



# Sovereign Credit Outlook

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Corficolombiana Conference  
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**Fitch**Ratings

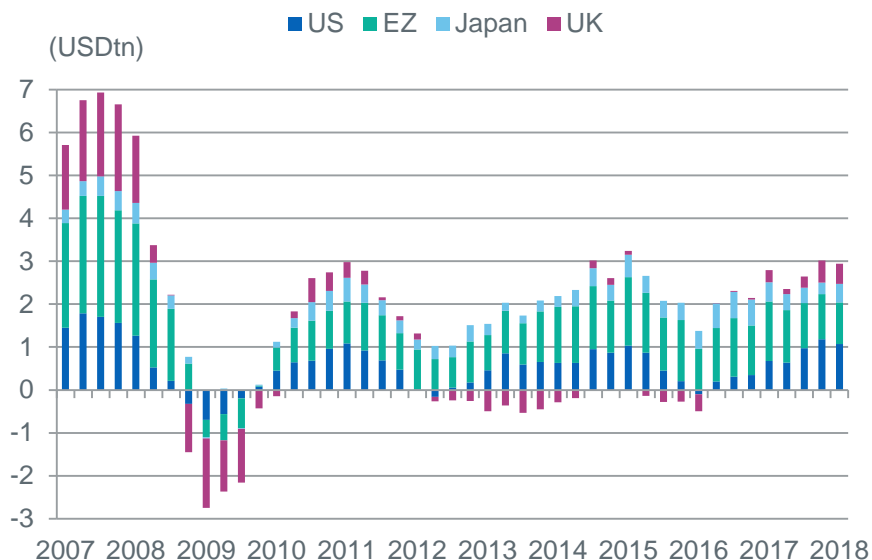


- Global Perspective
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- Oil Price Impact
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- Rating Sensitivities
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# Developed Market Capital Outflows – More Volatility to Come, Stronger Dollar Too

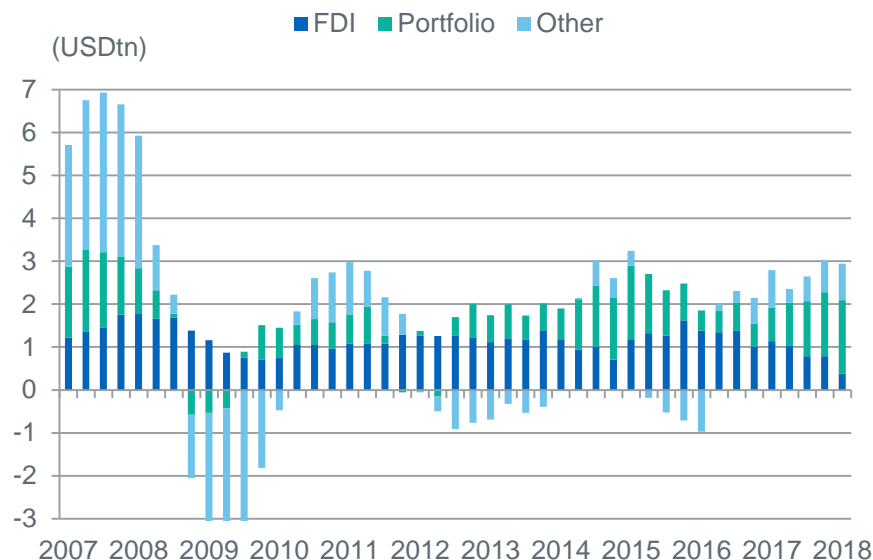


## Capital Outflows\* by Source Country (4-qtr sum)



- **UK** capital outflows have never recovered from the crisis
- **Eurozone** has had the largest outflows – current account surplus
- **US** outflows are now bigger than the Eurozone for first time
- **With stronger growth and higher rates, will US outflows fall?**

## Capital Outflows\* by Type (4-qtr sum)



- **“Other”** outflows (bank lending) never recovered from the crisis
- **FDI**, steady even during the crisis, is now in marked decline
- **Portfolio** outflows are the biggest capital outflow
- **Portfolio** flows can prove volatile

\*Resident investors' accumulations of external assets

Source: Datastream, Fitch



## Strong Dollar and Four EM Challenges

**Higher Debt Service in Local Currency Terms**

Lots of EM foreign-currency borrowing since 2007 and most EM external debt is dollar-denominated

**Lower Commodity Prices**

Usually, a strong dollar is correlated with lower commodity prices, although the relationship does not always hold

**Ambiguous Impact on Economic Growth**

Net trade is better, but investment spending is import-intensive

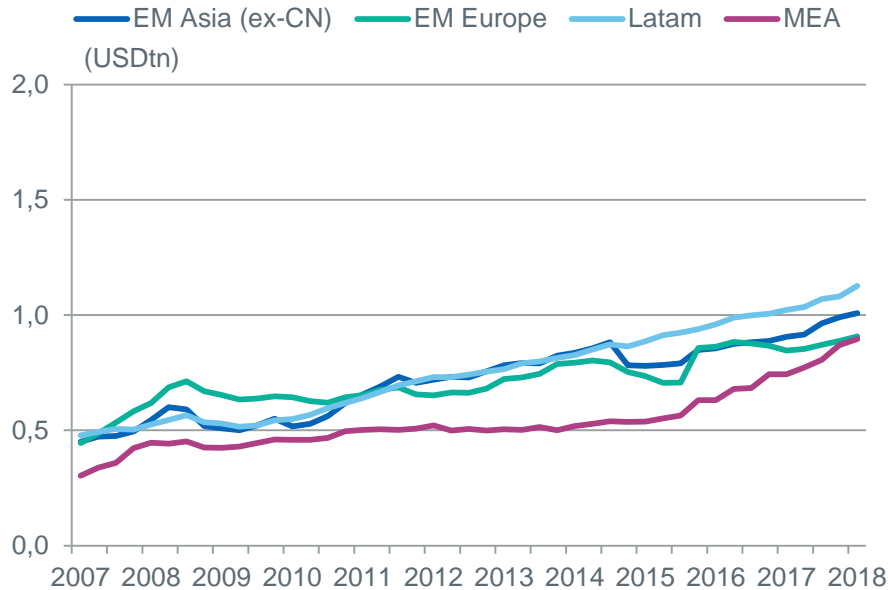
**Central Bank Reserves are Likely to Fall**

