S&P Global Ratings

The Ratings View

June 5, 2024

This report does not constitute a rating action.

Key Takeaways

- Decarbonizing metal production is hugely important but technically challenging.
- U.S. homebuilders are benefiting from strong demand and weak housing supply.
- Mexico's new government faces familiar economic challenges.

Decarbonizing metals is a pressing issue with uncertain fixes. The metal sector is one of biggest carbon emitters, prompting producers to increasingly set decarbonization targets. Nonetheless, relatively high-emission processes dominate steel and aluminum production. Metal companies could achieve near-term decarbonization goals with increased use of scrap and direct reduced iron, efficiency improvements, and renewable energy adoption. Longer-term decarbonization prospects are less certain given that large scale implementation of new technologies will be difficult. Currently strong credit metrics and likely supportive markets should help metals companies we rate mitigate the high cost of decarbonization. However, if higher costs coincide with a trough in the metals-price cycle then the pressure on the credit quality of some companies could materially increase.

Decarbonizing Metals Part One: A Pressing Issue With Uncertain Fixes
Decarbonizing Metals Part Two: Financial Strength Mitigates Rising Credit Risk

Low housing supply and resilient demand will support U.S. homebuilding sector growth and credit quality. The housing market remains significantly undersupplied and the existing supply in the resale market is still limited. Existing-home sales have dropped as homeowners are locked in to low-rate, long-term mortgages while housing starts continue to trend below historical levels. We expect mortgage rates to stay elevated, with the 30-year fixed mortgage rate hovering around 7% in 2024. In our view, homebuilders are well-positioned for growth in the next two years given inventory scarcity. Robust balance sheets and better-than-expected operating performance have pushed more homebuilders into investment grade, and early 2024 provided an opportunistic window for companies to refinance debt, albeit at noticeably higher rates.

U.S. Homebuilders Are Building On Improving Credit Quality

Mexico's new administration faces familiar challenges. Claudia Sheinbaum will take office as president of Mexico on Oct. 1. We don't believe the new administration is likely to materially change the country's fiscal, monetary, or trade policies. Like previous administrations, the country's new leadership will face the challenge of maintaining macroeconomic stability while meeting public expectations of better living standards and more public services. Although Mexico's economy grew 3.1% last year, it remains an underperformer compared to other emerging markets. Nearshoring provides difficulties and opportunities for the new administration. Greater success in attracting domestic and foreign direct investment could set the stage for higher economic growth, which could improve the country's economic resilience.

Mexico's New Administration Faces Old Challenges

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Asset Class Highlights

Corporates

Notable publications include:

- Sustainability Insights: Decarbonizing Metals Part One: A Pressing Issue With Uncertain Fixes
- Sustainability Insights: Decarbonizing Metals Part Two: Financial Strength Mitigates Rising Credit Risk
- CRE Debtholders Are Confronting Increasing Refinancing Risk And Charge-Offs In 2024; Outcomes Will Vary
- U.S. Homebuilders Are Building On Improving Credit Quality
- Cable Industry Intertwining With Wireless
- The Permian Basin's Dominance Continues--But For How Long
- China Commodities Watch: Trade Tensions Add To The Pain
- German Residential REITs Remain Supported By Funding Access And Solid Rent Fundamentals
- Credit FAQ: Thames Water: Possible Rating Trajectories
- Corporate, Financial Institution, And Government Ratings That Exceed The Sovereign Rating
- China ahead in delivering affordable electric mobility

Financial Institutions

Over the past week, we took several rating actions:

- Research Update: Toronto-Dominion Bank Outlook Revised To Negative On Risk Management And Controls Weaknesses; 'AA-' Rating Affirmed
- Research Update: Pershing Square Holdings Ltd. Outlook Revised To Positive On Expected Deleveraging; 'BBB+' Ratings Affirmed
- Research Update: Coinbase Global Inc. Outlook Revised To Stable From Negative On Improving Business Performance; 'BB-' Ratings Affirmed
- Outlook On Six Indian Banks Revised To Positive On Sovereign Action; Ratings Affirmed; ICICI, Axis Bank SACP Revised Up
- Research Update: Norwegian Eksportfinans ASA Outlook Revised To Positive On Receding Wind-Down Risks; 'A-/A-2' Ratings Affirmed
- Research Update: Outlook On UBS Holdings Revised To Stable On Decreasing Tail Risks; Ratings Affirmed
- Research Update: La Poste, La Banque Postale, And CNP Assurances Downgraded After Similar Action On France; Outlook Revised To Stable

