S&P Global
Ratings

COVID-19 Weekly Digest

June 10, 2020

Key Takeaways

- Latin America COVID-19 deaths are still surging. For emerging markets generally, lockdowns are proving difficult to sustain, risking more damaging health and economic outcomes.
- Buoyant asset prices leave little room for error along a difficult path to recovery.

Contents

Key developments

Global COVID-19 death rates have started rising again as the epicenter of the epidemic has moved to Latin America and the Caribbean. Brazil currently has the highest weekly death toll globally, ahead of the U.S., with Mexico ranking third. This week, S&P Global Ratings published a report assessing how Brazilian Companies Are Struggling Under The Burden Of COVID-19. We have lowered 21 global scale and 17 national scale ratings, and revised 95 outlooks to negative on Brazilian corporations. About 65% of them retain a negative bias; utilities, infrastructure assets, transportation, and agribusiness companies have borne the brunt of the actions so far.

Our Emerging Markets Monthly Highlights report sets the wider context for EMs: Financial conditions and activity are improving, underpinned by central bank support, easing lockdowns, and ultra-accommodative policy in advanced economies. However, broad lockdown fatigue has taken hold, driven by mounting political pressures and economic costs, consequently risking undermining a recovery. India is a prime example, with the lockdown easing despite the growing prevalence of COVID-19 in major cities such as Mumbai. We now expect the Indian economy to contract sharply in 2020, by 5%.

Industries most affected by COVID-19 suffered further negative rating actions, encompassing hotels and travel (Accor, Hilton Grand Vacations, InterContinental Hotels Group), airlines (SAS, American Airlines, Alaska Air), airports (JFK International Air Terminal), and cinema (AMC Entertainment). S&P Global Ratings analysts published research assessing the outlook for heavily affected industries: Credit FAQ: Q&A: COVID-19 And The Auto Industry-What's Next? and COVID-19 Accelerates Structural Shifts In Global Office Real Estate And REITs.

In terms of how industry pressures translate to defaults, **we now expect the European trailing-12-month speculative-grade corporate default rate to rise to 8.5%** by March, from 2.4% in March of this year and 2.7% in April.

Unease at whether liquidity-inflated asset prices are disconnected from fundamentals remains a core concern, alongside the question of how resilient economies will be when stimulus efforts wind down. U.S. nonfarm payrolls offered succor with a welcome 2.5 million increase, regaining one-tenth of the jobs lost since March. Even so, grim data also continued to flow: German industrial production fell 25% year-on-year in April, exceeding the peak contraction of 22% in the global financial crisis. The longest ever U.S. economic cycle was officially marked over when the U.S. National Bureau of Economic Research declared that the world's biggest economy has been in recession since February.

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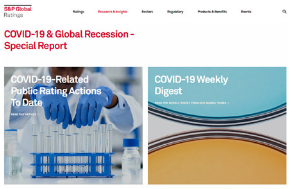
Links

Daily research updates, including a summary of related ratings actions, are available at:

https://www.spglobal.com/ratings/en/research-insights/topics/coronavirus-special-report



S&P Global Ratings acknowledges a high degree of uncertainty about the rate of spread and peak of the coronavirus outbreak. Some government authorities estimate the pandemic will peak about midyear, and we are using this assumption in assessing the economic and credit implications. We believe the measures adopted to contain COVID-19 have pushed the global economy into recession (see our macroeconomic and credit updates here: **www.spglobal.com/ratings**). As the situation evolves, we will update our assumptions and estimates accordingly.

