

Sector Roundup Asia-Pacific Q3 2022:

Inflation And China: Rough Ride Ahead

July 4, 2022

This report does not constitute a rating action

Key Takeaways

- **Rising costs intersect the economic slowdown.** Asia-Pacific is bracing for the double impact of surging input prices and higher borrowing costs. Inflation is eroding firms' margins and consumers' purchasing power. Market volatility is exacerbating risk aversion among lenders. This is driving tighter liquidity access, particularly for weaker-rated borrowers seeking to refinance. With China's property problems and sporadic COVID lockdowns hindering activity, we have lowered the country's expected growth in 2022 to 3.3% from 4.2%. For Asia-Pacific, expected growth falls to 4.2% from 4.6%.
- **Collision debris.** Weak global demand and subdued consumption will crimp firms' cost pass-through ability. Sectors recovering from COVID's earlier hit, and those reliant on discretionary spending, will feel the pain most. Weaker creditworthiness among corporates and households could spill over to other sectors. Banks and structured finance markets will face deteriorating borrower profiles. Meanwhile, external challenges could intensify fiscal burdens of local and regional governments, especially those in China already contending with property strains and COVID restrictions.
- **Potholes and pain abound.** Amid global and regional headwinds, the net rating outlook bias of Asia-Pacific issuers has deteriorated to negative 7% as of end-May, from negative 5% at end-February. More than half of our rated corporate sectors in the region face a worsening rating outlook bias, signaling more pain to come.

(Editor's Note: This report is an expansion of the "Sector Trends" section from our "Credit Conditions: Asia-Pacific Q3 2022: Costs Heighten, China Growth Tightens" report, published June 28, 2022.)

Inflation to sting. Producer and consumer prices are rising across the region. Amid slowing regional growth, and a possible shift to more selective consumer spending, the ability of corporates to pass through costs will be tested. This could squeeze profit margins and revenues, denting credit and financial buffers for the region's corporates, particularly the midstream and downstream industries (e.g., capital goods, chemicals, and building materials). And as higher food and energy prices bite, disposable income may fall, which would make consumer discretionary sectors (such as consumer products, hotels, gaming and leisure, and retail) especially vulnerable.

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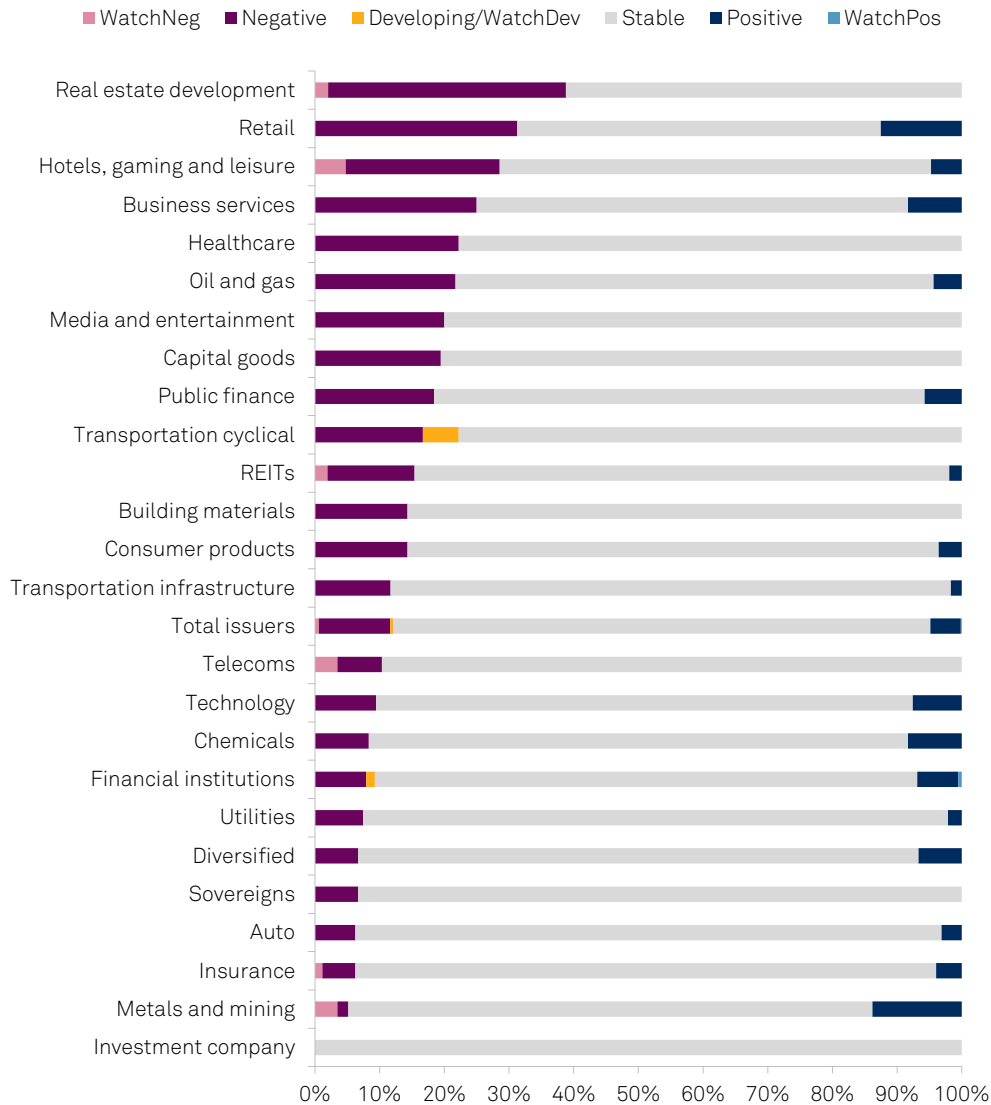
Debt-servicing costs to bite. Fears of global recession and U.S. stagflation have sparked market volatility and weakened investor confidence. Since January 2022, Asia-Pacific equities have tumbled by over 20% while the region's five-year government bond yields spiked by almost 150 basis points (bps) on average. Central banks across Asia-Pacific--except for those of China and Japan--have had and will continue to track the U.S. Federal Reserve's movements in raising policy rates. However, their currencies could depreciate if the magnitude and pace of rate hikes fail to catch up with those of the Fed. A weaker currency would favor the region's exporters but imported inflation (components) could hit corporates' profitability. Meanwhile, investors' demands for higher nominal yields (to offset higher inflation) could amplify debt-servicing costs and erode corporates' rating headroom. Risk-averse lenders are tightening lending standards, which may cause more pain for weaker-rated issuers and borrowers with substantial foreign-currency obligations due or looming debt maturity walls.

Lockdowns to stay. Most Asia-Pacific countries are shifting toward "living with COVID" whereas China, in stark contrast, is persevering with its dynamic-zero COVID policy. Sporadic lockdowns across cities and towns have hit consumption and economic growth. This is causing acute pain for mobility dependent sectors, and small and midsize enterprises (SMEs), raising concerns about unemployment and weaker investor confidence. In the beleaguered Chinese property sector, weaker sales and delays to housing construction and delivery are exacerbating the stress. Subsequently, we have trimmed China's GDP growth in 2022 to 3.3% from 4.2%. Meanwhile, Chinese local and regional governments could see additional debt burden risks if they turn to leveraging their state-owned enterprises (SOEs) in part to stimulate local economic growth, while concurrently providing support to these SOEs. The spillover from China's zero COVID tolerance could hurt countries that depend on tourism, exports, and imports of components.

Brace, brace. Potholes and pain points abound for Asia-Pacific issuers, in the face of additional credit headwinds from outside the region. Fears of persisting high inflation in the U.S. and ongoing energy market dislocations due to the Russia-Ukraine war are causing greater market volatility and rising macro uncertainties. Our net rating outlook bias across asset classes has worsened to negative 7% as of end-May (see table 1). Of the 21 corporate sectors we cover, 12 sectors had a worsening net outlook bias as of May 31, 2022, compared with seven in Feb. 28, 2022.

Chart 1

Outlook Distribution Of Asia-Pacific Issuers By Sector



Data cut-off is at May 31, 2022.

Source: S&P Global Ratings.

Table 1

Net Outlook Bias Of Asia-Pacific Issuers By Sector, May 31, 2022

	May 2021	Aug 2021	Oct 2021	Feb 2022	May 31, 2022	No. of entities	Notional average rating
Auto OEM and suppliers	-42%	-24%	-12%	-3%	-3%	32	BBB
Building materials	0%	-6%	-6%	-7%	-14%	14	BBB-
Business services	-21%	-8%	-25%	-23%	-17%	12	BB+
Capital goods	-19%	-17%	-17%	-29%	-19%	36	BBB
Chemicals	-20%	-13%	-7%	0%	0%	36	BBB-
Consumer products	-3%	-4%	-4%	-8%	-11%	28	BBB
Diversified	0%	13%	13%	20%	0%	15	A-
Healthcare	-14%	-14%	-14%	-11%	-22%	9	BB+
Hotels, gaming, and leisure	-45%	-25%	-20%	-19%	-24%	21	BB+
Investment company	-11%	0%	0%	0%	0%	8	A-
Media and entertainment	-22%	-20%	-20%	-20%	-20%	10	BBB+
Metals and mining	-9%	5%	11%	9%	9%	58	BB+
Oil and gas	-16%	-21%	-21%	-26%	-17%	23	BBB+
Real estate development	-13%	-12%	-18%	-32%	-39%	49	BB-
Real estate investment trusts	-11%	-8%	-12%	-12%	-13%	52	BBB+
Retail	-29%	-29%	-29%	-31%	-19%	16	BBB
Technology	-8%	0%	0%	0%	-2%	53	BBB-
Telecommunications	-26%	-24%	-21%	-7%	-10%	29	BBB+
Transportation cyclical	-32%	-26%	-11%	-11%	-17%	18	BBB-
Transportation infrastructure	-20%	-10%	-8%	-7%	-10%	60	A-
Utilities	-2%	-4%	-5%	-4%	-5%	94	BBB+
Total corporates	-15%	-10%	-9%	-9%	-10%	673	BBB
Financial institutions	-6%	-1%	1%	3%	-1%	378	BBB+
Insurance	-3%	-2%	-1%	-3%	-2%	176	A
Public finance	-19%	-16%	-14%	-13%	-13%	87	A+
Sovereign	-14%	-10%	-7%	-7%	-7%	30	BBB+
Total issuers	-11%	-7%	-5%	-5%	-7%	1,344	BBB+

