



Favorable market conditions reduced global airlines' credit risk but long-term outlook remains cloudy

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- **NUS-CRI Agg 1-year PD indicates that globally listed airlines' credit risk decreased amid improved liquidity**
- **Despite the short-term improvement in the industry's credit outlook, long-term credit risk is heightened as illustrated by the NUS-CRI Forward PD**

As vaccination efforts recently gained ground, investors are becoming increasingly optimistic about prospects of travel restarting and economic recovery. Leveraging on the benign market condition, airlines have been raising debt at a near-record pace to beef up their balance sheet and cover their cash burn. Amid the improvement in airlines' liquidity position in conjunction with lower borrowing costs, the NUS-CRI Aggregate (median) 1-year Probability of Default (Agg PD) has shown a downward trend since Feb 2021 (Figure 1a). The long-term credit outlook, as demonstrated by the NUS-CRI Agg 1-year Forward PD (Forward PD¹) in Figure 1b, however, remains cloudy with potential headwinds from high debt burden, uncertainty in future travel demand, and environmental, social and governmental (ESG) concerns.

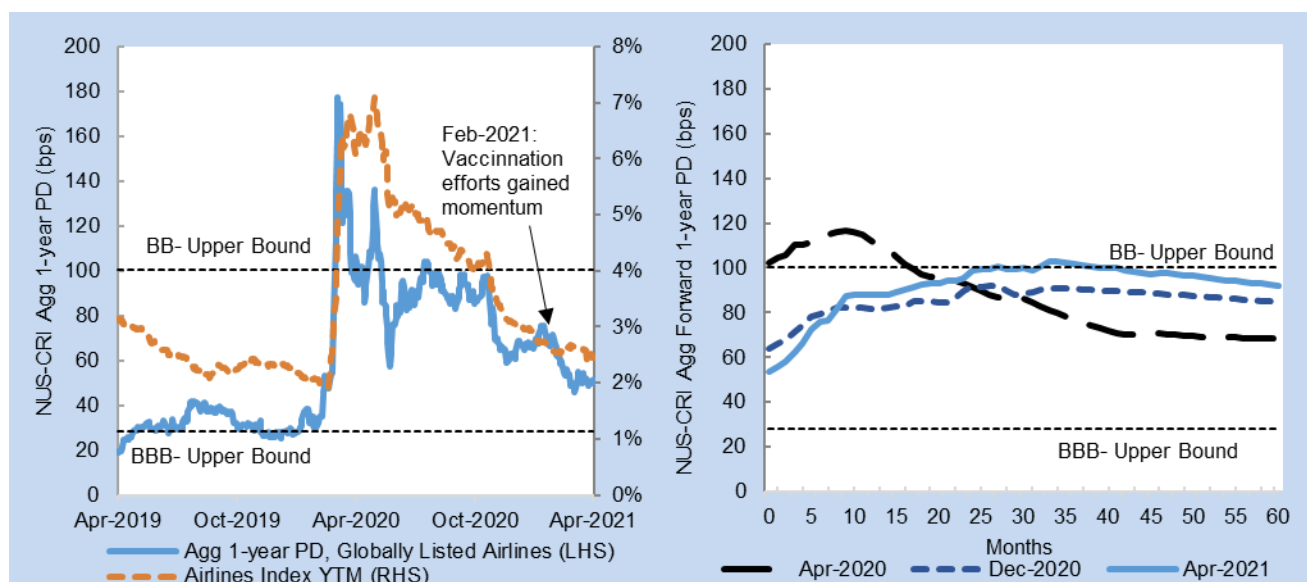


Figure 1a (LHS): NUS-CRI Agg 1-year PD for globally listed airlines from Apr 2019 to Apr 2021 with reference to PDiR2.0² bounds and Bloomberg Barclays Global Aggregate Corporate - airlines index YTM. Figure 1b (RHS): NUS-CRI Agg Forward 1-year PD for globally listed airlines based on information available in Apr 2020, Dec 2020 and Apr 2021. Source: NUS-CRI, Bloomberg

