

Despite debt restructuring, Argentina is not out of the woods

By: Emerging Markets Debt Team | September 22, 2020

Boston - Argentina took a significant step forward with its recent debt restructuring by alleviating fears that it was headed for a long, drawn out negotiation process. Nevertheless, the country has a long way to go both in terms of addressing near-term negative market sentiment and concerns over longer-term economic and market policy.

The government hoped that the restructuring would lead to a U-turn in sentiment for investors — one that would magically stabilize the dislocation of the peso in the foreign exchange (FX) market. That failed to materialize — Argentina's dollar-denominated bonds have continued to sell off, and yields are now above 13%. The drain on the country's reserves continues, as everyone is buying as much US dollars as possible.

During the recent restructuring negotiations, advisers to President Alberto Fernandez signaled that he wanted a "market-friendly" restructuring, and he appears to have achieved that. But we still have significant concerns that the fundamental rule of law and respect for free markets may be overshadowed by the whims of Vice President Cristina Fernandez de Kirchner (CFK). CFK is a former president who last year tapped Fernandez (no relation), a relative unknown, to run as president, while she ran as vice president. For example:

- The Argentine Senate removed three judges put in place that were investigating CFK and her family.
- The government decided to cut transfers to the City of Buenos Aires, which is controlled by an opposition politician, to fund wages for policemen in the Province of Buenos Aires, which is controlled by a CFK loyalist.
- The 2021 budget target of -4.5% primary deficit indicates minimal desire to cut spending.
- Number of companies have announced they are leaving the country, including airlines, department stores and even Nike.
- Instead of moving the official FX rate to a more market-determined level, the government is persisting with capital controls, which could lead to a full-blown currency crisis.

There are a few possibilities for brightening Argentina's outlook:

- Midterm elections are in a year, and widespread discontent could pave the way for a big victory by the opposition, which might prove to be a turning point in policy.
- Commodities that Argentina exports, like soy, wheat, corn and beef, have undergone a huge rally. This could significantly help exporters, especially if the peso is allowed to depreciate to a more market level.
- With consistent rhetoric from locals that Argentina is on its way to becoming a political and economic outcast like Venezuela, terrible sentiment may be bottoming out.

Bottom line: We continue to follow developments very closely, as there are frequently short-term opportunities that arise for the country's debt. But getting comfortable with a long-term view on Argentina is very difficult, given the policy direction we have seen so far from this government.



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