

Risk Remains For Weaker Borrowers Despite Cooling Inflation

This report does not constitute a rating action.

(Editor's Note: For additional exhibits on credit trends, including rating actions, outlooks, fallen angels, rising stars, weakest links, and the U.S. distress ratio, please see the related data publication: ["This Month In Credit: Data Companion."](#))

Primary Contacts

Evan Gunter
Montgomery
+1-212-438-6412
evan.gunter@spglobal.com

Nicole Serino
New York
+1-212-438-1396
nicole.serino@spglobal.com

Brenden Kugle
Centennial
+1-303-721-4619
brenden.kugle@spglobal.com

Patrick Drury Byrne
Dublin
+00353-568-0605
patrick.drurybyrne@spglobal.com

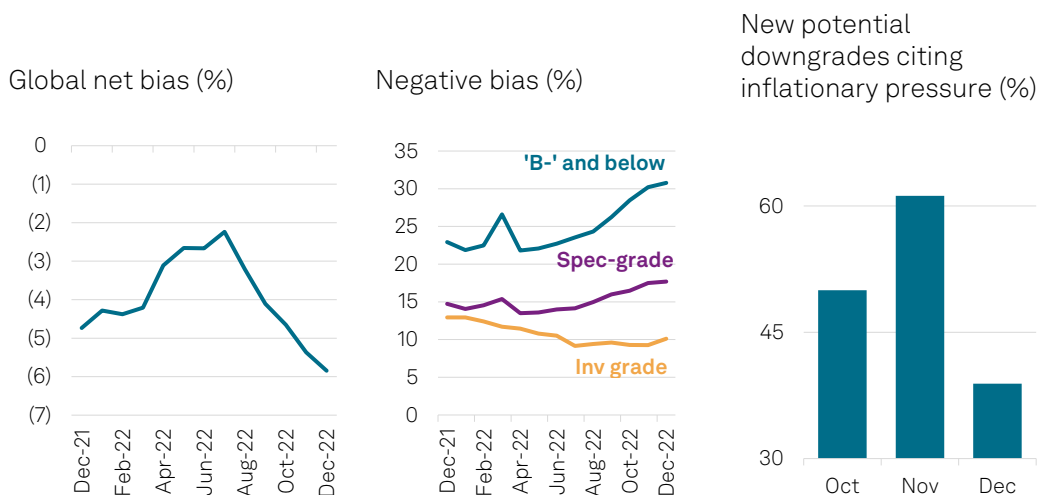
For a weekly snapshot of rating trends and credit conditions, please see **"This Week In Credit,"** released every Monday.

Key Takeaways

- Downgrades were more than twice the number of upgrades in December, and speculative-grade downgrades exceeded investment grade over 10 to 1.
- Inflation was a factor in over one-third of potential downgrades but also one-quarter of potential upgrades. Inflation was cited as a factor in fewer negative outlook revisions than in prior months.
- The number of 'B-' and lower rated borrowers is now more than 50% higher than five years ago, and these issuers are particularly vulnerable to slowing economic growth and rising funding costs.
- Weakest links (issuers rated 'B-' or lower with negative outlooks or on CreditWatch negative) surpassed their five-year average in December 2022, both in number (276) and as a share of speculative-grade corporate issuers (12%).

Chart 1

Cooling Inflation Hasn't Halted Growing Downgrade Risk



Note: Net bias is the positive bias minus the negative bias, including both speculative- and investment-grade sovereign, financial, and nonfinancial financial corporate issuers. Inflation pressure is one of several qualitative factors affecting new potential downgrades, and one rating action can have multiple qualitative factors. Data as of Dec. 31, 2022. Source: S&P Global Ratings Credit Research & Insights.

Credit Notes: 'B-' And Below Under The Microscope

While far too early to declare victory, CPI (Consumer Price Index) growth has cooled in many regions in recent months. The month-over-month change in the U.S. seasonally adjusted CPI fell to -0.1% in December from 0.4% in October and 0.1% in November. Inflation has been a contributing factor both to positive and negative outlook revisions in recent months, but as CPI cools, it is now being cited less frequently. In December, 39% of the outlook revisions cited inflationary pressures, down from near 50% in October.

But while direct effects of inflation may be easing, a closer examination of negative outlook revisions in December finds that weakening operating performance, macroeconomic factors, and high leverage were the primary reasons for new potential downgrades (issuers with negative outlooks or ratings on CreditWatch).

A myriad of factors, not least inflation, affect operating performance. After many companies entered 2022 rebuilding credit quality from pandemic-related shocks, many closed the year on weakened footing. They faced a surge in inflation, a steep rise in interest rates, and tight financing conditions, along with the Russia-Ukraine conflict and gas shortages.

