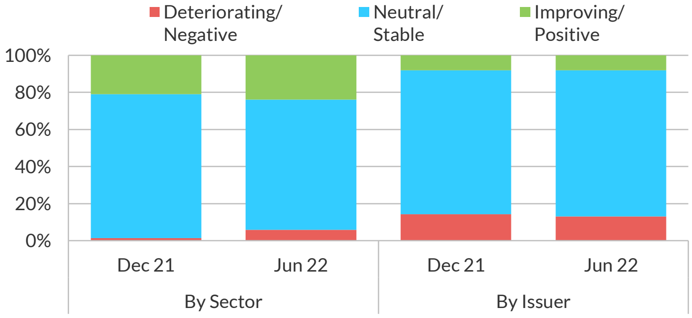
Global Corporates: 2022 Sector Outlook Update

Better Outlooks for Oil & Gas, and Mining; APAC Technology and Chinese Construction Worse

Outlook Balance



Source: Fitch Ratings

Fitch Ratings believes the global corporate sector is generally positioned to withstand rising geopolitical risk emanating from eastern Europe and China, continued supply chain challenges, inflationary pressure, monetary tightening and slower worldwide economic growth during 2022. Sector fundamentals remain mostly neutral.

Eleven sector outlooks changed as a result of our mid-year review incorporating changes in the geopolitical and macroeconomic environment since the start of 2022. Five were revised up, from neutral to improving, and six revised down: three from improving to neutral and three from neutral to deteriorating (see table on page 2).

Limited Changes to 2022 Sector Outlooks

Seventy percent of our 2022 corporate sector outlooks globally are neutral, compared with about 80% at end-2021. Improving outlooks represent 24% of sector outlooks, compared with 21% at end-2021. Six percent are deteriorating compared with 1% at end-2021.

Four sectors now have deteriorating outlooks: two construction-related sectors in China that are affected by the decline in new housing sales and China's Zero-Covid policy; Asia-Pacific technology, due to weakening post-pandemic demand and rising input prices; and EMEA High Yield and Leveraged Finance due to expected higher refinancing risk and default rates.

Sectors with outlooks changed to improving are benefitting from higher commodity prices and include mining and oil and gas. We have maintained an improving outlook on the global airline sector, as it is further recovering from a low 2020 base marked by the pandemic. An acceleration of deteriorating conditions could prompt a revision of our sector outlook.

Factors Driving Status Quo Outlook Views

The limited effect of deteriorating geopolitical and macroeconomic conditions is due in large part to the low base of comparison as many sectors have not yet fully recovered to their pre-pandemic level and still have some potential to rebound, pointing to improving prospects. In addition, some sectors are still able to pass along rising costs to customers via prices or are fairly recession resilient.

Sector vulnerability would increase under a stagflation scenario, leading to potential Outlook changes, Rating Watches and rating downgrades, as outlined in our adverse scenario heatmap (see table on page 2). The potential abrupt interruption of Russian gas supply could lead to additional sector outlook revisions, particularly in Europe, as it would cause a major macro-economic shock to the region.

The distribution of rating Outlooks is slightly less positive than that of sector outlooks, due to issuer-specific factors. Nearly 80% of global corporates' rating Outlooks are Stable, 13% are Negative, and only 8% are Positive.

Related Research

Inflation, Rate Hikes and Stagflation Risks Drive Deterioration in Sector Outlooks (June 2022)

Global Economic Outlook (June 2022)

APAC 'BBB-' & 'BBB' Corporates: Stagflation Downgrade Risk (May 2022)

Potential Fallen Angels Under a Stagflation Scenario (May 2022)

Cyclical, Energy-Dependent Corporate Sectors Most at Risk in a Stagflation Scenario (April 2022)

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Adverse Stagflation Scenario Rating Risk Heatmap – Global Corporates

High-Impact Sectors	**Mild-/Modest-Impact Sectors**
None	Utilities – EMEA Integrated/U.S.
Medium-/High-Impact Sectors	Consumer Products
Airlines	Retail
Medium-Impact Sectors	Chemicals – U.S./LatAm
Utilities – Generation Companies	Defense
Steel/Aluminum	Food Beverage & Tobacco
Building Materials	
Homebuilders	**Virtually No Impact Sectors**
Building Products	Pharmaceuticals
Energy – Refining	Energy – Exploration and Production
Diversified Industrials	Metals & Mining – Upstream/Integrated
Gaming, Lodging & Leisure	Healthcare
Autos	Telecom, Media & Technology
Aerospace	REITs
Chemicals – EMEA/APAC	Utilities – EMEA/APAC Regulated

Virtually No Impact	No rating/Outlook changes in the sector/region
Mild/Modest Impact	Very few potential rating changes, some Outlook changes
Medium Impact	Numerous Outlook changes; some Rating Watches; a few possible rating changes
Medium/High Impact	Heavy Outlook and Rating Watch activity; numerous rating changes
High Impact	Most or all ratings negatively affected

Source: Fitch Ratings

11 Corporate Sectors with Revised Outlooks

Sector	2022 Outlook – Dec 21	2022 Outlook – Jun 22	Trend
Global Mining	Neutral	Improving	⇧
Global Oil & Gas	Neutral	Improving	⇧
North American Energy (Oil & Gas)	Neutral	Improving	⇧
APAC Oil and Gas	Neutral	Improving	⇧
Indonesian Coal	Neutral	Improving	⇧
Global Gaming	Improving	Neutral	⇩
US Equity REITs	Improving	Neutral	⇩
LatAm Retail	Improving	Neutral	⇩
EMEA High-Yield and Leveraged Credit	Neutral	Deteriorating	⇩
China Engineering and Construction	Neutral	Deteriorating	⇩
Asia-Pacific Technology	Neutral	Deteriorating	⇩

Note: See pages 5-18 for details of all Corporate Sector Outlooks
Source: Fitch Ratings

Oil & Gas and Mining Outlooks Improve

The sharp increase in energy and other natural resource prices is positive for global commodity sectors, including Oil & Gas and Mining. Increased cash flow has enabled some issuers to reduce debt, resulting in improved credit profiles and recent rating upgrades.

High Oil Prices Support Sector Cash Flow

Average oil and gas prices are set to outperform our initial expectations and average prices in 2021. We believe oil prices will remain high, at least in the short term, because of the geopolitical tensions and solid demand.

Oil and gas producers are generating much stronger cash flows than anticipated at the beginning of 2022. We expect incremental operating cash flows to be allocated to increased capex, which will be beneficial for oil field services, more shareholder distributions and reducing debt. US domestic refiners are benefiting from above-normal crack spreads, enhancing the ability to reduce debt.

Cost inflation will intensify but will have a limited impact on most producers, as production costs are a relatively small proportion of revenue and will be more than offset by higher prices. Liquidity, which is a rating driver for small high-yield producers, should also improve.

Global Mining Supported by Robust Demand and Pricing

Supporting factors for metal prices include pent-up demand for steel production, low inventories for copper and aluminium, and favourable geopolitical factors for gold. In addition, prices for a few metals retreated at the start of the year, offering positive prospects for the rest of 2022.

Thermal and metallurgical coal are benefiting from strong seaborne prices linked to Europe's sanctions on Russian coal and a pledge by Japan to phase out Russian imports. Russia is a large producer of nickel and prices remain much higher than at the end of 2021.

Airlines' Improving Outlook and Auto's Neutral Outlook Maintained

Low Base of Comparison for the Airline Sector

Our improving outlook on the airline sector is underpinned by operating fundamentals that include pent-up demand and limited supply, which is supporting higher yields and helping to offset high fuel and labour costs. Several major airlines are also indicating that business travel is recovering faster than expected, potentially reducing one of the primary risks to our traffic forecasts.

Global travel restrictions are also easing and the effect of subsequent waves of coronavirus are diminishing as consumers increasingly become accustomed to living with Covid-19 as an endemic problem. Although materially increased debt due to the pandemic limits financial flexibility, sector liquidity is high, which provides some downside protection over the near term.

In addition, the sector is better positioned to manage typical recessionary pressures via pricing, limiting capacity growth and parking less efficient aircraft compared to the past two and half years when demand was artificially depressed due to Covid-19.

Nevertheless, risk is rising, due to the potential for a protracted period of high jet fuel costs and recession concerns. This is reflected in our Negative Outlooks for several airlines.

