Morningstar Corporate Credit Research Highlights
High-yield bonds continue to outperform investment grade.

Morningstar Credit Ratings, LLC
17 January 2017

Credit Market Insights

- Market data and insights.

Credit Rating Actions

- Rating Affirmations

Issuer/Ticker	Current Issuer Credit Rating	Previous Issuer Credit Rating
Zimmer Biomet ZBH	BBB+	BBB+
Becton Dickinson BDX	BBB+	BBB+
Hologic HOLX	BB+	BB+
Baxter BAX	A-	A-
Pioneer Natural Resources PXD	BBB-	BBB-
Scripps Networks SNI	BBB+	BBB+

Recent Notes Published by Credit Analysts

- **General Mills** issuing new 10-year senior notes to refinance maturing debt.
- **Valeant** begins divestitures to reduce debt.
- **JPMorgan** reports solid 4Q results driven by lower credit costs and higher trading revenue.
- **Bank of America** reports 4Q results consistent with recent quarterly trends.

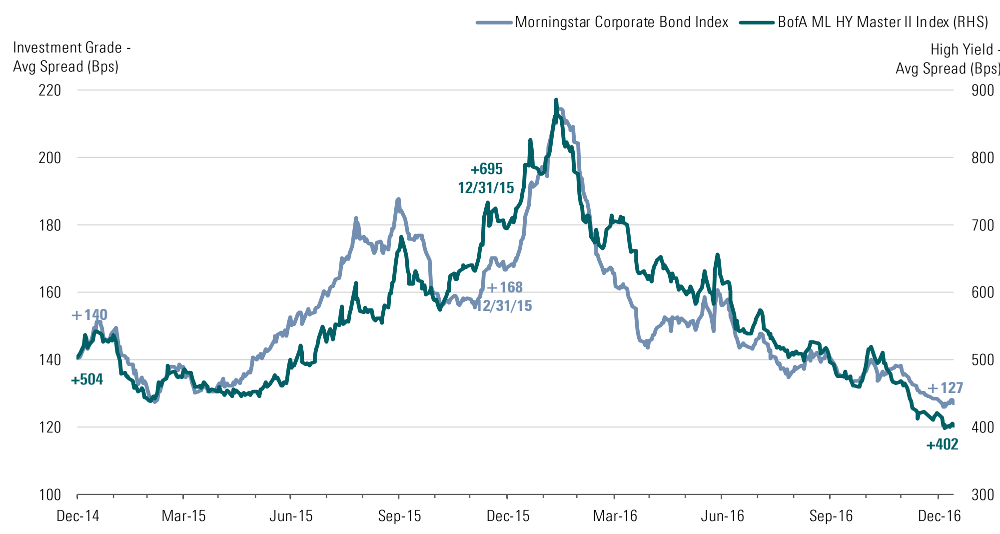
Credit Market Insights

High-Yield Bonds Continue to Outperform Investment Grade

The ongoing investor preference for higher-beta assets that has driven the market since oil prices bottomed in February 2016 has continued thus far in 2017. Since the beginning of the year, the average corporate credit spread of the Morningstar Corporate Bond Index, our proxy for the investment-grade bond market, has tightened 1 basis point, whereas in the high-yield market, the credit spread of the Bank of America Merrill Lynch High Yield Master Index has tightened 19 basis points. Between tightening credit spreads and a slight rebound in Treasury bonds, fixed-income securities have performed well. Year to date, the Morningstar Corporate Bond Index has risen 0.53% and the high-yield index has risen 1.08%. However, risk assets with higher betas have risen even higher; for example, the S&P 500 has risen 1.6% over the same period. The impetus for the movement has been the market's expectation that the economy is entering a reflationary environment based on renewed economic activity, which will be spurred by fiscal stimulus and tax reductions. In addition, oil prices and industrial commodities have not only stabilized but are trending upward.

At these levels, both investment-grade and high-yield corporate bonds are trading much tighter than their long-term averages, and the S&P 500 is only slightly below its all-time high. Currently, the average spread of the Morningstar Corporate Bond Index is +127, which is 41 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 +402, which is 178 basis points tighter than its long-term average of +580 basis points since the end of 1996. As a point of reference, the tightest that the Morningstar Corporate Bond Index has ever traded was +80 in February 2007, and the tightest the high-yield index registered was +241 in June 2007.

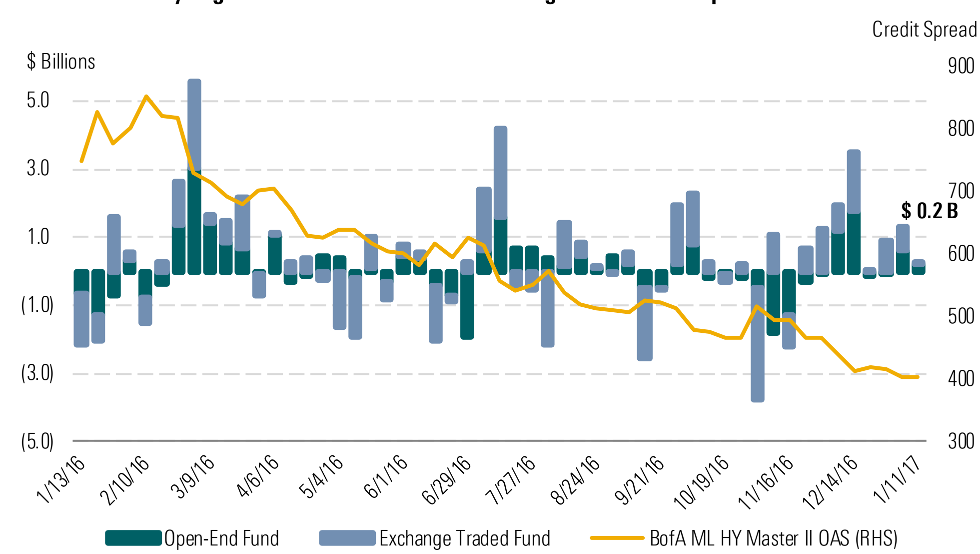
Corporate Bond Credit Spreads



Source: Morningstar,Inc., BofA Merrill Lynch Global Indexes. Data as of 01/13/2017.

