

# Credit Conditions North America: Unprecedented Uncertainty Slams Credit

March 31, 2020

*(Editor's Note: S&P Global Ratings' Credit Conditions Committees meet quarterly to review macroeconomic conditions in each of four regions (Asia-Pacific, Emerging Markets ex-Asia, North America, and Europe). Discussions center on identifying credit risks and their potential ratings impact in various asset classes, as well as borrowing and lending trends for businesses and consumers. This commentary reflects views discussed in the North America committee on March 25, 2020. Given the fluidity of current conditions, we have chosen to publish a truncated version of our usual article this quarter.)*

## Key Takeaways

- **Overall.** The U.S. and Canadian economies have plunged into what will likely be historically severe recessions, with evaporating liquidity plaguing both corporate borrowers and the real economy. With the COVID-19 pandemic continuing to spread, predicting an end to this period of unprecedented uncertainty is fraught with variables.
- **Risks.** With coronavirus-containment measures hammering the U.S. labor market—almost 3.3 million Americans filed jobless claims in one week, by far a record—the concomitant demand shock threatens to prolong the economic slump and stifle an expected second-half recovery.
- **Credit.** Historically low interest rates and massive government stimulus are helping to bolster financial markets, but slumping cash flows and tight financing conditions are pressuring the credit quality of issuers across our rating practices; S&P Global Ratings has taken roughly 350 ratings actions on borrowers in North America at least partially due to the coronavirus outbreak's effects.

Credit Conditions in North America look set to remain extraordinarily difficult for borrowers at least into the second half of the year, with the economic stop associated with coronavirus-containment measures continuing with no clear end in sight. Intense pressure on the credit quality of borrowers worldwide won't soon subside, as cash flows slump and financing conditions materially diverge between investment- and speculative-grade borrowers.

Though our base case sees GDP growth rebounding in the second half as consumer demand revives and firms rush to fill back orders and restock inventories, much economic activity that depended on household discretionary spending will be lost permanently—with risk to the downside increasing in conjunction with escalating unemployment. Residual scars could linger, especially if social distancing becomes a “new normal” and/or business and consumer spending doesn't bounce back.

**Economic conditions.** With almost 200 million Americans directed to stay at home, the longest economic expansion in U.S. history has come to an abrupt halt. We forecast GDP will shrink 2.1% in the first quarter and a massive 12.7% in the second. The unemployment rate could exceed 13% in May, which would be the highest on record, going back to 1948. Even a strong second-half rebound won't be enough to get the world's biggest economy back to even for the year. We now expect a full-year contraction of 1.3% before the economy regains its growth path next year.

Roughly 3.3 million Americans filed initial jobless claims in the week ended March 20—almost five times the 1982 record high. This comes as a massive pullback in discretionary spending looks set to lead to the sharpest quarterly contraction in consumer outlays on record for April-June. In addition, we expect business investment and trade to shrink by the most since the Great Financial Crisis. And while we continue to forecast a U-shaped recovery in the second half, the path and severity of the coronavirus outbreak will dictate when the rebound will start.

The Federal Reserve has responded by slashing benchmark borrowing costs to effectively zero and announcing a slew of emergency measures to inject liquidity into the financial system and ensure the orderly functioning of markets—pledging to use “its full range of tools to support the economy.” On the fiscal side, lawmakers have agreed to a \$2 trillion stimulus package meant to address widespread health and economic problems created by the outbreak.

## Regional Credit Conditions Chair

**David C Tesher**

New York  
david.tesher@spglobal.com  
+1-212-438-2618

## U.S. Chief Economist

**Beth Ann Bovino**

New York  
bethann.bovino@spglobal.com  
+1-212-438-1652

## Senior Economist, U.S. and Canada

**Satyam Panday**

New York  
satyam.panday@spglobal.com  
+1-212-438-6009

## Global Head of Research

**Alexandra Dimitrijevic**

London  
alexandra.dimitrijevic@spglobal.com  
+44-207-176-3128

## Financing Conditions

**Nick Kraemer**

New York  
nick.kraemer@spglobal.com  
+1-212-438-1698

## Research Contributors

**Joe M Maguire**

New York  
joe.maguire@spglobal.com  
+1-212-438-7507

**Yucheng Zheng**

New York  
yucheng.zheng@spglobal.com  
+1-212-438-4436

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While all of this will likely help, our assessment of the U.S. economy is dour across most private sectors. Indeed, it's not clear that the monetary and fiscal stimuli will fully offset the drag on economic activity. How much GDP contracts really hinges on when and how strongly consumer demand comes back to life, which, in turn, depends on the duration of containment/mitigation policies. In our deep-recession scenario, the possible economic damage would far exceed the Great Recession.

