An APS conference call

# Outlook 2021: Emerging markets sovereign and corporate debt

December 10, 2020

Steven Abrahams, sabrahams@apsec.com, 1 (646) 776-7864
Stephen Stanley, sstanley@apsec.com, 1 (203) 428-2556
Siobhan Morden, smorden@apsec.com, 1 (646) 776-7777
Jose Kliksberg, jkliksberg@apsec.com, 1 (646) 776-7778

# Overview

- Markets: Five things to know for 2021
- Economy: Upside surprises in 2021
- Latin America Sovereigns: Choose wisely
- Latin America Corporates: Split the difference

# MARKETS: FIVE THINGS TO KNOW FOR 2021

- The yield curve should steepen faster than forward rates imply
- Lower-rated credits should outperform higher-rated credits
- Private debt should deliver strong returns
- Debt from best-in-class niche platforms should do well
- Returns to informationally intensive assets should run above average

# ECONOMY: UPSIDE SURPRISES IN 2021

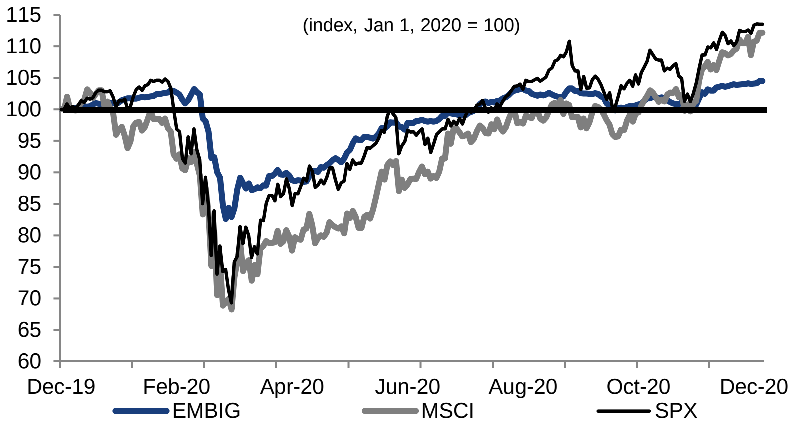
- Consensus 2021 economic forecasts: 3% real GDP growth, unemployment rate falls to around 6% by end of year, and inflation settles at 1¾%.
- Three possible surprises for next year:
- 1. A Near-Complete COVID Recovery
- 2. Labor Market Approaches Full Employment by End-2021
- 3. Inflation Could Be Up or Down in 2021

# APPETITE FOR YIELD BUT REQUIRES CAREFUL SELECTION OF SINGLE B CREDITS

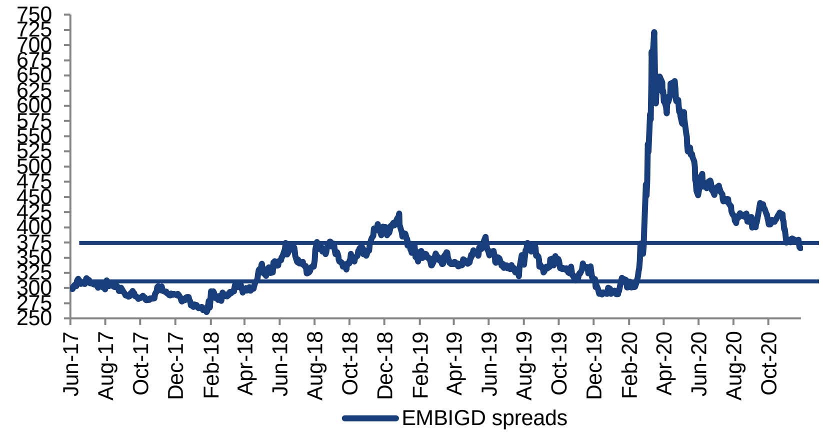
- The abundant global liquidity prioritizes high yield returns. EM and specifically LatAm offer high yield but also require careful credit risk selection.
- The solvency and potentially rollover/liquidity problems explain why there hasn't been normalization of B credit yields to pre-Covid levels.
- The excess global liquidity and negative yields does not infer liquidity access for all credits.
- The IMF role is important, but execution risk is high for difficulty of pro-cyclical fiscal austerity amid slow economic recovery and sometimes election or ideological constraints.
- Argentina is my least favorite credit. Ecuador valuations appear fair on assessment of political and policy risks ahead of elections.
- The normalized Costa Rica yields do not compensate for high rollover risk and unresolved solvency risks for a country in a debt trap that can't agree on an IMF program.
- There is better risk/reward for high El Salvador yields, manageable rollover risk near term and the positive shock of an IMF program post elections.
- Uruguay global local linkers have been our secular favorite trade.