EM central banks resist currency depreciation, using FX reserves to do so

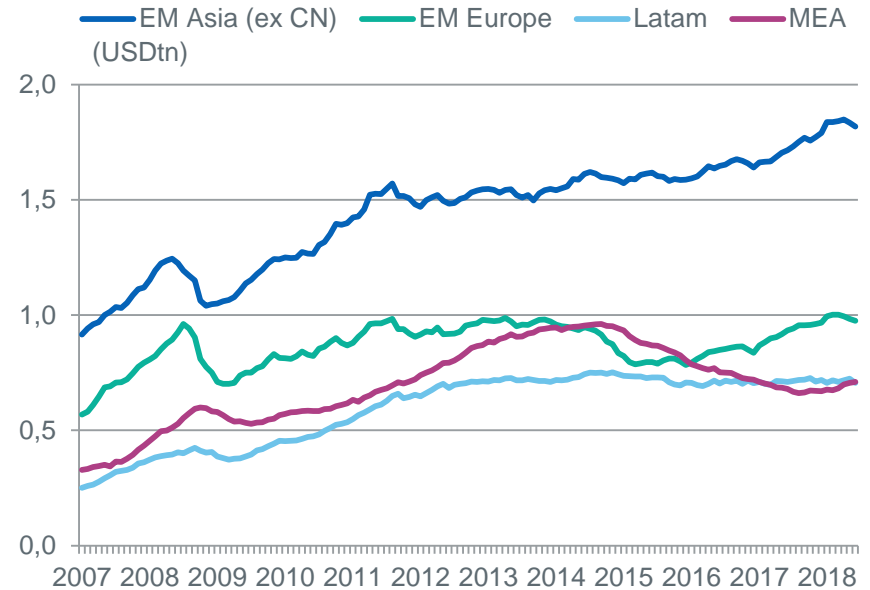
# Stronger Dollar – External Balance Sheet Stresses Most Evident in Latin America



## Non-Bank FX Borrowing (bank credit + securities) by EM Region



## Official FX Reserves by EM Region

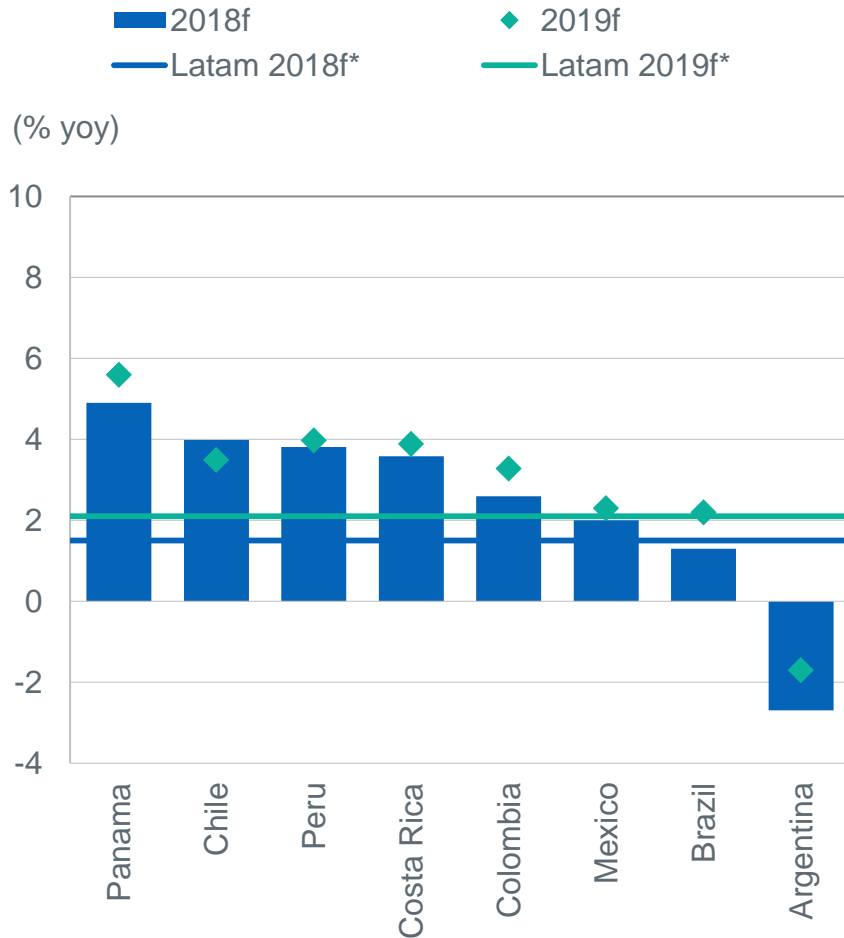


- **EM Asia (ex China):** FX Reserves are nearly twice FX debt
- **EM Europe:** FX Reserves increasing since 2015, and now exceed FX debt
- **Latin America:** FX Reserves flat since 2013; FX debt still growing and nearly twice FX Reserves
- **Middle East & Africa:** FX Reserves falling since late 2014 (recovering in 2018); FX debt accelerated since 2015, now exceed Reserves

