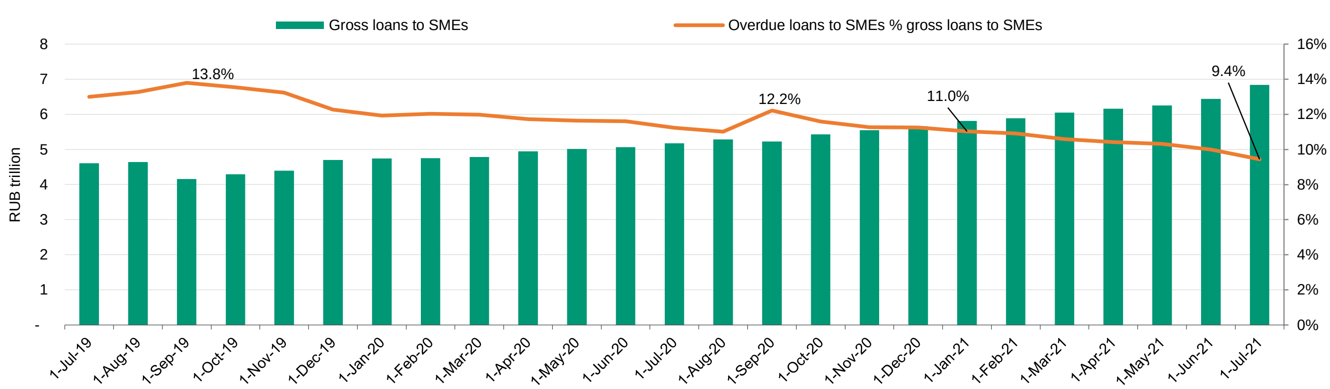
The CBR will reduce to 20% from 100% banks' required risk weights for SME loans guaranteed by the state joint-stock company Russian Small and Medium Business Corporation JSC (RSMBC), reducing the capital banks need to set aside for the loans. The CBR will also expand the eligibility criteria for loans issued based on banks' in-house credit underwriting methodologies and without obtaining an SME borrower's official financial report (i.e., a report prepared in accordance with Russian generally accepted accounting principles). The CBR has not specified the details of its revisions to loan eligibility criteria.

We estimate that SME Bank (B3/B3 developing, caa2[1]), which is wholly owned by RSMBC, will be most affected by the changes because it specialises in SME lending. Other banks with large SME loan market shares are Sberbank (Baa3/Baa3 stable, ba1) and Bank VTB, PJSC (Baa3/Baa3 stable, b1).

We expect that the substantially lower capital requirements for RSMBC-guaranteed SME loans will likely disincentivise banks from thorough borrower credit analysis. If execution of the guarantee for a defaulted loan became a slow and complicated process, it would undermine the bank's asset quality, profit generation and cash position. Likewise, for SME loans where only borrower management data are available and not the official financial report, the lender may find it difficult to confirm the borrower's credit strength and the loan's credit quality.

SME lending is the fastest growing loan segment at Russia's banks. As of 1 July 2021, SME loans had increased 32% year on year, compared to a 10% increase for large corporate loans and 22% for retail loans. Although the rouble volume of overdue SME loans increased by 11% for the year to July 2021, overdue loans as a percent of overall SME loans declined to 9.4% of total SME loans as of 30 June from 11.0% at year-end 2020 because of the fast growth of SME loans (Exhibit 1). Nevertheless, overdue SME loans at 9.4% as of 30 June is much higher than the 6.8% share of overdue loans to large corporations and individual entrepreneurs.