Credit Market Update

Credit Market Research

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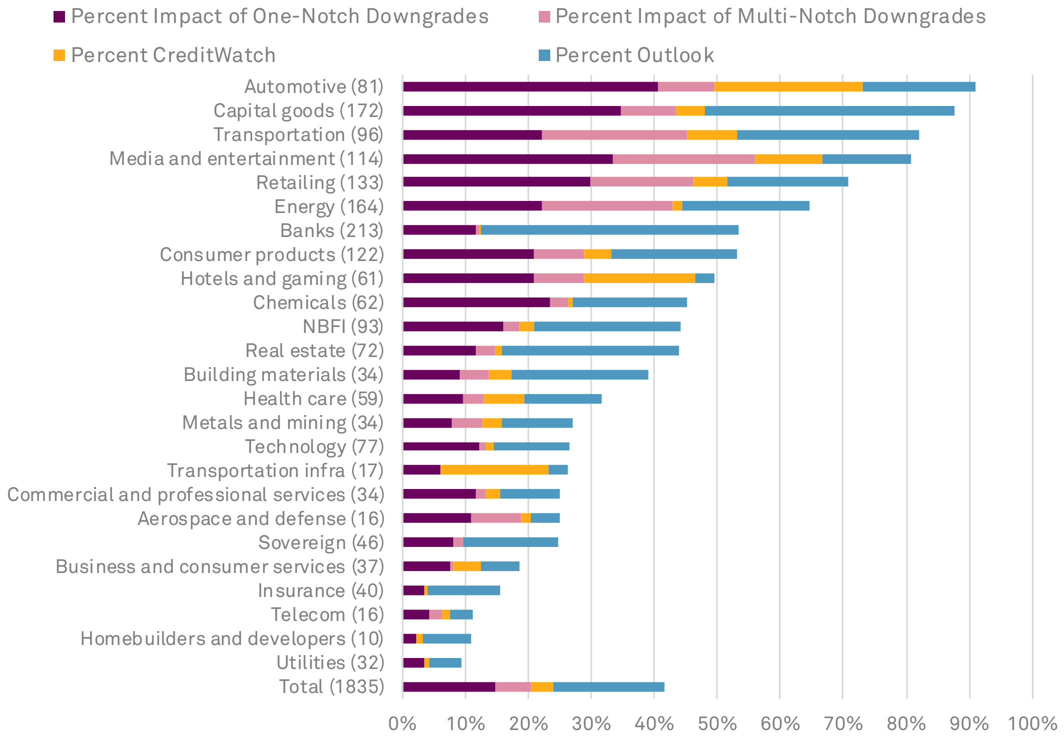
Ratings Trends

Chart 1

Percent of Issuers Downgraded Due To COVID-19 & Oil Prices By Sector



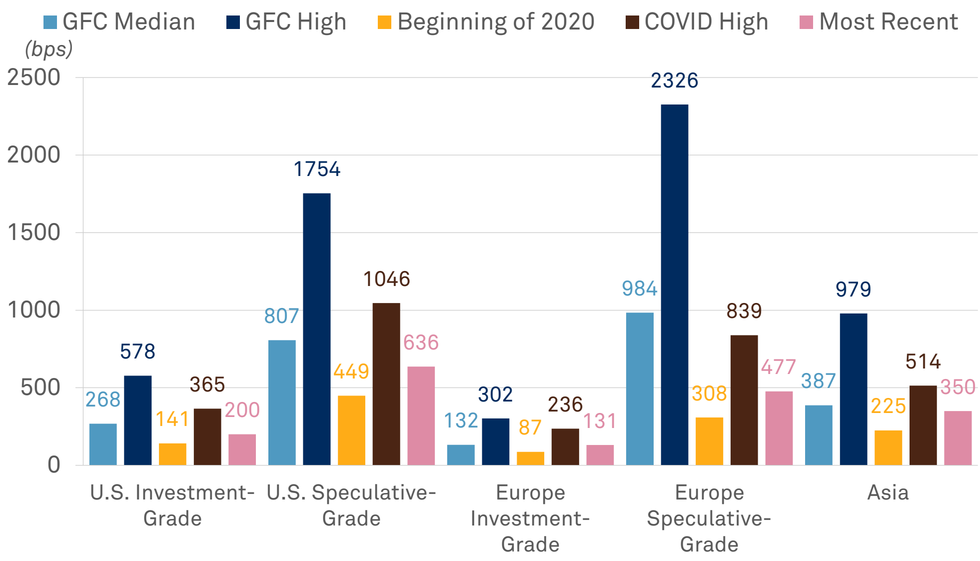
Source: S&P Global Ratings. Data as of June 9, 2020