S&P Global Ratings economists' most recent forecasts (from November 2022) expect that global GDP growth will slow to 2.2% in 2023 from 3.4% in 2022, including contraction in the U.S. (with a shallow recession), the U.K., Germany, and Italy. Even as economic growth is poised to slow, and a recession a distinct possibility, we project benchmark interest rates to continue to rise, with the fed funds rate peaking at 5.25% and the European Central Bank lifting the deposit rate eventually to 3%. These twin forces of slowing growth and rising funding costs will continue to weigh on credit quality into 2023. And companies with lower credit quality, especially those already at risk of downgrade, could be particularly challenged. U.S. nonfinancial corporate issuers rated 'B-' showed median EBITDA interest coverage of 1.9x as of June 30, 2022 (while 'CCC+' issuers had a median of 1.1x), suggesting that many of these lower-rated issuers may have little headroom to absorb falling earnings or rising funding costs.

Furthermore, issuers rated 'B-' and lower already show higher downgrade risk, with a negative bias (the percentage of issuers with negative outlooks or ratings on CreditWatch negative) approaching 31%, which is above that of higher-rated entities. These 'B-' and lower issuers with a negative bias are mostly U.S. companies, led by the high technology and consumer products sectors. The negative bias for 'B-' and lower has risen by eight percentage points over the past year. While negative bias remains below its five-year average, the cohort of issuers at this rating level is now more than 50% larger than it was five years ago.

Related, the number of weakest links (issuers rated 'B-' or lower with either negative outlooks or on CreditWatch negative) just surpassed its trailing-five-year average, reaching 276 in December, and now accounts for 12% of speculative-grade corporate issuers. This growing population of weakest links brings a larger pool of issuers that carry elevated risk of default. Weakest link default rates are, on average, 8x higher than overall speculative-grade ('BB+' or lower) default rates. So far, the speculative-grade default rate has been relatively constrained, holding below 2% over the past year, but it's now rising, and we forecast the speculative-grade corporate default rate will rise to 3.75% in the U.S. (and to 3.25% in Europe) by September 2023.

While several of our credit indicators undoubtedly point to rising credit quality issues, these risk indicators are rising from exceptionally low levels at the beginning of 2022 (before the start of the Russia-Ukraine conflict). Even though the negative biases for investment grade, speculative grade, and 'B-' and lower have been steadily increasing in recent months, they remain below their

For more
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data, [click here](#)

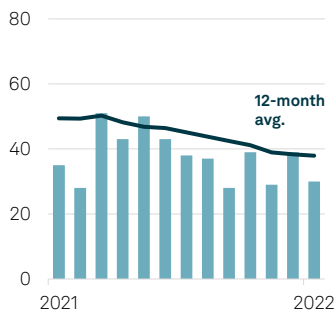
Risk indicators are rising from exceptionally low levels at the beginning of 2022 (before the start of the Russia-Ukraine conflict).

five-year averages, and the positive bias (the percentage of issuers with positive outlooks or ratings on CreditWatch positive) holds above its five year average. Furthermore, the credit market-based measure of the U.S. distress ratio (the percent of speculative-grade bonds trading more than 1,000 bps wider than treasuries) remains below its midyear high from July 2022. At 7.9%, the distress ratio is only slightly above its five-year average of 7.3%.

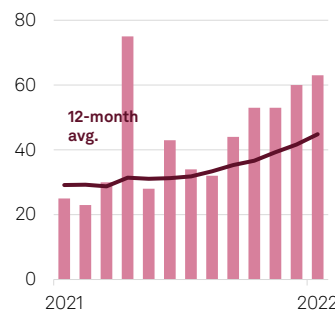
Credit quality is turning more negative faster for weaker borrowers. As the impact of global central banks' concerted tightening becomes more fully felt through higher financing costs, and if earnings are challenged by the slowing global economy, lower-rated companies' resilience will be increasingly tested.

