Juan Manuel Pazos
Chief Economist
jmpazos@tpcgco.com
+54 11 4898 6606

Santiago Resico
LATAM Strategist
sresico@tpcgco.com
+54 11 4898 6615

LATAM Strategy – Ecuador

May 5, 2023

ESG throws the ECUA curve a lifeline

The administration profited from the battered ECUA space with the repurchase.

Credit Suisse finally repurchased USD1.6bn in ECUA bonds, with the maneuver being linked to a larger liability management operation carried on by the Ecuadoran government.

Credit Suisse finally repurchased USD1.6bn in ECUA bonds, with the maneuver being linked to a larger liability management operation carried on by the Ecuadoran government. The purchasing mechanism presented by Credit Suisse relied on a modified Dutch Auction and applies to all the bonds on the ECUA curve, save for the 2030 PDI, which was excluded from the buyback. The price paid for each bond finally was 53.25c for the 2030s, 38.5c for the 2035s, and 35.5 for the 2040s, all at the upper limit of the suggested price range for each security. The final amount repurchased totaled USD1.6bn, with the buyback centered around 35s, of which Credit Suisse bought USD1bn in notional. The second most purchased bonds were the 40s, with the total face value bought amounting to USD420mn, while the amount for 30s stood at USD200mn. In cash, the operation amounted to USD642mn, roughly 150mn short of the proposed. Accrued interest for the repurchased bonds amounted to 5mnfor the 30s, USD11mn for the 35s, and 2mn for the 40s, putting the total amount of the operation at USD660mn, roughly USD140mn short of the USD800mn which was initially envisaged. Even if the offer came from a private party, the administration already issued a statement relating this operation to a broader liability management deal, which was announced late in 2022. The administration is expected to issue an USD800mn blue bond, to pay Credit Suisse for the repurchased bonds, and to later use the savings resulting from the buyback to fund sustainability projects in the Galapagos islands. In addition to the repurchase operation, the blue bond will count with an IDB guarantee of USD85mn. The new issuance is planned to have an annual financing cost of around 7%, nearly one-third of the average current yield of the ECUA curve.

Figure 1: The amount of bonds repurchased totalled USD1.6bn

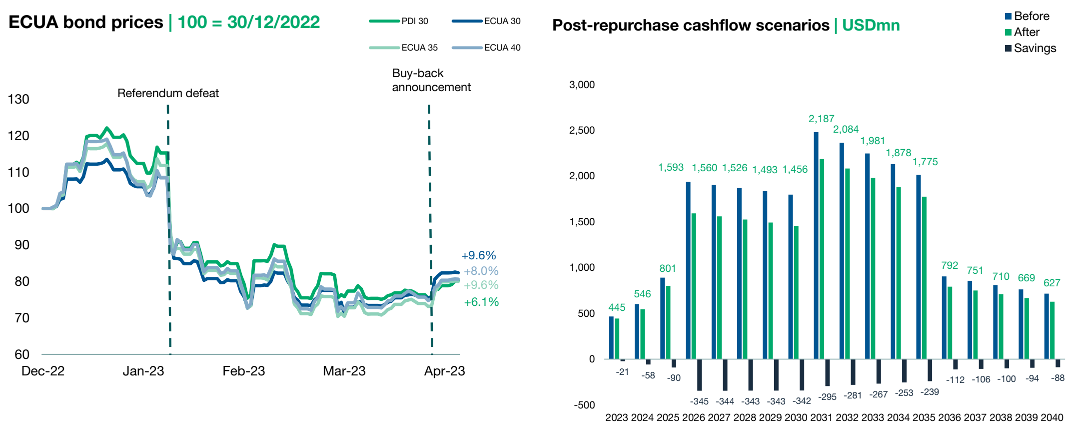
	ECUA30			ECUA35			ECUA40			Total		
Possible buy-back scenarios	in USDmn	Nominal value	As % of Out.	in USDmn	Nominal value	As % of Out.	in USDmn	Nominal value	As % of Out.	in USDmn	Nominal value	As % of Out.
ECUA30 centered	800	1502	40.6%	0	0	0%	0	0	0%	800	1502	10%
ECUA35 centered	0	0	0.0%	800	2078	25%	0	0	0%	800	2078	13%
ECUA40 centered	0	0	0.0%	0	0	0%	800	2254	66%	800	2254	14%
33% of each	267	501	13.5%	267	693	8%	267	751	22%	800	1945	12%
50/50 30's and 35's	400	751	20.3%	400	1039	12%	0	0	0%	800	1790	12%
50% in 30s 40% in 35s 10% in 40s	400	751	20.3%	320	831	10%	80	225	7%	800	1808	12%
Actual	108	202	5.5%	385	1000	12%	149	420	12%	642	1623	10%

