S&P Global
Ratings

Latin American Corporate And Infrastructure Credit Outlook 2024

A Case For Renewed Optimism

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This report does not constitute a rating action

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Key Takeaways

- After corporate defaults peaked at 1.6% in 2023, Latin America (LatAm) heads to a more stable 2024. Most of the region's main economies are set to grow modestly in 2024, and elections will probably introduce some volatility, but we don't anticipate a major shift in current trends.
- The year started strong in bond issuances and we believe market access in 2024 will widen thanks to lower rates and healthy fundamentals. Investment-grade companies and speculative-grade ones with stronger profiles are likely to benefit the most. Debt maturity volumes in 2024 are low, so companies would use the proceeds to finance growth and refinance medium-term liabilities. Domestic markets' strength remains an important credit factor in Brazil, Mexico, Chile, and lately, Argentina.
- Capital allocation has been conservative in 2023, and we expect companies to invest more decisively in 2024, as interest expenses decline and free cash flow improves. Asset returns look healthy compared with historic levels and should support our expectation of an investment resumption.
- There are risks to monitor in sectors such as retail, telecom and cable, metals, protein, and airlines (transportation), but overall conditions remain largely stable.

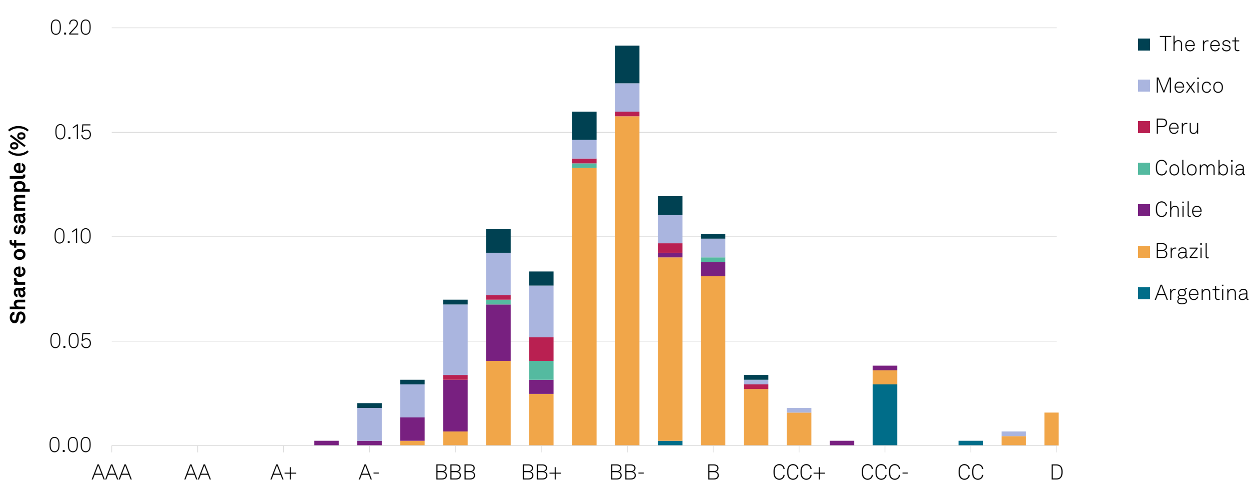
Credit trends are relatively stable for LatAm corporate and infrastructure entities. Reasonable leverage, adequate asset returns, low debt maturities, and growing domestic markets will help the companies to face challenges. Among the main risks we identify in 2024 are still high interest rates, subdued consumer spending, above-average inflation--though declining in most countries--modest growth trends, increasing competition from imports, and policy unpredictability.

The regional ratings distribution moved to the left after we upgraded Brazil to 'BB' from 'BB-' in December 2023, which triggered a bunch of corporate upgrades. The LatAm corporate and infrastructure ratings distribution is centered at the 'BB' category with about 43% of the ratings in that category, while roughly 23% are investment grade ('BBB-' or above) and the remaining 34% are speculative grade.

Chart 1

Ratings distribution

LatAm corporate ratings centered at 'BB'



Source: S&P Global Ratings.

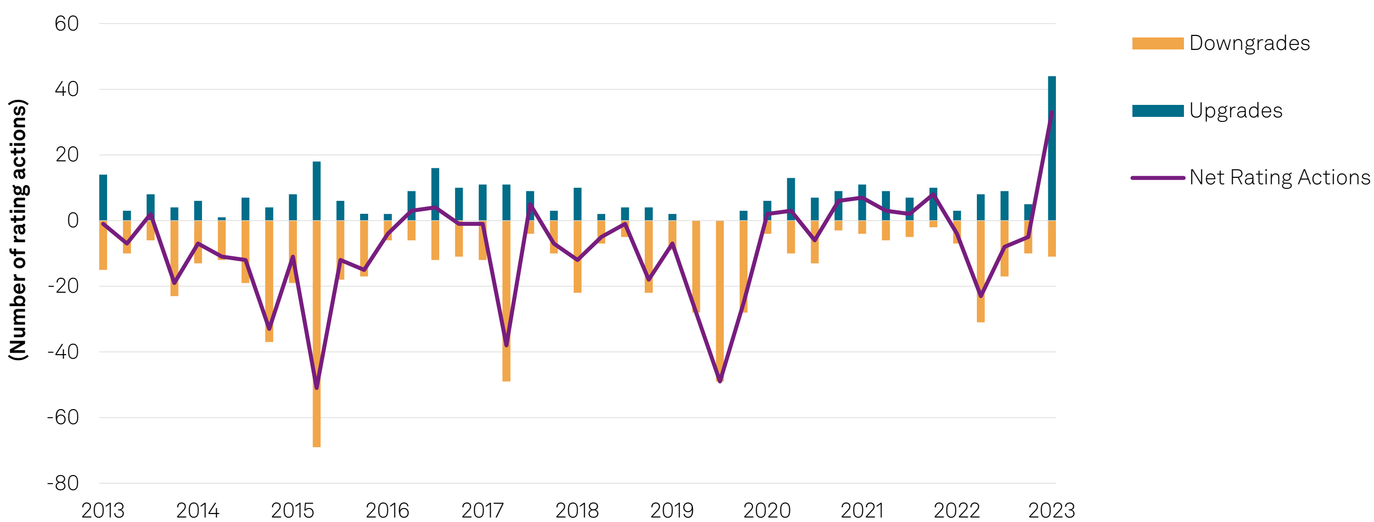
Downgrades dominated the first part of 2023, while the second half was decisively more positive. Credit conditions were tough in Brazil mainly, where most of the region's downgrades occurred in the first half of the year. A combination of high interest rates, weak consumption, and credit market restrictions after the unexpected defaults (such as Americanas S.A. and Light S.A.) hit hard sectors like retail, homebuilders, consumers, telecoms, and airlines in Brazil.

Brazil and Argentina accounted for 73% of total downgrades and 74% of upgrades--the latter owed only to Brazilian entities. In December 2023, we upgraded Brazil to 'BB' from 'BB-' after Congress approved finally the fiscal reform. The sovereign rating action triggered several upgrades of companies that were--and mostly still are--capped at the sovereign rating level. The other big cause of downgrades in the region was Argentina's downgrade to 'CCC-' in March 2023.

In Mexico, upgrades and downgrades were evenly distributed, driven mostly by weak conditions in the chemicals industry and the resurgence of companies from defaults. Meanwhile, downgrades in Chile were almost double the upgrades, mostly in telecoms, retail, and mining.

Chart 2

Corporate rating actions across selected LatAm countries



Downgrades include defaults. Data as of Dec. 31, 2023. Source: S&P Global Ratings Credit Research & Insights.

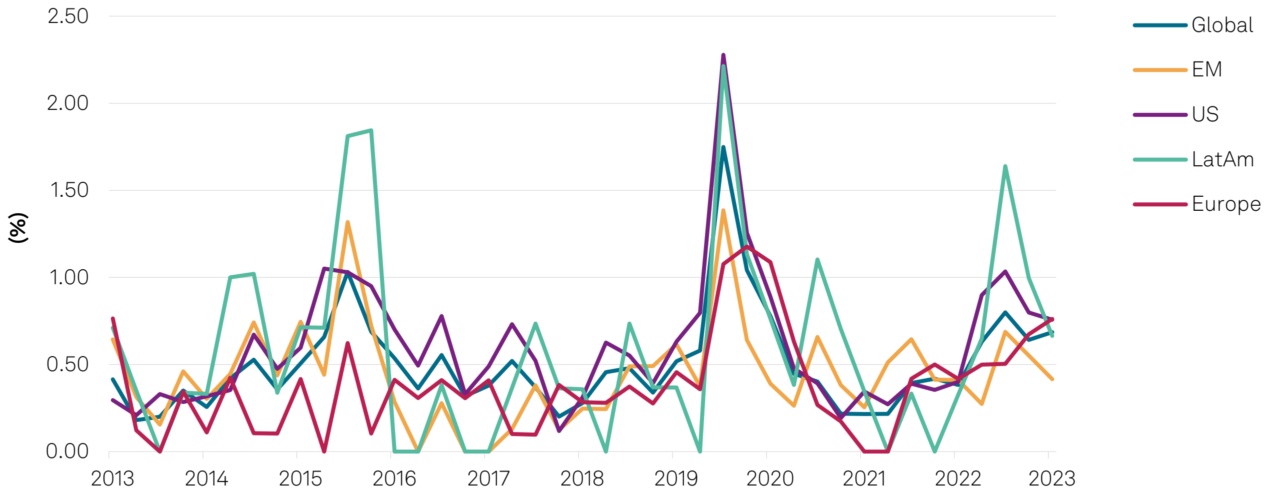
The corporate default rate peaked at 1.6% in LatAm in June 2023. The main driver was a whopping 13.75% policy rate in Brazil (SELIC) until July 2023 when the central bank started the easing phase to the 11.25% level currently. The rate for the first half of the year proved too high for domestic corporations, exposing them to the interest-rate risk and prompting several entities to restructure their debts.

The good news is that nominal recovery rates of senior unsecured debts were close to 100%, given the predominance of distressed exchanges among the rated entities. In all those cases, companies emerged fairly rapidly by exchanging their unsecured notes for new bonds with longer maturities--and for the most part similar coupons.