# Regional Growth to Accelerate Moderately in 2019

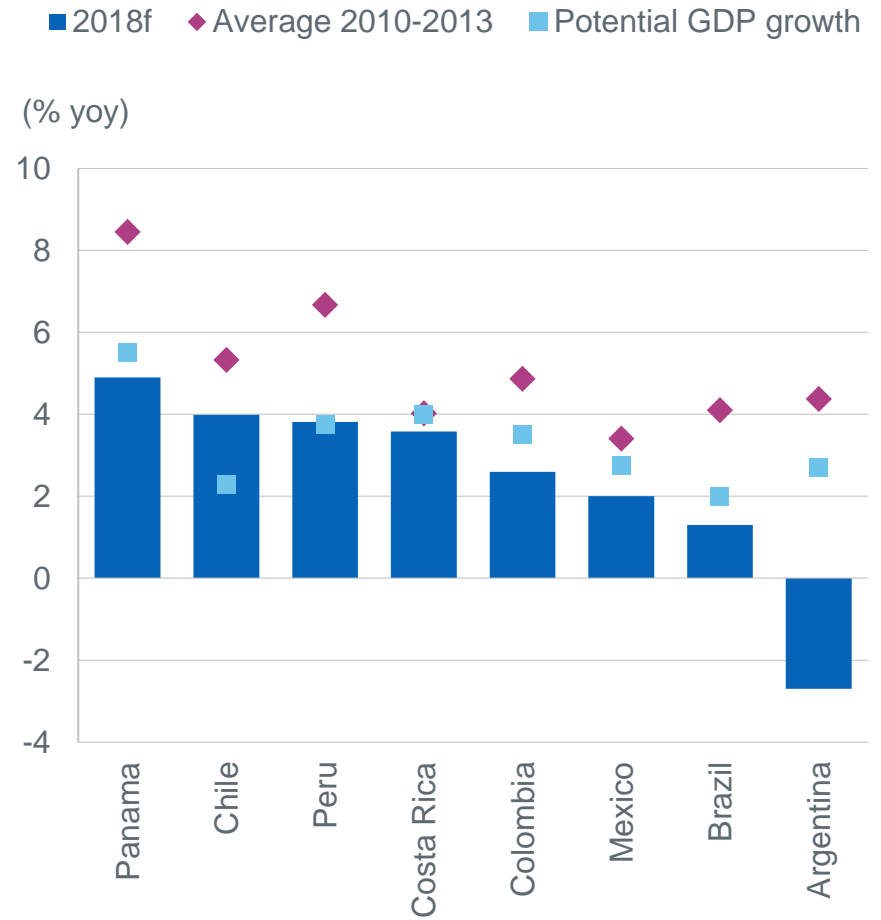


## Real GDP Growth



\*Excluding Venezuela  
 Source: Fitch

## Most Countries are Growing Below Potential

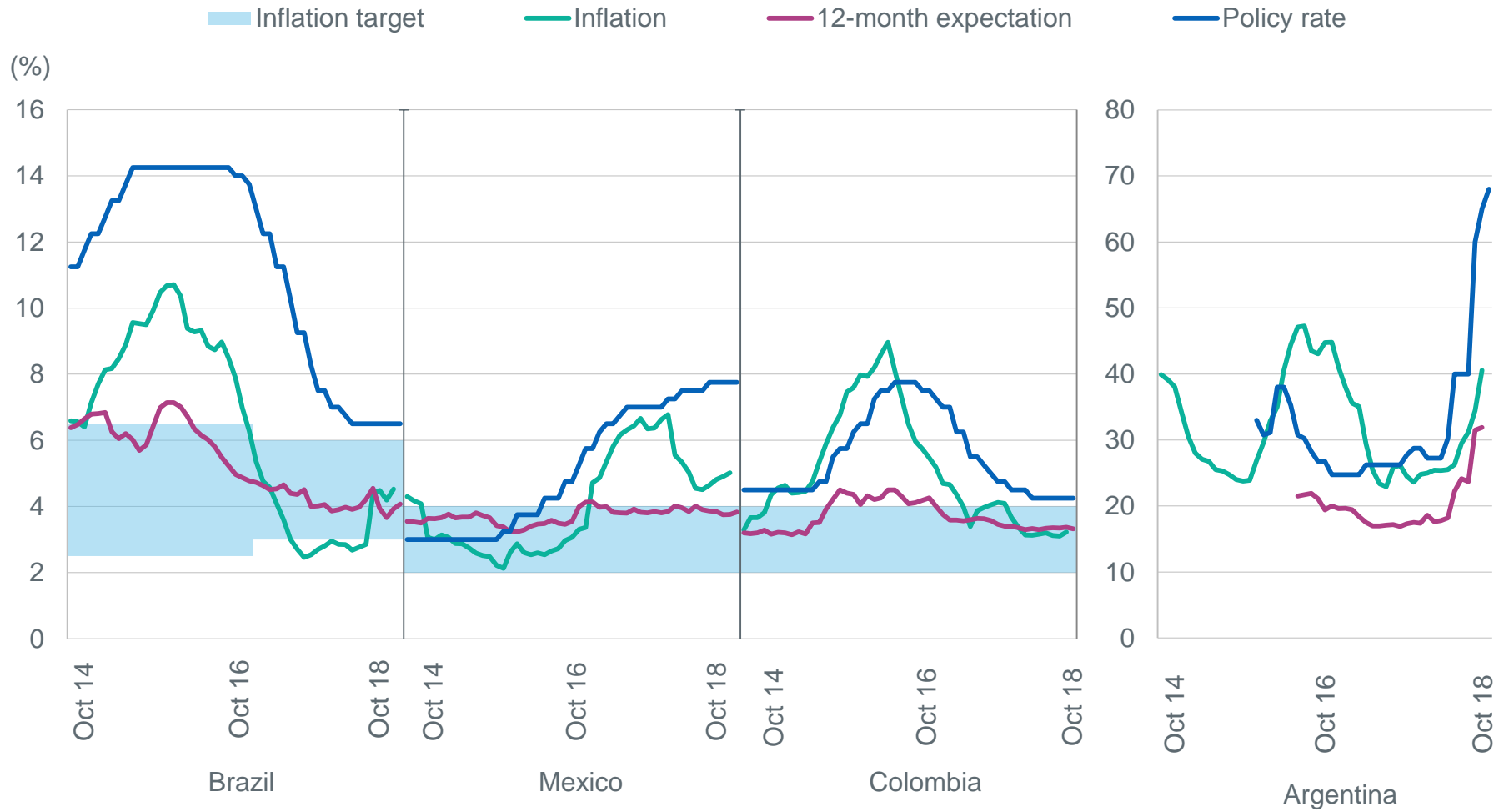


Source: Potential GDP growth from IMF, GDP growth from Fitch

# Moderate Inflation in 2018 With Some Exceptions



## Central Banks Contain Inflationary Pressures



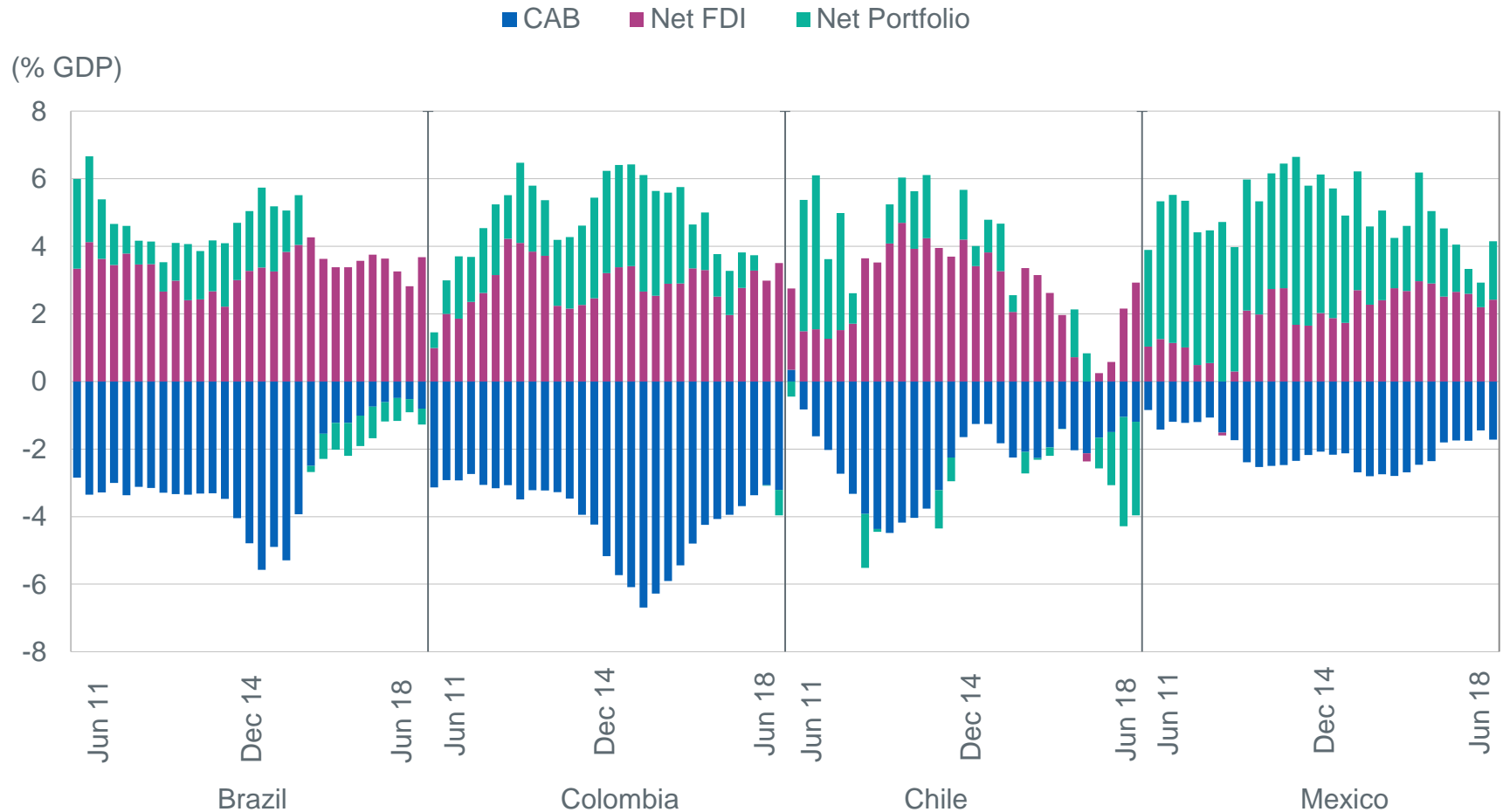
Source: National authorities, Fitch

# Supportive Balance of Payments



## Resilient FDI & Shrinking CAD

4Q Rolling Sum



Source: National authorities, Fitch





## Negative Rating Pressures

- 3:1 ratio of Negative to Positive Outlooks/Watches
- Tightening external financing conditions, lukewarm and uneven growth, and persistent fiscal challenges and political risks will continue into next year

## Negative Actions in 2018

- Ecuador to 'B-' from 'B', with Stable Outlook
- Nicaragua to 'B' from 'B+' (June 2018) and to 'B-' from 'B' (Nov 2018), with Negative Outlook
- Argentina Outlook to Negative from Positive
- Aruba Outlook to Negative from Stable
- Brazil to 'BB-' from 'BB', with Stable Outlook
- Costa Rica Outlook to Negative from Stable (on Rating Watch Negative)

## Positive Actions in 2018

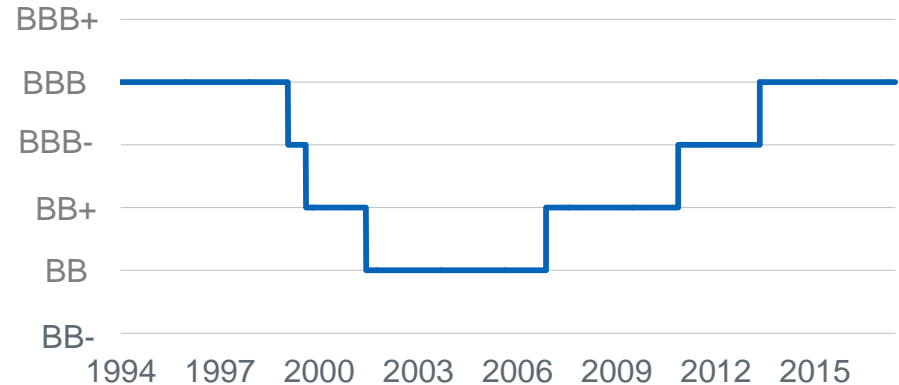
- Suriname Outlook to Stable from Negative
- Jamaica Outlook to Positive from Stable

Sovereign	LTFC	Outlook
Chile	A	Stable
Mexico	BBB+	Negative
Peru	BBB+	Stable
Colombia	BBB	Stable
Panama	BBB	Stable
Aruba	BBB-	Negative
Uruguay	BBB-	Negative
Costa Rica	BB	Negative (RWN)
Guatemala	BB	Stable
Paraguay	BB	Positive
Bolivia	BB-	Stable
Brazil	BB-	Stable
Dom. Republic	BB-	Stable
Argentina	B	Negative
Jamaica	B	Positive
Nicaragua	B-	Negative
Ecuador	B-	Stable
