

Policy Brief

| *Wider Atlantic Program* |

In Brief: The government of Argentina's new president, Mauricio Macri, has many challenges ahead. In the initial 10 months of his government, he has devalued the currency, lifted significant trade and capital barriers, and launched conversations with international investors and creditors, and has changed international perceptions toward Argentina. Macri's election immediately generated a positive reaction from the private sector toward the new government. However, indicators for 2016 show a weak economy for Argentina. Most estimates expect GDP to shrink by around 1.5 percent this year. In this context, the government will have to be pragmatic in its international agenda, concentrating efforts on policies that will have a direct and short-term impact on its economy and in the consolidation of Argentina's international credibility. Africa is not on the priority radar screen for Argentina. It is not likely that one will see a structured change on the part of Argentina, seeking a special or strategic relationship with Africa or even specific countries. It may require a move from African countries to invite Argentina to tango.

Argentina's Shifting Politics: New Prospects for Collaboration with Africa?

by *Rafael Benke*

Introduction

It is commonly accepted that Argentina opened a new chapter in its history with Mauricio Macri's election as president in November 2015. His predecessor, Cristina Fernández de Kirchner, led the country for two terms following her husband Néstor Kirchner's term as president from 2003 to 2007.

Altogether, the Kirchners dominated Argentina for more than 12 years and brought it to one of its critical points in history. Their government was synonymous with strong state intervention in the economy, government interference in the private realm, international isolationism, fixed exchange rates, barriers to capital investment and trade, and manipulation of official data. Cristina's successor, Daniel Scioli, was not able to continue these policies into a fourth presidential term. Instead, Argentines voted for a change, although by a narrow margin of roughly 51.3 percent to 48.7 percent.¹ Indeed, "*Cambiamos*" ("Let's Change") was the official slogan of Macri's campaign.

1 Pablo de León, "Escrutinio Definitivo: Cuál fue la Diferencia Final entre Mauricio Macri y Daniel Scioli [Definitive Count: What the Difference was Between Mauricio Macri and Daniel Scioli]," *Clarín*, November 30, 2015, http://www.clarin.com/politica/Escrutinio-Mauricio-Macri-Daniel-Scioli_0_1477052651.html.

Macri's vision strongly contrasts to that of his predecessors. Fundamentally, he supports an economy based on market-friendly and international-integration principles; a macro structure of discipline on public spending, currency flexibility, and inflation control; and drivers for growth based on free competition, attraction of investment, exports, and productivity increases.

The new driver in Argentina's presidential seat has undoubtedly taken his country down a very different road. This road is not necessarily easier, and there are significant obstacles and adjustments involved in overturning many of the Kirchners' measures that have choked development and productivity. The country's institutional and production structures will not change overnight.

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Macri's government is a coalition of parties rather than a Peronist government,² which remains the dominant force in Argentine politics. Combined with the fact that it does not have a majority in Congress and has a weak presence in relevant provinces, the current government finds it challenging to govern. Furthermore, many of the economic reforms it says are necessary are not very popular and require public sacrifice, generating protests and rallies. This has the potential to affect the ability to move forward with an ambitious agenda of restructuring and shifting priorities in an effective and timely manner.

However, Macri has not sat on his hands. The initial 10 months of his government already has a strong record

² In its different forms, Peronism has dominated Argentine politics since its inception in 1946 (Peronist candidates have won 9 out of the 12 presidential elections).

of accomplishments, and it has changed international perceptions toward Argentina. He devalued the currency, lifted significant trade and capital barriers, and launched conversations with international investors and creditors. Early in 2016, Argentina reached a deal with debt holdout creditors who had refused to settle in the earlier 2005 and 2010 deals following the 2001 government default, earning them the name "vulture funds." This deal allowed the country to return to capital markets after isolation following the 2001 default.

These and other changes are the focus of this policy brief, including a discussion of what the changing economic environment in Argentina might mean for its international partners, including those in Africa.

