EMFI

Suriname

Country Report: Smokes and Mirrors

- The new crawling peg regime established a lower band of 14,290 SRD/USD and an upper band of 16,300 SRD/USD.
- The government also established anti-market measures such as mandatory repatriations and foreign exchange surrender requirements for exporters.
- We calculate that the net international reserves reach USD 129 mn, enough to cover only around 3 weeks of imports.
- The recently announced measures are a momentary solution that does not really tackle the underlying fiscal issues.
- SELL: The news about the government measures is not market-friendly, but Suriname's debt remained unchanged in recent weeks due to the low volume of operations.

News Highlights

- Apache concluded drilling operations at Keskesi East-1 well due to high pressure
- 3,021 Surinamese have been vaccinated

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Emerging Markets

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Background

Negotiations between the Surinamese government and the International Monetary Fund are stalled pending exchange rate and budget reforms. **On March 1, the government took a step forward and relaxed its exchange rate policy, shifting to a crawling peg from a de facto fixed exchange regime.** The Central Bank established a lower band of 14,290 SRD/USD, which is the same rate that the old fixed system had, and an upper band of 16,300 SRD/USD.

In some exchange houses, the FX rate quickly reached the upper band of 16,300 SRD, a devaluation of 12.4%. This rate is still below the parallel market rate, which is between 18,200 and 18,500 SRD/USD according to local media. Although the crawling peg is a more flexible model than the previous one, it is not a market-determined exchange rate regime like the one recommended by the IMF. The government seems not to be willing to go that far, but will the crawling peg be enough for the IMF?

Along with the FX regime reform, the government introduced other complementary measures to stabilize the exchange rate as of March 1: 1) All residents exporters must repatriate all their export proceeds (from 60% in the previous law), 2) exporters must convert 30% of their proceeds to local currency, and 3) importers will have to pay for their imports through Surinamese foreign exchange banks. All these measures will be part of an amendment to the controversial Foreign Exchange Law amended a year ago by the Bouterse government.

The “New” Foreign Exchange Policy

Fixed exchange regimes have a long history in Suriname. Since its independence in 1975, the government has sometimes abandoned them temporarily, but always ends up returning to this type of scheme. Suriname had an official crawling band scheme between 1975 and 1982, and between 1999 and 2000. It also maintained a de facto crawling band between 1994 and 1998. The “new” exchange regime would be the fourth attempt at a band policy.