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 Demand softness	Margin pressure Resilient balance sheet
Building materials	Lower profitability on input cost hike Weaker-than-expected recovery in China for the rest of 2022	High energy costs to stay
Capital goods	Slower recovery and margin erosion Aggressive spending but weaker cash flow	Slower recovery in credit measures
Chemicals	Weaker chemical demand Cost inflation	Weakening albeit still healthy product spreads
Consumer products	Inflation Higher working capital needs	Divergence across the region
Financial institutions	Economic downside risks intensify	Revised economic base case holds Highly supportive governments
Gaming	Regulatory risks Uncontrolled COVID cases	Gaming visits to return
Insurance	Persistent market volatility Increasing frequency of natural disasters	Capital buffer will narrow
Media and entertainment	Macro slowdown and further lockdown measures in China Tightening capital markets could exacerbate liquidity issues	Revenue growth in the slow lane
Metals and mining	Subdued growth slowing China's commodities demand Russia-Ukraine conflict adds to supply disruptions, adding volatility to prices China's decarbonization drive to move markets	China's slower growth Elevated prices point to another year of strong profits and cash flow
Oil and gas	Demand shock Government intervention Urgency for the energy transition	Brent at US\$100/barrel and Henry Hub at US\$8.25 per metric million British thermal unit (mmBtu) for 2022 Investment in hydrocarbon reserves and renewable assets
Public finance	Economic shock Delayed fiscal recovery	Public finance systems largely stable
Real estate development	COVID resurgence could slow Chinese developers' sales recovery Structural supply shortage continues to support home prices in Hong Kong Indonesian developers' credit quality will remain largely stable despite moderating sales growth	We expect an "L-shaped" recovery in Chinese developers' contracted sales
Real estate investment trusts	Structural shift continues Lower occupancies	Steady credit outlook
Retail	Household consumption slumps China's stringent COVID policy	EBITDA margins to be squeezed
Sovereign	Sudden capital swings Growth and fiscal recoveries interrupted	Global economic activity recovers, albeit less robustly than earlier expected

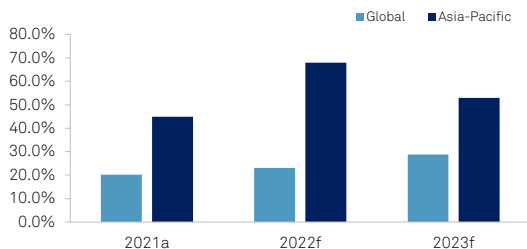
Summary of Key Risks and Assumptions for Asia-Pacific's Industries (cont.)

Sector	Key risks	Key assumptions
Structured finance	Inflation and its impact on households Effect of COVID policies in China	Structural supports
Technology	Macroeconomic risks emerge Logic semiconductor oversupply in 2023	Further slowdown in global IT spending
Telecommunications	Intense competition Cost inflation	Mergers and restructurings
Transportation cyclical	Liquidity crunch Energy cost	Air traffic recovery is uneven and passenger volumes remain below pre-pandemic levels
Transportation infrastructure	Return of government restrictions or border closures due to new variant Weakened government fiscal positions dampen support in most of Asia-Pacific	Air traffic to recover but international will remain well short of pre-COVID levels Inflation and supply chain risks rising
Utilities	Aggressive pace of new investments and funding Supply chain issues Interest rate risks	Profitability will be mixed across markets Capital expenditure to lift

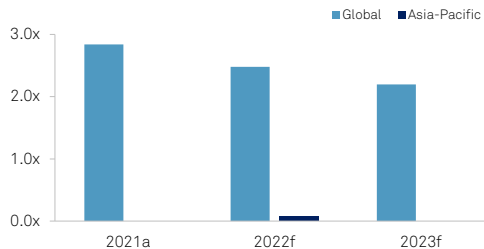
Auto

Carmakers To Brace For Tougher Industry Conditions

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

- Prolonged supply-chain disruption and slower economic growth are dampening auto production and sales in Asia-Pacific.
- We see increasing margin pressure on the sector because of the softer demand outlook, production inefficiencies, and higher input costs.
- Most rated auto companies have the financial strength to withstand tough industry conditions and maintain their credit quality over the next 12-24 months.

What's changed?

Deteriorating prospects for auto sales. Supply-chain bottlenecks, disruption from China's efforts to curb COVID-19, the Russia-Ukraine conflict, and high inflation in the U.S and Europe are suppressing global auto production and sales. We now anticipate China's light vehicle sales could decline by up to 3% in 2022, compared with our previous assumption of 1%-3% growth.

Key risks

Supply chain disruption. Component shortages and logistics hurdles have eased materially in China following the lifting of lockdown measures in Shanghai. We expect automakers and suppliers' capacity utilization to normalize to pre-lockdown levels in the second half. However, a resurgence of COVID-19 and any similar lockdown measures in other auto manufacturing hubs in China would disrupt the supply chain again. Meanwhile, the industry continues to suffer from tight chip supply. Auto manufacturers that rely on a rigid supplier network are suffering more than carmakers that have flexible chip procurement.

Demand softness. China's slowing economy and rising unemployment are weakening household purchasing power. Despite the government's stimulus measures, macro uncertainties could cause consumers to avoid spending on big-ticket items. As such, we see higher uncertainty in auto demand.

Key assumptions

Margin pressure. Operational inefficiencies amid the pandemic and elevated raw material prices continue to squeeze auto companies' profitability and working capital. Those better placed to absorb the impact include producers with improving product portfolio--and hence rising average selling prices--and more stringent cost control measures.

Resilient balance sheet. Increasing earnings pressure and continued investment in electrification could weigh on the cash flow of rated auto companies. Nevertheless, most of them have the financial strength to withstand industry adversities and will remain in low leverage or net cash positions.

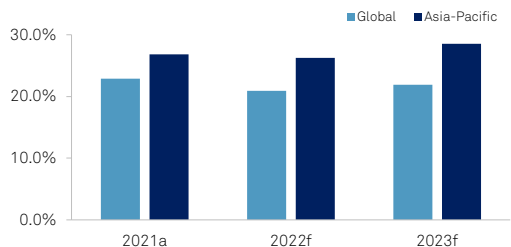
What to look for

China's COVID policy. The pandemic-induced lockdown in the country has disrupted the region's supply chain. Similar restriction measures in other important auto hubs will worsen the supply bottleneck.

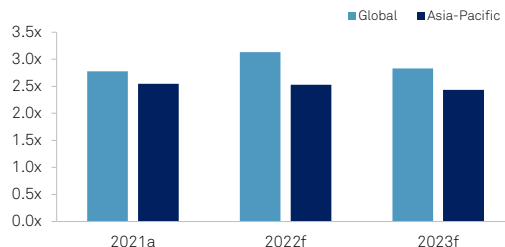
Building Materials

Diverging Recovery From COVID Across The Region

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. Includes "Forest products, building materials, and packaging" entities. FFO--Funds from operations. a--Actual. f--Forecast.

Key Takeaways

- Diverging recovery from COVID across the region--with China lagging versus moderate recovery in the Australian and Korean market.
- Key risks include rising costs eroding margins and weaker-than-expected recovery in China in the second half of 2022.
- Industry consolidation and carbon trading will benefit industry leaders.

What's changed?

Diverging recovery from COVID. The shockwaves from China's COVID lockdown and the stressed property sector have hit construction activities, spurring a decline in demand and weakening in prices. On the other hand, the Australian and Korean markets show a moderate recovery, where the easing of COVID restrictions has meant limited disruption of construction. In Australia, the pipeline for detached housing projects remains strong despite an extension in completion times. In Korea, the healthy sentiment is supported by the expectation the president will seek to boost housing supply projects and deregulate reconstruction.

Key risks

Lower profitability on input cost hike. Higher costs on fuel, raw materials, and labor pose a risk to corporate profitability. A larger-than-expected drop in selling prices because of sluggish demand in China will impede the ability of building materials producers to fully pass through the cost inflation to downstream. Australian and Korean corporates face relatively lower risk because more robust demand supports hikes in selling price.

Weaker-than-expected recovery in China for the rest of 2022. A slower-than-expected economic recovery, including a weak ramp-up of property and infrastructure construction projects, could continue to pressure demand. China's zero-COVID policy will also result in occasional regional lockdowns, which might interrupt the transportation of end products and construction.

Key assumptions

High energy costs to stay. Thermal coal is the major energy source for building materials producers. Corporates with limited long-term coal supply contracts would be more exposed to volatile coal prices. We expect coal prices to remain high in 2022. Several factors are constraining supply, including the Russia-Ukraine conflict, the escalating sanctions on Russia, and tight supply because of wet weather in Australia and Indonesia.

What to look for

Industry consolidation and carbon trading. The financial strength of China's leading cement manufacturers means they stand to benefit most from industry consolidation, in our view. Industry leaders are also able to meet tighter environmental requirements by investing in new technologies. Carbon trading will likely benefit players with lower emissions. We expect more countries to introduce their own emission-trading systems, but the impact on the sector will depend on the design of the schemes and the price of carbon.



