Credit Benchmark

Fallen Angels: Potential Defaults Climb as Ranks Grow

July 2020

Rating agency downgrades have hit unprecedented levels over the past few months, but the majority of these are companies that were already classed as high yield. Fallen Angels – companies that cross the boundary from Investment-Grade to "Junk" – are still in a minority, as agencies (and their corporate clients) display an understandable reluctance to avoid the "BBB cliff".

Consensus credit data from Credit Benchmark – which gathers the collective credit quality estimates of lenders to these firms – shows that a growing number of companies are falling over the cliff edge, providing clues to likely future default rates.

Consider the full set of global sectors. In this sample, of 6,894 companies, 578 (about 8%) have migrated to and remained in sub-Investment-Grade territory over this period, as seen in Figure 1.

Figure 1: Fallen Angels % by Global Sector

Sector	Sample of IG companies end-Feb 20	Cumulative # Fallen Angels Mar - Jun 20	Cumulative % Fallen Angels Mar - Jun 20
Travel & Leisure	189	65	34.4%
Leisure Goods	22	5	22.7%
Industrial Metals & Mining	64	13	20.3%
Automobiles & Parts	384	55	14.3%
Media	151	19	12.6%
Oil & Gas Producers	492	61	12.4%
Chemicals	388	44	11.3%
Forestry & Paper	63	7	11.1%
General Retailers	605	66	10.9%
Personal Goods	65	7	10.8%
Aerospace & Defense	76	8	10.5%
Construction & Materials	316	30	9.5%
Full Sample	6894	578	8.4%
Household Goods & Home Construction	169	14	8.3%
Industrial Transportation	346	28	8.1%
Support Services	469	29	6.2%
Food Producers	396	24	6.1%
Software & Computer Services	253	15	5.9%
Electronic & Electrical Equipment	204	12	5.9%
Technology Hardware & Equipment	104	6	5.8%
Beverages	87	5	5.7%
Industrial Engineering	219	12	5.5%
Mining	220	12	5.5%
Oil Equipment, Services & Distribution	168	9	5.4%
Food & Drug Retailers	77	4	5.2%
Pharmaceuticals & Biotechnology	142	5	3.5%
General Industrials	62	2	3.2%
Gas, Water & Multi-utilities	303	7	2.3%
Health Care Equipment & Services	227	5	2.2%
Fixed Line Telecommunications	141	3	2.1%
Electricity	448	6	1.3%
Mobile Telecommunications	19	-	0.0%
Tobacco	25	-	0.0%

The sector showing the most significant deterioration is Travel & Leisure, with about 34% of firms now classified as Fallen Angels. The Leisure Goods and Metals & Mining sectors follow with roughly 23% and 20% of constituents now classified as Fallen Angels, respectively.

Other sectors showing double-digit rates in this month's update include Automobiles & Parts, Media, and Oil & Gas Producers, with about 14%, 13%, and 12% of constituents classified as Fallen Angels, respectively.

The deterioration can also be seen further down in the chart. In the Oil Equipment, Services & Distribution sector, for instance, the percentage of Fallen Angels has grown from around 4% to about 5%.

Only two sectors – Mobile Telecommunications & Tobacco, each of which is new to the dataset – have no firms in the Fallen Angels category.

In the previous update, we noted that Ed Altman suggested that up to a third of all corporate bonds in the BBB category could move to "Junk" status, an estimate consensus credit data supports.

The consensus credit sample examined above is based on issuers as opposed to issues and includes all Investment-Grade companies, not only BBB. Still, the growing Fallen Angel rates shown here – which cover just four months of the COVID crisis – indicate that the shift for some sectors by the end of 2020 may be even higher than has so far been suggested.