

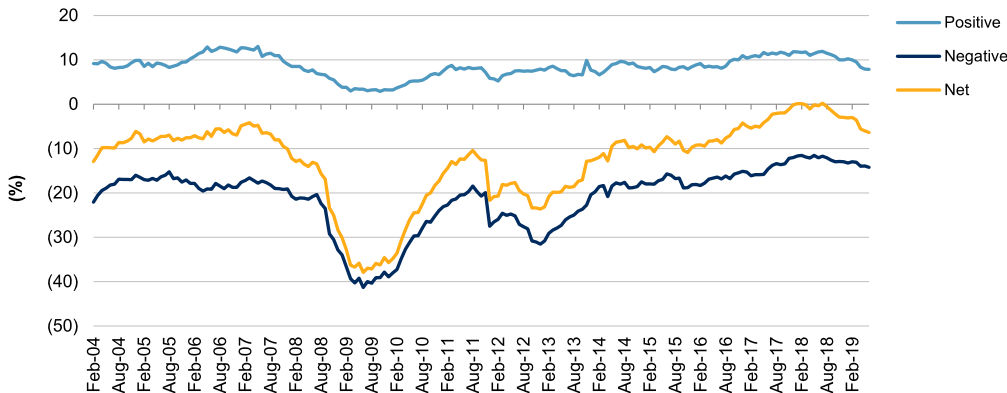
Credit Trends:

European Corporate Credit Quality Is Expected To Decline Following A 10-Year Peak

August 15, 2019

Chart 1

Credit Quality Prospects Have Declined Following A 10-Year Peak



Net ratings bias is positive bias minus negative bias. Data as of June 30, 2019. Source: S&P Global Ratings Research. Copyright © 2019 by Standard & Poor's Financial Services LLC. All rights reserved.

S&P GLOBAL RATINGS RESEARCH

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Key Takeaways

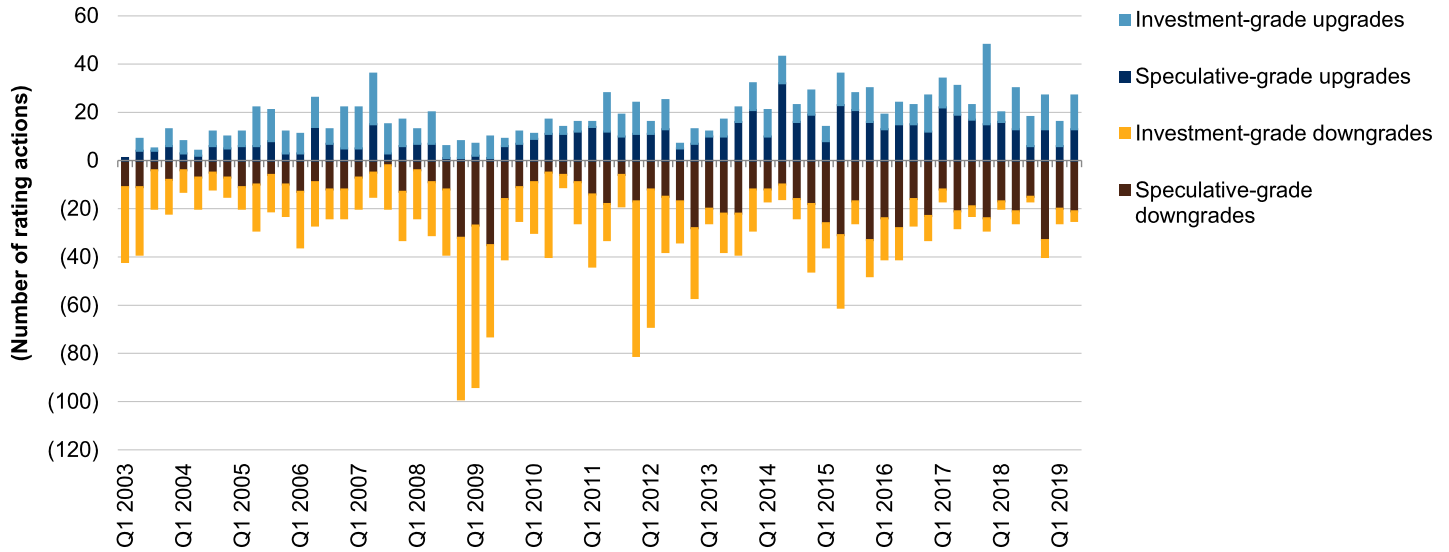
- In the second quarter, there were 27 upgrades and 25 downgrades among European financial and nonfinancial companies. The pace of rating actions was consistent with the long-term average of recent years.
- European corporate credit quality is expected to decline over the next year or so, given that the region's negative bias increased to 14.2% in the second quarter.
- That said, the rising negative bias is still well below the long-term average, and we don't currently expect a surge of downgrades. Rather, the region is winding down from a period of particularly strong credit trends, notably among financial services companies.
- The aerospace and defense sector continues to exhibit the highest downgrade potential, with a negative bias of 33%. However, the automotive sector is a close second at 30%, being particularly vulnerable to potential global trade disruptions.