The tone of corporate bond market ended the week on a positive note as earnings season swung into gear, starting with the major global banks. Fourth-quarter results were favorable, as earnings were bolstered by modestly higher net interest income, significant reductions in operating costs, and lower credit losses. Among the banks we rate, JPMorgan Chase (rating: A-, stable) reported solid fourth-quarter results, including net income available to common shareholders of $6.2 billion, which was 26.1% higher than a year ago and 7.7% higher sequentially. Compared with the relatively weak year-earlier quarter, results were supported by modestly higher net interest income revenue. However, the bottom line benefited more from lower expenses across the board. Operating costs decreased 3.0% year over year, while credit costs decreased an impressive 30.9%. Relative to the more robust results reported in the third quarter, total revenue decreased 5.2%, but fourth-quarter results were aided by lower operating, credit, and tax expenses. Bank of America (rating: BBB, stable) reported generally solid fourth-quarter results that were considerably higher than relatively weak results reported a year ago but modestly below those reported in the prior quarter. While our credit assessment is strengthened modestly by a third consecutive quarter of respectable results, Bank of America's profitability remains at modest levels and continues to trail key peers.

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 Jan. 13, 2017
(000,000s $ unless otherwise noted)

Issuer			Issue				
Name	Ticker	Morningstar Corporate Rating	Size	Coupon	Description	Maturity	Approx Spread to US Treasuries
General Mills	GIS	BBB+	$750	3.20%	Senior Unsecured	2027	+88
General Motors Financials	GM	BBB-[1]	$1,250	3.45%	Senior Unsecured	2022	+160
General Motors Financials	GM	BBB-[1]	$500	L+155	Senior Unsecured	2022	NA
General Motors Financials	GM	BBB-[1]	$750	4.35%	Senior Unsecured	2027	+200
Met Life Global Funding	MET	BBB-[1]	$250	0.30%	Senior Secired	2026	+24
Stryker	SYK	A+	$500	1.80%	Senior Unsecured	2019	+65

Source: Advantage Data, Company SEC fillings.

(1) Morningstar's issuer credit rating is assigned at the holding company level.

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-**	**4,620**	**6.8**	**127**	**(1)**	**(1)**	**0.52**	**0.52**
FINANCIAL	**A-**	**1,423**	**5.5**	**122**	**(1)**	**(1)**	**0.35**	**0.35**
Bank	A-	881	5.0	123	1	1	0.24	0.24
Finance	A	254	5.7	117	(3)	(3)	0.54	0.54
Insurance	A	209	7.7	119	(3)	(3)	0.74	0.74
REITs	BBB+	71	6.0	131	(4)	(4)	0.63	0.63
INDUSTRIAL	**A-**	**2,648**	**7.4**	**129**	**(1)**	**(1)**	**0.55**	**0.55**
Basic Industries	BBB+	229	7.5	173	(7)	(7)	1.18	1.18
Consumer Products	A-	285	7.5	108	1	1	0.38	0.38
Energy	A-	409	7.0	156	0	0	0.58	0.58
Healthcare	A-	406	7.6	115	0	0	0.39	0.39
Manufacturing	A-	377	6.2	107	(3)	(3)	0.49	0.49
Media	BBB+	193	8.2	157	(2)	(2)	0.65	0.65
Retail	A-	165	8.0	112	4	4	0.10	0.10
Technology	A+	271	7.1	102	(3)	(3)	0.65	0.65
Telecom	BBB+	150	8.3	157	(1)	(1)	0.62	0.62
Transportation	BBB+	122	9.1	131	(2)	(2)	0.89	0.89
UTILITY	**BBB+**	**505**	**8.3**	**146**	**(6)**	**(6)**	**1.11**	**1.11**
Electric Utilities	A-	303	8.7	132	(3)	(3)	0.98	0.98
Gas Pipelines	BBB+	194	7.8	167	(9)	(9)	1.32	1.32
Rating Bucket								
AAA Bucket		100	7.6	67	1	1	0.41	0.41
AA Bucket		536	5.9	82	(1)	(1)	0.41	0.41
A Bucket		1,764	6.8	106	(0)	(0)	0.43	0.43
BBB Bucket		2,220	7.0	162	(2)	(2)	0.64	0.64
Term Bucket								
1-4	A-	1,440	2.3	89	(4)	(4)	0.20	0.20
4-7	A-	1,136	4.6	114	(2)	(2)	0.39	0.39
7-10	A-	874	7.1	138	1	1	0.45	0.45
10PLUS	A-	1,170	13.6	176	1	1	1.07	1.07

