DECEMBER CREDIT OUTLOOK

Resilient Labor Market but Recession Looming

Inflation

Inflation continued to ease in November with the consumer price index coming down to 7.1% from 7.7%, compared to prior month. This marks 5 months of declines from its peak in June, which was attributed to fuel, electricity, and vehicles. The consumer price index was down for all items at .01% from .04% compared to the prior month. Inflation is finally trending in the right direction and the Fed will likely ease its rate hikes to 50 basis points going forward.

Unemployment

The U.S. added 263,000 jobs in November, which was above economist expectations of 200,000. The unemployment rate was unchanged at 3.7% and remains close to historic lows. Average wage growth was 0.6%, which exceeded expectations and is the fastest increase since the start of the year. The labor market continues to show its resilience and strength, despite persistent and continued rate hikes. We expect the news will be unwelcomed by the Fed and that they will continue to act accordingly.

Insolvencies

Filings continue to increase with total bankruptcies for November up at 6% when compared to a year ago. Small business subchapter V bankruptcy increased to 38% and Commercial Chapter 11 was up to 74% when compared to prior year. Please note that the large increase in Chapter 11 filings is due to FTX bankruptcy, which has attributed to over 100 cases. Also, Canada is experiencing a similar trend with bankruptcies up 22.5% in the third quarter, which is the biggest increase in 13 years. Overall, we are seeing businesses utilize bankruptcy as a lifeline as liquidity markets have tightened and debt borrowing has become too expensive.

CURRENT & EVOLVING CREDIT RISKS

Trade Payments

We are seeing an increase in past due invoices and protracted default being reported within our subscriber base. Generally, these incidents have been cases of significantly past due invoices beyond 60 to 90 days or non-payments. Muted growth and the impact on cash flows from higher interest rates are putting downward pressure on credit quality, which is impacting the ability to pay invoices on time or at all.

Liquidity

Liquidity constraints have been increasingly cited as reasons for financial distress. Companies holding speculative or "junk" rated debt are the most sensitive to a higher interest rate environment and will likely be the first to show strain. Many privately held companies are facing the same issues as they battle higher cost structures and working capital needs.

Risk Rating Trends

Corporate credit quality continues deteriorate as downgrades outpace upgrades. This is no surprise as borrowing costs are rising significantly on the back of weaker operating results. With the risk of a recession in 2023 becoming increasingly possible, this trend may continue, and more defaults are expected.

U.S. Annual Inflation Rate