INSIGHTS FROM THE FIELD

FOR POLICYMAKING AND BUSINESS IN LATIN AMERICA

This is a quarterly bulletin produced in Buenos Aires, Argentina with the aim of providing in-country perspectives on politico-economic and security issues in the Latin American region. It draws on insights from regional scholars, government leaders and business executives.

EDITOR´S NOTES

SOUTH AMERICA is looking increasingly attractive in light of the economic turmoil in Europe, social upheaval in the Middle East and the lethargic recovery in the United States. With the exception of isolated protests and corruption allegations affecting several governments, the sub-region is relatively calm and experiencing strong economic growth. Not surprisingly, internationals want to do business in and cooperate with South American countries today.

China, of course, woke up to the potential over a decade ago and is now a key trading partner and investor in the region. Somewhat lesser known is the growing affluence of the Chinese immigrant population in South America. In this edition of *Insights*, we reveal the success of the Chinese diaspora in Argentina's supermarket business. We also showcase a new fiscal policy proposed by Brazilian President Rousseff aimed at doubling the size of the defense production industry, a pillar of economic development and technological transformation. Lastly, we turn to how cooperation with the United States has helped Argentina launch satellites into space and build its own satellite and radar production capabilities.

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Happy Holidays,

Janie Hulse
EDITOR

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ECONOMIC POLICY SHIFTS

▸ Long accustomed to being the recipient of foreign aid, Brazil has announced that it will shift from a debtor to a creditor nation by offering funds to the International Monetary Fund. Its contribution will help the organization minimize the effects of the European sovereign debt crisis. Brazil is operating from a position of strength after years of sound macroeconomic management. The contribution amount will be determined in a February 2012 meeting of the BRIC countries (Brazil, Russia, India, China and South America).

▸ Venezuelan President Hugo Chávez announced in August that he will nationalize his country's gold industry. With gold selling at close to US$2,000 an ounce, he plans to use the industry's output to bolster international reserves. It will also help him to raise money and consolidate power before the upcoming presidential election in October 2012. At the same time, Mr Chávez also moved to recall nearly US$11bn in reserves held in U.S. and European banks. Many analysts conjecture that the latter shift was aimed at protecting Venezuelan capital from being frozen should international sanctions be imposed.

▸ After a landslide re-election vote on October 23, Argentinean President Cristina Fernández de Kirchner swiftly ended her government's bloated subsidy regime that helped make her popular. In November, she called to

▸ SPECIAL REPORT ◂

"SHOULD ARGENTINA BE WELCOMED BACK BY INVESTORS?"
WORLD ECONOMICS July–September 2011
By Arturo C. Porzecanski

After a relatively brief interruption in access to the world's financial markets in late 2008 and early 2009, Latin America has been experiencing a renewed wave of capital inflows...

[Continued on page 9]

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cut US$800m in utility subsidies enjoyed by homes and businesses. The change will first affect the wealthy and big businesses but will later be applied to all with the exemption of lower income families. A few weeks prior, a similar decision was made to cut 100% of government assistance to oil, gas, mining, banks and insurance companies. The savings will help the government cushion dwindling international reserves.

BUSINESS MOVES

▸ In early December, the Brazilian government ordered Chevron Corp to close one of its offshore wells as a result of tougher monitoring following an accident at another one of its wells in November. The US company was fined US$28m for a 2,400 barrel oil spill into the ocean. Though a relatively small accident, it will likely strengthen a trend toward stronger government control of the growing oil industry in Brazil. Since of the findings of large deep water reserves in 2007, Brazil´s government is increasingly directing the complex excavation preparations to ensure its future status as one of the world´s largest oil producers.

▸ The Venezuelan government under Hugo Chávez will pay US$600m to compensate Mexico´s Cemex for a 2008 nationalization of Venezuela´s cement sector. Cemex confirmed the deal and expressed satisfaction, but it is receiving less than the US$1.3bn originally requested. In late 2010, the World Bank´s International Centre for Settlement of Investment Disputes recognized Cemex´s right to sue for the loss of assets. The government take-over occurred after the Venezuelan government accused the Monterrey-based company of polluting; Cemex has denied wrong-doing.

▸ According to the Business Software Alliance (BSA), US$59bn worth of software was stolen last year around the world. The BSA claims that emerging markets now account for more than half the global value of PC software theft, US$31.9bn. According to the research group, Latin America is one of the world's worst culprits with a 64% piracy rate, much greater than the 42% world average and higher than the 58% rate in the Middle East and Africa.

DEFENSE MATTERS

▸ Brazilian President Dilma Rousseff launched a plan in June to strengthen border security to combat drugs and arms trafficking. It is a shared initiative between the Brazilian Defense and Justice departments. The so-called Strategic Border Plan requires cooperation between the armed forces and federal police in 112 municipalities in 11 states bordering South American countries. As part of the initiative, 5,000 troops will be deployed and will be supported by military boats, planes, vehicles and monitoring satellites. The President recently ordered three unmanned aircraft to control the notorious triple frontier area 24 hours a day.

▸ The conflict over the Malvinas/Falkland island continues. In September , during her UN assembly address, Argentinean President Cristina Fernández de Kirchner threatened to rescind a 1999 agreement permitting commercial flights to the disputed island territory. The agreement, signed during the presidency of Carlos Menem, allows for a lay-over in Argentina´s Patagonian city Rio Gallegos en route to the island from Chile´s Punta Arena. Rather than bowing to the pressure, Britain added more salt to the wounded relationship by announcing in November that Prince William will be deployed to the island for helicopter pilot training.

▸ In September, UNASUR carried out its first military exercise in Buenos Aires called Combined Regional Joint Exercise of Peace Keeping Operations, UNASUR 1. The activity was carried out by the South American Defense Council (CDS), with the participation of the defense ministries and Armed Forces from Argentina, Bolivia, Brazil, Chile, Colombia, Ecuador, Paraguay, Peru, Uruguay and Venezuela. The objective of the exercise was identifying inter-operability standards on planning and development of peace keeping operations. According to UNASUR´s 2012 Action Plan, Argentina will host a similar event, UNASUR 2, next year.

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CHINA IN ARGENTINA: A BELATED DEBUT

First published by Americas Quarterly, Council of the Americas

BY JANIE HULSE*

ARTICLE SUMMARY

THE CHINESE ARE THE FASTEST GROWING NON-LATIN AMERICAN IMMIGRANT POPULATION IN ARGENTINA. WHILE THEY REMAIN SOCIALLY ISOLATED, THE CHINESE COMMERCIAL SUCCESS IN THE COUNTRY IS NOTHING SHORT OF ASTOUNDING. A CHINESE SUPERMARKET OPENS EVER TWO DAYS IN BUENOS AIRES. AT 120,000-STRONG, THESE SMALL STORES HAVE BECOME A STAPLE FOR CITY-DWELLERS AND EVEN OFFER THEIR OWN PRODUCTS AND CREDIT CARDS. YET THEY HAVE ALSO BECOME THE TARGET FOR CRIME, LARGELY PERPETRATED FROM WITHIN THE CHINESE COMMUNITY ITSELF. AS CHINA´S TRADE AND INVESTMENT INCREASE IN ARGENTINA, THE CHINESE DIASPORA IS GROWING INCREASINGLY AFFLUENT.

ON WEEKEND EVENINGS IN BUENOS AIRES´ upscale Palermo neighbourhood, newly washed sedans and SUVs line up along the wide Libertador Avenue, creating a shimmering cascade of lights as their occupants eagerly await valet parking.

The restaurant of choice is a fashionable American-style bistro, aptly named Kansas. It has become a staple for well-heeled Porteños whose frequent trips to Miami and New York leave them craving burgers and good service. Known for remarkable consistency in a land of improvisation, the only thing that has changed since its opening six years ago is its clientele. It's now packed with Chinese.