Data as of 01/13/2017

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

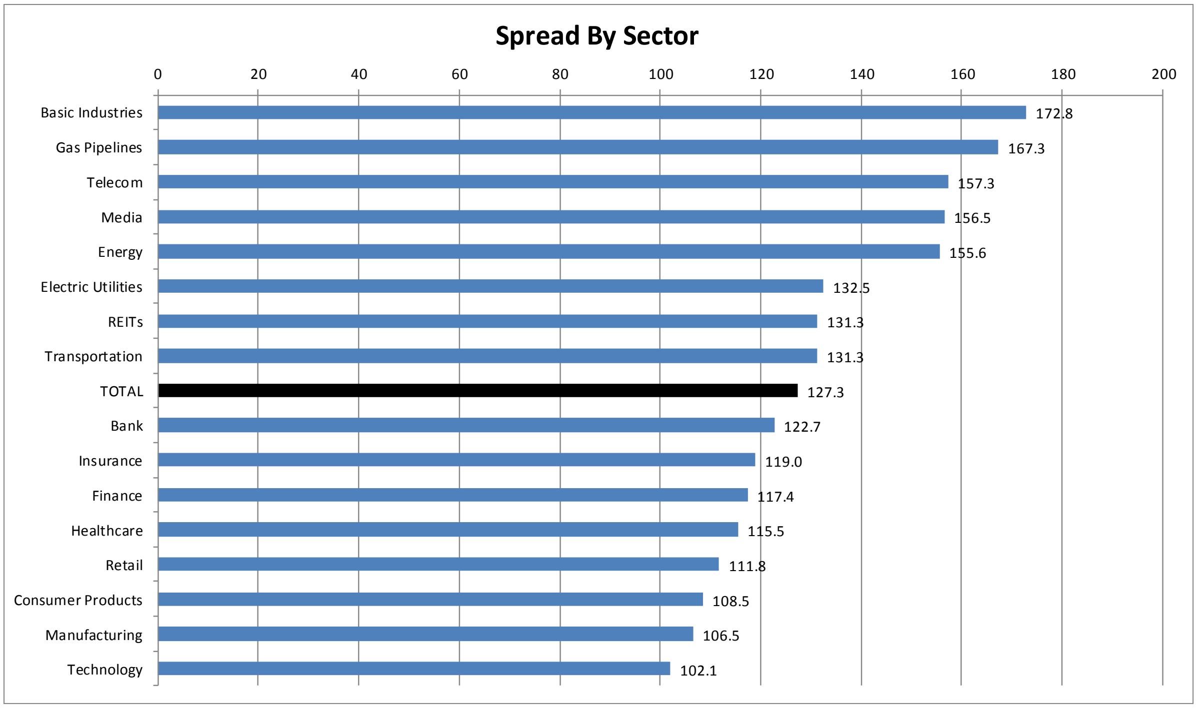


Exhibit 4 Morningstar, Inc. Corporate Bond Index YTD Spread Change

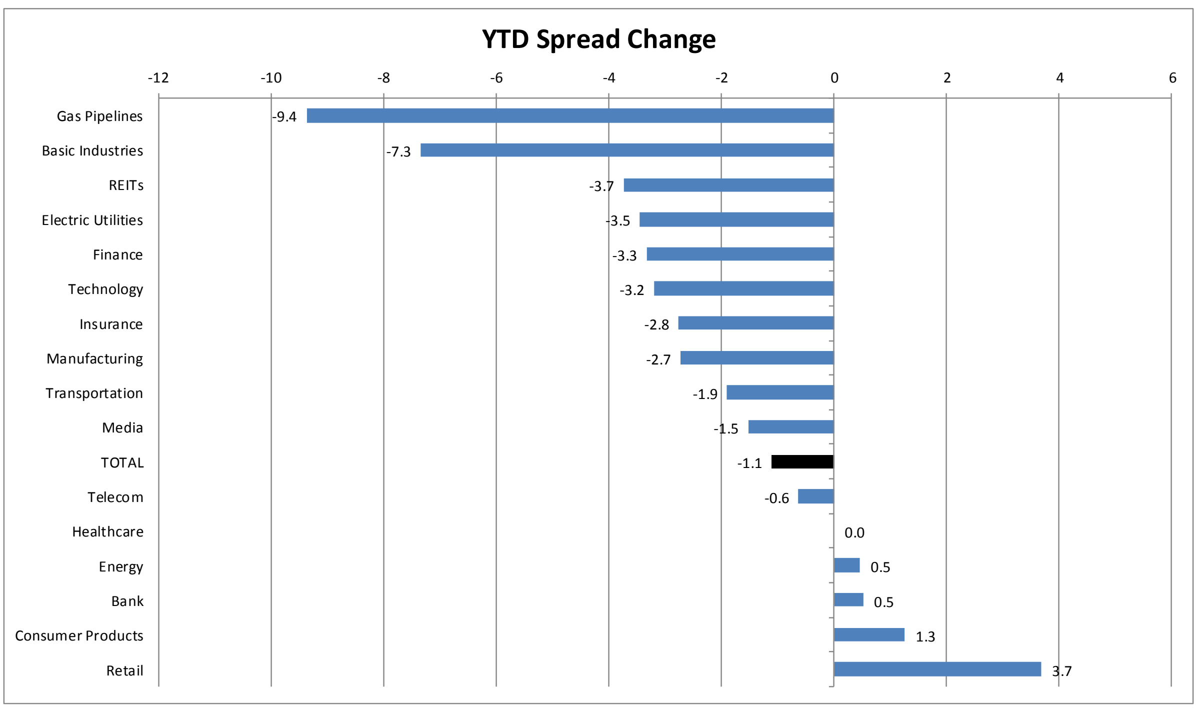
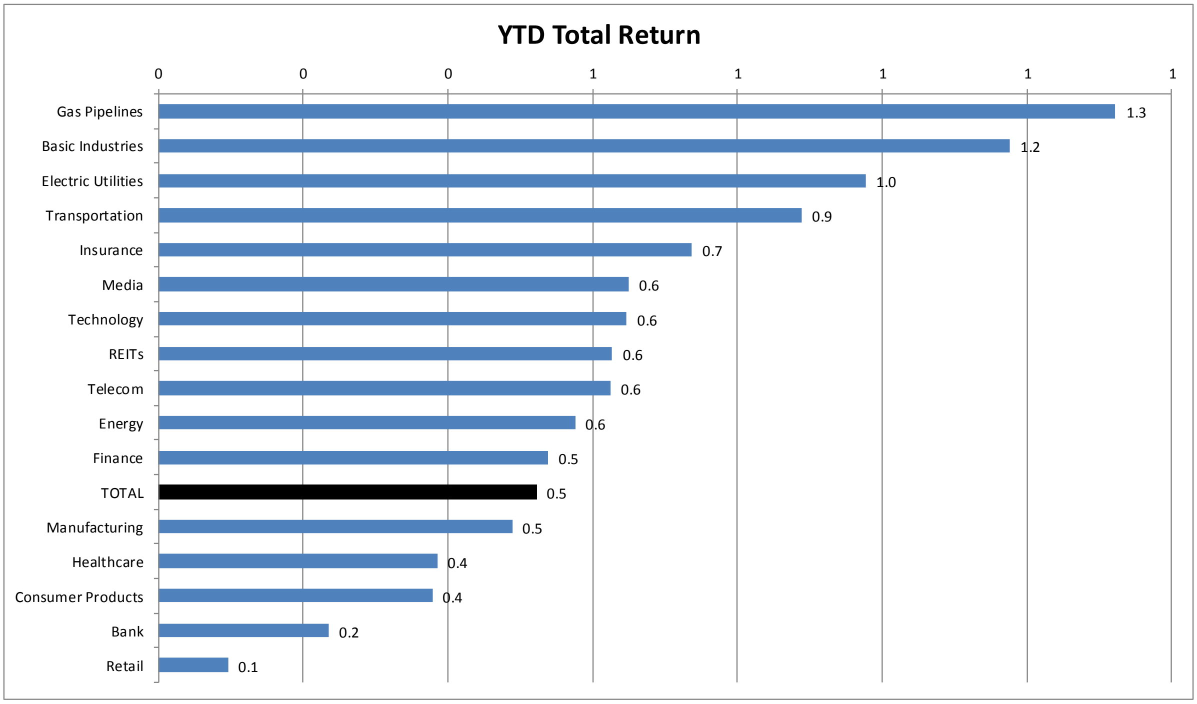