Upgrades Increased In The Second Quarter, Just Outpacing Downgrades

In the second quarter of 2019, S&P Global Ratings upgraded 27 European corporate companies, a healthy uptick from the 16 upgrades reported in first quarter. The number of downgraded entities fell to 25 in the second quarter from 26 in the first quarter, which is the fewest downgrades for any second quarter since 2014 (see Chart 2). Overall, rating actions in Europe during the second quarter closely reflected long-term averages rather than any marked shift in rating trends.

Chart 2

European Corporate Rating Actions



Rating changes exclude entities with no rated debt. Negative numbers signify downgrades. Data as of June 30, 2019. Source: S&P Global Ratings Research.

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As a result, the downgrade ratio contracted to 48% in the second quarter from 62% in the first quarter. There were nine upgrades among financial services, while nonfinancial companies had 18 upgrades, bringing the upgrade ratios to 33% and 66%, respectively. The financial services sector had two downgrades in the second quarter, bringing the downgrade ratio to 8% and following two consecutive quarters without any downgrades. The Netherlands' Euronext N.V. was downgraded on the basis of rising leverage, while U.K.-based Motability Operations Group Plc. was downgraded due to a reserves reduction. Twenty-three nonfinancial companies were downgraded, yielding a downgrade ratio of 56%.

European Credit Quality Is Likely To Decline Somewhat

We expect overall corporate credit quality to decline slightly over the next year based on the current outlook and CreditWatch distribution, our expectation for a slowing economic backdrop, and the potential for multiple geopolitical stressors to have a negative impact on the region. The negative bias of European corporates expanded to 14.2% in the second quarter from 13.1% in the first quarter, while the positive bias contracted to 7.9% from 9.5%. This resulted in a net rating bias of negative 6.3%, reflecting that downgrades will likely outnumber upgrades in the coming quarters.

That said, we do not expect a surge of downgrades in the near term. Although increasing, the negative and net-negative biases are both well below their averages since 2004. We consider the current period to be a decline from one of the strongest periods of credit performance in recent

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years (see Chart 1).

While financing conditions have been favorable in Europe for some time, they have become even more so in the last two months. That said, some risk aversion exists, as easier terms of borrowing have generally been limited to borrowers with higher ratings. This point was corroborated by the change in lending conditions the European Central Bank (ECB) reported in its most recent senior bank lending survey. It showed a net tightening of 5% for small and medium-sized firms as well as a net neutral reading for standards on loans to large corporations. This was the first shift toward tightening standards in several years.

The anticipated stimulus by the ECB was also largely the result of a slowing regional economy, low inflation and inflation expectations, and efforts to counteract the negative impact of global trade disputes. The Eurozone region is highly integrated in the global value chains and is vulnerable to the adverse effects of a slowdown in the global trade. Despite strong internal demand in the Eurozone, if trade continues to slow, the region could be affected by weakness in external demand.

Upgrades Were In Both The Investment- And Speculative-Grade Segments

The 27 upgrades among European corporate companies in the second quarter of 2019 were split between 18 nonfinancial companies and nine financial services firms. The resulting upgrade ratio was the lowest in any second quarter in the past three years. Of the 25 corporate downgrades reported, 23 were nonfinancial companies, and the remaining two were financial (see Table 1).

Table 1

European Corporate Ratings Statistics (Second-Quarter 2019)

	Overall	Investment grade	Speculative grade	Financial	Nonfinancial
Downgrades					
Number of issuers	25	4	21	2	23
Debt volume (Bil. \$)	62	13	49	5	57
Upgrades					
Number of issuers	27	14	13	9	18
Debt volume (Bil. \$)	359	332	26	297	62
Total rating actions					
Number of issuers	52	18	34	11	41
Debt volume (Bil. \$)	421	345	76	302	119
Downgrade ratio (%)					
Q2 2019	48	22	62	18	56
Historical average*	65	65	62	58	67
High, quarter	100, Q1 1995	100, Q1 2003	100, Q1 2002	100, Q1 2013	100, Q1 1997
Low, quarter	27, Q2 2014	13, Q4 2017	0, Q1 1998	0, Q1 2019	25, Q4 1996
Negative bias (%)					
As of June 30, 2019	14	11	18	9	16
Historical average*	21	20	22	22	21

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Table 1

European Corporate Ratings Statistics (Second-Quarter 2019) (cont.)

	Overall	Investment grade	Speculative grade	Financial	Nonfinancial
High, quarter	41, Q2 2009	36, Q2 2009	56, Q2 2009	49, Q4 2012	41, Q2 2009
Low, quarter	11, Q4 1997	10, Q4 2017	0, Q3 1995	3, Q1 2007	11, Q2 2014
Positive bias (%)					
As of June 30, 2019	8	7	9	11	7
Historical average*	9	7	15	8	9
High, quarter	14, Q3 1998	12, Q1 2018	56, Q4 1995	19, Q1 2018	18, Q3 1998
Low, quarter	3, Q1 2009	2, Q1 2009	4, Q3 2009	1, Q1 2009	4, Q3 2009

*From first-quarter 1995 to second-quarter 2019. Rating actions and bias figures exclude issuers with no rated debt outstanding. Data as of June 30, 2019. Source: S&P Global Ratings Research.

