Global Credit Conditions Q4 2024

Policy Rates Easing, Conflicts Simmering

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This report does not constitute a rating action

Editor's Note: S&P Global Ratings' Credit Conditions Committees meet quarterly to review macroeconomic conditions in each of four regions: Asia-Pacific, Emerging Markets, Europe, and North America, which cascade into our global coverage. Discussions center on identifying credit risks and their potential rating impact in various asset classes, as well as borrowing and lending trends for businesses and consumers. This commentary reflects views discussed in the Global Committee on September 23, 2024.

Contents

Key Themes

Credit resilience amid stormy seas: Despite geopolitical risks increasing and rates remaining high through most of this year, refinancing activity has been strong across most ratings and sectors. Upgrades continue to outpace downgrades, and defaults have started to moderate in recent months. We expect the default rate to fall, but at a slower pace than it rose due to residual strain for the lowest-rated borrowers.

Some grow, some slow: Most economies are set to grow this year, led by strong momentum in the U.S. due to resilient consumer spending and increased productivity. This is partially offset by only a gradual growth rebound in Europe and a sequential slowdown in China, which has been held back by its still flagging property sector. We expect global growth to slow modestly in 2025 as the U.S. moderates, Europe's pace picks up, and China's slows further.

Vulnerability amid optimism: Market turmoil in early August proved short-lived, but has revealed market vulnerability to negative headlines, quickly unwound carry-trade positions, and currently rich valuations. Optimism is rooted in assumptions for sustained interest rate cuts ahead, but yields are likely to stabilize at higher long-term levels than pre-pandemic-era lows. The current geopolitical landscape and potential trade barriers ahead remain risks.

Global credit conditions: key highlights

Diverging GDP trends in 2025

Change from 2024 ▲ Positive ▼ Negative

▼ Global: **3.1%**
▼ U.S.: **1.8%**
▲ eurozone: **1.3%**
▼ China: **4.3%**

Expected path of Fed Funds Rate

S&P Global Ratings Economists' expectations for the effective Federal Funds Rate.

Q3 2024: **5.21%**
Q4 2024: **4.63%**
Q4 2025: **3.13%**

Undeterred issuance amid geopolitical and trade risks*

2022: **$3.4 tril.**
2023: **$3.6 tril.**
2024: **$4.3 tril.**

Falling negative outlook bias

As of Sept. 16, 2024

Investment-grade: **9.8%**
Speculative-grade: **17.8%**
'B-' & lower: **32.7%**

'CCC+' and lower

All corporates (% of all spec-grade)
As of Aug. 31, 2024

Global: 9.5%

U.S.: **11.8%**
Europe: **8.9%**
RoW: **5.8%**

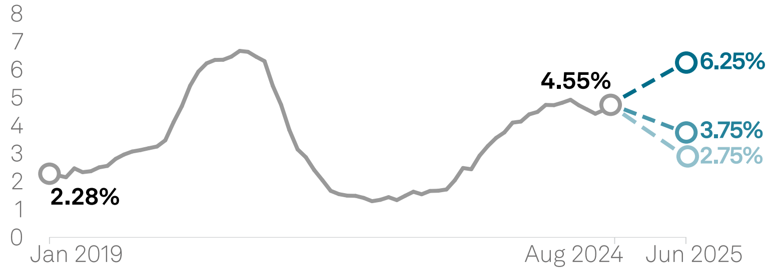
Corporate debt

As of July 1, 2024

$1.27 tril.
rated 'B-' or lower and
70%
due through 2028

Trailing-12-month speculative-grade default rate and June 2025 forecast

U.S.



Europe

*Year-to-date bond issuance among nonfinancial corporates and financial services, through Sep. 12, 2024. ROW--Rest of world. YTD—Year-to-date.
Source: Worldbank, S&P Global Ratings. Most recent published default forecasts: "Resilient Growth, Resilient Yields, And Resilient Defaults To Bring The U.S. Speculative-Grade Corporate Default Rate To 4.5% By March 2025," May 16, 2024, and "The European Speculative-Grade Default Rate Should Level Out At 3.75% By March 2025," May 22, 2024.

Global Top Risks: Rate Cuts Begin, But Risks Remain

Geopolitical tensions threaten supply chains, trade, and market sentiment

Risk level:	High	Risk trend:	Worsening

The protracted Russia-Ukraine and Middle Eastern conflicts, along with domestic polarization in certain markets, could escalate and provoke greater unpredictability in governments' responses, force increased spending by already stretched government budgets, disrupt investment flows, and increase financial market volatility. Most of this year's elections have concluded, but policy uncertainties remain in some places. Much will depend on the outcome of the U.S. general election, which is extremely unpredictable at this time, and can have ramifications on various conflicts and trade fronts, which are already material.

The interest rate descent could disappoint

Risk level:	Elevated	Risk trend:	Unchanged

Central banks have started cutting rates, and more are expected. Still, the pace of cuts will vary between jurisdictions, and will be slower than their rise. A key risk is that rates settle at higher terminal rates than financial markets expect. This could lead to durable bouts of market volatility, and keep borrowing costs elevated, especially for weaker borrowers. Higher rates in developed markets would further burden emerging market debt, both directly and through unfavorable exchange rates on nondomestic debt. Divergence in rate trajectories between the U.S. and other major central banks could produce shifts in foreign exchange rates, despite recent improvements, and capital flows.

Growing protectionism threatens global trade

Risk level:	Elevated	Risk trend:	Unchanged

Widening tariffs on Chinese goods, along with further proposals by the Biden administration and similar rhetoric from presidential candidate Donald Trump, will likely strain bilateral trade flows between the world's two largest economies. Europe, a traditionally open trading block, has recently also decided on trade protection measures to counter state subsidies to strategic industries in China, including electric vehicles (EVs). While we do not anticipate any major trade hurdles being implemented in other emerging markets, this may further prompt some businesses to review supply chains and diversify from China. This could have a global impact, producing yet unknown winners and losers, with increased supply chain complexities and possible inflationary pressure in certain markets. This could upend prior monetary easing policies by central banks.

A sharper global economic slowdown would lead to greater credit stress

Risk level:	Elevated	Risk trend:	Unchanged

Resilient economies have reduced recession odds in recent months, but we expect many countries to see slower growth in 2024 and 2025. China, in particular, is facing the risk of structural deflation. Still elevated interest rates and the lingering impact of permanently higher prices pose headwinds globally. Savings buffers have been declining, and fiscal headwinds are building, with many countries having taken on increased debt through the pandemic. Labor market resilience will remain a key headwind to any slowdown, but the state of the global consumer is showing some cracks, with increased delinquencies in the U.S. and still low consumer confidence in China.

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.

Moderate	Elevated	High	Very high

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

Improving	Unchanged	Worsening

Source: S&P Global Ratings.

Global Top Risks (Continued)

Global real estate markets are facing multiple challenges

Risk level: Elevated **Risk trend:** Unchanged

High interest rates, falling valuations and cash flow, hybrid work environments, high leverage among some countries' homebuilders, and the potential for continued selective market access and high financing costs have combined to present headwinds for both the commercial and residential real estate sectors globally. These risks remain greatest in the U.S. office sector. Meanwhile, China's sticky property crisis has yet to find a bottom despite government stimulus. Spillover effects from vulnerable real estate holdings could further affect many banking systems via falling asset values or increased write-downs. These pressures could also spill over to broader economies, through negative effects on consumer confidence, spending, employment, and tax revenues.

Structural risks

Cyber attacks and the potential for rapid technological change threaten global business and government infrastructure

Risk level: Elevated **Risk trend:** Worsening

Amid increasing technological dependency and global interconnectedness, cyber attacks pose a potential systemic threat and significant single-entity event risk. The Russia-Ukraine conflict is raising the prospect of major attacks. Criminal and state-sponsored cyber attacks are likely to increase, and with hackers becoming more sophisticated, new targets and methods are emerging. A key to resilience is a robust cyber security system, from internal governance to IT software, all requiring additional costs. Entities lacking well-tested playbooks (such as active detection and swift remediation) are the most vulnerable. Meanwhile, increased digitization and the introduction of AI by public and private organizations will foster broader operational disruptions, and potentially increase market volatility for short periods or even pose greater economic adjustments.

Climate risks and energy transition affect business operations

Risk level: Elevated **Risk trend:** Worsening

Larger and more frequent natural disasters increase the physical risks that public and private entities face, and threaten to disrupt supply chains, such as for agriculture and food. The El Nino phenomenon, although expected to fade, has disrupted agricultural commodities this year, particularly among emerging markets. At the same time, the global drive toward a "net-zero" economy heightens transition risks (such as legal, technology, and market sentiment) and will likely require significant investments. That said, geopolitical fragmentation, with increased focus on energy security and domestic industrial policies, raises the risk of abrupt, and potentially contradictory, changes in climate policies. In the U.S., we see transition risks as less acute currently than in Europe, since U.S. legislative policies focus more on subsidies and incentives rather than carbon taxes and trading.

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.

Moderate	Elevated	High	Very high

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

Improving	Unchanged	Worsening

Source: S&P Global Ratings.

Economic Conditions

Still Resilient, With Gradual Rate Cuts Ahead

Data as of September 2024. Policy rates as of Dec. 2023, and forecasts are for year-end values. *Simple average. †Median for EM 18 countries. §Refi rate. ‡Weighted average based on purchasing power parity. f—Forecast. Source: S&P Global Ratings.

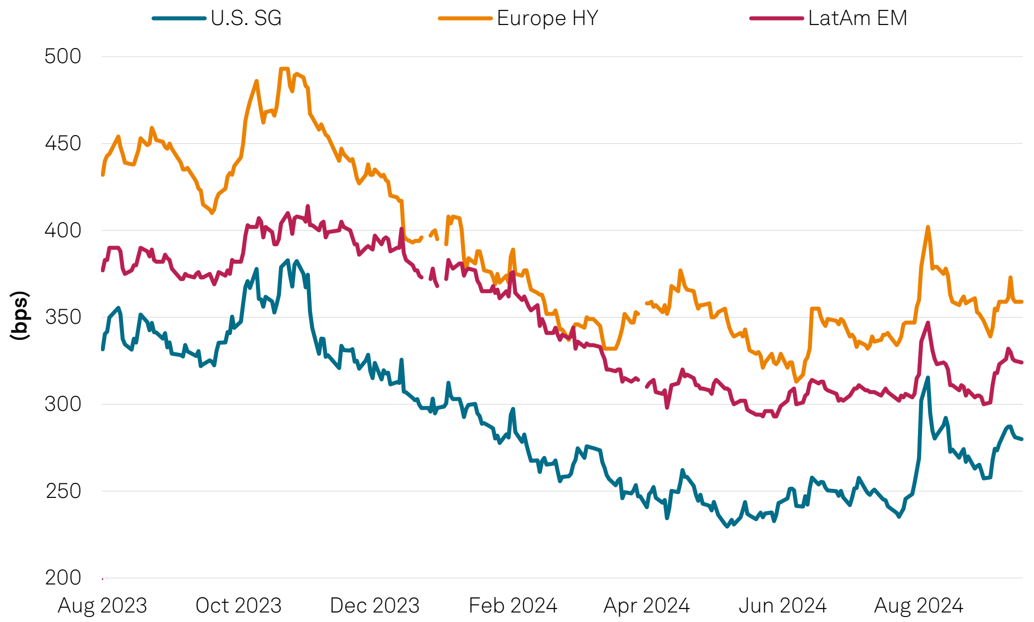
- The global policy rate easing cycle is now in full swing following a 50-basis-point cut by the U.S. Federal Reserve in mid-September. The rate cut creates space for a swath of central banks to follow suit, particularly in emerging markets.
- Economies remain more resilient than we had expected, but outcomes are diverging across the main regions. The U.S. is slowing, the eurozone is recovering, and China faces property-related headwinds.
- Global GDP growth remains subdued. We are forecasting 3.2% growth in 2024 and 3.1% in 2025. The bright spots are economies with strong domestic demand or exposure to the global tech cycle.
- The risks to our baseline remain on the downside. These include sharply lower labor demand and a spike in bond yields and geopolitical risks. Terminal policy rates (and r*'s) remain key unknowns.
- See "Global Economic Outlook Q4 2024: So Far, So Smooth--Can It Last?," Sept. 26, 2024.

Financing Conditions

Signs Of Vulnerability: Market Rattled By August Headlines, But Calm Prevails

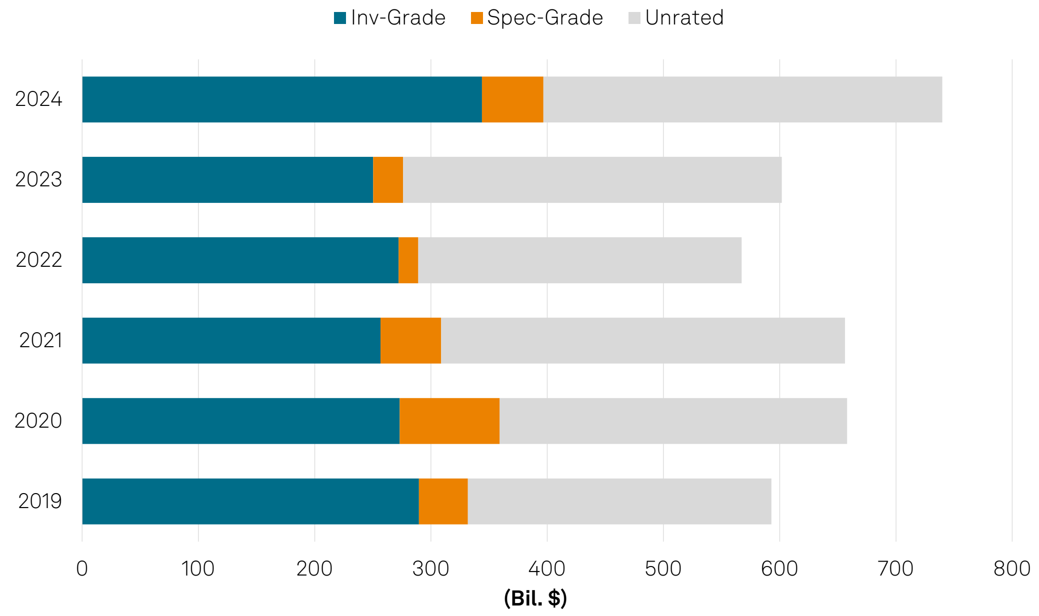
- In early August, market volatility spiked in response to U.S. nonfarm payroll figures. The initial reaction was also exacerbated by the unwinding yen carry-trade--a large change in financial holdings due to the growing divergence between U.S. and Japanese yields.
- This volatility would prove short-lived, with recent issuance testing high points seen over the last six years, across all rating levels.
- Nonetheless, the U.S. speculative-grade bond spread saw some of its fastest relative widening ever--a signal of underlying vulnerability in current markets to negative economic news or interest rate implications.