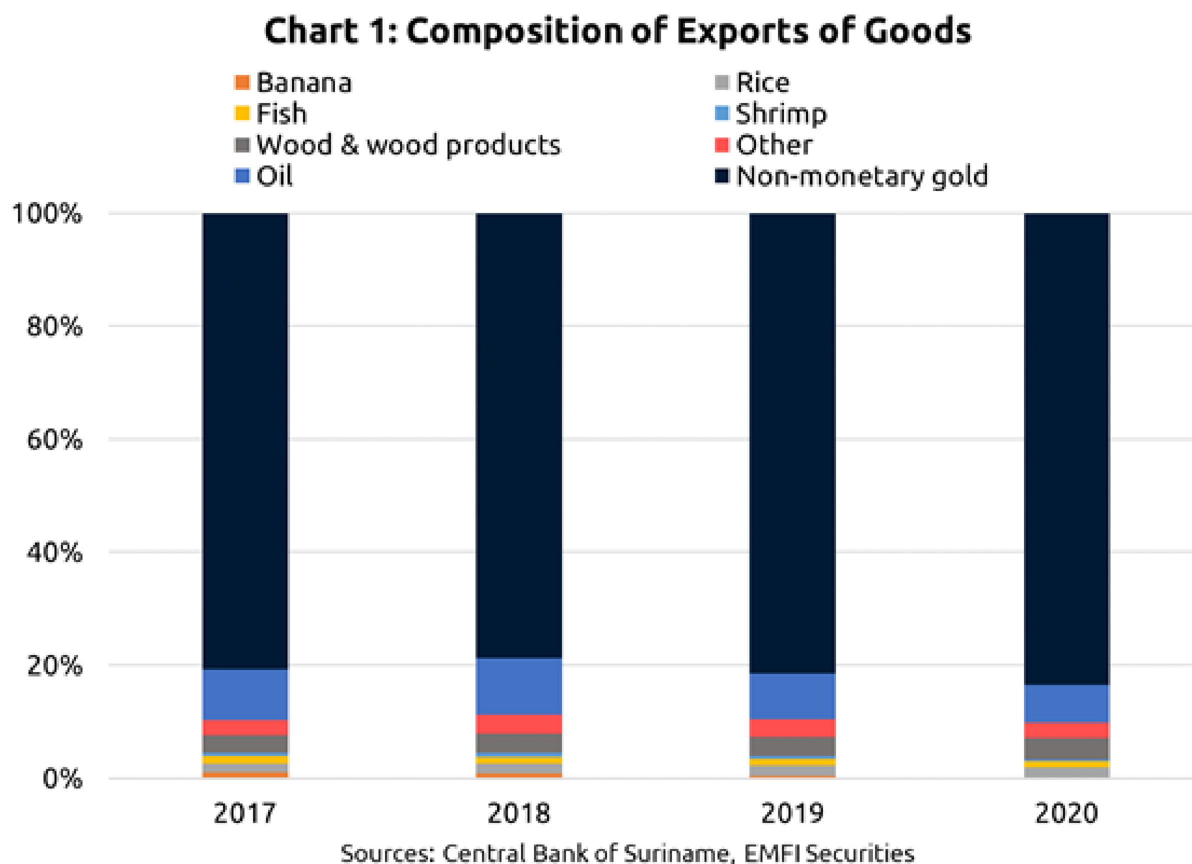
The Suriname Association of Economists urged the government to let the exchange rate float and be determined by the market. The IMF has repeatedly recommended that Suriname should adopt a flexible exchange rate given its position as a commodity exporter, which makes it vulnerable to external shocks. However, President Santokhi thinks that allowing the exchange rate to float freely is irresponsible, because if it does so, "who knows where the exchange rate will end?" At the press conference in which the government announced the new exchange rate regime, the Minister of Finance and Planning, Armand Achaibersing, said “the government is there for our people and not for the IMF”. These kinds of statements resemble those made by the Bouterse administration when it abandoned the agreement with the IMF, arguing that it was "too much" for the citizens of Suriname.

The policies that regulate export revenues are not new either. Until May 2002, all exporters had to repatriate all their export proceeds and partially surrender foreign currency to the Central Bank. In this sense, **the measures proposed by the government of President Santokhi not only recall the past but also bring to mind non-market-friendly countries like Sri Lanka and Argentina.** Sri Lanka recently implemented such measures in an attempt to move away from the IMF and towards China instead, as the Sri Lankan government clearly expressed its preference for "non-interventionist" lenders. **It seems contradictory for the Surinamese government to take similar heavy-handed measures amid friendly negotiations with the IMF.**

Agricultural exporters rejected the foreign exchange surrender requirements and demanded that it be reversed immediately. The Federation of Agricultural Exporters said that “it cannot imagine how the same government that promotes the importance of the manufacturing sector (…) makes decisions that are a dagger for agricultural production and exports”. Indeed, these measures will, in the medium term, discourage exports, and could even worsen external imbalances.

These measures do not affect non-residents exporters. The largest component of exports is gold exports which amounted to 83.6% of the total in 2020 (see **Chart 1**). Two large international companies (Iamgold and Newmont) produced around 50% of gold exports in 2020. We calculate resident exports totaled USD 1.2 bn in

2020. Taking this number, we calculate that the surrender requirements during 2021 would amount to USD 543.4 mn. This would be enough for the Central Bank to absorb 15.6% of the broad money (considering that it keeps the broad money of January constant). However, a more credible assumption would be that broad money will grow at the same rate as in 2020 (62.1%). In this scenario, Central Bank would absorb 9.7% of broad money. Although the impact would be substantial in stabilizing the exchange rate, it would also create disincentives to trade, raising transactional costs and hurting domestic exporters.