Similarly, we now forecast a full-year contraction in Canada's GDP, down 2% with a material increase in unemployment, as the economy is battered on two fronts: the effects of the COVID-19 pandemic and the tumble in oil prices. Rail blockades and the global recession will only make it worse. The Canadian economy is also more vulnerable to a drying up of international trade than its southern neighbor is, nor was the trend of GDP growth as strong as the U.S.' heading into the crisis.

Regionally, it's worth noting that the economic damage associated with the outbreak is nonlinear. That means, for example, that if containment takes twice as long as expected, the economic damage will be more than twice as bad. Therefore, recovery could take longer and be weaker (with more lost output) than projected.

**Financing conditions.** The lending environment in the U.S. has turned sharply negative. With a recession in full swing and expected to deepen in the second quarter, further credit market deterioration is expected, particularly for speculative-grade borrowers. As is typical of a recession, borrowing costs will likely remain elevated, keeping bond and loan issuance largely subdued. Extraordinary stimulus measures by the Fed will likely help bolster liquidity, but the benefits will be largely, if not exclusively, enjoyed by investment-grade issuers until the economic recovery takes hold. We expect defaults to increase markedly this year, which will further constrain a largely frozen issuance environment for weaker borrowers.

Before this latest crisis, a long stretch of low interest rates, combined with investors' thirst for yield, enabled more firms to increase leverage or to issue rated debt for the first time. In fact, the number of spec-grade issuers grew 44% in the past decade. This is important because lower ratings typically suffer more downgrades during downturns than higher ratings do. Our Negative Bias—the proportion of issuers with negative outlooks or on CreditWatch with negative implications—has risen considerably, to about 24% from 19% before this crisis. Further, 30% of spec-grade borrowers are rated 'B-' or lower—an all-time high. This is a level at which we see higher incidences of not only downgrades but defaults.

**Sector trends.** Borrowers face adversity on three fronts: the sudden stop in the global economy, the collapse in oil prices, and record volatility in the capital markets. Together, these conditions are putting significant pressure on borrowers' creditworthiness and will undoubtedly lead to increased defaults, with the magnitude of the effects varying substantially by industry, geography, and rating level. Currently, we expect the default rate to hit 10% by year-end, as collapsing demand from social distancing measures strains working capital, free operating cash flow, and liquidity; particularly for the weakest borrowers in the most at-risk industries.

Industries most exposed to the collapse in global demand—e.g., airlines, transportation, retail, gaming/casinos, lodging, oil and gas—or those heavily dependent on cross-border supply chains are likely to suffer most, both from slumping cash flows and much tighter financing conditions. S&P Global Ratings has already taken roughly 350 ratings actions on borrowers in North America at least partially due to the coronavirus outbreak's effects (see charts 1 and 2). Notably, the ratings on two large U.S. corporations—Ford Motor Co. and Delta Airlines Inc.—have slipped into speculative-grade. Both are vulnerable to slumping demand as consumer confidence crashes and job losses mount.

Protracted uncertainty regarding demand and supply/production disruptions are adding downside pressure to credit metrics across the rating spectrum. In terms of specific rating levels, we expect that companies rated 'B' and below will come under the most pressure, as these low ratings indicate higher vulnerability to adverse business and financial, and economic conditions. By contrast, we expect entities with investment-grade ratings to exhibit stronger resilience and have more flexibility to absorb the effects of a global recession—although this isn't to say we don't expect a certain number of rating actions on these companies, particularly for those in sectors most exposed to the economic disruption.

Meanwhile, companies' draws on bank credit facilities have surged and could exceed those during the Great Financial Crisis. But most banks are, in our view, better-positioned than they were then to handle this. Based on year-end 2019 data, banks subject to the liquidity coverage ratio (or LCR, a

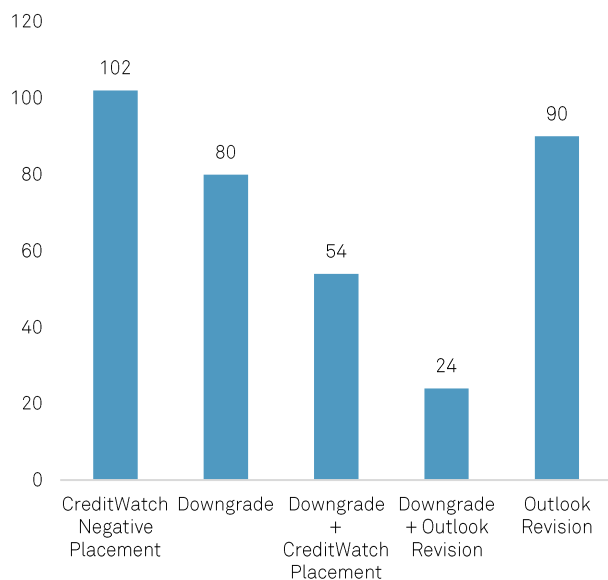
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rule requiring them to hold enough high-quality liquid assets to cover cash outflows for 30 days) assumed that about \$550 billion would be drawn. Banks have about \$2.9 trillion of assets to withstand these draws—so even if borrowers draw the full \$550 billion, banks’ median LCR would still be close to required levels. Moreover, bank-deposit inflows have been robust, and the Fed’s new round of quantitative easing should boost deposit levels further. And when borrowers draw on revolving credit lines, they typically deposit the funds in the banks whose lines they used.

