S&P Global
Ratings

Sector Roundup Asia-Pacific Q4 2021:

Improved Rating Trend Likely To Wane

Sept. 28, 2021

Key Takeaways

- **Negative rating bias**. Our net ratings bias has improved to negative 7% (previous quarter: negative 11%), its best level since the COVID-19 crisis broke. However, this momentum is unlikely to continue into the fourth quarter of 2021 given the slowing pace of economic recovery.
- **COVID-19 recurrence.** Despite higher vaccination coverage across Asia-Pacific, COVID outbreaks have resurged. Continuing or further lockdowns and social distancing restrictions would further drag on the rate of recovery. This could also disrupt supply chains, from upstream semiconductor chips-assembling in countries such as Malaysia, to downstream chip-users such as the auto, consumer product, retail, and tech sectors.
- **China's policy shifts**. The country's toughening socioeconomic policy has heightened uncertainty over the trajectories of credit and GDP growth in China. This may have consequences for the business models of domestic sectors with spillover effects to issuers outside the country dependent on China for exports or supplies.

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This report does not constitute a rating action.

Rating outlook bias. The ratings of a net negative 7% of Asia-Pacific issuers are on negative outlook or CreditWatch with negative implications (as at end-August 2021). While this ratio has been improving over several quarters, the momentum is unlikely to continue toward end-2021. This is because new COVID outbreaks have slowed economic activity, and China's recent policy heightens investment uncertainty. For instance, rattled investor confidence from China Evergrande Group's recent troubles and likely default could spell a potential funding crunch for the Chinese property sector and speculative-grade issuers, adding to downside pressure on our outlook bias.

Delta variant unwinds progress. The economic recovery from a COVID-driven trough has benefited a number of sectors. However, downside rating risk persists heading into the fourth quarter of 2021 (see "COVID, China Risks Won't Pass For Years, Say Panelists," published on RatingsDirect on Sept. 9, 2021). Indeed, the recovery path has become less certain. This week we revised down our growth expectations for Asia-Pacific (see "Economic Outlook Asia-Pacific Q4 2021: Growth Slows On COVID-19 And Rising China Uncertainty," Sept. 27, 2021). Consequently, most issuers won't likely recover to pre-COVID credit metrics until well into 2022.

China rewinds policy. On the health front, China is sticking to its "zero tolerance" strategy, which is introducing additional burdens for corporates, particularly those in mobility-sensitive sectors such as travel and retail. On the policy front, we see authorities emphasizing "common prosperity" principles and signaling intentions to curb state support. Sharper government scrutiny of property-sector risks has tightened refinancing conditions, in turn weakening liquidity positions for some developers. A liquidity crunch or downturn in the sector could derail a recovery in interlinked sectors such as building materials (see "China Developers Battle Tight Liquidity And Plummeting Profitability," Sept. 6, 2021). This, on top of recent regulatory crackdowns in education services, the technology sector and gaming signal more policy uncertainty to come.

Financial institutions: Outlook is mixed across banking jurisdictions. The impact of COVID-19 continues to weigh heavily on banks, with regional divergences growing apparent. Although support from public authorities has contained damage (our net rating outlook bias has also improved to negative 1% from negative 6%), downside risks remain as the region contends with further infections. We estimate that credit losses will rise by about an additional US$563 billion in 2020-2022, mainly because of COVID-19 stresses, compared with 2019 levels.

Insurance: Restored capital buffers absorb volatility. A resilient premium recovery continues. Against the backdrop of low interest rates and market volatility, insurers' credit and market risk appetite will likely increase. The sector is still vulnerable to intensifying capital market turmoil, and a continued resurgence of infections that could derail demand for insurance coverage.

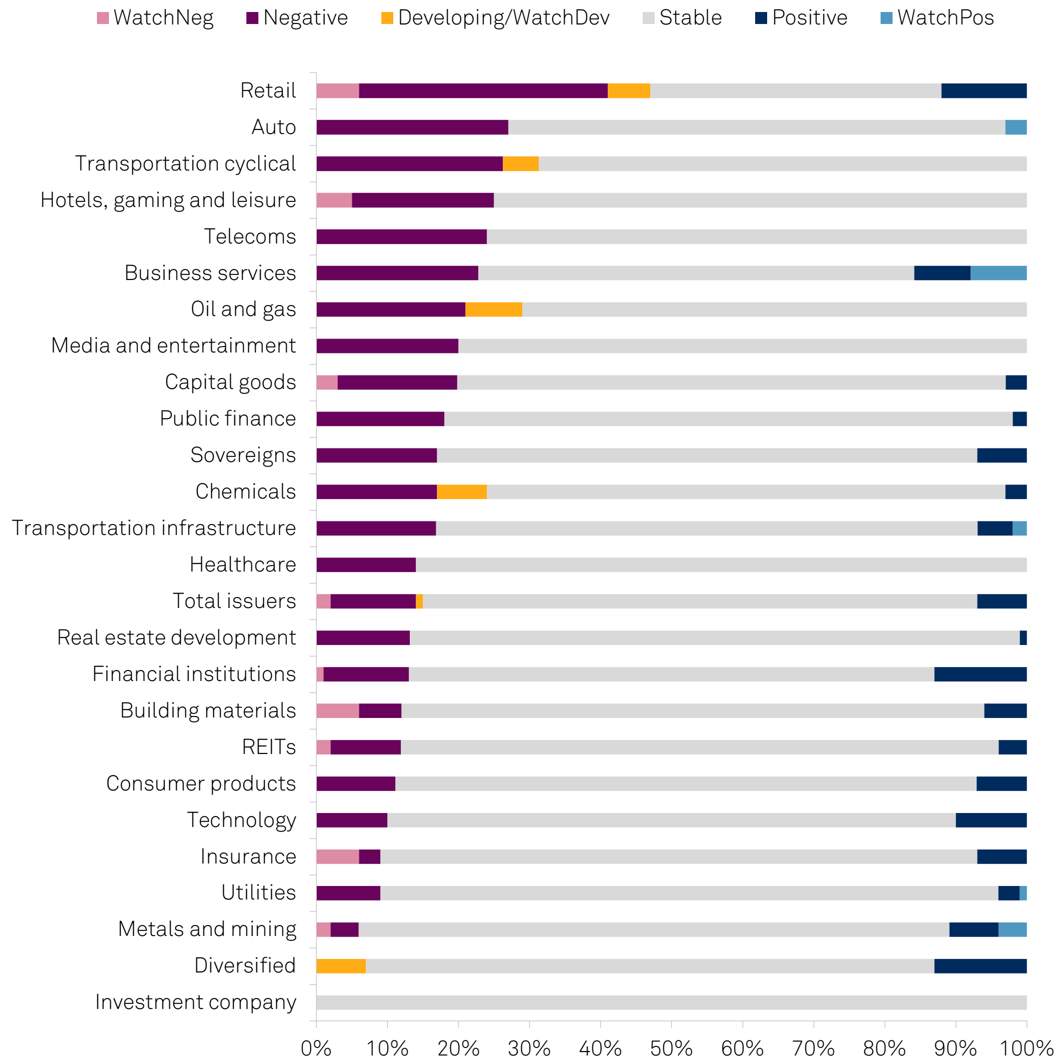
Public finance: Policy steps to contain COVID effects. Public spending across the region remains elevated to keep infection waves at bay while sustaining economic recovery. Meanwhile in China, local and regional governments (LRGs) are likely to benefit from additional credit buffers in expectation of tightening control over public finances and higher demand for local fiscal discipline.

Sovereigns face risks to external demand. Consumer prices have ticked up in Europe and the U.S., and pressures on policy rates may exacerbate if inflation shows no sign of abating. Uncertainties on the external front, from semiconductor chip shortages to container shipping bottlenecks, could derail the export-driven rebound. Setbacks for the recovery of sovereign credit metrics could include the emergence of new COVID-19 variants, sudden capital swings leading to swift capital outflows, and a dampened manufacturing recovery.

Structured finance: Resilient households and buoyant issuance. Stable employment outcomes across most markets have propped up household balance sheets in Asia-Pacific. However, any signs of worsening virus trends could drag on consumer confidence. Moreover, we question whether regulatory interventions can effectively contain pockets of asset price inflation in the region. New originators, low interest rates, and changing regulatory landscapes may shift risk profiles across structured finance markets in Asia-Pacific.

Chart 1

Outlook Distribution Of Asia-Pacific Issuers By Sector



Data cut-off: Aug. 31, 2021. Source: S&P Global Ratings.

Table 1

Net Outlook Bias of Asia-Pacific Issuers by Sector, August 31, 2021

	Aug. 2020	Oct. 2020	Mar 2021	May 2021	Aug 31 2021	No. of entities	Notional average rating
Auto OEM and suppliers	-67%	-65%	-45%	-42%	-24%	33	BBB
Building materials	-20%	-13%	7%	0%	-6%	17	BBB-
Business services	-36%	-42%	-25%	-21%	-8%	13	BB+
Capital goods	-15%	-19%	-24%	-19%	-17%	36	BBB
Chemicals	-46%	-31%	-26%	-20%	-13%	30	BBB-
Consumer products	-21%	-18%	-13%	-3%	-4%	27	BBB
Diversified	-13%	-13%	-7%	0%	13%	15	A-
Healthcare	-38%	-38%	-29%	-14%	-14%	7	BB+
Hotels, gaming and leisure	-67%	-44%	-42%	-45%	-25%	20	BB+
Investment company	-20%	-10%	0%	-11%	0%	8	A-
Media and entertainment	-22%	-44%	-40%	-22%	-20%	10	BBB+
Metals and mining	-22%	-24%	-17%	-9%	5%	55	BB+
Oil and gas	-39%	-39%	-24%	-16%	-21%	24	BBB+
Real estate development	-11%	-12%	-9%	-13%	-12%	75	BB-
Real estate investment trusts	-22%	-18%	-16%	-11%	-8%	52	BBB+
Retail	-38%	-22%	-29%	-29%	-29%	17	BBB-
Technology	-20%	-20%	-11%	-8%	0%	51	BBB-
Telecommunications	-26%	-33%	-25%	-26%	-24%	29	BBB+
Transportation cyclical	-40%	-40%	-42%	-32%	-26%	19	BB+
Transportation infrastructure	-31%	-29%	-27%	-20%	-10%	60	BBB+
Utilities	-6%	-4%	-5%	-2%	-4%	91	A-
Total corporates	**-25%**	**-23%**	**-19%**	**-15%**	**-10%**	**689**	**BBB**
Financial institutions	-17%	-18%	-15%	-6%	-1%	376	BBB+
Insurance	-4%	-8%	-4%	-3%	-2%	177	A
Public finance	-10%	-12%	-20%	-19%	-16%	90	A+
Sovereign	-10%	-10%	-17%	-14%	-10%	29	BBB+
Total issuers	**-19%**	**-19%**	**-16%**	**-11%**	**-7%**	**1,361**	**BBB+**

Note: We calculate the net outlook bias by deducting the percentage of negative outlooks and CreditWatch negative listings against the percentage of positive outlooks and CreditWatch positive listings. A minus figure indicates that the former exceeds the latter, and a positive figure, vice versa. OEM--Original equipment manufacturer.

