S&P Global Ratings

Regional Credit Conditions Chair

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Credit Conditions EMEA:

Any Cure For The Trade And Brexit Blues?

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Key Takeaways

Overall: The economy has weathered recent shocks quite well. But the Teflon is wearing thin as increasingly nationalistic policies threaten to undermine confidence in global institutions and their ability to cushion systemic shocks. Trade and Brexit are two areas where policy has the potential to create systemic stress.

- **What's changed:** Rising trade tensions engulfing long-standing U.S. allies; stalling Brexit talks; threats to the EU by an Italy-first agenda—all highly distracting for the eurozone ahead of a changing of the guard at the EU Commission and Parliament in 2019.
- **Risks and imbalances:** The risks in Europe are no longer purely external to the region. Nationalistic and populist governments adopting social and economic policies that test EU regulations and solidarity present a key challenge. The financial markets are becoming sensitive to these cues and credit spreads are starting to widen in both developed and emerging markets as the Powell Fed sets a course for higher rates.
- **Macroeconomic conditions:** Eurozone growth remains above trend but momentum is slipping as concerns about trade and the investment climate increase. The Italian economy remains the most vulnerable given its less favorable fundamentals. The fog of Brexit does not help sentiment.
- **Financing conditions:** Credit conditions still remain favorable, supported by the ECB's accommodative monetary policy, particularly in the bank market where lenders have capital to deploy. Even so, credit markets are soft and investors are becoming more selective at the lower end of the rating spectrum. In the U.K., funding conditions appear tighter, mainly reflecting modest appetite for new borrowing by business and households.
- **Sector themes:**

Banks. The outlook bias remains stable and positive, at +7.8%, with 17.2% of EMEA ratings carrying positive outlooks. However, political uncertainty is starting to weigh on debt pricing for banks, primarily in periphery countries where further work to repair balance sheets is required.

Corporates. The European outlook bias remains negligible at -3.5%, with U.K. bias showing a deterioration to -10.8%, which is close to the U.S. level (-10.0%).

Insurance. Western European markets display credit stability thanks to prudent investments, gradual life product shifts, and disciplined underwriting amid tough competitive dynamics and pressures on traditional business models.

Public Finance. Ratings on U.K. entities remain under downward pressure.

Structured Finance. European ratings should continue to see a neutral to positive migration while macroeconomic conditions remain benign.

(Editor's Note: S&P Global Ratings' Credit Conditions Committees meet quarterly to review macroeconomic conditions in each of four regions (Asia-Pacific, Latin America, North America, and Europe, the Middle East, and Africa). Discussions center on identifying credit risks and their potential ratings impact in various asset classes, as well as borrowing and lending trends for businesses and consumers. This commentary reflects views discussed in the EMEA committee on June 25, 2018.)

Contents

Table 1

Top European Risks

Global Trade

Risk level*	Very low	Moderate	Elevated	**High**	Very high	**Risk trend****	Improving	Unchanged	**Worsening**

Growing downside risk of a material escalation in trade tension if the U.S. administration opens a new front against Europe, and the German auto industry in particular, provoking a tit-for-tat response.

Disruptive Brexit

Risk level*	Very low	Moderate	Elevated	**High**	Very high	**Risk trend****	Improving	Unchanged	**Worsening**

The next three-six months will be a critical period in the transition to Brexit, with little evidence of any meeting of the minds over the future relationship within either the U.K.'s political establishment or between the European Commission and the U.K. government.

Asset price volatility

Risk level*	Very low	Moderate	**Elevated**	High	Very high	**Risk trend****	Improving	Unchanged	**Worsening**

There is growing sensitivity in certain European financial markets such as the Italian bond market to adverse developments. For now, the financial market outlook in Europe appears to represent only a moderate systemic risk.

Weakening European political cohesion

Risk level*	Very low	Moderate	**Elevated**	High	Very high	**Risk trend****	Improving	Unchanged	**Worsening**

Recent political developments risk undermining political cohesion between national governments in the EU. The risk comes from more nationalistic and populist governments adopting social and economic policies that challenge EU regulations and solidarity. Immigration from sub-Sahara Africa, a significant concern for many EU citizens, is one highly divisive issue that may yet undermine the principle of free movement of people within the Schengen area. This issue is playing an outsized role in German and Italian domestic politics.

Sources: S&P Global Ratings.

Table 2

Top Middle East and Africa Risks

Dependence on external debt

Risk level*	Very low	Moderate	Elevated	**High**	Very high	**Risk trend****	Improving	Unchanged	**Worsening**

This risk is particularly relevant for Turkish and Qatari banks. The risk for Turkish banks is compounded by uncertainties about policy direction post-elections and the deterioration of the country's relationship with Western allies. For Qatari banks, the risk somewhat receded over the past quarter.

Geopolitical risk

Risk level*	Very low	Moderate	**Elevated**	High	Very high	**Risk trend****	Improving	**Unchanged**	Worsening

This risk is materializing through the reinstatement of sanctions on Iran, the boycott of Qatar by a few Arab states, and internal political developments in Saudi Arabia. Our base case scenario excludes any significant escalation at this stage.

U.S. Federal Reserve interest rate Increase

Risk level*	Very low	**Moderate**	Elevated	High	Very high	**Risk trend****	Improving	**Unchanged**	Worsening

The risk is moderate for GCC banks as we foresee a 15% decline in commercial debt issuance by GCC government in 2018 thanks to higher oil prices and domestic policies implemented over the past three years. For Turkey, the increase in interest rates will weigh on the capacity of banks and corporates to refinance their external debt.

Sources: S&P Global Ratings.

* **Risk levels** may be classified as very low, moderate, elevated, high, or very high, 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.

** **Risk trend** reflects our current view on whether the risk level could increase or decrease over the next twelve-months

Regional credit-conditions

What's changed?

Credit performance across most asset classes in terms of rating actions and the outlook balance has continued to be positive, although cracks are starting to appear. Eurozone growth remains above trend but momentum is slipping. The European Central Bank's first rate increase in years is now firmly on the rating horizon. But the trend toward nationalism and populism in developed economies appears to be gaining critical mass, with a new populist government installed in Rome being the latest example. The seeming Teflon-coated financial markets are starting to pay attention. Volatility has picked up, risk premiums have started to rise, and investment returns are under pressure.

Global trade remains our top risk both globally and regionally. Given the imposition of tariffs by the U.S. administration, and retaliation from target countries, the question now is not whether this risk will materialize but rather how big the economic impact will be. At this stage, we believe the impact on corporate credit will likely be muted overall and unlikely to greatly affect the economies of the two main protagonists, the U.S. and China. However, if the dispute escalates further beyond tariffs on goods, the systemic implications for the global economy could become severe.

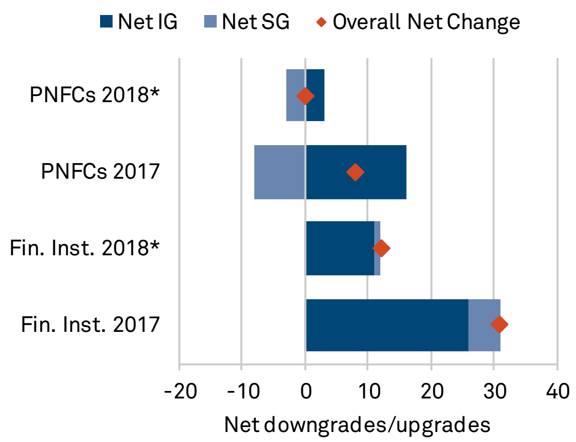
Global trade tensions remain Europe's top risk both globally and regionally. The question now is how big the economic impact will be

Regionally, several risks appear to be worsening. Brexit negotiations are stalling as technical negotiations struggle with the scale and complexity of the task of placing the U.K. at arm's length from the EU before Article 50 takes effect on March 31, 2019. The sensitivity of financial markets to event risk is clearly increasing as we saw when the new Eurosceptic government took office in Italy. We anticipate that their program will test EU orthodoxy, in particular over social and economic policies that challenge EU regulations and solidarity.

These risks will be playing out as quantitative easing (QE) in the eurozone draws to a close, the guard changes in Strasbourg and Brussels in 2019, and a new President takes charge of the ECB from November 2019. Any loss of momentum over key policy initiatives such as the banking or capital markets union could leave the eurozone less resilient in the face of any future economic shocks. Italian banks, for instance, still retain too many nonperforming loans (NPLs) on their balance sheets and sovereign bond exposures are very high compared to their economic capital.

Chart 1

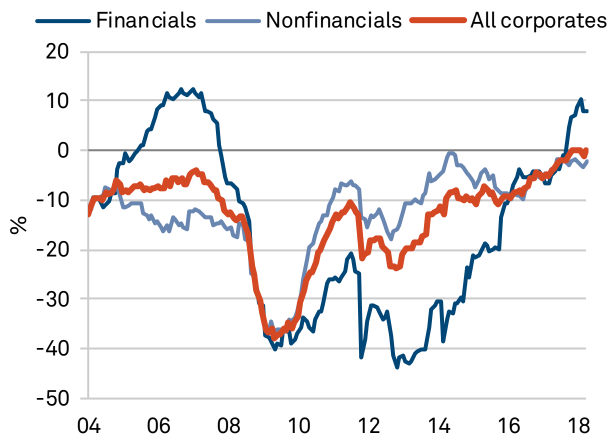
Europe -Positive rating actions dominate in 2018



*Data as of May 2018. PNFCs-Private nonfinancial corporates.
Source: S&P Global Fixed Income Research

Chart 2

European corporate rating bias remains positive



Net ratings bias is positive bias minus negative bias. Source: S&P Global Fixed Income Research

Assessment of key risks in Europe

Global trade - High, worsening

Growing downside risk of a material escalation in trade tension if the U.S. administration opens a new front against Europe, and the German auto industry in particular, provoking a tit-for-tat response. The risk relates more to the implications for the institutional framework governing global trade and undermining business and consumer confidence globally, rather than the specific economic impact of the U.S. applying 20% or 25% tariffs on German car imports.