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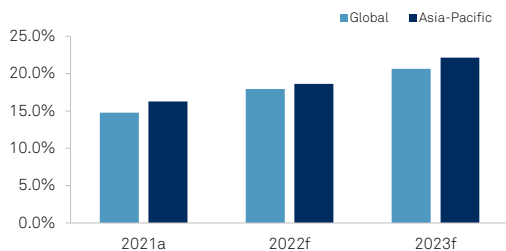
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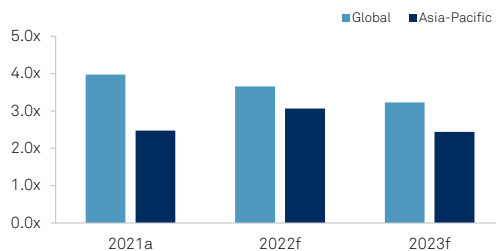
Capital Goods

Inflation And COVID Dampen Profitability And Leverage Improvements

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

- We expect the pace of recovery in earnings and leverage to be slower than previously assumed.
- Other key risks include margin erosion because of increased costs, and corporate customers' weaker sentiment on spending.
- Demand outlook and the degree of margin protection, as well as cash flow management, will be key drivers for credit quality.

What's changed?

Despite an improvement, rating-outlook bias has been outpaced by downward action. As a result of active rating actions, the net outlook bias improved to negative 19% at end-May 2022 from negative 29% a quarter earlier. Rating actions varied but downward actions outpaced upward actions. We believe this reflects our weakening view of earnings recovery and leverage improvement.

Key risks

Slower recovery and margin erosion. Continued shortages in key components, and higher materials and logistics costs may further dampen the recovery in earnings. If capital goods companies fail to pass the increased costs to customers, margins will likely weaken. COVID-19 lockdowns in China and uncertainties caused by the war in Ukraine may weaken economic activities and depress investment sentiment of corporate customers, delaying decisions on capital spending.

Aggressive spending but weaker cash flow. Capital expenditures (capex) are likely to increase for capital goods companies alongside the ongoing, albeit slower, recovery in earnings and cash flow. However, supply chain disruptions and inflation are eroding cash flow. If cash flow deteriorates further because of mismanagement of working capital or weaker demand, credit measures will be strained.

Key assumptions

Slower recovery in credit measures. Global growth has slowed, but we continue to assume increasing corporate capital investment, though at lower levels than previously assumed. We expect the earnings recovery among Asia-Pacific capital goods companies to persist. However, momentum will slow and delay the recovery back to pre-COVID levels.

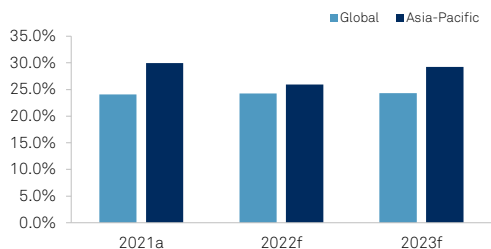
What to look for

Demand outlook and capability to protect margins. The pace and extent of the earnings recovery will depend on the sentiment of capital goods customers. The extent to which capital goods companies can pass on cost hikes to customers will determine the impact on profitability. Meanwhile, a key trend to watch will be the recent currency depreciation. We view this as broadly neutral for Chinese companies and slightly positive for Japanese companies.

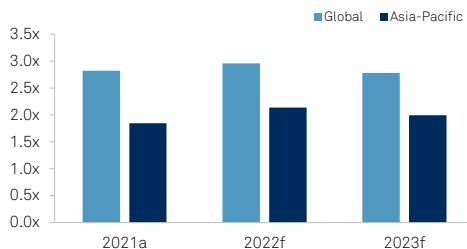
Chemicals

Strong Balance Sheet Could Ease Downside Risk On Profitability

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

- We expect profitability in 2022 to be weaker than earlier assumptions but remain above the average of past cycles.
- Rising oil prices, growing supply, and a weaker demand outlook could pose further downside risk on profitability for the rest of the year.
- Strong balance sheets and a healthy cash position after a robust 2021 could cushion downside risk on profitability.

What's changed?

Weaker demand outlook and high input costs amid rising supply. Rising supply in China could prevent chemical companies in Asia from fully passing on to customers the higher costs associated with rising oil prices. Further deterioration in the demand outlook because of the slowing Chinese economy and supply chain disruptions caused by the conflict between Russia and Ukraine could exacerbate margin contraction.

Key risks

Weaker chemical demand. An unexpected downturn in global GDP could cause weaker exports and consumption in Asia, leading to weaker demand for chemicals.

Cost inflation. Chemical companies, especially commodity producers, may not be able to pass through rising input costs if market conditions become less favorable. Rising supply, particularly in China, could suppress chemical companies' pricing power while further increases in oil and energy prices could drive feedstock and other costs higher.

Key assumptions

Weakening albeit still healthy product spreads. Chemical companies could still largely pass on high input costs to sustain healthy margins in 2022. However, the pass-through ability could be weaker for companies that are more dependent on commodity chemicals (such as propylene and PTA) because of significant capacity additions across the region.

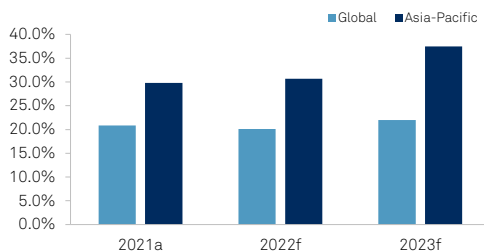
What to look for

Rising downside. Strong balance sheets and high cash balances will provide room to absorb a likely demand shock on the profitability of chemical companies. We expect companies to maintain adequate credit metrics over the next 12 months.

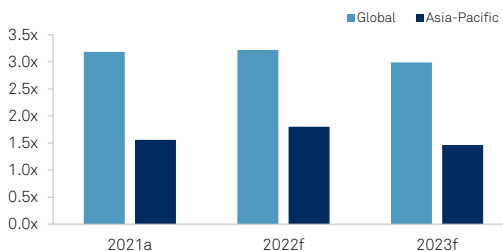
Consumer Products

Weak Demand And Inflation To Hit Chinese Discretionary Goods

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

- China's zero-COVID policy is hurting consumption and may further temper sentiment.
- Elevated material costs could erode margins and push up inventory in Asia-Pacific.
- Credit quality will depend on the ability of companies to pass through cost increases, adapt to changing consumer habits, and maintain balance-sheet strength.

What's changed?

Fragile consumption in China. Regional lockdowns under the country's zero-COVID policy and high unemployment could further temper retail sales, particularly among discretionary goods and food services throughout the year. Staples demand will be fairly resilient, but the premiumization trend may stall amid the weaker growth outlook.

Key risks

Inflation. Raw material costs could stay high throughout the year and hurt margins. Weakening Asia-Pacific currencies against the U.S. dollar could add to inflationary pressure for firms relying on imported ingredients. Inflationary pressure will be acute for firms with a high material input cost structure, and a weak ability to pass on cost increases, particularly price takers and weaker brands.

Higher working capital needs. Higher safety stocks to avoid logistics disruptions as well as inflationary prices will lead to greater inventory along the supply chain, resulting in increased cash outflow.

Key assumptions

Divergence across the region. China's zero-COVID policy will depress consumption. Meanwhile, slower GDP growth and the negative wealth effect from higher unemployment could further dampen discretionary sales in China in coming quarters. Outside China, the region's governments are shifting to living with COVID. This will spur mobility and raise consumer sentiment. That said, the rise in consumer spending could be suppressed in countries that rely heavily on imports or are experiencing higher food price inflation (such as Japan and India).

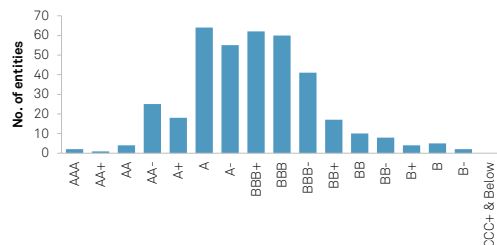
What to look for

Consumer confidence. Prolonged control measures from the pandemic, inflationary material costs, and unemployment could dampen demand for apparel and discretionary durables, especially in China. China is rolling out vouchers and incentives to boost consumption, but the effect may be limited due to the small scale. Pandemic-related fatigue could also begin to weigh on consumer sentiment and shopping behavior.

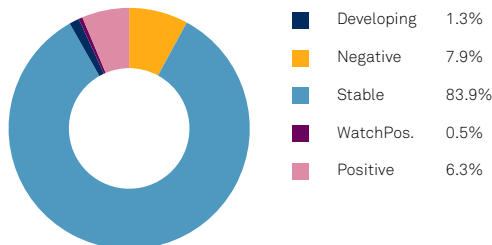
Financial Institutions

Economic Headwinds Will Challenge Banks

Rating Distribution



Outlook Distribution



Source: S&P Global Ratings, As of May 31, 2022.

Key Takeaways

- The notably weaker growth outlook and prospects for higher inflation in many jurisdictions will increasingly burden bank borrowers and in turn banks' asset quality.
- While most banking systems have some resilience at current rating levels, financial institutions in Malaysia, Indonesia, Thailand, and New Zealand face greater challenges.
- A further economic step-change toward the downside may prove to be a more broad-based test of ratings and outlooks for both banks and nonbank financial institutions.

What's changed?

Economic pressures are building. Weaker economic conditions and tighter financial conditions will increasingly strain banks. We expect a lag between when the stresses currently being felt by borrowers will hit banks. Should economic drags be more severe or persistent beyond our base case, negative ratings momentum would seem inevitable.

Negative trends may become more broad-based. Of the 19 Asia-Pacific banking jurisdictions we cover, economic trends affecting banks may spread beyond the four jurisdictions that we currently identify are most vulnerable (Indonesia, Malaysia, Thailand, and New Zealand). Further, greater credit differentiation could arise between strong, systemically important banks versus small banks. Also, typically smaller, and lower rated, certain nonbank financial institutions may also fare worse as economic prospects deteriorate.