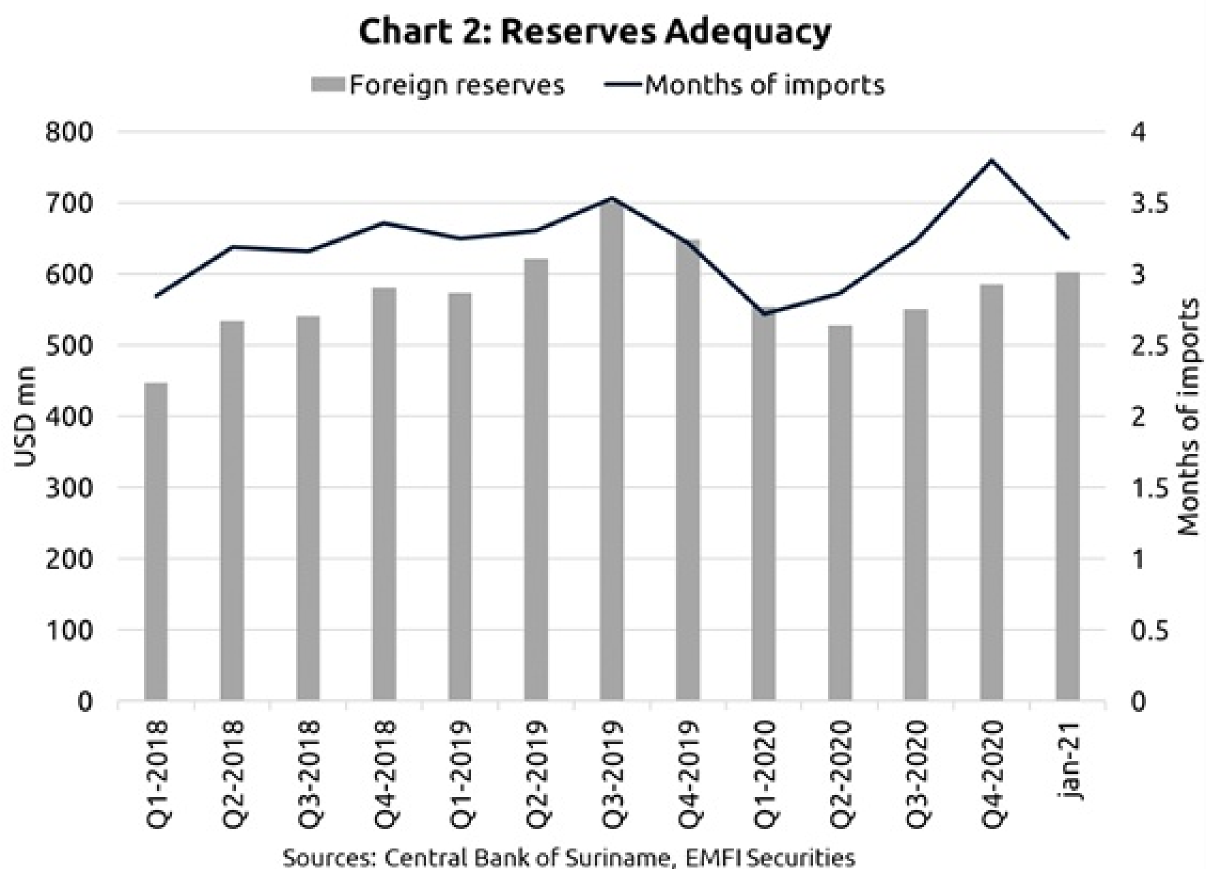
Desperate Times Call for Desperate Measures

The measures approved by the government of Suriname aim to strengthen the country's external buffers, namely the FX reserves. Gross international reserves stood at USD 601mn in January, and while that represents an increase of 2.9% compared to December, it also means that reserves would barely cover 3.3 months of imports (See **Chart 2**). Although there was an improvement compared to 1Q20, it is not enough. According to the latest Article IV of the IMF, an adequate level of reserves must be greater than 4 months of imports.