Source: TPCG Research based on TPCG Trading Desk

The operation pushed the ECUA curve to timidly rally, reverting the trend exhibited since the start of the year, as the space bled profusely since the referendum's defeat.

The operation pushed the ECUA curve to timidly rally, reverting the trend exhibited since the start of the year, as the space bled profusely since the referendum's defeat. Taking a look at valuations, ECUA bonds started the year very strongly, as both macro fundamentals and politics seemed to be aligning. Up until the referendum, the space had gained ground significantly, rallying close to its climax, as the final steps for impeachment against Mr. Lasso near. Since the electoral defeat in February, which marked the administration's inability to bypass the Assembly, the space continued to bleed, with bond prices dropping by nearly -18.8% on average. However, the buyback announcement triggered a slight rebound, with the bonds having recovered around 8% price-wise.

Figure 2: The timid rebound of the space is consistent with the light short term impact of the repurchase.



Source: TPCG Research based on Finance Ministry and TPCG Trading Desk

While the liability management operation does decompress Ecuador's payment profile, its effects in the short run are relatively meager, with the bulk of the savings coming beyond 2025.

While the liability management operation does decompress Ecuador's payment profile, its effects in the short run are relatively meager, with the bulk of the savings coming beyond 2025. Taking a look at how the maneuver affected Ecuador's payment profile, we note that it should generate around USD2.7bn in savings up to 2040, with USD1.6bn coming from the slashed principal payments, and USD1.1bn from the reduction in interest cost. Therefore, the operation can be labeled as a success for the administration, even if it will not be able to profit from it, as most of the savings take place beyond the current tenure. In fact, savings up to 2025 amount only to USD169mn over three years. When the first bonds start to sink in 2026, then the savings become more sizable, totaling nearly 880mn by 2030. Still, the benefits of the buyback are very lopsided, as most (nearly 1.9bn) will be seen beyond 2030. So even if the deal does provide a substantial relief to Ecuador's debt profile, it does not do it in the short, or even medium term.

For comparison, we designed several scenarios to see how the distribution of the 800mn in the different bond series could affect Ecuador's debt profile.

For comparison, we designed several scenarios to see how the distribution of the 800mn in the different bond series could affect Ecuador's debt profile. From a maturity standpoint, the strategy that would have provided a shorter-term relief would have been concentrating all the firepower in the 2030 bond, as it starts to sink in 2026. However, from a price standpoint, the strategy that would have maximized savings in USD would have been to repurchase as much of the 40s as possible. Using the price finally paid in the operation we find the administration could have saved up to USD4.3bn (USD2.2bn in principal payments, USD2.1bn in interest payments) if it had used the entirety of the 800mn in repurchasing 2040 bonds. Instead, if it had used all its cash to buy back the 2030s, the result would have been as significant, as savings would have been halved to USD2bn, mostly from principal payments (1.5bn). Focusing on the 35s would have saved the administration nearly USD3.4bn, being an intermediate scenario in between the ones described above. We also designed several mixed scenarios, including one where the available cash was divided equally between the three bonds, one where it was split between the 30s and 35s, and a final one that modeled a front-loaded repurchase, with all offering weaker total savings than buying 2040's outright in the long run, albeit surpassing the savings of the directional purchases of the 2035's and 2040's up to 2030. The administration finally opted for a balanced strategy, focusing on the intermediate maturity, which is also the one with the largest outstanding principal, trying to smooth principal payments over time, while also using some resources to repurchase part of the 30s and 40s. This is consistent with the fact that for all our scenarios, savings before 2025 ranged between USD200mn and USD250mn.