We identified the airline sector as potentially suffering a medium/high impact from our adverse stagflation scenario, and therefore a crystallisation of these assumptions could prompt a downward revision of our sector outlook. This could come from a further and accelerating deterioration of economic conditions or if leisure traffic wanes once pent-up demand is exhausted.

Solid Auto Demand Offsets Production Issues

Global automotive production remains affected by supply chain issues, in particular tight semiconductor availability. However, there are signs the chip shortage will abate in 2H22 for auto manufacturers.

The Ukraine conflict will weigh on European production through 2022 and pandemic-related lockdowns will continue to affect Chinese production over the near term. However, Fitch's estimate for global production was already conservative going into the year.

Commodity and other costs have risen significantly, due in part to the Russia/Ukraine conflict, but year-on-year comparisons should ease in 2H22. Automotive manufacturers continue to demonstrate strong pricing power and an ability to manage limited supply with a higher-margin product mix.

The pandemic and microchip shortage have created material pent-up global demand that will mitigate any potential effects of entering a cyclical downturn. However, demand could be affected in a stagflation scenario as new vehicle sales tend to be correlated with macroeconomic conditions, although there are signs that this will abate in 2H22. We have classified the auto sector as having medium rating risk in our adverse stagflation scenario.

The industry is managing the shift to electrification with an acceleration of electric offerings and sales, particularly in Europe and China, which will weigh on short-term profitability and cash generation. However, this will put the industry in a more favourable position over the longer term.

Global Gaming Outlook Revised Down to Neutral

There is more downside risk than upside potential in global gaming, prompting us to revise our sector outlook to neutral from Improving. The recovery in the US remains rapid, with US regionals and Las Vegas continuing to show strength. However, there is risk to consumer discretionary spending from high inflation, despite strong performance so far in 2022. Suppliers have achieved de-leveraging; credit profiles have already moved higher and are now stable.

In EMEA, the outcome of the UK Gaming Act Review of 2021 remains unclear. We expect that safer gambling initiatives will affect the profitability of operators in 2022, ahead of new regulation being enforced.

Performance in some Asian countries is more consistent with an improving outlook, particularly Singapore, Malaysia and Australia. However, Asia's performance is still missing meaningful outbound Chinese visitation given the Mainland's continuation of a Zero-Covid policy. Macau remains weak.

Region-Specific Outlook Changes

Most Outlook Changes in APAC

APAC had the largest number of outlook changes, at four out of 10. We revised two sector outlooks to improving from neutral and two to deteriorating from neutral. The new deteriorating outlooks are for China Engineering & Construction (E&C) and Asia-Pacific Technology. Our outlook for Chinese Property Developers remains deteriorating.

Chinese construction activities were subdued in 1H22 despite fairly robust orderbooks, particularly from infrastructure projects, mostly due to operational challenges caused by China's Covid-19 control measures. We view the sector as particularly vulnerable to liquidity strain if further outbreaks of Covid-19 cause serious and prolonged disruption.

We expect a pickup in construction activities in 2H22 on the back of accelerating infrastructure investments, given front-loaded local government special bond issuance, which is supportive of ramp-up related spending for 2H22. However, if China's pandemic-related restrictions persist for more than a few months, it would be challenging for the sector going into the winter months. This could result in liquidity pressure for Chinese E&C firms, as working capital collection becomes challenging.

We revised Asia-Pacific technology due to weakening post-pandemic demand combined with rising input prices. Chinese internet majors' short-term profitability and cash generation will be dampened by the challenging macroeconomic environment due to slower consumption spending, stringent Covid-19 lockdowns and the aftermath of last year's regulatory tightening.

For APAC Consumer Hardware, overall demand is weakening, exacerbated by the war in Ukraine and China's lockdown, while rising input costs are likely to put pressure on profitability. Companies with limited ability to pass through incremental costs to customers are likely to suffer the most in the heighted inflationary environment. Persistent chip shortage and logistics issues add to supply-side disruption.

However, things are improving for Indian IT Services. We expect demand to remain robust due to the strong pipeline for digital transformation, with around double-digit-percentage revenue growth. Wage inflation is not significantly higher than our expectations at the end of 2021.

US Equity REIT Outlook Revised Down to Neutral

We revised down our outlook for US Equity REITs to neutral from improving, and we revised up our North American Energy (Oil & Gas) outlook from neutral to improving. Property-level net operating income growth remains positive for most sectors, but the rate of improvement has decelerated to more 'normalised' levels. Moreover, a stagflation scenario would challenge REIT cash flows and property values given less demand for space and higher interest and capex expenses along with higher capitalization rates.

The enclosed mall and office sectors face fundamental challenges. Moreover, recent star performers, such as the industrial sector, are likely to be at, or near peak occupancies and rent growth, given some challenges in the technology sector, including Amazon's easing of its aggressive industrial footprint growth posture.

REITs are well positioned for a challenging environment, given historically low leverage and excellent liquidity profiles, supported by availability under committed revolving credit facilities and limited near-term unsecured debt maturities, aided by proactive liability management.

Latin America Retail Revised Down to Neutral

There was only one change among the 11 Latin America (LatAm) regional outlooks: we revised the outlook for Retail to neutral from improving. This downward revision reflects stagflation risk, as this would lead to demand volatility. For 2H22, Fitch expects discretionary spending to be affected by higher inflation and fewer commercial campaigns.

Profitability recovery from the pandemic could be partly supported by supply chain issues, as an extended inventory life cycle might reduce the frequency of commercial discounts. Higher interest rates should not materially affect this, but the effect will be more pronounced in Brazil due to the recent rates spike.

However, omnichannel development may continue to put pressure on margins, as logistics and IT-related expenses are keys to success.

Sector Outlooks Remain Neutral in EMEA

There were no changes to the 14 outlooks for the EMEA region, except for the broad High Yield and Leveraged Finance category, which we revised down to deteriorating. We assessed that all sectors still have a neutral outlook, balancing deteriorating macroeconomic conditions and a more challenging geopolitical environment with the low base of comparison and stronger balance sheets built to face the pandemic.

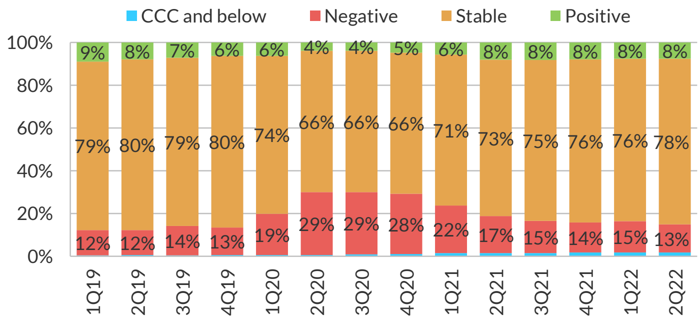
However, our updated outlooks do not include the potential abrupt interruption of Russian gas supply. We believe that this would cause a major macro-economic shock in Europe and lead to the revision of some of our outlooks. Discontinuation of gas supply could lead to government intervention in several countries and sector prioritisation in favour of industries such as agriculture and suppliers including manufacturers of fertilisers, food and beverages, and pharmaceuticals.

Other sectors with the most intensive use of gas, in particular manufacturing ones, could face production interruption in the short term and structural changes in the medium to long term as companies transition to alternative energy sources. Nonetheless, the pace of this transition is subject to economic viability and returns on the investment needed into new technology.

Distribution of Rating Outlooks Less Positive than Sector Outlooks

The distribution of rating Outlooks is slightly less positive than that of sector outlooks, due to issuer count and distribution within sectors, and issuer-specific dynamics. For example, Fitch could assess a sector outlook as neutral but within that sector a large number of companies could have a Negative Outlook due to factors such as M&A or strategic missteps.

Global Outlooks by Quarter

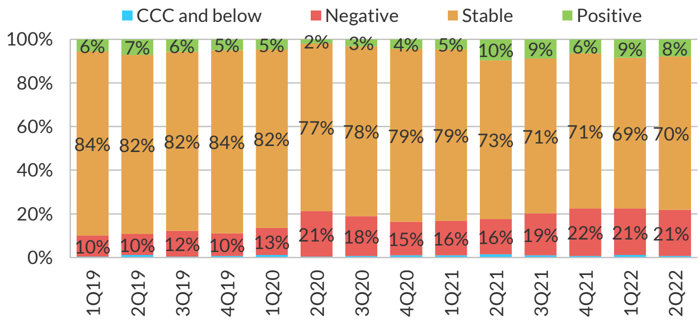


Source: Fitch Ratings

Only 8% of global corporates' rating Outlooks are Positive, compared with 24% of sector outlooks being Improving. By region, LatAm has the greatest share of Positive Outlooks, representing 11% of the region's portfolio, and the EMEA region the lowest proportion, at just more than 5%.

