S&P Global
Ratings

Asia-Pacific Sector Roundup Q2 2023

China Rebound Steadies Sector Outlooks

March 30, 2023

This report does not constitute a rating action

Key Takeaways

- **Costlier and narrower funding.** The era of low interest rates and easy credit is over. Amid greater market volatility and slower economies, funding access could tighten sharply. Banks, which dominate the region's funding channels, could turn selective. The banking turmoil could see lenders turning more risk averse, slowing credit availability further for borrowers, especially highly leveraged ones.
- **China returns.** China's exit from COVID earlier this year will aid economic recovery, as social mobility resumes. This rebound will also benefit sectors, especially chemicals, gaming, technology, and transportation cyclical markets. That said, weaker than expected consumption and external demand could hinder that recovery.
- **Slowing growth.** We expect Asia-Pacific's real GDP to grow 4.6% in 2023, supported by China's expected rebound following the end of its zero-COVID policy. That said, the region will have to contend with economic slowdowns in other parts of the world, external pressure from rising U.S. interest rates, and the persistence of elevated core inflation in some of its economies.
- **Net rating outlook bias**. The region's net rating outlook bias was steady at negative 3% as of end-February 2023. But a confluence of headwinds arising from tepid global demand, tighter and more uneven financing, and high input prices are downsides to ratings headroom.

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(Editor's Note: This report is an expansion of the "Sector Trends" section from our "Credit Conditions Asia-Pacific Q2 2023: Still Steady, Banking Turmoil Risk Is Moderate Here" report, published March 28, 2023.)

Tighter credit availability. Financing costs have already been rising in Asia-Pacific on the back of volatile global markets. Combined with the ongoing banking turmoil, the region's borrowers could see funding access squeezed. Risk aversion among lenders, investors, and depositors is growing. Demand for higher risk premia and tighter credit availability could create liquidity challenges. Domestic funding channels (including bank loans) remain available, but the risk remains that banks could turn increasingly selective and curtail lending, given uncertain economic outlooks.

Costlier inputs and borrowing. Inflation remains pronounced in some Asia-Pacific economies, including Australia, India, and the Philippines. Global commodity and energy prices have retreated as of late, but with domestic currencies still soft against the U.S. dollar, import prices could remain elevated. Meanwhile, weak demand is making it difficult for corporates to pass higher input costs onto customers--particularly in the building materials, capital goods, consumer products, and metals and mining sectors. Coupled with costlier borrowings, nonfinancial corporates could face higher stresses and default pressures (see "Corporate Top Trends Update: Asia-Pacific Corporate Credit Outlook 2023," published Feb. 21, 2023).

Concurrently, the undoing of energy price controls previously provided by some governments (to support households and businesses) could exacerbate inflation. Such inflationary pressures could constrain consumer sentiment and dent demand in the auto, consumer products, media and entertainment, real estate development, and retail sectors.

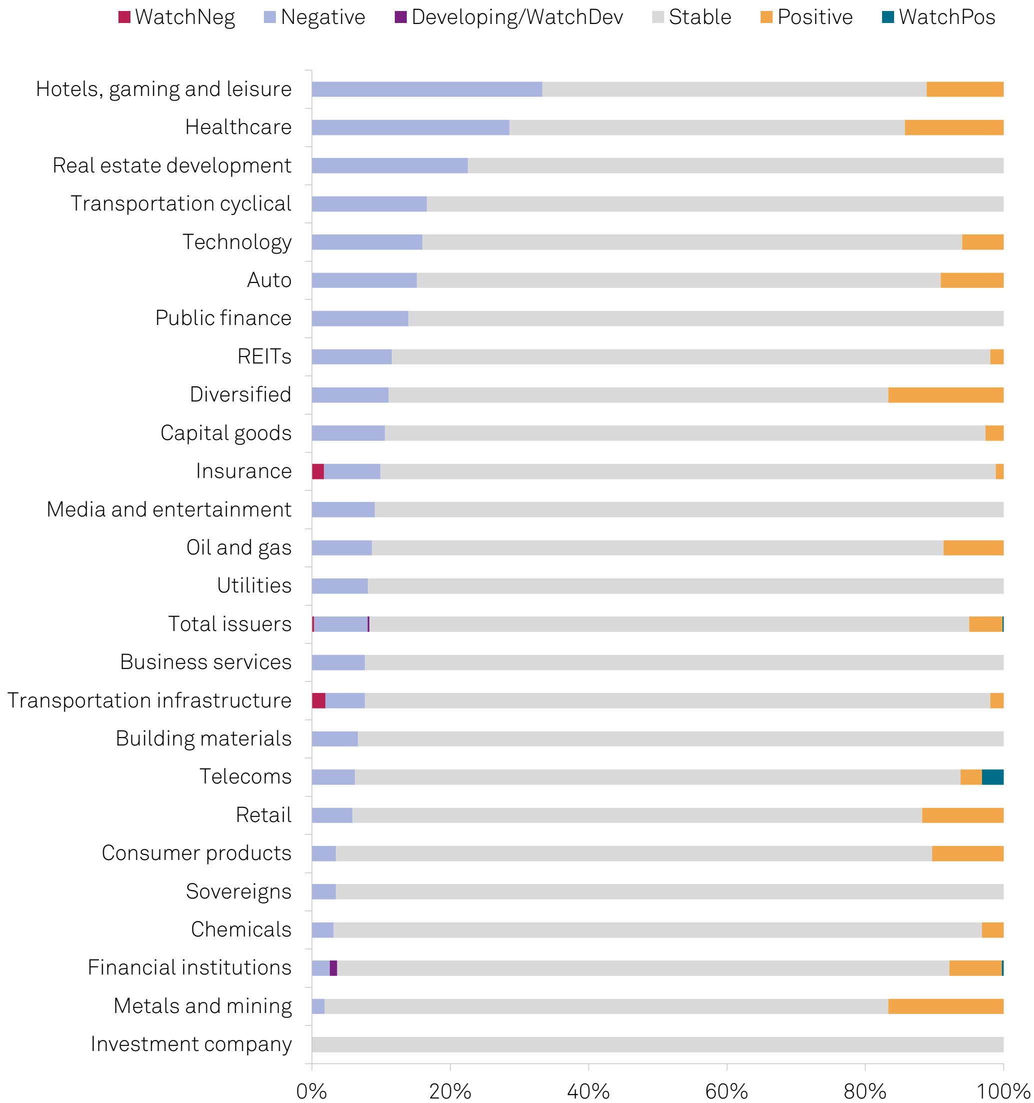
Exports down. Weaker global demand emanating from economic slowdowns would be a drag on the region's export-centric economies. Capital goods and capex investment could contract as business confidence wanes. Concurrently, second order effects from the banking turmoil--tighter financing access and higher risk premia--could become more pronounced should contagion spread more widely.

China's recovery. China's economy is on track to recover this year following the abrupt removal of COVID restrictions. Amid the country's return to normality, mobility and confidence have picked up. However, the recovery could face setbacks from subdued domestic consumption and weak external demand (see "Economic Research: The Case For Cautious Optimism On China's Rebalancing And Openness," published March 13, 2023). Meanwhile, Beijing looks to fortify debt risk controls as part of the focus on financial system stability, which was highlighted at the recent "Two Sessions". As such, local government financing vehicles (LGFVs) could face refinancing challenges (see "China's Local Governments Are Shedding Their Ties To Struggling SOEs," published March 2, 2023).

Downsides rising. While the net rating outlook bias remains steady at negative 3% as of end-February, more sectors are seeing deterioration in their net rating outlook bias (see table 1). Of the 25 sectors we cover (including nonfinancial corporates, financial services, sovereign, and public finance), seven sectors saw a deteriorating trend (Feb. 28, 2023), compared with five in Oct. 31, 2022.

Chart 1

Outlook Distribution Of Asia-Pacific Issuers By Sector



Note: Data cut-off is at Feb. 28, 2023.
Source: S&P Global Ratings.

