S&P Global
Ratings

Latin American Corporate And Infrastructure Midyear Credit Outlook 2024

Coming Off A Solid First Half

August 21, 2024

This report does not constitute a rating action

Contacts

Diego Ocampo
Buenos Aires
diego.ocampo@spglobal.com

Julyana Yokota
Sao Paulo
julyana.yokota@spglobal.com

Key Takeaways

- Rating activity during the first half of 2024 was overall positive, with upgrades outpacing downgrades by 60%. This was partly owing to Argentina's upgrade but also to improving conditions for sugarcane producers, some telecom and cable companies, and oil and gas producers, among others. Downgrade activity was mostly among retailers, chemicals producers, and a few real estate and homebuilders. Net bias remained slightly negative at -7%, which indicates a fairly stable horizon for corporate ratings.
- While 70% of sectors are growing, only 45% are doing it above inflation rates. We believe that puts pressure on future margins, although it doesn't show yet. Similarly, still high interest rates should continue to pressure issuers' funds from operations. Among best performers are some real estate and homebuilders in Brazil, which are thriving thanks to reinvigorated demand for government housing plans, and certain airlines that benefit from improving business conditions. Margins and credit ratios of retailers, and oil and gas companies are also improving as well.
- Weakening trends are more evident among chemicals producers and steel companies. Both sectors are suffering from low prices. Steel companies in Brazil are facing high imports from Chinese steelmakers, which are pressuring domestic prices despite solid demand.
- Lastly, international bond issuance slowed meaningfully after a strong first quarter of the year. And corporations tapped domestic markets, particularly in Brazil and Mexico. The trend is in part owed to the resurgence of the infrastructure investment in Brazil as domestic interest rates decline, but also due to better pricing conditions. Moreover, international bond maturities for the rest of the year and for 2025 remain manageable.

Upgrades Dominated The First Half Of 2024

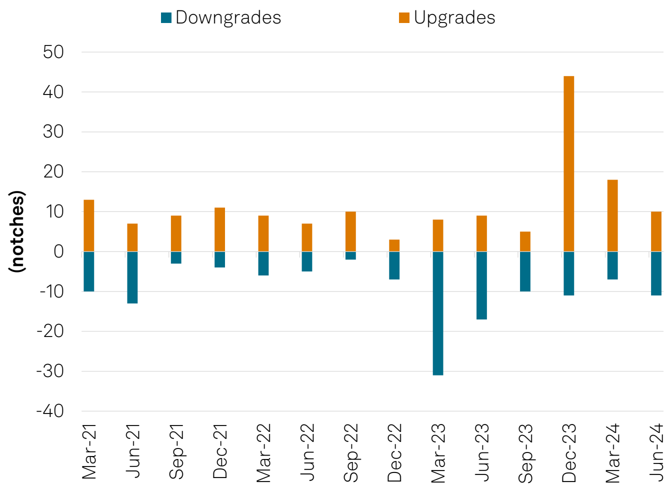
Rating activity has been overall positive in the first half of the year partly thanks to Argentina's upgrade to 'CCC/C' from 'SD/D' on March 15, improving conditions for agribusiness, and positive impact for power generation and utility issuers due to the implementation of the sector-specific criteria in April 2024 (chart 1). Downgrades were spread across all corporate and infrastructure sectors but with a larger incidence among retailers, chemicals producers, and a few real estate and homebuilders (chart 2).

There were only five defaults during the first six months of the year or slightly above 1% of all regional corporate issuers. Among recent defaults, there were two companies that had already defaulted in the past five years: CLISA – Compania Latinoamericana de Infraestructura y Servicios S.A. and Enjoy S.A. We studied these two cases and other emerging market re-defaulters in the commentary titled "Emerging Market Re-Defaulters' Business Overhaul Plans May Be Falling Short", published July 18, 2024.

