MOODY'S ANALYTICS

WEEKLY MARKET OUTLOOK

Will Excessive Stimulus Lead to Excessive Leverage?

Moody's Analytics Research

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Credit Markets Review and Outlook

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

Will Excessive Stimulus Lead to Excessive Leverage?

High yield bond issuance and newly rated loans from high-yield issuers have soared thus far in 2021. Layers of fiscal stimulus on top of monetary stimulus have boosted risk tolerance. The most stimulus since WWII might yet drive private-sector leverage up to heights that significantly increase long-term debt repayment risk.

Could it be that today's endless stimulus does more to increase default risk than to increase consumer price inflation risk? Nevertheless, elevated default risk may not become manifest until corporate earnings are expected to contract materially and that may not occur until 2023 at the earliest.

There is widespread agreement that 2021's prospective advance by real GDP will be the liveliest since 1984's 7.2%. As derived from Federal Reserve data, the yearly increase of fourth-quarter nonfinancial-corporate debt outstanding accelerated from 1982's 8.8% to 1983's 10.4% before peaking at 1984's 16.9%.

Perhaps worth noting is how 1984 was at the start of the high-yield bond phenomenon. Prior to Drexel's Michael Milken, the high-yield bond market mostly consisted of formerly investment-grade issuers. It was not until the early 1980s that newly issued bonds started off with speculative-grade ratings.

Note that 1984's rapid expansion of corporate debt occurred despite a rise by corporate borrowing costs. For example, after dropping from 1982's recession-inflated 15.77% to 1983's 12.90%, the calendar-year average of Moody's Analytics long-term Baa industrial-company bond yield jumped to 13.84% in 1984. By contrast, the long-term Baa industrial-company bond yield has declined from 2020's 3.81% average to a 2021-to-date average of 3.53%, where the latter includes a recent 3.67%.

In addition, unlike the rise by the annual average of the effective federal funds rate from 1983's 9.09% to 1984's 10.23%, 2021's ultra-low 0.125% midpoint for fed funds is unchanged from its reading of April-December 2020.

Both low yields from other investment-grade credit market instruments and above-average confidence in the very positive outlook for corporate earnings have helped to narrow the Bloomberg/Barclays high-yield bond spread to April 7's 290 basis points, which is less than each of its previous monthly readings going back to June 2007's 256 bp.

As it turned out, the high-yield bond market's supreme optimism of June 2007 was misplaced and by August 2007 a financial crisis had surfaced that was soon followed by the Great Recession. After June 2007, the high-yield bond spread began a protracted climb that included a bone-jarring ascent to December 2008's 1,874 bp zenith for the high-yield spread's month-long average.

For corporate credit, in general, the continued growth of corporate earnings practically rules out anything remotely similar to what transpired in 2008-2009. Nevertheless, it would not be surprising if 2021's likely combination of very low Treasury bond yields, rapid economic growth, and a breakneck expansion of corporate earnings prompts a jump in corporate debt outstanding.

Taken together, unsustainably thin corporate bond yield spreads and expectations of significantly higher Treasury bond yields constitute a powerful incentive to bring corporate borrowing forward. In addition to refinancing outstanding obligations at lower interest rates and longer maturities, new corporate bond issues and leveraged loans may fund current and future acquisitions, equity buybacks, dividends, and capital spending. Financial-company issuers may also borrow to augment their capitalization.

Market-Based Metrics of Default Risk Are the Lowest since 2007

The market's assessment of high-yield default risk now resides at its lowest level since the early summer of 2007. As mentioned earlier, the Bloomberg/Barclays high-yield bond spread trails each of its prior month-long averages going back to June 2007. In addition, the 1.84% April-to-date average of Moody's Analytics expected default frequency metric for U.S./Canadian high-yield issuers is less than each of its prior month-long averages going back to the 1.59% of June 2007, or when the high-yield bond spread averaged 256 bp.

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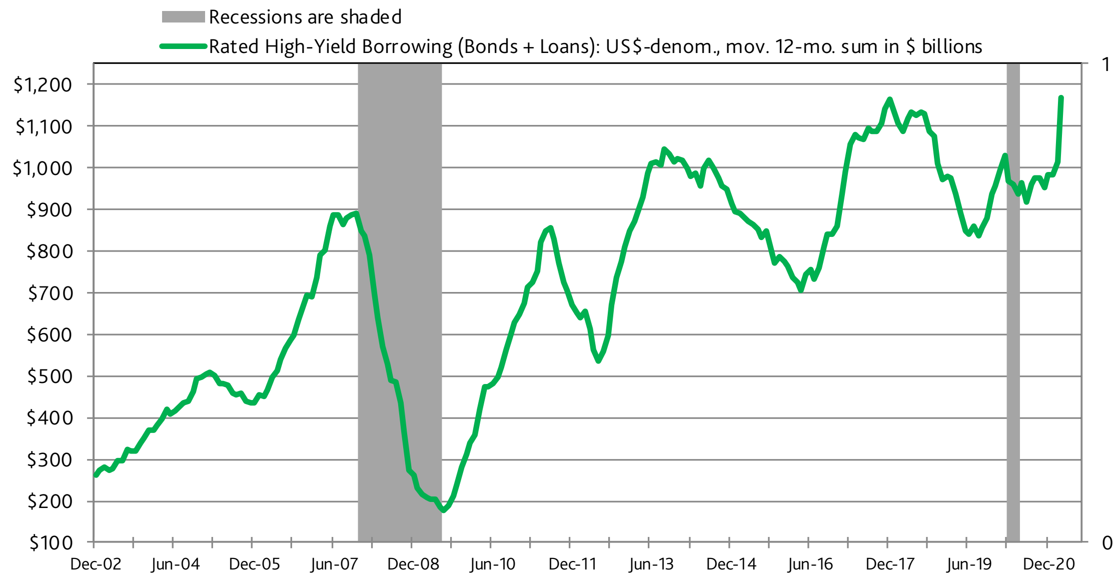
High-Yield Borrowing Sets New Record High in 2021's First Quarter

An abundance of systemic financial liquidity can be inferred from February's 27% year-over-year surge by the M2 measure of highly liquid financial assets, which is the fastest such increase since 1959 at least. Prior to 2020, M2's biggest yearly advance was February 1976's 13.8%. For each month beginning with May 2020, M2's yearly growth rate has exceeded 20%. Thus, in terms of both growth rates and relative to GDP, M2 now far exceeds anything observed during the inflationary 1970s. Still, most do not expect history to repeat itself If only because of today's more intense global competition and America's much older workforce and population.

Figure 1: Total Rated High-Yield Borrowing Activity Grew by 20.8% Annually during 12-Months-Ended March 2021...Will Probably Set a Series of Record Highs Going Forward

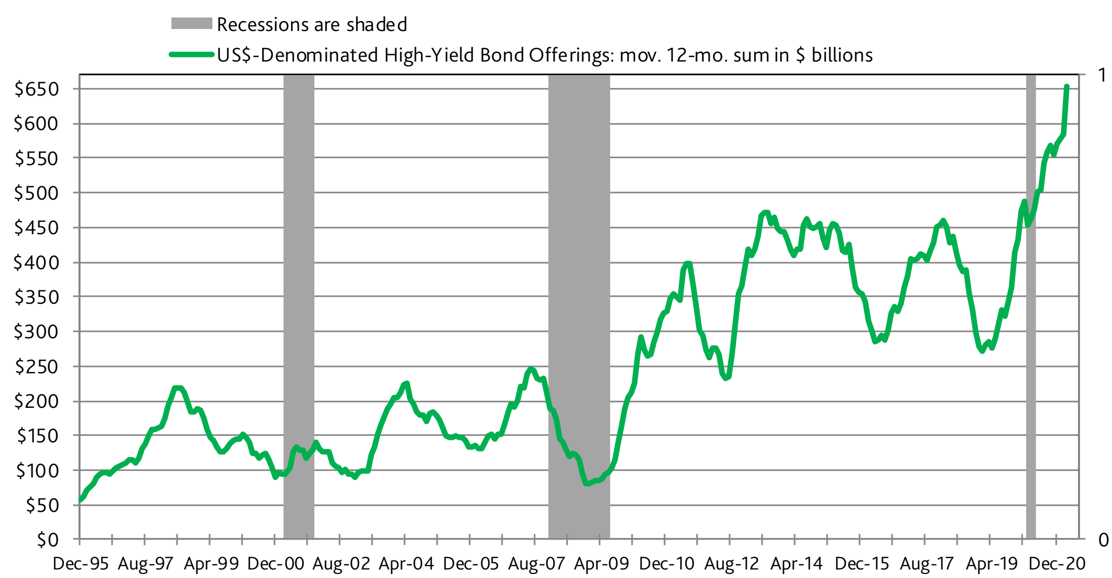
sources: : Dealogic, NBER, Moody's Analytics



High-yield borrowing activity—the sum of high-yield bond offerings plus newly rated loans from high-yield issuers—set a new record-high $445 billion in 2021's first quarter. US$-denominated high-yield bond issuance soared 64% annually to a record-high $212 billion, while newly rated loans from high-yield issuers advanced 82% annually to $233 billion. The latter fell short of second-quarter 2018's $245 billion record-high for newly rated high-yield loans.