- **S&P Global Ratings has taken 1789 negative rating actions** (as of June 9) on global corporate nonfinancial and financial issuers, including 878 downgrades, 749 outlook revisions to Negative, and 162 placements on CreditWatch with Negative Implications. The **downgrades** for **nonfinancial companies represent roughly 20% of the rated portfolio**, significantly higher than that of financial institutions (12%) and sovereigns (9%). By comparison, **structured finance saw roughly 3% of the rated portfolio experience negative actions**, primarily **negative CreditWatch placements**.
- Of the **54 rating actions this week** for corporate financial and nonfinancial issuers, the **bulk (74%) were on speculative-grade issuers**. Of those, 25 were downgrades, 14 were Negative Outlook revisions, and the remaining one was a Negative CreditWatch Placement. There was **one fallen angel this week**, namely Queens Ballpark Company (downgraded from 'BBB' to 'BB+', keeping its CreditWatch Negative Placement). Queens Ballpark Company is a real estate manager, owned by baseball team New York Mets and owns and operates New York's Citi Field. Companies with business in leisure activities and travel saw a marked decline in revenues as social distancing and travel restrictions have impeded their ability to do business, pressuring their creditworthiness in the process.
- **Banks dominated rating actions** in the past week with **ten**, largely as a result of the **Outlook revisions of the sovereigns of Japan (to 'A+'/Stable from 'A+'/Positive Outlook) and Uzbekistan ('BB-'/Negative Outlook from 'BB-'/Stable)**. Four Japanese banks saw single-notch downgrades while the remainder were Negative Outlook revisions. The **transportation sector** followed with more **airlines downgraded**, including Alaska Air Group ('BB+' to 'BB-', Outlook Negative) and SAS AB ('B+' to 'CCC'/CreditWatch Negative) following last week's downgrades of American Airlines and many European airlines in prior weeks.

Financing Conditions

Chart 2

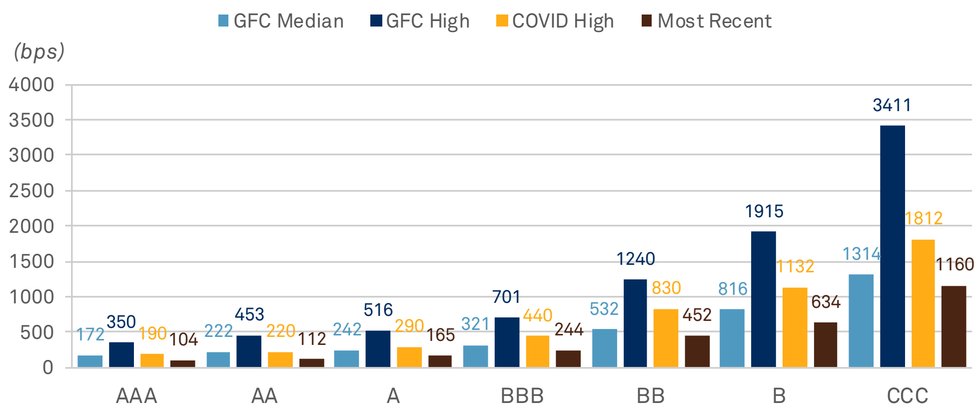
Secondary Market Credit Spreads, U.S. and Emerging Markets



Source: ICE Benchmark Administration Limited (IBA), 'ICE BofAML High Grade Emerging Markets Corporate Plus Sub-Index Option-Adjusted Spread', 'ICE BofAML Emerging Markets Corporate Plus Index Option-Adjusted Spread', 'ICE BofAML Asia Emerging Markets Corporate Plus Sub-Index Option-Adjusted Spread', 'ICE BofAML Latin America Emerging Markets Corporate Plus Sub-Index Option-Adjusted Spread', 'ICE BofAML Europe, the Middle East, and Africa (EMEA) Emerging Markets Corporate Plus Sub-Index Option-Adjusted Spread', retrieved from FRED, Federal Reserve Bank of St. Louis; https://fred.stlouisfed.org/series/BAMLEMRECRPIEMEAOAS, U.S. Investment-Grade and Speculative-Grade Spreads from S&P Global Ratings. June 9, 2020.