Chart 1

Corporate rating changes in Latam

Since 4Q 2023 ratings' upgrades were substantial

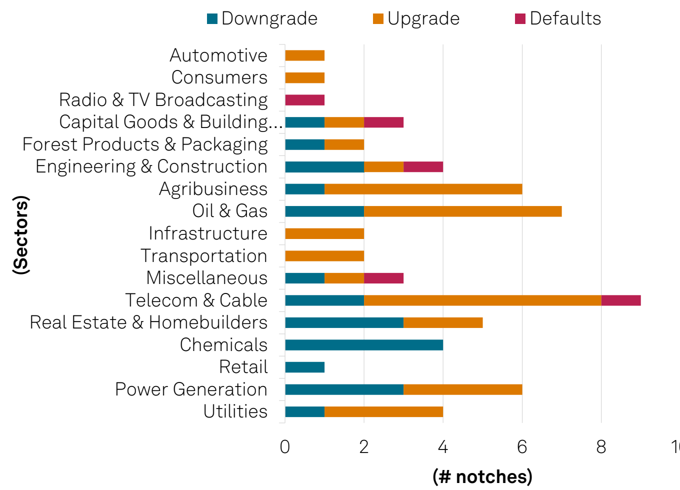


Source: S&P Global Ratings.

Chart 2

Corporate rating changes and defaults broken by sectors

Upgrades and downgrades broadly distributed



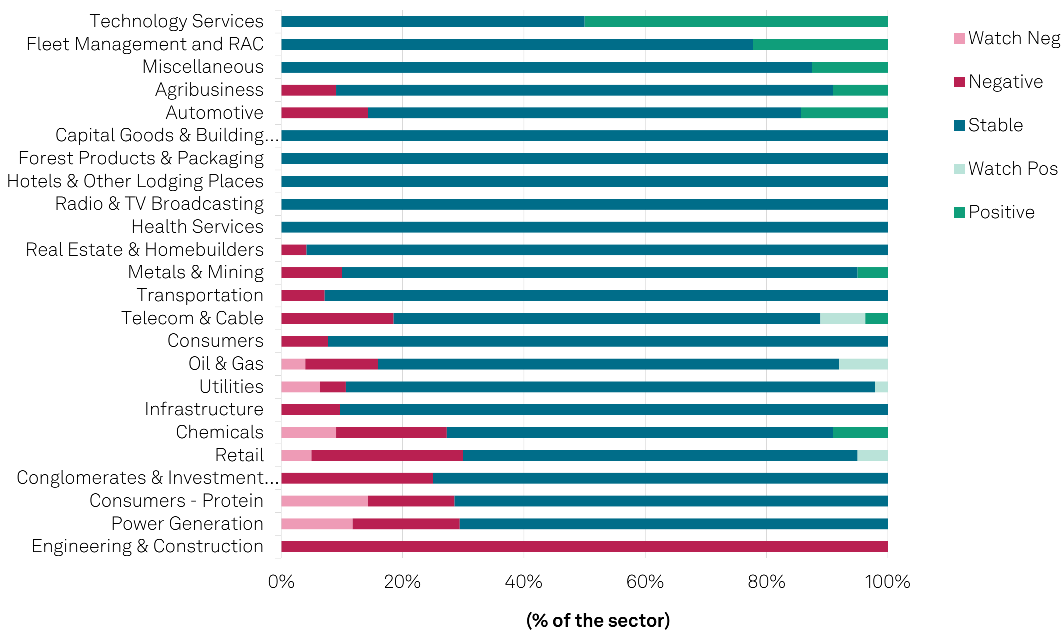
Source: S&P Global Ratings.

Sector outlooks remain largely stable with a net bias of -7% (see chart 3). Sectors with a larger proportion of negative outlooks are retailers, chemicals producers, and power generators. Even though the latter sector accounts for the large portion of the negative bias among the sectors, this is because of specific credit rating fundamentals, rather than industry-related factors, resulting in the stable outlook for more than 70% of the rated issuers.

Chart 3

Outlook distribution by sector

Outlooks remain largely stable



Source: S&P Global Ratings. Outlooks as of July 31st.

Inflation Pass-Through Costs And Persistently High Interest Rates Dent Profitability

Although 75% of corporate sectors in LatAm are growing, only 40% are doing so above inflation rate. The trend coincides with our view that major economies in the region such as Brazil, Mexico, and Argentina will grow slower in 2024 than in 2023. Sectors that are expanding above inflation rate are infrastructure, transportation, real estate and homebuilders, agribusiness, health services, and fleet management and rent-a-car (RAC).

Real estate operators (FIBRAs in Spanish) in Mexico are benefitting from strong demand as industrial companies increase stocks to cope with rising demand due to nearshoring trends, particularly among auto-parts companies. In Brazil, homebuilders are increasing housing starts amid rising as demand has grown steadily thanks to the broadening of the government's Minha Casa Minha Vida housing program. Also, the operations of some airlines are improving, given growing travel demand, amid the industry's rational supply in the region, allowing for stronger margins and credit profiles. We expect these sectors to thrive in 2024.