Ratings Trends Snapshot – Through Dec. 31, 2022

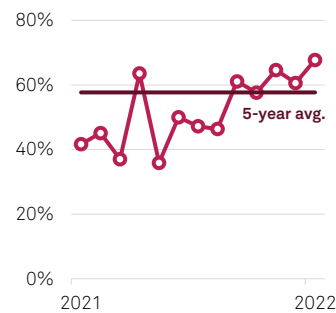
Upgrades



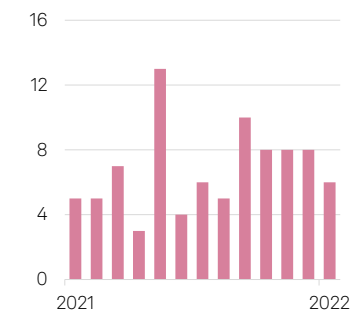
Downgrades



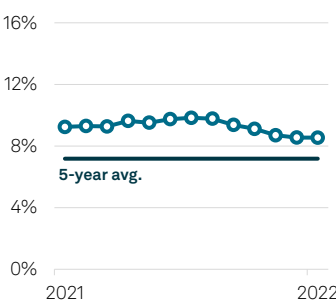
Downgrade Ratio



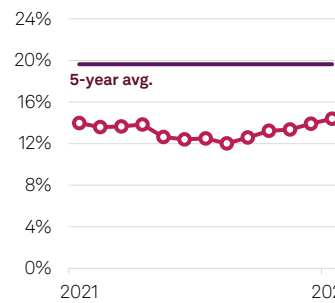
Defaults



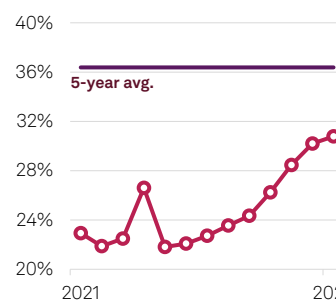
Positive Bias



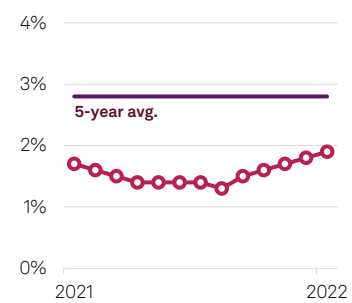
Negative Bias



Neg Bias 'B-' And Lower



SG Default Rate



Data represents rating actions and biases for sovereign, financial, and nonfinancial corporates issuers globally. Downgrade counts exclude defaults. Defaults and speculative-grade default rate exclude sovereigns. Data as of Dec. 31, 2022. Source: S&P Global Ratings Credit Research & Insights.

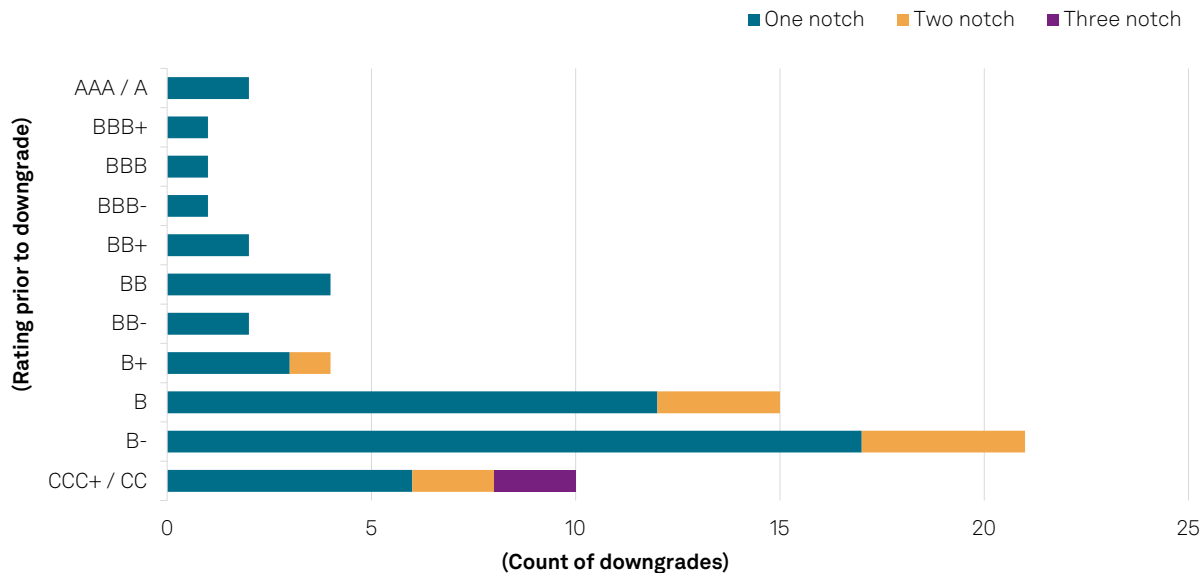
Credit Trends

Rating actions continue to trend more negative, with twice as many downgrades as upgrades. Downgrades (excluding defaults) rose by three (to 63) in December, even as the number of investment-grade downgrades fell in the month (to five from 11). But speculative-grade downgrades more than made up for the difference (rising to 58 from 49).

