



FitchRatings

Richmond Federal Reserve

John Olert, Chief Credit Officer

Date May 13, 2014



Tapering

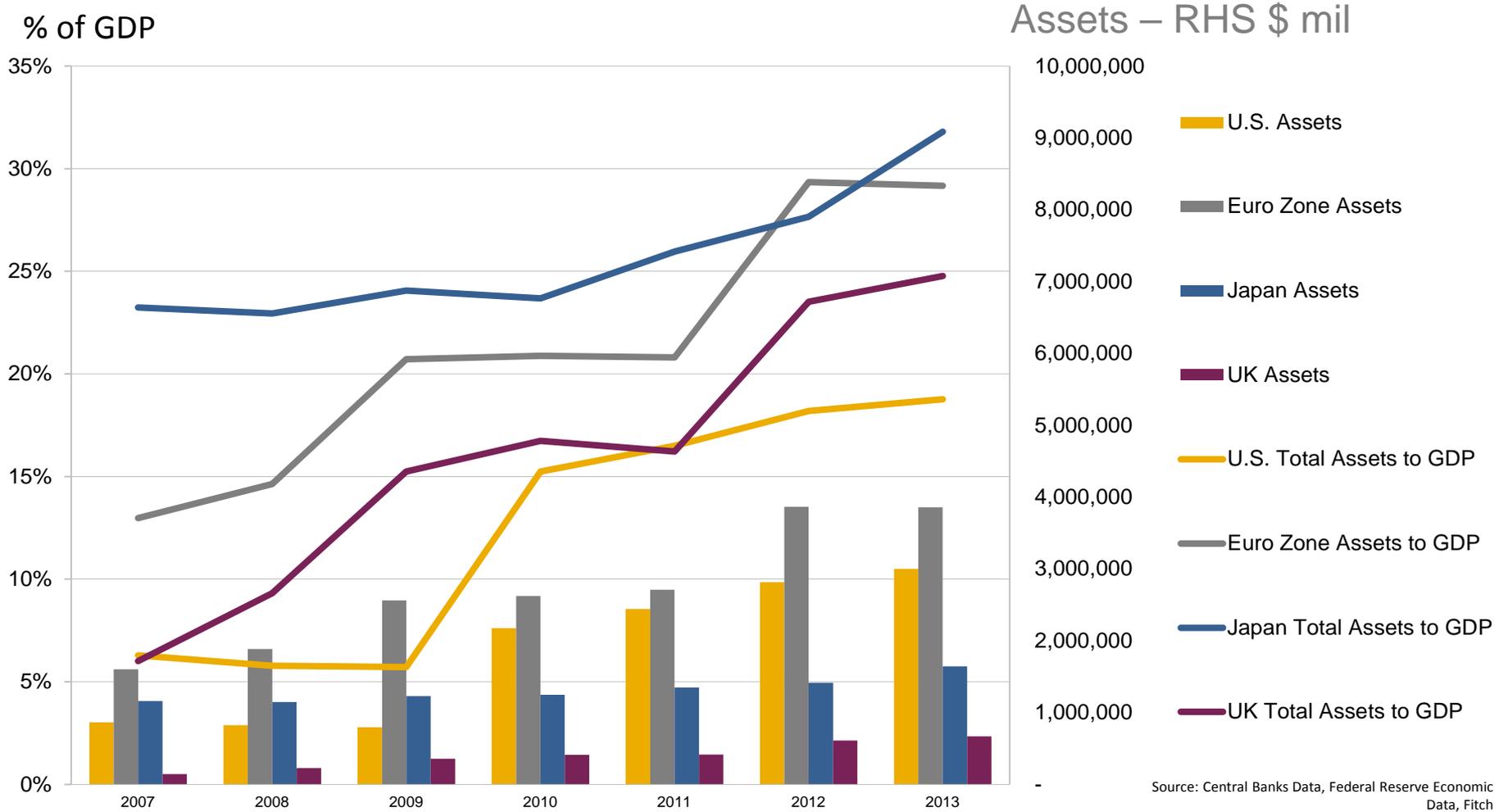
Accommodative Policy

**Risk Radar – Conducive to
Tapering**

Benefits & Consequences

Valuations

Central Banks Assets to GDP

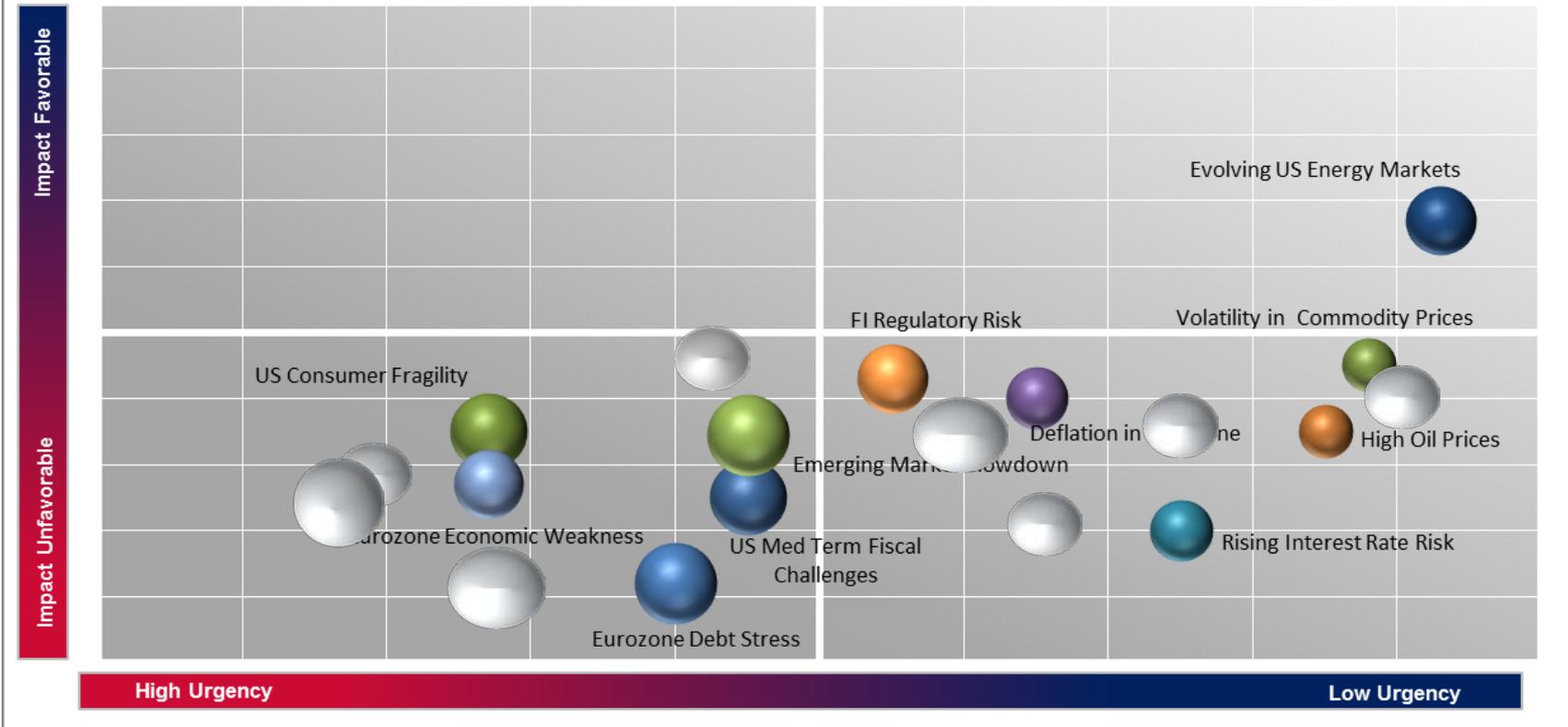


Growth Forecasts Slowly Improving

	US		EZ		China	
	Fitch	Oxford	Fitch	Oxford	Fitch	Oxford
• 2014	• 2.8	• 3.0	• 1.1	• 0.9	• 7.3	• 7.3
• 2015	• 3.1	• 3.4	• 1.4	• 1.4	• 7.0	• 6.8
• 2016		• 3.3		• 1.4		• 7.1

