

Latin American 2021 Corporate Credit Outlook:

A Year Of Varying Recovery

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S&P Global
Ratings

LatAm Corporate Credit Outlook 2021

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Key Takeaways

Economies in the region are picking up steam, but they remain vulnerable to setbacks due to the fragility of the recovery and the fact that governments don't have much room for additional fiscal stimulus if a second wave occurs.

Latin American countries are more resilient to withstand crises than a few decades ago, which has helped substantially to sustain credit quality among corporations. In fact, most sectors managed to reduce debts by taking decisive measures to control damages and protect cash.

The hit from the pandemic has varied widely among sectors. S&P Global Ratings expects industries like airlines, transportation infrastructure, gaming and leisure, hotels, retail restaurants, oil & gas, and commercial and office real estate not to recover to pre-pandemic credit ratios until at least 2022. Additionally, a further wave of COVID-19 could be catastrophic for them. On the other hand, other sectors had impressive performances this year, such as building materials, homebuilding and long steel, while copper and iron ore exporters enjoyed record prices. Supermarkets were among the top performers of all retail categories.

The corporate default rate has stayed low. The rate remains at an impressively low 3.3%; well below our previous estimates. This is mainly due to the abundant and timely credit supply from banks and the active rollover the debt markets offered. Although the rate could climb further, we don't think it will reach 5%.

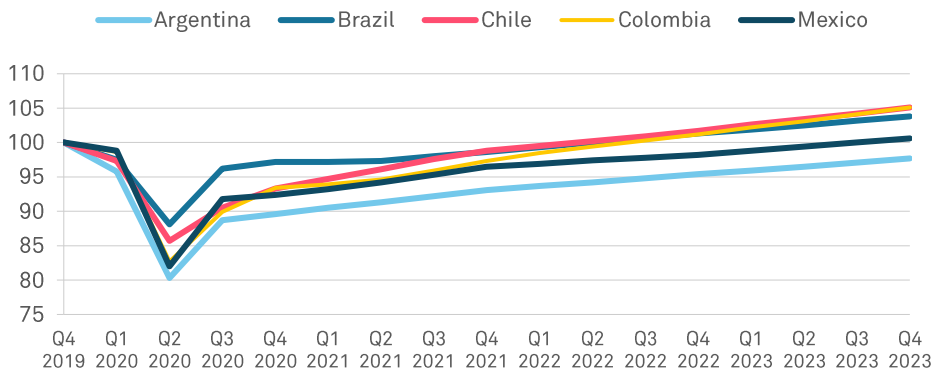
Debt market conditions to keep improving. Overall, we expect international debt markets to continue improving for Latin American issuers as credit conditions improve, illustrated by the recent compression in spreads. We also forecast domestic markets to recover some of their lost shine as currencies recover ground and medium-term visibility improves.

S&P Global Ratings believes there remains a high degree of uncertainty about the evolution of the coronavirus pandemic. While the early approval of a number of vaccines is a positive development, countries' approval of vaccines is merely the first step toward a return to social and economic normality; equally critical is the widespread availability of effective immunization, which could come by mid-2021. We use this assumption in assessing the economic and credit implications associated with the pandemic (see our research here: www.spglobal.com/ratings). As the situation evolves, we will update our assumptions and estimates accordingly.

• Recovery Trajectories Are Uneven Among Countries

Since September 2020, every major economy in Latin America has been on a clear recovery path. However, in our view the speed of the recovery will be slowest in emerging markets, with those economies on average returning to 2019 levels sometime between June 2022 and June 2023, with the only exception being Argentina that will likely reach that point in 2024 (see chart 1).

Chart 1 – Projected GDP Level Versus Pre-Pandemic Level



Source: S&P Global Market Intelligence, S&P Global Ratings estimates.

The relatively slowness of the region's recovery results from a combination of the severe damage inflicted by lockdown measures to the labor markets, the economic imbalances that these countries faced before COVID-19, and the relatively low investment patterns. What's more, **the region remains vulnerable to setbacks due to the fragility of the recovery and the fact that governments don't have much room for additional fiscal stimulus if a further wave unfolds.** On the positive side, COVID-19 cases have been dropping as most of the countries in the region head into summer, and by the time the temperature starts falling (at least in South America), vaccination programs will likely be fairly advanced.

Argentina. We expect the country's GDP to contract 11.7% in 2020 and bounce back only 4.0% in 2021. We think the country will likely only reach its pre-pandemic GDP by 2024 as it deals with several economic problems such as high inflation, a heavy foreign-currency debt burden, and low international reserves. We cap most of the Argentine companies we rate at 'CCC-'; the level of our assessment of Argentina's transfer and convertibility (T&C) assessment, which signals a high chance of these entities not being able to make foreign currency payments if the country restricts them to protect reserves.