El Salvador	B-	Stable
Suriname	B-	Stable
Venezuela	RD	-



- Rating affirmed at 'BBB' with stable outlook in November 2018.
- Fitch expects broad macroeconomic continuity under the new administration.
- Expected to meet fiscal targets in 2018-2019 but with increased uncertainty.
- Tax reform seeks to reduce corporate tax rates, increase personal income taxes and broaden the VAT base.
- Fitch forecasts growth acceleration in 2019 to 3.3% driven by higher exports, supportive consumption and higher investment.
- General government debt largely stabilized at near 41% of GDP.

## Rating History



Source: Fitch Ratings

## Key Indicators

	2017	2018f	2019f
Real GDP growth (%)	1.8	2.6	3.3
Inflation (%)	4.3	3.8	3.3
Central government balance (% of GDP)	(3.6)	(3.0)	(2.5)
General government debt (% of GDP)*	40.3	41.2	40.8
Current account balance (% of GDP)	(3.4)	(3.2)	(3.2)
International reserves, incl. gold (USDbn)	47.1	48.7	50.0
Net external debt (% of CXR)	51.2	42.8	36.0

Source: Fitch

\*General government includes central government, provincial, regional and local governments, social security funds and extra-budgetary funds.



- Growth consolidating towards medium term potential of 3.5% after three years of underperformance (with average growth of 2.1% in 2016-18).
- Fitch forecasts 3.3% growth in 2019 (in line with the BBB median) and 3.5% in 2020 (up from 1.8% in 2017).
- Higher exports, supportive consumption and higher investment are expected to underpin higher growth.
- Infrastructure projects related to the 4G investment roll-out have witnessed several bottlenecks that have slowed their progress, representing downside risks to the outlook.
- Sustained lower oil prices could negatively impact growth outlook as well.

