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Morningstar Corporate Credit Research Highlights

Corporate credit spreads tighten following Trump's address to Congress.

Morningstar Credit Ratings, LLC
6 March 2017

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Credit Market Insights

- Market data and insights.
- Probability of March interest rate hike soars.
- High-yield fund flows remain muted in contrast to rapidly tightening credit spreads.

Credit Rating Actions

- Rating Changes

Issuer/Ticker	Current Issuer Credit Rating	Previous Issuer Credit Rating
Arconic ARNC	BB+	None
Abbott Laboratories ABT	BBB+	A

- Rating Affirmations

Issuer/Ticker	Current Issuer Credit Rating	Previous Issuer Credit Rating
Bed Bath & Beyond BBBY	BBB+	BBB+
Sysco SYY	A-	A-
Kraft Heinz KHC	BBB-	BBB-
Hormel Foods HRL	AA-	AA-
Comerica CMA	A-	A-
Regions Financial RF	BBB	BBB
Royal Dutch Shell RDS.B	A	A
Biogen BIIB	A	A
BP BP	A-	A-
Teva Pharmaceutical Industries TEVA	BBB-	BBB-
Citigroup C	A-	A-
Stryker SYK	A+	A+
Zions ZION	BBB-	BBB-
Goldman Sachs GS	BBB+	BBB+
Morgan Stanley MS	BBB	BBB
Bank of America BAC	BBB	BBB

Recent Notes Published by Credit Analysts

- **Perrigo** selling Tysabri royalty stream; focuses on debt reduction.
- **Discovery** announces new 7-year senior notes and reopens the 2026 notes.
- **J&J** issuing debt for share repurchases and commercial paper repayment.
- **Tenet** disappoints in 4Q, and management delays deleveraging timeline.
- **Endo** gets a major haircut, targets lower leverage.
- **Frontier** battles operational headwinds in 4Q, but 2017 outlook is better.
- **Disney** announces new 5-year senior notes.
- And more.

Credit Market Insights

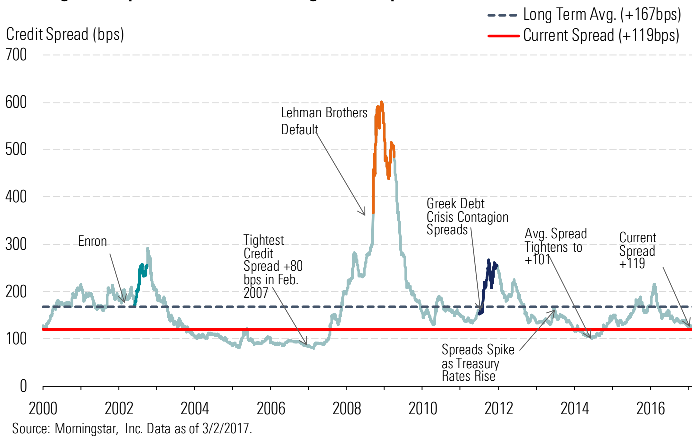
Corporate Credit Spreads Tighten Following Trump's Address to Congress

While the markets pulled back slightly in the latter half of the week, risk assets remained near their highs after a significant boost Wednesday following President Donald Trump's address to Congress. The average spread of the Morningstar Corporate Bond Index, our proxy for the investment-grade bond market, tightened 5 basis points to +118 last week. In the high-yield market, the credit spread of the Bank of America Merrill Lynch High Yield Master Index tightened 24 basis points to +360.

While current levels are wider than their historical lows of 2007, the corporate bond market levels are the tightest that credit spreads have registered since the fall of 2014 and significantly tighter than their long-term averages. The average spread of the Morningstar Corporate Bond Index is 50 basis points tighter than its long-term average of +168 since the end of 1998. The average spread of the Bank of America Merrill Lynch High Yield Master Index is currently 220 basis points tighter than its long-term average of +580 basis points since the end of 1996.

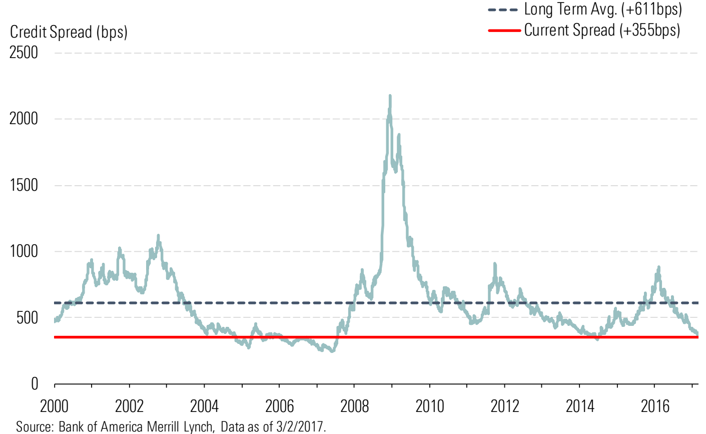
As an indication of how tight corporate credit spreads have become compared with their historical averages, since the beginning of 2000, the average spread of the Morningstar Corporate Bond Index has registered below the current level only 26% of the time. In the high-yield market, the average spread of the Bank of America Merrill Lynch High Yield Master Index has registered below its current level less than 13% of the time over the past 17 years. The preponderance of the time that the index resided at a level tighter than the current credit spread occurred during the buildup to the 2008-09 credit crisis. During 2004-07, corporate credit spreads were pushed to historically tight levels as new structured investment vehicles were engineered to arbitrage the differentials in expected default risk; however, once the credit crisis emerged, investors found that many of these vehicles did not perform as advertised.

Morningstar Corporate Bond Index Average Credit Spread



Source: Morningstar, Inc. Data as of 3/2/2017.

BofA Merrill Lynch US High Yield Option-Adjusted Spread



Source: Bank of America Merrill Lynch, Data as of 3/2/2017.

Probability of March Interest Rate Hike Soars

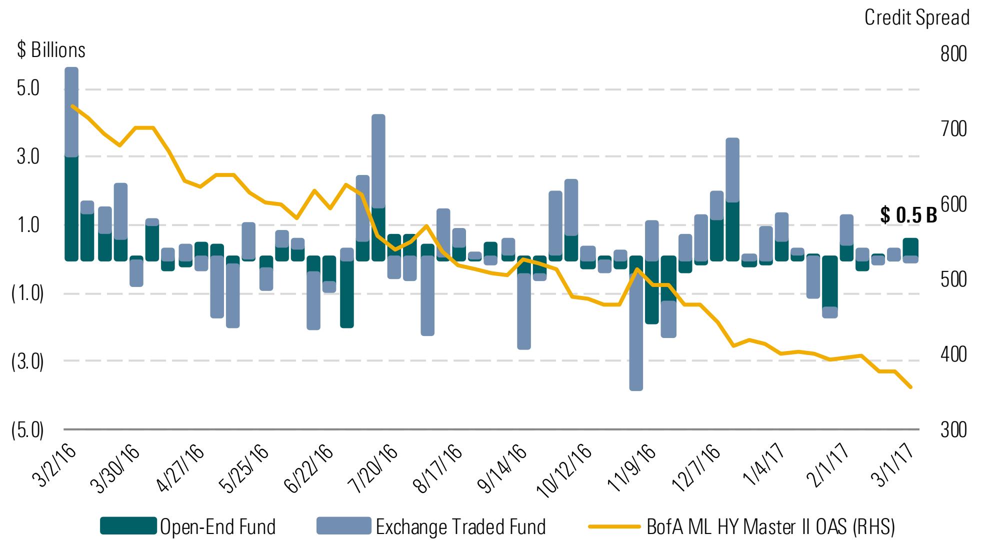
While risk assets performed well last week, U.S. Treasury bond prices fell precipitously as the market re-evaluated the probability that the Federal Reserve will increase the federal funds rate following the Federal Open Market Committee meeting March 14-15. Between language in the minutes released from the prior Fed meeting and intimations contained in the speeches by several Fed governors, the market-implied probability of a March rate hike rose to over 80%, according to CME, from only 22% the prior week. As bond prices fell, interest rates rose across the yield curve. The yield on the 2-year Treasury bond rose 17 basis points to 1.31%, the highest yield the 2-year bond has reached since 2009. The 5-year bond rose 21 basis points to 2.01%, the 10-year increased 17 basis points to 2.48%, and the 30-year rose 12 basis points to 3.07%. Even if the Fed increases the federal funds rate by 25 basis points to 75-100 basis points, this range still represents a highly simulative monetary policy. Before the 2008-09 credit crisis, the lowest the federal funds rate had been targeted was 1.00% in 2003, when the Fed was trying to prop up the economy after the tech bubble burst.

Sovereign interest rates in other developed markets also rose last week. The interest rate on Germany's 2-year bond, which had hit new historical negative yields the prior week, rose 16 basis points to negative 0.80%. The yield on Germany's 10-year bond rose 17 basis points to 0.36%. The spread between German and French sovereign bonds also began to normalize last week after having widened in reaction to National Front leader Marine Le Pen's rise in recent French presidential election polls. The National Front has long advocated against the European Union, and Le Pen's platform advocates for a referendum on France's membership in the EU as well as restoring a national currency.

High-Yield Fund Flows Remain Muted in Contrast to Rapidly Tightening Credit Spreads

Although credit spreads tightened, the amount of inflows into the high-yield asset class remained subdued last week. Among the high-yield open-end mutual funds and exchange-traded funds, only $0.5 billion of funds flowed into the asset class. The inflows were concentrated in the open-end mutual fund category (generally considered a retail investor product) as fund flows into ETFs (generally considered an institutional investor category) were essentially unchanged for the week.

Estimated Weekly High-Yield Bond Fund Flows and High Yield Credit Spreads



Source: Morningstar , Inc. and BofA Merrill Lynch Global Indexes.

Exhibit 1 Morningstar Credit New Issue Monitor
Week ended March 3, 2017
(000,000s $ unless otherwise noted)

Issuer			Issue				
Name	Ticker	Morningstar Corporate Rating	Size	Coupon	Description	Maturity	Approx Spread to US Treasuries
Air Liquide Finance	AI	BBB+[1]	€ 600	1.00%	Senior Unsecured	2027	+85
American Express Credit	AXP	A-[1]	$2,000	2.20%	Senior Unsecured	2020	+72
American Express Credit	AXP	A-[1]	$450	L+43	Senior Unsecured	2020	NA
American Express Credit	AXP	A-[1]	$1,750	2.70%	Senior Unsecured	2022	+82
American Express Credit	AXP	A-[1]	$300	L+70	Senior Unsecured	2022	NA
Charles Schwab	SCHW	A+	$650	3.20%	Senior Unsecured	2027	+85
Chevron	CVX	AA-	$550	1.69%	Senior Unsecured	2019	+45
Chevron	CVX	AA-	$450	L+9	Senior Unsecured	2019	NA
Chevron	CVX	AA-	$600	1.99%	Senior Unsecured	2020	+50
Chevron	CVX	AA-	$400	L+21	Senior Unsecured	2020	NA
Chevron	CVX	AA-	$700	2.50%	Senior Unsecured	2022	+60
Chevron	CVX	AA-	$300	L+48	Senior Unsecured	2022	NA
Chevron	CVX	AA-	$1,000	2.90%	Senior Unsecured	2024	+70
Coca-Cola	KO	A+	€ 1,500	L+25	Senior Unsecured	2019	NA
Coca-Cola	KO	A+	€ 500	0.00%	Senior Unsecured	2021	+10[2]
Coca-Cola	KO	A+	€ 500	0.50%	Senior Unsecured	2024	+23[2]
Discovery Communications	DISCA	BBB	$450	3.80%	Senior Unsecured	2024	+165
Discovery Communications	DISCA	BBB	$200	4.90%	Senior Unsecured	2026	+185
Johnson & Johnson	JNJ	AAA	$1,000	2.25%	Senior Unsecured	2022	+37
Johnson & Johnson	JNJ	AAA	$1,000	2.95%	Senior Unsecured	2027	+57
Johnson & Johnson	JNJ	AAA	$1,500	2.63%	Senior Unsecured	2037	+65
Johnson & Johnson	JNJ	AAA	$1,000	3.75%	Senior Unsecured	2047	+77
Pfizer	PFE	AA-	€ 1,250	Euribor+20	Senior Unsecured	2019	NA
Pfizer	PFE	AA-	€ 1,000	0.00%	Senior Unsecured	2020	+12[2]
Pfizer	PFE	AA-	€ 1,000	0.25%	Senior Unsecured	2022	+20[2]
Pfizer	PFE	AA-	€ 750	1.00%	Senior Unsecured	2027	+45[2]
Vodafone Group	VOD	BBB	€ 175	0.63%	Senior Unsecured	2027	+53
Walt Disney	DIS	A+	$600	1.95%	Senior Unsecured	2020	+40
Walt Disney	DIS	A+	$400	L+13	Senior Unsecured	2020	NA
Walt Disney	DIS	A+	$500	2.45%	Senior Unsecured	2022	+50
Walt Disney	DIS	A+	$500	L+39	Senior Unsecured	2022	NA

Source: Advantage Data, Company SEC fillings.
(1) Morningstar's issuer credit rating is assigned at the holding company level.
(2) Spread over mid-swaps.

