

Corporate Credit Monthly Update

October 2020

After a rise in COVID-19 cases in the eurozone in September, stricter social distancing and lockdown measures were introduced in several countries, including Spain, France and the UK. As such, COVID-19 remained the main obstacle to economic activity amid signs of an economic contraction in the region. European figures continued to highlight major discrepancies between the manufacturing and service sectors, with fears of a second wave of the pandemic weighing particularly heavily on the service sector's recovery. Meanwhile, uncertainty about the outcome of Brexit took centre stage again in September after a few months on the back burner. A trade deal between the UK and the EU is still a possibility, but the British government's proposed legislation is a sticking point.

Against this backdrop, credit spreads stayed above pre-COVID levels in Europe, despite being considerably below where they were at the height of the crisis. The German 10-year Bund yield dropped 13 basis points to -0.52% over the month. The European corporate index yield ended the month at 3.81%.

In the United States, the Federal fiscal stimulus package boosted consumer spending, which accounts for around 70% of the country's GDP of USD 21 trillion. The housing market is robust, with historically low interest rates appealing to buyers. A wave of fresh COVID-19 infections in certain states has not stalled economic activity as much as we might have feared. The composite PMI index remained in expansionist territory for the third consecutive month and activity gained momentum in both the service and manufacturing sectors. However, the pace of growth was slower than it had been in August. With one month to go before the US presidential elections, the possibility of a contested election is a key concern. Many investors are expecting a ballot recount and so have hedged their positions – some until January 2021 according to futures contracts.

On the credit market, new bond issuance stabilised in the third quarter after reaching record highs in Q2. Credit spreads became both narrower and less uniform, compared with levels at the end of March, which were the highest seen since the financial crisis of 2008. Investment grade securities' risk premia fell substantially after new measures were introduced by the Federal Reserve. The yield on 10-year US Treasury bills only fell by 3 basis points over the month, to +0.68%. The US corporate index stands at 4.99%.

Most economic indicators suggest that business activity is recovering in emerging markets, albeit unevenly across the regions. In China, a V-shaped recovery seems to be emerging. Economic forecasts in Brazil and Turkey were better than expected. The Turkish central bank announced a surprise interest rate hike (+2%) after a wave of cuts. This measure is intended to stop the Turkish lira from weakening further and limit the extent to which domestic investors choose to hold assets denominated in strong currencies. In a surprise move, Argentina announced new capital controls for local companies with short-term debt denominated in dollars.

Emerging market bond yields remained high in Q3 despite falling relative to Q2. Credit spreads between sovereign bonds and corporate bonds changed very little. Corporate bond issuance reached USD 113 billion in Q3 as issuers made the most of these lower levels. In this context, the EM corporate index yield stood at 7.34%.

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Companies in the Spotlight

Thyssenkrupp Elevator

Thyssenkrupp's results were better than expected. The overall order intake development in Q3/19-20 was relatively resilient, given the pandemic-related impact on the company's markets. Positively, there has been no margin pressure so far for new contracts, and tendering activity has stayed robust. As a result, management upgraded its guidance for 2020 and now calls for order intake and sales to fall in the low single-digit percentage level, with adjusted EBIT either remaining stable or up in the low single-digit percentage area.

ServiceMaster

ServiceMaster, a US-based specialist in termite and pest control, home cleaning and inspection, detailed the proceeds of its USD 1.1bn (after tax proceeds) sale of the ServiceMaster brand business to Roark Capital. The company will change its name to Terminix and termite and pest control will become the entire strategic focus of the company. Proceeds will target the retirement of the 2024 HY bond and a portion of the Term Loan B. The company will, for now, operate below its 2.5x-3.0x net leverage target. However, it will also enter into a three-year USD 400m stock repurchase programme.

Tecnoglass

Tecnoglass manufactures and sells architectural glass, windows and related products. The company offers its products throughout North, Central and South America and serves the global residential and construction business. Its main plant is based in Colombia, benefiting from both a competitive workforce and quick access to Colombian ports in order to serve the US market. In 2019, Tecnoglass achieved revenues of USD 431m for an adjusted EBITDA of USD 88m, while its net leverage ratio reached 2.7x. The company is listed on the NYSE, but circa 60% of the shares are still held by its founders, the Daes brothers.