Exhibit 1
Fast growth of Russian banks' loans to SMEs masks weakening in the credit quality of loans



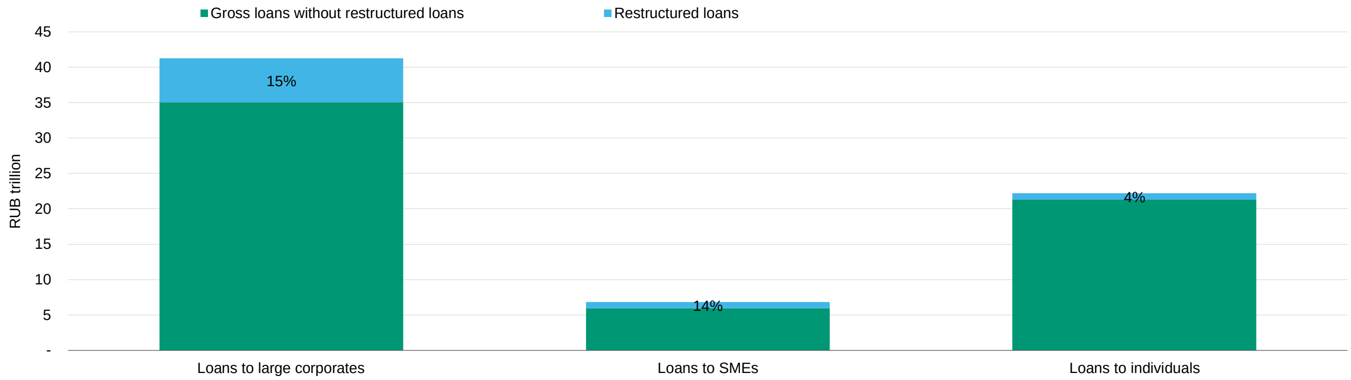
Source: Central Bank of Russia

Additionally, as of 30 June, the proportion of restructured SME loans was high at around 14% of total SME loans, almost the same as 15% for large corporates and much higher than 4% for the retail lending segment. The high incidence of restructured SME loans reflects the effect of pandemic-induced lockdown measures. The lasting financial hardships of some SME borrowers whose loans were restructured because of the pandemic will add to the segment's accumulating asset quality pressures.

Exhibit 2

Around 14% of all loans to SMEs were restructured during the pandemic

As of 30 June 2021



Source: Central Bank of Russia

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Brazil's credit-positive loosening of auto insurance regulations will revitalize the industry

Originally published on 31 August 2021

On 1 September, new simplified rules for Brazil's auto insurance industry went into effect. The regulatory changes aim to increase auto insurance penetration in Brazil by allowing insurers to offer more flexible products with wider pricing options. These new rules are credit positive for Brazil's auto insurers because they will allow products to match evolving market demands, which will lead to premium growth and help revitalize the industry.

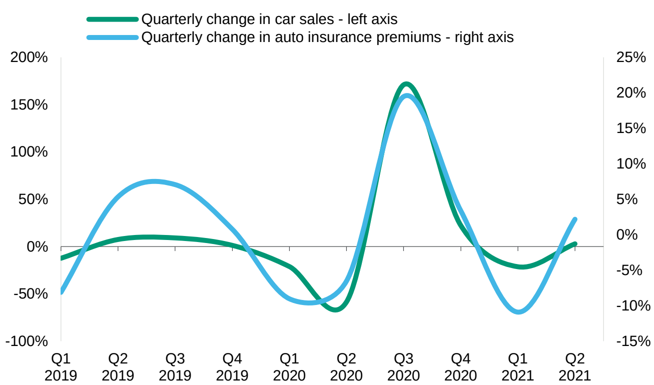
The measures will benefit all Brazilian auto insurers, including the largest ones in the market such as Porto Seguro Companhia de Seguros Gerais, Bradesco Auto/Re Companhia de Seguros and Tokio Marine Seguradora, which account for almost 40% of the market, as well as niche auto insurers, insurtechs and newcomers.

Auto insurance is not mandatory in Brazil, and only 16% of the country's car fleet had insurance coverage in 2019. The auto insurance industry relies heavily on new car sales (see Exhibit 1), with Brazilian car owners tending to drop their insurance as their vehicles age. Auto insurers now will be able to provide select coverage such as theft, collision or fire damage on a stand-alone basis, something they were not allowed to offer previously. Additionally, insurers now can include auto insurance coverage in a bundle with other coverage such as property insurance. We this flexibility to lead to an increase in premiums and decrease insurers' reliance on new car sales in a country where only 16% of are less than five years old. (see Exhibit 2).