The number of issuers downgraded to 'CCC+' or below also increased. When issuers are downgraded below the 'B' category, financing becomes increasingly tough, with portfolio and CLO managers limited in the amount of this debt they can hold. New additions to the 'CCC+' and below category in December included 21 'B-' issuers and three 'B' issuers, an increase from nine 'B-' issuers and two 'B' issuers in November.

Chart 2

Downgrades Concentrated Among 'B' And 'B-' Issuers In December



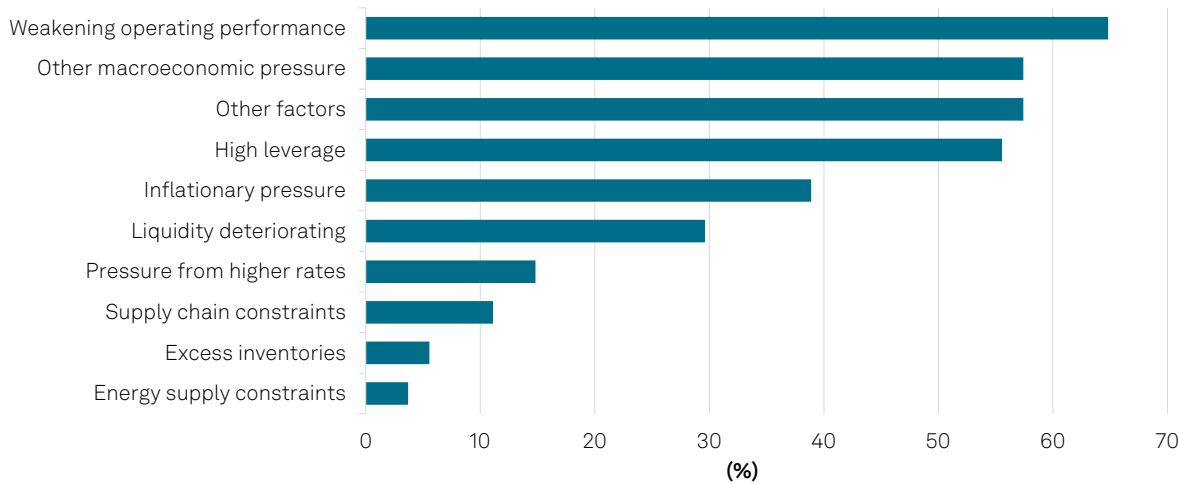
Includes sovereign, financial, and nonfinancial corporate downgrades globally, excluding defaults, from the month of December 2022. Source: S&P Global Ratings Credit Research & Insights.

Rating biases point toward continued downgrade risk ahead. The negative bias edged slightly higher, to just over 14% in December, while the positive bias held steady at 9%. By region, Europe, and Eastern Europe, the Middle East, Africa had the largest increases in their negative biases, each up by over a percentage point. The aerospace and defense sector had the largest increase in negative bias (up five percentage points to near 20%).

Among companies that were added to the list of potential downgrades, most outlook revisions cited "weakening operating performance" (at 65%), followed by "other macroeconomic pressure" (at 57%).

Chart 3

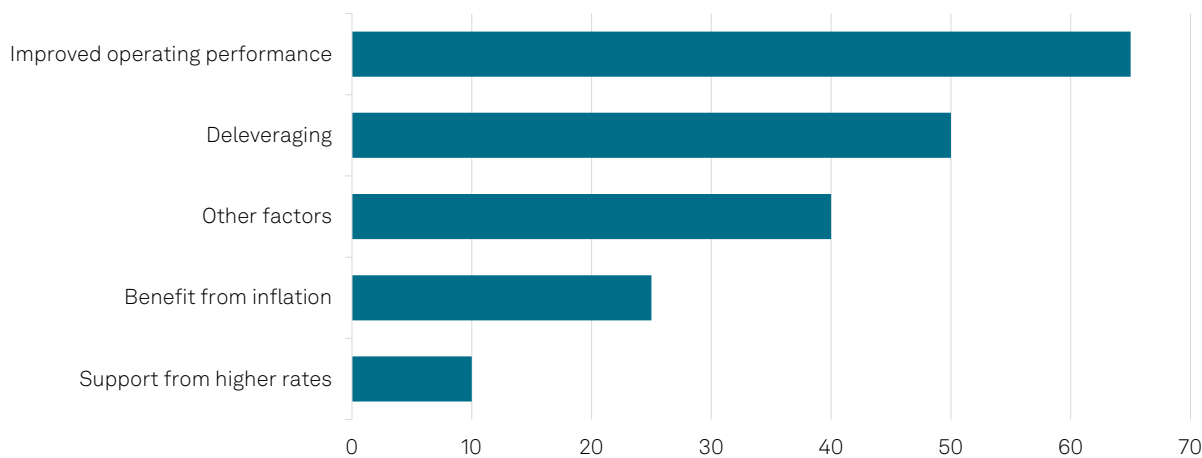
Inflation Factored In Less Than 40% Of New Potential Downgrades In December