Chart 3

Corporate default rates for the past decade by global regions

Corporate default rate peaked at 1.6% in June 2023 in LatAm



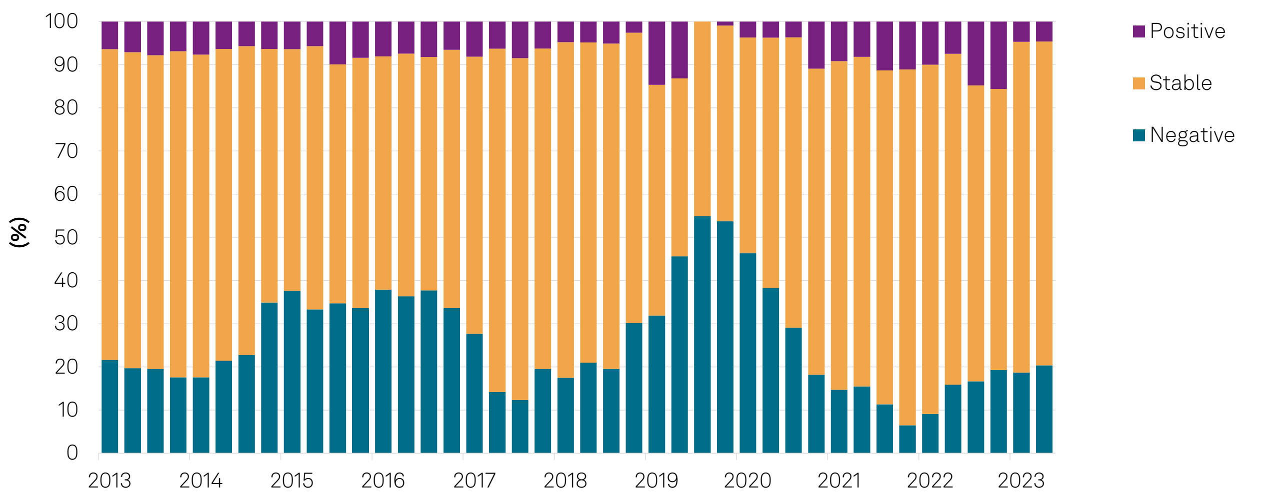
One quarter trailing default rate by region. LatAm 6 includes Argentina, Brazil, Chile, Colombia, Mexico, and Peru. Source: S&P Global Ratings Credit Research & Insights.

The net outlook bias reached negative 15% as of late January 2024, given mostly the negative outlook revisions on Argentina, Colombia, and Chile. Current downside risks are on par with those seen in periods of relative stability. We think that's the case for the region as the more severe risks such as high interest rates and/or low commodity prices are fairly contained. Still, there are a few sectors with greater chances for upgrades and downgrades, as we comment below.

Chart 4

Outlook bias of LatAm corporate sector

Outlook distribution is slightly skewed to the negative



Source: S&P Global Ratings Credit Research & Insights.

There is downside risk concentration across the retail, telecom and cable, chemicals, power generation, and protein sectors. Forty percent of the region's downgrades occurred in these sectors during 2023, so a big portion of the ratings adjustment has already taken place.

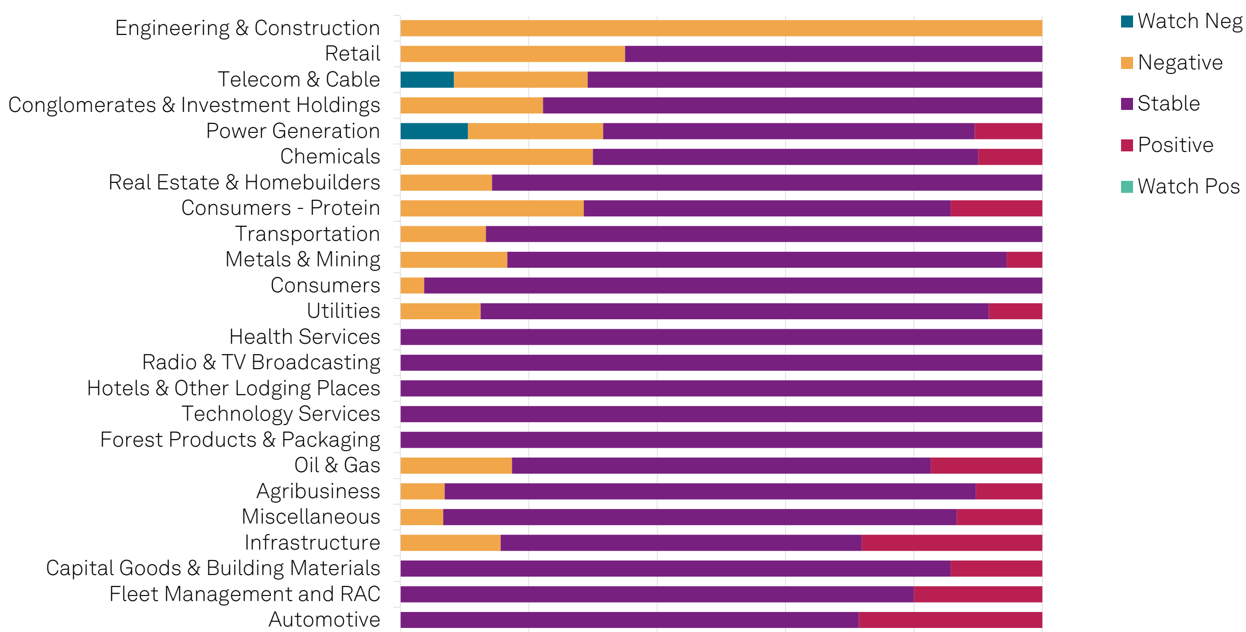
The reasons for the credit weaknesses are varied (i.e. high input costs for protein; stiff competition for retailers especially in online marketplace and sluggish consumption; price compression owed to fierce competition in telecom and cable coupled with aggressiveness in debt usage and high capex; margin compression for chemical companies due to continued low prices resulting from increasing global capacity combined with sluggish global demand growth; etc. See detailed comments on each sector in the last section.

On the positive side, infrastructure, building materials, fleet management, and automotive credits stand out. Several issuers in the infrastructure were upgraded in 2023 following the upgrade of Brazil. Still, there's a potential for further upgrades as interest rates decline and companies improve their cash flow and leverage profiles.

Chart 5

Outlook distribution by sector

LatAm corporate outlooks are predominantly stable



Source: S&P Global Ratings.

Argentina's Risk Premia, Brazil, Chile, And Colombia's Fiscal Paths, And Mexican Elections

With the exception of Argentina, we expect the region to grow modestly in 2024, while central banks to continue easing monetary policies. The latter is based on our expectations the Federal Reserve to start lowering rates by mid-year. The speed of both factors could attract higher-than-expected capital flows to the region.

In general, we forecast LatAm to be favored by capital flows in 2024, which should help widen access to international markets for regional corporations. We expect issuers with the strongest credit profiles in the speculative-grade space to benefit the most as they were largely unattended in 2023 and 2022. The trend was evident in January during which issuances from LatAm corporations topped at $7.6 billion, the third strongest January level in the past 10 years.

Table 1

Main economic assumptions for main LatAm economies

Low growth, and still high inflation and policy rates are our main economic assumptions for 2024

	GDP growth % 2024	Policy rates % (year-end)	Average inflation % (year average)
Argentina	-1.5	100.0	190
Brazil	1.5	9.0	3.6
Chile	1.9	5.5	3.5
Colombia	1.3	10.0	5.5
Mexico	1.8	9.5	4.1
Peru	2.2	4.5	3.2

2024 GDP growth assumptions are in real terms. Policy rates are on a year-end basis while inflation rates are averages. All of them were published on Nov. 27, 2023. Source: S&P Global Ratings.

Clearly Argentina continues to present the biggest challenge for investors and corporations. The country risk premia remains dramatically high with sovereign bond spreads over the U.S. Treasuries at nearly 2,000 basis points (bps). Due to Argentina's macroeconomic fragility, companies will struggle to remain profitable, but access to capital may be improving as seen in the recent bond issuance by YPF S.A. (CCC-/Negative/--) at yields slightly below 10%.

Garnering political support will be crucial for Milei's administration to pass a myriad of reforms that aim at deregulating the economy and reducing fiscal spending. Frictions are on the rise and social support could wane, while monthly inflation remains in double digits. Meanwhile, the country's external front has strengthened a bit after the peso's devaluation in December 2023, the government's measures to contain monetary base expansion, and the resumption of the IMF lending program.

In general, all sectors should benefit from a reduction in Argentina's risk premia but we believe oil and gas, power generation, telecom and cable, and agribusiness companies should benefit the most from growing exports, better domestic prices, and fewer regulations.

We upgraded Brazil to 'BB' from 'BB-' on Dec. 19, 2023, after the approval of the tax reform. Although the implementation of the reform will be gradual (becoming fully effective in 2027), it is a significant overhaul of the tax system and will likely translate into productivity gains over the long term. Also, the reform extends the track record of structural and microeconomic reforms since 2016, which in our opinion, reflect an increasingly pragmatic institutional framework that helps to anchor macroeconomic stability.

In general, we expect a more benign environment for Brazilian corporations. This will be due to the decline of domestic rate to about 9% by year-end from 11.25% currently and inflation below 4%. Still, economic growth will remain modest at 1.5% due mainly to high fiscal deficit and debt burden, among other factors.

Brazilian corporations suffered the most from high interest rates in 2023 as 70% of sectors showed higher cost of debt than their return on capital. And 35% of sectors had median EBITDA interest coverage ratios below 2x. The decline in domestic rates should benefit sectors with weaker leverage metrics, such as homebuilders, retailers, transportation, consumers and power generation companies.

We also expect entities with the strongest credit profiles (rated 'BB' or higher) to speed up their growth plans. The would do so by tapping international and domestic debt markets to invest more aggressively or to preserve cash. Companies at such a rating category are diverse such as export-oriented businesses like mining and agribusiness and domestic sectors with large capital base such as infrastructure, utilities, and railroads.

On Oct. 19, 2023, we assigned a negative outlook on our sovereign ratings on Chile (A/Negative/A-1), based on political wrangling that has slowed the approval of meaningful policies to boost the country's economic growth and rebuild fiscal resilience. With a packed electoral calendar that includes regional elections in 2024 and national election in 2025, the political environment will be challenging.