Disruptive Brexit - High, worsening

The next three to six months will be critical for the transition to Brexit, with little evidence of any meeting of the minds over the future relationship within either the U.K.'s political establishment or between the European Commission and the U.K. government. The scale and complexity of the task and the limited time available are raising the risk of an intemperate breakdown in relations. That could trigger a change of leadership in the U.K.'s governing party and throw wide open the whole Brexit debate, with the not insignificant risk of a disruptive exit even in March 2019. Visible Brexit fatigue in Berlin, Brussels, and other European capitals also signifies limited flexibility on the European side to enable the U.K. government to negotiate a deal very different from Canada's.

Not insignificant risk of a disruptive exit, even in March 2019

Asset price volatility - Elevated, worsening

There is growing sensitivity in certain European financial markets, such as the Italian bond market, to adverse developments. Perhaps the key contributor to the remarkable recent volatility in Italian government security markets has been the failure by domestic banks to step in and support the market. This reflects explicit warnings from the ECB to Italian banks not to get involved (as visible also in the Target 2 data for May), given upcoming measures intended to break the doom loop between domestic banks and their national sovereign.

At this stage, the financial market outlook in Europe appears to represent only a moderate systemic risk. However, we think that downside risks are growing as we approach the end of the ECB's asset purchase programme and as the U.S. Federal Reserve continues to steadily raise interest rates.

Weakening European political cohesion - Elevated, worsening

Recent political developments risk undermining political cohesion among national governments in the EU. The risk comes from more nationalistic and populist governments adopting social and economic policies that challenge EU regulations and solidarity. Immigration from sub-Sahara Africa, a significant concern for many EU citizens, is one highly divisive issue that may yet undermine the principle of free movement of people within the Schengen area. This issue is playing an outsized role in German and Italian domestic politics.

Political and social cohesion is necessary to improve the resilience and responsiveness of the bloc to future economic shocks

Political and social cohesion is necessary to reinvigorate structural reform in the eurozone and to improve the resilience and responsiveness of the bloc to future economic shocks. Fostering stronger growth through productivity improvements, particularly in the periphery countries, remains critical to restore fiscal and monetary space to counter the next cyclical downturn. Strengthening the institutional framework of the eurozone including in the areas of banking union, capital market union, and a common eurozone budget all remain work in progress.

Assessment of key risks in the Middle East and Africa

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Dependence on external debt - High, worsening

Turkish banks' external debt remains high, exposing them to potential shifts in global credit conditions, notably in terms of the rollover and cost of funding. The significant decline in the Turkish lira and the uncertainty related to policy direction post-elections and the deterioration of the country's relationship with Western allies might weigh further on investor sentiment toward Turkey. Moreover, the ongoing U.S. investigation into the large state-owned bank, Halkbank (over allegations of violations of U.S. sanctions against Iran) are not helping. At the end of March 2018, the total external debt of Turkish banks reached $109.2 billion, out of which $42.9 billion have a maturity of less than 12 months. We take comfort from the fact that banks still hold significant foreign currency assets, as we do not rule out a blip in rollover rates.

Outflows of external funds from Qatar started to reverse somewhat in the first quarter of 2018. Total outflows dropped to $10 billion at March 31, 2018, compared with $22 billion at year-end 2017. Nevertheless, the new inflows of funds came primarily from interbank funding, which can prove volatile in case of any escalation of geopolitical risks. The injection of government funds stabilized at $42.2 billion at March 31, 2018.

Post-election policy uncertainty might weigh further on investor sentiment towards Turkey

Mounting geopolitical risk in GCC region - Elevated, unchanged

Despite the recent reinstatement of sanctions on Iran, we still consider the trend for geopolitical risk as stable in the region. Sanctions against Iran, which will be officially reintroduced in August 2018, have already caused significant upward volatility in oil prices, which is beneficial for Gulf Cooperation Council (GCC) countries. At this stage, we do not foresee any direct impact of Iranian sanctions on geopolitical stability in the GCC. The main risk continues to be the boycott of Qatar and any potential escalation, which is not part of our base case scenario.

Impact of Fed rate increase - Moderate, unchanged

For the GCC countries, we think any Fed rate increases will be mirrored by the local authorities to preserve their local currency peg to the U.S. dollar (except for Kuwait), but we do not expect a significant economic impact. We also expect commercial debt issuance of GCC governments to decline by around 15% in 2018 due to higher oil prices and fiscal consolidation measures.

For Turkey, the Fed rate increase will weigh on the capacity of corporates and banks to refinance their external debt. Following the recent restructuring of external debt by Dogus Holding and Yildiz Group (due to high leverage), we do not rule out that other corporates will follow as the refinancing of external debt becomes more difficult and expensive.

Financing conditions

U.K.: Slowing private-sector credit growth from tighter financing conditions and limited corporate demand

Pockets of risk where excess liquidity may be becoming problematic

Financing conditions appear to be tightening somewhat on the supply side for consumer finance while for corporates demand appears more the constraining factor. The latest Bank of England Credit Conditions Survey points to some tightening in the terms and conditions for consumer credit that is weighing a little on supply, although annual growth remains relatively strong at 8.8% (excluding student loans) at the end of April 2018. The availability of unsecured credit has fallen very sharply in first-quarter 2018 as lenders tightened their scoring criteria.

Competition amongst lenders in the household mortgage market remains intense, particularly in the more profitable high loan-to-value segment, partly because the origination of new mortgages has slowed. Even so, the volume of remortgaging is rising, helped by attractive fixed-rate deals. Business borrowing remains subdued (-1.7% year to May 2018) as the fog of Brexit lingers on and expectations that the BoE may start walking interest rates higher in the autumn.

Eurozone: Easy credit fueling pockets of risk

Private-sector credit conditions remain highly borrower-friendly in the eurozone, with credit standards continuing to ease in first-quarter 2018 for bank loans to corporates (see chart 3) and housing loans. Even consumer credit standards eased somewhat. This mainly reflects heightened competition, banks' increasing risk appetite, stronger balance sheets, and an improving economy.

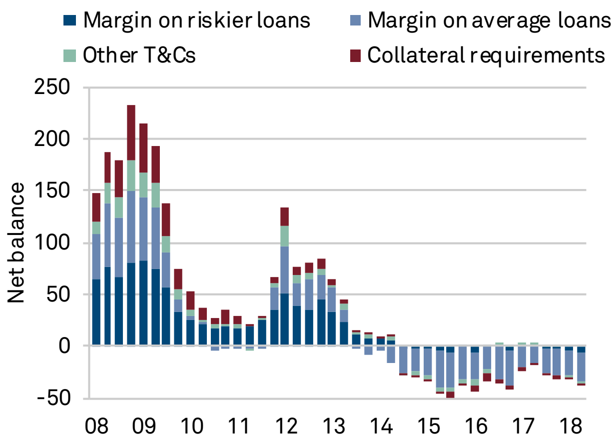
However, there are pockets of risk where excess liquidity may be becoming problematic. First, excess lending capacity in the bank market globally is leading to potential spillovers as cross-border lending picks up. Japanese banks are the largest cross-border lenders, having grown their foreign claims by 72% to $4.2 trillion (end-2017) since the end of 2009. Anecdotally, Chinese banks have also become major liquidity providers.

Closer to home, there are some signs of overheating in certain property markets with a knock-on impact on construction activity. In the Netherlands, for instance, residential property prices are soaring in the four largest cities which, if continued, will drive up mortgage debt as borrowers move or refinance. Supply shortages are also driving a boom in construction as reflected in construction order books standing at, or close to, record levels in the Netherlands, Germany, and Austria.

Thirdly, net demand for financing by corporates is largely supporting investment and acquisition activity (see chart 4). The marked pickup in large debt-funded M&A transactions across the region is quite reminiscent of shareholder behavior seen before the financial crisis in 2006-2008.