Figure 2: Massive Monetary and Fiscal Stimuli Stoke 44% YY Surge by Moving 12-Month Sum of High-Yield Bond Issuance to Record $653 Billion for Span-Ended March 2021

sources: Dealogic, NBER, Moody's Analytics



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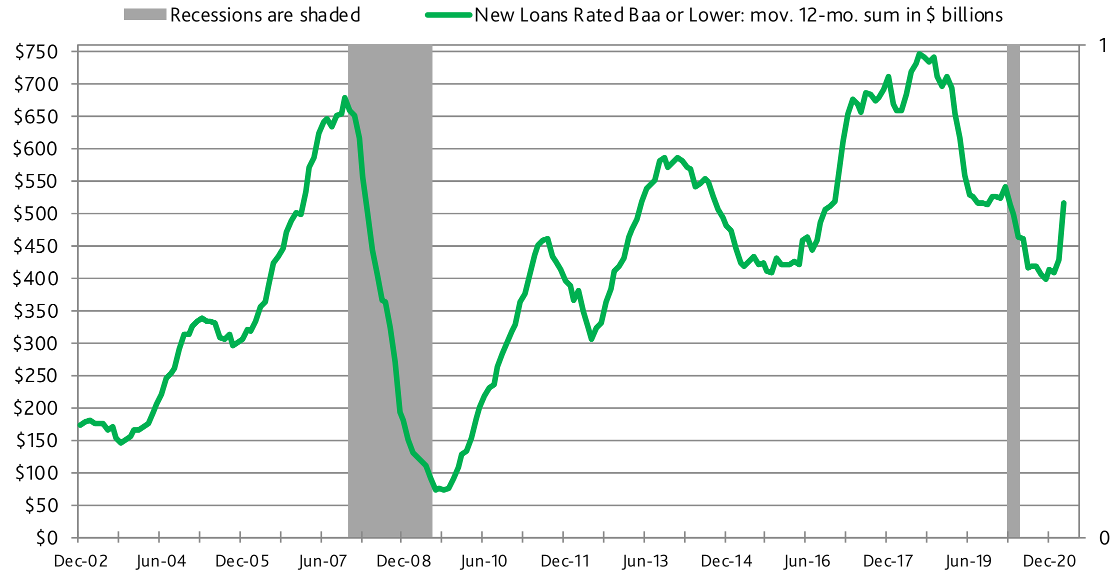
The lion's share of new speculative-grade borrowings refinanced outstanding debt. For the most part this benefited credit quality by extending maturities (which lessens refinancing risks) and by lowering interest expense (which boosts cash flow). In addition, the funding of M&A figured prominently among uses of funds secured by newly rated loans.

Figure 3: Moving 12-Month Sum of New Loans from High-Yield Issuers Rose by 0.5% YY to $517 Billion for Span-Ended March 2021...May Reach July 2018's Record High of $745 Billion
sources: NBER, Moody's Analytics



Finally, the build-up of liquidity, or working capital, was cited with an atypically high frequency among first-quarter 2021's speculative-grade borrowings. The latter may reflect an attempt by high-yield bond issuers to avoid a future jump in fixed-rate borrowing costs that would accompany a greater-than-2% 10-year Treasury yield. High-yield borrowers also boosted cash balances to fund future acquisitions. Finally, corporate borrowers may decide to hold above-average amounts of cash as insurance against a possible disruptive assurance of COVID-19.

The supply of newly rated loans from speculative-grade borrowers was unevenly distributed across rating categories. First-quarter 2021 showed a 27.6% yearly plunge by new loans rated Baa to $6.8 billion and an 88.9% yearly surge by new loans graded less than Baa to $224 billion. The latter included a 214.5% annual advance by new loans rated single-B to $147 billion. In addition, 2021's first quarter included a 0.4% yearly dip by Ba-grade loan borrowing (to $68.7 billion) and a 184.7% yearly jump by new Caa-rated loans (to merely $8.6 billion).

As far as the moving 12-month sum of high-yield borrowing activity goes, the COVID-19 recession was the mildest on record. The moving 12-month sum of high-yield bond issuance and new loan borrowing fell by 10.7% from its February 2020 peak of $1,029 billion to a July 2020 bottom of $919 billion.

In stark contrast, 2008-2009's Great Recession triggered a much deeper dive by high-yield borrowing. For example, the moving 12-month sum of high-yield bond issuance and new loan borrowing plummeted 80.0% from a November 2007 high of $892 billion to a July 2009 bottom of $178 billion.

February's jump by job openings complements small-business survey results

The NFIB small business survey for February found that the most frequently cited biggest problem facing small businesses was the labor quality followed by taxes and regulations. In February, the net percent of businesses claiming that labor quality was their biggest problem was 24 percentage points compared with only a 6-point average during the first five years of the 2010-2019 business cycle upturn.

Also, in February, a record 40% of surveyed small businesses claimed they had "hard to fill" job openings. By contrast, the share of surveyed small businesses reporting "hard to fill" job openings averaged a much lower 15.4% during the first five years of the previous business cycle upturn.

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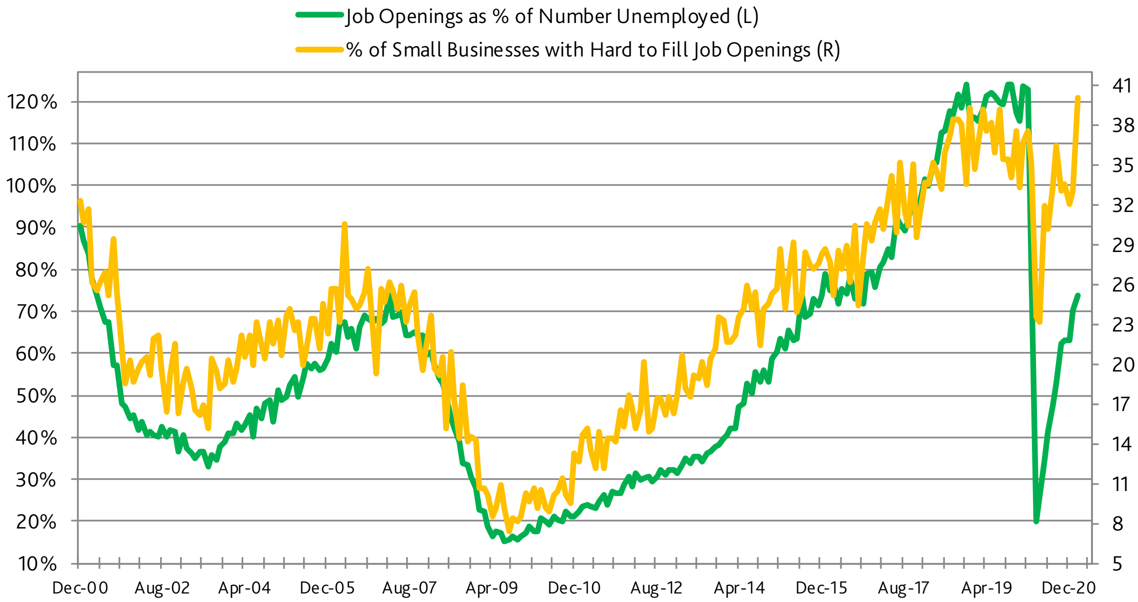
The number of unfilled job openings in the U.S. economy jumped up to 7.367 million in February 2021, which was the strongest reading for this barometer of labor demand since the 7.478 million of January 2019. Also, February's job openings approximated 74% of the accompanying number of officially unemployed individuals. During the five years following the June 2009 end to the Great Recession, job openings not only averaged a much lower 28.4% of the number of unemployed persons, but the ratio also peaked at June 2014's relatively low 53.0% (which was exactly five years after the end of the Great Recession).