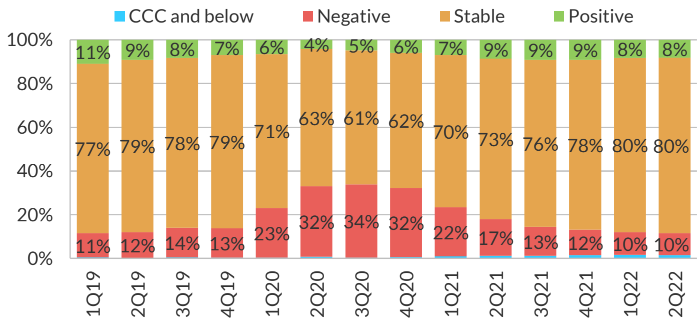
Just over 5% of sector outlooks are 'deteriorating', but nearly 15% of issuer rating Outlooks are Negative. By region, about 20% of our issuer rating Outlooks in APAC and 10% in North America are Negative.

APAC Outlooks by Quarter



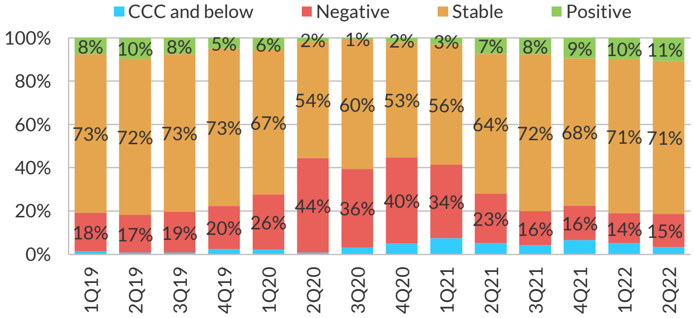
Source: Fitch Ratings

North America Outlooks by Quarter



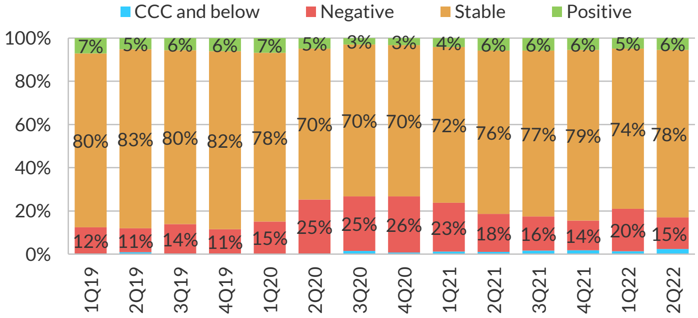
Source: Fitch Ratings

LATAM Outlooks by Quarter



Source: Fitch Ratings

EMEA Outlooks by Quarter



Source: Fitch Ratings

Global Outlooks (13)

Sector	2022 Outlook – Dec 21	2022 Outlook – Jun 22	Trend	Comments
Airlines	Improving	Improving	⇔	• Risk is rising, due to inflation, high jet fuel costs, and recession concerns, and is reflected in our Negative Outlooks on several airlines. • Our improving sector outlook is underpinned by pent-up demand and limited supply, which is supporting higher yields and helping to offset higher fuel and labour costs. This is in addition to easing global travel restrictions and the diminishing effect of each subsequent wave of coronavirus on traffic. Sector liquidity is high, which provides some downside protection. • The sector outlook could be revised to negative in 2H22 or 2023 should economic conditions continue to deteriorate. There is also a risk that leisure traffic wanes once pent-up demand is exhausted. Materially increased debt balances due to the pandemic limit financial flexibility.
Aerospace & Defence	Improving	Improving	⇔	• China demand for new aircraft is vulnerable in 2022 given economic pressures and Covid-related shutdowns. However, overall demand remains strong as the travel market continues to improve, particularly in the US. Order books are long, with particularly high demand for new narrow-body aircraft, which are generally more fuel efficient, potentially helping airlines offset higher fuel costs. • Large commercial aircraft production is ramping up. OEMs and many suppliers have cited a moderate inventory buildup to offset near-term supply chain pressure, but challenges could increase if the conflict in Ukraine persists for a prolonged period. OEM production and delivery rates remain key watch items. Higher production costs are generally passed through to customers. • The defence market remains generally robust and stable, with several developed nations pledging spending increases. The US budget increased more than expected and defence spending in Europe is likely to rise to 2% of GDP.
Lodging	Improving	Improving	⇔	• The improving outlook reflects the low base in 2021, which was still largely disrupted by the pandemic and travel restrictions. • The budget segment, domestic and leisure focused, should remain more resilient in an inflationary environment, while the pace of international travel recovery remains uncertain, especially for business travel. • In Europe, we forecast revenue per available room at 25%-30% below pre-pandemic levels, due to a strong willingness of consumers to resume travelling, despite higher costs of living. In the US, leisure demand has recovered ahead of expectations and subsequent Covid variants appear so far to have less negative impact on travel demand, while corporate travel has been picking up as companies start to enforce return-to-office policies. • China is an exception to the overall improving sector, with demand constrained by stringent restrictions and recent lockdowns halting the sector recovery. Fitch assumes that the country's "dynamic zero-Covid" policy will only gradually phase out over the course of 2023. • Increased staff costs due to post- pandemic labour shortages and rising utilities costs will be key challenges.
Mining	Neutral	Improving	⇧	• We revised up several of our metal price decks, including iron ore, copper and aluminium, zinc, nickel, gold and thermal coal. • Supporting factors include pent-up demand for steel production, low inventories for copper and aluminium, favourable geopolitical factors for gold, and retreating prices for a few metals at the start of the year, offering positive prospects for the rest of 2022. • Thermal and metallurgical coal's outlooks are improving due to strong seaborne prices linked to Europe's sanctions on Russian coal and a pledge by Japan to phase out Russian imports. • Russia is a large producer of nickel and prices remain much higher than at end-2021.

Global Outlooks (13) (Cont.)

Sector	2022 Outlook – Dec 21	2022 Outlook – Jun 22	Trend	Comments
Oil & Gas	Neutral	Improving	⇧	• Average oil and gas prices are set to outperform our initial expectations and average prices in 2021. We believe oil prices will remain high, at least in the short to medium term, because of the geopolitical tensions and improving demand. • Oil and gas producers are generating much stronger cash flows than they expected at the beginning of the year. We expect incremental operating cash flows to be allocated to increase capex – which also will be beneficial for oilfield services – but also increase shareholder distributions and reduce debt. US domestic refiners are benefiting from above-normal crack spreads, enhancing the ability to reduce debt. • Cost inflation will intensify but will have a limited impact on most producers, as production costs are a relatively small proportion of revenue and will be more than offset by higher prices. Liquidity will improve for high-yield smaller producers, for which liquidity is a key rating driver.
Gaming	Improving	Neutral	⇩	• There is more downside risk than upside potential in the US, given the continued fast recovery and risk to consumer discretionary spending amid high inflation even though performance so far in 2022 does not indicate any immediate impact on spending levels. US regionals and Las Vegas continue to show strength despite macro/consumer spending risks, but risk is skewed to the downside. • In EMEA, the outcome of the UK Gaming Act Review of 2021 remains unclear. Safer gambling initiatives may affect the profitability of operators in 2022, ahead of new regulation being enforced. • Asia's performance is still missing meaningful outbound Chinese visitation given the Mainland's continuation of a "Zero-Covid" policy, but performance in some countries is more consistent with an "Improving" outlook (Singapore, Malaysia and Australia). Macau remains weak. Suppliers de-leveraged; credit profiles have already moved higher and are now Stable.
Automotive	Neutral	Neutral	⇔	• Global production remained affected by supply chain issues in 1H22. However, tight semiconductor availability is showing signs of improvement for 2H22. • Fitch's estimate for global production in 2022 was already conservative at the start of the year, but the Ukraine conflict will weigh on European production and lockdowns will constrain Chinese production. • Commodity and other costs have risen significantly in 2022, driven in part by the Ukraine conflict, but yoy comparisons are likely to ease in 2H22. • The pandemic and chip shortage have created material pent-up global demand that could mitigate the effects of a potential cyclical downturn. • Auto manufacturers continue to demonstrate strong pricing power and an ability to manage limited supply with a richer product mix. • The industry is managing the shift to electrification with an acceleration of electric vehicle offerings and sales, particularly in Europe and China, which will weigh on short-term profitability and cash generation, but will put the industry in a more favourable position over the longer term. • Demand could ultimately be affected by stagflation as new vehicle sales tend to be correlated with macroeconomic conditions.
Food, Beverage and Tobacco, Consumer, and Restaurants (US and EMEA)	Neutral	Neutral	⇔	• Packaged Food, Beverages and Consumer companies are experiencing input cost increases but we expect them to gradually pass these costs on to customers to protect profits. A mild adverse effect on volumes is likely as consumer spending power starts to erode, partly offset in the earlier part of 2022 by post-Covid re-openings. We have a more cautious outlook on emerging-market companies, due to more severe inflationary pressures. Shareholder remuneration and M&A are being managed in a way that should not affect ratings. • Commodity processors will continue to perform very well in 2022 but we generally do not expect upward rating pressure, as our ratings factor in scope for temporary upside/downside. • Tobacco is also stable: EMEA-based companies are becoming more shareholder friendly but this is in the context of better headroom and good trading performance. • Protein companies are effectively managing inflation through restructuring initiatives, particularly toward more price-variable mechanisms implemented earlier in the pandemic as well as some improved product and channel mix that has more than offset ongoing labour challenges.

