



## Argentina - Position for the upturn

- Argentina's FX and fixed income markets have had a relatively muted response to the recent upside surprises in both domestic activity and better-than-expected primary results / electoral polls since the PASO. In this report we review recent macro developments and outlook in Argentina, and discuss how to position for this stage in the cycle.
- In our view, this muted response is natural at this stage of the cycle and the policy priorities of this administration. The need to fund widening current account deficits and anchor disinflation requires tighter monetary policy for longer, which weighs on fixed income.
- Although this mix still supports carry, an overvalued currency requires more active management of USD shorts.
- The choice of instrument in the short-end of local markets is important given wide dispersion in valuations. The macro dynamics favors floating rates over fixed rate instruments given both supply and monetary policy risks
- At the mid-section of the curve (up to 22s), the flat forward curve implied by the BOTEs and the adverse carry/roll and skew underscore our preference for floaters. BOPOM 20s offer superior liquidity and remain a popular choice in positioning for carry, but valuation looks very rich according to our analysis.
- A back-loaded fiscal adjustment, which would pick up after presidential elections in 2019 (assuming the incumbent is re-elected) is consistent with a back-loaded real depreciation – not appreciation – in longer tenors. This argues for a preference of external bonds for duration exposure.
- While valuation in credit looks tight vs. its current credit standing, there is still scope for further tightening due to a). Potential multiple-notch credit ascension if politics stay on track; b). The flattening of spread / quality curve in EM credit markets under the long-term constructive external backdrop of continued inflows; and c). Alternative opportunities (with spread pickup) offered by EUR bonds, select local law USD bonds, and select provincial bonds.
- In the external markets, EUR denominated bonds are more attractive than USD counterparts in the belly of the curve; USD Pars remain very attractive at the long end. Among Argentina's provincial bonds, we retain a preference for 7-year bonds from Cordoba (7.45% '24s) and Salta (9.125% '24s).
- While we retain our long-held constructive view on GDP Warrants on our belief that the government will eventually go with the market-friendly resolution on the choice of base case GDP (likely via a buyback), we would only look to buy on dips given the uncertainty in growth (near borderline) after the recent outperformance.