Chart 3

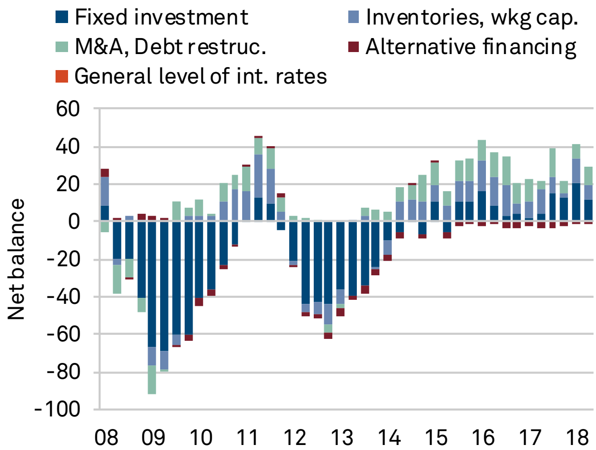
Competition is keeping downward pressure on loan margins



Source: ECB Bank Lending Survey, Thomson Reuters Datastream

Chart 4

Investment and M&A is driving company loan demand



Source: ECB Bank Lending Survey, Thomson Reuters Datastream

Macroeconomic developments and assumptions

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- GDP growth remains solid although growth projections for 2018 and 2019 have been scaled back to 2.1% and 1.8%, still higher than potential growth.
- German domestic demand should provide a cushion against the slowdown in external demand.
- Italy has less favorable fundamentals and is much more vulnerable to a deterioration in the external climate.
- We continue to expect a gradual strengthening of the euro against the US$ in the coming two years on the back of diverging fundamentals.
- Brexit headwinds continue to weigh on the relative growth performance in the U.K. and downside risks are rising as business rolls out preparations for the worst.

Eurozone

What's changed?

Eurozone GDP growth slowed sharply in first-quarter 2018 to 0.4% quarter on quarter versus an average of 0.7% during 2017. The disappointing performance was partly due to transitory factors. Nonetheless, the economy is experiencing an underlying slowdown, with leading indicators indicative of a loss of momentum in the coming quarters. Improving net export contributions generated a growth spurt in 2017, but this effect is somewhat reversing, exacerbated by the lagged effects of currency appreciation. The global trade-sensitive manufacturing sector has slowed sharply, while the rise in oil prices is crimping household real income growth and dampening consumption. Rising uncertainty over various issues is also set to hold back investment, which was also a key contributor to the step-up in growth in 2017.

Key assumptions

In our June forecast update, we reduced our eurozone GDP growth projections for 2018 and 2019 to 2.1% and 1.7%, respectively, which are still higher than potential growth (estimated around 1.0%-1.3%). Although the reversal of the distortions to the first–quarter data will give a small temporary boost to GDP growth in the second quarter, the second half of 2018 should see a continuation of the underlying slowdown. The prospects for exports and investment will be the focal point.

Total investment growth across the eurozone increased from 1.9% in 2014 and 3.0% in 2015 to 4.5% in 2016, before easing back to 3.4% in 2017. Investment intentions have improved in line with strengthening business confidence, and received a further leg up from easier credit conditions. Importantly, various ECB measures to help a resumption of lending to the nonfinancial sector, alongside extremely low rates, have provided an important spark to an improved investment cycle. A solid economic environment and currently high business confidence should support investment in 2018 and 2019. However, the upside may be limited by periodic spikes in political uncertainty and the risk of a global trade war in light of emerging U.S. protectionism.

Key risks

Individual countries' vulnerability to the slowdown varies. In Germany, domestic demand should provide a cushion against the slowdown in external demand, with the labor market in good shape, wage growth picking up, and fiscal policy becoming a bit more stimulatory. It is also less vulnerable to exchange rate swings given strong underlying competitiveness and its exports of higher value-added products, although a deterioration in international trade relations and a broadening of protectionist policies is an obvious downside risk.

Italy, in contrast, has much less favorable fundamentals and is much more vulnerable to deterioration in the external climate, while escalating political risks have led to a pronounced tightening of financial conditions. Previously fast-growing peripheral economies should continue to outperform, but leading indicators also signal a moderation.

Propelled by higher oil prices and base effects, a jump in energy inflation saw the headline rate of inflation rise to 1.9% in May's flash estimate, its highest level in more than a year. Base effects from unprocessed food prices have also contributed. Aside from short-term seasonal volatility, the trend in various core inflation measures has remained broadly flat at around 1%. A pickup is still likely given wage developments in Germany and reduced slack overall, but we continue to expect this to be gradual given limited bargaining power for higher pay in most economies. Business surveys suggest rising input costs are not being passed on to customers through higher prices, suggesting a squeeze on profit margins. In other words, the risk of "second-round effects" from higher commodity prices looks limited. The profit squeeze is an additional potential hindrance to investment.

What to look for over the next quarter

The ECB will maintain an accommodative policy stance, and continue to use forward guidance to push back expectations of future policy rate hikes. Our baseline forecast remains for a first hike in the deposit facility rate in the third quarter of 2019. Meanwhile, we still expect the central bank to end its asset purchase program at the close of this year -- as President Mario Draghi already outlined in the ECB's June conference. The exchange rate is likely to be weaker for longer than we had expected as growth in the U.S. exceeds that in the eurozone, which alleviates one headwind to export performance. We continue to expect a gradual strengthening of the euro exchange rate against the U.S. dollar in the coming two years on the back of diverging fundamentals such as current account balances.

U.K.

What's changed?

The economy slowed in first-quarter 2018, posting quarterly GDP growth of just 0.1%, down from 0.4% in fourth-quarter 2017. While extraordinarily bad weather in the first quarter of this year contributed to the weaker performance, experts differ on the extent. Monthly data available so far for the second quarter, while mixed, still suggests some improvement in growth compared with the first quarter.

Headline labor market numbers continue to paint a positive picture. The unemployment rate continues to hover around 4.2%--the lowest in over 40 years. However, wage growth has not accelerated to a degree that such a tight labor market would suggest. Inflation is now well past its post-Brexit referendum peak and had fallen faster than many market observers had expected, although the recent increase in oil prices will slow that pace now. Still, as a result, growth of real wages turned positive in April, and is set to improve further and to support household spending over the next quarters.

Business investment contracted in the first quarter. While this may partly reflect that businesses are increasingly activating their Brexit contingency plans, the need for replacement investment, not least to catch up with persistent underinvestment since the crisis, means business investment doesn't have to continue contracting, but will likely grow moderately.

Since the U.K. and the EU in March reached a political agreement to a transition period lasting until the end of 2020, Brexit negotiations have all but stalled. The U.K. government remains divided over what kind of Brexit it wants. And where the government announced any plans, the EU has signaled more often than not that it will reject them. This applies in particular to solutions aimed at avoiding a physical border on the island of Ireland--the single most-important stumbling block in the negotiations. As a result, it is unlikely that such progress will be made at the EU council at the end of June, which means that all remaining issues--including that of the Irish border--would be pushed back to the council meeting in mid-October, and maybe even to December (or a special meeting in November). Our base case remains that reason will eventually prevail and expect the transition period to come into force.

Key risks

Should no progress be made during Brexit negotiations in October, there are not many agreeable options left for the U.K. Of course, the worst case would be if domestic political divisions escalate and the government is in even less of a position to negotiate with the EU. In that case the U.K. might involuntarily leave the EU under default World Trade Organization rules, which would be a major negative shock to its economy. A currently unthinkable, second option would be a U.K. U-turn where it would ask the EU to stay in. While the best option in purely economic terms, to support it public opinion would need to shift substantially in favor of remaining. The third and least dramatic option would be for the U.K. to ask for more time. The EU would, in our view, likely concede to avert the worst-case scenario, but only in return for major concessions, especially financial contributions, as the new EU budget starts in 2021 and an extension for the U.K. is currently not factored in. Major financial contributions may not find sufficient support in the U.K., so that option also carries a risk of an abrupt U.K. exit.

What to look for over the next quarter

Notwithstanding Brexit, could there be a robust rebound in economic growth in the second quarter? In May, the BoE skipped the signaled and widely expected rate hike for that month--from 0.5% to 0.75%--on account of softer data, especially GDP. However their assessment of still relatively robust underlying growth had not materially changed. We currently still expect a rebound sufficient to justify a hike in August. Indeed, should GDP growth for the second quarter come in significantly short of the bank's expectations of around 0.4%, with wage growth not improving, the bank could abstain from hiking until the end of the year.

EMEA Emerging Markets

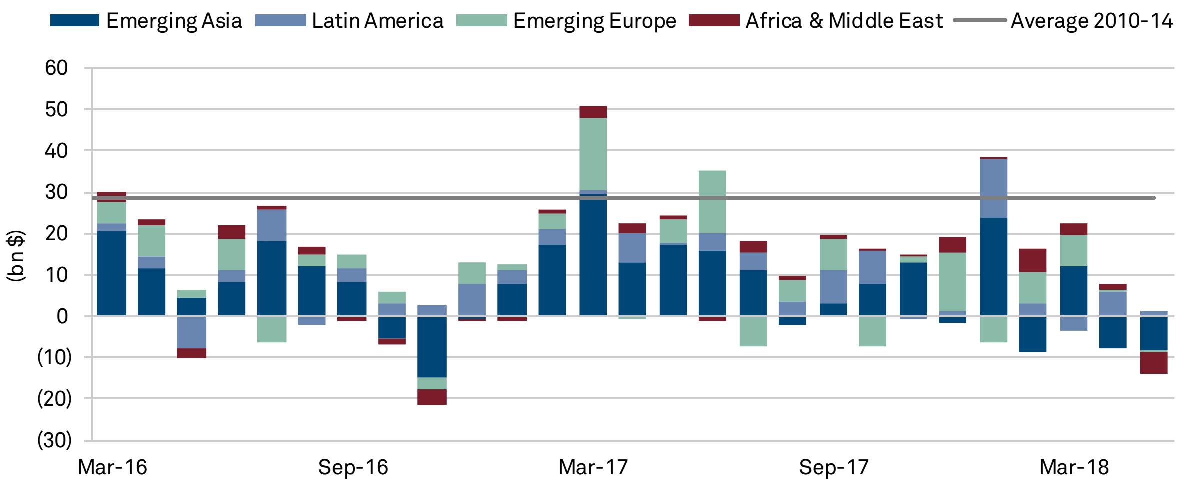
What's changed?