Exhibit 5 Morningstar, Inc. Corporate Bond Index YTD Return



Credit Rating Actions

► Rating Affirmations

Issuer/Ticker	Current Issuer Credit Rating	Previous Issuer Credit Rating
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Pioneer Natural Resources PXD	BBB-	BBB-
Scripps Networks SNI	BBB+	BBB+

Zimmer Biomet's Rating Affirmed at BBB+; Initiating Negative Outlook

Morningstar Credit Ratings, LLC is affirming its credit rating on Zimmer Biomet Holdings Inc at BBB+ and initiating a negative outlook on weaker-than-expected credit fundamentals following the merger. We had assumed Zimmer would deleverage quickly after its merger with Biomet in mid-2015. Instead, the company's leverage has remained inflated on acquisition and shareholder return activities in 2016. If the firm does not make meaningful progress on deleveraging in the next year or so, we would consider downgrading our rating, which is reflected in our negative outlook.

Our BBB+ credit rating on Zimmer Biomet reflects substantial competitive advantages after the mid-2015 merger of Zimmer and Biomet, which contribute to a strong Business Risk pillar. Positively for our Business Risk pillar, we think Zimmer Biomet has enhanced its competitive advantages and scale by combining the two organizations. Market share in orthopedic devices typically stays extremely steady, which we believe stems primarily from the substantial switching costs for surgeons associated with orthopedic tool sets. The extensive instrumentation used to prepare bones and install implants is specific to each supplier, and the learning curve to become proficient in using one company's instrumentation is steep. Additionally, relative to other procedures, orthopedic surgeon skill and experience play an outsized role in clinical outcomes for patients. These issues leave surgeons reluctant to train and master multiple instrumentation systems. Switching to another system would require taking time out for training, developing a relationship with a new sales rep, and working less efficiently during the early period of mastering another vendor's tools, which could raise risks for patients and reduce the number of procedures and income for the surgeon. This dynamic has helped top-tier orthopedic firms like Zimmer Biomet dig wide moats, according to Morningstar Research Services, LLC.

Without substantial deleveraging progress after the Biomet merger so far though, the company's Cash Flow Cushion, Solvency Score, and Distance to Default pillars appear weak for the BBB+ rating category. Since the merger, Zimmer Biomet has not shied away from tuck-in acquisitions and even some share repurchases, which has kept leverage higher than we anticipated when initially analyzing the firm's potential deleveraging after the merger. At the end of September, we estimate gross debt/EBITDA stood around 4 times, and the company currently aims to reach gross debt/EBITDA of 2.5 times by the end of 2018.

However, we currently have a negative outlook on the company's rating. If Zimmer Biomet does not make material progress on deleveraging, we would consider downgrading the rating in the next year or so. For example, since late October, the firm's stock has fallen substantially, cutting into the equity cushion underneath its debt obligations, on supply chain management problems in a few high-growth product sets. Also, some regulatory issues have emerged from recent manufacturing facility inspections. If weak operating fundamentals like that or capital allocation decisions further delay deleveraging, we would consider a downgrade. While we see few catalysts to upgrade our rating in the near future, an upgrade is possible if the firm deleverages substantially below its target, which could boost its Cash Flow Cushion, Solvency Score, and Distance to Default pillars.