Key risks

Economic downside risks intensify. Materially weaker economic prospects outside our base case, including weaker growth and higher-than-anticipated inflation and borrowing costs, would eventually hurt banks. These higher risks are superimposed upon already more highly levered corporate and government sectors compared to pre-pandemic levels, and some property markets already under stress, notably China. While some negative risks may take longer to manifest upon banks compared with other sectors, they could eventually be significant especially if the downside scenario takes center-stage.

Key assumptions

Revised economic base case holds. While our base case has been revised negatively during 2022, the negative effect on banks so far is constrained to a few jurisdictions. We expect many banking sectors to continue to show some resilience; nonetheless, this assumption will be tested should our downside scenario become the new normal.

Highly supportive governments. We expect extraordinary government support would be extended to many systemically important banks, in the unlikely event it were required.

What to look for

Severity and timing. A more severe or prolonged downturn is likely to be the key precursor for more broad-based and less-nuanced negative ratings momentum across the sector.



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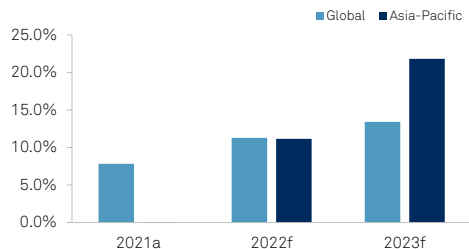
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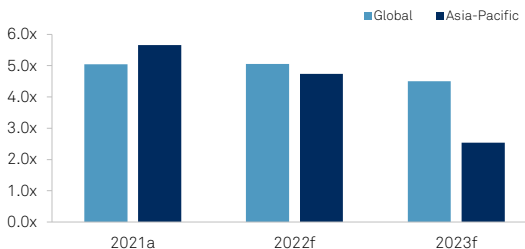
Gaming

Divergent Recovery In Macao And The Rest Of Asia

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

- China's COVID surge and control measures will delay Macao's recovery in 2022. This is a downside risk to ratings.
- Other Asian markets such as Singapore and Australia continue to open.
- Regulatory risks persist across Asia.

What's changed?

Macao is falling behind. Our base case assumes Macao gross gaming revenue (GGR) in 2022 to come in at the low end of our forecast of 30%-40% of 2019 levels. We may lower our GGR forecasts if China's COVID control measures continue and outbreaks persist, leading to a subdued recovery in the second half of 2022 and into 2023. In contrast, the rest of the gaming markets in Asia have seen an increase in visits and a resumption of activities.

Key risks

Regulatory risks. Details for upcoming license rebidding and regulatory changes in Macao will be key monitoring points in the next six months. Regulatory risks on governance issues remain a core focus for Crown Resorts Ltd. In Japan, Universal Entertainment is exposed to stricter regulations on machines with high payouts.

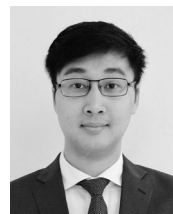
Uncontrolled COVID cases. A worsening of the infection rate or new virus strains with increased severity could hamper the recovery of casinos and gaming tourism and disrupt operators' recovery path. This is particularly true for Macao, where the Chinese authorities' zero-tolerance strategy could choke customer inflow.

Key assumptions

Gaming visits to return. We expect gaming revenue across most Asian markets to gradually recover to pre-pandemic level through 2022. For Macao, we don't anticipate a substantial recovery until 2023.

What to look for

Pace and magnitude of recovery. As most Asian markets are set for a turnaround in operating performance in 2022, we monitor signs of possible structural changes in gaming-visit trends or spending behavior due to shrinking consumer pockets or COVID-19-associated travel fears.



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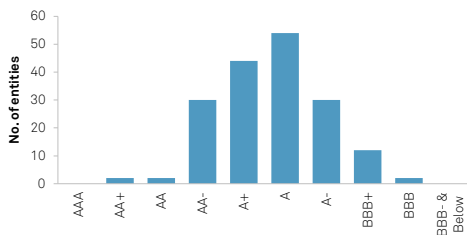
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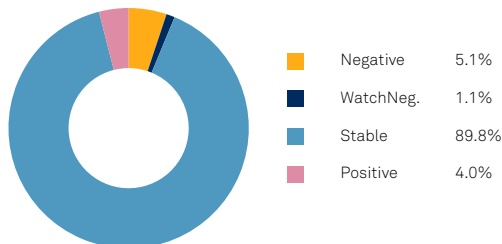
Insurance

Volatile Capital Markets Strain Profitability

Rating Distribution



Outlook Distribution



Source: S&P Global Ratings, As of May 31, 2022. Includes public ratings only.

Key Takeaways

- Stable credit trends should largely prevail, but lower asset valuation will dampen capital buffers.
- Volatile share market and heightening counterparty risk could strain overall profitability.
- Slowing economic growth in some markets could impede premium recovery.

What's changed?

Fluctuating capital market dents earnings prospect. This will in turn narrow insurers' capital buffer. Those that previously increased their appetite for credit risk could be exposed to rising defaults. Rate hikes in many markets (though not in China) will knock asset valuation. Further, a gradual rise in interest rate differential could hike hedging costs. Insurers' unhedged foreign exchange exposure could also add to earnings volatility. On the other hand, higher rates will ease demand on reserve positions for life insurers. Meanwhile, COVID insurance policies in Taiwan and Thailand could see mounting losses, diluting insurers' capital buffer.

Uneven growth recovery. China's zero-COVID stance constrains new business momentum, evident from the limited sales activity during the Shanghai lockdown. Meanwhile, insurers undergoing product and channel reform could face slower interim growth.

Key risks

Persistent market volatility. Spillovers from slowing growth in the region's major economies and the Russia-Ukraine conflict could increase market volatility. Sharp and prolonged market fluctuations and asset impairments could dent insurers' capital and earnings.

Increasing frequency of natural disasters. Climate change and rapid urbanization in emerging Asia calls for more regular updates on catastrophe models. Increasing reinsurance costs could weigh on non-life insurers' profit margins.

Key assumptions

Capital buffer will narrow. Asset valuation declines eat into capital buffers, despite being shored up from previously realized investment gains. Pressure for reserve provisioning will gradually ease amid rising interest rates (except in China).

What to look for

Evolving regulatory and accounting developments. These signify prospective changes in business and investment strategies, resulting in rising operational costs.



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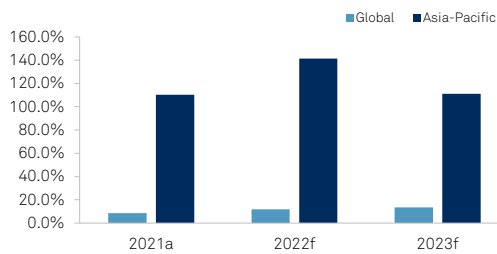
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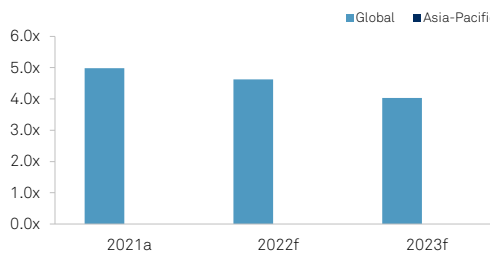
Media And Entertainment

A Recovery Could Be On The Horizon In 2023

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

- China's slowing growth amid COVID lockdowns will weigh on revenues and profits for many Chinese internet companies. Weaker operating performance is offset by big cash buffers and good cash flow.
- Easing lockdown measures could support a recovery for Chinese internet firms in the second half of 2022.
- Companies with little exposure to China are faring better.

What's changed?

China's COVID-related lockdowns have hurt consumption and advertising. Lockdown measures in Shanghai and other regions in China have heavily disrupted supply chains, retail, and transportation since March 2022. Advertising revenues already declining because of regulations will fall further due to lockdowns and weakening consumer sentiment.

Outside China, media and entertainment companies are benefiting from loosening COVID restrictions. E-commerce revenues outside of China are growing at a healthy pace as consumers continue their online spending patterns after COVID. Companies exposed to live events could see a recovery along with loosening restrictions.

Key risks

Macro slowdown and further lockdown measures in China. Advertising is highly correlated to economic growth. Slowing growth and waning consumer sentiment will hurt consumer spending and dampen advertising spending and e-commerce sales. Additional lockdowns could further strain revenue and profits for these companies.

Tightening capital markets could exacerbate liquidity issues. Smaller media and entertainment companies could face more severe liquidity strains as capital markets tighten amid rising inflation, interest rates, and macroeconomic uncertainties. Moreover, persistent COVID outbreaks could continue to shift consumer behavior, hurting companies exposed to live events.

Key assumptions

Revenue growth in the slow lane. Chinese internet companies will experience slowing growth amid regulatory tightening and a broader slowdown in 2022. However, a recovery could occur in the second half of 2022 should lockdown measures ease. Online media and entertainment companies outside of China are more insulated, though competition remains intense.

What to look for

Inflection in government regulations and policies toward internet firms. China's stringent regulatory policies and lockdown measures are the major drivers of weakening operating results for internet companies in 2022. Any changes to such policies could have significant implications for internet companies in China.



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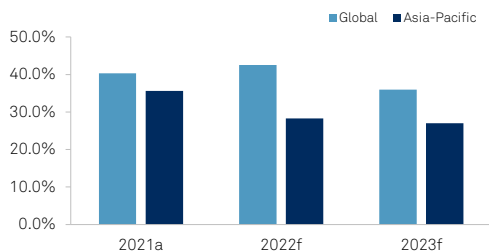
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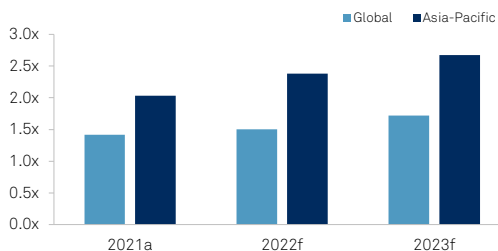
Metals And Mining

Price Visibility The Lowest In 50 Years

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

- Lower growth expectations for China are likely to dampen the outlook for commodities, but stimulus measures to revive its economy are likely to provide support in the second half.
- The Russia-Ukraine conflict will cause further shortages and fuel price spikes.
- Geopolitical risks, an uneven recovery path out of COVID, and additional supply disruptions will exacerbate the volatility in commodity markets.