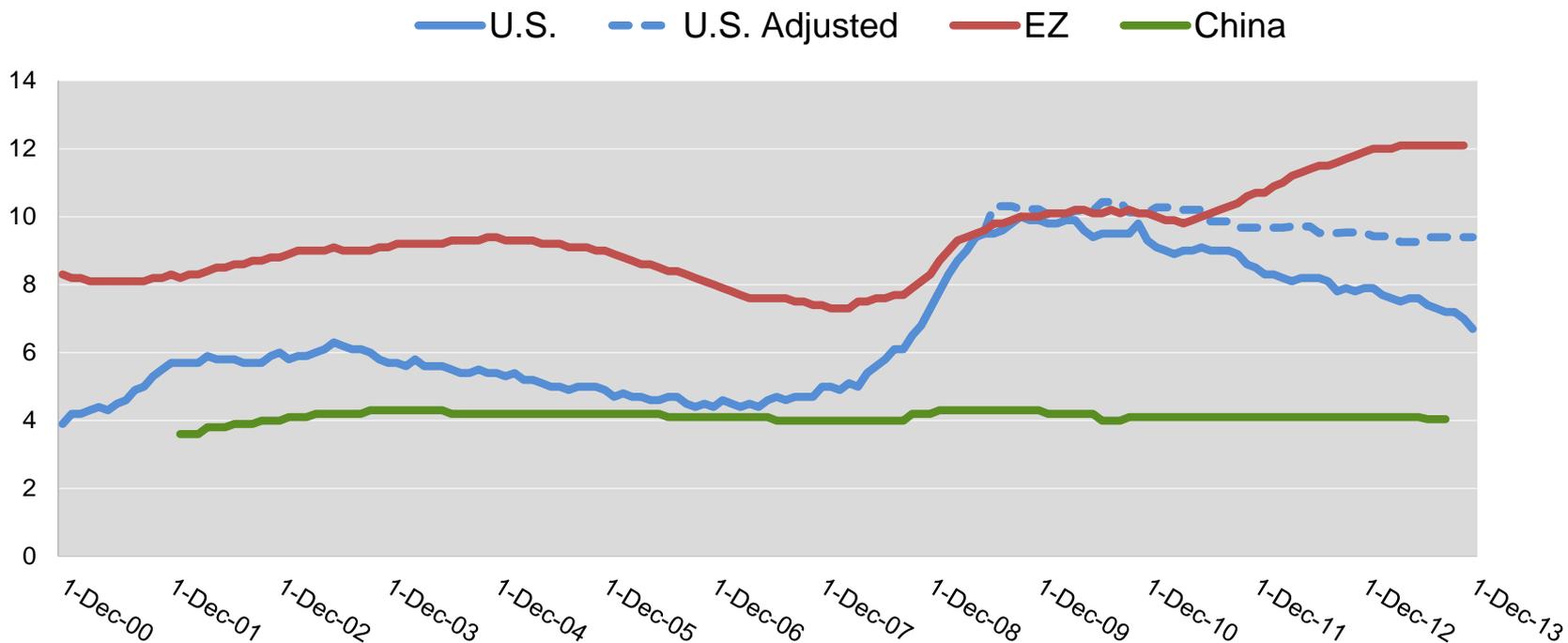
- Fitch Global Economic Outlooks is for some growth improvement.
- Tapering by US Fed is positive economic sign.
- Recovery in Eurozone but pace expected to be slow.
- China growth slowing, but remains significant.

Global Macro Factors Impacting Credit



Diverging Employment Picture

Unemployment Rates

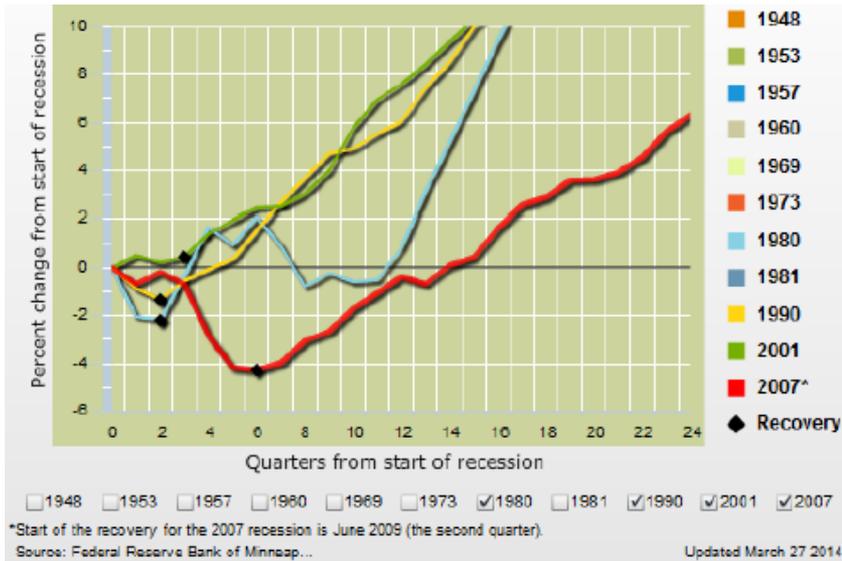


Source: FactSet Economics Standardized Database

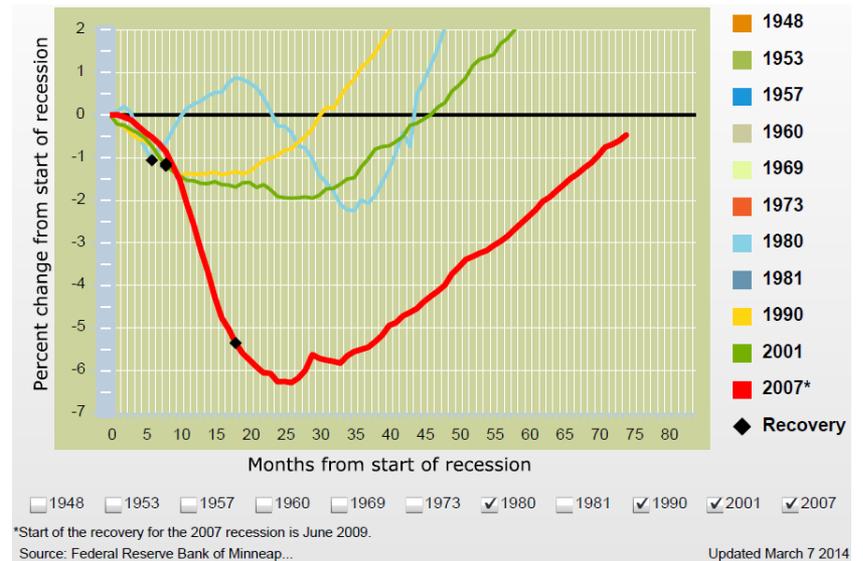
- Unemployment challenging in DM, Fully recovered in China.

