

# FRIEDBERG'S

## LDC DEBT COMMENTS

Friedberg Commodity Management Inc.



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### Argentina

Our comments and recommendation dated June 13, 1988, need to be reappraised. In the first place, the fundamental background continues to deteriorate, almost hopelessly. Secondly, our earlier, rather more optimistic assessment, has hit the market with a lag, raising the price of Bonex and consequently lowering their yield. This "delayed effect" gives us an excellent opportunity to realize a capital gain.

#### The fundamental background

The much talked about Primavera Plan was just more of the same. More social pacts; more deals between unions, industrialists, and the government; more tampering with foreign exchange rates with the government trying to profit from the difference between an incredibly overvalued official austral and a slightly less so unofficial austral; more charity from the World Bank and the IMF. Not the slightest hint of carrying out the only truly sensible reform: laying off 75% of the bureaucracy.

In the meantime, privatization efforts have been stalled in Congress while the prices charged by government-owned enterprises have been frozen in relative terms. This is an absurd attempt to keep notional monthly inflation numbers below double digit levels and in the process imperiling the solvency of these companies that are now being run on a hand-to-mouth basis.

An election has been called for May 1989, and the populist Peronista party is well ahead in the unofficial polls. Its leader, Mr. Carlos Menem, will most likely draw his support from the union ranks. As a result, he is an unlikely candidate for trimming the bloated bureaucracy.

In sum, the country is being managed with mirrors and is being held together by toothpicks, with the ruling party hoping to come to the election with some semi-decent macro-economic numbers.

We doubt it.

**STRATEGY:** *Our favorite Argentinian trading financial asset, the Bonex series 82 (see FC&CC, June 13, 1988) has moved up from 80.50 at the time of recommendation to a recent 85.00 after having paid the August 15 coupon. Total annualized return to date, if the Bonex is liquidated at present levels, is equal to 24.9%.*

*We recommend liquidating these positions simply because at these levels the yield to maturity, 18 $\frac{3}{8}$ %, does not compensate us enough for the risk of chaos and default.*

### Chile

In the plebiscite held on October 5, the united opposition parties defeated the incumbent government candidate, General Pinochet, by 55% to 43% of the vote. In accordance with the present constitution, Presidential and Congressional elections will be held before the end of 1989.

The opposition parties are likely to nominate a candidate from the center-left, most probably a Christian Democrat leader. The right-of-center and other right-wing parties have as yet not crystalized their position nor has the government indicated who its ideal candidate would be. This transitional year is fraught with additional uncertainty because of the demand for some constitutional changes being made by the opposition parties and because of the government's apparent initial intransigence.

The left-of-center parties have admitted that in general, the economic scheme in operation has much to be praised, particularly the openness of the economy to the world and the favorable treatment received by foreign investors. They have, however, also indicated that they would like to see a more active government participation in the economy, a far stronger emphasis on social spending, and the eradication of poverty. In practice, this policy could spell large budget deficits and much higher inflation rates.

The economic picture continues to improve: the balance of trade is likely to show a surplus of more than \$2 billion, \$600 million better than anticipated earlier in the year, thanks in part to very strong primary commodity prices, including copper. The rate of inflation has continued to fall, and now hovers around 10%-11% per annum.

Government finances are in excellent shape as the budget is likely to be balanced for the year. Not a single week goes by without some further privatization move and/or announcement: The latest target is Lan Chile, the flag airline, control of which is being offered domestically and abroad before the end of 1988. The gigantic Escondida copper project is well advanced with more than 15% of eventual expenditures already in place. Finally, the foreign debt continues to fall (see Chart 2) via debt-for-debt and debt-for-equity swaps.

Should the world economy and copper hold up through 1989, the foreign debt problem may disappear almost completely. The new government will thus inherit a clean slate, and risk to Chilean creditors will diminish considerably.

In the interim, the uncertainty surrounding the coming events and the possibility that the next President and Congress of Chile will be much less laissez faire oriented than the present one increases substantially the risks of holding Chilean debt for investment purposes (as pointed out in our March 10, 1988, issue).

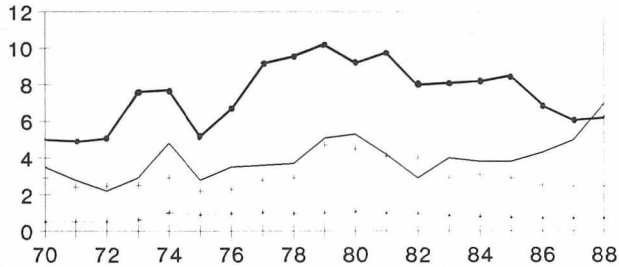
**STRATEGY:** *We estimate that a 16%-18% current yield is sufficient to compensate creditors/investors for the higher risks. Therefore, we advise buying Chilean debt, specifically Banco Central, only in the 45-53 range.*

**LATE NOTE:** As we go to press, Chile's central bank announced that it has bought back \$299 million of debt owed to international creditors, paying \$168.4 million dollars, for an effective discount of 43.7¢ on each dollar of debt. The central bank received 129 offers for a total of \$280 million in the tender process that closed October 31.