## Real GDP growth

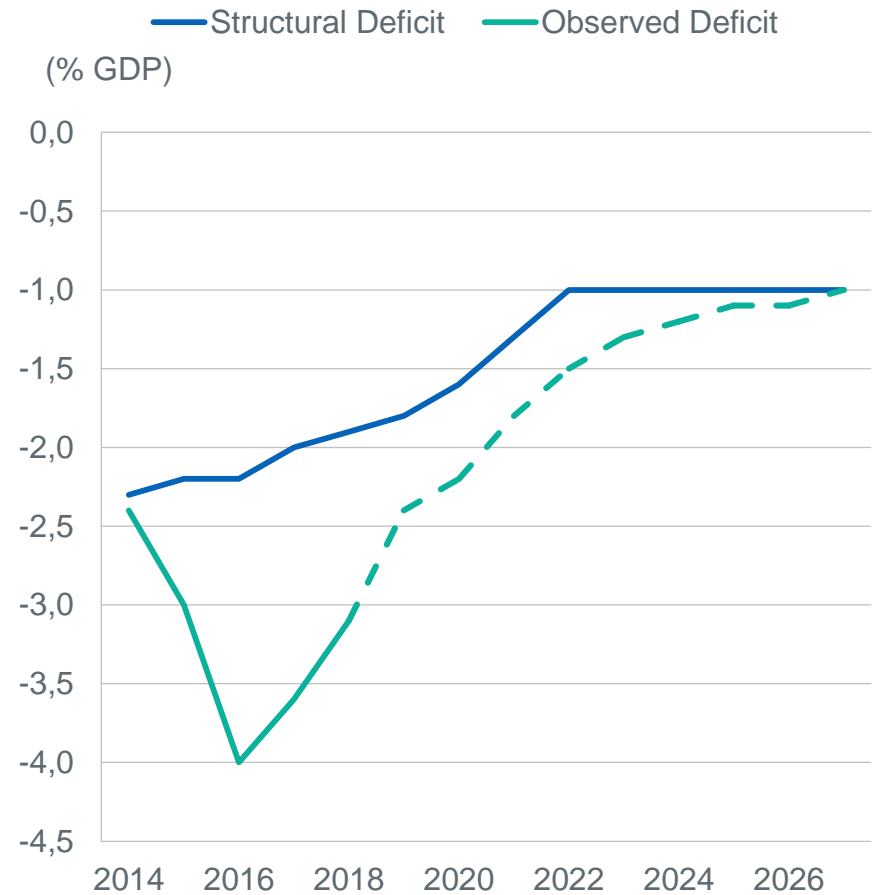


Source: Fitch



- In May 2018, Fiscal Council revised fiscal consolidation path by changing target date for convergence to 1% of GDP actual deficit by 2027 (originally 2022).
- Fitch expects government to meet its 3.1% of GDP central government deficit target in 2018, down from 3.6% in 2017 and 4% in 2016. The target for 2019 is 2.4% of GDP.
- Government spending is highly rigid. Generating net new revenues from proposed tax reform is key to achieving the target. Failing to pass reform would require sharp cuts in capital expenditure.
- Sustained fall in oil price represents further downside risk to meeting the fiscal target.

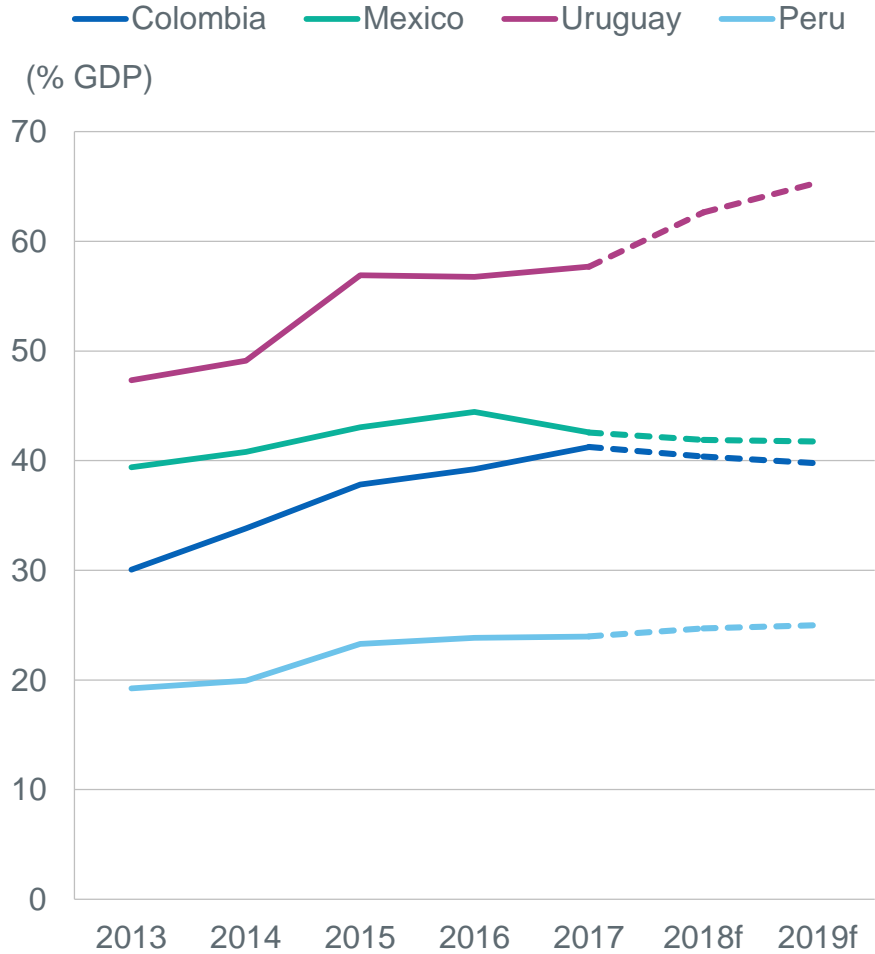
## Colombia's Fiscal Deficit



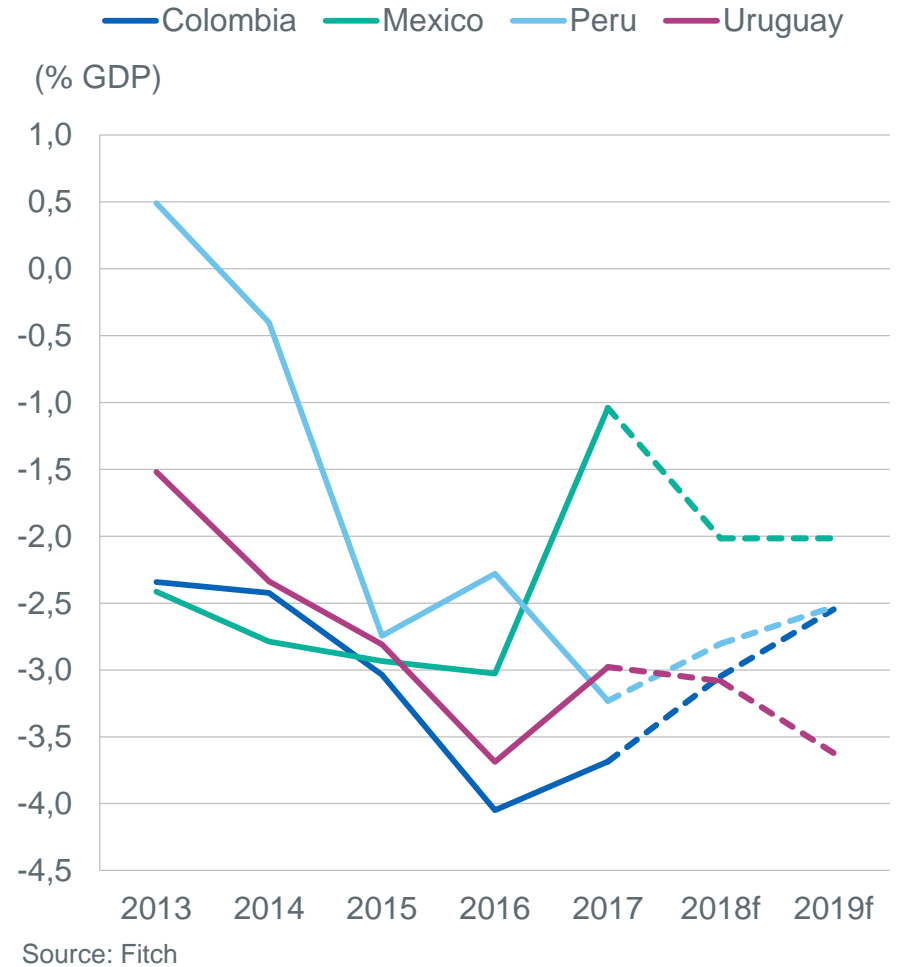
Source: Colombia's Fiscal Rule Consultant Committee and Ministry of Finance