Significative Primary Issues

EUR				
Issuer	Coupon	Maturity	Amount	Rating
Lorca Telecom	4.00%	2027	€720M	B1
Maxeda	5.00%	2080	€1Bn	Ba1
US				
Issuer	Coupon	Maturity	Amount	Rating
Tenet Healthcare	6.125%	2028	\$2.5Bn	CCC+
Yum Brands	3.625%	2031	\$1.05Bn	B+
EM				
Issuer	Coupon	Maturity	Amount	Rating
Arcos Dorados	5.875%	2027	\$150M	B2
Cemex SAB de CV	5.20%	2030	\$1Bn	BB

Rating moves

British Airways	Moody's	▼	Ba2
Europcar	Moody's	▼	Caa2
Garrett Motion	Moody's	▼	Caa1
IAG	Moody's	▼	Ba2
Merlin Entertainments	S&P	▼	CCC+
Rolls-Royce	S&P	▼	BB-
Sappi	S&P	▼	BB-
Selecta	S&P	▼	CC
Teva	S&P	▼	BB-
Trivium Packaging	S&P	▼	B
Unibail-Rodamco-Westfield	Moody's	▼	Baa1
Vale	Fitch	↗	BBB

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Macro Economic Events

Eurozone: the EU is aiming to increase the region's GDP by 3% by 2027 through a new programme of green and social bonds. Demand for green bonds has been high among environmentally aware investors for a number of years, but now major governments are getting involved too. European countries play a leading role in this area. Germany, Europe's largest economy, recently issued a green 10-year sovereign bond that attracted record demand, raising EUR 6.5 billion.

Germany: despite the ongoing second wave of coronavirus infections, the fact that the business climate indicator for German SMEs recorded its fifth consecutive rise was a reassuring sign. The confidence index ended September up slightly at 93.4 compared with 92.6 a month earlier. Nevertheless, the resurgence of the pandemic -on an alarmingly large scale that could put the recovery in jeopardy- may prove an ever-greater obstacle for the economy.

France: activity in the manufacturing sector in France fell again in August. The PMI index fell to 49.8 from 52.4 in July. according to its 2021 budget released in late September, the French government plans to safeguard the economy from the impact of the coronavirus pandemic by injecting a stimulus of EUR 42 billion next year. The French economy is expected to shrink by 10% this year, which would constitute its worst recession since the Second World War.

United States: Democrats and Republicans may agree the details of a new set of measures aimed at helping companies and individuals and stimulating economic growth, with a proposed budget in the region of USD 2 trillion. This would be a substantial addition to the spending commitments already made by the US authorities since the start of the COVID-19 crisis.

China: the latest macroeconomic data shows sustained growth for the tertiary sector and an uptick in tourism against a backdrop of limited numbers of COVID-19 cases.

Japan: Shinzo Abe, the Japanese Prime Minister, suddenly resigned for health reasons, a year ahead of the planned date. the Japanese parliament elected Yoshihide Suga as the country's new Prime Minister after the surprise resignation of Shinzo Abe on health grounds. A close ally of the outgoing Prime Minister, Yoshihide Suga should continue the policies pursued by his predecessor.

Argentina: the central bank raised its rates by 200 basis points, whereas the consensus view was that no changes would be made. This decision was taken with a view to upholding price stability with the lira at historically low levels.

Market Data Indices (end of September)		Performance		Duration	Yield
High Yield		MTD*	YTD*	DTW*	YTW*
HE00	High Yield Europe	-0.61%	-2.55%	3.87	4.13%
JOA0	High Yield United States	-1.04%	-0.23%	3.78	5.74%
H7PC	High Yield Europe BB/B Excluding Financials	-0.74%	-3.18%	3.80	3.81%
JC4N	High Yield United States BB/B Excluding Financials	-1.24%	0.48%	3.88	4.99%
HYEF	High Yield Emerging Countries Excluding Financials	-1.03%	0.81%	3.40	7.34%
Investment Grade					
ER00	Investment Grade Europe	0.35%	0.68%	5.28	0.53%
COA0	Investment Grade United States	-0.26%	6.61%	8.16	2.06%
EMIC	Investment Grade Emerging Countries	-0.17%	4.24%	5.77	2.31%
Governments					
G4D0	10-Year German Bond	0.84%	2.47%		-0.52%
G402	10-Year US Bond	0.27%	11.40%		0.68%