Exhibit 2 Morningstar, Inc. Corporate Bond Index Sector Summary

Sector	Average Rating	Number of Issues	Modified Duration	Spread (bps)	MTD Spread Chg (bps)	YTD Spread Chg (bps)	MTD Total Return (%)	YTD Total Return (%)
TOTAL	**A-**	**4,668**	**6.8**	**118**	**(3)**	**(10)**	**(0.49)**	**0.99**
FINANCIAL	**A-**	**1,437**	**5.5**	**110**	**(3)**	**(12)**	**(0.39)**	**0.93**
Bank	A-	887	5.1	111	(3)	(11)	(0.35)	0.82
Finance	A	259	5.7	103	(2)	(18)	(0.42)	1.26
Insurance	A	212	7.6	113	(3)	(9)	(0.55)	1.08
REITs	BBB+	71	6.0	124	(2)	(11)	(0.51)	1.11
INDUSTRIAL	**A-**	**2,672**	**7.4**	**121**	**(3)**	**(9)**	**(0.53)**	**0.98**
Basic Industries	BBB+	226	7.6	154	(1)	(26)	(0.48)	2.86
Consumer Products	A-	292	7.5	102	(2)	(5)	(0.65)	0.54
Energy	A-	402	7.1	144	(3)	(11)	(0.46)	1.50
Healthcare	A-	392	7.6	107	(5)	(9)	(0.50)	0.94
Manufacturing	A-	386	6.2	97	(2)	(13)	(0.48)	0.92
Media	BBB+	192	8.2	152	(3)	(6)	(0.66)	0.77
Retail	A-	163	8.0	106	(3)	(2)	(0.64)	0.38
Technology	A+	291	7.1	95	(4)	(10)	(0.47)	0.84
Telecom	BBB+	157	8.5	160	(1)	2	(0.55)	0.01
Transportation	BBB+	130	8.9	125	(3)	(8)	(0.71)	1.06
UTILITY	**BBB+**	**515**	**8.2**	**142**	**(2)**	**(10)**	**(0.71)**	**1.38**
Electric Utilities	A-	302	8.6	127	(2)	(9)	(0.74)	1.13
Gas Pipelines	BBB+	205	7.7	163	(2)	(14)	(0.64)	1.77
Rating Bucket								
AAA Bucket		110	7.7	65	(1)	(1)	(0.56)	0.26
AA Bucket		546	5.9	74	(3)	(9)	(0.46)	0.67
A Bucket		1,742	6.8	98	(3)	(8)	(0.55)	0.73
BBB Bucket		2,270	7.0	151	(3)	(14)	(0.46)	1.33
Term Bucket								
1-4	A	1,460	2.4	78	(3)	(15)	(0.13)	0.62
4-7	A-	1,145	4.7	103	(3)	(12)	(0.39)	0.91
7-10	A-	883	7.1	129	(2)	(8)	(0.56)	1.07
10PLUS	A-	1,180	13.6	170	(3)	(4)	(0.95)	1.42

Exhibit 3 Morningstar, Inc. Corporate Bond Index Spread by Sector

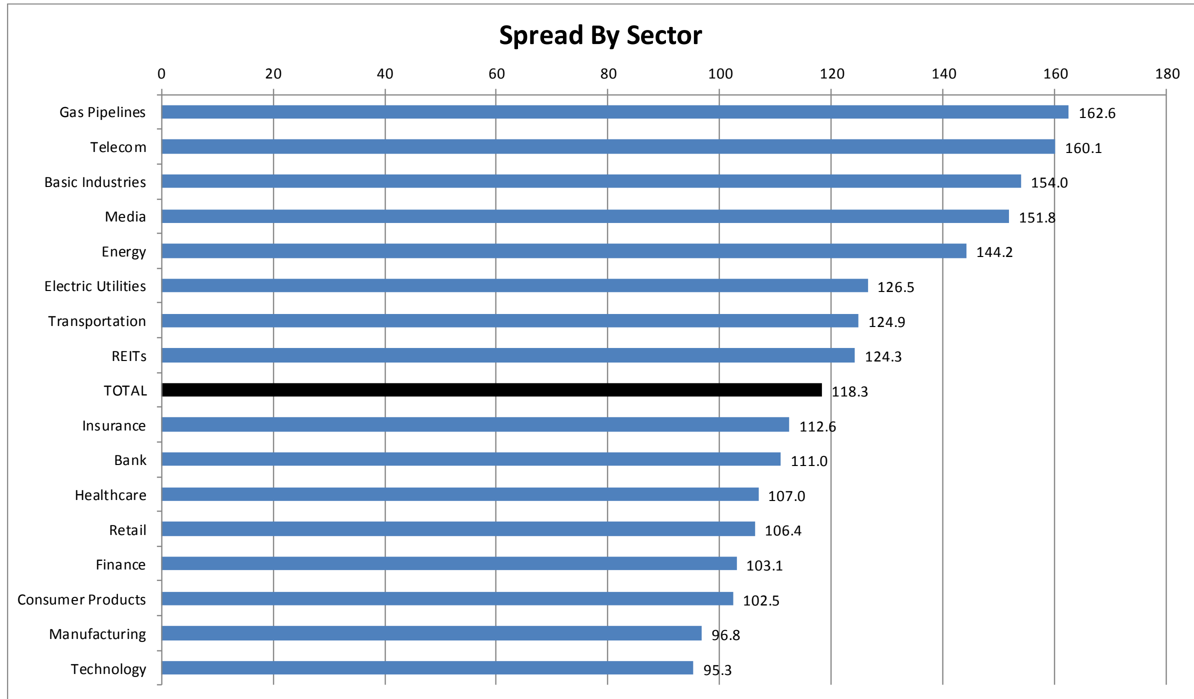


Exhibit 4 Morningstar, Inc. Corporate Bond Index YTD Spread Change

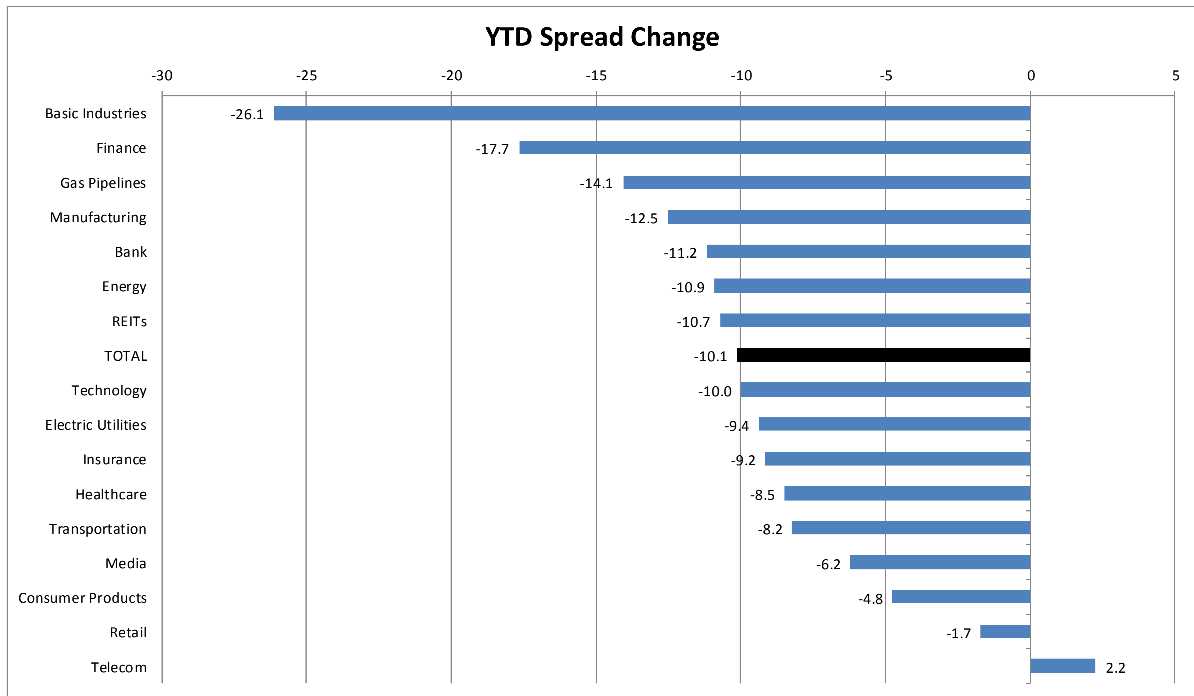
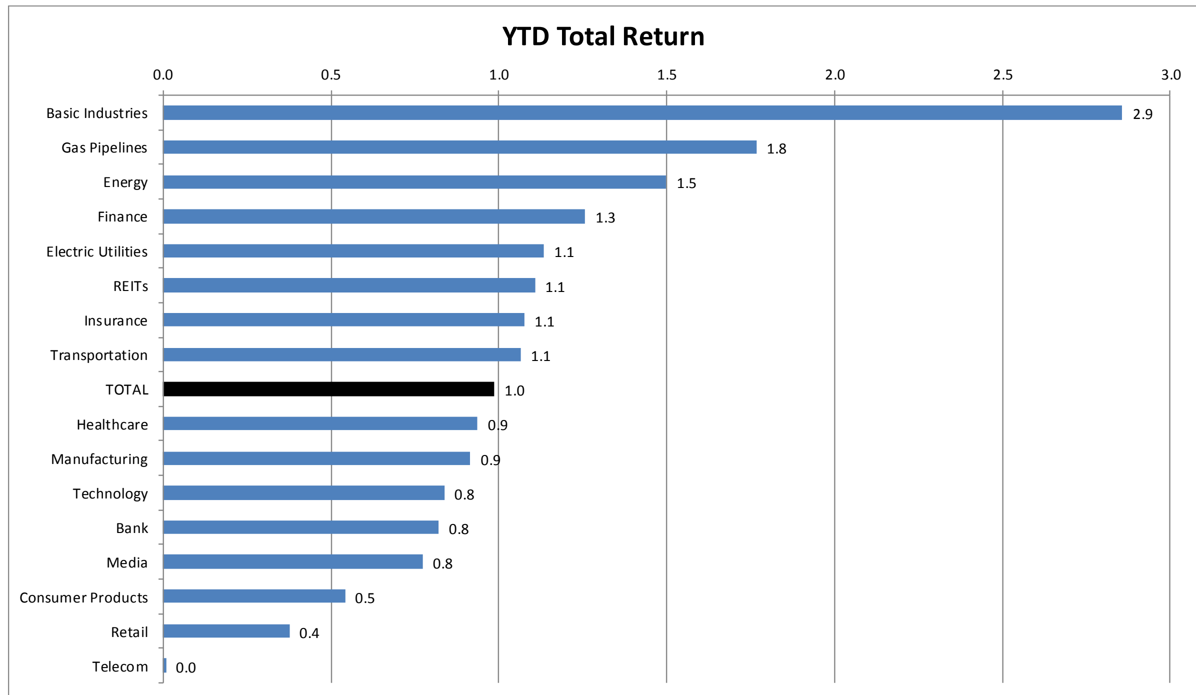


Exhibit 5 Morningstar, Inc. Corporate Bond Index YTD Return



Credit Rating Actions

▶ Rating Changes

Issuer/Ticker	Current Issuer Credit Rating	Previous Issuer Credit Rating
Arconic ARNC	BB+	None
Abbott Laboratories ABT	BBB+	A

▶ Rating Affirmations

Issuer/Ticker	Current Issuer Credit Rating	Previous Issuer Credit Rating
Bed Bath & Beyond BBBY	BBB+	BBB+
Sysco SYY	A-	A-
Kraft Heinz KHC	BBB-	BBB-
Hormel Foods HRL	AA-	AA-
Comerica CMA	A-	A-
Regions Financial RF	BBB	BBB
Royal Dutch Shell RDS.B	A	A
Biogen BIIB	A	A
BP BP	A-	A-
Teva Pharmaceutical Industries TEVA	BBB-	BBB-
Citigroup C	A-	A-
Stryker SYK	A+	A+
Zions ZION	BBB-	BBB-
Goldman Sachs GS	BBB+	BBB+
Morgan Stanley MS	BBB	BBB
Bank of America BAC	BBB	BBB

Bed Bath & Beyond's Rating Affirmed at BBB+; Negative Outlook Assigned

Morningstar Credit Ratings, LLC is affirming Bed Bath & Beyond Inc.'s BBB+ credit rating and assigning a negative outlook. The affirmation is based on Bed Bath & Beyond's position in a competitive, commoditized retail category, coupled with strong free cash flow and a moderately leveraged capital structure. The negative outlook reflects multiyear declines in profitability and weakening credit metrics.

Bed Bath & Beyond's average Business Risk score reflects a solid market position with an estimated 10% share of the $100 billion-plus U.S. retail home furnishing industry, operating over 1,500 stores under five brands plus additional online-only brands, which combined provide some economies of scale. Bed Bath & Beyond operates in a very competitive, commoditized retail category that is increasingly penetrated by online rivals that maintain pricing pressure. The company has focused on offering more differentiated products, services, and solutions to better compete in an increasingly transparent retail price environment. As such, Bed Bath & Beyond offers products and services in bridal registry, baby registry, new mover, back to college, and decorating. In addition, over the past couple of years the company has increased investments to develop its e-commerce platform and to integrate it with its store base and within its broader omnichannel distribution. Despite its large scale, we do not believe Bed Bath & Beyond commands pricing power in the industry, which is reflected in the lack of an economic moat as assigned by Morningstar's Equity Research Group. Although same-store sales and margins have been declining, the firm has continued to increase its store base modestly over the past few years.

Comparable-store sales declines have accelerated through the first three quarters of fiscal 2016, including a 1.4% decline in the third quarter reflecting declining store traffic. For the last 12 months ended with the third quarter of 2016, total revenue of $12.1 billion was essentially flat with full-year 2015, yet adjusted EBITDA declined 11% to $1.57 billion. Adjusted EBITDA margins were 13.0% for this period, about 150 basis points lower than full-year 2015. Margins reflected an increase in coupon expenses, higher direct-to-customer shipping expenses, and payroll. Full-year 2016 results are forecast to show similar comparable store sales and margin declines.

Bed Bath & Beyond's debt leverage has increased substantially following its $1.5 billion debt issuance in fiscal 2014, which was largely used for share repurchases. Adjusted debt totaled $6.0 billion at the end of the third quarter ended Nov. 27 after adjusting for $4.5 billion of operating lease commitments. Total adjusted debt/EBITDAR was 2.8 times, slightly higher than year-end fiscal 2015. Bed Bath & Beyond does not have any debt maturities until 2024, and liquidity includes nearly $600 million in cash and full availability under a $250 million revolver. Share repurchases have slowed over the past few quarters. During the last 12 months, the company repurchased $700 million, down about $400 million from full-year 2015. Bed Bath & Beyond stated its share repurchase program had a remaining balance of approximately $1.9 billion, which is expected to be completed in fiscal 2020.

The negative outlook reflects the potential for Bed Bath & Beyond's rating to be lowered if the multiyear trend of lower profitability and weakening credit metrics fails to stabilize in the near-term. While a higher rating is unlikely given the negative outlook, the outlook could be revised to stable if management's initiatives to increase sales and margins stabilize profitability and credit metrics.

Abbott Laboratories Downgraded to BBB+ From A on Acquisition Activity; Outlook Stable

We are downgrading our credit rating on Abbott Laboratories to BBB+ from A on the firm's leverage-increasing acquisition of St. Jude Medical. While the Alere acquisition is still possible, recent divestiture inflows have helped us gain comfort with our new rating in either a stand-alone (including St. Jude) or acquisition (including Alere and St. Jude) scenario. Therefore, this rating action resolves our review of Abbott's credit rating. Also, our outlook is stable given the lack of catalysts that could positively or negatively affect our credit rating in the next couple of years, barring another unforeseen credit event.

Our BBB+ credit rating for Abbott reflects its recent acquisition of St. Jude, recent divestiture activities, and potential acquisition of Alere. Abbott's credit rating remains supported by its large, diverse operations and advantages in medical products, which contributes to its solid Business Risk pillar. Since spinning off its pharmaceutical division in early 2013, Abbott has focused on nutritional products, medical devices, diagnostics, and established pharmaceuticals. By acquiring St. Jude, Abbott has expanded its medical device segment by adding cardiac, vascular closure, surgery, and neuromodulation products. Prior to the acquisition, Morningstar's Equity Research group gave St. Jude a wide moat assessment, and while Abbott still only earns a narrow moat assessment, it appears situated on the strong end of that moat category after the St. Jude deal.