## GG Debt



## Central Government Overall Balance





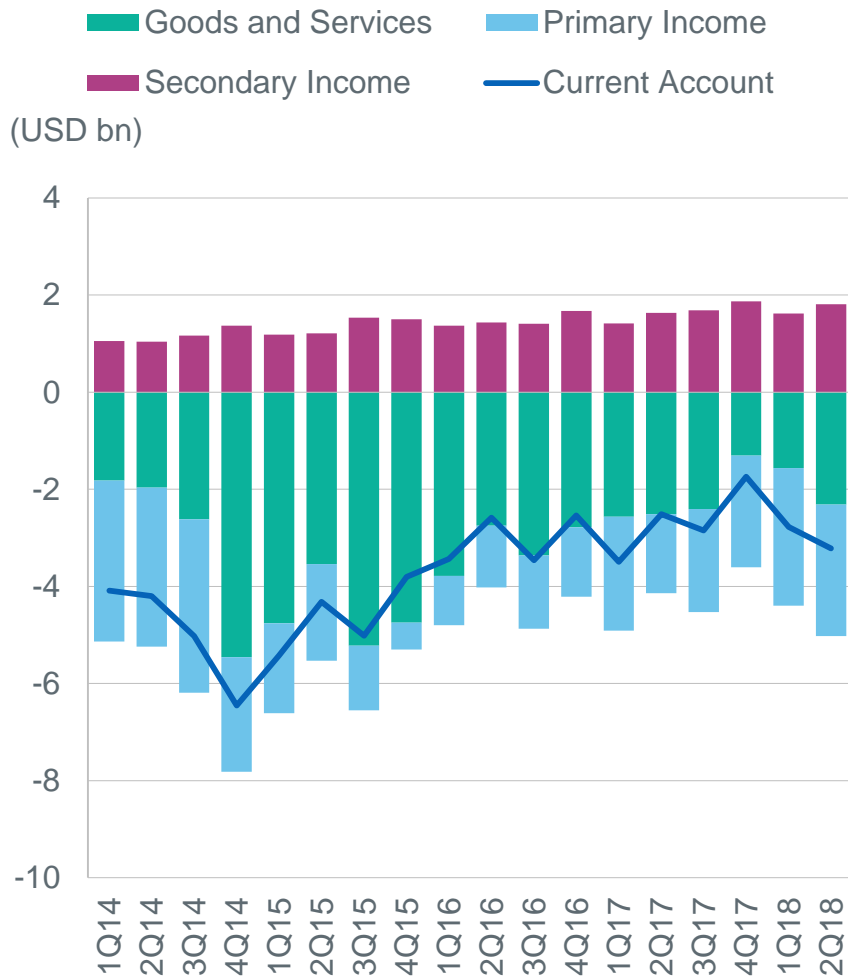
- The Duque administration submitted a comprehensive tax reform package that includes:
  - cutting the corporate income tax rate,
  - increasing personal income taxes,
  - broadening the VAT tax base.
- Prior tax reform efforts have been watered down in Congress. The current reform will likely be as well.
- Broadening VAT to basic food items has now been eliminated.

<b>Impact of Original Proposed Reform (% of GDP)</b>		
<b>Tax Measures</b>	<b>2019</b>	<b>2020</b>
Corporate Rate Cut and Incentives	0.0	-1.1
<b>VAT changes (net)</b>	<b>1.0</b>	<b>1.1</b>
Wealth tax	0.1	0.1
Personal Income Taxes	0.2	0.2
Net Impact of Tax Changes	1.3	0.3
<b>Other Measures</b>		
<b>Lower Spending</b>	<b>0.1</b>	<b>0.1</b>
Tax Administration	0.1	0.5
Privatization	0.2	0.3