After the second rejection of a constitutional change on Dec. 17, 2023, the government would have to find consensus to approve and implement reforms to rebuild Chile's fiscal and external buffers, which deteriorated during the recent economic crisis, as well as to bolster economic growth and improve social standards. These include pension and income tax reforms and a regulatory overhaul, among others.

Chilean corporations would also experience a relief from a drop in interest rates and inflation. We believe sectors like telecom and cable, retail, and transportation are going to benefit the most, given their heavier balance sheets and in the case of the first two, the high sensitivity of their products and services' demand to interest rates and inflation.

Similarly, we revised our 'BB+' rating outlook on Colombia to negative on Jan. 18, 2024. This was mainly driven by the risk of persistently weak private-sector confidence, resulting in low levels of investment and economic growth, contributing to fiscal slippage and/or higher external vulnerabilities.

Most of our ratings on Colombian corporations have negative outlooks as they are capped at the sovereign rating level. The nature of their businesses is essentially domestic (utilities, power generators, conglomerates, and state-owned oil and gas entities) and despite their healthy performances, they are vulnerable to a scenario of weakening domestic conditions.

Mexico's presidential elections will take place on June 2, 2024. We don't expect meaningful changes to current political and economic trends after the election. Our growth estimates for the year are driven by strong consumption (helped by robust remittances), resilient manufacturing output, and a sharp uptick in public nonresidential investment.

Consequently, we expect credit trends for Mexican corporations to remain stable and healthy. Still, we identify some small telecom operators and telecom infrastructure companies, bearing riskier profiles as leverage among them is high and margins and cost of capital aren't improving.

Peru has been in a recession for several quarters in 2023 amid social unrest and weather disruptions to economic activity, while the risks to our projections of just above 2% growth in 2024 are mostly to the downside. The country's relatively favorable external and fiscal profiles remain vulnerable to adverse political developments that could further erode investment or worsen economic policies under a more extreme scenario.

January 2024: The Third Strongest Bond Issuance In The Past Eight Years

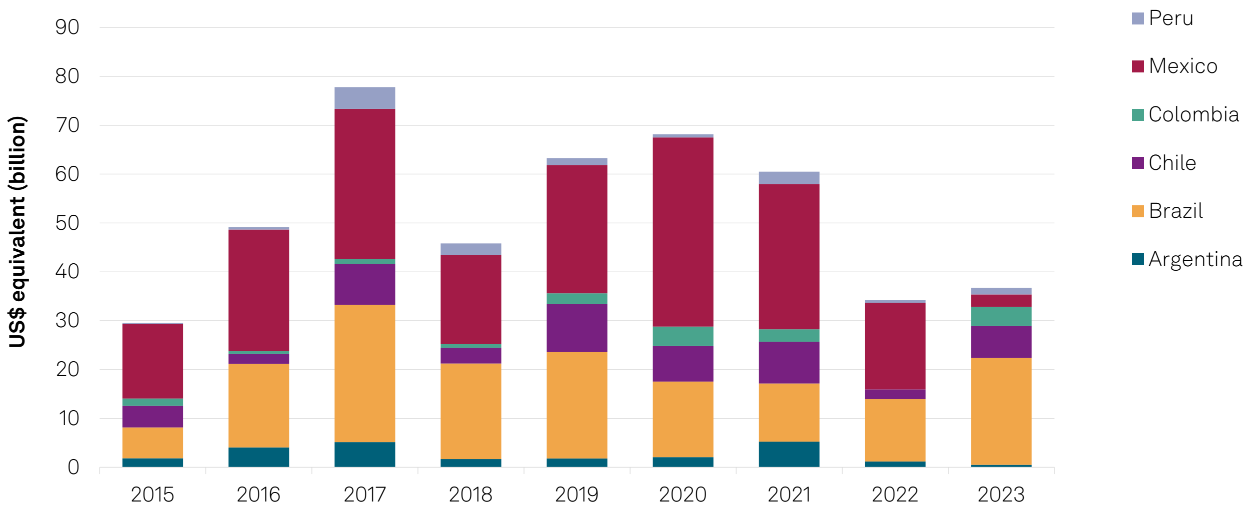
International bond issuance among LatAm corporations in 2023 remained subdued, totaling only $36.7 billion (see chart 6). This level was similar to the one in 2022 and well below the 2016-2021 average. High interest rates were undoubtedly the main reason.

2024 started vigorously, with nearly $7.6 billion in new issuances. The number of bond deals in the first month of the year was the third highest in the same month during 2015-2023. The companies that issued were benchmark credits in some of the region's main countries, such as Corporacion Nacional del Cobre de Chile (Codelco; BBB+/Stable/--) in Chile, Ecopetrol S.A. (BB+/Negative/--) in Colombia, America Movil S.A.B. de C.V. (AMX; A-/Stable/--) in Mexico, and YPF in Argentina.

Chart 6

International bond issuances

Issuances in 2023 remained low for rated and unrated LatAm corporations

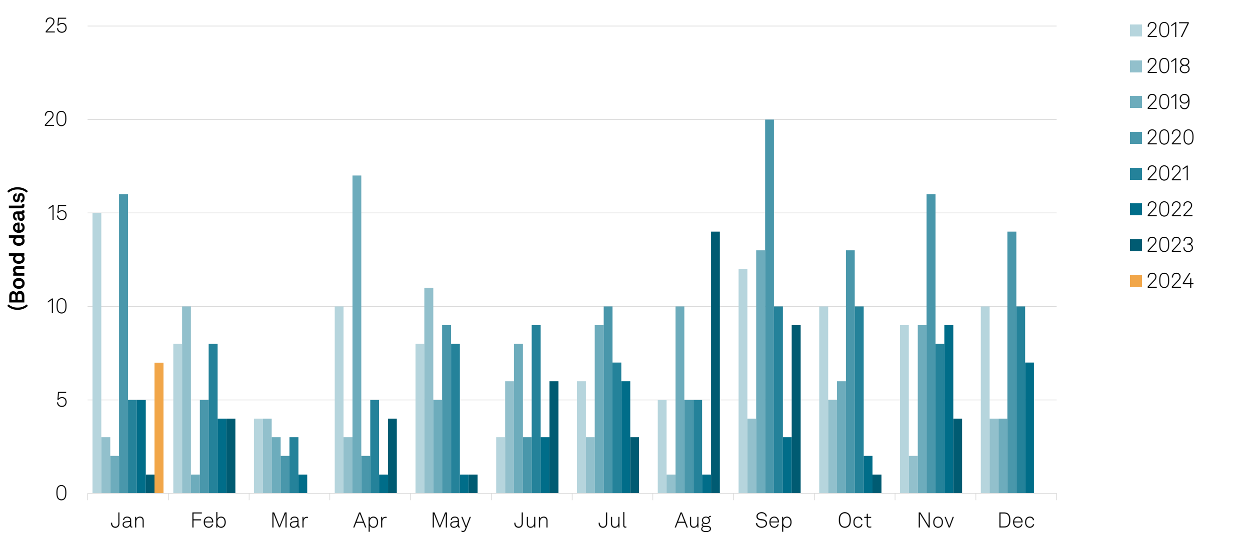


Source: S&P Global Ratings based on Thompson Reuters.

Chart 7

International debt markets' windows

Amount of bond deals by the rated and unrated LatAm corporations



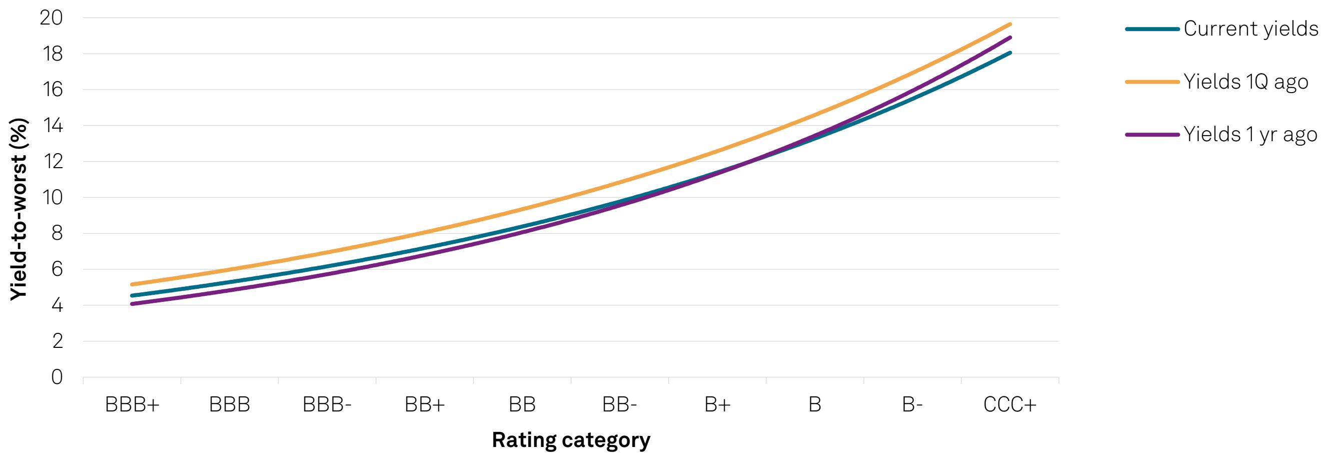
Source: S&P Global Ratings based on Thompson Reuters.

Borrowing costs have improved slightly in January 2024, especially for the issuers in the 'BB' and 'B' rating categories as the rates have gone down by as much as 100 bps. Those rate levels (between 8% to 10%) are of course higher than the historic ones, but way more reasonable for the stronger credit profiles. And although refinancing needs are low in 2024, we believe these companies would tend to be more active in debt markets during the year. Also, if the benchmark rates go down more substantially in the second half of 2024, the market activity will speed up more decisively.

Chart 8

Median yields of international bonds by rating category

Borrowing costs are improving



Source: S&P Global Ratings based on Thompson Reuters.

Regional debt markets continued to gain steam in 2023, as cross-border market activity remained subdued. Larger and deeper domestic capital markets such as those in Brazil, Chile, and Mexico have served well domestic funding needs and they keep growing in size, which is always an important factor for sustained credit health.