EMEA emerging-market economies are facing a more challenging external environment, against the backdrop of higher U.S. rates, a stronger U.S. dollar, and the escalation of global trade tensions. The outlook for capital flows to emerging markets has worsened, as investors' expectations regarding the U.S. economy have shifted toward stronger growth and higher inflation, and a steeper path for U.S. rates. This narrative also implies a stronger U.S. dollar, at least in the short term. Institute of International Finance (IIF) estimates suggest that a 10% increase in the trade-weighted U.S. dollar would reduce annual net capital inflows to emerging markets by some $95 billion.

Foreign portfolio investors pulled back $300 million in April and $2.3 billion in May out of emerging market debt and equity, based on preliminary IIF estimates (see chart 5). A tentative revival of portfolio flows into emerging markets in the beginning of June was again reversed as the announcement of possible U.S. tariffs on China triggered a renewed wave of trade fears, souring investors' sentiment. Across major EMEA emerging markets in the second quarter, currencies weakened and bond yields rose (see charts 6 and 7).

Chart 5

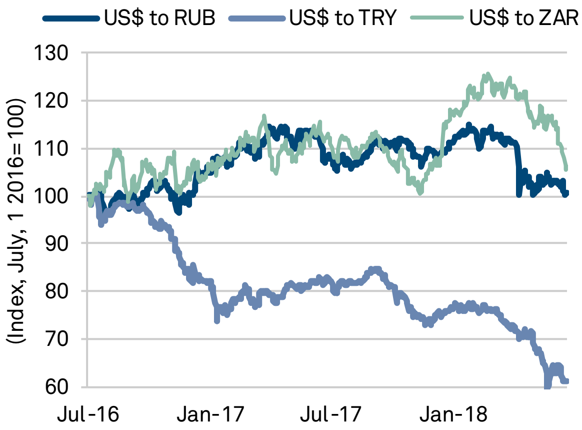
Net Non-Resident Portfolio Flows to Emerging Markets



Source: IIF, S&P Global Ratings calculations

Chart 6

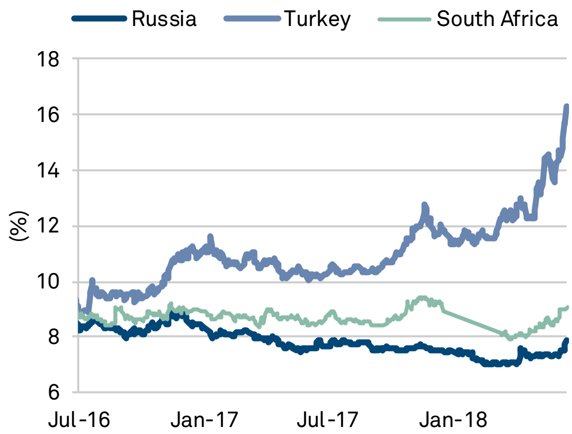
U.S. Dollar Foreign Exchange Rates



Source: Thomson Reuters Datastream, S&P Global Ratings

Chart 7

Ten-Year Government Bond Yields (Local Currency)



Source: Thomson Reuters Datastream, S&P Global Ratings

Emerging-market economies with weak macro fundamentals have been hit particularly hard during the recent stress episode, and remain vulnerable to further worsening of external financing conditions.

Turkey

Turkey's economy stands out as the most exposed in EMEA, due to its large current account deficit and significant external financing needs. In our view, the inflation, external, and fiscal outlook for Turkey's overheating, credit-fueled economy have worsened, and the risks of a hard landing have increased[1]. Reflecting investors' concerns about domestic policies that propel growth but lead to widening macroeconomic imbalances, the Turkish lira has lost about 15% of its value since end-March, while 10-year local currency bond yields jumped by more than 400 basis points (bps) over the period (see charts 6 and 7).

Severe currency pressures prompted Turkey's central bank to sharply hike interest rates, raising the average cost of funding by a cumulative 500 bps over April-June, to 17.75%, which has brought real interest rates into positive territory. The central bank has also reactivated the one-week repo rate as the key policy rate. If accompanied by a gradual withdrawal of various stimulus measures, this could lead to a narrowing of internal and external imbalances, with GDP growth falling from currently elevated levels (above 7%) to more sustainable 3%-4%. In the aftermath of June 24th parliamentary and presidential elections, a key question is whether the government will indeed return to more prudent economic policies or continues to stimulate the overheating economy, which is likely to lead to further widening of internal and external imbalances and raise the risk of a hard landing.

South Africa

In South Africa, the recent turmoil has largely reversed gains in currency and bond markets in the aftermath of political transition. The South African rand and 10-year local currency bond yields have returned to their mid-December levels (see charts 6 and 7). A disappointing first-quarter GDP report, showing that the economy contracted by an annualized 2.2% in the first quarter from the previous quarter, has played into investors' concerns about South Africa's poor growth track record, which weighs on its fiscal position. Some temporary factors can partially explain the first-quarter weakness, and we expect a rebound in the coming quarters, with GDP growth close to 2% in

[1] Research Update: Turkey Ratings Lowered On Deteriorating External Performance and Higher Inflation; Outlook Stable, May 1, 2018

2018. More fundamentally, the country's growth prospects remain dependent on the implementation of key economic and social reforms[2].

Russia

We expect Russia's economic expansion to continue at a modest pace of below 2% over the next few years. We have made some downward adjustments to our 2018 growth forecast, due to tighter financial conditions, which largely reflect the impact of the new round of U.S. sanctions announced in early April. The sanctions led to short-term market turmoil, and while the situation stabilized quickly, the risk premium on Russian assets has risen. In addition, sanction-related risks have prompted the central bank to put its easing cycle on hold, despite low inflation which is running at 2.4%, well below the 4% target. The central bank is also concerned about the inflationary impact of the government proposal to raise the VAT next year, to 20% from current 18%. We now expect only one rate cut this year, bringing the key rate to 7% by year-end.

The Russian ruble weakened by 10% over the past three months, despite the rise in oil prices. We see this as a welcome development, which would support the price competitiveness of domestic goods and partially offset the impact of tighter credit conditions.

The Russian government has announced plans to raise the pensionable age for men and women, which can boost labor supply, while also freeing budget resources that can be reoriented to growth-enhancing spending such as infrastructure and human capital. Indeed, new presidential decrees have outlined health care, education, and infrastructure as spending priorities for the next six years, which can raise productivity and trend growth. At the same time, the impact is likely to be modest in the absence of broader structural reforms. A further tightening of sanctions remains a key downside risk.

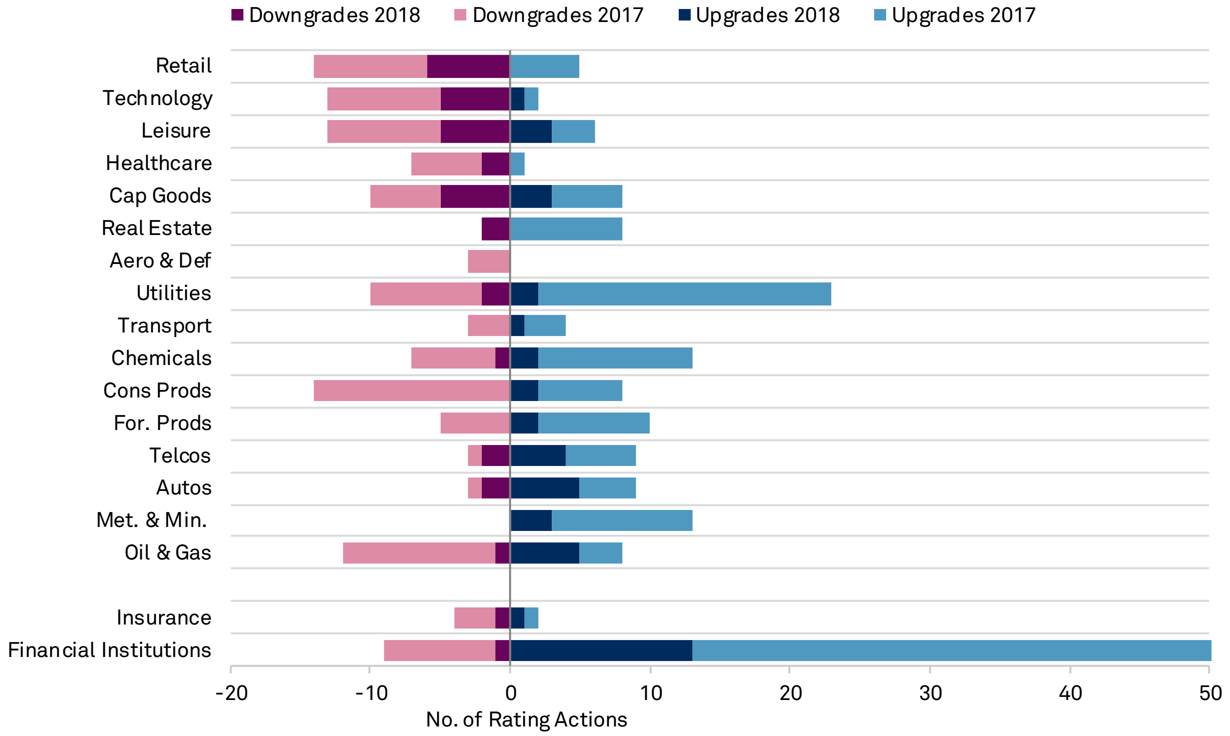
[2] Research Update: South Africa Foreign And Local Currency Ratings Affirmed At 'BB' And 'BB+'; Outlook Stable, May 25, 2018

Sector themes

- Nonfinancial corporate rating actions in 2018 are very balanced, although notably negative in retail and technology and positive in commodity related sectors.
- The ratings outlook bias for nonfinancial corporates remains close to flat. Little changed from March 2018.
- For banks, the outlook bias remains largely positive, with 17% of EMEA ratings carrying positive outlooks. Moderate economic momentum should help banks to maintain sound or improving balance sheets, and offer modest support to revenues.