Corporate spreads widened quickly, and globally



Data through Sep. 13, 2024. HY—High yield. EM—Emerging markets.
Sources: S&P Global Ratings Research & Insights, ICE BofA spreads series, retrieved from FRED.

Recent bond issuance undeterred by market volatility

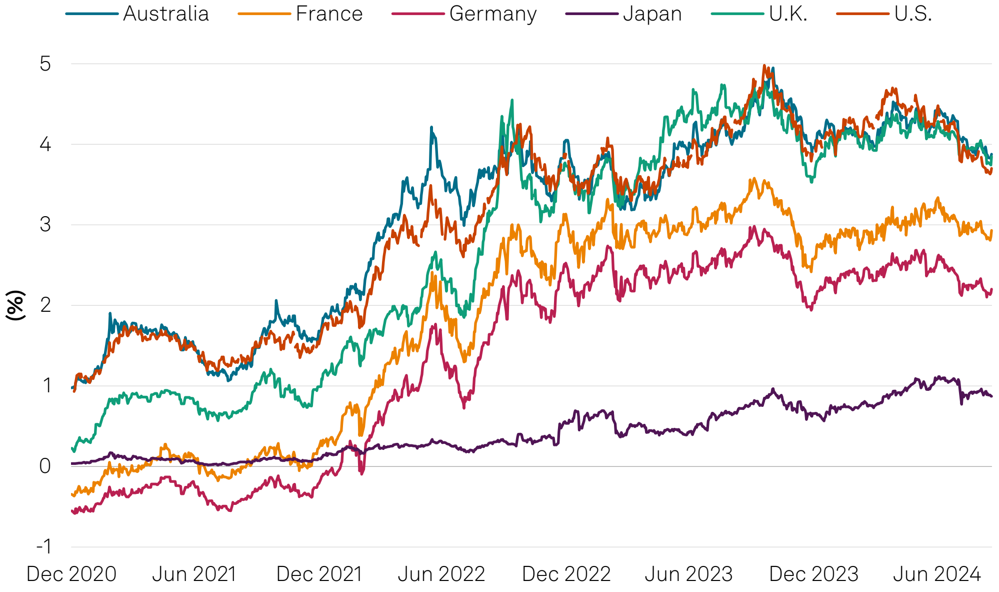


Corporate bond issuance for August through Sep. 12th.
Sources: Refinitiv and S&P Global Ratings Research & Insights.

Yields Start To Moderate, But May Remain Historically Higher

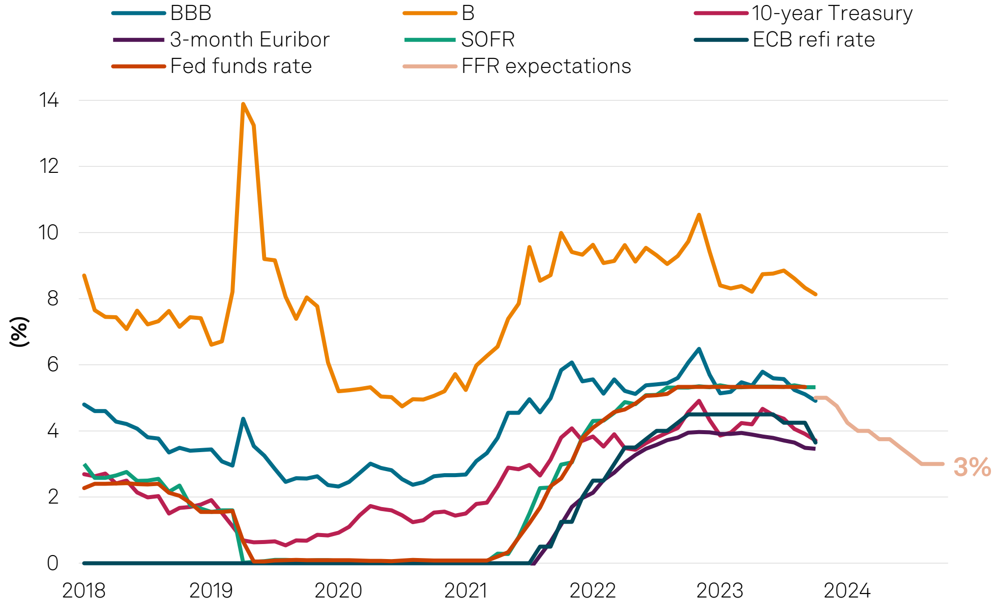
- Sovereign bond yields fell on Aug. 5 and have remained lower since in anticipation of Fed rate cuts.
- Floating-rate benchmarks (SOFR, EURIBOR) tend to move tightly with changes in policy rates, but longer-term bond yields are stickier.
- Even with relief in sight, policy rates will likely remain higher than during the pre-pandemic period as "R*" has arguably increased in recent years, putting a floor on interest rate declines ahead.

Sovereign yields dip in August in anticipation of Fed cuts offering room for others



Data through Sep. 18, 2024.
Sources: S&P Global Market Intelligence and S&P Global Ratings Credit Research & Insights.

Interest rates may remain elevated if terminal rates are higher in the future

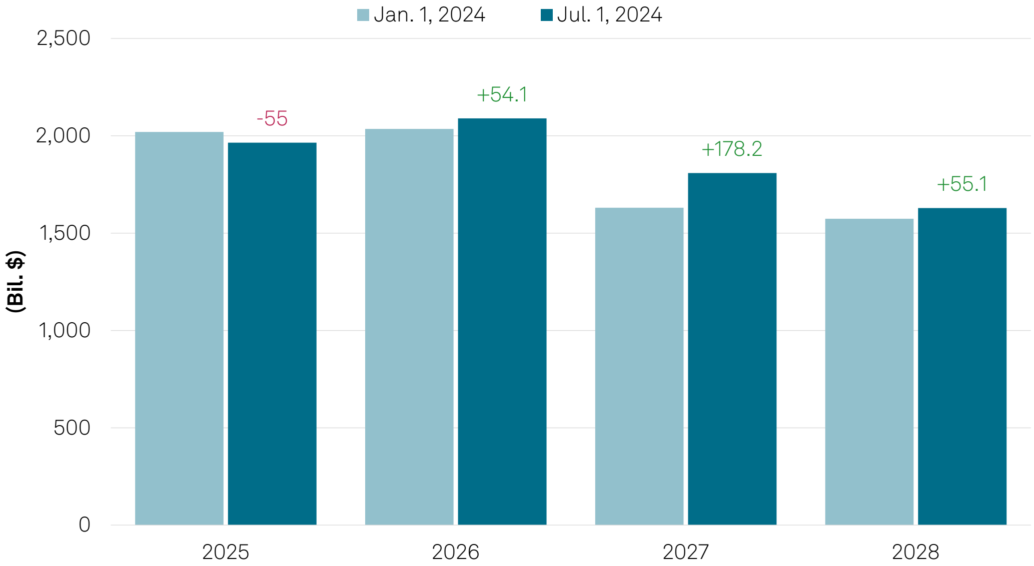


FFR expectations – Federal funds rate expectations, as of Sep. 17, 2024; CME Group. ECB--European Central Bank.
Sources: CME Group, S&P Global Market Intelligence, S&P Global Ratings Research & Insights.

A Year For Refinancing

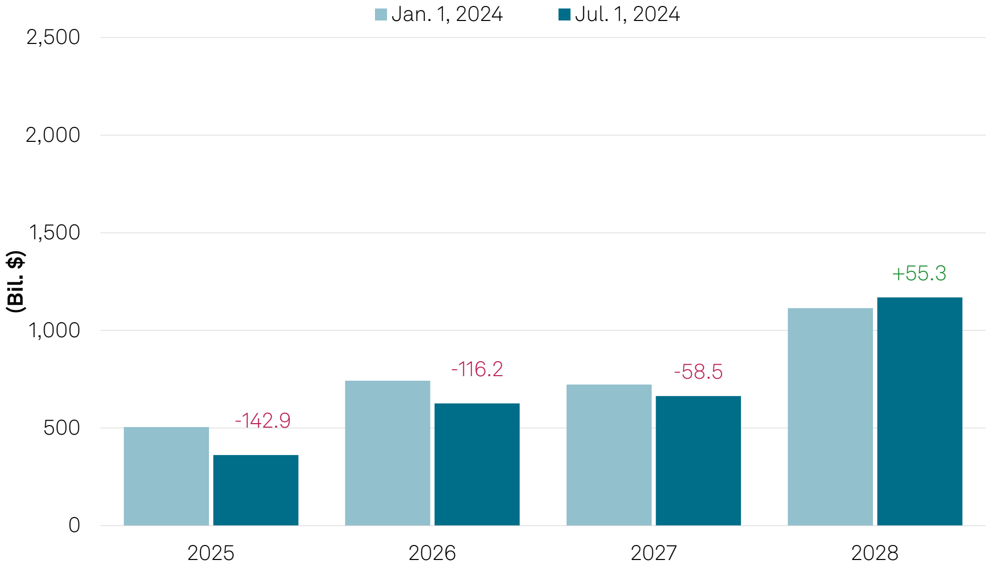
- Roughly 77% of all speculative-grade bond and leveraged loan issuance in the year to date has been for refinancing, or repricing (in the case of loans).
- This has helped ease near-term liquidity pressure on many speculative-grade issuers, giving some wiggle room if further bouts of volatility arise.
- Meanwhile, investment-grade companies have paid down only 2024 maturities to a meaningful extent, likely biding their time to address the next few years' obligations after rate cuts work their way through.

Many inv-grade issuers seem to be biding their time for more cuts ahead
Investment grade



As of Jul. 1, 2024, includes rated outstanding debt from corporates and financial services issuers, globally. Includes bonds, loans, and revolvers. Source: S&P Global Ratings Research & Insights.

While spec-grade issuers aren't taking chances
Speculative grade



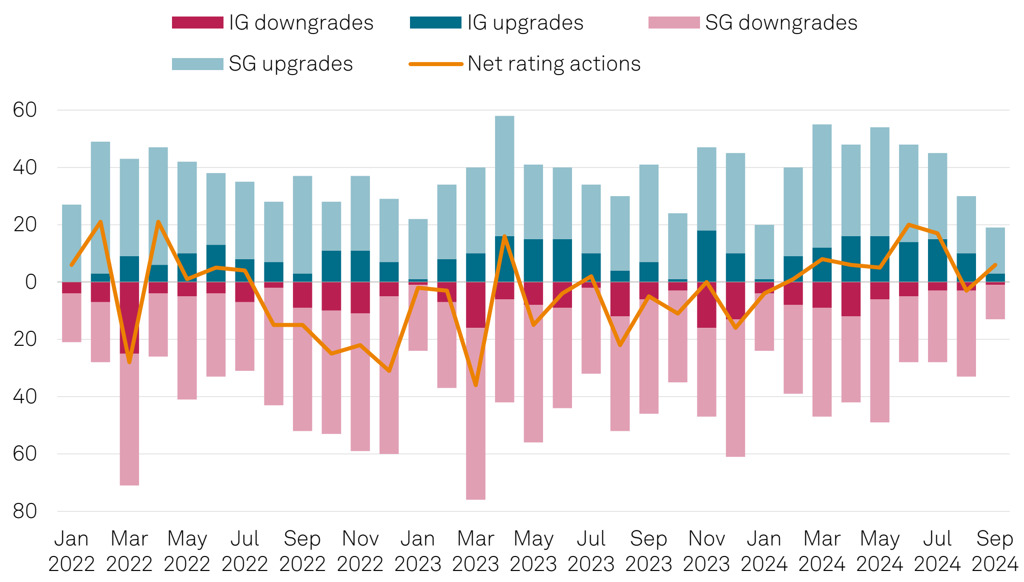
As of Jul. 1, 2024, includes rated outstanding debt from corporates and financial services issuers, globally. Includes bonds, loans, and revolvers. Source: S&P Global Ratings Research & Insights.

Rating Trends And Expectations

Rating Actions Have Been Net Positive In 2024

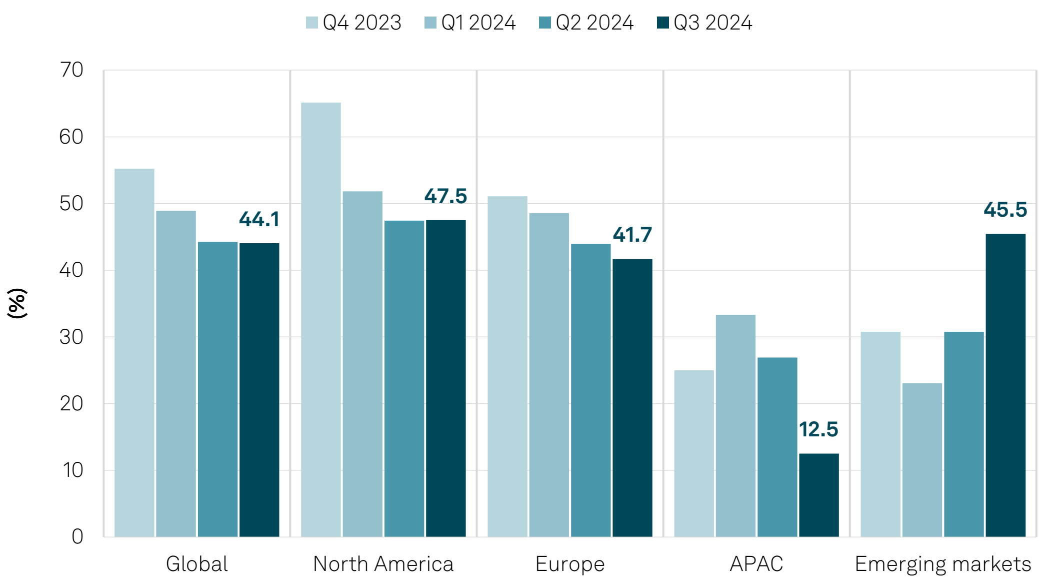
- Improvements in aggregate credit quality continue in 2024, with the year-to-date downgrade ratio among corporates, financial services, and sovereigns reaching 46% through mid-September. Over half of all rating actions have occurred among issuers rated 'B+' through 'CCC+'.
- Through mid-September, third-quarter speculative-grade rating actions have been roughly balanced between upgrades and downgrades (72, and 73, respectively). However, at the lowest rating levels ('B-' and lower), the count of downgrades has been double that of upgrades (40, and 19, respectively).
- For two quarters in a row, all regions have seen more upgrades than downgrades, though North America has been much closer to parity, largely because of its greater proportion of speculative-grade issuers, especially more at the 'B-' level and lower.