# Falling External Imbalances

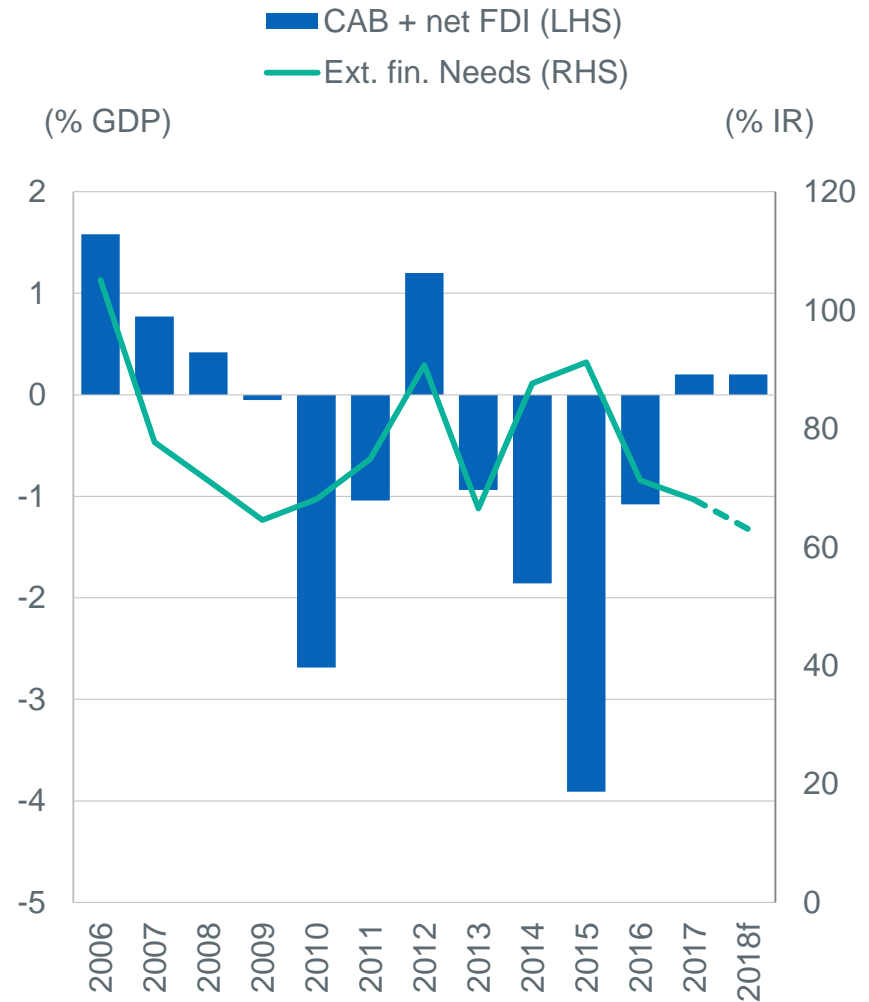


## Gradual CAD Adjustment



Source: Banrep, Fitch

## External Financing Needs & FDI

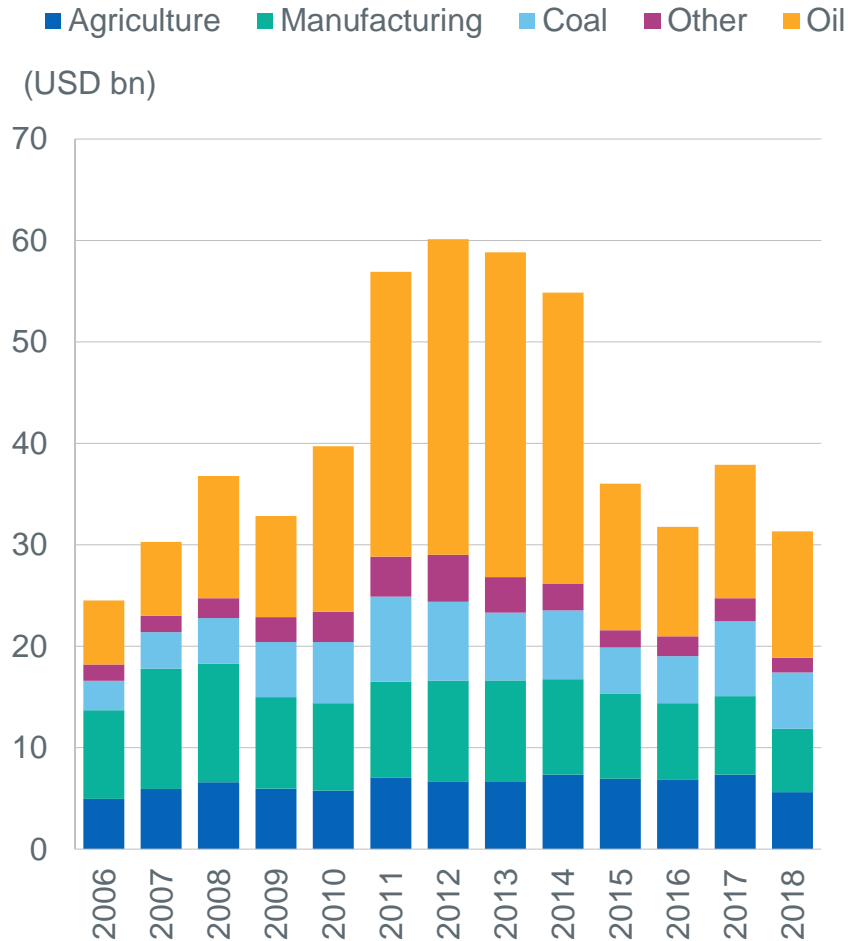


Source: Minhacienda, Banrep, Fitch

# Oil prices recovering but still volatile



## Exports



Source: DANE, Fitch, \*2018 through September

## ICE Brent Crude



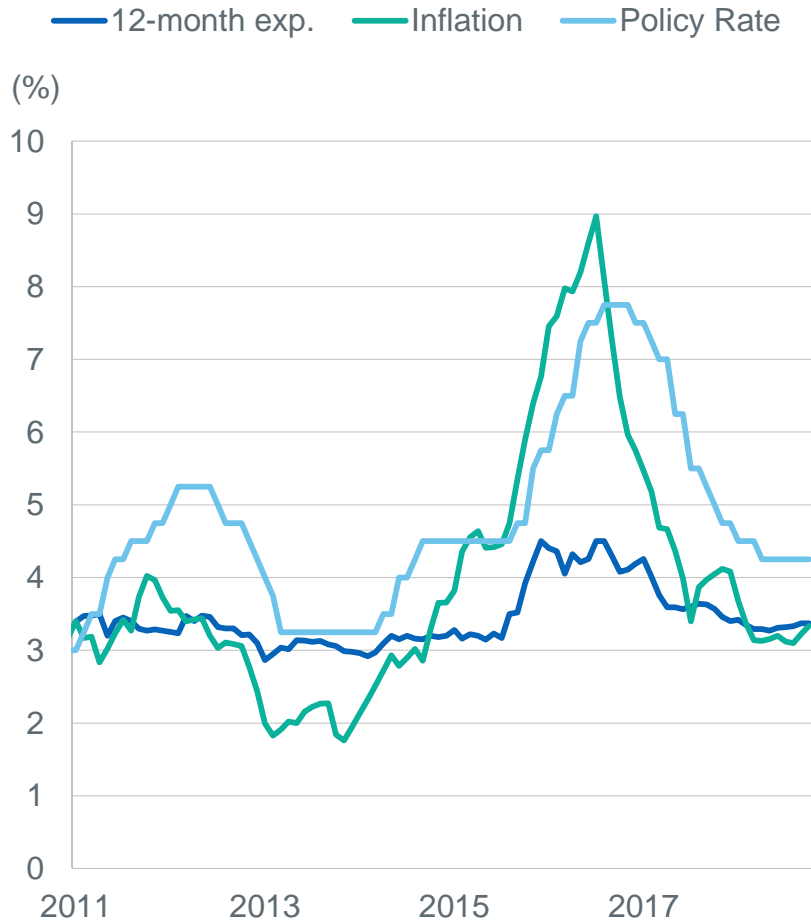
Source: Bloomberg, through November 20, 2018



# Credible Inflation Targeting Regime & Flexible FX



## Response to High Inflation



Source: Banrep, Fitch

## TOT Shock



Source: Banrep, Bloomberg



SRM output	Qualitative overlay	FC IDR
	<b>Factor</b>	<b>Notch adjustment</b>
	Macro	+1
	<ul style="list-style-type: none"> <li>• Long track record of prudent and consistent macroeconomic policies</li> </ul>	
<b>BBB-</b>	Public finances	0
	External finances	0
	Structural features	0
	<b>Total</b>	<b>+1</b>

