MORNINGSTAR®

Morningstar Corporate Credit Research Highlights

Macroeconomic data takes center stage.

Morningstar Credit Research
7 August 2017

Contents

2 Credit Market Insights
10 Credit Rating Actions
13 Recent Notes Published by Credit Analysts
43 Credit Contacts

Credit Market Insights

- Market Data and Insights

Credit Rating Actions

- Rating affirmations

Issuer/Ticker	Current Issuer Credit Rating	Previous Issuer Credit Rating
Comcast **CMCSA**	A-	A-
Discovery Communications **DISCA**	BBB/UR-	BBB
Scripps Network Interactive **SNI**	BBB+/UR-	BBB+

Recent Notes Published by Credit Analysts

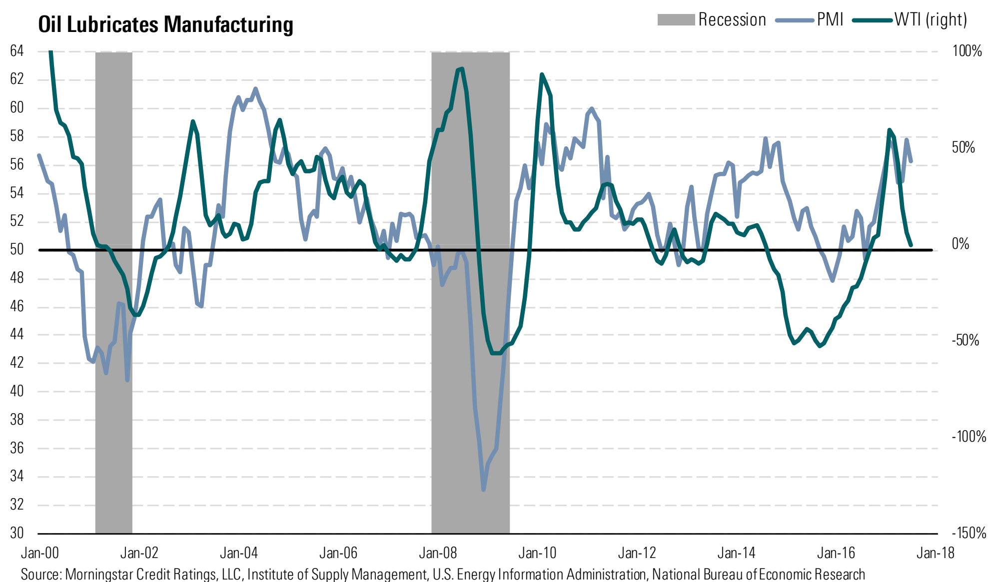
- **LabCorp** to Acquire Chiltern and Delay Deleveraging
- **Celgene** Issuing Debt Maturing in 2021, Which Could Be Used to Refinance August Debt Maturity
- **Fresenius** Maintains 2017 Outlook Despite Margin Headwinds
- **Pfizer** Posts Flat Top-Line Operational Growth in 2Q; Shareholder Return Isolated to Dividend
- **Sprint**'s Long-Term Operating Risks Remains High Despite Improving Profitability
- **Martin Marietta Materials** Reports 2Q EBITDA Growth of 9.7% Year Over Year
- Strong Performance Continues for **Allstate** Through 1H
- **Frontier**'s EBITDA Margin Weakens in 2Q as Revenue Decline Offsets Progress on Cost Reductions
- **Cardinal Health** Gives Weak Guidance for Fiscal 2018 and Completes Leverage-Increasing Acquisition
- Net Leverage Rises in **DaVita**'s 2Q, Reinforcing Our Negative Outlook
- **Owens & Minor** Experiences Tough 2Q and Completes Leverage-Increasing Acquisition
- Uptick in Mac Sales Drives Fiscal 3Q Revenue Growth for **Apple** Ahead of Fall IPhone Launches
- **Hologic**'s 2017 Outlook Disappoints on Cynosure Woes, but Net Leverage Ticks Down Further
- **Shire** Announces Strategic Options for Neuroscience Business; Debt Reduction Remains Top Priority
- **AmerisourceBergen** Deleverages Moderately in 3Q, but Acquisition Appetite Appears Strong
- **AIG** Reports Solid Earnings Growth Through 1H, but Reserve Position Still Troubling
- Decline in Legacy Revenue Drags on **CenturyLink**'s 2Q Operating Performance
- **Becton Dickinson** Preps for Bard Acquisition by End of 2017
- **CA** Reports Solid Fiscal 1Q on Growth in New Sales and Higher Free Cash Flow
- **Allergan** Slightly Increases 2017 Sales Guidance After a Solid 2Q; Debt Balance Falling
- **Teva** Significantly Revamps Outlook After Difficult 2Q; Deleveraging Efforts Pressured
- Despite Sequential Decline in 2Q Oil and Gas Pricing, **Apache** Still Generates Free Cash Flow
- More

Credit Market Insights

Macroeconomic Data Takes Center Stage

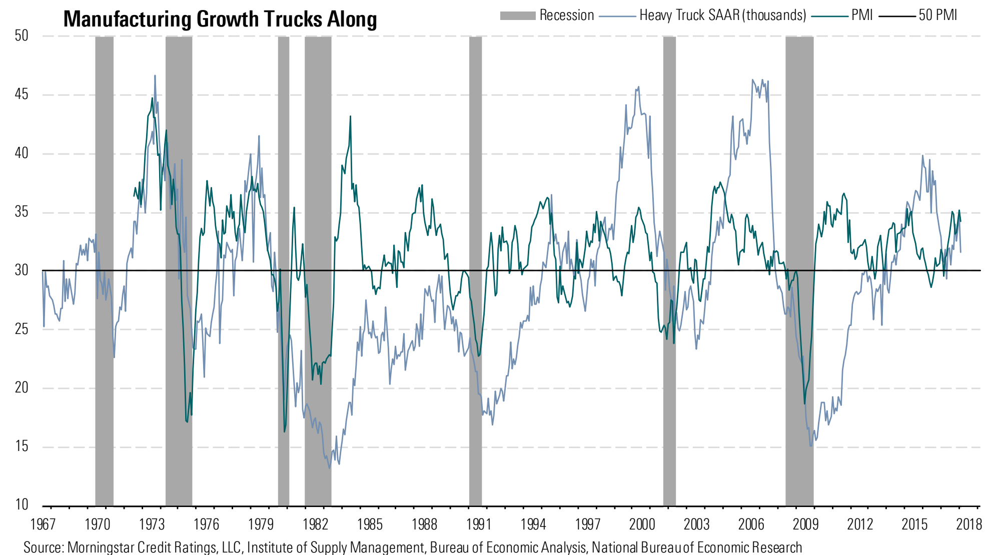
Despite the announced merger of two media firms, macroeconomic reports stole the show last week, although earnings releases continued to roll in with weakness in the healthcare sector. The highly anticipated nonfarm payroll report noted that the U.S. economy added 209,000 jobs last month, besting estimates of a 183,000 gain, and registered a 4.3% unemployment rate. Overall, 2017's average monthly growth of 184,000 jobs is on par with 2016's average monthly gain of 187,000. However, we consider employment figures—especially the unemployment rate—to be at best coincident indicators because they provide little indication of the future travel of economic activity. Two indicators that we think provide a better economic prognostication are the Institute of Supply Management's Purchasing Managers Index and monthly heavy-truck sales, both of which were reported this month.

July's PMI reading of 56.3 was down 1.5 points from June's but consistent with the year-to-date average reading of 56.4. As we explored in our February report "Diversified Industrials: A Tale of Two Tax Reforms," there is a strong positive relationship with yearly changes in the rolling three-month average West Texas Intermediate price and the PMI. This relationship stems from the massive increase in U.S. oil and gas production and the subsequent growing energy exposure among diversified industrials. We think looking at the combination provides a better lens through which to analyze future developments. Although July's WTI oil prices posted their strongest monthly increase since April 2016, the rate of increase has decelerated since May. Moreover, the current $50 per barrel price is consistent with levels seen in the back half of 2016, suggesting that manufacturing growth may slow somewhat over the coming quarters.



Source: Morningstar Credit Ratings, LLC, Institute of Supply Management, U.S. Energy Information Administration, National Bureau of Economic Research

Another indicator we think has proved its mettle is heavy-truck sales, although it is commonly downshifted in importance because of the release of monthly auto sales. A notoriously volatile series, heavy-truck sales have been a decent leading indicator heading into recessions and a coincident to lagging on the way out. The July figure increased a modest 2.4% to a seasonally adjusted annualized rate of 379,000 units. This is approximately 10% above the historical average and down from the average annualized rate of 392,000 units experienced since the start of the year.



Source: Morningstar Credit Ratings, LLC, Institute of Supply Management, Bureau of Economic Analysis, National Bureau of Economic Research

We see decent prospects for the manufacturing landscape, but the pace of growth may still be underwhelming. An interesting dynamic of late is the U.S. dollar's tumultuous turn down. This week, the U.S. dollar index hit a 15-month low against its rival currencies. The dollar weakness could stem the tide of foreign-currency headwinds and help propel reported results.

The latest in the content-is-king saga is the announcement that Discovery Communications Inc (rating: BBB/UR-) is acquiring Scripps Networks Interactive Inc (rating: BBB+/UR-) in a stock-and-cash transaction that values the owner of Food Network and HGTV at an enterprise value of $14.6 billion. Following the deal, we placed both firms under review negative. Elsewhere, earnings reports continued to trickle in last week with notable weakness in healthcare, including at Cardinal Health Inc (rating: A/UR-), Teva Pharmaceutical Industries LTD (rating: BBB-, stable), DaVita Inc (rating, BB+, negative), and Hologic Inc (ratings: BB+, positive).

In the corporate bond market, the average spread of the Morningstar Corporate Bond Index (our proxy for the investment-grade bond market) remains near the tightest levels of the year, although the index widened 1 basis point to end the week at +107. In the high-yield market, the BofA Merrill Lynch High Yield Master Index widened as well, closing the week at +363 basis points, +4 basis points wider than last week's ending level of +359. In the equity market, the S&P 500 was up slightly, the Dow Jones hit a record high, and volatility continued to sink to new lows.

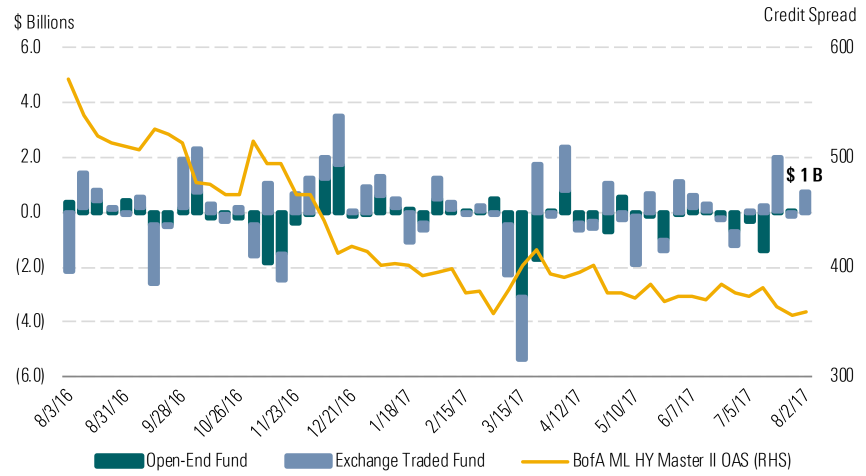
Corporate Bond Credit Spreads

Source: Morningstar,Inc., BofA Merrill Lynch Global Indexes. Data as of 08/03/2017.

Bond issuance was down meaningfully versus the previous week with the absence of AT&T Inc's (rating: BBB/UR-) $22.5 billion, seven-part transaction that was the third-largest deal in corporate bond history. We note that automakers General Motors Co (rating: BBB, stable) and Ford Motor Co (rating: BBB, stable) successfully issued $4.5 billion in multitranche paper despite monthly auto sales figures that all but confirm U.S. light-vehicle sales peaked last year.

Fund flows in the high-yield market increased by $1 billion this week, with nearly $750 million coming from high-yield exchange-traded funds and the remainder from open-end funds. This marks the fifth-highest inflow level this year, although it is approximately 45% of the peak weekly inflow so far in 2017, which occurred the week ended April 7.