What's changed?

Further economic slowdown and lockdowns in China. China is emerging from restrictions following one of the worst outbreaks of COVID-19 since the start of the pandemic.

China infrastructure stimulus could spur demand for commodities. The government has been accelerating infrastructure spending and will call on state-owned policy banks to provide Chinese renminbi 800 billion in funding for infrastructure projects, as China emerges from the latest round of COVID-19 restrictions.

Supply remains tight. Commodity markets remain volatile. Supply disruptions have contributed to the inability of supply to keep pace with demand growth. We expect these conditions to continue throughout 2022.

Key risks

Subdued growth slowing China's commodities demand. Given China accounts for over half of global demand for raw materials, any prolonged weakness in its economy would weaken key support for prices.

Russia-Ukraine conflict adds to supply disruptions, adding volatility to prices. Our metals price assumptions were already around decade-highs before sanctions on Russian materials; other disruptions point to further inventory drawdowns. Price visibility is worse than any time in the past 50 years.

China's decarbonization drive to move markets. We expect China's decarbonization drive to continue. Government-mandated production cuts and decarbonization policies will affect both supply and demand.

Key assumptions

China's slower growth. We now assume China GDP growth will decrease to 3.3% from 4.2%. However, government measures to boost the economy are likely to provide some support for steel demand.

Elevated prices point to another year of strong profits and cash flow. The credit quality for many issuers in metals and mining has been improving with greater capital discipline and lower debt. Our positive ratings bias reflects this.

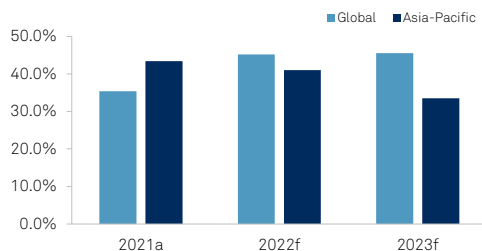
What to look for

COVID, China, and geopolitical risks. Lower growth prospects and resurgent pandemic risks pose a key threat to demand, while decarbonization policies in China could alter the profitability of its steel industry and the demand for commodities. Rising geopolitical risks and how they unfold further limit price visibility.

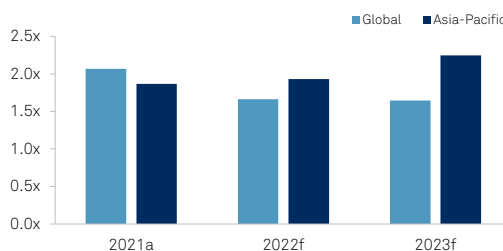
Oil And Gas

Price Strength Fueled By Persistent Risks

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

- Persistent geopolitical tensions, supply concerns, and fragile recovery underpin high crude oil prices.
- Demand remains fragile despite China's easing pandemic restrictions. Sustained oil prices drive the risk of a recessionary impact in the medium term.
- An increase in earnings will enable the region's oil companies to reinforce their hydrocarbon portfolios and simultaneously address the energy transition. Windfall earnings could lead to more government intervention on national oil companies.

What's changed?

Sustained volatility in oil prices. Oil prices will be buoyed by the EU sanctions on Russian oil, which will eliminate about 90% of Russian oil imports by end-2022. Supply remains tight despite the OPEC+ alliance increasing its production volume by 648,000 barrels per day in July and August. In the short-term, oil consumption in Asia-Pacific is driven by pent-up demand and seasonal effects as COVID restrictions ease.

Key risks

Demand shock. Rising inflation and rising interest rates could temper economic performance and hinder oil demand recovery in the medium-to-long term.

Government intervention. Rated oil and gas giants in Asia-Pacific--most of which are national oil companies (NOCs)--are vulnerable to increasing regulatory risks as governments will likely consider various intervention measures to curb high fuel prices and inflation. The implementation of profit-sharing schemes or subsidies could erode oil companies' profitability and weigh on rated companies' balance sheets.

Urgency for the energy transition. Elevated hydrocarbon prices will increase the urgency for countries in Asia-Pacific, and consequently NOCs, to increase their renewable energy assets. The investment costs of doing so, however, will likely be extortionate under current industry conditions and amid rising interest rates.

Key assumptions

Brent at US\$100/barrel and Henry Hub at US\$8.25 per metric million British thermal unit (mmBtu) for 2022.

We assume Brent will be US\$85/barrel in 2023 before stabilizing at US\$55/barrel from 2024. Henry Hub will likely be US\$5.50/mmBtu in 2023 and US\$2.75/mmBtu in 2024.

Investment in hydrocarbon reserves and renewable assets. Bolstered by windfall earnings, Asian companies will likely allocate capital to reinforcing hydrocarbon portfolios and accumulating renewable assets over the next two to three years.

What to look for

Supply response by oil producers and any further ban on Russian gas. The responsiveness of North American producers to this supply-demand situation--currently delayed by labor shortages and supply chain disruption--could determine the direction of oil prices. It remains to be seen if the OPEC+ group will increase its production quota post-August. In our view, increased volumes from Iran or Venezuela are unlikely in 2022.



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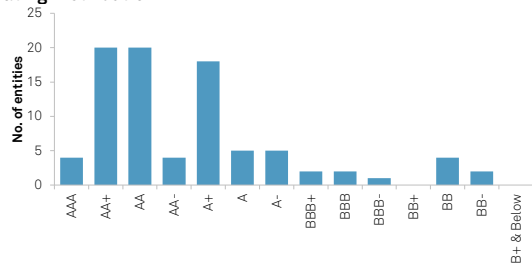
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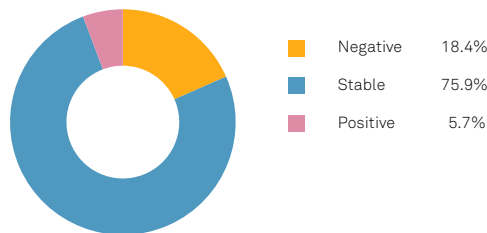
Public Finance

Fiscal Consolidation Amid External Challenges

Rating Distribution



Outlook Distribution



Source: S&P Global Ratings, As of May 31, 2022.



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Key Takeaways

- Energy price shocks, inflation risks, and rate hikes will hit local governments and their associated enterprises.
- China to face additional challenges amid property strains as well as extensive lockdown to contain COVID cases.
- Local governments in Australia, New Zealand, and China are using large infrastructure projects to stimulate economies, a practice that will persist until at least 2023.

What's changed?

Reopening of borders in most parts of Asia-Pacific. Most localities are easing border restrictions to live with the virus while China continues its zero-COVID policy.

China's strict containment slows growth. Extensive lockdown in major cities, such as Shanghai, have led to weakening macro factors since March, and social discontentment.

Key risks

Economic shock. Unexpected external factors or resumption of COVID restrictions beyond China could further pressure local consumption, supply chains, and economic growth. This would shrink or delay revenue growth for local and regional governments (LRGs). China's pursuit of zero-COVID weakens fiscal strength for its LRGs.

Delayed fiscal recovery. To prevent slowdown or restore social confidence, selective LRGs could resume aggressive fiscal stimulus, including tax cuts and more spending that will disrupt fiscal recovery and lift debt burdens. In China, prolonged weak land demand will slow local growth, prompting LRGs to focus fiscal stimulus on new infrastructure projects.

Key assumptions

Public finance systems largely stable. Most regions seek transition to a post-COVID world and gradual recovery of fiscal performance. Australian and New Zealand LRGs continue to utilize their spending discretion to fund an economic and fiscal recovery, but expansionary policies weigh on their finances. Easing border restrictions in Australia are supporting the higher-education sector. China's LRGs can still rely on large cash transfers and new borrowings, subject to support from the central government. The finances of Indian LRGs remain stretched and are handicapped by limited financial flexibility. That said, support from the Reserve Bank of India has been providing states with sufficient external liquidity. Japanese LRGs continue to look to the central government to undertake nationwide economic stimulus, as they seek to shift budgets to a fiscal recovery phase.

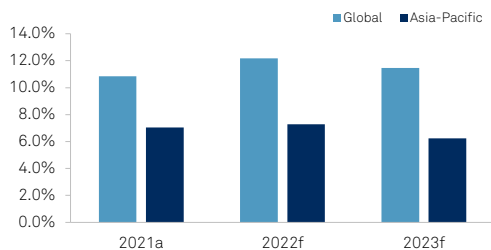
What to look for

Policy shifts. Any aggressive LRG fiscal expansion, either to sustain growth or to maintain social stability, could erode credit quality. Chinese LRGs will see additional debt burden risks if they turn to leveraging their SOE investments to stimulate local economic growth, while concurrently providing support to their SOEs.

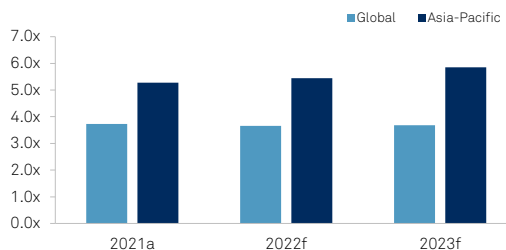
Real Estate Development

Chinese Developers Will Face An 'L-Shaped' Recovery

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

- The down cycle of China's residential housing market has further to go despite some policy easing.
- Lockdowns could further dampen developers' sales outlook in 2022.
- Sales momentum can prevail due to the ongoing economic recovery, higher land sales, and if the easing of restrictions continues.

What's changed?

Green shoots on policy easing have sprung up in China. Policy support so far derives mainly from the demand side, such as the reduction in down payments and mortgage rates, and the removal of purchasing restrictions in some cities. On the supply side, we have yet to see clear evidence of easing on escrow requirements on presale proceeds.