However, leverage has risen substantially on a pro forma basis because of this acquisition, cutting into Abbott's Cash Flow Cushion and Solvency Score pillars. By our estimates, net leverage stood around 4

times in early January after the St. Jude transaction. Abbott's management team has stated that its primary capital allocation goal is rapid deleveraging. With some debt repayment and growing profits, we estimate net leverage could decline to the low-2s within a few years in a stand-alone scenario. Those deleveraging efforts could stagnate if Abbott is forced to complete the disputed Alere transaction, though. In early 2016, Abbott agreed to acquire Alere, which would require a $6 billion cash outflow and the assumption of Alere's debt. Since then, uncertainty has surrounded the deal due to various problems at Alere, and Abbott is trying to back out of the acquisition. If the Alere acquisition is completed, though, net leverage could remain inflated in the near term.

With its stable outlook, we currently see few fundamental catalysts that could change Abbott's rating within the next couple of years, even the disputed Alere acquisition. However, if Abbott uses recent divestiture proceeds for shareholder returns rather than for deleveraging (in a stand-alone scenario) or acquisition payment (in an Alere acquisition scenario), we may consider a downgrade. Significant deleveraging delays beyond the potential Alere acquisition could also pressure Abbott's rating. Positively, our Business Risk pillar could improve enough to warrant an upgrade if Abbott digs a wide moat while also maintaining its significant size and diversity. Since Morningstar's Equity Research Group has noted Abbott's strength in its current narrow moat category after acquiring (previously wide moat) St. Jude, we would not be surprised to see that assessment improve eventually if the acquisition integration process is successful, which could be an upgrade catalyst.

Sysco's A- Rating Affirmed; Outlook Stable on Improving Credit Measures

Morningstar Credit Ratings, LLC is affirming Sysco Corporation's A- credit rating, assigning a stable outlook, and removing it from under review negative. Our rating on Sysco reflects the successful execution of its strategic plan to increase operating margins and returns on invested capital, which has resulted in improving the company's credit measures. In the absence of debt financed share repurchases, we anticipate further strengthening of Sysco's credit profile.

Sysco's focus on customer case growth, improving profitability margins, leveraging its supply chain costs, and reducing administrative costs have resulted in greater operating earnings. Sysco's positive business performance and the Brakes acquisition have led to the company increasing its adjusted operating income growth target to $600 million to $650 million by the end of fiscal 2018 from $500 million. Leverage (debt/adjusted EBITDA), while expected to improve slightly, was 2.7 times for the latest 12-month period ended Dec. 26, 2016, which we consider slightly weak for the rating category. We continue to believe food-service distribution is a locally competitive market in which Sysco is not always the leader, and as such, we expect Sysco will remain a consolidator in this highly fragmented space (about 70% of the market) by pursuing smaller bolt-on acquisitions.

Sysco's total debt was $8.4 billion at Dec. 31, 2016. Maturities are as follows: $1.1 billion in 2017 composed mainly of commercial paper borrowings, $536 million in 2018, $770 million in 2019, $755 in 2020, $504 million in 2021, and $4.7 billion thereafter. Liquidity is provided by the company's cash balance of $847 million, of which approximately 73% was held by its international subsidiaries and subject to additional taxes, if repatriated. Financial flexibility is afforded by Sysco's $2.0 billion revolving credit facility that supports the company's commercial paper program and expires on Nov. 2, 2021.

Sysco's capital structure, while more leveraged than it has been historically, is manageable. The step-up in leverage is likely to be more than temporary, considering the focus on shareholder returns and the influence of activist investors on the board of directors. The company spent $1.2 billion on share repurchases during the first half of its 2017 fiscal year and has a remaining authorization totaling $689 million under multiple programs. Based upon our intermediate term time horizon, leverage, excluding debt financed acquisitions and share repurchases, is likely to average under 2.5 times.

The forecast range of free cash flow (cash flow from operations less dividends and capital expenditures) has been revised and is substantial at $800 million-$900 million annually during the near-to-intermediate term. As a result, Sysco should not have any issues servicing its debt load or future maturities. However, debt financed acquisitions and share repurchases could weaken the company's credit profile. The current dividend yield is around 3%. We expect dividends to increase in the mid-single-digits annually longer term. We also expect the company's dividend payout ratio to level out at approximately 60% in fiscal years 2017 and 2018.

A positive rating action could occur if Sysco's operating margin and cash flow continue to expand, the company reduces debt levels, or meaningfully extends maturities improving its Cash Flow Cushion and Solvency Score. Conversely, higher debt levels from acquisitions or share repurchases could increase the company's dependency on capital markets and weaken its Business Risk score, pressure its Cash Flow Cushion and Solvency Score, and result in a negative rating action.

Kraft Heinz's Rating Affirmed at BBB- Following Withdrawal of Proposal to Acquire Unilever
Morningstar Credit Ratings, LLC is affirming The Kraft Heinz Company's corporate credit rating of BBB- and assigning a stable outlook following the withdrawal of its proposal to acquire Unilever (rating: A+, stable). Kraft Heinz's current rating is based on our view of the risk profile of the firm as a standalone entity and does not incorporate a substantial acquisition.

Kraft Heinz's credit rating reflects the expectation that the firm's Solvency Score and Cash Flow Cushion will improve based upon our forecasts that management would achieve its $1.7 billion of cost-savings goals and reduce debt. Kraft Heinz refinanced its $8.3 billion 9% Series A cumulative redeemable preferred security, primarily with senior unsecured debt and significantly reduced its financing cost. The company had continued to make deleveraging progress with debt/adjusted EBITDA of 4.2 times for the year ended Dec. 31, 2016, which is still high for the rating category.

The credit rating incorporates 3G owner/operator's exceptional track record of cost reduction through manufacturing efficiency, procurement savings, and decreasing selling, general, and administrative expenses by reducing headcount and implementing zero-based budgeting. We are forecasting very low-single-digit top-line growth and a slight improvement in operating margins. We estimate that free cash flow (cash flow from operations less capital expenditures and dividends) over the next three years will average over $2.0 billion annually in our base case, providing ample flexibility for management to meet its deleveraging target, even after including the revision in integration and restructuring cost to $2.0 billion and capital expenditures to $1.3 billion. However, we expect that near-term cash flow and earnings could be somewhat distorted and negatively affected by restructuring costs. The rating also

considers Kraft Heinz's narrow, but stable economic moat as assigned by Morningstar's Equity Research Group, that is supported by its leading market positions and brand strength and reinforced by the company's increased scale and portfolio breadth. We believe Kraft Heinz's size also provides the company with greater merchandising and promotional bargaining power within the retail channel.

Kraft Heinz's capital structure is manageable. The company's total debt at Dec. 31, 2016, was $32.4 billion, composed of $29.7 billion of long-term debt, $2.1 billion of current maturities, and $645 million of other short-term debt, primarily commercial paper. Excess liquidity is provided by Kraft Heinz's $4.2 billion of cash at Dec. 31, 2016. Approximately $1.3 billion of the company's cash balance was held by international subsidiaries, which could be repatriated to the United States without incurring any additional material tax expense. Financial flexibility is provided by Kraft Heinz's senior credit facilities, composed of $4.0 billion senior unsecured revolving credit facility and a $600 million term loan facility. Subject to certain conditions, the firm may increase the amount of revolving commitments and/or add additional tranches of term loans in a combined aggregate amount of up to $1.0 billion. At Dec. 31, 2016, $600 million aggregate principal amount of the term Loan Facility was outstanding. No amounts were drawn on the company's revolving credit facility at year-end.

Kraft Heinz's major pension plans were substantially funded, and we do not believe that any subsequent funding will affect the company's credit profile. We anticipate that the firm's dividend payout ratio will be at about 50% similar to industry peers and that the moratorium Kraft Heinz placed on share repurchases will be lifted when it reaches its leverage target.

A debt financed acquisition that significantly increases Kraft Heinz's leverage and weakens its Cash Flow Cushion or Solvency Score could result in a ratings downgrade. Failing to achieve debt reduction, altering its commitment to net debt/EBITDA of 3.0 times or below, and a weakening of its Cash Flow Cushion or Solvency Score could also result in a negative rating action. A rating upgrade is possible if Kraft Heinz meets its 2017 debt reduction targets, maintains its leverage commitment of net debt/EBITDA of 3.0 times or below, and improves its Solvency Score or Cash Flow Cushion. Maintaining operating margins, while achieving revenue growth and lower leverage, could also be a positive for the rating.

Hormel Foods' AA- Rating Affirmed; Stable Outlook on Strong Credit Measures

Morningstar Credit Ratings, LLC is affirming Hormel Foods Corporation AA- credit rating and assigning a stable outlook. Hormel's credit rating reflects its low business risk, exceptional Solvency Score and Cash Flow Cushion. The company is successfully positioning itself as a branded food company and its diversified food portfolio and prudent allocation of invested capital has earned it a narrow economic moat as assigned by Morningstar's Equity Research Group. Hormel's portfolio of value-added products allows the company to target consumers who are willing to pay a premium for convenience and healthy foods. As a result, we think Hormel is better than its competitors at absorbing commodity cost pressures. The company's diversification also tends to offset the volatility in any one operating segment.

We believe the firm's most attractive brands reside in niche categories in which Hormel commands sizable shares and faces less private-label competition. Furthermore, several of Hormel's brands (Spam

and Skippy, for instance) have meaningful international presence. Hormel's acquisitions of Applegate Farms, a processor of natural and organic meats, CytoSport, the maker of Muscle Milk and a leader in premium protein products, and Skippy peanut butter have positioned the company to benefit from consumers' increased protein demands and health-oriented dietary trends.

Hormel is financially conservative with a minimal amount of debt within its capital structure. The company's total debt at Jan. 29, 2017, consisted of its 4.125% $250 million bond maturing 2021. Hormel's cash balance was $609.8 million at the period ended. Current leverage (debt/adjusted EBITDA) is below 0.2 times; accordingly, interest coverage will remain very high. Barring any significant animal protein supply/demand imbalances, we are forecasting low- to mid-single-digit revenue growth and that operating margins will remain stable. We anticipate that the company will utilize purchase contracts and futures contracts to manage commodity cost volatility.

Free cash flow generation (cash flow from operations less capital expenditures and dividends) is projected to be in excess of $400 million annually, throughout the forecast period and has averaged $474 million annually since 2014. Adjusted EBITDA/interest is forecast to exceed 100 times. Hormel continues to grow dividends in the mid-teens (17% for fiscal 2017), and although its dividends are growing faster than earnings, its payout ratio was about 33%, below its peers, and as a result will probably continue to grow at a high rate. We believe that given the Hormel Foundation's 48.5% ownership of the company, the board of directors will favor dividends over share repurchases, and that the foundation ownership also reduces the event risk of Hormel receiving an unsolicited bid. We expect Hormel will use its cash flow to support its dividend and the excess to fund brand acquisitions.

Hormel's continued development and growth of value-added brands, increasing profitability, and diversification while maintaining an exceptional Cash Flow Cushion and Solvency Score would be positive for the rating. Conversely, higher leverage, lower profitability that weakens the company Cash Flow Cushion or Solvency Score would be negative for the rating.

Comerica's Rating Affirmed at A-; Outlook Raised to Stable on Improved Profits and Solid Capital
Morningstar Credit Ratings, LLC is affirming its A- credit rating on Comerica Inc and raising its outlook on the company to stable from negative. The company's credit rating benefits from a solid Business Risk and Stress Test assessment, as well as a Solvency Score that is comparable to regional banking peers. We are revising our outlook to stable from negative to reflect a more constructive outlook on the company's energy loan portfolio and stable or improved credit metrics --including higher capital levels-- compared with a year-ago.

Comerica's good Business Risk score benefits from the company's reasonably diverse operations and good funding mix. Revenue is split between net interest income, which represents about 63% of 2016 revenue, and fee-based sources, including credit card and fiduciary income that contribute the remainder. Comerica is primarily a commercial lender. By segment, the company generated about 89% of annual income from business banking operations and around 10% from wealth management activities. Retail banking operations produced minimal income during the year, down from around 5% of income a year earlier. During recent years, Comerica has expanded its operations outside its original home of

Michigan and relocated its headquarters to Dallas. During the most recent year, operations in California generated approximately 37% of core earnings, while Michigan accounted for 34%. Other markets, including Florida and Arizona, accounted for 31% while operations in Texas generated a small loss for the year. Comerica benefits from a decent funding mix with deposits representing about 90% of liabilities at year-end and long-term debt representing about 8%. The company had minimal short-term funding outstanding at year-end, which contributes favorably to the Business Risk score. Further, Morningstar's Equity Research Group assigns Comerica a narrow economic moat because of high customer switching costs associated with deep customer relationships the bank has developed across products and geographies, a factor that positively influences the company's Business Risk assessment.

Comerica generates an average Solvency Score. Positive attributes of our assessment include above-average levels of capital that have improved from our prior review. By our calculations, tangible common equity represented 9.9% of tangible assets, which compares favorably with a peer average around 8%. Similarly, Comerica's common equity Tier 1 capital ratio of 11.1% compares favorably with a peer average around 10.5%. Earnings power, as measured by pre-provision profit per average assets, is roughly average relative to a broad set of U.S. banks. By our calculations, return on average common equity during the second half of the year was 8.0%, representing a level comparable with peers and a significant improvement from 2.1% reported in the first half of the year and 6.9% reported in the prior year. Comerica's level of reserves for delinquent and non-performing assets ranks above average relative to a broad set of banks and contributes positively to our Solvency Score assessment. However, Comerica's assets quality measures have deteriorated modestly from a year earlier to levels that we consider modestly below average. Non-performing loans represent 1.19% of total loans compared with 0.77% a year ago. Current levels are modestly above a peer average for regional banks around 0.75%.

Comerica generates a good score on our Stress Test, which compares favorably with most regional banking peers. The company benefits from a reasonably diverse loan portfolio that is split between commercial and industrial loans, 63.1%, commercial real estate, 24.0%, and consumer loans, 9.1% of loans at year-end. Energy loans and related exposures represented 5.4% of loans as of December 2016, down from 7.5% a year earlier. Other than its energy loans, we consider most of Comerica's loan portfolio to be of average credit risk. Results on the Stress Test reflects Comerica's above average initial capital position and our expectations for decent pre-provision profits over our forecast horizon. Taken together, forecast capital levels are maintained at acceptable levels under our stress-case assumptions.