Figure 4: As Inferred from Job Openings and Hard-to-Fill Jobs, Today's Labor Market Offers More Opportunities Compared to That of 2009-2013

sources: BLS, NFIB, Moody's Analytics



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

THE U.S.

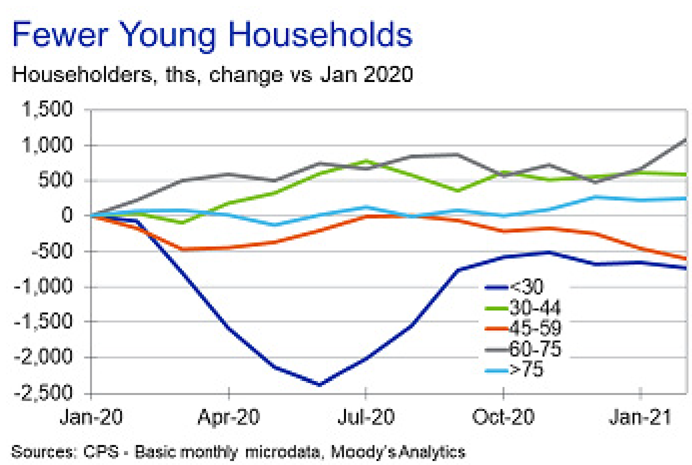
By Mark Zandi, Chief Economist of Moody's Analytics

Real GDP Growth and Job Gains Set to Boom

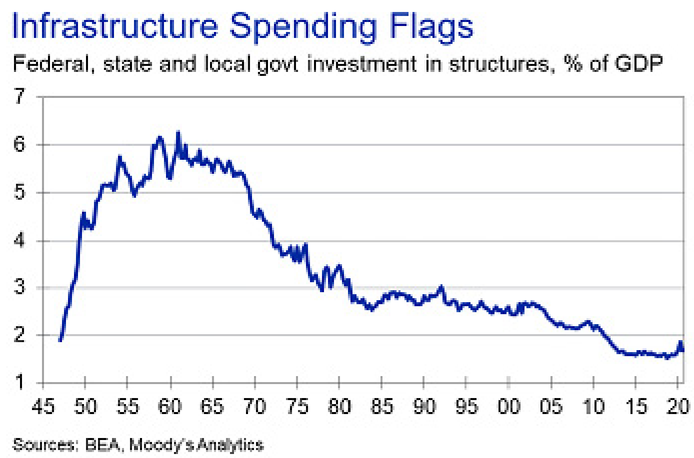
I have been a professional economist for more than 30 years and have made many projections during that time. Some of those forecasts I've made with confidence, others not so much. But I can't remember a time when I've been so sure of the U.S. economy's near-term prospects. It is going to be rip-roaring. For the next six months, probably for the next year, and perhaps even well into next year, real GDP growth and job gains will boom, and unemployment will quickly decline.

The economy is already rapidly gaining strength. That's clear in the March jobs numbers. Employment increased by more than 900,000 in the month with an impressive over 70% of industries reporting job gains. Weather played a role with the rebound from awful winter storms in February, but business and school reopenings added a lot to payrolls. Unemployment fell to 6% at the same time labor force participation notched higher. The benefit from the $1.9 trillion in fiscal support provided by the American Rescue Plan didn't materially impact the numbers, but it will starting in April. ARP-funded stimulus checks probably did help power the gangbuster 17.7 million new vehicles sold (at an annualized rate) in March. There are fewer than a dozen other months in history in which more vehicles were sold. No surprise then that manufacturing is booming. The Institute of Supply Management manufacturing survey posted its strongest reading since 1983. The other economic statistic that stood out was the quick revival in consumer confidence. According to the Conference Board, sentiment is already stronger than it has been on average in the more than 50-year history of the survey.

The pandemic's demographic blow may also begin to fade. According to micro data from the Current Population Survey, the number of households fell sharply when the pandemic hit a year ago, particularly among younger households. Households headed by someone less than 30 years old fell by close to 2.5 million between January and June of last year. Apparently, many young people chose to move back home or crash with roommates during the lockdown. But household formation rebounded with the economy's reopening last summer. Cushioning the hit to households early on during the pandemic was the increase in the number of households headed by those in their 60s and early 70s. That's tougher to explain. Is it possible that families segregated their elderly parents because they were worried about exposing them to the virus?



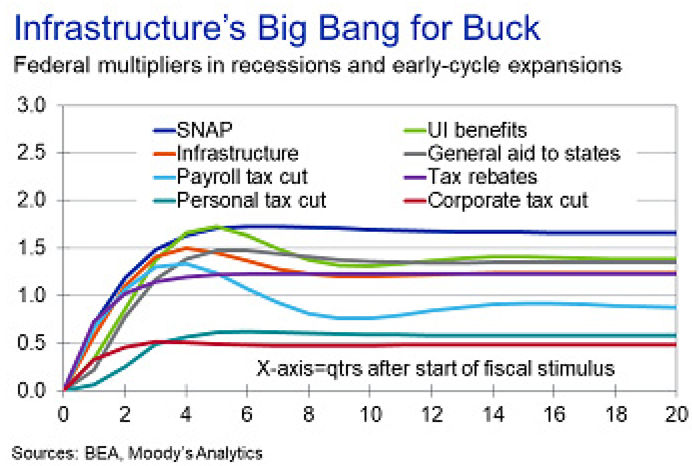
The economy's long-term prospects also brightened with President Biden's proposed American Jobs Plan, the part of his Build Back Better Presidential campaign agenda focused on investing in the nation's infrastructure. There is no argument that the nation's infrastructure needs are great. The U.S. has underinvested in infrastructure for decades. Federal, state and local government spending on infrastructure peaked at close to 6% of GDP in the 1950s and 1960s when the Interstate Highway System was built. It fell sharply in the 1970s and again in the wake of the financial crisis in the early 2010s. Infrastructure investment as a share of GDP is well below 2% of GDP, the lowest in the data available since World War II.



The result has been a steady aging of the nation's stock of public infrastructure. For example, the average age of the nation's highways is close to 30 years, double what it was in the 1960s. The average age of the nation's dams is even older. If maintained, this would not necessarily present a problem or urgent need for replacement, but maintenance has not been performed in many cases, and the need for additional spending is intensifying. Take the nation's more than 600,000 bridges. The Department of Transportation classifies more than one-fourth as structurally deficient or functionally obsolete. Many of the larger and most heavily used of these bridges were built in the same period and will reach replacement age—the theoretical life of a bridge is approximately 50 years—around the same time.

Biden's American Jobs Plan calls for $2.2 trillion in increased government spending over the 10-year period from 2022 to 2031, and $400 billion in tax credits. Two-thirds of the cost of the plan is paid for over the decade with $1.8 trillion in higher corporate taxes. The nation's budget deficit thus increases more than $800 billion over the decade on a static basis—that is, before accounting for the economic benefit of the plan on the government's finances. The biggest boost to spending goes to traditional infrastructure, including transportation projects such as roads, bridges and ports, and to shore up the nation's crumbling water and power infrastructure. Social infrastructure, including education, healthcare and housing, also receives substantially more financial support. To lift the nation's competitiveness, the plan allocates more funds to basic research and development, manufacturing, and broadband. Workforce development funds are also provided to fund the training needed to prepare the workforce for future jobs, including those created by the infrastructure projects. One seemingly incongruous part of the plan is $400 billion in spending on better care for the elderly and disabled. This has much more in common with Biden's next proposed fiscal package to build out the nation's social safety net.