Global Outlooks (13) (Cont.)

Sector	2022 Outlook – Dec 21	2022 Outlook – Jun 22	Trend	Comments
Steel	Neutral	Neutral	⇔	• The operating environment has become more challenging, particularly in Europe, where the energy gap for industrial sectors is significant. However, Chinese stimulus feeding through later in the year for infrastructure and fixed-asset investment should provide support to domestic demand, mostly compensating for weaker private consumption including in the property sector. The US, Brazil and India remain reasonably resilient. • Favourable market dynamics outside China are normalising now faster than expected (Chinese recovery was running ahead of other markets, so that steel margins had already corrected towards the end of 2021), but earnings will remain robust in 2022, as realised sales and order books will carry steel companies through 1H22, with a weaker outlook for margins outside China for the rest of the year. • With forecast global GDP growth slowing by around 0.5% for 2022 due to challenges from inflation and consumer confidence, incrementally more export volumes will compete for demand in less protected markets such as Europe. India, Brazil and the US are less exposed due to section 232 or trade barriers.
Pharmaceuticals	Neutral	Neutral	⇔	• Pharmaceutical demand has normalised rapidly after the lockdowns and global pharma names have exited the pandemic in good shape, particularly those involved in the Covid response. • This has boosted rating headroom but prompted M&A and consolidation in line with an acceleration in business model specialisation. However, M&A is now more targeted and includes cooperation rather than mergers, as valuations remain very high. There has also been comparatively low shareholder pressure to increase returns/payouts, and we expect a prioritisation of investments in growth and consolidation opportunities over shareholder returns. • We expect structural demand growth in pharma due to innovation, improving treatment access and longer life expectancy. Innovation remains a key growth driver and focus on R&D productivity is increasing across the sector. • Energy and labour cost inflation could become an issue, particularly at the more generic, commoditised, and consumer end of the market, but this could be largely offset by pass-through mechanisms. • The regulatory environment remains stable in the near term (with the exception of China), although the US continues to carry the highest regulatory event risk in the Western developed world.
FinTech (North America and Europe)	Neutral	Neutral	⇔	• Payment-oriented FinTechs continue to benefit from healthy consumer spending trends and pandemic recovery. • The Russia-Ukraine conflict has created some challenges, with certain FinTechs exposed to the region exiting or suspending operations. • E-commerce penetration continues to grow, but revenue growth slowed meaningfully in 2022 due to pandemic-induced growth in 2020-2021. • Fintech-oriented businesses with exposure to cross-border travel and corporate spending are experiencing stronger growth in these areas as travel resumes, borders re-open and corporate spending picks up.
Shipping	Neutral	Neutral	⇔	• Supply-chain issues, coumpounded by the war in Ukraine, continue to support higher rates, although container rates are off their recent peaks, reflecting the lockdowns in China. • Stagflation could weigh on demand but we do not expect a near-term rebalancing of capacity leading to a significant drop in rates. • Bulk, tanker and LNG carrier rates are likely to remain supported by route disruptions caused by the war in Ukraine, with bulk and tanker rates also likely to benefit when Chinese lockdowns ease.
GCC Corporates	Neutral	Neutral	⇔	• Strong fundamentals, high oil revenues and government spending are driving market recovery in 2022. • Increased raw materials, taxation and inflationary pressures should affect most sectors, with limited ability to pass costs through to end-users. Government-sponsored mega projects are driving strong order backlog for building materials and E&C. Homebuilders, Hospitality and Property/Real Estate are benefitting from strong demand in Saudi Arabia and the United Arab Emirates. • A potential scaling back of oil and gas investments could limit private sector growth in 2H22.

Source: Fitch Ratings

APAC Outlooks (10)

Sector	2022 Outlook – Dec 21	2022 Outlook – Jun 22	Trend	Comments
APAC Oil and Gas	Neutral	Improving	⇧	• Average oil and gas prices are set to outperform our initial expectations and average prices in 2021. Fitch's revised price assumption of Brent average USD105/bbl in 2022 is significantly higher than average USD71/bbl recorded in 2022. Increased prices are driven by an improving yoy global demand, OPEC+'s cautious stance with regards to production growth and, more recently, Russia's attack on Ukraine and reducing oil flows from Russia. Natural gas prices in 2022 have also been revised upward, reflecting tight supply further exacerbated by shrinking supply from Russia and Europe's gradual phase-out of Russian gas – effectively competing with consumers in Asia. • APAC upstream and integrated oil and gas producers are generating stronger cash flows than they expected at the beginning of the year. We expect incremental operating cash flows to be partly allocated to increase capex for the national oil companies and to reduce debt, resulting in improving credit metrics. Downstream-focused entities are likely to experience some margin compression from high crude costs, although we expect the impact on their leverage profiles to be small, offset by stronger demand and earnings contribution from new capacitiy starting operations.
Indonesian Coal	Neutral	Improving	⇧	• Seaborne thermal coal prices are set to outperform our initial expectations and average prices in 2021. While China demand is likely to be weaker than we expected at the beginning of the year due to a new wave of Omicron variant infections, demand in south and southeast Asian markets is recovering robustly. India demand has been particularly stronger so far in 2022 due to an unexpected heat wave. • Notwithstanding moderating China Qinhuangdao prices since March, reflecting increasing China production and softening demand, seaborne prices are likely to remain above historical levels in 2022. Europe's sanctions on Russian coal exports will become effective in August 2022 after a four-month grace period, which could increase demand for APAC coal. Higher prices will enable Indonesian coal companies to achieve higher profits and operating cash flow generation, leading to stronger credit metrics.
APAC Utilities	Neutral	Neutral	⇔	• A strong post-pandemic rebound of demand outside China is offset by softening China demand as a result of the country's stringent public health and mobiilty restrictions to contain Omicron variant infections. • Fuel cost remains high. Most APAC utilities can pass through higher costs, although the extent of pass-through for Chinese power gencos and Korea Electric Power Corporation is less than full. • Chinese city gas distributors will experience declining gas connections amid the property market downturn, but the impact will be mitigated by connection demand from old-town renovation, and higher profit contribution from integrated energy businesses. Rated city gas operators' strong financial profiles also provide sufficient rating headroom.
Indonesian and Vietnamese Homebuilders	Neutral	Neutral	⇔	• We have maintained our neutral 2022 outlook for both Indonesian and Vietnamese homebuilders: pre-sale growth will slow from last year as expected but remain healthy, with Vietnamese homebuilders in particular still likely to have strong double-digit growth. This is because companies continue to invest in land banks, leading to higher sellable resources. Both countries will experience a rebound in economic activity as movement curbs have been largely removed. This should counterbalance the potential drag from rising interest rates, which will put some pressure on mortgage-funded home sales. Inflationary pressures will mainly affect the sector via higher construction costs and weaken EBITDA margins by 1%-2% according to our estimates. • However, the impact on EBITDA will be felt beyond 2022 when projects launched this year are completed. FCF will remain neutral for Indonesian homebuilders but may turn negative if larger issuers pursue expansion plans to use balance-sheet headroom. Vietnamese homebuilders will have meaningful negative FCF as they invest in land bank to support mid-term growth, but their leverage should remain healthy as rated issuers have low leverage to begin with. Liquidity is sufficient for most issuers in 2022 in both markets, with most large debt maturities termed out to 2023 or thereafter, with some exceptions.