Among nonfinancial corporates, the capital goods sector had the highest number of downgrades in the second quarter with six (see Chart 3). Media and entertainment followed with four downgrades, then oil and gas and retail and restaurants with three downgrades each. Downgrades in the remaining nonfinancial sectors were in line with quarterly levels in the past five years.

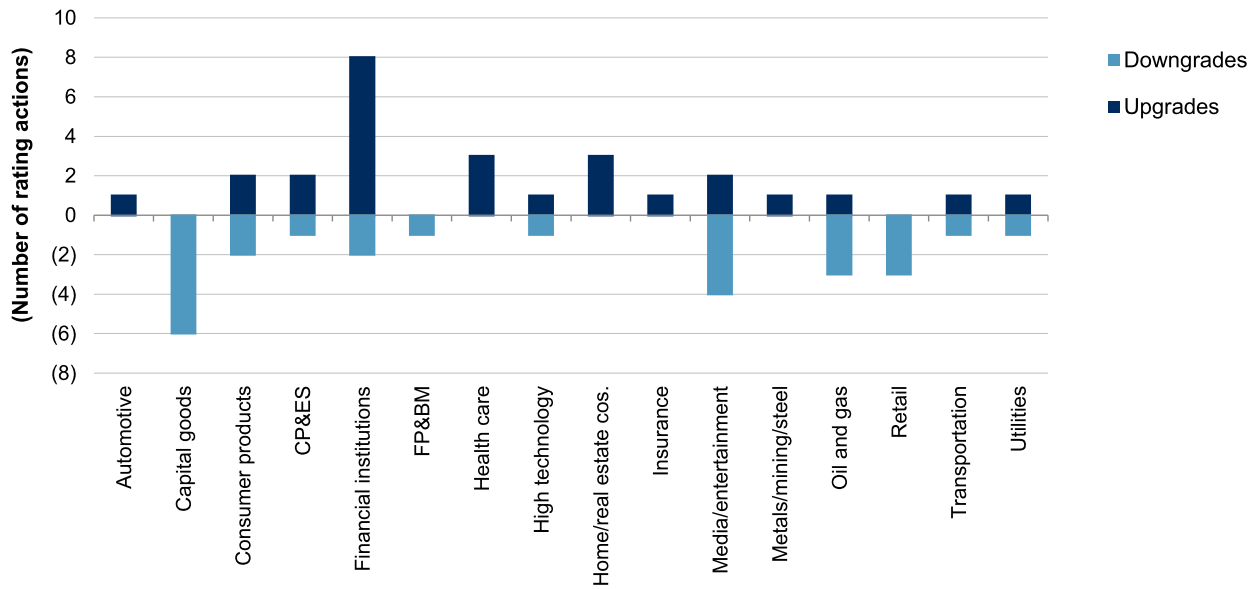
There were four investment-grade companies downgraded in the second quarter, the lowest number for any second quarter going back to 2014 (see Chart 1). The only investment-grade company to be downgraded into the speculative-grade category was Austria-based Novomatic AG, a media and entertainment company that was downgraded to 'BB+' from 'BBB-'. This action was result of S&P Global Ratings' expectation that the company's EBITDA margin will not improve in 2019, therefore translating into lower free operating cash flow.

There were 21 downgrades among speculative-grade companies, up from 20 in the first quarter. Three of these resulted in selective defaults. For investment-grade companies, there were just four downgrades, down from six in the previous quarter. Upgrades increased for both speculative-grade (14) and investment-grade (13) companies.

The highest concentration of downgrades were in the capital goods sector, which had six. Half of these came from Luxembourg-based Galapagos Holding S.A., which was downgraded three times in the second quarter. Sevon Holding GmbH, a Germany-based capital goods company, was downgraded twice over the same period. The ratings on both companies went to 'SD' (selective default) following missed interest payments, and these account for two of the three corporate defaults in the second quarter. The remaining default was by the U.K.-based department store Debenhams PLC as a result of distressed debt issuance.

Chart 3

European Corporate Rating Actions Varied By Sector (Second-Quarter 2019)