We published several commentaries including:

- U.S. GSIBs Q1 2024 Update: Strong Performance Underscores Resiliency
- EMEA Financial Institutions Monitor 2Q2024: Robust Profitability, Resilient Performance

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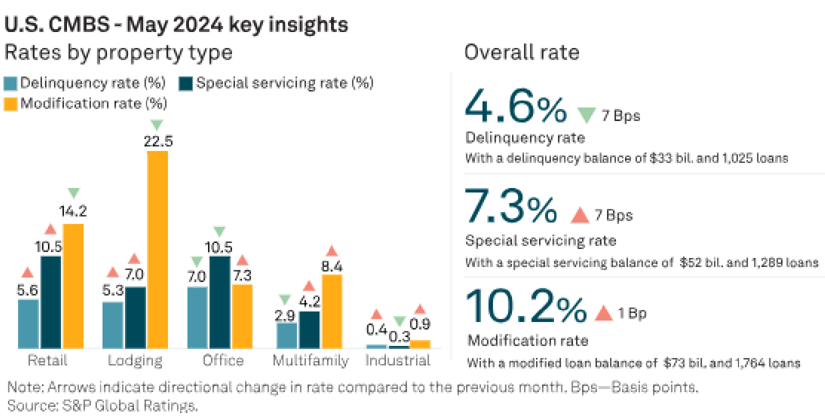
Sovereign

- France Long-Term Rating Lowered To 'AA-' From 'AA' On Deterioration Of Budgetary Position; Outlook Stable
- Estonia Ratings Lowered To 'A+/A-1' From 'AA-/A-1+' On Economic, Fiscal, And Security Risks; Outlook Stable
- Lithuania Ratings Lowered To 'A' From 'A+' On Economic, Fiscal, Security Risks; Outlook Stable
- Latvia Long-Term Ratings Lowered To 'A' On Economic, Fiscal, And Security Risks; Outlook Stable
- India Outlook Revised To Positive On Robust Growth And Rising Quality Of Government Spend; 'BBB-/A-3' Ratings Affirmed

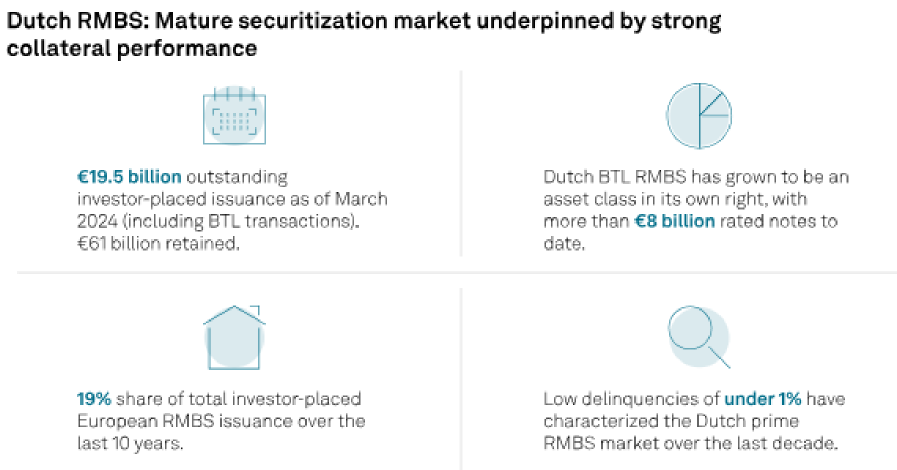
Structured Finance

- **Basel 3.1 and Bank Securitizations:** Here are a few “Key Takeaways” from a recent article:
    - The upcoming implementation of Basel 3.1 by regulators around the world could affect banks' use of securitization for both capital relief and funding.
    - Higher capital charges could incentivize more use of securitization to manage risk-weighted assets through so-called significant risk transfer (SRT) transactions.
    - However, such transactions will likely become more challenging and costly than under current rules, given that Basel 3.1 also changes capital charges on the resulting securitization exposures.
    - Relative shifts in the regulatory treatment of assets pre- and post-securitization could also affect transactions issued for funding purposes, even if capital charges are not banks' primary consideration.
    - All these effects will strongly depend on the underlying asset type and the final implementation details, some of which remain uncertain.
    - See “ABS Frontiers: Looming Basel 3.1 Rules Could Incentivize More Bank Securitization", published June 3, 2024.
- **U.S. CMBS:**