APAC Outlooks (10) (Cont.)

Sector	2022 Outlook – Dec 21	2022 Outlook – Jun 22	Trend	Comments
Asian Palm Oil	Neutral	Neutral	⇔	• Malaysian benchmark crude palm oil prices have strengthened in 2022, driven by a weaker outlook for supply of substitute vegetable oils, due to uncertainty about sunflower seed oil from Ukraine and Russia along with the impact of drought on South American soybean, and Indonesia's steps to curb palm oil exports. • However, price realisations for companies in Indonesia, the world's largest producer, have been curbed by export levies and measures such as the three-week export ban. These measures were taken by the government to control domestic price inflation of key commodities such as cooking oil, and we expect further steps to keep prices in check. • We also expect crude palm oil prices to decline gradually over the next year, helped by higher output of palm and other vegetable oils.
China Steel	Neutral	Neutral	⇔	• We expect China's steel sector outlook to remain neutral, as industry fundamentals remain intact. Demand has been subdued in the first few months, both due to seasonality and Covid-19-related lockdowns, which translated into low construction activities. However, policy-driven supply reduction was apparent, offsetting the impact of weaker demand. We expect construction activities, accounting for 55% of sector demand, to pick up during 2H22, particularly from infrastructure investments, which is likely to offset the impact of slower property sales. This is aided by a positive growth outlook in the manufacturing sector such as machinery, auto, shipping and energy-related equipment, which together account for 35% of total steel demand. • Supply restriction remains a government mandated target to achieve a yoy crude steel production decrease. This will be achieved through policy interventions such as production restrictions. • We expect prices for steel products to remain high due to high raw material prices (iron ore and coking coal). Despite some ability to pass on raw material costs to end-customers as production and capacity remain restricted, revenue generation is likely to remain restricted until Covid-19-related lockdowns are eased. However, we expect limited impact on leverage for the sector due to prudent capex.
Asia-Pacific Telecoms	Neutral	Neutral	⇔	• Demand for telecommunications services is relatively insulated from inflation and economic growth threats. • As it is a highly capital intensive sector, operating cost inflation is not a major threat to cash generation. We do not expect capex cost inflation to be significant for companies' capital budgets. • Price competition may ease in some jurisdictions as some smaller operators consolidate. • Although telcos are not immune from supply chain disruptions we do not forecast any significant business disruption from any potential delays in obtaining capital equipment. • Regulatory regimes remain relatively benign across the region.

APAC Outlooks (10) (Cont.)

Sector	2022 Outlook – Dec 21	2022 Outlook – Jun 22	Trend	Comments
China Engineering and Construction	Neutral	Deteriorating	⇩	• Activities have been subdued in 1H22, mostly due to operational challenges caused by control measures, despite fairly robust order books for the sector, particularly from infrastructure projects. We view the sector as particularly vulnerable to liquidity strains if further outbreaks of Covid-19 cause serious and prolonged disruption in 2022. • We expect a pickup in construction activities in 2H22 due to accelerating infrastructure investments, given front-loaded local government special bond issuances, which supports a ramp-up in related spending for 2H22. However, if pandemic-related restrictions persist for more than a few months, it will be challenging for the sector going into the winter months. This could result in liquidity pressure for E&C firms, as working-capital collection becomes challenging. • We expect stronger growth for state-owned E&C companies with higher exposure to infrastructure and industrial projects than those that focus on property-development projects. Fitch-rated entities in this sector are mostly large and state owned, which should enable them to weather increased liquidity strains, but smaller companies with higher exposure to property, and those with weaker access to government support would be more vulnerable. • Financial leverage of E&C issuers will remain high in 2022 due to sustained operating and investing cash outflows associated with public-private partnership and other investment projects.
Asia-Pacific Technology	Neutral	Deteriorating	⇩	• China internet majors: We revised the sector outlook to deteriorating from neutral and it is only likely to start to improve towards late 2022 or 2023. Chinese internet majors' short-term profitability and cash generation will be dampened by the challenging macroeconomic environment due to slower consumption spending, stringent Covid-19 lockdowns and the aftermath of last year's regulatory tightening. • Consumer Hardware: We revised the sector outlook to deteriorating from neutral as overall demand is weakening after the pandemic, exacerbated by the war and China's lockdown, while rising input costs are likely to put pressure on profitability. Companies with limited ability to pass through incremental costs to customers are likely to suffer the most in the heighted inflationary environment. Persistent chip shortage and logistics issues add to supply-side disruption. • Indian IT Services: The sector outlook remains improving. We expect demand to remain robust due to the strong pipeline for digital transformation, with around double-digit-percentage revenue growth. Wage inflation is not significantly higher than our expectations at the end of 2021. • Semiconductor: The sector outlook remains neutral. Revenue growth remains supported by the extended global chip shortage and the growing electric vehicle trends for APAC-rated issuers. However, medium-term growth may be affected by: supply issues of raw materials due to the conflict in Europe and China's lockdown; lower end-market demand due to the weaker economy; and high capacity growth from integrated device manufacturers and foundries in 2023.
Chinese Property Developers	Deteriorating	Deteriorating	⇔	• New housing sales continued to fall steeply in 1Q22, with many registering declines of 30%-45% yoy. • The decline in housing sales may moderate in the coming months, as the government has provided clearer support and 2H21 sales were low, although recent pandemic-related lockdowns may hinder any recovery. Nevertheless, Fitch expects full-year sales value to fall by 25%-30%. • More developers have become financially distressed, as capital market access remained closed and they had limited internal cash to meet capital market maturities. We expect capital market access to remain limited for most developers this year. • Fitch expects modest recovery to only come in 2023.

Source: Fitch Ratings

EMEA Outlooks (14)

Sector	2022 Outlook – Dec 21	2022 Outlook – Jun 22	Trend	Comments
High-Yield and Leveraged Credit	Neutral	Deteriorating	⇩	• Adverse capital market conditions raise refinancing risk for highly leveraged credits rated 'B' and below with maturities coming due in 2022 and 2023. This represents less than 5% of the portfolio by volume. • Many of the higher leveraged credits from the travel and leisure sector continue to see strong bookings and pricing power through 3Q22. • We expect default rates for leveraged loans to be around 2.5% at end-2022 and default rates for developed market high yield bonds to be 1.5% at end-2022. • Outlooks could be revised from Positive to Stable or from Stable to Negative, or ratings could be downgraded, for credits exposed to declining volumes and lack of pricing power offseting rising input prices, if revised forecasts indicate limited de-leveraging progress. • Most vulnerable leveraged credits are those exposed to consumer demand destruction and industrial price takers. • Sterling loan and bond markets appear most vulnerable to longer-term disruption in comparison to euro and US dollar borrowers.
Building Materials and Construction	Neutral	Neutral	⇔	• Strong demand in building products is driven by strong residential renovation and structural shortages of new build in developed markets. A key risk remains consumer confidence in the face of rising inflation and interest rates. However, demand is still supported by environmental and infrastructure stimulus packages. • Building materials demand is underpinned by stimulus packages for infrastructure. Robust demand supports continuing price increases. Rising energy costs are a constraint because of the sector's high energy usage but the solid short-term order book, effective hedging and increasing in-house generation mitigate impacts.
Chemicals	Neutral	Neutral	⇔	• Chemical companies' financial profiles are supported by high prices, from sustained robust demand, tight supply in most chemical sectors, low inventories and increasing production costs. Most companies expect high profits in 1Q22 to be repeated in 2Q22. • In 2H22, risks exist on the demand side due to the inflationary environment and expected economic slowdown, whereas the supply side could gradually lenghthen as the supply chains recover. Gas rationing risk in Europe casts some doubt on the sector's outlook.
Fertilisers	Neutral	Neutral	⇔	• Supply remains tight following reduced Russian export volumes and high production costs because of higher and volatile European gas prices. Signs of demand erosion are now present, despite strong crop prices. The impact of EU quotas on most fertiliser imports from Russia will be minimal, apart from reduced MOP availability. Prices remain high, but demand erosion and market stabilisation following Russia's invasion of Ukraine has led to some softening from the peaks in March. • Uncertainty is growing about possible European natural gas availability, which could affect production.
Petrochemicals	Neutral	Neutral	⇔	• Demand remains strong in most end-markets despite challenging conditions in the automotive sector, due to low inventories and pent-up demand, and despite significant inflation. Supply is also tight as logistics issues make markets more regional. This supports higher prices. • Margins remained strong in 1Q22 as product prices firmed, but pressure is likely in 2Q22 as feedstock and energy costs rise. • Producers are adapting to volatile market conditions: quarterly contracts have been switched to monthly and producers are increasing the amount of feedstock and energy hedged to mitigate volatile prices. • Uncertainty about European natural gas supply for the sector could affect production later this year. Downward revision in GDP growth for 2022 could also signal weaker demand in 2H22.
Specialty Chemicals	Neutral	Neutral	⇔	• We expect producers' profitability to come under pressure as energy and feedstock costs remain high. • End-market demand for specialties is generally strong, but lower consumption from some weaker industries is affecting specialties sales volumes. Supply chain constraints are hindering some producers' sales volumes. • Concerns are growing about the availability and cost of intermediate chemicals used as feedstock because of limited supply and potential gas supply restrictions in Europe.