Our stable outlook on Comerica Inc implies that we are unlikely to change our rating within the next year. Our rating assumes that the company returns profit measures to levels observed during recent periods associated with more favorable energy lending conditions. Specifically, we expect return on average assets around 0.85% and return on common equity around 8.0% during our forecast horizon. Our rating also assumes that the company maintains capital levels near current levels. If profits were to fall below expectations, we could consider a negative outlook or a lower rating. In addition, lower levels of tangible capital relative to tangible assets could also lead to a lower Solvency Score and a lower rating. Higher levels of short-term wholesale funding could contribute to a lower Business Risk score. A riskier loan portfolio or lower underwriting standards could contribute to a lower Stress Test score and a lower credit rating. Conversely, higher levels of deposits relative to total liabilities or higher levels of pre-

provision profits relative to average assets could contribute to a higher Solvency Score and a higher Business Risk score. Higher capital levels relative to tangible assets could also lead to a higher Solvency Score and a higher credit rating.

Regions' Rating Affirmed at BBB; Outlook Raised to Stable on Credit Metrics and Improved Profits
Morningstar Credit Ratings, LLC is affirming its BBB rating on Regions Financial Corporation and raising its outlook on the company to stable from negative. The company's credit rating benefits from a solid Business Risk score as well as Solvency and Stress Test scores that are comparable to regional banking peers. We are revising our outlook to stable from negative to reflect a more constructive outlook on the company's energy loan portfolio and stable or improved credit metrics--including higher regulatory capital levels--compared with a year ago.

Regions' good Business Risk score benefits from the company's reasonably diverse operations and good funding mix. Revenue is split between net interest income, which represents about 61% of 2016 revenue, and fee-based sources that contribute the remainder. By segment, the company generated about 44% of income (trailing 12 months as of September) in business and corporate banking operations, 45% from consumer banking, and around 6% from wealth management activities. Other activities contributed the remaining 5% of net income during the period. Regions benefits from a decent funding mix with deposits representing about 91% of liabilities at year-end and long-term debt representing about 7%. The company had no short-term funding outstanding at year-end, which contributes favorably to the Business Risk score. However, Morningstar's Equity Research Group does not believe that Regions possesses an economic moat because of higher operating costs and lack of a funding cost advantage, which negatively influences the company's Business Risk score.

Regions generates an average Solvency Score. Positive attributes of our assessment include pre-provision profit levels that are modestly above average relative to a broad set of U.S. banks. Return on average assets for 2016, a related measure, was 0.87%, which compares favorably with a peer average around 0.85%. As we calculate it, return on average common equity was 6.9% during the period, representing an improvement from 6.2% reported a year ago. We note modest improvement in revenue during the year, success controlling operating costs, and an improvement in the company's efficiency ratio to 64.2% from 66.2% a year earlier. Our Solvency Score assessment also benefits from above-average levels of capital that have improved from our prior review. By our calculations, tangible common equity represented 8.9% of tangible assets, which compares favorably with a peer average around 8%. Similarly, Regions' common equity Tier 1 capital ratio of 11.2% compares favorably with a peer average around 10.5%. However, Regions' assets quality and loan-loss reserve levels have deteriorated modestly from a year-earlier to levels that we consider below average. Non-performing loans represent 1.24% of total loans, while reserves represent around 110% of nonperforming loans. Both measures trail peer averages around 0.75% and 150%, respectively.

Regions generates a good score on our Stress Test that is generally consistent with regional banking peers. The company benefits from a diverse loan portfolio that is split between commercial and industrial loans, 52.7%, commercial real estate, 8.1%, and consumer loans, 39.2%. While we consider most of Regions' commercial and industrial loan portfolio to be above-average credit risk, we consider its

consumer loans to represent average credit risk. Results on the Stress Test reflects Regions' above average initial capital position and our expectations for decent pre-provision profits over our forecast horizon. Taken together, forecast capital levels are maintained at acceptable levels under our stress-case assumptions.

Our stable outlook on Regions Financial implies that we are unlikely to change our rating within the next year. Our rating assumes that the company maintains profitability measures during our forecast horizon near levels observed during recent years, including a return on average assets around 0.85% and return on common equity around 7.5%. Our rating also assumes that the company maintains capital levels near current levels. If our expectations for profits were to fall below those expected for peers, we could consider a negative outlook or a lower rating. In addition, lower levels of tangible capital relative to tangible assets could also lead to a lower Solvency Score and a lower rating. Higher levels of short-term wholesale funding could contribute to a lower Business Risk score. A riskier loan portfolio or lower underwriting standards could contribute to a lower Stress Test score and a lower credit rating. Conversely, higher levels of deposits relative to total liabilities or higher levels of pre-provision profits relative to average assets could contribute to a higher Solvency Score and a higher Business Risk score. Higher capital levels relative to tangible assets could also lead to a higher Solvency Score and a higher credit rating.

Royal Dutch Shell's Rating Affirmed at A and Stable Outlook Established

Morningstar Credit Ratings, LLC is affirming its A corporate credit rating on Royal Dutch Shell and establishing a stable outlook, based on our renewed oil and gas and refined product price forecasts.

Our rating reflects estimated companywide, organic production growth of oil and gas, refined and chemical products each at a low- to mid-single-digit percentage rate per year for the next few years. Our forecast accounts for the ramp up of Shell-operated projects, including the Stones project (Gulf of Mexico, Shell 100% interest) and downstream petrochemical expansions in North America and Europe. Further, we incorporate participation in the ramp-up of Australian LNG, many deep-water oil and gas developments offshore Brazil, developments in the Niger Delta, and developments offshore Brunei and Malaysia. Our rating also reflects the inherent cyclicality for both exploration and production (upstream) and refining (downstream) activities, often counterbalancing each other, and the view of Morningstar's Equity Research Group that Shell does not benefit from an economic moat. The rating outlook incorporates our expectation that operating margins will gradually increase in light of cyclically rebounding oil and natural gas price realizations and refined product pricing over the next several quarters.

When the sharp decline in oil and gas prices began in fall 2014, Shell focused on cost savings, deferring certain long-term upstream projects and monetizing noncore assets. Cost-reduction measures include ongoing field and capital efficiency gains and capture of deflation in exploration and production supply-chain inputs, resulting in a steadily declining cash operating cost per barrel of oil equivalent. Shell's scale, diversified cash flow and financial strength allowed the company to continue to invest through the bottom of the price cycle, in particular, the purchase of BG Group in early 2016.

Shell ended the year 2016 with $19.1 billion in cash and equivalents. Including full availability on a $7.5 billion credit facility, the company's liquidity remains excellent. Shell has guided for capital and exploratory expenditures to be $21 billion in 2017, which is about 5% below the prior year. After adjusting for capital expenditures, dividends, acquisitions and divestments, we estimate positive free cash flow for Shell in 2017 (equivalent to 20% of year-end 2016 total debt) and following years, resulting in an average Cash Flow Cushion score. However, an increasing return on invested capital drives a continuously-improving Solvency Score through our forecast period.

In our base-case forecast, we estimate the company's EBITDAX margin gradually rising to 16% by 2020, after bottoming at about 12% in 2016. Commensurate with this, we estimate the ratio of total debt/trailing EBITDAX to have peaked at about 3 times in 2016, then declining back to around 1.5 times by 2019. Our base operating forecast incorporates an average 2017 price assumption of $3.50 per million British thermal units for U.S. natural gas and $55/barrel for WTI oil. Our forecast incorporates natural gas pricing 6%-10% above the futures price curve (as of Feb. 27) through 2020. For oil (WTI basis), our yearly forecast is 8%-12% above the futures price curve through 2020, at the top end of our range for the last two years of our forecast. Furthermore, we assume non-core asset sales of $12.5 billion in both 2017 and 2018, in line with company projections. Thereafter, we estimate asset sales of $1 billion per year, which is conservative, in our view. The company realized $4.7 billion in proceeds from divestments in 2016 and $5.5 billion in 2015.

Our rating outlook is stable and assumes that the company can incrementally reduce leverage from higher price realizations that should come about from the gradual improvement in oil and gas supply/demand fundamentals. However, if spot pricing continues to languish, further squeezing margins, we may consider a downgrade of the credit rating. Alternatively, if oil and gas supply/demand fundamentals and the pricing outlook improve more quickly than our current expectation, we would consider raising the credit rating.

Biogen's Rating Affirmed at A; Stable Outlook Assigned

Morningstar Credit Ratings, LLC is affirming Biogen Inc.'s A credit rating to reflect its leading position in multiple sclerosis treatment along with its historically cash-rich balance sheet. We are also assigning a stable outlook based on our estimation that new medicines may offset headwinds on the firm's MS portfolio and result in solid operational performance that keeps debt leverage steady over the next few years.

Biogen maintains leadership in MS with Avonex, Fampyra, Plegridy, Tecfidera, Tysabri, and Zinbryta, that collectively generated 77% of total revenue in 2016. This contribution rises to almost 81% of the total if we exclude contributions from Bioverativ, which was spun off in February 2017. Tecfidera alone accounts for 36% of all sales after removing the contribution from hemophilia products. While still growing in the low single digits, heavy reliance on these medicines increases vulnerability to new MS competition and weighs on our Business Risk pillar. Some relief stems from the European launch of Benepali, a biosimilar of Pfizer's Enbrel, as well as the recent introduction of the novel drug Spinraza to the U.S. market for the rare condition of spinal muscular atrophy. However, a significant reduction in revenue concentration may require commercialization of high-risk neurology developmental projects,

notably the firm's leading Alzheimer's candidate, aducanumab. Risk-adjusting for this program, we estimate sales and EBITDA growth in the midsingle digits through 2020 compounded annually. Biogen is moving forward with its opicinumab project despite unfavorable phase 2 data from the anti-Lingo program in multiple sclerosis, and if canceled, our estimated long-term growth may be affected. Hiring a long-time industry veteran as the new CEO has eased some event risk. However, in our view, the near-term risk of significant acquisitions remains elevated, especially if key research assets falter in clinical investigation.

Our rating also considers Biogen's solid balance sheet, with cash and investments of $7.7 billion exceeding debt of $6.5 billion at the end of 2016, which supports our Cash Flow Cushion and Solvency Score pillars. After jumping by more than one turn due to incremental debt to repurchase $5 billion in shares in 2015, gross leverage ended 2016 at 1.0 times EBITDA, remaining relatively consistent with 1.2 times at the end of 2015. Supported by our forecast for solid operational performance, we estimate that Biogen will produce free cash flow averaging around $4 billion annually through 2020 that we believe will be more than sufficient to manage modest long-term debt maturities of $550 million in 2018 and $1.5 billion in 2020. With internal investment into its research program expected to be about $2 billion per year (about 17% of sales), we anticipate more capital may be directed to share repurchases and to filling product and research portfolio gaps in 2017. We could also see a step-up of business development in the near term given the current makeup of the firm's late-stage pipeline, which consists of high-risk neurology projects, most notably Alzheimer's disease treatments that traditionally carry low probabilities of regulatory approval. If internal product candidates do not succeed in clinical trials or in the marketplace, we would not be surprised to see Biogen get more aggressive with its balance sheet to repurchase shares to placate investors. At the end of 2016, around $4 billion of authorization remained under Biogen's $5 billion share repurchase program, which it established in July 2016.

We see Biogen continuing to operate at the strong end of the rating category because of its solid balance sheet and attractive earnings growth prospects. If the company eases sales reliance on its multiple sclerosis portfolio to yield an improved Business Risk pillar while maintaining solid cash generating capability to hold already good Cash Flow Cushion and Solvency Score pillars, we believe positive rating action could follow. Conversely, we believe that aggressive competition in the MS treatment area coupled with late-stage research failures that lowers operating performance far below our expectation such that net leverage rises and remains near 2 times and pressures our Cash Flow Cushion and Solvency Score may result in a downgrade.

BP's Rating Affirmed at A- and Stable Outlook Established

Morningstar Credit Ratings, LLC is affirming its A- corporate credit rating on BP and establishing a stable outlook based on our renewed oil and gas and refined product price forecasts.

Our rating reflects estimated companywide, organic production growth of oil and gas at a mid-single-digit percentage rate and for refined and petrochemical products at a low-single-digit rate per year for the next few years. Our forecast accounts for the ramp-up of BP-operated projects, including Thunder Horse South Expansion (Gulf of Mexico, BP 75.0% interest), and participation in the In Salah Gas Southern Fields project (Algeria, BP 33.15% interest). Further, we incorporate BP's renewed ADCO

onshore oil concession (Emirate of Abu Dhabi, BP 10.0% interest) and the recent dissolution of the German refining joint operation with Rosneft. Our rating also reflects the inherent cyclicality for both exploration and production (upstream) and refining (downstream) activities, often counterbalancing each other, and the view of Morningstar's Equity Research Group that BP does not benefit from an economic moat. The rating outlook incorporates our expectation that operating margins will gradually increase in light of cyclically rebounding oil and natural gas price realizations and refined product pricing over the next several quarters. This should bring credit metrics more in line with the rating category.

Long before oil and gas prices began to sharply decline in the fall of 2014, BP had been aggressively monetizing non-core assets to pay for the settlement stemming from the 2010 Gulf of Mexico oil spill. When pricing tanked, BP renewed its focus on cost savings, deferring certain long-term upstream projects and continuing with its broad asset-monetization program. Cost-reduction measures include ongoing field and capital efficiency gains and capture of deflation in exploration and production supply-chain inputs, resulting in a steadily declining cash operating cost per barrel of oil equivalent. BP's scale, diversified cash flow and financial strength allowed the company to continue to invest through the bottom of the price cycle while making significant progress in resolving oil spill-related liability claims.

BP ended 2016 with $23.5 billion in cash and equivalents. Including full availability on $7.4 billion aggregate committed bank facilities, the company's liquidity remains excellent. BP has guided for organic capital expenditures of $15 billion to $17 billion in 2017, which is about 3% higher than the prior year. The company also estimates 2017 cash payments related to GOM oil spill-related liabilities of $4.5 billion to $5.5 billion, less than $7.1 billion paid in 2016, further declining to around $2 billion in 2018 and $1 billion per year thereafter. After adjusting for capital expenditures, dividends, acquisitions and divestments, we estimate positive free cash flow for BP in 2017 (equivalent to 14% of year-end 2016 total debt) and following years, resulting in an average Cash Flow Cushion score. However, an increasing return on invested capital drives a continuously-improving Solvency Score through our forecast period.