Brazil. The Brazilian economy is recovering faster and stronger than we expected. We anticipate Brazil's economy to be the least affected in the region, contracting merely 4.7% this year and expanding 3.2% in 2021. The fall has been among the lowest due to Brazil's less stringent lockdowns, large government transfers to low-income inhabitants, and the fact that the prices of the country's main export commodities remained strong. In general, Brazilian companies have enjoyed support from the government and the domestic financial system to roll over their debts and secure liquidity. The combination of government measures and funding availability yielded corporate credit resiliency.

Chile. The economy showed some lag in Q3, mostly due to retightening of lockdowns, but we expect a strong recovery in Q4 that will moderate the GDP contraction to 6.4% in 2020. GDP would then expand 5.2% in 2021. Still, the Chilean society is demanding significant political changes including a new constitution, which heightens downside risks to our assumptions. In any case, we don't expect meaningful adverse impacts from those changes to Chilean corporations.

Colombia. The country's oil exports were severely hit during the first semester and lockdowns were re-installed in August in certain cities such as Bogota, which hurt economic performance further. We still expect GDP to contract 7.8% in 2020 and a relatively strong bounce back in 2021 of 5.1%.

Mexico. The Mexican economy has had one of the worst performances of 2020 in the region. We expect it to shrink by 9.3% because mild government stimulus couldn't contain much of the damage inflicted on small and midsize enterprises (SMEs) while the country also suffered from low oil demand and prices and the complete stall of the tourism industry; two important fiscal revenue contributors for Mexico. We expect the country to grow 3.9% in 2021.

For more economic insights, please read "[Latin America's Economic Recovery From The Pandemic Will Be Highly Vulnerable To Setbacks](#)," Dec. 1, 2020.

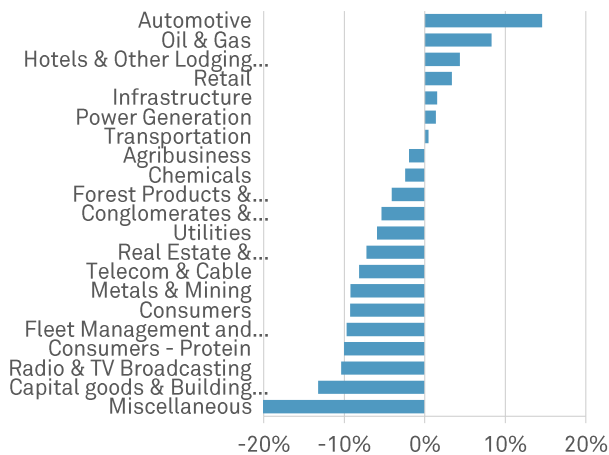
• **The First Wave Put Corporates To Test**

In our view, one of the most important takeaways the region learned from the COVID-19 pandemic is that government stimulus created real positive effects, helping companies and individuals to weather tough times. Second, lockdowns won't make viruses go away, but they do delay the effects and buy precious time to prepare. Third, extremely stringent lockdowns cause deep damage across multiple layers of an economy from which recovery is very difficult (Argentina is an example of this).

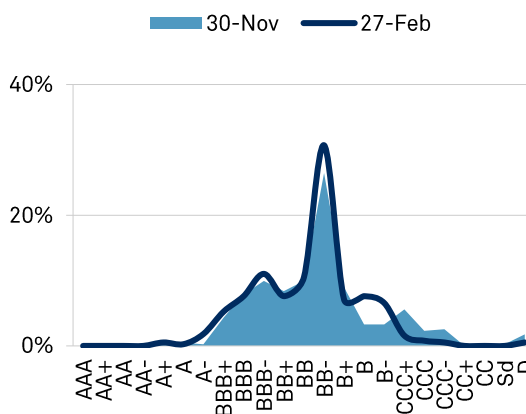
Unlike in past crises, this time the region was generally much better prepared to deal with the economic and financial side effects. With a few exceptions like Argentina, at the onset of the pandemic **countries' debts were mostly domestic, Latin American countries' international reserve levels were higher than in previous crises, and the financial systems were well capitalized and had overall good awareness of credit risk.** These factors, combined with governments' financial assistance to companies and individuals, played a decisive role in containing damage and reducing default rates (please see default rate estimates a few sections below). **In fact, leverage actually improved in most sectors as companies adopted more stringent financial policies and protected cash.** Chart 2 shows that the number of sectors that reduced net debt as of September 2020 versus March 2020 was double those that increased debt. Of the sectors that ended up with more debt, only one exceeded 10% growth (automotive).

Chart 3 shows that companies with higher ratings ('BB-' and above) withstood the impact of the pandemic better than those with weaker ratings--as we expected. We downgraded many issuers that we rated in the 'B' category at the onset of the pandemic, with some eventually defaulting.