Chart 1

**REAL EXPORTS**  
CHILE & ITS NEIGHBORS

Billions of U.S.\$



— CHILE                      —•— ARGENTINA  
+ PERU                        - - - - BOLIVIA

Deflated by U.S. PPI  
1988 projected on basis of first quarter.

Chart 2

**Chile**  
**EXTERNAL DEBT**  
BILLION OF DOLLARS

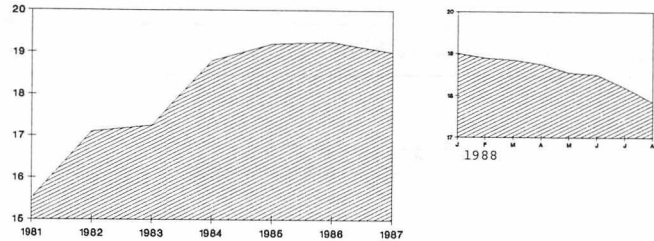
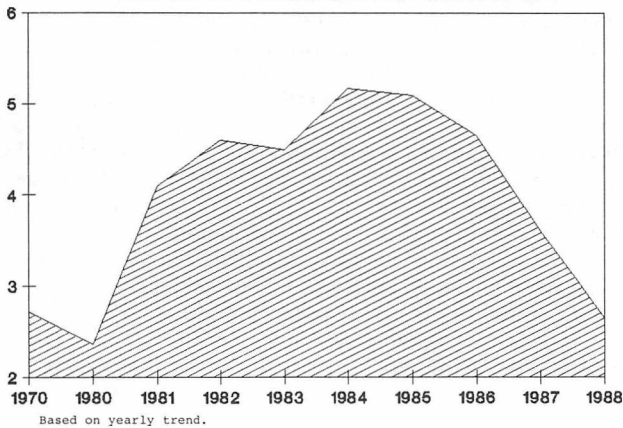


Chart 3

**Chile**  
**DEBT/EXPORT RATIO**



Based on yearly trend.

Chart 5  
**Argentina**

PUBLIC SECTOR  
(in % of GNP)

	1983	1984	1985	1986	1987	1988(e)
REVENUES .....	19.53	18.42	23.24	21.76	20.43	22.96
EXPENDITURES...	34.92	28.84	28.65	25.86	27.81	26.85
NATIONAL PUBLIC SECTOR..	27.32	22.95	22.59	19.21	21.31	19.33
TRANSFERS TO PROVINCES...	7.60	5.89	6.06	6.65	6.50	7.52
DEFICIT .....	15.40	10.42	5.42	4.10	7.38	3.90

SOURCE: SHE.

Chart 6  
**Argentina**

PUBLIC ENTERPRISES : CRITICAL INDICATORS

	Y P F		ENTEL		FERROCARRILES		GAS DEL ESTADO	
	Jan-Sep.87	Jan-Sep.88	Jan-Sep.87	Jan-Sep.88	Jan-Sep.87	Jan-Sep.88	Jan-Sep.87	Jan-Sep.88
SALES	8.059	9.990	2.251	2.185	729	730	2.599	2.442
INVESTMENTS	1.532	1.304	1.211	1.653	407	282	698	919
DEBT	19.660	24.267	2.445	2.339	5.185		10.029	10.864
PERSONNEL	33.936	34.800	45.963	46.657	98.208	97.300	9.274	9.660

In millions of Australes, except personnel  
Source : SIGEP

Chart 4

LATIN AMERICA - SOCIAL INDICATORS

	LIFE EXPECTANCY AT BIRTH(1985)	ADULT ILLITERACY (1985)	MOTHER MORTALITY RATE(1985)	% COVERAGE DRINKING WATER URBAN CENTERS	% COVERAGE SEWAGE SERVICES URBAN CENTERS	CHILD MORTALITY RATE(1986) per thousand
COSTA RICA	74	6.5		100	87	18
CHILE	71.5	3.5	55	97	77	18.7
ARGENTINA	70	4.5	85	72	66	33
URUGUAY	69	6.5	56	95	35	27
MEXICO	67	10	92	91	60	48
ECUADOR	65	18	220	73	72	64
BRAZIL	65	22.5	154	86	48	65
COLOMBIA	65	11.5	126	84	73	47
PERU	64	15.5	314	73	44	91
BOLIVIA	53	25.5	480	77		

SOURCE: EL MERCURIO

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