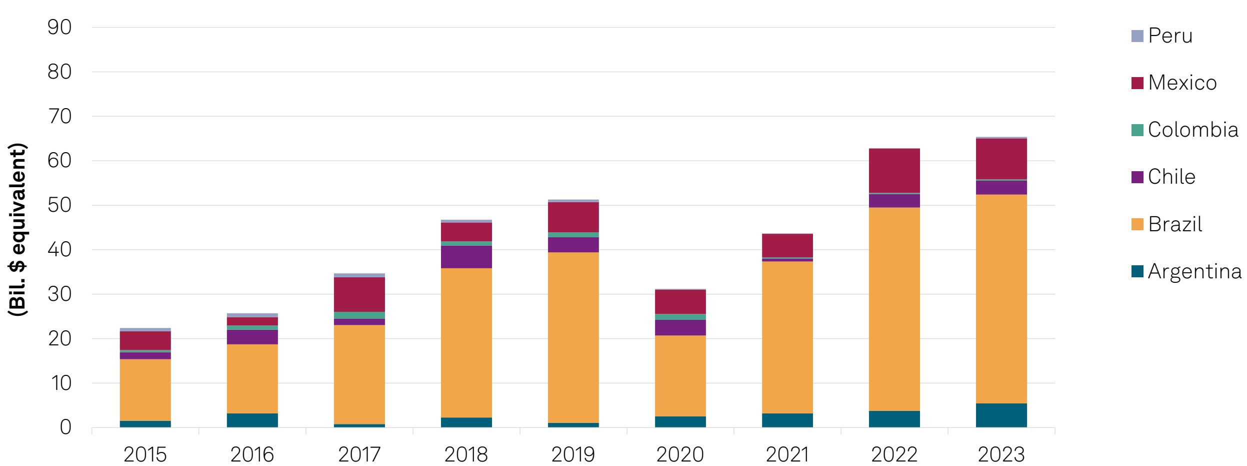
The growth of the Argentine domestic debt market in 2023 is also a relevant factor that we expect to continue. It has been critical in providing funding to domestic large and mid-size entities while credit from international markets and banks remained muted. But currency risks may increase as domestic issues are dollar-linked notes primarily--as investors favor those securities over those bearing peso coupons.

Colombia's macroeconomic conditions and high interest rates kept issuance levels low in 2023 with only $250 million equivalent issued domestically in 2023. We expect conditions to mildly improve in 2024 as interest rates drop, but governments reforms will play a role too.

Chart 9

Domestic bond issuances

Domestic markets are becoming a reliable source of funding for LatAm corporations



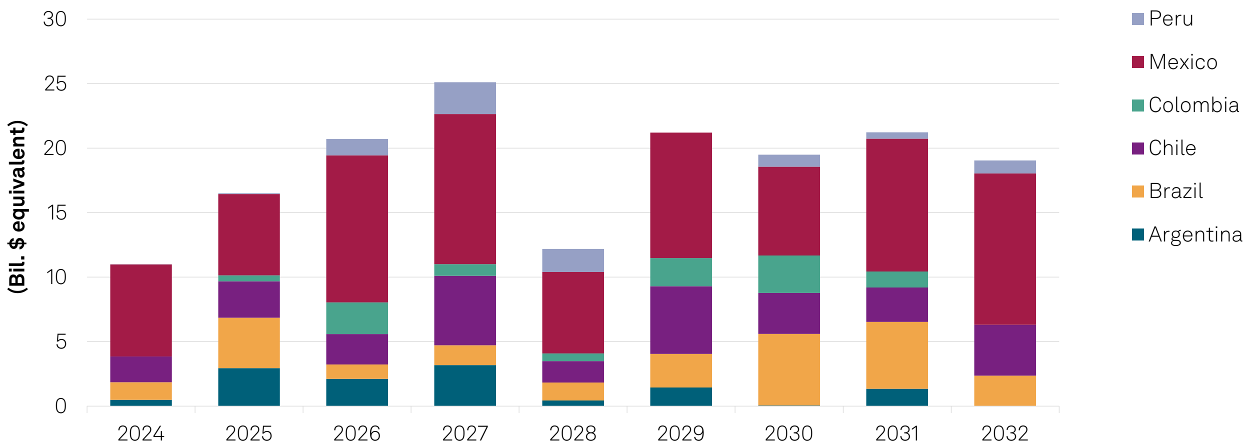
Source: S&P Global Ratings based on Thompson Reuters.

Maturities in 2024 are low with a total of $11 billion coming due. Out of which $7 billion are among the Mexican entities, followed by slightly less than $2 billion among Chilean and Brazilian entities, and the rest are across mostly Argentine corporations. Main Mexican issuers with maturities in 2024 are Petroleos Mexicanos (Pemex), AMX, Sigma Alimentos S.A. de C.V., Kimberly-Clark Mexico S.A.B. de C.V., Grupo Bimbo S.A.B. de C.V., el Puerto de Liverpool S.A.B. de C.V., and Gruma S.A.B. de C.V. Meanwhile main Chilean corporate bonds maturing in 2024 were issued by AES Andes S.A., Codelco, Celulosa Arauco y Constitucion S.A. (Arauco), Empresa Nacional de Telecomunicaciones S.A., and Enel Generacion Chile S.A.

Chart 10

International bond maturities of LatAm corporations

Refinancing needs look manageable in 2024 and 2025



Source: S&P Global Ratings based on Thompson Reuters.

The Capital Allocation Puzzle

In 2023, LatAm companies remained very conservative in order to get through harsh times. Chart 11 shows the deterioration in coverage metrics across sectors that took place in 2023 as borrowing costs increased. The response was the reduction in investments to protect cash flow and balance sheets, and because projects' attractiveness fade as their internal rate of returns wane amid rising funding costs.

Half of corporate sectors in LatAm invested below historic levels, while some couldn't fund capex and interests internally. Chart 12 shows underinvestment in sectors such as real estate and homebuilders, fleet management, telecom and cable, agribusiness, hotels and retail. The last two though were posting strong operating cash flow in the last 12 months ended in September 23, so we expect them to improve their leverage profiles in 2024.

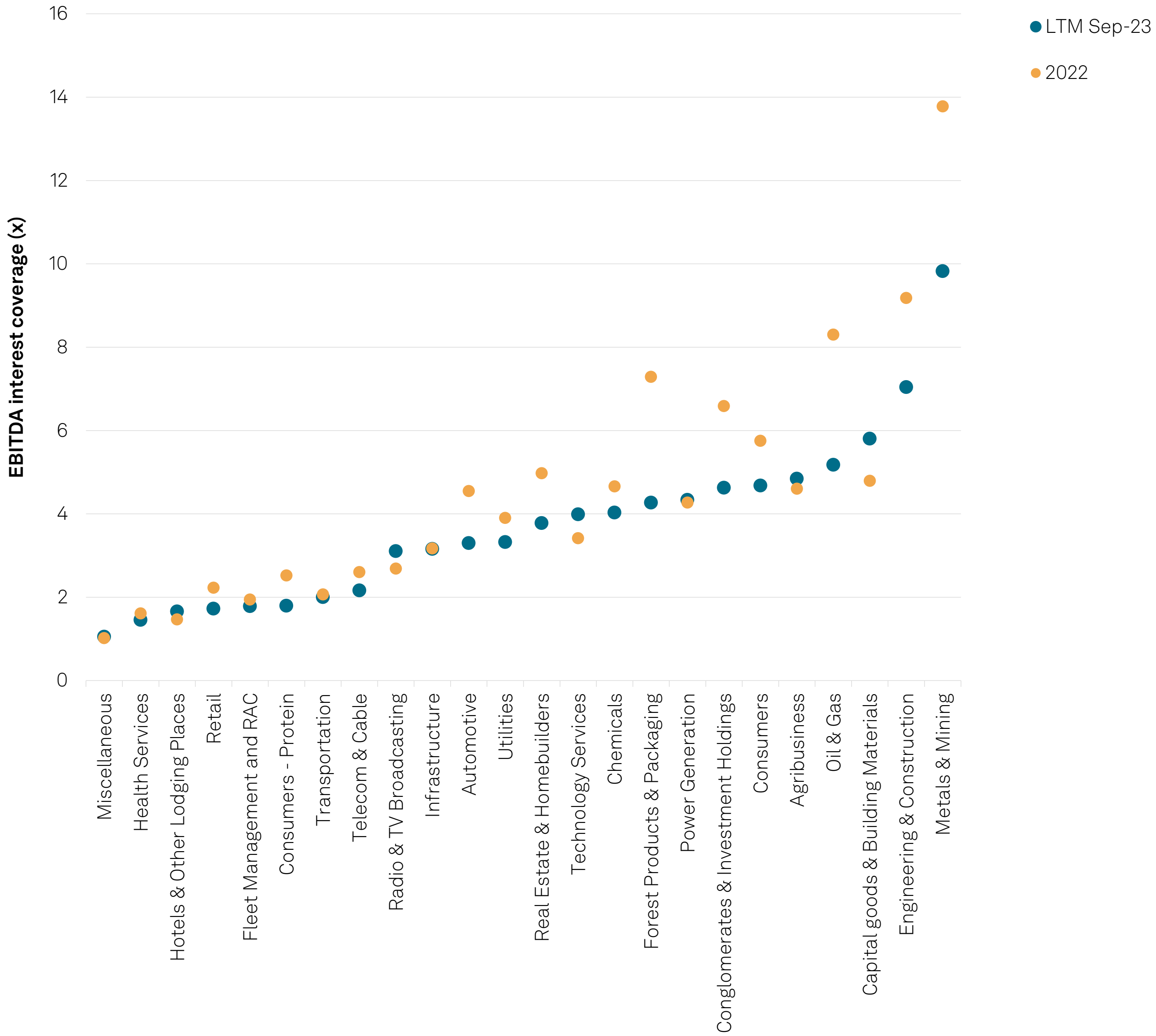
A few sectors continued investing heavily in 2023 while generating enough operating cash to cover capex and debt interest. The main ones were mining, building materials (mostly in Mexico), consumer products, and power generators. These sectors are enjoying healthy fundamentals on average for the region and we expect them to grow solidly in 2024 with generally solid credit profiles. Their median coverage ratios are among the strongest too. Lastly, forest products, and oil and gas companies have shown stronger investment patterns than in the past.