# EM LAGGING OTHER RISKY ASSETS WITH SINGLE B CREDITS FAILING TO NORMALIZE

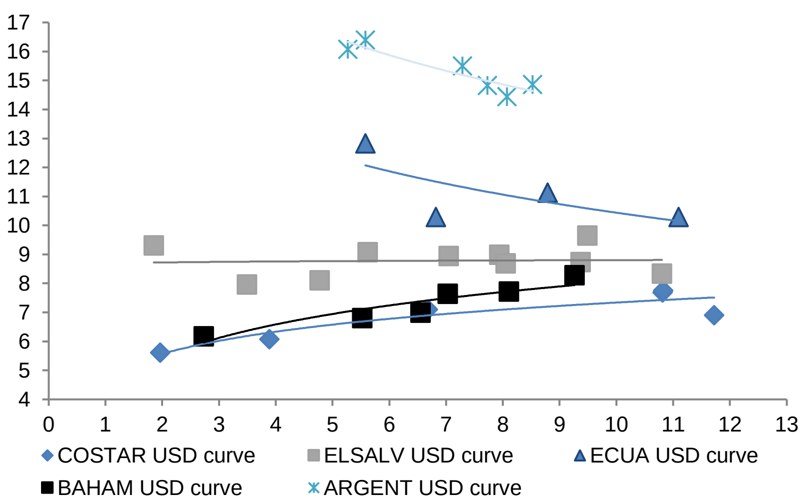
## EMBIG now in YTD positive territory



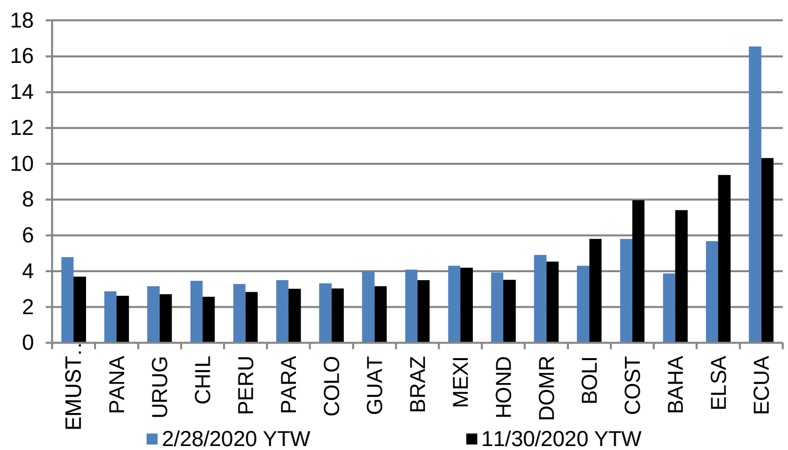

## EMBIG spreads still above pre-Covid levels




## The distressed curves for B/BB credits




## The failure of single B credits to normalize

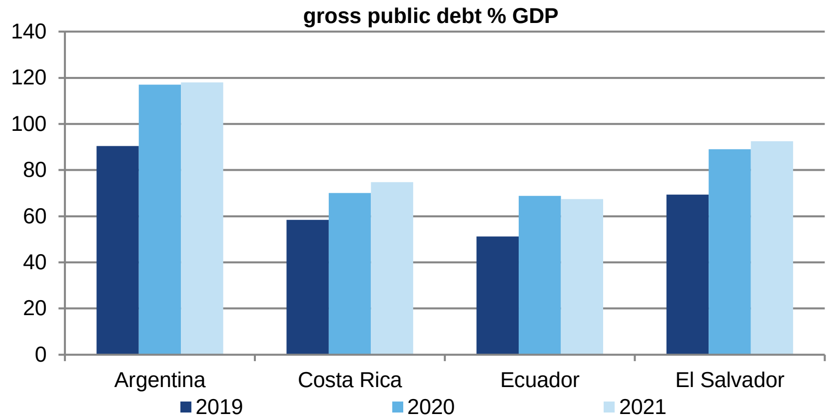



Source: Bloomberg, Amherst Pierpont Securities

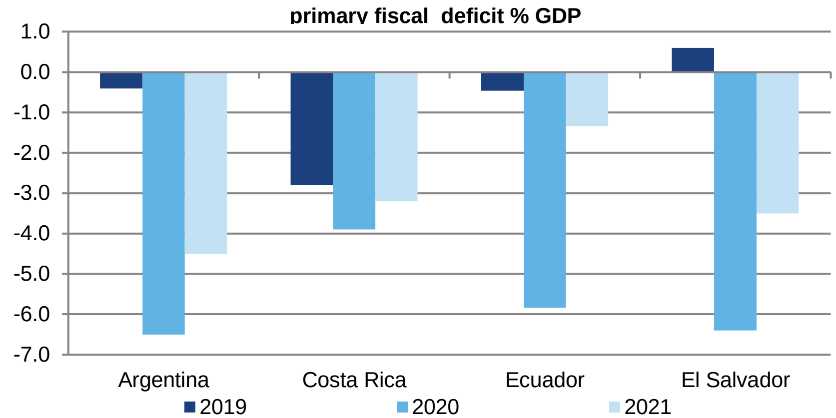
Siobhan Morden

# THE DETERIORATION IN SOLVENCY RATIOS POST COVID SHOCK

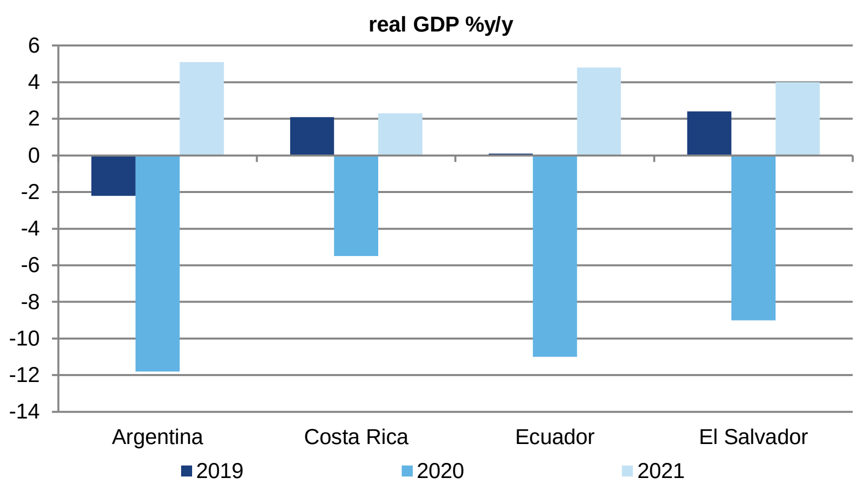
## Worsening debt ratios



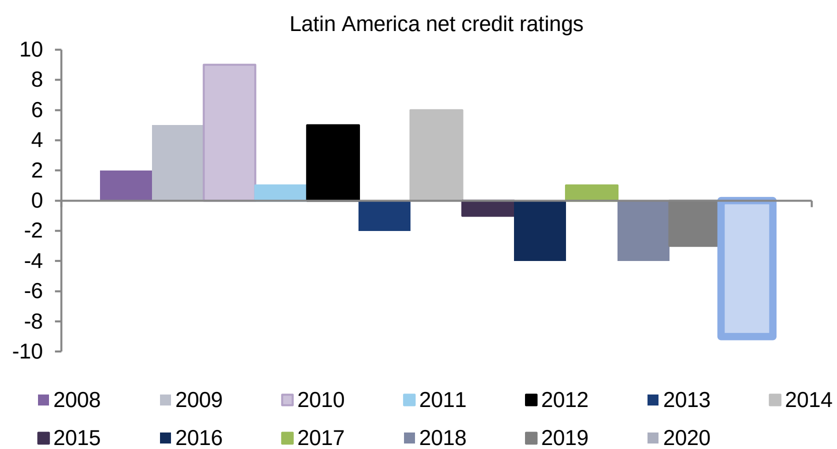

## The hit to cashflow




## The slow path to return to trend growth



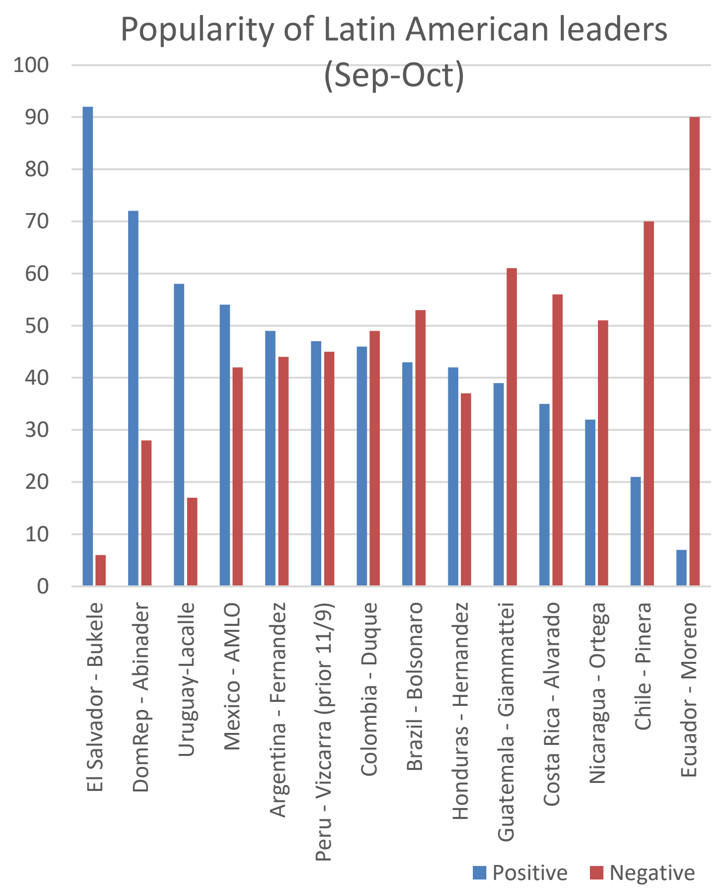

## The net decline in Moody's credit ratings +/- one notch upgrade/downgrade for Latin America



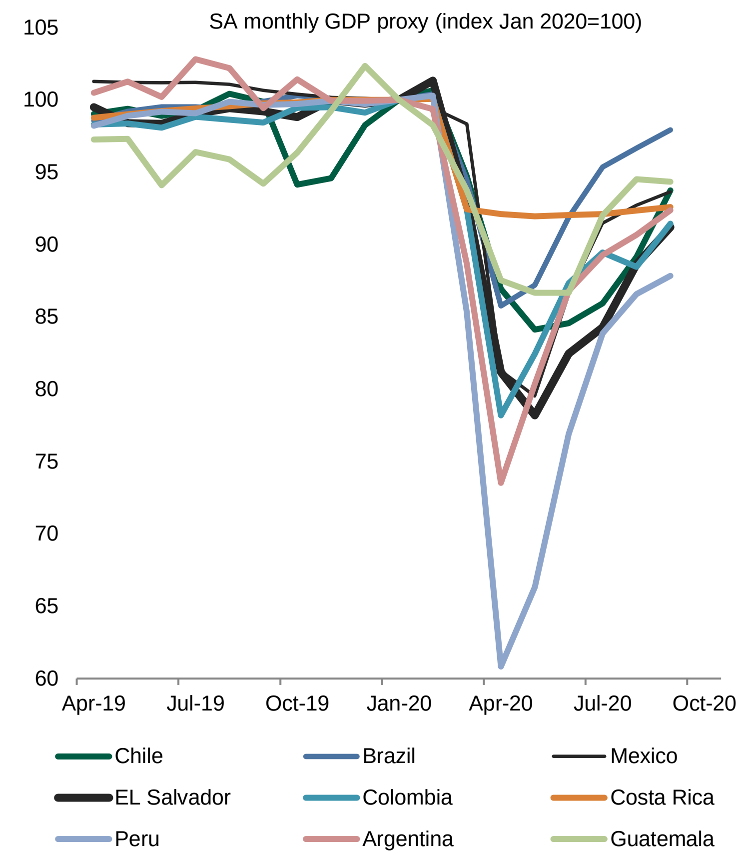

Source: Bloomberg, IMF, official sources, Amherst Pierpont Securities

# THE EXECUTION RISKS FOR IMF PROGRAMS

## The governability of leaders




## The pace of economic recovery




Source: www.latercera.com, official sources, Amherst Pierpont Securities

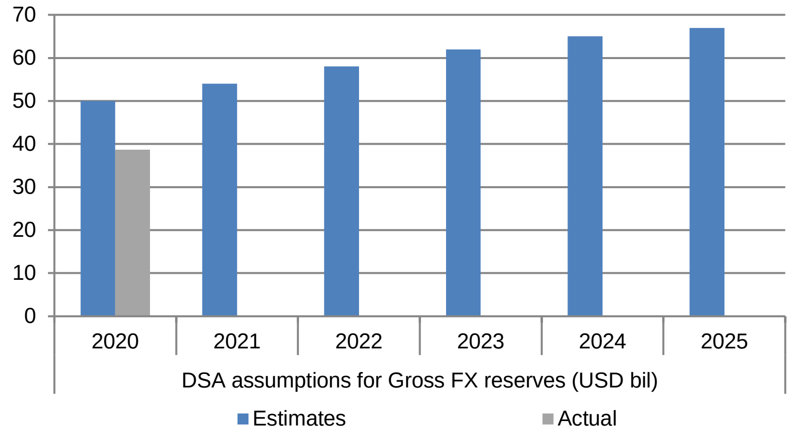




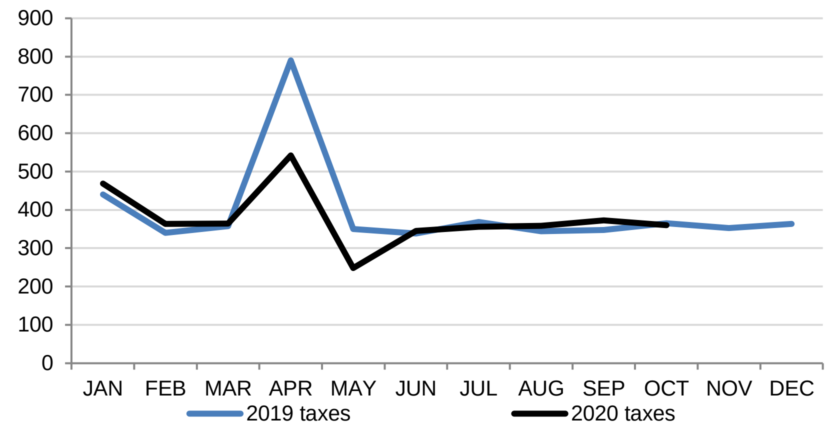