Upgrades still dominate, but approaching parity with downgrades



Data as of Sep. 16, 2024. Downgrades exclude defaults. IG--Investment grade. SG--Speculative grade. Source: S&P Global Ratings Credit Research & Insights.

All regions show net upgrades for two quarters in a row

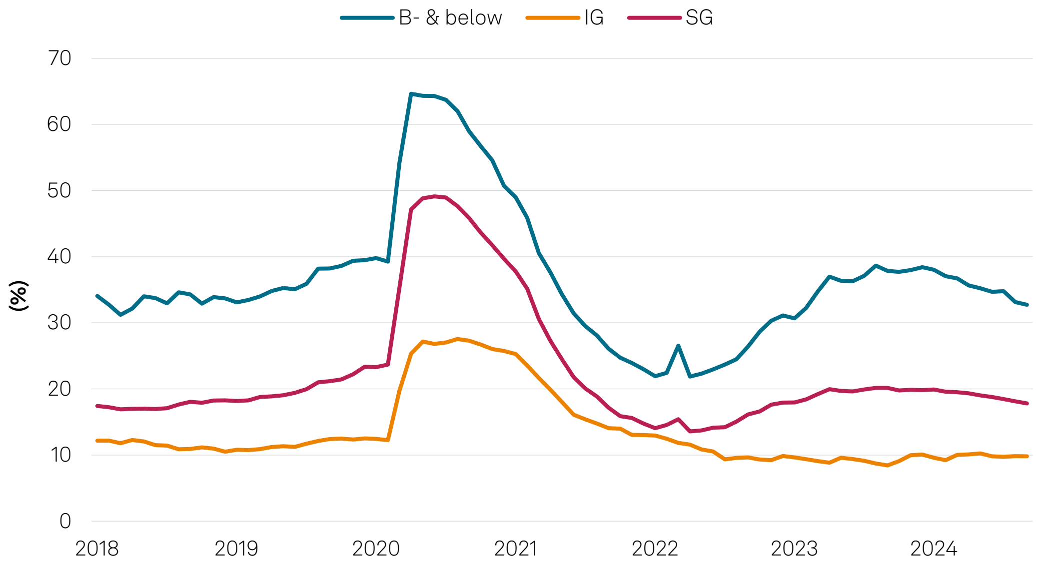


Data as of Sep. 16, 2024. Chart displays downgrade ratios excluding defaults. Downgrade ratios include financials and nonfinancials. Source: S&P Global Ratings Credit Research & Insights.

Downgrade Potential Continues To Slowly Ease

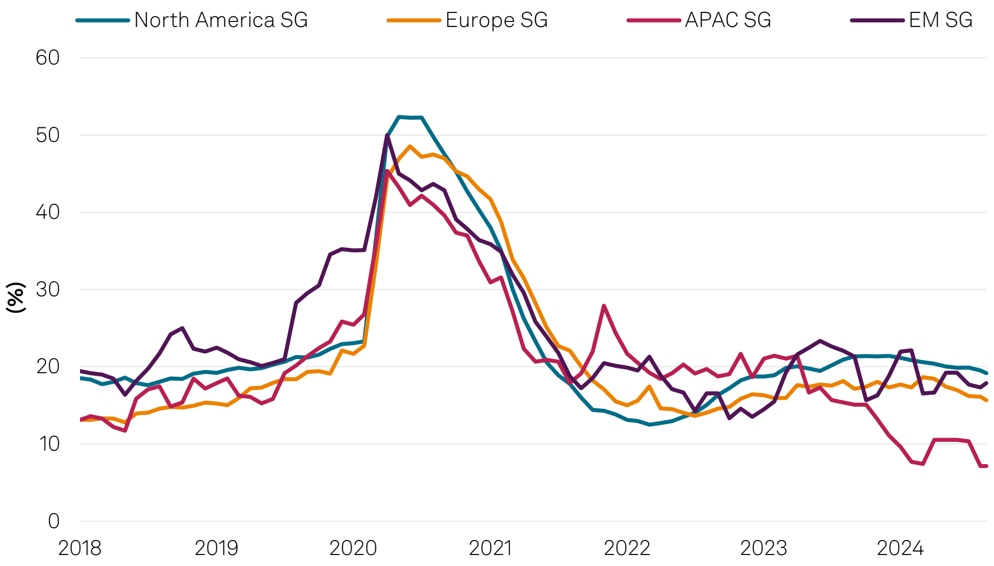
- Downgrade potential for speculative-grade issuers continues to slowly decline, with negative bias (the proportion of issuers with negative outlooks or ratings on CreditWatch negative) falling below 18% for the first time in nearly two years.
- Investment-grade companies remain on solid footing, with a negative bias slightly below 10%. Large buffers after the surge of pandemic-era issuance and more fixed-rate debt secured with very long maturities and low fixed coupons should provide tailwinds for an extended period, allowing time for interest rate cuts to make their way through the financial system.
- Similar to positive rating trends, downgrade potential is falling across all regions this year for speculative-grade issuers.

Falling negative bias points to fewer downgrades ahead



Excludes sovereigns. Data as of Sep. 16 2024. IG--Investment grade. SG--Speculative grade.
Source: S&P Global Research & Insights.

All regions expecting fewer downgrades ahead



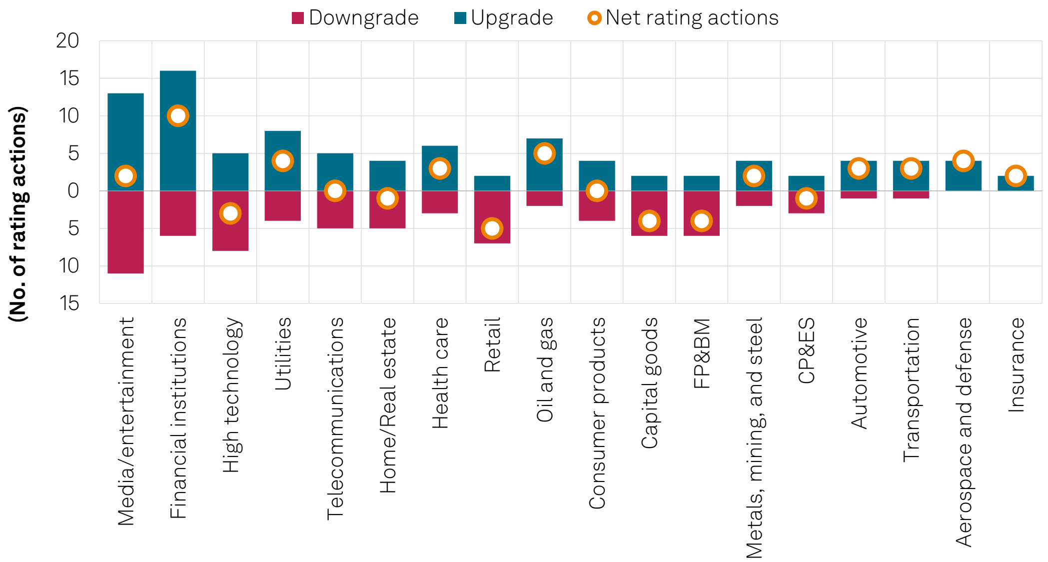
Excludes sovereigns. Data as of Sep. 16, 2024. EM--Emerging markets. IG--Investment grade.
SG--Speculative grade. Source: S&P Global Research & Insights.

One-Third Of Sectors Had Net Downgrades; Outlooks Generally Improving

- The overall net upgrade rate in the third quarter was supported by many sectors, but the net 10 upgrades from financial institutions were the biggest single contributor. While the sector has seen multiple sources of upgrades, the largest contributor was Greek banks--following our improved assessment of their resilience to economic cycles and improving funding profile.
- Retail led the tally of *net* downgrades in the third quarter, with seven downgrades. This included Walgreens Boots Alliance Inc., which we downgraded to 'BB' from 'BBB-'.
- The average negative bias across sectors has fallen over the last four quarters, to 14.5% from 15.4%. The most notable exceptions to this are telecommunications and transportation--the sectors' negative bias has risen over 3% each since the second quarter.

Financial institutions account for half of all net upgrades

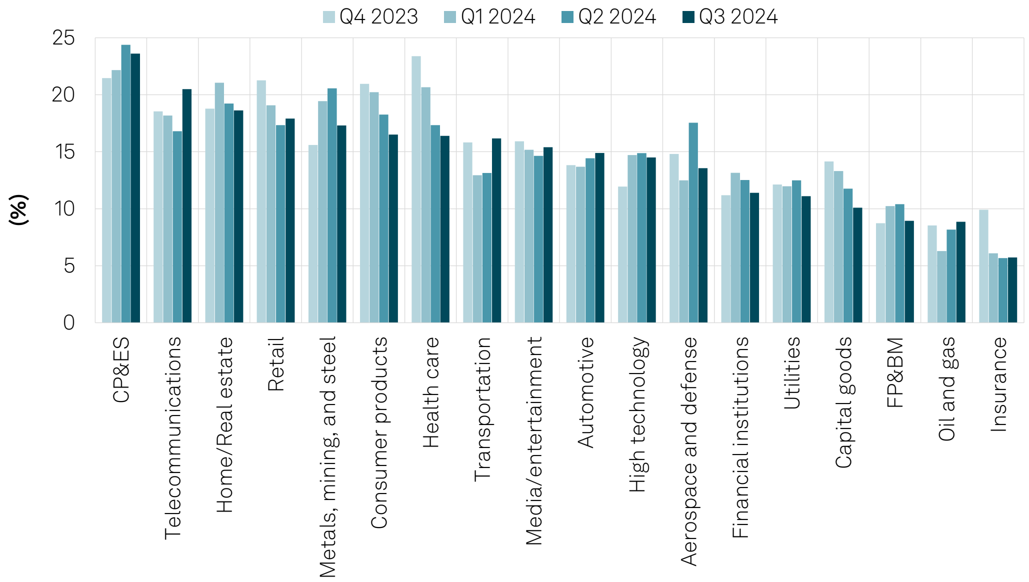
Third-quarter 2024 rating actions by sector*



Excludes sovereigns. *Rating action data as through Sep. 16, 2024. CP&ES--Chemicals, packaging, and environmental services. FP&BM--Forest products and building materials.
Source: S&P Global Research & Insights.

Telecom and transportation see the largest increase in negative bias

Sector-level negative bias

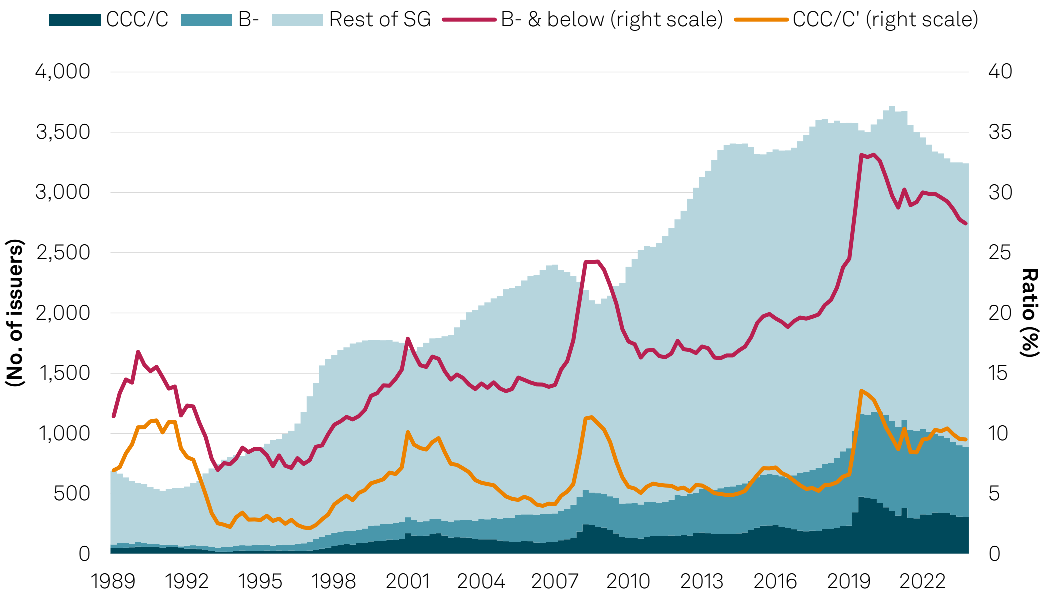


Excludes sovereigns. Bias data as of Sep. 16, 2024. CP&ES--Chemicals, packaging, and environmental services. FP&BM--Forest products and building materials. Source: S&P Global Research & Insights.

