

Atradius Country Report

Argentina – January 2011



Overview

General information

| | |
|------------------|---|
| Capital: | Buenos Aires |
| Government type: | Republic |
| Currency: | Argentine peso (ARS) |
| Population: | 40.5 million |
| Status: | Upper middle income country (GDP/capita: US\$ 9,869 in 2011) |

Most important sectors (2009, % of GDP)

| | |
|--------------|------|
| Services: | 57 % |
| Industry: | 33 % |
| Agriculture: | 10 % |

Main import sources (2009, % of total)

| | |
|----------|--------|
| Brazil: | 30.5 % |
| USA: | 13.2 % |
| China: | 12.4 % |
| Germany: | 5.1 % |
| Mexico: | 3.0 % |

Main export markets (2009, % of total)

| | |
|------------------|--------|
| Brazil: | 10.7 % |
| Chile: | 7.9 % |
| China: | 6.6 % |
| USA: | 6.1 % |
| The Netherlands: | 4.4 % |

Main expenses of foreign exchange

Intermediate products (35 %), capital goods (22 %)

Main sources of foreign exchange

Agricultural origin exports (52 %), industrial exports (48 %)

Key indicators

| | 2007 | 2008 | 2009 | 2010* | 2011** |
|--|---------|---------|---------|---------|---------|
| GDP (US-\$ million) | 262,451 | 330,196 | 308,740 | 361,315 | 403,660 |
| Real GDP growth (%) | 8.7 | 7.0 | 0.6 | 8.3 | 5.1 |
| GDP per capita (US-\$) | 6,646 | 8,280 | 7,665 | 8,917 | 9,869 |
| Inflation p.a. (%) | 8.8 | 8.6 | 6.3 | 10.7 | 13.6 |
| Fiscal balance (% of GDP) | 1.1 | 1.4 | -0.6 | -1.3 | -2.5 |
| Total foreign debt (US-\$ million) | 127,758 | 128,285 | 118,379 | 128,620 | 131,101 |
| Foreign debt/GDP (%) | 49 | 39 | 38 | 36 | 32 |
| Foreign debt/XGS (%) | 175 | 146 | 169 | 152 | 140 |
| Short-term debt/inter. reserves (%) | 88 | 81 | 66 | 65 | 68 |
| Debt service ratio (%) | 18 | 14 | 15 | 12 | 10 |
| Current account balance (US-\$ m.) | 7,354 | 6,856 | 11,494 | 6,975 | 5,269 |
| Current account/GDP (%) | 2.8 | 2.1 | 3.7 | 1.9 | 1.3 |
| Nom. exchange rate to US-\$ (average) | 3.10 | 3.14 | 3.71 | 3.88 | 4.15 |
| International reserves (US-\$ million) | 43,373 | 46,112 | 45,432 | 49,763 | 51,925 |
| In months of merchandise imports | 11.6 | 9.6 | 13.9 | 12.0 | 9.1 |

* estimate **forecast

Source: Economist Intelligence Unit (EIU), International Monetary Fund (IMF)

Political situation: Some uncertainty after Néstor Kirchner's death

Head of government: President Cristina Fernández de Kirchner (since December 2007)

Form of government: Government of the Partido Justicialista (Peronist umbrella organisation)

Internal situation

The presidential election on 28 October 2007 delivered a clear victory for Cristina Fernández de Kirchner, who formally succeeded her husband Néstor Kirchner on 10 December 2007. However, since mid-2009 she has suffered several political setbacks, facing mounting opposition from within her own party ranks and decreasing popularity. After the mid-term elections in June 2009, Fernández de Kirchner finally lost her legislative majority in Congress, making governance more complicated.

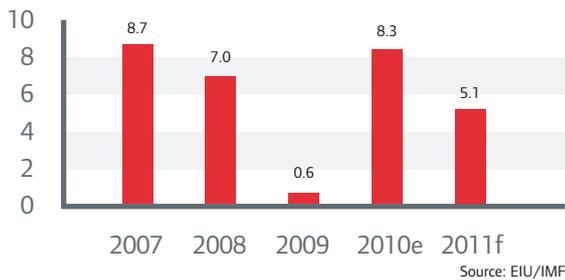
The sudden death of Néstor Kirchner at the end of October has changed Argentina's political landscape, as he was the de facto leader of the Peronist party and was also considered to be the driving force behind his wife's policy decisions and actions. It is uncertain whether Cristina Fernández de Kirchner will run again for president in the elections due in October 2011. Her political position has been definitely weakened by her husband's death, and she could be challenged by other Peronist candidates, as the party is deeply split between pro- and anti-Kirchner factions.