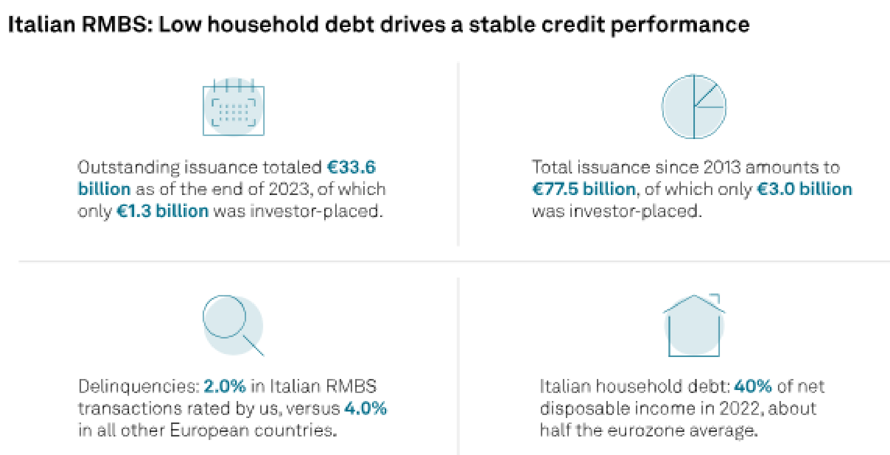
See "SF Credit Brief: U.S. CMBS Overall Delinquency Rate Drops Seven Bps To 4.6% In May 2024; Updates Provided On Modification Rate By Property Type", published June 3, 2024.

- **Dutch RMBS**:



See "A Primer On The Dutch RMBS Market", published June 3, 2024.

- **Italian RMBS:**



RMBS--Residential mortgage-backed securities. Source: S&P Global Ratings.

See "A Primer On Italy's RMBS Market" published June 3, 2024.

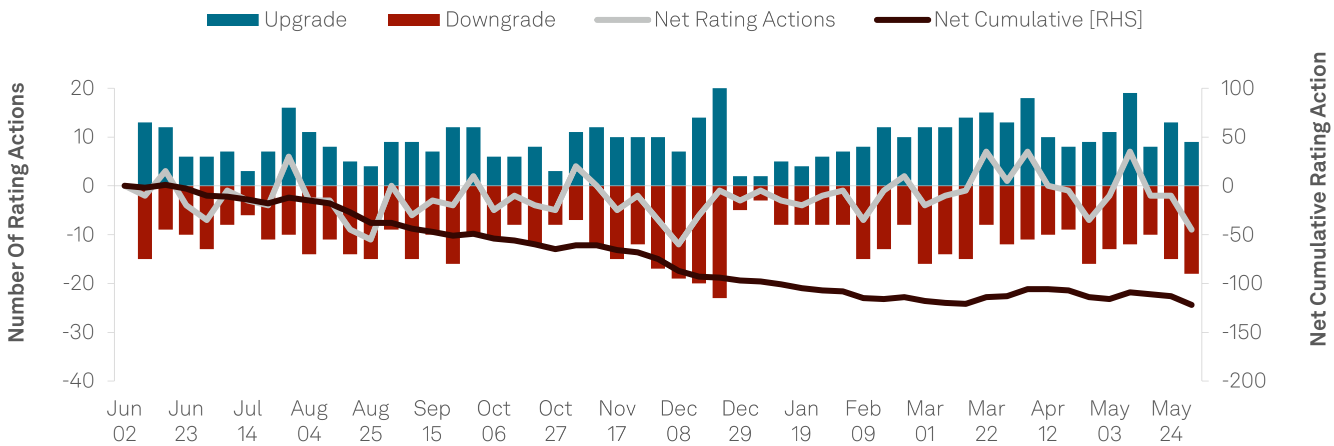
- **Australian RMBS:** Australian RMBS mortgage arrears rose during the first quarter of 2024. This is likely to continue amid lingering high interest rates and rising unemployment, according to S&P Global Ratings' recently published "RMBS Performance Watch: Australia". Most borrowers have been resilient on the debt-serviceability front, though some are handling this by significantly reprioritizing their spending and drawing on savings. But not all households face the same levels of pressure in servicing their debts and this has helped to keep overall arrears low to date. While improving wage growth is helping with debt serviceability, increases in mortgage repayments are still outstripping income increases for many borrowers. This is occurring alongside significant increases in key household expenditures like insurance premiums and energy costs.