Suriname's situation is even more critical because gross international reserves include the required reserves of commercial banks that the government cannot use to pay for imports. The reserve requirement figures included in international reserves are not public. If the figure reported by the finance ministry in the presentation to investors in September remained in proportional terms, **we estimate that net international reserves amount to USD 129 mn, enough to cover around 3 weeks of imports.**

Considering the level of net international reserves, we understand why the government implemented these measures that seem opposite to the IMF's suggestions. With that said, they still feel like desperate measures that serve as a momentary solution while waiting for IMF funds. However, it is striking that the government has not communicated it in this way: the government has not explained whether these measures are provisional, nor did it highlight the solution to the underlying fiscal issues, which are the main cause of exchange rate imbalances. On the contrary, the government announced a new fuel subsidy and froze certain basic goods prices. Also, the government has not yet fulfilled the promise it made in mid-January to publish another budget bill.

We believe that the communication of these measures is a setback for President Santokhi, as the measures appear isolated and undermine the credibility of a potential stabilization plan.



What to expect?

The Santokhi government appears to have taken an unexpected turn towards heterodox economic policies. Suriname has followed in the footsteps of countries such as Sri Lanka or Argentina by imposing anti-market measures such as mandatory repatriations and foreign exchange surrender requirements for exporters. Although government representatives defended the new measures despite not being in line with IMF advice, they still maintain that the talks with the IMF are on the right track. Thus, while we believe that the new measures reduced the odds of an agreement with the IMF, we maintain our baseline scenario that Suriname will reach an agreement with the multilateral institution.

On the other hand, the outlook for oil activities is positive. In the announcement of its quarterly results, Apache Corp revealed that most of its upstream Capex in 2021 will go to Suriname. **The company will invest USD 200mn in the construction of two rigs, as part of its exploration program.** Apache expects to be pumping crude oil in 2025.

However, the heterodox "solutions" in the present could cloud the bright future. After almost eight months in the presidency, Santokhi has only implemented the so-needed currency devaluation and no other major policy measure to stabilize the economy. The recently announced policies are a short-term fix that does not really tackle the underlying fiscal issues, throwing a wrench into the relationship with the IMF while kicking the can down the road for the most important challenges facing the country.

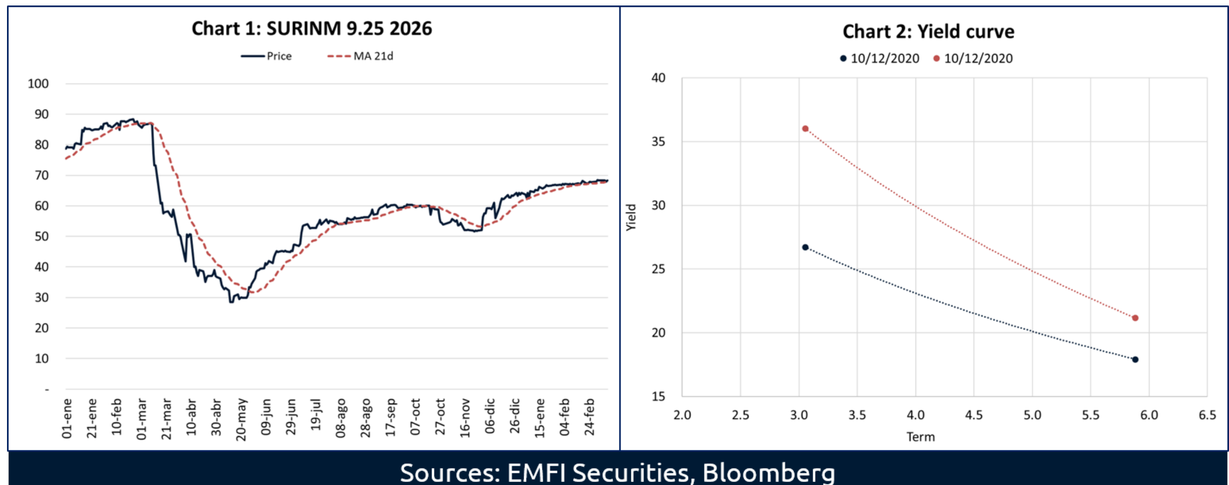
Credit Strategy

EMFI Team Evaluation	SELL

SURINM 26 is trading at 66.27 cents on the dollar, just 6 bp less than the previous month. Meanwhile, the yield increased by 25 bps to 18.5%. The price of the bond over the last three months has averaged 67 cents on the dollar, which may serve as the best indication of investors' expectations regarding an eventual debt restructuring.