International relations

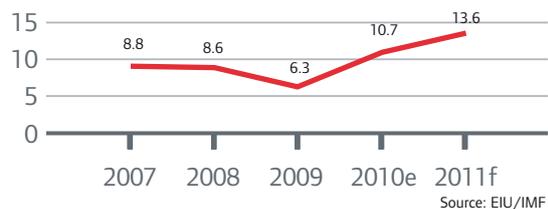
There had been tensions with neighbouring Uruguay over the construction of two cellulose plants at the Río de La Plata (the River of Silver or, as it is sometimes known, the River Plate), as Argentina feared that the plants may cause environmental damage. This conflict also hampered regional cooperation within Mercosur. The case was solved by the International Court of Justice, which, in April 2010, ruled that there was no evidence that the river has been polluted by the plants.

Internal economic situation: Strong recovery

Real GDP growth (%)



Inflation p.a. (%)



Fiscal balance (% of GDP)



General situation

In 2009 the global slowdown, falling commodity prices and reduced agricultural output (down 30 % because of severe drought) put an end to Argentina's surge in growth that had begun in 2004. Private consumption declined because of increased unemployment and waning household borrowing, and fixed investment also plummeted. GDP growth decreased to 0.6 %, according to 'official', though unreliable, data. A contraction of 2.5 % is said to be more likely.

However, in 2010, the economy recovered strongly, with GDP growth of 8.3 %, thanks to benign external conditions, record grain harvests and expansionary macroeconomic policies. Strong demand for commodities from the booming markets of Brazil and China has propelled Argentine exports. The expansive economic policy (e.g. a child support system for poor families and cheap mortgages for first-time buyers) has also contributed to the upswing, stimulating domestic demand, albeit artificially. Private consumption increased by 8 % and government consumption by 11 %. Unfortunately, the recovery has also triggered a rise in inflation since the second half of 2009, which is officially estimated to be 10.7 % for 2010, but probably exceeds 30 %. Official inflation figures have become questionable since former president Néstor Kirchner sacked the head of the official statistical office INDEC in 2007, for publishing inflation figures that - while accurate - were unpalatable.

While the Argentine banking sector is not exposed to toxic assets, general confidence in banks is low. Despite adequate provisioning and capitalisation, savers still clearly remember the peso-crisis of 2001. There is a growing divergence between public and private banks, with state banks generally in a poorer state because of increasing exposure to public sector debt.

Economic policy

Argentina's interventionist and pro-cyclical policy has led to increased state control and the current inflationary climate. The economic strategy continues to be too ad hoc and interventionist, with the government resorting to price controls, export bans and trade protectionism. Monetary policy is highly politicised. After years of decline, public sector debt stabilised at 51 % of GDP in 2010. Because of adverse international investors' sentiment and the still unresolved issue with bondholders, who boycotted a debt restructuring in 2005, the government cannot borrow freely on the international markets. To bolster public finances, government and Congress approved the nationalisation of a private pension fund worth US\$ 30 billion in 2008. A part of its foreign reserves has been transferred to the Treasury, averting liquidity problems in the public sector and possible sovereign default.

With constantly recurring fiscal deficits, due to robust public spending and subsidies to consumers, and with elections scheduled in 2011, there is a high risk that the government may turn to other public sector agencies to cover its finance gap: already, in January 2010, the president had ordered the central bank to transfer US\$ 6.6 billion of its foreign reserves to a fund to service the public debt. Fortunately, at 1.3 % of GDP, the fiscal deficit in 2010 has turned out to be lower than anticipated, thanks mainly to the economic upswing.

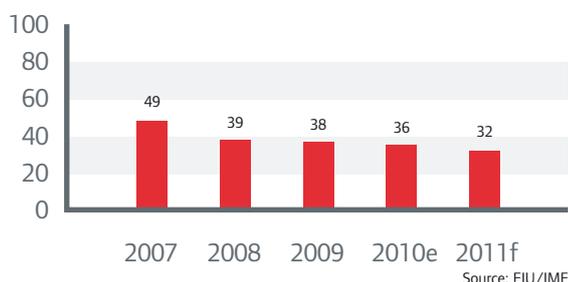
So far, structural reforms have remained minimal (banks, pension funds, energy sector, provincial/local governments). Price controls cover 70 % of items in the consumer basket, and foreign investors had already turned their back on Argentina before the credit crisis because they were not allowed to raise prices to consumers.

