

# Still Above Water

Dec. 1, 2022

*This report does not constitute a rating action*

## Key Takeaways

- **Soft rebound.** Unlike in the U.S. and Europe, growth in Asia-Pacific is likely to pick up slightly--to 4.3% in 2023 from 4.1% in 2022 as China begins easing on COVID lockdowns.
- **Japan to hike.** We now expect Japan will follow other Asia-Pacific central banks (China being the exception) to hike policy rates. Financing conditions may tighten in 2023.
- **Inflation tail.** Despite commodity prices softening from weaker demand, Asia-Pacific's weak currencies will keep imported prices high, with a flow-on effect on inflation.
- **China recovery.** An easing of COVID containment policies by China is critical for its economic growth recovery, as the impact of support initiatives are likely to be limited.
- **Downside remains.** Notwithstanding the soft economic rebound, global credit headwinds and structural risks (including climate and cyber) indicate still-high downside risks.

*Editor's Note: S&P Global Ratings' Asia-Pacific Credit Conditions Committee took place on Nov. 22, 2022.*

**Slower global growth.** Tightening global monetary policies are dampening demand, increasing risks of protracted U.S. and European recessions and a weak recovery in China. With GDP growth (Asia-Pacific excluding China) decelerating to 3.9% in 2023 (see further research under "Read more"), declining exports and corporate revenue will slow corporates' capital expenditure investment.

**Continuing rate hikes.** We expect most regional central banks (except in China) to hike policy rates further. Japan, having kept rates flat in 2022, could begin raising rates to limit the yen's depreciation. Rated corporates are struggling with higher input costs and rates.

**Imported inflation.** Asia-Pacific's currency weakness has led to costlier imports, despite lower global commodity and energy prices. Corporates have not been able to pass on higher costs to consumers. Meanwhile, high food prices are pressing down on households.

**China's COVID policy easing.** Recurring COVID-19 outbreaks in China may constrain consumption. A significant lifting of COVID measures may only occur in the second quarter of 2023. On property, the government's recent step to inject RMB1 trillion of liquidity may slow the downward spiral for developers.

**Geopolitical pains.** Despite an amicable meeting between President Xi and President Biden at the G-20 summit, U.S.-China disagreements remain. The U.S. tightening of export restrictions on advanced semiconductor technology to China raises risks for regional tech majors.

**Other risks.** Energy and food security concerns are an added complication for global economies. Extreme weather events have threatened agriculture and food.

**Limited headroom.** The rating outlook bias remains steady at negative 3% on a net basis (October 2022), but a gloomy economic backdrop and profit margin squeezes limit ratings' headroom.

## Regional Credit Conditions Chair

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[Asia-Pacific's Strong-Dollar Problem: Inconvenience Today, Headache Tomorrow](#), Nov. 10, 2022

[China Property Is Heading For A Transformation, And Maybe A Turnaround](#), Nov. 21, 2022

[Asia-Pacific Tech Firms Face Long-Term Risk From China Chip Restrictions](#), Oct. 14, 2022

[Agriculture Industry Is Still Sweating This Year's Droughts](#), Oct. 13, 2022

[China's Zero-COVID Stance Poses A Bigger Threat To Firms Than Inflation](#), Sept. 20, 2022

# Top Asia-Pacific Risks

## Higher borrowing costs or tighter financing-access to hit business operations and debt serviceability

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

Most central banks are pushing up policy rates except China. Inflationary expectations could see investors seek higher yields. Access to dollar debt funding has tightened. While domestic funding is accessible if economies slow sharply, banks may tighten credit. This could squeeze liquidity, particularly of lower-rated and highly leveraged borrowers. Unhedged debtors are exposed to further U.S. dollar appreciation.

## Sharper-than-expected global economic slowdown, further depressing aggregate demand and exports

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

Economic strain in the U.S., Europe, and China could intensify because of policy missteps, falls in business and consumer sentiment, more supply chain disruption, or geopolitical, health, and natural disaster shocks. The region is vulnerable to tepid global demand (affecting exports) and weak domestic consumption. Capital outflows may worsen for some economies if currencies weaken further, or investors turn more risk adverse.

## Inability to pass through persistently high prices will drag on already thin profit margins

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

The region is grappling with higher commodity, energy and food prices and shortages. While CPI inflation could peak soon, input prices may remain high. Weak consumer sentiment is dissuading corporates, particularly SMEs, from fully passing on increased input costs. Stresses and defaults will rise if corporates remain unable to pass on costs. If the slowdown worsens, stagflation-like conditions may manifest.

## China's COVID policy and property sector pains dim its economic recovery, business, and household confidence

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

China's COVID lockdowns and a weak property sector have dampened growth, business activity, and employment. Soft consumption is stressing the services and SME sectors. A more systematic lifting of COVID restrictions may only begin in Q2 2023 or later. For property developers, Beijing's policy easing could help refinancing conditions, but sales look subdued. Weak corporate and household sentiment could retard 2023's economic rebound.

## Increased geopolitical tensions will squeeze trade, financial, and investment flows

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

China and the U.S. may co-operate in some areas (e.g., global climate change) but are competing in others (e.g., U.S. export restrictions on semiconductor technology to China). China is now Russia's largest energy customer, complicating Beijing's relationship with the West. Partial decoupling of China from the West would alter supply chain, financial, and investment flows, incurring an economic cost for the world.

## Structural risks

### Natural disasters threaten energy and food supplies, implicating supply chains and risking another wave of inflation

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

Extreme weather events have increased. Droughts and floods threaten agriculture supply. China's drought this year stalled hydroelectricity generation, hit lithium and aluminum production, and reduced shipping activity. Crop disruption can lead to food inflation and increased social unrest. On energy, redirection of funding away from less-green investments, could curtail fossil-fuel-based power capacity, adding to energy costs

### Increasing threats from cyberattacks and digitalization can disrupt business models, hiking costs

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

Increasing technological interconnectedness makes cyber risk a systemic threat and significant single-entity risk. Borrowers need to incur additional ongoing and rising costs to combat the threat. Businesses slow to adapt to current and emergent information and other technologies could see their credit profiles decline. Increasing demand for key minerals, hardware, and software for use in technology could point to higher costs.

Source: S&P Global Ratings.

**Risk levels** may be classified as moderate, elevated, high, or very high. They 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 about whether the risk level could increase or decrease over the next 12 months.

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