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Seeing default coming: **what almost 3,700 corporate failures teach lenders about early warning**

What more than 900 recent corporate failures – viewed against a 45-year record of 3,674 defaulters – reveal about identifying deterioration early in a corporate credit portfolio

Why we conducted this research

At BDO Advisory's Credit Risk Solutions team, we build and maintain IFRS 9 credit risk frameworks for lenders. One of the most consequential settings in any such framework is the Significant Increase in Credit Risk (SICR) trigger — the rule that decides when an exposure moves from Stage 1 to Stage 2 and provisioning jumps from 12-month to lifetime expected credit losses. Set it too loose and deterioration is recognised late; too tight and provisions whipsaw with every downgrade. Yet at many institutions these triggers were calibrated once, at IFRS 9 adoption, and have not been re-evidenced since — which means they are calibrated to a pre-COVID world.

That is not how we think calibration should work. When S&P Global published its 2025 Annual Global Corporate Default and Rating Transition Study in March 2026, our research team put our own framework on the bench: we extracted every publicly rated defaulter from eight years of annual studies (2018–2025), rebuilt the trigger derivation from scratch on the pooled 702-name dataset, and back-tested the framework against the 2025 defaulted population. The calibration held — the evidence for that sits in our working papers. But the dataset also told a bigger story about how corporate failure announces itself, and those findings are worth sharing beyond our audit files.

Five of them follow.

The evidence base

To test whether our SICR framework remained supported by recent default experience, we considered the evidence at three levels.

First, we looked at the recent default environment. Across the eight S&P Global annual default studies from 2018 to 2025, approximately 1,000 corporate defaults were recorded globally, as shown in Figure 1. This population provides the broader context for how corporate defaults have evolved through the pre-COVID, pandemic and post-COVID periods.

Second, from these annual studies we extracted 702 publicly rated defaulters with the relevant rating information available for detailed analysis. This is the dataset on which we performed our own migration analysis, tracing how credit ratings changed in the period leading up to default. It is this analysis that allows us to assess whether rating deterioration occurs sufficiently early to provide a meaningful SICR signal and to evaluate the calibration of rating-migration triggers.

Third, we considered the 45-year S&P historical record covering 3,674 corporate defaulters from 1981 to 2025. This broader dataset provides the long-run benchmark for understanding the relationship between credit ratings and default, including cumulative default rates by rating category and the time typically remaining to default as credit quality deteriorates.

The three populations therefore answer different but connected questions: the recent default population tells us what the current default environment looks like; the 702-name sample tells us how recent defaulters migrated before failure; and the 45-year history tells us whether those observations are consistent with longer-term patterns in corporate credit risk.

Taken together, they provide the evidence base for the five findings below — and, importantly, for considering when observed credit deterioration should prompt a reassessment of SICR and potential migration from Stage 1 to Stage 2.

1. Defaults are falling — but the cycle is not over

Global corporate defaults declined for a second consecutive year to 117 in 2025, down 19% from 145 in 2024 and far below the pandemic peak of 226. Credit quality broadly improved: 9.4% of issuers were upgraded in 2025 against 5.6% downgraded. But the composition of defaults should temper any comfort. Distressed exchanges — debt restructurings that crystallise losses without a formal bankruptcy — accounted for 58% of 2025 defaults. Lenders are increasingly being asked to accept impaired terms long before a payment is ever missed, which means default risk is arriving through the back door of consensual restructuring rather than the front door of arrears.

What this means for SICR: Arrears should not be the only trigger for reassessing credit risk. A distressed restructuring, request for concessions or amendment of contractual terms because of financial difficulty may indicate material deterioration before a payment is missed and should therefore prompt an immediate reassessment of SICR and, where relevant, whether the exposure is already credit-impaired.

2. Ratings still rank-order risk with remarkable power

Over the full 1981–2025 record, roughly a quarter of CCC/C-rated companies default within one year and half within ten. B-rated issuers reach a 23% cumulative default rate over 15 years against just 2.3% for investment-grade names — a tenfold difference. The rank-ordering power of a well-calibrated rating scale remains the single most reliable early-warning instrument available to a lender.

What this means for SICR: A well-calibrated internal rating system provides an appropriate foundation for identifying changes in credit risk. However, SICR should not be assessed solely by the borrower's current rating; the relevant signal is also how far credit quality has deteriorated relative to the rating at origination.