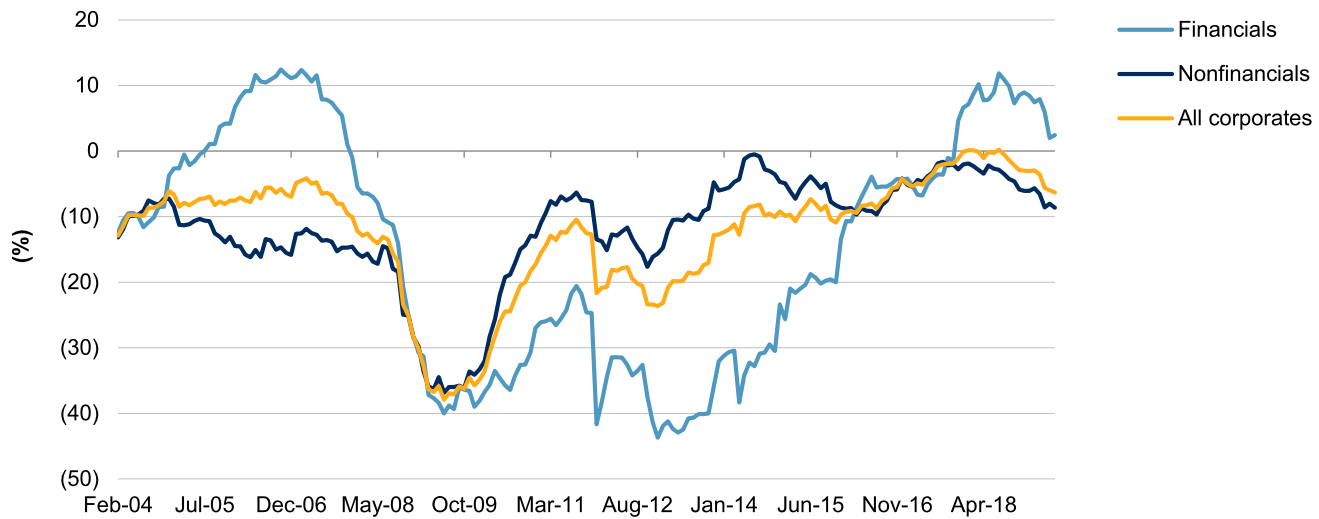
Rating changes exclude entities with no rated debt. Negative numbers signify downgrades. CP&ES--Chemicals, packaging, and environmental services. FP&BM--Forest products and building materials. Data as of June 30, 2019. Source: S&P Global Ratings Research. Copyright © 2019 by Standard & Poor's Financial Services LLC. All rights reserved.

Credit Stress Is Expected To Be Largely Limited To Lower-Rated Nonfinancials

Positive ratings bias among European financial and nonfinancial companies tightened to 7.9% in the second quarter compared to 9.5% in the first quarter. The positive bias represents the proportion of companies that either had a positive outlook or ratings on CreditWatch positive. Positive bias peaked at about 13% in early 2007 and has been declining gradually since December 2017, when it was 11.9%. The overall decline in the positive bias has stemmed from a more prominent decline on the side of financial companies.

Chart 4

European Corporate Net Ratings Bias Trend



Net ratings bias is positive bias minus negative bias. Data as of June 30, 2019. Source: S&P Global Ratings Research. Copyright © 2019 by Standard & Poor's Financial Services LLC. All rights reserved.

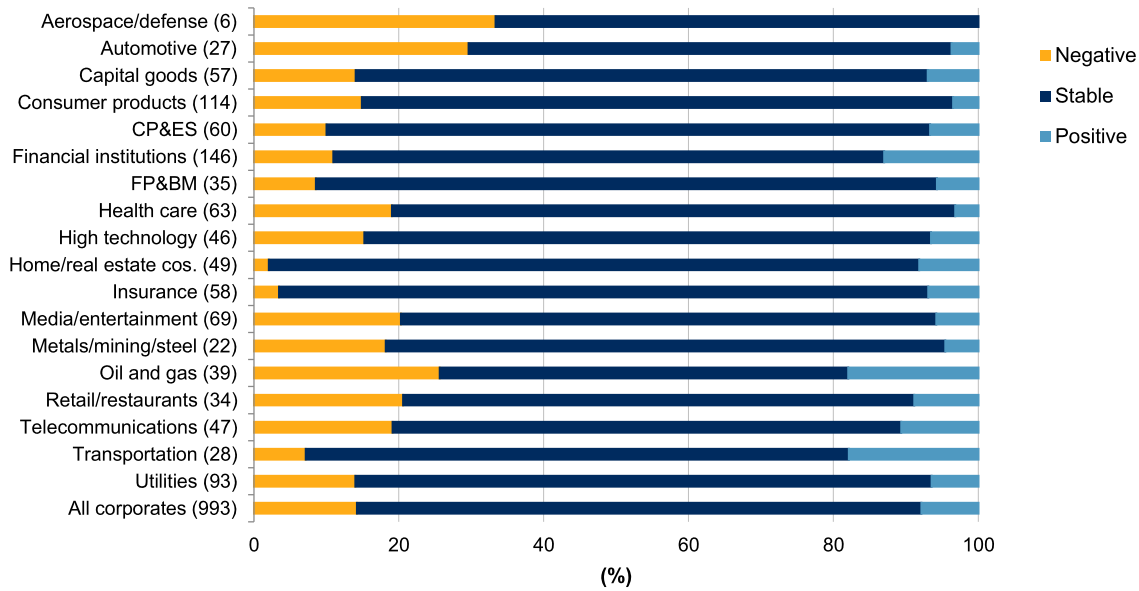
The negative bias for European corporates increased to 14.2% in the second quarter from 13.1% in the first quarter. Overall negative bias has been gradually increasing since the second quarter of 2018, when it was 11.7%. Negative bias for financial companies has increased to 8.8% in the second quarter of 2019 from 6.7% in the second quarter of 2018. The negative bias for nonfinancial companies increased to 15.6% from 13% over the same period.