Comparing Output and Employment

US Output



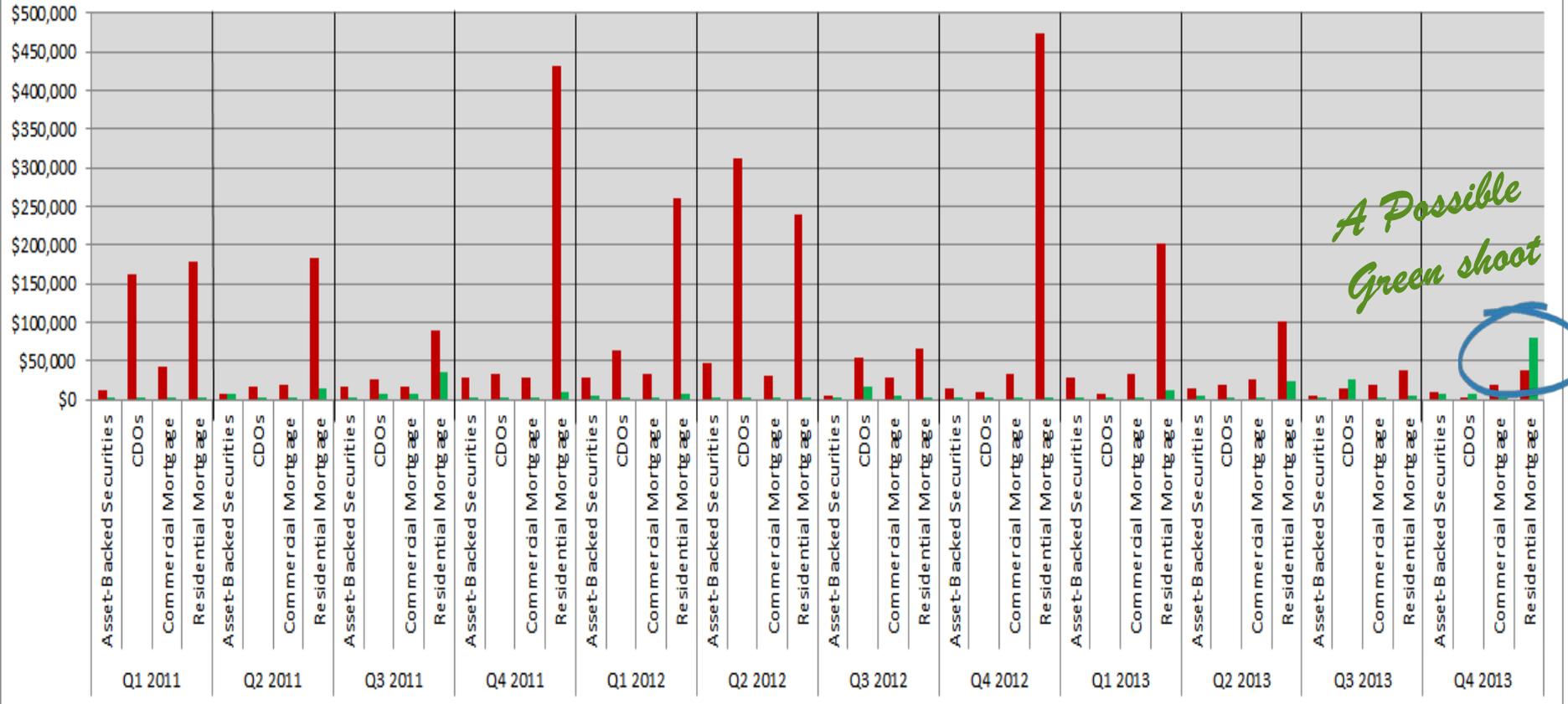
US Employment



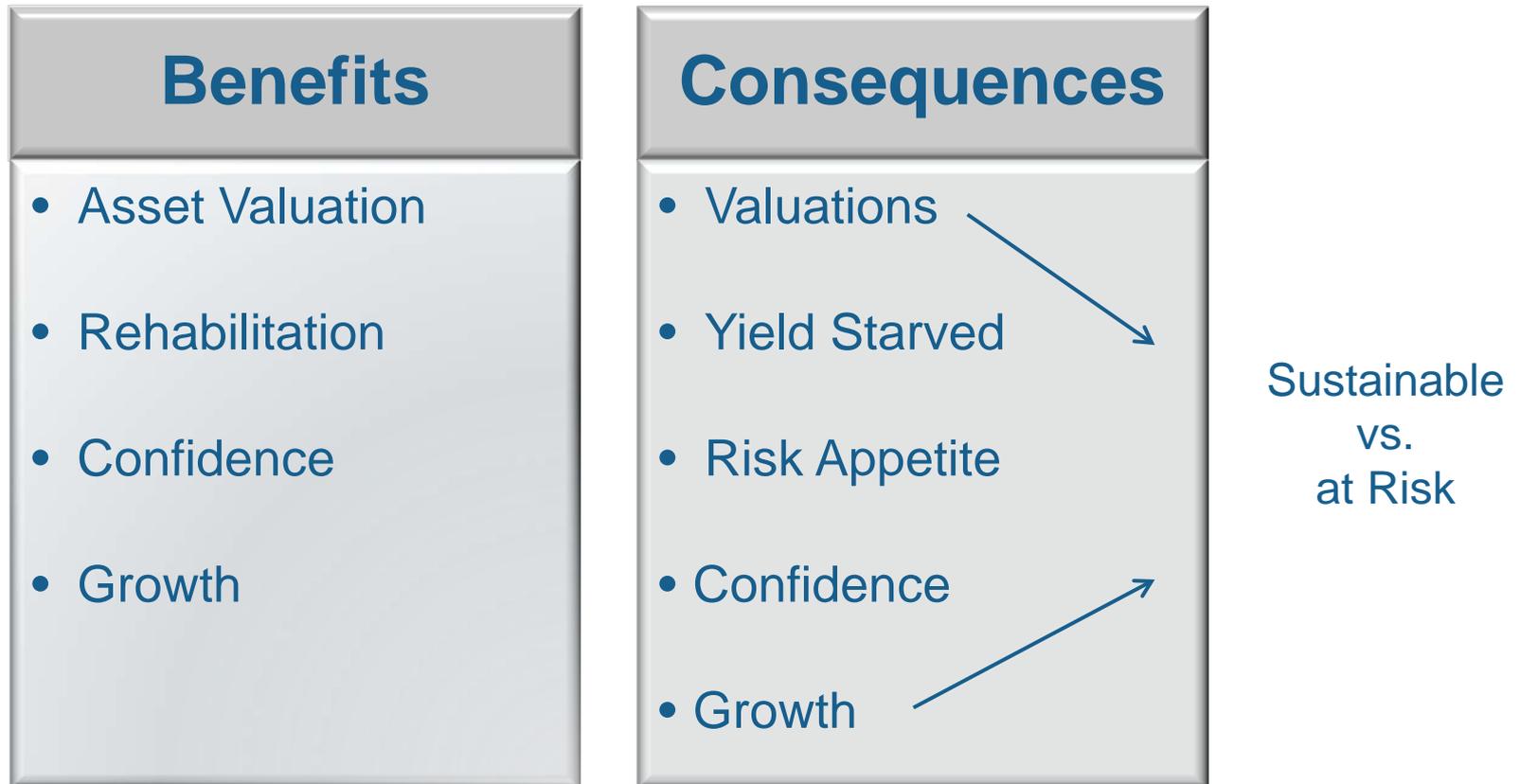
SF: Quarterly Rating Change Snapshot

Global SF Outstanding Amt (\$millions) by MS2: Upgrades vs. Downgrades

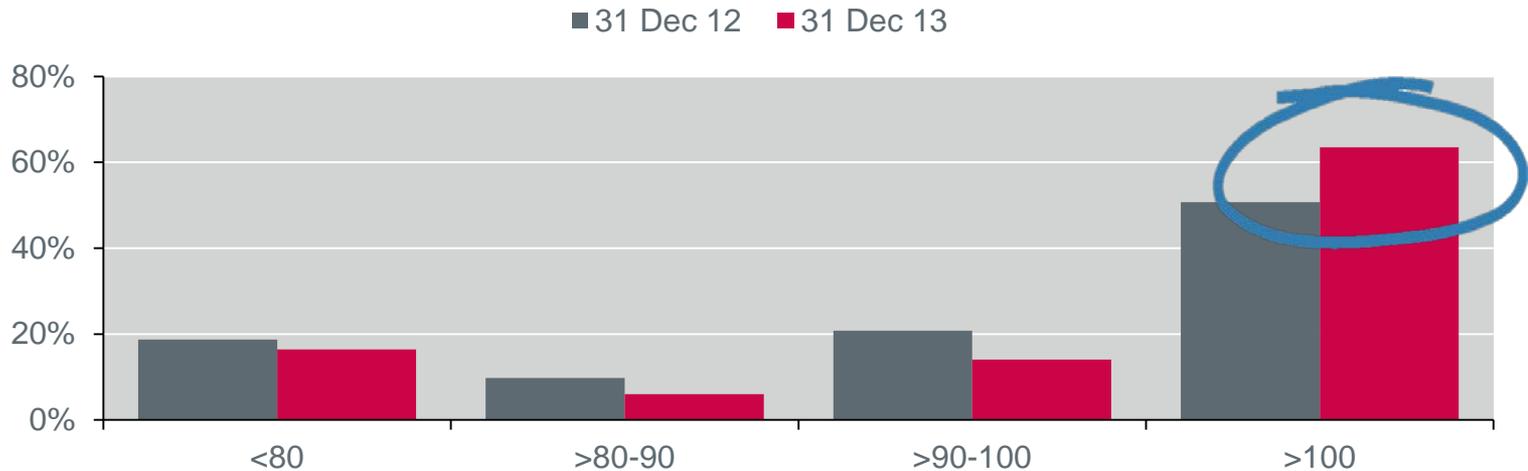
Downgrade Upgrade