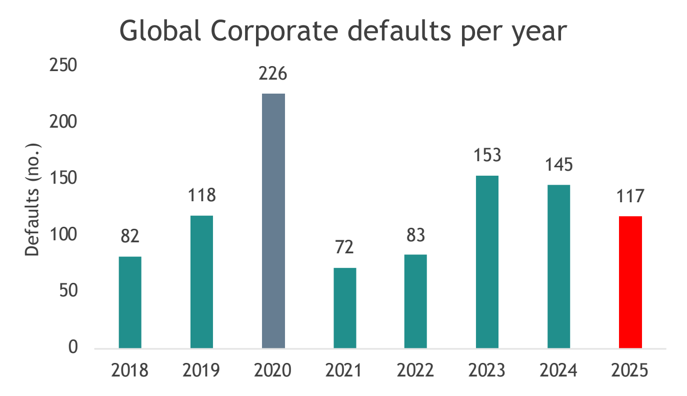

Figure 1: Global corporate defaults by year. Sources: S&P Global annual default studies, 2018–2025.

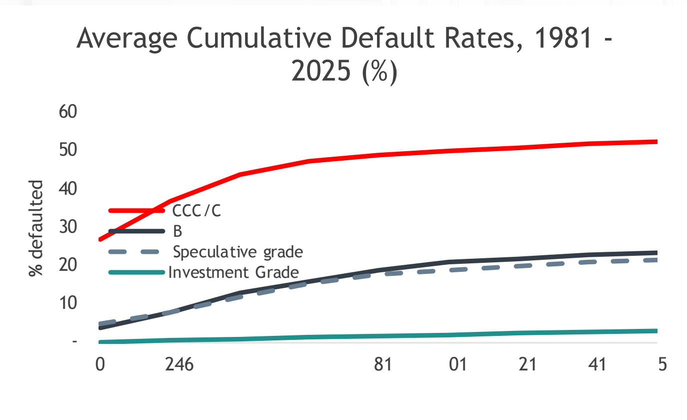

Figure 2: Average cumulative default rates by rating, 1981–2025. Source: S&P 2025 study, Table 24

3. The warning window slams shut as credit deteriorates

A company originally rated BBB that eventually fails takes almost a decade to do so, on average. Once rated B, it takes around 5 years to default. But once a name migrates into the CCC/C category, the average remaining time to default is just 0.9 years — and the median a mere five months. For a lender, the practical implication is stark: by the time a counterparty carries a CCC-equivalent internal grade, the time available to restructure security, reduce limits or exit has largely evaporated.

Risk frameworks should treat entry into the CCC band as an automatic escalation event, not another step on a gradual watchlist.

What this means for SICR: Relative rating migration should be supplemented by an absolute credit-quality threshold. Migration into a CCC-equivalent risk grade should trigger immediate reassessment and escalation, irrespective of whether the borrower has crossed the normal notch-based SICR threshold. Waiting for arrears at this point risks identifying deterioration too late.

4. Most defaulters telegraph their failure — if you track migration

Across the 702 defaulters we analysed from the 2018–2025 studies, 90% of those originally rated investment grade had already been downgraded at least one notch a full year before they defaulted, as had 85% of BB-originated and 76% of B+/B-originated names. Rating migration — not arrears — is the dominant observable warning. A counterparty that misses payments has usually been signalling through its risk grade for years.

What this means for SICR: Rating migration from origination is an observable early-warning signal and should form a key quantitative component of the SICR assessment. Our calibration supports graduated migration thresholds, with stronger credits requiring a larger movement before escalation and weaker credits requiring fewer notches. This ranges from approximately four notches for investment-grade originations to one notch for exposures originated at B- and below.

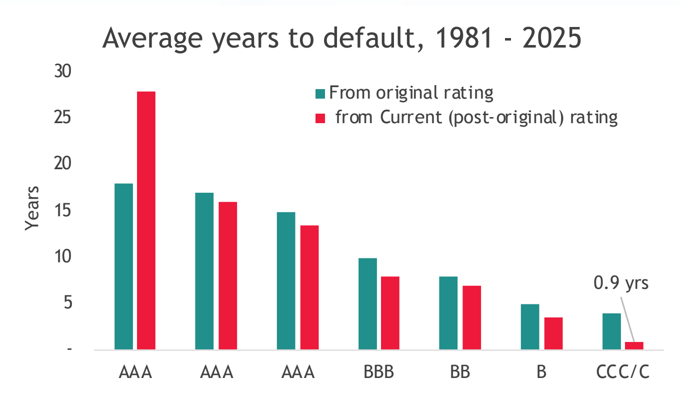

Figure 3: Average years to default from original vs current rating, 1981–2025. Source: S&P 2025 study, Tables 10–11

