News Release

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IACPM

Stimulus Flood Drives Away Fear of Default in North America; Latest IACPM Credit Outlook Survey Has Positive Risk Retention Result for First Time Since Covid Pandemic Began.

New York, NY – For the first time since the Coronavirus pandemic struck early last year, risk retention turned positive in the latest IACPM Credit Outlook survey, meaning credit portfolio managers are either increasing their risk exposures or at least not cutting them. The wall of liquidity flowing from the U.S. government's $1.9 trillion stimulus program has chased away fears of rising corporate credit defaults in North America and has stabilized credit portfolios. In response, many financial institutions are increasing their risk exposure and are actively looking for new credit assets.

"The amount of liquidity is immense and credit portfolios are stabilizing, creating pressure to put money to work," said Som-lok Leung, Executive Director of the International Association of Credit Portfolio Managers. "People are hunting for ways to deploy their funds."

For the first time since the fourth quarter in 2013, survey respondents, who manage corporate loan portfolios at more than 100 global banks, insurance companies and asset management firms, believe corporate defaults will fall in North America over the next 12 months. The latest quarterly reading is 16.7, which means more survey respondents believe defaults will fall in the region than think they will rise. Similarly, respondents expect credit spreads to either tighten or stay the same in both North America and Europe. The overall index score is 13.2, which is the first positive reading since the first quarter in 2015.

"Longer term, portfolio managers are certainly worried all the stimulus will lead to rising inflation and higher interest rates," commented Mr. Leung. "But that reckoning is at least a year or two away and perhaps even longer."

When the pandemic first hit a year ago, the IACPM Diffusion Index for retained portfolio risk fell to minus-38.1 in the first quarter 2020 survey, which meant on balance managers were reducing risk. The Index fell even further in the second quarter before recovering in the third and fourth quarters last year. The latest reading is 4.2, the first positive reading since the beginning of the crisis.

Credit portfolio managers now find themselves under intense pressure to find assets which provide a reasonable return because no one can afford to stay in cash equivalents. Markets have become extremely competitive and deal structures have loosened considerably.

"Make no mistake, given all the stimulus, there are deals out there but not enough good ones, said Mr. Leung. "Everyone is looking for the same thing and deal structures reflect the imbalance between supply and demand."

While the credit outlook has improved across the globe, there are differences between North America and the rest of the world, especially Europe. The European Corporate Credit Default Outlook Index score is minus -31.4 this quarter, which is a significant improvement over the previous quarter but still reflects the fact that far more survey respondents believe European defaults will increase rather than fall. Respondents say they are particularly worried about high yield debt, noting there is no stimulus package in Europe and a third wave of the coronavirus is hitting the region.

"A number of survey respondents point out there is far less concern over investment grade debt," said Mr. Leung, noting the relatively small difference in expectations for investment grade credit spreads in Europe versus North America. "Respondents also point out interest rates remain low in Europe and bank performance is strong."

The Credit Outlook Survey is conducted among members of the IACPM, an association of 125 financial institutions in 26 countries around the world. Members include portfolio managers at many of the world's largest commercial banks, investment banks and insurance companies, as well as a number of asset managers. Members are surveyed at the beginning of each quarter.

Survey results are calculated as diffusion indexes, which show positive and negative values ranging from 100 to minus -100, as well as no change which is in the middle of the scale and is recorded as "0.0." Positive numbers signify an expectation for improved credit conditions, specifically fewer defaults and narrower spreads, while negative numbers indicate an expectation of deterioration with higher defaults and wider spreads.

About IACPM

The IACPM, with 125 member institutions located in 26 countries, is a professional association dedicated to the advancement of credit portfolio management. The organization's programs of meetings, studies, research and collaboration are designed to increase awareness of the value and the function of credit portfolio management among financial markets worldwide, and to discuss and resolve issues of common interest to its members.