We take stock of main risks outlined in new potential downgrade and weakest links rating reports and group them in different qualitative factors as shown in the chart. Note: One rating action can have multiple qualitative factors. Data as of Dec. 31, 2022. Source: S&P Global Ratings Credit Research & Insights.

Chart 4

Of New Potential Upgrades, 25% Benefit From High Inflation



We take stock of main factors outlined in new potential upgrades rating reports and group them in different qualitative factors as shown in the chart. Note: One rating action can have multiple qualitative factors. Data as of Dec. 31, 2022. Source: S&P Global Ratings Credit Research & Insights.

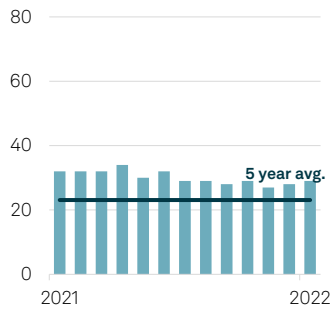
The number of corporate defaults declined slightly in December, with the monthly count falling by two to six defaults. The global 12-month-trailing speculative-grade corporate default rate rose slightly to 1.94% (from 1.83% in November). Despite fewer defaults in December, three of the 10 largest downgrades (excluding defaults) by debt amount in December were of entities lowered to 'CC', signifying that future defaults are possible.

The largest corporate or sovereign issuers lowered to 'CC' during the month were the **sovereign Republic of Ghana**, movie theater chain **AMC Entertainment Holdings**, and homebuilder/real estate group **Adler Group S.A.** (which is an operating subsidiary of ADO Group Ltd.).

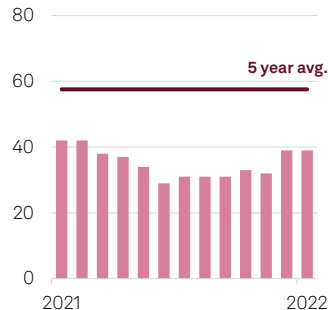
While credit trends are certainly leaning more negative, with downgrades and defaults on the upswing, these are rising from low levels last year.

Specific Credit Indicators

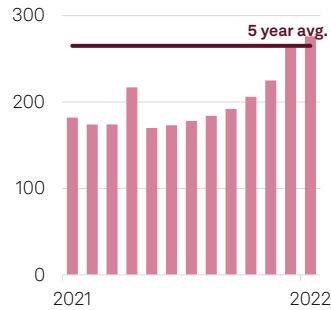
Potential Rising Stars



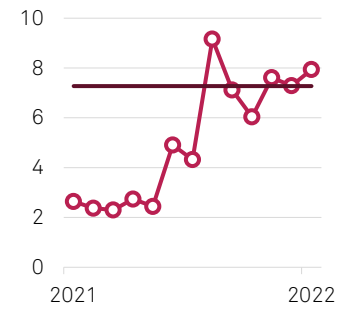
Potential Fallen Angels



Weakest Links



Distress Ratio



Data represents sovereign, financial, and nonfinancial corporates issuers globally, except for the S&P Global U.S. distress ratio, which is defined as the number of U.S. speculative-grade issues with option-adjusted spreads of more than 1,000 basis points above U.S. Treasury bonds. Data as of Dec. 31, 2022. Source: S&P Global Ratings Credit Research & Insights.

Fallen angels: One new fallen angel (an issuer downgraded to speculative grade from investment grade) was added in December (slowing the pace of four additions from November). U.S. real estate developer **SL Green Realty Corp** was the lone fallen angel of the month and was among the five largest downgrades in December. The number of potential fallen angels remains unchanged at 39 for the month. The financial institutions and homebuilder/real estate sectors have the highest number of potential fallen angels, with eight and six, respectively.

The number of potential fallen angels (issuers rated 'BBB-' with negative outlooks or ratings on CreditWatch negative) was unchanged in December at 39. This count rose by six in the fourth quarter yet remains below the five-year average. The largest number of potential fallen angels are financial institutions (with eight), and these are mostly from the emerging markets. The homebuilder/real estate sector follows with six, as demand for new housing has fallen amid surging interest rates.