Chinatown apparently is unable to satisfy the increasingly sophisticated tastes of Argentina's Chinese immigrants. At 120,000-strong, when including Taiwanese and temporary visa holders, the Chinese are the fastest growing non-Latin American immigrant population. Since 2004, Argentina has granted over 26,000 visas to the Chinese—a figure topped only by neighbouring Paraguayans, Bolivians and Peruvians, many of whom find work with the Chinese upon arrival.

A Chinese supermarket opens every two days in Buenos Aires. With over 10,000 in total, it's rare to walk more than a few blocks without coming across one. Los chinos, as they are known, collectively generate a whopping $6 billion a year. Their secret to success? Location. Location. Location. They also manage to maintain competitive prices thanks to their broad wholesale distribution network; this is especially difficult with inflation topping 20 percent yearly since the 2003 economic recovery.

Ever evolving, this year the Chinese markets began branding their own products and offering a credit card financed with an initial $20 million by the Chamber of Chinese Supermarkets (CASRECH) and backed by the Chinese government.

Success, however, comes at a price. There are a shocking 120 crimes per day perpetrated against their markets, some of them bloody. This has led to conjecture about a Chinese mafia. The Argentine security forces are now grappling with the appearance of an underground network that relies on provincial dialects and unusual codes.

Though ubiquitous, these newcomers have not developed an immediate rapport with the locals. The Chinese immigrants´ non-existent or sloppy Spanish leads to social isolation, and, in some situations, arouses suspicions. The March 2011 opening of a dramatic comedy directed by Sebastián Borensztein and starring Argentina´s favorite actor, Ricardo Darín, hilariously portrays this cultural and linguistic disconnect between the Italian-like Spanish speakers and the Chinese among them. Darín´s character, forced to share a roof with a young Chinaman, takes extreme measures to locate the young man's long-lost uncle since cohabitation proves to be comically unbearable—a twist on the play and U.S. sitcom The Odd Couple.

Social ineptness, however, has not hampered Chinese commercial prowess or

CHINATOWN APPARENTLY IS UNABLE TO SATISFY THE INCREASINGLY SOPHISTICATED TASTES OF ARGENTINA'S CHINESE IMMIGRANTS. AT 120,000-STRONG, WHEN INCLUDING TAIWANESE AND TEMPORARY VISA HOLDERS, THE CHINESE ARE THE FASTEST GROWING NON-LATIN AMERICAN IMMIGRANT POPULATION.

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CHINA IN ARGENTINA: A BELATED DEBUT

the attractiveness of their millennial culture and language. China´s international rise coupled with its growing diaspora have fuelled Argentineans' demand for chow mein, tai chi and Mandarin classes. Today, there are around 2,000 Argentineans enrolled in private Mandarin courses.

To level the playing field, the mayor of the Buenos Aires municipality of Tigre, Sergio Massa, just launched a program sponsored by the Chinese Embassy to provide free Mandarin classes in public libraries. "We are preparing the future generations for the world to come," said the government official to the press.

The Chinese prefer a low profile. Given their proliferation and commercial inroads, they have received relatively little media attention in Argentina. This also holds true for Chinese diplomacy in South America in general where modesty is not only a cultural virtue but a practicality since chest-beating could alarm the superpower to the North or upset their hosts. The Chinese government's reticence to talk to the media, however, has done little to promote transparent exchange and mutual understanding.

After Chinese President Hu Jintao´s momentous trip to South America in November 2004, news reports exaggerated short-term investment promises to Argentina and created confusion surrounding the Asian giant's real intentions for the country. For a number of years, it looked like China would stick solely to extracting commodities—foodstuffs, energy and metals—and exporting cheap manufactured goods.

While these remain its principal activities, major deals in the last three years have revealed China´s more nuanced, long-term intentions for Argentina. And the Chinese government is just now beginning to talk openly about its plans for this so-called "strategic partner."

In an unprecedented move, the Chinese embassy acquiesced to a meeting with the foreign press on September 16. "This is the first time they agreed to meet in 26 years," boasted the president of Argentina's foreign correspondents´ association, Ricardo Rivas. Yet Mr. Yang Shidi, the Chinese embassy's commercial attaché, did little more than confirm trade and investment reports.

In sum, China is now Argentina's second most important trading partner after Brazil with bilateral commerce reaching $12.9 billion in 2010. Argentina is China´s fourth largest trading partner in Latin America after Brazil, Chile and Mexico. Chinese investment in the country has escalated in the last three years with an estimated $15 billion injected primarily into petrochemicals and agriculture but also into telecommunications, mining, finance, transport, energy, and manufacturing.

China emerged a player in Argentina's oil business with Sinopec´s $2.5 billion purchase of Occidental last year, and it will triple its stake in the industry should CNOOC Ltd´s pending $7.1 billion acquisition of BP´s Pan American Energy holdings go through as expected this year. These deals along with loftier promises to revamp dilapidated rail in the north-western interior, turn arid land green in Patagonia, and clean-up the toxic Riachuelo water basin in Buenos Aires have vindicated the 2004 investment rumors.

The embassy official touted the plethora of ministerial and business exchanges between his country and Argentina. Yet hiccups are frequent with one row interrupting Argentina's all-important soy oil exports in May 2010—a $2 billion a year blow. After painstaking negotiations, the Chinese lifted the ban a year later with no apparent strings attached. Argentina maintains 36 anti-dumping measures against China—more than when the conflict began. Stifled Chinese imports include thermoses, bicycles, ovens, dishware, shoes, and fabrics.

To allay concerns about China´s ever-growing presence, Mr Shidi insisted that China looks to provide social as well as economic benefits to Argentineans. He lamely held up the Riachuelo sanitation project as proof of their altruism.

The diplomat declined to discuss the commercial bonanza of the Chinese population in Argentina, piquing curiosity as to how the government could exploit this formidable network in the future. Yet the embassy's belated debut was met mostly with shoulder shrugging. ■

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NEW TAX BREAKS TO SPUR MAJOR NEW INVESTMENT BY BRAZIL'S DEFENSE INDUSTRY

First published by Diálogo Americas

BY JANIE HULSE*

ARTICLE SUMMARY

BRAZIL´S DEFENSE INDUSTRY IS EXPECTED TO DOUBLE IN SIZE OVER THE NEXT DECADE THANKS TO NEW FISCAL INCENTIVES. PRESIDENT DILMA ROUSSEFF PROPOSED A POLICY TO PROVIDE TAX BREAKS TO BRAZILIAN MANUFACTURERS, LEADING TO SAVINGS OF ABOUT 30%. THE INITIATIVE RESPONDS TO BRAZIL´S NATIONAL DEFENSE STRATEGY THAT AIMS TO BUILD UP DEFENSE PRODUCTION AND ALSO DOVETAILS WITH THE COUNTRY'S ECONOMIC DEVELOPMENT PLANS FOCUSED ON TECHNOLOGICAL CAPABILITIES. THE MEASURE IS EXPECTED TO GENERATE 23,000 DIRECT AND 90,000 INDIRECT JOBS, TWICE THE SIZE OF THE CURRENT WORKFORCE.

BRAZIL'S DEFENSE INDUSTRY — the largest of any Latin American nation — could double in size over the next 10 years, thanks to a new fiscal policy proposed by President Dilma Rousseff.

That policy will soon provide tax breaks to Brazilian defense manufacturers, giving them lucrative incentives to make new investments and acquisitions. As a result, thousands of new defense-related jobs are likely to be created. This initiative responds to Brazil's national defense strategy and dovetails with the country's industrial, technological and economic development plans.

On Sep. 29, the president signed a provisional measure that exempts the defense sector from paying the industrialized products tax (IPI), the social security tax (Cofins) and the Social Integration Program tax (PIS) for five years. This could translate into savings of 30 percent for defense companies. It's a relief for business executives who rank the tax burden along with poor infrastructure as the top impediments to growth.

"These measures are important to promote the defense sector, because the industry lacks adequate conditions for domestic enterprises to compete with foreign companies inside and outside Brazil," explained Armando Lemos, technical director for the São Paulo-based Brazilian Association of Manufacturers of Materials for Defense and Security (ABIMDE).