Figure 3: The buyback could yield up to USD2.7bn in savings

	Up to 2025			Up to 2030			Total		
	Ppal Savings	Interest Savings	Total Savings	Ppal Savings	Interest Savings	Total Savings	Ppal Savings	Interest Savings	Total Savings
30' Intensive	0	235	235	1,502	520	2,023	1,502	520	2,023
35' Intensive	0	213	213	0	930	930	2,078	1,324	3,402
40' Intensive	0	186	186	0	860	860	2,254	2,065	4,318
33/33/33	0	211	211	501	770	1,271	1,945	1,303	3,248
30's & 35's	0	224	224	751	725	1,476	1,790	922	2,712
50/40/10	0	221	221	751	718	1,469	1,808	996	2,804
Actual	0	169	169	202	678	880	1,623	1,092	2,715

Source: TPCG Research based on Finance Ministry and TPCG Trading Desk

Even if the operation will provide some relief to public finances, its lack of immediate effect prevents it from nudging Mr. Lasso's impeachment from the spotlight.

Even if the operation will provide some relief to public finances, its lack of immediate effect prevents it from nudging Mr. Lasso's impeachment from the spotlight. The timing to perform the operation could not have been better, as the administration waited for bond prices to be near lows before announcing the repurchase. This should allow it to profit largely from the buyback, as with very low parities, thecash was able to clear a sizable chunk of Ecuador's external payments. However, as commented above, the measure will yield practically no short-term benefits, with the brunt of the savings coming beyond the current tenure, starting in 2026. Furthermore, most of the savings would come beyond 2030, especially as the repurchase is not centered around the 30s. Therefore, it is difficult to envisage the repurchase effect outweighing the strong political instability in the price action, especially as the impeachment against Mr. Lasso reaches critical mass. Currently, the Control Commission in the Assembly is preparing the report recommending (or not) the impeachment attempt. Said commission has until the 6th of May to do so. But before the report can go to the General Assembly, it must be approved by the members of the commission, where voting patterns tend to be somewhat irregular. Technically, the administration has the majority in the commission, initially formed by three members from Mr. Lasso's bloc, three correists, one member of the PSC and two independent members, the president of the commission, Mr. Villavicencio, and Mr. Segovia, who is an ex-Pachakutik member. Mr. Villavicencio has usually favored Mr. Lasso, so the one to tilt the balance to either side generally is Mr. Segovia, who in recent sessions has sided mostly with the bloc in favor of the impeachment, signaling that it is likely the opposition will manage to form a majority and pass the report through the commission into the Assembly.

The political situation has evolved slightly to the administration's satisfaction in the last weeks, as it has been able to play the members of the opposition against each other. This, however, by any means implies Mr. Lasso is out of the woods yet.

The political situation has evolved slightly to the administration's satisfaction in the last weeks, as it has been able to play the members of the opposition against each other. This, however, by any means implies Mr. Lasso is out of the woods yet. Inside the bloc promoting the president's impeachment, several conflicts of interest between factions exist. Correism pushed for Mr. Lasso to call for the Muerte Cruzada, as with a solid election in February, the party fancied its chances to win the new electoral bout and secure a new majority in the Assembly. However, this is not functional for the PSC, which prefers the impeachment to take place and Mr. Borrero to assume the presidency until the end of Mr. Lasso's tenure. This would allow the party to recover from the battering it suffered in the elections early this year, losing both Guayaquil and the Guayas province. This is also true for the ID and Pachacutik, as the latter's fracture leaves the current Assembly members with little chance of being reelected if the Muerte Cruzada takes place. Mr. Lasso's weak electoral position made his strategy clear from the start, only calling for the Muerte Cruzada if it was clear he was going to be ousted in the impeachment. With this threat, the administration was able to play with the opposition's fears and managed to gain some ground politically. However, these advances cannot be translated into any tangible results. In addition, the threat of the Muerte cruzada vanishes the second Mr. Lasso's impeachment debate starts in the Assembly. And without said threat, the opposition's incentives, which currently seem to be slightly off, might align, as with no chance of they themselves being ousted, then they can vote freely to displace Mr. Lasso from the presidential chair. To avoid destitution, Mr. Lasso must build alliances in the Assembly that are not cemented on the Muerte Cruzada threat. And the inability to do just that is what forced him into the current situation.