Table 1

Net Outlook Bias Of Asia-Pacific Issuers By Sector, Feb. 28, 2023

	Feb. 2022	May 2022	Aug. 31, 2022	Oct. 31, 2022	Feb. 28, 2023	No. of entities	Notional average rating
Auto OEM and suppliers	-3%	-3%	0%	0%	-6%	33	BBB
Building materials	-7%	-14%	-8%	-7%	-7%	15	BBB-
Business services	-23%	-17%	-15%	-8%	-8%	13	BB+
Capital goods	-29%	-19%	-11%	-11%	-8%	38	BBB
Chemicals	0%	0%	3%	0%	0%	32	BBB
Consumer products	-8%	-11%	-4%	-3%	7%	29	BBB
Diversified	20%	0%	0%	0%	6%	18	A-
Healthcare	-11%	-22%	-13%	-29%	-14%	7	BB
Hotels, gaming, and leisure	-19%	-24%	-15%	-20%	-22%	18	BB
Investment company	0%	0%	0%	0%	0%	7	A
Media and entertainment	-20%	-20%	-22%	-11%	-9%	11	BBB
Metals and mining	9%	9%	11%	12%	15%	54	BB+
Oil and gas	-26%	-17%	-9%	-4%	0%	23	BBB+
Real estate development	-32%	-39%	-32%	-28%	-23%	31	BB+
Real estate investment trusts	-12%	-13%	-13%	-13%	-10%	52	BBB+
Retail	-31%	-19%	-6%	-6%	6%	17	BBB
Technology	0%	-2%	0%	-5%	-10%	50	BBB
Telecommunications	-7%	-10%	-10%	0%	0%	32	BBB
Transportation cyclical	-11%	-17%	-17%	-17%	-17%	18	BBB
Transportation infrastructure	-7%	-10%	-3%	-4%	-6%	52	A-
Utilities	-4%	-5%	-6%	-6%	-8%	99	BBB+
Total corporates	**-9%**	**-10%**	**-7%**	**-6%**	**-5%**	**649**	**BBB**
Financial institutions	3%	-1%	3%	6%	5%	383	BBB+
Insurance	-3%	-2%	-11%	-11%	-9%	172	A
Public finance	-13%	-13%	-12%	-9%	-14%	86	AA-
Sovereign	-7%	-7%	-7%	-7%	-3%	29	BBB+
Total issuers	**-5%**	**-7%**	**-5%**	**-3%**	**-3%**	**1,319**	**BBB+**

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

Teal colored cells indicate improvement from prior period, red, deterioration.

Source: S&P Global Ratings.

Auto

Carmakers to navigate market uncertainties

What we expect over the next 12 months

- The rating headroom for most rated Asia-Pacific auto companies will remain sufficient over the next 12 months, a function of entities' largely stable market position and low leverage.
- However, the net rating outlook bias turned more negative, mainly due to margin pressure caused by electrification and supply-chain disruption.
- These issues could continue to weigh on the profitability and cash flow of the carmakers amid demand headwinds in 2023.

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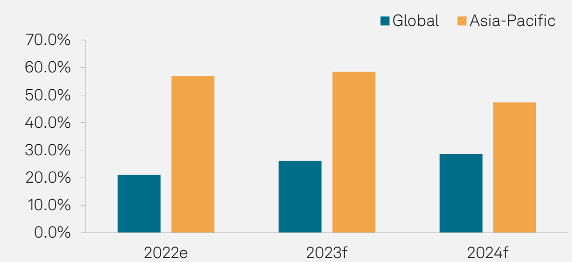
FFO/Debt (Median, adjusted)



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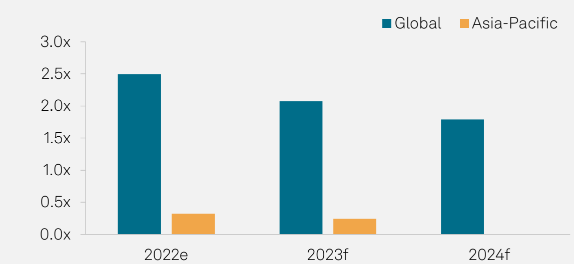

All figures are converted into U.S. dollars using historical exchange rates. Forecasts are converted at the last financial year-end spot rate. FFO--Funds from operations. e--Estimated. f--Forecast. Source: S&P Global Ratings.

Downside risks...

Slowing global economy. High inflation and mild recession risk in the U.S. and Europe could dampen consumption. While China's termination of its zero-COVID policy may advance economic recovery, we have less certainty about consumers' willingness to spend on big-ticket items.

Supply chain disruption. While we expect a gradual normalization in global auto supply chains, semiconductor and electric component shortages could be protracted. U.S. restriction on China's import of semiconductors may also bring operational challenges to the new car development for Chinese carmakers.

Intensifying competition. Growth momentum for China's electric vehicle (EV) sector could soften, with the EV penetration rate already about 30% and with the central government phasing out consumer subsidies. Pricing conditions have worsened with EV producers cutting prices at the start of the year to gain market share.

...and what they mean for the sector

Uncertain demand outlook. We expect China's light vehicle unit sales to grow 2% in 2023, reflecting improving consumer sentiment and the end of government stimulus measures. Consumers' propensity to save could present downside risk. The 3%-8% sales recovery in the U.S. and Europe depends on the resilience of demand, given weakening economic fundamentals and high interest rates.

Margin and cash flow pressure. Automakers that are on the fast lane of electrification already felt the pain of margin dilution, given high battery costs. Price competition in China, a less favorable pricing environment in the U.S. and Europe, and supply-chain issues could also dent Asia-Pacific carmakers' profitability and cash flows. Rating buffers would tighten if softer commodity prices, improving operating efficiency, and product upgrades are insufficient for issuers to mitigate these pressures.

Building Materials

Asia-Pacific producers to brace for market volatility

What we expect over the next 12 months

- The creditworthiness of most rated Asia-Pacific building material companies will stay stable over the rest of 2023, given a sufficient financial buffer to weather through uncertainty on demand and profitability.
- With China's reopening from COVID-19 lockdowns and the bottoming out of the sluggish property sector, Chinese producers are likely to see a recovery in demand and financial performance around mid-year.
- The Korean market is likely to weaken after a robust 2022. Rising interest rates and waning housing prices in the recent months could continue to weigh on demand. The operating conditions in the Australian market remain the most favorable in the region. Residential activity should stay strong on a material backlog over the near term and public sector investment supportive.

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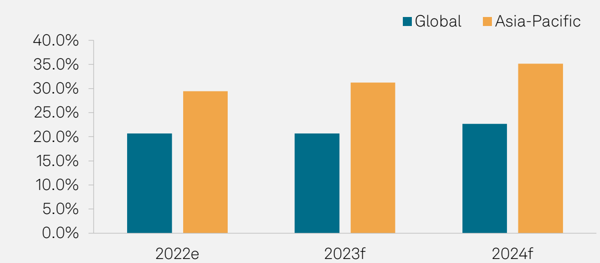

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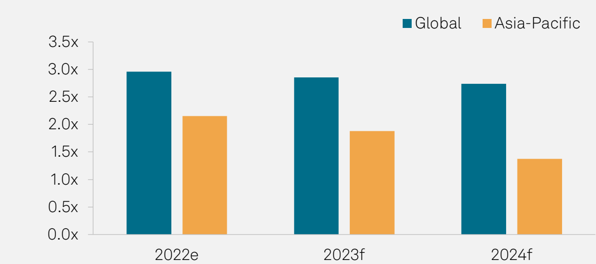

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Downside risks...

Subdued recovery in China post-pandemic and rising interest rate outside of China. Local governments' tight debt control post-pandemic could result in a weaker-than-expected acceleration of infrastructure investment. China's property crisis may turn around in the next three to six months, with a recovery possible in the second half of 2023. But the recovery could be fragile and the uptick of construction activities mild. Outside China, the macro risk largely comes from the higher interest rates that could subdue the property sector.

Elevated input cost and supply chain constraints. This includes higher fuel prices (mainly coal) and power costs driven by supply constraints and geopolitical risks, and higher labor costs. The industry could also continue to face raw material shortages due to a supply chain bottleneck caused by geopolitical and extreme weather events.

...and what they mean for the sector

Demand pressure. Subdued economic growth and low property new launches in China could continue to hit construction activities and thus the demand for building materials. Supply chain constraints for the rest of the region could cause construction delays and limit demand growth for building materials.

Margin squeeze. Still-high raw material and fuel prices are likely to squeeze building material companies' profitability. Managing costs through operational efficiencies and execution of price increases is key to mitigating input cost inflation. Chinese players could still have a weaker cost pass-through than peers in the rest of the region before demand recovery and ease of oversupply.

Capital Goods

Demand and cash flow outlook mixed

What we expect over the next 12 months

- We expect the outlook on earnings to be mixed due to China's recovery not fully offsetting the weakening economic activities outside Asia-Pacific.
- Key risks include recession-related slowdowns in capital spending by corporate customers and weak ability to pass on costs.
- Demand outlook and the degree of margin protection, as well as cash flow management, will be key drivers for credit quality.

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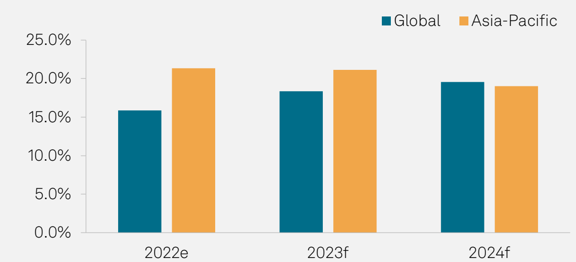

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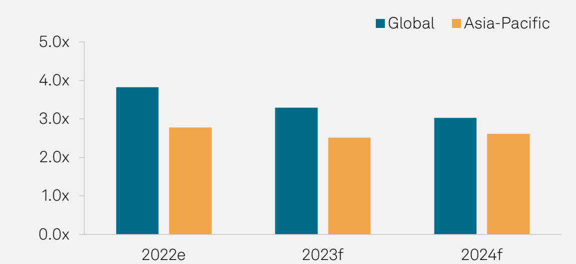

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Downside risks...