But profit margins are resilient as 75% of corporate sectors' gross margins are in line with historical levels (chart 4). Among the underperformers are chemicals companies that are still suffering from weak pricing conditions, and metals and miners that posted a disappointing first-quarter performance, as copper and iron ore prices were below 2023 levels. Copper prices improved substantially in the second quarter of 2024, while Brazilian steel producers are dealing with weak global steel prices. We expect steel prices to remain subdued as global demand is likely to remain lackluster.

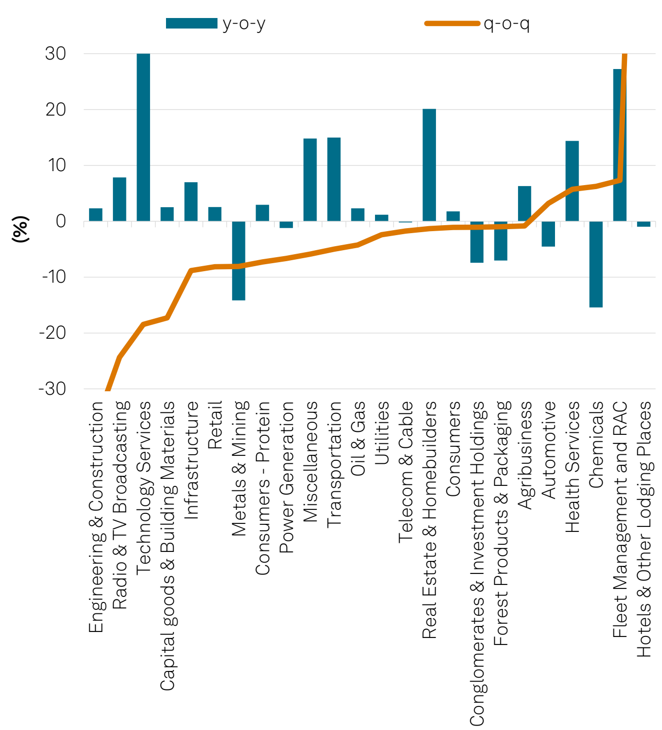
Among the strongest performers in profitability are transportation, real estate and homebuilders, retailers, and oil and gas companies (chart 5). The first two sectors benefit from good conditions as we mentioned earlier, while Peruvian and Mexican retail operations are showing resilience.

Almost 60% of sectors are grappling with higher effective rates than historical. Still-high policy rates in Brazil, Chile, and Mexico are the main drivers. Even though most of the region's central banks have lowered their rates, and we expect them to keep dropping, the benefits haven't been noticeable yet.

Chart 4

Corporates' revenue growth patterns

40% of sectors growing above inflation

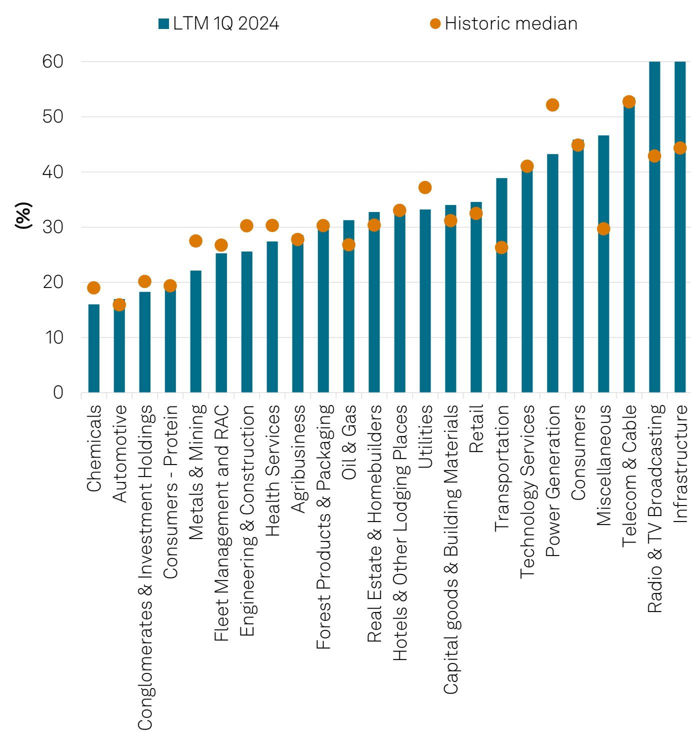


y-o-y--Year-over-year. q-o-q--Quarter-over-quarter as of March 31, 2024. Source: S&P Global Ratings.