AMHERST PIERPONT

# The main challenges for single B credits in Latin America

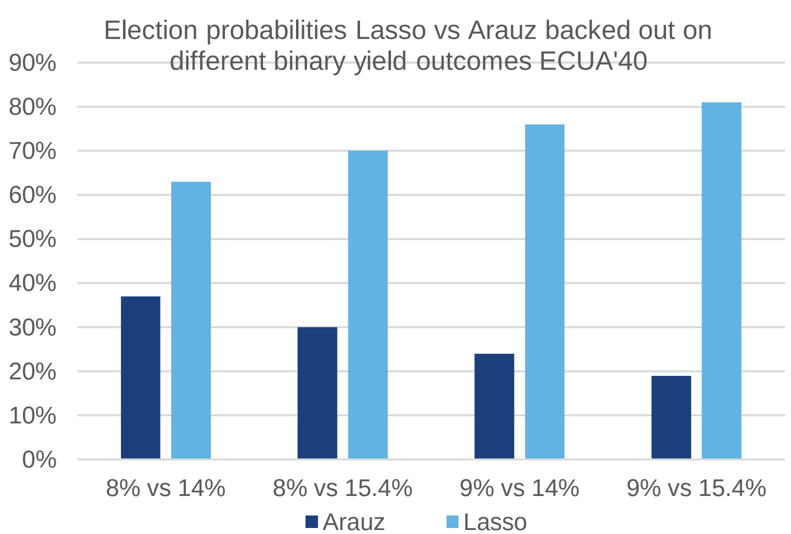
## Argentina needs to rebuild liquidity



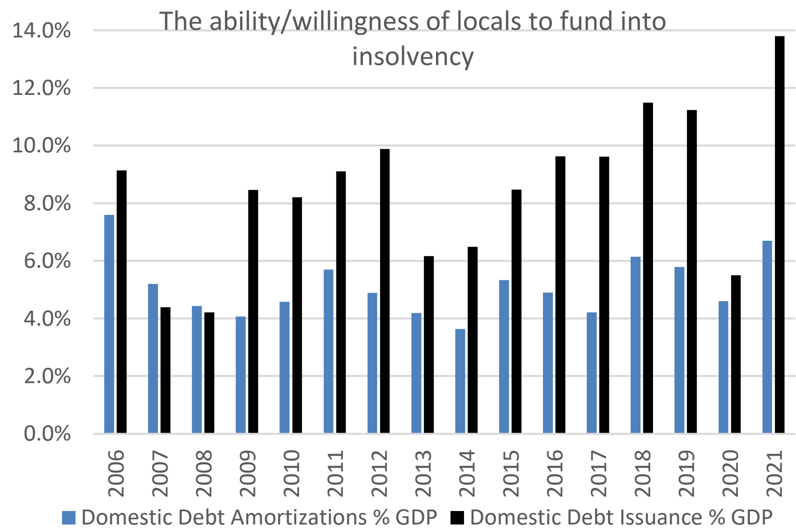

## El Salvador taxes show full recovery




## Ecuador – election risk and policy risk




## Costa Rica faces high rollover risks next year




Source: Bloomberg, BCRA, BCR, Hacienda.go.cr,Amherst Pierpont Securities





AMHERST PIERPONT

## LATAM CORPS STILL OFFER YIELD BUT CREDIT DIFFERENTIATION IS PARAMOUNT TO FIND IT

- EM corporates are still a compelling asset class, offering both yield and spread compared to DM. However, yield and returns are concentrated in certain regions and pockets
- Ample global liquidity and still under-allocation to EM corps could be a driver for excess returns in years ahead
- The case for EM Corporate debt is there: the JPMorgan CEMBI broad diversified index with a spread to UST of 300 bps and YTW 3.7% versus Barclays US Corporate Aggregate Index OAS of 100 bps and YTW 1.85%
- Our preference is for Latam corps. Within Latam HY over IG, given potential US rates moves affecting steeper Latam IG curves within EM, underlying sovereigns still exposed to weaknesses, and outperformance of IG Vs. HY in 2020.