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 Aug. 4, 2017
(000,000s $ unless otherwise noted)

Issuer			Issue				
Name	Ticker	Morningstar Corporate Rating	Size	Coupon	Description	Maturity	Approx Spread to US Treasuries
Celgene	CELG	A-	$500	2.25%	Senior Unsecured	2021	+83
Comcast	CMCSA	A-	$1,650	3.15%	Senior Unsecured	2028	+90
Comcast	CMCSA	A-	$850	4.00%	Senior Unsecured	2047	+115
Ford Motor Credit	F	BBB[1]	$600	L+108	Senior Unsecured	2022	NA
Ford Motor Credit	F	BBB[1]	$900	2.979%	Senior Unsecured	2022	+115
General Motors	GM	BBB	$500	L+80	Senior Unsecured	2020	NA
General Motors	GM	BBB	$750	4.20%	Senior Unsecured	2027	+195
General Motors	GM	BBB	$1,000	5.15%	Senior Unsecured	2038	+230
General Motors	GM	BBB	$750	5.40%	Senior Unsecured	2048	+255
Huntington National Bank	HBAN	BBB+(1)	$700	2.50%	Senior Unsecured	2022	+73
Penske Automotive	PAG	BB	$300	3.75%	Senior Unsecured	2020	+226
US Steel	X	B	$750	6.88%	Senior Unsecured	2025	+471
Verizon Communications	VZ	BBB	$3,000	4.50%	Senior Unsecured	2033	+165

Source: Bloomberg, company SEC filings
(1) Morningstar's issuer credit rating is assigned at the holding company level

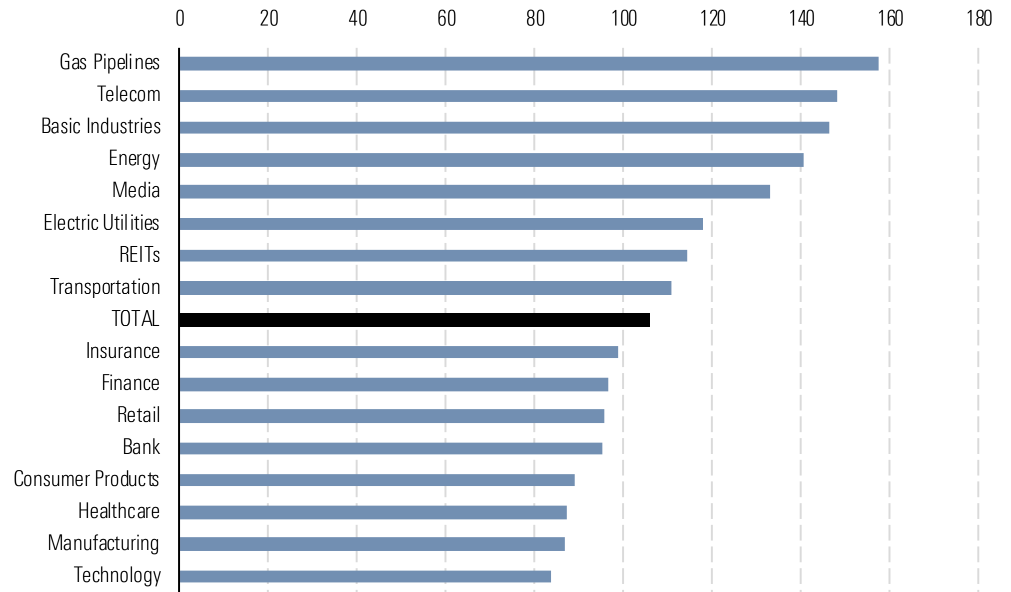
Exhibit 2 Morningstar, Inc. Corporate Bond Index Sector Summary

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-**	**4,794**	**7.0**	**107**	**2**	**(22)**	**0.14**	**4.80**
FINANCIAL	**A-**	**1,466**	**5.5**	**95**	**(0)**	**(27)**	**0.21**	**4.39**
Bank	A-	891	5.1	94	(0)	(29)	0.18	4.23
Finance	A	276	5.7	97	1	(24)	0.12	4.18
Insurance	A	214	7.9	97	(1)	(25)	0.46	5.71
REITs	BBB+	76	5.9	111	(2)	(24)	0.28	4.80
INDUSTRIAL	**A-**	**2,758**	**7.6**	**111**	**3**	**(19)**	**0.06**	**4.93**
Basic Industries	BBB+	220	7.7	145	0	(36)	0.25	7.39
Consumer Products	A-	312	7.7	91	2	(16)	0.13	4.47
Energy	A-	408	7.3	142	3	(13)	0.14	5.11
Healthcare	A-	399	7.9	92	5	(23)	(0.13)	5.46
Manufacturing	A-	412	6.3	88	2	(21)	0.08	3.88
Media	BBB+	192	8.4	139	5	(19)	(0.18)	5.48
Retail	A-	161	8.2	98	3	(10)	0.13	4.21
Technology	A+	317	7.2	87	3	(18)	0.01	4.48
Telecom	BBB+	151	8.6	151	3	(6)	0.10	4.26
Transportation	BBB+	140	9.1	111	0	(22)	0.32	5.77
UTILITY	**BBB+**	**531**	**8.6**	**131**	**(0)**	**(21)**	**0.40**	**5.92**
Electric Utilities	A-	312	9.1	113	(1)	(23)	0.51	6.07
Gas Pipelines	BBB	209	7.8	157	1	(20)	0.24	5.71
Rating Bucket								
AAA Bucket		112	8.2	58	2	(8)	0.09	4.07
AA Bucket		484	6.1	66	1	(17)	0.16	3.54
A Bucket		1,854	6.9	85	1	(21)	0.18	4.40
BBB Bucket		2,344	7.2	138	3	(26)	0.09	5.52
Term Bucket								
1-4	A-	1,520	2.4	65	1	(29)	0.04	2.19
4-7	A-	1,160	4.7	90	1	(25)	0.08	4.16
7-10	A-	895	7.1	120	3	(18)	0.12	5.21
10PLUS	A-	1,219	13.9	159	3	(15)	0.30	8.12

Data as of 08/04/2017

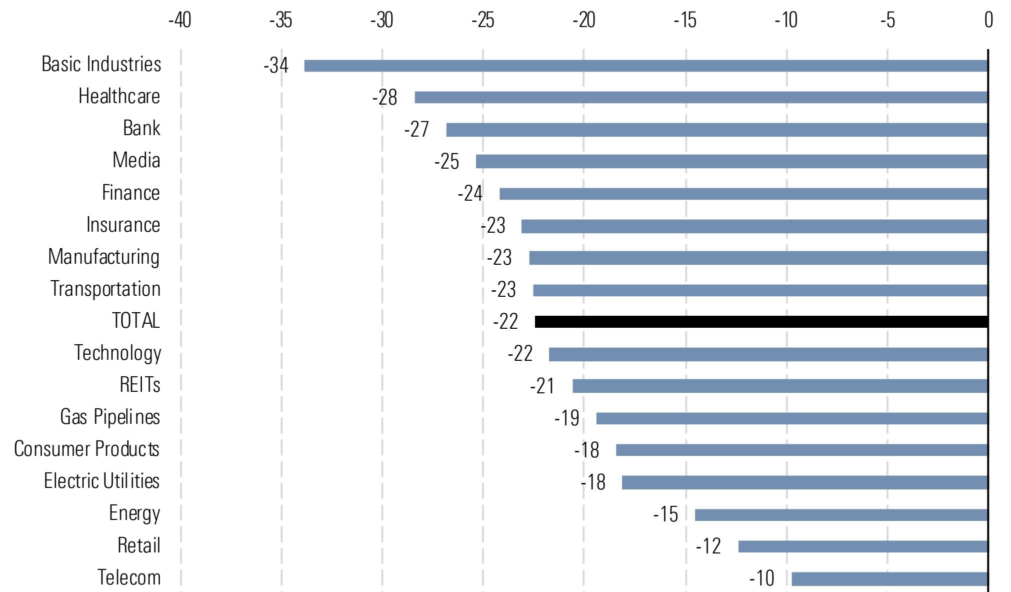
Source: Morningstar, Inc.

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



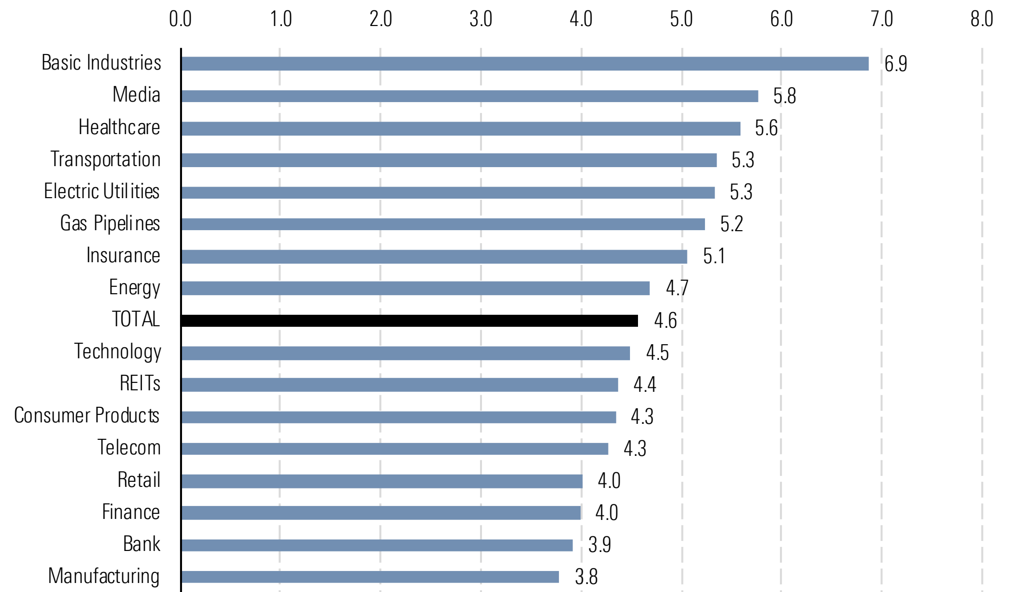
Source: Morningstar, Inc.

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



Source: Morningstar, Inc.

Exhibit 5 Morningstar, Inc. Corporate Bond Index YTD Return



Source: Morningstar, Inc.

Credit Rating Actions

Rating affirmations

Issuer/Ticker	Current Issuer Credit Rating	Previous Issuer Credit Rating
Comcast **CMCSA**	A-	A-
Discovery Communications **DISCA**	BBB/UR-	BBB
Scripps Networks Interactive **SNI**	BBB+/UR-	BBB+

Comcast's Rating Affirming at A-; Outlook Stable
Morningstar Credit Ratings, LLC is affirming its corporate credit rating on Comcast Corp. at A- and maintaining a stable outlook. The rating reflects a strong Business Risk score offset by comparatively weaker Cash Flow Cushion and Solvency pillars relative to similar-rated peers. As the second-largest U.S. pay-TV provider, Comcast remains in a very strong competitive position, in our view, despite growing competition from nontraditional video platforms. Its balance sheet also remains a consistent source of credit support despite net leverage which is a bit elevated following recent acquisitions. Management has historically adhered to a disciplined financial strategy to balance the need for a conservative leverage profile while still providing reasonable capital returns to shareholders.

Morningstar's Equity Research Group assigns Comcast a wide economic moat rating, driven by the speed and reach of the company's networks and its ability to add capacity and services through new technology at relatively modest cost. Its size and broad market footprint also provide a considerable advantage when negotiating with content providers, and its investment in NBC Universal gives Comcast access to a library of popular content. We expect the secular decline in video and pay-TV subs is likely to continue in the years ahead as new delivery platforms slowly gain share, but we believe this erosion will be offset by higher demand for high-speed Internet connections.

At the end of the June quarter, we calculate that net debt was 2.2 times EBITDA, up about two tenths of a turn from a year ago. However, the company continues to produce solid free cash flow, with growth of 26% over the past 12 months while its payout ratio has declined to 70% from 91% a year ago.

Our current rating assumes revenue growth of about 3% per year over the next 5 years, with operating margin remaining stable at 20%. We also assume that management is committed to a net debt/EBITDA target in the low 2.0 times area and that the company will remain consistently profitable despite erosion in cable penetration. We may consider an upgrade if the company materially improves either its Cash Flow Cushion or solvency pillars. Conversely, we may consider a downgrade if management appears to move away from its historical focus on a conservative and flexible balance sheet.

Discovery's Rating Under Review Negative Following Scripps Merger Announcement
Morningstar Credit Ratings, LLC is affirming its BBB corporate credit rating on Discovery Communications but placing it under review negative following the July 31 announcement of an agreement to acquire Scripps Networks Interactive (rating: BBB+/UR-). Discovery will pay $90 a share for a total enterprise valuation of $14.6 billion through a combination of cash and stock. The financing is targeted to include around $8 billion of cash consideration with the balance in Discovery common stock.

We project the merger will have no material impact on Discovery's Business Risk pillar as the risk factors for both issuers are similar. Morningstar's Equity Research Group maintains narrow economic moat assessments for both Discovery and Scripps, based on their respective content portfolios and significant cost barriers to entry for new entrants in the media business. However, we do expect the merger to significantly weaken both Cash Flow Cushion and Solvency Score as a result of incremental debt as well as some dilution of initial return on invested capital levels as a result of the increase in goodwill.

The acquisition of Scripps will bring its leading lifestyle brands Food Network and HGTV to Discovery's nonscripted, documentary-style content portfolio, which includes Animal Planet, TLC, and its flagship network Discovery channel. Discovery estimates the combined content portfolios will represent one fifth of domestic ad-supported television viewers and reach 3 billion subscribers across more than 220 countries. This includes 800 million pay-TV subscribers in the U.S. and Canada. Strategically, the acquisition of Scripps may help Discovery to increase the number of female viewers to its platform as Scripps networks have historically skewed heavily toward this demographic while much of Discovery's content tends to skew toward male viewers. The additional scale from combining the two portfolios may also increase Discovery's negotiating leverage with its distribution partners, though we still expect long-term pressure on fees. Discovery may also generate value from increasing the exposure of Scripps' U.S.-focused brands in markets outside the U.S., where it has historically found marketing success with its own programming. However, the combination does not appear to reduce Discovery's focus on nonscripted, reality-based programming or its dependence on advertising, which we believe will contribute around 54% of revenue on a combined basis following the merger.

Discovery reported net debt of $8.1 billion in the second quarter, or 3.3 times its trailing four-quarter EBITDA by our calculations, while Scripps reported its debt at $2.9 billion, or 2.0 times EBITDA. We project the pro forma net debt/EBITDA of the combined companies to approach 4.8 times at the time of the merger. Management has suspended its share repurchase plan and has pledged all available free cash flow to reduce net leverage below 3.5 times by early 2020. We project pro forma combined free cash flow for the firms to grow to around $2.0 billion by 2018, which we believe is consistent with management's debt reduction target.

Our credit review will focus on interim performance of the two firms prior to the merger close, which is anticipated in early 2018. We will also consider the combined company's long-term competitive positioning in the advertising-supported television market within the context of an industry trend toward nontraditional content distribution channels. If the merger is completed as proposed, we may downgrade Discovery's credit rating. If the deal is not completed, we will re-evaluate our rating in the context of Discovery's financial strength and operating condition at that time.

Scripps' BBB+ Rating Under Review Negative on Agreement to Merge With Discovery

Morningstar Credit Ratings, LLC is affirming its BBB+ corporate credit rating on Scripps Networks Interactive Inc. (rating: BBB+/UR-) but placing the rating under review negative following the July 31 announcement of the agreement for Scripps to be acquired by Discovery Communications Inc. (rating: BBB/UR-). Discovery will pay $90 per Scripps share through a combination of cash and stock for a total

enterprise valuation of $14.6 billion. The proposed financing package is targeted to include around $8 billion of cash consideration with the balance paid in Discovery common stock.

We project the merger will have no material impact on Scripps' Business Risk pillar as the factors for both issuers are similar. Morningstar's Equity Research Group maintains narrow economic moat assessments for both Discovery and Scripps, based on their respective media portfolios and significant cost barriers to entry for new entrants to the media business. However, we do expect the merger to significantly weaken both the Cash Flow Cushion and Solvency Score as a result of incremental debt as well as some dilution of initial return on invested capital levels as a result of the increase in goodwill.

