News Release

January 12, 2023

Jon Teall 212 317-8296

IACPM

IACPM Credit Outlook Survey Strongly Forecasts Rising Corporate Defaults Globally Over the Next 12 Months; No Region Will Be Spared; Timing Remains Elusive

New York, NY – Respondents to the latest IACPM Credit Outlook Survey overwhelmingly forecast rising corporate defaults globally over the next 12 months. Ninety one percent of respondents expect defaults to rise in Europe. Eighty eight percent say defaults will increase in North America and 68% think they will rise in Asia. At the same time, respondents point out defaults remained low last year despite higher inflation and rapidly rising interest rates. Indeed, there has not even been much credit deterioration.

"After more than 15 years of exceptionally low interest rates and few defaults, we now have higher interest rates," commented Som-lok Leung, Executive Director of the International Association of Credit Portfolio Managers. "But, as we're seeing, it's taking time for defaults to rise. As our survey respondents noted last summer, corporations, particularly in the United States, were flush with liquidity. Many of them borrowed money when interest rates were low and those loans had not yet come to maturity. This has helped shield these companies from rising interest rates, at least for the time being."

While a deluge of defaults has not taken place so far, that could change in either the near term, later in 2023 or perhaps even later than that. Fresh signs could come as soon as the next few weeks as corporations, including banks, report quarterly earnings results. That said, distress signals have been limited thus far to particularly vulnerable sectors, such as leveraged lending and energy credits impacted by the war in Ukraine.

“It’s still early in the cycle,” noted Mr. Leung, “and we may not see the full impact of higher interest rates and other factors, such as big layoffs at a number of large corporations, until the end of 2023.”

Financial markets appear to be pricing in an easier interest rate environment in the second half of the year after exceptional tightening last year and in the face of central banks continuing public resolve to raise rates until inflation is under control. Key questions going forward are how high will rates rise and how long will they stay at higher levels.

“Obviously, there will be fewer defaults if rates only go as high as five percent, instead of seven,” said Mr. Leung. “Additionally, we’ll have to see how long rates stay at elevated levels because, naturally, the longer they remain higher, the bigger the impact.”

Survey respondents are forecasting wider credit spreads globally over the next three months, even though spreads have actually narrowed recently in Europe. The Credit Spread Outlook Index for European Investment Grade Debt is minus -41.4 in the latest reading but that is an improvement from negative -64.5 last quarter. The Outlook Index for European High Yield Debt is currently minus -51.9 versus negative -66.7 in the previous reading. Sixty two percent of respondents say credit spreads will widen on North American Investment Grade Debt. Seventy four percent believe spreads will widen on North American High Yield Debt.

While the latest Outlook Survey calls for deteriorating credit conditions in the form of rising defaults and wider credit spreads, a possible soft landing is not completely off the table. At least some survey respondents say it is possible a recession could be put off until 2024 which might create some disruption in financial markets but would give corporations more time to strengthen their balance sheets.

The Credit Outlook Survey is conducted among members of the IACPM, an association of 136 financial institutions in 29 countries around the world. Members include portfolio managers at many of the world's largest commercial banks, investment banks and insurance companies, as well as a number of asset managers. Members are surveyed at the beginning of each quarter.

Survey results are calculated as diffusion indexes, which show positive and negative values ranging from 100 to minus -100, as well as no change which is in the middle of the scale and is recorded as "0.0." Positive numbers signify an expectation for improved credit conditions, specifically fewer defaults and narrower spreads, while negative numbers indicate an expectation of deterioration with high defaults and wider spreads.

About IACPM

The IACPM, with over 136 member institutions located in 29 countries, is a professional association dedicated to the advancement of credit portfolio management. The organization's programs of meetings, studies, research and collaboration are designed to increase awareness of the value and the function of credit portfolio management among financial markets worldwide, and to discuss and resolve issues of common interest to its members.