Light blue colored cells indicate improvement from prior period, navy blue, deterioration.

Table 2

Summary of Key Risks And Assumptions For Asia-Pacific's Industries

Sector	Key risks	Key assumptions
Autos	Supply-chain disruption Heightened cost pressure	Gradual and uneven recovery in global sales
Building materials	New infections and ineffective vaccines Sharper global slowdown, slower recovery	Recovery to continue Curtailed capital expenditure and investment
Capital goods	Back to slower recovery Aggressive spending for growth and shareholder returns	Debt to EBITDA slightly improves toward 2022
Chemicals	China fails to bounce back Volatile oil prices	Chemical sector to remain exposed to macro weaknesses in the region
Consumer products	COVID-19 variant strike Higher input costs	Weaker consumption
Financial institutions	A downturn that is more severe than our base case Leverage, corporate insolvencies, and property	Strong economic rebound Highly supportive governments
Gaming	Uncontrolled COVID-19 cases Regulatory risks	Gaming visitation to remain solid in the long term Digital gaming and online casino earnings growing for certain Australian and New Zealand operators
Insurance	Intensified capital market turmoil COVID resurgence risk persists	Asset risk will rise
Media and entertainment	Speed of economic recovery and intensity of regulatory actions. Liquidity crunch	Advertising revenues to rebound in 2021
Metals and mining	Demand risk for commodities Financial policy Environmental, social, and governance (ESG) factors	Commodity markets to normalize
Oil and gas	Prolonged pandemic Structural change in oil demand	Brent at US$65/barrel for 2021 and US$60/barrel for 2022 Long-term overhangs for oil and gas
Public finance	Public spending stays high to sustain economic momentum Contagion fears weigh on recovery prospects	Few signs that governments will pull back their countercyclical measures Public finance systems largely remain stable across the region
Real estate development	Property sales slowdown in China Renewed risks for developers with weaker funding	Slower recovery and sales
Real estate investment trusts	Secular change for office Shorter lease term will test landlords' stability	Rental pressure could continue
Retail	New infection waves Higher input prices and supply-chain constraints	Challenging deleveraging paths
Sovereign	More COVID-19 variants Sudden capital swings Dampened manufacturing recovery may weigh on growth and fiscal recovery	Global economic activity will recover without major volatility

Summary of Key Risks and Assumptions for Asia-Pacific's Industries (cont.)

Sector	Key risks	Key assumptions
Structured finance	Virus resurgence and threat to consumer confidence Asset price inflation and effectiveness of regulatory "handbrakes"	Structural supports
Technology	Uncertain COVID-19 trajectory and aggressive capital expenditures Faster technology shifts	Further acceleration in global IT spending
Telecommunications	Intense competition Deeper recession	Mergers and restructurings
Transportation cyclical	Liquidity crunch High uncertainty over the recovery of travel patterns	Global air traffic won't return to normal until 2024
Transportation infrastructure	Weakened government fiscal positions dampen support Elevated macro and geopolitical risks	Lasting damage Some flexibility in capital expenditure
Utilities	Unwinding of economic support and infection resurgence Pace of new investments and funding may slow	Profitability will see mixed trends across markets Capital expenditure growth to resume

Auto

Negative Bias Likely To Moderate As Sales Recovery Continues

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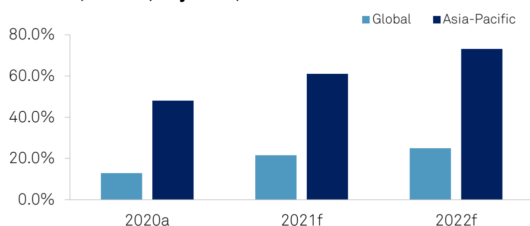
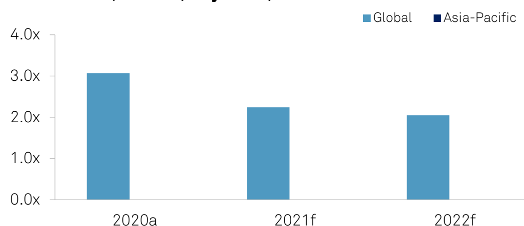
FFO/Debt (Median, Adjusted)



Debt/EBITDA (Median, Adjusted)



Source: S&P Global Ratings. All figures are converted into U.S. dollars using historical exchange rates. Forecasts are converted at the last financial year-end spot rate. FFO--Funds from operations. a--Actual. f--Forecast.

Key Takeaways

- Backed by a recovery in global car sales, negative rating bias in Asia-Pacific auto companies is likely to moderate over the next one to two years.
- Some pressure on cash flows will remain due to a prolonged semiconductor chip shortage, material price hikes, and high research costs for new technologies such as electrification.
- Asia-Pacific automakers still retain generally solid financial standing with low debt.

What's changed?

Negative rating pressure is moderating. Our base case assumes global light-vehicle sales will grow 8%-10% year over year in 2021 and 3%-5% in 2022. This is after a 15% drop in 2020. Automakers' strategic efforts, such as cost reduction and new model rollouts, are also decreasing credit downside risk.

Key risks

Supply chain disruption. Due to the recent semiconductor shortage, Toyota and Honda already lowered their annual production target by 3%-4%. Although those companies maintain their initial earnings guidance and expect solid sales recovery over the next one to two years, more lockdowns could drag on earnings.

Heightened cost pressure. Higher prices for precious metals and other raw materials could significantly hurt earnings of select Asia-Pacific automakers. Earnings pressure could also arise due to the heavy financial burden of implementing electrification strategies.

Key assumptions

Gradual and uneven recovery in global sales. China is likely to register growth of 5%-9% in 2021 and 2%-4% in 2022. We expect U.S. light-vehicle sales to rise by 14%-16% year over year to over 16 million in 2021 and stabilize at that level. In Europe, we forecast a protracted recovery in 2021 (9%-11%) after a 21% decline in 2020.

What to look for

Signs of cash flow stability. A number of factors could weigh on profitability and cash flows over the next two years. These include components shortages, material price hikes, inflexible research costs and capital expenditure, and an increasing number of lower-margin non-internal combustion engine vehicles. How Asia-Pacific automakers manage the pressure on free operating cash flow is an increasingly important analytical focus amid an uncertain operating environment.

Building Materials

Sustainability Of Demand Growth Key To Credit Quality

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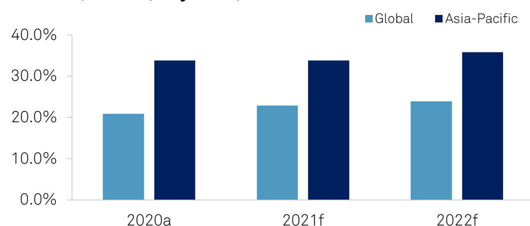
FFO/Debt (Median, Adjusted)



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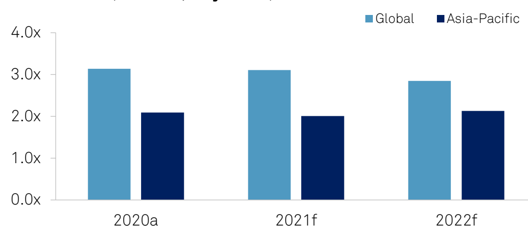

Source: S&P Global Ratings. All figures are converted into U.S. dollars using historical exchange rates. Forecasts are converted at the last financial year-end spot rate. Includes "Forest products, building materials, and packaging" entities.
FFO--Funds from operations. a--Actual. f--Forecast.

Key Takeaways

- Amid continued uncertainty about COVID, the sustainability of economic recovery will be the key driver for the sector.
- Rising liquidity risks and the Chinese government's closer scrutiny of property developers may slow construction of new projects, retarding demand for building materials.
- Overcapacity, especially in China, may be a structural risk lasting beyond 2021.

What's changed?

Rising cases of COVID-19 variants. Uneven vaccination progress globally and rebounding COVID cases in some countries will polarize demand outlooks. Though slower than we previously expected, the economic recovery in Asia-Pacific will still support the credit quality of our rated building materials companies.

Key risks

New infections and ineffective vaccines. Rising cases in some countries, including in Asia-Pacific, may extend lockdowns or trigger fresh ones, dragging on demand for building materials. Though vaccinations are progressing, effectiveness of vaccine types is still being tested, and new variants complicate the situation.

Sharper global slowdown, slower recovery. Further drags on the global economic recovery could strain prices and demand for building materials. In China, another demand drag could come from the tougher financing and liquidity environment for Chinese property developers. This adds to limitations for building materials, such as overcapacity in China.

Key assumptions

Recovery to continue. While our economists have lowered their initial forecasts for 2021, they still expect Asia-Pacific economies to expand by 6.7% in 2021. Our base case assumes that as vaccination rollouts proceed, economic activity will gradually improve, boosting demand for building materials.

Curtailed capital expenditure and investment. Companies are likely to restrain their capital expenditure and acquisitions over the next two years as they remain cautious about the recovery. Therefore, we forecast largely stable debt levels and operating cash flows for Asia-Pacific building material companies over the same period.

What to look for

COVID containment and vaccines. The pandemic's global path and the effectiveness of vaccines remain the ultimate determinant of economic recovery and demand for building materials. Oversupply and liquidity risks persist for smaller players, particularly in China.