Chart 2 – Change In Net Debt Since The Outbreak, By Sector **Chart 3 – Corporate Ratings Distributions In LatAm, Current And Before The Outbreak**



S&P Global Market Intelligence, S&P Global Ratings calculations.

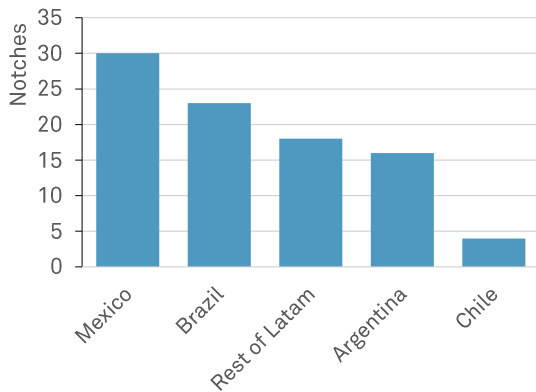


S&P Global Market Intelligence, S&P Global Ratings calculations.

Out of about 90 downgrades we made in Latin America from March to November, the most were based in Mexico, followed by Brazil, Argentina, and Chile (see chart 4). However, judging by the size of the rated portfolio in each country, Argentina's and Mexico's credit deterioration were much worse than those of Brazil and Chile. Additionally, the proportion of entities with negative outlooks remains higher in Argentina and Mexico, further discussed in the next section.

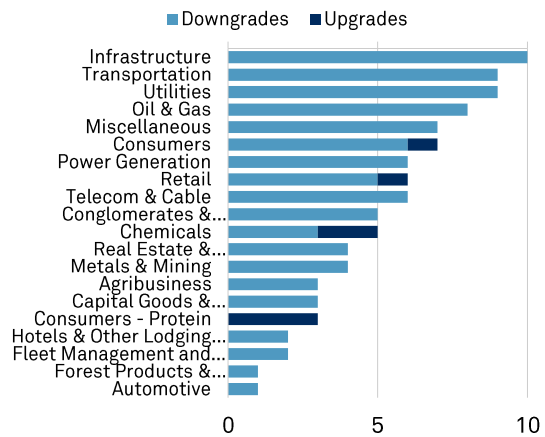
Lockdown measures hit hardest for assets that have cash flows correlated to human or goods mobility such as airports (infrastructure), airlines (transportation), oil and gas producers and distributors, and leisure and gaming companies (grouped in miscellaneous and hotel and lodging). Nonessential retail and consumption, automotive, and commercial real estate (office and shopping malls), sectors also struggled (see chart 5).

Chart 4 – Rating Downgrades Since The Outbreak, By Country (Notches)



S&P Global Market Intelligence, S&P Global Ratings calculations.

Chart 5 – Rating Actions Since The Outbreak, By Sector (Notches)



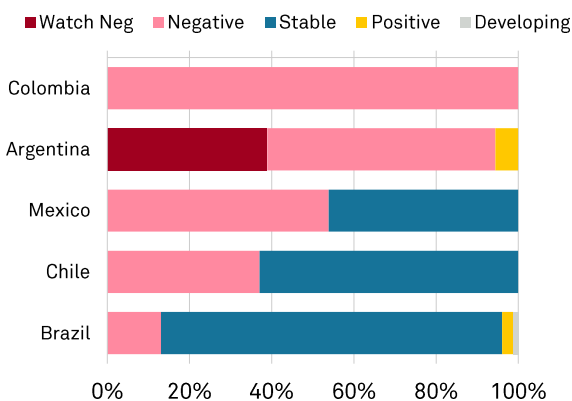
S&P Global Market Intelligence, S&P Global Ratings calculations.

• More Sectors Have Improving Prospects, But Full Recovery Won't Arrive Until After 2021

The proportion of ratings with negative outlooks or on CreditWatch with negative implications remains elevated, at 33% for the region, but downside risk is not evenly distributed by country. Most corporations in Colombia and Argentina have negative outlooks or are on CreditWatch negative, while credit conditions in Brazil (where 13% have negative outlooks) and Chile (37%) are more stable (chart 6). Much of the downside risk corporations face in Colombia, Argentina, and Mexico stem from those countries' weaknesses detailed in the prior section, and the negative outlooks on those sovereigns pressure the corporate ratings there.