Proportion Of The Most Stressed Issuers Remains Elevated

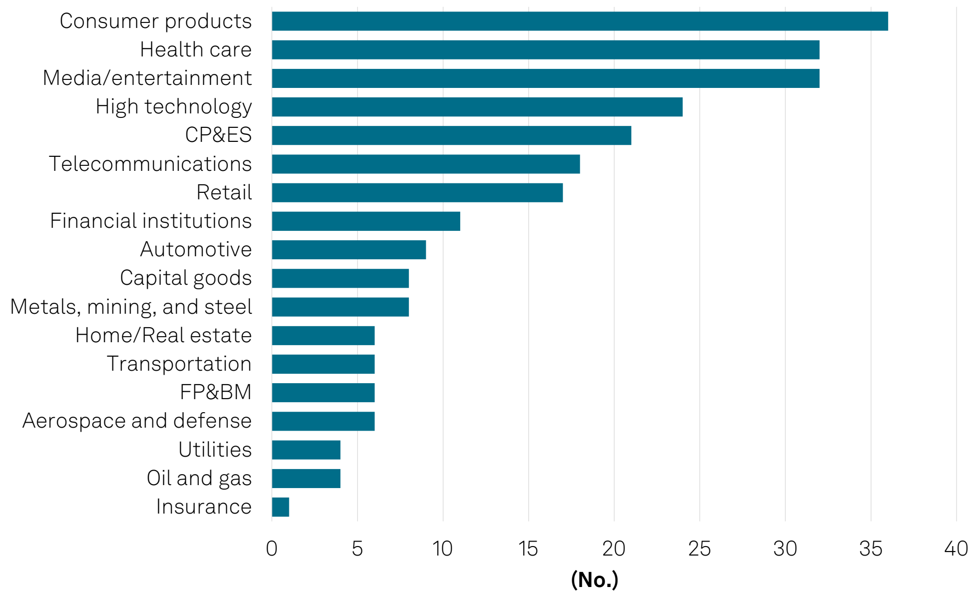
- Consumer-facing sectors, chemicals, and those with a high proportion of floating-rate debt continue to be the most vulnerable to downgrades or defaults.
- Weakest links tend to default at a rate of roughly 8x that of the overall speculative-grade population, but the population of weakest links has been falling for eight straight months. The proportion of speculative-grade ratings that are weakest links has also been flat or falling for over a year. (Weakest links are issuers rated 'B-' and lower with negative outlooks or on CreditWatch negative.)
- After years of relative stability, even at the lowest rating levels, high tech is now one of the larger sectors for weakest links.

Proportion of 'CCC's holds steady at elevated levels



Data as of Aug. 31, 2024. SG--Speculative grade.
Sources: S&P Global Ratings Credit Research & Insights and S&P Global Market Intelligence's CreditPro.

Weakest links are highly concentrated: ~40% are in consumer products, health care, and media & entertainment

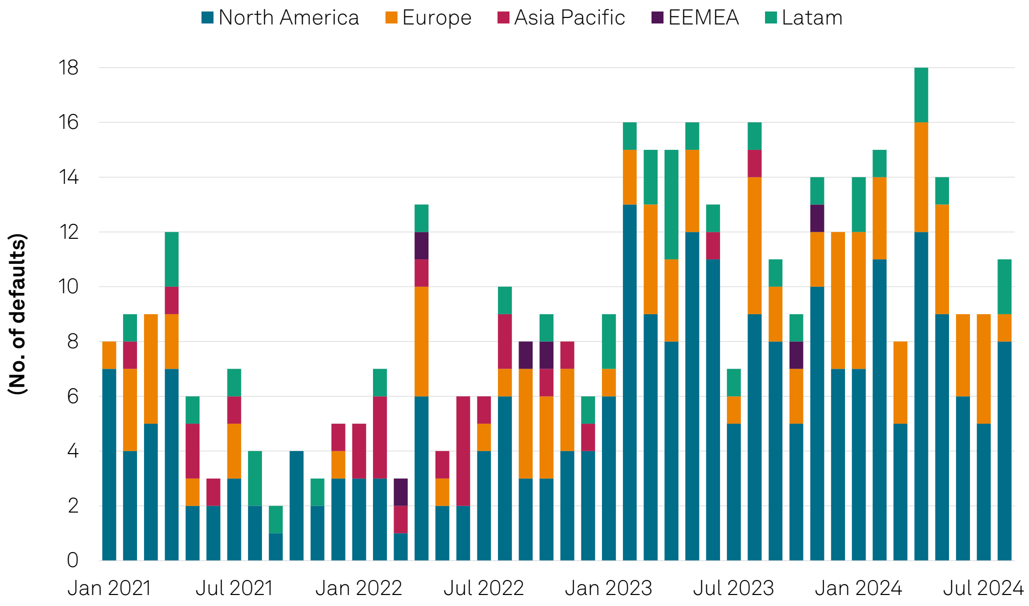


Data as of Aug. 31, 2024. CP&ES--Chemicals, packaging, and environmental services. FP&BM--Forest products and building materials. RE--Real estate. Source: S&P Global Ratings Credit Research & Insights.

Global Defaults Decline Over The Summer

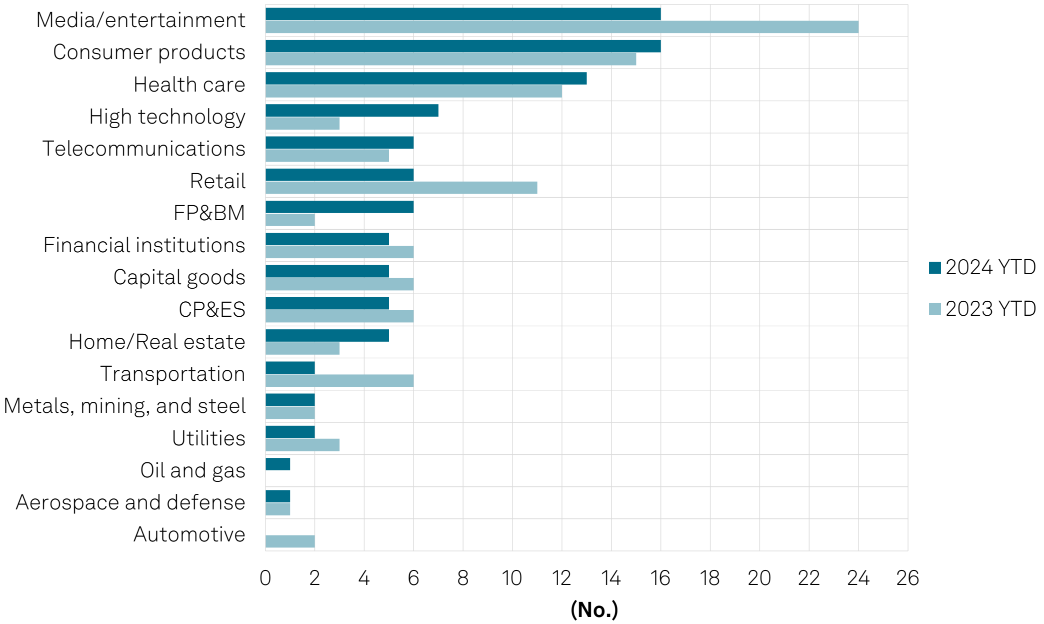
- The pace of global defaults has started to decline in recent months, relative to the pace in 2023.
- The top three sectors by default count are the same as last year, and they account for 46% of this year's tally, similar to the 48% through August 2023.
- Most of the leading sectors are the largest users of very low-rated, floating-rate debt in recent years. While we expect some improvement in overall conditions for floating-rate debt, these sectors also lead among our population of 'CCC'/'C' issuers, which tend to finance through bonds, as opposed to loans, once at that rating level. Many at these rating levels also suffer from an extended period of negative cash flow, so these sectors are more likely to continue to lead the default tally.

Pace of defaults starts to slow



Data as of Aug. 31, 2024. Source: S&P Global Ratings Credit Research & Insights.

Consumer products, media, and health care lead defaults two years in a row

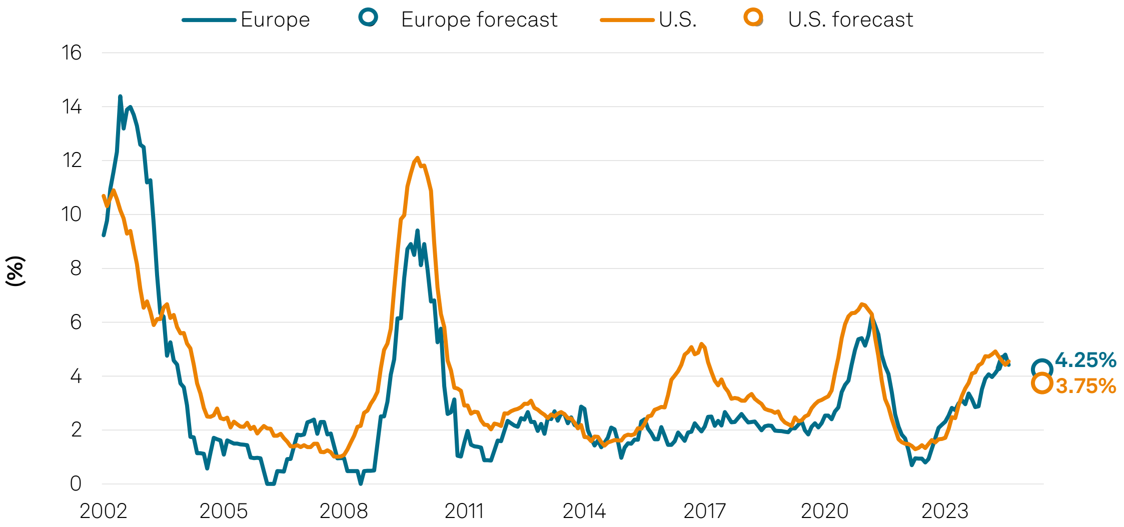


Data as of Aug. 31, 2024. CP&ES--Chemicals, packaging, and environmental services. FP&BM--Forest products and building materials. YTD--Year-to-date. Source: S&P Global Ratings Credit Research & Insights.

We Expect Defaults To Gradually Decline, Led By Distressed Exchanges

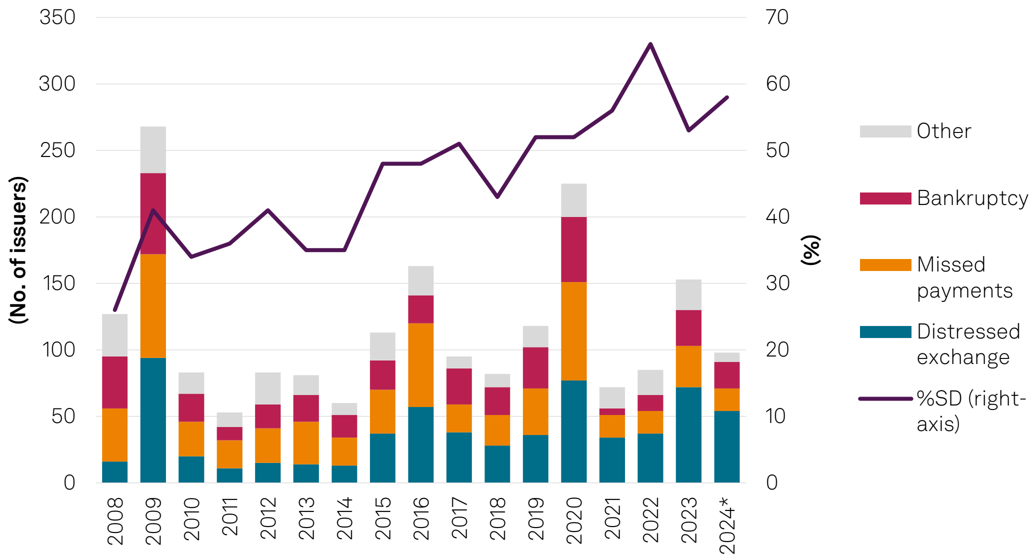
- Distressed exchanges are now a majority of all defaults this year (55%), roughly the same contribution as all selective defaults (58%). This trend should continue in the near term as fixed-rate yields remain elevated for speculative-grade issuers and a soft-landing scenario plays out.
- Through August, the U.S. speculative-grade default rate was 4.6% and Europe was 4.4%, above both regions' long-term averages. These are declines from recent highs but, as expected, still consistent with a more gradual decline than default rates' recent increases.
- As inflation cools and policy rates decline, this should ease interest burdens, particularly for leveraged loans, whose benchmark rates are tightly bound to policy rates.
- Risks to the baseline projections include slower-than-expected economic growth (especially if fueled by declining consumption), any resumption in inflation, and potential liquidity squeeze for lower-rated issuers in primary markets if recent signs of vulnerability resurface or spread.

Defaults expected to decline more slowly than they rose



Through Aug. 31, 2024. Source: S&P Global Ratings Research & Insights.

