JANUARY 25 THROUGH JANUARY 31

GRAMERCY EM WEEKLY:

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FEATURING:

ARGENTINA | PERU | UKRAINE

Debt amortizations, elections and central bank decisions take center stage.

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Province of Buenos Aires debt amortization payment of $250 million due on January 26th

Market Relevance: The approach taken with the province's debt will be watched closely, particularly in the context of foreshadowing of the strategy for sovereign debt negotiations. The government has given BUENOS 2021 investors the ultimatum of postponement of payment until May 1st or risk hard default. The authorities need to achieve consent of 75% of holders by January 31st to delay the payment and avoid default. They will have a 10-day grace period beginning January 26th (ending February 7th) to cure the default if payment is not made and consensus is not reached. The price of the bonds dropped 25 points this month reversing the rally witnessed throughout December.

Gramercy View: Absent obtainment of necessary consent, we believe there is a non-negligible chance for hard default on the provincial debt given the authorities' statements on the topic thus far, limited upside from draining sovereign resources to pay, and arguably weakened negotiating power in sovereign negotiations if the government decides to bail out the province. The government's approach to the province may provide indication of their plans for sovereign debt. The administration has made clear efforts to ensure sovereign USD bond payments are made in the short-term but it is likely that this prioritization of debt service will be temporary, especially as the redemption profile becomes more challenging into the spring. The government may attempt to use the threat of a hard default at the sovereign level, which risks policy radicalization and prolonged period of non-payment, to its advantage. An example of this could be an offer to bondholders that results in acceptable recovery levels relative to current prices, but in turn provides the government with flexibility on the timeline of IMF negotiations as well as commitment to policy trajectory. If the market did not accept such a proposal due to lack of policy anchors, both the administration and investors risk further entrenchment of the ongoing crisis. Conversely, acceptance of this type of deal could limit the scope of the sovereign's market access until additional clarity is provided on the IMF and the government's policy agenda.

Peru to hold legislative elections on January 26th

Market Relevance: President Vizcarra controversially dissolved Congress last fall and scheduled new elections for this Sunday to improve governability. The Constitutional Tribunal has since ruled the action as constitutional, confirming this weekend's vote. Peru remains vulnerable to latent political and social volatility risks given a strong distrust of the political class amid high corruption and inequality.

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Gramercy View: The election will likely result in a moderate improvement to governability and support for Vizcarra in the short-term. However, we anticipate only limited reform momentum given the brief timeframe between now and the next general election scheduled for April 2021, at which point, the prospects for emergence of an anti-establishment candidate are decent. This could threaten policy credibility, albeit it is too soon to discern the details of possible outcomes. In the meantime, we believe growth will pick-up to around 3% this year compared to an estimated 2.5% last year. The fiscal situation should remain largely unchanged in the near-term.

National Bank of Ukraine's (NBU) policy decision on January 30th

Market Relevance: It is a question of how much the NBU will cut its monetary policy rate next week, not if it will cut its rate. Market consensus calls for a 200bps cut to 11.5% from 13.5%, but it will not be a huge surprise if the NBU delivers even more easing. Supported by continuing disinflation, real interest rates in Ukraine are currently the highest (~9.5%) in global EM, which leaves the central bank with plenty of space to deliver further monetary stimulus and support the already good macroeconomic performance expected for Ukraine in 2020.

Gramercy View: Ukrainian local currency assets were one of the best investment stories in EM in 2019. Given the disinflationary dynamics, improving macroeconomic framework and fading geopolitical concerns, the NBU will very likely remain on an interest rate cutting path throughout 2020 while still being able to maintain a solid real rates buffer relative to most EM peers. As such, exposure to local assets in Ukraine gives fixed income investors a unique combination of declining rates and, at a minimum, a stable currency (after significant Hryvna appreciation in 2019).

Please contact our Co-Heads of Sovereign Research with any questions:

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