The measure is expected to generate 23,000 direct and 90,000 indirect jobs. This would nearly double the defense sector's current workforce of 25,000 direct and 100,000 indirect jobs, said Lemos. In all, 186 companies will benefit from the program, including industry leaders Avibras (aerospace), Embraer (aircraft), Helibras (helicopters) and Odebrecht Defesa (technology).

"While the measure is still pending formal implementation, it will define the registration criteria for strategic defense companies and detail the specific tax regime that will apply to them," said Lemos.

The 2008 National Defense Strategy document, published during the presidency of Luiz Inácio Lula da Silva and devised by former Defense Minister Nelson Jobim, was a major milestone for Brazil's defense establishment after years of neglect following the country's return to democracy. One of its primary missions was to resuscitate the largely abandoned defense industry and turn it into an efficient, competitive business capable of contributing to Brazil's international prestige and economic growth.

"Brazil's defense requires the reorganization of the national defense industry," the document explicitly states. A guideline set forth by the report to achieve this reorganization highlights the need for independent technological capacity through international partnerships — as well as the importance of subordinating commercial considerations to so-called strategic imperatives, such as a special legal, regulatory and taxation regime for the defense industry.

Since the document's publication, technology transfer arrangements have been made between Embraer and overseas suppliers to produce the KC-390 military transport aircraft. Brazil´s cooperation with France to build four conventional submarines and one nuclear submarine also includes a similar technology transfer agreement.

A key pillar of Brazil's new strategy is to bolster its defense industry, thereby ensuring that equipment needs are met by domestic companies capable of competing in external markets. That would guarantee economies of scale for production.

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NEW TAX BREAKS TO SPUR MAJOR NEW INVESTMENT BY BRAZIL'S DEFENSE INDUSTRY

IN ESSENCE, THE PLAN PUTS HOME-GROWN INNOVATION AND VALUE-ADDED PRODUCTION AT THE FORE-FRONT AND AIMS TO MAKE BRAZILIAN COMPANIES MORE COST-COMPETITIVE GLOBALLY.

"Whether owing to the size of our territory or our borders, or to the fact that our country has been blessed with enormous wealth, we need this industry because it is strategic for our sovereignty," Rousseff said following the announcement of tax breaks for the sector.

The defense industry is not alone in receiving preferential treatment.
Last August, Rousseff announced the Bigger Brazil Plan (Plano Brasil Maior) aimed at protecting domestic manufacturers from increased Asian competition and a rising currency. The pilot program supports the production of clothing, shoemaking, furniture and software by offering $16 billion in tax breaks to support innovation, investment, productivity, foreign trade, human capital, sustainable production, and small and medium size companies in these sectors.

In essence, the plan puts homegrown innovation and value-added production at the forefront and aims to make Brazilian companies more cost-competitive globally.

"We need to develop technology in Brazil in order to add even more value to our industrial production by reducing costs through tax reductions and by minimizing bureaucracy," said Labor Party Sen. Acir Gurgacz, in arguments shortly before the plan's passage in August.
Brazilian defense companies already receive some direct financial support from the federal government. For example, Optovac, which created a uranium valve for Brazil's future nuclear submarine, counts on resources from the São Paulo State Research Foundation as well as FINEP, an agency of the Ministry of Science and Technology.

According to the 2008 National Defense Strategy, the largest industrial projects of Brazil's armed forces will require investments of at least $40 billion. Addressing all military needs expands the total to about $120 billion, said ABIMDE's president, Orlando José Ferreira Neto.

Brazil's ambitious goals appear achievable. In 2010, the country was Latin America's highest defense spender at $33.5 billion, and the only one in the region to rank among the world's top 15 spenders, according to the Swedish research center SIPRI. The new fiscal incentives will help free up even more capital for investments in this sector. ■

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ARGENTINA, UNITED STATES PARTNER IN SPACE

First published by Diálogo Americas

BY JANIE HULSE*

ARTICLE SUMMARY

THE UNITED STATES AND ARGENTINA RECENTLY SIGNED A BILATERAL FRAMEWORK AGREEMENT TO ADVANCE SPACE COOPERATION. IT UPDATES AN EXPIRED AGREEMENT AND PROVIDES LEGAL GUIDELINES FOR PRESENT AND FUTURE COOPERATION. THE COUNTRIES HAVE BEEN WORKING TOGETHER IN SPACE TECHNOLOGY FOR OVER 20 YEARS AND IN JUNE 2011 SUCCESSFULLY LAUNCHED THE FOURTH OF SERIES OF EARTH-MONITORING SATELLITES. THE MOST RECENTLY LAUNCHED SATELLITE, THE SAC-D, WILL PROVIDE DATA ON OCEAN SALINITY VARIATION. THIS IS AN UNPRECEDENTED CAPABILITY THAT WILL CONTRIBUTE TO CLIMATE CHANGE RESEARCH. THE SPACE PARTNERSHIP HAS BEEN MUTUALLY BENEFICIAL BUT HAS ESPECIALLY BENEFITED ARGENTINA, WHICH HAS GAINED NATIONAL SATELLITE AND RADAR PRODUCTION CAPABILITIES AS A RESULT OF THE COOPERATION.

"THIS IS THE FIRST TIME IN HISTORY THAT WE CAN PRODUCE AN IMAGE OF SALINITY LEVELS AROUND THE WORLD," HISAS SAID. "BEFORE, WE HAD TO RELY ON PIECEMEAL MEASURES TAKEN BY BOATS."

BUENOS AIRES - The United States and Argentina have signed a long-anticipated Framework Agreement on Cooperation in the Peaceful Use of Outer Space.

The bilateral treaty, signed Oct. 25, updates a 1991 framework agreement that was extended until 1996, when it expired. Scientists in both countries welcomed the accord, which lays out guidelines and procedures to be applied to present and future cooperation in areas of common interest like Earth monitoring and exploration.

The signing follows on the heels of the successful joint launch of an Argentine satellite June 10 from California's Vandenberg Air Force Base. That marked the fourth satellite launched by Argentina's National Commission on Space Activity (known by its Spanish acronym, CONAE), together with NASA.

Since the 1990s, the two countries have collaborated in the development and launch of Argentina's SAC-series satellites, which gather data on natural resources, human activity and climate.

"Cooperation between NASA and CONAE extends back more than 20 years, when in the 1980s we began preparing for the 1996 launch of SAC-B, which was then followed -out of order -by SAC-A in 1998 and SAC-C in 2000," said Fernando Hisas, manager of CONAE´s SAC-D-Aquarius program.

"Both parties have benefited from SAC satellite collaboration, with CONAE gaining insight and capacity-building and NASA gaining an economically viable alternative to produce and operate satellites with its Aquarius technology," he said.

Hisas explained that the two satellites are now out of commission, but SAC-C is still in orbit collecting data. "SAC-C has been in orbit for 11 years and is still providing data. Its expected life span was five years so its longevity has made it a total success. We are squeezing the last drops out of it now, so to speak."

The latest SAC-D satellite -like the first SAC-C launched in 2000 -was built by the state run Rio Negro based technology company INVAP. Like its predecessor, the satellite's primary instrument, Aquarius, was built and operated by NASA.

SAC-C was focused on collecting data related to the Earth's surface. SAC-D is more geared toward oceanic properties, though it has special instruments suitable for land studies as well.

SAC-D is designed to provide monthly global measurements of sea water salinity variation at the ocean´s surface, which will lead to better understanding of water cycles and their effect on global warming. It will also be able to identify hot spots on the Earth's surface to create fire risk mapping, as well as measure soil moisture for early warnings of flooding and other natural disasters.

"This is the first time in history that we can produce an image of salinity

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ARGENTINA, UNITED STATES PARTNER IN SPACE

levels around the world," Hisas said. "Before, we had to rely on piecemeal measures taken by boats. This is a huge value-add for the scientific community and furthers our understanding of water density and movement, both important variables in climate change."