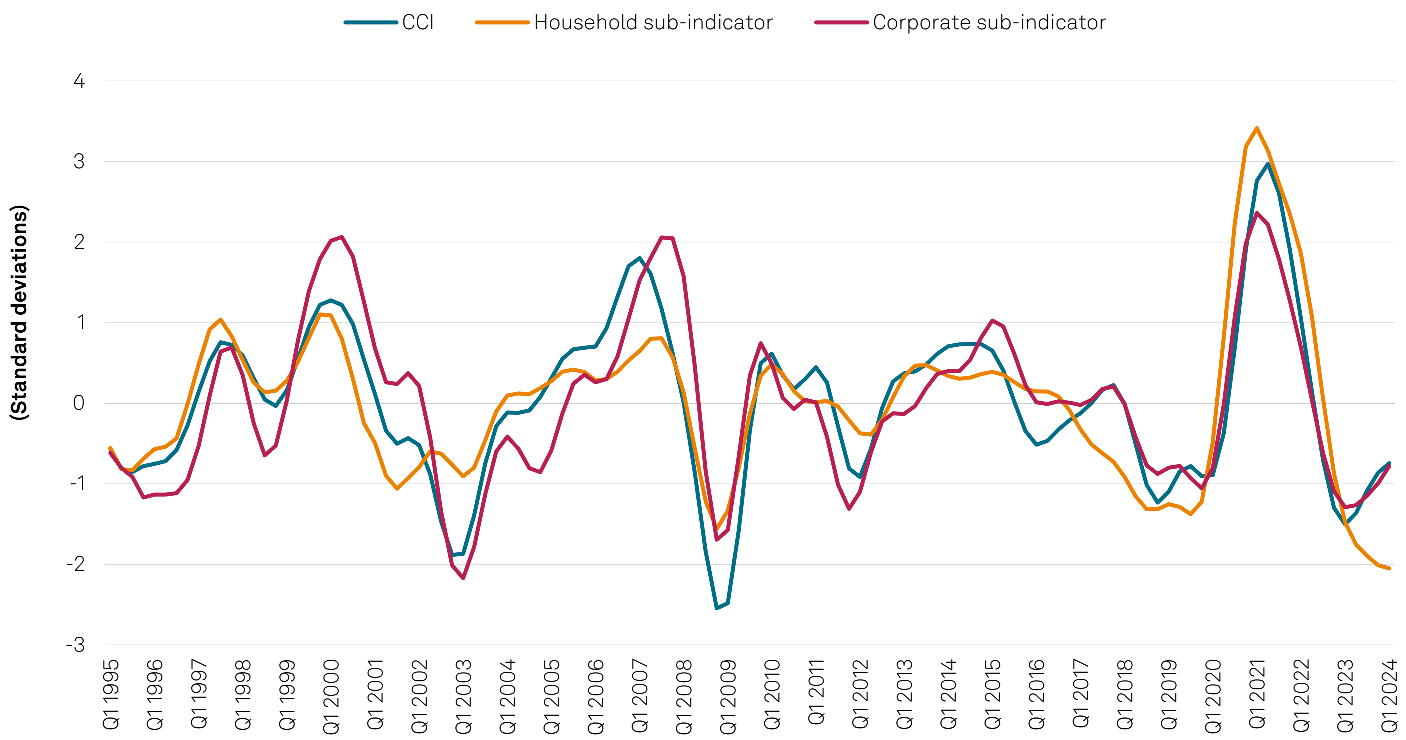
Distressed exchanges now account for majority of defaults in 2024



*Through Aug. 31, 2024. SD--Selective default. Source: S&P Global Ratings Research & Insights.

Credit Cycle Indicator | Credit Recovery Prospects Are Mixed Across Markets

The credit recovery could play out differently across markets and sectors
Global credit cycle indicator



Peaks in the CCI tend to lead credit stresses by six to 10 quarters. When the CCI's upward trend is prolonged or the CCI nears upper thresholds, the associated credit stress tends to be greater. Sovereign risk is not included as a formal part of the CCI. The CCI period ends in the first quarter of 2024. For more details about our proprietary CCI, see "White Paper: Introducing Our Credit Cycle Indicator," published on RatingsDirect, June 27, 2022.

Sources: Bank for International Settlements. Bloomberg. S&P Global Ratings.

- Our forward-looking credit cycle indicators (CCI) continue to signal a potential credit recovery in 2025, as they emerge from the early-2023 trough. This is taking place in the backdrop of rate cuts by central banks, and prospects of a soft landing in major economies.
- On one hand, the corporate subindicator is seeing positive momentum from recovering earnings, stronger equity prices, and improving market conditions that support financing.
- On the other, the household subindicator continues to decline, suggesting ongoing deleveraging by households as elevated cost pressures bite into purchasing power. In many markets, real residential prices are still weak.
- Increasing divergence among our regional CCIs spell different paths towards a credit recovery. The eurozone and emerging markets ex-China CCIs continue to rise from a trough. However, the earlier increase in the North America and some Asia CCIs is stalling.

Regional Credit Conditions

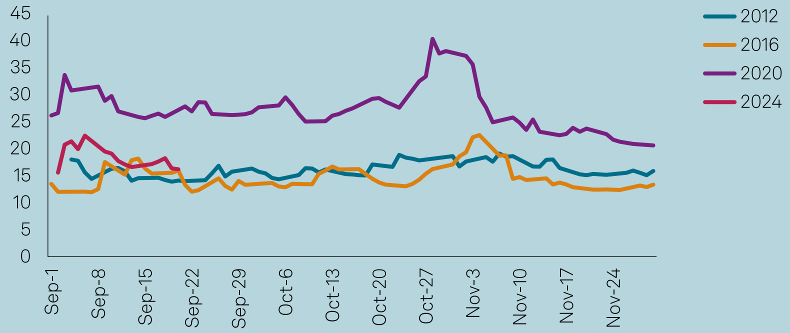
North America | Set For Improvement, With Eyes On The Election

U.S. elections 2024: What's at stake for credit

Risks to credit

- Financial-market volatility, especially if result of presidential election is unclear or in dispute
- Political polarization and policy uncertainty
- Could generate a wait-and-see investment climate, hurt business and consumer sentiment, and reduce economic activity

VIX measure of equity market volatility tends to increase during U.S. presidential elections



Policy areas to watch

Fiscal policy

We don't expect meaningful federal deficit reduction regardless of outcome, given pledges not to reform mandatory spending

We view the CHIPS Act, IRA and infrastructure spending as less likely to change given some areas of bipartisan support

Expiry of the TCJA at end-2025 opens the possibility for changes in tax regime

Trade policy

More trade restrictions—specifically, higher tariffs—could result in inflationary pressures, especially for sectors exposed to cross-border supply chains

We expect U.S.-China tensions to remain irrespective of the outcome of the election

Regulation

M&A may become more active if regulatory hurdles lessen for large business combinations

Uncertainties around energy and climate regulations could affect relevant sectors.

Financial regulation could be affected over time

VIX is through Sept. 20, 2024, and sourced from S&P Capital IQ Pro. Source: S&P Global Ratings.

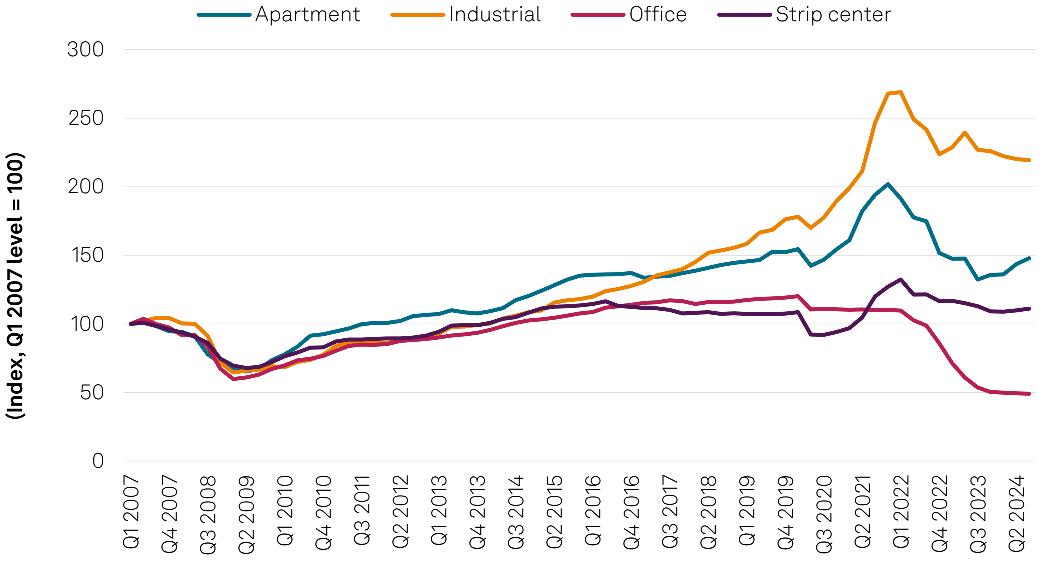
- **Overall:** Credit conditions look set to steadily improve, but the looming U.S. elections could create some financial market volatility and policy uncertainty.
- **Risks:** Financing costs could remain overly burdensome for some borrowers, especially those at the lower end of the ratings spectrum, if monetary-policy easing is derailed or risk aversion increases. Cost pressures could persist, threatening to hurt credit.
- **Ratings:** The region's net outlook bias has improved to -9.2%. We expect the U.S. trailing-12-month speculative-grade corporate default rate to fall to 3.75% by June 2025.

North America | Commercial Real Estate Remains Under Pressure

- **CRE fundamentals remain under pressure**, despite some relief that might come with the Fed's rate cuts. Office is grappling with secular headwinds, which further weighs on valuations and cash flows. Certain segments and regions within the multifamily sector are also facing challenges as rent growth softens.
- All this may lead to **more broad-based, and in some cases severe, loan losses for debtholders**, such as U.S. banks (with regional lenders having proportionately higher exposure to CRE than larger U.S. lenders do), insurers, REITs, and commercial mortgage-backed securities (CMBS). Higher office vacancy rates and shuttered ground-level businesses could also affect tax revenue for cities.

Office valuations still under acute stress

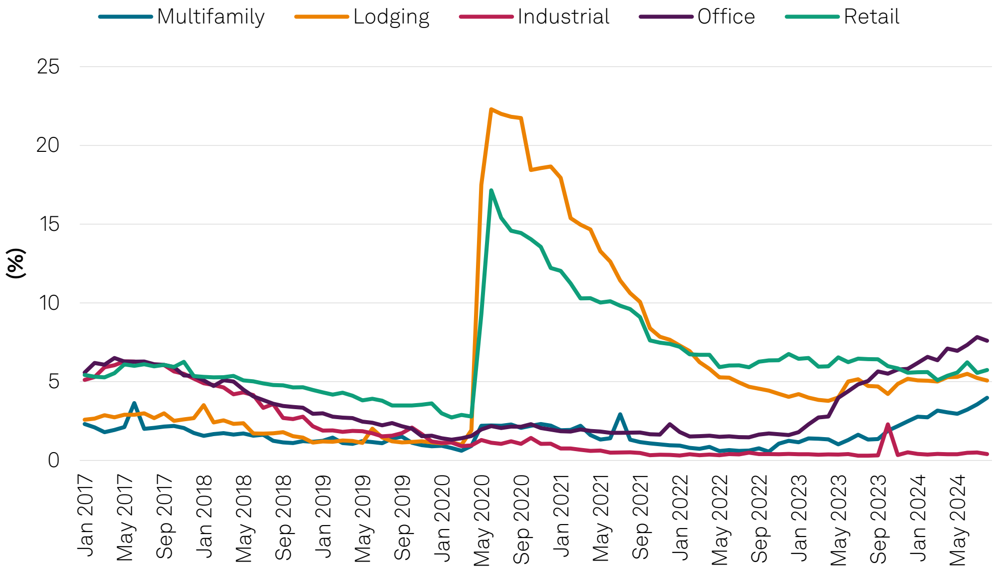
Green Street Commercial Property Price Index by property type in the U.S.



Q3 2024 data as of Sept. 9, 2024. Sources: Green Street and S&P Global Ratings' calculations.

Office loans maintain the highest delinquency rate

U.S. CMBS delinquency rate by property type



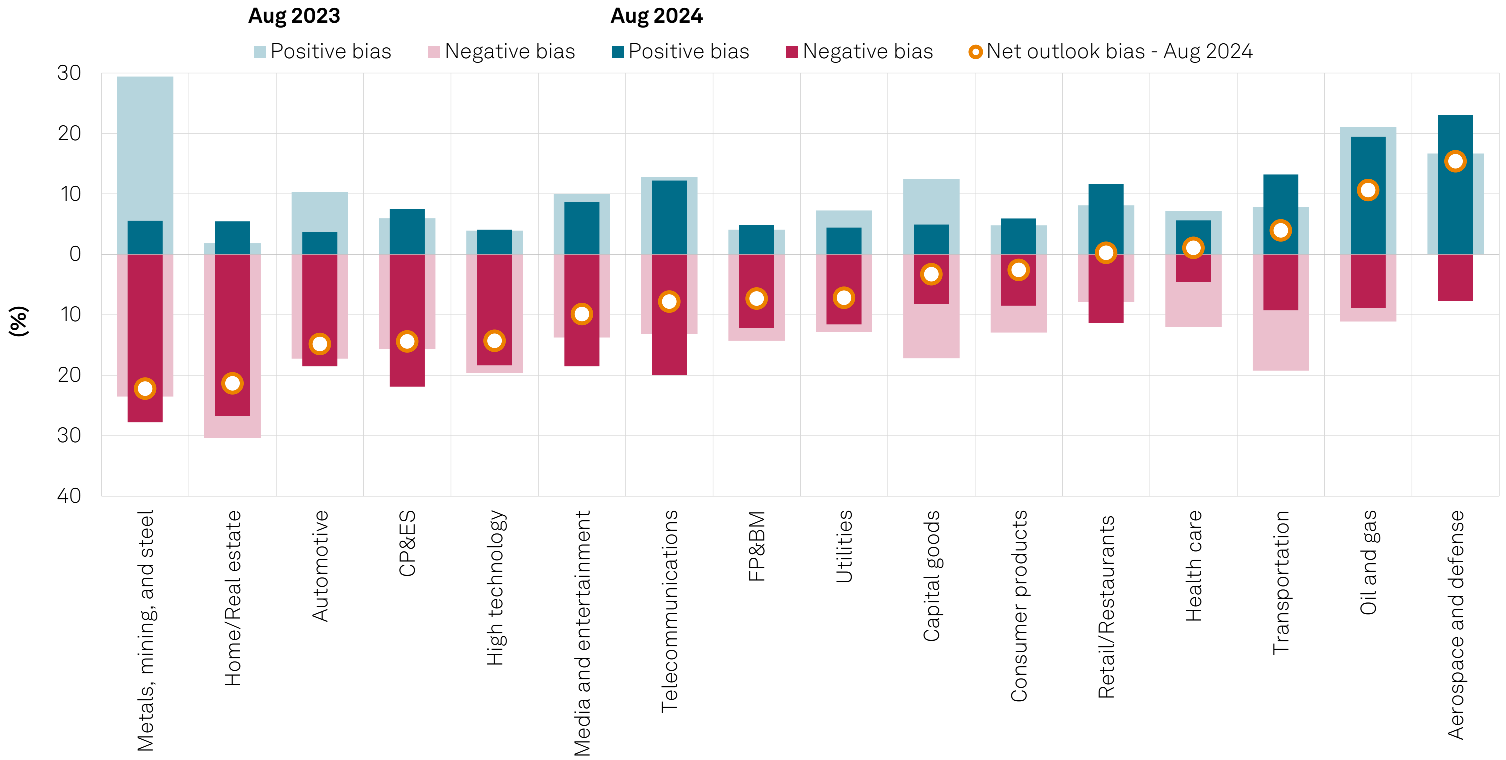
Data through Aug. 2024. Source: S&P Global Ratings.