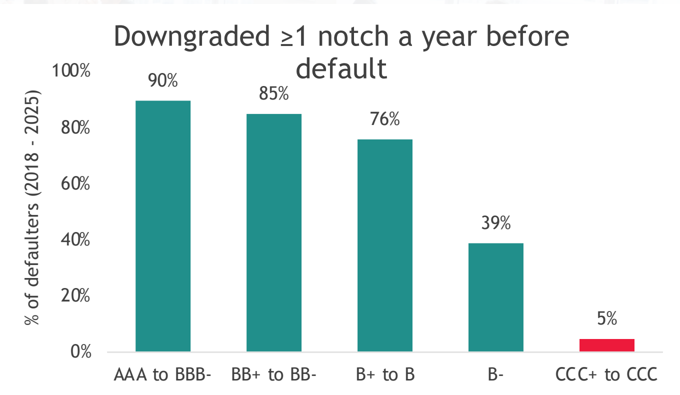

Figure 4: Share of 2018–2025 defaulters downgraded at least one notch a year before default. Source: Cyte analysis

117
global corporate defaults in 2025, down 19% year on year

58%
of 2025 defaults were distressed exchanges, not missed payments

0.9 yrs
average time from CCC/C migration to default

94%
of defaulters were rated B+ or lower one year before failing

5. The weakest credits give the least warning

The migration signal has a blind spot. One year before default, 46% of defaulters already sat in the CCC/C band and a further 26% at B-. Names that start life at the bottom of the scale rarely show a further downgrade before failing — only 5% of CCC-originated defaulters were downgraded again before default, simply because there is nowhere left to go. For these exposures, notch-based triggers add little; monitoring must shift to liquidity indicators, covenant performance, payment behaviour and days-past-due backstops.

What this means for SICR: Notch migration cannot operate as a standalone SICR trigger. For exposures already originated at weak credit grades, there may be insufficient rating distance for further migration to provide an effective warning. These exposures require greater reliance on absolute rating thresholds and qualitative indicators such as liquidity pressure, covenant breaches, restructuring activity and payment behaviour, supported by the 30-day and 90-day past-due backstops.

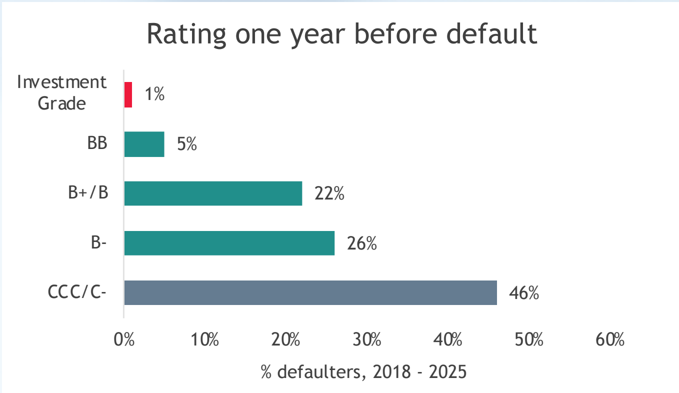

Figure 5: Rating one year before default, pooled 2018–2025 defaulters. Source: Cyte Analysis of S&P study defaulter lists

What this means for corporate lenders

- **Track notch migration from origination, not just point-in-time grades.** The distance a counterparty has travelled since you priced the deal is the strongest single default signal — our analysis supports graduated triggers of 4 notches for investment-grade originations down to 1 notch for B- and below.
- **Treat CCC-equivalent grades as an automatic escalation.** With 0.9 years of average runway, waiting for arrears forfeits most of your recovery options.
- **Watch for distressed exchanges.** A majority of modern defaults arrive as restructuring proposals; treat any request to amend terms under stress as a default-risk event in your staging and provisioning.
- **Layer your signals.** Migration triggers capture roughly half of defaults a year in advance; combine them with qualitative triggers and 30/90 days-past-due backstops for full coverage — the architecture IFRS 9 SICR frameworks are built on.

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Are your SICR triggers still fit for purpose?

Credit risk does not stand still – and neither should the frameworks used to identify it.

SICR frameworks should be periodically reviewed and re-evidenced against recent default experience to ensure triggers remain responsive, proportionate and effective. Should your staging triggers require a health check, BDO Advisory's Credit Risk Solutions team are able to perform a comprehensive review of your SICR framework and trigger definitions against our latest research and publicly available data.

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