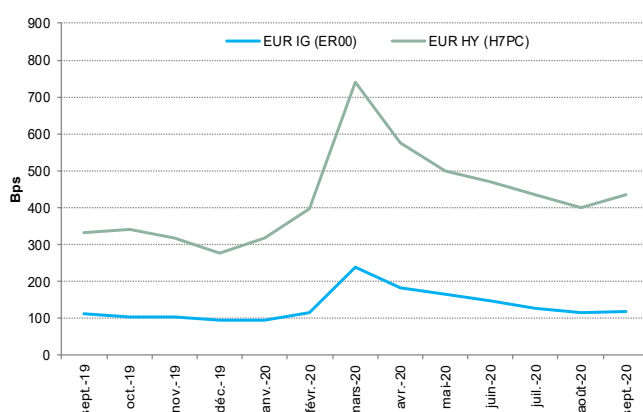
Inflation (end of September)						
Expected inflation		September	August	July	6M	12M
EURO INF	Expected inflation for 2020 in Europe	0.40%	0.40%	0.40%	1.00%	1.20%
US INF	Expected inflation for 2020 in the United States	1.10%	1.00%	0.90%	1.70%	1.80%
Realized inflation		September	August	July	6M	12M
EUR CPI	Realized inflation in Europe (rolling 12-month)	-0.30%	-0.20%	0.40%	0.70%	0.80%
US CPI	Realized inflation in the United States (rolling 12-month)		1.30%	1.00%	1.50%	1.70%

*MTD = Month-to-date, YTD = Year-to-date, DTW = Duration-to-worst, YTW = Yield-to-worst

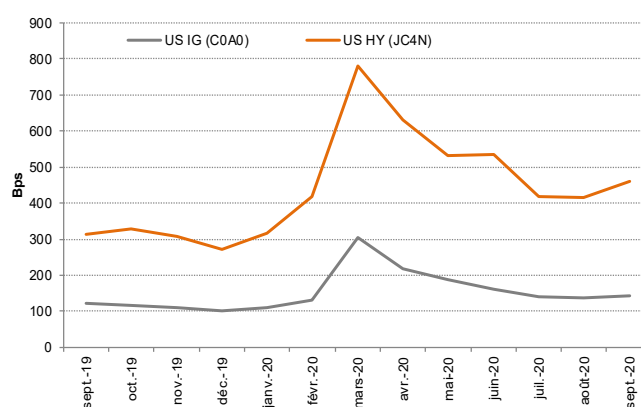
Source : Merrill Lynch

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EUR Corporate Bond Spreads (OAS) by Index



US Corporate Bond Spreads (OAS) by Index



Corporate Bond Spreads		September	August	July	12 months
Europe					
ER00	Investment Grade Europe	117	114	127	111
HE00	High Yield Europe	477	450	491	373
H7PC	High Yield Europe BB/B Excluding Financials	439	406	441	339
ER30	Bonds rated A Europe	96	92	104	93
ER40	Bonds rated BBB Europe	146	142	159	135
HE10	Bonds rated BB Europe	363	330	366	262
HE20	Bonds rated B Europe	618	582	624	530
United States					
C0A0	Investment Grade United States	139	131	137	120
J0A0	High Yield United States	542	503	519	417
JC4N	High Yield United States BB/B Excluding Financials	467	419	425	334
C0A3	Bonds rated A United States	103	95	99	93
C0A4	Bonds rated BBB United States	178	170	180	154
JUC1	Bonds rated BB United States	400	355	359	251
JUC2	Bonds rated B United States	578	532	552	439
Emerging Countries					
EMIC	Investment Grade Emerging Countries	193	187	204	158
HYEF	High Yield Emerging Countries	709	672	722	559
EMAQ	Bonds rated A Emerging Countries	145	139	153	120
EM2B	Bonds rated BBB Emerging Countries	250	242	264	209
EM3C	Bonds rated BB Emerging Countries	473	461	500	361
EM6B	Bonds rated B Emerging Countries	884	789	849	626

Source : Merrill Lynch

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Anaxis Asset Management

Anaxis specialises in corporate credit for investors who firmly believe in fundamental investing based on in-depth knowledge of issuers. For more than 10 years, Anaxis has focused on corporate credit strategies and has developed comprehensive expertise and methods renowned for their reliability by its clients.

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