Prospects of earnings recovery in China and outside may diverge. The earlier-than-expected exit from zero-COVID in China bodes well for the recovery of China's corporate sector, enabling a turnaround for Chinese capital goods companies' earnings. However, companies outside of China, such as in Japan, are also exposed to slowdowns in the U.S. and Europe. That could depress corporate investment sentiment, slowing capex investments owing to weaker customer demand (especially the semiconductor and auto sectors).

Cost pass-through continues to be challenging. Cost pressure is easing. However, if demand from customers softens before capital goods companies can fully pass on increased costs, their profit growth will suffer.

High spending but weaker cash flow. Capital goods companies' own capex and spending for shareholders' return are likely to increase. But EBITDA and cash flow would be eroded by inflation or the weaker macroeconomy, potentially hurting credit metrics.

...and what they mean for the sector

Margin erosion. We do not believe capital goods companies in Asia-Pacific, especially in Japan, can pass on most of their cost increases to customers, given harsh competition. A lowered ability to pass on costs, together with weaker demand and sales, will result in reduced profitability.

Cash flow management. Given our continued expectations of a weaker economic environment, we assume capital goods companies will tighten working capital management and control discretionary spending, such that the industry's ratio of debt to EBITDA may improve in 2023. However, if a recession is prolonged, or a faster-than-expected recovery in China poses a burden to working capital, the ratio may remain at 2022 level.

Chemicals

China's reopening could stabilize Asia's chemical market

What we expect over the next 12 months

- China reopening could stabilize chemical prices in Asia and prevent a deeper downturn.
- High feedstock costs could continue to subdue the profitability of crude oil-based chemical companies in Asia.
- Weak profitability and cash flow will test financial buffers for companies that are more exposed to commodity chemicals.

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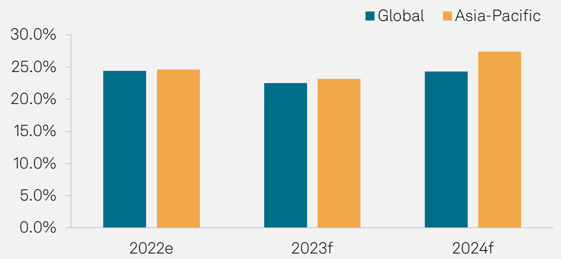

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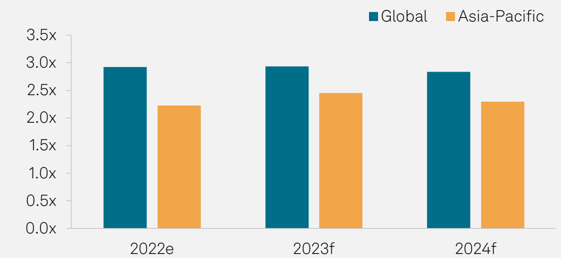

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Downside risks...

Weaker chemical demand. Recovering demand in China after its swift reopening from COVID lockdowns may not sufficiently lift domestic consumption in Asia to offset the negative effect of weaker exports.

Weaker cost pass-through ability. Chemical companies, especially commodity producers, may not be able to pass-through still-elevated input costs. Greater supply, particularly in China, and imports from low-cost producers could suppress Asian chemical companies' pricing power.

Rising debt. Weaker profitability, high cash dividends, and continued capital spending will increase debt, further raising debt leverage from 2022.

...and what they mean for the sector

Weaker-than-expected profitability. Chemical companies' profitability in 2023 is likely to stabilize at a level below the average of past cycles.

Manageable debt leverage. Rated entities' debt leverage is likely to remain largely within rating triggers in 2023, despite higher debt.

Limited financial headroom for an extended downturn. Downside rating pressure could rise if the current downturn extends beyond 2023 and further narrows rating buffers, particularly for companies that have high exposure to commodity chemicals.

Consumer Products

Pinched consumers = pinched margins

What we expect over the next 12 months

- Recovery in consumer sentiment to remain modest despite the reopening of China.
- Profitability squeeze. Companies won't likely be able to fully pass on high input costs amid challenging economic conditions, including falling real incomes of consumers.
- Prudent financial policies will support credit profiles of consumer-product companies.

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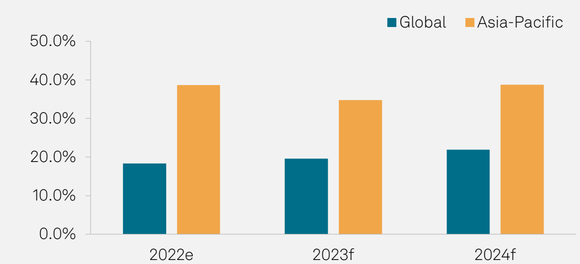
FFO/Debt (Median, adjusted)



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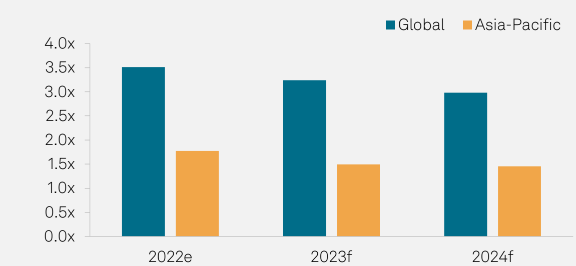

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Downside risks...

Price competition intensifies. This means further margin compression given inflationary environments. Where higher prices do pass through, this could benefit private-label brands--as consumers trade down to cheaper, no-brand goods.

Consumers tighten discretionary spend. The weak global economic outlook hits consumer confidence hard, and further dampens demand, especially for more discretionary products or big-ticket items.

Souring financing conditions. Growing refinancing costs from unfavorable exchange rates and higher interest rates weigh on companies with highly leveraged capital structure.

...and what they mean for the sector

Brand equity matters. Ability to pass on higher costs hinges on differentiated value propositions of each company, enabling them to protect profitability amid intensified price competitions and elevated input costs.

Bifurcation in performance. Companies operating in discretionary categories face softer demand than those in staples, polarizing performance within the consumer products sector.

Slower debt growth. Higher funding costs urge highly leveraged companies to take a prudent financial policy. Challenging economic environments also encourage companies to focus more on their core businesses than large M&A transaction.

Financial Institutions

Banking sector volatility may chart the course

What we expect over the next 12 months

- Most Asia-Pacific banks can absorb contagion effects from global banking stresses at current rating levels, unless risks intensify significantly.
- We believe the direct exposures of Asia-Pacific banks to Silicon Valley Bank, and Credit Suisse's additional Tier-1 instruments are negligible.
- Much weaker growth and higher rates outside our base case will test rating outlooks. A significant escalation of banking sector stress in the U.S. regional bank sector, or in Europe after the Credit Suisse takeover, could transmit to Asia-Pacific.

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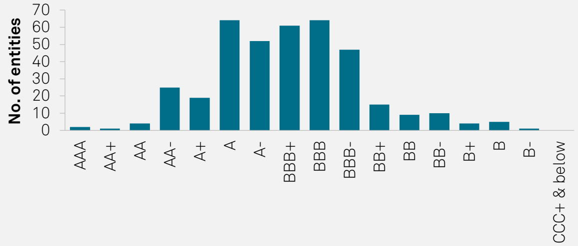
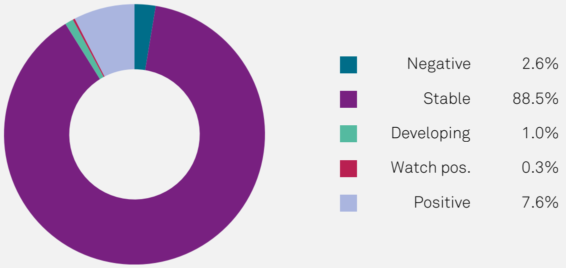
Rating distribution



Outlook distribution



As of February 28, 2023. Source: S&P Global Ratings.

Downside risks...

Economic downside risks intensify. Banks' net interest margins benefit from higher interest rates, but materially weaker economic prospects or higher-for-longer interest rates will eventually hurt banks' asset quality. A much weaker economic outlook, superimposed upon already-highly leveraged corporate, household, and government sectors, and a property market experiencing pockets of stress, could manifest negatively for Asia-Pacific financial institutions.

Weaker confidence. A significant escalation of global banking turmoil, or greater contagion spillover, could side-swipe otherwise sound Asia-Pacific banks.

Structural risks. Climate change, cyber attacks, and the need to invest in and execute on digitalization will increasingly test banks and their borrowers.

...and what they mean for the sector

Strain asset quality. Net interest margins for most financial institutions are benefitting from higher interest rates. However, if economic headwinds are much worse than we now anticipate, this will dampen credit demand and strain corporate and household borrowers.

Greater credit differentiation. Asia-Pacific financial institutions with high direct exposures to weak counterparties or sectors, or that are inherently weaker and non-systemically important, are more vulnerable. Greater credit divergence could result from worsening contagion.

Gaming

Macao gaming: better prospects of a revenue recovery

What we expect over the next 12 months

- Gaming revenue in most Asian markets should largely recover to pre-pandemic levels in 2023.
- Improving revenue in Macao amid China's shift away from zero-COVID should help operators turn around cash burns and support stronger credit metrics.
- Regulatory risks persist across Asia.