Banks also have access to liquidity either by borrowing from the Federal Home Loan Bank or the discount window (with now longer payback terms). Moreover, the Fed has put in place facilities to help investment-grade corporates borrow without having to tap existing credit lines: the Commercial Paper Funding Facility, which helps them issue short-term commercial paper for working capital purposes; and the Primary Market Corporate Credit Facility, which helps them issue longer-term bonds.

Chart 1

North America COVID-19-Related Rating Actions As Of March 27, 2020

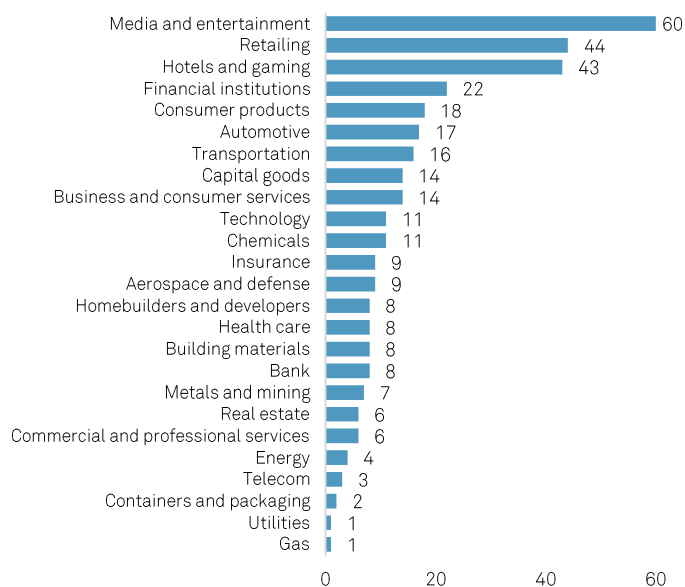


Note: These 350 rating actions pertain to ratings where we mention COVID-19 as one factor or in combination with others.

Source: S&P Global Ratings. COVID-19: Coronavirus-Related Public Rating Actions On Corporations And Sovereigns To Date, March 30, 2020.

Chart 2

North America COVID-19-Related Rating Actions By Sector As Of March 27, 2020



Note: These 350 rating actions pertain to ratings where we mention COVID-19 as one factor or in combination with others.

Source: S&P Global Ratings. COVID-19: Coronavirus-Related Public Rating Actions On Corporations And Sovereigns To Date, March 30, 2020.

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](http://www.spglobal.com/ratings)). As the situation evolves, we will update our assumptions and estimates accordingly. “[Coronavirus Impact: Key Takeaways From Our Articles](#)” periodically summarizes our latest research related to COVID-19.

This report does not constitute a rating action.

# Appendix 1: Top North America Risks

Table 1

## Top North America Risks

### Coronavirus outbreak widens substantially in the U.S.

**Risk level\*** Very low Moderate Elevated **High** Very high **Risk trend\*\*** Improving Unchanged **Worsening**

Some government authorities estimate the pandemic will peak about midyear. However, should this prove not to be the case, then a protracted and more prolonged period of coronavirus-containment measures will further amplify the current U.S. economic recession. Our base case assumes GDP growth rebounding in the second half as consumer demand revives and firms rush to fill back orders and restock inventories. Absent this bounce back, economic activity dependent on increased household discretionary spending will be lost—spilling over into hardening unemployment. The drag on business activity and cash-flow for borrowers across S&P Global Ratings could thus persist into 2021.

### Stresses on corporate funding continue to pressure credit quality

**Risk level\*** Very low Moderate Elevated **High** Very high **Risk trend\*\*** Improving Unchanged **Worsening**

Recent financial-market volatility underscores the liquidity and financing risks that many highly leveraged borrowers face. Fiscal stimulus and moves by the Federal Reserve to slash interest rates, repair market liquidity, and reinvigorate credit across the borrower universe may all help, but corporate bond spreads have widened sharply, especially at the speculative-grade level where issuance has all but disappeared. The build-up in corporate debt over the past decade has led to a concentration of investment-grade ratings in the 'BBB' category and spec-grade ratings in the 'B' category. In this light, investors and regulators are focused on transition and liquidity risk.