Becton Dickinson's BBB+ Rating Affirmed; Stable Outlook Initiated

Morningstar Credit Ratings, LLC is affirming its BBB+ credit rating on Becton, Dickinson and Co and establishing a stable outlook. BD's credit profile benefits from its top-tier positions in a variety of attractive medical instrument and equipment businesses. However, its acquisition of CareFusion keeps financial leverage much higher than historical norms. With the firm closing in on its current leverage target and the potential for management to allocate capital for the benefit of shareholders rather than further deleveraging in the near future, we view the firm's rating trajectory as merely stable for now.

Our rating on Becton Dickinson reflects its ongoing advantages in medical instrumentation and equipment and its recent deleveraging after the CareFusion acquisition. BD scores well in its Business Risk pillar, given the essential nature of its medical technology and scale advantages. As the largest manufacturer of needles and syringes, BD's scale advantages keep competitors at bay in this price-sensitive part of the healthcare industry. BD also competes in various diagnostic, flow cytometry, and cell-imaging businesses, which we view as attractive niches. The CareFusion merger primarily added an infusion pump business that competes in a virtual oligopoly within developed markets and has significant expansion opportunities in emerging markets.

BD primarily used debt financing to close the CareFusion acquisition in 2015. Initially after that combination, debt stood at $13.2 billion. In 2016, BD actively deleveraged by repaying debt and growing profits; as of September, total debt stood at $11.6 billion, or gross debt/EBITDA in the mid-3s and net leverage around 3 times. The company's share-repurchase program remains suspended until the firm reaches its gross debt/EBITDA goal of 3.0 times, which management expects to achieve by March 2017. However, even with this ongoing deleveraging, we project BD's Cash Flow Cushion and Solvency Score pillars will only remain at moderate levels given the substantial debt still on its balance sheet and related cash obligations.

This substantial debt constrains BD's credit profile, in our opinion, and with the firm looking set to maintain rather than reduce its leverage after meeting its target, our outlook is currently stable. However, if the firm continues to meaningfully reduce its debt leverage, we would consider upgrading. Net leverage would likely need to be sustained around 2.0 times, though, to positively affect our Solvency Score and Cash Flow Cushion pillars enough for us to upgrade. We would consider a downgrade if the firm increases debt leverage to make returns to shareholders or another large acquisition.

Baxter's Credit Rating Affirmed at A-, Positive Outlook Initiated

Morningstar Credit Ratings, LLC is affirming its A- credit rating on Baxter International Inc and establishing a positive outlook. Our rating continues to reflect the firm's significant advantages in various medical equipment and therapeutic businesses along with its robust financial position. Given recent deleveraging, we have established a positive outlook on our rating, although Baxter has not committed to operating near recent low leverage levels in the long run.

Our rating on Baxter remains A-, reflecting its solid Business Risk profile and easily manageable debt leverage after eliminating its stake in Baxalta, its biopharmaceutical spin-off that recently merged with Shire. Immediately after separating from Baxalta in 2015, Baxter's size and diversification declined along with Morningstar Research Services, LLC's moat rating (narrow) relative to the combined entity (wide). However, we still view the firm as advantaged in a variety of medical technology businesses. Specifically, Baxter remains a leading provider of dialysis equipment, including a dominant position in peritoneal dialysis and a solid position in hemodialysis. Baxter also provides a variety of IV pumps and related solutions to help caregivers manage hospitalized patients. The company is a top-tier provider of anesthesia agents, as well. Even in the businesses that we do not view as particularly advantaged (such as compounding, contract manufacturing, and injectable generic drugs), Baxter benefits from synergies with its other manufacturing and marketing operations.

Along with those positive Business Risk factors, Baxter's financial health improved in 2016 after eliminating its stake in Baxalta. In 2016, Baxter was able to redeem more than half of its debt outstanding, which led to better Cash Flow Cushion, Solvency Score, and Distance to Default pillars, primarily by exchanging its Baxalta shares for outstanding debt. Also, Baxter's other refinancing activities helped extend its remaining maturity schedule. As of September, the firm owed $2.8 billion in debt, or just 1.5 times EBITDA, and a nearly net neutral debt position when considering its $2.6 billion of cash. However, management recently discussed boosting net leverage to pursue tuck-in acquisitions and returns to shareholders, which keeps us cautious with our rating for now.

Our positive outlook reflects the firm's recent deleveraging and its ability to operate with a more conservative balance sheet in the long run. If Baxter looks likely to keep its net leverage between its current net neutral position and about 1 times EBITDA, our Cash Flow Cushion, Solvency Score, and Distance to Default pillars could remain strong enough for us to consider an upgrade. To downgrade our rating, Baxter would probably have to increase net leverage above 2 times for the long run, which would have negative effects on several of our rating pillars. We could envision this scenario if Baxter were to pursue a large, debt-funded acquisition or large returns to shareholders.

Pioneer Natural Resources' Rating Affirmed at BBB-; Positive Outlook on Rising Energy Prices

Morningstar Credit Ratings, LLC is affirming the BBB- corporate credit rating on Pioneer Natural Resources and assigning a positive outlook. Our rating reflects Pioneer's large inventory of repeatable, low-risk, oil-weighted drilling opportunities in the Permian Basin of Texas; estimated organic production growth of about 15% per year for the next few years; the cyclicality of exploration and production (upstream) activity; cost- and production growth-related synergies coming about from the recent acquisition of acreage in the Midland segment of the Permian Basin; and excellent liquidity and low debt leverage. The revised rating outlook incorporates our expectation that operating margins will gradually increase in light of cyclically rebounding oil and natural gas price realizations over the next several quarters. Our rating also reflects the view of Morningstar Research Services, LLC that Pioneer does not benefit from an economic moat.