Chart 3

S&P Global U.S. Composite Spreads By Rating, Secondary Market



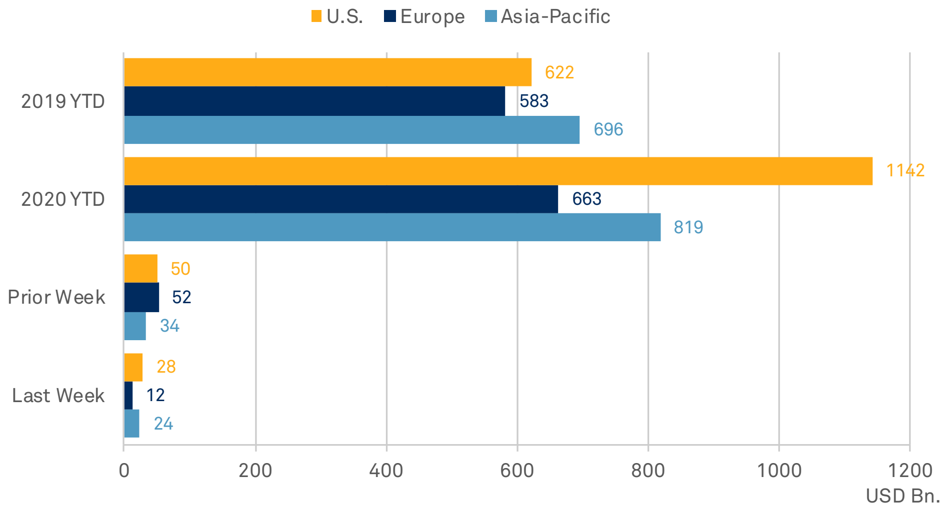
Source: S&P Global Ratings. Data as of June 9, 2020

- **Debt issuance.** Issuance slowed this week though new bonds total $2.8 trillion, nearly 40% higher than the volume at this time last year. Europe saw the first large LBO deal since the beginning of the crisis and global speculative-grade issuance is seeing demand, especially for 'BB' category deals.
- **Spread compression.** Spreads continue to compress across the curve, though there is still high vulnerability at the 'CCC' level where default risk is most pronounced. The gap between spreads on 'BBB' and 'BB' remains high (46% premium for 'BB' issuers) and roughly equal to that between 'B' and 'CCC' categories, while most other rating categories see roughly a 30% premium between each other. Ratings typically move in a continuum, though these distinct "shelves" are indicative of risk aversion for both potential fallen angels and weakest links.

Debt Capital Markets

Chart 4

Financial and Non-Financial New Bond Issuance



Source: S&P Global Ratings. Data as of June 2, 2020.

- **Global.** Low rates continue to ease capital costs and demand for 'BB' new issuance is gaining some traction, though riskier 'B' and 'CCC' categories still have little risk appetite.
- **Asia.** Market spreads continued to gradually converge toward normalcy, while primary market activity remained robust. Volumes were not as strong as last week.
- **Europe**. Market conditions remained conducive to new issuance, prompting some corporations to revisit the primary market and take advantage of comparatively lower capital costs.
- **U.S.** Amid strong issuance, credit spreads continued to tighten as rising oil prices, gradual reopening of the economy and Federal Reserve's support boosted market demand.