Increasing infrastructure investment by more than 1% of GDP over the next decade as Biden has proposed has both near- and long-term benefits. Near term it has a large so-called multiplier—the increase in GDP for a dollar increase in investment. In a period of high unemployment and significant slack in the economy, like today, the one-year multiplier on traditional infrastructure spending is close to an estimated 1.5, among the highest compared with other types of federal government spending and tax policy. With close to 3 million more workers still permanently unemployed as a result of the COVID-19 pandemic, an infrastructure plan that provides new jobs in communities across the country would be particularly effective.



Long term, economic research is in strong agreement that public infrastructure provides a significantly positive contribution to GDP and employment. It lowers business costs and thus improves competitiveness and productivity, allows workers to live closer to where they work and thus reduces commute times, improves labor participation, and reduces carbon emissions. There is more debate on whether public infrastructure spending boosts GDP by as much as private capital does. One reason for this is that, unlike private investment, federal investment is not driven solely by market forces or by maximizing economic returns of firms. Federal infrastructure also has the goal of improving quality of life, reducing inequities, supporting the work of the federal government itself, and addressing other broader social objectives that policymakers may have. The federal government also imposes various requirements that can increase the costs of the projects that it funds. We estimate the average return on private capital to be close to 10%—that is, a $1 increase in private investment, all else being equal, increases GDP by 10 cents over a year—while it is almost 7% for public infrastructure.

Still, the state of the economy makes this is an especially propitious time to increase infrastructure investment, since extraordinarily low interest rates make the return on that investment substantially greater than the government's cost of financing. Thirty-year Treasury yields are just over 2%, while the return on almost any public infrastructure project is likely to be meaningfully greater than that.

The infrastructure plan results in a stronger economy over the coming decade, with higher GDP, more jobs and lower unemployment. However, the most immediate impact in early 2022 is to marginally reduce growth. That is because the higher corporate taxes take effect right away, while the increased infrastructure spending does not get going in earnest until later in the year. This changes quickly. By 2023 and throughout much of the middle of the decade the ramp-up in infrastructure spending significantly lifts growth. The apex in the boost to growth from the plan is in 2024 when real GDP is projected to increase 3.8%, compared with 2.2% if the plan fails to become law. In terms of jobs, with the infrastructure plan the economy recovers the jobs lost in the pandemic recession in the next couple of years, not much different than without the plan. But the plan does result in substantially more jobs mid-decade, with employment under Biden's term as president increasing by 13.5 million jobs. Unemployment is also meaningfully lower with the plan, falling to a low of 3.5% by the end of Biden's term in 2024, consistent with the low reached just prior to the pandemic. Labor force participation by then is also expected to fully recover from the impact of the pandemic.

Macroeconomic Impact of American Jobs Plan

	2020	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030	Avg annual 2021-30
Real GDP, % change												
With AJP	-3.49	7.23	3.86	2.30	3.77	2.85	1.86	1.63	2.02	2.23	2.24	2.99
Without AJP	-3.49	7.23	3.91	1.90	2.23	1.82	1.79	2.01	2.14	2.07	2.06	2.70
Difference	0.00	0.00	-0.04	0.41	1.54	1.03	0.07	-0.38	-0.13	0.16	0.18	0.29
Nonfarm employment, mil												
With AJP	142.26	146.37	150.89	152.47	155.14	156.89	157.82	158.60	159.47	160.35	161.24	
Without AJP	142.26	146.37	150.91	152.45	153.67	154.38	155.01	155.73	156.62	157.57	158.55	
Difference (ths)	0	0	-23	19	1,472	2,514	2,818	2,869	2,843	2,780	2,690	
Unemployment rate, %												
With AJP	8.12	5.59	4.44	4.38	3.76	3.63	3.67	3.81	3.83	3.84	3.83	
Without AJP	8.12	5.59	4.44	4.39	4.31	4.36	4.51	4.52	4.47	4.44	4.43	
Difference	0.00	0.00	0.01	-0.01	-0.55	-0.73	-0.83	-0.71	-0.64	-0.60	-0.59	

Sources: BEA, BLS, Moody's Analytics

Long term, the economy enjoys stronger productivity growth. The improvement is marginal through the first half of the decade but will be measurable by decade's end as the stock of public infrastructure meaningfully increases, adding as much as 0.1 percentage point to annual real GDP growth.

The nation's deficits and debt load are higher over the 10-year budget horizon, because the infrastructure plan is not fully paid for. On a static basis, the 10-year cumulative deficit increases by nearly $850 billion. On a dynamic basis—accounting for the benefits of the stronger economy resulting from the plan on government revenues and expenditures—the 10-year cumulative deficit is expected to be close to $625 billion. It is important to note that the spending under the plan winds down after 10 years, while the increased tax revenue continues to accrue to the Treasury, so that after about 15 years the infrastructure plan is fully paid for.

There are many potential political impediments to passage of the plan, but we expect that an infrastructure plan similar in spirit and size to what the president has proposed will become law later this year via the budget reconciliation process.

Next Week

The numbers on new residential construction in March, due late in the week, should be highly instructive. As home prices continue to climb amid low inventories, housing starts in February dropped 10.3% to 1.421 million annualized units. Winter storms were likely behind that decline, and with weather returning to seasonal norms, starts should have begun to climb over the subsequent month. The consumer price index for March will get a lot of attention, since inflation is poised to stage a noticable though transient acceleration over the next few months. Other data we will be watching include the NFIB small business survey and bankruptcy filings. On the labor market, we continue to look at weekly jobless claims for indications of labor market health, though the numbers in this indicator have been choppy of late.

EUROPE

By Ross Cioffi of Moody's Analytics

U.K. Output Decline Likely Slowed in February

Next week come three major euro zone releases. The final estimate for the harmonized index of consumer prices in the euro zone, industrial production, and external trade. On the inflation front we aren't expecting divergence from the preliminary estimate of 1.3% y/y in March. According to the preliminary estimate, energy prices supported the month's headline rate as nonenergy goods price inflation slowed considerably. However, the deceleration in core goods inflation will revert later in the second quarter as producers pass cost increases on to consumers and store reopenings lead to a boom in consumer demand. Meanwhile, base effects in energy prices will be a force pushing up the inflation rate all year. Among the major economies, inflationary pressures are mounting most in Germany, where the harmonized inflation rate is expected to reach 2% y/y in March. Thanks to the manufacturing sector, Germany's economy has been more resilient than those of other euro zone members.

We expect industrial production in the euro zone to have increased 0.8% m/m in February, and upbeat PMI releases have us betting on an increase in March output. The manufacturing PMI rose to a reading of 60.7 in February from 57.1 a month earlier on the back of stronger demand. Supply disruptions are weighing on firms as costs jump and deliveries of inputs are delayed. But the supply concerns amid the global recovery have also pushed firms to stock up on inventory. On a similar note, we expect that the euro zone trade surplus increased in February to €24 billion from €23 billion a year earlier. Recovering demand in the U.S. and China will have fueled exports for capital and intermediate goods. Imports are likely to lag in year-ago terms with consumer demand still suppressed by lockdowns.

The U.K.'s monthly GDP estimate for February will be released as well. We expect output slid 0.5% from the previous month. However, this will be better than the 2.9% m/m decline in January. Lockdown measures and struggling trade with the EU will have weighed further on the economy. U.K. GDP won't start recovering more sustainably until the second quarter, when social distancing starts to ease.