In previous reports, we highlighted the Santokhi administration's market-friendly approach, but the latest restrictions on foreign trade and capital mobility are a setback on our opinion of the Santokhi administration. The new measures are unlikely to help in the negotiation with bondholder, especially given that an IMF package is necessary. The standstill will expire on March 31 unless the government reaches an agreement with the IMF before March 24 (in which case the end of the standstill moves to April 26). The deal with the Fund appears to be delayed (at best), increasing the odds over the days of a disorderly default in the next month.

Although we have mentioned in recent reports that bonds are not the main problem in Suriname's overall debt structure, the reality is that the government is not doing enough to address its macro problems. The IMF's SDR allocation, which could bring some USD 150 mn (106% of net international reserves) for Suriname, could help in the short-term, but won't address the long-term problems. In this context, we think that the current price of bonds reflects excessive optimism as to both the probability that the government will resume payments and the recovery value in an eventual debt workout.



Sources: EMFI Securities, Bloomberg

Table 1: Credit Indicators

Indicator	Value	Credit Impact
Credit Rating		
Composite Rating	DDD+	Negative
Liquidity (bonds only)		
12m External Debt Service (% of Exports)	3%	Positive
12m External Debt Service (% of Fiscal Revenues)	8%	Neutral
12m External Debt Service (% of FX Reserves)	12%	Neutral
Solvency		
Total Public Debt (% of GDP)	140%	Negative
Total Public Debt (% of Fiscal Revenues)	369%	Neutral
Total Public Debt (% of Exports)	131%	Positive
Probability of Default		
1y CDS-Implied Probabilities of Default (%)	N/A	N/A
5y CDS-Implied Probabilities of Default (%)	N/A	N/A