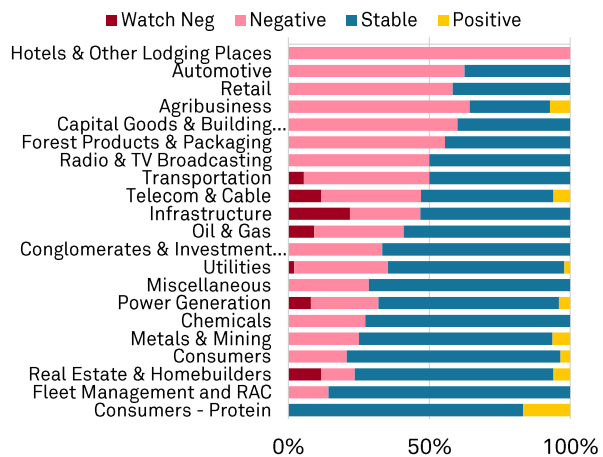
Some sectors were hit harder than others, and their recovery will last a few years. Sectors like hotels and other lodging, automotive, retail, capital goods and building materials, forest products, radio and TV broadcasting, and transportation still constitute a large portion of the downside risk--at least 50% of the rated entities in these sectors have negative outlooks (chart 7).

Chart 6 – Outlook Distribution By Country



S&P Global Market Intelligence, S&P Global Ratings calculations, as of Nov. 30, 2020.

Chart 7 – Outlook Distribution By Sector

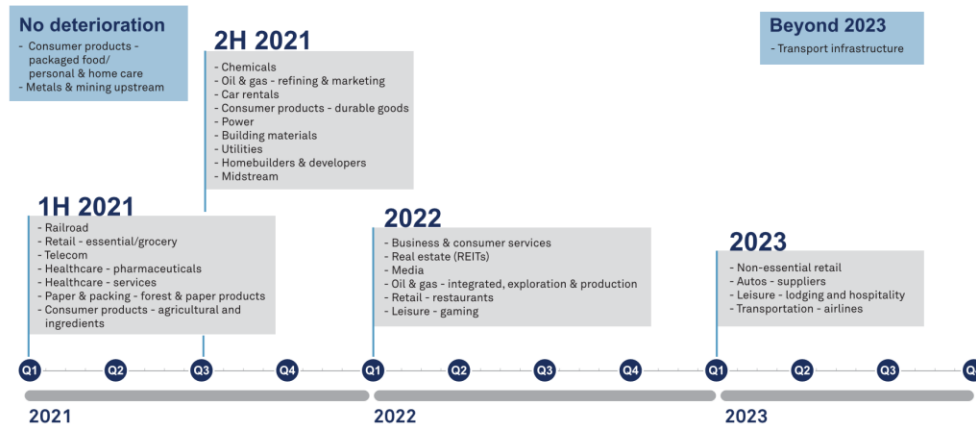


S&P Global Market Intelligence, S&P Global Ratings calculations, as of Nov. 30, 2020.

The timetable below shows what we think could be the recovery speed of the main rated sectors in Latin America. While we expect large sectors like consumers- durable goods, essential retail, forest &

paper products, agribusiness, power, building materials, utilities, homebuilders, and car rentals to bounce back to the credit ratios they had before the pandemic in 2021, sectors like oil & gas exploration and production; retail – restaurants; leisure, gaming, and lodging; real estate; auto suppliers, non-essential retail; transportation – airlines and transportation – infrastructure are likely to take more than 24 months to recover.

Timeframe Of Recovery Of (Run Rate) Credit Metrics To 2019 Levels
Latin America

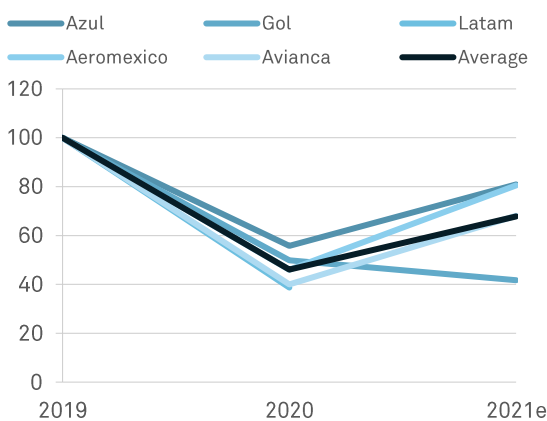


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These estimates don't incorporate a full-fledged new wave of COVID-19. We assume that any resurgence of the virus wouldn't trigger large-scale lockdowns, and that it wouldn't be as contagious and deadly as the prior one provided that vaccination reaches the more exposed sections of the population by the time the virus resurges, which might be around April 2021 when temperatures start to fall more markedly in the southern hemisphere.

Our forecasts also assume that if the virus spreads again rapidly; governments would try to alleviate mobility restrictions as much as possible to lessen the economic impact. That--combined with the high rate of adoption of online trading, online payments, and remote working—would help soften the impact. Still, a new wave of COVID-19 could be catastrophic for industries like airlines, transportation infrastructure, gaming and leisure, hotels, retail restaurants, oil & gas, and commercial and office real estate. The impact of COVID-19 on the airline industry is one of the most striking: of the five airlines we rate or rated in Latin America, the three that more exposed to international flights defaulted while the other two that were more domestic are rated in the 'CCC' category. The chart below details the impacts.