When the sharp decline in oil and gas prices began in the fall of 2014, Pioneer refocused its resources on the best acreage and undertook aggressive cost-reduction measures. These actions include ongoing field and capital efficiency gains, centralization of activities, and capture of deflation in exploration and production, or E&P, supply-chain inputs, resulting in a steadily declining production cost per barrel of oil equivalent. The issuance of 19.8 million shares of common stock during the first half of 2016 for cash proceeds of $2.5 billion helped fund 2016 investing activities, including the purchase of producing acreage in the Permian Basin and redemption of long-term debt.

We regard Pioneer's liquidity as excellent. Pioneer ended the September quarter with $2.6 billion in cash and equivalents and full availability on its $1.5 billion unsecured revolving credit facility. Pioneer has guided for E&P capital expenditures to be $2.1 billion in 2016, which is about $100 million lower than the prior year, and has a preliminary midpoint estimate of $2.75 billion for 2017. After capital expenditures, dividends, acquisitions and divestments, we estimate negative free cash flow for Pioneer in 2016, about neutral in 2017, and positive thereafter.

In our base-case forecast, we estimate the company's EBITDAX margin gradually rising to 70% by 2020, after bottoming at about 60% in 2016. Commensurate with this, we estimate the ratio of total debt/trailing EBITDAX to have peaked at about 2 times in 2016, declining back to around 1 time by 2018. Further, we estimate net leverage to have peaked near 1 time in 2016 and to remain below 1 time thereafter. 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 approximately 2%-4% above the futures price curve (as of Jan. 5) through 2020. For oil (WTI basis), our 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 have incorporated $500 million net proceeds in 2016 from the final installment for the sale of the Eagle Ford Shale midstream business. We assume no asset sales after 2016. The company realized $553 million in proceeds from asset divestitures in 2015 and $877 million in 2014.

Our positive outlook indicates a possible increase in Pioneer's credit rating, largely predicated on the gradual improvement in oil and gas supply/demand fundamentals and, therefore, higher price realizations. This would allow company operating margins and cash flow to expand commensurate with our forecast. A rating upgrade would also assume no significant increase in financial leverage from the current level for an extended period. Although we do not anticipate this, we may consider a downgrade of the credit rating if energy prices sharply decline, squeezing margins, or if the company undertakes a large acquisition, increasing financial leverage.

Scripps' Rating Affirmed at BBB+; Outlook Stable

Morningstar Credit Ratings, LLC is affirming its corporate credit rating on Scripps Networks Interactive at BBB+ and maintaining a stable outlook. Our rating on Scripps primarily reflects the impact of debt-funded acquisitions, which weakened its Cash Flow Cushion. Meanwhile, we view its Business Risk as moderate. Morningstar Research Services, LLC assigns the company a narrow economic moat, which it attributes to Scripps' attractive cable properties and high barriers to entry in producing content. Its narrow moat allows the company to generate solid returns on invested capital which, in turn, support a strong Solvency Score.

However, we view its portfolio as more niche-focused than its larger media peers, which may position Scripps less attractively for emerging video distribution models compared with more-diversified peers. The company also depends on advertising for about 70% of its domestic revenue.

With the acquisition of Polish network TVN in 2015, Scripps now derives 15% of its revenue from outside the U.S. at much lower profit margins compared with its domestic business. We believe the outlook for non-U.S. margins may improve to the extent the company can rationalize its cost base in its new markets. Domestically, the company operates six cable channels and owns 98% of the content that airs on its channels. Its channels collectively reach over 90 million households subscribing to basic cable in the U.S. Two of its channels, HGTV and Food Network regularly rank within the top 25 networks in the U.S., particularly appealing to upscale females, age 24-54—an attractive category for advertisers.

Scripps reported total debt at the end of September at $3.6 billion, supported by $330 million of cash and investments. Debt is up $1.7 billion over the past year, driven by $500 million of acquisitions in 2015 as well as $1.5 billion for share repurchases. Since the end of 2015, management has cut back dramatically on share repurchases, applying this cash flow to paying down debt. We calculate that net debt ended the September quarter at 2.4 times EBITDA compared with year-end 2015's level of 3.0 times. Accounting for the maturity of $500 million of 2.7% senior notes due in December 2016, management expects to report total debt of around $3.1 billion at the end of the December quarter, which we believe implies year-end net debt of around 2.2 times trailing 12-month EBITDA, using our calculation.

We project annual revenue growth of around 3% over the next five years, with operating margins holding at about 37%. Our rating outlook is stable and assumes that management will continue to make progress at reducing leverage, which should contribute to a stronger Cash Flow Cushion. We do not currently anticipate an upgrade of the rating given the company's lower content diversity and dependence on advertising. We may consider a downgrade of the rating if the company resumes a more aggressive capital allocation strategy or if it raises additional debt to pursue acquisitions.

Recent Notes Published by Credit Analysts

General Mills Issuing New 10-Year Senior Notes to Refinance Maturing Debt

Market News and Data

General Mills Inc (rating: BBB+, stable) is reportedly in the market with an issuance of new 10-year senior notes. Proceeds from the notes are expected to refinance the company's $1.0 billion 5.7% notes due Feb. 15, 2017. Comparables are Campbell Soup Co (rating: A-) and Kellogg Co (rating: BBB, stable). According to pricing services Advantage Data, price indications for selected senior notes of General Mills and its comparables are as follows:

General Mill's existing 3.65% notes due 2024 are indicated at +81 basis points,
Campbell's 3.30% notes due 2025 are indicated at +101 basis points;
Kellogg's 3.25% notes due 2026 are indicated at +114 basis points.