The acquisition will bring Scripps' leading brands, including Food Network and HGTV, to Discovery's nonscripted, documentary-style portfolio, which includes Animal Planet, TLC, and its flagship Discovery channel. Discovery estimates the combined content portfolios will represent one-fifth of domestic ad-supported television viewers and reach 3 billion subscribers across more than 220 countries. This includes 800 million pay-TV subscribers in the United States and Canada. Strategically, the acquisition may help Discovery to increase the number of female viewers to its platform as Scripps' networks have historically skewed more heavily toward this demographic.

The additional scale from combining the two portfolios may increase Discovery's negotiating leverage with its distribution partners, though we still expect long-term pressure on fees. Discovery may generate value from increasing the exposure of Scripps' U.S.-focused brands in markets outside the U.S., where it has historically found success with its own programming. However, the combination does not appear to reduce Discovery's focus on nonscripted, reality-based programming or its dependence on advertising, which we believe will contribute around 54% of revenue on a combined basis following the merger.

Scripps reported net debt of $2.9 billion in the second quarter, or 2.0 times its trailing four-quarter EBITDA, while Discovery reported its debt at $8.1 billion, or 3.3 times EBITDA. We project pro forma net debt/EBITDA to approach 4.8 times at the time of the merger. However, Discovery's management has suspended its share-repurchase plan and has pledged all available free cash flow to reduce net leverage below 3.5 times by early 2020. We expect pro forma combined free cash flow to be around $2.0 billion by 2018, which appears to be consistent with Discovery's debt reduction target.

Our credit review will focus on interim performance of the two firms before the merger's close, which is anticipated in early 2018. We will also consider the combined company's long-term competitive positioning in the advertising-supported television market in the context of an industry trend toward nontraditional content distribution channels. If the merger is completed as proposed, we may downgrade Scripps' credit rating. If the deal is not completed, we will re-evaluate our rating in the context of Scripps' financial strength and operating condition at that time.

Recent Notes Published by Credit Analysts

LabCorp to Acquire Chiltern and Delay Deleveraging Further

MCR Credit Risk Assessment

On July 31, Laboratory Corp of America Holdings (rating: BBB+, stable) announced plans to acquire contract research organization, or CRO, Chiltern, for $1.2 billion by the end of 2017. Strategically, we think the combination makes sense and are pleased to see LabCorp pursue more of a tuck-in acquisition than a larger merger like the one rumored earlier in 2017--Pharmaceutical Product Development LLC (not rated), which probably would have been valued around $8 billion. With the Chiltern transaction and some existing debt redemption, management projects gross leverage will tick up only slightly, but we have a negative view of the ongoing delay in LabCorp's deleveraging, as creditors have been waiting for the company to deleverage toward its target since the early 2015 Covance combination.

Strategically, the acquisition of Chiltern will expand LabCorp's reach in the CRO field. While specific growth rates were not revealed for the private target, management views the combination as positive to its growth prospects in the CRO business. Also, LabCorp found Chiltern's focus on oncology indications attractive. Geographically, the deal should help expand LabCorp's reach, particularly in the Asia-Pacific and Eastern Europe regions. LabCorp expects Chiltern to generate around $550 million in sales and $95 million in EBITDA in 2017.

From a credit perspective, management does not expect this acquisition to change its current financial health substantially. As of June, the company owed $6.1 billion in debt, or 3.2 times adjusted EBITDA. With the expected debt-financed acquisition of Chiltern and redemption of some existing debt obligations, management expects gross leverage to tick up to only 3.3 times on a pro forma basis by the time the deal closes in late 2017. However, this ongoing delay in deleveraging is disappointing for creditors and a far cry from the plan to return to 2.5 times gross debt/EBITDA by year-end 2016 when it initially announced the 2015 Covance transaction. On the call, LabCorp management expressed a desire to deleverage following the Chiltern transaction. However, the company views its former 2.5 times target as a floor and appears likely to operate between 2.5 times and 3.0 times in the long run, or slightly higher to where key peer Quest Diagnostics Inc (rating: BBB+, stable) operated as of June at 2.5 times gross debt/EBITDA.

Market Data

LabCorp's closest comparable from a business and credit perspective is Quest, and their bonds recently traded roughly in line with each other's bonds. All of the following bond data is sourced from Interactive Data.

In the approximate five-year maturity bucket, bonds from these two issuers recently traded over the nearest Treasury as follows:
LabCorp's 3.20% notes due in 2022 at +85 basis points.
Quest's 4.70% notes due in 2021 at +82 basis points.

In the approximate 10-year maturity bucket, bonds from these two issuers recently traded over the nearest Treasury as follows:
LabCorp's 3.60% notes due in 2025 at +113 basis points.
Quest's 3.45% notes due in 2026 at +114 basis points.

For comparison with the roughly 10-year maturities, Morningstar Inc.'s Corporate Bond Index was recently at +94 basis points at A- and +125 basis points at BBB+.

In the approximate 30-year maturity bucket, bonds from these two issuers recently traded over the nearest Treasury as follows:
LabCorp's 4.70% notes due in 2045 at +162 basis points.
Quest's 4.70%% notes due in 2045 at +157 basis points.

Celgene Issuing Debt Maturing in 2021, Which Could Be Used to Refinance August Debt Maturity
MCR Credit Risk Assessment
Celgene's A- rating reflects solid demand for its multiple myeloma drug franchises, primarily Revlimid, which we expect to support revenue and EBITDA increasing by double-digit rates, compounded annually over the next five years. This positive trend was recently demonstrated by strong operating results in the second quarter, as total revenue increased 19%, led by strong demand for cancer medicines Revlimid (up 20%) and Pomalyst (rose 23%) and the autoimmune-disorder treatment Otezla (jumped 49%). Our expectation for solid operational performance is also backstopped by Celgene's advancing research portfolio as the firm awaits the potential approval of IDHIFA (enasidenib), a treatment for acute myeloid leukemia that has a review deadline of Aug. 30, 2017 from the FDA. Also, before the end of the year, the firm hopes to begin pivotal trials for four cancer projects--CC-122, bb2121, JCAR017, and marizomib. Celgene has some time to commercialize its research pipeline, including the potential blockbuster ozanimod for treatment of ulcerative colitis and multiple sclerosis, as direct generic competition to Revlimid is anticipated on a limited basis in March 2022 and fully in January 2026, per a patent settlement with Teva.

Market Data
Celgene Corp (rating: A-, stable) is in the market with a proposed offering of fixed-coupon maturities maturing in 2021. According to a preliminary prospectus filed on Aug. 1, net proceeds will be used for general corporate purposes, including refinancing existing indebtedness, internal investment, and share repurchasing. The firm specifically mentioned the repayment of 1.90% senior notes maturing in August 2017 ($500 million outstanding) as a potential use of proceeds. Celgene was a featured issuer in the most recent edition of Morningstar Credit Ratings' Potential New Issue Supply report published July 20.

For nearest comparison to Celgene's notes, we look to higher-rated peers Biogen Inc (rating: A, stable) and Amgen Inc (rating: A, stable). Within this comparable group, Celgene's five-year bonds trade close to those of its peers. All bond data is sourced from Interactive Data.

In the approximate five-year maturity bucket, bonds from these issuers recently traded over the nearest Treasury as follows:
Celgene's 3.25% notes due 2022 at +69 basis points.
Amgen's 2.70% notes due 2022 at +66 basis points.
Biogen's 3.63% notes due 2022 at +70 basis points.

Fresenius Maintains 2017 Outlook Despite Margin Headwinds

MCR Credit Risk Assessment

On Aug. 1, top-tier dialysis service provider, Fresenius Medical Care AG & Co. KGaA (rating: BBB-, stable) turned in operating results that allowed it to maintain its outlook for 2017, despite headwinds on its bottom line. The company's net leverage also continued to tick down, reinforcing our investment-grade rating on the firm. Also, during the quarter, the company was able to refinance its credit agreement, making its capital structure more consistent with its investment-grade status.

Fresenius turned in solid second-quarter operating results, albeit with margin pressure, and management maintained its financial outlook for the full year. Excluding the effects of the VA agreement for outstanding payments, revenue grew 9% in constant currency to EUR 4.5 billion. On an organic basis, Fresenius' services segment grew a solid 6% year over year, including same market growth of 3%. The firm's coordinated care segment grew at a high pace of 19% organically year over year. Fresenius' product segment (around 18% of sales) continues to create synergies with the dialysis business, in our opinion, and grew at a healthy 8% rate in constant currency. Notably, constant currency growth in the EMEA (6%), Asia-Pacific (15%), and Latin America (10%) regions offset weakness in the North American market (flat), which suffered from capital spending pullbacks at independent, smaller service providers. Management does not believe it has lost market share to competitors in North America, though, and expects those product sales eventually will be captured in future periods. However, the company's adjusted operating income grew only 2% year over year in constant currency to EUR 591 million, or a margin of 13.2%, which is down about 100 basis points year over year. Management blamed that margin contraction mostly on foreign currency translation effects, particularly the euro's strength versus key currencies like the U.S. dollar (around 70 basis points), higher personnel costs (around 20 basis points), and higher bad debt expense, particularly in its care coordination segment. Management did not change its outlook for 2017, though, and continues to expect roughly high-single-digit growth in both revenue (8%-10%) and net income (7%-9%) in 2017 on a constant currency basis.

From a credit perspective, the story remains positive for Fresenius. As of June, net debt/EBITDA ticked down to 2.2 times from 2.3 times in March. Also, during the quarter, the company amended its $4 billion credit agreement. Specifically, the credit agreement is now unsecured, reflecting the firm's investment-grade rating, and will be ranked pari passu with future bond issues. Also, the firm extended the maturities on its credit agreement to 2020 and 2022 from 2019 previously.

Market Data

In the healthcare services sector, we compare bonds from Fresenius to bonds from DaVita Inc. (rating: BB+, negative), and HCA Holdings Inc. (rating: BB, stable). However, given its new investment-grade

status, Fresenius' bonds trade well tight of these firms, and we include Walgreens Boots Alliance Inc. (rating: BBB-, stable) as a similarly rated healthcare firm albeit in a different sector. All of the following bond data was sourced from Interactive Data:

Fresenius 4.75% notes due 2024 at +139 basis points.
Walgreens 3.45% notes due 2026 at +119 basis points.
DaVita 5.00% notes due 2025 at +275 basis points.
HCA 5.38% notes due 2025 at +233 basis points.

For comparison with the roughly 10-year maturities, Morningstar Inc.'s Corporate Bond Index was recently at +164 basis points at BBB-.

Pfizer Posts Flat Top-Line Operational Growth in 2Q; Shareholder Return Isolated to Dividend
MCR Credit Risk Assessment
Pfizer Inc (rating: AA-, stable) saw flat top-line growth operationally in the second quarter as announced on its Aug. 1 conference call. Despite solid revenue performance of Pfizer's Innovative Health segment that grew 9% operationally in the quarter propelled by 66% global growth of Ibrance (cancer), a 50% increase in contribution from Eliquis (blood thinner), and a 55% rise in Xeljanz (auto immune disorders), continued pressure from the Essential Health businesses (down 12% operationally) flattened growth. Excluding the influence of foreign exchange swings and the contribution from Hospira Infusion Systems (divested in February), total revenue increased 2% in the second quarter. While foreign currency changes may have a lighter impact on sales during 2017, the firm maintained revenue guidance of $52 billion to $54 billion in 2017. We think that Pfizer may sustain sales growth in the low single digits compounded annually, including a hit from a moderate patent cliff in 2018-19 due to the U.S. patent lapses of Lyrica (10% of sales) and Viagra (3% of sales). The expectation depends on sustained strong demand for newer therapies, notably Xeljanz and Ibrance, together with commercialization of the late-stage pipeline, including expanded indications for the new immuno-oncology medicine Bavencio.

From a credit perspective, Pfizer's balance sheet remains stretched after significant acquisitions over the past few years, including the purchases of Anacor, Hospira, and Medivation that together totaled $34 billion. With no balance sheet details on Pfizer's quarterly conference call, we anticipate that its debt load at the end of the second quarter remained relatively consistent with the first quarter level of $44 billion or gross leverage around 2 times for the trailing 12 months. Pfizer generates tremendous free cash flow that we see averaging over $15 billion annually through 2021 that could be used to term out more than $15 billion in debt maturing through 2021. However, we see increasing EBITDA paralleling revenue growth as the main way to improve leverage over the intermediate term. On a positive note, management remains on the sidelines for large acquisitions until greater clarification emerges about possible changes to U.S. tax policy. During the second quarter, shareholder returns were limited to the firm's quarterly dividend of approximately $1.9 billion after $5 billion of accelerated repurchases in the first quarter. Pfizer still had repurchase authorization of $6.4 billion as of Aug. 1.

Market Data
For closest comparison to Pfizer's bonds, we look to similarly rated companies, Roche AG (rating: AA-, stable) and Bristol-Myers Squibb & Co (rating: AA-, stable). Adjusted for bond maturities, Pfizer's 10-year bonds traded close to the bonds of this peer group. Pfizer's 10-year bonds also recently traded close to Morningstar Inc.'s Corporate Bond Index in the AA category. All of the following bond date was sourced from Interactive Data.

In the approximate 5-year maturity bucket, bonds from these issuers recently traded over the nearest Treasury as follows:
Pfizer's 3.00% notes due 2023 at +42 basis points.
Roche's 1.75% notes due 2022 at +54 basis points.
Bristol-Myers Squibb's 2.00% notes due 2022 at +31 basis points.

In the approximate 10-year maturity bucket, bonds from these issuers recently traded over the nearest Treasury as follows:
Pfizer's 2.75% notes due 2026 at +59 basis points.
Roche's 2.38% notes due 2027 at +66 basis points.
Bristol-Myers Squibb's 3.25% notes due 2027 at +67 basis points.

For comparison to the approximate 10-year maturities, Morningstar Inc.'s Corporate Bond Index is at +66 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:
Pfizer's 4.40% notes due 2044 at +101 basis points.
Roche's 4.00% notes due 2044 at +95 basis points.
Bristol-Myers Squibb's 4.50% notes due 2044 at +110 basis points.