Chart 8

European 2017-2018 Corporate Ratings Rating Actions by Sector



Source: S&P Global Ratings, S&P Global Fixed Income Research. Data as of May 31, 2018.

Table 3

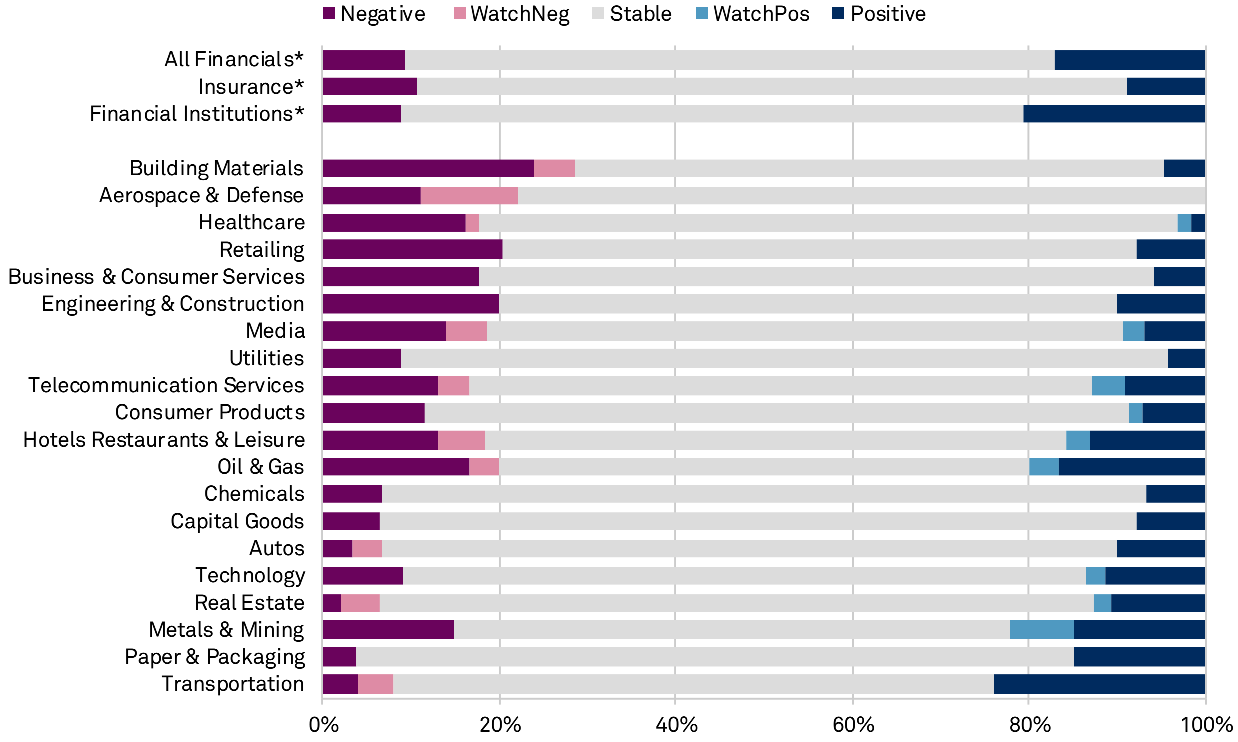
European Non-Financial Corporate Net Outlook Bias by Industry

	No. of Entities	Q4 12	Q4 13	Q4 14	Q4 15	Q4 16	Q4 17	Q1 18	Q2 18
Building Materials	21	-9.1	-15.4	+23.5	+5.3	+4.8	-21.7	-27.3	-23.8
Aerospace & Defense	9	+20.0	+14.3	-12.5	-12.5	-37.5	-30.0	-30.0	-22.2
Healthcare	62	+0.0	+4.2	-3.0	-4.3	-5.4	-15.3	-18.6	-14.5
Retailing	64	-13.6	-4.0	+0.0	-12.2	-2.0	-10.7	-12.5	-12.5
Business & Consumer Services	85	+0.0	+8.8	+0.0	+1.8	+0.0	-9.9	-4.2	-11.8
Engineering & Construction	10	-33.3	-20.0	+12.5	-25.0	-22.2	-45.5	-45.5	-10.0
Media	43	+0.0	+5.3	+0.0	-3.4	+2.9	-17.1	-11.4	-9.3
Utilities	91	-25.4	-17.1	-5.4	+0.0	-8.0	-9.9	-10.1	-4.4
Telecommunication Services	54	+0.0	-10.5	-9.3	+6.1	+5.9	+1.9	-1.9	-3.7
Consumer Products	69	-8.3	-6.7	-6.1	-5.9	+0.0	+0.0	-1.6	-2.9
Hotels Restaurants & Leisure	38	-15.4	-5.6	+13.6	-10.7	+2.8	+0.0	+2.4	-2.6
Chemicals	45	+0.0	-3.8	-9.7	-19.4	-11.8	-9.1	-9.1	+0.0
Oil & Gas	30	-22.7	+3.8	-24.1	-55.2	-48.4	-16.1	+0.0	+0.0
Capital Goods	63	+3.8	-2.8	-7.0	-17.0	-25.0	-1.9	+0.0	+1.6
Autos	30	+21.1	+9.5	-4.0	-7.4	+6.9	+21.4	+10.3	+3.3
Technology	44	-9.1	-8.3	+5.3	+0.0	+0.0	+8.5	+7.1	+4.5
Real Estate	47	-6.3	+9.1	+4.0	-9.7	+5.9	+9.8	+4.9	+6.4
Metals & Mining	27	-58.8	-55.6	-19.0	-45.0	-4.3	+12.0	+4.0	+7.4
Paper & Packaging	27	-7.1	-6.3	-11.8	-4.5	+23.1	+12.0	+16.7	+11.1
Transportation	25	-21.1	-13.6	-6.9	-11.8	-22.9	+8.6	+11.4	+16.0
Western Europe	**884**	**-12.1**	**-6.8**	**-4.2**	**-9.1**	**-5.6**	**-4.5**	**-4.3**	**-3.5**

Source: S&P Global Economics

Chart 9

European Corporate Ratings Bias Distribution by Sector



Source: S&P Global Ratings, S&P Global Fixed Income Research. Data as of May 31, 2018. *--excludes developing outlook or Watch placements

Banks

- Our outlook bias remains largely positive, with 17% of EMEA ratings carrying positive outlooks.
- Moderate economic momentum should help banks to maintain sound or improving balance sheets, and offer modest support to revenues.
- Systemic banks will continue to build their bail-in buffers, improving protection for senior creditors if they fail.
- We acknowledge, however, that political risks have risen and that increased political uncertainty is being translated into the debt prices of banks, primarily in periphery countries.
- In addition to the persistence of political uncertainty, a disruptive Brexit and an abrupt correction of market prices are the main risks to our base case scenario.

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What's changed?

Political uncertainty has increased. Italy just announced the formation of a new coalition government, which has still to define its economic and fiscal policies. A new minority government also just took office in Spain, after a no-confidence vote against the prior president and ruling party. There are no signs of progress in Brexit negotiations.

Risk premiums for banks on the eurozone's periphery widened because of increased political uncertainty in Italy and expectations of the ECB ending asset purchases by the year-end, which was duly confirmed. Weaker investor confidence could in the short term delay banks' issuance of minimum requirement for own funds and eligible liabilities (MREL) or make it more expensive than initially planned. In the longer run, a prolonged period of weak investor confidence could undermine banks' ongoing recovery, particularly in Italy.

We took diverging rating decisions in two major cases involving bank restructurings. We upgraded the core operating entities of the Royal Bank of Scotland group and assigned positive outlooks reflecting our views about the bank's restructuring progress, but downgraded Deutsche Bank for the opposite reason: the need for a longer and deeper business model restructuring than originally envisaged, which entails execution risks and that would make it underperform peers, many of which have now finished restructuring.

Some large European banks started to disclose their MREL requirements, which we view as a positive development supporting transparency and investors in making better informed decisions.