As a result, the net ratings bias (the positive bias minus the negative bias) for European companies widened to negative 6.3% (see Chart 3), the lowest measure since September 2016, implying that future downgrades could outnumber upgrades. (The trends in positive, negative, and net ratings bias for financial, nonfinancial, and European corporates are shown separately in the appendix.)

Negative bias remains the highest (33%) in the aerospace and defense sector, though this is an unusually small sector with only six issuers (see Chart 4). Negative bias in the automotive sector has been increasing rapidly, rising to 30% in the second quarter from 8% in the second quarter of 2018. Auto sales in Europe have been stagnant in 2019 compared to our expectation of low but positive growth of 1%-2%. The sector is further exposed to environmental and social risk, as European Union regulations on carbon emissions are expected to shrink margins further in 2019 and 2020 as the companies look out for sizeable investments in developing new nature-friendly technology and infrastructure. The sector is also sensitive to social risk in its natural association with consumer habits and preferences for mobility. The sector faces challenges from technology sector that are developing autonomous mobility services.

Chart 5

European Corporate Bias Distribution By Sector



CP&ES--Chemicals, packaging, and environmental services. FP&BM--Forest products and building materials. Figures in parentheses are the number of rated issuers in that sector. Data as of June 30, 2019.

Source: S&P Global Ratings Research.

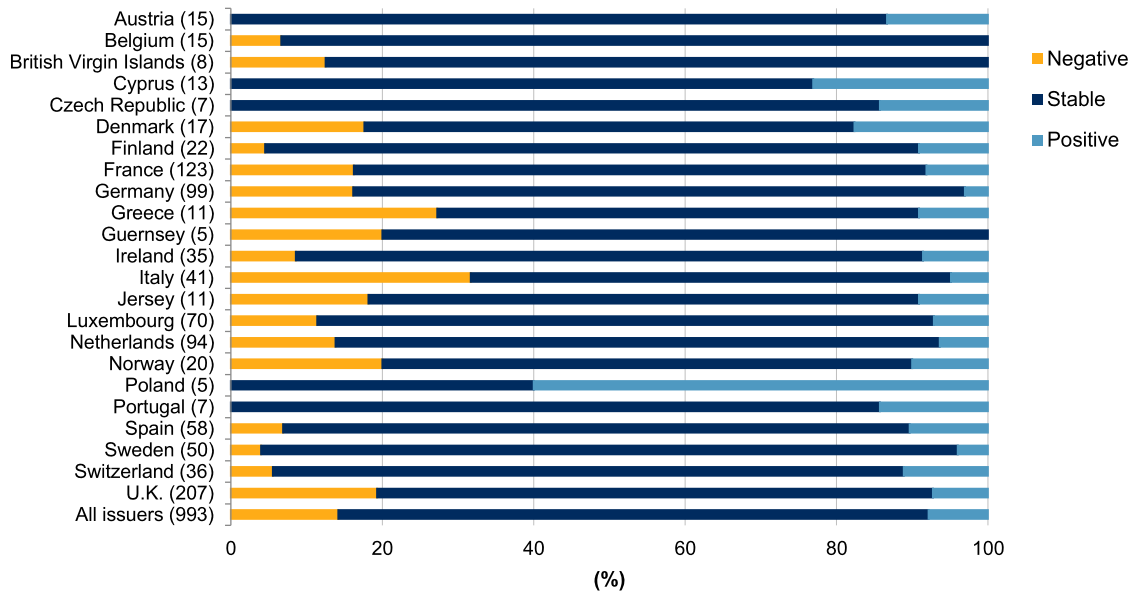
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Of those countries with five or more rated issuers, Italy reported the highest negative rating bias at 32% at the end of the second quarter of 2019, while Poland had the highest positive rating bias at 60% (see Chart 6). Issuers in Italy are operating against a backdrop rife with potential stress from the sovereign situation, characterized by lingering budget issues, political unease, and a slowing economy.

Credit Trends: European Corporate Credit Quality Is Expected To Decline Following A 10-Year Peak