Benefits & Consequences

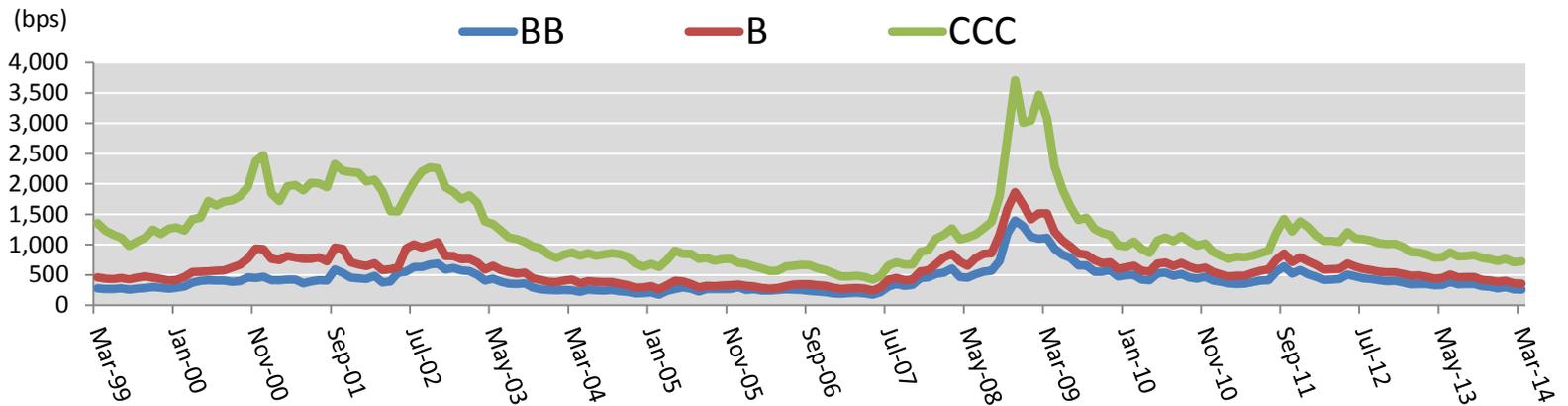


Valuations – CCC Pricing



Source: Fitch U.S. High Yield Default Index, Bloomberg, Advantage Data.

Corporate Spreads



Issuance Trends for US High Yield Bonds & Loans

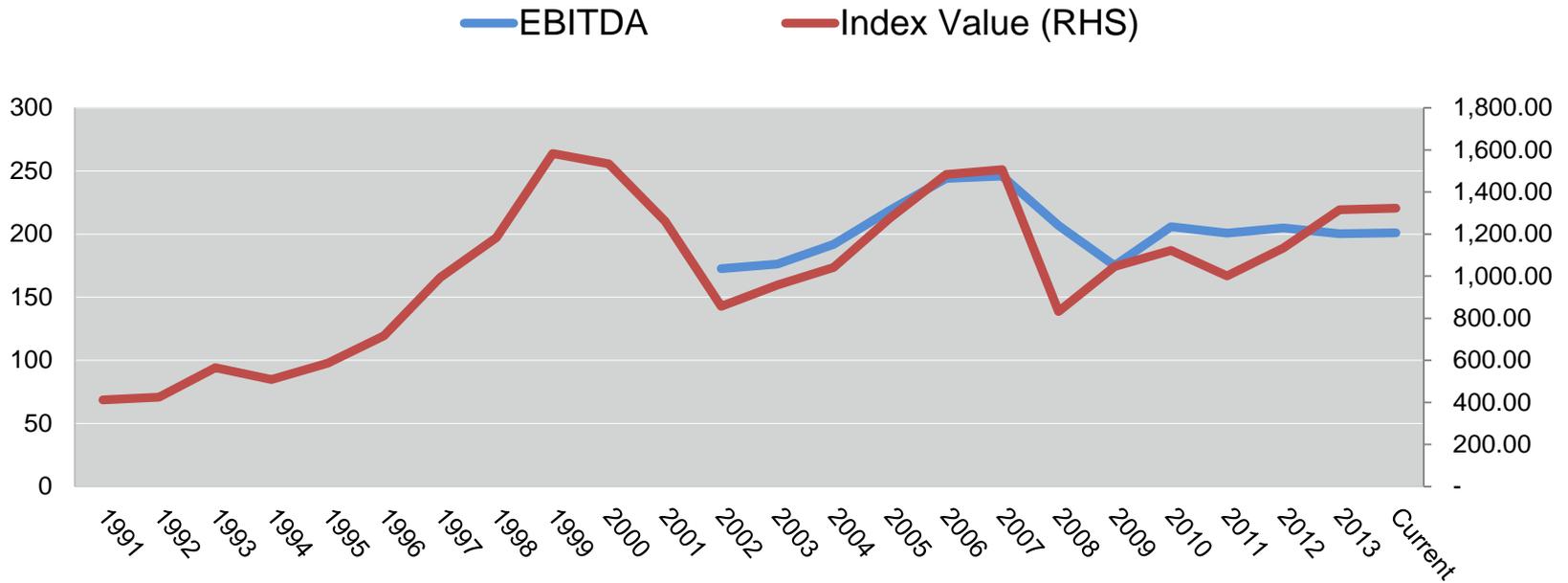
(Billions of U.S. dollars)