The recently launched satellite has produced its first map of global ocean salinity since becoming operational Aug. 25. The map, which can be seen on NASA's website, is a composite of the first two and a half weeks of data.

"What today is largely a scientific or environmental issue could become a global security threat if we don't take measures today to slow climate change," Hisas responded when asked about the strategic nature of this cooperative endeavor.

Argentina has advanced in aerospace research and development over the past decade, thanks in large part to its cooperation with the United States. The Kirchner governments, in particular, have promoted the expansion of the strategic sector.

"Few presidents have shown so much interest in science as President Cristina Fernandez de Kirchner," said NASA Administrator Charles Bolden, as quoted by Argentine news agency Telam. "For men of science to come across government leaders with such determination to apply science for the wellbeing of their people is always a source of inspiration."

In 2005, the late Argentine President Nestor Kirchner signed a decree declaring space technology advancement a state policy and a national priority. Subsequently, Argentina's National Space Plan 2004-15 earmarked about $240 million for investments in science and technology, with the idea of working toward the development of a South American Space Agency along with Brazil.

Like Argentina, Brazil has yet to launch its own satellites. It has suffered a number of setbacks, with its third failed launch attempt in August 2003 producing a massive explosion and killing 21 people, including many distinguished space scientists.

"The United States is to Argentina's space program what China is to Brazil's," said CONAE's Hisas. "Brazil has already launched three of its satellites from China and has another two pending."

The U.S. collaboration with Argentina does not exclude third parties. Brazil participated in both the SAC-C and SAC-D preparations by providing facilities for environmental testing before launch. France and Italy also contributed instruments to both projects, turning them into multilateral endeavors.

Argentina's space cooperation with the United States has led to the development of its own satellite and radar production capabilities. INVAP now manufactures its own earth-observation satellites -SAOCOM 1A and 1B -which will be equipped to survey Argentine farmland. CONAE is leading the effort, and has contracted the private U.S. company SpaceX to launch the first satellite in 2014.

INVAP's experience with CONAE has prepared it to develop its own surveillance radars, one of which is the country's first 3D radar. It was commissioned by the national government to support its Escudo Norte [North Shield] operation, which is focused on controlling aircraft entering and leaving Argentina's northern frontiers with Paraguay, Brazil and Bolivia - where drug trafficking is on the rise.

ARGENTINA'S NATIONAL SPACE PLAN 2004-15 EARMARKED ABOUT $240 MILLION FOR INVESTMENTS IN SCIENCE AND TECHNOLOGY, WITH THE IDEA OF WORKING TOWARD THE DEVELOPMENT OF A SOUTH AMERICAN SPACE AGENCY ALONG WITH BRAZIL.

Hisas said these spinoff projects will help generate even more satellite business for Argentina, noting that "there is always more security for a nation when it controls the production of such technologies, rather than operating foreign equipment by following an instruction manual." ■

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SPECIAL REPORT *[continued]*

– so much so that the issue of how best to ride this wave has become a major policy concern (Eyzaguirre et al. 2011).

The intensity of investor interest in the emerging markets generally, and in Latin America in particular, has been heightened by the prospect of continued lax monetary conditions in the United States, and thus by the outlook for persistently low interest rates and bond yields in the world's leading financial centres. The search for fixed-income returns higher than the 1–4% range that prevails in much of Europe, as well as in Japan and North America, has prompted bond investors to venture into increasingly risky territory, such as single-B-rated credits – Argentina among them, the country involved in the largest sovereign default in history (Moody's 2010a).

This is why, for the first time in over a decade, a number of single-B-rated Argentine corporations, plus three provinces and the municipality of Buenos Aires, have been able to issue international bonds in 2010 and so far this year, raising more than $6 billion in the 16 months to the end of April 2011 at yields mostly in the range of 8% to 12%.[1] In October 2010, an Argentine property developer (TGLT) completed the first initial public offering of shares in Buenos Aires in more than two years, with two-thirds of the $56 million in stocks sold to foreign investors as global depositary receipts. And, recently (April 2011), Arcos Dorados Holdings, the Buenos Aires-based operator of McDonald's Corp. restaurants in Latin America and the Caribbean, raised $1.25 billion (one-third more than it expected) in an initial share sale, listing itself on the New York Stock Exchange. Evidently, even equity investors are jumping on the bandwagon.

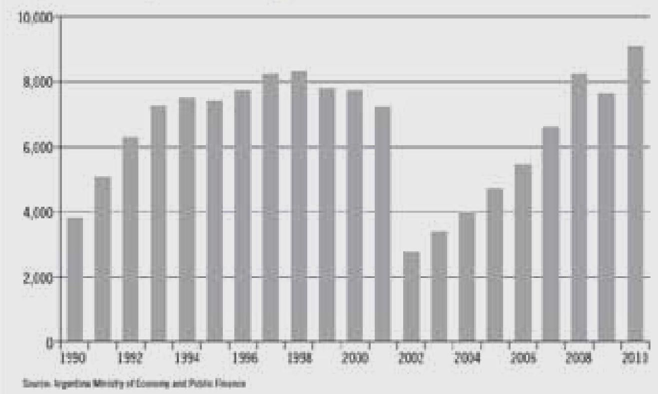
The return of Argentina to the world capital markets is a watershed event worth noting and analysing. After all, this is one of the few emerging- market countries characterised by nearly a decade's worth of capital flight measured in the many billions of dollars per annum – namely, a place from which most investors had been fleeing for safer and more attractive destinations elsewhere, much like investors have been doing (on a larger scale) in Venezuela under the populist and increasingly arbitrary President Hugo Chávez.[2] It is also a country whose national government has defaulted on its loan and bond obligations numerous times in recent decades, and, despite having failed to fully cure its 2001 default to official and private creditors, has stated its intention of returning to the international markets to issue a sovereign bond as soon as it finds it sufficiently attractive to do so. Thus, the question of whether financial intermediaries and institutional investors should welcome Argentina back to the global capital markets the way some are certainly doing is certainly relevant –especially for those with short or partial memories, who may be tempted to rush in without a full understanding of the credit, market and political risks involved.

AT FIRST SIGHT

A bird's eye view of Argentina could easily lead some to believe that it has come such a long way from its troubled past that its creditworthiness might be underappreciated by the rating agencies, and that its riskiness in fact may be exaggerated by the bond markets. After all, Argentina is a member of the G20 club of leading nations; it ranks among the top 30 economies in the world; it is a stable and peaceful democracy; and many of its main economic indicators look very healthy.

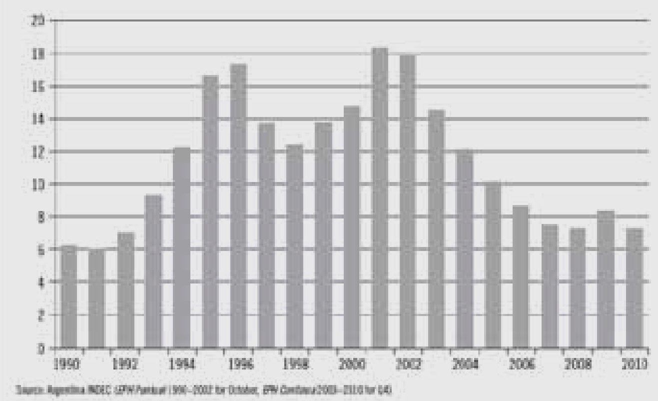
For example, Argentina's per capita income measured in current dollars, a variable that usually correlates quite well with sovereign ratings because it is a general measure of capacity to pay foreign-currency obligations, has recuperated strongly in recent years. It now stands at about $9,000 *(Figure 1)*, such that Argentina currently fits comfortably within the range of per capita incomes of developing countries that are rated BBB/Baa1– Baa3 (Moody's 2010b, p. 11).[3]

Figure 1: Per capita income (US$ per annum)



Argentina's vigorous economic recovery from the protracted and deep recession of 2000–2002 is reflected in the steady drop in urban unemployment, which has come down from above 20% and has averaged below 8% during the past three years *(Figure 2)*. These are very good levels, last seen in the early 1990s before the economy was restructured and many low value-added jobs in inefficient companies disappeared. This is another achievement that normally supports a country's creditworthiness, because it correlates with higher private-sector incomes and government revenues.