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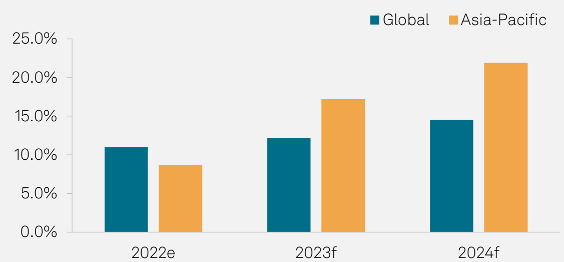

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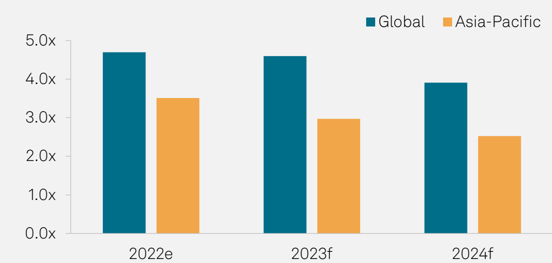

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Downside risks...

Dimmer economic outlook. This will affect travel demand and discretionary spending on leisure activities.

Regulatory changes and pressures. Increased regulations across the region to address social risks in gaming could introduce volatility in gaming revenue and profitability. This is a risk for casino resorts operators in Macao and Singapore, as well as the gaming machine business in Japan.

Growing refinancing costs from higher interest rates and still-weak operating performances. These will test companies' liquidity and management of capital structures.

...and what they mean for the sector

Outlook on Macao casino ratings remains negative. Macao's gross gaming revenue beat our expectations in January. We will be monitoring whether this is a trend or holiday boost. Overall, we see lower downside risks to ratings compared with the start of the year.

Pace and magnitude of recovery. As Asian gaming markets return to pre-pandemic levels in 2023, we will be watching for possible structural changes in gaming visits or spending behavior, due to shrinking consumer wallets amid weaker economies.

New concession award in Macao eliminates license uncertainty. Investment commitments are high but should be manageable as long as Macao's gross gaming revenue recovers this year.

Insurance

Restoring revenue amid volatile earnings

What we expect over the next 12 months

- Credit trends remain stable, though market strains could create volatility.
- Capital market and foreign-exchange swings could squeeze capital and earnings.
- A normalization in mobility after the lifting of COVID controls may facilitate growth.

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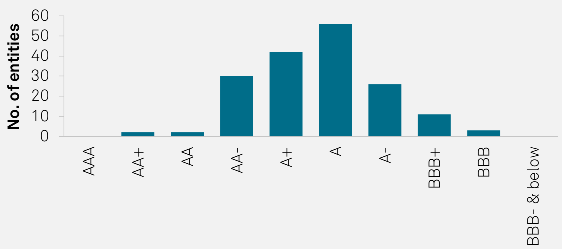
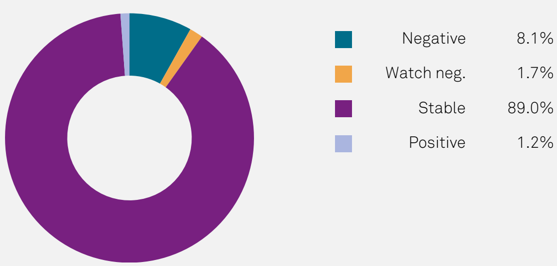
Rating distribution



Outlook distribution



As of February 28, 2023. Includes public ratings only.
Source: S&P Global Ratings.

Downside risks...

Contagion spillovers. Second-order effects from the banking turmoil could result in greater market volatility, hitting insurers' investment portfolios. While direct exposure to the banking sectors of the U.S. and Switzerland is small, some insurers may have concentrated counterparty exposure.

Dimming earnings. For the non-life insurers, slowing economic growth could depress commercial insurance as trade activity slips. A hike in reinsurance costs amid extreme weather could dent insurers' underwriting profits.

...and what they mean for the sector

Market volatility could dent capital and earnings. Challenging capital market and rising foreign-exchange hedging cost could hit earnings. Prolonged equity market volatility could dilute capital buffers. Still-high interest rate differentials will keep hedging costly. Except for China, rate hikes across the region could dent asset valuations and result in unrealized losses. That said, higher interest rates may ease pressure for reserve provisioning (except in China).

Narrowing insurance margin. Rising reinsurance costs could weigh on non-life insurers' profit margins if they are unable to fully pass this expense to customers. Global climate change and rapid urbanization across emerging Asia could result in higher catastrophe losses.

Hurdle for premium recovery. Slower economies could drag on premium growth momentum. However, the exit from COVID-19 restrictions globally could restore revenues in some markets. In addition, still-low insurance penetration and government initiatives should support the elasticity of insurance demand.

Media And Entertainment

China's social media platforms could benefit the most from the winter thaw

What we expect over the next 12 months

- China's reopening could benefit Chinese online media platforms, particularly e-commerce. Advertising spending--particularly for social media platforms--could pick up, catching the consumption recovery.
- Rising interest rates and slowing growth remain key concerns for the region. Slower economic activity could inhibit consumers, and, therefore, advertising spending.
- Most Asia-Pacific media and entertainment companies have sufficient financial buffer to withstand an economic slowdown.

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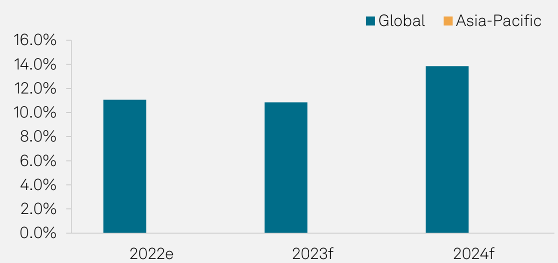
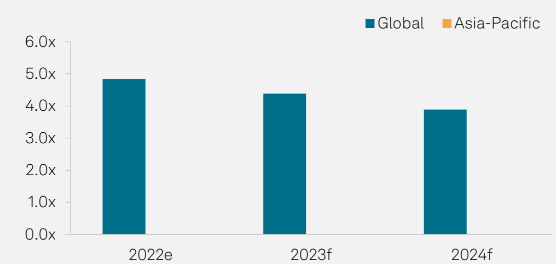
FFO/Debt (Median, adjusted)



Debt/EBITDA (Median, adjusted)



Note: All figures are converted into U.S. dollars using historical exchange rates. Forecasts are converted at the last financial year-end spot rate. More than half of the Asia-Pacific media & entertainment rated portfolio has zero debt on an adjusted basis. FFO--Funds from operations. e--Estimated. f--Forecast. Source: S&P Global Ratings.

Downside risks...

Rising interest and global economic slowdown could weigh on consumption recovery. Though consumer and advertising activity picked up in China during the first two months of 2023, challenging macro conditions globally could still constrain the consumption recovery. This could hit internet companies that have resumed investment spending in anticipation of better growth, after cutting costs in 2022.

Intense competition could squeeze margins and cash flows. Internet companies across Asia-Pacific face intense competition from existing and newer entrants. In China, short-form video platforms are entering into segments long dominated by incumbents such as e-commerce, food delivery, and games. In other regions, competition for the nascent businesses remains stiff, for example e-commerce in Southeast Asia.

...and what they mean for the sector

Advertising-driven social media platforms to experience a stronger recovery in 2023. Online social media companies should benefit the most from a recovery in advertising spending, following a decline in non-e-commerce advertising spending last year. E-commerce advertising revenues fared better last year, as consumers diverted spending online given sporadic COVID-related restrictions across China.

Most Asia-Pacific companies within the sector have sufficient financial buffers. Most of our rated media and entertainment issuers are net cash or have large financial buffers to withstand challenges posed by slowing economic growth and rising interest and inflation. A small minority will benefit from the lifting of lockdown measures across Asia-Pacific countries and recovery of outdoor activities.

Metals And Mining

Improved macroeconomic developments on China reopening

What we expect over the next 12 months

- China's removal of pandemic restrictions and its energy transition will drive a demand recovery for some metals products; the weaker growth of the U.S. and Europe may partially offset the positive impact.
- Supply tightness or the shortage of some commodities products may provide price support. Supply rigidity may result from the Russia-Ukraine conflict, lack of project development in the previous years, export bans, extreme weather, or ESG matters.
- Geopolitical risks, China's recovery path out of COVID, and additional supply-disruptions will exacerbate the volatility in commodity markets.

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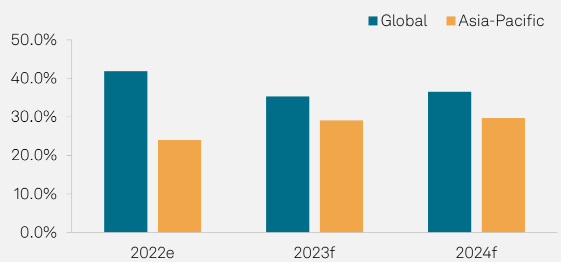
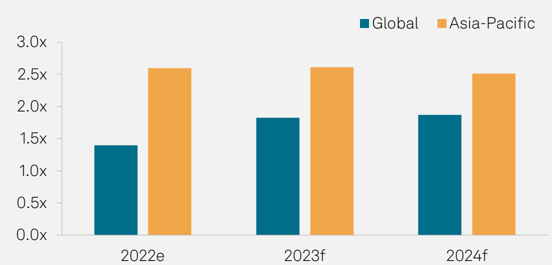
FFO/Debt (Median, adjusted)



Debt/EBITDA (Median, adjusted)



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Downside risks...