	Key indicators	Units	Moody's Analytics	Last
Mon @ 11:00 a.m.	Euro Zone: Retail Sales for February	% change	3.2	-5.9
Tues @ 8:00 a.m.	U.K.: Monthly GDP for February	% change	-0.5	-2.9
Tues @ 10:00 a.m.	Italy: Industrial Production for February	% change	1.4	1.0
Wed @ 9:00 a.m.	Spain: Consumer Price Index for March	% change yr ago	1.3	0.0
Wed @ 11:00 a.m.	Euro Zone: Industrial Production for February	% change	0.8	0.3
Thur @ 8:00 a.m.	Germany: Consumer Price Index for March	% change yr ago	1.7	1.3
Thur @ 8:45 a.m.	France: Consumer Price Index for March	% change yr ago	1.1	0.6
Thur @ 10:00 a.m.	Italy: Consumer Price Index for March	% change yr ago	0.8	0.6
Fri @11:00 a.m.	Euro Zone: Consumer Price Index for March	% change yr ago	1.3	0.9
Fri @11:00 a.m.	Euro Zone: External Trade for February	€ bil	24.0	6.3

Asia-Pacific

By Katrina Ell and Shahana Mukherjee of Moody's Analytics

China see strong, although slightly uneven, growth in first quarter

China's March-quarter GDP growth likely hit 18.5% year over year, following the 6.5% expansion in the December quarter. Base effects are severely inflating the annual comparisons, but underlying growth momentum was strong in the first quarter, albeit uneven.

The nationwide lockdown early last year halted nonessential activities, causing deep dips in many economic indicators. To eliminate the impact of the low base, we compare the latest data with the same period in 2019 and look at the two-year growth rate. China's industrial production in the first two months was up by 16.9% from 2019, translating into an 8.1% average annual increase, which was well above the average year-on-year growth rate before the pandemic. High-tech manufacturing grew by more than 27% over the two years. This reflects the surging external demand for pharmaceutical and remote-working equipment from countries under prolonged lockdowns, as well as the government's push to move up the manufacturing ladder to achieve technological self-reliance.

The above-pre-pandemic output level was mostly buttressed by exports, as domestic consumption hasn't gotten back on track. China's retail sales rose by 6.4% compared with the same period in 2019, equivalent to a 3.2% yearly gain, far below the 8% pre-pandemic growth. Urban consumption showed more resilience than rural because of the proliferation of e-commerce through which goods sales jumped by 34% over the past two years. This suggests huge potential in China's consumer market, and the government may fully unleash domestic demand by facilitating the extension of e-commerce and delivery services to rural areas. This would help toward enhancing domestic circulation as well as achieving the government's rural revitalization goal.

China's recovery is expected to continue benefiting from the global rebound this year. Stable external demand remains crucial for supporting growth of industrial production in the near term. As domestic consumption gains pace, it's likely to become the key driver in the second half of the year. To achieve that, labor market and income stability is a prerequisite, and that relies on the recovery of services and vaccination progress. Policy support, especially for small and medium-size firms, is also critical to a persistent and balanced expansion through the year.

	Key indicators	Units	Moody's Analytics	Confidence	Risk	Last
Mon @ 10:00 p.m.	India Industrial Production for February	% change yr ago	1.0	3	←	-1.6
Mon @ 10:00 p.m.	India Consumer Price Index for March	% change yr ago	4.9	3	↑	4.8
Mon @ Unknown	China M2 Money Supply for March	% change yr ago	10.2	3	↑	10.1
Tues @ 1:00 p.m.	China Foreign Trade for March	US$ bil	103.3	3	↑	66.8
Wed @ 9:50 a.m.	Japan Machinery Orders for February	% change	2.6	3	↑	-4.5
Thurs @ 10:00 a.m.	South Korea Monetary Policy for April	%	0.5	4	←	0.5
Thurs @ 11:30 a.m.	Australia Unemployment Rate for March	%	6.2	2	←	5.8
Thurs @ 2:00 p.m.	Indonesia Foreign Trade for March	US$ bil	1.6	3	←	2.0
Thurs @ 10:20 p.m.	India Foreign Trade for March	US$ bil	-13.8	2	↓	-12.6
Fri @ 10:30 a.m.	Singapore Nonoil Domestic Exports for March	% change yr ago	4.7	3	↑	4.2
Fri @ 12:00 p.m.	China GDP for Q1	% change yr ago	18.5	3	↓	6.5
Fri @ 12:00 p.m.	China Industrial Production for March	% change yr ago	20.3	2	←	35.1
Fri @ 12:00 p.m.	China Retail Trade for March	% change yr ago	31.4	2	←	33.8
Fri @ 12:00 p.m.	China Fixed Asset Investment for March	% change yr ago YTD	27.9	3	←	35.0

The Long View

First-quarter 2021's US$-denominated bond offerings sank 9% yearly for investment-grade but grew 65% yearly for high-yield.

By John Lonski, Chief Capital Markets Economist, Moody's Capital Markets Research
April 8, 2021

CREDIT SPREADS

As measured by Moody's long-term average corporate bond yield, the recent investment grade corporate bond yield spread of 93 basis points was less than its 116 basis-point median of the 30 years ended 2019. This spread may be no wider than 105 bp by year-end 2021.

The recent composite high-yield bond spread of 323 bp approximates what is suggested by the accompanying long-term Baa industrial company bond yield spread of 131 bp but is much narrower than what might be inferred from the recent VIX of 17.1 points. The latter has been historically associated with a 475-bp midpoint for a composite high-yield bond spread.

DEFAULTS

February 2021's U.S. high-yield default rate of 7.9% was up from February 2020's 4.5%. The recent average high-yield EDF metric of 2.0% portend a less-than-3% default rate by 2021's final quarter.

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.

For 2019, worldwide corporate bond offerings grew 5.8% annually (to $2.456 trillion) for IG and advanced 51.6% for high yield (to $570 billion). The annual percent increases for 2020's worldwide corporate bond offerings are 19.7% (to $2.940 trillion) for IG and 23.9% (to $706 billion) for high yield. The expected annual declines for 2021's worldwide rated corporate bond issuance are 14% for investment-grade and 2% for high-yield.

U.S. ECONOMIC OUTLOOK

Unacceptably high unemployment and other low rates of resource utilization will rein in Treasury bond yields. A now-rising global economy, as well as forthcoming fiscal and monetary stimulus suggest the upper bound for the 10-year Treasury yield will be 2%. The corporate credit market has priced in the widespread distribution of a COVID-19 vaccine by mid-2021.

Europe

By Ross Cioffi of Moody's Analytics
April 8, 2021

GERMANY

In volume terms, factory orders in Germany increased by 1.2% m/m in February, signaling a healthy March release for industrial production. Global supply chain disruptions have caused delivery delays and surging producer input prices. All this is happening as demand muscles its way through ongoing lockdowns in Europe. As a result, German manufacturers, whose 4% m/m increase in domestic orders outweighed a 0.5% decrease in foreign orders, are building up their inventories to prepare for rising foreign and domestic demand despite issues on the supply side. Capital goods orders increased by 2.1% m/m in February while intermediate goods orders were up 0.5%. In yearly terms, capital goods orders were 5% higher and intermediate goods orders were 8.7% higher.

According to the manufacturing PMI, producer backlogs are ballooning, so the gains might not show in the March release. But the uptick in orders is a good sign for the economy as we head into the second quarter. Not only will investment in inventories help support GDP, but the increase in orders for capital goods also speaks to resilient demand for fixed investment. We caution against reading too much into factory orders, but they are in line with the PMI and other indicators that suggest investments are mitigating at least some of the damage from the ongoing pandemic in the first four months of the year.

EURO ZONE

Meanwhile, the euro zone construction PMI rose to 50.1 in March from 45 in February. This is the first reading above the break-even 50 score since February 2020, which signals a marginal increase in construction activity during the month. Homebuilding drove the increase in the survey while commercial construction disappointed again. The contraction registered in the commercial segment was the 13th in a row, although the pace of contraction continued to slow in March. Homebuilding led growth, but it was modest overall. The segment did better in Italy and France; in Germany, homebuilding declined. The industry will likely start recovering more solidly in April and May when the weather improves and European economies edge closer to reopening. New orders are already starting to grow, and employment demand has stabilized.

SWEDEN

Sweden's industrial production increased by 1% m/m in February after a 0.5% decline in January. In yearly terms, production expanded by 1.6% after no change in the previous month. Swedish manufacturers are benefiting from the drive to restock and prepare for reopening. This gave a boost to capital and intermediate goods during the month. The semiconductor shortage is still making itself felt, however, as output of other transport equipment remains a weak spot. Other transport equipment includes the production of vehicle parts and of vehicles such as planes and ships. The absence of conductors and other inputs is eating into production among major Swedish producers of other transport equipment such as Volvo and Saab, and the major foreign producers that many of Sweden's firms cater to.