In our base-case forecast, we estimate the company's EBITDAX margin gradually rising to 15% by 2020, after bottoming at about 5% in 2015. Commensurate with this, we estimate the ratio of total debt/trailing EBITDAX to have peaked near 5 times in 2016, declining back to around 1.5 times by 2018. Our base operating forecast incorporates an average 2017 price assumption of $3.50 per million British thermal units for U.S. natural gas and $55/barrel for West Texas Intermediate oil. Our forecast incorporates natural gas pricing 6%-10% above the futures price curve (as of Feb. 27) through 2020. For oil (WTI basis), our yearly forecast is 8%-12% above the futures price curve through 2020, at the top end of our range for the last two years of our forecast. Furthermore, we assume noncore asset sales of $5.0 billion in 2017 (midpoint of company guidance) and $2.5 billion per year in 2018 and thereafter, which is conservative, in our view. The company realized $3.2 billion in proceeds from asset divestitures in 2016 and $2.8 billion in 2015.

Our rating outlook is stable and assumes that the company can incrementally reduce leverage from higher price realizations that should come about from the gradual improvement in oil and gas supply/demand fundamentals. However, if spot pricing continues to languish, further squeezing margins,

we may consider a downgrade of the credit rating. Alternatively, if oil and gas supply/demand fundamentals and the pricing outlook improve more quickly than our current expectation, we would consider raising the credit rating.

Teva's Rating Affirmed at BBB-; Stable Outlook Assigned

Morningstar Credit Ratings, LLC is affirming Teva Pharmaceutical Industries Ltd.'s BBB- credit rating to reflect its dominance in the global generic pharmaceutical industry balanced against its stretched balance sheet following its acquisition of Actavis (Allergan's generic drug business). We are also assigning a stable outlook based upon our expectation that the firm will make significant progress toward improving gross leverage.

Management has set an aggressive leverage reduction target, which should improve Teva's Solvency Score and provide longer-term support to the credit rating. However, we remain skeptical that Teva can actually achieve its aggressive leverage reduction goals as quickly as it has targeted. Meanwhile, our Business Risk pillar remains Teva's strongest given its scale, geographic reach, and breadth of product offering that were all enhanced with the Actavis purchase. Key wildcards in the near-term include a search for a new CEO after an abrupt departure in late 2016 and emerging U.S. generic competition to Teva's best-selling medicine Copaxone (40 mg dosage) that represents the vast majority of prescriptions for the multiple sclerosis franchise.

Incorporating generic introductions in 2017 to the MS drug that accounted for around 19% of total sales in 2016, we still anticipate revenue and EBITDA growth in the mid-single digits compounded annually through 2020, assuming the firm reaches the $1.4 billion of cost synergies by 2019 expected from the integration of Actavis. We see recovery of top-line growth in 2019 helped by potential new brand name medicines, including the specialty drug candidate SD-809 for Huntington disease and tardive dyskinesia, and new generic entrants given a broadened pipeline with more than 300 generic drug filings under review at the FDA including over 100 first-to-file applications that offer higher profitability given a 180-day market exclusivity period.

Total debt spiked to nearly $37 billion in the third quarter of 2016 from about $10 billion in 2015 after Teva issued $20 billion of new debt in July to fund its acquisition of Actavis completed in August 2016. Total debt eased to $35.8 billion by the end of 2016, but gross leverage remained elevated at 5.2 times on a pro forma basis, in our estimation, compared with 1.6 times at the end of 2015. Meanwhile, pro forma net debt stood at 5.1 times EBITDA, including Teva's modest year-end 2016 cash and investments balance of $988 million. Operational pressure stemming from generic competition to Copaxone (40 mg) dampens free cash flow generation that we see averaging $4 billion through 2020. Given Teva's commitment to its dividend, which represents $1.4 billion of cash outflow per year, we believe the firm is hard-pressed to repay long-term debt maturities comprising $810 million in 2017, $5.3 billion in 2018, $3.9 billion in 2019, $4.0 billion in 2020, and $4.2 billion in 2021. We also believe it will be difficult for Teva to achieve its aggressive leverage reduction goals. In July 2016, management laid out guidance for net leverage to fall to 2.1 times by the end of 2018. Later in the year, the firm also stated a target for gross leverage of 3.5 times by 18 months after the close of the Actavis transaction. In our opinion, these targets look optimistic, particularly given actual EBITDA is trending far below Teva's original

expectations and the potential for lower-than-anticipated cash flow generation in light of looming Copaxone (40 mg) generic competition. Nonetheless, we estimate the firm may achieve the gross leverage goal a few years later than planned through a combination of debt reduction and increased profitability, which supports the current BBB- rating. We recognize that management values its investment-grade rating and has taken steps to preserve cash flow for debt reduction, including stopping share repurchasing and curtailing larger M&A activities.

We see Teva operating at the low end of the BBB- category due to its inflated debt leverage following the acquisition of Actavis. If the firm missteps in the integration of Actavis that jeopardizes achievement of cost synergies or that causes significant disruption of its generics business such that EBITDA generation is hindered and keeps gross debt leverage and net debt leverage above 4.5 times and 4.0 times, respectively, then downgrade of the present rating may follow. In addition, greater-than-expected generic competition to Copaxone (40 mg) that dampens cash flows and minimizes debt reduction may also limit leverage improvement and pressure the current rating. On the other hand, if Copaxone generic introductions are delayed significantly or Actavis synergies are greater than expected, such that the company drives a high level of profitability that allows the firm to reach its leverage target within its original time frame, then upward movement to the rating could ensue.

Citigroup's A- Rating Affirmed on Solid Capital Levels and Stable Asset Quality; Outlook Stable
Morningstar Credit Ratings, LLC is affirming its A- credit rating and stable outlook on Citigroup Inc. The company's credit rating benefits from solid capital levels, which support the company's favorable Solvency Score and Stress Test assessment. Citigroup's vast size and diverse operations support the company's Business Risk score.

Citigroup's good Business Risk score benefits from the company's global reach and diverse operations, the positive effects of which are partly offset by a significant need for wholesale funding. With over $1.7 trillion of assets at year-end spread across 97 countries, Citi is the most global of the large U.S. banks. It organizes its operations into a global consumer bank, which generated about 45.5% of 2016 net revenue, and an institutional client group, which was responsible for 48.4% of net revenue. Most of the remaining revenue was generated in Citi Holdings, the noncore segment that holds the company' remaining runoff assets. The global consumer bank includes retail banking, credit card operations, and commercial banking operations across 19 countries. The institutional clients group includes transaction services, a scaled-back investment bank, private banking, and commercial lending activities. Overall, about 37.1% of 2016 earnings came from the faster-growing economies of Latin America and Asia, which we consider positive longer term, but which may cause volatility over the near term. Citigroup has made considerable progress reducing Citi Holdings to about 3% of total assets as of December 2016, 33.3% lower than a year ago, which has contributed to lower credit costs for the group. Further, Morningstar's Equity Research Group assigns Citigroup a narrow economic moat rating because of cost advantages in its core banking operations and intangible assets in its investment banking operations, a factor that positively influences the company's Business Risk assessment. However, Citigroup's deposits represent only 59.4% of total liabilities, implying a significant need for wholesale funding sources, which negatively affects our Business Risk score.

Citigroup generates an average Solvency Score. Positive attributes of our assessment include solid levels of tangible common equity relative to tangible assets and tangible capital as a buffer for impaired loans. By our calculations, tangible common equity represented 10.1% of tangible assets at year-end, which compares favorably to a peer average of around 8%. Similarly, Citigroup's common equity Tier 1 capital ratio of 14.3% under transitional Basel III measures compares favorably to a peer average around 11.5%. Citigroup also ranks above average with respect to earnings power. Relative to a broad set of U.S. banks, Citigroup's pre-provision profit-to-average assets ranks in the 64th percentile. By our calculations, return on average assets for 2016, a related measure, was 0.79%, which trails a peer average around 0.85%. We believe that Citigroup's relatively high loan-loss charge-off ratio of 1.06% of gross loans for the year contributed to weaker performance of this measure. Similarly, Citigroup's return on average common equity was 6.7% as we calculate it which also trails an average of 8.6% for a broad set of U.S. banks. We consider Citigroup's asset quality and reserves for loan losses to be roughly average. At year-end, nonperforming loans represented 0.89% of loans, while loan-loss reserves represented about 216% of nonperforming loans. However, Citigroup's relatively low level of deposit funding detracts from the company's Solvency Score. Deposits represented about 59% of liabilities at year-end, which ranks in the bottom-decile relative to a broad set of U.S. banks and detracts from the Solvency Score.

Citigroup generates a strong score on our Stress Test, which compares favorably with banking peers. The company benefits from a diverse loan portfolio, which is relatively evenly split between consumer loans, which represented 51.5% of loans as of September 2016, and commercial loans, which represented 48.5%. We consider most of Citigroup's loans to represent average credit risk. Results on the Stress Test reflects Citigroup's above-average initial capital position and solid levels of loan-loss reserves and our expectations for decent pre-provision profits over our forecast horizon. Taken together, forecast capital levels are maintained at above-average levels under our stress-case assumptions.

Our stable outlook on Citigroup Inc. implies that we are unlikely to change our rating within the next year. Our rating assumes that the company maintains profitability measures during our forecast horizon near levels observed during recent years, including a return on average assets around 0.85% and return on common equity around 7.5%. Our rating also assumes that the company maintains capital levels near current levels and above those of more domestically-focused peers. If profits were to fall below our expectations, we could consider a negative outlook or a lower rating. In addition, lower levels of tangible capital relative to tangible assets or lower levels of reserves relative to non-performing assets could also lead to a lower Solvency Score and a lower rating. A riskier loan portfolio or lower underwriting standards could contribute to a lower Stress Test score and a lower credit rating. Conversely, higher levels of deposits relative to total liabilities or higher levels of pre-provision profits relative to average assets could contribute to a higher Solvency Score and a higher Business Risk score. Higher capital levels relative to tangible assets could also lead to a higher Solvency Score and a higher credit rating.

Stryker's Credit Rating Affirmed at A+; Outlook Increased to Stable

Morningstar Credit Ratings, LLC is affirming its A+ credit rating on Stryker Corp and increasing the outlook to stable from negative. After some deleveraging following the Sage Products and Physio-Control acquisitions in early 2016, Stryker's position in the A+ rating category has strengthened. With a

solid near-term outlook, we see less risk of the firm tripping into a lower rating bracket absent a major credit event like a debt-funded acquisition, which informs our stable outlook.

Our A+ credit rating for Stryker reflects the firm's significant advantages in the medical device industry and elevated leverage relative to historical norms. Stryker scores well on its Business Risk pillar, reflecting its substantial size, decent diversity, and competitive advantages in the medical device industry. Stryker earns a wide moat from Morningstar's Equity Research Group with operations in three segments: orthopedics, medical equipment, and neurotechnology and spine devices. We particularly like Stryker's position as a top-tier provider of orthopedic devices. That business has high barriers to entry, and Stryker should be a key beneficiary of growth in surgical procedures to repair joints through that division and its surgical equipment business. In general, we believe demographic trends in developed countries should drive solid volume growth in Stryker's chosen niches, as populations age and increasingly suffer from the health problems its devices treat. Because of these trends, we estimate solid future cash flows as the firm expands in the U.S. and international markets.

Stryker only scores moderately on our Cash Flow Cushion pillar, though, given its moderate cash position relative to pending debt maturities and expected returns to shareholders through its growing dividend and share-repurchase programs. Also on a pro forma basis including the early 2017 new debt issuance, Stryker's leverage remains elevated with gross debt/EBITDA in the mid-2s and net debt/EBITDA in the low 1s by our estimates. Historically, Stryker operated with a net cash or net neutral debt position, so financial leverage is higher than the past. However, relative to our coverage universe, leverage still remains quite light, and Stryker scores best on its leverage-sensitive pillars, the Solvency Score and Distance to Default.

With a stable outlook, we currently see few fundamental catalysts that could change Stryker's rating within the next couple of years. But we could downgrade our rating if Stryker pursues a significant acquisition that increases leverage, which could pressure its Solvency Score and Distance to Default pillars. Also, Stryker's medical equipment business is sensitive to hospital capital spending cycles. If Affordable Care Act repeal/replacement efforts result in insured patient volume falling enough to cut into hospital capital spending in the United States, weaker-than-expected financial results could cut into its Cash Flow Cushion or Solvency Score. More positively, new product launches, such as the Mako robotic system for orthopedic implants in 2017, could boost the firm's cash flow, which could positively affect its currently mediocre Cash Flow Cushion. Assuming the firm doesn't just push that potential excess cash flow to shareholders, a credit rating upgrade could be warranted.

Zions' BBB- Rating Affirmed; Outlook Raised to Positive on Favorable Risk Assessment
Morningstar Credit Ratings, LLC is affirming its BBB- credit rating on Zions Bancorporation and changing its outlook on the company to positive from stable. Our more favorable view of the company includes a more constructive outlook on the company's energy loan portfolio, a lower-risk investment portfolio than previously, and increased profitability since our previous review.

Zions' fair Business Risk score benefits from the company's good funding mix, the positive effects of which are partially offset by its smaller size, as well as concentrations in certain geographic areas and

loan products including commercial real estate and energy loans. By our calculations, most of Zions' funding comes from sources that we consider stable. Deposits represented about 96% of liabilities as of December 2016, long-term debt represented 1%, while short-term funding sources represented just 1.5% and a positive factor in our rating assessment. However, Morningstar's Equity Research Group does not believe that Zions possesses an economic moat because of higher operating costs and profits that have trailed its estimated weighted average cost of capital, a factor that negatively influences the company's Business Risk score. Zions is primarily a commercial lender. At year-end, approximately 51% of loans outstanding were considered commercial and industrial, 26.6% commercial real estate, and 10% consumer loans. The company generated around 78% of revenue from net interest income, which limits its Business risk score.

Zions generates a fair Solvency Score. Positive attributes of our assessment include high levels of deposit funding as well as above-average levels of tangible common equity relative to tangible assets when compared to a large set of U.S. By our calculations, tangible common equity represented 9.5% of tangible assets, which compares favorably to a peer average around 8%. Similarly, Zions' common equity Tier 1 capital ratio of 12.1% compares favorably to a peer average around 10.5%. The positive effects of these measures are partially offset by below-average levels of reserves for nonperforming loans and higher balances of nonperforming assets. At year-end, nonperforming assets represented 1.34% of loans and real estate owned up from 0.88% a year ago. At the same time, loan-loss reserves represented about 100% of nonperforming loans, down from around 173% a year ago. Both measures trail peer averages around 0.75% and 150%, respectively. However, excluding energy loans, asset quality compares favorably to peers, with nonperforming assets representing 0.69% of loans at year-end. Since our prior review, we note that earnings power, as measured by pre-provision profit per average assets, has improved significantly to levels we would consider average from levels in the bottom third of our bank peer group. We attribute the improvement to a more favorable asset mix of government agency securities relative to higher cash balances, which contributed to higher net interest income during the year. In addition, Zions sold its holdings of lower-rated CDO securities during 2015, balances that had suppressed non-interest income with realized losses on security sales since 2007. Without these holdings, non-interest income increased 38.7% in 2016 from the prior year.