We believe companies in 2024 will speed up investments as interest rates go down. We expect to see a gradual increase in investments towards the second half of the year. As chart 13 indicates, most of corporate sectors in LatAm are generating returns at or above historic patterns, so the incentive to keep growing is high.

Chart 11

Coverage ratios weakened in 2023 as rates went up

There was a clear deterioration in EBITDA interest coverage ratios in 2023

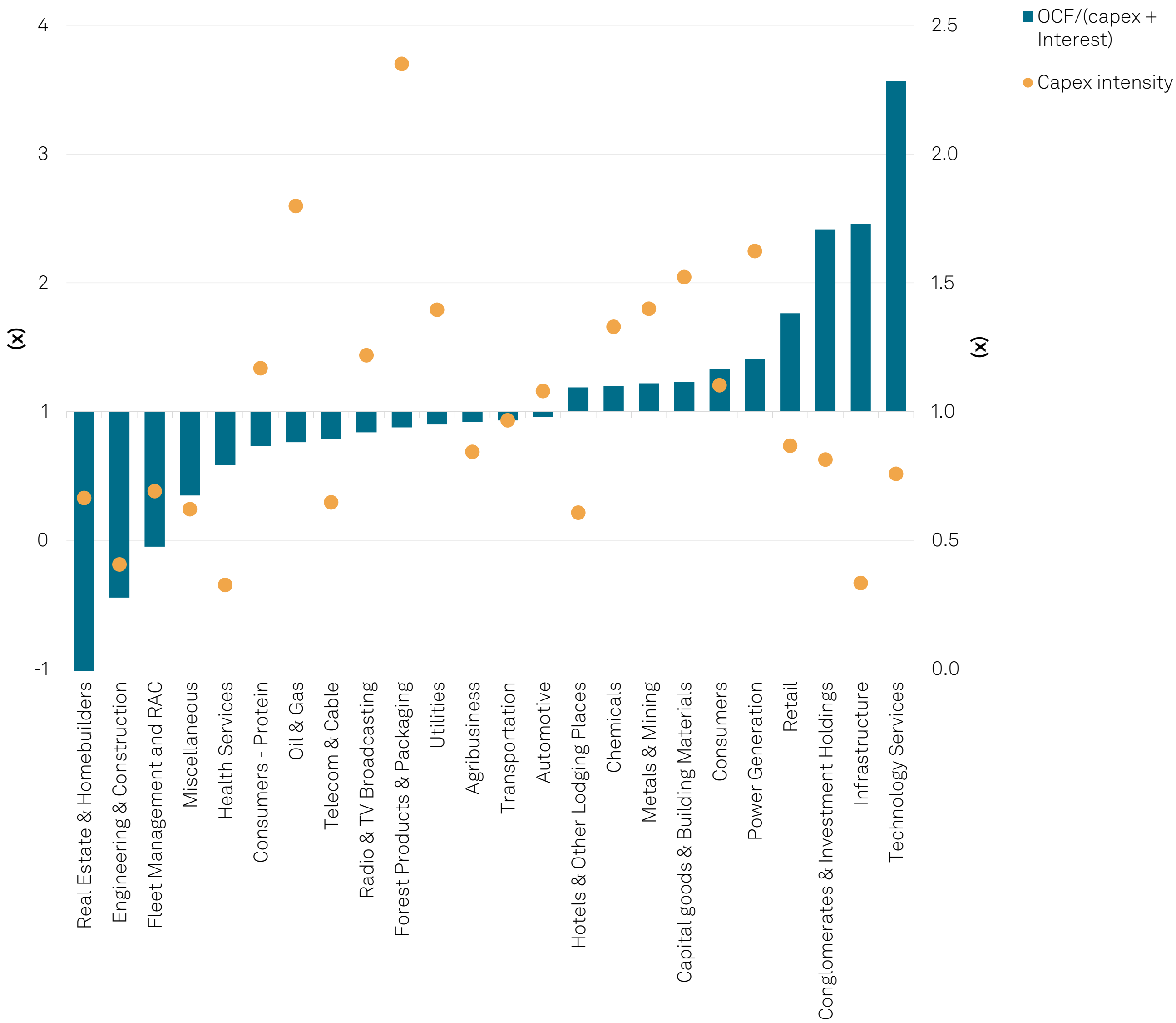


Median coverages were calculated using unadjusted data from Market Intelligence. Source: S&P Global Ratings.

Chart 12

Many sectors reduced capex intensity, defensively

Many sectors are investing below historic medians due to poor cash flow

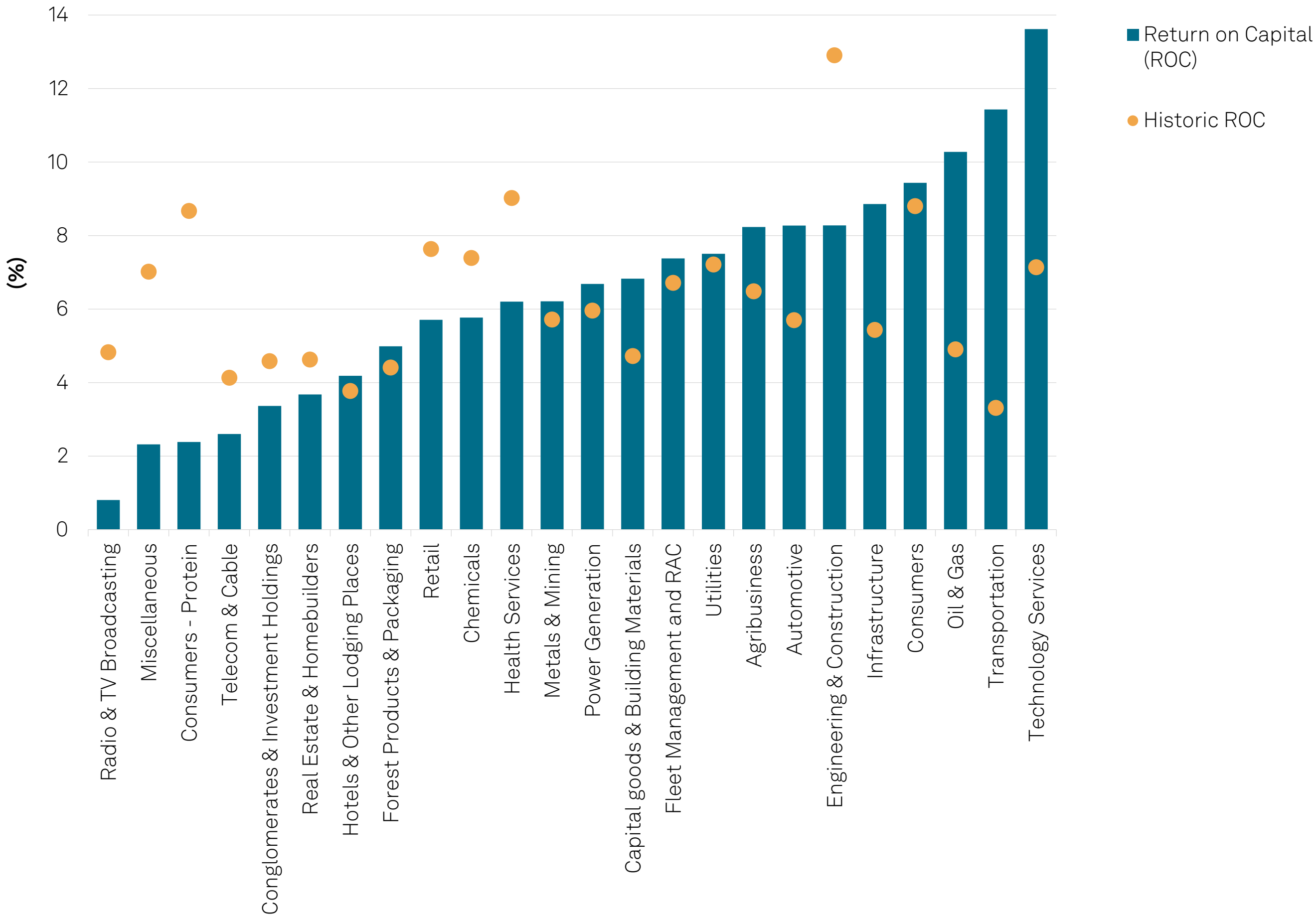


Capex intensity is calculated by dividing last-twelve months capex-to-assets / historic capex-to-assets. OCF: Operating cash flow=net income + D&A + other non-cash items + change in working capital. Source: S&P Global Ratings.

Chart 13

Most sectors with healthy returns

Several sectors are producing returns at or above historic medians



ROC= EBIT*(1-Tax Rate)/Capital. Source: S&P Global Ratings.

Sectoral Trends

Agribusiness

Ethanol producers started the year with a bunch of negative rating actions. The record volumes of sugarcane crushed last year in Brazil bolstered ethanol production, but weak demand lowered the price parity with gasoline, shrinking ethanol's profitability. As a result, many players hold inventories to sell during the inter-harvest period, but sizable inventories and still stronger preference for the gasoline could continue pressuring profits in the next few months.

The companies with less flexibility to switch to sugar from ethanol will suffer the most, while the mills that can produce more sugar are optimizing the mix to benefit from record-high prices of the sweetener and offsetting the biofuel's weak margin.

Mexican sugar producers continued to benefit from soaring prices in 2023, which has helped them to maintain a solid financial position. We expect this favorable pricing trend to continue in 2024 considering a relative sugar scarcity in the combined Mexico-U.S. market as a result of several droughts in the country that resulted in poor harvest yields.

Mexico's sugar production will reach about 5.0 million tons for the 2023-2024 harvest, according to the Mexican National Committee for the Sustainable Development of Sugarcane. From the demand side, we expect volumes to remain broadly stable and insulated from the country's expected economic slowdown, since most of volumes are for direct consumption--food and beverages--which have high inelasticity. We expect sugar producers to allocate more than 90% of their output to the combined Mexico-U.S. market, which has some of the highest prices in the world, with a little need to export to the international market that offers lower prices and leads to lower profitability.