Europe | Turn In Credit Cycle Won't Be Easy

- **Base case:** The macro credit outlook for Europe differs little from the previous quarter and remains constructive as the rate cycle turns, although visibility on the economic outlook is relatively poor.
- **Credit:** Ratings actions are quite balanced even in speculative -grade. However, autos, chemicals, and tech are corporate sectors to watch given some deteriorating outlooks on a net outlook basis. Somewhat counterintuitively, the European speculative-grade default rate remains elevated at 4.4% in August 2024, and we expect it to decline toward 4.25% by June 2025.
- **Pockets of risk:** More vulnerable segments include commercial real estate (CRE), with some arrears building in European CMBS and U.K. nonconforming and legacy buy-to-let. European sovereigns remain strained by high debt levels, while corporate entities increasingly focus on strengthening the resilience of supply chains and improving their competitiveness.

Net outlook bias deteriorated over last year in auto and chemicals; still weak, but improving, in real estate

European nonfinancial sector outlook bias



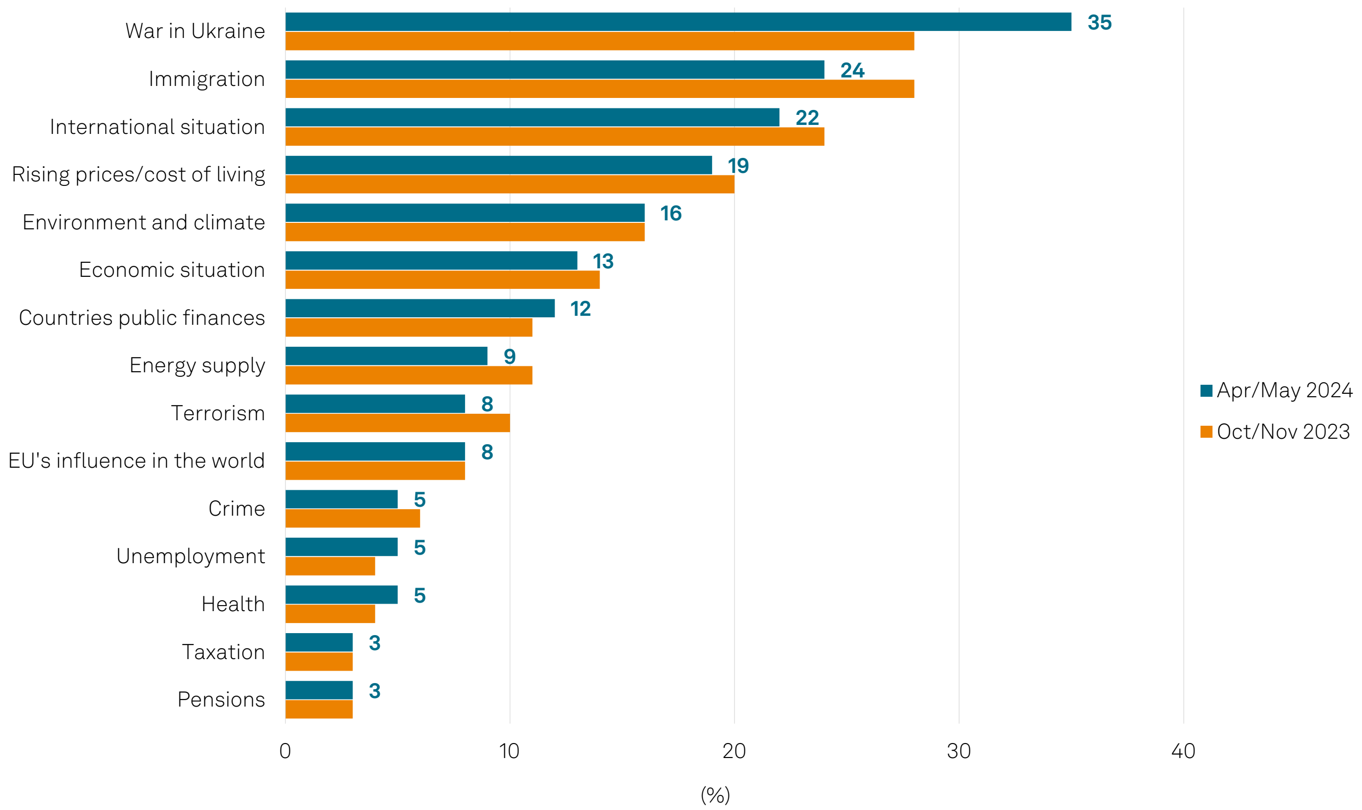
CP&ES--Chemicals, packaging, and environmental services. MM&S—Metals, mining and steel. FP&BM--Forest products and building materials. Data as of Aug. 31, 2024. IG--Investment-grade. SG--Speculative-grade. Source: S&P Global Ratings Credit Research & Insights.

Europe | Geopolitical Uncertainty Remains A Key Concern

- **Regional wars:** Geopolitical risk remains our top regional risk with the potential to disrupt supply chains, trigger risk aversion and a flight to quality, and shift governments' spending priorities.
- **Trade and tariffs:** The EU is trying to navigate a path through the simmering U.S.-China trade tensions, although ensuring economic security and supply chain resilience is growing in importance.
- **Macro:** The two main macro risks are the tail risks of interest rates not needing to fall to the terminal rate, and a protracted period of slower European growth if the regional economy remains weighed down by weak investment and an aging workforce.
- **CRE:** Some positive signs, from a credit perspective, are valuations starting to stabilize and financing conditions improving. However, certain segments, such as non-prime office and German residential real estate, remain weak. More adverse developments could be detrimental for the broader economy and impair European banks' asset quality.

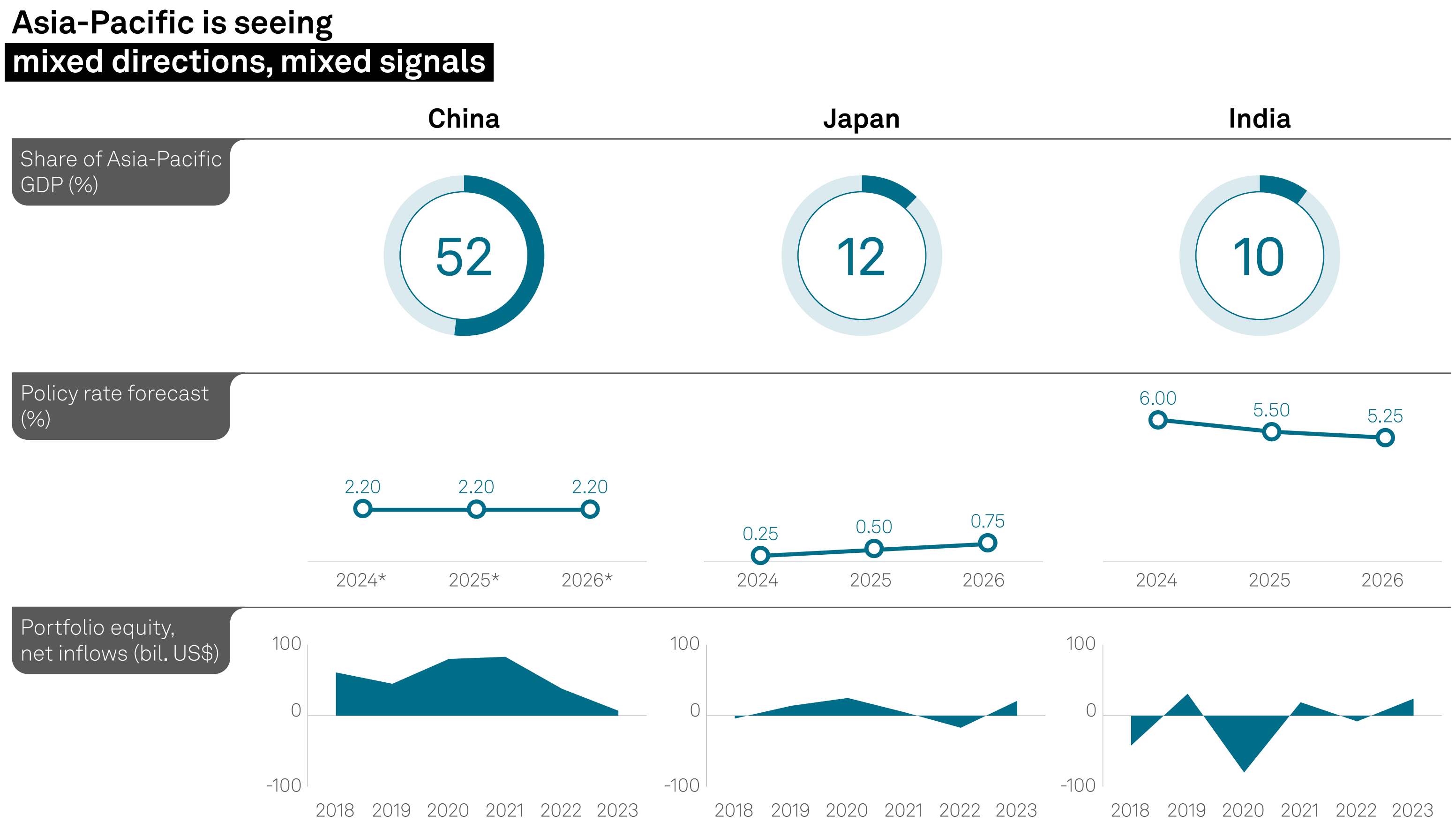
Russia-Ukraine war remains the public's overriding concern in Europe

What do you think are the two most important issues facing the EU-27 at the moment?



Source: Eurobarometer (April/May 2024).

Asia-Pacific | Mixed Signals: Growth And Rates



*The forecast is as of Sept. 24, 2024. GDP refers to annual 2023 nominal figures. For China's policy rate, the one-year medium-term lending facility rate is shown.
Data source: GDP--S&P Global Market Intelligence. Policy rate forecast--S&P Global Ratings Economics. Portfolio equity, net inflows--World Bank DataBank.

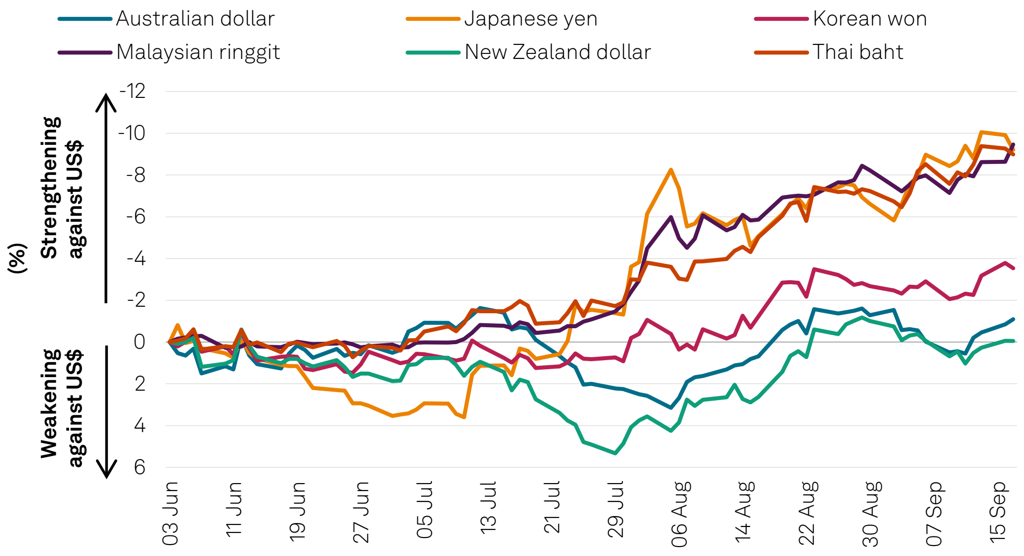
- **Between a rock and a hard place:** China's property crisis is severe, and the risk of systemic deflation is increasing. While recent monetary stimulus can boost credit in the system, weak confidence will continue to drag growth. We lowered our growth forecast for China to 4.6% in 2024 and 4.3% in 2025.
- **Shifting gears:** Most APAC central banks will gradually follow the Fed in cutting rates, but domestic factors will determine the pace. Refinancing conditions should improve, with issuers able to tap offshore markets.
- **Walking a fine line:** Strong global demand and diversification of manufacturing to outside China generate growth opportunities for export-centric Asia-Pacific countries. But a slower China could spill over to hit other countries, particularly those dependent on Chinese demand.
- **Volatility rising:** An unexpected global hard landing could spur risk-off sentiment and capital outflows. Worsening geopolitical tensions could stifle the region's growth momentum. Japan's exit from negative rates risks the abrupt unwinding of carry trades and longer-term shifts in asset allocation.

Asia-Pacific | The Great Divide

- **Uneven conditions.** The net rating outlook bias of APAC issuers remains at -2% in August. The skewed distribution points to uneven conditions across sectors. While China's economic risk is mounting, strong exports and recovering domestic consumption are supporting growth elsewhere in the region, especially for manufacturers. In some sectors, appetite for mergers and acquisitions and expansion could return.
- **Uncertainty abound.** Geopolitical risks are stoking uncertainty. Trade tensions between China and the West continue to simmer. Businesses may diversify supply chains and revenue sources to cope, but this is costly. Meanwhile, rising uncertainty and market volatility could prompt lenders to become selective.

Asia-Pacific currencies are regaining strength...