TPCG Analysts & Staff

Research

Juan Manuel Pazos	**Chief Economist**	**jmpazos@tpcgco.com**	**+54 11 4898-6606**
Paula La Greca	Corporate Research Analyst	plagreca@tpcgco.com	+54 11 4898-6638
Federico Martin	Strategist	famartin@tpcgco.com	+54 11 4898-6633
Santiago Resico	LATAM Strategist	sresico@tpcgco.com	+54 11 4898-6615

Sales & Trading

Juan Manuel Truppia	**Head of Sales & Trading**	**jmtruppia@tpcgco.com**	**+54 11 4898-6659**
Lucia Rodriguez Pardina	S&T Director	lrodriguezpardina@tpcgco.com	+54 11 4898-6614
Agustina Guadalupe	Sales	aguadalupe@tpcgco.com	+54 11 4898-6682
Maria Pilar Hurtado	Sales	mhurtado@tpcgco.com	+54 11 4898-6616
Juan Ignacio Vergara	Sales	jivergara@tpcgco.com	+54 11 4898-1936
Santiago Baibiene	Sales	sbaibiene@tpcgco.com	+54 11 4898-6648
Pedro Nollmann	Sales	pnollmann@tpcgco.com	+54 11 4898-6617
María Ruiz de Castroviejo Salas	Sales	mruizdecastroviejo@tpcgco.com	+54 11 4898-6643
Victoria Faynbloch	Desk Analyst	vfaynbloch@tpcgco.com	+54 11 4898-6635
Felipe Freire	Trader	ffreire@tpcgco.com	+54 11 4898-1921
Homero Fernandez Bianco	Trader	hfbianco@tpcgco.com	+54 11 4898-6667
Andres Robertson	Trader	arobertson@tpcgco.com	+54 11 4898-6693

Corporate Banking

José Ramos	**Head of Corporate Banking**	**jramos@tpcgco.com**	**+54 11 4898-6645**
Camila Martinez	Corporate Sales	cmartinez@tpcgco.com	+54 11 4898-6621
Fernando Depierre	Corporate Sales	fdepierre@tpcgco.com	+54 11 4898-6636
Sol Silvestrini	Corporate Sales	ssilvestrini@tpcgco.com	+54 11 4898-6641
Nicolas Iglesias	Corporate Sales	niglesias@tpcgco.com	+54 11 4898-6612

Capital Markets

Fernando Lanus	**Head of Capital Markets**	**flanus@tpcgco.com**	**+54 11 4898-6632**
Nicolás Alperín	Investment Banking Analyst	nalperin@tpcgco.com	+54 11 4898-6604

Asset Management

Ileana Aiello	**Portfolio Manager**	**iaiello@tpcgco.com**	**+54 11 4898-6611**
Claudio Achaerandio	**Portfolio Manager**	**cachaerandio@tpcgco.com**	**+54 11 4898-6618**

Important Disclaimer

The document, and the information, opinions, estimates and recommendations expressed herein, have been prepared by TPCG Valores SAU to provide its customers with general information regarding the date of issue of the report and are subject to changes without prior notice. TPCG Valores SAU is not liable for giving notice of such changes or for updating the contents hereof. The document and its contents do not constitute an offer, invitation or solicitation to purchase or subscribe to any securities or other instruments, or to undertake or divest investments. Neither shall the document nor its contents form the basis of any contract, commitment or decision of any kind.