Zions generates a good score on our Stress Test which is compares favorably with many regional banking peers. We consider most of the company's commercial and industrial loan portfolio, which represents about 58% of total loans, to be above-average credit risk. This portfolio includes $2.2 billion of loans to the energy sector. While this exposure is still large relative to peer averages around 2-3% of loans, we note the progress the company made during the year, reducing the portfolio 17.7% during the year to levels representing 5.1% of loans from 5.8% a year-earlier. Zions maintains reserve balances for this portfolio equal to 9% of energy loans which reduces potential losses. We consider Zions consumer loans to represent average credit risk. Results on the Stress Test reflects Regions' above average initial capital position and our expectations for decent pre-provision profits over our forecast horizon. Taken together, forecasted capital levels are maintained at acceptable levels under our stress-case assumptions.

Our positive outlook on Zions Bancorporation implies that we are more likely to upgrade our rating in the next year than downgrade it. We could raise our rating if asset quality improves from current levels to levels more comparable to peers. A higher rating assumes that energy prices increase gradually over the next two years and that higher forecast interest rates contribute to net interest income growth over 10%. We expect these conditions to lead to higher profits during our forecast period, with return on common equity averaging around 9% and return on assets around 1%. In addition, a higher rating assumes that the company maintains capital levels above those of larger and more diversified regional banks. If profits were to fall below expectations, we could consider moving our outlook to stable or negative. Lower levels of tangible capital relative to tangible assets could also lead to a lower Solvency Score and a lower rating. Higher levels of short-term wholesale funding could contribute to a lower Business Risk score. Lower energy prices, a riskier loan portfolio, or lower underwriting standards could contribute to a lower Stress Test score and a lower credit rating. Conversely, higher levels of deposits relative to total liabilities or higher levels of pre-provision profits relative to average assets could contribute to a higher Solvency Score and a higher Business Risk score. Higher capital levels relative to tangible assets could also lead to a higher Solvency Score and a higher credit rating.

Goldman's BBB+ Rating Affirmed on Earnings Power and Solid Regulatory Capital; Outlook Stable
Morningstar Credit Ratings, LLC is affirming its BBB+ credit rating and stable outlook for Goldman Sachs Group, Inc. The company's credit rating benefits from solid competitive positions in investment banking, underwriting, and trading, which support a favorable Business Risk assessment. Although regulatory requirements and challenging market conditions in some of Goldman's key product lines have contributed to lower profits recently than in prior years, our outlook on the company remains stable.

Goldman's good Business Risk score benefits from the company's global reach, scale, and solid competitive positions in investment banking, including financial advisory and underwriting, as well as fixed-income and equity client trading. During 2016, revenue from client trading represented 47.3% of net revenue, with 24.7% from fixed-income and related products, 22.6% from equities, 20.5% from investment banking activities, 13.3% from investing and lending activities, and 18.9% from investment management operations. Management has demonstrated competence over multiple business cycles, adapting its business model to an evolving regulatory landscape and volatile market conditions, which contributes to an above-average management grade. Also contributing positively to the Business Risk score is Morningstar's Equity Research Group's narrow economic moat assessment, which reflects intangible assets in the firm's distribution platform and investment banking relationships. However, the aforementioned factors are mitigated by a material need for wholesale funding. Largely a function of its role as an investment bank where deposits aren't central to the business model, Goldman's deposits represent only 16% of total liabilities at year-end, implying a large need for wholesale funding sources, a factor that negatively affects our Business Risk score.

Goldman generates a below-average Solvency Score, with many of the components scoring below average relative to a broad set of U.S. banks. Regulatory requirements restricting certain trading activities, large legal expenses, and more rigorous capital requirements have constrained profits during recent years. Earnings power, as illustrated by preprovision profit/average assets, deteriorated during 2016 to levels modestly below average from above-average levels following the financial crisis of 2008-

09. Because Goldman Sachs typically doesn't report material provision expense, this measure may not fully capture its earnings power. Return on average assets for the year, a related measure, was 0.82% as we calculate it, in line with peers. However, Goldman's return on average common equity for the year was 9.4%, which compares favorably with an average of 8.6% for a broad set of U.S. banks. Net of issuance for share-based compensation, the company returned around 71% of net income to shareholders during 2016, which constrained further capital growth and improvement in the company's Solvency Score measure. Relative to our peer set, Goldman's ratio of tangible common equity/tangible assets was 8.3% by our calculations, modestly below average. However, the company's regulatory capital measures compare favorably with a broad set of U.S. banks, with a common equity Tier 1 capital ratio of 13.1% and a Tier 1 capital ratio of 15.0% compared with averages of 11.5% and 12.5%, respectively, for the group. Although lending isn't Goldman's primary focus, we consider the company's capital levels relative to problem loans, as well as its overall level of delinquent and nonperforming assets, to be roughly average. The low level of deposit funding, which ranks in the bottom decile of our peer set, detracts from the company's Solvency Score.

Goldman Sachs generates a strong score on our Stress Test, which compares favorably with global banking peers. Unique to its investment banking business model, the company holds a very small loan portfolio, equal to only 7.4% of assets, and a very large securities trading portfolio, representing 34.4% of assets of asset at year-end. We consider most of the company's loan portfolio, which consists mainly of corporate loans and loans collateralized by real estate, to represent below-average credit risk. We consider the company's trading portfolio to represent average credit risk. Results on the Stress Test reflects Goldman's good initial capital position and solid levels of loan-loss reserves and our expectations for decent preprovision profits over our forecast horizon. Taken together, forecast capital levels are maintained at solid levels under our stress-case assumptions.

Our stable outlook for Goldman Sachs implies that we are unlikely to change our rating within the next year. Our rating assumes that the company improves profitability measures during our forecast horizon to levels observed during recent years, including a return on average assets around 0.85% and return on common equity around 11%. Our rating also assumes that the company maintains capital levels near current levels. If realized profits were to fall below our expectations, we could consider a negative outlook or a lower rating. In addition, lower levels of tangible capital relative to tangible assets or lower levels of reserves relative to nonperforming assets could also lead to a lower Solvency Score and a lower rating. Higher levels of preprovision profits relative to average assets could contribute to a higher Solvency Score and a higher Business Risk score. Higher capital levels relative to tangible assets could also lead to a higher Solvency Score and a higher credit rating.

Morgan Stanley's BBB Rating and Stable Outlook Affirmed on Diverse Revenue, Solid Regulatory Capital

Morningstar Credit Ratings, LLC is affirming its BBB credit rating and stable outlook on Morgan Stanley. The company's credit rating benefits from solid competitive positions in investment banking, underwriting, and trading, which support the company's favorable Business Risk assessment. The company's move into wealth management during recent years provides a diversifying effect on revenue and decreases risks to the firm. Although regulatory requirements and challenging market conditions in

some of Morgan Stanley's key product lines have contributed to lower profits recently than in prior years, our outlook on the company remains stable.

Morgan Stanley's average Business Risk score benefits from the company's global reach, scale, and solid competitive positions in wealth management and investment banking, including financial advisory and underwriting, as well as fixed income and equity client trading. During 2016, wealth management revenue represented 44.3% of total revenue, while revenue from client trading represented 35.5% of revenue, which favored equity trading over fixed income and related products. Investment banking contributed 12.9% of revenue, and institutional asset management contributed 6.1% of revenue during the year. Also contributing to the Business Risk score is Morningstar's Equity Research Group's narrow economic moat rating, which reflects intangible assets in the firm's distribution platform and investment banking relationships. However, the above factors are mitigated by a material need for wholesale funding. Although Morgan Stanley has increased deposits during recent years, at year-end, deposit balances represented only 21% of total liabilities, implying a large need for wholesale funding sources, which diminishes our Business Risk score.

Morgan Stanley has a below-average Solvency Score, with many of the components scoring below average relative to a broad set of U.S. banks. Regulatory requirements restricting certain trading activities, large legal expenses, and more rigorous capital requirements have constrained profits during recent years. Earnings power, as illustrated by preprovision profit/average assets, ranked below average during 2016 from above average before the financial crisis of 2008-09. Because Morgan Stanley typically doesn't report material provision expense, this measure may not fully capture the company's earnings power. However, return on average assets for the year, a related measure, was 0.69% as we calculate it, which trailed a peer average around 0.85% for the year. Similarly, Morgan Stanley's return on average common equity for the year was 8.1%, which also trails an average of 8.6% for a broad set of U.S. banks. During the first three quarters of 2016, the company returned over 100% of net income to shareholders, which restrained tangible capital measures and hurt the company's Solvency Score. Relative to our peer set, Morgan Stanley's ratio of tangible common equity/tangible assets was 7.4% by our calculations, which ranked below average. However, the company's regulatory capital measures compare favorably to a broad set of U.S. banks, with a strong common equity Tier 1 capital ratio of 16.8% and a Tier 1 capital ratio of 16.8% compared with averages of 11.5% and 12.5%, respectively, for the group. Although lending isn't Morgan Stanley's primary focus, we consider the company's capital levels relative to problem loans, as well as its overall level of delinquent and nonperforming assets, to be modestly above average. However, Morgan Stanley's low level of deposit funding, which ranks in the bottom decile relative to our peer set, detracts from the company's Solvency Score.

Morgan Stanley generates a strong score on our Stress Test, which compares favorably with global banking peers. Unique to its investment banking business model, the company holds a very small loan portfolio, equal to around 10% of assets, and a very large securities trading portfolio that represents 33.6% of assets as of September. We consider most of the company's loan portfolio, which consists mainly of corporate loans, loans to wealth management clients, and loans collateralized by real estate, to represent below-average credit risk. We consider the company's trading portfolio to represent average credit risk. Results on the Stress Test reflect Morgan Stanley's good initial capital position and solid

levels of loan-loss reserves and our expectations for decent preprovision profits over our forecast horizon. Taken together, forecast capital levels are maintained at solid levels under our stress-case assumptions.

Our stable outlook on Morgan Stanley implies that we are unlikely to change our rating within the next year. Our rating assumes that the company improves profitability measures during our forecast horizon to levels more consistent with U.S. global banking peers, including a return on average assets around 0.85% and return on common equity around 11%. Our rating also assumes that the company maintains capital near current levels. If realized profits were to fall below our expectations, we could consider a negative outlook or a lower rating. In addition, lower levels of tangible capital relative to tangible assets or lower levels of reserves relative to nonperforming assets could also lead to a lower Solvency Score and a lower rating. Conversely, higher levels of preprovision profits relative to average assets could contribute to a higher Solvency Score and a higher Business Risk score. Higher capital levels relative to tangible assets could also lead to a higher Solvency Score and a higher credit rating.

Bank of America's BBB Rating and Stable Outlook Affirmed on Improving Asset Quality
Morningstar Credit Ratings, LLC is affirming its BBB credit rating and stable outlook on Bank of America Corporation. The company's credit rating benefits from a solid competitive position reflected in its Business Risk score as well as improving asset quality. Our outlook on the company remains stable.

Bank of America's good Business Risk score benefits from the company's size, scale, and diverse operations, the positive effects of which are partly offset by a significant need for wholesale funding. With over $2.1 trillion of assets at year-end, Bank of America is the second largest U.S. bank by assets. It organizes its operations into four primary operating segments: a consumer bank, servicing individuals and businesses through deposit taking, lending, and credit cards; a commercial and wholesale banking unit catering mainly to large corporations; a wealth and investment management unit, focusing on brokerage, wealth, and investment management services; and markets group, providing equity and fixed income trading services. During 2016, revenue was well-diversified across the segments with consumer banking generating 37.5% of revenue, global banking, 21.8%, and wealth and investment management, 20.9%, and global markets, 19.0%. Despite its breadth, Bank of America is the most domestically focused of the global U.S. banks with just 13.1% of assets from non-U.S. geographies at the end of 2016. Morningstar's Equity Research Group assigns Bank of America a narrow economic moat because of cost advantages in its core banking operations and intangible assets in its investment banking operations, a factor that positively influences the company's Business Risk assessment. However, Bank of America's deposits represent only 65.6% of total liabilities at year-end, implying a significant need for wholesale funding sources that negatively impacts our Business Risk score.

Bank of America generates a below-average Solvency Score with all of the components scoring below average relative to a broad set of U.S. banks. Earnings power, as illustrated by pre-provision profit-to-average assets, has improved during 2016 but still ranks in the 45-percentile. Return on average assets for the year, a related measure, was 0.75% as we calculate it, which trails a peer average around 0.85%. Similarly, Bank of America's return on average common equity was 6.8%, which also trails an average of 8.6% for a broad set of U.S. banks.

The bank's asset quality score, which includes delinquent and non-performing assets to total assets, has been improving recently but along with reserves for problem assets, is below average as compared with its peers. At year-end, reserves for non-performing assets represented about 139% of loans and other real estate owned, which trails an average for global banks of around 200%. Although Bank of America has reported higher capital levels than a year ago, the company's level of tangible common equity relative to tangible assets ranks lower than average. By our calculations, tangible common equity represented 8.1% of tangible assets at year-end, modestly above a peer average around 8%. Bank of America's regulatory capital compares more favorably with a common equity Tier 1 capital ratio of 11.0% that is approximately average relative to peers. Similar to other global banks, Bank of America's relatively low level of deposit funding detracts from the company's Solvency Score. Deposits represented about 65.6% of liabilities at year-end, which ranks in the bottom-decile relative to a broad set of U.S. banks and detracts from the Solvency Score.

Bank of America generates a good score on our Stress Test. The company benefits from a diverse loan portfolio that is evenly split between consumer loans and commercial loans that each represented about half of loans held for investment at year-end. We consider most of Bank of America's loans to represent average credit risk. Results on the Stress Test reflect Bank of America's initial capital position and loan-loss reserves combined with our expectations for decent pre-provision profits over our forecast horizon. Taken together, forecast capital levels are maintained at acceptable levels under our stress-case assumptions.

Our stable outlook on Bank of America Corp implies that we are unlikely to change our rating within the next year. Our rating assumes that the company improves profitability measures during our forecast horizon to levels closer to those expected for global bank peers. This would include a return on average assets around 0.85% and return on common equity around 7.5%. Our rating also assumes that the company maintains capital levels near current levels. If realized profits were to fall below our expectations, we could consider a negative outlook or a lower rating. In addition, lower levels of tangible capital relative to tangible assets or lower levels of reserves relative to non-performing assets could also lead to a lower Solvency Score and a lower rating. A riskier loan portfolio or lower underwriting standards could contribute to a lower Stress Test score and a lower credit rating. Conversely, higher levels of deposits relative to total liabilities or higher levels of pre-provision profits relative to average assets could contribute to a higher Solvency Score and a higher Business Risk score. Higher capital levels relative to tangible assets could also lead to a higher Solvency Score and a higher credit rating.

