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Bonds: International markets support Venezuelan spree

by Jason Mitchell

Venezuela is issuing more bonds in the international markets than the rest of Latin America combined, so that it is in a position to increase government expenditure in the run-up to presidential elections next year.

On October 11, the republic issued a new bond for $3 billion, maturing in 2026 and with a coupon of 11.75%. Unlike previous offerings, the bond was not issued at par but with a discount of 5%.

This year the sovereign and PDVSA, the state-owned oil company, have in total issued more than $15.2 billion, including private placements and the latest offering, according to Barclays Capital. The republic issued $7.2 billion and the oil company $8 billion. This surpasses all of the issuance from the rest of the region combined. Originally, Barclays Capital had forecast total Venezuelan and PDVSA issuance at $12 billion this year.

"This transaction confirms that the government is planning a big increase in public expenditures in the next 12 months ahead of the presidential elections," says Alejandro Arreaza, an emerging markets research analyst at Barclays Capital. "Already we are seeing a huge fiscal expansion to stimulate the economy. Although Venezuela grew faster between 2005 and 2008 than we are estimating for next year, the main problem today is that there has been a lack of investment in the country since that time. This has created a lot of bottlenecks and it is not clear that the economy can absorb the stimulus well. This could well lead to even higher inflation and imports."

Barclays Capital is forecasting economic growth at 4.3% this year and at around 4% next year. Inflation is expected to be around 22.9% this year, according to Morgan Stanley.

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Victor Rodriguez, LatamAlternatives

Arreaza says that Venezuela probably issued the latest bond internationally because it is quicker than issuing in the domestic market. Venezuela has an Indebtedness Law that prevents the sovereign from borrowing more than Bs99 billion ($23 billion) this year. It has already borrowed the equivalent of Bs71 billion. From the remaining Bs28 it has agreed to borrow Bs9 billion from multilateral agencies, meaning the government has only Bs 19 billion available to issue for the rest of the year.

Barclays Capital expects most of that to be issued in the international markets. However, the Indebtedness Law does not apply to PDVSA, which is closely linked to the state. Many experts say it is difficult to distinguish the finances of the oil company from those of the republic. PDVSA is expected to issue in large amounts again next year.

According to LatamAlternatives, a hedge fund consultancy based in Florida, total Venezuelan debt stands at $113 billion and annual debt service payments are $8 billion.

"Venezuela should still have the capacity to pay back the debt until 2012," says Victor Rodriguez, chief executive at LatamAlternatives. "The paper is very liquid, with excellent returns. Investors are prepared to back Venezuela because it has so much oil. But there is little institutional investor allocation towards the country and that could create problems."

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