Figure 2: Unemployment rate (% as of year-end)



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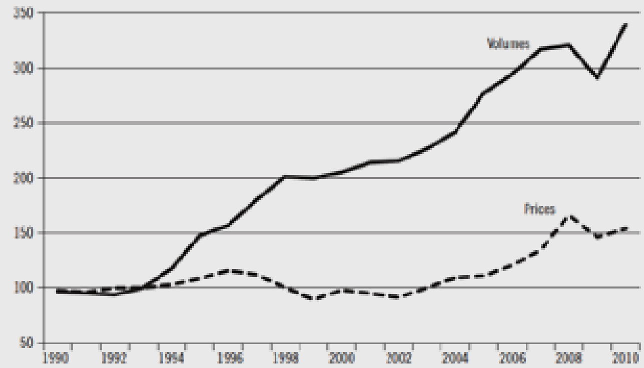
Argentina's economy has been helped by a boom in the prices of its commodity exports, stimulating greater investment and output, particularly in export-orientated agriculture. Indeed, export prices and volumes each averaged about 60% higher during 2008–2010 than in 1999–2000 *(Figure 3)*, and the country's terms of foreign trade (incorporating the evolution of both export and import prices) during 2008–2010 were the most favourable in nearly three decades.

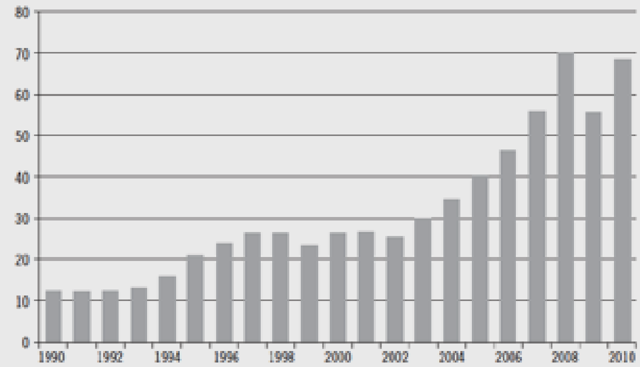
As a result, the country's merchandise export earnings have more than doubled, from around $25 billion per annum a decade ago to a yearly average of over $60 billion during 2008–2010 *(Figure 4)*. This is the kind of noteworthy expansion in hard-currency earnings that improves several of the ratios (e.g. external debt to exports) that are usually calculated to help assess a country's creditworthiness.

Figure 3: Export prices and volumes (1993=100)



Source: Argentina Ministry of Economy and Public Finance

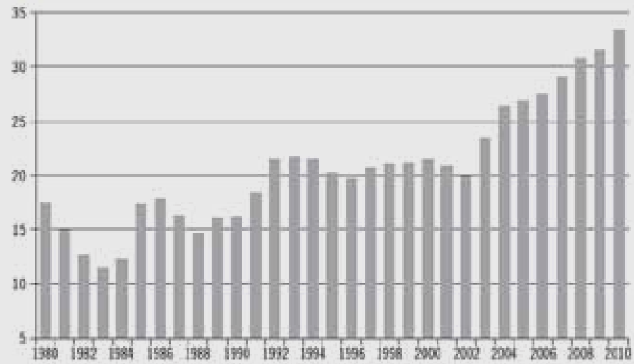
Figure 4: Merchandise exports (US$ billions)



Source: Argentina Ministry of Economy and Public Finance

The export boom has generated a significant expansion of government revenues, because commodity exports have been taxed directly, and once the export-led recovery trickled down to urban consumers, a virtuous cycle of higher private-sector incomes and enlarged government revenues and spending ensued. Indeed, Argentina has never before seen as great an expansion of government income as in recent years, such that revenues have grown to the equivalent of more than 33% of GDP from an average of around 21% of GDP in the late 1990s *(Figure 5)*.[4]

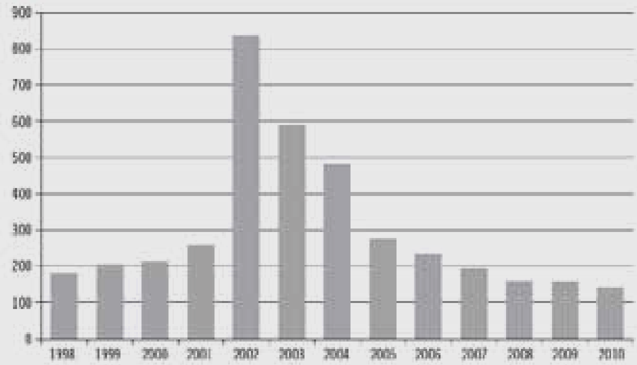
Figure 5: Government revenues (% of GDP)*



Note: *Net of tax rebates and inclusion of mandatory social security contributions and provincial revenues.
Source: Argentina Ministry of Economy and Public Finance

The fast pace of revenue growth has allowed for a massive reduction of the burden that government obligations – whether paid or in arrears – imposed on the government's revenue base *(Figure 6)*. This sovereign creditworthiness indicator, which has now dropped to around 150% from a peak of over 800% in 2002, is actually below the levels prevailing in the late 1990s, when the government's foreign-currency obligations were rated BB/BB/Ba3.[5]

Figure 6: Government debt (% of revenues)*



Note: *Includes debts that were not tendered to the exchanges of 2005 and 2010.
Source: Argentina Ministry of Economy and Public Finance

The export bonanza, which has made it possible for Argentina to run substantial surpluses in its foreign trade (averaging in excess of $15 billion per annum during 2002–2010), despite a surge in imports, has more than compensated for the previously mentioned net capital outflows. If Argentina had had a market-based exchange-rate regime, the resulting net influx of foreign exchange would have led to a meaningful appreciation of the Argentine peso. However, it has been government policy to have the Central Bank of Argentina (BCR A) intervene frequently in the currency market in order to keep the peso (ARS) weaker than otherwise. In the period from the start of 2006 to the end of April 2011, the ARS has depreciated in nominal terms by 35%, from ARS 3.03/US$ to ARS 4.08/US$, a time during which most emerging-market currencies, including those of Argentina's neighbours, have appreciated.[6]

One result of frequent central bank intervention to mop up excess

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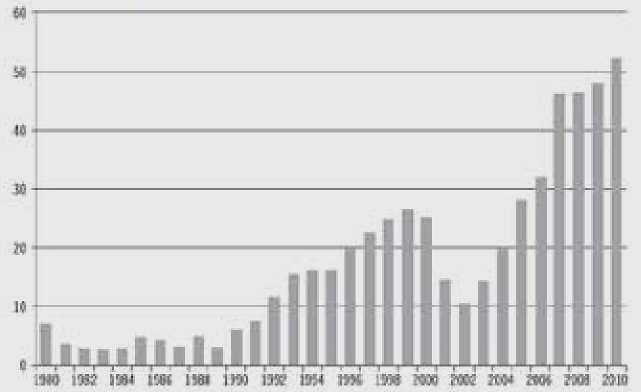
dollars coming into Argentina has been a major accumulation of official international reserves. Despite having had to transfer periodically many billions of dollars out of reserves to the government, the central bank has seen its hoard of foreign exchange boosted to more than $50 billion since mid-2010, up sharply from less than $20 billion prior to 2005. As can be seen in *Figure 7*, and as is true about its fiscal revenues, Argentina's official international reserves have likewise reached their highest point in contemporary history.