Recent Notes Published by Credit Analysts

Perrigo Selling Tysabri Royalty Stream; Focuses on Debt Reduction

MCR Credit Risk Assessment

On Feb. 27, Perrigo (rating: BBB-, negative) offered preliminary, unaudited results for fiscal 2016 that indicated a rise in reported revenue to $5.6 billion from $5.4 billion in 2015. Few specifics of Perrigo's overall operating performance were detailed during the conference call, as the company needs more time to determine the financial impact of the just-announced divestment of the firm's Tysabri royalty-bearing stream. In part, this situation will cause a delay in its 10-K reporting until March 16 at the latest. Earlier in the day, Perrigo announced a definitive agreement to sell its royalty stream from sales of Tysabri (multiple sclerosis) to a subsidiary of Royalty Pharma, for total consideration of up to $2.85 billion, comprising $2.2 billion upon closing of the transaction and $650 million in revenue milestone payments. We previously stated that if the Tysabri asset, which currently represents nearly one third of earnings, were to be sold without a concomitant decrease in the debt load to ease leverage, then a downgrade to the current rating may occur. However, management reiterated its commitment to an investment-grade rating and stated that some proceeds of the sale would be utilized for debt reduction over the next two years.

At the end of 2016, Perrigo had a cash balance of $662 million and owed debt of $5.8 billion. In order to simply maintain gross leverage at the same level of 3.6 times for the latest 12 months at the end of September, the firm would need to repay more than $2 billion in debt following completion of the transaction. On its conference call, management mentioned its intention to pay down coming long-term debt maturities of $560 million in 2017, as well as the potential for more substantial reductions. The firm also has $600 million in long-term debt maturing in 2018. As part of its strategy, Perrigo looks to preserve cash by holding back on share repurchases and targeting bolt-on acquisitions. Our BBB- rating and negative outlook consider that Perrigo's strategy to repair struggling segments may potentially create variability in earnings and cash flows over the length of its efforts. As such, we think the firm's operational results will likely stay volatile as the company carries out its strategic initiatives to reinvigorate flagging performance through increased internal investment and corporate pruning.

Market Data

For closest comparisons to Perrigo's notes, we look to similarly rated companies Mylan (rating: BBB-, stable) and Shire (rating: BBB-, stable). Within this comparable group and adjusted for bond maturities, Perrigo's 10-year bonds trade close to those at Mylan and wider than those at Shire. Perrigo's 10-year bonds also trade wider than the level of the Morningstar Inc.'s BBB- Corporate Bond Index. All of the following bond data is sourced from Advantage Data and Finra TRACE.

In the approximate five-year maturity bucket, bonds from these issuers recently traded over the nearest Treasury as follows:
Perrigo's (rating: BBB-, negative) 3.50% notes due 2021 at +139 basis points;
Mylan's (rating: BBB-, stable) 3.15% notes due 2021 at +138 basis points; and
Shire's (rating: BBB-, stable) 2.40% notes due 2021 at +108 basis points.

In the approximate 10-year maturity bucket, bonds from these issuers recently traded over the nearest Treasury as follows:
Perrigo's 4.38% notes due 2026 at +201 basis points;
Mylan's 3.95% notes due 2026 at +195 basis points; and
Shire's 3.20% notes due 2026 at +147 basis points.

For comparison with the approximate 10-year maturities, Morningstar Inc.'s Bond Index is at +156 basis points in the BBB category and at +179 basis points in the BBB- category.

In the approximate 30-year maturity bucket, bonds from these issuers recently traded over the nearest Treasury as follows:
Perrigo's 4.90% notes due 2044 at +228 basis points;
Mylan's 5.25% notes due 2046 at +227 basis points; and
Shire's (Baxalta) 5.25% notes due 2045 at +171 basis points.

Discovery Announces New 7-Year Senior Notes and Reopens 2026 Notes
Market News and Data
Discovery Communications (rating: BBB, negative) has announced a $450 million issuance of 2024 notes and is also re-opening its 4.90% notes due 2026 for $200 million. The 2026 notes were originally issued in March 2016 at +313 basis points and recently traded at +190 basis points over the nearest Treasury, 123 basis points tighter from issue a year ago. For comparison, the Morningstar Corporate Bond BBB Index is 178 basis points tighter over the same period and is now quoted at +150 basis points.

According to a regulatory filing filed by Discovery on Feb. 28, the proposed notes will be issued by Discovery's operating subsidiary Discovery Communications LLC and guaranteed by Discovery, consistent with Discovery's existing notes. In its filing, the company did not indicate a specific use of proceeds for the notes. However, we believe a portion of the proceeds will be directed toward repaying the $550 million of borrowings against the revolving credit facility, as well as $48 million of commercial paper outstanding at year-end. We also anticipate a continued focus on share repurchases.

For market comparables, we reference similarly-rated technology peers Viacom Inc. (rating: BBB, negative) and CBS Corp. (rating: BBB, stable). The following market pricing data is from pricing sources Advantage Data and FINRA TRACE.

In the 7-year area, comparable issues recently traded as follows:
Discovery's 3.25% notes due 2023 at +146 basis points over the nearest Treasury;
CBS' 3.70% notes due 2024 are indicated by Advantage Data around +135 basis points;
Viacom 3.88% notes due 2024 at +169 basis points.

In the 10-year area, comparable issues recently traded as follows:
Discovery's 4.90% notes due 2026 at +190 basis points;
CBS' 4.00% notes due 2026 at +143 basis points;
Viacom 3.45% notes due 2026 at +175 basis points.

MCR Credit Risk Assessment

Our BBB rating reflects Discovery's competitive strength, particularly in non-U.S. markets, consistent cash flow generation, and relatively low capital expenditure needs. This has contributed to stability in Discovery's credit rating pillars, despite high debt levels and its shareholder-focused use of capital. However, our negative outlook incorporates management's financial policy, uncertainty around the pace of international growth and future content costs, and ongoing headwinds from currency translation, particularly in Europe. We currently view Discovery's media portfolio as more competitive than Viacom, particularly with respect to marketability of its brands outside the U.S. Viacom's uncertainty is also higher due to its recent management shakeup. Meanwhile, Discovery does not benefit from the portfolio diversity of CBS, a disadvantage that we view as partially offset by its lower reliance on advertising revenue. At 4.1 times EBITDA, Viacom's net debt is much higher than Discovery's due to declining profitability over the past year, while CBS' net debt remains stable at 2.5 times.

Discovery's debt ended 2016 at $7.9 billion, up $188 million from a year ago on net new debt issuance while cash declined $90 million during the year. Total debt ended the year at 3.3 times EBITDA, a slight increase from 2015, while net debt was unchanged at 3.1 times. Meanwhile, free cash flow for the most recent 12 months was 1.3 billion, up 9.5% from 2015.

Although net leverage held steady during 2016, we remained concerned about Discovery's capital allocation policy. Net share repurchases and dividend payments in 2016 represented a payout of 106% of free cash flow. While that marks an improvement from 2015's payout of 131%, it still appears aggressive given Discovery's elevated debt level. For 2017, management did not provide specific share repurchase guidance but expects to continue to prioritize return of capital to shareholders. Management reiterated that it is comfortable with its target range for gross leverage at or below 3.4 times EBITDA.

J&J Issuing Debt for Share Repurchasing and Commercial Paper Repayment

Market News and Data

Johnson & Johnson Inc. (rating: AAA, negative) is in the market with a proposed offering that includes five-, 10-, 20-, and 30-year fixed-coupon maturities. According to a preliminary prospectus filed on Feb. 27, net proceeds will be used for general corporate purposes, including share repurchasing and the payment of outstanding commercial paper. As of Jan. 1, J&J had outstanding commercial paper outstanding of approximately $2.7 billion. Also on Jan. 1, J&J had around $2.7 billion of remaining authorization against its $10 billion share-repurchase program from October 2015.

For closest comparisons to J&J's notes, we look to lower-rated companies Eli Lilly and Co (AA, stable), Novartis AG (AA, stable) and Merck & Co (AA, stable). All of the following bond data is sourced from Advantage Data and Finra TRACE.

In the approximate five-year maturity bucket, bonds from these issuers recently traded over the nearest Treasury as follows:

J&J's (AAA, negative) 1.65% notes due 2021 at +19 basis points;

Merck's (AA, stable) 2.35% notes due 2022 at +41 basis points; and

Novartis' (AA, stable) 2.40% notes due 2022 at +48 basis points.

In the approximate 10-year maturity bucket, bonds from these issuers recently traded over the nearest Treasury as follows:
J&J's 2.45% notes due 2026 at +55 basis points;
Eli Lilly's (AA, stable) 2.75% notes due 2025 at +60 basis points;
Merck's 2.75% notes due 2025 at +66 basis points; and
Novartis' 3.0% notes due 2025 at +66 basis points.

For comparison with the approximate 10-year maturities, the Morningstar Corporate Bond Index is at +67 basis points in the AAA category and +77 basis points in the AA category.

In the approximate 30-year maturity bucket, bonds from these issuers recently traded over the nearest Treasury as follows:
J&J's 3.7% notes due 2046 at +70 basis points;
Eli Lilly's 3.7% notes due 2045 at +90 basis points;
Merck's 3.7% notes due 2045 at +91 basis points; and
Novartis' 4.0% notes due 2045 at +89 basis points.

MCR Credit Risk Assessment
Johnson & Johnson's AAA credit rating reflects its diversified position across the entire healthcare space that provides exceptional financial flexibility. Our expectation that this flexibility may be compromised over the next few years from aggressive capital deployment while J&J battles key drug patent expirations through 2019 informs our negative outlook. Diverse operations that span pharmaceuticals, medical devices, and over-the-counter medicines (representing roughly 45%, 35%, and 20% of total sales, respectively) buffer J&J from weakness in a particular segment at any given time. Diversification is an important cog in our top-tier Business Risk pillar and gives us confidence that the firm can withstand losses of market exclusivity for multiple blockbuster drugs (Remicade, Velcade, Invega Sustenna, Zytiga, and Prezista) over the next three years; these blockbuster drugs currently represent around 18% of total revenue. A highly productive drug research program that plans to ready 10 potential blockbusters for regulatory registration through 2019 may help offset the expected patent losses, leading to growth in the low single digits through 2020, compounded annually.

J&J's earnings growth prospects fall at the low end of the large pharmaceutical industry, with EBITDA rising in the low single digits through 2020 compounded annually, in our estimation. New debt issuances during 2016 to help fund heavy repurchasing activity have driven the firm's debt load to nearly $27 billion at the end of 2016 from about $20 billion at the end of 2015. But J&J remained in a net cash position in 2016, with $42 billion of cash and investments supporting our Cash Flow Cushion and Solvency Score pillars. While we see reduced financial flexibility over the next year given the pending purchase of Actelion Ltd. for $30 billion, we would need to see larger debt-funded repurchases or acquisitions to make a cut in J&J's very strong credit rating. J&J's tax-effective use of overseas cash to fund the transaction will have no impact on the debt load or gross debt leverage, which will remain below 1 time.

Tenet Disappoints in 4Q, and Management Delays Deleveraging Timeline

MCR Credit Risk Assessment

On Feb. 28, Tenet Healthcare Corp (rating: B, negative) reported disappointing fourth-quarter operating results that contributed to increasing leverage and the equity down nearly 15% in early morning trading. After several divestitures, net operating revenue in the fourth quarter declined 3% to $4.9 billion, or slightly below consensus. These results were influenced by a 6% decline in hospital operations after recent divestitures but also included 3% growth on same-hospital basis on a slight decline in admissions after being pushed out-of-network with Humana Inc (rating: BBB+/UR-) and 4% growth in revenue per admission. Tenet also experienced a deceleration in its other operations, including 20% growth in ambulatory care (6% on a same-facility basis) and 5% growth from its Conifer revenue cycle management subsidiary. These lower results were negatively influenced by the Humana network change, as well, and one less surgical day in the quarter. With these trends, adjusted EBITDA of $613 million was flat versus the previous-year period, and adjusted earnings per share were only $0.06 per share (or significantly below consensus estimates of $0.22 for the period).

On these reported results and new debt issuance in the fourth quarter, Tenet's leverage rose by about a quarter of a turn since September. As of December, gross debt stood at $15.3 billion, or around 6.3 times trailing 12-month EBITDA by our estimates, and cash stood at $716 million, leading to net leverage of around 6.0 times. This increase in leverage was not particularly surprising given the expected payment ($517 million) on the Clinica de la Mama settlement in the fourth quarter.

However, with a lackluster outlook for 2017, including proposed investment activities, Tenet's leverage may remain elevated above target for the next couple of years, which informs our negative outlook. For example, management expects adjusted EBITDA of $2.5 billion to $2.6 billion in 2017, or up in the mid-single-digits from the $2.4 billion produced in 2016. The company expects adjusted free cash flow of $600 million to $800 million in 2017, up from $380 million in 2016 when adjusted for restructuring and other charges like the Clinica de la Mama outflow. Tenet would have to meet those expectations and use virtually all free cash flow in 2017 for debt reduction in order to make meaningful progress toward its net leverage goal of around 5 times. However, in 2017, management aims to increase investments in affiliated ambulatory surgery businesses ($320 million to $350 million to buy another 12.5% stake in USPI to push its ownership stake to 69% plus $100 million to $150 million to invest in its other ambulatory operations), which could keep net leverage in the high-5s in 2017. With plans to invest another roughly $1 billion to boost its stake in USPI to 95% in the next few years, the company has delayed its deleveraging timeline to 5 times or less by about a year to 2019. Management did note that this timeline could be positively influenced by unannounced divestiture activities, though.

Market Data

In our coverage universe, Tenet Healthcare Corp (rating: B, negative) is rated much lower than its healthcare service peers, such as HCA Holdings Inc (rating: BB, stable). Therefore, we use other B rated healthcare companies as its key credit comparables, including Endo International PLC (rating: B, negative) and Valeant Pharmaceuticals International Inc (rating: B, negative). In the approximate 5-year maturity bucket, Tenet's bonds recently traded at a yield roughly 60 basis points tighter than similar bonds from Endo. Valeant's bonds recently traded much wider than bonds from both of those firms.

Recent bond data from all of these firms are sourced from Advantage Data and Finra TRACE, which can be seen as follows:

Tenet's 8.13% notes due in 2022 at 105.25, yield to maturity of 6.88% and spread to maturity of +494 basis points;
Endo's 5.75% notes due in 2022 at 93.00, yield to maturity of 7.49% and spread to maturity of +566 basis points;
Valeant's 7.50% notes due in 2021 at 93.25, yield to maturity of 9.42% and spread to maturity of +763 basis points.