Economic pressures exacerbate. Our current base-case price assumptions assume a mild recession, but risks to a harsher downside persist. The U.S. and Europe could experience heavier GDP contractions. China's property sector continues to weigh on the economic growth and the demand for some metals.

Geopolitical risks escalate. That, and how they unfold, further limit price visibility.

Lower prices and inflationary pressure eat into margin. With prices moderating, costs rising, margins and cash flow are dropping. Some issuers continue to distribute trailing dividends to shareholders. Therefore, we expect weaker profits and lower cash holdings to consume some credit buffer.

...and what they mean for the sector

Improved demand as China reopens. Given China accounts for over half of global demand for raw materials, the demand recovery from China could provide support to key metals prices. Furthermore, government measures to boost the economy and stabilize the real estate sector may support steel demand.

Credit quality is generally good in the sector, but credit buffers could be eroded. The credit quality for many issuers in metals and mining has been improving with greater capital discipline and lower debt. While our ratings bias remains positive, the pace of positive rating actions should slow as earnings weaken.

Earnings visibility is blurred by the high volatility in prices for commodities and energy. This is the result of different catalysts, including economic uncertainty, currency swings and geopolitical risks.

Oil And Gas

Supportive hydrocarbon prices to continue in 2023

What we expect over the next 12 months

- Supply factors will ensure hydrocarbon prices and refining margins will remain supportive through 2023. Brent oil prices will likely average US$95 per barrel in 2023, and US$85 per barrel in 2024.
- The demand outlook in Asia-Pacific is mixed. Easing COVID restrictions in China will stimulate consumption in the short term, while the possibility of a global recession weighs on the long-term outlook.
- Increasing risks from government regulation, taxation, and policies amid concerns over energy affordability and security, and decarbonization.

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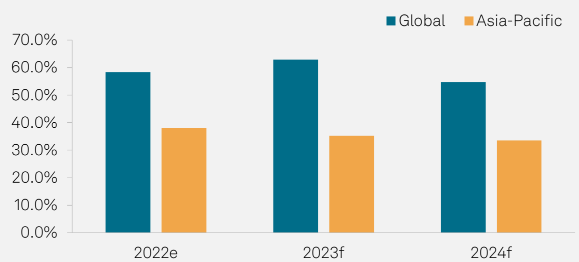

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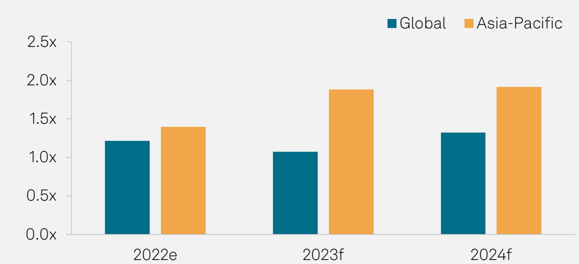

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Downside risks...

Volatility in demand growth. Given the slow growth momentum in the U.S. and Europe, demand from China will be crucial in supporting oil prices. Chinese demand, however, is subject to many variables, including the country's post-COVID recovery, local consumption, and the ramping up of downstream capacities. An escalation in the Russian-Ukraine war could lead to energy price spikes, worsening the supply-push inflation and with eventual implications for demand.

Low supply situation. Global inventory levels will remain low in 2023. Any significant increases in the OPEC+ production will be unlikely given that some OPEC+ members are already struggling to maintain their current production targets. The EU embargo on Russian energy means volatility, especially for liquid natural gas (LNG), will continue as the EU looks for new supply to replace Russian gas.

Government intervention. Rated oil and gas companies in Asia-Pacific are exposed to increasing regulatory risks as governments attempt to curtail energy price spikes. A subdued economic outlook could limit governments' ability to keep up with the funding of their oil subsidy programs, incurring sizable account receivables at some rated oil companies.

...and what they mean for the sector

More industry volatility up ahead. Demand pullback could offset earnings headwinds stemming from high prices. Governments' negative intervention may temper rated companies' profitability and cash flow viability.

Urgency to invest in renewable assets. Fossil-fuel supply shortages will add urgency for rated producers to increase their renewable energy assets. Given rising interest rates, rated producers will have to balance investment needs and their need to bolster balance sheets, with earnings strained over the next 12 months.

Public Finance

Fiscal weaknesses amid persisting external challenges

What we expect over the next 12 months

- Inflation and rate hikes will weigh on local and regional governments (LRGs) and their associated enterprises.
- China will keep high capital spending to ensure its recovery in 2023, while gradually transitioning to a consumption-led recovery alongside fully reopened borders.
- Local governments in Australia and New Zealand are using large infrastructure projects to stimulate economies; the practice will persist until at least 2023.

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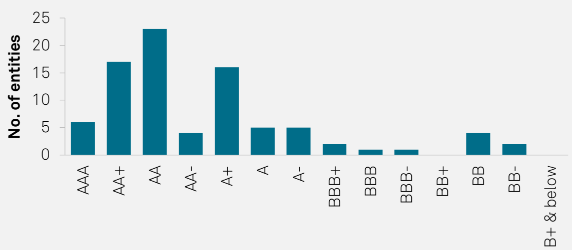
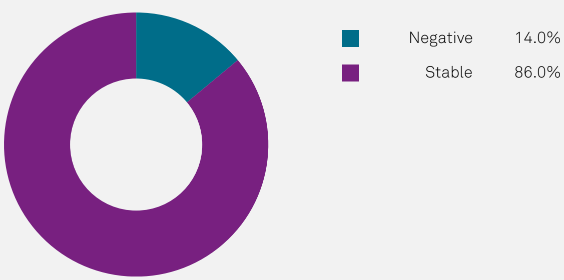


Outlook distribution



As of February 28, 2023.
Source: S&P Global Ratings.

Downside risks...

Economic shock. Persisting inflation and higher interest rates, and downside risks to the global economy, could further squeeze the region's consumption, supply chains, and economic growth, leading to declining revenues for LRGs.

Property market correction. Most LRGs in the region are fiscally dependent on revenues tied to domestic property sales and prices. China's "L-shaped" property correction will remain as risks to local recovery and market confidence.

Policy shifts. To ameliorate the economic slowdown and restore confidence, select LRGs could roll out aggressive fiscal stimulus, including tax cuts and additional spending. The Three Waters Reform in New Zealand may alter its public finance system as details are disclosed in upcoming legislation.

...and what they mean for the sector

Delayed fiscal recovery. To counter the GDP slowdown and restore confidence, some LRGs may push forward aggressive fiscal stimulus that would disrupt their fiscal recovery and lift debt.

Resumption of leveraging SOE investments in China. Chinese LRGs may add to leverage if they let their SOEs use debt to support public investment to stimulate local economic growth, while also committing to support the entities in a stress scenario. China's increased tolerance of SOE defaults, meanwhile, may stymie or otherwise disrupt local economies.

Real Estate Development

China property is on the cusp of a recovery

What we expect over the next 12 months

- The China property market's L-shaped recovery may see a turning point in the second half of 2023.
- Transaction volumes in Hong Kong may rebound in 2023 supported by lowered prices and pent-up demand.
- Lower-rated Indonesia developers will continue to face a constrained offshore funding environment.

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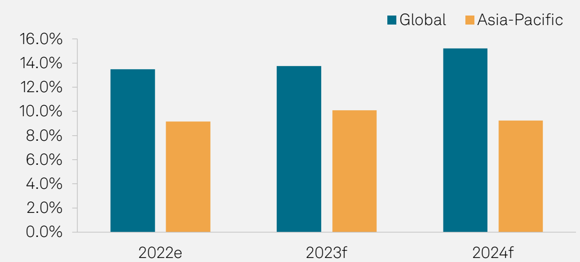
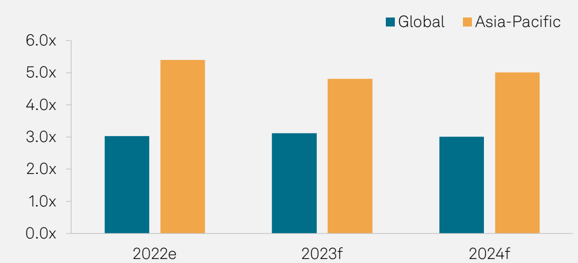
FFO/Debt (Median, adjusted)



Debt/EBITDA (Median, adjusted)



Note: 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. e--Estimated. f--Forecast. Source: S&P Global Ratings.

Downside risks...

Property sales are still weak in China. On the back of government's supportive measures and the earlier lifting of COVID-related lockdowns, the physical market may recover in the next three to six months. That said, sales of the top 100 property developers still dropped by about one-third in January.

High inventory levels will weigh on Hong Kong's residential property prices. After dropping by 15% in 2022, prices have shown early signs of stabilization in January. Prices will likely linger at a lowered level as inventory in the primary market reached a 15-year high as at end 2022.