- Existing pockets of yield and/or value in Latam include:
    - Brazilian companies in a deleveraging path with exposure to commodities and China's growth (Braskem, Cosan, Suzano, CSN)
    - Perpetuals like AES Gener with callability potential
    - Mexican non-bank lenders & subordinated bank debt (Banorte)
    - Less liquid but solid names in Central America (AES El Salv & Dom)
    - Very selective Argentine Corps (Aeroar)
    - Themes: Colombia downgrade, Mexico's gov't linked bonds

# Disclaimer



This material is intended for discussion purposes only and is not meant to be, nor shall it be construed, as an offer or commitment by Amherst Pierpont or any of its affiliates to enter into any transaction. Should Amherst Pierpont subsequently seek to enter into any transaction, any such transaction would be subject to the conditions stated in the documentation therefore at that time.

In connection with recipient's decision to enter into any transaction, or to purchase or sell securities or other financial instruments, the recipient is advised to undertake an independent review of this material, and the potential legal, tax, regulatory and accounting implications of any transaction described herein to determine whether such a structure would be suitable for such recipient's particular situations. Amherst Pierpont is not providing any investment, legal, accounting, tax, financial or other advice to the recipient, nor is it acting as an advisor or fiduciary in respect of the recipient. This presentation is not intended to form the basis of an investment decision and contains insufficient information to make an investment decision. Amherst Pierpont accepts no responsibility or liability as to any reliance placed, or investment decision made, on the basis of such information by the recipient. Any illustrations contained herein are provided as examples only.

In making this material available, Amherst Pierpont (i) is not making any predictions or projections, (ii) intends that any recipient to which Amherst Pierpont has provided this material is an "institutional investor" (as defined under applicable law and regulation, including FINRA Rule 4512) and (iii) intends that this material will not be disseminated, in whole or part, to any third party by the recipient without Amherst Pierpont's prior written consent.

This material (i) has been prepared for information purposes only and does not constitute a solicitation or an offer to buy or sell any securities, related investments or other financial instruments, (ii) is neither research, a "research report" as commonly understood under the securities laws and regulations promulgated thereunder nor the product of a research department, (iii) has not been prepared in accordance with legal requirements designed to promote the independence of investment research, and is not subject to any prohibition on dealing ahead of the dissemination of investment research.

Amherst Pierpont (i) makes no representation or warranties as to the appropriateness or reliance for use in any transaction or as to the permissibility or legality of any financial instrument in any jurisdiction, (ii) believes the information in this material to be reliable, but has not independently verified such information, parts of which may have been obtained from third party sources, and makes no guaranty or representation, express or implied, with regard to the accuracy or completeness of such information, and (iii) does not undertake, and disclaims any duty to undertake, to update or to revise the information contained in this material. Unless otherwise stated, the views, opinions, forecasts, valuations, or estimates contained in this material are those solely as of the date of publication of this material, and are subject to change without notice.