Capital Goods

Receding Expectations For A Faster Recovery

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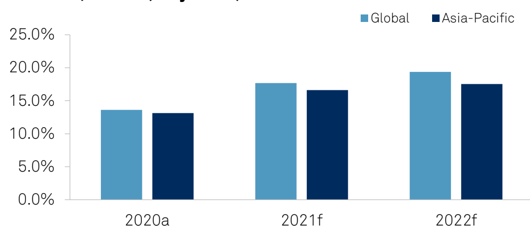
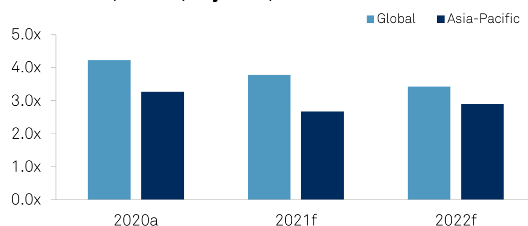
FFO/Debt (Median, Adjusted)



Debt/EBITDA (Median, Adjusted)



Source: S&P Global Ratings. All figures are converted into U.S. dollars using historical exchange rates. Forecasts are converted at the last financial year-end spot rate.
FFO--Funds from operations. a--Actual. f--Forecast.

Key Takeaways

- We still expect a recovery in earnings and steady leverage for Asia-Pacific capital goods companies.
- Key risks include further slowing in the recovery path, or more hikes in material prices.
- Growing investment and shareholders' return would also undo some of the improvement on leverage compared with 2020.

What's changed?

The net negative bias in ratings remains elevated. Our net negative bias improved marginally to negative 17% from negative 19% a quarter earlier. In other words, the underlying credit trend remains unchanged at slightly improving for Asia-Pacific capital goods companies, in our view. Overall, recent earnings results were strong.

Key risks

Back to slower recovery. The recovery in corporate spending could undershoot our current expectations should vaccination rollouts in Asia-Pacific face delays, or further waves of COVID-19 hit, in line with high COVID-19 caseloads globally. Even in China, where the COVID caseload is relatively low, government restrictions will constrain corporate activities. Rising costs related to materials and freight are another matter to weigh on profitability.

Aggressive spending for growth and shareholder returns. Because of the recovery in earnings and cash flow, companies have already restarted (previously suspended) capital expenditure alongside other growth-focused investments. They may also return dividends to pre-COVID levels or restart share buybacks. Given the risk of further pandemic-related disruptions, such initiatives may delay the recovery in credit metrics.

Key assumptions

Debt to EBITDA slightly improves toward 2022. We assume recovery in global economies will lead to an increase in corporate capital investment, benefiting the recovery in earnings across Asia-Pacific capital goods companies. Leverage will improve only moderately despite increasing capital spending across the sector, given that some of our rated companies will also significantly increase investments.

What to look for

Financial policy. Recovery in credit metrics and credit quality will depend on companies' financial policies. If the earnings recovery is much slower than our assumptions, adherence to a disciplined financial policy would be the more important credit driver. We are watching how such policies may play out, particularly if such initiatives can protect credit quality from the negative effect of increased capital spending.

Chemicals

Expanding Capacity Remains An Overhang

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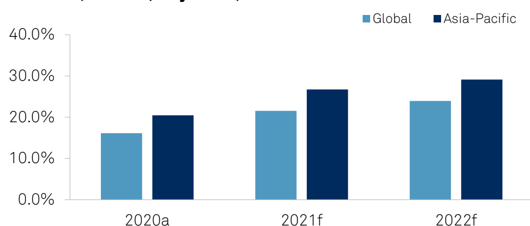
FFO/Debt (Median, Adjusted)



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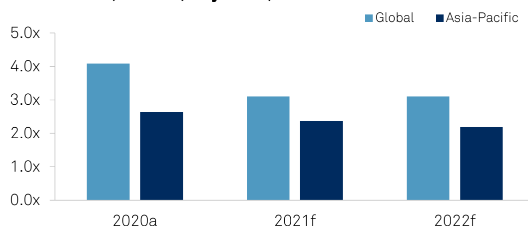

Source: S&P Global Ratings. All figures are converted into U.S. dollars using historical exchange rates. Forecasts are converted at the last financial year-end spot rate.
FFO--Funds from operations. a--Actual. f--Forecast.

Key Takeaways

- Polymer spreads have remained bearish as major U.S. crackers resume operations, following seasonal turnarounds.
- With the regional economic recovery losing some momentum due to COVID resurgence, we expect spreads to remain below mid-cycle levels.
- Ample global capacity expansion over the next two to three years will also constrain improvement in chemical spreads.

What's changed?

COVID's comeback. Led by India and Southeast Asian countries, rising COVID infections have squeezed petrochemical demand in the region. Given the overhang of global capacity expansion plans, combined with limited visibility in demand pickup, we expect petrochemical spreads to remain strained. Supply outpaces demand in the sector. As the pandemic continues to aggravate regional economic conditions, we remain skeptical of a sustained and widespread recovery in the regional chemical sector.

Key risks

China fails to bounce back. Considering that China is the global demand driver for petrochemical goods, any unforeseen economic slowdown could further weaken the sector's supply-demand balance.

Volatile oil prices. Big oil price moves--up or down--could pose risks to chemical producers. Entities may not be able to pass on a sharp oil price hike to buyers of chemical products. Meanwhile, a sharp decline in product prices could sideline buyers as they wait for the market to bottom before resuming their purchases.

Key assumptions

Chemical sector to remain exposed to macro weaknesses in the region. The pandemic has been particularly hard on the chemical sector, but our net ratings bias for Asia-Pacific chemical issuers has improved to negative 13%. This compares with negative 46% a year ago.

What to look for

Polymer spreads to remain subdued amid supply gluts and slack demand. We expect petrochemical product spreads to show limited recovery over the next 12 months as the supply glut persists. That's our base case. Keep in mind, however, that movements in this industry can be swift. If the pandemic abates, demand could quickly improve.

Consumer Products

Higher Costs And Weak Demand Will Dampen Discretionary Sales

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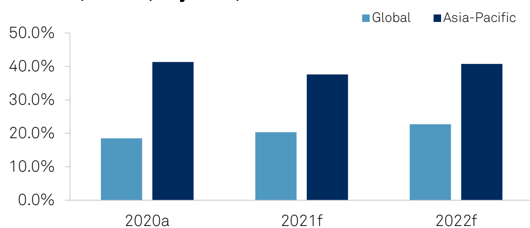
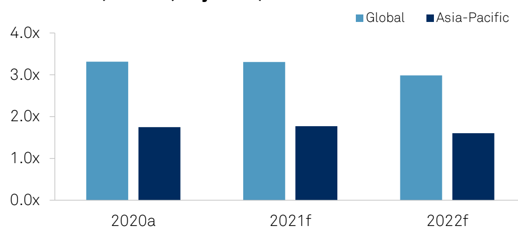
FFO/Debt (Median, Adjusted)



Debt/EBITDA (Median, Adjusted)



Source: S&P Global Ratings. All figures are converted into U.S. dollars using historical exchange rates. Forecasts are converted at the last financial year-end spot rate. FFO--Funds from operations. a--Actual. f--Forecast.

Key Takeaways

- COVID resurgence appears to be dampening consumer sentiment and could further delay the recovery in consumption.
- Supply chain disruptions, elevated material costs, coupled with weak consumer demand in the region will lead to fiercer competition.
- Credit quality will depend on balance sheet strength, brand equity, market position, ability to pass through cost increases, and access to liquidity.

What's changed?

Logistics disruption. Lockdowns and stricter quarantine measures at shipping terminals and airports, especially in China, following the delta variant outbreak will add to operating costs for consumer product firms. This together with higher material costs will further compress margins. Margin pressure will be higher for product segments reliant on trade and those with weaker ability to pass on cost increases, such as smaller brands or private-label manufacturers.

Key risks

COVID-19 variant strike. New lockdowns and restrictions across Japan, China, and Australia could temper recoveries in discretionary sales and food services. Countries with low vaccination rates will feel more pain as the government enforces strict lockdowns given their more fragile conditions after previous waves.

Higher input costs. Rising material prices are squeezing margins for mid-stream food processors across grain, oilseed, and packaged meat. Credit metrics for hog producers in China are weakening as they face tumbling prices, and higher costs amid new capital expenditure cycle.

Key assumptions

Weaker consumption. Struck by COVID-19 variants and slow vaccination, consumption could be hit again following stricter virus control measures. Discretionary goods sales in China, Japan, Australia, and Korea may face new setbacks, while India and Indonesia won't likely return to pre-COVID levels until 2023.

What to look for

Access to funding and unemployment. Entities' operating controls and their ability to manage liquidity will be a key differentiator of credit quality. The speed of vaccine rollouts and the persistence of high unemployment in some markets will be important to consumer confidence and company performance.

Financial Institutions

Outlook Is Mixed Across Banking Jurisdictions

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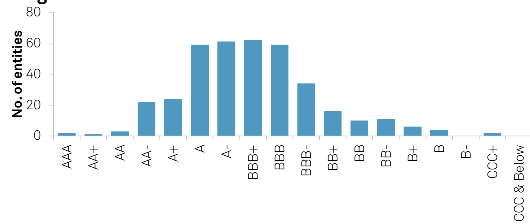
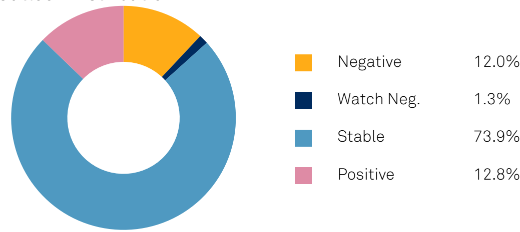
Rating Distribution



Outlook Distribution



Source: S&P Global Ratings. As of August 31, 2021.

Key Takeaways

- COVID's hit to our economic outlook continues to be the key factor weighing on banks, although effects vary across the 19 Asia-Pacific jurisdictions where we rate banks.
- Support by public authorities is containing the damage on the real economy and banks, but downside risks for banks remain as the region contends with further infections and slow vaccinations.
- We estimate that credit losses will rise by about an additional US$563 billion in 2020-2022 mainly because of COVID-19 stresses, compared with 2019 levels. This is slightly lower than our previous estimate in early 2021 of US$581 billion.

What's changed?

Mixed outlook. Persistent COVID waves are increasingly challenging emerging Southeast Asian banking systems. We recently revised downward our 2021 economic growth expectations for this region. Elsewhere, economic trends affecting banks are generally stable.

Still-high credit losses. Post-COVID credit losses remain high compared with that of 2019 (pre-COVID). Peak credit losses will likely now be lower than we initially forecast in mid-2020.

Ongoing support from authorities is important. Fiscal and monetary policy support and regulatory forbearance offer significant buffers for banks. But for this support, ratings would likely be lower.

Key risks

A downturn that is more severe than our base case. A slower or patchier economic rebound will intensify the damage on households and corporates, magnifying banks' credit losses. Regionally, slow vaccinations and periodic lockdowns mean credit losses are vulnerable until the health situation improves.