EMEA Outlooks (14) (Cont.)

Sector	2022 Outlook – Dec 21	2022 Outlook – Jun 22	Trend	Comments
Healthcare and Pharmaceuticals	Neutral	Neutral	⇔	• Performance was robust during the pandemic but future revenue growth is unclear. Profitability could come under pressure from general and wage inflation, and limited availability of staff. However, the European regulatory frameworks remain generally supportive, and we expect some inflation to be passed on. • The sector has some exposure to a possible energy supply shock, but the healthcare sector could be prioritised in a rationing scenario. • The European healthcare market remains fragmented and consolidation strategies remain intact. However, it remains to be seen how these will develop in an environment of reduced access to, and higher cost of, capital and still high valuations. These market segments are heavily reliant on private equity involvement. • The overall break-up and fragmentation of the pharma/healthcare value chains will continue, perhaps accelerated due to inflationary pressures. The role of tech will accelerate, following already increased use during the pandemic.
Diversified Industrials and Capital Goods	Neutral	Neutral	⇔	• Pent-up demand is offset by rising raw materials pricies, but we expect margins to remain broadly stable. • We anticipate a limited impact from energy cost inflation as price rises can be passed through to customers, albeit with some time lag.
Engineering & Construction	Neutral	Neutral	⇔	• A strong backlog is driven by government infrastructure, and improving margins in general. The sector has limited exposure to energy price rises, especially where contracts are "cost plus" or "target cost". • There is a potential for greater inventory builds with accelerated project purchasing to lock in prices, which may put pressure on sub-contractors.
Packaging	Neutral	Neutral	⇔	• The sector has strong cash flows and demonstrates good raw material structural cost pass-through under contract with limited delay. • There have been some instances of restricted shortages of raw materials, but we do not expect these to be significant, with most large companies using global sourcing.
Real Estate	Neutral	Neutral	⇔	• A division between prime offices (modern, good location, flexible for changing office work practices, and ESG conducive) and secondary offices persists. • UK retail asset classes have reached their near-60% peak-to-trough valuation declines, and some rents have stabilised on re-leasing. However, some landlords' passing rents have still got further reductions to crystallise, upon re-leasing. Continental European retail had less severe rental declines, in part due to shorter leases regularly rebased to market levels, and yoy CPI increases. • The underlying supply and demand features of Logistics, including rising e-commerce and scarcity of land, portends well for this continued growing sector. • Residential-for-rent stock continues its steady growth. Many European residential markets have regulated, RPI-linked rents. • Rising interest rates point to weaker property values, less so for asset classes whose rents will increase with inflation (some contractually within the lease). Property companies have significant headroom under interest cover ratios and have large proportions of interest rate fixing (at past years' low rates), so near-term debt service is less of a concern.

EMEA Outlooks (14) (Cont.)

Sector	2022 Outlook – Dec 21	2022 Outlook – Jun 22	Trend	Comments
Telecom	Neutral	Neutral	⇔	• The sector has not faced any significant incremental degradation in pricing and cost structures in 2022. • No western European operator has any significant exposure to Russia and many operators have one- or two-year hedged energy costs. These typically range between 2% and 4% of revenues. • The easing of Covid restrictions is helping a recovery in roaming revenues, while ongoing cost optimisation measures are supporting margins. • FCF margins and growth remain constrained due to local access, fibre network deployments. As a result, operators continue to explore consolidation opportunities in certain markets and partnerships and JVs for fibre networks, which exploit a lower cost of capital of infrastructure and pension funds.
Retail	Neutral	Neutral	⇔	• Food retailers have a relatively resilient revenue base but, as low-margin businesses, cannot pass on higher costs (from food price, wages and utilities). This could weigh on profit margins, even as a tactical way to protect market shares amid high inflation. • Food retailers focused on higher-end customers and/or benefitting from a large scale are better positioned to pass on inflation and preserve margins, helped by cost-cutting initiatives. • For non-food retailers, general consumer sentiment and higher costs of living could delay the post-pandemic recovery, particularly in sectors where competition is acute (e.g. apparel and consumer electronic goods). • Segments that benefitted from the pandemic (e.g. home equipment) could be affected by lower consumer spending, on top of normalisation of activity levels. Discounters are gaining market share, but their profitability could come under pressure from their limited ability to pass on cost inflation, because of their customer base and commitment to low prices. • Supply-chain disruptions can cause selective product unavailability and longer lead times, especially in non-food retail categories, adding to working capital and near-term cash flow volatility. Retailers with large committed revolving credit facilities and/or a history of positive free cash flow should prove resilient.
Utilities	Neutral	Neutral	⇔	• Many utilities, especially with exposure to fixed- and low-cost generation, benefit from the high energy price environment. Higher inflation is also generally positive for regulated networks, while supply businesses may face additional margin pressure. • However, the environment features high political and regulatory risk and the EU is set to radically reduce its energy dependence on Russia. An extreme scenario of a complete halt of Russian gas supplies could, depending on governments' reactions, affect ratings of utilities with significant exposure to gas imports from Russia. • The EU's strategic direction highlighted in the REPowerEU document is putting electricity and gas companies on divergent paths. A faster development of hydrogen could represent a mitigant for gas companies, although with material execution risk.

Source: Fitch Ratings

North America Outlooks (17)

Sector	2022 Outlook – Dec 21	2022 Outlook – Jun 22	Trend	Comments
Business Services Data and Analytics	Improving	Improving	⇔	• Sustained growth and margin momentum reflect continued normalization. Organic growth is supported by onging digital transformation. • M&A focus continues, albeit at a lower pace than in 2020-2021, with increased emphasis on capability enhancement, analytics and software. • ESG and related data is increasingly becoming a key differentiator among data and analytics providers, prompting acquisitions that may put pressure on credit metrics in the near term but will lead to enhanced growth profiles and improved diversification over the medium term.
Midstream Energy	Improving	Improving	⇔	• The operating backdrop continues to improve as the benefits from the constructive commodity price environment have accelerated since the beginning of the year. This should continue to support healthy earnings for the midstream sector, in the absence of adverse extreme weather. • The Ukraine-Russia conflict has made energy security a top priority around the world, with North America expected to play an increasingly important role in improving energy security for other countries, which will benefit midstream companies. • Even with the improving industry conditions, midstream management teams remain focused on balance-sheet improvement. Capital discipline remains a central theme, with potential dividend increases and/or share buybacks also garnering added attention. • Midstream issuers are largely insulated from cost pressures, due to largely fixed-cost operating structures and inflation escalators in tariffs.
Leisure	Improving	Improving	⇔	• Domestic travel remains robust, with international travel slowly picking up. Theme park attendance is now surpassing 2019 levels, budget gyms have fully recovered membership and the cruise recovery is becoming more viable, even though we remain cautious given the Covid variant risk.
Lodging and Timeshare	Improving	Improving	⇔	• As local governments reopen and the population adapts to living with Covid, leisure demand has recovered ahead of expectations. Subsequent variants appear, so far, to be having a less negative impact on travel demand, and corporate travel has been picking up as companies start to enforce return-to-office policies.
Media & Entertainment	Improving	Improving	⇔	• Out-of-home entertainment trends are normalizing and the digital transformation is continuing. • Content investment continues to increase and M&A activity, which is affected by government regulation, is focused on gaining scale.
Telecommunications and Cable	Improving	Improving	⇔	• Issuers are focused on deleveraging after costly spectrum auctions. • 5G mid-band deployments and capex are ramping up. Broadband spending on fibre is also rising. • Linear TV remains under pressure. • Potential clarity on regulatory policy is on the horizon.
Energy (Oil & Gas)	Neutral	Improving	⇧	• Average oil and gas prices are set to outperform our initial expectations and average prices in 2021. We believe that oil prices will remain high, at least in the short to medium term, because of the geopolitical tensions and improving demand. • Oil and gas producers are generating much stronger cash flows than they expected at the beginning of the year. We expect incremental operating cash flows to be allocated to increase capex – which also will be beneficial for oil field services – but also increase shareholder distributions and reduce debt. US domestic refiners are benefiting from above-normal crack spreads, enhancing the abilityto reduce debt. • Cost inflation will intensify but will have a limited impact on most producers, as production costs are a relatively small proportion of revenue and will be more than offset by higher prices. Liquidity will improve for high-yield smaller producers, for which liquidity is a key rating driver.