Indonesia's residential sales will experience a flat to single digit decline in 2023. This compares with about 5% growth in 2022. Elevated inflation, higher mortgage rate expectation, and the lack of new policy incentives will constrain consumer sentiment.

...and what they mean for the sector

The Chinese government's recent policies could spark property demand. Such measures include lifting home purchasing restrictions and easing downpayment requirements. Furthermore, Chinese banks in multiple cities further lowered their mortgage rates for first-time homebuyers recently.

Lowered prices may support volume recovery in Hong Kong. In 2022, residential property transaction volumes fell by 39%. However, supported by a potential economic recovery due to the lifting of COVID restrictions, transaction volumes could rebound in 2023 on the back of solid mass-market demand.

Indonesia developers' free operating cash flow will remain thin. Cash positions will be further eroded as entities refinance U.S.-dollar debt obligations through domestic amortizing bank loans. This will increase the likelihood that developers conduct debt market transactions below par ahead of actual maturity dates.

Real Estate Investment Trusts

Most Asia-Pacific REITs will remain resilient

What we expect over the next 12 months

- Ongoing soft office demand, coupled with oversupply, will exert downward rental pressure for offices in markets such as Hong Kong and Japan.
- A further recovery in tourism will boost the performance of hotels and downtown retail malls in gateway cities.
- More measured pace of acquisition and development given higher financing costs and economic headwinds.

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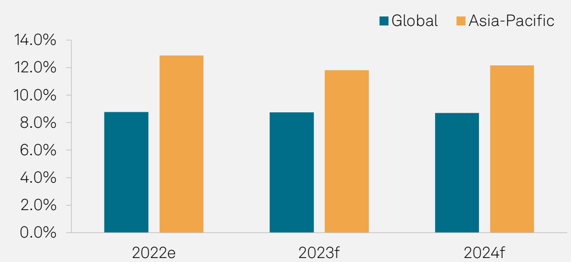
FFO/Debt (Median, adjusted)



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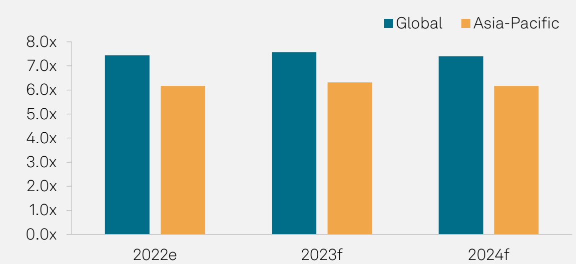

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Downside risks...

Interest rates higher for longer. Leading to subdued credit metrics, further cap rate expansion, declining asset valuations, and an erosion in covenant headroom.

Shorter and costlier financing. REITs are relying on shorter dated bank loans (relative to bonds) to manage their refinancing costs.

Further deterioration in business, consumer, and investor confidence. Leasing conditions may become more challenging. Vacancies may also be higher than expected. Waning investor confidence could accelerate wholesale fund redemptions in Australia.

...and what they mean for the sector

More challenging conditions will test buffers. While financial headroom could deteriorate, we expect most rated Asia-Pacific REITs can tolerate the challenging operating and financial conditions. Elevated interest rates and operating costs will likely erode ongoing rental income improvements. For asset classes that are not facing structural challenges, we expect asset valuation to remain largely stable for high-quality assets, given favorable supply-demand dynamics and higher replacement costs.

REITs have to manage shorter debt maturity profile. REITs' refinancing risk remains manageable. However, further shortening of debt maturity profile could weigh on their capital structure and credit quality.

"Flight to quality" benefits prime assets. Tenants' preference for prime retail locations and sustainable office buildings will support rated Asia-Pacific REITs, given they own quality assets.

Retail

Retailers to battle it out for consumers' limited disposable income

What we expect over the next 12 months

- Consumers are likely to pull back on consumption because of higher cost of living pressures that have resulted in lower savings buffers.
- Retailers' margins will be squeezed as their ability to pass through higher input costs has diminished; discounting activity increases as retailers try to unwind inflated inventories.
- Challenging refinancing conditions for speculative-grade issuers with weaker profitability and higher debt levels.

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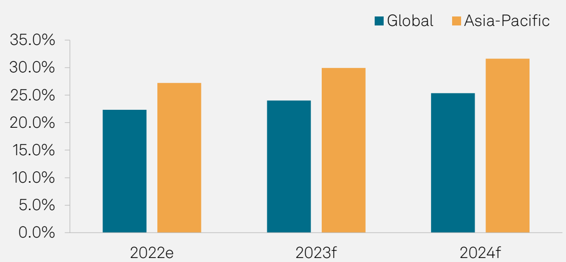
FFO/Debt (Median, adjusted)



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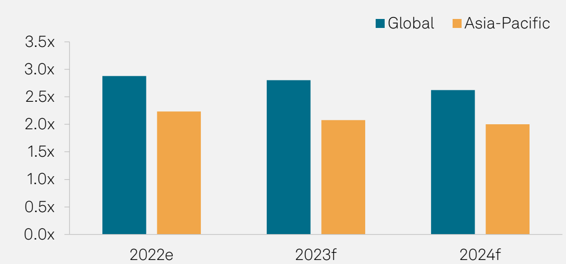

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Downside risks...

Consumers pull back significantly. A cash flow squeeze on households leads to a more dramatic reduction in spending than expected, leaving retailers to face an even more challenging operating environment. The reopening of China's economy does not provide an offset or translate into the consumption boost that Asia-Pacific domestic economies need at a time when growth is scarce.

Persistent inflation. Supply chain challenges and geopolitical tensions keep inflation high. Consumers' purchasing power continues to dwindle, lowering demand and squeezing margins.

Refinancing on favorable terms will be tricky. Retailers with higher debt levels and weaker profitability will find raising debt challenging.

...and what they mean for the sector

Profitability squeeze. Retailers will have to absorb rising input prices. Maintaining EBITDA margin stability will depend on the ability to pass on higher input and operating costs. Retailers also face price increase requests from suppliers, whose margins are eroding.

Working capital management comes into focus. As the cost of living rises and consumers forgo discretionary purchases, retailers carrying excess or more seasonal products are potentially at risk of being left with inventory that consumers no longer want or can afford.

Rising cost of debt to have divergent effects. Rising debt costs will test capital structures of speculative-grade issuers. While challenging capital markets will steer investment-grade issuers to a more conservative capital management approach, staying away from large debt-funded investments.

Sovereign

External uncertainties increase

What we expect over the next 12 months

- Global economic activity and financing conditions weaken, but not so sharply that it creates financial volatility in Asia-Pacific. Uncertainties associated with recent U.S. banking sector instability could weigh on investments.
- Current account balances in most economies should improve, especially if energy prices fall further with global economic uncertainties.
- We still expect some governments to meaningfully lower fiscal deficits, although a return to pre-COVID fiscal performances will take longer.

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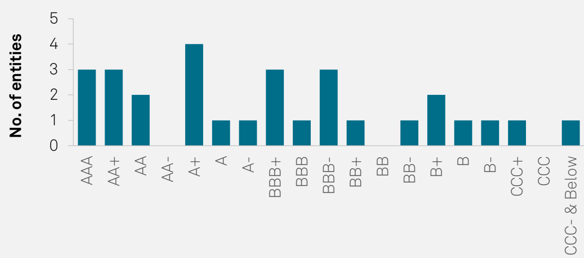
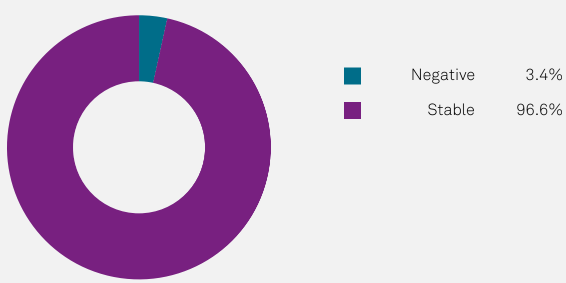
Rating distribution



Outlook distribution



Note: As of Feb. 28, 2023. Includes public ratings only, and ratings on policy-related financial institutions and corporates. Source: S&P Global Ratings.

Downside risks...

Sudden capital swings. An unexpected deterioration of global financial stability, geopolitical risks or interest rate expectations could see investors withdraw from emerging markets in Asia-Pacific, making financing conditions significantly more challenging for some.

High energy prices seriously undermine external and fiscal metrics. Amid the recent increase in economic uncertainties, current account deficits could remain wide in some Asia-Pacific economies, especially in places where governments subsidize energy consumption. A supply shock that raises energy prices sharply could still pose threats to external and fiscal support for regional sovereign ratings.

...and what they mean for the sector

Sharp increase in funding costs could weaken fiscal support and economic growth. Interest payments could rise to weaken fiscal support for sovereign ratings, especially where government debt is high and non-residents are important sources of funding. If higher financing costs also affect economic growth significantly, it could exacerbate the negative impact on fiscal performance.

High energy imports can damage external support for some Asia-Pacific sovereigns. Net external indebtedness would weaken where current account deficits persist or widen because of energy imports. Additionally, this deterioration could worsen investor confidence to raise financing costs further. These deteriorations could damage credit support of some sovereigns.