Chart 5

Corporate gross margins

Margin erosion isn't generalized

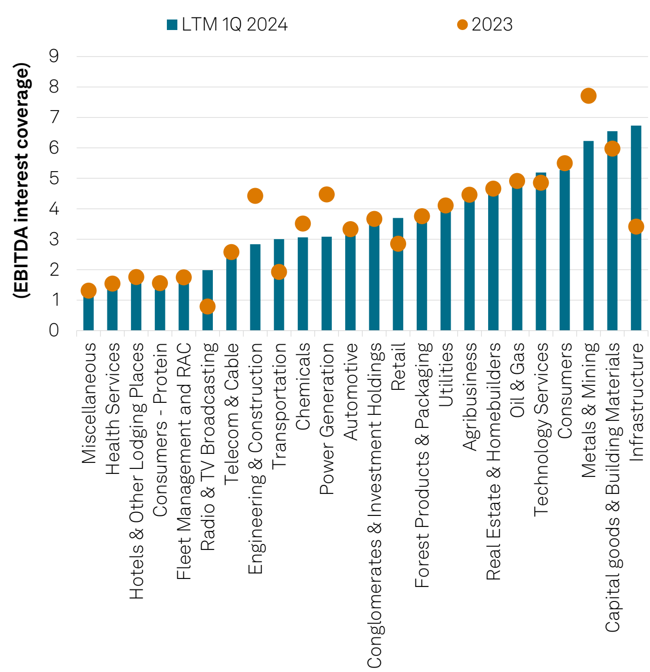


Source: S&P Global Ratings. Gross margins last twelve months as of March 31, 2024 vs Medians 2015-2023.

Chart 6

Corporates' interest coverages

Ebitda interest coverages remain fairly aligned with 2023

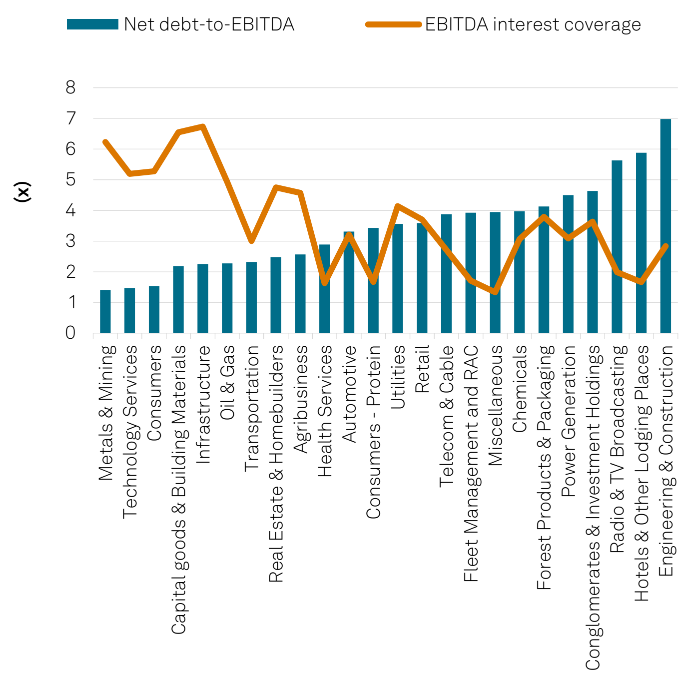


Median coverages calculated on a twelve month basis, as of March 31, 2024.
Source: S&P Global Ratings.

Chart 7

Corporate leverage and interest coverage

High borrowing costs results in weak coverage parameters



Source: S&P Global Ratings.