Sprint's Long-Term Operating Risk Remains High Despite Improving Profitability
MCR Credit Risk Assessment
Sprint Corp. (rating: B, negative) reported its fiscal first quarter Aug. 1. During the quarter, Sprint added 88,000 net new postpaid phone customers, compared with a gain of 173,000 in the year-ago quarter. However, other postpaid subscribers declined 127,000 and overall postpaid churn was flat on a comparable basis sequentially and higher year over year at 1.73%. Prepaid subscribers increased 35,000, compared with a gain of 291,000 last quarter and a gain of 728,000 a year ago.

Overall revenue was up 1.8% year over year, driven by a 39% increase in equipment revenue that offset the 7% decline in service revenue. Installment-billing adjusted average revenue per user declined 1% year over year, reflecting Sprint's promotional activity during the quarter. EBITDA grew 15.1% to $3.0 billion, primarily due to a 18% decline in service costs, which absorbed a 9% increase in equipment expenses and a 1% increase in sales and administrative costs. For fiscal 2017, management now expects

adjusted EBITDA in the range of $10.8 billion-$11.2 billion and is maintaining capital expenditure guidance in the range of $3.5 billion-$4.0 billion.

Sprint's net leverage ended the quarter at 3.0 times, down from the March quarter despite a $1.5 billion increase in net debt. However, basic net leverage does not account for the substantial amount of equipment lease debt that Sprint has taken on over the past two years. We estimate lease-adjusted net leverage at 5.0 times trailing 12-month EBITDAR at the end of the June quarter, based on the most recent reported lease expense of $2.1 billion in fiscal 2016. During the past year, lease expense has grown 7% as the company has expanded its reliance on leased-assets to provide short-term liquidity. For comparison, we calculate that EBITDA, $10.8 billion over the last 12 months, was up 6% from last quarter and 23% from a year ago.

During the quarter, Sprint raised $900 million of new financing and repaid $2.1 billion of existing notes and financing, including the 9% guaranteed notes due 2018. Secured debt now represents 27% of total debt, compared with 15% a year ago. Cash and investments ended the fourth quarter at $6.8 billion, down $1.5 billion during the latest quarter on a net reduction in borrowings. Sprint's revolving credit facility remained undrawn at fiscal year-end. For the 12 months ended June, Sprint generated positive net free cash outflow of $291 million. For fiscal 2017, Sprint faces $5.1 billion of maturities, including $2.2 billion of senior notes and $2.9 million due under financing obligations.

Our B rating on Sprint reflects the company's position as one of the smaller of the four major U.S. wireless carriers. By improving customer perception of its network quality over the past two years, the carrier has made tangible progress in attracting and retaining customers without a significant sacrifice in profitability. However, its ability to maintain this rate of progress in the coming years remains uncertain, in our view. Our rating also takes into account Sprint's high levels of debt and lease obligations and the increasing reliance on short-term, working-capital financing to fund term maturities. Our negative outlook reflects our concern that Sprint is likely to face significant operating challenges to remain competitive in the years ahead, many of which may require reliable access to stable, long-term financial resources. We also expect event risk to remain high for Sprint, most recently spurred by management's public comments around potential mergers with cable operators and wireless competitors. Despite its relatively weak overall market position, we expect Sprint to remain a popular subject for the market rumor mill in the coming quarters.

Market Data

According to Interactive Data, Sprint's 7.63% senior notes due 2025 were indicated on July 31 at a yield of 5.48% to maturity (+338 basis points over the nearest Treasury), 21 basis points tighter on a spread basis from May 1. For comparison, Advanced Micro Devices' (rating: B-, stable) 7.00% notes due 2024 are indicated at a yield of 4.75% to maturity (+342 basis points over Treasuries), 57 basis points tighter from May 1, while T-Mobile (rating BB, stable) 6.50% notes due 2026 are indicated at a yield to the 2021 call of 3.87% (+230 basis points), 18 basis points tighter. Finally, we note that the Bank of America Merrill Lynch High Yield B Rated Index average spread was quoted on July 31 at +357 basis points, or 17 basis points tighter over the past three months.

Martin Marietta Materials Reports 2Q EBITDA Growth of 9.7% Year Over Year

MCR Credit Risk Assessment

Martin Marietta Materials Inc. (rating: BBB-, stable) reported second-quarter results Aug. 1 that showed EBITDA of $292 million compared with $266 million in the year-ago period. Revenue increased to $996 million from $915 million a year ago, or nearly 9%. Debt remains at approximately $1.8 billion, resulting in debt to latest 12-month EBITDA of 1.8 times. As usual, cash and equivalents on hand as of June were minimal at approximately $36 million, and free cash flow after capital expenditures for the first six months was $14 million. Dividends and share repurchases for the first half were $53 million and $100 million, respectively. For the latest 12 months, free cash flow was approximately $300 million with dividends and share repurchases at approximately $100 million and $150 million, respectively.

The company anticipates closing on its Bluegrass Materials acquisition ($1.6 billion) in the fourth quarter and will probably fund the transaction in the capital markets. The acquisition will add 23 active sites across Georgia, South Carolina, Maryland, Kentucky, and Tennessee. While the company has disclosed few financial details on the Bluegrass transaction, we estimate that after closing, the acquisition will raise debt/EBITDA to approximately 3.0 times. On the call, management said it intends to get to its targeted debt/EBITDA level of 2.0-2.5 times approximately 12-18 months after the transaction closes.

Market Data

According to Finra Trace, Martin Marietta's 4.25% notes due July 2, 2024, recently traded at a spread of +90 basis points to the nearest Treasury. Similar-rated competitor Vulcan Materials' (rating: BBB-, stable) 4.5% notes due April 1, 2025, recently traded at a spread of +96 basis points. For an index comparison, we look to the Morningstar BBB- Corporate Bond Index, which is quoted at a spread of +164 basis points.

Strong Performance Continues for Allstate Through 1H

MCR Credit Risk Assessment

Allstate (rating: BBB+, stable) posted another quarter of strong results following a good first quarter, with the insurer reporting $550 million in net income compared with $242 million in the prior-year quarter. Through the first half of 2017, profits of $1.2 billion represent a 165% increase over first-half 2016 results. The company's personal auto profit improvement plan continues to pay dividends as auto underwriting gains are attributable to higher average premiums, decreases in claims frequency, and favorable reserve development. The Allstate brand auto segment reported 5.4- and 6.9-percentage-point decreases in the combined ratio through the second quarter and first half of 2017, respectively. These factors drove the 4.2-percentage-point improvement in the company's consolidated combined ratio, reported at 95.4% through the first six months of 2017. We reiterate our view that underwriting discipline at the expense of growth in a soft, fiercely competitive market is a credit positive for Allstate, demonstrated by the ongoing outperformance in the auto line of business.

Other highlights include revenue increasing 5% to $9.6 billion in the second quarter and 6% to $19.0 billion for the six months ended 2017. Allstate Financial, the company's life segment, also reported improved results mainly due to higher net investment income linked to private equity value appreciation

in the Allstate annuities subsegment. Debt/capital was unchanged at 23% and operating EBIT/interest expense for the quarter was solid at 10.8 times, though interest coverage including preferred dividends reported at 8.0 times is roughly half a turn lower than the five-year average.

Rated peers we compare with Allstate include American International Group (rating: BBB, negative) and Travelers (rating: A-, stable). AIG was downgraded and assigned a negative outlook in March due to large, material fourth-quarter reserve charges, its capital return plan, and uncertainty surrounding its business direction following the resignation of CEO Peter Hancock. While we believe the hiring of new CEO Brian Duperreault is a step in the right direction due to his experience, discontinuation of the capital return plan, and plans for growth, we are wary about further fourth quarter reserve charges. Travelers reported earnings of $595 million for the second quarter of 2017, a 10% decrease from the prior-year quarter. Year to date, earnings decreased 11% to $1.2 billion from $1.4 billion. The decline in performance is mainly a result of elevated losses from catastrophes and continued weak performance in the personal auto segment.

Market Data
The following spreads over the nearest Treasury are provided by Interactive Data.
The Allstate 3.28% notes due in 2026 are indicated at +74 basis points.
The Travelers 3.90% notes due in 2020 are indicated at +47 basis points.
The AIG 3.90% notes due in 2026 are indicated at +116 basis points.

Frontier's EBITDA Margin Weakens in 2Q as Revenue Decline Offsets Cost-Reduction Progress
MCR Credit Risk Assessment
Frontier Communications Corp. (rating: B, negative) released its second-quarter operating results on Aug. 1, featuring a nearly 12% decline in revenue from a year ago and a 30-basis-point decline in EBITDA margin over the same period despite lower operating expenses. Subscriber erosion continued during the quarter, though at a pace in line to slightly better than last quarter. Involuntary churn (Frontier terminations) moderated as the number of delinquent account clean-ups declined from the prior two quarters. However, voluntary churn (subscriber cancels) increased sequentially from the first quarter, which management attributed to legacy DSL losses. However, the company indicated a modest sequential decrease in voluntary churn in the California, Texas, and Florida markets, which may speak to better in-market competitiveness of FiOS versus Frontier's legacy services. Meanwhile, average subscriber revenue across the portfolio declined 3.3% year over year, led by a 3.7% decline in average revenue per user, or ARPU, from CTF customers, offset by a slight increase in legacy ARPU. Results for the quarter were also affected by a $670 million charge against goodwill, which still represents a third of Frontier's asset base.

Weakness in operating performance continues to weigh on Frontier's credit metrics. Net debt ended June at $17.4 billion, or 4.2 times trailing 12-month adjusted EBITDA, as reported by the company, still above management's near-term leverage target of 4.0 times by 2019. On closer inspection of the adjustments to EBITDA, around $700 million of the amount of the calculation appears to be allocated to realized or expected cost synergies, up from $188 million implied by last quarter's disclosure. For

comparison, operating costs declined $179 million on a nominal basis in the second quarter from a year ago, suggesting $716 million of annualized savings, lending support to the higher synergy adjustment. By the end of the year, management is guiding to an unadjusted EBITDA run rate of $3.8 billion compared with $3.6 billion in the second quarter.

Total debt includes $3.6 billion of secured term loans, including a new $1.5 billion term loan due 2024. Proceeds of the loan were applied to repay existing senior notes, leaving $83 million due in the second half of 2017 and $748 million in 2018. We view the refinancing transaction as positive for liquidity, addressing near-term maturities and freeing management to focus on turning around operating performance.

Our forecast still assumes Frontier's subscriber base will begin to stabilize in the coming years, with declines in legacy services offset by growth in Internet access. However, given the stiff competition in many of its markets, stability may come at a cost to ARPU. We expect net debt to end 2017 around its current level, based on our adjusted EBITDA forecast of $4.0 billion. We may downgrade the rating further if customer losses continue to deteriorate over the next few quarters and margin pressure continues beyond next year, putting additional stress on cash flow and credit metrics while increasing the carrier's dependence on external capital.

Market Data
According to data from Finra Trace, Frontier's 6.88% notes due 2025 traded on Aug. 1. at $79.00 to yield 11.09 % to maturity (+900 basis points over the nearest Treasury). Meanwhile, its 11% notes due 2025 traded at $92.25 to yield 12.54% to maturity (+1,041 basis points). Since May 1, the yields on the Frontier notes widened 100 and 94 basis points, respectively. Among comparably-rated issues, B+ rated Dish's 7.75% notes due 2026 traded Aug. 1 at a yield to maturity of 4.91% (+272 basis points), 56 basis points wider, while B- rated Windstream Holdings 7.63% notes due 2023 traded at a yield of 10.43% (+850 basis points), 156 basis points wider since May 1. For comparison, the BofA Merrill Lynch B rated High Yield Index, now quoted at +358 basis points, is 16 basis points tighter over the past three months.

Cardinal Health Gives Weak Guidance for Fiscal 2018, Completes Leverage-Increasing Acquisition
MCR Credit Risk Assessment
Cardinal Health Inc (rating: A/UR-) reported fiscal fourth-quarter operating results Aug. 2 that exceeded consensus expectations, but the company also gave earnings guidance for fiscal 2018 that came in below expectations. For creditors, the company also completed its $6.1 billion leverage-increasing acquisition of Medtronic's patient-care, deep vein thrombosis, and nutritional insufficiency businesses earlier this week. By our estimates, Cardinal's gross leverage has increased by roughly a turn to fund this acquisition, and the company plans to keep leverage above its previous target for several years, which could result in a downgrade from us in the near future.

Fiscal fourth-quarter operating results were strong for Cardinal, but its near-term outlook includes one-time costs that look set to constrain its organic operating results in fiscal 2018. In the fourth quarter, revenue grew 5% to $33.0 billion, or slightly above consensus of $32.7 billion, and adjusted earnings per

share grew 15% to $1.31, or above consensus of $1.24. The quarterly results looked strong, with mid-single-digit growth from its two major segments, pharmaceutical distribution and medical products. However, the company's guidance for fiscal 2018, excluding the effects of the Medtronic product acquisition, called for a 5% to 10% decline in adjusted earnings of $4.85 to $5.10 from $5.40 in fiscal 2017. Management described this weak outlook for fiscal 2018 as a reset to invest in its future growth opportunities. Specifically, it plans to invest in its IT systems for the pharmaceutical business in an effort to stem the opioid crisis, and in tax-related planning. Given this weak outlook, management tried to assure investors that this was just a one-year decline by giving guidance for fiscal 2019 that revealed it expects at least $5.60 in earnings as it moves beyond these largely one-time investment activities. This guidance for fiscal 2019 does not include results from the company's Chinese pharmaceutical distribution business that it plans to exit in the near future, although they are included in its fiscal 2018 outlook. From a credit perspective, we currently do not expect this potential divestiture to benefit creditors at this point, as the company maintained its debt-reduction guidance for the next few years.

By the end of June, Cardinal had largely financed the Medtronic product acquisition that was completed on July 29, and it owed $10 billion in gross debt, or 2.7 times pro forma EBITDA by our estimates. That leverage is significantly higher than the company's 1.6 times gross leverage at the end of March and well above its previous target of 1.50-1.75 times. The company also held nearly $7 billion of cash on its balance sheet at the end of June, but most of that has been drained to complete the $6.1 billion purchase of the Medtronic businesses, meaning net leverage probably stands around 2.5 times now. Management still expects to repay about $1.5 billion of debt in the three years after the acquisition (or about $500 million annually), and it estimates gross leverage will remain above 2.0 times through June 2020. For comparison, Cardinal's key drug distribution peers recently operated with gross leverage in the mid- to high-1s.