Leverage, corporate insolvencies, and property. We see our top risks as higher corporate and government sector leverage, and likely higher corporate defaults in 2021. Also, banks' property exposures are significant, and the institutions have not yet reckoned with the full effect of COVID on their asset quality. Further, low interest rates are fueling imbalances via strong asset price increases in some jurisdictions and sectors.

Key assumptions

Strong economic rebound. A return to pre-COVID metrics for asset quality and profitability will be slow and is unlikely to occur until end-2022 for many banking systems. Capitalization trends are expected to remain broadly stable, however.

Highly supportive governments. Fiscal and monetary policy support for households and corporates from public authorities will continue to stabilize bank credit. Ultimately, we expect extraordinary government support would be extended to many systemically important banks in the unlikely event it were required.

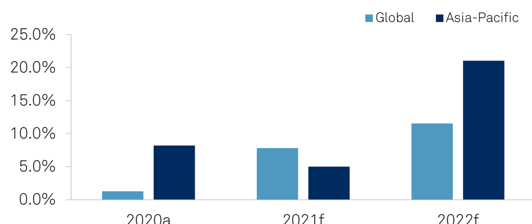
What to look for

Recovery from COVID. We expect interest margins to remain thin over 2021-2022. Higher inflation will likely alleviate some pressure on interest margins but will commensurately weigh on credit losses. Enduring stabilization will ultimately be driven by a persistent improvement in the health situation.

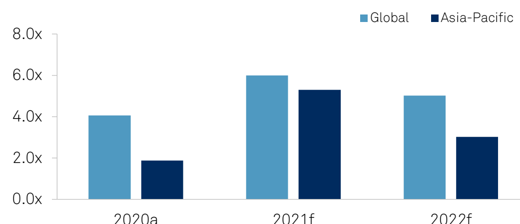
Gaming

COVID Resurgence Is The Wild Card

FFO/Debt (Median, Adjusted)



Debt/EBITDA (Median, Adjusted)



Source: S&P Global Ratings. All figures are converted into U.S. dollars using historical exchange rates. Forecasts are converted at the last financial year-end spot rate.
FFO--Funds from operations. a--Actual. f--Forecast.

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Key Takeaways

- Downgrade risks are heightened. A full sector recovery may now only happen in 2023.
- The withdrawal of the Yokohama IR Bid may prompt gaming operators to look elsewhere for growth.
- Stricter gaming law would worsen odds for Macau casinos.

What's changed?

A full recovery may now only happen in 2023, instead of 2022, for most markets in the region. The delta variant has forced the temporary closures of casinos and tighter travel-related restrictions in several markets. Credit metrics on some operators may remain outside of our rating thresholds for longer than we anticipated. Net negative rating bias persists across the portfolio with some casinos remaining closed, affecting cashflows and leverage metrics.

Yokohama IR bid cancellation. On Sept. 10, 2021, Yokohama City cancelled the Yokohama Integrated Resort Bid after a five-year process. Rated issuers Melco Resorts and Genting Bhd's Singapore subsidiary were the only two candidates still competing for this Japanese gaming concession. We viewed the bid process as an event risk for operators; they are now likely to look elsewhere for growth.

Key risks

Uncontrolled COVID cases. A worsening of the infection rate or new strains of the virus could delay reopenings of casinos and gaming tourism, disrupting cashflow for already weakened operators.

Regulatory risks. Possible amendments to Macau's gaming law heighten policy risk for casino operators. While immediate credit effects are limited, future risks include further government intervention on casino operations and fund extractions. Regulatory risks remain a key focus for Crown Resorts Ltd. over governance issues.

Key assumptions

Gaming visits to remain solid in long term. Nonetheless, we are monitoring for possible structural changes in gaming visitation trends or spending behavior as a result of COVID.

Non-casino operators. Digital gaming and online casino earnings are growing for certain Australian and New Zealand operators.

What to look for

Pace of recovery. COVID is the wild card, with operators reliant on international gaming tourism most vulnerable. The mixed efficacy of vaccines against new variants of COVID and slow mass vaccination rollout in some emerging markets may prolong the gaming recovery.

Insurance

Restored Capital Buffers Absorb Volatility

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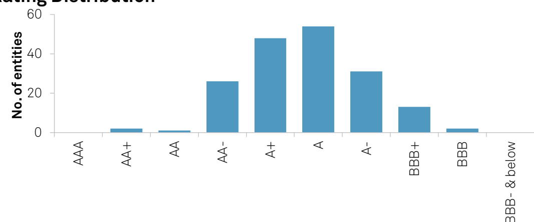
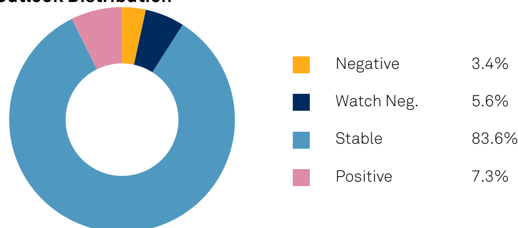
Rating Distribution



Outlook Distribution



Source: S&P Global Ratings. As of August 31, 2021. Includes public ratings only.

Key Takeaways

- Shored up capital buffers help absorb volatilities, supporting a stable credit trend.
- Reinvestment challenges persist amid low interest rates and fluctuating investment markets.
- Insurers' revenues should prove resilient to a resurgence of COVID.

What's changed?

Persistent reinvestment challenges to prompt heightened risk appetite. Low rates and capital market volatility weigh on investment returns. This signifies a likely increase in insurers' appetite for credit and market risk. Coupled with rising counterparty risk, this could dilute restored capital buffers. Insurers' unhedged foreign exchange exposure may lead to further earnings volatility.

Premium recovery to continue even as fresh COVID waves break out. Evolving digital capability and accelerated digital sales will support the resumption of sales activities for life insurers. A resurgence in COVID cases will likely hinder sales momentum in some Southeast Asian markets. Economic recoveries and improved premium rates for commercial lines should uphold property and casualty insurers' revenue growth.

Key risks

Intensified capital market turmoil. Sharper market swings and asset impairments could dent insurers' capital and earnings. Markets that adopt moving-average discount factors could demand hikes in life reserves.

COVID resurgence risk persists. COVID resurgence may constrain economic recovery, hindering demand for insurance coverage. Jumps in unemployment could lead to more loan delinquencies. This combined with withdrawals and the limited scope of some governments' stimulus measures in the region will hit mortgage-insurance providers.

Key assumptions

Asset risk will rise. Persistent reinvestment challenges will likely prompt insurers to take on greater credit and market risks. This is in addition to the inherent asset-liability mismatch positions among many life insurers in the region.

What to look for

Greater insurance protection awareness. Demand for health and medical insurance coverage will rise, post pandemic.

More extreme weather. Rapid urbanization and the increased frequency of weather-related events will demand increasing reinsurance arrangements and more regular updates on catastrophe models. Increased reinsurance costs should weigh on the profit margins of property and casualty insurers.

Regulatory and accounting updates. Evolving regulatory and accounting developments signify prospective changes in business and investment strategies, and result in rising operational costs.

Media And Entertainment

Regulatory Hurdles Add To Uncertainty

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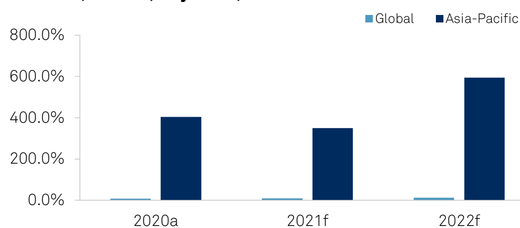
FFO/Debt (Median, Adjusted)



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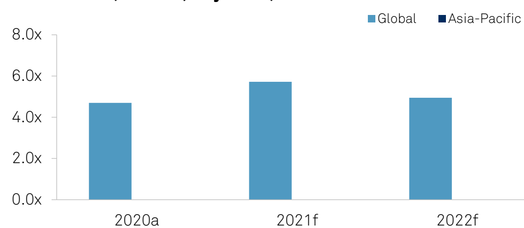

Source: S&P Global Ratings. All figures are converted into U.S. dollars using historic exchange rates. Forecasts are converted at the last financial year-end spot rate. FFO--Funds from operations. e--Estimated. f--Forecast.

Key Takeaways

- China's tightening of antitrust and fintech regulations could decelerate growth and pressure margins for large Chinese internet companies.
- Vaccine rollout is likely to be uneven across Asia and the timing of the recovery for many Asia-Pacific media and entertainment companies will be uncertain.
- Liquidity remains the key risk for many of the smaller media and entertainment companies, especially those exposed to live events.

What's changed?

Tightening regulations could dampen growth for China's internet giants. We believe dominant Chinese internet companies and some e-commerce companies could face slowing growth or margin compression due to increased scrutiny by regulators. This could result from possible delays in acquisitions or investments as these companies evaluate the new regulatory environment, or from intensifying competition as large internet companies cut down on anticompetitive practices and dial down margins to defend and solidify their long-term competitiveness.

Key risks

Speed of economic recovery and intensity of regulatory actions. Advertising is highly correlated to economic growth. A prolonged recovery would likely result in a sharper decline and slower recovery of advertising revenues, including online advertising. More severe regulatory outcomes could also drag on growth for some internet players in China.

Liquidity crunch. Smaller media and entertainment companies could face more severe liquidity strains, especially those with heavy exposure to live events, given little or no revenues during the outbreak. Tightening credit markets, particularly for speculative-grade issuers, will exacerbate liquidity issues for these companies.

Key assumptions

Advertising revenues to rebound in 2021. Advertising revenues should rebound this year, after setting a low base in 2020 and with renewed efforts to roll out vaccinations toward the second half of 2021. However, the pace of rollouts, and, therefore, the economic recovery, is likely to differ in each country.

What to look for

Normalization of consumer behavior. The prospects of some media and entertainment companies will depend on whether consumers return to their normal routines once vaccines are rolled out. Continued caution toward attending events with large gatherings could hurt companies exposed to live events or big venues. However, consumers' online habits are likely to stick post-COVID, benefiting online service providers and internet platforms.