Outlook Bias	+3.4
% Downgrades in 2023	2.9
% Upgrades in 2023	0.0
Gross Margin change %*	+3.9
Net debt to EBITDA §	2.6x
EBITDA Ints Coverage §	4.8x

*medians, last twelve month as of Sep 2023 vs. 2022
§ medians, last twelve months as of Sep 2023
% of downgrades and upgrades are relative to total count

Forest Products And Packaging

We expect pulp prices to remain flat or to drop by as much as 5% in 2024 from 2023 levels. Suzano S.A.'s Cerrado project should start up in Q2 2024 and is expected to continue holding prices back. This project will close a global pulp expansion phase (including Arauco's MAPA project and UPM-Kymmene Oyj's Paso de Los Toros among others) that will add more than 7.5 million tons of gross pulp production capacity between 2023 and 2025, the bulk of which is competitive South American hardwood.

Still, we expect average prices in 2024 to be significantly higher (between 20% and 40% depending on the grade) than the lows of 2020. An important factor behind higher prices in the downturn is cost inflation, which has pushed marginal cost upwards. Lower prices have dented EBITDA and cash flow during 2023, and we have seen to a larger or lesser extent increase in leverage as well. In 2024, amid higher pulp volumes, lower capex, and the proceeds from assets sales for Arauco, we expect improved cash flow and leverage metrics for Chilean pulp producers. For Suzano and Klabin S.A., somewhat higher volumes should be offset by sizable investments (capex and forest acquisitions), which will probably push leverage slightly up again in 2024. Nevertheless, we believe these companies will surf the market downturn without major and prolonged deviations from credit metrics for the ratings level.

Outlook Bias	+0.0
% Downgrades in 2023	1.4
% Upgrades in 2023	1.5
Gross Margin change %*	-22.2
Net debt to EBITDA §	3.8x
EBITDA Ints Coverage §	4.3x

*medians, last twelve month as of Sep 2023 vs. 2022
§ medians, last twelve months as of Sep 2023
% of downgrades and upgrades are relative to total count

Protein Producers

We expect the protein segment's overall margins to rise thanks to stable cattle costs in South America and lower costs of grains--especially corn. Pork and poultry processors should benefit the most, while margins for beef producers in Brazil should remain supportive. Companies with higher exposure to the U.S. market will continue to suffer from low cattle availability that will keep curtailing margins.

Also, we have recently revised our outlook on Frigorifico Concepcion S.A. to stable from positive, as the company announced the issuance of new $300 million secured notes to finance further growth that we believe will raise capex and working capital outflows during 2024. While the volume growth and increased geographic diversification improves our view of the company's business, we have revised our base-case forecast to reflect higher leverage through 2025.

Outlook Bias	-14.3
% Downgrades in 2023	1.4
% Upgrades in 2023	1.5
Gross Margin change %*	-3.3
Net debt to EBITDA §	6.4x
EBITDA Ints Coverage §	1.8x

*medians, last twelve month as of Sep 2023 vs. 2022
§ medians, last twelve months as of Sep 2023
% of downgrades and upgrades are relative to total count

Building Materials

We expect credit quality for LatAm building materials companies to remain broadly stable in 2024. The industry players have leverage and liquidity headroom to withstand downside risks. We anticipate revenue growth to decelerate to close to 6% in 2024, compared with an expected pace of 10% in 2023, although this will vary across countries. That's because we now expect slower price increases to ensure steady volume growth.

Our base-case scenario contemplates some recovery in residential investments and an uptick in nonresidential investments in Brazil and Mexico, the two largest economies in LatAm. In Brazil, we think business conditions for building materials will be more supportive in 2024 than in the past two years, thanks to lower interests and inflation expectations, which should bolster a recovery in residential investments, as well as public and private infrastructure investments, especially toward the second half of 2024. In Mexico, the building materials sector will continue to benefit from robust remittances that support informal housing and home improvements, and from the recent sharp uptick in public nonresidential investments.

We also expect that easing input costs will stabilize gradually operating margins, with only some room for further improvements. Following a reduction in EBITDA margins by an average of 210 bps in 2022 stemming from input cost inflation, particularly for energy, electricity, and transportation costs, we expect building materials companies will stabilize their operating margins in 2024. This follows a solid partial recovery in 2023, thanks to companies' ability to pass on price hikes and due to resilient demand.

Regarding capital allocations, we believe that the rated LatAm building materials entities will remain prudent, balanced between growth--through capex, potential tuck-in acquisitions, and debt reduction. The latter will support deleveraging, with adjusted debt to EBITDA inching toward 2x on average. Yet some rated companies with leverage leeway and solid cash reserves might increase capex and M&As, particularly in the U.S. or Brazil, to expand and diversify their operations.

Even though some entities might increase slightly or resume dividend payments over the next few years, we do not expect a significant shift in financial policies. Moreover, LatAm building materials companies' debt maturity profiles bear limited short-term refinancing risks.

Outlook Bias	+14.3
% Downgrades in 2023	5.8
% Upgrades in 2023	0.0
Gross Margin change %*	-5.7
Net debt to EBITDA §	2.4x
EBITDA Ints Coverage §	5.8x

*medians, last twelve month as of Sep 2023 vs. 2022
§ medians, last twelve months as of Sep 2023
% of downgrades and upgrades are relative to total count

Finally, we acknowledge that CO2 regulations remain limited in scope across LatAm, but decarbonization strategies could enable companies to prevent longer-term operating and financial risks. We note that many cement manufacturers in the region are reducing their CO2 emissions with manageable budgets so far. Most of the rated building materials issuers in LatAm generally maintain extended debt maturity profiles, with no refinancing risk in 2024. However, speculative-grade issuers remain more vulnerable to longer periods of high interest rates, refinancing risks, and sticky inflation.

Oil And Gas

Outlook Bias	+0.0
% Downgrades in 2023	4.3
% Upgrades in 2023	12.1
Gross Margin change %*	+5.7
Net debt to EBITDA §	2.8x
EBITDA Ints Coverage §	5.2x

*medians, last twelve month as of Sep 2023 vs. 2022
§ medians, last twelve months as of Sep 2023
% of downgrades and upgrades are relative to total count

We assume Brent averaging $85/bbl and WTI $80/bbl. Those are favorable price levels that will help companies maintain solid balance sheets and generally ample liquidity in 2024. Despite our assumption that global oil supply will probably outpace demand growth, we believe that OPEC+ will maintain production cuts to sustain oil prices at reasonable levels to balance their budgets.

In such scenarios, we expect companies to continue investing heavily to raise output and replenish reserves. Government ownership of national oil companies across the region remains a key credit factor, given the sovereigns' strong influence on ratings.

Petrobras announced at the end of 2023 its five-year strategic plan, with higher investments than in the previous plan. It incorporates a continued focus on exploration and production, but also larger investments in refining and low carbon initiatives, in line with the government speech during last year.

In Colombia, Ecopetrol is well positioned to accelerate energy transition given its already extensive pipeline projects for the next 8-10 years. In addition, the last acquisitions will contribute to its plan to transition to more sustainable power transmission, as part of its diversified portfolio, while it continues to widen its diversification of country risk.

We assume the next administration in Mexico to continue supporting Pemex.

Argentine oil and gas companies are likely to keep increasing production (and exports) at a rapid pace as the country expands midstream capacity and the government continues to incentivize the gas production growth. At the same time, the devaluation of the official exchange rate will improve crude oil realized prices and bring them closer to import parity. Argentine oil and gas company YPF is at the top of the list in investment and growth. We expect it to keep expanding its oil production, doubling it by 2026 (compared with 2022).

The rated Brazilian junior exploration and production companies enter 2024 with acquisitions from past years fully integrated. These companies acquired mature assets from Petrobras over the past few years and are now directing investments largely to the revitalization process of those assets and drilling campaigns.

We could see some market consolidation among these small players to continue increasing the scale and asset diversification, as we don't expect additional asset divestments by Petrobras.

Some of these companies have wide access to domestic and international credit markets. For instance, 3R debuted on the U.S. bond market in January this year with a $500 million issuance.

Metals And Mining

Brazilian steel companies are suffering from a flood of Chinese steel imports, which are depressing prices. Chinese steelmakers are pushed to dump excess stocks elsewhere as the country's economy slows down amid lower global steel demand. In response, several countries are adopting protection measures like import duties. Although steel consumption grew by 1.5% in 2023 in Brazil, the share of imported products increased by 50% in the period, and reached more than 20% of market share.

The weaker prices have shrunk margins with Usinas Siderúrgicas de Minas Gerais S.A. reporting negative EBITDA in the third quarter, and we have limited visibility for price-adjustment capacity in the next few months. Companhia Siderúrgica Nacional benefits from the supportive iron ore prices to compensate for weak EBITDA from steel, while Gerdau S.A. has a broader geographic footprint that bolsters profits.

The mining companies in LatAm continue performing relatively stable with favorable prices of copper, zinc, silver, gold, and tin. These are main metals that the rated players produce. In general, cash generation should be enough to cover investments and debt service, with the probable exceptions of Antofagasta plc (the second concentrator at the Centinela mine) and Codelco (a sizable capex plan to recover gradually its production).

In Mexico, companies are struggling with higher inflation and the peso's appreciation against the U.S. dollar. We revised the outlook on Grupo Penoles and Fresnillo to negative because of these factors. On the regulatory front, the amendment to Mexico’s Mining Law, which increases regulation and ESG standards, shouldn't impact the rated industry players.

Outlook Bias	-11.1
% Downgrades in 2023	2.9
% Upgrades in 2023	0.0
Gross Margin change %*	-17.2
Net debt to EBITDA §	1.3x
EBITDA Ints Coverage §	9.8x

*medians, last twelve month as of Sep 2023 vs. 2022
§ medians, last twelve months as of Sep 2023
% of downgrades and upgrades are relative to total count

Retail

We believe business conditions for Brazilian retailers will start to improve in 2024 after a tough 2023. We expect slight improvements in profitability and cash flow in 2024 driven by the decreasing interest rates, high employment, and stable inflation.