Asset Class Trends

Corporate

- During the week ending June 5, 2020, further notable downgrades included in hotels and gaming: Hilton Grand Vacations Inc. lowered to 'BB' from 'BB+' and remained on Watch negative; and InterContinental Hotels Group PLC lowered to 'BBB-'from 'BBB', with a negative outlook. There were four more defaults, 24 Hour Fitness Worldwide Inc., California Pizza Kitchen Inc. and Valaris plc on missed interest payments, and Noble Corporation PLC on a distressed debt purchase.
- New reports include highlighting how unprecedented employment challenges stemming from the coronavirus pandemic are rippling across the broader economy and affecting how employees operate and interact with their employers, see People Power: COVID-19 Will Redefine Workforce Dynamics In The Post-Pandemic Era, Jun 04, 2020. Also, in China, how total credit in China will rise about 14% in 2020, year on year, as the country uses debt to stimulate the economy, see China Debt After COVID-19: Flattening The Other Curve, Jun 04, 2020.

Banks and Financial Institutions

- Downgrade in the past week of one U.S. based non-bank financial institution, and outlooks on four Uzbek financial institutions revised to negative following a similar action on the sovereign.

Insurance

- Very limited rating actions over the last week.
- We continue to expect insurance related claims to be manageable but expect pressure on some business lines, for example event insurance, insured by Property & Casualty insurers and reinsurers over 2020. Future downside pressure will also stem from a prolonged macro-economic recovery, even lower for even longer interest rates, outsized exposure to speculative grade, CLOs, CMBSs and 'BBB' rated corporate bonds and any further financial market deterioration.

Sovereign

- On June 5, 2020, S&P Global Ratings affirmed **Uzbekistan**'s 'BB-' long-term rating and revised our outlook to negative from stable. Uzbekistan's fiscal and external debt levels have been increasing faster than we anticipated. We expect fiscal borrowing and the current account deficit will remain high in 2020 as the government funds investment and modernization plans and the fight against COVID-19. By year-end 2020, we estimate that the economy's liquid external assets will no longer cover gross external debt, as the government continues borrowing from abroad.
- On June 9, 2020, S&P Global Ratings revised its outlook on **Japan** to stable from positive. The outlook revision reflects increased uncertainty that Japan's general government debt could stabilize against nominal GDP in the next one to two years as fiscal performance deteriorates. We affirmed our 'A+' long-term sovereign credit rating on Japan.

Structured Finance

- **Global SF:** See "COVID-19 Activity in Global Structured Finance for the week ending May 29, 2020" published June 4, 2020.
- **US CMBS:** On June 3rd, ratings on 96 classes from 30 U.S. CMBS conduit transactions placed on CreditWatch Negative. The CreditWatch negative placements primarily reflect the subject bonds' exposure to the adverse impact of COVID-19 on the lodging and retail sectors, and the related uncertainty about the duration of the demand disruption. In our view, the subject bonds, which are primarily speculative-grade classes (i.e., rated 'BB+ (sf)' or lower) from the CMBS 2.0 cohort (80 of the 96 affected bonds; 27 of the 30 affected deals), are at an increased risk of experiencing monthly payment disruption or reduced liquidity.
- **US CLOs:** Watch a replay of our June 3rd webinar: "U.S. CLOs, Corporate Loans and COVID-19". Here is the link: "Replay US CLOs, Corporate Loans and COVID-19 Webinar".