Chart 8 – Latin American Airlines, Change In Available Seat Per Kilometer (ASK) (2019:100)



In 2020, airlines had to cut capacity to an average of 46% of the previous year. We expect them to increase it back to just below 70% in 2021, also compared to 2019. Even though they renegotiated lease agreements on their fleets and shrunk them, their capital structures remain overleveraged as losses squeezed equity. Absent a substantial recovery in demand and meaningful equity contributions, these companies will struggle to come back to pre-pandemic credit ratios.

In contrast, demand for building materials has recovered to pre-

S&P Global Ratings calculations.

pandemic levels or even above, in the case of Brazil. The recovery of the building materials sector is impressive and, in our opinion, was largely driven by cash transfers to low and middle income sectors, which in Brazil and Chile took the form of micro-withdrawals from the pension savings—nicknamed "corona checks" in Brazil. It was also driven by the need to refurbish homes to adapt to working from home and by the low interest rates. The rise in cement demand (chart 9) is also occurring in other steps of that value-chain, such as long steel and homebuilding.

Supermarkets' operations were among the least affected of the retail spectrum. Still, of the main five countries we analyzed in South America, as of September 2020 Argentina and Mexico's supermarket sales were below last year's, adjusted by inflation (chart 10). That is for the most part the performance observed in the main categories of essential retail.

Chart 9 – Cement Volumes Sold In Selected Latin American Countries (Nov-2018 Volumes=100)

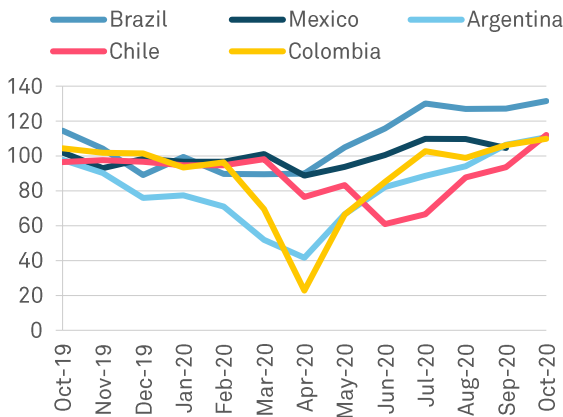
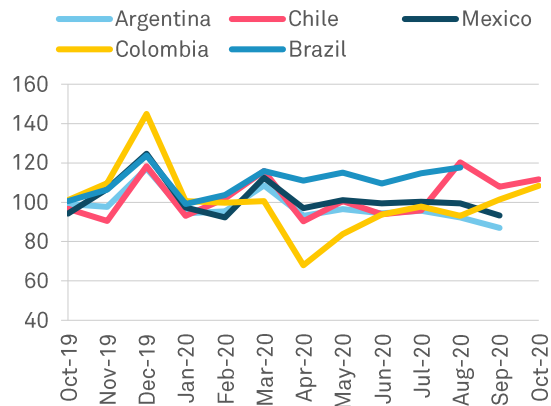


Chart 10 – Supermarket Sales Adjusted For Inflation, Selected Latin American Countries (Nov:2018 Sales=100)

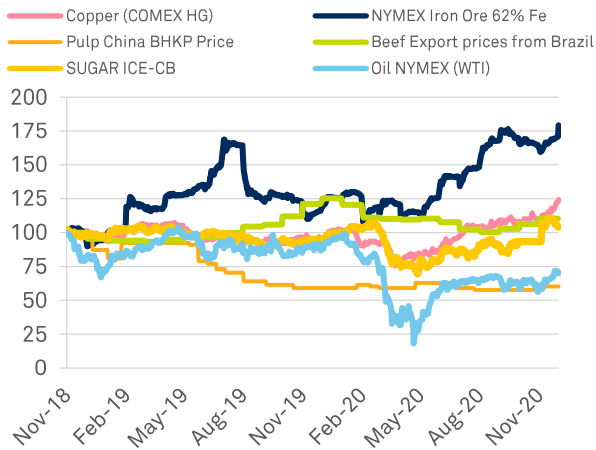


S&P Global Ratings based on public information.