### Oil-price decline hurts Canada and U.S.

**Risk level\*** Very low Moderate Elevated **High** Very high **Risk trend\*\*** Improving Unchanged **Worsening**

Diminished global demand prospects coupled with the plunge in oil prices amid the OPEC-Russia squabble casts a shadow over the economies of Canada and the U.S.—both of which are net oil exporters. Not only will the price collapse put the oil and gas industry to the test, it may also hurt related sectors while weighing on oil-producing provinces/states.

### Trade disputes cloud world growth

**Risk level\*** Very low Moderate Elevated **High** Very high **Risk trend\*\*** Improving **Unchanged** Worsening

As companies and markets turn their focus to coronavirus, trade concerns have become less pronounced—though the uncertainty overhang continues to weigh on business confidence and growth forecasts. The "Phase One" deal between the U.S. and China doesn't fully address the dispute over technology, intellectual property, and market access, with the economic headwinds from the COVID-19 potentially hindering China's ability to fulfill its 2020 Phase One pledge. As such, trade tension can potentially reemerge and coincide the U.S. presidential election cycle. Meanwhile, the U.S. and Europe remain in disagreement over digital-services taxes, which may again exacerbate tensions.

### Cybersecurity threats to business activity

**Risk level\*** Very low Moderate **Elevated** High Very high **Risk trend\*\*** Improving **Unchanged** Worsening

Increasing global interconnectedness means cyber risk poses a systemic threat and significant single-entity risk. As cyberattacks become more sophisticated, new targets and methods are emerging. Companies and governments face the risk of criminal, proxy, and direct state-sponsored cyber-attacks. This has led to a fast-growing cyber-insurance market, though insured losses from cyber-attacks are still small compared with economic losses.

Sources: S&P Global Ratings.

\* **Risk levels** may be classified as very low, moderate, elevated, high, or very high, and are evaluated by considering both the likelihood and systemic impact of such an event occurring over the next one to two years. Typically these risks are not factored into our base case rating assumptions unless the risk level is very high.

\*\* **Risk trend** reflects our current view on whether the risk level could increase or decrease over the next 12 months.

## Appendix 2: COVID-19 Impact On North America Sectors

For analytical contacts, please see Appendix 4.

Table 2

### COVID-19 impact on North America sectors

| Sector                 | Impact* | Comment  |
|------------------------|---------|--|
| Aerospace & Defense    | High    | <p>The chilling effect of COVID-19 on air travel and the global economy will likely lead to order deferrals and cancellations. Cutbacks in airline capacity because of significant declines in air travel have reduced demand for aftermarket parts and services.</p> <p>Commercial aerospace companies will experience pressure in earnings and cash flow, and in turn see a reduction in headcount, furloughing employees, and other actions to offset some of the impact. Defense contractors are much less affected near-term.</p>   |
| Autos                  | High    | <p>Prolonged muted prospects for auto sales globally as the virus has impaired consumer discretionary spending this year. Specifically, we project that sales will decline 15%-20% in the U.S. Aftermarket suppliers are also under pressure, given less driving and sharply reduced consumer spending.</p> <p>Automakers have announced temporary production shutdowns and have switched to liquidity protection mode. However, during a complete production shutdown, a company's ability to cover its fixed costs deteriorates sharply, which would lead to faster cash burn.</p>   |
| Building Materials     | Medium  | <p>Supply chain risks from China have largely abated with good logistics and higher costs, so that inventories are stocked in western Europe and North America ahead of a sharp drop in demand in the important spring and summer selling seasons.</p> <p>Even though the total manufactured products exposure is 15-20%, various components could still cause a backup in output.</p>   |
| Capital Goods          | Medium  | <p>There has been direct impact from supply chain disruption as most issuers have facilities in China. From a demand standpoint, it is a growing concern as some issuers have meaningful exposure in China and outside the U.S.</p> <p>Company margins will likely suffer for 2020 due to lower production volumes and incremental operating expenses stemming from the effects of the COVID-19 pandemic.</p>  |
| Chemicals              | High    | <p>The pandemic and related recessionary conditions we expect across the globe will reduce demand this year for most chemical products. Exceptions to this reduction will include chemicals used in sanitation, and similar applications.</p> <p>We expect demand declines from key end markets including auto, and general industrial to reduce demand for both commodity and specialty chemicals, although commodity petrochemicals may be hit harder. Our base case considers a decline in EBITDA for many chemical companies relative to 2019, and a related weakening in credit metrics, which will create downward pressure on credit quality in general.</p>  |
| Consumer Products      | Medium  | <p>We expect a divergence in performance of sectors in the consumer products universe in the short term. U.S. consumer products companies in shelf-stable foods, home-cleaning products, and personal care are well-positioned to benefit from shelter-in-place mandates and consumers' health concerns. We believe this will have a modest positive impact on credit quality. This is attributable to the initial spike in demand from pantry loading and consumers now replenishing at a rapid rate because of shift to at-home consumption.</p> <p>That said, there is heightened risks for sectors exposed to social activity and discretionary spending. COVID-19 has heightened the risk of rating downgrades for consumer discretionary issuers, reduced revenues, and tight leverage headroom. Issuers with links to the retail and restaurant sectors are vulnerable.</p> |
| Financial Institutions | Medium  | <p>The Fed's return to quantitative easing, zero interest rates, and commercial paper (CP) funding and primary dealer credit facilities should bolster market and bank liquidity, lowering the probability banks will face liquidity strains resulting from the coronavirus crisis and bolstering their ability and willingness to meet client demands for funding.</p> <p>Still, the crisis and ultra-low interest rates could lead to substantially lower earnings and significantly worse asset quality, particularly in industries more affected by the virus outbreak.</p>  |
| Forest Products        | Medium  | <p>The impact has been limited because this is a highly automated industry often in remote areas or small urban centers in the U.S. and Canada, but has become a growing concern as we start to see a trickling effect that hinders commodity demand.</p>  |