Metals And Mining

Commodity Markets To Fall As China Stumbles

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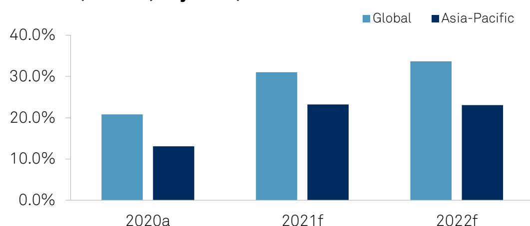
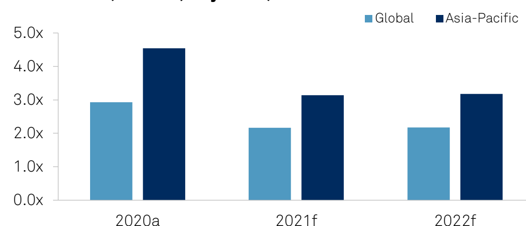
FFO/Debt (Median, Adjusted)



Debt/EBITDA (Median, Adjusted)



Source: S&P Global Ratings. All figures are converted into U.S. dollars using historic exchange rates. Forecasts are converted at the last financial year-end spot rate. FFO--Funds from operations. a--Actual. f--Forecast.

Key Takeaways

- A slowing Chinese recovery and the country's policy to cut emissions will weigh on commodities demand for the remainder of 2021.
- While commodity prices are down from cyclical highs, the pricing environment remains supportive.
- However, further outbreaks would undermine growth, hurt sentiment, and add volatility to commodity markets.

What's changed?

China's widening COVID outbreak hits commodity prices. The latest outbreak and a slowing Chinese pace of recovery, particularly in property and infrastructure, curtail the prospects for steel and raw materials.

Commodity prices fall from cyclical highs. Commodity prices remain volatile, having cooled off from record highs earlier this year for iron ore and copper. This comes as uncertainty rises surrounding China's economic recovery and its government's pledge to keep steel production flat in 2021.

China to limit steel production in an effort to cut carbon emissions. Chinese steel mills have pledged to cut output in the second-half of 2021, in line with the government's pledge to keep 2021 crude steel production at the same levels as 2020. We expect this to weigh on demand for commodities for the remainder of 2021.

Supply remains tight. Supply disruptions have contributed to the inability of supply to keep pace with demand growth. China has been selling state reserves for some commodities in an effort to cool exorbitant prices.

Key risks

Demand risk for commodities. China is executing targeted restrictions to control the infectious delta variant. Given that China accounts for over half of global demand for raw materials, a prolonged weakness in demand from its downstream sectors may strain global miners.

Financial policy. A return of heavy spending on capital expenditure or shareholder distributions may erode miners' liquidity, refinancing prospects, and balance sheets.

Environmental, social, and governance (ESG) factors. Access to capital is becoming increasingly challenging for metals and mining companies with poor ESG profiles.

Key assumptions

Commodity markets to normalize. The pricing environment remains supportive, given the ongoing economic recovery in Asia and optimism fueled by progress in COVID vaccines rollouts.

What to look for

COVID, China, and global trade. Resurgent pandemic risks pose a key threat to demand, while any change in environmental-related production controls in China could affect the profitability of its steel industry and the demand for commodities.

Oil And Gas

Price Resilience Does Not Negate Industry Risks

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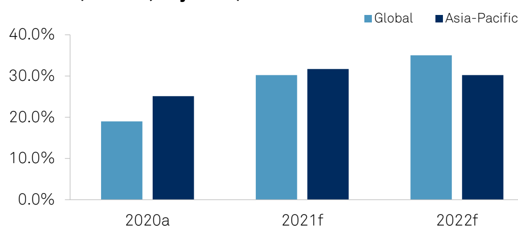
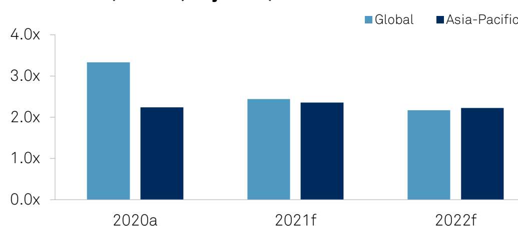
FFO/Debt (Median, Adjusted)



Debt/EBITDA (Median, Adjusted)



Source: S&P Global Ratings. All figures are converted into U.S. dollars using historical exchange rates. Forecasts are converted at the last financial year-end spot rate.
FFO--Funds from operations. a--Actual. f--Forecast.

Key Takeaways

- Recent oil price resilience is supported by demand recovery and production cuts.
- The willingness of oil-producing countries to constrain production will likely start to wane over the next two years.
- Oil companies, especially the majors, are positioning for long-term energy transition. Most of the sector entities we rate are national oil companies (NOCs) that also play a role in energy security.

What's changed?

Oil prices remain resilient. Despite retreating from the recent high of US$75/barrel, the Brent oil price is trading within the healthy US$65-$70/barrel range on demand recovery and production cuts by OPEC and Russia. The sustainability of these factors will determine the oil price trend.

Key risks

Prolonged pandemic. Even as vaccination rollouts continue, the uncertain effectiveness on new variants complicates the situation. A prolonged pandemic and revival of lockdowns would delay the recovery in demand, thereby hitting oil prices.

Structural change in oil demand. Diminished oil demand due to environmental concerns, prompting an energy transition, are rising secular risks. More governments are setting target dates for net-zero carbon emissions and banning the sale of fossil fuel-powered vehicles. Financial institutions may become increasingly reluctant to finance hydrocarbon projects or companies. Companies with weaker balance sheets and financing capabilities will be most vulnerable.

Key assumptions

Brent at US$65/barrel for the rest of 2021 and US$60/barrel for 2022. Demand recovery and controlled supply from oil producing countries underpin the rebound of oil prices from 2020. That said, we do not expect OPEC to target high oil prices for an extended period, for fear of reactivating large-scale U.S. shale production. We maintain our Brent assumption at US$55/barrel in 2023 and beyond, reflecting secular shifts in industry risks, which may see lower demand for oil.

Long-term overhangs for oil and gas. We raised the industry risk for oil and gas integrated, exploration and production at the beginning of the year. Yet we believe many of our rated NOCs play an important role in securing energy supply for their countries.

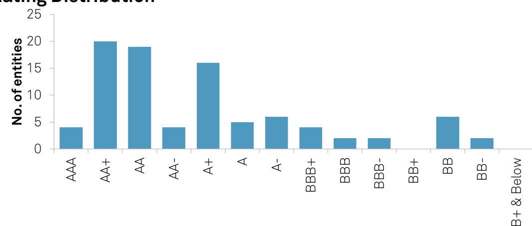
What to look for

COVID containment and supply response by oil producers. COVID control will set the shape of demand recovery, and determine support for oil prices. On the supply side, OPEC and Russia's pace of revision of production cuts will signal the oil price range with which they are comfortable.

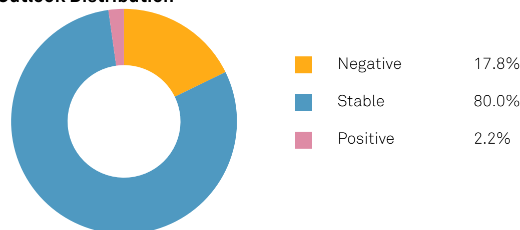
Public Finance

Policy Steps To Contain COVID Effects

Rating Distribution



Outlook Distribution



Source: S&P Global Ratings. As of August 31, 2021.

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Key Takeaways

- Fresh COVID infection waves suggest ongoing government measures are needed to address the economic and fiscal costs of the pandemic, in most systems.
- Local governments in Australia, New Zealand, and China are using large infrastructure projects to stimulate economies, and this practice will persist until at least through 2022.
- Tighter controls on public finances in China adds to the credit buffers on the country's local governments.

What's changed?

China credit migration follows an institutional framework uplift. Our rating distribution for the country has migrated to the stronger end, following our upward revision of the institutional framework assessment in China, in anticipation of tightened central controls and increased discipline at the local level.

Low infection strategy. Multiple local and regional governments (LRGs) in Australia and New Zealand have imposed strict lockdowns to suppress rising COVID cases, adding to the regions' economic and fiscal risks.

Key risks

Public spending stays high to sustain economic momentum. While picking up, vaccination rates remain low in Asia-Pacific and a commitment to lower infection rates should result in more lockdowns and tight containment measures. These controls imply LRGs need to maintain heavy spending on projects.

Contagion fears weigh on recovery prospects. Fear of infection will continue to deter travel and hinder consumption in Asia-Pacific. The variants are making regions that seek low to zero caseloads reluctant to reopen borders. This is a risk for a range of public-finance segments, such as Australian universities.

Key assumptions

Few signs that governments will pull back their countercyclical measures. LRGs that plan increased capital expenditure to sustain growth risk diminishing their fiscal standing.

Public finance systems largely remain stable across the region. Australian and New Zealand LRGs have greater spending discretion to prompt a recovery, but expansionary policies weigh on their finances. China's LRGs can still rely on large cash transfers and new borrowings, subject to ongoing support from the central government. The finances of Indian LRGs remain stretched and are handicapped by limited financial flexibility. Japanese LRGs will look to the central government to undertake nationwide economic stimulus, rather than squeezing their already damaged budgets.

What to look for

Policy shifts. Any aggressive LRG fiscal expansion, either to sustain growth or to maintain social stability, could erode credit quality. LRGs in economies experiencing stronger economic rebounds should be able to normalize more quickly. China has recovered, yet we see greater scope for state-owned enterprises to experience strains. Any moves to provide large-scale bailouts to stressed entities would be a credit negative for their local-government owners.

Real Estate Development

Weaker Players May Lose Access To Financing

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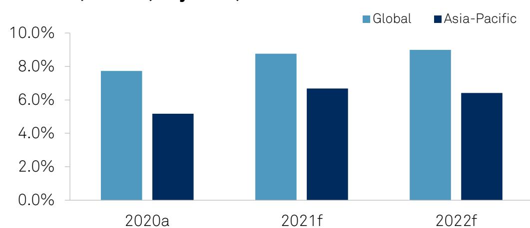
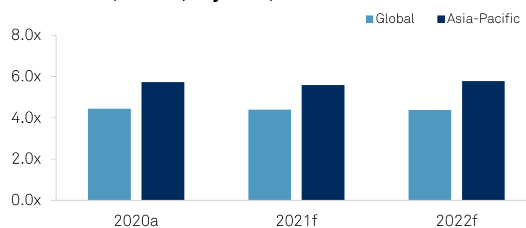
FFO/Debt (Median, Adjusted)



Debt/EBITDA (Median, Adjusted)



Source: S&P Global Ratings. All figures are converted into U.S. dollars using historical exchange rates. Forecasts are converted at the last financial year-end spot rate. FFO--Funds from operations. a--Actual. f--Forecast.