The Forward PD based on the Apr 2021 data feed in Figure 1b indicates that the short-term credit outlook for the airline industry has steadily improved over the last year. The continued debt binge, however, could lead to heightened credit risks in the long term as airlines find themselves saddled with an increasingly levered balance sheet. The Forward PD in Figure 1b indicates that the long-term credit outlook in Apr 2021 has worsened when compared to that of Apr 2020. For instance, the 36-month Forward PD increased from 90.7bps in Dec 2020 to 104.0bps in Apr 2021.

¹ The Forward PD estimates the credit risk of a company in a future period, which can be interpreted similarly to a forward interest rate. For example, the 6-month Forward 1-year PD is the probability that the firm defaults during the period from 6 months onwards to 18 months – this is conditional on the firm's survival in the next 6 months

² The Probability of Default implied rating version 2.0 (PDiR2.0) provides a more familiar interpretation through mapping the NUS-CRI 1-year PDs to the S&P letter grades. The method targets S&P's historical credit rating migration experience exhibited by its global corporate rating pool instead of relying solely on the reported default rates

The credit migration matrix by CriAT's iRAP³ presents the NUS-CRI Probability of Default implied rating version 2.0 (PDiR2.0) distribution of globally listed airlines. Even though the majority of companies in this industry are non-investment grade (non-IG) (see Figure 2a), the rising proportion of investment-grade (IG) companies from Apr 2020 to Apr 2021 demonstrates an improvement in credit health for airlines, with the proportion of IG companies increasing from 21% to 31%. The forecasted credit migration from now to next year, however, suggests that the industry might face a larger proportion of firms migrating into the non-IG category.

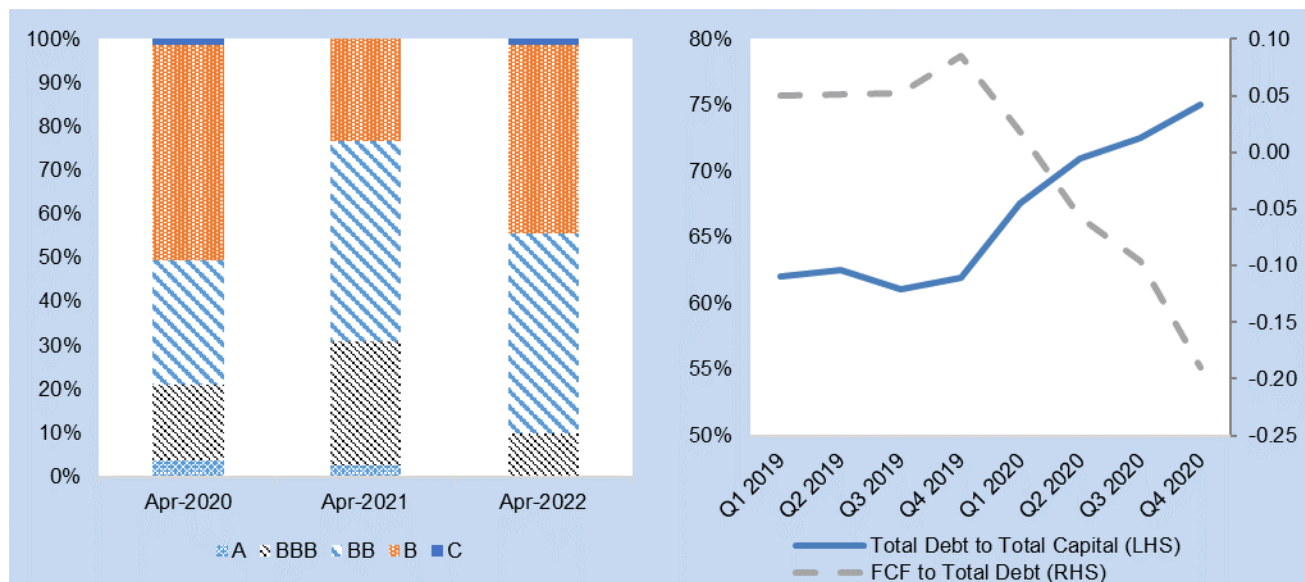


Figure 2a (LHS): Apr-2020, Apr-2021 and Apr-2022 (forecasted) credit distributions for globally listed airlines. Figure 2b (RHS): Total debt to total capital and FCF to total debt for airline industry from 2019 to 2020. *Source: CriAT, Bloomberg*