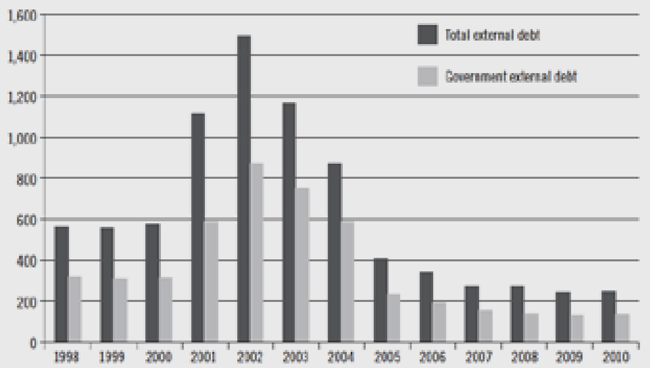
Figure 7: Official International reserves (US$ billions)



Source: International Monetary Fund

Until recent years, the country's total foreign debt, and the government's own obligations to non-resident investors, used to be a huge multiple of the central bank's international reserves. Now the country's external debt liabilities are two and a half times the level of reserves, a fraction of their magnitude even in the late 1990s (nearly six times the level of reserves), when Argentina was deemed to be a much better credit *(Figure 8)*. At these levels, the country's foreign debt is once again compatible with higher sovereign credit ratings.[7]

Figure 8: External debt (% of international reserves)*



Note: *Excludes government bonds owned by non-residents that were not tendered into the debt exchanges of 2005 and 2010.
Source: Argentina Ministry of Economy and Public Finance

A closer look There is a great deal of country risk that is not captured by these indicators, however, so it would be naive to rush to the conclusion that Argentina is a creditworthy or relatively safe place in which to invest.

First, the government has been spending all its enormous revenue windfall, such that in fact there are hardly any extra, genuine resources available to support the existing – or any new – public indebtedness. The Argentine authorities have not been publishing comprehensive data on the public-sector accounts, but whatever statistics they do release for the central government show, despite the windfall, a string of only modest fiscal surpluses during 2002-2008 and again in 2010, with a small deficit for 2009, when the economy and tax revenues went through a temporary downturn.

However, the International Monetary Fund (IMF) has been publishing a more comprehensive data set that includes provincial government finances, and where spending is recorded on an accrual, rather than cash, basis – namely, it includes all payments that are contractually due to be made by the government (IMF 2011). As can be seen in *Table 1*, the IMF's figures show a string of operating deficits and no surpluses. This is consistent with the fact that the public debt has grown from mid-2003 until mid-2010 by the equivalent of $37 billion (net of all debt forgiveness), which is equivalent to around 15% of average GDP during that seven-year period.[8]

Table 1: Fiscal accounts (% of GDP)

	2006	2007	2008	2009	2010
As per IMF:					
Public sector revenues	29.9	31.5	33.4	36.1	38.9
Public sector spending	31.0	33.6	34.2	39.9	40.6
Overall balance	–1.1	–2.1	–0.8	–3.8	–1.7
As per Argentina:					
Overall balance*	1.8	1.1	1.4	–0.6	0.2

Note: * Non-financial public sector, excluding provinces and municipalities.
Source: International Monetary Fund; Argentina Ministry of Economy and Public Finance

Therefore, the impressive trend in tax revenues to GDP, or in the ratio of government debt to revenues highlighted previously, paints a completely misleading picture of Argentina's renewed capacity to pay its domestic or foreign obligations. The growth in spending apparently has been channelled as follows: the civil-service headcount in the central government has increased by one-third from the 1999-2002 average; subsidies to consumers (mainly on energy) have increased by at least three percentage points of GDP; and other forms of social spending have likewise risen by over three percentage points. This has happened during a period of rapid GDP growth, such that all spending categories have increased to a greater or lesser extent, and government expenditures as a whole have tripled in nominal terms from 2005 through 2010.[9]

The provincial and municipal governments that have issued bonds abroad, or might do so in the near future, are all rated single-B, and all indications are that their financial situation is precarious, indeed. As a group, their financial performance has tended to deteriorate: they ran a collective overall budgetary surplus equivalent to 1% of GDP in 2004, then moved to a balance in 2006–2007, and they have been in deficit ever since. It is troubling to see them printing dollar-denominated bonds with doubledigit coupons when there is no reasonable assurance that their revenues measured in dollars will grow at double-digit rates during the life of those bonds.[10]

Second, serious allegations have been made in recent years about the

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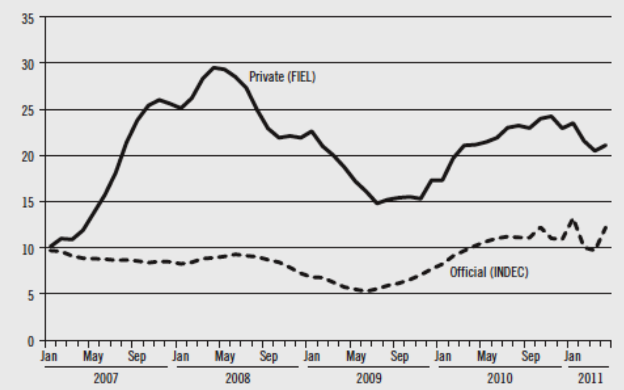
accuracy and integrity of official inflation data in Argentina, casting doubt on all kinds of economic indicators that use price indexes as a deflator, as in the case of real GDP, real wages, real interest rates and real exchange rates. Numerous private-sector estimates of inflation, as well as official inflation measures computed by several provincial governments, point to a much higher inflation rate than calculated and published by the national statistical agency. The agency, known by its acronym IND EC, was purged of key staff in early 2007, allegedly for the individuals' unwillingness to keep fudging the numbers to keep reported inflation down. Numerous economic consultants, universities and business groups have started a veritable cottage industry sampling consumer prices and calculating alternative inflation figures, although they have been persecuted and fined by the government as of late for allegedly providing misleading information.

The credibility gap has become so large that, in the IMF's leading publication, the World Economic Outlook, Argentina is the only country in the world whose inflation and GDP statistics are accompanied by a footnote explaining that the numbers cited have been challenged by private analysts. According to the government's figures, inflation in Argentina (using year-on-year monthly figures) has averaged less than 9% per annum during the period from January 2007 through April 2011. In contrast, according to the Fundación de Investigaciones Económicas Latinoamericanas (FIEL), for example, which is a highly reputable, business-sponsored economic research institute, inflation during that period has averaged more than 20% per year – a time-and-a-half difference. As can be seen in *Figure 9*, the gap between the two measures of inflation has been persistently large, and other independent estimates of inflation produced in the capital city and in distant provinces yield a statistical discrepancy that is of the same order of magnitude.

Figure 9: Inflation (% year-on-year)



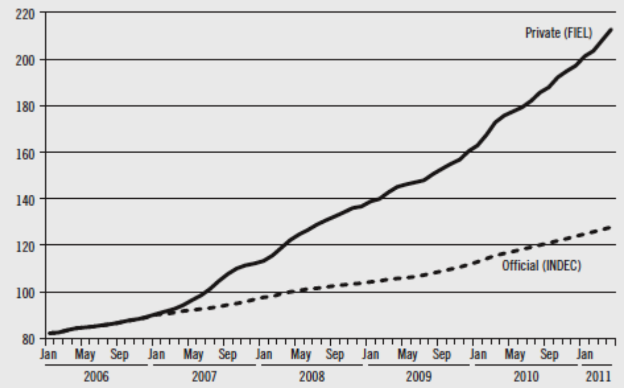
Source: INDEC and FIEL

The passage of time means that the cumulative difference in inflation statistics has grown very large: according to the government, prices have gone up by less than 50% since the beginning of 2006, but as reckoned by FIEL and several other alternative sources, prices have actually skyrocketed by almost 130% *(Figure 10)*.