Key Takeaways

- Weakening funding access is a key risk, especially for developers with an uneven operating performance and concentrated maturity profile.
- Contracted sales will taper for Chinese developers amid overall credit tightening and capital-market volatility.
- A sales recovery for Indonesian developers is on track, but the recent resurgence of COVID poses risks and uncertainties.

What's changed?

Volatile market and tighter funding are leading to higher risks. Bond prices are fluctuating wildly for some lower-rated Chinese developers, amid China Evergrande's likely default and a few distressed cases in the sector. Bank and trust funding continues to tighten and this adds to the risks.

Key risks

Property sales slowdown in China may complicate things. Slower cash generation will be an additional negative for companies struggling to access funding. Sales have slowed since mid-year for rated Chinese developers, with July average sales contracting 9%. We think sales may remain sluggish for the next six to 12 months, in tandem with the recent credit and policy tightening.

Renewed risks for developers with weaker funding. In China, financial institutions and investors are becoming increasingly selective. Evergrande's likely default is creating contagion risk to players with concentrated maturities, and faltering investor confidence may lead to a downward funding access spiral. We have therefore taken negative rating actions on five Chinese developers.

In Indonesia, sales are recovering but the outlook is uncertain due to the COVID threat, given the country's vaccination rate is low. Liquidity remains tight with higher construction spending, leading to three out of four sectors ratings at 'B-' or below.

Key assumptions

Slower recovery and sales. Indonesian developers' EBITDA recovery will be constrained by construction delays due to thin liquidity. As such, the recovery of credit metrics will lag behind sales. For rated Chinese developers, sales have expanded 26% year to date, but will likely taper in the second half.

What to look for

How policy changes will shape the sector. In Indonesia, we anticipate supportive regulatory measures (e.g., higher loan-to-value ratio) will stay in place and support property sales. In China, slowing growth may prompt some easing measures. However, in our view, these would need to be balanced against the Chinese government's long-term goal of steering speculation and financial risks away from the housing sector.

Real Estate Investment Trusts

Expenditure Curtailment To Create Financial Headroom

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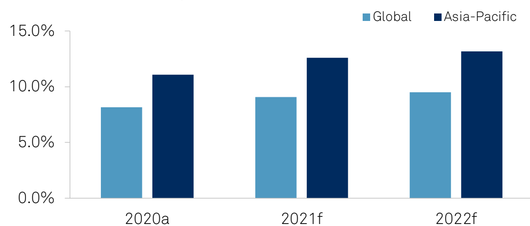
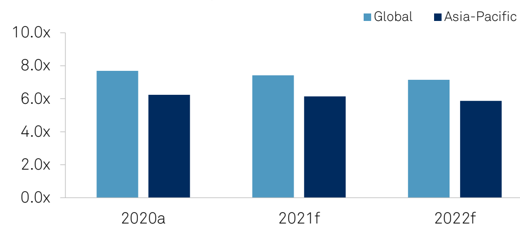
FFO/Debt (Median, Adjusted)



Debt/EBITDA (Median, Adjusted)



Source: S&P Global Ratings. All figures are converted into U.S. dollars using historical exchange rates. Forecasts are converted at the last financial year-end spot rate. FFO--Funds from operations. a--Actual. f--Forecast.

Key Takeaways

- Office landlords will see lower rent levels and cash flows as new incremental demand stays muted.
- We expect retail REITs to curtail expenditures, reduce cash distributions and take other cash-preservation measures to offset the effect of the pandemic.
- The sector's rating trend continues to be negative, with ongoing risk that some Asia-Pacific entities may lose their investment-grade status.

What's changed?

Retail out of the woods in some countries. We recently revised outlooks to stable from negative on three out of four Australian retail landlords. This reflects the prudent responses adopted by these landlords. They have reduced operating expenses and are holding back on noncommitted investments to build a buffer to weather further disruptions.

Social distancing and idiosyncratic risks. Many countries remain willing to reinforce social distancing when infections spike, hurting physical retailers. The outlook for physical space will be determined by local factors including the supply and demand dynamics of individual cities, the health of their economies, vaccination rates, and the corporate culture of office and retail tenants.

Key risks

Secular change for office. The pandemic has prompted some international firms to cut office space in Asia-Pacific, given that some employees prefer to work from home. This preference will likely continue long after COVID subsides.

Shorter lease term will test landlords' stability. Bargaining power is waning for landlords amid weaker retail performance and uncertain demand from office. Landlords could face shorter and more flexible lease terms to stop occupancy rates from dropping further. This trend has already been observed in recent interim results.

Key assumptions

Rental pressure could continue. We expect rents to drop for both retail and office classes amid weaker occupancy levels. We account for the risk that a prolonged pandemic could derail economic recoveries, upending demand.

What to look for

Deeper and longer vacancy to linger. We expect high vacancy rates to stay and rental reversions to slide even more for the key gateway cities in the region. However, this could still require further adjustments if economic activity doesn't pick up as much as we expect.

Retail

Emergent Delta Variant Supressing Consumer Confidence

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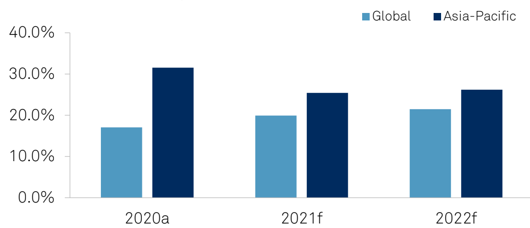
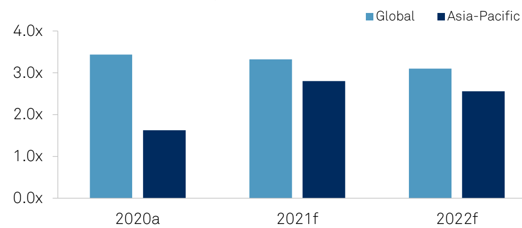


Debt/EBITDA (Median, Adjusted)



Source: S&P Global Ratings. All figures are converted into U.S. dollars using historic exchange rates. Forecasts are converted at the last financial year-end spot rate.
FFO--Funds from operations. a--Actual. f--Forecast.

Key Takeaways

- The recovery paths of our rated retailers remain tied to the fortunes of their respective geographies and their ability to adapt to new disruptions and changing consumer behavior.
- High input prices and supply-chain constraints in some markets may create inflationary pressures, constraining margins and delaying the recovery.
- The gap in credit metrics between Asia-Pacific and global retailers will narrow on the back of prolonged pandemic-related impacts in the region and growth investments.

What's changed?

The delta variant poses new risks and challenges. Rising infection rates and elongated lockdown periods are materially hampering a recovery in consumer confidence. This is adding to problems for issuers, which have already taken a severe hit since the inception of the pandemic.

Key risks

New infection waves. The COVID threat remains high. Many Asia-Pacific markets could suffer from low vaccination rates or exposure to more-infectious COVID-19 variants despite progress in vaccination coverage. Store closures and constrained consumer sentiment would likely restrict consumption, raising credit risks for retailers with high sensitivity to shifting tastes, consumer behavior, and reduced discretionary spending.

Higher input prices and supply chain constraints. Prices for raw materials and the cost of shipping remain elevated in some markets as global demand outstrips constrained supply. Higher inflationary pressures could crimp margins and delay recoveries for our rated issuers.

Key assumptions

Challenging deleveraging paths. Many retailers have focused on improving liquidity through additional financing measures amid turbulent operating conditions. For more highly leveraged retailers, we expect a long deleveraging path with a lumpy recovery in consumer demand.

What to look for

Divergent paths for retail segments. A continuation of COVID-related restrictions will suppress recovery of discretionary retailers focusing on out-of-home consumption. The longer the pandemic lasts, the more embedded changing consumer behaviors become, making the recovery of physical retailers post-COVID even more challenging.

Sovereign

COVID Concerns Remain

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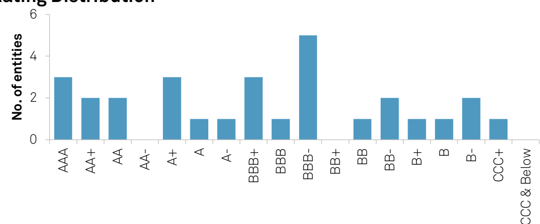
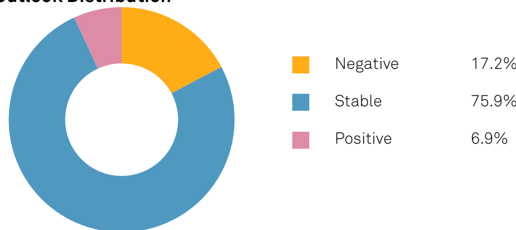
Rating Distribution



Outlook Distribution



Source: S&P Global Ratings. As of August 31, 2021. Includes public ratings only, and ratings on policy-related financial institutions and corporates.

Key Takeaways

- The delta variant is driving waves of new infections.
- New virus strains and fading vaccine efficacy add to the health risks.
- Supply chain bottlenecks and volatile financial conditions could slow the recovery of entities' credit metrics.

What's changed?

Supply and logistical risks to export recovery. A shortage of semiconductor chips and bottlenecks in container shipping have disrupted production and raised manufacturers' costs.

Inflation rates in Europe and the U.S. have picked up. Consumer prices rose quickly in 2021 in major advanced economies. Policymakers continue to believe the increases to be temporary but strains on policy rates could increase if higher inflation proves persistent.

Delta variant spreads. This highly infectious variant has forced some Asia-Pacific governments to tighten movement restrictions.

Key risks

More COVID-19 variants and sudden capital swings. Sharp deterioration in investor sentiment in emerging markets could see swift capital outflows. In lower-rated sovereigns dependent on imported energy, higher oil prices would weaken their external balances and exacerbate capital outflows.

Dampened manufacturing recovery may weigh on growth and fiscal recovery. Rising component and commodity prices, as well as shipping costs, could hobble production recoveries. Shortages of semiconductors have also caused some car manufacturers to temporarily halt production. If these trends persist and government support tapers off, weaker demand may intensify pressures on manufacturers and exports out of Asia-Pacific.

Key assumptions

Global economic activity will recover without major volatility. Recoveries to become more entrenched as the vaccination rates in key economies rise, supported by gradually climbing interest rates and commodity prices.

What to look for

Geopolitical developments that could disrupt momentum. U.S.-China tensions are increasingly accompanied by displays of military prowess. Accidental contacts that escalate these tensions could spill over into trade and financial interactions.