Exhibit 1

Auto insurance premiums in Brazil have highly depended on car sales since 2019

Quarterly changes in car sales and auto insurance premiums

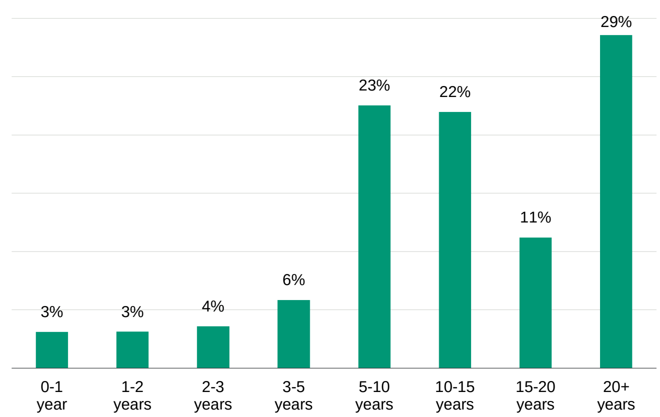


Sources: Federação Nacional da Distribuição de Veículos Automotores (FENABRAVE), Superintendência de Seguros Privados (SUSEP) and Moody's Investors Service

Exhibit 2

Only 16% of Brazil's car fleet is fewer than years old

Distribution of the Brazilian car fleet by age



Sources: Brazilian Ministry of Infrastructure and Moody's Investors Service

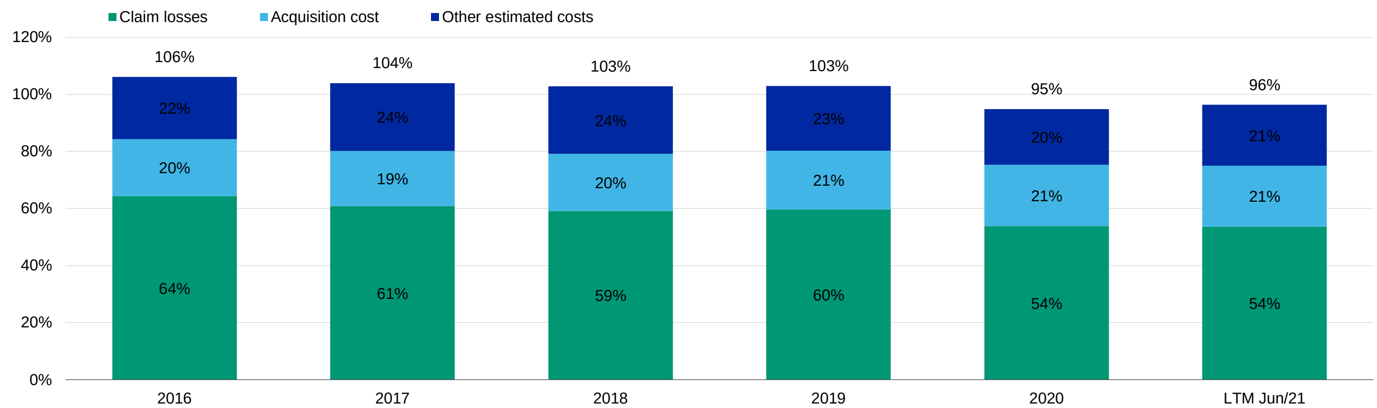
The regulatory changes also considers the needs of the ride-hailing industry, where it is common practice for drivers to use rented cars. The new regulation will allow insurers to provide policies to individuals rather than specific vehicles.