Structured Finance

Reopening, inflation, and interest rates shape outlook of households

What we expect over the next 12 months

- China's reopening may see structured finance issuance recover in 2023. Risks remain in China's housing sector.
- For markets where rates are rising, we expect delinquencies to increase and house prices to fall or moderate as borrowing capacity and serviceability stretch borrowers' budgets.
- We expect modest weakening in asset performance because employment remains at low and stable levels across markets.

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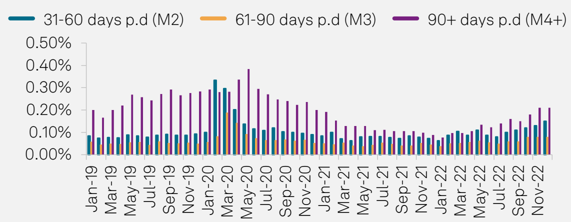
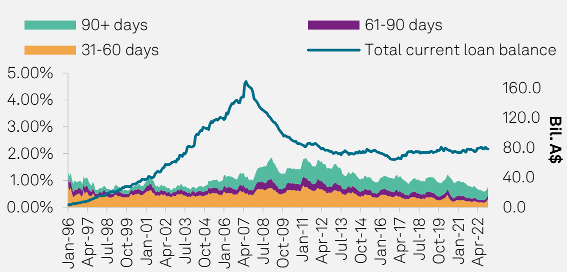
China auto loan ABS w.a. asset delinquency rates



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

Australian RMBS prime SPIN data



Note: Data as of Dec. 31, 2022. Source: S&P Global Ratings.

Downside risks...

Rates and inflation. Inflation remains a key issue for most Asia-Pacific economies. Australia, Korea, and New Zealand are continuing to grapple with higher interest rates to tackle inflation. This is likely to translate into some borrower cohorts facing strains from both higher costs of living and higher mortgage repayments. Recent moves on interest rates and increases in inflation in Japan have not been dramatic, however, we consider these changes to be meaningful for the country, after years of low interest rates and persistent deflation. In our view, inflation could stress household finances if it is unaccompanied by growth in real wages.

China's housing sector risk. For China, a further prolonged weakening of sentiment in housing markets will continue to hit house prices and resale values.

...and what they mean for the sector

Issuance is likely to diverge. Lower lending activity and concerns around macroeconomic factors could see less issuance of structured finance assets, particularly in the second half of the year. On the other hand, following the rapid shift in COVID-19-related policies, China's structured finance issuance volume should mildly recover, with about 4% growth this year.

Delinquencies to rise. We expect that delinquencies are likely to increase across most markets and asset types, particularly those exposed to rapid interest rate increases, however this is off historically low levels and are generally supported by low and stable employment trends.

Structural supports are in place. Most transactions have or can build up supports to mitigate downside risks. We may see prepayment levels affected by constrained household budgets and also the level of refinance activity.

Technology

Outlooks are turning negative amid growing downside risk

What we expect over the next 12 months

- Rising rating pressure among tech companies due to deteriorating macroconditions and rising rates.
- A semiconductor downturn in 2023 due to weakening demand and industry-wide overstocking.
- China's recovery could be a key determinant for Asia-Pacific's tech sector in 2023.

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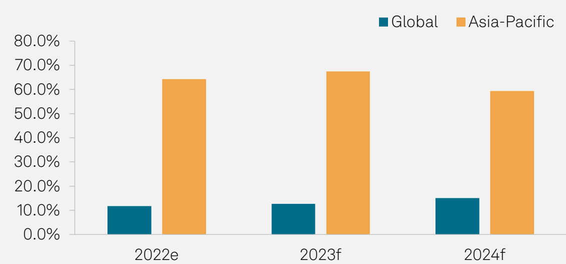
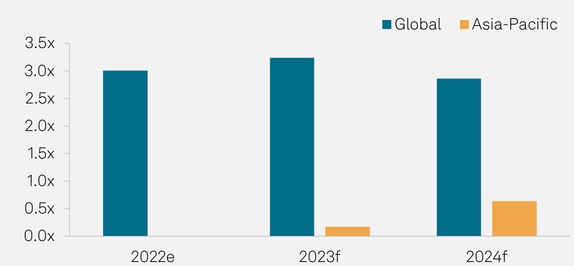
FFO/Debt (Median, adjusted)



Debt/EBITDA (Median, adjusted)



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Downside risks...

Macroeconomic risks. Deteriorating macroeconomic conditions and an uncertain recovery in China demand could contribute to weakening global hardware sales in the year. Geopolitical tensions expose Asia-Pacific tech firms to long-term risk. On the other hand, cloud spending such as on data centers, and recuring service revenue will likely support IT spending through macro downturns.

Inventory correction takes time. Industry-wide inventory correction could take time with falling demand. The correction, which is spreading through the value chain, could last for several quarters in 2023. Semiconductor demand is particularly weak; the memory sector could see the sharpest decline this year.

Narrowing financial buffer. Most of our Asia-Pacific technology hardware issuers have enough cash flow and leverage buffer to withstand a moderate shortfall in revenue and profitability. However, a prolonged downturn in demand could reduce such headroom.

...and what they mean for the sector

Lower global IT spending. The current IT spending growth of 3.3% could be lowered due to a pessimistic macroeconomic outlook, which would be meaningfully negative to certain tech hardware issuers.

Increasing cash flow volatility amid inventory correction. Higher cash flow volatility for rated hardware companies during the downcycle in 2023, with declining operating cash flow before meaningfully destocking.

Rating bias could turn more negative. Despite a still-stable credit outlook for Asia-Pacific tech firms, the macro downturn and rising rates could turn the rating bias more negative.

Telecommunications

Telcos divest to invest

What we expect over the next 12 months

- Telecom operators' earnings will benefit, and rise mildly, from increased mobile data traffic, wireline adoption, and the return of roaming revenues.
- Capex intensity should ease slightly, but remain high. Investments into 5G and fiber will stay to support increasing adoption.
- Divestment and investment momentum will persist.

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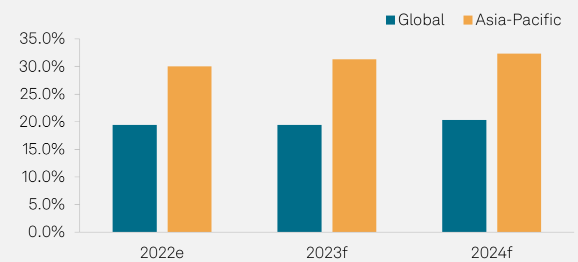
FFO/Debt (Median, adjusted)



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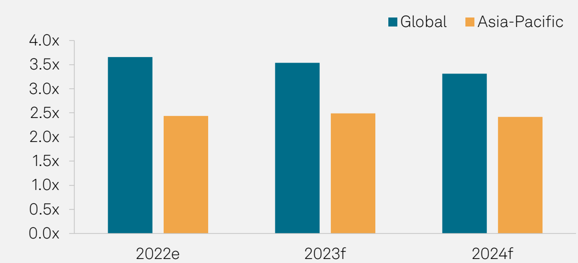

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Downside risks...

Global recession fears could hurt consumer sentiment. Consumers' spending could dip amid slow upgrades to higher-priced services and newer devices. The ability of telcos to hike prices to counter inflation-driven margin pressure could also weaken.

Rising competition in some markets. Markets with new entrants, such as in the Philippines (Dito Telecommunity Corp.) could face more intense competition than in the past.

Heavy, upfront investments could increase leverage pressure. Telcos must make upfront 5G network and spectrum investments, while meaningful monetization from industrial-use cases remains distant. Sporadic spectrum auctions could lead to balance sheet stress and deviations from our base case. In addition, telcos are raising investments in new growth engines to boost long-term growth. Such investments, if debt-funded, can erode rating headroom. The rising interest rate environment adds a layer of balance sheet burden, as investments are now more expensive to fund.

...and what they mean for the sector

Telcos' earnings growth could slip temporarily. Consumers delaying discretionary upgrades, or even trading down, will dampen earnings. Telcos with a high proportion of prepaid subscribers will be hit the hardest. But it should not inflict significant or permanent harm to our rated telcos due to the longer-term trend of rising data demand.

Leverage balancing act remains key. We expect telcos to continue reevaluating infrastructure asset portfolios, non-core assets, and business structures. This is to create balance sheet capacity for continued investments into connectivity, as well as investments further away from the traditional connectivity business to boost longer-term growth.

Transportation Cyclical

Uneven recovery amid macroeconomic headwinds

What we expect over the next 12 months

- Earnings recovery will gain further momentum, particularly among aviation and tanker shipping sectors, buoyed by China's reopening and low order books.
- Still, a slowing global economy, elevated costs, and ongoing geopolitical tensions remain a threat to the pace of recovery.
- We expect the decarbonization agenda to regain importance as airline and shipping operators gradually transition toward cleaner-energy and more fuel-efficient models, gearing toward the net-zero target.