It is going to take much longer for global airlines to stop burning through cash. According to the International Air Transport Associations (IATA), the industry has burned [around USD 125bn](#) cash from Q2 2020 to Q4 2020 and is projected to burn [USD 75-95bn](#) in 2021, even though they have managed to cut costs since the breakout of the COVID-19 pandemic. After the lockdowns and travel bans, cash flow for airlines became negative (see Figure 2b). The recently borrowed cash will help fortify airlines' balance sheets and provide liquidity as uncertainty remains on whether operations will revert to pre-pandemic levels. Despite the ambitious vaccine rollout, wide vaccination is expected to take some time. Bookings for the summer of 2021 are still [78% lower](#) than the same period in 2019 and a full recovery will likely [take several years](#). Before mass vaccinations, airlines will continue to suffer from weak demand and travel restrictions, which in turn, pose risks on their top lines.

Airlines have been borrowing substantially in the bond market since the outbreak of COVID-19, enabled by investors' appetite for higher yields amid the low interest rate environment. In 2020, airlines raised a record-high USD 42.6bn in the debt markets. As a result, the total debt to total capital ratio for the airline industry rose continuously from 61.97% at the end of 2019 to 75.01% in Q4 2020 (Figure 2b). With a substantial USD 53bn amount of debt maturing from 2021 to 2023 and uncertainties in travel demand recovery, globally listed airlines could face increasing difficulties in servicing their debts. Furthermore, the possibility of an increase in borrowing cost in the future as proxied by the rising US Treasuries' yield could complicate airlines' refinancing plan.

To add on, pressures from governments and regulators on airlines' environmental impact have intensified with the development of multilateral legal frameworks such as ICAO's Carbon Offsetting and Reduction Scheme for International Aviation (CORSIA) and EU's Emission Trading System (ETS). For instance, the [CARES act](#), which provided vital stimulus to the US airline industry, has covenants that aim to reduce carbon emission in half by 2050. Similarly, the Dutch government's package for KLM requires the airline to [reduce its greenhouse gas emissions](#), driven by the use of more [sustainable jet fuels](#). As airlines are prompted to phase out older and less fuel-efficient airplanes to become more environmentally friendly, airlines' free cash flow could dampen moving forward.

³ iRAP (intelligent Risk Analysis Platform) is a software developed by CriAT (<https://www.criat.sg/>) for conducting both firm-level and portfolio level credit analysis. iRAP utilizes the NUS-CRI Probability of Default (PD) model and links it to the live NUS-CRI database offering PDs on almost 80,000 exchange-listed corporates globally

Credit News**Coalition of big investors pushes banks to defund carbon emitters**

Apr 19. A group of investors has put pressure on 27 global banks to stop financing carbon-intensive projects and to scale up their green lending practices. The coalition has called on banks to align their financing with a goal of net-zero emissions while asking executive pay to be linked with the meeting of this target. This follows the trend of climate-focused investors shifting their targets from big carbon emitters such as oil and gas to those providing their finances. Though these efforts aid in reducing the accessibility of finances for carbon-intensive projects, critics argue that they do not have the intended impact, citing green metrics don't include emissions produced by customers and suppliers. ([FT](#))