Rising stars: Likewise, there was one new rising star (an issuer upgraded to investment grade from speculative grade) for the month, **Hyatt Hotels Corp**, and this was among the 10 largest upgrades (by debt amount) for the month. The number of potential rising stars continues to show slight month-over-month increases, up by one in December to 29.

The number of potential rising stars (issuers rated 'BB+' with positive outlooks or on CreditWatch positive) rose by one in December to 29, and remains above its five year average. The financial institutions and media and entertainment sectors have the largest number of potential rising stars (at five each). For both of these sectors, the majority of the potential rising stars are from the U.S.

Weakest links: December saw a notable jump in the number of media and entertainment weakest links, up by seven from November. Higher interest rates have added to the media and entertainment sector's woes, weakening interest coverage and cash flows (even as some issuers, such as Hyatt Hotels Corp, have benefited from the rebound in leisure travel). Media and entertainment is now tied with consumer products for the largest number of weakest links, with

Media and entertainment is now tied with consumer products for the largest number of weakest links, with 48 each.

48 each. The technology sector recorded the largest increase in weakest links for full-year 2022-- up by 17. By region, weakest links in the U.S. and Europe now exceed their five-year averages as the ongoing energy supply and price volatility are compounding the challenges of rising rates and slowing growth for domestic issuers in Europe. For the lower-rated issuers in Europe and globally, earnings resilience will be closely watched.

Distress ratio: Even though the U.S distress ratio more than doubled to 7.9% in December 2022 from 2.6% in December 2021, it remains below the recent peak of over 9% reached in July 2022. Health care experienced the greatest percentage-point increase in its distress ratio in 2022, and the sector leads with the highest distress ratio of 19% as of Dec. 31, 2022, as rising labor costs, supply chain disruptions, and regulatory changes have further constrained margins and cash flow in an industry that faces lingering effects of the COVID-19 pandemic.

For more data and charts on fallen angels, potential fallen angels, rising stars, potential rising stars, weakest links, and the U.S. distress ratio, please see the related publication: "This Month In Credit: Data Companion."

Relative Risks By Region And Sector

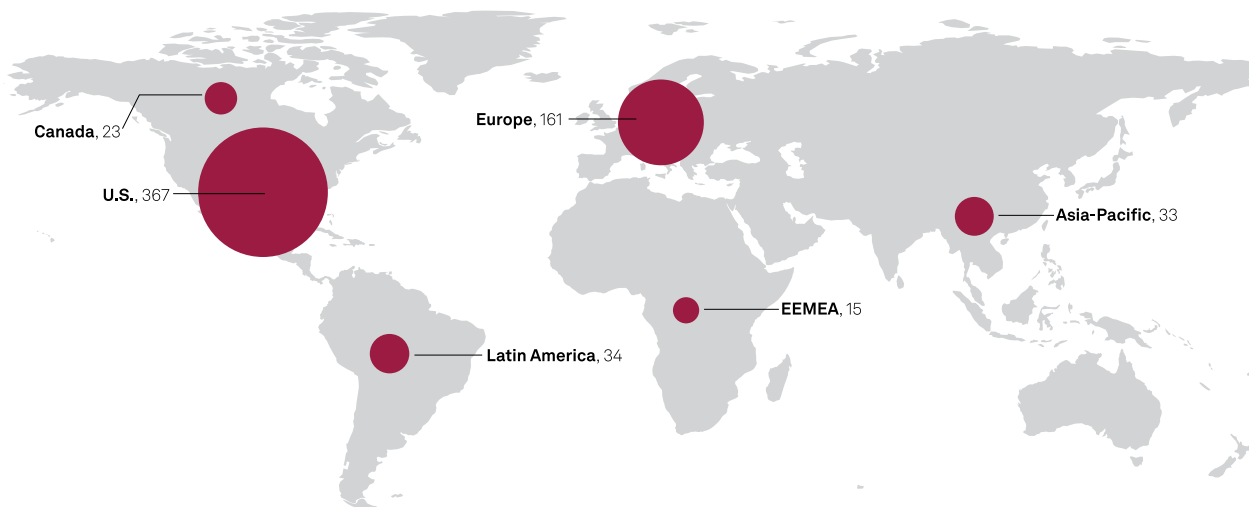
By region, Latin America had the highest negative bias, near 17% as of Dec. 31, 2022, and this is up one percentage point since November. This is marginally higher than both the U.S. and Europe at 16% and 15%, respectively. Latin America has 34 potential downgrades. The financial institutions sector accounts for the highest concentration (with 13) of Latin America's potential downgrades. For many of these financial institutions, the negative outlook or CreditWatch negative reflects either a sovereign rating or a Banking Industry Country Risk Assessment (BICRA). The negative trend in the BICRA for Chile led to several of the potential downgrades, as did the negative outlooks on the sovereign ratings on Argentina, Honduras, and Panama.