NORWAY

Meanwhile, industrial output in Norway slumped by 1.2% m/m in February. Losses were registered across manufacturing industries such as food, machines and equipment, and refined petroleum products and chemicals. Falling energy output and oil and gas extraction steepened the decline in production. Despite this decrease, we expect industrial production to grow in the coming months. As lockdowns and social distancing restrictions ease at home and in Europe, demand for oil and other Norwegian goods will rebound. The same is true for Sweden, though supply issues will be a thorn in the side for both countries' producers.

Asia Pacific

By Katrina Ell and Shahana Mukherjee of Moody's Analytics
April 8, 2021

AUSTRALIA AND INDIA

Central bank meetings this week from Australia and India highlight how economies are experiencing divergent recoveries and challenges in 2021. The Reserve Bank of Australia and the Reserve Bank of India both kept their respective accommodative settings on hold in April. For the RBA, the recovery is progressing, and interest rates are not forecast to rise until 2024, as stubborn spare capacity will keep inflation and wage growth subdued. The near-term concern is the property market. For the RBI, the challenge is inflation and localized COVID-19 outbreak pockets driving fresh restrictions threating the recovery in domestic demand.

RBA HOLDS STEADY

The Reserve Bank of Australia kept all monetary settings steady in April. The cash rate was held at 0.1%, the target on the three-year government bond yield was maintained at 0.1%, and the parameters of the Term Funding Facility were left unchanged. The RBA struck a positive tone, noting that global and local growth had improved, and the outlook brightened. But it will be a while before the hefty monetary support is normalised given that low underlying inflation and stubborn labour market slack will keep wage growth subdued for some time.

Indeed, in the December quarter, wage growth came in at just 1.4% year over year, unchanged from the September quarter, but well down from the decade average of 2.6%. The RBA does not expect to see inflation back in the 2% to 3% range along with wage growth being substantially higher until 2024 at the earliest. We have pencilled in a slightly faster tightening of the labour market, and our baseline forecast is for the tightening cycle to begin in the second half of 2023, two to three quarters ahead of the RBA's expectations.

But there are near-term clouds. Treasury estimates that there were 1.1 million workers still receiving the wage subsidy JobKeeper payment in the first quarter, prior to it being removed late in March. We estimate that around 100,000 employees will lose their job with the end of this payment, equivalent to 0.8% of the labour force. We expect that the fall in net employment will be less as more than half are expected to find a new job within a short period. This will result in an increase in the June quarter unemployment rate and some wavering in consumer spending, but the broader economic recovery will help absorb more than half of these workers in the second half of 2021.

WARMING HOUSING MARKET IS A CONCERN

A notable change in the RBA's April statement was its stance on the property market. The RBA is more concerned about the pace of price growth this month and, specifically, ensuring that lending standards are maintained in this sustained low interest-rate environment. This concern is to be expected given that national home values were up 2.8% month over month in March, the fastest expansion since October 1988.

The uptick is mainly coming from owner-occupiers, which historically have been leveraged lower than investors. But if the housing market continues to heat up, we will see action from the regulator, likely via targeted measures such as loan-to-value restrictions, to ensure that lending standards are not wavering with the cheap availability of money.

INDIA ISN'T OUT OF THE WOODS

The Reserve Bank of India kept its monetary settings steady in April. The benchmark repo rate was held at 4%, while the reverse repo rate was kept unchanged at 3.35% in its April announcement.

A challenge for policymakers is the resurgence of COVID-19 cases, which threatens to disrupt the domestic recovery by ensuring households and businesses remain cautious. The most affected cities have introduced targeted restrictions including weekend shutdowns, but generally weak compliance has meant that their effectiveness is mitigated and increases the likelihood of more aggressive shutdowns ahead. Although vaccinations are expected to gain pace in the weeks ahead to mitigate transmission risks, a moderation in domestic demand is pencilled in for the next couple of quarters.

Another concern is inflation. Although inflation pressures have moderated in recent months, largely owing to softer food inflation, but supply-side pressures coming from fresh COVID-19 restrictions remain.

Ratings Round-Up

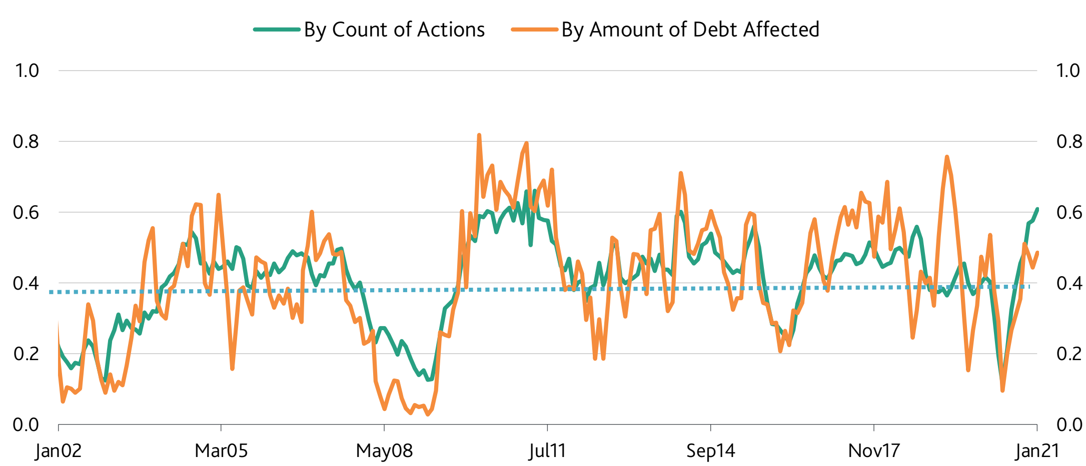
Latest U.S. Changes Are Credit Positive

By Steven Shields
April 8, 2021

U.S. rating change activity was credit positive in the latest period. For the week ended April 6, upgrades accounted for 86% of total changes and roughly three-quarters of the affected debt. Rating activity was confined to speculative-grade companies. This week's most notable upgrade was issued to Titan International Inc., with Moody's Investors Service upgrading the firms' senior secured credit and corporate family rating to Caa1 from Ca. The upgrades reflect Moody's expectations that favorable demand recovery in Titan's end markets, specifically agricultural equipment, will translate to a stronger adjusted EBITDA margin and material deleveraging in 2021. On April 5, Moody's Investor's Service upgraded Houghton Mifflin Harcourt Publishers Inc.'s senior secured and corporate family rating to B3 from Caa1. The change affected approximately $690 million in rated securities. According to the ratings action, the upgrades reflect Moody's expectation for a substantial reduction in HMH's financial leverage following an expected debt paydown after the close of its planned divestiture of HMH Book & Media business, coupled with the expectation of a faster than previously anticipated earnings recovery in 2021. The debt reduction will provide HMH with additional financial flexibility to execute its planned investment strategy and manage its exposure to the competitive and cyclical K-12 education market. The largest downgrade in terms of debt affected was issued to Nine Energy Service Inc. with its senior unsecured ratings lowered to Caa3 from Caa2. The company's outlook remains negative with the downgrade reflecting higher debt refinancing and restructuring risks.

Ratings activity was light across Europe with only two changes in the period. Paysafe Group Holdings II Limited's corporate family rating and senior secured rating was lifted to B1 from B3 following the closing of the SPAC transaction that resulted in its transition to a public company and a significant reduction in leverage. Moody's Investors Service downgraded DEMIRE Deutsche Mittelstand Real Estate AG's senior unsecured rating to Ba3 from Ba2 reflecting the company's limited financial flexibility and expectation that the company's credit ratios will weaken further.