Key risks

COVID resurgence could slow Chinese developers' sales recovery. National property sales fell 26% year on year in the first quarter of 2022, according to the National Bureau of Statistics of China. COVID-related lockdowns caused a near halt in sales activities in April in cities such as Shanghai. The top 100 developers' aggregate sales were down about 58% year on year in April, according to CRIC data. This could further tighten some developers' liquidity.

Structural supply shortage continues to support home prices in Hong Kong. Residential property prices only fell by about 2.6% year-to-date as of early May 2022 amid the resurgent COVID cases. While we expect transaction volume to decline in 2022 from 2021, rated Hong Kong developers have ample rating buffers due to their conservative financial management.

Indonesian developers' credit quality will remain largely stable despite moderating sales growth. In Indonesia, we expect aggregate sales growth to slow as favorable policies taper off this year. However, overall sales will continue to derive support from the economic recovery and eased social and travelling restrictions. While refinancing will be challenging for lower rated developers over the next six to 12 months, debt maturity through 2023 is not significant.

Key assumptions

We expect an "L-shaped" recovery in Chinese developers' contracted sales. We expect national sales will shrink by 15%-20% in 2022 and drop by a further 3% in 2023. There could be downside risks to our 2022 forecasts if there are widespread and prolonged COVID lockdowns.

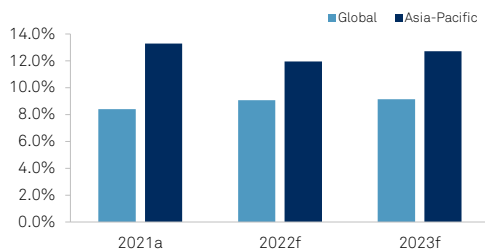
What to look for

Restoring homebuyers' confidence in China is the key. The market awaits more signals of stabilizing sales, as this is one of the prerequisites for stabilizing developers' liquidity. We believe it will take several quarters, at least, for regulatory easing to feed through to the physical market.

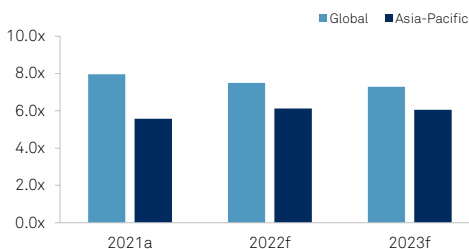
Real Estate Investment Trusts

Recovery Amid Easing Pandemic Restrictions; Structural Shift Continues

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

- Relaxation of pandemic restrictions across the region (except China) will drive operational recovery.
- Credit upside is hampered by structural changes in consumer behavior especially for the office sector.
- Rising funding costs and M&A amid the rate hike cycle are key credit monitoring events.

What's changed?

Post-COVID recovery. With the gradual lifting of pandemic restrictions across the region, Asia-Pacific REITs are poised for improved operational metrics. Footfalls and consumer spending at discretionary-focused malls have risen from the low base, and physical occupancy at offices has increased. Overall cash collection has also improved, with narrowing negative rental reversions. On the other hand, COVID lockdowns could cause cash collection pain for China REITs.

Key risks

Structural shift continues. We expect divergence across landlords with different asset profiles and leasing strategies to continue amid shifting customer behavior. Increased acceptance of online shopping will drive retail landlords to shift tenant mix toward service.

Lower occupancies. We see lower occupancy and rent assumptions for Japan and China REITs due to greater supply and a weaker economic outlook. The transition to a hybrid/remote business model would limit office occupancy upside for most Asia-Pacific REITs, while new demand from growing sectors, such as technology, might mitigate the impact for top-tiered office assets.

Key assumptions

Steady credit outlook. We expect improvements in retail rents and occupancy, supported by limited new supply and the post-COVID recovery, to underpin stable leverage of retail landlords. The performance of office landlords (except for Tokyo "CBD" offices) will begin to bottom out, while those with fixed rent reviews, or with superior asset quality, will fare better. That said, ongoing structural changes will continue to constrain upside.

What to look for

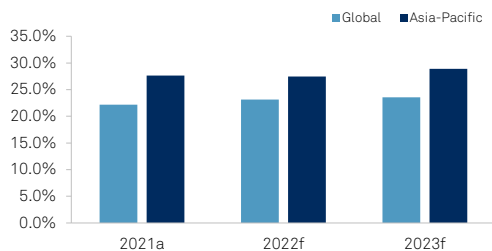
Development cost pressure. The disruption of global supply chains has led to higher construction costs, which has squeezed development profitability. A-REITs, with more exposure to new projects and redevelopments, are more affected. Market leaders such as Goodman are better placed to absorb the cost pressure due to their more sophisticated business practices. Other Asia-Pacific REITs focused on completed properties are less affected.

M&A strategy. We expect Asia-Pacific REITs to become more selective in acquisitions as funding costs rise. Both S-REITs and H-REITs will continue to focus on overseas opportunities to diversify their portfolio and seek better returns. We also expect to see stronger interest in logistics assets following Link REIT's recent deals. The funding mix of potential M&A activities and impact on leverage profiles are also key drivers for future credit changes.

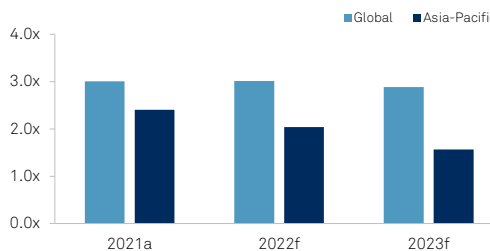
Retail

Lockdowns, Inflation, And Supply Chains

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

- The impact of China's lockdowns is spreading across Asia-Pacific retailers through their China operations.
- Inflation has set in across most Asia-Pacific economies, which along with weaker consumer sentiment, threatens profitability of retailers.
- Higher global interest rates present challenging funding conditions; and refinancing risks grow for speculative grade issuers.

What's changed?

China's lockdown. The lockdown in major cities including Shanghai is constraining China's domestic retail consumption and putting greater pressure to global supply chains.

Key risks

Household consumption slumps. Consumer confidence is at risk amid a rise in basic living costs across Asia Pacific. The combination of increased food shelf prices and elevated petrol prices will continue to depress consumer confidence levels.

China's stringent COVID policy. Uncertainties remain with the imposition of mobility controls as long as the Chinese government maintains the zero-COVID policy. This exposes retailers and restaurants operating in China to potentially significant pressure. Spillover risks from China's policy also relate to wider Asia-Pacific retail players through supply chain disruption.

Key assumptions

EBITDA margins to be squeezed. Retailers will have to absorb rising input prices, elevated shipping costs, and depressed consumer confidence. The degree to which these affect EBITDA margins will be determined by the ability of retailers to pass through higher prices to consumers.

What to look for

Challenging funding conditions amid rising global interest rates. Central banks across Asia-Pacific will likely raise interest rates where inflation is exceeding target ranges, leading to higher funding costs. Speculative-grade issuers in emerging markets may face reduced headroom in key coverage ratios to absorb increasing interest expenses. This may test the sustainability of some capital structures. Meanwhile, rising debt costs will also likely constrain further large debt-funded investments.



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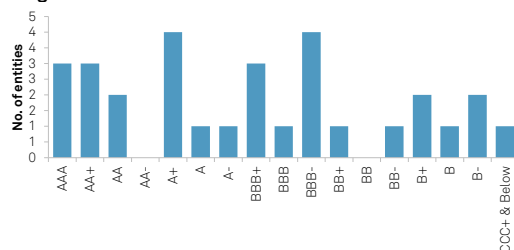
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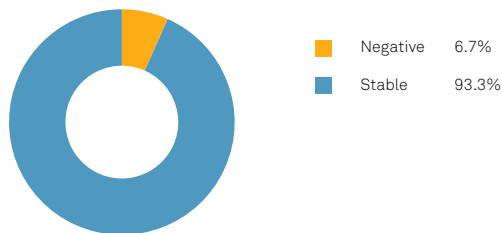
Sovereign

Inflation Takes Center Stage

Rating Distribution



Outlook Distribution



Source: S&P Global Ratings. As of May 31, 2022. Includes public ratings only, and ratings on policy-related financial institutions and corporates.

Key Takeaways

- The war in Ukraine has stoked inflation and increased risks to growth. These developments could slow the credit improvement among Asia-Pacific sovereigns.
- The recovery from the pandemic should continue despite these headwinds.

What's changed?

Intensifying sanctions on Russia prop up commodity and food prices. Some governments have increased subsidies to cushion rising living costs, with a few imposing food export restrictions. These moves may curtail credit improvements if they become persistent.

Rising interest rate expectations. Expectations of monetary tightening in the U.S. and Europe have also pushed up interest rates in Asia-Pacific. Exchange rate volatility, especially on the yen and won, has increased.

Outside China, COVID restrictions have eased markedly. Reduced border controls have allowed a return of tourism and business, relieving burdens on services industries across the region. Investment spending should strengthen and domestic consumption should benefit from these changes, offsetting downward growth pressures from negative external developments.

Key risks

Sudden capital swings. An unexpected deterioration of geopolitical risks or interest rate expectations could see investors withdraw from emerging markets in Asia-Pacific, making financing conditions significantly more challenging for some. Steep exchange rate depreciations could also worsen imported inflation.

Growth and fiscal recoveries interrupted. High inflation, weaker demand and increased uncertainty arising from the Russia-Ukraine war and continued supply chain disruptions may slow the economic and fiscal recoveries much more than expected.

Key assumptions

Global economic activity recovers, albeit less robustly than earlier expected. Economic recoveries continue but are slowed by higher inflation and uncertainties associated with the Russia-Ukraine conflict. Governments can still lower fiscal deficits meaningfully although a return to pre-COVID fiscal performances will take longer.