The implications are serious. The Argentine authorities believe that their fiscal and monetary policies are sound and appropriate; the great majority of independent economic analysts and the IMF itself, on the other hand, disagree, and think that these policies have been highly expansionary and downright imprudent (IMF 2011, October 2010 issue, pp. 29–30). Clearly, inflation measured in single digits tends to support the government's position, whereas inflation measured continuously in double digits provides ammunition to its critics. If annual inflation is indeed running above 20%, it suggests that the government would be well advised to slow down the growth of public spending, and that the central bank should tighten monetary policy by moving away from an informal exchange-rate target, because its purchases of dollars have contributed – despite costly sterilisation operations – to an excessive monetary expansion.

Indeed, the monetary aggregates (from the narrow monetary base to the wide M2 measure) have been growing at year-on-year rates of over 30% since late 2010, well beyond what anyone would deem consistent and prudent if inflation is indeed running at the relatively slower pace the government says it is (BCR A 2011).

Figure 10: Consumer price indexes (April 2008=100)



Source: INDEC and FIEL

Inflation running at close to 10%, never mind at close to 25%, also undermines the case for regarding Argentina as creditworthy. Inflation rates have historically correlated quite well with sovereign credit ratings; in general, the higher the inflation, the lower the ratings, especially in years past when the worldwide dispersion of inflation rates was much greater than nowadays. Still, the mean annual inflation rate for investment-grade developing countries was 4% in 2009, whereas for single-B countries it was 6%; indeed, the single-B category is the only one that encompasses half a dozen countries with double-digit inflation, Argentina and Venezuela among them (Moody's 2010b, pp. 30–32). They probably belong there, because high-inflation countries are usually characterised by imprudent fiscal and monetary policies, feature unsustainable exchange rates, and tend to engender costly distortions and even social and political unrest – sooner or later.

Moreover, higher-than-officially-recognised inflation in Argentina has cheated domestic and international investors who held inflation--

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adjusted (so-called CER-indexed), peso-denominated bonds, large quantities of which were issued in 2002–2004 paying 2% plus the inflation adjustment.

In 2005–2006, before inflation allegedly escaped out of control, these inflation protected' securities accounted for more than 40% of Argentine government debt outstanding, but by late 2010 the proportion has fallen to less than 25% of the total, as investors shunned them because they realised that they would not be compensated appropriately. As investor appetite for CER-indexed debt dried up, government bonds, which pay a floating interest rate (BADL AR), have taken their place.

Third, investors must be mindful of the implications of Argentina having yet to fully cure its massive default to private and official creditors. In early 2010, the government reopened its punishing debt exchange of 2005 and a number of holdout bondholders capitulated and accepted the steep losses and new long-term bonds offered by Argentina. They had held out in the understandable hope that the country's strong economic recovery of recent years, and the government's historic revenue bonanza, would have led to an improved offer such that they would not have to renounce up to two-thirds of their principal claim.

By now, about 92% of bondholders have tendered their old, defaulted bonds, either in 2005 or in 2010, but the remainder, who are owed more than $15 billion (including accrued and penalty interest), now constitute a hard core of unpaid creditors. Many of them have won court judgments worth billions of dollars against Argentina, and are pursuing every remedy legally available to enforce them. Should the government decide to come back to the international bond markets, the creditors could conceivably attempt to block any such issuance until Argentina satisfies its outstanding judgments and, failing that, the creditors probably would try to attach any of the proceeds from the sale of new securities before they reach the government's pockets.

Argentina is also in protracted arrears to certain foreign commercial banks and suppliers, in excess of $700 million, and it has not paid on several awards for nearly $1 billion entered against the government as a result of arbitrations under the International Centre for Settlement of Investment Disputes (ICSID). Moreover, there are a number of additional cases making their way through ICSID that could result in multi-billion-dollar awards. As of early 2011, there were 27 cases pending against Argentina.

They represented more than one-fifth of all cases currently before ICSID, and a whopping 84% of all cases brought against any of the G20 member nations. All of these claims against Argentina constitute actual or contingent liabilities that could cause complications for new investors down the road, and which eventually will have to be settled one way or another. A related concern is the fact that Argentina has not cured its default on debts to the Paris Club of official bilateral lenders (export credit and foreign aid agencies, typically), who are owed more than $7 billion, of which over $5 billion is in arrears. Indeed, Argentina is the only G20 member government that is in default on its loan obligations to its fellow club members – and it has been in default to them for nearly a decade. The Argentine authorities have repeatedly stated their intention to negotiate with the Paris Club and to reach a rescheduling agreement. Until this becomes a reality, however, investors contemplating purchasing a new global bond issued by Argentina should be mindful that, if and when the Argentine government and its creditor counterparts negotiate a restructuring of these past-due amounts, the Paris Club is likely to apply its principle of 'comparable treatment' to private creditors.

For instance, when countries as diverse as Indonesia (1998), Pakistan (1999), Russia (1999) and the Dominican Republic (2004) encountered financial difficulties and reached out to their official creditors, the debt relief they obtained from the Paris Club was conditional on securing comparable relief from their bankers and bondholders. This was true even when debt to private creditors was small or was not yet falling due, as in the cases of Pakistan and the Dominican Republic.[11] Therefore, potential foreign investors in (and lenders to) the government of Argentina may well become embroiled in a restructuring of their claims as a concession to any future accord between the country and its official creditors. For all practical purposes, in sum, new creditors to the government of Argentina have a target on their back.

Fourth, the controversy over the true rate of inflation is part of a larger picture of lack of transparency in Argentina. Argentina is also the only member of the G20 that refuses to abide by its treaty obligations to the IMF, which include allowing the IMF to inspect its books and evaluate the country's economic performance and policies – especially its exchangerate policies under a so-called Article IV Consultation. The IMF is supposed to hold bilateral discussions with its member governments usually every year, but Argentina has not hosted the IMF since 2006. Apparently, the authorities in Buenos Aires do not wish to be questioned on their economic statistics – a contentious issue because countries are obligated to furnish reliable data to the IMF under Article VIII, Section 5 of its Articles of Agreement – nor to be criticised for their economic policies – including their manipulation of the exchange rate.

The country is also the only member of the G20 that was recently put on probation by the Financial Action Task Force (FATF), an inter-governmental body whose purpose is the development and promotion of policies, both at national and international levels, to combat money laundering and terrorist financing. In late 2010, the FATF plenary meeting 'expressed its disappointment and serious concern regarding Argentina's failure to implement an adequate and effective AML/CFT [anti-money laundering and counter-terrorist financing] system and will engage closely with Argentina to ensure that it quickly rectifies the identified deficiencies' (FATF 2010a). Argentina has either failed to comply, or has complied only partially, with 46 out of the 49 standards recommended by the FATF. The FATF

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complete report denounces corruption and impunity in Argentina, and is the harshest ever published by that high-level group on any of its member governments (FATF 2010b). Part of the problem may be related to Argentina's protracted default on its foreign obligations, its ongoing effort to prevent state funds from falling into the hands of disgruntled creditors, and its non-compliance with court judgments and arbitral awards. As a result, the government has had to minimise its bank accounts abroad, make payments in cash (e.g. to its own diplomats abroad), move money in roundabout ways through the international financial system, and keep as little a paper trail as possible.

However, for the most part, the problems noted by the FATF are probably explained more by the spread of corruption in government ever since Mr and Mrs Kirchner have been in the presidential palace.

Indeed, many stories of official corruption and maladministration, or of suspected illicit or improper activities on the part of government officials, have come to light in recent years in Argentina. This is something else for potential investors to consider, particularly since neither the government nor the judiciary has been keen to investigate – never mind prosecute – them. To recall just two of the most prominent episodes, the late President Néstor Kirchner used to boast that, while he had been the governor of the province of Santa Cruz in the 1990s, he had 'safeguarded' hundreds of millions of dollars of provincial funds by moving them into Swiss banks ahead of the peso's devaluation in 2002.