Macri's Kick Off: Big Change, Big Challenges

The first 10 months of the new government have already seen fundamental changes and significant progress toward reshaping Argentina. Aside from reaching a deal with the debt holdout creditors, Macri's government has also gradually removed a series of controls on profit repatriation. Since August, it has abolished the limits for conversion of pesos to dollars. Furthermore, it reformed the National Institute of Statistics and Census (INDEC), restoring credibility in the official numbers after a long period of untrustworthy data. Other important changes include action on utility prices, an improved relationship with the private sector, and promoting trade and investment.

Updating Utility Prices

Since taking office in December 2015, Macri has begun to liberalize the utilities sector by lifting price controls and ending government subsidies for gas, electricity, and water in an effort to correct distortions. These efforts have resulted in unpopular price increases.

Argentina relies on natural gas for nearly 60 percent of its energy mix. Natural gas prices have been kept artificially low for many years, affecting companies' profit-

ability, which is compensated for through subsidies (approximately \$5.7 billion was spent in subsidies for natural gas consumption last year).

Macri's government sent a clear message that it would not tolerate this level of intervention and has moved toward significant price hikes, and has laid out a series of additional biannual 10 percent increases to reach market prices in October 2019. The price adjustments for consumers will be proportionally transferred to natural gas producers, who are also expected to receive more for their output.

The increase in prices for consumers will improve the profitability of companies across the supply chain and bring prices to market levels, but will also cause social dissatisfaction. This has already led to protests and strikes by opposition movements and labor unions, in addition to prompting lawsuits and court rulings against the measures across the country. This resistance may compromise some aspects of the reforms, but the government will continue to implement market-oriented changes, seeking to manage these tensions.

Relationship with the Private Sector

Macri's election immediately generated a positive reaction from the private sector toward the new government. National and international business leaders, investors, and analysts spontaneously sought contact with the new administration, reactivated channels of communication, and resumed their interest in analyzing trends, scenarios, and opportunities.

This new approach by the private sector was not only reciprocated by the new government but also encouraged. A fundamental pillar for the new government is to restore credibility so that international finance and investments flow back into Argentina. The government has fostered an ambitious external agenda both on the private and public fronts to build momentum.

In September 2016, for instance, the government put together the Argentina Business and Investment Forum, which attracted several hundred investors and businesspeople looking at the country's new phase and opportunities for business and investment, which mobilized international interest and positive public opinion. On the government front, the country has been visited by several heads of state, including Barack Obama, François Hollande, and Matteo Renzi; Argentine government officials have been promoting the country at roadshows around the world.

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Investment and Trade Agenda

Promoting trade and investment is on the top of the agenda; it is critical for Argentina to see investment inflows and to activate trade flows, especially exports. The above-mentioned active relationship with the private sector and international community is a clear effort to develop the "public relations" agenda. It is interesting to note, however, that this engagement is combined with concrete measures that sustain the interest of both public and private agents.

On the trade front, as soon as Macri took power, he announced the end of the infamous *Declaración Jurada Anticipada de Importación* [Sworn Statement of Intended Importation]—a restrictive and discretionary bureaucratic step that prevented imports and was being challenged in the WTO (World Trade Organization)—as well as the removal of export tariffs on beef and grains.

The government also announced a substantive infrastructure plan for 2016-19 totaling more than \$30 billion with the intention of doubling the level of infra-

structure investment in the country to 4 percent of GDP. In this vein, Minister of Transportation Guillermo Dietrich went on an international trip to attract investors, visiting Italy, Spain, Germany, the U.K., France, and China.

Simultaneously, efforts are being made in bringing predictability and enforceability to contracts and investments. On November 6, 2016, Vice President Gabriela Michetti signed a bilateral investment treaty (BIT) with Qatar during a state visit to Doha. The agreement provides investors with additional guarantees of transparency, predictability, and security regarding potential arbitrary decisions, discrimination, or expropriations.

This is a significant move given that Argentina last signed a BIT in 2001. BITs were one of the pillars of the country's foreign policy strategy to promote investments in the 1990s, but have since been neglected. Even though Argentina has BIT agreements with 58 countries (the largest number in South America), the track record of compliance with international arbitration awards to foreign companies by the previous government was not a positive one, particularly regarding the World Bank's International Centre for Settlement of Investment Disputes (ICSID). Macri has entered into negotiations for settlement of disputes with some companies in an attempt to find negotiated settlements and improve the country's image abroad. This is undoubtedly a key development for any current and potential investors.