  So far, low unemployment and, for some borrowers, savings buffers have kept arrears low. Lingering higher interest rates will see more borrowers enter arrears, though, as unemployment rises. In the months ahead, this will result in a continued rise in arrears, which are a lagging indicator and one of the last places where financial stress manifests. Provided unemployment remains low overall, however, we expect most borrowers to avoid going into arrears, minimizing any dislocation in mortgage markets and systemic risk.

- **China Auto ABS and RMBS:** S&P Global Ratings published on May 30, 2024 its "China Securitization: ABS And RMBS Tracker April 2024". Highlights from the chartbook, which tracks the performance of China asset-backed securities (ABS) and residential mortgage-backed securities (RMBS) that we rate, include the following:
    - A decline in the Shanghai Interbank Offered Rate has led to lower coupon rates on the most senior tranches of auto ABS. Some repeated issuances were priced below 2% in May 2024.
    - Severe delinquency ratios increased for auto loan ABS that we rate, mainly due to rising arrears of deals with distinct pool attributes.
    - The rapid paydown of underlying pools in RMBS transactions that we rate has led to a rise in cumulative delinquency rates. That said, we expect the strong credit enhancement available to maintain the stability of our RMBS ratings.
    - Consumer loan ABS had higher and more volatile delinquency rates compared with auto loan ABS. The utilization of excess spreads and high credit enhancement available provided rating support for rated notes in the Anyihua transaction that we reviewed in the chartbook.
- **Australian Auto ABS:** Australian auto asset-backed securities (ABS) arrears fell in April. That's according to S&P Global Ratings' recently published "Auto ABS Arrears Statistics: Australia". The Standard & Poor's Performance Index (SPIN) for Australian auto ABS and mixed auto pool arrears decreased to 1.17% in April from 1.40% the previous month. The drop was partially driven by a 14% increase in the underlying receivables balance. Our economic forecast is for the Australian cash rate to remain at its current level for the remainder of the year and inflation-driven financial pressures to persist. Therefore, we expect arrears will remain higher than last year. However, the stage 3 personal income tax cuts that take effect from July 1 may provide some relief in the second half of this year.
- **Australian ABS:** Arrears levels increased for most Australian and New Zealand asset-backed securities (ABS) transactions during the first quarter (Q1) of 2024. That's according to the recent edition of S&P Global Ratings' "ABS Performance Watch: Australia And New Zealand". Although arrears increased, cumulative losses experienced to date remain relatively low and, by and large, there has been a buildup of credit support for rated notes. We believe this would provide a buffer for transactions should there be any deterioration in performance.
- **U.S. Credit Card ABS:** We published the "U.S. Credit Card Quality Index: Monthly Performance--April 2024" on June 3, 2024. The CCQI is a monthly performance index that aggregates performance information of securitized credit card receivables in key risk areas.

Chart 1

Global Rating Actions (Rolling 52-Weeks)



Source: S&P Global Ratings. Net rating actions means downgrades minus upgrades. Net cumulative means total net rating actions. Data as of May 31, 2024. Global rating actions include actions on both financial and non-financial corporates and sovereign issuers.

Table 1

Recent Rating Actions

Date	Action	Issuer	Industry	Country	To	From	Debt vol (mil. $)
31-May	Downgrade	Republic of France	Sovereign	France	AA-	AA	24,426
31-May	Downgrade	Republic of Latvia	Sovereign	Latvia	A	A+	16,160
31-May	Downgrade	Republic of Lithuania	Sovereign	Lithuania	A	A+	14,659
29-May	Upgrade	George Weston Ltd.	Retail/restaurants	Canada	BBB+	BBB	9,105
31-May	Upgrade	Fairfax Financial Holdings Ltd.	Insurance	Canada	BBB+	BBB	8,879
31-May	Downgrade	CPI Property Group S.A.	Homebuilders/real estate co.	Luxembourg	BB+	BBB-	6,299
30-May	Downgrade	AMC Entertainment Holdings Inc.	Media & entertainment	U.S.	SD	CCC+	4,784
31-May	Downgrade	Republic of Estonia	Sovereign	Estonia	A+	AA-	4,326
30-May	Upgrade	Madison IAQ LLC (Madison Industries Holdings LLC)	Forest products & building materials	U.S.	B	B-	4,275
31-May	Upgrade	Ascent Resources Utica Holdings LLC	Oil & gas	U.S.	BB-	B+	3,661

Source: S&P Global Ratings Credit Research & Insights. Data as of May 31, 2024. U.S. means United States, U.K. means United Kingdom and U.A.E. means United Arab Emirates. NBFI - NonBank Financial Institutions (ex. Insurance)

For further credit market insights, please see our **This Week In Credit** newsletter**.**