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- Managers work to add value for investors in benign economic environments, as well as protect against downside risk during more turbulent times. The credit profile of U.S. CLO collateral pools has shifted more rapidly over the past several months than at any other point in the history of the CLO market. On average, U.S. BSL CLO managers have traded about 8.75% of their portfolio since early March, and reduced their 'CCC' and nonperforming loan exposures by about 1.23% at the cost of 21 bps in par (see "Under stress: assessing CLO manager performance during COVID-19" published June 1, 2020).
- **US Non-QM RMBS:** More than 70% of the properties backing loans in non-QM securitizations are in either California, Florida, or New York. California has the highest portion of self-employed borrowers, Florida has the highest average loan to value (LTV) ratio and lowest average FICO score, and New York has the highest COVID-19 exposure and the highest share of debt service coverage ratio (DSCR) loans as a percentage of loans in the state. Loan-level credit characteristics, along with the regional COVID-19 impact and early remittance data, suggest that the greatest credit sensitivity should be in New York, followed by California and Florida. Adverse credit behavior (as measured by reported delinquency information) is weighted in self-employed borrowers and DSCR loan borrowers (see "Non-QM RMBS And COVID-19: locking down states' exposure" published June 1, 2020).
- **US Auto ABS:** For the seven weeks ended April 25, 2020, approximately 33.5 million new jobless workers filed for unemployment. With the majority of newly unemployed or furloughed workers indicating that their job loss was temporary--likely the result of COVID-19 social distancing and containment measures--lenders responded by giving extensions to affected borrowers. As a result, US auto loan extensions (as reported in Reg AB II loan level reports) in auto loan ABS rose significantly in April relative to March (see "Will Spring U.S. auto loan extensions bring Summer payments?" published June 4, 2020). At the same time, delinquencies held stable, recovery rates on charged-off loans fell to record lows and losses rose (see U.S. Auto Loan ABS Tracker: April 2020 Performance, published June 4, 2020).
- **EMEA SF:** Our report includes a round-up of the latest credit developments that we've observed across EMEA structured finance sectors, along with data on recent EMEA rating actions and underlying performance indicators. We also highlight the key takeaways from our recent research publications (See "EMEA Structured Finance Surveillance Chart Book" published June 2, 2020).
- Watch a replay of our June 3rd webinar: "S&P Global Ratings LIVE: EMEA Structured Finance Market Updates –June 3, 2020". Here is the link: "Replay EMEA Structured Finance Market Updates -June 3, 2020 Webinar".
- **EMEA ABS and RMBS:** In order to assess how loan servicers across Europe are dealing with the unprecedented situation related to the COVID-19 pandemic, we have had discussions with servicers for European residential mortgage-backed securities (RMBS) and asset-backed securities (ABS) transactions to understand their business continuity plans and the nature and scale of disruption (if any). We have also looked at the rate of borrowers' payment holiday utilization and whether these will be reported as arrears (see "How European ABS And RMBS Servicers are managing COVID-19 disruption and Payment Holidays" published June 4, 2020).
- **Irish RMBS:** All lenders and servicers of the Irish RMBS transactions we rate are currently offering payment holidays to support borrowers facing economic hardship caused by COVID-19. Given the nature of the underlying collateral, Irish reperforming RMBS transactions are particularly vulnerable to performance deterioration, especially as there was already evidence of weak performance before the pandemic. We have performed a scenario analysis to examine the impact of a low, medium, and high shock on Irish reperforming RMBS. Our analysis shows that while 'AAA' to 'BBB' ratings should remain largely stable, 'B' and 'BB' rated tranches, which have less credit support to protect against performance deterioration and are more reliant on excess spread, are most at risk to rating changes (see "How Credit Distress Due To COVID-19 could affect Irish reperforming RMBS" published June 3, 2020).

U.S. Public Finance

- We are hosting a live webcast on June 11th: U.S. Public Finance Market Update.
- We have reviewed all U.S. state budgets and provided a 50 state review: Covid-19 Induced Recession Throws Curveball To U.S. State Budgets. We also published several state specific reports including California, Florida, Illinois, and New York which can be found here. We have done additional analysis on oil dependent states Oil Producing States Dealt Double Blow From Price Collapse and COVID-19.
- An update was provided by our Transportation Infrastructure team provides activity estimates across the transportation infrastructure sub-sectors and what it may mean for credit quality: Activity Estimates For U.S Transportation Infrastructure Show Public Transit And Airports Most Vulnerable To Near-Term Rating Pressure.
- Our not-for profit and corporate health care team provided an update on health care sector trends: A Bumpy Recovery Is Ahead For Hospitals And Other Health Providers As Non-Emergent Procedures Restart.
- We updated our U.S. Public Finance COVID-19 Rating Activity.

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