Beyond public investment, the Argentine government estimates private and public-private investments at around \$58 billion from 2016 to 2019 as of November 2016, with nearly two-thirds being international.³

³ Ministry of Treasury and Public Finances, "Anuncios de Inversiones Consolidadas (2016-2019) [Consolidated Investment Announcements (2016-2019)," <http://www.economia.gob.ar/anunciosdeinversiones/>.

The International Agenda: Reality Check

Certain constraints will play a role in shaping Argentina's international agenda. Macri's debut clearly demonstrated an ambition for renewal, international integration, and opening to international investments. However, domestic reality is imposing itself in several ways.

Indicators for 2016 show a weak economy for Argentina. Most estimates expect GDP to shrink by around 1.5 percent this year. The government anticipates 3.5 GDP growth in 2017 and a sharp drop in inflation (to 17 percent from around 36 percent in 2016). It also estimates that the fiscal deficit will close to 4.2 percent of GDP. Independent estimates for 2017 are somewhat more conservative. The IMF predicts growth of 2.5 percent in 2017, while Moody's expects inflation

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to close next year at around 20 percent, with a fiscal deficit closer to 5 percent of GDP. On the political front, actors are now looking ahead to mid-term elections in October 2017. The economic reform agenda may advance more carefully in order to avoid electoral setbacks. At the end of the day, the new government will have to manage the tension between its reform ambitions and its popularity.

Despite the initial trade liberalizing measures described above, the international community was surprised by tax rebates between 4 and 15 percent offered to the Argentine automotive industry in exchange for producing higher local content for cars, buses, and trucks. This is a program similar to Brazil's "Inovar-Auto" currently being challenged in the WTO's dispute settlement system as inconsistent with

the WTO's subsidies rules.⁴ Of course, Argentina is in recession and the automotive sector is one of those hardest hit, with a decline of more than 12 percent in 2015 and a persistent decrease in 2016.

Analysts say these types of protective measures are the exception rather than the rule, as under previous governments, and the fundamental free-trade orientation of the new government still prevails. Certainly, the market will watch closely how frequent these measures will be, but the bottom line is that economic and political realities will play a significant role in Macri's ability to fully implement his vision.

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In this context, the government will have to be pragmatic in its international agenda, concentrating efforts on policies that will have a direct and short-term impact on its economy and in the consolidation of Argentina's international credibility. Thus, Argentina's government can be expected to continuously be looking at expanding opportunities to boost exports and at attracting international capital and direct investment.

On the trade front, this will mean a strong effort to strengthen ties with traditional trading partners, such as Brazil, and major relevant markets, including the United States, China, and the European Union. As to the latter, the Common Market of the South customs union (Mercosur)⁵ has intensified its attempt to finalize negotiations with the EU on a free trade

⁴ See "Dispute DS472: Brazil – Certain Measures Concerning Taxation and Charges," World Trade Organization, https://www.wto.org/english/tratop_e/dispu_e/cases_e/ds472_e.htm.

⁵ Comprised of Argentina, Brazil, Paraguay, Uruguay, and Venezuela.

agreement, but this has not had great traction—and likely will not in the short term—given the competing negotiation between the EU and the United States on the Transatlantic Trade and Investment Partnership (TTIP), combined with renewed focus on parochial interests and upcoming national elections in some European countries. Nonetheless, the EU-Mercosur agreement is a priority for Argentina as well as Brazil.

Beyond traditional partners, Argentina may explore opportunities with new trading partners. Although Argentina is in theory tied to Mercosur's requirement of negotiating as a bloc, both Brazil and Argentina under new governments have exchanged views on the notion of the potential "flexibility" on this rule if necessary. In June, Macri attended the Pacific Alliance⁶ summit as an observer and alluded to the idea of an agreement between the Pacific Alliance and Mercosur, highlighting the relevance of Argentina to the Alliance.