What to look for

Widening geopolitical tensions that affect Asia-Pacific more materially. If the war in Europe expands or involves more parties, it would seriously damage investor sentiment and stoke further price increases. Knocks on economies and financial markets in Asia-Pacific may worsen significantly.

New variants that may prolong the pandemic. Vaccines may be less effective against new variants of COVID, prolonging the pandemic.



PRIMARY CREDIT ANALYST

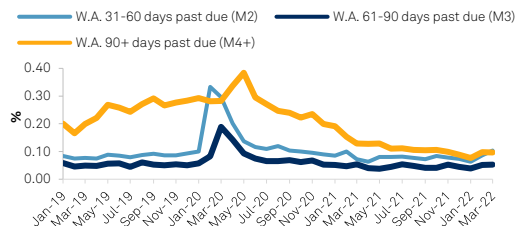
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Structured Finance

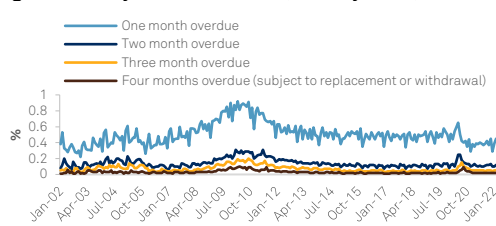
Inflation Spillovers Could Temper Outlook

Weighted Average Asset Delinquency Rates Of China Auto Loan ABS



Data as of Mar. 31, 2022. The delinquency rates of the first three months after transaction close are excluded. ABS --Asset-backed securities. W.A.--Weighted average. Source: Trustee reports published on Chinabond's website; compiled by S&P Global Ratings.

Japan Housing Finance (JHF) Delinquency Rate Of Overall Regular Monthly Note Series Pool (Monthly Basis)



Data as of Feb. 2022. Source: S&P Global Ratings, based on company materials.



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Key Takeaways

- Mixed outlooks in the region in relation to COVID, interest rates, and inflation.
- Unemployment remains steady, supporting our stable outlook for consumer asset classes.

What's changed?

COVID-19 disruptions in China. Borrowers may see some liquidity stress as a result of lockdowns and related knock-on effects to employment, especially in the hardest-hit sectors and for self-employed borrowers.

Key risks

Inflation and its impact on households. Households are well placed, with high and stable employment across most markets in the region. Inflation dynamics are mixed across markets; however, price pressures may start to undermine household balance sheets and purchase decisions. Interest rates have started to increase in some markets across the region, which we expect will slow house price growth in those markets.

Effect of COVID policies in China. We expect that any prolonged restrictions on mobility in China may affect delinquency. These effects may vary given the scope of any lockdowns and different geographical distribution of the securitized pools

Key assumptions

Structural supports. We expect ratings to remain stable, with low numbers 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 (RMBS).

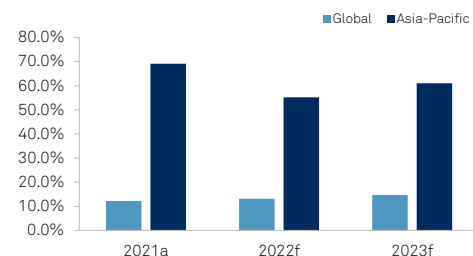
What to look for

ESG in securitization. We are seeing further development of ESG in securitization markets and are likely to see assets with an "E" factor, including for "green" housing assets in Australian RMBS. An increase in new energy vehicles (NEV) sales in China may see increased NEV assets in auto ABS.

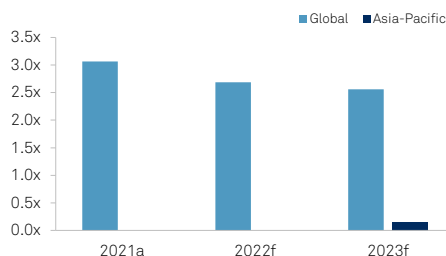
Technology

Strong Profits Support Credit Profiles

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

- Strong profitability supports a relatively stable sector credit outlook, despite risks from further macroeconomic slowdown.
- End markets are diverging as consumer electronics are turning weaker, but server, auto, and industrial markets remain strong.
- Oversupply could emerge in 2023, particularly for logic semiconductors, given record capital expenditure and the potential for fading demand from COVID mitigations.

What's changed?

End markets are diverging. Demand for consumer electronics such as PCs (particularly Chromebook) and TV is weakening due to demand pull-forwards over the past two years. Demand weakness in China also suppressed the increasing 5G penetration in the smartphone market. However, robust data center spending continues to support the cloud server market. With supplies in the automotive and industrial markets remaining constrained, semiconductor suppliers (particularly advanced products) could maintain their strong pricing power.

Key risks

Macroeconomic risks emerge. Increasing macroeconomic risks--such as inflation, rising interest rates, the Russia-Ukraine conflict, and COVID-related lockdowns in China-- could decelerate economic growth momentum. Weaker borrowers, particularly hardware companies, could see rating headroom dilute.

Logic semiconductor oversupply in 2023. Record investment by logic IC chip manufacturers will come online in late 2022 and 2023, especially for more mature chips. This could lead to oversupply in 2023 onward, if strong demand from cloud, electric vehicles, and 5G communications fail to offset waning demand from work-from-home tech purchases.

Key assumptions

Further slowdown in global IT spending. We estimate global IT spending to be lower at 4.5% this year from our previous forecast of 5.1%, mainly because of a lower global macroeconomic outlook. This comes despite the companies' investment in new technologies. Smartphone and PC shipments will be particularly weak, with a 7% and 5% decline respectively given their consumer-end market exposure. However, we expect semiconductor sales to be resilient, with 9% growth in 2022, supported by both increasing chip shipment and ASP.

What to look for

Relatively stable credit outlook for Asia-Pacific tech firms. Tech companies' strong profitability has reinforced balance sheets and resilience to business volatility, despite the increasing expansion. However, the macro downturn and rising rates could turn rating bias negative.



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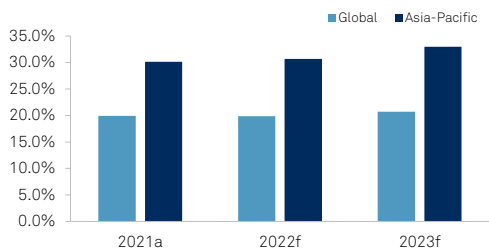
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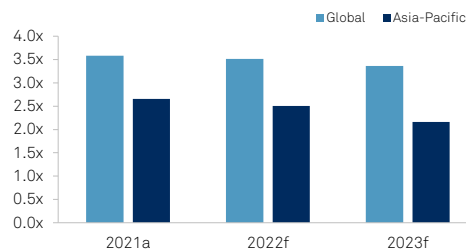
Telecommunications

Steady Operating Performances Despite Inflationary Pressure

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

- Many telecom operators are well positioned after robust operating and financial performances owing to the sector's low cyclicality and utility-like demand characteristics.
- Cost-input inflation could hurt margins and cash flow for telecom operators.
- Data traffic should continue to expand because of rising demand for connectivity. Intense competition, large capital investments/shareholder returns, and debt-funded acquisitions could be negatives.

What's changed?

Rising connectivity demand. Increasing needs for remote access and mobility should support growth in data traffic, including demand for 5G and high-speed broadband services. Asia-Pacific telcos are also making active investments to grow their data center businesses. However, lower consumer spending and higher unemployment 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 the Philippines, Singapore, and Thailand. The entrance of new operators in Japan (Rakuten Inc.), Singapore (TPG Telecom) and the Philippines (Dito Telecommunity Corp.) will increase wireless competition.

Cost inflation. Cost-input inflation and supply chain disruptions could hurt margins and cash flow for telecom operators. The impact has been largely muted given lower sensitivity in their cost structure. Risks to profitability risk can be acute, if not for inflation-linked tariffs, as higher costs could be difficult to pass on. Supply chain constraints will also remain under scrutiny in 2022 as they could affect 5G and fiber rollout, and squeeze telcos' margins, especially when combined with labor shortages.

Key assumptions

Mergers and restructurings. We expect continued M&A activity in the region given the telecom-media convergence trend and the appetite of some telcos to restructure their businesses. This follows from the ongoing trend for firms to monetize their telecom infrastructure assets, notably the recent sell down of tower businesses by PLDT, Telstra, Singtel Optus, and CK Hutchison Telecom. In Korea, all three telecom players (KT Corp, SK Telecom Co. Ltd., and LG Uplus Corp.) have completed acquisitions on cable TV operators to strengthen their media and pay-TV market position.

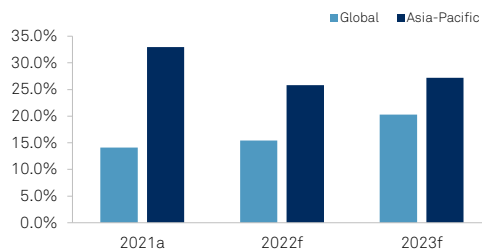
What to look for

Growing 5G services. 5G adoption remains steady but more profitability use-cases remain distant. 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 must manage investment burdens for 5G spectrum auctions and network expansions. The development of new and profitable 5G use-cases also remains challenging for all operators.

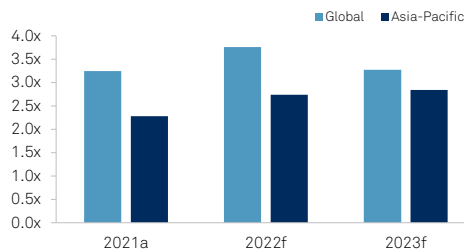
Transportation Cyclical

Bumpy Road To Recovery

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

- Passenger traffic across Asia-Pacific will further diverge because of discrepant COVID strategies; the region is expected to lag the traffic recovery in Western countries.
- Local currency depreciation amid Fed rate hike lifts funding costs of Asia-Pacific companies, and compounds already high energy prices. Small airlines are particularly susceptible.
- Lockdowns disrupt traffic and logistics in China. The zero-COVID policy clouds operation and liquidity of domestic players. State-owned airlines or aircraft lessors should enjoy extraordinary liquidity support.