Market Data

We use Cardinal's key drug distribution peers as its credit comparables, given their similar credit profiles and exposure to industry trends. All of the following bond data is sourced from Interactive Data.

Spreads in the approximate 5-year maturity bucket for the drug distribution sector can be seen over the nearest Treasury as follows:
Cardinal Health Inc's 2.62% notes due in 2022 at +64 basis points.
AmerisourceBergen Corp's (rating: A, stable) 3.50% notes due in 2021 at +75 basis points.
McKesson Corp's (rating: A-, stable) 2.70% notes due in 2022 at +73 basis points.

Spreads in the approximate 10-year maturity bucket for the drug distribution sector can be seen over the nearest Treasury as follows:
Cardinal Health's 3.41% notes due in 2027 at +100 basis points.
AmerisourceBergen's 3.25% notes due in 2025 at +80 basis points.
McKesson's 3.80% notes due in 2024 at +85 basis points.

For comparison, the Morningstar Corporate Bond Index is at +84 basis points in the A category and +94 basis points in the A- category.

Spreads in the approximate 30-year maturity bucket for the drug distribution sector can be seen over the nearest Treasury as follows:
Cardinal Health's 4.37% notes due in 2047 at +127 basis points.
AmerisourceBergen's 4.25% notes due in 2045 at +142 basis points.
McKesson's 4.88% notes due in 2044 at +131 basis points.

Net Leverage Rises in DaVita's 2Q, Reinforcing Our Negative Outlook
MCR Credit Risk Assessment
On Aug. 1, DaVita Inc (rating: BB+, negative) released solid second-quarter operating results that beat consensus estimates. However, with significant outflows to stakeholders and weak cash flow during the quarter, the company's net leverage rose toward the top end of its long-term target range. If these outflows and leverage trends continue, we could envision a downgrade of DaVita's credit rating in the near future, which is reflected in our negative outlook.

DaVita's second-quarter results beat consensus on both the top and bottom lines, allowing the firm to maintain its cash flow outlook for 2017. In the quarter, DaVita's net revenue grew 4% year over year to $3.9 billion, slightly above consensus of $3.8 billion. Also, the firm turned in $0.92 of adjusted earnings per share in the quarter, above consensus of $0.90 but still down about 9% year over year. By segment, the kidney care business continued to produce decent top-line results with 1% net revenue growth, but operating profits declined in line with the broader business at 9% to $391 million. Within the kidney care segment, operating profits in U.S. dialysis services were flat while U.S. ancillary services/strategic initiatives and international businesses remained drains on the segment's results. However, given the relatively low expectations for 2017, management was able to increase the bottom end of its adjusted operating income range for the kidney care business to $1.565 billion (from $1.525 billion) and kept the top end of the guidance range at $1.625 billion. The DMG segment's net revenue grew 13% year over year, but adjusted operating profits in this segment declined 23% year over year to $34 million. Given these results, management was able kept its adjusted operating income guidance for the DMG segment intact at $110 million-$150 million in 2017, although it will probably be near the bottom end of that range given recent trends. DaVita's team made no changes to its operating cash flow guidance of $1.75 billion-$1.95 billion for 2017, down from $1.96 billion in 2016.

After a brief improvement in the first quarter because of the $538 million settlement from the U.S. Department of Veterans Affairs, DaVita's net leverage increased in the second quarter to 3.4 times as of June, from 3.0 times in March. While net leverage remained within its long-term target range of 3.0-3.5 times, we would note that DaVita pushed out significant cash to stakeholders despite burning through cash in the quarter. It burned through $38 million on an unadjusted free cash flow basis in the second quarter and still pushed out $232 million for share repurchases and $73 million for distributions to noncontrolling interests. These outflows and the related increase in net leverage push DaVita to the

weak end of BB+ territory, and if these trends continue, we may downgrade our rating in the next year or two, which is reflected in our negative outlook.

Market Data
In the healthcare services sector, we compare DaVita's bonds with bonds from Fresenius Medical Care AG & Co. KGaA (rating: BBB-, stable) and HCA Healthcare Inc (rating: BB, stable). While Fresenius' bonds recently traded the tightest in this peer group with its new investment-grade status, DaVita's bonds traded wider than lower-rated HCA. All of the following bond data was sourced from Interactive Data.

DaVita's 5.00% notes due 2025 at 101.48, yield to worst of 4.70%, spread to worst of +275 basis points.
Fresenius' 4.75% notes due 2024 at 107.63, yield to worst of 3.50%, spread to worst of +138 basis points.
HCA's 5.88% notes due 2026 at 109.00, yield to worst of 4.53%, spread to worst of +233 basis points.

Owens & Minor Experiences Tough 2Q, Completes Leverage-Increasing Acquisition
MCR Credit Risk Assessment
On Aug. 2, Owens & Minor Inc. (rating: BBB/UR-) released second-quarter operating results reflecting continued weakness after a key customer loss in late 2016. Along with these results, the company announced that it recently completed the Byram Healthcare acquisition for $380 million in cash. This transaction was financed with new borrowings, and this higher leverage could cause us to downgrade our rating of Owens & Minor, which is reflected in its under review negative status.

During the second quarter, the company experienced continued declines in revenue and profits after the loss of a key customer in late 2016. Year over year, net revenue declined 9% to $2.3 billion (below consensus of $2.4 billion), and adjusted earnings per share declined 22% to $0.43 (in line with consensus). On the call, management gave its outlook through 2018 and noted some factors that revealed less optimism about its base business. Specifically, the company has seen weakness in the margins of renewals and new business wins. Also, management noted softer utilization trends in the marketplace. To offset these headwinds somewhat, the company is undergoing efforts to cut $50 million-$60 million off its cost structure this year (with full benefits expected in 2018) and $100 million-$150 million in benefits over three years. And despite the weaker outlook for its base business, the company did raise its outlook for earnings in 2017 and 2018, which now includes benefits from the Byram acquisition. In 2017, the company now expects $1.90-$2.00 per share in earnings (up from $1.75-$1.85 previously) and $2.25-$2.35 in 2018 (up from $2.05-$2.20 previously).

Earlier, Owens & Minor acquired Byram Healthcare, a distributor of medical supplies directly to patients and home-healthcare providers. While this transaction makes sense strategically, we estimate that gross debt had to nearly double to about $1.0 billion from $0.6 billion as of June just to finance the transaction. Considering this acquisition and weak operating results, we estimate gross leverage rose at least a turn and a half since the end of March to the mid-3s on a pro forma basis after the transaction. We estimate net leverage pro forma for the acquisition has risen to at least the low-3s, up from the mid-1s at the end of March. Owens & Minor operates with large lease obligations, too, and we estimate

lease-adjusted leverage has risen to at least the mid-4s from the mid-3s as of March. This increase in leverage may cut into the firm's Cash Flow Cushion, solvency score, and distance to default pillars enough to cause a downgrade, which is reflected in our under review negative status.

Market Data
Because of Owens & Minor's split-rating from the agencies, we compare Owens & Minor's bonds to bonds from Walgreens Boots Alliance Inc (rating: BBB-, stable) and below-investment grade service firms, DaVita Inc (rating: BB+, negative) and HCA Healthcare Inc (rating: BB, stable). All of the following bond data is sourced from Interactive Data.

In the approximate 10-year maturity bucket, recent trades were as follows over the nearest Treasury:
Owens & Minor's 4.38% notes due 2024 at +195 basis points.
Walgreen's 3.45% notes due 2026 at +120 basis points.
DaVita's 5.00% notes due 2025 at +273 basis points.
HCA's 5.88% notes due 2026 at +231 basis points.

For comparison to the roughly 10-year maturities, the Morningstar Corporate Bond Index is +136 basis points in the BBB category and +164 basis points in the BBB- category while the BofA Merrill Lynch BB Index was recently at +219 basis points.

Uptick in Mac Sales Drives Fiscal 3Q Revenue Growth for Apple Ahead of Fall IPhone Launches
MCR Credit Risk Assessment
Apple Inc. (rating: AA-, negative) released its fiscal third-quarter operating results on Aug. 2, featuring strong performance across all business segments, led by a pickup in volumes for Mac and iPad. Total revenue increased 7% from the prior year, while gross margin improved 50 basis points to 38.5% year over year. IPhone revenue, which accounts for 55% of total revenue, was up 3% year over year on a 2% increase in volumes, implying a modest increase in average selling price. IPad sales were up 2% from a year ago on a 15% increase in volume, including 32% growth in demand from education consumers. Meanwhile, Mac sales were up 7% on a 1% increase in volumes despite generally weak expectations for PC sales in the quarter. For the fiscal fourth quarter, we would expect Mac sales to benefit from back-to-school seasonal volumes. Apple services revenue, which includes iTunes, grew 22% and now contributes 16% of revenue. For the fiscal fourth quarter, management is guiding to midpoint revenue growth of 8% from a year ago at the midpoint of the range. Management is also guiding to gross margin remaining flat year over year at 38% and operating expenses up 11 to 12%. From this guidance, we estimate EBITDA between $14 billion and $16 billion, which indicates midpoint growth of around 5% from the prior year.

Apple reported total debt of $108 billion for the June quarter, moving total leverage slightly higher from last quarter to 1.5 times trailing 12-month EBITDA. Meanwhile, cash and investments ended the fiscal year at $261.5 billion, up $4.7 billion from last quarter, supported by $2.5 billion of cash flow after dividends, $9 billion of net new senior debt issuance and offset by $7 billion of net share repurchases. Cash and investments minus total debt ended the quarter at 2.2 times EBITDA. Domestic cash reserves

remained at 6% of the global total, down $1.2 billion year over year, while global cash and investments expanded by $30 billion. For the trailing 12 months, Apple's free cash flow increased 1% to $51.5 billion. The company paid out $43.2 billion to shareholders in the form of dividends and share repurchases, a payout ratio of 84%. We estimate that Apple has returned $158.5 billion of its $210 billion share repurchase authorization, leaving the company with $51.5 billion of remaining capacity. With no apparent foreign tax holiday legislation likely in the near term, we do not expect Apple to make any material changes to its capital policy over the next quarter.

Our AA- rating reflects Apple's moderate Business Risk and its strong Solvency and Cash Flow Cushion rankings, which are supported by high returns on invested capital and over $200 billion of overseas cash and investments. However, Apple's credit picture remains clouded by slowing revenue growth and management's focus on increasing debt to maintain large share repurchase volume. Our rating assumes average revenue growth of 8% over the next two years, buoyed by iPhone 8 sales. However, we still expect growth to moderate toward 3% or 4% for the long-term, with operating margin settling in the mid 20% area by 2021 compared with 28% in 2016. Our negative outlook takes into consideration a recent slowdown in revenue growth and the growing concentration of revenue in the iPhone product line.

Market Data

According to pricing from Interactive Data as of Aug. 1, Apple's 3.00% notes due June 2027 were indicated at +74 basis points over the nearest Treasury, 8 basis points tighter than their original issue spread on Jun. 20. Meanwhile, Apple's 2.45% notes due 2026 were indicated at a spread of +71 basis points, 2 basis points tighter since the last earnings release on May 2. For comparison, higher-rated Cisco Systems' (AA, stable) 2.50% notes due 2026 were indicated at +69 basis points, 5 basis points tighter from May 2. Meanwhile, Oracle (AA-, stable) 2.65% notes due 2026 were indicated at +72 basis points, about 13 basis points tighter from the beginning of May.

Hologic's 2017 Outlook Disappoints on Cynosure Woes, but Net Leverage Ticks Down Further

MCR Credit Risk Assessment

On Aug. 2, Hologic Inc (rating: BB+, positive) reported fiscal third-quarter results that exceeded consensus expectations. However, management pulled back on its 2017 outlook, primarily because of weakness in the recently acquired Cynosure business, calling for top-line results below consensus in fiscal 2017. Positively from a credit perspective, however, the firm's pro forma net leverage ticked lower toward its long-term leverage target, and management continued to indicate comfort with recent net leverage levels.

In the quarter, Hologic generated $806 million in revenue (slightly above consensus of $800 million), or 12% growth in constant currency and 3% growth excluding the effects of recent portfolio changes. Also, the firm turned in adjusted earnings per share of $0.50, a slight decline year over year but still above consensus of $0.49. Highlights from the quarter included the firm's molecular diagnostics division growing 10% in constant currency year over year, driven by strength in its Aptima virology products on the Panther and Tigris platforms. While Breast Health dragged with only 1% constant-currency growth in the quarter, management noted two new mammography system launches (the first since 2011) that

should help accelerate growth in future periods. We were also pleased to see positive trends emerge in Hologic's international division, which was a star performer with 11% constant-currency growth year over year (versus 1% growth in the U.S.).

Despite these positive trends, management cut its top-line outlook for the rest of fiscal 2017 because of ongoing challenges with its Cynosure business. Management now expects Hologic to generate roughly $3.0 billion of sales in fiscal 2017 versus $3.1 billion previously, and management increased the bottom end of its adjusted EPS guidance to $2.00 from $1.98 previously, while keeping its top end at $2.02. This guidance is a bit confounding, as Cynosure experienced a large sequential increase in the third quarter to $110 million, or closer to its historical revenue run rate of over $100 million each quarter from only $77 million in sales in the second quarter (which was mostly under previous management). The Hologic team explained that Cynosure beat expectations in the third quarter through its international division, and that geography may not be able to carry the business in the fourth quarter because of practitioner vacation schedules in July and August. The U.S. Cynosure business did not perform as hoped in the third quarter, and management believes its new salesforce needs time to ramp up to speed. Therefore, management expects Cynosure's revenue to fall well below the $106 million generated in the fourth quarter last year, as the firm works through its growing pains after a salesforce exodus shortly before the Cynosure acquisition was completed.

From a credit perspective, Hologic's leverage continues to tick down toward its leverage target. As of early July, Hologic's pro forma net leverage stood just above its 2.5 times long-term target, down from an adjusted 2.7 times in early April. Management commented on the call that it feels comfortable operating in with net leverage in the mid-2s, and the company looks set to continue operating on the strong end of its BB+ rating, if it maintains leverage as stated.