Still, Brazilian retailers that focus on discretionary goods will continue facing challenges given their high debt and depressed consumption--which lags in its reaction to decreasing interest rates. Consequently, we currently have negative outlooks on Magazine Luiza S.A. (brAA-/Negative/--) and Grupo Casas Bahia S.A. (brBBB-/Negative/--). On Jan. 28, 2024, Magazine Luiza announced a private capital increase of up to R$1.25 billion, which should improve slightly its capital structure and support investments, while the company continues to develop its online platform. Casas Bahia should continue working on its turnaround plan, focusing on its physical stores, which we believe will reduce its capital outflows during the next few years.

Brazilian apparel retailers should benefit from streamlined inventories and improving demand, which should result in better EBITDA margins and cash flow. That's the case for Lojas Renner S.A., Grupo de Moda Soma S.A., and SBF Comércio de Produtos Esportivos S.A. In addition, Grupo Soma announced the largest deal in the Brazilian retail segment in the last decade by combining its business with Arezzo & Co. (not rated), which prompted us to place our rating on Grupo Soma on CreditWatch positive on Feb. 6, 2024.

For Brazilian food retailers, we expect a more stable year after a deflationary trend during 2023, resulting in better growth prospects for top-line revenue and EBITDA for Atacadão S.A. We believe the segment will also benefit from high employment and stable inflation in the country.

Outlook Bias	-35.0
% Downgrades in 2023	10.1
% Upgrades in 2023	4.5
Gross Margin change %*	+1.8
Net debt to EBITDA §	3.8x
EBITDA Ints Coverage §	1.7x

*medians, last twelve month as of Sep 2023 vs. 2022
§ medians, last twelve months as of Sep 2023
% of downgrades and upgrades are relative to total count

In Mexico, we expect a modest slowdown in consumption in 2024, after a surprisingly strong 2023, in line with our GDP growth expectations. We expect revenue growth for the rated companies of 8%-9% in 2024 and an EBITDA margin contraction of a few basis points.

Although we anticipate continuity in a few factors that drove consumption in 2023, such as real wage growth and credit availability, a potential slowdown in the U.S. economy and a stronger Mexican peso could moderate the remittance flows, in addition to general elections in Mexico and the U.S.. This leads to our view of a less favorable environment for consumption in 2024, especially for discretionary goods and services.

Retailers' need to enhance their omnichannel capabilities will remain key to serve and attract customers, given the recent entrance of Chinese online retailers into Mexico's market, which have gained popularity quickly, especially in soft-line categories. Additionally, we anticipate a slowdown in dining out, as it is commonly one of the first expenses that consumers pull back during the economic slowdown, while labor costs would continue rising above inflation.

Hence, we consider that restauranters will continue focusing on efficiency and keeping lean structures, with selective openings. Yet Mexican rated retailers have the liquidity and credit metrics cushion to face tougher business conditions.

Like in Brazil, Chile's lower inflation and interest rates should bring some relief, but we don't expect major recovery in domestic consumption or construction activity. This will result in a somewhat better but still challenging scenario for Falabella S.A. (BB+/Negative/--). Nevertheless, we believe the deep inventory reduction completed during 2023, the efficiency plan implementation, and asset sales should improve profitability and credit metrics.

We expect to see some refocusing of the online strategy among some retailers. In the post-pandemic era, some of them have struggled to compete with pure marketplace players. In line with this trend, we expect them to increasingly leverage and invest more on their physical capabilities to adapt them to interact with and strengthen their digital channels.

The outlook for Colombian retailers remains challenging in 2024. The decrease in interest rates began in December 2023 and would gradually moderate during 2024. In this context, we do not expect a noticeable improvement in domestic demand in line with our growth forecast for the Colombian economy of 1.3%. Companies have tried to maintain their market share and continue to invest in improving their logistic capabilities in omnichannel and online platforms. However, rising double-digit wage costs in the past two years will continue to pressure margins.

Real Estate And Homebuilders

All LatAm real estate operators that we rate have a stable outlook, signaling our expectations for rating stability in 2024. Higher-for-longer interest rates remain a key risk for real estate assets, especially for distressed assets, such as office properties. However, half of the rated companies are investment grade, with a significant credit buffer to absorb downside risks; the other half are mostly in the 'BB' rating category, with the exception of one rated entity in the 'CCC' category (due to its vulnerability to external events given its unsustainable capital structure).

Outlook Bias	-14.3
% Downgrades in 2023	2.9
% Upgrades in 2023	4.5
Gross Margin change %*	-10.6
Net debt to EBITDA §	4.3x
EBITDA Ints Coverage §	3.8x

*medians, last twelve month as of Sep 2023 vs. 2022
§ medians, last twelve months as of Sep 2023
% of downgrades and upgrades are relative to total count

Industrial real estate companies in the region will continue to ride the positive momentum given nearshoring and growing e-commerce tailwinds, particularly in Mexico. We expect retail portfolios will perform well due to resilient consumption trends but with limited upside in terms of expansions. We also believe office properties will remain under pressure due to hybrid work, slowing economic growth, inflation, and the expectation for interest rates to remain high. The anticipated slowdown in the U.S. and LatAm economies may affect some of these companies' tenants; however, we estimate the impact on operating indicators will be relatively mild. We consider most of the rated entities to be relatively well positioned to weather a challenging year amid high financing costs. On average, we expect a rise in revenue and EBITDA to approach 10% for these entities.

Funding needs for industrial real estate operators will increase for growth initiatives, although financing is available and committed in most cases. For retail and office operators, funding needs will be significantly lower, given the absence of gross leasable area growth in these asset classes. We estimate relatively stable coverage ratios despite higher financing costs, and for refinancing risks to be limited in 2024. In most cases, the rated entities maintain well-extended debt maturity profiles. Moreover, there are some planned asset recycling and divestments for this year, though pressure on office property valuations could delay some of these plans.

Our outlook on LatAm homebuilders and developers remains mostly stable. More than 70% of the rated entities have a stable outlook and less than 15% a negative outlook, representing a slight improvement from last year. In Brazil, we forecast significant improvements in homebuilders’ gross margins and cash flow during 2024 driven by the recognition of more profitable projects launched between 2022 and 2023, stable inflation, a decrease in interest rates, and the expansion of the Minha Casa Minha Vida (MCMV) program last year. During 2023, the companies’ figures were severely impacted by the delivery of less profitable projects launched during 2021 and 2022, which were hit by record-high inflation, a trend that should be reverse in 2024.

Taking into consideration the 16 rated Brazilian homebuilders, we expect launches' potential sales value to reach R$41 billion in 2024 (an increase of 18% year on year) driven mainly by the changes in the MCMV program that allowed higher price increases and by strong demand. We also expect an average increase of 5 percentage points in gross margins, which coupled with the basic interest-rate decrease (currently 55% of homebuilders’ debt is linked to basic interest), should result in average operating cash flow of R$176 million during the year, versus operating cash flow losses of R$38 million in 2023.

Currently 60% of rated homebuilders’ debt consists of debentures and other corporate debt, with the remainder linked to project debt. Out of this, 30% or about R$3 billion are due in the next 12 months. With expected positive cash flow, we believe some companies will repay upcoming maturities with cash, refinancing the remainder with new corporate debt. We expect new launches to be financed through project debt.

In Mexico, housing production has reached another historically low point of 131,059 units in 2023, according to Registro Unico de Vivienda. Yet we expect credit quality of homebuilders Consorcio Ara S.A.B. de C.V. (mxAA-/Stable/--), Inmobiliaria Ruba S.A. de C.V. (mxAA-/Stable/mxA-1+), and Vinte Viviendas Integrales S.A.B. de C.V. (BB-/Stable/--; mxA-/Stable/--) to remain stable through 2024. In our view, this mostly stems from their flexible business models to adapt to market demand, geographic and segment diversification, and healthy balance sheets, including low leverage and solid liquidity positions.

We expect Mexico’s housing starts to stabilize at 130,000 – 135,000 units in 2024 amid still difficult business conditions, including persistent inflation, which increases home prices and creates affordability concerns for a large part of the population, a large informal labor force with no access to financing, labor scarcity in the sector, while some states of the Mexican republic face water scarcity issues.

On a more positive note, we believe that the sector will continue benefiting from favorable structural factors including the housing deficit in the country, supportive demographic trends, and slowly growing formal employment, but also from mortgage availability, at fairly stable rates, from well capitalized financial institutions. Moreover, we expect the government-owned entities Instituto del Fondo Nacional de la Vivienda para los Trabajadores (Infovanit) and Servicios Sociales de los Trabajadores del Estado (Fovissste) will continue expanding their housing programs and customer base, which will attract potential homebuyers to the market.

General elections will take place in Mexico during 2024 and we will continue to monitor any potential shift in the national public housing policy and its potential implication for the sector, although we currently expect a high degree of policy continuity. Thus, for 2024, we expect the rated Mexican homebuilders to continue leveraging their competitive positions and business flexibility from inventories and landbank reserves; and geographic, product, and financing diversification to raise top-line revenue growth and increase their market share in this highly fragmented market without weakening their credit quality.

Colombia's high interest rates and restricted access to financing have strained homebuilders' liquidity and margins, and increased their leverage. Moreover, the sharp decrease in domestic demand and homebuyers' lower payment capacity accelerated the drop in home purchases. In 2023, a construction company Inverfam (not rated) defaulted on bond payment. In 2024, the government's decisions about housing subsidies and the recent decrease in prices of raw materials, such as steel, could boost the sector, although the sector's complex conditions have limited the start of new projects and will delay its recovery.

Telecom And Cable

Outlook Bias	-29.2
% Downgrades in 2023	5.8
% Upgrades in 2023	7.6
Gross Margin change %*	-3.1
Net debt to EBITDA §	5.5x
EBITDA Ints Coverage §	2.2x

*medians, last twelve month as of Sep 2023 vs. 2022
§ medians, last twelve months as of Sep 2023
% of downgrades and upgrades are relative to total count

The overall trend is positive for the Brazilian telecom players in 2024, after a year marked by an evolving mobile market with the start of 5G and a deceleration in investments by the regional independent service providers (ISPs). A more favorable macroeconomic environment of falling interest rates and higher employment should help expand the client base and improve profitability of most of the rated companies.

We expect larger Brazilian rated players, Telefonica Brasil S.A. and Algar Telecom S.A. to continue growing and posting sound operating performance and margins, with a focus on delivering bundled products, more value-added services, and 5G coverage across Brazil.