Prolonged pandemic possible if vaccines become less effective. Poor efficacy of vaccines against potential new variants of COVID or fading vaccine efficacy against existing variants present risks that could prolong the pandemic.

Structured Finance

Buoyant Issuance, Households Remain Resilient

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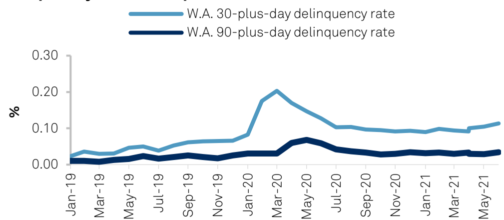
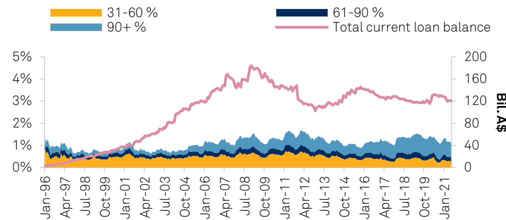
China Auto Loan ABS: 30-Plus-Day And 90-Plus-Day Delinquency Rate Composite



Data as of July 31, 2021. ABS --Asset-backed securities. W.A. --Weighted average. Source: Trustee reports published on Chinabond's website; compiled by S&P Global Ratings.

Australia Prime SPGR Mortgage Performance Index



Data as of Jun. 30, 2021. Source: S&P Global Ratings.

Key Takeaways

- Strong issuance volumes especially in residential mortgage-backed securities across the region.
- New originators, low interest rates, and changing regulatory landscapes will likely shift risk profiles across structured finance markets

What's changed?

Asia-Pacific. Consumer asset classes have demonstrated stability and resilience. Employment indicators remain stable for most major markets. Structured finance markets in Asia-Pacific are seeing strong issuance volumes, which is consistent with the global trend for structured finance in 2021.

Lockdown measures in parts of Australia have seen a return of temporary forbearance measures for mortgages, but take-up rates are unlikely to be as high as during the first phase of the pandemic.

Key risks

Virus resurgence and threat to consumer confidence. The resurgence of the virus, particularly in countries that have largely contained the pandemic to date, may dent consumer confidence. This would ultimately affect the performance of consumer credit-backed and mortgage-backed loans. In Australia and New Zealand, the return to lockdowns has hit immediate measures of confidence.

Asset price inflation and the effectiveness of regulatory "handbrakes". Rising house prices in some markets may test the effectiveness of regulatory interventions designed to cool emerging pockets of overheating.

Key assumptions

Structural supports. We expect ratings to be stable, with low levels of speculative-grade ratings and structural supports to cushion some deterioration. Broadly stable employment trends and low interest rates support debt serviceability on residential mortgage-backed securities.

What to look for

Green financing gathers momentum in China. Decarbonization is an important theme in China's new five-year plan. Regulators have released measures in aspects such as guidance for green project assessment. These policies will likely drive more green elements in securitization transactions in China, though the rollout of transactions backed by green assets will likely be gradual.

Libor cessation. Publication of Libor in many currencies, including the Japanese yen, ceases at the end of 2021. We anticipate a further acceleration in the transition to new benchmarks before the end of 2021.

Housing market dynamics. The impact of further lockdowns across parts of Australia may see a pause in activity and confidence impacting housing markets in the coming months, however longer-term factors relating to affordability, interest rate outlooks, and supply are likely to return to the mix as key factors.

Technology

Strong Profitability Could Sustain

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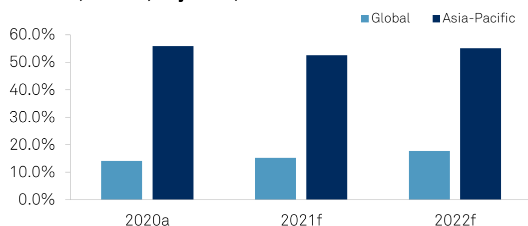
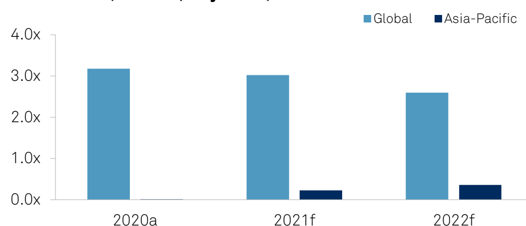
FFO/Debt (Median, Adjusted)



Debt/EBITDA (Median, Adjusted)



Source: S&P Global Ratings. All figures are converted into U.S. dollars using historic exchange rates. Forecasts are converted at the last financial year-end spot rate. FFO--Funds from operations. a--Actual. f--Forecast.

Key Takeaways

- An extended component shortage could cap revenue growth but keep tech companies' profitability strong with sustained demand.
- Oversupply could emerge in late 2022 or 2023, particularly for semiconductors, because of record capital expenditure and fading demand from COVID mitigation.
- Strong profitability moderately strengthens the sector credit outlook, which is partly offset by risks from technology shifts and the tech war between the U.S. and China.

What's changed?

Prolonged shortage in semiconductors. Shortages in semiconductors could extend beyond the end of 2021, keeping hardware companies from fulfilling strong customer orders and capping revenue growth. Nonetheless, undersupply will continue to sustain tech companies' strong margins. We anticipate favorable growth for 5G communications, cloud computing, internet of things and electrical vehicles, despite fading demand for remote working and learning equipment.

Key risks

Uncertain COVID trajectory and aggressive capital expenditure. The acute shortage in semiconductors and the optimistic growth outlook have stimulated record investments. Growing concerns over tech-supply-chain security in major economies could also add to spending. However, the reversal of demand for COVID mitigation and slower adoption of new technologies from current high expectations could cause oversupply in late 2022 or 2023.

Faster technology shifts. These present material risks alongside increased capital expenditure needs, shortened product lifecycles, and shrinking demand for legacy technology such as enterprise servers, traditional IT services, digital cameras, and office equipment. The pandemic has accelerated such risks, adding pressures for the companies that focus on those legacy products and services.

Key assumptions

Further acceleration in global IT spending. A stronger economic recovery and still strong demand for remote working and learning equipment could further push global IT spending growth to 9.4% in 2021, up from our previous forecast of 5.8%. Semiconductor demand will grow much stronger at 16% in 2021 (previous: 9%). PC shipments could expand 15% for the full year 2021. Smartphone shipments could reverse the decline seen in 2019-2020, and post a 6% growth in 2021 with the strong sales of 5G-enabled smartphones.

What to look for

Rating actions could tilt slightly positive over the next three to four quarters. Strengthening profitability has strengthened balance sheets and resilience to business volatility for tech companies. However, technology shifts and structural changes could burden some Japanese companies, while the U.S. blockade on the Chinese tech industry may weigh on some rated Chinese companies.

Telecommunications

Steady Today, Steady Tomorrow

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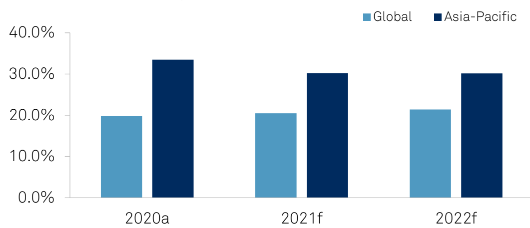
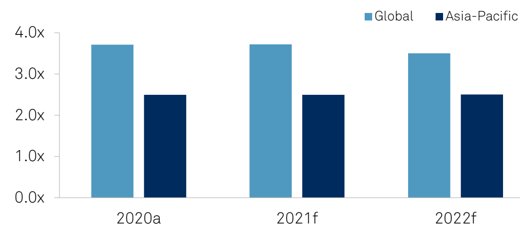
FFO/Debt (Median, Adjusted)



Debt/EBITDA (Median, Adjusted)



Source: S&P Global Ratings. All figures are converted into U.S. dollars using historic exchange rates. Forecasts are converted at the last financial year-end spot rate. FFO--Funds from operations. a--Actual. f--Forecast.

Key Takeaways

- Most telecom operators can maintain steady operating and financial performances amid prolonged COVID, owing to the sector's low cyclicality and utility-like demand characteristics.
- However, we see downward pressure for some Asia-Pacific operators due to intense competition, large capital investments, and debt-funded acquisitions.
- Data traffic should continue to expand on rising connectivity demand, but due to the pandemic, telecom operators face slack demand for roaming services.

What's changed?

Rising connectivity demand. Continued movement restrictions should support growth in data traffic, including demand for high-speed broadband services. However, higher unemployment and lower consumer spending may weigh on some operators' roaming, pre-paid wireless, and business-to-business services.

Key risks

Intense competition. Competition remains intense with wireless tariff cuts or aggressive marketing in countries such as the Philippines, Singapore, and Thailand. The entrance of new operators in Japan (Rakuten Inc.), Singapore (TPG Telecom) and the Philippines (Dito Telecommunity Corp.) will further increase wireless competition.

Deeper recession. Sluggish Asia-Pacific economies, reduced spending on telecom services, and rising bad debt may dent the region's telecom operators. We saw a modest revenue and profitability decline in 2020 but anticipate a recovery in 2021 and onwards.

Key assumptions

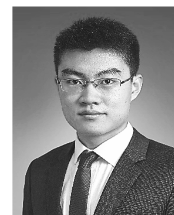
Mergers and restructurings. We expect continued merger and acquisition activity in the region given the telecom-media convergence trend and the appetite of some telcos to restructure their businesses. In Korea, all three telecom players (KT Corp, SK Telecom Co. Ltd., and LG Uplus Corp.) have acquired cable TV operators to strengthen their media and pay-TV market position. In Malaysia, Axiata Group Bhd.'s Malaysia subsidiary plans to merge with Telenor ASA's Malaysia subsidiary. Axiata also recently announced a proposed acquisition of broadband and cable TV operator PT Link Net Tbk. In addition, we anticipate an ongoing trend of monetizing telecom infrastructure assets, as seen with Telstra's recent sell down of its tower business.

What to look for

Growing 5G services. After Korea's 5G rollout began in April 2019--followed by Australia, China, and Japan--we see steady new 5G subscriptions. Despite potential revenue growth opportunities from higher 5G wireless tariffs, telecom operators need to manage investment burdens for 5G spectrum auctions and network expansions. Also, developing new and profitable 5G use-cases remains challenging for all operators at the current stage.