According to data from Morningstar, Inc., the A- tranche of Morningstar Corporate Index is 115 basis points, while the BBB+ tranche of the index is +147 basis points. Historically, General Mills has priced tighter than its rating category, and the consumer products sector has priced tighter than the index as a whole.

MCR Credit Risk Assessment

Our BBB+ rating on General Mills reflects a strong Business Risk score offset by comparatively weaker Cash Flow Cushion. Though General Mills has a slightly stronger Business Risk score due to less uncertainty reflecting the wider breadth of its portfolio and greater diversification, both Campbell's Cash Flow Cushion and Solvency Score is one notch better than General Mills. Meanwhile, Kellogg's Business Risk is two notches weaker than General Mills, and its Cash Flow Cushion and Solvency are about the same.

Our rating outlook for General Mills is stable, as it is a leading packaged food company with roughly 30% share of the domestic ready-to-eat cereal aisle, 26% yogurt market share, 70% share of refrigerated baked goods, and more than 40% share of grain snacks. Based on strong shelf presence and brand power that drives traffic, General Mills is a valued partner for retailers. As with many firms within the packaged food sector with mature categories, there is a continuous focus on efficiency and cost savings. We believe that General Mills' multiyear restructuring initiatives to increase efficiency by consolidating and eliminating excess production capacity and redirecting those savings into high-growth areas are sound strategies to restore long-term sustainable growth for the company. These efforts, combined with new, innovative, and organic products in cereal and yogurt under its Annie's, Yoplait, and Liberté brands align well with consumer demand and could spur consumption and drive operating earnings higher.

General Mills' total debt/adjusted EBITDA for the latest 12 months ended Nov. 27, 2016, was 3.0 times, and adjusted EBITDA/interest expense was approximately 11 times. Barring acquisitions, these credit measures are expected to remain stable. For comparison, Campbell's debt/adjusted EBITDA was approximately 2.0 times, and Kellogg's was 3.0 times for their respective latest 12-months' period ended.

General Mills' total debt was $10.3 billion at Nov. 27, 2016, and its cash balance was $809.7 million, a substantial portion of which resided offshore and will be used to finance foreign operations. Additional liquidity and financial flexibility is provided by General Mills' committed credit facilities totaling $2.9 billion, composed of a $2.7 billion facility expiring May 2021 and a $200 million facility expiring June 2019. The credit facilities contain a financial covenant that requires the company to maintain a fixed charge coverage ratio of at least 2.5 times, which we view as easily achievable.

Valeant Begins Divestitures to Reduce Debt

MCR Credit Risk Assessment

Valeant Pharmaceuticals International Inc (rating: B, negative outlook) has announced its intention to divest its Dendreon division and three skin-care brands in order to ease its large debt burden. The firm plans to sell the skin-care brands--CeraVe, AcneFree, and Ambi--to L'Oreal for $1.3 billion and its Dendreon unit to Sanpower Group for approximately $820 million. We expect no hiccups in the regulatory process, and management sees both transactions closing in the first half of 2017. Valeant will use the proceeds to reduce its heavy debt load left over from its prior aggressive merger and acquisition strategy, which stood at more than $30 billion at the end of September 2016. We had suspected that assets sales could be the cleanest way to shore up Valeant's balance sheet, and believe that additional significant divestitures may ensue to further decrease the debt level. We view the actions as positive, as elevated gross leverage, which currently nears 7 times, will fall by around one half of a turn following the divestments and subsequent debt repayment. Moreover, management targets decreasing its secured debt balance, which should provide more cushion under recently amended financial covenants in its credit agreement that requires secured leverage to remain at 2.5 times or less.

We remain most concerned about Valeant's lowered earnings expectations for both 2016 and 2017, as they could make it difficult for the firm to maintain compliance with the interest-coverage covenant in its credit agreement that calls for the ratio to stay at 2.0 times or more. As a reminder, management reduced its 2016 guidance at its third-quarter conference call to revenue of $9.55 billion-$9.65 billion, down from $9.90 billion-$10.10 billion previously. The company also reduced its adjusted EBITDA guidance to $4.25 billion-$4.35 billion, from $4.80 billion-$4.95 billion previously. Additionally, the firm noted that it expects 2017 results to trend lower than 2016 on continued declines of neurology products that are losing exclusivity and a potential drop off in its generics business.

Market Data

We compare Valeant's bonds with key peers that are also rated B with a negative outlook in the healthcare industry, which includes specialty pharmaceutical firm Endo International PLC (rating: B, negative outlook) and healthcare provider Tenet Healthcare Corp (rating: B, negative outlook). In the approximate five-year maturity bucket, Valeant's bonds are recently indicated much wider than its key peers, including about 325 basis points wider than Endo's indicated level and roughly 350 basis points wider than Tenet's bonds, which can be seen as follows:

Valeant's 7.50% notes due in 2021 indicated at 86.25, yield to maturity of 11.49% and spread to maturity of +966 basis points;

Endo's 5.75% notes due in 2022 indicated at 89.63, yield to maturity of 8.33% and spread to maturity of +641 basis points;
Tenet's 8.13% notes due in 2022 traded at 100.00, yield to maturity of 8.12% and spread to maturity of +615 basis points.