Shire Announces Strategic Options for Neuroscience Business; Debt Reduction Still Top Priority
MCR Credit Risk Assessment
On its quarterly conference call Aug. 3, Shire PLC (rating: BBB-, positive) announced strong operating performance in the second quarter for both its legacy operations and its acquired Baxalta business. In the quarter, total reported product sales increased by 55% and by 7% on a pro forma basis composed of legacy Shire sales rising 7% and Baxalta revenue growing by 8%. The star of the quarter was Baxalta's immunology medicines, including immunoglobulins such as Gammagard, which rose by 18%, with hematology growing 15% on a reported basis, genetic diseases increasing 2%, internal medicine increasing 15%, and neuroscience falling 3%. Despite this strong result, the firm reduced its expectation for revenues during 2017 to $14.9 billion to $15.3 billion (including royalties and other revenues) from a prior outlook of $15.1 billion to $15.5 billion due to earlier-than-expected U.S. generic competition to Lialda (gastrointestinal disorders). Operating leverage from a trimmer cost structure, as Shire already achieved $400 million in synergies from the Baxalta integration in the first year (compares to its goal of $300 million in year one and $700 million in year three), supported EBITDA margin of 43%, nearing its long term target in the mid-40s. With this performance in hand, the firm raised its earnings guidance at the midpoint by $0.10 to $14.80-$15.20 per ADS. Also of note, Shire sees its overall structure comprising two distinct businesses: neuroscience and rare diseases, and hoping to maximize the potential of each

of these segments, the firm initiated a strategic review of the neuroscience portfolio that may include a public offering with management offering more certainty by the end of 2017.

We are pleased to hear Shire maintain its commitment to reducing net leverage into the range of 2-3 times EBITDA in 2017 after the debt balance exploded after the $32 billion purchase of Baxalta in June 2016. Accordingly, the firm reduced its debt load by more than $1 billion in the second quarter to $21 billion, dropping pro forma net debt leverage to approximately 3.8 times for the trailing 12 months considering a modest cash and investments balance of $264 million. While we recognize Shire's progress towards its leverage goal so far this year, we still remain skeptical that Shire can hit its target in 2017, but expect net leverage to comfortably fall below 3 times in 2018 due to a combination of debt reduction and solid operational performance. Currently, the firm has little financial flexibility for shareholder distributions beyond its modest dividend given its deleveraging goal.

Market Data
For best comparisons to the Shire PLC's notes, we look to similarly rated companies, Allergan PLC (rating: BBB-, positive) and Mylan NV (rating: BBB-, stable). Within this comparable group and adjusted for bond maturities, Shire's 10-year bonds recently traded close to those at Allergan, and tighter than those at Mylan. Shire's 10-year bonds also traded much tighter than the levels of both Morningstar Inc.'s BBB- and BBB Corporate Bond Indexes. All of the following bond data is sourced from Interactive Data.

In the approximate 5-year maturity bucket, bonds from these issuers recently traded over the nearest Treasury as follows:
Shire's 2.88% notes due 2023 at +92 basis points.
Allergan's) 3.25% notes due in 2022 at +77 basis points.
Mylan's 4.20% notes due in 2023 at +122 basis points.

In the approximate 10-year maturity bucket, bonds from these issuers recently traded over the nearest Treasury as follows:
Shire's 3.20% notes due 2026 at +112 basis points.
Allergan's 3.80% notes due in 2025 at +106 basis points.
Mylan's 3.95% notes due in 2026 at +146 basis points.

For comparison to the approximate 10-year maturities, Morningstar Inc.'s Corporate Bond Index is at +136 basis points in the BBB category and +164 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:
Shire's (Baxalta) 5.25% notes due 2045 at +141 basis points.
Allergan's 4.75% notes due in 2045 at +141 basis points.
Mylan's 5.25% notes due in 2046 at +182 basis points.

AmerisourceBergen Deleveraged Moderately in 3Q, but Acquisition Appetite Appears Strong

MCR Credit Risk Assessment

On Aug. 3, AmerisourceBergen Corp. (rating: A, stable) turned in fiscal third-quarter operating results that beat consensus on the bottom line but missed on the top line. While management increased the bottom end of its earnings target range for 2017, it reduced the outlook for revenue and free cash flow in 2017, which was disappointing to investors. More positively for creditors, the company redeemed its bonds that came due in May, helping it deleverage below the low end of its target range. Management's comments about potential acquisitions suggest this relatively light leverage may be short-lived, though, and we remain comfortable with our A rating and stable outlook.

In the fiscal third quarter, revenue grew 5% to $38.7 billion (slightly below consensus of $39.1 billion), and adjusted earnings per share grew 4% to $1.43 (above consensus of $1.37). The company's top line remains challenged by the year-over-year hepatitis C slowdown (a 120-basis-point headwind this quarter), weak branded drug inflation (7% to 9%), and significant generic drug place deflation (negative 7% to negative 9%). Despite these challenges, the company has been controlling costs while benefiting from a lower-than-expected tax rate and lower share count. In terms of guidance for fiscal 2017, management pulled back on its revenue growth rate again, which is now about 5%, down from 5.5% to 6.5% last quarter and 6.5% and 8.0% before that. It also bumped up the bottom end of its earnings per share outlook to $5.82-$5.92 from $5.77-$5.92 last quarter and $5.63-$5.88 at the beginning of the fiscal year. Because of an expected litigation payment and the onboarding of the Prime business, management now expects free cash flow of just $750 million to $1.0 billion in fiscal 2017, or roughly 50%-60% of adjusted net income. In fiscal 2018, management anticipates that free cash flow trends will rebound to more normalized levels of 125% of adjusted net income, which would be a positive development.

From a credit perspective, recent trends remain positive, but AmerisourceBergen appears open to mergers or acquisitions that could negatively influence its currently conservative balance sheet in the intermediate term. During the quarter, the company paid down $600 million of notes, pushing down debt to about $3.4 billion. We estimate gross debt/EBITDA declined by about a quarter of a turn since March to 1.4 times as of June, or slightly below its 1.5 to 2.0 times long-term target range. Net leverage actually ticked up during the quarter, as the firm burned through cash, to 0.9 times as of June from 0.7 times as of March. On the call though, management addressed the company's growing appetite for acquisitions. Specifically, the company feels comfortable pursuing acquisitions in the $500 million to $3 billion range. This potential for acquisitions creates event risk for creditors since debt-funded acquisitions could eventually cut into its currently very strong financial health.

Market Data

We use AmerisourceBergen's drug distribution peers as its credit comparables. We sourced all of the following bond data from Interactive Data:

In the approximate 5-year maturity bucket, bonds recently traded as follows over the nearest Treasury:
AmerisourceBergen Corp's 3.50% notes due in 2021 at +78 basis points.
Cardinal Health Inc.'s (rating: A/UR-) 2.62% notes due in 2022 at +66 basis points.
McKesson Corp's (rating: A-, stable) 2.70% notes due in 2022 at +75 basis points.

In the approximate 10-year maturity bucket, bonds recently traded as follows over the nearest Treasury:
AmerisourceBergen's 3.25% notes due in 2025 at +82 basis points.
Cardinal's 3.25% notes due in 2027 at +108 basis points.
McKesson's 3.80% notes due in 2024 at +87 basis points.

For comparison to the 10-year maturity bucket, Morningstar Inc.'s Corporate Bond Index is at +84 basis points in the A category and +94 basis points in the A- category.

In the approximate 30-year maturity bucket, bonds recently traded as follows over the nearest Treasury:
AmerisourceBergen's 4.25% notes due in 2045 at +131 basis points.
Cardinal's 4.34% notes due in 2047 at +131 basis points.
McKesson's 4.88% notes due in 2044 at +133 basis points.

AIG Reports Solid Earnings Growth Through 1H, but Reserve Position Still Troubling

MCR Credit Risk Assessment

American International Group's (rating: BBB, negative) first-half profits increased 34% over the prior-year period, with the company reporting $2.3 billion of net income. Strong performance in the consumer insurance segment drove the results, as the company reported increases in pretax operating income in all five subsegments of its life and personal property/casualty insurance operations. However, total revenue declined 5% as premium volume decreased 12% due to the absence of the UGC mortgage insurance business (sold in 2016 to Arch Capital Group) and the continued pullback from challenged commercial lines of business. Despite shrinking its books and trimming unprofitable business, AIG reported a 102.4% combined ratio in the commercial insurance segment, a 4.5-percentage-point deterioration from the prior six-month period. Liability and financial lines contributed to the larger underwriting loss, as the property and special risks combined ratio was unchanged year over year. Overall, improvement in the personal lines combined ratio was not sufficient to offset deterioration in commercial lines, as AIG reported a 99.1% combined ratio for the first half, a 1-percentage-point increase over the 98.1% reported in the prior-year period.

We are not comforted by the remarks made during the conference call in relation to future adverse reserve development and believe there is a better-than-average chance of further material charges, as certain problem areas such as commercial property and casualty lines are expected to continue developing unfavorably. Through the first half of 2017, AIG reported $66 million of unfavorable development as opposed to $60 million of favorable development through the first half of 2016. Recent history suggests the annual in-depth reserve true-up will occur in the fourth quarter, and further rating actions will probably depend on these results.

On a positive note, we believe the discontinuation of the capital return plan is a step in the right direction to bolster AIG's equity cushion and maintain adequate capitalization. Comments from new CEO Brian Duperreault point toward an opportunistic share repurchase strategy, though it is not clear what share price point would trigger further buybacks. The company's plans to grow and expand are feasible, in our opinion, though we'd prefer that AIG get its reserve issues under control and focus on improving commercial lines profitability before implementing any aggressive growth strategies. Debt/capital ticked up slightly over the prior quarter to 30%, and we note that growth driven by additional debt funding would be a credit negative.

Rated peers we compare with AIG include Chubb (rating: A-, positive) and Travelers (rating: A-, stable). Chubb reported strong first-half results that were bolstered by $94 million in net realized gains following $610 million of realized losses in the first half of 2016, and the combined ratio improved to 87.8% from 90.6% in the prior-year period. Travelers reported earnings of $595 million for the second quarter, a 10% decrease from the prior-year quarter. Year to date, earnings decreased 11%, to $1.2 billion from $1.4 billion. The decline in performance is mainly a result of elevated losses from catastrophes and continued weak performance in the personal auto segment.

Market Data
The following spreads over the nearest Treasury are provided by Interactive Data:
The AIG 3.90% notes due in 2026 are indicated at +121 basis points.
The Chubb 3.35% notes due in 2026 are indicated at +69 basis points.
The Travelers 3.90% notes due in 2020 are indicated at +51 basis points.

Decline in Legacy Revenue Drags on CenturyLink's 2Q Operating Performance

MCR Credit Risk Assessment
CenturyLink Inc. (rating: BB/UR-) reported second-quarter results Aug. 2. Revenue, adjusted for the May 1 sale of the colocation and data center assets, declined 5% year over year, reflecting the company's ongoing struggles to attract revenue growth. The weak performance was driven by a 10% decline in legacy services revenue and a 0.7% adjusted decline in strategic revenue. In strategic, CenturyLink eked out modest growth in enterprise high-speed data and IT and managed services, though revenue from other strategic enterprise services was flat on an adjusted basis. In legacy products, revenue declined across all product categories in the latest quarter as demand for traditional voice and DSL services continued to weaken. Meanwhile, operating profit excluding nonrecurring items declined 20%, driven by top-line weakness and an increase in overhead expenses. For the third quarter, management is guiding revenue growth 2% lower at the midpoint of guidance and EBITDA flat with the second quarter.

The decline in operating performance continues to have a disproportionate impact on cash generation. Free cash flow for the trailing 12 months decreased $1.5 billion from the comparable period a year ago to $1.7 billion on a 27% decline in operating income over the period compounded by a net decrease in noncash add-backs including depreciation and amortization and an increase in cash used for net working capital. Capital spending increased by $400 million over the year to $3.3 billion. During the

second quarter, the company received $1.5 billion of proceeds from the asset sale and paid out a total of $784 million for dividends and modest share repurchases, leaving $1.2 billion of net cash flow.

CenturyLink also raised $7 billion of new debt, including a $6 billion term loan B due 2025 to fund the pending acquisition of Level 3 Communications (not rated), which is expected to close at the end of the third quarter. In addition to the term loan, the company also signed for just under $4 billion of undrawn additional financing, including a $2 billion revolving facility due 2022. The new facilities, which will likely be drawn at closing, initially bear financial covenants that cap net leverage at 5 times EBITDA for the first two years following the acquisition and require minimum EBITDA coverage of 2.0 times interest expense.

With the new debt issuance, total debt ended the quarter at $25.1 billion, supported by $6.4 billion of cash, including $6 billion of financing classified as restricted. Net debt increased from a year ago to 3.1 times from 2.8 times, on account of the carrier's weaker profitability. Based on both companies' most recent trailing 12-month results, we expect pro forma net debt to increase to around 4.0 times at the outset of the merger. Management now expects operating synergies of $925 million within three years of the closing date, which if realized would reduce leverage to around 3.7 times. CenturyLink's management is maintaining its long-term net leverage target of 3.0 times, but indicated that leverage will remain above the target for three to four years after the merger.

Our credit rating remains under review negative pending the final regulatory approvals for the merger. In combination with already-weak operating performance, we expect the additional debt from Level 3 to put material pressure on the Cash Flow Cushion and other pillars, which may lead to a downgrade. Strategically, we expect Level 3 to provide CenturyLink with enhanced fiber network capacity and allow it a larger penetration into small/midsize enterprise communications services. Level 3 will provide an additional 200,000 route miles of fiber, including 33,000 subsea miles and 64,000 miles located throughout 350 metro areas around the world. Pro forma, the combined companies will draw 76% of their revenue from business customers, with the contribution from the consumer businesses shrinking from 36% to 24%.

Market Data

According to pricing provided by Interactive Data as of Aug. 2, CenturyLink's 5.63% notes due 2025 are indicated at a yield to maturity of 5.83% (+373 basis points over the nearest Treasury). For comparison, Dish Network Corp.'s (rating: B+, stable) 7.75% notes due 2026 are indicated at a yield to maturity of 5.01% (+283 basis points). Compared with levels on May 3, the spread to Treasury for the CenturyLink notes is 6 basis points tighter, while the Dish notes are tighter by 42 basis points. Over the same period, the BofA/Merrill Lynch High Yield BB Index, now quoted at +219 basis points, is 18 basis points tighter.