Chart 6

European Corporate Bias Distribution By Country



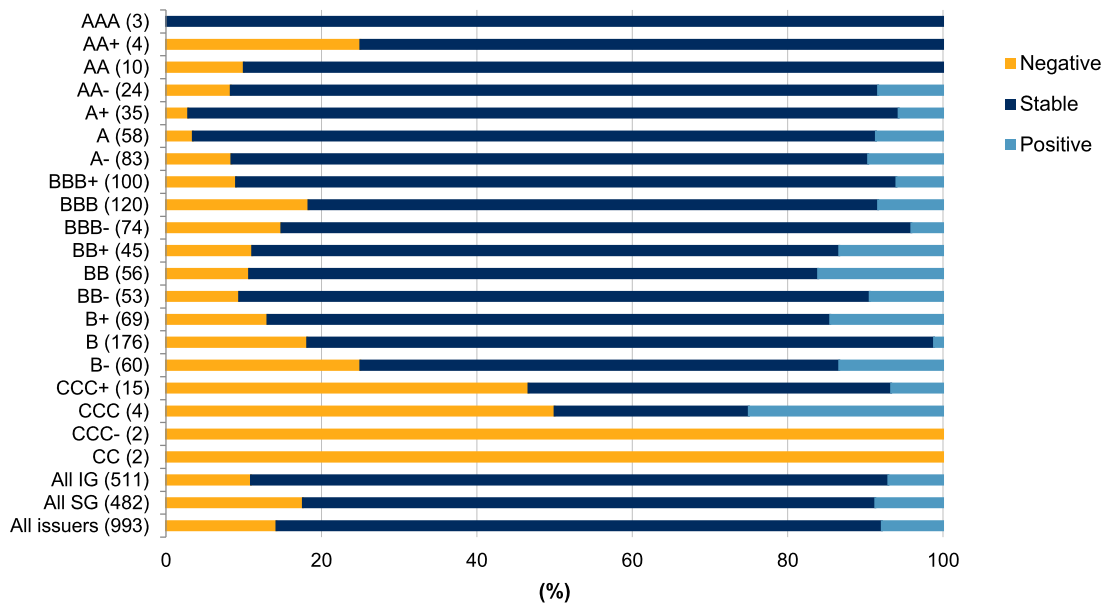
Data as of June 30, 2019. Excludes issuers with no rated debt outstanding. Figures in parentheses show the number of rated issuer in that country. Countries with fewer than five rated issuers are not shown. Source: S&P Global Ratings Research.

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Chart 7

European Corporate Bias Distribution By Rating



IG--Investment grade. SG--Speculative grade. Figures in parentheses Are the number of issuers with that rating.

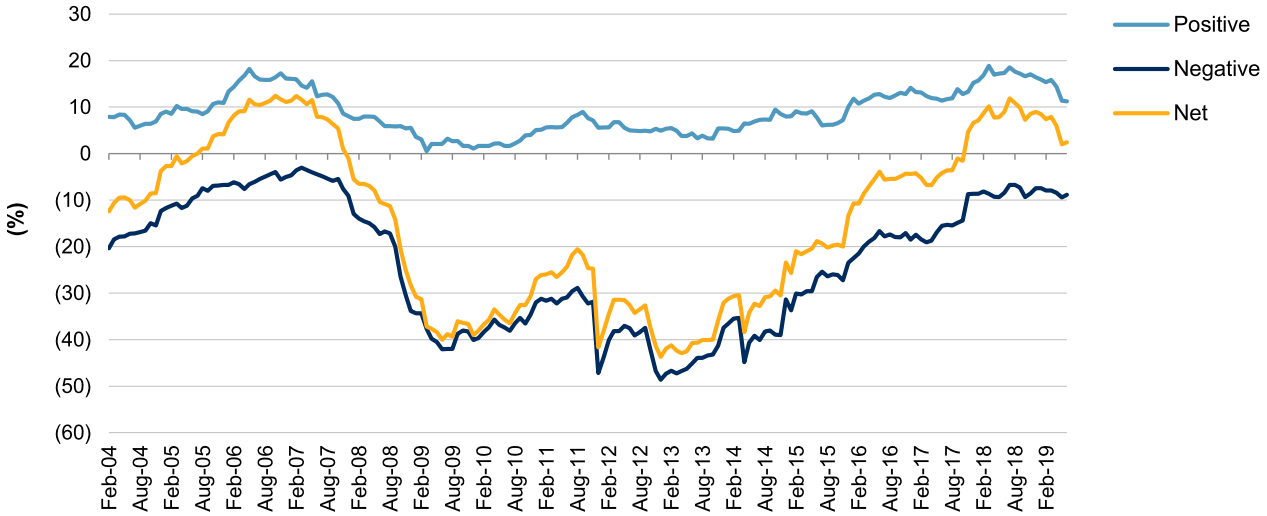
Data as of June 30, 2019. Source: S&P Global Ratings Research.