Frontier Battles Operational Headwinds in 4Q, but 2017 Outlook Is Better
MCR Credit Risk Assessment
Frontier Communications (rating: BB-, negative) reported fourth-quarter and full-year results Feb. 27. Execution remains a challenge for the carrier three quarters after its acquisition of Verizon's FiOS markets in California, Texas, and Florida (CTF). The customer service transition has required more management attention than expected, which made the carrier late in executing on new customer marketing. As a result, Frontier has seen material net customer declines in the acquired markets along with ongoing erosion of legacy subscribers and continued pressure on operating margins. Fourth-quarter operations were adversely affected by adverse weather conditions, which hurt service calls and installations. The company also took a $45 million revenue hit to clean up delinquent accounts and expects an additional $25 million of negative revenue impact in first quarter. However, over the long term, we continue to view the well-maintained CTF fiber network as supportive of Frontier's long-term competitive position in its markets. We also expect the premium revenue from FiOS markets to help support network improvements in less competitive areas.

Frontier reported fourth-quarter legacy revenue down 9.3% year over year, while revenue from the CTF assets was down 3% from last quarter, excluding the $45 million cleanup headwind. As reported, the adjusted operating margin declined 150 basis points from a year ago, though it improved 40 basis points from third quarter. Management is expecting a sequential decline in first-quarter revenue, excluding the remaining account cleanup impact, but expects the operating trend to become less negative compared with the fourth quarter. For 2017, we believe organic revenue may decline around 3%-4%, offset by an additional $1 billion from CTF contribution in the first quarter that was not reflected in first-quarter 2016 results.

Frontier's net debt ended 2016 at $17.8 billion, or 4.4 times EBITDA by our calculation. We believe pro forma net leverage should remain flat or decrease modestly in 2017, based on our preliminary projection for EBITDA of $3.5 billion-$4.0 billion. Cash and equivalents ended the year at $522 million, up $221 million from the third quarter. For the most recent 12 months, Frontier reported free cash flow of $407 million compared with $591 million in the year-ago period, a decline that reflects over $400 million of cash costs relating to integration. For the full year, the dividend payout was 121% of trailing free cash flow, down considerably from 335% through the third quarter. Over the next few years, assuming operating performance stabilizes, we believe the payout should decline to around 50%.

Frontier faces $363 million of debt maturities in 2017 and $733 million in 2018. From our base forecast of 2017 EBITDA, we estimate that Frontier can produce free cash flow of $1 billion per year. This assumes no further material write-off in accounts receivable or other significant working capital changes. With dividends at around $531 million per year, we estimate that the shortfall of cash available for debt repayment would be less than $200 million, which can be covered through its revolving credit facility.

During the quarter, Frontier increased its revolving credit facility by $100 million, to $850 million, and extended the maturity by four years to 2022. The amendment also included a restated leverage covenant schedule, with maximum leverage at 5.25 times EBITDA through the second quarter of 2018. From there, leverage will decline in 0.25-turn increments until mid-2020, when the leverage cap will be 4.50 times. For the fourth quarter, the carrier disclosed current leverage of just under 4.1 times as calculated for covenant purposes. Management expects leverage to remain around 4 times over the next few years.

Though Frontier's Cash Flow Cushion and Solvency Score remain pressured by high debt levels, interest expense, and low returns on invested capital, we still consider its long-term credit position to be stronger than current conditions indicate. Compared with its peers, Frontier has a bit more debt than either Sprint Corp. (rating: B, stable) at 3.2 times or Dish Network (rating: BB-, negative) at 3.4 times. We think this is offset by a less complicated debt structure than either of these comps. We also view Frontier's long-term ability to compete in its markets to be as strong or better than either Sprint or Dish.

Market Data
Frontier's 6.88% notes due 2025 recently traded at a yield of 9.80% to maturity (+760 basis points over the nearest Treasury). Its 11% notes due 2025 recently traded at a yield to maturity of 11.09% (+884 basis points). Over the past three months, the yield on the 6.88% notes has tightened 58 basis points while the spread on the 11% notes has widened 21 basis points. For comparison over the same period, the BofA/Merrill Lynch BB index widened 14 basis points. Among comparable issues, same-rated Dish's 7.75% notes due 2026 are now indicated to yield 5.47% to maturity (+313 bps). Lower-rated Sprint's 7.63% notes due 2025 are indicated at a yield of 5.80% to the 2024 call date (366 basis points).

Disney Announces New 5-Year Senior Notes

Market Data
Walt Disney (rating: A+, positive) has announced a multi-tranche issue of both fixed and floating senior notes including 3- and 5-year maturities. We believe the primary use of proceeds of the proposed notes will be to refinance current debt maturities, which totaled $5.7 billion at the end of the December quarter.

For market comparables, we reference Comcast Corp. (rating: A-, stable) and Apple Inc. (rating: AA-, negative). The following market pricing data is from pricing sources Advantage Data and FINRA TRACE.

In the 5-year area, comparable issues recently traded as follows:
Disney's 2.35% notes due 2022 at +41 basis points;
Apple's 2.50% notes due 2022 at +54 basis points;
Comcast's 1.63% notes due 2022 at +57 basis points.

MCR Credit Risk Assessment
Disney's net debt has been slowly rising over the past two years, but remains at the low end of its historical range between 1 and 1.5 times EBITDA. Net debt ended 2016 at 1.0 time trailing EBITDA, up slightly from a year ago.

For comparison, lower-rated Comcast ended its most recent quarter with net debt at 2.2 times EBITDA, while higher-rated Apple ended its December quarter with an excess of cash over debt equivalent to 2.2 times (although its total debt is now at 1.3 times EBITDA, in line with Disney at 1.2 times).

Over the past 12 months, Disney produced $7.7 billion of free cash flow, with $2.3 billion deployed to fund the common dividend and $6.3 billion toward net share repurchases, bringing the payout ratio to 112% of free cash flow compared with 147% a year ago. The company funded the deficit with $1.8 billion of funds from net new debt issuance over the past year. Though share repurchases remain high, Disney's credit pillars continue to indicate solid credit support we believe management remains committed to a conservative use of debt.

Our A+ rating reflects Disney's moderate Business Risk, strong Cash Flow Cushion, and improving Solvency Score pillar, driven by expanding profits in film and consumer brands. Our positive outlook reflects growth in Disney's operating margins and returns on invested capital. Disney's core network assets still attract large numbers of viewers and enjoy significant negotiating leverage with cable operators as a result. While ESPN garners the highest affiliate fees of any basic cable channel, we are concerned that a secular decrease in pay-TV penetration may contribute to a slowing of revenue growth. Longer term, we view the rise of video streaming as a threat to ESPN and other network properties. We view the recently announced investment in video streaming technology company BAMTech as an effort to address the threat, providing Disney with a platform to explore alternatives to traditional cable for its content delivery.

CRH Reports 41% Increase in Full-Year EBITDA
MCR Credit Risk Assessment
CRH PLC (rating: BBB-, stable) reported full-year results for 2016 on March 1 that showed a 41% increase in EBITDA in 2016 compared with 2015. EBITDA increased to EUR $3.1 billion in 2016 from EUR 2.2 billion a year earlier and was helped by a full-year contribution of assets acquired in the third quarter of 2015--LH Assets and the C.R. Laurence acquisition. CRH's balance sheet debt declined to EUR 7.8 billion at year-end from EUR 9.2 billion at the end of 2015, resulting in debt/EBITDA improving to 2.5 times (1.7 net) from 4.2 times (3.0 net) a year ago. Revenue for the company rose 15% year over year to EUR 27.1 billion and was split geographically 46% Europe, 52% Americas, and 2% Asia. Generally speaking, margins and ROICs are higher in the Americas for the company compared with Europe as the Americas constituted 61% of firmwide EBITDA, while Europe was responsible for 36% and Asia 3%. Free cash flow for the company in 2016 was approximately EUR 1.5 billion compared with EUR 1.4 billion in 2015 on similar cash flow from operations and capital spending levels.

Guidance provided by management indicated that it expected the U.S. construction sector would continue to see positive momentum as well as U.S. infrastructure spending. In Europe, the company

stated that it believes most countries will experience a modest impact of an early-stage economic recovery. CRH expects capital spending for 2017 will be in line with depreciation levels (approximately EUR 1 billion), which would be a slight increase over 2016's capital expenditures of EUR 853 million. The company also said that acquisitions may well be in its future and that it now has a lot of balance sheet capacity for deals.

Market Data

According to Advantage Data and Finra Trace, CRH's 3.875% notes due on May 18, 2025, recently traded at a spread to nearest Treasury of +122 basis points. Meanwhile, we compare CRH to similarly rated LafargeHolcim's (rating: BBB-, stable) 3.5% notes due on Sept. 22, 2026, which recently traded at a spread of +143 basis points. For an index comparison, we look to the Morningstar's Corporate BBB- index, which is at +176 basis points.

Mylan Ends 2016 Strongly; Leverage Reduction Target Manageable

MCR Credit Risk Assessment

On March 1, Mylan (rating: BBB-, stable) reported strong operating results for the fourth quarter and full-year 2016. Total revenue increased 31% in the fourth quarter and almost 18% in 2016, helped in part by the August acquisition of Meda. Mylan achieved solid growth during the year from each of its new business segments, with the North American business rising 10%, Europe increasing 34%, and the rest-of-the-world division up 16%. Undaunted by integration efforts, the firm increased adjusted earnings by 14% to $4.89 in 2016, reaching the top end of its guidance of $4.70-$4.90. On solid footing, Mylan is marching toward its long-term plan of adjusted EPS of $6.00 in 2018, anticipating adjusted earnings of $5.15 to $5.55 in 2017. The firm hopes to grow total sales in 2017 to $12.25 billion to $13.75 billion, representing an increase of 17% at the midpoint of the range. Despite pressure on Mylan's EpiPen franchise from the availability of an authorized generic version, we remain optimistic that overall revenue and EBITDA may rise in the high single digits and low double digits, respectively, over the next five years compounded annually, backstopped by an expanding generic segment.

Mylan's debt load more than doubled to around $15.5 billion at the end of 2016 from $7 billion at the end of 2015 in conjunction with debt funding needed to consummate the Meda acquisition for $10 billion. Accordingly, pro forma gross leverage and net leverage increased to 3.6 times and 3.4 times, respectively, in 2016 from 3.1 times and 2.6 times, respectively, in 2015. We think the company may reach its commitment to reduce gross debt leverage to 3 times in 2017, which we expect can be attained through a combination of debt reduction and strong EBITDA growth. Mylan will see $2.4 billion of term loan borrowings mature in 2017, offering the company a great opportunity to achieve its deleveraging goal. We expect Mylan's $1.7 billion in reported free cash flow during 2016 may expand to an average of $2.5 billion annually through 2020. This level of free cash flow together with a year-ending cash balance of almost $1 billion provides enough flexibility to rapidly reduce leverage. Mylan's rating also considers aggressive capital deployment that keeps leverage elevated, punctuated by only intermittent periods at the firm's stated leverage goal.

Market Data

For closest comparisons to Mylan's notes, we look to similarly rated companies, Perrigo (rating: BBB-, negative) and Shire (rating: BBB-, stable). Within this comparable group and adjusted for bond maturities, Mylan's 10-year bonds trade wider than those at Perrigo and Shire, and wider than Morningstar Inc.'s BBB- Corporate Bond Index. All of the following bond data is sourced from Advantage Data and Finra Trace.

In the approximate 5-year maturity bucket, bonds from these issuers recently traded over the nearest Treasury as follows:
Mylan's (rating: BBB-, stable) 3.15% notes due in 2021 at +134 basis points;
Perrigo's (rating: BBB-, negative) 3.50% notes due in 2021 at +131 basis points; and
Shire's (rating: BBB-, stable) 2.40% notes due in 2021 at +102 basis points.

In the approximate 10-year maturity bucket, bonds from these issuers recently traded over the nearest Treasury as follows:
Mylan's 3.95% notes due 2026 at +193 basis points;
Perrigo's 4.38% notes due 2026 at +181 basis points; and
Shire's 3.20% notes due 2026 at +144 basis points.

For comparison to the approximate 10-year maturities, Morningstar Inc.'s Corporate Bond Index is at +154 basis points in the BBB category and at +176 basis points in the BBB- category.

In the approximate 30-year maturity bucket, bonds from these issuers recently traded over the nearest Treasury as follows:
Mylan's 5.25% notes due 2046 at +222 basis points;
Perrigo's 4.90% notes due 2044 at +205 basis points; and
Shire's (Baxalta) 5.25% notes due 2045 at +167 basis points.

LafargeHolcim's Leverage Drops to 3.8 Times

MCR Credit Risk Assessment

LafargeHolcim Ltd (rating: BBB-, stable) reported fourth-quarter and full-year results that showed both debt reduction and EBITDA improvement. The company reduced gross balance sheet debt to CHF 19.7 billion at year-end 2016 from CHF 21.8 billion a year earlier. Full-year EBITDA for 2016 rose to CHF 5.2 billion from CHF 4.6 billion in 2015, which equates to a 13% increase. Net revenue was down 8.7% because of the company's divestiture program but only 1.4% on a like-for-like basis. Net margin improvement accounted for the EBITDA increase, driven by increased pricing and cost discipline. Because of the EBITDA improvement and debt reduction, debt/EBITDA for 2016 declined to 3.8 times (2.8 net) from 4.7 times (3.7 net) in 2015. Full-year cash from operating activities also improved, to CHF 3.3 billion from CHF 2.5 billion for 2015, and free cash flow sharply improved to CHF 1.5 billion in 2016 from CHF 0.4 billion in the prior year. Cash and equivalents were CHF 4.9 billion as of the end of 2016, an increase over the CHF 4.4 billion at the end of 2015.

Management guidance for 2017 includes 2%-4% revenue growth, in line with its markets. Management also indicated that it is proposing to increase its dividend to CHF 2 per share from CHF 1.5 and buy back up to CHF 1 billion of its shares during 2017-18. Additionally, LafargeHolcim indicated that it is targeting net debt/adjusted EBITDA of around 2 times.

A credit comparable is CRH PLC (rating: BBB-, stable), whose debt/EBITDA is 2.5 times (1.7 net) and produced EUR 1.5 billion in free cash flow in 2016. CRH also indicated on its year-end 2016 conference call that it currently possesses a lot of balance sheet capacity for potential acquisitions.

Market Data
According to Advantage Data and Finra Trace, LafargeHolcim's 3.5% notes due on Sept. 22, 2026, recently traded at a spread to nearest Treasury of +136 basis points. Meanwhile, CRH's 3.875% notes due on May 18, 2025, traded recently at a spread of +121 basis points. For an index comparison, we look to the Morningstar's Corporate BBB- index, which is at +173 basis points.

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