Public news suggested the European Council has proposed to exclude banks under €100 billion in assets from needing to meet MREL requirements with subordinated instruments. The final aim seems to be to make the buildup of MREL buffers more affordable for midsize banks. We feel, however, that any bail-in exercise may prove more difficult in such cases. Banks' ratings would unlikely benefit from ratings uplift if buffers primarily comprise senior obligations, and the cost of these senior MREL buffers may not be that much cheaper as investors will incorporate into their pricing the likelihood of senior debt absorbing losses in resolution.

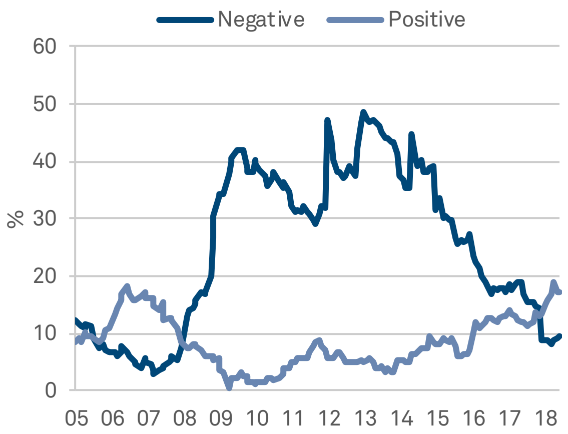
We started assigning Resolution Counterparty Ratings (RCRs) to European banks, which we expect to be subject to an effective bail-in resolution if they reach the point of non-viability. Our aim is to reflect that certain banks' liabilities will be excluded from bail-in as part of a resolution and therefore have a lower default risk than traditional senior obligations. We have generally set up the RCRs at one notch above the banks' issuer credit ratings.

Key assumptions

- Economic conditions will remain supportive.
- Brexit will not be disruptive.
- The ECB shift toward tightening monetary policy will be gradual, allowing banks time to adjust.
- Resolution authorities and banks will continue to enhance bank resolvability, strengthening the safety net for senior creditors if a systemic bank fails.

Chart 10

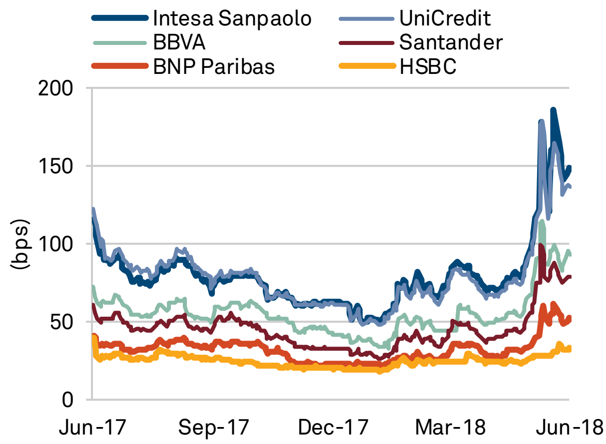
European financials' net rating bias remains positive



Parents only. Excludes entities on Developing outlook or CreditWatch.
Source: S&P Global Fixed Income Research. Data as of May 31, 2018

Chart 11

Recent evolution of five-year CDS pricing for selected banks



Source: Bloomberg

Key risks

A reversal of the current economic momentum, which would challenge our expectations of benign asset quality and slow the ongoing reduction of legacy problematic assets in the periphery would complicate the repositioning of banks' business models, including those that have not completed restructuring, and could stagnate banks' profitability at very low levels, weakening investor confidence in banks.

A disorderly Brexit would be damaging for the U.K. economy, and thus a difficult scenario for U.K. banks to manage. But, regulatory uncertainty post-Brexit, particularly about the reciprocal recognition of legal frameworks and enforceability of judgments, could also have implications for continental European banks, primarily regarding cross-border financing, derivative contracts, and the eligibility of debt instruments issued under English law for capital/MREL purposes.

An abrupt correction of market prices in the fixed-income markets would likely put more pressure on weaker players and banking systems. A sudden and meaningful repricing of risk could push up banks' funding costs, squeeze margins and profits, hit capital through the mark to market of securities portfolios, reduce and make lending more expensive, and constrain the access of weaker players to market financing.

What we will be monitoring over the next quarter

- Policy direction of the new government in Italy. For Italian banks to continue repairing their balance sheets--a process far from being completed--continued economic growth and investor confidence will need to be preserved. We await more details about the new government's economic and fiscal plans to assess their impact on the country's creditworthiness, economy, and banks.
- Market response to the ECB's announced reduction of monetary stimulus.
- Developments on the resolution front. Individually, we will monitor whether more banks make public their MREL requirements and plans to fulfill them, so we can assess whether they should be eligible for some rating uplift in the future. And, more generally, we will monitor:

  1. Any amendments to local insolvency and resolution frameworks to incorporate senior non-preferred debt as a new liability class.

  2. Any clarification by authorities on a number of topics, including the extension of moratorium powers in resolution, authorities' stance regarding the sale of MREL instruments to retail investors, guidelines on MREL downstreaming to subsidiaries, the possibility of extending deposit preference to noninsured deposits, and arrangements to ensure entities have access to the funding needed in resolution.

Non-Financial Corporates

- The corporate credit outlook remains quite stable under our base case rating assumptions.
- Particular sector challenges that we observe mainly relate to rising commodity prices, the disruption to operating models, and a changing competitive landscape.
- Trade and Brexit are two key risks with potential for systemic impact. Commodity price inflation, investment, M&A, and excessive leverage are additional risks we are tracking.

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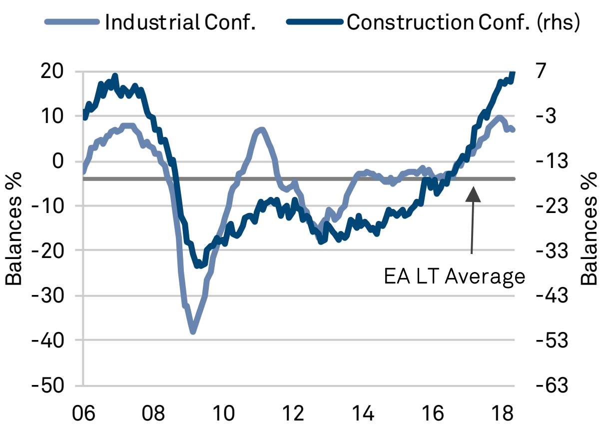
What's changed?

We expect a moderate rebound in the European economy for the rest of 2018 to support corporate credit quality. This base case assumption is reflected in stable outlooks across most nonfinancial corporate sectors we track. Particular sector challenges that we observe mainly involve rising commodity prices, the disruption to operating models, or a changing competitive landscape. So far, headline risks relating to trade and Brexit have had limited real impact, although both could have systemic implications if not resolved in a mutually advantageous and timely manner.

Chart 12

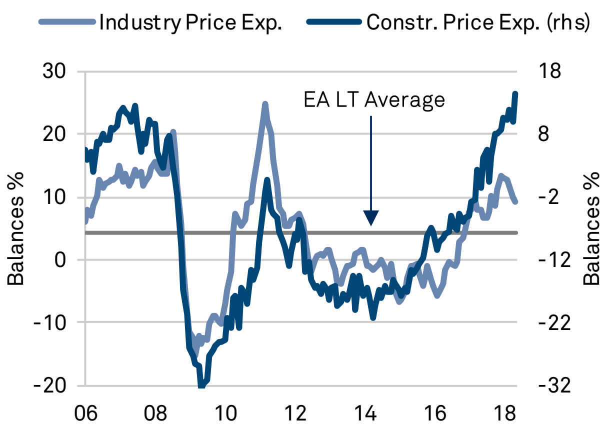
Eurozone Confidence Indicators Close to Record Highs



Source: Thomson Reuters Datastream

Chart 13

Eurozone Selling Price Expectations Well Above LT Average



Source: Thomson Reuters Datastream

Key assumptions

Some sectors with positive, or positive to stable, outlooks are upstream commodity-based sectors such as oil & gas where we expect solid free cash flow generation after years of cutting costs and discretionary capital expenditure (capex), or forest products where strong demand provides paper producers pricing power to protect margins even as cost pressures build. Ironically, downstream steel producers should experience some beneficial tailwind in tariff-affected areas. The unregulated utility sector, also with positive to stable outlooks, benefits from a focus on derisking portfolios (reduced exposure to merchant risk, growth in renewables, improving plant efficiencies, and continued cost discipline).

More negatively, we expect credit quality to come under some pressure in sectors such as pharma where there is continued price pressure in certain therapeutic categories and (plastic) packaging where many companies are struggling to pass resin price increases through to customers. Consumer-facing sectors also continue to face structural change and increasingly that includes food as well as nonfood retail, particularly where suppliers are no longer prepared to absorb price inflation. Fast-moving consumer goods companies are focused on improving organic growth, which is subdued, by refining their product portfolios and being innovative.

Elsewhere, we also anticipate continued headwinds in the media sector where advertising agencies are exposed to digital disruption and disintermediation in a highly competitive environment, while traditional broadcasters' business models increasingly require investment in new content development and new digital distribution channels.