Energy Transition: A Big Driver Of Future Growth

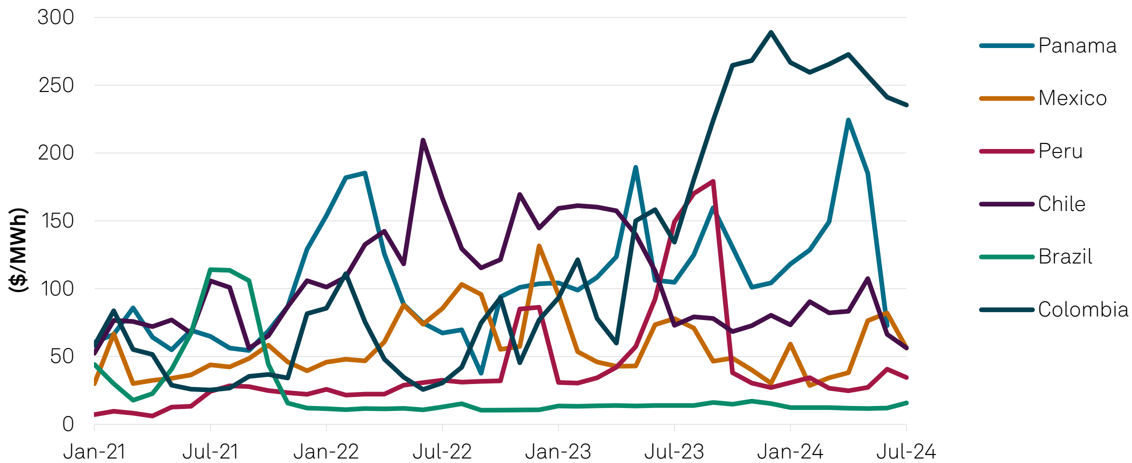
We expect the LatAm oil and gas sector to continue to expand robustly in the next few years. Small and medium exploration and production oil and gas companies are bolstering production in Brazil and Argentina amid favorable pricing conditions and prospects for natural gas as a clean energy source. Argentine oil and gas companies are expanding strongly in Vaca Muerta shale and tight formation fueled by the new regime called RIGI (the Spanish acronym for *Regimen de Incentivo para Grandes Inversiones*) that sets favorable tax, currency, and exporting conditions for investments of above $200 million. In fact, on top of ongoing important midstream investments, such oil pipelines Vaca Muerta Sur and Oldelval II, future investments in LNG facilities are under study and with probable date of confirmation in early 2025.

The expansion of unconventional renewable capacity will accelerate, particularly in Mexico starting in 2025 during the Sheinbaum administration. This should allow energy prices to decrease in the medium term, meanwhile, spot energy prices will continue to be driven by hydrological regimes, and oil and gas prices in the next 12 months. A strong climate event--La Niña, expected to start in September 2024--may result in varying effects on LatAm countries. This is the opposite with El Niño, which alleviated spot prices in Brazil and Chile, and elevated them in Colombia and Peru (chart 8).

Chart 8

Energy spot prices in Latin America

Price volatility is substantial in some countries



Source: S&P Global Ratings.

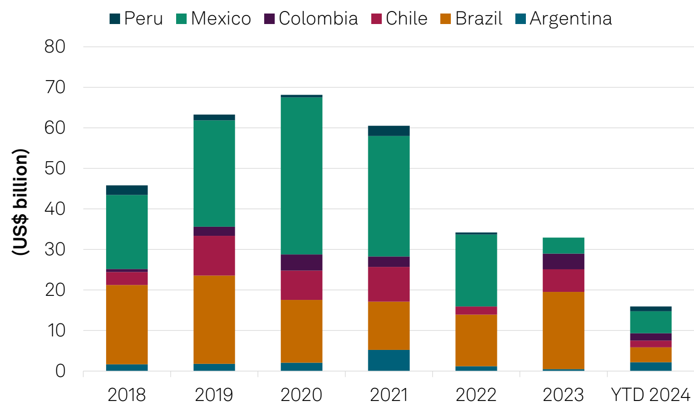
Capital Markets: Corporate Issuers Turning To Domestic Markets

After a promising start of the year, international bond issuances have slowed notably (chart 9). In the first seven months of 2024, corporate and infrastructure entities in the region's largest six economies (Argentina, Brazil, Colombia, Chile, Mexico, and Peru) had issued roughly $16 billion. With the exceptions of Chilean and Argentine issuers, the rest of the rated corporations opted to issue domestically (chart 10). While Chilean corporations have opted to issue less, their Argentine peers took advantage of a few windows and issued more in the first seven months of 2024 than in 2023 and 2022, thanks to improving risk appetite following the government change. The trend is particularly evident in Brazil where domestic issuance doubled compared to same period a year before.