Another change will allow auto insurers to impose customers use specific repair shops. Previously, policyholders would generally select a repair shop and pay an insurance deductible, with the remainder charged to insurer. Such a practice gave pricing power to independent repair shops, raising the costs borne by insurers: during 2016-19, claim losses averaged 61% of retained premiums of automobile insurance (see Exhibit 3). The new regulation will help auto insurers improve cost efficiency and increase overall underwriting results.

Exhibit 3

Claim losses in Brazil equaled 61% of retained premiums before during 2016-19

Evolution of combined ratio of automobile insurance by component



Sources: Superintendência de Seguros Privados and Moody's Investors Service

Overall insurance penetration in Brazil is relatively low, particularly for nonlife insurance, with premiums reaching 1.78% of gross domestic product in 2019, versus 3.88% globally and 8.51% in the US. In the last 12 months to June 2021, auto insurance premiums amounted to BRL36.5 billion ($7.3 billion), and accounted for 46% of total nonlife premiums.

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Policy support and strong loss buffers will help sector weather coronavirus resurgence

Originally published on 31 August 2021

Summary

A resurgence of coronavirus cases in Indonesia will hinder economic recovery, raising asset risks for banks in the country. Yet regulatory support for borrowers will limit the deterioration of banks' asset quality, and they have sufficient loan-loss buffers to absorb expected increases in loan losses.

» **Regulatory support for borrowers will prevent a spike of loan defaults.** A resurgence of coronavirus cases will hinder plans to reopen the economy and increase financial distress among borrowers, raising asset risks for banks. However, regulators have eased rules for banks to restructure loans for pandemic-hit borrowers without classifying them as nonperforming until March 2022, and they are planning to extend the measure. This will give affected borrowers time to recover financially and help banks maintain asset quality.

» **Loan-loss buffers are sufficient to absorb new NPLs.** Indonesian banks have large loan-loss reserves and strong pre-provision profitability backed by high net interest margins to cover expected loan losses. Reflecting these strong buffers, even under an extreme scenario where 50% of restructured loans become impaired, capital ratios at five out of nine rated banks could still rise by the end of 2022 from two years earlier. The capital and liquidity of Indonesian banks remain strong.

» **Growth prospects for banks remain intact.** Despite the immediate economic challenges, Indonesian banks continue to have ample room for growth because the country, with a large, young population, has a huge untapped market for the sector. A pandemic-fueled acceleration in the adoption of digital financial services will help banks expand.

Click here for the full report.

Coronavirus resurgence in Thailand raises asset risks but banks will maintain adequate solvency

Originally published on 30 August 2021

Summary

A resurgence of coronavirus infections in Thailand will hamper the country's economic recovery and raise asset risks for banks in the country. Yet government measures to support borrowers will limit the deterioration of banks' asset quality, and banks have sufficient buffers to absorb expected credit losses.

» **Slow economic recovery in Thailand will weigh on asset quality for banks.** We project that Thailand's GDP will grow at the slowest pace among large ASEAN economies in 2021 as the tourism sector continues to suffer from the pandemic amid low vaccination rates. Loans to small and medium enterprises (SMEs), many of which are tied to tourism, will drive growth in nonperforming loans (NPLs).

» **Yet banks will maintain adequate solvency.** The overall deterioration of banks' asset quality will be modest, helped by support measures for borrowers, with NPLs to grow to about 5%-6% of gross loans by the end of 2022 from about 4% at the end of June 2020. Thai banks have sufficient capacity to absorb loan losses of this magnitude. Under a worst-case scenario where 50% of loans under relief turn into NPLs in two years, with a high 75% Loss Given Default rate, banks would still maintain adequate capital levels.

» **Banks still have ample potential for long-term growth.** Thai banks operate in a large, well-diversified economy, supported by a high degree of policy credibility of key institutions, such as the Bank of Thailand and the Ministry of Finance. As such, Thai banks have abundant potential for growth for the next 10 years, assuming the economic shock from the pandemic fades in 2022-23. In addition to the fundamental foundation for growth, Thai banks will continue to expand through digital and mobile financial services, which have gained significant traction in the past year thanks to social-distancing measures.

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