Key risks

We have listed two systemic risks in our regional risk table:

- **Disruptive Brexit:** An increased but still fairly low probability but high impact for certain nonfinancial corporate sectors if it were to occur in March 2019. Any lack of regulatory alignment would be disruptive for the airline, pharmaceutical, and chemical industries. Weakness in sterling would feed into inflation pressures, risking higher interest rates and further depressing domestic economic activity. U.K. real estate would see downward pressure on commercial property valuations, especially for prime assets in London.
- **Trade disruption:** A further material escalation in global trade tensions could create a weaker economic environment if business confidence became impaired. This would be damaging for the shipping industry, for instance. Also, any material slowdown in China's industrial expansion resulting, perhaps, from tougher restrictions on heavily polluting industries, could have a similar effect on the bulk shipping segment given the heavy investment in new vessels to service China's economic expansion.

  Other more specific corporate risks that we will continue to monitor include:
- **Commodity price inflation:** A concern for certain (competitive) industries such as autos and building materials is the ability to pass through higher costs to protect margins. Looming on the horizon is the new global cap on sulfur content in marine fuels from Jan. 1, 2020. The ramifications for the oil market and refining could be significant.
- **Investment:** Significant investment is being made in certain industries subject to technological and business model disruption. The risk here is that the investment may not prove to be successful and investment returns may not reach their intended levels. These sectors include auto original equipment manufacturers and suppliers, consumer goods and utilities.
- **M&A:** Financing conditions are highly favorable for large debt-funded acquisitions with potential negative rating implications depending on the strategic fit of the businesses, capital structure, cashflow generation and the quality of integration over the rating horizon. Pharma, chemicals, telcos, and (unregulated) utilities are all exposed to this risk.
- **Excessive leverage:** A growing concern as the credit cycle matures in Europe is weak or vulnerable companies with high debt levels generating little free operating cash flow and exhibiting minimal growth. Refinancing could become a real challenge particularly when funding costs start to rise. Weaker companies operating in the chemicals, capital goods, business services, and retail sectors, among others, are being monitored.

What to look for over the next quarter

Brexit: Uncertainty builds given lack of progress in Brexit negotiations, with no clarity even on whether the withdrawal agreement and transition will be agreed before the U.K. leaves the EU at the end of March 2019. We view the risk as elevated and worsening. The implication is that companies will increasingly roll out their backstop contingency plans. This comes at a cost to companies and the wider economy in terms of growth, investment, and jobs.

Italy: Political developments appear to be supportive for corporate credit in the short term as potential expansionary fiscal measures could provide a boost to growth. In the medium term, questions about its sustainability will arise that could undermine business confidence and investment, particularly if a rising political risk premium caused financing conditions to tighten.

Oil prices: Recent price increases reflect ongoing OPEC production cuts, supply disruptions, and temporary production declines, as well as positive market sentiment about demand. However, we assume these specific supply issues will be addressed during the next several months, with OPEC currently contemplating partially reversing their output cuts. We expect global supply to broadly match demand in the second half of 2018, so prices could consolidate around these levels barring any further unexpected supply disruptions.

Insurance

- Western European markets display credit stability thanks to prudent investments, gradual life product shifts, and disciplined underwriting amid tough competitive dynamics and pressures on traditional business models.
- Emerging-market credit quality remains more volatile than Western Europe's due to high correlation to sovereign risk, as well as economic and political uncertainties.
- Despite strong credit fundamentals, business conditions remain weak for reinsurers who will struggle to generate the returns of the past, due to still pressured pricing conditions in 2018 despite severe catastrophe losses in 2017.

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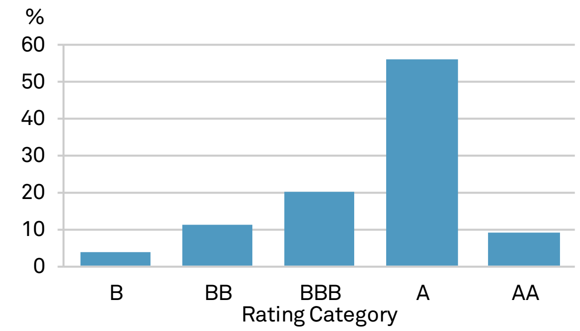
What's changed?

Life insurance players continue their efforts to shift product offerings toward less interest-rate-sensitive products. Most insurers execute such transformation organically by closing older product ranges and orienting premium collection toward new products. However, headline M&A moves underline insurers' willingness to drastically reduce their dependence in interest rates. Examples are AXA's IPO of its U.S. activities and acquisition of XL, and the reduction of its exposure in the Swiss pension market. Evidence is also Standard Life's disposal of its insurance business.

At the same time, managing the digital transformation attracts increasing attention from insurers. While the lack of prominent pure players shelters the sector from severe short-term disruption, insurers increasingly embed digitalization in their product offering and client interface platforms, and take interest in startups to face such emerging risk.

Chart 14

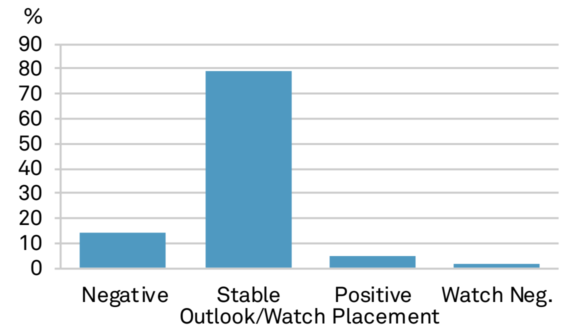
Rating distribution for the EMEA insurance sector



Source: S&P Global Market Intelligence, S&P Global Ratings

Chart 15

Outlook distribution for the EMEA insurance sector



Source: S&P Global Market Intelligence, S&P Global Ratings

Key assumptions

- Gradual interest rate increases over the next two years.
- Disciplined pricing despite pressure on prices in most Western European personal and commercial lines and property/casualty markets, with mostly moderate price increase expectations across Europe (0% to 3%).
- Pressured pricing in reinsurance, with an expectation for a 0% to 5% increase in 2018.

Key risks

- Asset price volatility
- Low interest rates

What to look for over the next quarter

The ending of QE by the ECB could negatively affect asset prices and therefore asset allocations, as the prospect of rising interest rates could prompt insurers to sell parts of their bond portfolios. We expect such risk to remain marginal as we believe insurers will prefer tight long-term asset-liability management. While the prospects for increasing interest rates are likely to ease the pressure on earnings, we expect life insurers to continue their efforts to move their product offering to less-interest-sensitive products.

International Public Finance

- Ratings on U.K. public-sector entities remain under downward pressure.
- The election in Catalonia has not materially affected relations with the central government; the economic recovery and liquidity support from the central government is giving Spanish regions a lift.
- Changes in tax and pension systems as well as new spending mandates will unlikely materially affect Russian regions.

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What's changed?

We're observing rising financial pressure on various U.K. public-sector entities due to limited revenue sources, combined with rising inflation. Brexit is adding uncertainty to their financial plans.

Local governments continue to use reserves to balance their budgets, since additional council taxes are failing to offset cuts in central government grants. Despite an overall weakening of the local government's budgetary performance, we still view the substantial mismatch of revenues and expenditures in Northamptonshire as an isolated case and driven by relatively weak financial management.

We understand the U.K. government would like to encourage local councils and social housing entities to boost social housing construction. We expect the U.K. social housing sector will increase capital spending with additional borrowings. We also observe a rising dependence on proceeds from market sales as a source of funding for social housing development. To a large extent, these revenues make up for reduced grants and constrained social rents. Now, sizable development for sale is becoming a core business for many social housing providers, while previously this strategy was pursued mostly by large London-based entities to offset temporary funding gaps. A price correction and delays in transactions in case of real estate market stress may erode their liquidity positions and delay the implementation of development projects.

U.K. universities are entering into a period of potential turbulence due to a number of external factors, which in our opinion could result in the erosion of their competitiveness and financial performance. We expect that most U.K. universities will in some way experience pressure on their operating margins due to constraints on fees paid by U.K. undergraduates and rising staff costs, including pension contributions. The potential effects of Brexit still remain to be seen, though it may reduce the U.K.'s attractiveness to international students and academics. While we believe that the sector itself will remain resilient, we expect that top-tier universities will be able to withstand these pressures better than the rest of the sector.

On May 14, 2018, the Catalan parliament elected Mr. Quim Torra to the presidency of the Catalan government, following the initial elections of Dec. 21, 2017, but we expect political confrontation with the central government to persist for a prolonged period.

We believe the future is looking brighter for most other Spanish regions. Around half of the 11 regions that we rate have a positive outlook, while seven have been upgraded in the past year. The improvement in creditworthiness primarily reflects our forecasts for better budgetary performances, which largely hinge on the currently supportive economic conditions for the country. Spain's GDP in real terms has risen by 3.2% over 2016-2017 and we expect growth of 2.8% this year. In this economic climate, we believe 2018 could mark a turning point after 10 years of surging Spanish regional debt since the financial crisis.

The Russian president and the federal government have recently announced a string of changes in tax and pension systems, as well as new spending mandates mostly in health care, education, and infrastructure. Although the full impact on Russian local and regional governments (LRGs) remains to be seen, we believe the new measures will tarnish their financial performance only marginally, if at all. The government plans to raise the VAT rate, which is entirely allocated into the federal budget, adjust the tax regime of the oil & gas industry, gradually raise the state pension age, and increase spending on capital investment in areas that are predominantly the responsibility of the federal government. If LRGs are involved, for example in road building and maintenance, or health and child care infrastructure, we think the federal government will likely provide earmarked grants.