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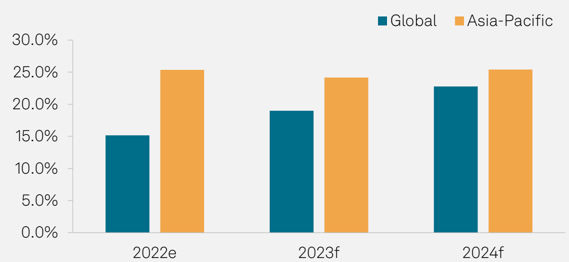
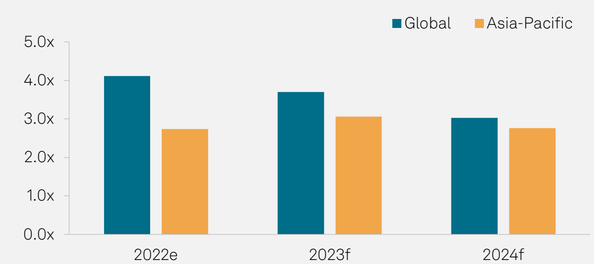
FFO/Debt (Median, adjusted)



Debt/EBITDA (Median, adjusted)



Note: 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. e--Estimated. f--Forecast. Source: S&P Global Ratings.

Downside risks...

Economic slowdown. A global economic downturn could lower the pace of recovery on the back of weakening consumer demand and softening prices. Container shipping lines and airlines with large exposure to air cargo could face further freight rate corrections amid subdued global trade and capacity oversupply.

Elevated interest rates and costs. Rising rates will increase funding costs, which could be substantial for companies with high leverage and refinancing needs. While oil prices should ease from 2022 peaks, it remains high for a recession. That, along with labor inflation could pose structural risks to transportation operators' earnings recovery.

Supply side constraints, despite some easing. Delays in new aircraft deliveries, backlogs in aircraft maintenance, and staffing issues continue to weigh on aviation since the factors limit capacity restoration.

...and what they mean for the sector

Recovery is uneven across sub-sectors and faces multiple headwinds. Pent-up demand for travel and China's border reopening should continue to drive demand for passenger-focused companies, at least in the next few quarters. Yet the profitability of freight transportation could face higher downside risk from a slowing economy given high fuel and labor costs. Refinancing and liquidity risks could increase for lower-rated transport companies, particularly for those reliant on foreign debts and domestic revenues.

A refocus toward green agenda could mean higher capital expenditure (capex). Improving industry prospects could encourage freight operators to invest in more fuel-efficient fleets, following reduction in capex during the pandemic. This could limit meaningful deleveraging over the next few years.

Transportation Infrastructure

Support from improving demand, offset by rising interest rates

What we expect over the next 12 months

- Increasing interest rates (except China) and the economic slowdown may pose challenges to the sector just as most economies emerge from the pandemic.
- Domestic travel has picked up sharply for Asia-Pacific airports, and international traffic is recovering faster than we expected, following an easing of travel restrictions. China is seeing a robust rebound in traffic after it removed mobility curbs.
- Among the entities we rate, a net outlook bias of negative 6% (as of Feb. 28, 2023) reflects pressure on passenger rail companies.

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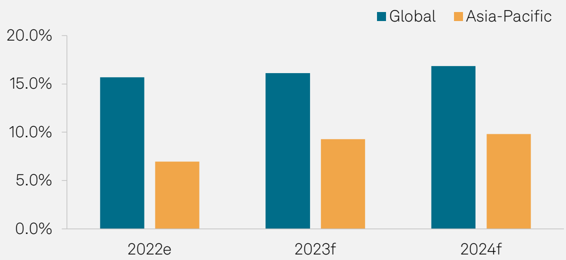
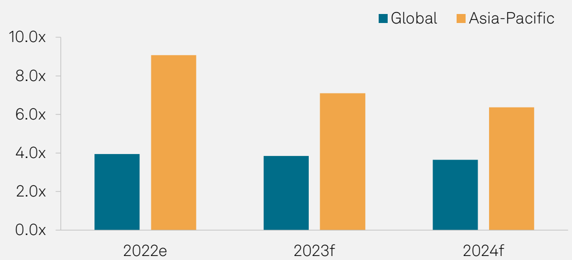
FFO/Debt (Median, adjusted)



Debt/EBITDA (Median, adjusted)



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Downside risks...

Inflation and supply chain risks rising. Increasing cost of living could weigh on travel and demand for goods, while high energy costs and supply chain disruptions also pose risks.

Higher interest rates could create some financial pressure. This could be acute, particularly for issuers more reliant on dollar funding, and those with large refinancing or capex needs.

...and what they mean for the sector

Potential margin pressures. Higher energy prices fueled by the Russia-Ukraine conflict, potential wage inflation, and supply-chain risks could squeeze margins.

Financial metrics could weaken for some issuers. Rising interest rates in most countries due to high inflation could put pressure on the financial metrics of leveraged infrastructure players. Meanwhile, China has lowered rates, and this could benefit some infrastructure players.

Domestic air traffic should recover, but international traffic 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 we forecast domestic traffic in India will recover fully by March 2023. By mid-2023, China domestic travel should recover to around 70% of 2019 levels, while international travel will recover to around 50% by mid-2023. Reopened borders in China and Hong Kong will support a fast recovery. Other transport infrastructure sectors will grow in line with the economy.

Utilities

Fuel cost and ESG risks for coal; leverage and interest rate risks for renewables

What we expect over the next 12 months

- Most countries in the region will continue to diversify into renewables, which will keep capex high.
- Investment in grid infrastructure and energy storage to support renewables is drawing attention from market operators, raising questions about cost management and timing.
- Negative rating bias due to high leverage in the sector and fuel cost pressures, as well as a lag in recovering costs in some markets. Outlook is stable for Chinese issuers, based on profitability recovery amid deepening market-based reform.

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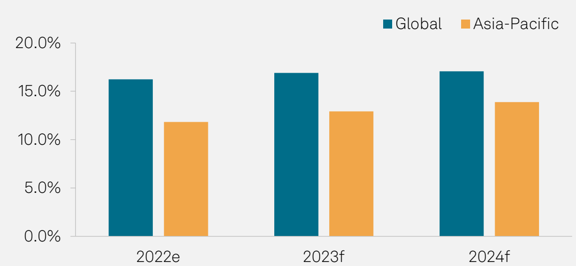
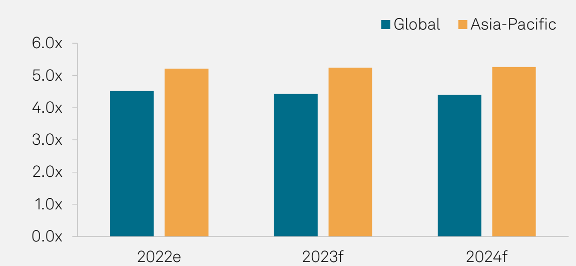
FFO/Debt (Median, adjusted)



Debt/EBITDA (Median, adjusted)



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Downside risks...

Inflation and high interest rates to weigh. Fuel costs are passed through in most markets; but cost pass-through ability may not be even across all entities. Inflationary risk will be a key factor for new projects. Rising rates in most markets could alter funding options and costs for most entities, except those in China.

High pace of new investments and funding. We view excessive debt funding of new developments, adverse regulatory reforms or interventions, and grid constraints as risks. Capex will likely be mainly on renewable projects, integrated hybrid projects, grid and energy storage, or coal majors buying renewable assets.

Supply chain issues. These remain a risk to the cost and time to completion for new projects, depending on the project's stage. Companies may still have to factor this risk in budgeting and capex delivery processes as it may take a few months for supply chains to normalize. Chinese issuers benefit from resilient supply chains.

...and what they mean for the sector

Higher working capital due to timing mismatch of recovering higher costs and electricity price volatility. In China, with stabilizing fuel costs and a growing mix of renewable power, profitability will recover faster.

Liquidity risk: Restrained access to funding sources could increase interest costs and lead to capex reviews. Most Chinese players benefit from government support.

Lack of offtake contracts that support capex progress can hit balance sheets. Chinese issuers are mostly making heavy investments in renewable energy.

Appendix 1
Related research

- Credit Conditions Asia-Pacific Q2 2023: Still Steady, Banking Turmoil Risk Is Moderate Here, March 28, 2023
- Economic Outlook Asia-Pacific Q2 2023: China Rebound Supports Growth, March 27, 2023
- Credit Conditions Asia-Pacific Special Update: Why Asia-Pacific Banks Are Shielded From Current Turmoil, March 22, 2023
- Credit FAQ: What The "Two Sessions" Say About Chinese Government Finances, March 20, 2023
- SVB Default And Asia-Pacific Banks: Secondary Effects Are The X-Factor, March 16, 2023
- Economic Research: The Case For Cautious Optimism On China's Rebalancing And Openness, March 13, 2023
- Sovereign Debt 2023: Asia-Pacific Central Government Borrowing To Fall Below US$4 Trillion, March 9, 2023
- China's Local Governments Are Shedding Their Ties To Struggling SOEs, March 2, 2023
- Corporate Top Trends Update: Asia-Pacific Credit Outlook 2023: Sand In The Gearbox, Feb. 21, 2023

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