Chart 9

International bonds issued by LatAm corporates

Mexican and Brazilian corporates issuing notably less

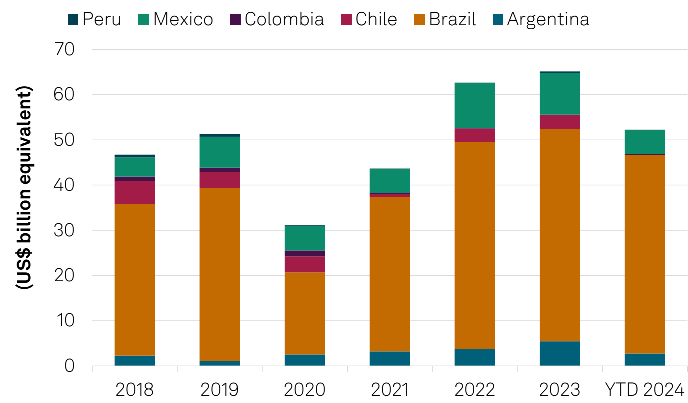


Source: S&P Global Ratings.

Chart 10

Domestic bonds issued by LatAm corporates

Once again Brazilian domestic market testing new highs



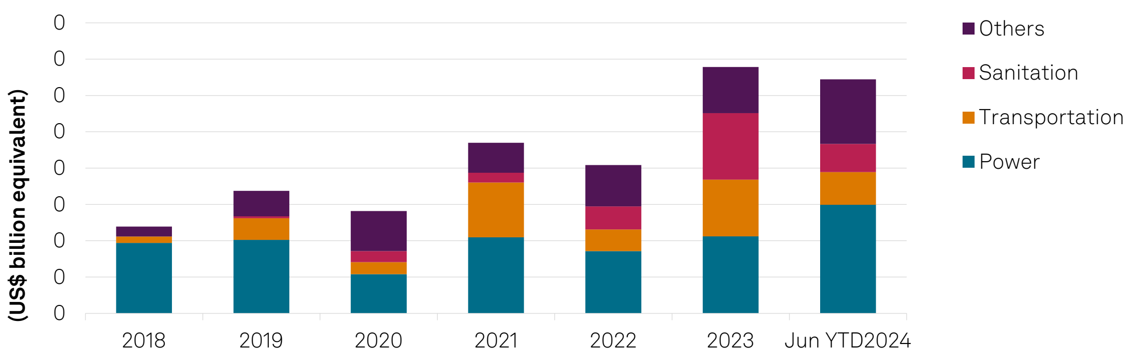
Source: S&P Global Ratings.

Part of the rise in domestic issuance in Brazil is owed to increasing appetite for infrastructure credits, which issued R$64 billion in debentures up to June 2024 (chart 11). We continue to expect utilities, power generation, and transportation infrastructure issuers to attract investor appetite given the solid performance of the sector, which is more resilient to macroeconomic adversities, as observed by its rapid recovery from the pandemic.

Chart 11

Infrastructure debentures in Brazil, broken by segment

Issuances have risen massively



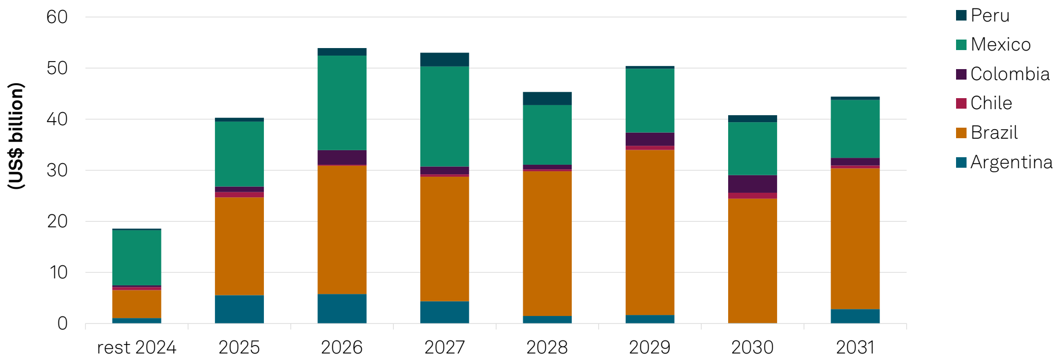
Source: S&P Global Ratings based on ANBIMA.

International bond maturities remain manageable through year-end. In 2025 and 2026, bond maturities are more pronounced, particularly among large Mexican and Colombian issuers (chart 12).

Chart 12

International bond maturities of LatAm corporations

Refinancing needs look manageable in 2023 and 2024



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

Related Research

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