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|                               |        | There is a greater risk of deficit and increased draws on credit facilities, mainly tied to the current uncertain macroeconomic, notably linked to COVID-19 and the potential for logistical disruptions.   |
| Gaming, Leisure & Lodging     | High   | <p>Given the rapid increase in reported restrictions, the travel downturn could persist into the second quarter. Containment may occur by the end of the second quarter followed by a slow recovery.</p> <p>Restrictions on travel and consumer activity for a prolonged period is causing cancellations and an unprecedented decline in revenue at travel-related companies and out-of-home entertainment providers. Gaming operator and gaming equipment sectors are facing an unprecedented decline in revenue resulting from the temporary closures of casinos across the U.S.</p>  |
| Health Care & Pharmaceuticals | Medium | <p>We anticipate limited rating actions for the health care universe. However, the situation is evolving and the longer and more widespread the outbreak, the higher the potential for more negative ratings actions.</p> <p>Hospitals, surgical centers, dental and other healthcare providers that rely on more discretionary, lower acuity procedures will see a significant decline in patient volume, and that can have an adverse ripple effect on manufacturers supplying the sector. Hospitals also face the potential that increased COVID-19 patients could stress near-term capacity and disrupt operations. Subsectors such as pharmaceuticals and life sciences may be more resilient, but would be increasingly hurt if the drop in activity were to become more prolonged.</p> |
| Homebuilders                  | Medium | <p>U.S. homebuilders are seeing a negative effect on foot traffic now, which has turned into better sales conversion from more serious buyers.</p> <p>Looking ahead, however, job losses and potential construction site closures cloud the picture for new orders over the next few months in a previously healthy U.S. housing market.</p>  |
| Insurance                     | Medium | <p>Volatile financial market and recessionary economic conditions test balance sheet strength of the U.S. insurance sector. Asset risk is the most immediate risk factor. P/C insurers hold record unaffiliated common stock. Life insurers' high 'BBB' exposure presents elevated credit risk from corporates most vulnerable to the containment measures and the energy sector.</p> <p>Unprecedented low interest rates pressure life insurers' reserve adequacy and spread income prospects. However, the sector has been effectively navigating this headwind for over a decade.</p>  |
| Media & Entertainment         | High   | <p>The pandemic is having meaningfully immediate negative impact across event organizers, live-events companies, travel-related companies, and movie exhibitors. More than 25 ratings actions on those sectors most exposed have already been taken.</p> <p>The broadest threat to media is a pullback in advertising spending. Advertising, which remains a key revenue component for much of the media industry, is already being reduced for certain media subsectors, with little ability to offset the majority of the declines.</p>   |
| Metals & Mining               | High   | <p>Copper &amp; steel inventories rose as COVID-19 led to an industrial slowdown in China, demand-pull for intermediate metals products globally has stalled as the outbreak has spread.</p> <p>Expect several rating actions within the following weeks because of our lower metal price assumptions (lower by 5%-10%). High yield issuers could breach leverage triggers with 2021 maturities on the horizon.</p>   |
| Midstream Energy              | High   | <p>The combination of the pandemic and the oil price war is hurting the U.S. midstream energy sector. Volume declines and counterparty credit quality are the top risks to the sector but the severity of these risks to midstream credit profiles is uncertain.</p> <p>Investment-grade companies are better-positioned than their spec-grade peers to deal with the severe supply and demand shocks as many companies are self-funding, credit facilities have been extended, and liquidity on revolvers is sufficient. Spec-grade companies are unable to access the capital markets and a prolonged downturn will likely cause significant credit deterioration in 2021.</p>  |
| Oil & Gas                     | High   | <p>The industry is facing a severe supply-demand imbalance. The price of oil has plummeted, political risks have amplified, and producers are facing negative investor sentiment, capital markets access, and coronavirus concerns.</p> <p>We assume Brent oil price will recover to US\$50/bbl level in 2021 from US\$30/bbl this year based on our expectation that COVID-19 will be contained this year leading to demand recovery; and both OPEC and Russia might come up an agreement or some U.S. shale players will be forced out of market.</p>   |
| Oil Refineries                | High   | <p>Independent oil refiners' margins are under pressure from falling demand, and the drop in oil prices may significantly impact working capital and reduce cash positions.</p> <p>We believe first quarter EBITDA will be weaker than expected, due to the substantial decline in demand for jet fuel and gasoline. Cracks for both products has been negative at times, and anemic</p>  |

