

Argentina Business Forecast Report Q3 2014

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Abstracts

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Core Views

The Argentine economy is reeling following the January 2014 currency devaluation. Economic growth has slowed markedly, prompting us to revise down our real GDP forecasts, as soaring inflation discourages investment and erodes purchasing power. Despite the negative impact that the devaluation has had on the domestic economy, it has yet to pay dividends for the external account; the goods trade surplus continues to shrink relative to GDP, and we have recently revised our forecasts to account for a wider current account deficit in 2014 than was the case in 2013. Furthermore, the slowdown in economic activity has prompted a widening of the fiscal deficit, in line with our expectations, as government spending accelerates and weak growth weighs on revenues. After several weeks of stability at the ARS8.000/USD mark, monetary authorities have once again opted for a gradual depreciatory policy, returning to the crawling peg against the US dollar, broadly in line with our forecast for this year.

Politically, we are starting to see signs of strain. The perception of heightened street crime prompted incidents of vigilante justice in March and April, undermining the narrative that President Cristina Fernandez de Kirchner has presented, in which she, and her husband Nestor Kirchner before her, presided over a decade of economic expansion and social inclusion. While we expect that political pressures will not boil over into larger protests, with moderate policies and candidates gaining ascendance up to the October 2015 general election, we highlight the potential for greater social unrest as the economy slows this year and crime remains high.

Major Forecast Changes

Real GDP growth will slow to 0.4% in 2014, a downward revision from our earlier forecast of 1.2%, as the impacts of the January currency devaluation weigh on private consumption and fixed investment to a greater extent than we had originally factored in. This forecast implies a substantial slowdown from 3.0% real GDP growth recorded in 2013.

Weaker-than-expected exports in the first four months of 2014 have caused us to revise our goods trade forecast for this year, implying that the current account deficit will widen to 0.8% of GDP compared to 0.7% of GDP in 2013.

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Domestic Politics

Rising Crime Concerns Another Challenge For Fernández

Crime in Argentina has eclipsed inflation as a top concern among survey respondents recently, likely in response to a spate of vigilante justice and mob attacks carried out against alleged street criminals. We believe that this situation highlights the popular frustration with Fernández' perceived failings on security policy, and reveals an issue that will remain front and centre during the 2015 presidential campaign, likely benefiting opposition candidates.

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Long-Term Political Outlook

Significant Structural Challenges Ahead

Argentina scores above average for Latin America in our Long-Term Political Risk Ratings, but we see growing policy challenges that the country must confront over the next decade. Moreover, Argentina's increasing international isolation and the continued dominance of the ruling Frente Para la Victoria party limit policy options going forward. If the government cannot address high inflation and a weakened business environment, we believe it will likely face a sharp macroeconomic adjustment over the next decade.

CHAPTER 2: ECONOMIC OUTLOOK

SWOT Analysis

BMI Economic Risk Ratings

Economic Activity

Weakening Consumption And Investment To Drive GDP Slowdown

Argentine real GDP growth will slow to 0.4% in 2014, a downward revision from our earlier forecast of 1.2%, as the impacts of the January currency devaluation weigh on private consumption and fixed investment to a greater extent than we had originally factored in.

This forecast implies a marked slowdown from 3.0% real GDP growth recorded in 2013.

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Weaker-than-expected exports in the first four months of 2014 have caused us to revise our goods trade forecast for this year, implying that the current account deficit will widen to 0.8 % of GDP this year compared to 0.7 % of GDP in 2013. That said, we expect that the effects of a substantially weaker exchange rate, combined with stronger domestic energy production, will lead to a narrower current account deficit of 0.7% of GDP in 2015.

Table: Current Account

Fiscal Policy

2014 TO SEE LARGEST BUDGET SHORTFALL IN A DECADE

Argentina's fiscal deficit will widen this year, as the inflationary impact of the January 2014 currency devaluation and higher spending on wages boost government expenditures, at the same time as a major slowdown in economy activity depresses revenue growth. We forecast the primary budget deficit will widen from 0.7% of GDP in 2013 to 0.9% of GDP this year.

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