JPMorgan Reports Solid 4Q Results Driven by Lower Credit Costs and Higher Trading Revenue
MCR Credit Risk Assessment:
JPMorgan Chase (rating: A-, stable outlook) reported solid fourth-quarter results, including net income available to common shareholders of $6.2 billion, which was 26.1% higher than a year ago and 7.7% higher sequentially. Compared with the relatively weak year-earlier quarter, results were supported by modestly higher net interest income revenue. However, the bottom line benefited more from lower expenses across the board. Operating costs decreased 3.0% year over year, while credit costs decreased an impressive 30.9%. Relative to the more robust results reported in the third quarter, total revenue decreased 5.2%, but fourth-quarter results were aided by lower operating, credit, and tax expenses in the fourth quarter. By our calculations, annualized return on common equity for the quarter was solid at 10.8%, which compared favorably to 10.1% in the prior quarter and 8.9% a year earlier. For calendar 2016, return on common equity was solid at 10.1%, which was modestly below 10.3% and 10.6% reported in the two prior years. These results compare favorably to lower-rated global banking peer Bank of America (rating: BBB, stable outlook), which reported earlier in the day an annualized return on common equity for the quarter of 7.1% and 6.8% for the year. At the segment level, strong trading revenue in fixed income, up 30.9% year over year, and equity, up 8.1%, contributed to earnings for the corporate and investment bank segment that was 96.3% higher than a year ago and 17.8% above the prior quarter.

JPMorgan's balance sheet notched steady improvement during the quarter. Due mainly to lower risk-weighted assets, Regulatory capital measures generally improved, with the common equity Tier 1 ratio finishing the year at 12.4% compared with 12.0% in the prior quarter and 11.8% a year earlier. While JPMorgan's regulatory capital measures compare favorably to global banking peers, the bank's tangible common equity/tangible assets ratio of 7.4% (our calculations) trails a peer average around 8% and detracts from our credit opinion. Nonperforming loans represented 0.77% of totals at year-end, which was modestly below prior-quarter levels and in line with those seen a year ago. Loan-loss reserves remained solid representing 200% of nonperforming loans, which compares favorably with peers.

Market News and Data:
We compare JPMorgan with large global U.S. banks including Citigroup, Bank of America, and Wells Fargo. Because of the company's presence in investment banking and investment management, we also consider Goldman Sachs and Morgan Stanley.

JPMorgan's 2.95% senior notes due in 2026 are indicated by pricing service Advantage Data at +121 basis points over the nearest Treasury, while 10-year notes of Citigroup (rating: A-, stable outlook) are indicated at +141 basis points. Similar maturity notes of Wells Fargo (rating: A, negative outlook) are indicated at +123 basis points. Among lower-rated companies, Goldman Sachs' (rating: BBB+) 3.75% notes due in 2026 are indicated at +141 basis points, while Morgan Stanley's (rating: BBB, stable outlook) 3.125% notes due in 2026 are indicated at +139 basis points. By comparison, Bank of America's 3.50% notes due in 2026 are indicated at +132 basis points.

Bank of America Reports 4Q Results Consistent With Recent Quarterly Trends

MCR Credit Risk Assessment:

Bank of America (rating: BBB, stable outlook) reported generally solid fourth-quarter results that were considerably higher than relatively weak results reported a year ago but modestly below those reported in the prior quarter. While our credit assessment is strengthened modestly by a third consecutive quarter of respectable results, Bank of America's profitability remains at modest levels and continues to trail key peers. By our calculations, annualized return on common equity for the quarter was 7.1%. For calendar 2016, return on common equity was 6.8% while return on average assets was 0.7%. These results trail average levels for global banking peers, especially JPMorgan Chase (rating: A-, stable outlook), which reported annualized return on common equity for the quarter of 10.8%, 10.0% for the year, and return on average assets of 0.9%. Total revenue increased modestly relative to the year-earlier quarter due mainly to higher interest income, which benefited from higher net interest margin. Other than Global Markets, which benefited from higher fixed-income trading revenue (12.2%) and equity trading (7.5%), revenue at most of the reporting segments improved only slightly. Net income available to common shareholders of $4.3 billion reported during the quarter was positively affected by lower costs across the board. Operating expenses decreased 6.1% year over year due mainly to lower legal and restructuring costs. Bank of America reported a still mediocre efficiency ratio of 66% for 2016, which improved relative to 70% reported in the prior year. Results also benefited from lower credit costs, which decreased 4.4%, and lower tax expense, which decreased 8.1%.

Bank of America's balance sheet notched incremental improvement during the quarter. Nonperforming loans finished the quarter representing 0.85% of total loans, 7 basis points below the prior quarter and 19 basis points below the year-earlier quarter. Loan-loss reserve coverage improved 15.3% year over year and finished the quarter representing around 146% of nonperforming loans. However, current levels trail key peers such as JPMorgan and Citigroup (rating: A-, stable outlook), which have reported reserve coverage levels around 200% in the most recent quarter.

Market News and Data:

We compare Bank of America with large global U.S. banks including Citigroup, JPMorgan Chase, and Wells Fargo. Because of the company's presence in investment banking and investment management, we also consider Goldman Sachs and Morgan Stanley. Bank of America's 3.50% senior notes due in 2026 are indicated by pricing service Advantage Data Inc. at +132 basis points over the nearest Treasury, while 10-year notes of Morgan Stanley (rating: BBB, stable outlook) are indicated at +129 basis points. Among higher-rated companies, Goldman Sachs' (rating: BBB+, stable outlook) 3.75% notes due in 2026 are indicated at +141 basis points, while Citigroup's 3.40% notes due in 2026 are indicated at +142 basis points. By comparison, JPMorgan's 2.95% due in 2026 are indicated at +121 basis points, while 10-year notes of higher-rated Wells Fargo (rating: A, negative outlook) are indicated at +123 basis points.

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