Becton Dickinson Preps for Bard Acquisition by End of 2017

MCR Credit Risk Assessment

On Aug. 3, Becton, Dickinson and Co (rating: BBB+/UR-) reported fiscal third-quarter operating results with sales below and earnings above consensus. The company also updated the timing on the potential closing of the C.R. Bard Inc (rating: A+/UR-) acquisition to November or December, which is slightly later than we anticipated when it was initially described as a potential fall closing. BD's credit rating remains under review with negative implications on this leverage-increasing planned combination.

In the quarter, BD turned in $3.0 billion in sales (slightly below consensus of $3.1 billion), a reported decrease of 5% but 2% constant-currency growth excluding the recent respiratory solutions divestiture. BD's medical segment grew 1% on an organic, constant-currency basis, which was weaker than anticipated. Within this segment, the medication management solutions division was the noticeable laggard with a roughly 4% constant-currency decline year over year on a recent change in its dispensing business model in the United States and delayed orders in the international infusion business. The former may remain a drag until the change (which results in recording revenues ratably over the contract term versus recognizing the entire contract value up front with a hardware placement) is anniversaried next year. The delayed international orders are merely expected to move into next quarter's results. BD's life sciences segment grew 5% on a constant-currency basis with strength across its divisions. By geography, the U.S. business was roughly flat on an organic basis, with the dispensing business model change providing the key headwind, while the international business grew 5% on an organic constant-currency basis. Adjusted earnings per share grew 5% to $2.46, or slightly above consensus of $2.44, primarily on continued operating margin expansion. The company raised its outlook for adjusted earnings per share to $9.42-$9.47 from $9.35-$9.45 on expected foreign currency benefits.

The planned acquisition of C.R. Bard, which management now expects to be completed in November or December pending regulatory reviews and the Bard shareholder vote, promises to cut into the financial health of BD. Less than three years after the leverage-increasing CareFusion acquisition, leverage may rise yet again. Initially after the CareFusion combination, debt stood at $13.2 billion, or gross leverage in the mid-4s by our estimates. Since then, BD has actively deleveraged by repaying debt and increasing profits; as of March, total debt stood at $10 billion, or gross debt/EBITDA around its target of 3 times. By the company issuing about $10 billion of new debt in the second quarter and assuming BD's debt, leverage looks set to rise the high 4s on a pro forma basis initially after the transaction closes. Although the firm plans to reduce leverage to below 3.0 times within a few years of the Bard combination, this leverage-increasing transaction may weaken its Cash Flow Cushion and Distance to Default pillars enough to consider a downgrade. BD looks likely to still score 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 has scale that creates a barrier to entry for competitors in this price-sensitive part of the healthcare industry. The CareFusion acquisition primarily added an infusion pump business that competes in a virtual oligopoly in developed markets and has significant expansion opportunities in emerging markets. The Bard acquisition promises to add top-tier positions in vascular, surgical, urology, and oncology devices.

Market Data

From a credit perspective, BD's closest comparables are similar-rated firms in the medical technology sector, including Zimmer Biomet Holdings Inc (rating: BBB+, negative) and Boston Scientific Corp (rating: BBB, positive). All of the following bond data is sourced from Interactive Data.

In the approximate 5-year maturity bucket, bonds from these issuers recently traded over the nearest Treasury as follows:
Becton Dickinson's 2.89% notes due 2022 at +94 basis points.
Zimmer Biomet's 3.15% notes due 2022 at +96 basis points.
Boston Scientific's 3.38% notes due 2022 at +78 basis points.

In the approximate 10-year maturity bucket, bonds from these issuers recently traded over the nearest Treasury as follows:
Becton Dickinson's 3.70%% notes due 2027 at +126 basis points.
Zimmer Biomet's 3.55% notes due 2025 at +123 basis points.
Boston Scientific's 3.85% notes due 2025 at +107 basis points.

For comparison with the approximate 10-year maturities, the Morningstar Corporate Bond Index is at +126 basis points in the BBB+ category and +137 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:
Becton Dickinson's 4.67%% notes due 2027 at +153 basis points.
Zimmer Biomet's 4.45% notes due 2045 at +153 basis points.

CA Reports Solid Fiscal 1Q on Growth in New Sales and Higher Free Cash Flow

MCR Credit Risk Assessment

CA Technologies Inc. (rating: A-, stable) released its fiscal first-quarter operating results Aug. 2. Revenue was up 3% year over year to $1 billion, or 4% on a constant-currency basis, while operating margin declined 200 basis points from a year ago. Revenue performance was driven by the contributions of recently acquired companies Automic and Veracode that together contributed about 6 percentage points of growth in the quarter, suggesting a 1% net decline in constant-currency adjusted organic revenue year over year. Bookings were down 48% year over year on a decline in renewal volume on tough comps from the year-ago period, although the revenue backlog increased 2% and billings were up 10% organically, driving an improved outlook for the year. Spurred by stronger-than-expected new sales in enterprise solutions, management is raising its full-year midpoint revenue growth guidance to 4%, from the prior range of 2%-3%. Management is also projecting upside for non-GAAP operating margin within the range of 36%-37% compared with previous guidance of 36%.

In the June quarter, enterprise solutions' revenue increased 12%, though this was entirely attributable to acquisitions. Organically, we estimate that enterprise revenue declined 2%. Mainframe revenue declined 2% on a currency-adjusted basis, reflecting the ongoing secular decline in mainframe sales and

license renewals. Meanwhile, profitability of the key segments was mixed during the quarter, with non-GAAP operating margin in Mainframe increasing to 65% from 62% on a reduction in personnel-related expenses, while operating margin in Enterprise Solution declined to 8% from 13%, as a result of operating losses associated with acquisitions.

At the end of June, CA reported total debt of $2.8 billion, or 1.9 times trailing 12-month EBITDA, with net debt remaining at close to zero. Cash and investments ended the first quarter at $3.0 billion, with 41% cash held in the U.S., reflecting $552 million expansion from prior year. For the trailing 12 months, CA's free cash flow increased 17% to $1.1 billion. Over the past 12 months, the company paid out $423 million to shareholders in the form of dividends and share repurchases, a payout ratio of 38%. CA also issued $850 million senior notes in March to finance $1.3 billion of acquisitions. Management curtailed its share repurchase activity last September in preparation for acquisitions, though CA had $650 million remaining share repurchase authorization as of June 30. Compared with lower-rated legacy-driven software and hardware peers, CA continues to operate with lower financial leverage and generate much higher margins and free cash flow.

Our rating on CA reflects the firm's competitive advantage, high returns on capital, and its conservative balance sheet. These attributes support a moderate Business Risk score and a high Solvency Score pillar. While CA has maintained solid operating margins and cash flows in recent years, revenue growth has been weak as demand for legacy mainframe technology has declined. The company has been focused on moving into enterprise software applications to spur top-line growth. We believe CA will continue to focus on strategic acquisitions over the next few years to capture growth from new software technology and delivery models. Management has targeted annual expenditures for acquisitions in the range of $300 million-$500 million, which we have incorporated into our forecast. On June 21, event risk spiked following financial news reports that CA was in discussion to be acquired by privately held software firm, BMC. However, on July 27, it was reported in the press that talks had ended, allegedly due to an inability to securing financing commitments.

Market Data

According to pricing provided by Interactive Data as of Aug. 2, A- rated CA's 4.70% notes due in 2027 are indicated at a spread of +182 basis points over the nearest Treasury, which is 54 basis points tighter from June 21 following reports of the potential buyout. For comparison, Hewlett Packard Enterprise Co. (rating: BBB, stable) 4.90% notes due 2025 are indicated at +195 basis points and Xerox Corp. 3.80% notes due 2024 are indicated at +158 basis points.

Allergan Slightly Increases 2017 Sales Guidance After Solid 2Q; Debt Balance Falling

MCR Credit Risk Assessment

On Aug. 3, Allergan (rating: BBB-, positive) reported strong performance in the second quarter, as net revenue increased by 9% supported by strong uptake of newer products, including the antipsychotic medicine Vraylar (increased nearly sixfold) and the gastrointestinal treatment Viberzi (doubled year over year). This solid sales growth more than offset headwinds from generic competition to Asacol HD (gastrointestinal disorders) and Minastrin 24 Fe (birth control). Given confidence of its results in the first

half, Allergan raised its sales outlook for 2017 by $50 million to $15.85 billion to $16.05 billion and its non-GAAP EPS to $16.05-$16.45 from $15.85-$16.35. We expect Allergan to easily manage the nearing patent loss of Namenda XR (around 3% of total sales) potentially in 2018 with its refreshed drug and medical device portfolio to drive sales growth greater than 6% over the next five years compounded annually.

Allergan's stubbornly elevated debt leverage remains our biggest concern, which was not fully alleviated by the firm's refinancing activities in the quarter, specifically its EUR 2.7 billion debt issuance and $2 billion debt tender offer. But, the firm has reduced outstanding debt by $2.6 billion so far in 2017 and hopes to further lighten the debt load by $3.8 billion by the end of 2018 in conjunction with its long term debt maturity schedule over that time frame. As of June 30, Allergan's total debt stood at $30.2 billion or around 4.5 times for the trailing 12 months. Considering Allergan's cash and marketable securities of $5.8 billion at the end of the second quarter, net leverage was 3.7 times for the latest 12 months ended June 30, 2017. This debt reduction, along with sustained operational improvement, could decrease gross leverage to Allergan's target of 3.0-3.5 times by 2018, in our estimation. We anticipate that Allergan has the financial flexibility to repay the coming debt maturities with its cash balance and solid free cash flow generation of $6 billion on average over the next five years, by our estimates. We recognize the firm's tendency to aggressively acquire assets as well as greatly reward shareholders via share repurchasing and dividend payments, which may hinder debt reduction efforts if the firm significantly steps up these activities over the next year.

Market Data

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

In the approximate 5-year maturity bucket, bonds from these issuers recently traded over the nearest Treasury as follows:
Allergan's 3.25% notes due in 2022 at +77 basis points.
Mylan's 4.20% notes due in 2023 at +122 basis points.
Shire's 2.88% notes due 2023 at +92 basis points.

In the approximate 10-year maturity bucket, bonds from these issuers recently traded over the nearest Treasury as follows:
Allergan's 3.80% notes due in 2025 at +106 basis points.
Mylan's 3.95% notes due in 2026 at +146 basis points.
Shire's 3.20% notes due 2026 at +112 basis points.

For comparison to the approximate 10-year maturities, Morningstar Inc.'s Corporate Bond Index is at +136 basis points in the BBB category and +164 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:
Allergan's 4.75% notes due in 2045 at +141 basis points;
Mylan's 5.25% notes due in 2046 at +182 basis points; and
Shire's (Baxalta) 5.25% notes due 2045 at +141 basis points.

Teva Significantly Revamps Outlook After Difficult 2Q; Deleveraging Efforts Pressured
MCR Credit Risk Assessment
Teva Pharmaceutical Industries Ltd. (rating: BBB-, stable) reported weak results for the second quarter, as troubles continued in Venezuela while pricing eroded faster than expected for its U.S generics business. While net revenue rose 13% in the second quarter, the primary driver was contribution from the acquisition of Actavis in August 2016. With dampened prospects from its generic businesses, Teva recorded goodwill impairment of $6.1 billion in the quarter, highlighting the greater-than-anticipated price erosion seen in its U.S. generic drug operations. As a result of the poor performance, Teva reduced its revenue outlook for 2017 to $22.8 billion-$23.2 billion from $23.8 billion-$24.5 billion. From a credit viewpoint, expected cash flow from operations was significantly lowered to $4.4 billion-$4.6 billion from $5.7 billion-$6.1 billion, while estimated EBITDA fell to a range of $7.4 billion-$7.6 billion from $8.0 billion-$8.4 billion originally. The reduced guidance does not account for the introduction of a generic version of Copaxone 40 mg., which if launched in the fourth quarter would shave earnings of $0.20-$0.25 per share from the $4.30-$4.50 per share expected for the full year (or $2.22-$2.42 in the second half considering $2.08 generated in the first half of 2017) without generic competition. On a positive note, accelerated action to streamline its operations, including the integration of Actavis, may yield $1.6 billion of cost savings in 2017 (increased from $1.5 billion). We still see recovery of top-line growth in 2019 helped by new brand-name medicines, including specialty drug Austedo (Huntington's disease), and new generic entrants given a broadened pipeline after the purchase of Actavis that spans 300 ANDAs (including 100 potential first-to-file opportunities).

We are concerned that Teva may be unable to reduce its heavy debt load left over from the acquisition as it originally intended. On June 30, the debt load stood at $35.1 billion, or gross leverage slightly greater than 5 times on a pro forma basis for the trailing 12 months. On its conference call, the firm reiterated its intention to decrease the debt balance by $5 billion, partially funded by divestiture proceeds expected around $2 billion. However, Teva is in danger of tripping its maximum leverage covenant in its credit agreement that calls for total leverage to be at or below 4.25 times at the end of 2017. In order to remain compliant with the financial covenant, the firm would need to drop the debt level to around $31 billion and hit the midpoint of its reduced EBITDA target in 2017. Divestment proceeds would propel the firm toward this level, but the timing of these transactions is uncertain and could jeopardize its covenant compliance, if divestments bleed into 2018. Teva announced a reduction its dividend, currently at $1.4 billion per year, by 75%, which grants the firm some flexibility as it tries to repair its operations, a positive from a creditor's perspective. Given its lowered financial expectations, we believe it will be nearly impossible for Teva to achieve its aggressive leverage reduction goals seeking to drop net leverage to 2.1 times by the end of 2018 and gross leverage of 3.5 times by 18 months after the close of the Actavis transaction. However, our stable outlook is informed by our

expectation that Teva operates at the low end of the BBB- category and maintains gross debt leverage and net debt leverage below 4.5 times and 4.0 times, respectively, in the long run. We previously highlighted these levels, which if exceeded on a sustained basis may contribute to a downgrade to the current rating.

Market Data

For closest comparisons to Teva's notes, we look to similar-rated Allergan PLC (rating: BBB-, positive), Mylan NV (rating: BBB-, stable), and Perrigo Co PLC (rating: BBB-, negative). Within this comparable group and adjusted for bond maturities, Teva's 10-year bonds trade closest to those at Mylan, wider than those at Allergan, and tighter than those at Perrigo. Teva's 10-year bonds also traded tighter to the level of Morningstar Inc.'s BBB- Corporate Bond Index. All of the following bond data is sourced from Interactive Data.