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Appendix

Chart 8

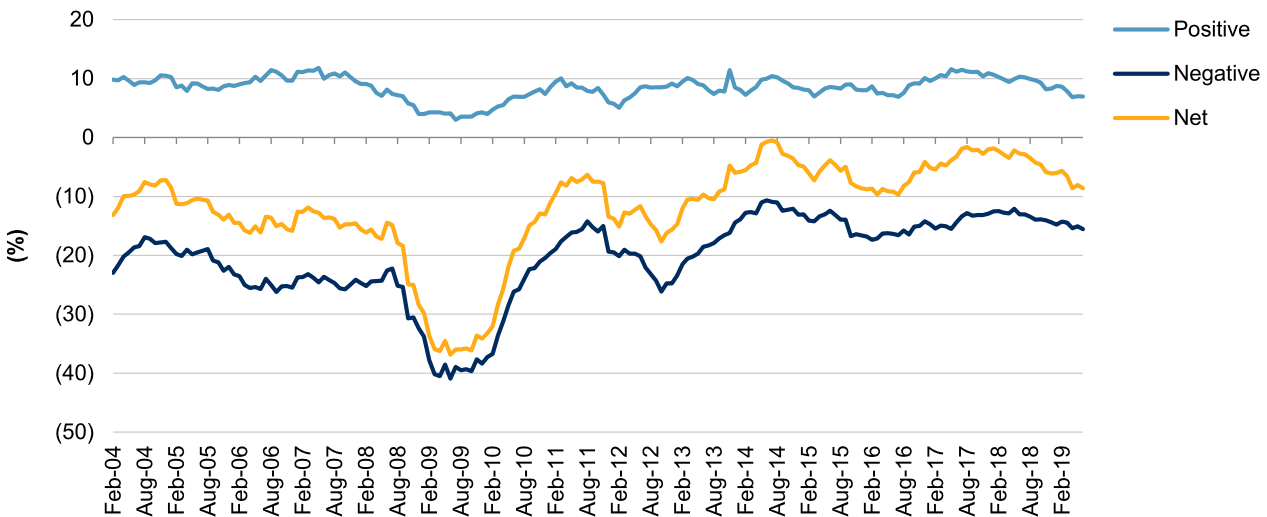
European Financial Corporate Ratings Bias Trend



Net ratings bias is positive bias minus negative bias. Data as of June 30, 2019. Source: S&P Global Ratings Research. Copyright © 2019 by Standard & Poor's Financial Services LLC. All rights reserved.

Chart 9

European Nonfinancial Corporate Ratings Bias Trend



Net ratings bias is positive bias minus negative bias. Data as of June 30, 2019. Source: S&P Global Ratings Research. Copyright © 2019 by Standard & Poor's Financial Services LLC. All rights reserved.

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Table 2

Trends In European Corporate Ratings

	Defaulted issuers	Weakest links	Fallen angels	Rising stars
Q1 2011	1	12	7	2
Q2 2011	1	16	1	4
Q3 2011	0	16	2	0
Q4 2011	2	20	8	2
Q1 2012	3	18	6	1
Q2 2012	3	19	8	0
Q3 2012	1	25	7	0
Q4 2012	2	30	5	2
Q1 2013	4	28	3	2
Q2 2013	4	23	1	1
Q3 2013	1	24	2	1
Q4 2013	2	26	2	4
Q1 2014	1	25	1	2
Q2 2014	0	18	1	2
Q3 2014	4	14	1	1
Q4 2014	2	15	1	7
Q1 2015	4	20	2	1
Q2 2015	7	16	2	2
Q3 2015	1	18	0	4
Q4 2015	4	22	0	3
Q1 2016	0	34	2	3
Q2 2016	6	33	1	3
Q3 2016	4	37	1	0
Q4 2016	3	32	3	1
Q1 2017	4	32	0	2
Q2 2017	4	24	1	4
Q3 2017	3	23	2	5
Q4 2017	5	20	1	2
Q1 2018	2	20	0	4
Q2 2018	2	21	1	2
Q3 2018	5	25	0	2
Q4 2018	4	26	1	4
Q1 2019	3	24	0	1
Q2 2019	4	30	1	1

Fallen angels and rising stars exclude issuers with no rated debt outstanding. Defaulted issuers include confidentially rated entities. Data as of June 30, 2019. Source: S&P Global Ratings Research.

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Table 3

European Corporate Rating Actions (Second-Quarter 2019)

Date	Issuer	Sector	Country	Rating action	To	From
April 1, 2019	Horizon Parent Holdings S.a r.l.	Chemicals, packaging, and environmental services	Luxembourg	Upgrade	B+	B
April 2, 2019	Centrica PLC	Utilities	U.K.	Downgrade	BBB	BBB+
April 4, 2019	Debenhams PLC	Retail/restaurants	U.K.	Downgrade	SD	CC
April 4, 2019	Saga plc	Consumer products	U.K.	Downgrade	BB	BB+
April 5, 2019	BNP Paribas	Financial institutions	France	Upgrade	A+	A
April 5, 2019	FAGE International S.A	Consumer products	Luxembourg	Downgrade	B+	BB-
April 8, 2019	Horizon Pharma plc	Health care	Ireland	Upgrade	BB-	B
April 12, 2019	Senvion Holding GmbH (Suzlon Energy Ltd.)	Capital goods	Germany	Downgrade	CC	CCC+
April 15, 2019	Deutsche Lufthansa AG	Transportation	Germany	Upgrade	BBB	BBB-
April 15, 2019	Europcar Mobility Group S.A.	Media and entertainment	France	Upgrade	BB-	B+
April 16, 2019	AB Volvo	Automotive	Sweden	Upgrade	A-	BBB+
April 16, 2019	Covivio S.A.	Homebuilders/real estate companies	France	Upgrade	BBB+	BBB
April 16, 2019	Swiss Life Holding AG	Insurance	Switzerland	Upgrade	A-	BBB+
April 17, 2019	Covivio Hotels (Covivio S.A.)	Homebuilders/real estate companies	France	Upgrade	BBB+	BBB
April 17, 2019	Daily Mail & General Trust PLC	Media and entertainment	U.K.	Downgrade	BB	BB+
April 18, 2019	Kering S.A.	Consumer products	France	Upgrade	A-	BBB+
April 18, 2019	Nexi SpA	Financial institutions	Italy	Upgrade	BB-	B+
April 19, 2019	Casino Guichard - Perrachon S.A.	Retail/restaurants	France	Downgrade	BB-	BB

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Table 3

European Corporate Rating Actions (Second-Quarter 2019) (cont.)