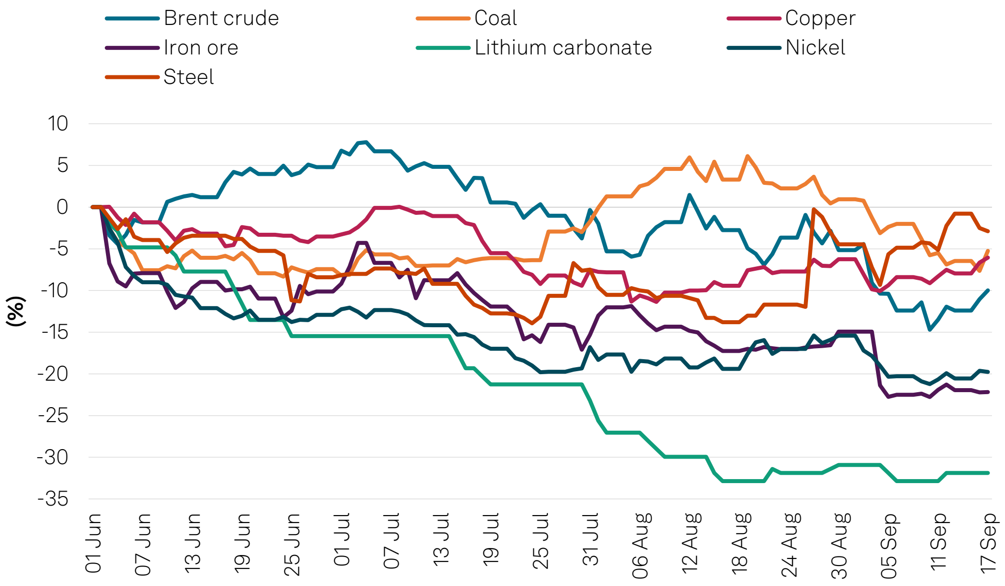
Percentage change since Jun. 1, 2024



Data as of Sep. 17, 2024. Source: S&P Global Market Intelligence.

...while energy and commodity prices are softening

Percentage change since Jun. 1, 2024

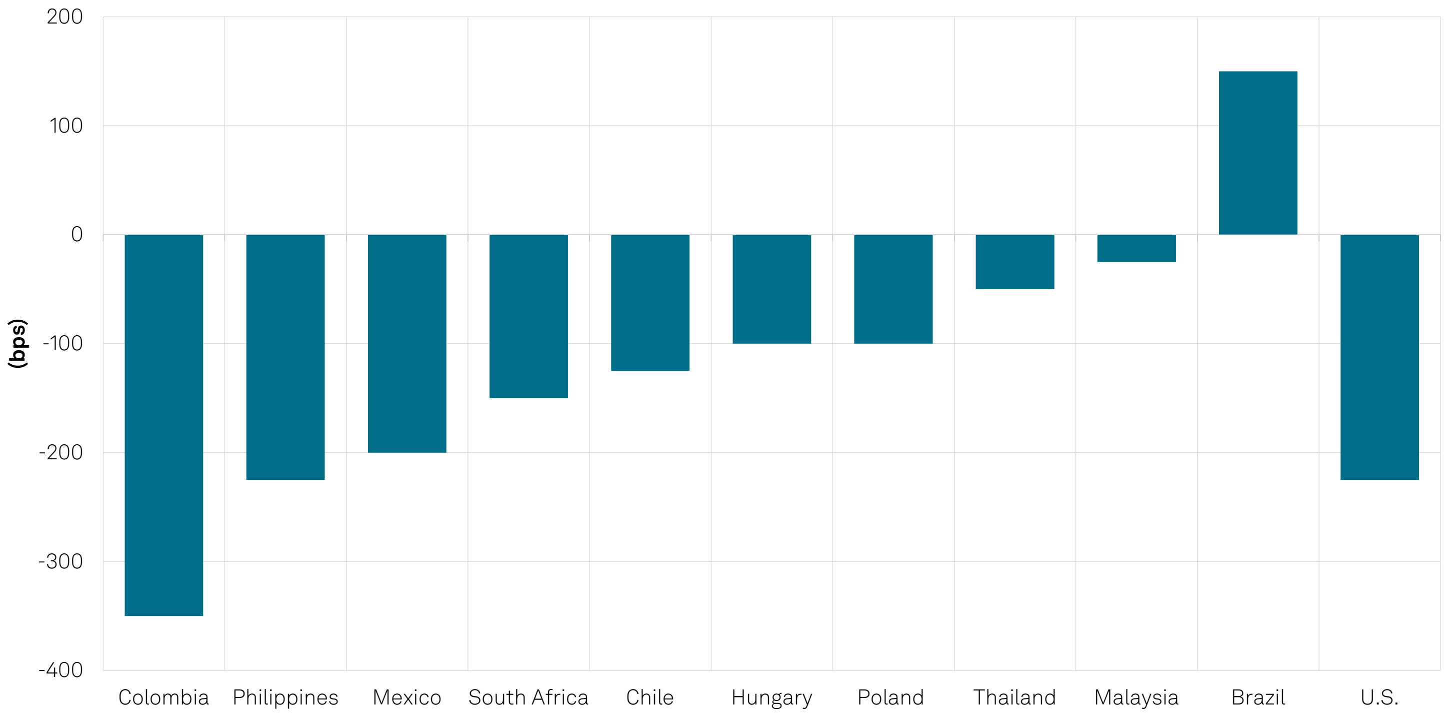


Data as of Sep. 17, 2024. Source: S&P Global Market Intelligence.

Emerging Markets | Risks Loom Amid A Fragile Stability

Fed cuts clear the path for more easing in EMs

Market-implied policy rate change in the next 12 months



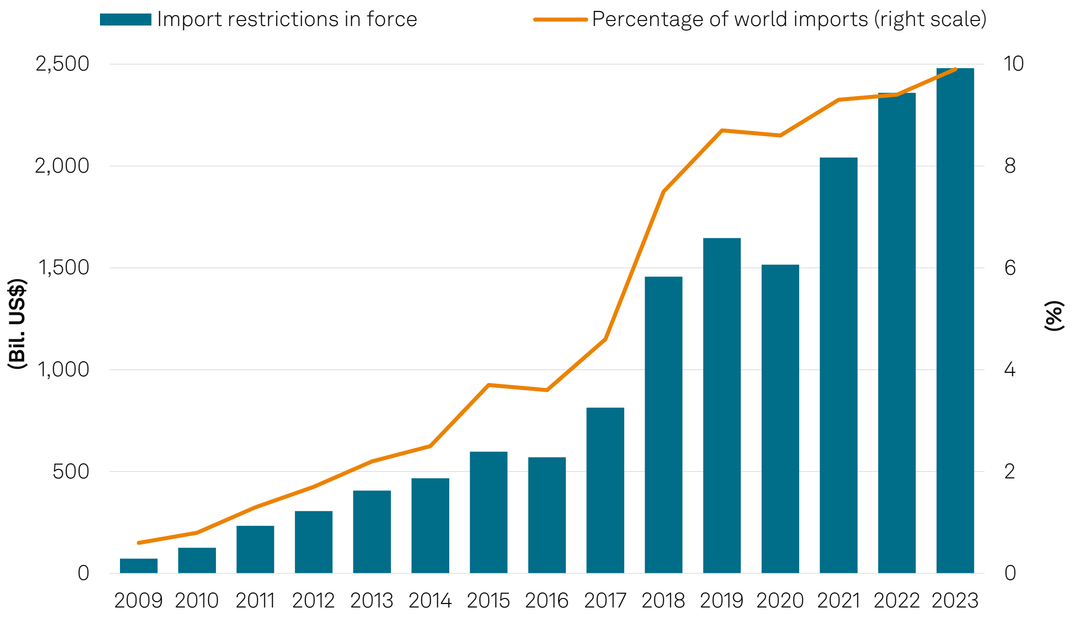
Sources: Haver Analytics and S&P Global Ratings.

- Credit conditions will likely remain supportive for emerging market (EM) issuers as long as a soft landing continues in the U.S.
- The Federal Reserve's interest rate cuts and the prospects for quicker monetary easing down the road will likely lead to continued improvement in financing conditions for EMs.
- Falling oil prices driven by market concerns over sluggish demand growth should also be conducive for most EMs, if recession in advanced economies is averted.
- Together, these factors should give room for most EM central banks to continue cutting interest rates, which, along with anchored expectations for lower inflation, should bring down borrowing costs for EM issuers.

Emerging Markets | Rising Protectionism Could Derail Favorable Conditions

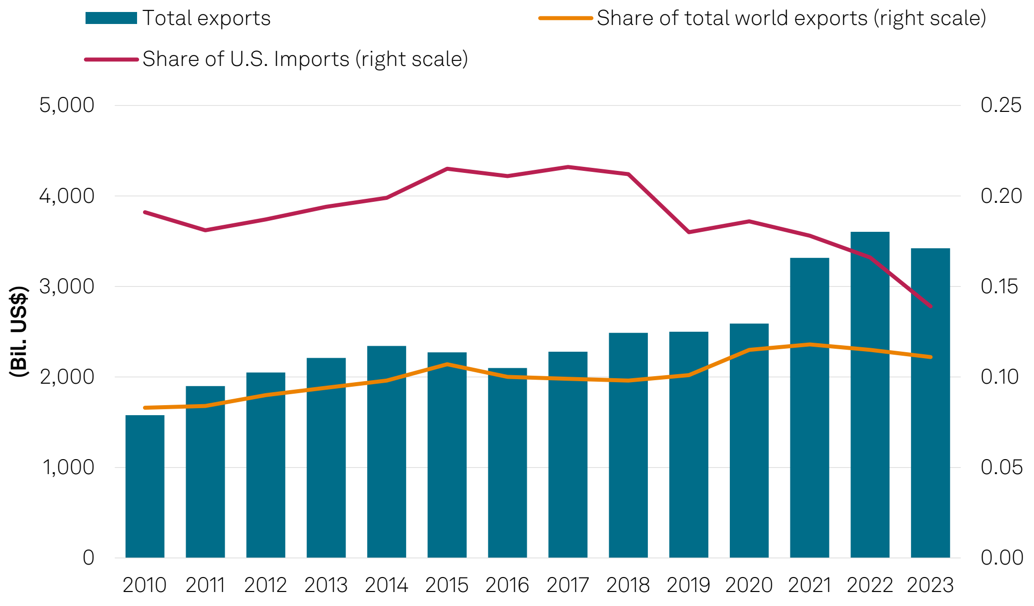
- U.S. and China trade tensions continue worsening, and we expect more protectionist measures over the coming months, regardless of the outcome of U.S. elections.
- Chinese economic growth could slow further upon continued real estate weakness and growing trade tensions.
- The Middle East conflict has escalated to a dangerous phase that could further disrupt supply chains and weigh on energy prices.

Protectionist measures have been increasing since 2017



Source: WTO end-of-year trade monitoring report 2023.

Chinese exports remain strong despite tariffs
China's figures



Sources: S&P Global Market Intelligence and World Bank.

Emerging Markets | A Slower Chinese Economy Could Spell Trouble For EMs

A deepening property crisis, weak confidence, high debt levels, and trade tensions slow economic growth for China

2023 exports to China by type (% of GDP)

	Energy	Materials	Industrial goods	Consumer goods	Information technology	Other	Total
Malaysia	11.4	3.2	2.0	1.2	7.9	0.1	25.7
Vietnam	0.0	1.7	2.6	3.8	12.0	1.6	21.6
Chile	0.0	11.4	0.0	1.4	0.0	0.0	12.8
Thailand	0.1	2.8	1.9	3.3	1.8	0.1	9.9
Peru	0.1	8.8	0.0	0.8	0.0	0.0	9.6
South Africa	0.1	7.9	0.0	0.5	0.0	0.0	8.4
Saudi Arabia	5.1	0.9	0.0	0.0	0.0	0.0	6.0
Brazil	1.1	1.8	0.0	2.7	0.0	0.0	5.6
Indonesia	1.6	2.8	0.1	0.9	0.0	0.0	5.4
Philippines	0.1	1.0	1.0	0.4	2.0	0.0	4.5
Hungary	0.0	0.1	0.8	0.6	0.6	0.1	2.2
Colombia	1.5	0.2	0.0	0.0	0.0	0.0	1.8
Mexico	0.1	0.3	0.1	0.2	0.2	0.1	1.1
Argentina	0.0	0.1	0.0	0.9	0.0	0.0	1.0
Poland	0.0	0.2	0.2	0.2	0.0	0.0	0.6
India	0.0	0.3	0.1	0.2	0.0	0.0	0.5
Turkiye	0.0	0.3	0.0	0.1	0.0	0.0	0.4

The shading per sector represents exposure. The darker the color, the greater the exposure. Source: S&P Global Market Intelligence.