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|                      |        | demand in the second quarter will likely require massive cuts to utilization. A prolonged demand response due to COVID-19 could damage credit quality.  |
| Public Finance       | Medium | <p>USPF is seeing pressure sector wide, some on the revenue side (transport, higher education, sales tax collections), and others from growing expenditures (health care).</p> <p>The volatility ties directly to credit deterioration; in cases where revenue growth is slowing and expenditures are rising, the imbalance can grow quickly.</p>   |
| REITs                | Medium | <p>The indirect impact from sharply slower economic growth and financial market volatility could be felt across all property types as the effects of social distancing, travel restrictions, and lower oil prices will take time to deteriorate the financial health of tenants.</p> <p>We expect rating downside on North American REITs to be mitigated by key credit strengths underpinning the sector, including cash flow stability, tenant diversity, and better balance sheets relative to the prior recession.</p>  |
| Regulated Utilities  | Low    | <p>We believe that the majority of North American regulated utilities are well-positioned to handle the immediate impact of COVID-19. However, the pandemic could hurt some companies, especially those issuers already facing downside ratings pressure prior to the arrival of the coronavirus.</p> <p>Some electric utilities with disproportionate exposure to commercial and industrial class of customers could be vulnerable to reduced sales volumes, absent any regulatory counter mechanisms such as decoupling.</p>  |
| Retail & Restaurants | High   | <p>Credit risks to the retail and restaurant sector have increased dramatically as the effort to contain COVID-19 results in store closures, changes to shopping habits, and heightened risk of a broad based macroeconomic decline.</p> <p>Sales will likely decline substantially in the short-term, with the hardest-hit issuers in casual dining and retail exposed to social distancing and discretionary spending (e.g., mall-based retailers). There are rating actions across the spectrum taking place with the vast majority concentrated in these retail segments.</p>   |
| Sovereign            | Low    | <p>We expect investment-grade sovereigns will show stronger resilience and more flexibility to withstand the shock. The ratings of countries with greater economic resilience, stronger financial profile, and better policy-making are likely to come under less pressure compared with others.</p> <p>In contrast, those at the lower end of our scale are more vulnerable to downgrades, given their inherently weaker finances and greater vulnerability to global shocks.</p>  |
| Structured Finance   | Medium | <p>Given the forecasts for weaker economic growth and higher unemployment, we expect some weakening in structured finance collateral performance, which was stable through most of the first quarter. Further, our ratings outlook has turned cautious, and we predict a stable-to-negative or negative trend for certain sectors. Risks remain to the downside, especially if economic forecasts worsen.</p> <p>Although we note that the ultimate impact of the COVID-19 pandemic yet uncertain, we believe it is likely to affect some sectors more than others. Current areas of focus include CLOs, whole business ABS, small business ABS, aircraft ABS, subprime auto ABS (non-IG), dealer floorplan ABS, retail &amp; lodging backed CMBS, and non-QM RMBS.</p> |
| Technology           | Medium | <p>COVID-19 will hurt enterprise and consumer IT spending, particularly, hardware and semiconductor segments. However, we expect some of the deferred spending to return gradually in the latter half of this year through heavy government stimulus in the U.S., China, and elsewhere.</p> <p>We expect significant negative ratings actions throughout the year as the impact of the revenue deferral, or revenue destruction in some cases, begins to emerge. Liquidity is a key concern among speculative-grade issuers given the market dislocation.</p>   |
| Telecom              | Low    | <p>Telecom and cable providers can withstand the effects of a surge in COVID-19 cases with limited impact to credit quality given their recurring, subscription-based business models.</p> <p>There are a handful of companies that have exposure to vulnerable sectors such as transportation and tourism, which could hurt their financial and operating performance in the near-term. In addition, issuers that have exposure to small- and mid-sized business customers are at risk since they are most likely to churn in a recession.</p>   |
| Transportation       | High   | <p>The ultimate impact of the coronavirus outbreak on our global airline ratings will depend on the duration and severity of the crisis, and the type and severity of measures airlines and governments take to mitigate it. Capacity reductions, along with sharply lower oil prices, will be insufficient to offset the decline in its travel demand.</p> <p>The global airline sector has weakened substantially and the pandemic threatens credit quality of operators. The aircraft-leasing sector should fare better than airlines in this coronavirus-related</p>  |