Structured Finance

- Solvency II revisions mark a significant change in securitization regulation.
- Issuance is on an upward trend, given improving regulatory visibility.
- Benign credit performance looks set to continue for now.

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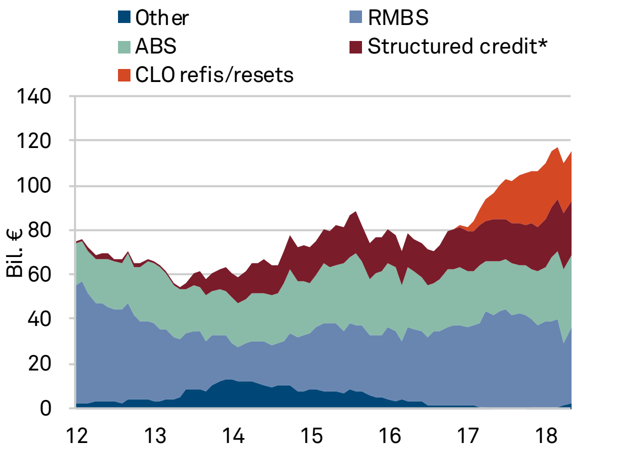
What's changed?

During the second quarter, the European Commission adopted revisions to the Solvency II framework for determining capital charges on EU insurers' securitization exposures. This could prove a significant development for the sector, as onerous requirements under the current framework have seen insurers largely withdraw from the market since 2016. The revisions will lead to lower charges for transactions that qualify for the "simple, transparent, and standardized" (STS) label under Europe's new Securitization Regulation from January 2019.

Chart 16

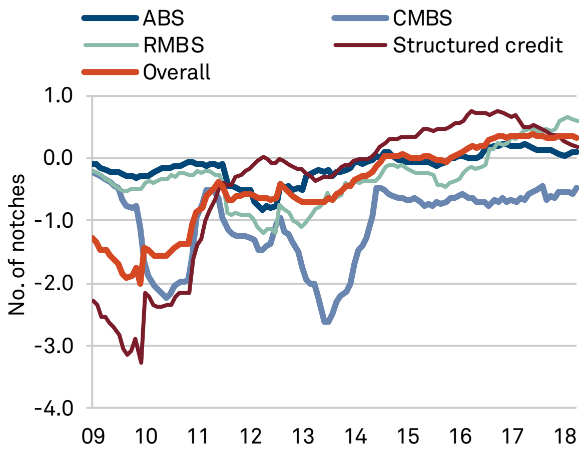
European structured finance issuance, 12-month trailing



* Predominantly leveraged loan CLOs, but includes some other transaction types, e.g. those backed by loans to small- and midsize enterprises (SMEs).
Source: S&P Global Fixed Income Research; LCD, an offering of S&P Global Market Intelligence.

Chart 17

Average change in credit quality, 12-month trailing



Source: S&P Global Fixed Income Research

Key assumptions

We expect that greater certainty over the regulatory environment for securitizations generally should prove supportive for investor demand and therefore originators' credit conditions in the medium term. Also, as European monetary policy begins to normalize, we expect that the floating-rate nature of most securitizations could make the asset class appealing to an increasing number of fixed-income investors, supporting volume growth (see chart 15). Rising demand could be matched by rising supply. In particular, the end of new drawdowns under the BoE's Term Funding Scheme earlier in the year (and, similarly, the ECB's targeted longer-term refinancing operations in 2017) could mean that bank originators begin to return to securitization as a funding tool, after years of declining activity. In terms of credit performance, our forecast of a benign macroeconomic environment suggests that we should continue to see neutral to positive ratings migration across our European structured finance ratings universe (see chart 16).

Key risks

In terms of credit performance, our structured finance ratings may be susceptible to a widespread impact from an idiosyncratic event, such as a rating action on a widely used financial counterparty. An upside example of this effect was in European residential mortgage-backed securities through 2017, where we raised around one-third of our ratings due to our assessment of reduced country and counterparty risk (and associated upgrades) on just two sovereigns and a single bank counterparty.

What to look for over the next quarter

Over the next quarter, we will continue to monitor implementation of the new EU securitization regulation, as regulators interpret the legislative text and finalize several technical standards and guidelines. We will also watch for signs of a more significant re-emergence of bank-originated securitization, although suspect that other forms of funding--especially MREL-related issuance--could take precedence. Finally, we will watch for any credit market response to the ECB's tapering of its asset purchase program and the extent to which any changes in spreads may cause a shift in the securitization investor base and therefore in credit conditions for originators.

Related Research

- Economic Research: Monetary Policy Normalization In The Eurozone: Will One Size Fit All? Jun. 26, 2018
- Italian Banks Need Economic Stability To Recover, But Still Face Market Turbulence, Jun. 11, 2018
- 2017 Annual Global Structured Finance Default Study And Rating Transitions, May 25, 2018
- In the firing line: Trump, trade and EU corporate credit, May 1, 2018
- The Resolution Story For Europe's Banks: The Clock Is Ticking, Apr. 25, 2018
- The potential impact of higher wage settlements on Germany’s trade balance, April 24, 2018
- Economic Research: the U.S. economic outlook is solid, but will trade tensions have the U.S. trading places soon?, March 29, 2018
- Global trade at a crossroads: if U.S. tariffs trigger a trade war with china, corporate credit will suffer, March 24, 2018
- Economic research: what will be the likely impact of U.S. steel and aluminum tariffs on Latin America?, March 20, 2018

Only a rating committee may determine a rating action and this report does not constitute a rating action.

Appendix: Ratings trends and surveys

Table 4

European Corporate Credit Conditions Survey – June 2018

Sector / Question	1. Current Business Conditions	2. Business Outlook Over Next 12 Months	3. Free Operating Cash Flow Over Next 12 Months	4. Capital Expenditure Over Next 12 Months	5. Sector Outlook Over Next 12 Months
Consumer Goods	Satisfactory	No change	No Change	No Change	Stable to Negative
Media	Satisfactory	No change	No Change	No Change	Stable to Negative
Packaging	Satisfactory	Moderately weaker	No Change	No Change	Stable to Negative
Pharma & Healthcare	Satisfactory	Moderately stronger	No Change	No Change	Stable to Negative
Retail	Weak	Weaker	Decrease	Increase	Stable to Negative
Aerospace & Defense	Satisfactory	No change	No Change	No Change	Stable
Autos – Manufacturers	Satisfactory	No change	No Change	No Change	Stable
Autos – Suppliers	Satisfactory	No change	No Change	No Change	Stable
Building Materials	Satisfactory	No change	No Change	No Change	Stable
Capital Goods	Satisfactory	No change	No Change	No Change	Stable
Chemicals	Satisfactory	No change	Increase	Decrease	Stable
Leisure	Satisfactory	No change	No Change	No Change	Stable
Oil & Gas - Downstream	Satisfactory	No change	No Change	No Change	Stable
Real Estate	Satisfactory	No change	No Change	No Change	Stable
Service Companies	Satisfactory	Moderately stronger	No Change	No Change	Stable
Technology	Satisfactory	No change	No Change	No Change	Stable
Telecoms – HY	Satisfactory	No change	No Change	No Change	Stable
Telecoms – IG	Satisfactory	No change	No Change	No Change	Stable
Transp. Infra. – Airports	Satisfactory	No change	No Change	No Change	Stable
Transp. Infra. - Rail	Satisfactory	No change	No Change	No Change	Stable
Transp. Infra. - Toll Roads	Satisfactory	No change	No Change	No Change	Stable
Transportation – Airlines	Satisfactory	No change	No Change	No Change	Stable
Transportation – Shipping	Satisfactory	No change	No Change	No Change	Stable
Utilities - Regulated	Satisfactory	Moderately weaker	No Change	No Change	Stable
Mining	Strong	No change	No Change	No Change	Positive to Stable
Oil & Gas - Upstream	Strong	Moderately stronger	Increase	No Change	Positive to Stable
Steel	Strong	No change	No Change	No Change	Positive to Stable
Utilities - Unreg. Power & Gas	Satisfactory	Moderately stronger	No Change	No Change	Positive to Stable
Forest Products	Satisfactory	No change	Increase	Decrease	Positive

S&P Ratings Services - European Corporate Credit Conditions Survey Questions

Change indicators

Weaker since March 2018

Stronger since March 2018

Question	Definitions
1. Current Business Conditions	Very strong/very weak = sharply above/below conditions unusual; Strong/weak = above/below average conditions
2. Business Outlook Over Next 12 Months	Stronger/weaker = more than 5% improvement/deterioration; Moderately stronger/weaker = up to 5% improvement/deterioration
3. Free Operating Cash Flow Over Next 12 Months	Substantial increase/decrease unusual for the industry historically; Increase/decrease
4. Capital Expenditure Over Next 12 Months	Substantial increase/decrease unusual for the industry historically; Increase/decrease
5. Sector Outlook Over Next 12 Months	Positive/negative = material number of potential upgrades/downgrades; Positive to stable /negative to stable = modest number of potential rating and outlook changes

Source: S&P Global Ratings
S&P Ratings Services' corporate analysts are surveyed quarterly as part of the S&P Credit Conditions Committee process

spglobal.com/ratings