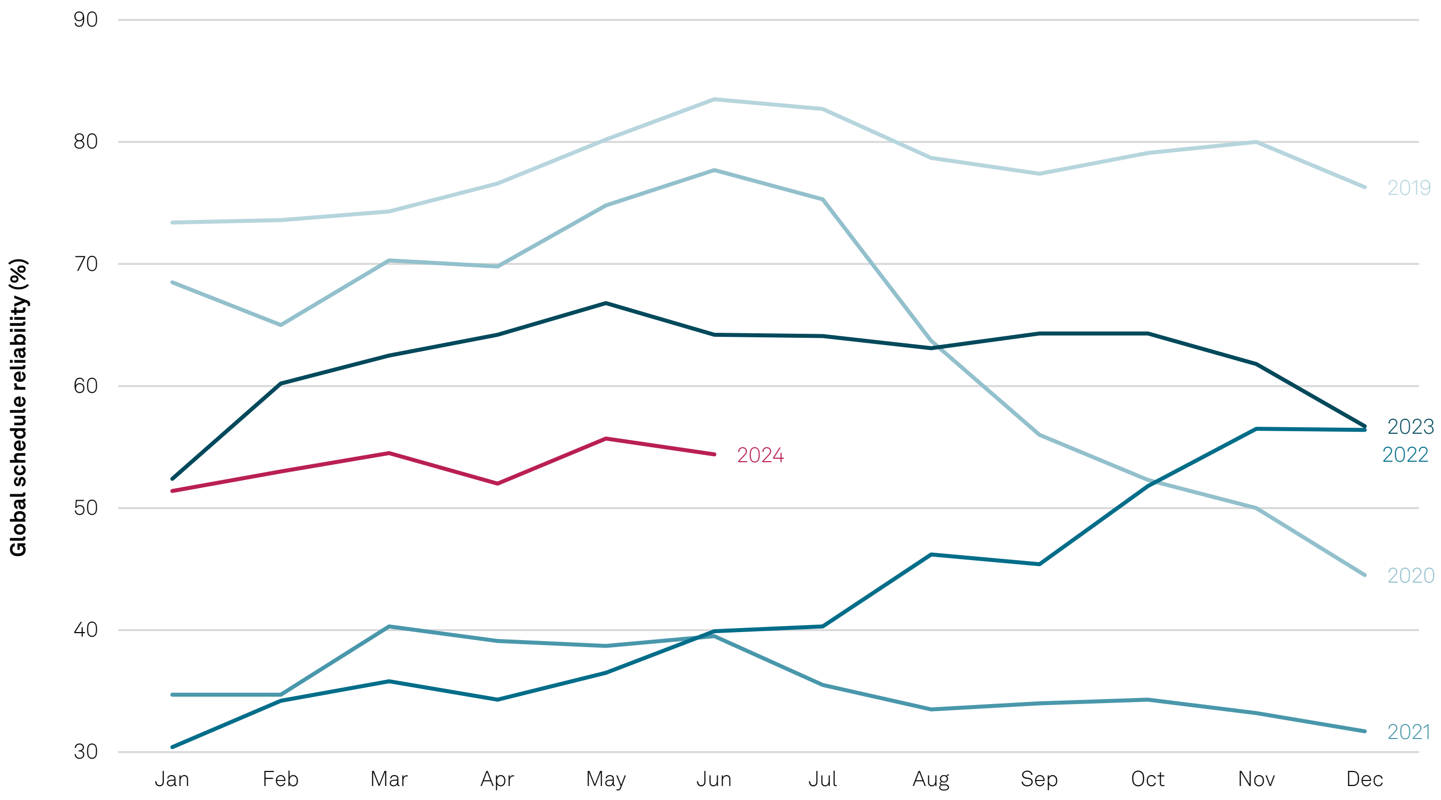
- The Chinese economy continues showing the drag from its real estate sector, which, along with weak consumer confidence and spending, indicates bleak recovery prospects. Furthermore, the combination of soft consumption and robust manufacturing investment has led to excess capacity in several goods markets, which is increasing structural deflation risk.

- Increasing tariffs could hit China's GDP growth meaningfully. A slower Chinese economy is bad news for many EMs, which have this country as a key destination for their exports. The potential impact could vary significantly depending on the degree of dependence on the Chinese economy.

Sector Trends

Corporates | Geopolitical Tensions Pressure Global Supply Chains

Container shipping schedule reliability lags

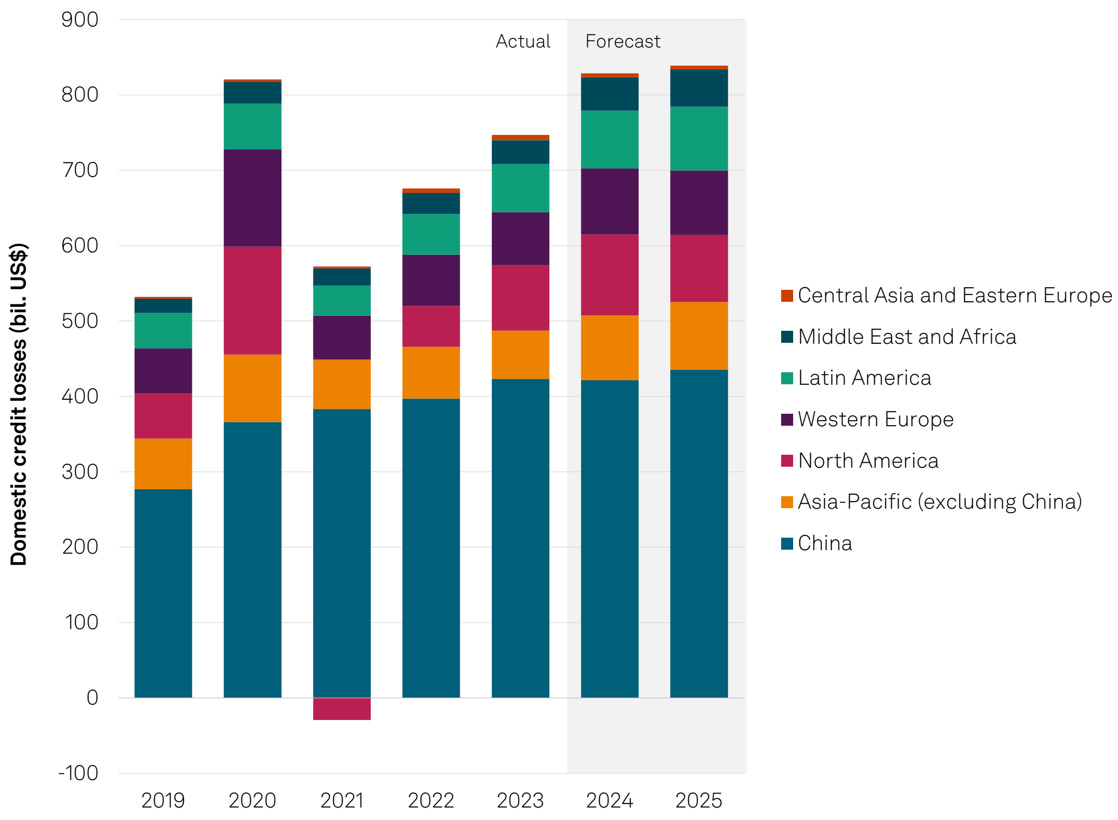


Source: Sea-Intelligence ApS - Monthly Report on Schedule Reliability in Container Shipping.

- Pressure on global supply chains is increasing due to geopolitical tensions related to the Red Sea crisis and the rerouting of cargo ships, inventory restocking, clear signs of container shortages, and looming industrial actions in some regions, among other factors.
- Shipping costs are increasing; companies are usually able to accommodate them because they represent 1%-2% of total sales for most industries.
- The delays in deliveries can be difficult to accommodate, particularly ahead of the peak holiday season.
- Many sectors rely heavily on logistic for sourcing and supplying. A deterioration of the current situation could create serious disruptions for several sectors.

Global Banks | Credit Losses Are Approaching The Peak

Credit losses will increase by 12% from 2023 to 2025



Data shown on a constant currency basis, based on 2023 year-end exchange rates. Data for China relates to commercial banks. Source: S&P Global Ratings.

Our latest outlook

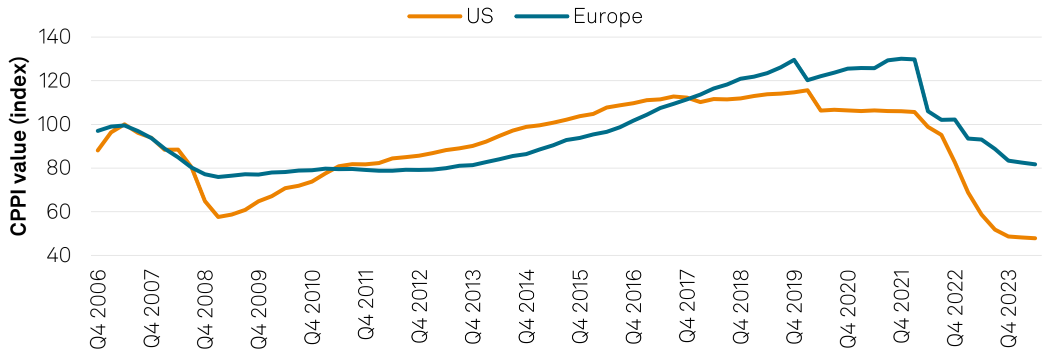
- Our base case is for relative ratings stability in 2025--currently about 75% of banking groups globally have stable ratings outlooks.
- We see three key downside risks to ratings--an economic downside materially outside our current expectations, worse-than-expected commercial property markets, and still-high government and corporate sector leverage.
- Geopolitical risks, domestic political risks in a year marked by a high number of elections, and structural risks are elevated and could hurt banks. Furthermore, we expect the turbulence affecting credit and equity markets to continue, though we anticipate that most banks will remain resilient at current levels.
- We forecast global credit losses will increase by about 12% to US$840 billion by year-end 2025--this is within our base case at current rating levels for most banks.

What we're watching

- Cyclical downside risks. Policy missteps as the rate easing cycle begins, much weaker economic growth, or a deterioration of other variables outside our base case may cause credit losses to worsen and more outlooks to turn negative.
- Regulatory developments. The continuing evolution of prudent banking regulations, especially for capital and liquidity, will buttress banks' creditworthiness.
- Government support. We anticipate governments may need to step in if a major adverse event or much worse-than-expected economic or other scenario hits banks.

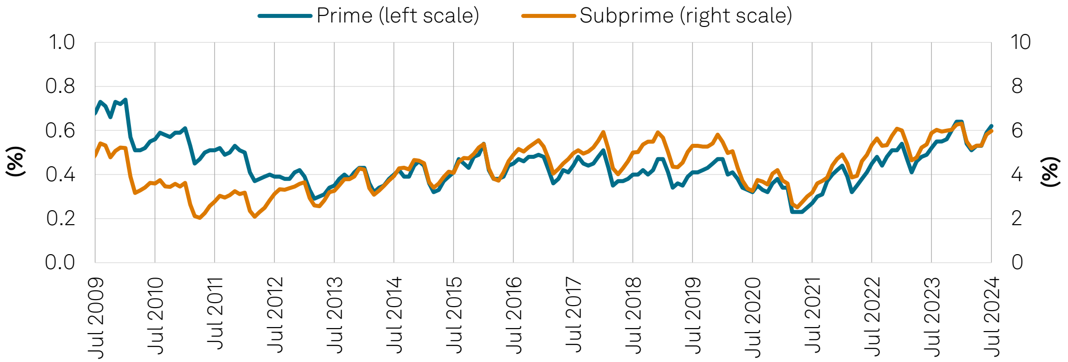
Structured Finance Ratings Resilient | CMBS And Some Consumer Headwinds

Green Street Office CPPI* (B/B+ Quality) Q4 2006-Q2 2024



Source: Green Street, S&P Global Ratings. *CPPI = Commercial Property Price Index

U.S. Auto loan ABS 60+ day delinquency rates*



*Based on auto loan ABS transactions rated by S&P Global Ratings. Source: S&P Global Ratings.

- On the commercial real estate/CMBS side, the challenging conditions for office buildings remain front and center, as uncertainty regarding future demand for space has led to unprecedented price declines, shaky fundamentals, and a much tighter financing environment.
- With elevated inflation rates during the past few years (although lower now) and the currently (relatively) high borrowing rates, it comes as little surprise that credit pressure on U.S. consumers is greater for the lower half of the income spectrum and obligors with weaker credit scores. However, we have also seen signs of deterioration within the “prime” borrower segment. Our recent U.S. auto loan ABS tracker showed 60-plus delinquencies at their highest July levels since 2009 for prime, and their highest ever July level for subprime.
- In Europe, the CMBS sector has seen property value declines greater than during the global financial crisis, though it's faring better than the U.S. There are also pockets of weakness among consumer-related securitizations, notably RMBS backed by U.K. nonconforming, U.K. legacy buy-to-let, or Irish nonprime mortgage loans. Among other risk factors, these subsectors are disproportionately exposed to floating-rate and interest-only loans, with more borrowers who have few refinancing options.

Related Research And Contacts

Related Research

Credit Conditions

- Credit Conditions Asia-Pacific Q4 2024: Mixed Signals: Growth And Rates, Sept. 25, 2024
- Credit Conditions Europe Q4 2024: Turn In Credit Cycle Won't Be Plain Sailing, Sept. 25, 2023
- Credit Conditions Emerging Markets Q4 2024: Risks Loom Amid A Fragile Stability, Sept. 25, 2024
- Credit Conditions North America Q4 2024: Set For Improvement—With Eyes On The Election, Sept. 25 2024

Regional Credit Outlooks can be found here

Economic Outlook

- Global Economic Outlook Q4 2024: So Far, So Smooth--Can It Last?, Sept. 26, 2024
- Economic Outlook Asia-Pacific Q4 2024: Central Banks To Remain Cautious Despite U.S. Rate Relief, Sept. 23, 2024
- Economic Outlook Eurozone Q4 2024: Consumer Spending To The Rescue, Sept. 24, 2024
- U.K. Economic Outlook Q4 2024: Disinflation And Rate Cuts Will Stimulate Growth, Sept. 23, 2024
- Economic Outlook Emerging Markets Q4 2024: Lower Interest Rates Help As Pockets Of Risk Rise, Sept. 24, 2024
- Economic Outlook U.S. Q4 2024: Growth And Rates Start Shifting To Neutral, Sept. 24, 2024

Regional Macro Updates can be found here

Additional research

- Credit Cycle Indicator Q4 2024: Credit Recovery Prospects Are Mixed Across Markets, Oct. 1, 2024
- Industry Credit Outlook: Asia-Pacific Sector Roundup Q4 2024: The Great Divide, Sept. 29, 2024
- U.S. GSIBs Q2 2024 Update: Well Positioned For Lower Rates, Aug. 27, 2024
- European Banks: Preparedness Is Key To Unlocking Central Bank Funding, Sept. 17, 2024
- Where Are China's Overinvestment Risks?, Aug. 7, 2024
- The U.S. Speculative-Grade Corporate Default Rate Will Continue Its Descent, Reaching 3.75% By June 2025, Aug. 19, 2024
- The European Speculative-Grade Default Rate Will Level Out At 4.25% By June 2025, Aug. 22, 2024
- Corporate Results Roundup Q2 2024: Slow recovery continues, driven more by margin improvement than revenue growth, Sept. 11, 2024
- Evolving Political Priorities Could Affect Energy Transition, Aug. 8, 2024
- The Energy Transition, Geopolitics, And Cannibalization Are Shaping Europe's Power Prices, Sept. 12, 2024
- U.S. 2024 Elections: How Dueling Tax Plans Could Matter For Corporates Post Election, Sept. 24, 2024

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