PILFOR
LENDING SOUNDNESS

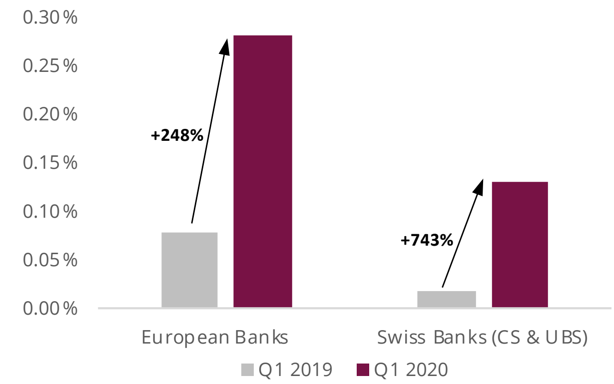
April 2020

Monthly Market Insights

COVID-19 loans vs. banks' risk ab<sorption capacities

April saw rescue packages worth several trillion unfold that governments around the world had started putting together in order to keep their shut-down economies afloat, assisted by their central banks resuming or accelerating balance sheet expansions by means of directly or indirectly lend against corporate bond collaterals. Most guarantee schemes expect commercial lenders to assume some residual risk. Banks at the same time were busy with increases of their loan loss provisions multiple-fold. This highly cyclical provisioning led the BoE to warning calls not to curb banks' lending ability in times of dire need. The Swiss scheme consisting of fully guaranteed "COVID19 loans" up to CHF 0.5 m and "COVID19 loans plus" for up to CHF 20 m and 85% government guaranteed got international attention. The former loan scheme went so smoothly that the Government doubled the volume to CHF 40 bn shortly after. Execution speed and volumes of the latter not surprisingly lacked similar success.

European and Swiss Banks' loan loss provision

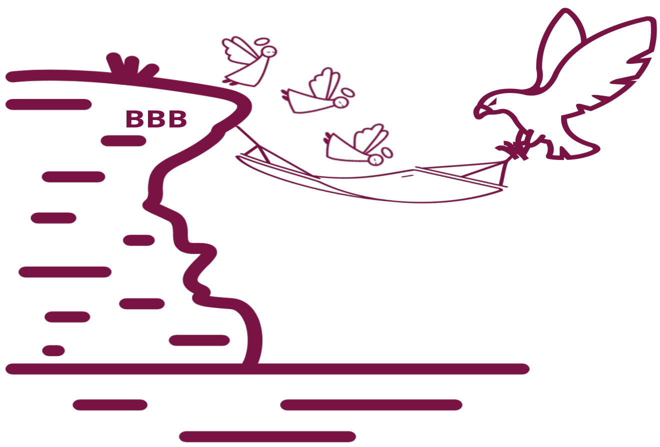


Source: Quarterly reports of Standard Chartered, RBS, Lloyds, HSBC, Barclays, DB, SG, Santander, CS, UBS

High yield market

Supported by abundant liquidity and ultra low rates corporates over the years increased leverage to the benefit of share performance and M&A, inflating the "BBB" rating segment to USD 5,700 bn, equaling more than half of total investment grade universe. The question in the virous-infected environment focuses on "fallen angels", i.e. the loss investment grade ratings by way of downgrade. The FED recognized the systemic risk and strengthened their wings amid first casualties of Ford, Kraft Heinz, and Occidential Petroleum. Expected fallen angels debt volume in 2020 is set to reshape the global HY market by an estimated USD 640 bn, both in terms of size and spread levels in the absence of adequate mitigating measures. It remains to be seen how well markets are able to absorb bonds from companies with weaker credit profiles in these highly volatile times where investors have stopped hunting for yield in exchange for safer haven rating classes.

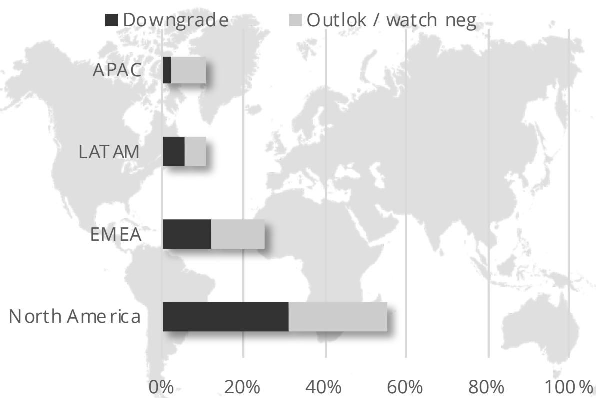
Central banks to the rescue of Fallen Angels



Rating market

The negative rating actions in April were unprecedented, more than doubling to north of 1'500 in the case of S&P, with Fitch and Moody's following suit. Downgrades accounted for nearly half of the rating actions with ¼ relating to a multi-notch downgrade. Sectors most impacted are Automotives, Media & Entertainment, Transportation, Capital goods and Retailing. Q1 results have highlighted the impact of the pandemic, resulting in dropping full year guidances, dividend cuts, postponements of investments and utmost efforts to secure liquidity. As we further move into Q2, it is safe to say that the balance has clearly shifted in favour of creditors vs borrowers. Shareholder value has made room for bondholder value, by means of searching for fundamental corporate soundness, solid capital structures with ample equity cushions, sustainable credit ratings and management's ability to navigate through stormy waters.

No near-term of the rating toll curve expected



Source: S&P (1542 corporates, sovereigns and project finance up to 28.04.2020)

PILFOR is an independent and specialized debt & capital advisor establishing and optimizing
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