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LATAM BONDWRAP: Fiscal Challenges Await High-Yielders in 2023

By Scott Squires

(Bloomberg) -- The biggest challenge facing Latin America's high-yield sovereign issuers in 2023 will be balancing fiscal accounts in a context of higher interest rates and continued global volatility, according to BancTrust & Co.

- "Fiscal consolidation needs to be stepped up in Latin America's high-yield sovereign credits for investors to return," said Ramiro Blazquez, head of research and strategy at BancTrust in Buenos Aires
- BancTrust is overweight Ecuador and El Salvador, which are oversold and could see spreads compress in 1Q23
 - "El Salvador has the resources to continue servicing its debt, which is in Bukele's interest. Non-payment will result in a recession and a spike in crime, which would undercut his popularity after running on a tough-on-crime platform"
 - El Salvador bonds are pricing in an aggressive restructuring, although a bond payment due this month should trigger spread compression
 - "We think El Salvador bonds should be priced at least at 50 to 60 cents on the dollar"



- BancTrust rates Peru, Panama and Honduras underweight, Blazquez said
 - Peru is rated underweight because of "political tensions and uncertainty over how the institutional fallout will work out after Castillo"

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- Panama is nearing a credit rating downgrade because its fiscal situation is vulnerable as authorities use aggressive subsidies to control high inflation
- “We don’t like Honduras very much,” Blazquez said. Although their fiscal balance has improved, they “have been afraid of spending, and are under-executing the budget”
- To be sure, Central American credits have made “noticeable leaps” in shoring up fiscal accounts after the pandemic
 - Many upcoming large maturities were addressed via liability management in recent years, and these countries have been keen on building reserves
 - Dominican Republic has issued aggressively, while also building significant reserves, and investors have rewarded Costa Rica for sticking with its fiscal consolidation plan
- Argentina’s bond rally may be short lived, as the FX situation is becoming more dire and risk is high that the government will devalue the currency before June or July
 - “The incoming government after this year’s elections needs to prove they have the willingness and capability to enact change. To improve bond prices further, they would need to present evidence for that, although Argentina will need to restructure its debt once again in 2024”

Index/Security	Latest	1W Chg
JPMorgan EMBIG Div. Latin Sov. Sprd (bps)	428	10
JPMorgan EMBIG Div. Sov. Sprd (bps)	465.7	10.4
Brazil 10-year yield (%)	6.03	-0.14
Mexico 10-year yield (%)	5.86	-0.11

PRIMARY MARKET

- Mexico started off 2023 with a \$4 billion sale of dollar bonds, becoming the first major emerging-market government to tap international debt markets this year

SECONDARY MARKET

- Investors have little faith in negotiations to restructure Unifin Financiera SAB’s defaulted debt with the bonds worth mere pennies as Mexico’s largest non-bank lender struggles to keep its businesses afloat
- Mexico’s Petroleos Mexicanos is evaluating debt payment options with the Finance Ministry as the company struggles to convert high oil prices into profits amid weak production and a focus on refining instead of exporting its crude
- Brazilian hedge funds enjoyed the best returns in six years in 2022, profiting from everything from hiking cycles to the sharpest decline in equity markets since the global financial crisis in 2008
- Brazilian President Luiz Inacio Lula da Silva has pledged to steer the state-controlled oil giant Petrobras in a more populist direction and investors aren’t happy

ECONOMY

- Chilean President Gabriel Boric on Thursday announced a new package of social spending worth \$2 billion as his approval levels fall and the economy shrinks
- Chile’s consumer prices posted the smallest monthly increase since last February, boosting expectations that inflation is slowly easing toward target

- Argentina's President Alberto Fernandez is seeking to impeach the leader of the nation's Supreme Court, a maneuver that's unlikely to succeed in congress
- Brazil's central bank will be even slower to cut its benchmark interest rate from the current level, according to economists who see inflation expectations deteriorating further in the first few years of Lula's administration

For more, see:

- LATAM BOND PIPELINE: Chile's CGE Transmission, Care Caledonia
- SOUTHAM DAYBOOK: Peru Protests Continue; Chile Inflation, Trade
- Bloomberg Latin America Index Down, OAS Widens

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