However, there has never been any disclosure of how much was shifted overseas, how much has been repatriated to Santa Cruz, or what happened to the earnings on those deposits abroad. In early 2010, a former vice governor of that province denounced that Mr Kirchner had stolen a portion of those funds, but various petitions for an investigation of the matter have come to nothing.

The 2007 presidential campaign of the incumbent head of state, Ms Cristina Fernández de Kirchner, was marred by the 'suitcase scandal,' which involved the arrival into Argentina of nearly $800,000 in cash carried in a suitcase by someone flying in from Venezuela on a jet chartered by an Argentine state-owned company. Several individuals connected Part of the problem may be related to Argentina's protracted default on its foreign obligations, its ongoing effort to prevent state funds from falling into the hands of disgruntled creditors, and its non-compliance with court judgments and arbitral awards. As a result, the government has had to minimise its bank accounts abroad, make payments in cash (e.g. to its own diplomats abroad), move money in roundabout ways through the international financial system, and keep as little a paper trail as possible.

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Fifth, key institutions of relevance to foreign investors have been undermined by recent governments in Argentina. Beyond the aforementioned interference with the official statistical agency (IND EC), an intimidation campaign against the country's two largest newspapers (Clarín and La Nación), and more recently the persecution of private economic consultants who are divulging higher inflation estimates, the central bank and the state-owned Banco de la Nación have been manhandled and the country's privately managed pension funds have been nationalised – all illustrating prominent instances of abuse of executive authority. For instance, in early 2010, President Fernández de Kirchner signed an executive order telling the central bank to transfer $6.6 billion to the government, and when the bank's president, Martín Redrado, refused because his legal counsel advised him that the central bank charter allowed him to transfer funds only with congressional approval, he was fired. A judge later reinstated Mr Redrado, because, according to said charter, President Fernández de Kirchner likewise did not have the power to dismiss a central bank president without congressional authorisation. In the end, the legislature approved the transfer of funds and Mr Redrado's dismissal, but the whole episode demonstrated vividly how institutions relevant to the country's financial stability and creditworthiness have been intimidated or trampled.

The country's private pension funds were nationalised in late 2008 under the guise of 'saving' them from losses related to the downturn in world financial markets in the wake of the collapse of Lehman

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Brothers. The government's initiative was duly passed by the legislature, but ever since then the pension funds have become buyers of first resort of the government's obligations, such that nearly two-thirds of their holdings consists of government bonds. The bonds they purchase carry very low interest rates, which is an expedient solution for the government, but a money-losing proposition for would-be pensioners. The nationalisation of the pension funds has therefore undermined the development of Argentina's capital markets and promises to impoverish pensioners over time. A final element is to consider where Argentina ranks according to various criteria that have some relevance to the assessment of a country's creditworthiness. For example, according to the World Bank's Doing Business 2011 report, Argentina ranks in 115th place in the 'Ease of Doing Business' category, out of a total of 183 economies. The country comes out in 87th place in the World Economic Forum's Global Competitiveness Report 2010–2011, out of a total of 139 economies. Argentina ranks in 105th place out of 178 countries in Transparency International's 2010 Corruption Perceptions Index, and in the Heritage Foundation–Wall Street Journal 2011 Index of Economic Freedom, Argentina is in 138th place, out of 179 countries.

The message conveyed by the uniformly low rankings obtained by Argentina – as can be seen in *Table 2*, on average it ranks in the bottom third of countries as per these four surveys – is that the country is a relatively unfriendly, uncompetitive, opaque and repressed place in which to invest or carry out other business.

Table 2: Argentina's ranking as per different surveys

	Argentina's rank	Total number of countries	Rank on 0–100 scale*
Doing business	115	183	39
Competitiveness report	87	139	37
Corruption perceptions	105	178	41
Economic freedom	138	179	25
Average			35

Note: * On this scale, 100 is the highest (best) score and 0 is the lowest (worst) score.
Source: World Bank, World Economic Forum, Transparency International and Heritage Foundation

CONCLUSION

In sum, does Argentina deserve to be welcomed back by investors in Europe, North America and beyond? All things considered, our answer is negative. Despite the allure of high yields, investors and financial intermediaries are well advised to approach Argentine fixed-income and equity investment and trading opportunities with extreme caution, because they still embody substantial market and default risks. Notwithstanding an impressive economic recovery, the country's ability to service its financial obligations remains quite limited, and the government's attitude towards official and private creditors, as well as towards court judgments and arbitral awards, remains one of contempt. The country is ranked uniformly low in various measures of the business climate, competitiveness, transparency, corruption and economic liberty. Therefore, Argentina – including its sovereign, sub-sovereign and most corporate issuers – is classified correctly as a very risky, single-B credit by the leading rating agencies.

Moreover, Argentina remains an outlier in the community of nations. It is the only nation in the G20 group of countries that is in protracted default on its financial obligations to its fellow club members. It is the only country in the G20 that refuses to abide by its treaty obligations to the IMF, under Articles IV and VIII. It is the only member of the G20 to have received a 'thumbs down' from the leading governmental organization that sets and monitors standards to combat transnational financial crimes. It is the G20 member with by far the most investor claims against it in the world's premier dispute resolution centre, ICSID. Argentina is, in conclusion, a risky rogue nation. ■

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1 Argentine issuers raised $676 million abroad during 2009, $4.1 billion in 2010, and $2.1 billion during January–April 2011. Banks and corporations accounted for 57% of the total raised. These data were kindly provided by Bloomberg, and are available upon request.

2 This author's estimates, based on official balance of payments data, are that net capital outflows excluding government and central bank transactions, and errors and omissions, averaged over $8 billion per annum in Argentina during 2004–2009. The Institute of International Finance estimates that capital flight ('net resident lending abroad') averaged nearly $7 billion per year during the same period. Estimates are available upon request.

3 The mean per capita income for Baa1–Baa3 developing countries was $8,100 in 2009; Argentina's per capita income is much higher on a purchasing-power-adjusted basis (around $14,000), and also falls within the Baa1– Baa3 range as per Moody's (2010b, pp. 16–18).

4 The revenue figures include pension contributions from employers and employees, but the renationalisation of the pension regime in late 2008 probably accounts for less than one-fifth of the ten-percentage-point increase in the ratio of revenues to GDP.

5 Sovereign foreign-currency ratings as per Standard & Poor's, Fitch and Moody's, respectively. Moody's downgraded Argentina to B1 in October 1999; the others first downgraded it in late 2000 (Standard & Poor's) and in early 2001 (Fitch).

6 During this same time period, for example, the Brazilian real (BRL) appreciated in nominal terms by 26%, and the Chilean peso (CLP) by 10%, versus the US$.

7 According to Moody's, the mean ratio of external debt to official international reserves for Baa1–Baa3 developing countries was 300% in 2009, and for Ba1–Ba3 countries it was 259% (see Moody's 2010b, pp. 201–202).

8 Perspectiv@as, 'La dinámica de la deuda pública en la era K', 24 September 2010, available upon request.

9 C urrent and capital outlays at the level of the non-financial public sector, excluding provinces and municipalities, was ARS 117 billion in 2005 and reached ARS 347 billion in 2010. See Argentina Ministry of Economy and Public Finance (2011), Public Finance, Table A6.1.

10 For example, in 2010 the Province of Córdoba issued nearly $600 million of dollar-denominated bonds with a coupon of 12.375%, the Province of Buenos Aires raised $800 million via bonds with a coupon of 11.75%, and the City of Buenos Aires sold $475 million of debt with a coupon on 12.5%. These data were kindly provided by Bloomberg, and are available upon request.

11 In return for a Paris Club debt rescheduling of payments due in 1999–2000 (along Houston terms), Pakistan was forced to reschedule three Eurobonds maturing during 1999–2000 even though the amounts involved were

relatively small. And, in exchange for a Paris Club debt rescheduling of some arrears and payments due in 2004 (along Classic terms), the Dominican Republic was required to reschedule a Eurobond maturing in 2006 and another one falling due in 2013 (see Porzecanski 2007, p. 202).

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