

Argentina Business Forecast Report Q4 2013

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Abstracts

Core Views

Data indicate that Argentina saw economic activity pick up more than expected in the second quarter of the year, raising the likelihood that we will revise up our 2013 real GDP growth forecast of 1.8% once we see data from Q213. That said, we believe over the longer term there are significant downside risks to Argentina's growth picture, as long-building imbalances both in the domestic economy and in the external accounts persist.

We forecast that Argentina's balance of payments picture over the next several years will be weaker than during much of the past decade, with the current account balance hovering around 0.0% of GDP over the next several years. This current account forecast assumes continued weakening in both goods and services exports, the result of lost competitiveness from high domestic inflation, and marks an abrupt narrowing from a current account surplus that averaged 2.4% of GDP over the past decade.

Expenditure and revenue growth trends in the first six months of 2013, along with our expectations of strong spending in advance of the October midterm election, lead us to believe that Argentina's primary and nominal fiscal deficits will be wider than we originally forecast. We have revised these forecasts for 2013 and 2014 to reflect greater deterioration in the country's fiscal accounts, and highlight that additional downward revisions are possible.

Major Forecast Changes

While we maintain our view for currency weakness, we are revising slightly both our 2013 and 2014 currency forecasts, as well as our view on how the Argentine government will manage the peso. Earlier, we had expected substantial downward

pressure on reserves to force the government into a large, one-off devaluation, but the Argentine government has instead dramatically increased the rate at which the crawling peg depreciates. We now believe continued depreciation is more likely than a one-off devaluation, and forecast an end-2013 exchange rate of ARS6.000/US\$.

Key Risk To Outlook

Risk To Real GDP Forecast: We believe that we may revise up our 2013 real GDP forecast due to stronger-than-expected growth in Q213, but many of the long-standing imbalances in the Argentine economy remain, including very high consumer price inflation, expansionary monetary and fiscal policies, and unstable external accounts. As such, we believe there is the risk of a sharp slowdown in growth over the medium term.

Risk To Political View: Fernández has proven willing to spend heavily in the run-up to elections in order to ensure support for the FPV. While such an effort over the next several months could potentially improve public opinion of her and her party ahead of the October legislative election, we maintain our view that she will not have enough political support to change the constitution and run for a third term as president in 2015.

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FPV Defeat In October To Empower Moderates

Recent polling data and the results of the August primary election reaffirm our view that the ruling Frente Para la Victoria (FPV) will lose to the opposition Frente Renovador in Argentina's midterm congressional election in October. We believe this result will ensure that President Cristina Fernández de Kirchner does not have the congressional support to amend the constitution and run for a third term, empowering more moderate political voices.

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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. 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

Stronger Q213 Poses Upside Risk To GDP

Signs indicate that Argentina saw economic activity pick up more than expected in the

second quarter of the year, raising the likelihood that we will revise up our 2013 real GDP growth forecast of 1.8% once we see data from Q213. That said, we believe over the longer term there are significant downside risks to Argentina's growth picture, as long-building imbalances both in the domestic economy and in the external accounts persist.

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We forecast that Argentina's balance of payments picture over the next several years will be weaker than during much of the past decade, with the current account balance hovering around 0.0% of GDP over the next several years. This current account forecast assumes continued weakening in both goods and services exports, the result of lost competitiveness from high domestic inflation, and marks an abrupt narrowing from a current account surplus that averaged 2.4% of GDP over the past decade.

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Regional Inflation Update: Divergent Trends In Place

Data continue to support our view for lower average consumer price inflation in Chile, Colombia, Peru, and Mexico this year compared to 2012, prompting central banks to cut rates in the first three countries in the face of sluggish economic growth. We believe Brazil's central bank will continue its hiking cycle to combat elevated prices pressures, while Argentina and Venezuela will consistently report some of the highest year-on-year price growth in the world.

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