On the investment front, Argentina can be expected to seek to consolidate frameworks that ensure investment security and trust, as well as agreements expanding financing and investment opportunities. In addition to the investment agreements noted above, Michetti signed an agreement with Qatari authorities to create a \$1.3 billion joint fund to finance infrastructure projects in Argentina. The Qatar Investment Authority, a sovereign wealth fund, will invest \$1 billion, while the Argentine state pension agency (ANSES) will contribute an additional \$300 million.

Restoring international credibility is critical for Argentina. International institutions have recognized the progress made so far toward reestablishing a trustworthy political and economic path. On October 29, the OECD announced it would raise Argentina's rating to 6 from 7 (with 7 representing the highest possible level of risk, shared by countries such as Venezuela, Iran, and North Korea). Moreover, Argentina is at the initial stages of applying to become an OECD member.

⁶ Comprised of Chile, Colombia, Mexico, and Peru.

On November 9, the International Monetary Fund lifted its censure motion in place against Argentina since 2013. Also in November, the Inter-American Development Bank board approved the removal of restrictions on loans imposed on Argentina in 2014. These are key steps in the direction of improving channels with international institutions—which will eventually guarantee access to loans and cheaper financing, in addition to restoring credibility vis-à-vis foreign investors.

Argentina will continue to examine opportunities and low-hanging fruit to restore its international credibility and reputation. The country will likely be more vocal in some international fora and expand efforts to host significant regional and international summits in order to project its renewed image. A clear example is the 2018 G20 meeting, which will be hosted by Buenos Aires.

Building Bridges “to” or “from” Africa?

Africa is not on the priority radar screen for Argentina. In fact, when we observe the international agenda being unfolded by top rank government officials, Africa is not on the itinerary. The current priority is very much guided by the pragmatism portrayed above: neighboring countries, large traditional markets, and potential investors. This means that one is not seeing any changes from the previous government in this regard. The Kirchners—unlike Brazil’s Luiz Inácio Lula da Silva—have not nurtured a bilateral strategy vis-à-vis the African continent, except for circumstantial interest in a couple of countries.

In the context of Mercosur’s agreements, some possibilities exist. For example, trade relations modestly advanced with the preferential trade agreement between Mercosur and the Southern African Customs Union (SACU), which entered into force April 1, 2016. Moreover, the Egypt-Mercosur Free Trade Agreement, the Framework Agreement for Trade and Economic Cooperation with Tunisia, and the kick-off

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of negotiations with Morocco all present opportunities for expanded trade between Argentina and certain African countries.

The immediate domestic challenges in Argentina and the current focus of its international agenda will hence not be conducive for a new look toward Africa. Therefore, despite the new government, it is not likely that one will see a structured change on the part of Argentina, seeking a special or strategic relationship with the continent or even specific countries.

Furthermore, it is necessary to stress that there still prevails a stereotypical and outdated view about Africa. Not only Argentina, but also Brazil and many people in the region, still have an old-fashioned regard for Africa. For many, it was therefore surprising to hear Brazil’s new Foreign Affairs Minister José Serra saying that Africa is on Brazil’s international affairs map not as a destination for philanthropic aid, but as a region for trade and investment cooperation. This regard toward Africa is one that needs to be encouraged, and words need to be put into concrete action. African countries should not wait, however, and should take advantage of opportunities to build their own bridges across the Atlantic.

Conclusion

It is clear that the domestic challenges for Argentina are overwhelming and most of the energy will be necessarily directed toward putting its house in order.

Doing this work and actually delivering concrete results domestically is what will consolidate international confidence in the country, enable greater integration in capital markets, and make it a destination of investments. Argentina will not be able to expand much the scope of an already ambitious international agenda, but one can expect selective efforts toward countries that have the potential to generate more immediate impact on trade and investments. In this context, it does not seem that the African continent is on the top of the list.

The fact that Argentina will not be able to prioritize Africa because of the factors examined above does not necessarily mean that nothing will happen. As the old saying goes “it takes two to tango,” and a well-structured and well-conceived engagement for expanding and strengthening the ties between both regions could pave the way for fruitful relations. It may require a move from African countries to invite not only Argentina to tango, but also Brazil given its importance in Mercosur. Of course, Brazil is also entangled in equally challenging domestic circumstances. The urgent attention required by leadership on the home front may mean that significant changes will have to come from African engagement toward Mercosur.

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