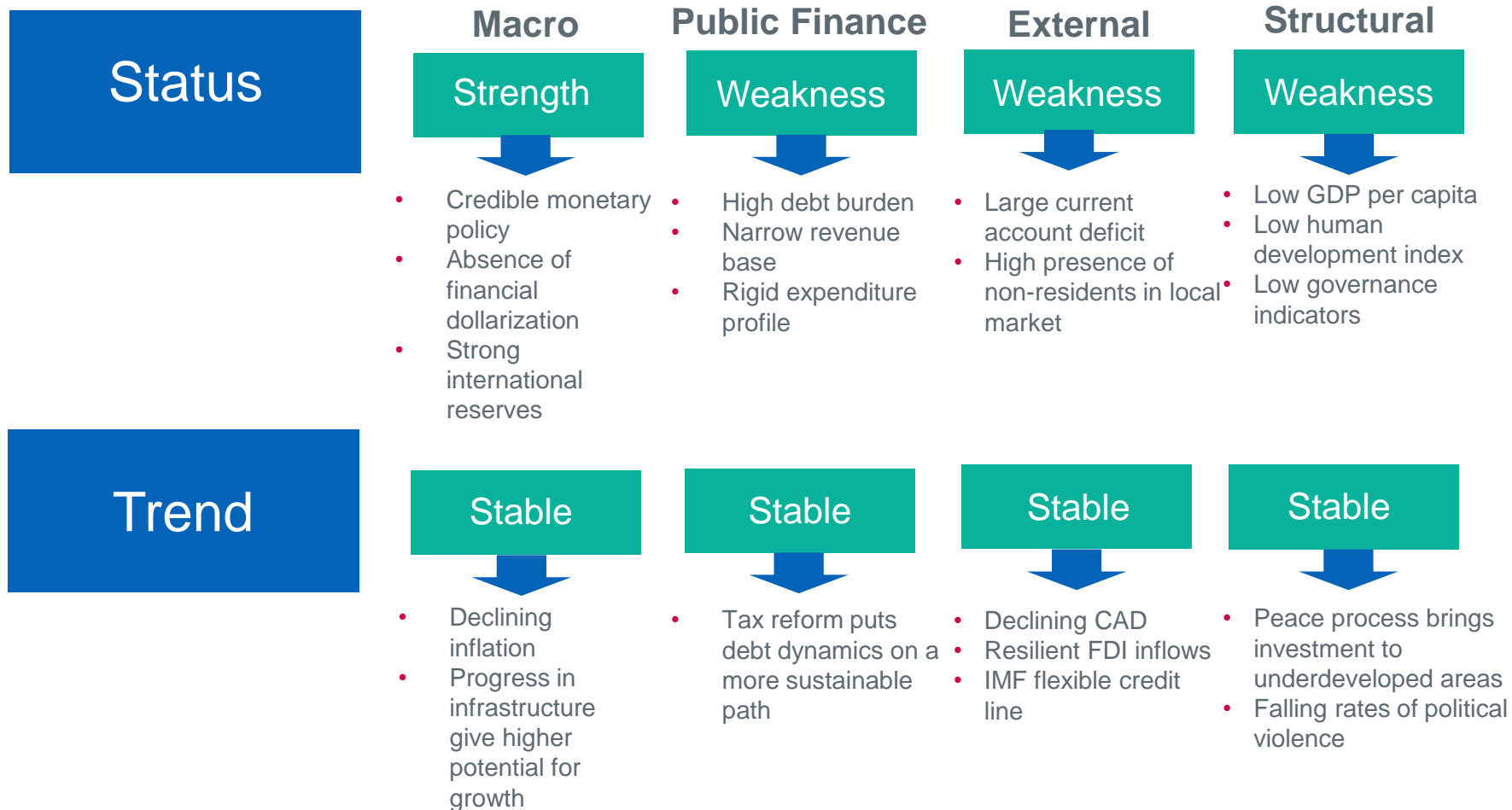
**BBB**

## Negative Sensitivities

- ✗ Weaker fiscal out-turns that lead to increasing debt and interest burdens or affect the credibility of the long-term fiscal consolidation path
- ✗ Persistence of low growth, undermining both fiscal performance and support for prudent macroeconomics policies
- ✗ Re-emergence of large external imbalances that lead to continued increase in the external debt burden

## Positive Sensitivities

- ✓ Fiscal consolidation consistent with an improved trajectory for public debt dynamics
- ✓ Higher growth prospects that supports improved debt dynamics and improves Colombia's income gap with higher-rated sovereigns
- ✓ Improved governance indicators reflecting a more stable security environment



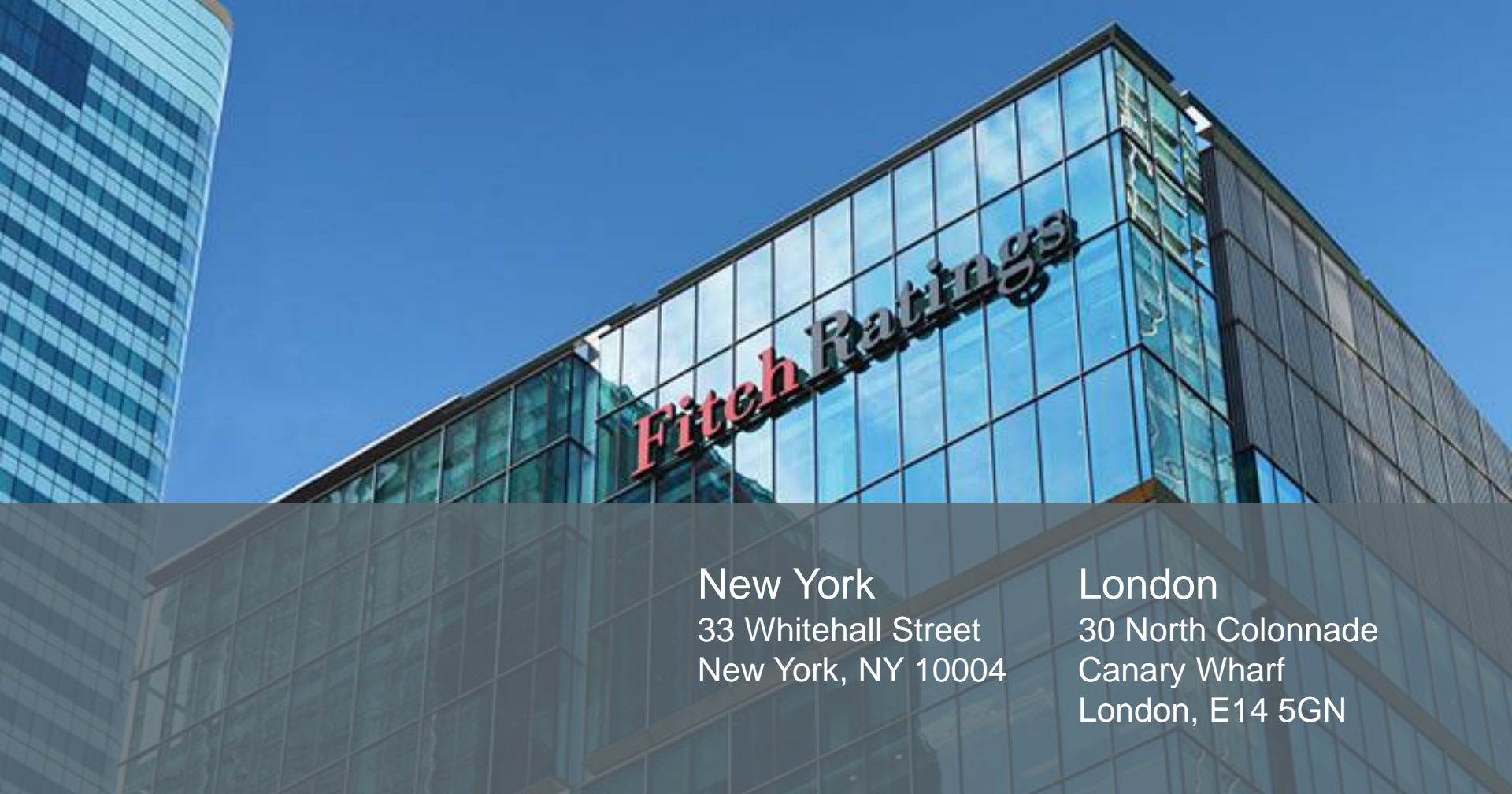
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