Rousseff Losing Bond Investors as Economy Falters: Brazil Credit

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By Paula Sambo and Filipe Pacheco

Oct. 27 (Bloomberg) -- The stagnant Brazilian economy and soaring inflation that almost cost President Dilma Rousseff her re-election bid yesterday haven't pleased bondholders.

The country underperformed developing-nation peers in both local and foreign debt markets during her first four years. Her second term may even bring worse returns as concern mounts that Brazil could lose its investment-grade rating after Standard & Poor's cut the country to one level above junk in March.

Quantitas Gestao de Recursos, a Porto Alegre-based investment boutique that manages 15 billion reais ($6.1 billion), estimated last week there is a 50 percent chance Brazil could be cut to junk in her second term.

"Unfortunately, this is very negative for Brazil," Bianca Taylor, a Boston-based sovereign analyst and strategist at Loomis Sayles, which oversees $223 billion of assets, including Brazilian bonds, said in a telephone interview last night.

Taylor expects a "natural negative reaction" in bond markets this week. "She has not managed the country in a good way so far."

Rousseff has boosted spending and stepped up government control of state-run companies, discouraging investment and helping sink the economy into stagflation. The country's gross domestic product shrank in the first half of the year while annual inflation soared to 6.75 percent in September, above the top end of the government's target range.

Bonds Fall

Brazil's benchmark dollar bonds due in 2025 fell 0.44 cent to 100.87 cents on the dollar at 8:51 a.m. in New York while yields on local fixed-rated notes maturing in 2023 rose 0.57 percentage point to 12.61 percent. The Ibovespa benchmark equity index slumped toward a bear market, falling 4.9 percent to 49,408.11. The real posted the world's biggest drop as it sank 2 percent to 2.5248 per dollar, a nine-year low.

Brazil’s dollar bonds returned 8.7 percent this year, trailing the average 10 percent advance for investment-grade developing nations, JPMorgan Chase & Co. indexes show. In Rousseff’s first three years in office, the notes posted an annual gain of 5.04 percent, lagging behind the 5.6 percent return for similarly rated sovereign peers.

At 4.79 percent, Brazil’s average dollar bonds yield 0.45 percentage point more than securities from other investment- grade developing nations. That’s the biggest gap since Rousseff succeeded her mentor, Luiz Inacio Lula da Silva, in 2011. She defeated opposition candidate Aecio Neves by 52 percent to 48 percent yesterday in the closest Brazilian presidential election in 69 years.

Investors in Brazil’s local debt market have fared even worse. A plunge in the real has saddled them with losses of 9 percent in dollar terms over the past four years, the worst among major currencies after the South African rand and Japanese yen, data compiled by Bloomberg show. The real has declined 34 percent against the dollar since she took office.

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