What's changed?

Fed rate hike and local currency depreciation. This may persist in some countries given the expectation of more Fed rate increases. Subsequently, the cost of foreign debt servicing and refinancing will increase. This particularly threatens regional airlines with high U.S. dollar-denominated debt exposure. Currency depreciation could also amplify the impact of high fuel costs. Freight transportation should, however, withstand this because of good cost pass-through.

Divergence continues. Diverging national pandemic strategies will exacerbate the unevenness of recovery across regions and subsectors. For instance, the performance of car rentals and airlines in China is volatile under the country's zero-COVID policy and the unexpected city lockdowns or travel bans that disrupt operation.

Key risks

Liquidity crunch. Liquidity remains a key credit factor for weaker transport companies and most airlines. The risk is more prominent in countries with prolonged COVID disruption and weaker government aid to industry. Fed rate increases, local currency depreciation, and fuel cost volatility add to liquidity challenges.

Energy cost. The high oil price weighs on profitability, particularly on passenger-based transportation with weaker cost pass-through at early recovery stages with low occupancy. This would hinder cash flow generation and leverage improvement. Depreciation of the local currency could worsen the impact.

Key assumptions

Air traffic recovery is uneven and passenger volumes remain below pre-pandemic levels. We estimate global air traffic will be 20%-30% below 2019 levels in 2022. Air traffic will recover to 2019 volumes by 2024. The recovery of passenger airlines' profitability would lag the traffic recovery, and this is further complicated by the fallout from the Russia-Ukraine conflict.

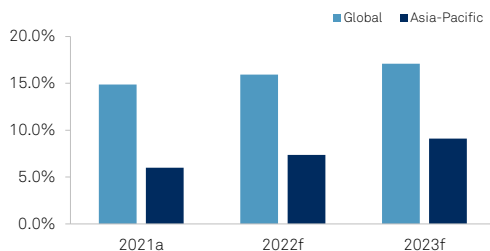
What to look for

China's COVID policy. We see significant pent-up demand for travel. The sector's performance and recovery depend on the evolution of the pandemic and updates of the government's antivirus policies, such as quarantine and mobility restrictions. Hypothetically, the relaxation of China's COVID policy could speed up the sector's recovery because it would bolster international travel within Asia-Pacific and beyond.

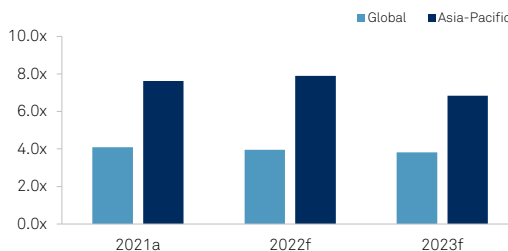
Transportation Infrastructure

Easing Travel And Testing Restrictions Support Recovery

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

- Outside China and Hong Kong, easing travel restrictions in most of Asia-Pacific will help the infrastructure sector recovery, albeit unevenly.
- Port volumes are robust while road traffic has largely recovered. Demand for domestic air travel is strongly up, but the international flight recovery will be slower for airports.
- Among our rated entities, the net outlook bias was negative 10% as of May 31, 2022, largely comprising of Pacific airports and Japanese railways.

What's changed?

Governments aiming for post-pandemic state. The easing travel and testing requirements--in economies such as India, Thailand, Singapore and Australia--will support recovery. However, China and Hong Kong's still low COVID tolerance and tight restrictions (as in Shanghai, Beijing) could lead to an uneven path for recovery. Robust demand supports growth for ports; and road traffic has largely normalized.

Key risks

Return of government restrictions or border closures due to new variant. Although we consider this unlikely, any new variant and consequential restrictions could further delay recovery in the airport sector. Other transportation infrastructure sectors are likely to remain resilient, but we could see bumps.

Weakened government fiscal positions dampen support in most of Asia-Pacific. We see less willingness and ability of governments to support stressed entities, particularly local and regional governments contending with diminished fiscal positions. This may hit government-backed infrastructure developers amid rising interest rates. As China is propping up infrastructure investments to sustain the economy, government bond proceeds may be increasingly used to support the sector. Efforts to contain funding costs are taking place.

Key assumptions

Air traffic to recover but international will remain well short of pre-COVID levels. Domestic travel will recover faster to about 80% of pre-pandemic levels by mid-2023 for key markets; and in India we expect full domestic passenger traffic recovery by 2023. International travel will be much slower to recover across the board, and we anticipate international passengers at about 30% of pre-COVID-19 levels at the end of 2022.

Inflation and supply chain risks rising. Higher energy prices fueled by the Russia-Ukraine conflict; wage inflation and supply chain risks are manageable or mitigated by pass-through mechanism to end customers.

What to look for

Material structural changes to mobility trends. Remote and hybrid working, virtual business meetings, and online shopping could affect the use of transportation infrastructure.

Changing funding and liquidity conditions. Credit differentiation could widen. Asia-Pacific high-yield capital markets are getting tighter with rising interest rates. In China, funding conditions for transportation infrastructure will remain supportive.



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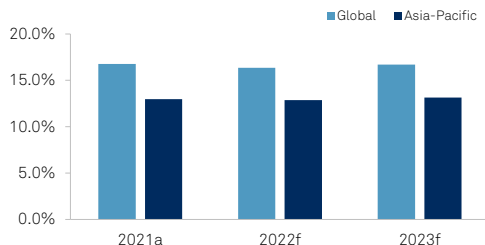
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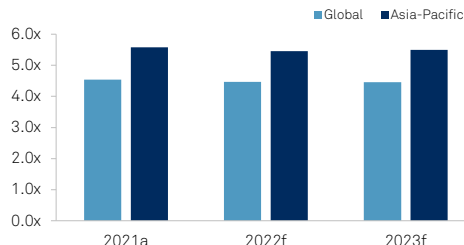
Utilities

High Fuel Cost And Rising Interest Rates Call For Caution On Investment

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

- Investors will keep a firm eye on leverage risk as investment in new projects gains traction.
- Investment in renewables to rise as countries manage the energy transition together with fuel supply and price risk.
- Negative bias remains due to high leverage in the sector, pressure to pursue new investments, and earnings risk for fossil fuel-based generation.

What's changed?

High fuel costs, inflation, and increasing interest rates add to industry woes. The fallout within the region will depend on how high fuels costs are recovered, interest rate hikes are managed as part of project costs and procurement, and how supply chain bottlenecks are managed for project completion.

Key risks

Aggressive pace of new investments and funding. Energy transition and rising fuel costs may point to accelerated investment in renewables. Excessive debt funding of new developments, adverse regulatory reforms or interventions and grid constraints are risks. We expect capex mainly in renewable projects, integrated hybrid projects or coal majors acquiring renewable assets.

Supply chain issues. Delays in material supplies are a risk to both cost and time of completion, subject to project stage. While COVID-related risks to supply chains have eased, equipment supply volumes have yet to return to pre-COVID levels.

Interest rate risks. Rising interest rates in most markets can alter funding options and costs.

Key assumptions

Profitability will be mixed across markets. Higher fuel and inflation-related costs can offset benefits from demand recovery and tariff changes in some markets. Tariff changes may lag costs to support end consumers. Lower open-market power prices and/or retail price controls will continue.

Capital expenditure to lift. Projects are being accelerated 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

Management of liquidity and funding costs by companies with limited financial cushion. Such companies face a higher risk of ratings downgrade.

Appendix 1

Related Research

- [Credit Conditions Asia-Pacific Q3 2022: Costs Heighten, China Growth Tightens](#). June 28, 2022.
- [Economic Outlook Asia-Pacific Q3 2022: Overcoming Obstacles](#). June 27, 2022.
- [Take A Hike 2022: Which Sovereigns Are Best And Worst Placed To Handle A Rise In Interest Rates](#). June 22, 2022.
- [APAC Corporates: Inflation, Rate Strains Set In](#). June 21, 2022.
- [The Heavy Hand Of Inflation On China Consumer Entities--Who Will Be Hit, And How](#). June 21, 2022.
- [Credit FAQ: U.S. Sanctions On China Banks--Investors Are Not Prepared For This High-Impact Risk](#). June 20, 2022.
- [Stablecoins: Common Promises, Diverging Outcomes](#). June 16, 2022.
- [China Local Governments: Navigating The Cost Of Zero-COVID](#). June 9, 2022.
- [China's COVID Wave Could Add RMB1.1 Trillion In Forborne Bank Loans](#). June 1, 2022.
- [China Signals Policy Support For Select Private Developers](#). June 1, 2022.
- [Cutting China From Supply Chains--Easy To Say, Hard To Do](#). June 1, 2022.
- [China's COVID Restrictions And Structural Risks Constrain Policy Support](#). May 30, 2022.
- [China Securitization: Auto ABS And RMBS Tracker April 2022](#). May 26, 2022.
- [A Primer On China's Residential Mortgage Backed Securities Market](#). May 24, 2022.
- [China's COVID Policy To Further Weigh On Economy, Credit](#). May 16, 2022.
- [China's Surging Defaults Test Courts And Bond Recovery](#). May 5, 2022.
- [China GRE Ratings List--The Stresses Pile On](#). April 28, 2022.
- [Energy Transition: Asia-Pacific Faces An Uphill Climb To A Cleaner Future](#). April 26, 2022.
- [Asia-Pacific Financial Institutions Monitor 2Q 2022: The Comeback Is Now Trickier](#). April 13, 2022.
- [Local Government Debt 2022: Emerging Market Borrowing Loses Momentum](#). April 13, 2022.
- [Local Government Debt 2022: Rising Risks Keep Global Borrowing High](#). April 12, 2022.
- [Sovereign Debt 2022: Asia-Pacific Central Governments To Borrow US\\$3.8 Trillion](#). April 6, 2022.

Appendix 2

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