Date	Issuer	Sector	Country	Rating action	To	From
April 24, 2019	ABH Financial Ltd.	Financial institutions	Cyprus	Upgrade	BB-	B+
April 24, 2019	CEVA Logistics AG	Transportation	Switzerland	Downgrade	B+	BB-
April 24, 2019	Galapagos Holding S.A.	Capital goods	Luxembourg	Downgrade	CCC-	CCC+
April 26, 2019	EVN AG	Utilities	Austria	Upgrade	A	A-
April 26, 2019	Rowan Companies PLC (Enesco Rowan plc)	Oil and gas	U.K.	Downgrade	B-	B
April 26, 2019	Samhallsbyggnadsbolaget i Norden AB (publ)	Homebuilders/real estate companies	Sweden	Upgrade	BBB-	BB
April 29, 2019	Kuwait Energy plc	Oil and gas	Jersey	Upgrade	B-	CCC+
May 2, 2019	Senvion Holding GmbH (Suzlon Energy Ltd.)	Capital goods	Germany	Downgrade	SD	CC
May 2, 2019	Thomas Cook Group PLC	Media and entertainment	U.K.	Downgrade	B-	B
May 13, 2019	Constellium N.V.	Metals, mining, and steel	Netherlands	Upgrade	B	B-
May 13, 2019	Weatherford International plc	Oil and gas	Ireland	Downgrade	CC	CCC
May 14, 2019	NIBC Bank N.V.	Financial institutions	Netherlands	Upgrade	BBB+	BBB
May 15, 2019	Evergreen Skills Lux S.ar.l. (Evergreen Skills Intermediate Lux S.ar.l.)	High technology	Luxembourg	Downgrade	CCC-	CCC+
May 16, 2019	Capgemini SE	High technology	France	Upgrade	BBB+	BBB
May 16, 2019	Royal Bank of Scotland Group PLC (The)	Financial institutions	U.K.	Upgrade	BBB	BBB-
May 21, 2019	Credit Suisse AG (Credit Suisse Group AG)	Financial institutions	Switzerland	Upgrade	A+	A

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Table 3

European Corporate Rating Actions (Second-Quarter 2019) (cont.)

Date	Issuer	Sector	Country	Rating action	To	From
May 21, 2019	London Stock Exchange Group PLC	Financial institutions	U.K.	Upgrade	A	A-
May 21, 2019	Tendam Brands S.A.U.	Consumer products	Spain	Upgrade	B+	B
May 22, 2019	Thomas Cook Group PLC	Media and entertainment	U.K.	Downgrade	CCC+	B-
May 23, 2019	Doncasters Group Ltd.	Capital goods	U.K.	Downgrade	CCC-	CCC+
May 23, 2019	Fresenius SE & Co. KGaA	Health care	Germany	Upgrade	BBB	BBB-
May 28, 2019	Cabot Financial Ltd. (Encore Capital Group Inc.)	Financial institutions	U.K.	Upgrade	BB-	B+
May 28, 2019	Casino Guichard - Perrachon S.A.	Retail/restaurants	France	Downgrade	B	BB-
May 31, 2019	Euronext N.V.	Financial institutions	Netherlands	Downgrade	A-	A
June 12, 2019	KCA DEUTAG Alpha Ltd.	Oil and gas	U.K.	Downgrade	CCC+	B-
June 13, 2019	Galapagos Holding S.A.	Capital goods	Luxembourg	Downgrade	CC	CCC-
June 13, 2019	Novomatic AG	Media and entertainment	Austria	Downgrade	BB+	BBB-
June 14, 2019	Motability Operations Group PLC	Financial institutions	U.K.	Downgrade	A	A+
June 19, 2019	Antin Amedes Bidco GmbH	Health care	Germany	Upgrade	B	B-
June 20, 2019	Diamond (BC) B.V.	Chemicals, packaging, and environmental services	Netherlands	Downgrade	B-	B
June 20, 2019	OCI N.V.	Chemicals, packaging, and environmental services	Netherlands	Upgrade	BB	BB-
June 21, 2019	Galapagos Holding S.A.	Capital goods	Luxembourg	Downgrade	SD	CC

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Table 3

European Corporate Rating Actions (Second-Quarter 2019) (cont.)

Date	Issuer	Sector	Country	Rating action	To	From
June 25, 2019	Springer Nature AG & Co. KGaA	Media and entertainment	Germany	Upgrade	B+	B
June 28, 2019	Lecta S.A.	Forest products and building materials	Luxembourg	Downgrade	B-	B

Rating actions exclude entities with no rated debt. Actions on subsidiaries show parents listed in parentheses. Data as of June 30, 2019. Source: S&P Global Ratings Research.

Related Research

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