Surge in illegal bank loan-funded China property buys worries regulators

Apr 16. The property market in China is increasingly being funded by fraudulent loans, worrying regulators of the country. Around CNY 878mn worth of loans were misused to fund housing in cities such as Shenzhen and Shanghai. This poses an issue for the government, as it hopes to provide strong credit support while quelling the misuse of loans. Cities are now insisting that homebuyers have residential permits for up to five years and providing a cash down payment of 30%. ([Reuters](#))

Global derivatives cling to Libor even as its finale nears

Apr 15. Hundreds of trillions of dollars' worth of derivatives are still being traded based on the Libor even though investors have been expecting a shift toward replacement benchmark rates. Markets such as the UK, US, and Japan are still trailing in terms of alternate benchmark transition even though the final use of Libor is set to take place at the end of this year. With the TONA still raking in only 2.4% of activity in Japan, SOFR accounting for only 4.7% of activity in the US, and Sonia accounting for 45% of activity in the UK, the lack of a clear transition timeline and scale represent the stickiness present in the current Libor benchmarking system. ([Bloomberg](#))

Bonds of China's largest debt investor plunge to record low

Apr 13. Huarong Asset Management has seen its bonds fall to record low prices as it faces uncertainty in its financial health. Its USD 350mn bond maturing in 2030 fell by 9% to 77 cents on the dollar and its USD 1.5bn perpetual bonds fell to 81 cents on the dollar. The company has delayed the release of its financial results, stating that auditors would need to finalize the transaction. In light of this, S&P has issued a warning on the credit health of the firm. Huarong Asset Management joins a slew of Chinese companies, such as China Fortune Land Development, that have faced trouble in international markets. Furthermore, the shares of Huarong have been suspended since the beginning of April. ([FT](#))

United Airlines to repay some of its US government bailout

Apr 13. United Airlines has paid back a sliver of the money it borrowed from the government during the height of the pandemic by using its USD 9bn fundraising across the bond and loan markets. The carrier paid off USD 520mn of its USD 7.7bn borrowings. As vaccinations continue to proceed and as air travel picks up in pace, debt markets are allowing companies to continue tapping into the capital markets. The company plans to borrow USD 5.5bn through bonds maturing in 2026 and 2029, and a further USD 3.5bn in the leveraged loan market. United Airlines also hopes to set up a new USD 1.75bn revolving credit line with its banks. As such, along with paying back some of its government debt, the company looks to refinance USD 2.4bn of other debt and USD 1bn of credit lines. ([FT](#))

India defaults spark rules that drag bond sales to 13-year low ([Bloomberg](#))

Bank of America joins post-earnings bond frenzy with six-part debt offering ([Bloomberg](#))

Tencent raises USD 4.2bn in its second major bond deal in a year ([Reuters](#))

Regulatory Updates**EU split over delay to decision on classing gas as green investment**

Apr 18. The European Commission faces a challenge on whether to classify fossil fuel-generated gas as a green energy source. Member states in the EU, such as Poland and Hungary, have pushed for gas to be recognized as a low-emission source to help meet their goal as a net-zero polluter by 2050. At the same time, France and the Czech Republic hope that Nuclear energy would be considered a transitional energy source. However, uncertainty remains as should these unsustainable energy sources be included under green energy classifications, greenwashing could occur. The EU has avoided using these classifications for green bonds to be issued under the EUR 800bn recovery and resilience fund. ([FT](#))

Turkey's new central bank chief leaves interest rate unchanged

Apr 15. Turkey's central bank, in its first rate-setting meeting since the new governor took charge, has left its policy rates unchanged while signaling loosening potential depending on inflation levels. The one-week repo rate remains at 19%, with the new governor citing that the policy rate will remain above the inflation rate of 16% to maintain a strong disinflationary effect to a medium-term inflation goal set at 5%. President Erdogan hopes to reduce both interest rates and inflation to single digits in the future. The country's unexpected dismissal of its previous governor rattled the capital markets, with the Turkish lira depreciating by 10% against the US dollar. ([FT](#))

PBOC to more than double scope of stress test ([Central Banking](#))

South Africa central bank governor sees room to keep rates low ([Bloomberg](#))

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