Sources: Bloomberg, Ministry of Finance, Central Bank, EMFI Securities

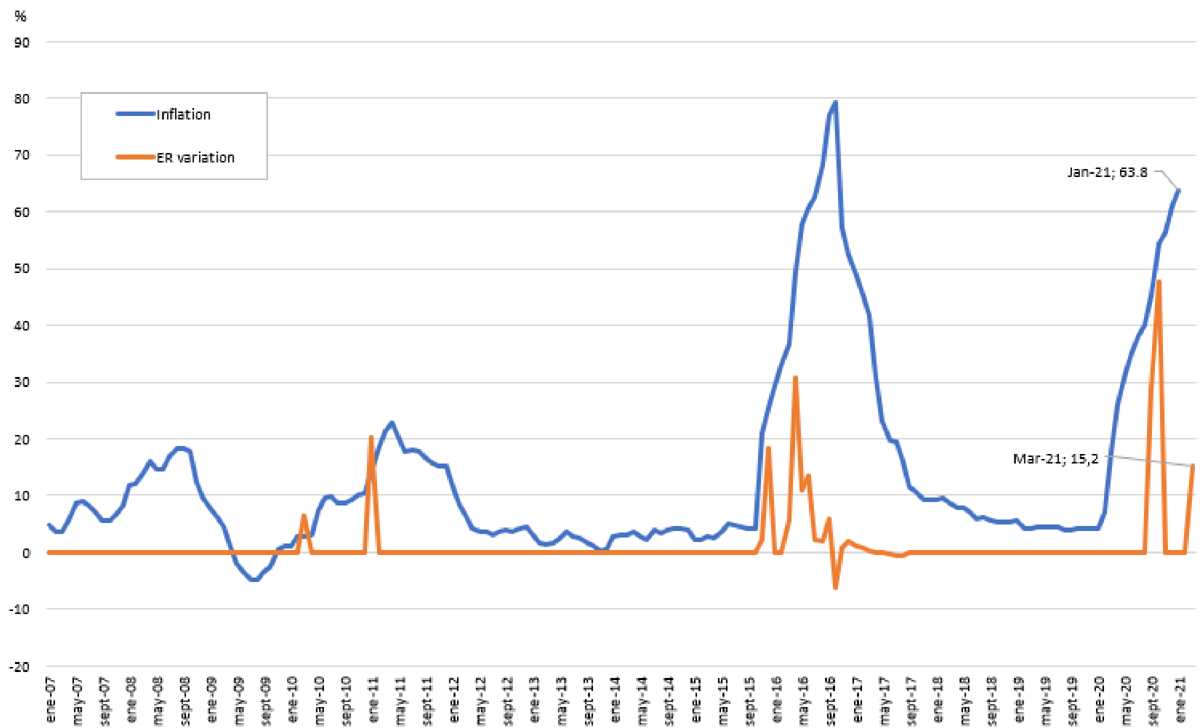
Key Macroeconomic Forecasts

The weak external asset position of the country and the real and fiscal adjustments that it demands constitute one of the main constraints to a vigorous economic recovery after the severe real GDP contraction of 2020. One positive development has been the significant reduction in the number of daily cases of Covid-19 during the last month, although it has not yet translated into a meaningful decrease in the strictness of government measures to control the virus (as measured by the Oxford Stringency Index, that went from 70.4 in January to 66.7% by the end of February). In a highly uncertain environment, we maintain our baseline scenario that depicts an increase of 3.6% in real GDP in 2021. Consumer prices rose 2.5% m/m (63.8% y/y) in January, a monthly rate that is consistent with the deceleration portrayed in our macroeconomic outlook for 2021 (end-of-year forecast 34.1% vs. 61.0% in 2020). Balance of payments headline figures for the 4Q-2020 were markedly positive, showing a current account surplus of USD 150 million (the best quarterly outcome since 2Q-2012 and around 6.2% of our estimated GDP), but the result was partially explained by a 29.1% y/y contraction in the level of imports, a discouraging number.

Figure 1

Inflation and the Official Exchange Rate

We expect annual inflation to moderate in the upcoming months, but the return to 1-digit levels will take time.



Source: Central Bank of Suriname, EMFI Securities estimates.

Suriname

Summary of Economic Indicators and Forecasts

	2017	2018	2019	2020 (E)	2021 (F)
Real GDP growth rate (%)	1.8	2.6	0.3	(16.1)	3.6
Inflation (end of period, %)	9.2	5.4	4.2	60.8	34.1
Unemployment (% of work force)	7.5	9.4	9.0	10.7	10.4
Output Gap (% of GDP)	(1.1)	2.6	4.5	(11.0)	(6.1)
Nominal GDP (in millions of USD)[1]					
A. Using average official exchange rate	3,215	3,466	3,696	3,454	2,545
B. Using EMFI's estimates[2]	3,215	3,466	3,696	2,435	2,575
Current Account [% of GDP(B)]	2.1	(3.4)	(12.1)	11.3	1.8
Exports (millions of USD)	2,152	2,242	2,290	2,448	2,567
Imports (millions of USD)	1,790	2,076	2,416	1,847	2,221
Nominal Exchange Rate (ave. SRD/USD)	7.49	7.46	7.46	9.31	17.56
Addenda, IMF estimates (October 2020)					
GDP (millions PPP, int'l dollars)	9,340	9,811	10,013	8,827	9,156
Population (millions)	0.583	0.590	0.597	0.604	0.612
GDP per Capita (PPP, int'l dollars)	16,021	16,629	16,772	14,614	14,961

[1] The analysis of nominal variables converted to dollars using market exchange rates must be done with caution, especially in a context of multiple exchange rates and/or when the real exchange rate shows sizeable misalignments from equilibrium.
[2] For analytical purposes, we use the nominal exchange rate that keeps the bilateral real exchange rate constant as the best indicator to estimate the value of nominal GDP in USD.
Note: Figures in brackets represent negative values.
Source: IMF, EMFI Securities estimates, Centrale Bank van Suriname.

SECURITY	BID	ASK	YIELD	SPREAD	CHANGE	52 WK LOW	52 WK HIGH
SURINM 9 7/8 12/30/23	69.40	69.90	27.30	5277	-0.10	0.00	95.00
SURINM 9 1/4 10/26/26	67.05	67.55	18.59	1951	0.00	0.00	100.20

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