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IMF Agreement & Credit Rating Revisions

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Event

On February 15th, 2013, the International Monetary Fund (IMF) announced that an agreement has reached with Jamaican authorities on a reform program to be supported by a four-year financing facility.

Significance

The combination of the debt-reduction initiative launched on February 12th and a multi-year IMF-supported economic program, yet to be approved by the Fund, is a positive development to address debt-sustainability challenges required to place the Jamaican economy on a sustainable growth trajectory.

Financial Market Reaction

Investor sentiment in foreign exchange and fixed-income markets remains weak following the announcement of the distressed-debt exchange which triggered multiple negative credit rating revisions. Following temporary gains seen in intra-day trading on February 12th, the Jamaican sovereign debt market regained a cautious tone this week; the market-benchmark EMBIG (yield spread) index closed the week at 685 basis points (bps) over US treasury bonds. The Jamaican government bond maturing in June 2019 trades at a yield of 8.58% (today). The Jamaican dollar (JMD), at 94.70 per US dollar, maintains a fragile tone.

Analysis and Outlook

The IMF stressed that a substantial improvement in the country's debt profile as a result of the announced debt exchange and the measures envisaged in a comprehensive structural and fiscal reform agenda will support the achievement of debt-sustainability goals in the medium term. It is worth highlighting that, through a 48-month Extended Fund Facility (EFF), the Fund acknowledges the complexities faced by the Jamaican authorities on the public sector administrative reform and fiscal consolidation agendas. The IMF estimates to have the US$750-million EFF approved by the end of March.

The Administration of Prime Minister Portia Simpson-Miller begins a new fiscal year on April 1st, 2013. Therefore, the IMF-supported economic plan will undoubtedly serve as a key pillar of negotiations and final approval of the government's budget. Targeting relatively large primary fiscal surpluses is a key element of the negotiated agreement. The administration maintains broad popular and parliamentary support to introduce the changes needed to comply with the agreement. Nevertheless, the negative precedent set by the previous debt exchange in terms of program implementation will keep investors in a cautious mood until visible progress on structural reforms are in place.

International credit rating agencies will closely monitor the final approval (and implementation) of the IMF arrangement in the months to come. However, the terms of the debt-reduction initiative clearly represent for the rating agency community a distressed-debt event which has led to multiple rating revisions. In fact, Standard and Poor's (S&P) placed Jamaica's foreign and local-currency credit ratings in the SD (selective default) category following the announcement of the domestic debt exchange on February 12th, 2013. S&P, which made a similar move when Jamaica conducted its restructuring three years ago, highlighted the presence of structural economic weaknesses as a key impediment for a rapid improvement in the country's financial profile. S&P stated that a "CCC" rating would be granted upon completion of the exchange. The same day, Fitch downgraded the country's rating from "B" to "C" highlighting that the proposed coupon reduction and maturity extension represent a significant change in the terms of the value of debt at the time of issuance. Finally, yesterday, Moody's placed Jamaica's long-term foreign-currency "B3" rating on review for a possible downgrade.

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