Energy situation

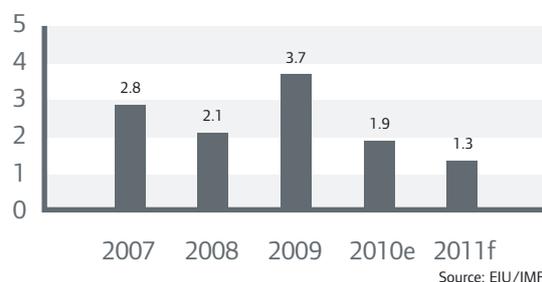
Reasonable: oil and gas deposits

External economic situation: Reasonable, but still in arrears

Foreign debt/GDP (%)



Current account/GDP (%)



Foreign debt

Level: Stable (in 2011 US\$ 131 billion – decreasing to 32 % of GDP and 140 % of exports of goods and services)

Structure: Relatively high short term share (25 % in 2010)

Debt service ratio: Declined to 12 %, including short term obligations (arrears) approximately 47 % in 2010

Remarks:

At the end of 2001, Argentina defaulted on US\$ 94.3 billion of public sector debt – mostly sovereign bonds – and, in June 2005, an involuntary debt restructuring with the bondholders was completed. US\$ 102.6 billion old debt (including interest due) was turned into US\$ 35.2 billion new debt after 76 % of the creditors accepted the deal. In June 2010 Argentina managed to restructure another swap of US\$ 12.2 billion in bonds omitted from the 2005 exchange, bringing the total amount of debt restructured to 92.6 %.

By prepaying the entire US\$ 9.8 billion of IMF debt by the end of 2005, Argentina terminated its links with that organisation. But there is as yet no solution for Paris Club arrears of US\$ 6.7 billion, and this still blocks Argentina's access to international financial markets. Without that access, Argentina faces ongoing problems in covering its external financing requirement.

As a result, the Argentine government has shown increased willingness to settle those outstanding issues as a way of regaining access to capital markets and avoiding a new sovereign default. In November 2010 President Fernández de Kirchner announced that the Paris Club had agreed to begin talks on the settlement of its outstanding debt without the IMF's supervision (a precondition demanded by Argentina), but a solution is still uncertain. Therefore, the solvency position remains, at least artificially, reasonable, despite the improved foreign debt ratios as a percentage of GDP and exports of goods and services.

Balance of payments

| | |
|------------------|---|
| Trade balance: | Large surpluses |
| Current account: | Surplus of 1.9 % of GDP in 2010 |
| Capital account: | Negative in 2008-2011 as a consequence of the unreliable business environment and the global crisis |
| Total account: | Recovering from deficits in 2008-2009, positive in 2010-2011 |

Remarks:

The economic upswing has triggered a growth in imports, exceeding the, also growing, exports of 2010/11, and causing lower trade/current account surpluses. Because of a negative capital account, with less foreign direct investment, substantial net outflows of the non-financial private sector and lack of access to commercial credit, the total balance of payments ended in deficit in 2008/09, but recovered in 2010. Argentina continues to be a highly dollarized economy.

International reserves

In months of imports (cif): Comfortable, with US\$ 52 billion (more than 9 months of import cover) in 2011

Outlook: Uncertain

Political situation

The next presidential elections are scheduled for October 2011. It is uncertain whether president Fernández de Kirchner will run again in 2011 and whether the pro- and anti-Kirchner factions within the Peronist party are able to overcome their differences.

Internal economic situation

Unreliable official economic figures point to a moderation of GDP growth in 2011 - to 5.1 % - and high inflation. Economic policy is too expansive in view of the real inflation figures of 15-20 % and the rising budget deficits. The peso is subject to ongoing real depreciation, but not strong enough to compensate for the high inflation. In the short term, the public sector will be able to meet its obligations, but a question mark still hangs over the mid-term future.

External economic situation

Argentina's sizeable international reserves (including the pension fund takeover) are a cushion against short-term rollover risks in 2011, but capital flight remains a threat. Despite the prospect of a final debt settlement with the Paris Club, the credit default swap (CDS) spreads on Argentina are still the highest in South America, and continue to bar its access to the global financial markets, including the issuing of bonds by larger Argentine corporations.

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