Capital markets

Creditors to Argentina's provinces fight to avoid painful restructurings

Lenders form committee to push for better deals than those secured at national level

Argentina's provinces are trapped between creditors and the national government, which wants to stabilise the economy and protect foreign exchange reserves © FT montage; Getty Images

Benedict Mander in Buenos Aires 18 HOURS AGO

Holders of Argentina's $15bn in provincial debt are growing nervous that pressure from the national government is behind "arbitrary" demands for debt restructurings, threatening investors with big losses.

After the successful restructuring of $65bn in sovereign debt with foreign creditors in August, Argentina's leftist government is now locked in talks with the IMF to renegotiate the repayment of $44bn lent since a currency crisis in 2018.

Foreign creditors to Argentina's provinces are next in line. They say the national government is strong-arming provincial authorities into demanding punitive debt restructurings affecting most of the market, forcing losses, or "haircuts", on them.

"The idea that every province, no matter its circumstances, should default and follow the same approach as the sovereign is deeply cynical. As creditors, we are not going to entertain such a framework, and the provinces recognise that," said Daniel Freifeld, founder of Callaway Capital Management, which owns Argentine provincial bonds.

Mr Freifeld added that "many provinces are trapped" between creditors and the national government, pointing out that in the meantime, provinces are putting off potential investment and accumulating unpaid interest bills.

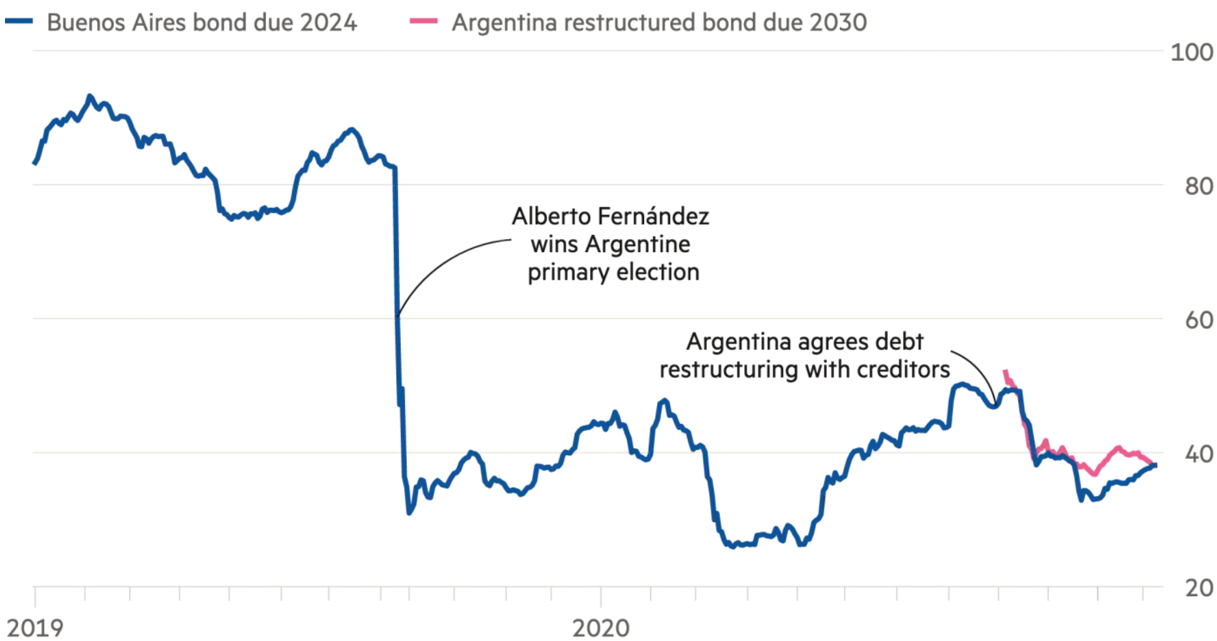
Callaway and other creditors have set up the first committee for Argentina's provincial bondholders, mirroring efforts at the national level. The committee, which includes bondholders owning a total of about $3bn of provincial debt, argues that the negotiations should be based on what provinces are able to pay — and not on what the national government would like them to pay.

Investors think the government's intransigence comes from a desire to protect the country's dwindling foreign exchange reserves, seen as a bulwark against currency weakness. The official peso rate has already lost a quarter of its dollar value this year, after the coronavirus crisis exacerbated a three-year recession.

"It would be penny-wise but pound-foolish of them to insist on arbitrary and artificial haircuts when they have much bigger fish to fry," said a senior executive at a hedge fund holding provincial debt, insisting that Argentina would struggle to attract capital to support its recovery if some provinces continue to demand what creditors regard as unreasonable terms of repayment.

Argentine and Buenos Aires debts remain deep in distress

Price (cents on the dollar)



Source: Bloomberg

Litigation "can't be ruled out," warned the investor. "Our preference is to avoid it, as it's harmful to everybody, and wasteful — but creditors don't have indefinite patience."

"There is no real argument for the provinces to seek out the same type of debt relief as the sovereign," agreed Walter Stoeppelwerth, chief investment officer at Portfolio Personal Inversiones, an investment firm in Buenos Aires.

While pre-restructuring debt servicing costs for the national government were more than 20 per cent of economic output, for most provinces that ratio is in single digits, Mr Stoeppelwerth added. Leverage is also lower at the provincial level.

Some provinces run by politicians independent of the national government have reached deals with their creditors, notably Mendoza and Neuquén, but others have preferred to play hardball.

The biggest battle is with the largest, the impoverished province of Buenos Aires that surrounds the capital city. With bonds in default since May worth more than $7bn, it not only accounts for about half of the provincial debt burden, but its governor, the former national economy minister Axel Kicillof, is a powerful figure in the ruling coalition. The province has proposed a debt restructuring that would leave investors with an estimated recovery value of 46 cents on the dollar, while bondholders are pushing for 85 cents.

The stand-off has knocked the province's 2024 bond deeper into distressed territory. It is hovering below 40 cents on the dollar, having traded at 50 cents in August.

Marcelo Etchebarne, country manager in Argentina for law firm DLA Piper, which represents several provinces in the debt negotiations, argues that given the "catastrophic" economic situation in Argentina — which he said is as bad as the country's 2001 financial crash — many investors are currently being offered "a very sweet deal in light of the circumstances".

He warned that in a worst-case scenario, provinces could declare bankruptcy, as Detroit did in 2013. "Ask Detroit's creditors how it went for them," he said, pointing out that unsecured creditors received less than 20 cents on the dollar.

"At the end of the day it's about the ability to pay, but not to pay debt only," added Mr Etchebarne. "Before paying debt, provinces have to pay judges, teachers, the police."

Despite the rising tension, some analysts think that many provinces will end up reaching a negotiated deal with their creditors by the end of the first quarter of next year. Such prospects could be improved if Argentina secures a relatively quick deal with the IMF — especially if that leads to a rally in Argentina's sovereign bonds.

One sovereign bond due to mature in 2030 has fallen below 40 cents on the dollar, despite the debt restructuring. It traded as high as 52 cents in September.

The provincial debt reckoning is seen as crucial to the country moving forward. "Argentina is not going to emerge from its current economic morass until this issue with the provinces is resolved," Mr Freifeld said.

Additional reporting by Colby Smith