	High-Yield Bond Ratings					Weaker Underwriting of High-Yield Bonds			Leveraged Loans	Weaker Underwriting of Leveraged Loans			CLOs
	BB	B	CCC	NR	Total	Zero Coupon	PIK Toggle	Total	Total	Second- lien	Covenant- lite	Total	Total
2007	31.8	67.0	50.6	4.4	153.9	0.5	17.5	18.0	388.8	30.2	115.2	145.3	93.1
2008	14.1	25.7	12.9	2.5	55.2	0.5	6.6	7.1	72.4	3.0	2.5	5.5	18.0
2009	58.9	103.5	14.9	2.2	179.5	0.0	1.9	1.9	38.3	1.5	2.7	4.3	0.6
2010	80.1	177.7	39.3	6.6	303.7	0.3	0.9	1.2	158.0	4.9	8.0	12.9	4.2
2011	80.4	131.9	39.8	5.3	257.4	1.0	3.7	4.6	231.8	7.0	59.1	66.1	13.2
2012	103.6	195.5	57.3	9.3	365.7	0.0	7.0	7.0	295.3	17.2	97.5	114.7	55.5
2013	128.8	172.4	72.9	4.2	378.3	0.0	15.2	15.2	454.9	28.9	279.1	308.0	82.2

Sources: Bank of America Merrill Lynch; and IMF staff estimates

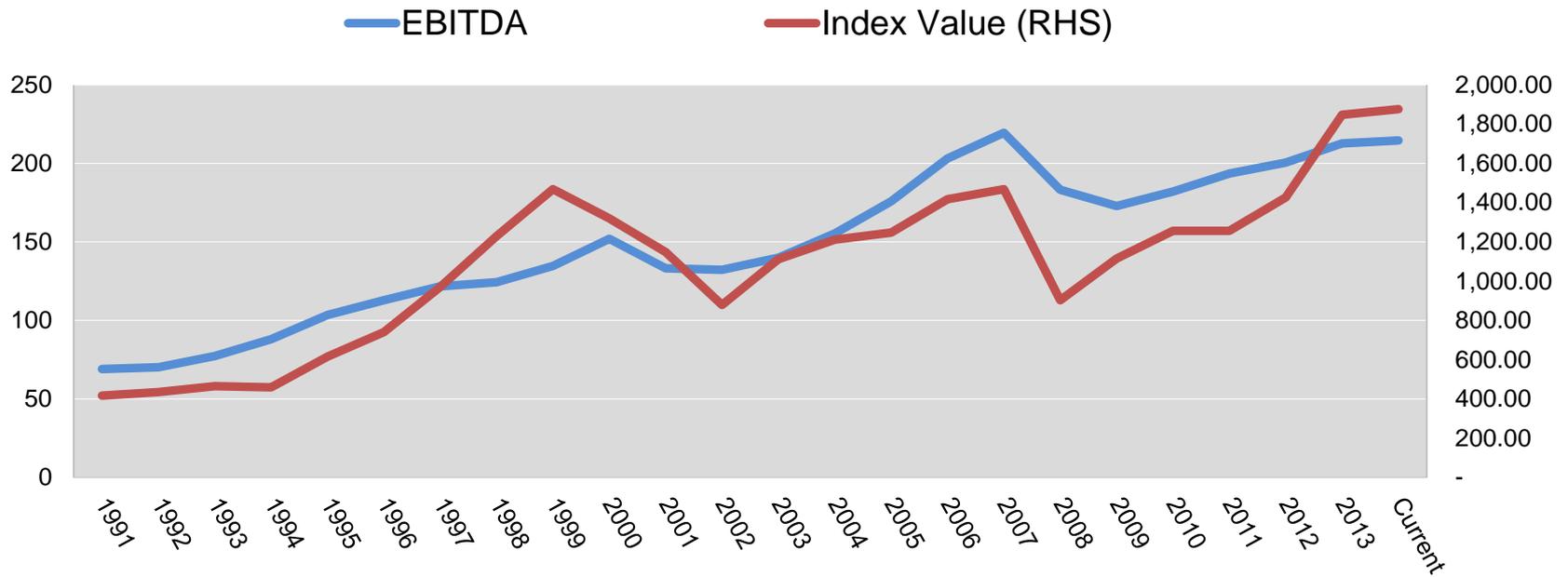
Note: CLOs = collateralized loan obligations; NR = not rated; PIK = payment-in-kind.