North America Outlooks (17) (Cont.)

Sector	2022 Outlook – Dec 21	2022 Outlook – Jun 22	Trend	Comments
Equity REITs	Improving	Neutral	⇩	• Property-level net operating income growth remains positive for most property sectors; however, the rate of improvement has decelerated to more "normalized" levels. Moreover, the growing probabiity of stagflation in the US economy would challenge REIT cash flows and property values due to less demand for space and higher expenses (i.e. interest and capex) and capitalization rates. • The enclosed mall and office sectors face fundamental challenges. Moreover, recent star performers, such as the industrial sector, are likely to be at or near peak occupancies and rent growth, given some challenges in the technology sector, including Amazon's retrenchment from its aggressive industrial footprint growth posture. • REITs are well posititioned for a challenging environment, given historically low leverage and excellent liquidity profiles, supported by availablity under committed revolivng credit facilities and limited near-term unsecured debt maturities, aided by proactive liability management.
Building Products and Materials	Neutral	Neutral	⇔	• Strong new housing and residential remodelling backlogs, and continued recovery in the commercial and public construction end-markets and selling price increases across product categories should continue to drive top-line growth for the sector in 2022. • Continued raw material cost inflation and persistent supply chain disruptions should be mostly offset by significant price increases implemented earlier this year and the continued strong pricing environment, but margins for certain product categories are likely to contract this year.
Chemicals	Neutral	Neutral	⇔	• Issuers are passing on raw material costs to customers by increasing prices and have even increased margins, but this ability may wane in 2H22. • Demand is holding up, despite rising, and in some cases historically high, prices but continued increases along with moderating levels of economic activity may lead to demand destruction. The recovery in auto production also continues to lag behind due to the prolonged semiconductor shortage. • The neutral outlook reflects moderate leverage, good liquidity and Fitch’s expectation that issuers prudently return cash to shareholders.
Diversified Industrials and Capital Goods	Neutral	Neutral	⇔	• Strong demand supports higher pricing, which mitigates the impact of inflation. • Supply chain constraints may limit revenue growth, but companies are adaptating by adjusting product designs and the supply base to adjust. • Direct exposure to Ukraine and Russia is low; exposure to China is higher but generally manageable. • Risk around the energy transition is offset by the technological capabilities of many companies to develop new products/services.
Utilities, Power & Gas	Neutral	Neutral	⇔	• We expect the sector to hold up well due to its defensive charateristics, although it is not entirely immune to the weakening macroeconomic backdrop. Electricity and gas sales were strong during 1Q22. We expect industrial sales to weaken in tandem with a slowing economy but residential sales, which are the highest-margin customer segment, are exhibiting strength due to a still-entrenched hyrid work environment. • Utilities are not experiencing high workforce attrition and have been able to offset inflationary pressures through cost controls. • Rising interest rates remain a challenge, but authorized return on equity should eventually start to increase to reflect the higher cost of capital. • The sharp jump in natural gas prices following Russia’s invasion of Ukraine is the biggest risk. If utilities are not able to pass higher energy costs on to residential customers, cash flow might come under pressure. We will consider the risk state by state. Operating and maintenance cost control and the ongoing energy transition to lower-cost renewables should provide some offset.
Healthcare and Pharmaceuticals	Neutral	Neutral	⇔	• Our expectations for volumes and capital allocation are generally unchanged. Inflationary pressures in certain sub-sectors, including providers and distributors, are increasing but not to the degree that will lead to rating implications.

North America Outlooks (17) (Cont.)

Sector	2022 Outlook – Dec 21	2022 Outlook – Jun 22	Trend	Comments
Homebuilders	Neutral	Neutral	⇔	• The rapid rise in mortgage rates in recent months is eroding affordability, which Fitch expects will weaken demand and limit pricing power more than originally anticipated. Fitch expects housing activity will fall low to mid single digits in 2022 and 2023, while home prices are likely to rise 10% in 2022. We expect home price growth to decelerate in 2023 as demand weakens. • Supply/demand dynamics remain favourable as home inventory remains very limited, which should support home prices. Signficant home equity and tight underwriting standards over the past decade should help limit foreclosures in the near term. • We expect the credit metrics of rated builders to remain comfortably within our rating sensitivities for our rating case analysis, which incorporates conservative capital allocation strategies consistent with behaviour in the last cyclical downturn.
Leverage Finance	Neutral	Neutral	⇔	• The outlook for the US leveraged finance segment reflects individual sector outlooks weighed by their aggregate size in the institutional leveraged loan and high yield bond markets. • Our 2022 leveraged loans and high-yield default rate forecasts remain unchanged at 1.5% and 1%, respectively, given the benign 0.5% and 0.6% levels so far in the year.
Retail	Neutral	Neutral	⇔	• Our base case scenario for 2022 contemplated moderation to top-line and margin growth across the retail sector following two very strong years. • Our ratings cases mostly assume more conservative operating trajectories than companies' current forecasts and market views. • Given some signs of softening consumer demand and inflationary pressures, the market has become more cautious on overall retail spending/earnings, and companies are starting to moderate expectations; however, these new forecasts are generally in line with, if not higher than, Fitch's models, which support our neutral sector view.
Technology	Neutral	Neutral	⇔	• Supply-chain constraints and capacity growth are continuing, with geopolitics driving regionalization of supply chains. • Inflationary pressures are extending beyond supply-chain issues. • Regulatory approval is delaying M&A activity.

Source: Fitch Ratings

Latin America Outlooks (11)