FIGURE 1
Rating Changes - US Corporate & Financial Institutions: Favorable as % of Total Actions



* Trailing 3-month average
Source: Moody's

Ratings Round-Up

FIGURE 2

Rating Key

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

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	New STD Rating	Old LGD	New LGD	IG/ SG
3/31/21	NINE ENERGY SERVICE, INC.	Industrial	SrUnsec/LTCFR/PDR	400	D	Caa2	Caa3	SGL-2	SGL-3			SG
4/1/21	TITAN INTERNATIONAL, INC.	Industrial	SrSec /LTCFR/PDR	800	U	Ca	Caa1	SGL-4	SGL-3	LGD-4	LGD-3	SG
4/1/21	DAYCO, LLC-DAYCO PRODUCTS, LLC	Industrial	SrSec/BCF /LTCFR/PDR		U	Caa2	Caa1					SG
4/1/21	LUCID ENERGY GROUP II BORROWER, LLC	Industrial	SrSec/BCF /LTCFR/PDR		U	B3	B2					SG
4/1/21	CARROLL COUNTY ENERGY, LLC	Industrial	SrSec/BCF		D	Ba2	Ba3					SG
4/2/21	BUENA VISTA GAMING AUTHORITY	Industrial	SrSec /LTCFR/PDR	205	U	Caa3	Caa1					SG
4/5/21	HOUGHTON MIFFLIN HARCOURT COMPANY-HOUGHTON MIFFLIN HARCOURT PUBLISHERS INC.	Industrial	SrSec/BCF /LTCFR/PDR	306	U	Caa1	B3	SGL-3	SGL-2			SG
4/5/21	CENTURY ALUMINUM COMPANY	Industrial	LTCFR/PDR		U	Caa1	B3					SG
4/5/21	CPM HOLDINGS, INC.	Industrial	SrSec/BCF /LTCFR/PDR		U	Caa3	Caa2					SG
4/5/21	APTOS CANADA INC.	Industrial	SrSec/BCF /LTCFR/PDR		U	Caa1	B3			LGD-4	LGD-3	SG
4/6/21	BLOOMIN' BRANDS, INC.	Industrial	SrSec/BCF		U	Ba3	Ba2	SGL-3	SGL-2	LGD-3	LGD-2	SG
4/6/21	FETCH ACQUISITION LLC	Industrial	SrSec/BCF /LTCFR/PDR		U	B2	B1					SG
4/6/21	ENVEN ENERGY CORPORATION -ENERGY VENTURES GOM LLC	Industrial	LTCFR/PDR		U	Caa1	B3					SG
4/6/21	TI FLUID SYSTEMS PLC-TI GROUP AUTOMOTIVE SYSTEMS L.L.C.	Industrial	SrSec/BCF		U	B1	Ba3					SG

Source: Moody's

FIGURE 4
Rating Changes: Corporate & Financial Institutions – Europe

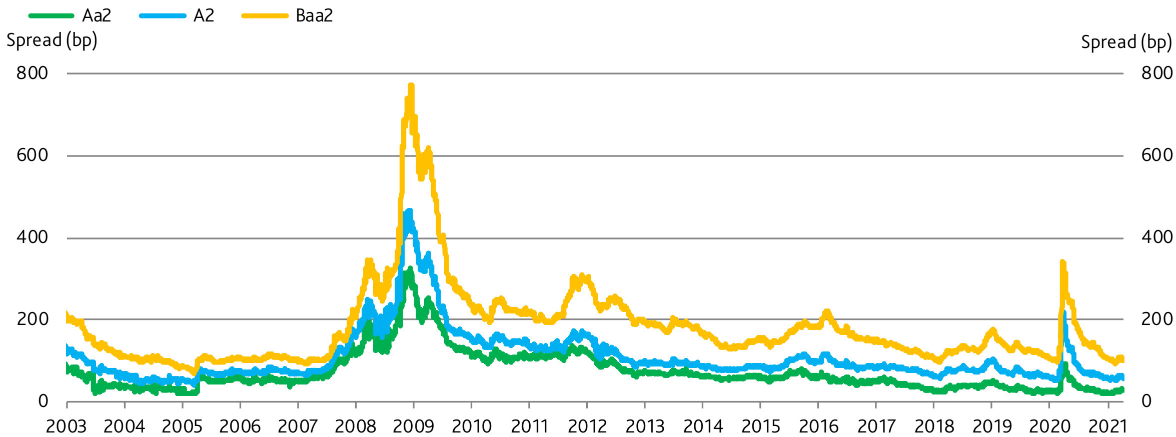
Date	Company	Sector	Rating	Amount ($ Million)	Up/ Down	Old LTD Rating	New LTD Rating	IG/ SG	Country
4/1/21	PAYSAFE GROUP HOLDINGS II LIMITED	Industrial	SrSec/BCF /LTCFR/PDR		U	B3	B1	SG	LUXEMBOURG
4/6/21	DEMIRE DEUTSCHE MITTELSTAND REAL ESTATE AG	Industrial	SrUnsec/LTCFR	706	D	Ba2	Ba3	SG	GERMANY

Source: Moody's

Market Data

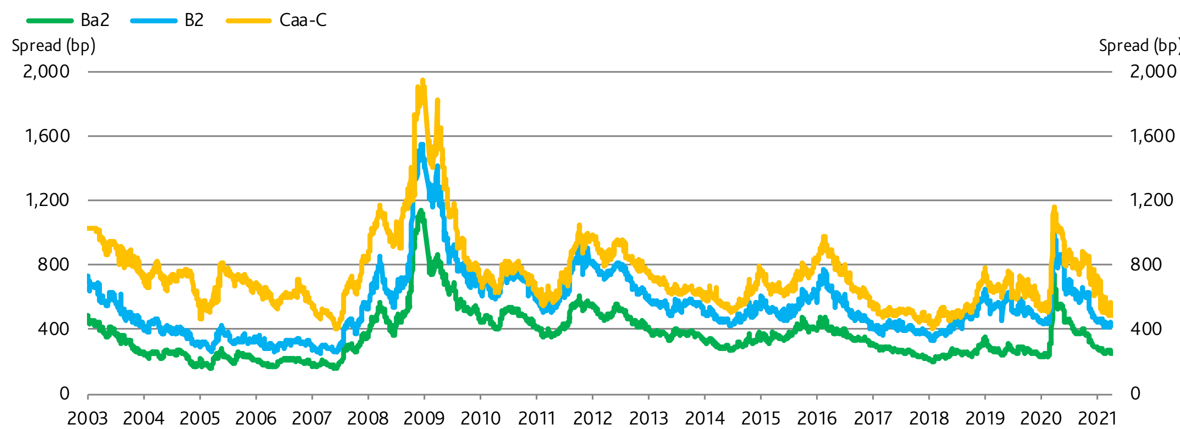
Spreads

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 (March 31, 2021 – April 7, 2021)

CDS Implied Rating Rises	CDS Implied Ratings		
Issuer	Apr. 7	Mar. 31	Senior Ratings
Carnival Corporation	B2	Caa2	B2
WEC Energy Group, Inc.	A3	Baa2	Baa1
TECO Energy, Inc.	A2	Baa1	Baa1
Philip Morris International Inc.	A2	A3	A2
Dish DBS Corporation	Caa2	Caa3	B2
Emerson Electric Company	Baa1	Baa2	A2
Republic Services, Inc.	A3	Baa1	Baa2
ConocoPhillips	Baa1	Baa2	A3
Royal Caribbean Cruises Ltd.	Caa2	Caa3	B2
Rite Aid Corporation	Ca	C	Caa3

CDS Implied Rating Declines	CDS Implied Ratings		
Issuer	Apr. 7	Mar. 31	Senior Ratings
Comcast Corporation	A2	Aa2	A3
Exxon Mobil Corporation	A2	Aa2	Aa2
International Business Machines Corporation	A2	Aa2	A2
Chevron Corporation	A2	Aa2	Aa2
General Mills, Inc.	A1	Aa1	Baa2
Kimberly-Clark Corporation	A1	Aa1	A2
XTO Energy, Inc.	A1	Aa1	Aa2
Toyota Motor Credit Corporation	Aa3	Aa1	A1
Apple Inc.	Aa3	Aa1	Aa1
Microsoft Corporation	Aa2	Aaa	Aaa