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economic downturn, but will still face pressure on their revenues and cash flow. Freight transportation is less affected but will be hurt indirectly through the unfolding global recession.

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|------------------------------|--------|--|
| Unregulated (Merchant) Power | Medium | <p>Most merchant power companies engage in ratable hedging and a high proportion—typically 90%—of their 2020 economic generation is hedged. Still, we expect companies with load shape risk (volumetric risk in hedges) and/or a higher proportion of Large commercial and industrial (LCI) customers will be disproportionately affected. We expect some companies that do not have a countercyclical retail power business to offset the risks in wholesale power business to experience some credit pressures should the current environment last into the third quarter.</p> <p>With average peak electric demand showing signs of declining about 10% at this stage, prompt and forward prices will decline. Decline in forward prices will expose these companies to backwardation in future cash flows due to lower priced hedges, or the prospects of higher merchant exposure in the hope for better pricing discovery later in the year.</p> |
|------------------------------|--------|--|

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\*The impact descriptor above (high, medium, low) is our qualitative view of the risk. It does not directly translate to risk of rating actions, which depend on a number of factors including initial headroom under a rating coupled with the expected length and severity of the epidemic.



## Appendix 3: Economic Data And Forecast Summaries

Table 3

### U.S. – S&P Global Ratings Economic Outlook

|   | 2019     | 2020f  | 2021f  | 2022f    | 2023f    |
|---|----------|--------|--------|----------|----------|
| Real GDP (year % ch.)   | 2.3      | -1.3   | 3.2    | 2.5      | 2.0      |
| Real consumer spending (year % ch.)                               | 2.6      | -1.4   | 2.6    | 2.8      | 2.2      |
| Real equipment investment (year % ch.)                            | 1.3      | -6.3   | 6.3    | 5.6      | 4.3      |
| Real nonresidential structures investment (year % ch.)            | -4.3     | -11.8  | 4.9    | 4.7      | 3.1      |
| Real residential investment (year % ch.)                          | -1.5     | 1.9    | 2.7    | 3.0      | 3.2      |
| Core CPI (year % ch.)   | 2.2      | 0.9    | 1.9    | 2.8      | 2.3      |
| Unemployment rate (%)   | 3.7      | 7.1    | 5.7    | 4.7      | 3.8      |
| Housing starts (annual total in mil.)                             | 1.3      | 1.3    | 1.3    | 1.3      | 1.3      |
| S&P Case-Shiller Home Price Index (Dec. to Dec. % ch.)            | 3.5      | 3.5    | 2.3    | 2.3      | 3.3      |
| Federal Reserve's fed funds policy target rate range (year-end %) | 1.5-1.75 | 0-0.25 | 0-0.25 | 0.5-0.75 | 1.25-1.5 |

Note: All numbers are in annual average basis, except the Fed's policy rate and housing starts. Core CPI is consumer price index excluding energy and food components. f—forecast. Forecasts were generated before the third estimate of Q4 2019 GDP was published by the BEA. Source: Oxford Economics, S&P Global Economics Forecasts.

Table 4

### Canada – S&P Global Ratings Economic Outlook

|   | 2019 | 2020f | 2021f | 2022f |
|---|------|-------|-------|-------|
| Real GDP (year % ch.)                               | 1.6  | -2.0  | 3.4   | 2.0   |
| Real consumer spending (year % ch.)                 | 1.6  | -0.8  | 2.8   | 2.3   |
| Real private business fixed investment (year % ch.) | -0.8 | -4.7  | 4.5   | 3.2   |
| Core CPI (year % ch.)                               | 2.1  | 1.7   | 1.9   | 1.7   |
| Unemployment rate (%)                               | 5.7  | 6.7   | 6.0   | 5.5   |
| Housing starts (annual total in thousands)          | 209  | 195   | 198   | 207   |
| CAD/USD exchange rate (per US\$1)                   | 1.33 | 1.40  | 1.37  | 1.34  |
| Government of Canada 10-year bond yield (%)         | 1.59 | 1.18  | 1.47  | 1.50  |
| Bank of Canada overnight rate (% end of period)     | 1.75 | 0.25  | 0.75  | 1.00  |

Note: All numbers are in annual average basis, except central bank rates and housing starts. Core CPI is consumer price index excluding energy and food components. f—forecast. Source: StatCan, Oxford Economics, S&P Global Economics Forecasts.