Transportation Cyclical

The Good, The Bad, And The Liquidity Challenged



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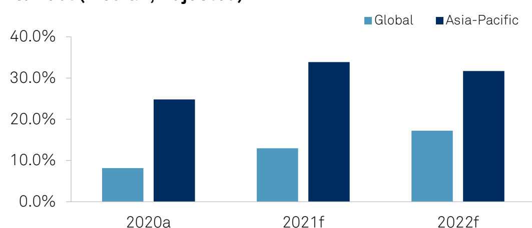
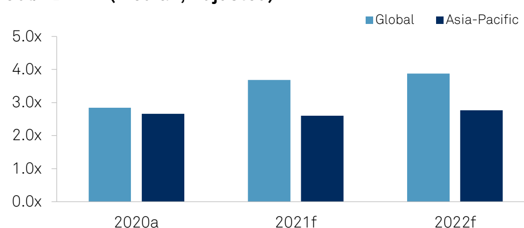
FFO/Debt (Median, Adjusted)



Debt/EBITDA (Median, Adjusted)



Source: S&P Global Ratings. All figures are converted into U.S. dollars using historic exchange rates. Forecasts are converted at the last financial year-end spot rate. FFO--Funds from operations. a--Actual. f--Forecast.

Key Takeaways

- Recovery paths of Asia-Pacific transport entities remain divergent in the aftermath of COVID.
- Airlines are the most exposed and their recovery will be gradual. Aircraft lessors can handle temporary disruptions, but a prolonged drop in air travel and the possible failure of some airlines may expose them to a significant second-order effects.
- Car rentals in China continue to benefit from significant pent-up demand for leisure travel, despite occasional resurgence of domestic COVID cases. Package express, postal services, and logistics companies are less exposed given their focus on domestic markets.

What's changed?

Divergence continues. While the demand shock to regional transportation bottomed in the second quarter of 2020, the recovery follows differing paths depending on the region and the subsector. For the hard-hit airline industry, rebounding trade volumes and capacity limitations will likely support high air-freight rates for the rest of 2021, benefiting airlines with greater freight exposure. Regional air-passenger traffic could remain weak while carriers with greater exposure to domestic markets could rebound more strongly. Travel activities have seen a sustainable recovery in China since March 2021, benefiting civil aviation and car rental markets.

Key risks

Liquidity crunch. Liquidity remains the main credit driver for weaker transport companies and most airlines, especially in cases where a prolonged disruption exposes firms to extended cash crunches. Government support and relationships with creditor banks are increasingly figuring into our ratings assessments.

High uncertainty over the recovery of travel patterns. Domestic leisure travel will likely lead the industry's recovery, with business and international travel trailing behind. Even with a recovery underway, entities are finding it hard to put the pandemic's effects behind them. A big and increasing disparity among countries and subsectors could lead to a widening variation in credit trends for the transport companies in the region.

Key assumptions

Global air traffic won't return to normal until 2024. We believe that 2021 traffic by revenue passenger kilometers and revenues will still be 40%-60% lower than in 2019 (in 2020, 65%-80% down from 2019's level), and we foresee only a gradual recovery to pre-COVID-19 levels by 2024. The path to normalization will likely be uneven across countries.

What to look for

Pace of demand recovery. The economic outlook and the evolution of the pandemic are the key variables driving the sector's recovery. We may have to wait until there is widespread vaccination and easing of border restrictions before a more complete rebound in mobility and travel is possible.

Transportation Infrastructure

Increasing Vaccinations May Open The Way For A Slow Recovery

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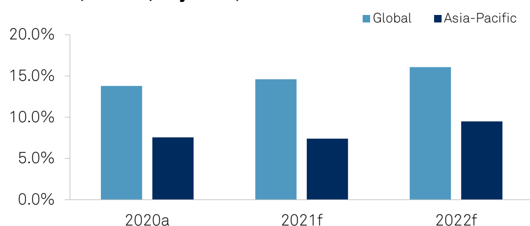
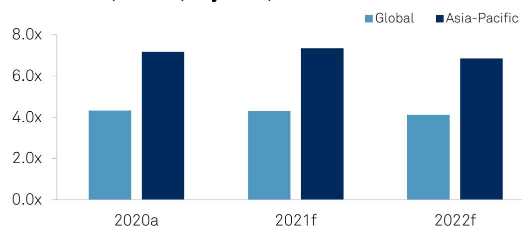


Debt/EBITDA (Median, Adjusted)



Source: S&P Global Ratings. All figures are converted into U.S. dollars using historic exchange rates. Forecasts are converted at the last financial year-end spot rate.
FFO--Funds from operations. a--Actual. f--Forecast.

Key Takeaways

- Differences in the pace of vaccination, virus variants, international travel bans, and domestic restrictions will result in continuing divergence across countries and sectors.
- Ports and roads will remain more resilient while for airports, the recovery has been further delayed.
- One in 10 ratings face downgrade risks as of July 31, 2021--halving the negative outlooks from May.

What's changed?

New variants and vaccination will drive COVID risks. The more virulent delta variant, still-slow vaccination in Asia, and continuing international travel restrictions weigh on the sector's outlook. Sudden targeted lockdowns and restrictions pose downside risks and uncertainties for cash flows. The withdrawal of government support and stimulus could also put the focus back on structural recovery.

Key risks

Weakened government fiscal positions dampen support. The willingness, ability, and form of government support will vary and can be an overhang on the sector. The severity of new waves is hurting several local and regional government's fiscal collections and may hit government-backed infrastructure developers.

Elevated macro and geopolitical risks. Uncertainty about the timing of widespread vaccination (particularly for emerging markets) and increasing policy risks weigh on the sector's outlook.

Key assumptions

Lasting damage. The sector will see lasting scars due to mobility restrictions and higher debt. Delays to the normalization of economies and the lifting of restrictions could result in more rating pressure.

Some flexibility in capital expenditure. Capital spending is on an upward trajectory, given significant infrastructure deficits and recovery stimulus. However, some expenditure deferrals or adjustments may occur given stressed corporate finances, labor shortages due to restrictions, and the erosion of structural demand.

What to look for

Re-emergence of restrictions. International travel restrictions remain tight with some signs of reopening. However, domestic travel can normalize when caseloads are manageable, like in New Zealand. On the contrary, countries such as India are adopting targeted lockdowns and route caps.

Funding and liquidity conditions. Capital markets are flush with liquidity, government and central banks' support measures have improved funding conditions for issuers, except in China. Credit differentiation continues.

Utilities

Lots Of Growth Options

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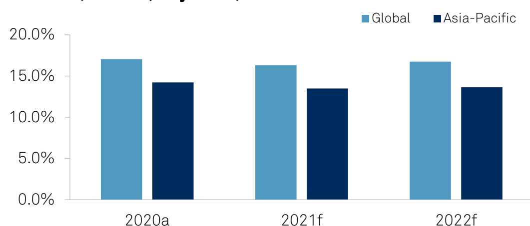

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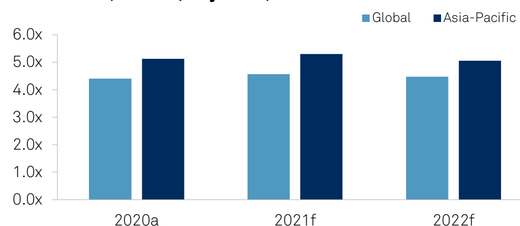

Source: S&P Global Ratings. All figures are converted into U.S. dollars using historic exchange rates. Forecasts are converted at the last financial year-end spot rate. FFO--Funds from operations. a--Actual. f--Forecast.

Key Takeaways

- Renewables remain in the forefront of most Asian markets and investments will gather pace as COVID recedes. This will call for some level of long-term network investments.
- Investors remain cautiously keen on this growth market.
- We have a negative bias on the sector, given relatively high leverage and expected debt-funded growth-related investments, plus earnings risk for fossil-fuel-powered generators.

What's changed?

COVID risks will linger across most markets. Investors/sponsors will have to work around this. Notwithstanding this, energy demand in Asia-Pacific will return to pre-COVID levels within a short time as virus risks abate. This is because of an expected rebound in industrial output, and impetus for infrastructure development by governments.

Key risks

Unwinding of economic support and infection resurgence. The winding-down of government economic support to small and midsize enterprises/industries or a return of secondary infections can limit demand growth and impede deleveraging. Weaker fiscal positions of state governments or of distribution utilities (off-takers) can be a drag.

Pace of new investments and funding may slow. Excessive debt funding of new developments, adverse regulatory reforms and long-term grid constraints are risks. The need to balance tariffs post-COVID versus issuers' return on investment may test regulatory frameworks. Significant investments can be driven by Integrated hybrid projects by renewable players and the acquisition of the renewable portfolio by coal majors.

Key assumptions

Profitability will see mixed trends across markets. We have not revised margin assumptions despite a demand recovery and tariff changes to pass-through fuel costs in some markets. This is because the effects may be short term. Lower open-market power prices and retail price controls will continue. In China, weather-linked rising fuel costs in winter may contain the profit expansion of power producers and city gas distributors.

Capital expenditure growth to resume. Potential ramp-up as some renewable projects are bought forward to replace deferred or cancelled fossil-fuel generation. We assume a cautious funding approach in line with parameters approved by regulators or bilateral contracts.

What to look for

Liquidity management to support short-term drops in demand and working capital shifting to investment. While rating headroom remains, aggressive growth can bring risks.

Appendix 1

Related Research

- Credit Conditions Asia-Pacific Q4 2021: COVID Besets, China Resets. Sept. 28, 2021.
- Economic Outlook Asia-Pacific Q4 2021: Growth Slows On COVID-19 And Rising China Uncertainty. Sept. 27, 2021.
- Credit FAQ: Evergrande Default Contagion Risk--Ripple Or Wave? Sept. 20, 2021.
- COVID, China Risks Won't Pass For Years, Say Panelists. Sept. 9, 2021.
- China's Zero-COVID Approach To Aggravate Rising Corporate Risks. Sept. 6, 2021.
- China Developers Battle Tight Liquidity And Plummeting Profitability. Sept. 6, 2021.
- Will COVID-19 Waves Wash Away Sovereign Credit Support In Asia-Pacific? Aug. 23, 2021.
- Pandemic Is Disrupting 2021 Growth Outlooks In Southeast Asia. Aug. 9, 2021.
- Global Banking Country Outlook Midyear 2021: Tantalizing Signs Of Stability. July 22, 2021.
- Global Banks Outlook Midyear 2021: Clawing Back To Normalcy. July 22, 2021.
- Indonesia's COVID-19 Struggle. July 15, 2021.

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