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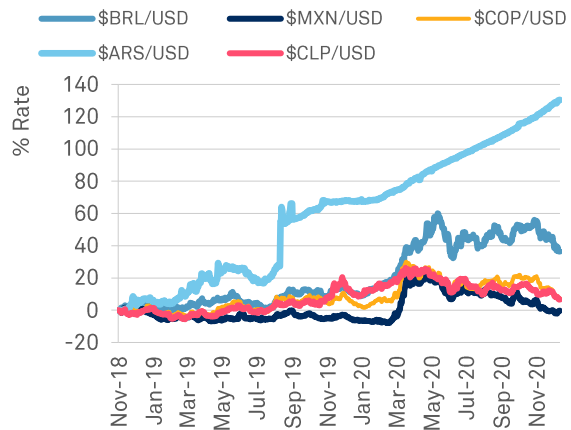
In terms of exports, the clear winners have been iron ore, copper, sugar, and animal protein (chart 11), mainly due to a strong expansion of Chinese infrastructure since August 2020 and the already favorable conditions the protein businesses were enjoying due to the slaughtering of a large part of the Chinese pork stock because of African Swine Fever. Oil prices continue to lag below pre-pandemic levels because transport of goods and people remain subdued. Pulp prices continue to suffer from oversupply and a sharp reduction in printing and writing paper demand, but we expect pulp prices to gradually recover in 2021 (which has already started in 4Q 2020), resulting from some capacity shutdowns and improving demand. Positive news for exporters is that currencies in Latin America have lost ground over the U.S. dollar, and given that exporters operations are largely domiciled in Latin America, that slightly improved margins (chart 12). However, this trend has started to revert since the U.S. election as new stimulus packages are expected that would weaken the dollar.

Chart 11 – Prices Of Main Latin American Exports (Nov-2018 Prices=100)



S&P Global Ratings based on CapIQ and RISI.

Chart 12 – Change In Currencies Relative To The U.S. Dollar, Selected Latin American Countries

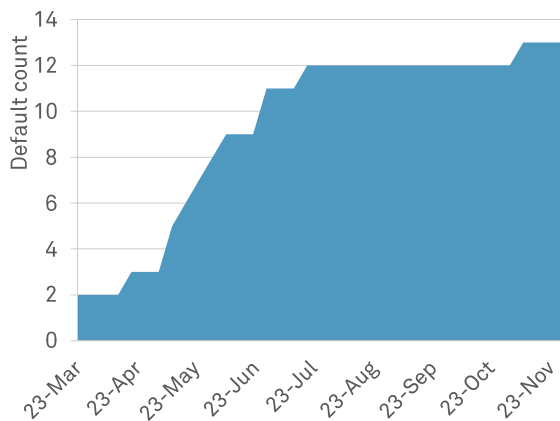


S&P Global Market Intelligence, S&P Global Ratings calculations.

• **Default Rate Has Stayed Markedly Low, But Risks Persist**

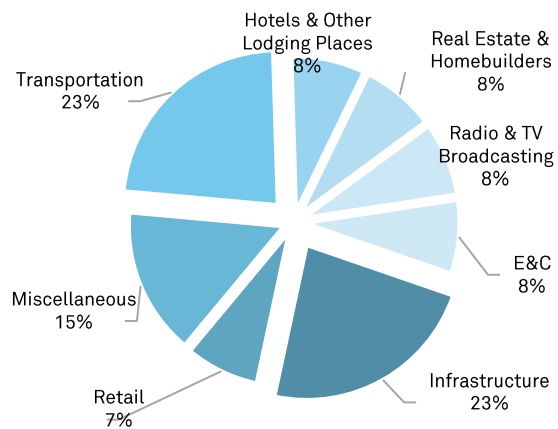
The default count has risen to 13 cases in 2020 (chart 13). Defaults had plateaued since late June after a quick rise in May and June. Corporates that defaulted were from sectors we had already singled out as at the core of the pandemic’s most affected (chart 14). Some of them were plain defaults and still remain non-complaint due to the serious blow to their businesses, while others were cases of debt exchanges that we deemed tantamount of default because in our view, the offer implied a loss of value to the lender.

Chart 13 – Corporate Defaults In Latin America As Of Nov. 30, 2020



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Chart 14 – Corporate Defaults In Latin America By Sector



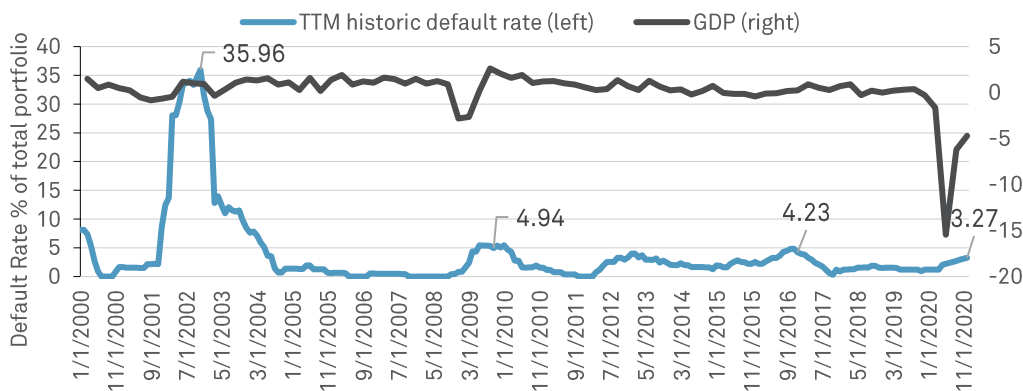
S&P Global Ratings.

