

Argentina Market Outlook

IEB - Report



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BUY Argentina: sovereign risk collapses as Macri's chances of winning the elections increase

As we anticipated in our previous reports, we always thought that President Macri would win the 2019 elections and as of yesterday, his chances have increased quite considerably. Under this framework, we think that the political events that occurred in the last 18 trading sessions have completely changed the trend in which Argentina's financial assets will evolve in the following months. Definitely, the trend is now positive. We do not discard many days of high volatility, but across a trend that will push Argentina's financial assets upwards as political risk evaporates and as President Macri consolidates his chances of a second period in charge.

Argentina's financial assets have been punished very substantially since the FX crisis in April 2018. This means that current valuations are very cheap provided that Cambiemos can win the presidential elections. We anticipate that this event will happen and therefore, since yesterday a very significant window of asset accumulation

has emerged igniting a positive medium term trend which will imply a consistent price recovery over the following five months. As of now, Argentina is a BUY in its three dimensions: fixed income, equity and FX.

Two significant events occurred in the last 18 trading sessions regarding Argentina's political landscape. First, kirchnerism announced a new formula with Alberto Fernández as candidate for President and Cristina Fernández as Vice President. Second, Cambiemos announced its own formula with Mauricio Macri running for President and Miguel Pichetto, a very powerful leader from moderate peronism, as Vice President.

These announcements have multiple impacts. First, the fact that Cristina Fernández no longer runs for the presidency implies a very significant sign of weakness. Second, the fact that Macri has now built a wider political alliance that includes the moderate side of peronism significantly increases its chances of winning the elections and also implies that eventually, in his second mandate he will be able to achieve a much stronger political support which will be essential given the long list of structural reforms still pending in Argentina.

Having said this, the announcement of President Macri's formula has been widely celebrated by Wall Street in many dimensions. First, in the last two trading sessions Argentina's 1yr CDS dropped 183 BPS. Second, in the same period Argentina's 5yr CDS dropped 90 BPS. Third, Argentina's equity markets have rallied approximately 20% in only two days and the Peso appreciated 2.70% against the dollar. And in the last 18 trading sessions combined, Argentina's 1yr CDS collapsed 690 BPS, Argentina's 5yr CDS dropped 224 BPS and equity markets rallied approximately 35%. We consider that these events imply a very substantial re-setting of Argentina's economic and political risk. Definitely, Wall Street celebrated the announcement with a historical rally in the three dimensions of Argentina's asset class spectrum: fixed income, equity and FX. Particularly, short-duration bonds outperformed longer-duration bonds implying that Argentina's sovereign curve is under a very aggressive disinversion process and far from being over.

In addition, global markets have turned very dovish in the last couple of weeks, which means that the demand for

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EM assets has increased very significantly. Therefore, as the EMBI index finally broke the 110 level, demand for EM bonds keeps rising searching for a reasonable story to follow through as it is the Argentine case. As the US yield curve keeps trending downwards, as the greenback keeps depreciating against foreign currencies, and as Argentina's political landscape keeps turning less uncertain and much more promising, the demand for Argentina's financial assets should increase in the following weeks feeding a significant price recovery.

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