CDS Spread Increases		CDS Spreads		
Issuer	Senior Ratings	Apr. 7	Mar. 31	Spread Diff
Louisiana-Pacific Corporation	Ba2	129	120	9
JetBlue Airways Corp.	Ba3	400	392	7
Corning Incorporated	Baa1	97	93	4
The Terminix Company, LLC	B1	213	209	4
BorgWarner Inc.	Baa1	74	71	3
Kohl's Corporation	Baa2	123	120	3
Amazon.com, Inc.	A2	36	34	2
Pioneer Natural Resources Company	Baa2	75	73	2
Vulcan Materials Company	Baa2	78	75	2
Mohawk Industries, Inc.	Baa1	65	63	2

CDS Spread Decreases		CDS Spreads		
Issuer	Senior Ratings	Apr. 7	Mar. 31	Spread Diff
Carnival Corporation	B2	311	398	-87
Royal Caribbean Cruises Ltd.	B2	373	453	-79
American Airlines Group Inc.	Caa1	822	887	-65
Pitney Bowes Inc.	B1	435	479	-44
Dish DBS Corporation	B2	406	446	-41
Rite Aid Corporation	Caa3	687	726	-39
Realogy Group LLC	Caa1	403	441	-38
Delta Air Lines, Inc.	Baa3	266	298	-32
Staples, Inc.	B3	742	774	-32
Goodyear Tire & Rubber Company (The)	B2	251	283	-32

Source: Moody's, CMA

Market Data

Figure 4. CDS Movers - Europe (March 31, 2021 – April 7, 2021)

CDS Implied Rating Rises	CDS Implied Ratings		
Issuer	Apr. 7	Mar. 31	Senior Ratings
VERBUND AG	A1	A2	A3
Boparan Finance plc	Ca	C	Caa1
Novafives S.A.S.	Ca	C	Caa2
Stena AB	Caa3	Ca	Caa1
United Kingdom, Government of	Aaa	Aaa	Aa3
Germany, Government of	Aaa	Aaa	Aaa
Belgium, Government of	Aaa	Aaa	Aa3
Austria, Government of	Aaa	Aaa	Aa1
Barclays Bank PLC	A3	A3	A1
Netherlands, Government of	Aaa	Aaa	Aaa

CDS Implied Rating Declines	CDS Implied Ratings		
Issuer	Apr. 7	Mar. 31	Senior Ratings
Spain, Government of	A1	Aa1	Baa1
Societe Generale	A1	Aa1	A1
Banco Bilbao Vizcaya Argentaria, S.A.	A2	Aa2	A3
Lloyds Bank plc	A1	Aa1	A1
Danske Bank A/S	A1	Aa1	A3
BNP Paribas Fortis SA/NV	A1	Aa1	A2
UBS AG	A1	Aa1	Aa3
Vinci S.A.	A2	Aa2	A3
HSBC Bank plc	A1	Aa1	A1
RWE AG	A1	Aa1	Baa3

CDS Spread Increases		CDS Spreads		
Issuer	Senior Ratings	Apr. 7	Mar. 31	Spread Diff
Italy, Government of	Baa3	74	71	2
Unione di Banche Italiane S.p.A.	Baa1	69	67	2
NXP B.V.	Baa3	64	62	2
Vue International Bidco plc	Ca	627	625	2
Schaeffler Finance B.V.	Ba2	54	52	2
France, Government of	Aa2	17	17	1
Societe Generale	A1	34	33	1
Greece, Government of	Ba3	75	73	1
Banca Monte dei Paschi di Siena S.p.A.	Caa1	194	193	1
Fresenius SE & Co. KGaA	Baa3	59	57	1

CDS Spread Decreases		CDS Spreads		
Issuer	Senior Ratings	Apr. 7	Mar. 31	Spread Diff
Vedanta Resources Limited	Caa1	831	939	-108
Deutsche Lufthansa Aktiengesellschaft	Ba2	259	289	-30
Stena AB	Caa1	557	583	-26
Boparan Finance plc	Caa1	687	711	-23
Iceland Bondco plc	Caa2	377	398	-21
Ineos Group Holdings S.A.	B2	243	261	-18
Ardagh Packaging Finance plc	Caa1	202	218	-16
CMA CGM S.A.	B3	388	404	-16
Jaguar Land Rover Automotive Plc	B1	340	355	-15
Piraeus Financial Holdings S.A.	Caa3	500	515	-15

Source: Moody's, CMA

Market Data

Issuance

FIGURE 5

Market Cumulative Issuance - Corporate & Financial Institutions: USD Denominated

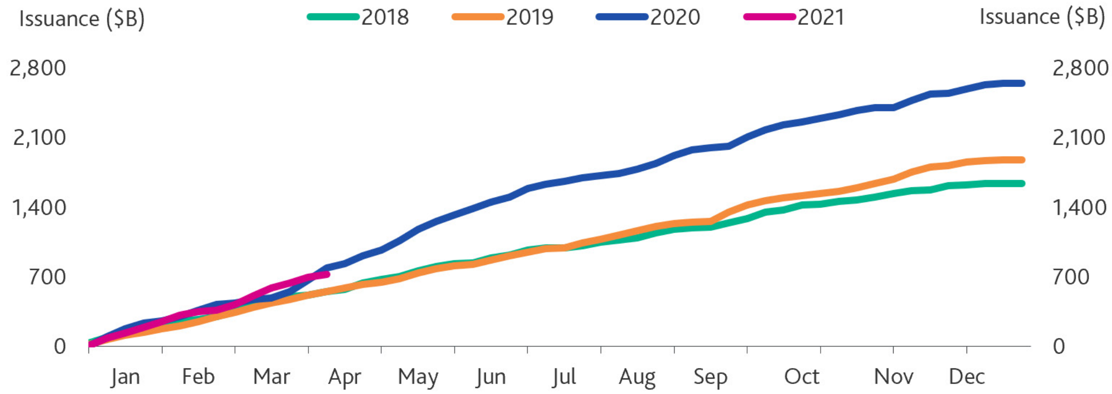
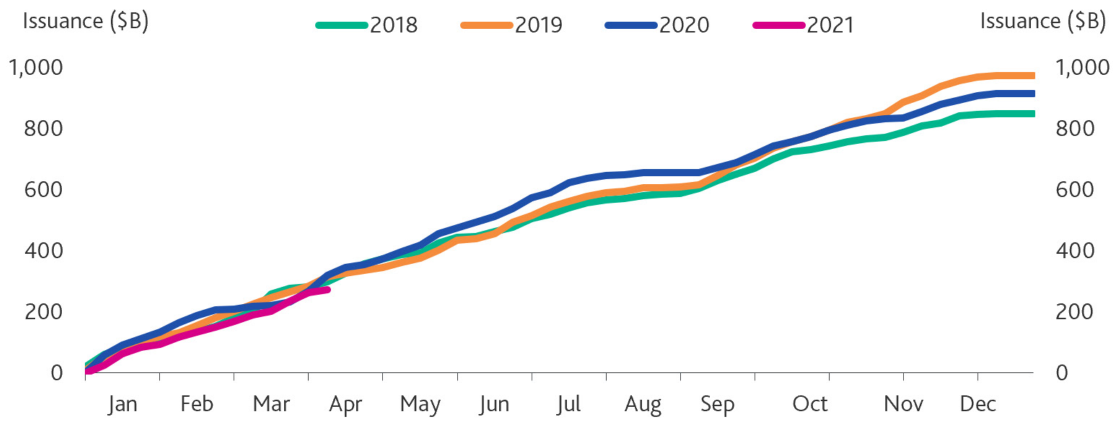


FIGURE 6

Market Cumulative Issuance - Corporate & Financial Institutions: EURO Denominated



Market Data

FIGURE 7

Issuance: Corporate & Financial Institutions

	USD Denominated		
	Investment-Grade	High-Yield	Total*
	Amount $B	Amount $B	Amount $B
Weekly	17.845	10.395	28.640
Year-to-Date	495.054	209.805	721.668

	Euro Denominated		
	Investment-Grade	High-Yield	Total*
	Amount $B	Amount $B	Amount $B
Weekly	7.528	0.618	8.146
Year-to-Date	218.104	42.775	271.171

* Difference represents issuance with pending ratings.

Source: Moody's/ Dealogic

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