One big surprise was the markedly low default rate observed for corporates in Latin America this year, which rose to 3.27%—far below the rate during previous crises that weren't nearly as severe as the current one, judging by the region’s GDP contraction (chart 15). A key driver in keeping that default rate low this year was the abundant refinancing banks offered. For example, the Brazilian National Development Bank massively refinanced its lines, easing the situation for more than 50 rated companies. Brazilian bank Caixa Economica Federal also offered automatic renewals, and the same happened in other countries in the region.

In addition, several entities completed exchange offers which helped contain defaults. According to our calculations, 12 Latin American corporations rated 'B-' or lower took debt moratoriums or

completed debt exchanges that we considered not equivalent to default. Had that option not been available, the corporate default rate would have risen to 6.3%—in an article we published on June 23, 2020, we estimated that the rate could grow up to 10%, but in light of how the rate has evolved, it would be hard to see it reaching 5%. Clearly, Latin American issuers and financial institutions have learned important lessons from past crises.

Chart 15 – Historical Corporate Default Rate In LatAm Versus GDP



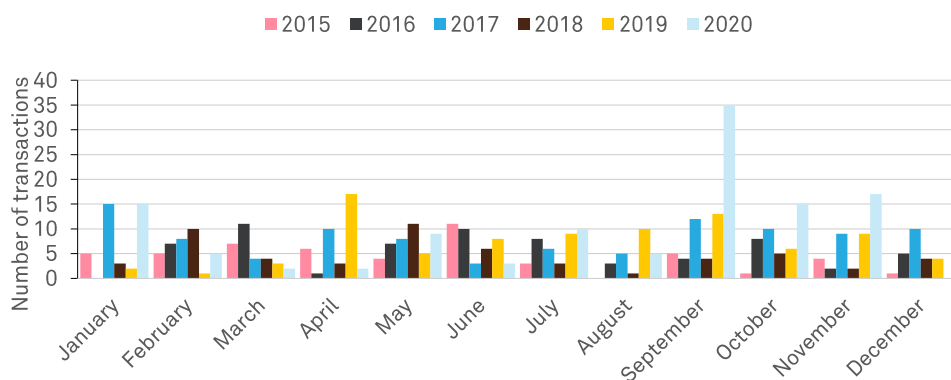
S&P Global Market Intelligence, S&P Global Ratings calculations.

• **Refinancing Risks Are Manageable**

Following a six-week shutdown of debt issuances in Latin America and credit spreads peaking in late March to the highest levels seen in a decade due to the COVID-19 pandemic, financing conditions have gradually improved and credit spreads have largely returned to pre-COVID-19 levels. A cautiously optimistic economic scenario for 2021, accommodative monetary conditions in advanced economies, positive news on the development of a COVID-19 vaccine, and more recently the U.S. election results have restored investor sentiment towards the region and moderated refinancing risk for corporate issuers.

In our view, low interest rates in key developed markets will continue to drive financing conditions in the first half of 2021, particularly for investment-grade issuers and those with less exposure to sectors with revenues directly affected by the pandemic. While there have been some pockets of high-yield primary market activity, investor appetite will remain selective for less creditworthy borrowers.

Chart 16– Number Of International Bond Issuances Made By Issuers Domiciled In Latin America (Non-Financial Corporations)



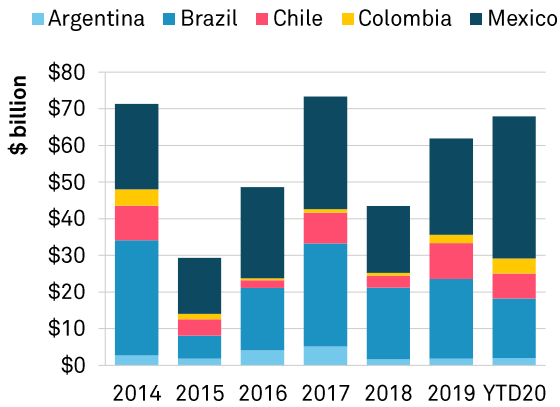
S&P Global Ratings calculations based on Thompson Reuters.