While Latin America has the highest regional percentage of issuers with negative outlooks or on CreditWatch negative, this is due to a substantially smaller population of rated issuers than the U.S. and Europe, which have most of the global potential downgrades and meaningfully higher absolute numbers (see chart 5).

Chart 5

Potential Downgrades

By Region



Data as of Dec. 31, 2022. Source: S&P Global Ratings Credit Research & Insights.

By sector, **consumer products** has the largest number of potential downgrades, with 100 globally, and this sector leads potential downgrades in both the U.S. and Europe. 48% of these potential downgrades are rated 'B-' or lower, and the downgrade risk of this sector is increasing as consumers pull back on spending while they face higher prices and potential recession fears.





















The media and entertainment sector follows, with 74 potential downgrades. Credit risk in this sector is highly concentrated among the lowest rated issuers--about half of the potential downgrades are already rated 'CCC+' or below.

Meanwhile, even though it has fewer potential downgrades, the high technology sector has a higher number of potential downgrades among its 'B-' rated issuers than other sectors. 14 of the 34 potential downgrades in the technology sector are rated 'B-'. These 'B-' technology companies with negative outlooks or on CreditWatch negative are largely U.S.-based, with a tilt toward software companies.

The high technology sector has a higher number of potential downgrades among its 'B-' rated issuers than other sectors.

Table 1





















Potential Downgrades Distribution By Sector And Region

Sectors	Global	U.S.	Europe	Asia-Pacific	Latin America	EEMEA	Canada
 Aerospace and defense	13	12	1				
 Automotive	21	10	8	3			
 Capital goods	31	21	8	1			1
 CP&ES	27	14	10		2		1
 Consumer products	100	75	20	1		2	2
 Diversified	1						1
 Financial institution	53	18	14	3	13	4	1
 Forest PBM	10	6	4				
 Health care	40	33	5	1	1		
 High technology	34	25	6	2			1
 Home/real estate	29	13	9	4	1		2
 Insurance	16	8	6	2			
 Media/entertainment	74	57	12	3	2		
 Metals, mining, and steel	14	8	1	1			4
 Oil and gas	12	4	2	1		3	2
 Retail/restaurants	31	18	10	2	1		
 Sovereign	17		8		5	4	
 Telecommunications	25	11	10		2		2
 Transportation	29	7	14	4	1	1	2
 Utilities	56	27	13	5	6	1	4

The darker red indicates more potential downgrades per region.
 PBM--Products and building materials. CP&ES--Chemicals, packaging, and environmental services.
 Data as of Dec. 31, 2022. Source: S&P Global Ratings Credit Research & Insights.

Table 2

Potential Upgrades Distribution By Sector And Region

Sectors	Global	U.S.	Europe	Asia-Pacific	Latin America	EEMEA	Canada
 Aerospace and defense	6	3	2	1			
 Automotive	8	5	3				
 Capital goods	16	4	9	1	1		1
 CP&ES	13	5	3	1		2	2
 Consumer products	25	16	5	1	1	1	1
 Diversified	2			1	1		
 Financial institution	48	19	17	7		3	2
 Forest PBM	8	5	2		1		
 Health care	14	11	1			1	1
 High technology	13	5	5	2	1		
 Home/real estate	14	11	1	1			1
 Insurance	12	6	4	2			
 Media/entertainment	42	29	10	1			2
 Metals, mining, and steel	21	11	3	3	2		2
 Oil and gas	26	15	6		1		4
 Retail/restaurants	12	8	4				
 Sovereign	5		1		1	3	
 Telecommunications	10	1	6			2	1
 Transportation	21	12	5	3	1		
 Utilities	22	12	6		2		2

The darker blue indicates more potential upgrades per region.
 PBM--Products and building materials. CP&ES--Chemicals, packaging, and environmental services.
 Data as of Dec. 31, 2022. Source: S&P Global Ratings Credit Research & Insights.