## Appendix 4: List Of Analytical Contacts

| Sector                        | Analyst Name and Contact  |
|-------------------------------|---|
| Aerospace & Defense           | <b>Philip Baggaley</b><br>+1 (212) 438-7683<br>philip.baggaley@spglobal.com   |
| Autos                         | <b>Philip Baggaley</b><br>+1 (212) 438-7683<br>philip.baggaley@spglobal.com   |
| Building Materials            | <b>Donald Marleau</b><br>+1 (416) 507-2526<br>donald.marleau@spglobal.com     |
| Capital Goods                 | <b>Ana Lai</b><br>+1 (212) 438-6895<br>ana.lai@spglobal.com                   |
| Chemicals                     | <b>Paul Kurias</b><br>+1 (212) 438-3486<br>paul.kurias@spglobal.com           |
| Consumer Products             | <b>Diane Shand</b><br>+1 (212) 438-7860<br>diane.shand@spglobal.com           |
| Financial Institutions        | <b>Stuart Plesser</b><br>+1 (212) 438-6870<br>stuart.plesser@spglobal.com     |
| Forest Products               | <b>Donald Marleau</b><br>+1 (416) 507-2526<br>donald.marleau@spglobal.com     |
| Gaming, Leisure & Lodging     | <b>Emile Courtney</b><br>+1 (212) 438-7824<br>emile.courtney@spglobal.com     |
| Health Care & Pharmaceuticals | <b>Arthur Wong</b><br>+1 (416) 507-2561<br>arthur.wong@spglobal.com           |
| Homebuilders                  | <b>Donald Marleau</b><br>+1 (416) 507-2526<br>donald.marleau@spglobal.com     |
| Insurance                     | <b>Joseph Marinucci</b><br>+1 (212) 438-2012<br>joseph.marinucci@spglobal.com |
| Media & Entertainment         | <b>Naveen Sarma</b><br>+1 (212) 438-7833<br>naveen.sarma@spglobal.com         |
| Metals & Mining               | <b>Donald Marleau</b><br>+1 (416) 507-2526<br>donald.marleau@spglobal.com     |
| Midstream Energy              | <b>Michael Grande</b><br>+1 (212) 438-2242<br>michael.grande@spglobal.com     |
| Oil & Gas                     | <b>Thomas Watters</b><br>+1 (212) 438-7818<br>thomas.watters@spglobal.com     |
| Oil Refineries                | <b>Michael Grande</b><br>+1 (212) 438-2242<br>michael.grande@spglobal.com     |
| Public Finance                | <b>Jane Ridley</b>  |

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|                                 |  |
|---------------------------------|--|
|                                 | +1 (303) 721-4487<br>jane.ridley@spglobal.com  |
| REITs                           | <b>Ana Lai</b><br>+1 (212) 438-6895<br>ana.lai@spglobal.com  |
| Regulated Utilities             | <b>Gabe Grosberg</b><br>+1 (212) 438-6043<br>gabe.grosberg@spglobal.com  |
| Retail & Restaurants            | <b>Sarah Wyeth</b><br>+1 (212) 438-5658<br>sarah.wyeth@spglobal.com  |
| Sovereign                       | <b>Joydeep Mukherji</b><br>+1 (212) 438-7351<br>joydeep.mukherji@spglobal.com  |
| Structured Finance              | <b>Winston Chang</b><br>+1 (212) 438-8123<br>winston.chang@spglobal.com<br><br><b>James Manzi</b><br>+1 (202) 383-2028<br>james.manzi@spglobal.com |
| Technology                      | <b>David Tsui</b><br>+1 (415) 371-5063<br>david.tsui@spglobal.com  |
| Telecom                         | <b>Allyn Arden</b><br>+1 (212) 438-7832<br>allyn.arden@spglobal.com  |
| Transportation                  | <b>Philip Baggaley</b><br>+1 (212) 438-7683<br>philip.baggaley@spglobal.com  |
| Unregulated (Merchant)<br>Power | <b>Aneesh Prabhu</b><br>+1 (212) 438-1285<br>aneesh.prabhu@spglobal.com  |

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