Investors who have access to the document should be aware that the securities, instruments or investments to which it refers may not be appropriate for them due to their specific investment goals, financial positions or risk profiles, as these have not been taken into account to prepare the report. Therefore, investors should make their own investment decisions considering the said circumstances and obtain such specialized advice as may be necessary.

The contents of the document are based upon information available to the public that has been obtained from sources considered to be reliable. However, such information has not been independently verified by TPCG Valores SAU, and therefore no warranty, either express or implicit, is given regarding its accuracy, integrity or correctness. TPCG Valores SAU. accepts no liability of any type for any direct or indirect losses arising from the use of the document or its contents. Investors should note that the past performance of securities or instruments or the historical results of investments do not guarantee future performance. The market prices of securities or instruments or the results of investments could fluctuate against the interests of investors. Investors should be aware that they could even face a loss of their investment.

Transactions in futures, options and securities or high-yield securities can involve high risks and are not appropriate for every investor. Indeed, in the case of some investments, the potential losses may exceed the amount of initial investment and, in such circumstances; investors may be required to pay more money to support those losses. Thus, before undertaking any transaction with these instruments, investors should be aware of their operation, as well as the rights, liabilities and risks implied by the same and the underlying stocks. Investors should also be aware that secondary markets for the said instruments may be limited or even not exist.

TPCG Valores SAU. and/or any of its affiliates, as well as their respective directors, executives and employees, may have a position in any of the securities or instruments referred to, directly or indirectly, in the document, or in any other related thereto; they may trade for their own account or for third-party account in those securities, provide consulting or other services to the issuer of the aforementioned securities or instruments or to companies related thereto or to their shareholders, executives or employees, or may have interests or perform transactions in those securities or instruments or related investments before or after the publication of the report, to the extent permitted by the applicable law.

TPCG Valores SAU or any of its affiliates' salespeople, traders and other professionals may provide oral or written market Commentary or trading strategies to its clients that reflect opinions that are contrary to the opinions expressed herein. Furthermore, TPCG Valores SAU, or any of its affiliates' proprietary trading and investing businesses, may make investment decisions that are inconsistent with the recommendations expressed herein.

No part of the document may be (i) copied, photocopied or duplicated by any other form or means (ii) redistributed or (iii) quoted without the prior written consent of TPCG Valores SAU. No part of the report may be copied, conveyed, distributed or furnished to any person or entity in any country (or persons or entities in the same) in which its distribution is prohibited by law. Failure to comply with these restrictions may breach the laws of the relevant jurisdiction.

For U.S. persons only:

This report is a product of TPCG, which is the employer of the research analyst(s) who has prepared the informative report. The research analyst(s) preparing this report is/are resident(s) outside the United States (U.S.) and is/are not associated person(s) of any U.S. regulated broker-dealer and therefore the analyst(s) is/are not subject to supervision by a U.S. broker-dealer and is/are not required to satisfy the regulatory licensing requirements of FINRA or required to otherwise comply with U.S. rules or regulations.

This report is intended for distribution by TPCG only to U.S. Institutional Investors and Major U.S. Institutional Investors, as defined by Rule 15a-6(b)(4) of the U.S. Securities and Exchange Act, 1934 (the Exchange Act) and interpretations thereof by the U.S. Securities and Exchange Commission (SEC), in reliance on Rule 15a 6(a)(2). If the recipient of this report is not a a US Institutional Investors nor a Major U.S. Institutional Investor, as specified above, then he should not act upon this report and return it to the sender. Further, this report may not be copied, duplicated and/or transmitted to any U.S. person, which is not a U.S. Institutional Investor, nor a Major U.S. Institutional Investor.

In order to comply with the US regulations, our transactions with US Institutional Investors and Major US Institutional Investors are effected through the US-registered broker-dealer Marco Polo Securities Inc. ("Marco Polo"). Transactions in securities discussed in this report should be effected through Marco Polo or another U.S. registered broker dealer.