FTSE Euro 300 Index



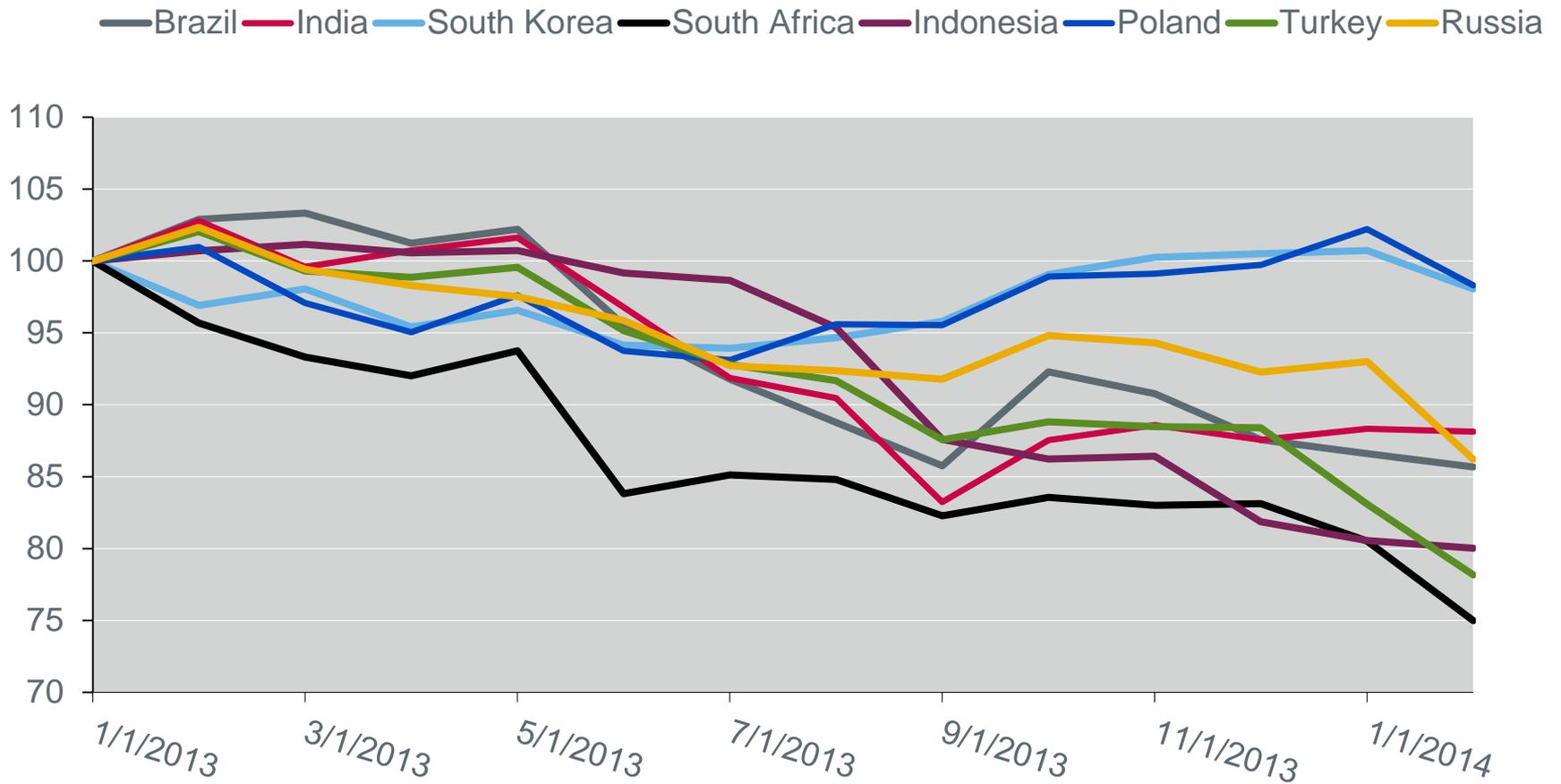
Source: Bloomberg

SPX 500 Index

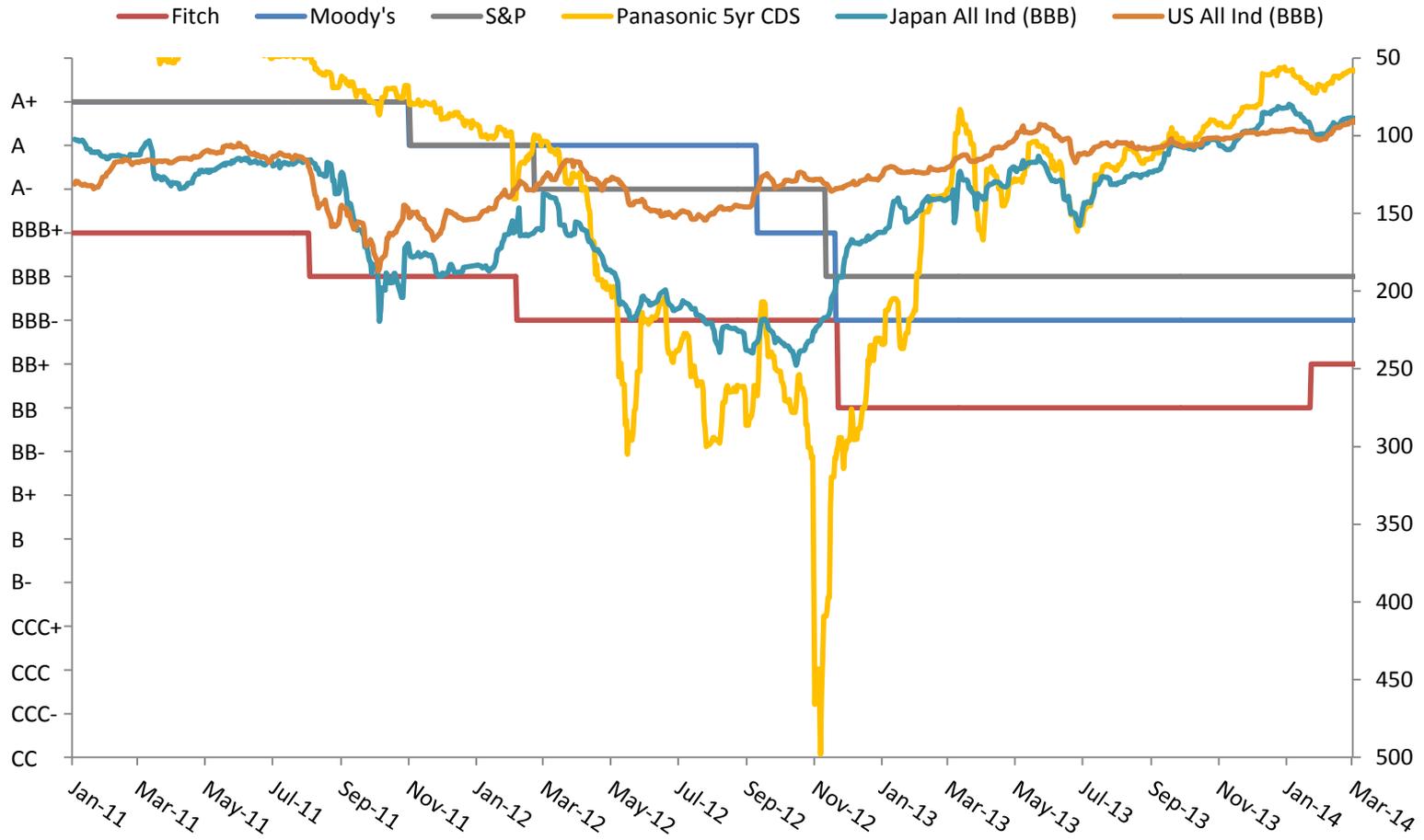


Source: Bloomberg

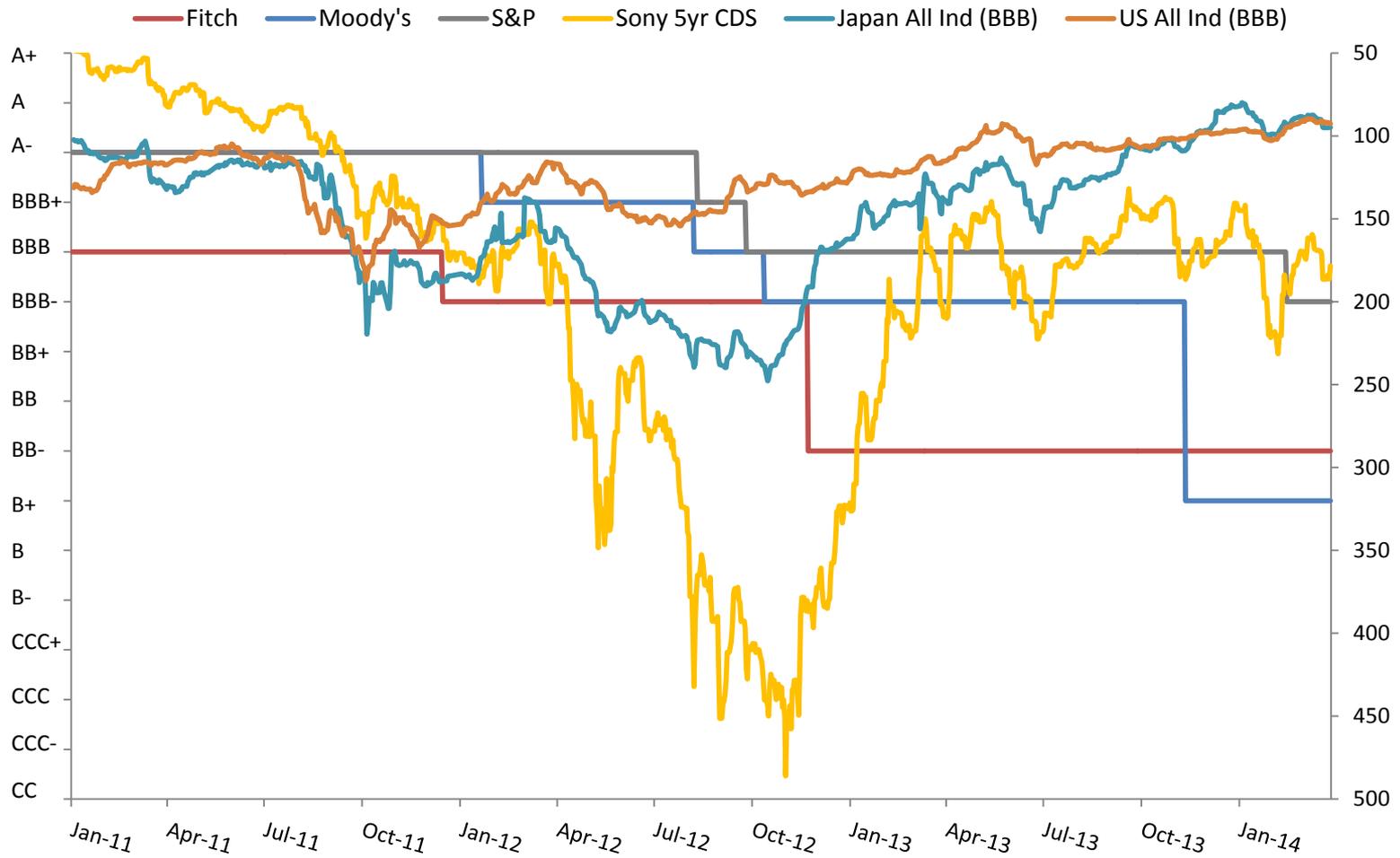
EM Challenges: FX Variability



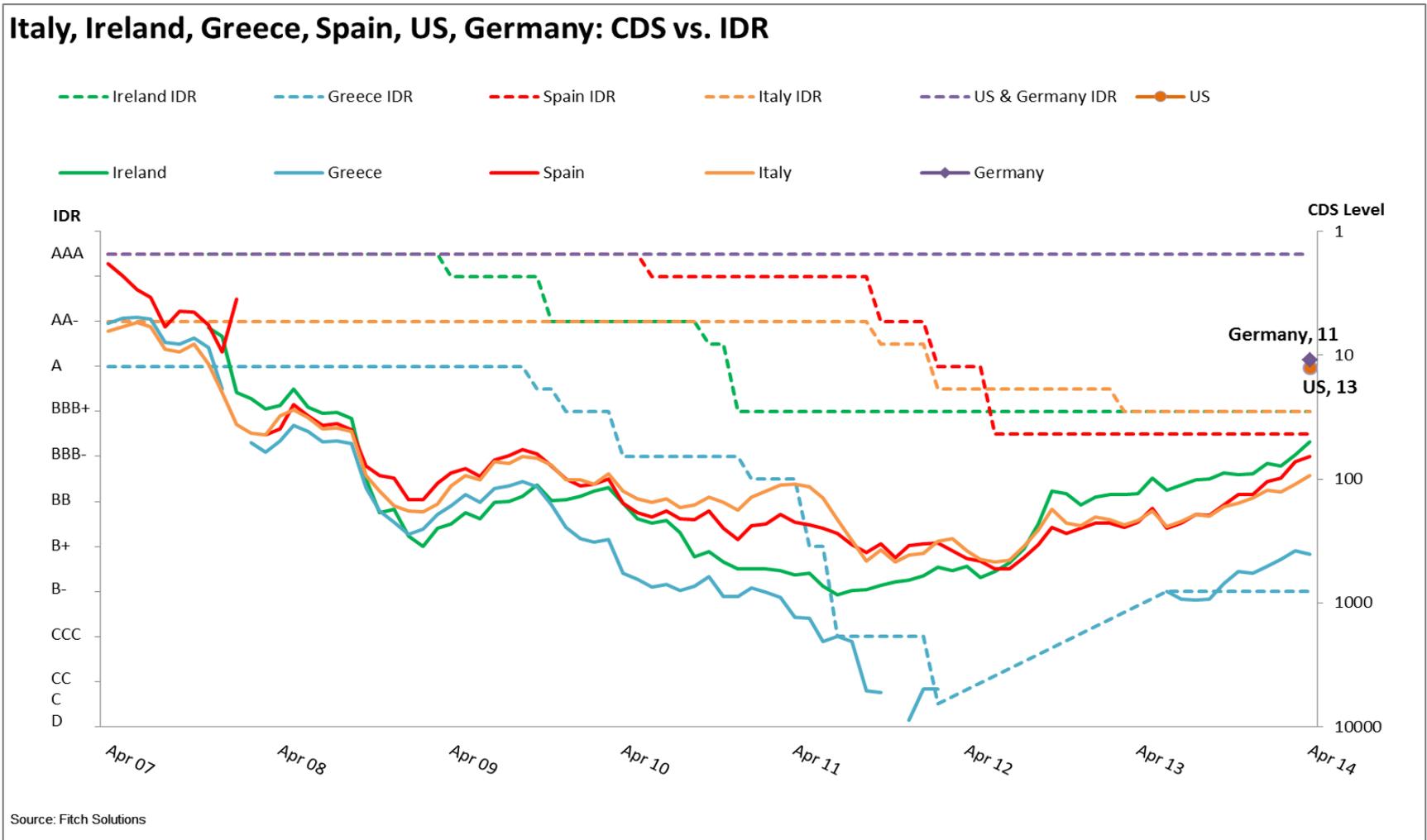
Panasonic



Sony



CDS Spreads



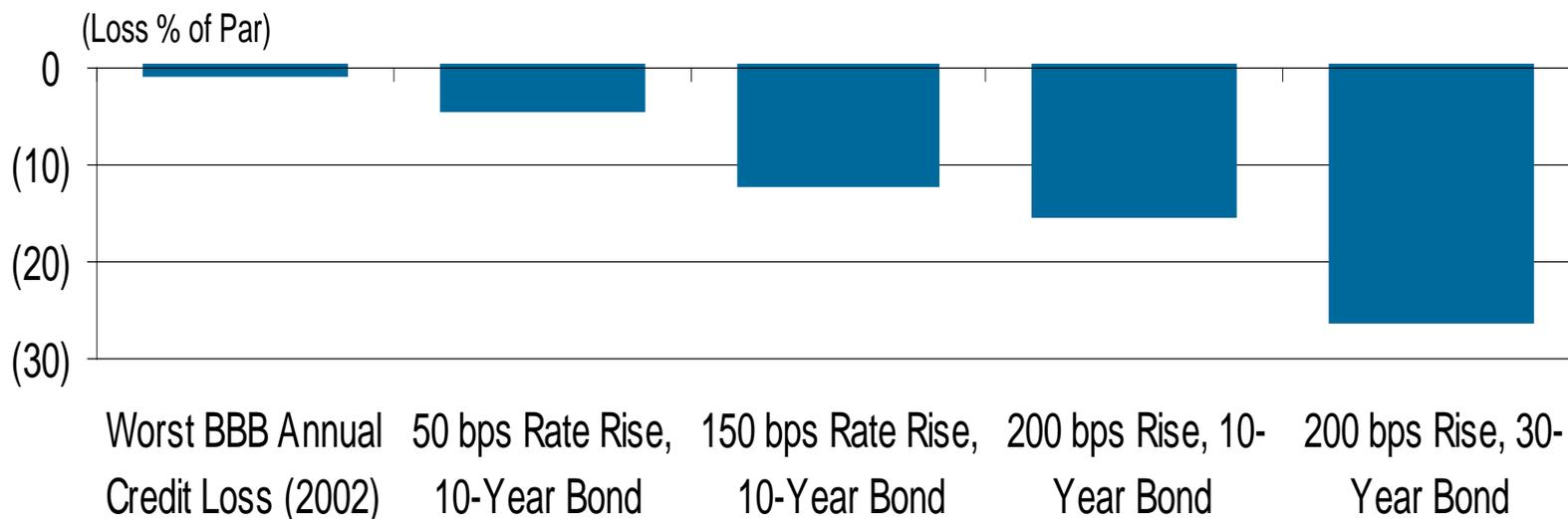
Implications

Rising Interest Rates Could Impact Housing Affordability

	Today				
30 Year Mortgage Rate	4.30%	4.80%	5.30%	5.80%	6.30%
Mortgage Payment per Month (\$)	792	792	792	792	792