The ISPs, on the other hand, are still implementing 5G coverage at a slower pace, given that most formal regulatory requirements start only in 2026 and that mobile is a new business for most of the regional companies. Brisanet Participações S.A. and Unifique Telecomunicações S.A. have been the first ISPs to launch mobile/5G services in their regions.

For fixed broadband in 2024, we expect to continue seeing a slow pace in network expansion, with companies slashing capex. Margins, however, are likely to improve amid better macro conditions and due to higher take-up rate (growing client base with marginal investments in backbone).

We expect more M&As during 2024, as interest rates fall and demand for broadband services resumes growth. Towards the end of 2023, Vero S.A. and America Net S.A. announced a business combination, creating the second largest independent ISP in Brazil (and the largest rated one).

Another factor to monitor during the year is the development of neutral network, as a way for ISPs to grow their client base without the need to increase capex. Vital – Rede Neutra de Comunicações S.A. is the main company in the business and has been diversifying its client base, especially to reduce the share of revenue coming from its main client, Oi S.A. Additionally, the approval of Oi's judicial recovery plan may give more clarity to what will happen with the sale of its Client Co.

Our main concern in the sector during 2024 is about companies with higher leverage and/or tighter liquidity positions, such as Ligga Telecom S.A. and Triple Play Participações S.A. We expect better operating performance and improving margins during the year to provide a relief; however, there are substantial risks that companies might not deliver credit metrics aligned with our expectations.

In Chile, the trend is flat to positive. Strong competition, higher inflation, and sizable investments have eroded margins, cash flow, and balance sheets of most of the Chilean players. Out of the four rated operators, one has a negative outlook (Telefonica Moviles Chile S.A.; BBB-/Negative/--), one a developing outlook (VTR Finance N.V.; CCC/Developing/--) and one on CreditWatch negative since December (Wom S.A.; B/Watch Neg/--).

There have been some signs of market rationalization, and we expect operators to continue increasing rates in 2024 in line with inflation. This should prevent further drops in ARPUs, along with gradual improvements in margins.

While the first phase of 5G investments is coming to an end, we expect capex to remain relatively high to keep expanding network and upgrades to defend the customer base in a very competitive market. This will continue placing pressure on cash flow, which we expect to slip or turn negative across the board in 2024. But given some recent announcements, we also expect lower dividends, some capital increases (like the one Telefonica Moviles completed in December) or retention of the proceeds from asset sales in order to strengthen balance sheets.

Our main concerns remain over Wom and VTR. The latter has an unsustainable capital structure. Since the completion of the joint venture (JV) with Claro Chile, there's been a lack of transparency regarding the JV's consolidated financial performance, business plan, and strategy to revert business results. On the other hand, Wom has maintained good operational performance, but its difficulty to complete the refinancing on the Nov. 2024 notes is raising obstacles to raise additional liquidity in the short term.

In Mexico, we expect larger players like AMX to continue growing, taking advantage of the realized investments in the 5G spectrum. However, growth in Colombia is somewhat constrained by the entrance of new players into the market, which has created some destabilization in the market with higher churn rates and lower ARPUs. We also see strategies such as JVs for the unification of mobile networks and spectrum (Colombia Telecomunicaciones S.A.; B/Watch Neg/--) and UNE EPM Telecomunicaciones to give greater deployment to commercial strategies and save resources in operations and capex. However, as a consequence of cost pressures, fierce competition, and a sluggish recovery of domestic demand and the Colombian economy, we expect lower margins and profits. In both countries, we continue to see higher investments in new technologies, such as the 5G deployment to improve customer loyalty.

For tower companies, we continue to view growth prospects as favorable, as under-penetration remains a driver for the expansion of their respective networks, compared with more developed markets, like the U.S.

Transportation

We expect industry dynamics for airlines to remain largely favorable. Despite modest economic growth in the region, expected lower inflation and interest rates should continue supporting travel demand in a still underpenetrated market. Furthermore, supply will likely remain constrained amid delays in aircraft deliveries, retirement of less efficient aircraft, exit of competitors (particularly in Peru and Colombia), and overall moderately competitive environment. Gol Linhas Aéreas Inteligentes S.A.'s recent filing for Chapter 11 protection will also increase rationality to the market, particularly in Brazil, as we don't expect the company to make significant capacity increases during the proceedings. Therefore, we expect airlines to continue benefitting from a high yield environment underpinning margins despite rising costs (fuel and labor particularly).

We expect Brazilian railroad companies will continue benefiting from volume growth this year. We forecast solid agricultural volumes in 2024, although crop yields will likely be smaller than record-high levels registered last year. Also, the expanded production, mainly among pulp and mining companies, should boost volumes of general cargo and heavy haul. Lower cost pressures with easing inflation and expected stable fuel prices will continue supporting profitability. We expect the companies to use solid operating cash flow to perform large capex over the next few years, linked to concession renewal requirements and/or expansion and modernization of existing assets. Although we assume debt increases for part of this capex, leverage should remain fairly stable thanks to increasing EBITDA.

Outlook Bias	-13.3
% Downgrades in 2023	8.7
% Upgrades in 2023	15.2
Gross Margin change %*	+43.1
Net debt to EBITDA §	3.9x
EBITDA Ints Coverage §	2.0x

*medians, last twelve month as of Sep 2023 vs. 2022
§ medians, last twelve months as of Sep 2023
% of downgrades and upgrades are relative to total count

Fleet Management And RaC

We believe that more stable macroeconomic conditions in Brazil, with the reduction in interest rates and controlled inflation, should support the car rental and fleet management industry growth this year. The production and sale of new light vehicles will likely increase 6.0%-6.5% in 2023, according to the National Association of Automotive Vehicle Manufacturers, similar to the 6.85% growth in 2022.

Some industry players have increased leverage over the past few years in order to grow and are now more focused on fleet renewal, rather than on expansion, to avoid cash flow pressures. We also expect the companies to continue increasing operational efficiency, mainly through higher utilization rates. The combination of these factors, along with lower inflation and base interest rates, should raise the sector's EBIT interest coverage, which was very low in 2022 and 2023, given base interest rates of about 13%.

The greater credit availability for used-car sales and improved macro conditions should also support solid demand in 2024. But EBITDA margins for the used-car sales segment has been normalizing over the past few quarters, and we expect them to be 3%-5% this year, similar to pre-pandemic levels.

Outlook Bias	+20.0
% Downgrades in 2023	0.0
% Upgrades in 2023	6.1
Gross Margin change %*	-10.3
Net debt to EBITDA §	3.6x
EBITDA Ints Coverage §	1.8x

*medians, last twelve month as of Sep 2023 vs. 2022
§ medians, last twelve months as of Sep 2023
% of downgrades and upgrades are relative to total count

Utilities

Currently, about 72% of the rated Latin American utilities have a stable outlook, as sovereign ratings continue to determine a significant portion of our largest regulated utilities. A strong El Niño will have varying effects on LatAm countries, alleviating spot prices in Brazil and Chile but elevating them in Colombia and Peru. Oil prices should remain volatile amid geopolitical risks.

Despite a sluggish economic scenario and still high cost of debt, we think creditworthiness of utilities will remain unchanged in 2024. Moreover, we think that companies in this sector have flexibility to not only postpone investments but also reduce dividends, if needed, to preserve cash. Moreover, many of the rated entities were able to refinance debt in 2023 and to extend debt tenors, alleviating short-term pressure on liquidity, and we expect this trend to continue in 2024.

In general, we continue to expect governments in the region to keep fostering green energy, except Mexico, given its plans to prioritize fossil fuel sources. But higher-for-longer interest rates and input cost inflation could trim returns on long-term generation projects, slowing the energy transition in LatAm, particularly in Brazil given the prevailing low spot prices.

Energy transmission bottlenecks remains a key risk in some jurisdiction in LatAm , including Chile, Argentina, Colombia, and Mexico. We will keep on monitoring the development of new t-lines concessions, particularly if the pace of new solar and wind energy continues surpassing the last five-year average.

Outlook Bias	-4.2
% Downgrades in 2023	11.6
% Upgrades in 2023	12.1
Gross Margin change %*	+4.6
Net debt to EBITDA §	3.5x
EBITDA Ints Coverage §	3.3x

*medians, last twelve month as of Sep 202 vs. 2022
§ medians, last twelve months as of Sep 2023
% of downgrades and upgrades are relative to total count

Transportation Infrastructure

Most of the rated LatAm airports, ports, roads and mass transit assets have a stable outlook. Mexico and the Caribbean passenger air traffic continues to grow above pre-pandemic levels, thanks to domestic and short-haul demand to and from the U.S. Meanwhile Brazil has fully recovered to pre-pandemic levels in 2023 driven by domestic traffic. Despite inflationary pressure on disposable income, we continue to forecast air traffic growth to be in line with GDP growth, driven by customers' willingness to travel. We expect most of the expansion investments will be in Brazil and Mexico.

We expect flat volumes for Brazilian ports in 2024, because higher exports of agricultural and protein will be mitigated by lower import volumes. In Peru, El Niño should hit both agricultural and pisciculture production, hampering export volumes.

Most LatAm rated toll road operators have stable outlooks, reflecting strong operational performance and headroom in financial metrics. Traffic volumes in most of countries rose at a 3x-4x elasticity to GDP in 2023, driven by heavy-vehicle volumes, in particular in Brazil and Mexico, where robust exports were a key driver of the economic performance. We expect increased expansion capex among Brazilian entities that extended their maturing concession portfolios by participating in new concession auctions. We also expect maintenance investments earlier than expected, due to the degradation of roadways caused by increased heavy-vehicle volumes. We expect financing conditions to be tighter for these investments, given higher interest rates across markets in LatAm countries. High inflation and weaker economic performance might hamper the performance of Chilean toll roads, as inflation-adjusted toll rates start to weigh on commuter traffic. Finally, we are monitoring the development of the early termination of the Rutas de Lima toll road in Peru, announced in early 2023.

Outlook Bias	+12.5
% Downgrades in 2023	5.8
% Upgrades in 2023	12.1
Gross Margin change %*	-4.7
Net debt to EBITDA §	2.8x
EBITDA Ints Coverage §	3.2x

*medians, last twelve month as of Sep 2023 vs. 2022
§ medians, last twelve months as of Sep 2023
% of downgrades and upgrades are relative to total count