In 2020, the number of transactions will be virtually the same as in 2019. However, the value of 2020 bond issuances in dollar terms will be lower than 2019 due to domestic market activity. The depreciation

of most currencies largely explains this decline, despite nominal growth of domestic debt issuances in markets like Mexico, Argentina, and Chile. In the case of Brazil, it was not only the depreciation of the Brazilian real affecting the value of debt issuances in dollar terms, but the market also suffered from about a 50% contraction in local currency.

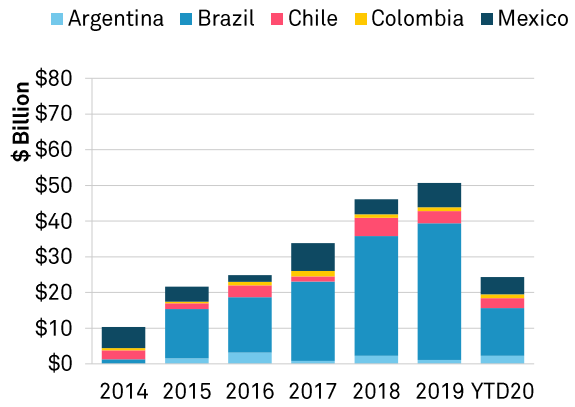
During the year, the shock to investor sentiment that generally affected market access resulted in a concentration of debt issuances in a few names, with six Mexican issuers and Petrobras accounting for about 60% of total market activity.

Chart 17 – International Corporate Bond Issuances, Selected Latin American Countries



S&P Global Ratings calculations based on Thompson Reuters.

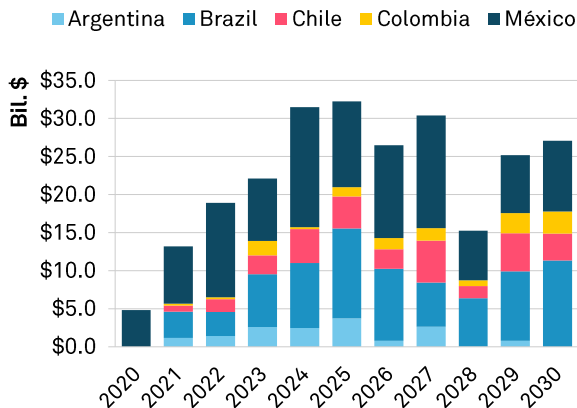
Chart 18 – Domestic Corporate Bond Issuances, Selected Latin American Countries



S&P Global Ratings calculations based on Thompson Reuters.

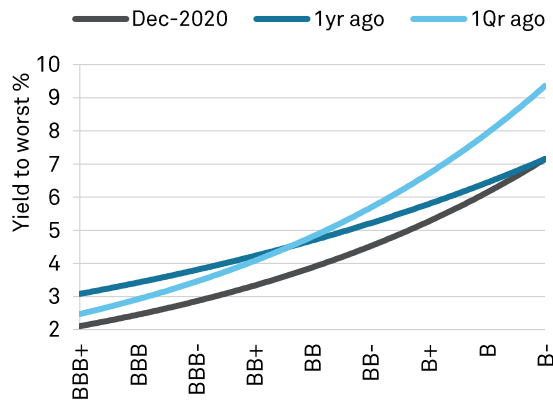
Mexican issuers face approximately \$14 billion maturing in 2021. The list of entities with significant debt maturities within the next twelve months is relatively short, with Petróleos Mexicanos (PEMEX) at the top of the list with \$5.0 billion, followed by America Movil with \$4.9 billion.

Chart 19 – International Bond Maturities Of Latin American Corporations, Selected Countries



S&P Global Ratings calculations based on Thompson Reuters.

Chart 20 – Evolution Of Yield Curves For Rated Latin American Corporations



S&P Global Ratings calculations based on CapIQ.

In Chile, Corporación Nacional del Cobre de Chile faces about \$230 million in international bonds' maturities in 2021, followed by Empresa Nacional del Petróleo (\$410 million) and Telefonica Moviles Chile (\$122 million), while in Argentina, YPF needs to pay off \$685 million and Telecom Argentina \$158 million.

In Brazil, debt maturities in 2021 will be \$13 billion, including Petrobras (\$1.6 billion), Natura Cosméticos S.A. (\$393 million), Votorantim S.A. (\$240 million), and Ambev S.A. (\$195 million).

Generally, 2021 debt maturities shouldn't pressure the liquidity of corporate issuers in the region. Less than 5% of total debt outstanding will come due next year, which in our view contains refinancing risk. There will be some cases where limited access to markets could elevate liquidity risks, particularly for entities at the lower end of the rating spectrum. We also expect some opportunistic debt issuances in the next 12 months, if market conditions allow, both domestically and abroad. Such debt financing would be aimed at addressing the 2021 debt maturities.

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