Implied Mortgage Balance (\$)	160,000	150,914	142,587	134,945	127,921
Home Price (\$)	200,000	188,643	178,234	168,681	159,901
Change in Home Price	(0%)	(6%)	(11%)	(16%)	(20%)

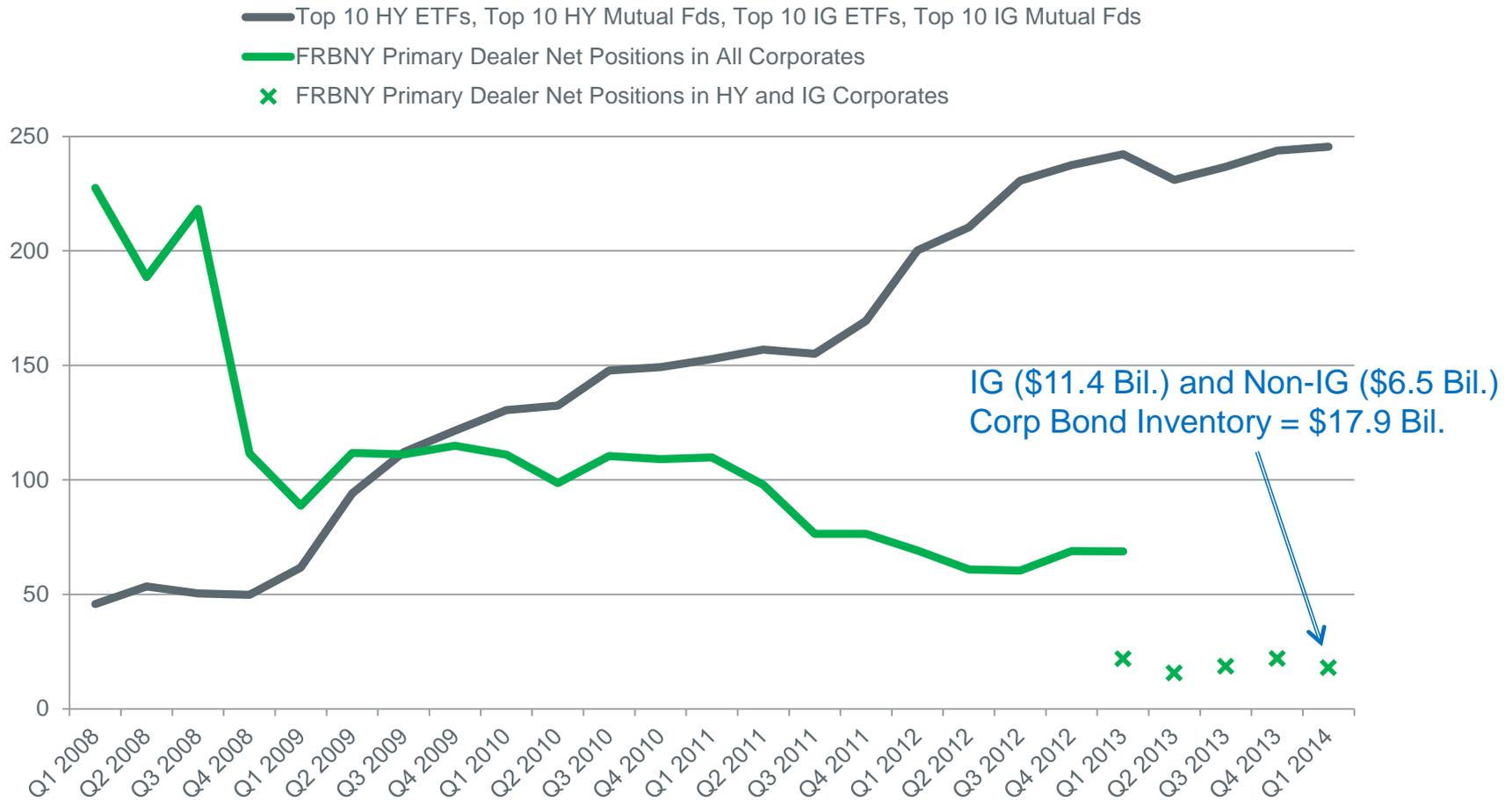
Source: Fitch

Risks to Corporate Investors: Interest Rate Trumps Credit



Source: Fitch Ratings, Bloomberg.

Corporate Bond ETFs and Mutual Funds Exceed Dealer Inventories



Note: At end-March 2013, the FRBNY changed the structure of its data on primary dealers' net positions in "Corporate" bonds. Before April 2013, the FRBNY included CMOs, REMICs and stripped securities issued by entities other than federal agencies and GSEs in their classification of "Corporates". From April 2013 onwards, the FRBNY removed CMOs and REMICs from their corporate classification but included ABCP and covered bonds. It is unclear how the pre-April "Corporate" net position data reconciles with the post-April "Corporate" data.

Source: Fitch Ratings, FRBNY, Bloomberg

People in pursuit of answers

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FitchRatings

New York

One State Street Plaza
New York, NY 10004

London

30 North Colonnade
Canary Wharf
London E14 5GN