In the approximate 5-year maturity bucket, bonds from these issuers recently traded over the nearest Treasury as follows:
Teva's 2.95% notes due in 2022 at +103 basis points.
Allergan's 3.25% notes due in 2022 at +77 basis points.
Mylan's 4.20% notes due in 2023 at +122 basis points.
Perrigo's 4.00% notes due in 2023 at +93 basis points.

In the approximate 10-year maturity bucket, bonds from these issuers recently traded over the nearest Treasury as follows:
Teva's 3.15% notes due in 2026 at +152 basis points.
Allergan's 3.80% notes due in 2025 at +106 basis points.
Mylan's 3.95% notes due in 2026 at +146 basis points.
Perrigo's 4.38% notes due in 2026 at +167 basis points.

For comparison to the approximate 10-year maturities, Morningstar Inc.'s Corporate Bond Index is at +136 basis points in the BBB category and +164 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:
Teva's 4.10% notes due in 2046 at +182 basis points.
Allergan's 4.75% notes due in 2045 at +141 basis points.
Mylan's 5.25% notes due in 2046 at +182 basis points.
Perrigo's 4.90% notes due in 2044 at +198 basis points .

Despite Sequential Decline in 2Q Oil and Gas Pricing, Apache Still Generates Free Cash Flow

MCR Credit Risk Assessment

On Aug. 3, Apache Corp. (rating: BBB-, positive) reported second-quarter revenue and other income of $1.4 billion, unchanged relative to the second quarter of 2016. Corresponding with this, net cash provided by operating activities was $751 million, a slight increase from $744 million in the year-ago

quarter. After capital expenditures, dividends, and $285 million received from divestments, we estimate second-quarter free cash flow was about $200 million. We view total liquidity of $5.2 billion as very good, including $1.7 billion in cash and equivalents and full availability on Apache's $3.5 billion five-year revolving credit facility.

Apache's second-quarter production was 35.4 million barrels of oil equivalent, or boe, slightly higher than the guidance midpoint of 34.8 million boe (excludes Egypt noncontrolling interest and Egypt tax barrels). The second quarter was characterized by better-than-expected production from the international segment, mostly driven by completion of the Callater-Beryl Alpha platform subsea tieback facility in the North Sea earlier than scheduled. Additionally, production from the North American segment was slightly more-than-planned, benefiting from strong initial results from new wells in the Midland portion of the Permian Basin. Recent rig additions at the new Alpine High play in the Delaware portion of the Permian Basin, the North Sea, and in Egypt are all contributing to a reacceleration of companywide production growth in the third quarter.

Apache expects to complete its sale of Canadian assets for total proceeds of $713 million in August. Given a lower cash margin on Canadian production, the sale should be accretive to the company's overall cash margin. Further, the company estimates the elimination of $800 million present value of related future asset-retirement obligations. Adjusted for the exit from Canada, Apache's full-year 2017 production guidance has been reduced by 6% to 167 million-172 million barrels of oil equivalent from 177 million-184 million boe, which we think is achievable.

There is no change to Apache's 2017 capital expenditure guidance of $3.1 billion. For full-year 2017, after adjusting for capital expenditures, dividends, and divestments, we estimate positive free cash flow of around $750 million, which includes our assumption of $1.4 billion in noncore asset sales.

At the end of June, Apache's total debt was $8.5 billion and net debt $6.8 billion. Apache's ratio of total debt/trailing adjusted EBITDAX is 2.3 times and net leverage 1.9 times, the ratios having declined by 0.4 turns each since the end of 2016. As of June, we estimate trailing 12-month adjusted EBITDAX to be $3.6 billion.

Anadarko Petroleum (rating: BB+, positive outlook), a larger, U.S.-centric exploration and production company, has more debt than Apache. At June, Anadarko had gross leverage of 2.9 times. Concho Resources (rating: BB+, positive) is a much smaller, Texas Permian-focused E&P peer. At June, Concho had gross leverage of 1.6 times, less than Apache.

Market Data

According to pricing service Interactive Data, the 2.63% notes due Jan. 15, 2023, from Apache recently traded at +98 basis points over the nearest Treasury. By comparison, Anadarko's 5.5% notes due in 2026 recently traded at +161 basis points. Additionally, the 4.38% notes due Jan. 15, 2025, from Concho Resources recently traded at +184 basis points over the nearest Treasury.

Film Division Lifts Viacom's 3Q Revenue, Though Margin Pressured by Programming Costs

MCR Credit Risk Assessment

For its fiscal third quarter ended June 30, Viacom Inc. (rating: BBB, negative) reported its third consecutive quarter of positive year-over-year growth. Revenue was up 8.3% as reported and 7% on an organic basis, excluding the impact from the integration of Argentine broadcast company Telefe as well as net foreign exchange impact.

Media networks' revenue grew 2%, led by higher affiliate fees (up 4%) and supported by 2% growth in advertising. Affiliate fees benefited partly from favorable timing in streaming contracts, which shifted more revenue to the June quarter. By geography, international dominated the quarter with 8% growth, driven by a 14% jump in ad revenue. However, most of the ad growth was contributed by the acquisition of Telefe as well as favorably currency impact. On an organic basis, international ad revenue declined 1%. Filmed entertainment revenue grew 36% from a year ago, driven by contributions from recent theatrical releases Transformers: The Last Knight and Baywatch, which compare favorably with last year's Teenage Mutant Ninja Turtle release despite box office performance running a bit below expectations.

Viacom's adjusted operating profit improved 5%, though margin declined year over year. Adjusted expenses increased 9.8% year over year, led by a 13.5% increase in programming expenses as well as 7% growth in sales and administrative expenses, again driven by acquisition costs associated with Telefe as well as higher employee costs.

Free cash flow over the past 12 months totaled $1.2 billion, a decline of 26% from the comparable period a year ago. Meanwhile, the company paid out just under $400 million of dividends over the period (down 37% year over year), with payout down to 18% from 43% a year ago, reflecting a positive credit impact from management's decision to cut the dividend. Viacom also received $570 million of proceeds from the sale of Paramount's 49.8% stake in the Epix movie library to MGM.

Total debt ended the June quarter at $11.1 billion, down $1 billion from last quarter, while cash ended the quarter down $246 million sequentially to $425 million. The decline in debt reflects the tender offer for certain of Viacom's senior notes, which was completed in June. Net senior leverage was 3.2 times trailing 12-month EBITDA, which is three-tenths of a turn lower from last quarter. Meanwhile, all-in net leverage, including the $1.3 billion of hybrid subordinated notes, was also lower, ending June at 3.7 times, down from 4 times the prior quarter. For comparison, competitor Discovery Communications (rating: BBB/UR-) reported net debt equivalent to 3.3 times EBITDA at the end of June while former subsidiary CBS (rating: BBB, stable) reported net debt at 2.8 times EBITDA at the end of March. Our rating on Discovery is under review pending its proposed acquisition with Scripps Networks Interactive Inc (rating: BBB+/UR-), an acquisition that Viacom was also reported to have been seeking.

Our BBB rating of Viacom reflects moderate Business Risk and Solvency Score supported by the company's globally positioned portfolio of widely known network TV brands that produce solid affiliate fees, high returns on invested capital, and solid free cash flow. These positive attributes are offset by a

weak Cash Flow Cushion driven by elevated debt levels and a recent decline in free cash flow. Distance to Default has also been weakening because of the higher leverage and volatility in Viacom's common stock. We expect event risk to remain elevated around potential acquisition restructuring activity in the wake of a recent failed attempt to acquire Scripps Networks.

Market Data
According to pricing data from Interactive Data as of Aug. 3, Viacom's 3.45% notes due 2026 are indicated at +162 basis points over the nearest Treasury, only 4 basis points tighter from the company's last earnings release May 3. For comparable issuers, we look to competitor Discovery Communications' its 4.90% notes due 2026 indicated at +163 basis points and CBS Corp's 2.90% notes due 2027 indicated at +116 basis points. Discovery's 2026 notes are 33 basis points tighter, while CBS' 2027 notes are 13 basis points tighter since May 3. Morningstar's BBB Corporate Bond Index, currently quoted at +129 basis points, is 18 basis points tighter over the past three months.

Despite Solid Operating Results, MetLife's Earnings Affected by Derivative Losses
MCR Credit Risk Assessment
MetLife (rating: BBB+, positive) has not completely recovered from derivative losses, but it appears that things are improving. First-half 2017 pretax operating return on average equity was virtually unchanged over the prior-year period at 9.3%. Due to first-half derivate losses totaling nearly $1.4 billion, though, MetLife's earnings decreased 27% over the prior-year period, with the company reporting $1.7 billion in net income and a subpar 5.0% annualized ROAE. However, losses in the second quarter decreased to $437 million from $926 million in the first quarter, hinting at a brighter outlook going forward as interest rates increase and the company reinvests into higher-yielding securities.

With the completion of the spin-off of Brighthouse Financial quickly approaching, we believe MetLife's risk profile will improve as more complex lines of business will largely follow with it to the new entity. While products such as variable annuities can give rise to more lucrative returns if properly priced and reserved for, they generally increase the risk profile of life insurers and lead to increased profit volatility. Following the separation, MetLife should benefit from renewed focus on the areas it excels in, as well as more stable, sustainable cash flow generation, both credit positives. Additionally, the court case governing MetLife's nonbank SIFI challenge has been placed in abeyance pending the Trump administration's review of the Dodd–Frank Wall Street Reform and Consumer Protection Act.

Debt/capital was unchanged over the prior quarter at 26%. Operating EBIT/interest expense, which excludes realized gains/losses and gains/losses on derivatives, slightly deteriorated to 6.2 times from 6.9 times at the close of first quarter 2017 but is stronger than the company's five-year average 5.3 times interest coverage.

Rated peers we compare against MetLife include Prudential Financial (rating: BBB+, stable) and AIG (rating: BBB, negative) due to the company's sizable life insurance segment. Prudential's second-quarter results included a $492 million reserve charge following the company's annual actuarial review, dampening earnings. AIG was downgraded and assigned a negative outlook in March due to large,

material fourth-quarter reserve charges, the company's capital return plan and uncertainty surrounding the company's business direction following the resignation of former CEO Peter Hancock. While we believe the hiring of new CEO Brian Duperreault is a step in the right direction because of his experience, his discontinuation of the capital return plan, and his plans for growth, we are wary about further fourth-quarter reserve charges.

Market Data

The following spreads over the nearest Treasury are provided by Interactive Data Corp.:
MetLife 3.60% notes due in 2025 are indicated at +76 basis points.
Prudential Financial 3.50% notes due in 2024 are indicated at +68 basis points.
AIG 3.90% notes due in 2026 are indicated at +121 basis points.

Credit Contacts

Basic Materials
Sean Sexton, CFA
sean.sexton@morningstar.com
+1 312 348-3077

Consumer
Dave Sekera, CFA
david.sekera@morningstar.com
+1 312 696-6293

Consumer Defensive
Wesley Moultrie, CPA, CGMA
wesley.moultrie@morningstar.com
+1 312 384-5405

Consumer Cyclical
Wayne Stefurak, CFA
wayne.stefurak@morningstar.com
+1 312 696-6114

Energy
Andrew O'Conor
andrew.oconor@morningstar.com
+1 312 348-3021

Financials – Banks
Chris Baker, CFA
christopher.baker@morningstar.com
+1 312 244-7533

Financials – European Banks
Erin Davis
erin.davis@morningstar.com
+1 312 384-4810

Financials – Insurance, Nonbank Financials
Jeremy Graczyk, CFA
jeremy.graczyk@morningstar.com
+1 312 244-7491

Healthcare
Julie Utterback, CFA
julie.utterback@morningstar.com
+ 1 312 696-6278

Healthcare
Michael Zbinovec
michael.zbinovec@morningstar.com
+ 1 312 348-3136

Industrials
Rick Tauber, CFA, CPA
rick.tauber@morningstar.com
+1 312 384-5431

Industrials
Basili Alukos, CFA, CPA
basili.alukos@morningstar.com
+1 312 384-4984

REITs
Chris Wimmer, CFA
chris.wimmer@morningstar.com
+1 646 560 4585

REITs
Mike Magerman, CFA
mike.magerman@morningstar.com
+1 267 960 6022

Technology, Media, and Telecom
Michael Dimler, CFA
michael.dimler@morningstar.com
+1 312 696-6339

For More Information

Gregg Novek
+1 646 560-4529
gregg.novek@morningstar.com

22 West Washington Street
Chicago, IL 60602 USA

©2017 Morningstar. All Rights Reserved. Unless otherwise provided in a separate agreement, you may use this report only in the country in which its original distributor is based. The information, data, analyses, and opinions presented herein do not constitute investment advice; are provided solely for informational purposes and therefore are not an offer to buy or sell a security; and are not warranted to be correct, complete, or accurate. The opinions expressed are as of the date written and are subject to change without notice. Except as otherwise required by law, Morningstar shall not be responsible for any trading decisions, damages, or other losses resulting from, or related to, the information, data, analyses, or opinions or their use. References to "Morningstar Credit Ratings" refer to ratings issued by Morningstar Credit Ratings, LLC, a credit rating agency registered with the Securities and Exchange Commission as a nationally recognized statistical rating organization ("NRSRO"). Under its NRSRO registration, Morningstar Credit Ratings issues credit ratings on financial institutions (e.g., banks), corporate issuers, and asset-backed securities. While Morningstar Credit Ratings issues credit ratings on insurance companies, those ratings are not issued under its NRSRO registration. All Morningstar credit ratings and related analysis are solely statements of opinion and not statements of fact or recommendations to purchase, hold, or sell any securities or make any other investment decisions. Morningstar credit ratings and related analysis should not be considered without an understanding and review of our methodologies, disclaimers, disclosures, and other important information found at http://morningstarcreditratings.com. Investment research is produced and issued by subsidiaries of Morningstar, Inc. including, but not limited to, Morningstar Research Services LLC, registered with and governed by the U.S. Securities and Exchange Commission. The information contained herein is the proprietary property of Morningstar and may not be reproduced, in whole or in part, or used in any manner, without the prior written consent of Morningstar. To license the research, contact Vanessa Sussman (+1 646 560-4541) or by email to: vanessa.sussman@morningstar.com.