Table 3

Top 10 Downgrades In December*

Issuer	Sector	Downgrade date	Downgrade to	Downgrade from	Country	Amount (bil. \$)
Amgen Inc.	Health care	12/12/2022	BBB+	A-	U.S.	41.3
Altice USA Inc.	Telecommunications	12/2/2022	B+	BB-	U.S.	22.8
Republic of Ghana	Sovereign	12/6/2022	CC	CCC+	Ghana	12.8
Radiate Holdco LLC	Telecommunications	12/15/2022	CCC+	B	U.S.	9.9
SL Green Realty Corp.	Homebuilders/real estate companies	12/22/2022	BB+	BBB-	U.S.	9.0
Telesat Canada (Telesat Holdings Inc.)	Telecommunications	12/16/2022	CCC+	B	Canada	6.7
AMC Entertainment Holdings Inc.	Media and entertainment	12/28/2022	CC	CCC+	U.S.	6.2
Adler Group S.A. (ADO Group Ltd.)	Homebuilders/real estate companies	12/6/2022	CC	CCC	Luxembourg	4.5
Magenta Buyer LLC	High technology	12/21/2022	B-	B	U.S.	4.3
Madison IAQ LLC (Madison Industries Holdings LLC)	Forest products and building materials	12/5/2022	B-	B	U.S.	4.3

*Downgrades excluding defaults. Table shows 10 largest issuer downgrades, excluding defaults, by debt amount, in December 2022. Data as of Dec. 31, 2022. Source: S&P Global Ratings Credit Research & Insights.

Table 4

Top 10 Upgrades In December

Issuer	Sector	Upgrade date	Upgrade to	Upgrade from	Country	Amount (bil. \$)
Dominican Republic	Sovereign	12/19/2022	BB	BB-	Dominican Republic	25.9
LVMH Moët Hennessy Louis Vuitton S.E.	Consumer products	12/5/2022	AA-	A+	France	12.0
Boston Scientific Corp.	Health care	12/7/2022	BBB+	BBB	U.S.	8.6
SBA Communications Corp.	Telecommunications	12/2/2022	BB+	BB	U.S.	5.3
CEMEX S.A.B. de C.V.	Forest products and building materials	12/8/2022	BB+	BB	Mexico	5.2
Weatherford International plc	Oil and gas	12/6/2022	B	B-	Ireland	4.5
Hyatt Hotels Corp.	Media and entertainment	12/19/2022	BBB-	BB+	U.S.	3.4
Thyssenkrupp AG	Capital goods	12/21/2022	BB	BB-	Germany	3.4
Bausch + Lomb Corporation (Bausch Health Companies Inc.)	Health care	12/1/2022	B-	CCC+	Canada	2.5
Autodesk Inc.	High technology	12/19/2022	BBB+	BBB	U.S.	2.3

Table shows 10 largest issuer upgrades, by debt amount, in December 2022. Data as of Dec. 31, 2022. Source: S&P Global Ratings Credit Research & Insights.

Related Research:

Ratings Performance Insights: 2022 In Review, Jan. 19, 2023

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SL Green Realty Corp. Downgraded To 'BB+' From 'BBB-' On Sustained Elevated Leverage, Dec. 22, 2022

Hyatt Hotels Corp. Upgraded To 'BBB-' On Deleveraging, Plausible Policy Targeting Low Investment Grade; Outlook Stable, Dec. 19, 2022

Global Macro Update: Surprising Resilience Unlikely To Last Into 2023, Nov. 30, 2022

Glossary And Abbreviations

Fallen angels--Issuers downgraded to speculative grade from investment grade.

Investment grade--Issuers rated 'BBB-' or above.

Negative bias--Percentage of issuers with negative outlooks or ratings on CreditWatch negative.

Net outlook bias--Percentage of issuers with a positive bias minus those with a negative bias.

OLCW--Outlooks and CreditWatch placements.

Positive bias--Percentage of issuers with positive outlooks or ratings on CreditWatch positive.

Potential downgrade--An issuer rated by S&P Global Ratings with a negative outlook or on CreditWatch negative.

Potential fallen angels--Issuers rated 'BBB-' with either negative outlooks or on CreditWatch negative.

Potential fallen angel ratio--The number of potential fallen angels divided by the population of issuers rated in the 'BBB' category.

Potential upgrade--An issuer rated by S&P Global Ratings with a positive outlook or on CreditWatch positive.

Rising stars--Issuers upgraded to investment grade from speculative grade.

Risky credits--Issuers in the 'CCC' rating category.

Speculative grade--Issuers rated 'BB+' or below.

U.S. distress ratio--Proportion of speculative-grade issues with option-adjusted composite spreads of more than 1,000 basis points relative to U.S. Treasury bonds. S&P Global U.S. distress ratio is defined as the number of speculative-grade issues with option-adjusted spreads above 1,000 basis points divided by the total number of speculative-grade issues.

Weakest links--Issuers rated 'B-' and below with either negative outlooks or on CreditWatch negative.

Weakest links ratio--The number of weakest links divided by the total speculative-grade ratings population.

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