Sector	2022 Outlook – Dec 21	2022 Outlook – Jun 22	Trend	Comments
Real Estate	Improving	Improving	⇔	• Performance of industrial real estate in Mexico will remain solid, with strong growth potential over the medium to long term, with rental prices growing in 2022 and 2023 due to imbalanced supply and demand. The pace of supply growth is limited by land availability in primary markets, and delays in obtaining land permits, licences and power supply to these properties. • Mall operators' main challenges are the fast-growing e-commerce sale channels and customers demanding new shopping interactions. E-commerce penetration is challenged by limited logistics and internet connectivity throughout the region, but it offers compelling future opportunities. Penetration rates are low compared to developed markets, with the highest penetration in the region being in Chile (7.9 malls per million people) and the lowest is Brazil (2.8 malls per million people). • Office spaces will have lower occupancy rates over the next two years as countries recover from the fallout of the pandemic. In Mexico, office rental prices should recover gradually and return to pre-pandemic levels beginning in mid-2024.
Retail	Improving	Neutral	⇩	• Stagflation would lead to demand volatility. • Omnichannel development might continue to put pressure on margins, as logistics and IT-related expenses are keys to success in the digital era. • Profitability recovery from the pandemic could be supported by supply chain issues, as an extended inventory lifecycle might reduce the frequency of commercial discounts. • Higher interest rates will have a manageable effect on cash flows, with the effect more pronounced in Brazil due to the recent rate spike. • For the rest of 2022, Fitch expects discretionary spending to be affected by higher inflation and fewer commercial campaigns.
Cement	Neutral	Neutral	⇔	• The cement sector would be affected by stagflation, due to a potential decline in volumes and continued inflationary pressure. • Local political and macroeconomic volatility, including higher interest rates and credit access, adds further pressure for some issuers. • High raw material prices, including pet coke and coal, have significantly increased, which is likely to have a major impact in 2Q22 and 3Q22. • Most issuers in the region are implementing price increases, which are likely to partially offset higher energy costs and inflation-linked SG&A. Increasing use of alternative fuels should also help. High prices and interest rates will affect consumers, mostly in the residential segment. • Sales trends across the region have been mixed. Volume growth in Peru and Argentina has been robust so far in 2022, volumes in Colombia and Chile are stable, and volumes are declining in Mexico and Brazil. • Most Fitch-rated issuers have adequate capital structures, while liquidity/refinancing risks are manageable.
Energy (Oil & Gas)	Neutral	Neutral	⇔	• Small independent energy companies' cash flow is benefiting from higher oil prices and most companies have curbed expansion plans and are focused on streamlining costs and maintaining production. Capex is focused on maintaining production and reserve levels. We expect excess cash flow to be allocated between returning cash to shareholders and debt repayment. • Government-related entities, including Ecopetrol, Pemex, Petrobras and YPF, will face political pressure to not fully execute their import parity pricing policies if Brent stays above USD100/barrel. High fuel prices combined with presidential elections in Colombia and Brazil are leading to government interference at Petrobras, and a plan to move away from energy dependence in Colombia. In addition, the Mexican government recently pivoted and withdrew its announced support for PEMEX. Risk of government interference is reflected in all government-related entity ratings.
Non-Alcoholic Beverages	Neutral	Neutral	⇔	• We expect volume growth despite inflation. On-premise and out-of-home sales are growing, with resilient traditional and modern channels. • Raw material cost pressures are likely to continue in 2022, particularly for sweetners and PET packaging, but hedging, price actions, better sales mix and operating efficiences are helping protect profitability. • Rating changes are not anticipated, as Fitch projects the median EBITDA margin will remain relatively stable at around 18% and median net leverage will be similar to the 1.0x in 2021 at around 0.9x in 2022.

Latin America Outlooks (11) (Cont.)

Sector	2022 Outlook – Dec 21	2022 Outlook – Jun 22	Trend	Comments
Packaged Foods	Neutral	Neutral	⇔	• The mix of growth between at-home and out-of-home consumption is more balanced, with low asset exposure to Russia and Ukraine. • High input costs, including corn, wheat, oil and sugar, packaging, labour and energy are challenges, but hedging, price increases, better sales mix and operating efficiencies will mitigate cost pressures. • Government price controls to lessen the effect of inflation on essential products are a risk. • Fitch projects median EBITDA margins of 9.6% in 2020, modestly lower than the 10% in 2021. We also expect the sector to maintain conservative financial positions and robust cash generation, with a stable median net leverage forecast of 2.3x for 2022.
Protein	Neutral	Neutral	⇔	• Demand remains robust, with the reopening of the food service industry and good access to export markets. However, we expect some EBITDA margin pressure in 2022 due to commodity, logistics and labour cost inflation. • Conservative capital structures and good liquidity increase the sector's resilience in a challenge operating environment.
Sugar and Ethanol	Neutral	Neutral	⇔	• The pricing scenario for sugar and ethanol has improved in 2022 as the Russian-Ukraine conflict has sent international oil prices higher. Higher oil prices will keep domestic ethanol prices at historically high levels and will help sustain sugar prices at an average level of over USD0.18/pound in 2022. Sugar prices in Brazilian real terms are at historical highs, also reflecting a weak local currency. However, the positive pricing scenario is tempered by high cost inflation, notably in labour, diesel and fertilizers. • Potential disruptions in supply of fertilizers and the possibility of a sluggish recovery of sugar cane crush volumes in the ongoing crop season bring additional uncertainty to cash flow prospects for most issuers. • High corn prices will put pressure on corn ethanol producers' cash flow. The recent rise in interest rates will also have a negative impact on the cash flows of sugar and ethanol companies. Leverage should benefit from strong EBITDA generation due to high prices and a stronger-than-anticipated Brazilian real due to US dollar-denominated debt in their capital structure. Most Fitch-rated ssuers have satisfactory liquidity for the rest of the year.
Pulp, Paper and Forest Products	Neutral	Neutral	⇔	• Fitch projects average bleached eucalyptus kraft pulp (BEKP) prices of USD700/ton in 2022, from USD677/ton in 2021. The pulp market remains tight and prices gained momentum at the beginning of 2022, supported by unexpected supply disruptions, maintenance downtimes, low inventories and logistics constraints, despite weakening demand from China. Increased supply from Latin America and weaker demand from paper producers due to margin pressure are likely to put pressure on pulp pricies during 2H22. Low inventories on the buyers' side should prevent a rapid drop in prices, and low availability of softwood will continue to support a larger gap than historical between BEKP and Northern bleached softwood kraft prices during 2022. Higher cash costs, mainly due to high brent prices, chemicals and wood, are likely to contribute to a new pulp price floor through the cycle.
Telecommunications	Neutral	Neutral	⇔	• Growing demand for data services should result in resilient demand for telecom services, particulary broadband and mobile services, with Pay-TV being more of a moderate differentiator among telecom providers. • Inflation will be broad based rather than spikes in certain tiers of cost structures. There is low direct exposure to commodities. Personnel expenses represent around 10% or less of cost structures and are periodically adjusted for inflation retroactively, allowing issuers to budget and include the expenses in their pricing strategies. Handsets and equipment represent 20%-30% of the cost structure and are more exposed to exhange rates. • Spinoffs of certain relevant assets, such as antennas or fibre optic infrastructure will continue due to the high commercial value of these assets, strong data demand and investment required for 5G. We expect 5G investments to acceletrate. However, the conclusion of other investment programmes, infrastructure sharing, and proceeds from the divesture or spin off of assets will lessen cash flow and balance-sheet effects.

Latin America Outlooks (11) (Cont.)

Sector	2022 Outlook – Dec 21	2022 Outlook – Jun 22	Trend	Comments
Utilities	Neutral	Neutral	⇔	• Argentina: The sector remains challenged by central bank capital controls restricting private companies' access to the FX market until December 2022. High fuel prices may put pressure on government subsidies to Compania Administradora del Mercado Mayorista Electrico S.A. • Brazil: Energy consumption returned to pre-pandemic levels in all segments, with slight growth of 0.5% expected for 2022 (+0.9% in 1Q22 vs 1Q21). Hydrological risk is lower in 2022, which will benefit distribution companies and hydro generators, with less energy purchases from expensive thermal plants for distribution companies and higher available energy to be sold by hydro generators. • Chile: The government is implementing a second mechanism for regulated customers to keep end-user tariffs under control, as the first price stabilization mechanism reached its cap without affecting the system payment chain. Additional pressure on marginal costs comes from lower hydro generation and higher international prices for coal and natural gas, causing Fitch to revise marginal cost assumptions up. Lower hydro production is shifting government decarbonization policies in the short term. • Colombia: Electricity demand is exceeding Fitch's expectation due to a strong economic recovery. We expect generation companies' median leverage to drop slightly to 2.9x in 2022 from 3.0x in 2021 due to robust operating cash flow and a balanced mix of funding sources to finance planned capacity expansion toward renewable sources. Possible delays in hydroelectric projects coming online or the addition of power from various renewable energy projects could result in upward pressure on energy prices. Delays in different transmission infrastructure projects is challenging the entrance of non-conventional renewable projects in the coastal region. • Dominican Republic: Marginal costs are up significantly due to rising coal and LNG prices and the country's dependence on imports of these commodities. In April 2022, 43% of generation was from natural gas, 26% from coal, 13% from fuel oil, 6% from hydro and 3% from solar. • Panama: As a result of high global LNG prices and Panama's lack of local gas supply, spot prices in 1Q22 were 118% higher than in March 2021. Fitch expects prices to moderate in the middle of the year as the country enters the rainy season, which will help hydrology conditions, and ramp up again in 4Q should LNG prices remain high. • Peru: Utilities are insulated from higher global energy prices, as Peru produces enough gas to support the country's needs. Electricity sources are 55% from thermal power plants and 45% from hydrological plants. However, slower-than-expected economic activity during 2022 will reduce demand and consumption, and slow public and private investment and new capex plans. Peruvian utilities are likely to manintain their low leverage, supported by stable cash flow, which helps offset the uncertainty surrounding political stability and governmental neutrality.

Source: Fitch Ratings