News Release

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IACPM

Global Credit Conditions Have Started to Deteriorate But Latest IACPM Forecast Sees Even More Defaults and Wider Credit Spreads Ahead in the Face of Stubborn Inflation and Rising Interest Rates

New York, NY – Even as credit conditions have begun to deteriorate globally, the latest IACPM Credit Outlook Survey forecasts even higher defaults and wider credit spreads in the months ahead. Survey respondents, who manage corporate loan portfolios at banks, insurance companies and asset management companies, overwhelmingly expect to see rising defaults over the next 12 months in almost every part of the world. Eighty two percent of respondents think corporate defaults will increase in North America. Seventy seven percent say defaults will rise in Asia and more than 90% believe defaults will rise in Europe. Globally, 83% expect defaults to increase.

"Inflation is a problem in most markets and central bankers are determined to slow growth in order to contain rising prices," commented Som-lok Leung, Executive Director of the IACPM. "In this environment, our members fully expect to see rising defaults and increased losses."

Perhaps exacerbating the outlook for credit defaults is a measure called TTM, or trailing twelve months, which looks at a company's performance data over the previous 12 months. As TTM calculations begin to include more high interest rate quarterly time periods, the expectation is more companies will fall below a debt service coverage ratio of 1.0x, which is a strong signal of a borrower's weakness.

"As the universe of companies that fall below a 1.0 coverage ratio grows, we would expect to see a reflective level of higher defaults," said Mr. Leung.

The forecast for credit spreads over the next three months is negative as well, even though spreads have started to widen, which is an expected part of the process during which financial markets begin to look for some form of equilibrium. The Major Market Credit Spread Outlook Index is negative -57.6 this quarter down from minus -69.8 last summer.

"Spreads have already moved quite a bit, so at some point sentiment will turn less negative," said Mr. Leung. "At this juncture, though, economic growth hasn't slowed sufficiently so it's certainly appropriate that sentiment remains negative."

Once again, the outlook for credit spreads is more negative in Europe than elsewhere. Seventy seven percent of survey respondents expect investment grade spreads to widen in Europe, while 53% think investment grade spreads will widen in North America. Fully 80% of respondents think European high yield spreads will widen, with 13% expecting them to narrow. Seven percent believe spreads will remain unchanged.

Europe is facing the same toxic brew of higher inflation and rising interest rates as the rest of the world but is especially vulnerable to rising energy prices and perhaps even shortages as a result of the war in Ukraine. That said, some respondents note Europe's results might have been skewed by recent market turmoil in the United Kingdom.

"The UK economy is already close to recession and the Bank of England appears to have its hands full with the country's trade deficit and the government's proposed plan to cut taxes, potentially raising the UK's fiscal deficit," said Mr. Leung. "Further, from the point of view of IACPM members, who manage corporate loan portfolios, the UK government's willingness to use its balance sheet to alleviate the pain of rising energy prices is much less generous for corporations than it is for consumers."

The Credit Outlook Survey is conducted among members of the IACPM, an association of 137 financial institutions in 29 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 high defaults and wider spreads.

About IACPM

The IACPM, with 137 member institutions located in 29 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.