



THOMAS WHITE - GLOBAL INVESTING
CAPTURING VALUE WORLDWIDESM



Country Profile: Argentina

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It has never been more important for you to understand what is occurring in the world beyond your country's borders. Whether you realize it or not, we are now all fellow citizens...Global Citizens.

The Thomas White organization was founded in 1992 with the goal of bringing the benefits of globalization to investors around the world. We believed that once investors understood that globalization was a positive force, they would also see the advantages of adding international equities to their portfolios. It only makes common sense that professional investors would begin searching the globe for the most attractive opportunities. Researching a wider universe of companies should improve long-term performance. Moreover, broad diversification typically lowers return volatility. Multinational corporations have been using this global strategy for years; why shouldn't investors do the same?

Now 15 years later, our firm growth and strong subsequent portfolio performance has confirmed our investment premise. Currently, Thomas White professionals are performing research and managing over one billion dollars in close to 50 countries. We believe one reason for our success is that the nationalities of these analysts are as globally diverse as our portfolios.

A handwritten signature in dark ink, reading "James S. White, Jr." in a cursive style.

Argentina: Towards Stability and Growth



This is how you do it. Argentines don't need a stage, occasion or reason to break into an impromptu tango – like this fashionably attired gentleman on a Buenos Aires sidewalk

icy glaciers, arid deserts high in the mountains, vast grassy plains and a very long coastline, Argentina is a land of incredible natural beauty. Its name is derived from the Latin word for silver, in reference to an ancient legend about a land rich in the shiny metal, somewhere up in the Andes Mountains. Early European explorers searched in vain for this mythical land. Instead, they established their very own *Provincias Unidas del Rio de la Plata*, or the United Provinces of the Silver River – Argentina's early name. They also built the fabulous city of Buenos Aires, in the image of the big cities they left behind in Europe.

Urbane people passionate about soccer, juicy beef steaks and wine, Argentines have experienced many economic swings during the last few decades, from financial crises, and hyperinflation to recessions and boom periods. The tide appeared to have turned early in this decade, when the Argentinean economy expanded rapidly. Unlike the many false dawns of the past, the recovery seemed more sustainable, as there was a significant improvement in political stability as well. However, that phase of fast growth ended with the global recession as the economy slipped again.

Though the country has since recovered, the pace of growth has been disappointing, now lagging most other emerging economies.

A history of booms and busts

Not many people have seen economic booms and busts as often as the Argentines have. During the first decade of the last century, they enjoyed the seventh highest income levels in the world – ahead of even the Germans and the French. By then, Argentina had completed nearly a century as an independent sovereign state. Buenos Aires, its capital, had well over a million

inhabitants, and was the second largest city in the Americas after New York. Europeans flocked to the city for business and in search of work, marking an indelible stamp on the culture and demographics.

The two World Wars and the Great Depression led to a dramatic fall in export demand and foreign investments, spoiling the economic fortunes of Argentina. The post-war period was marked by political instability and military dictatorships. Juan Peron, an army officer who was first elected as president in 1946 and again in 1952 and 1973, played a major part in shaping domestic policies. Economic policies during the period increasingly became inward looking and socialist, which prevented any meaningful and sustainable recovery.

Political instability peaked in 2001 when the country had as many as five presidents in just two weeks! These swift changes in political leadership followed a period of economic collapse and bloody riots in major cities. Things improved from 2003 under President Nestor Kirchner, and in 2007, his wife Christina Kirchner was elected as Argentina's first woman president.

Argentina and the World	
Nominal GDP (\$)	328.39 billion
GDP Rank	29/186
Per Capita GNI (\$)	7,200
Per Capita GNI Rank	84/210
Population Rank	31/227
Geographical Area Rank	8/249
Global Competitiveness Rank	89/134
Economic Freedom Index Rank	138/179
Human Development Index Rank	49/182
Major Industries	Food Processing, Automobiles, Consumer Goods, Textiles, Chemicals

Estancias and gauchos

Blessed with vast plains ideal for raising cattle, Argentina turned to livestock farming which fostered prosperity in the 19th century. A unique culture and lifestyle developed around the *estancias* – Spanish for ranch. The *estancias*, which included even small farms, were run by gauchos or cowboys, and continue to thrive today. More recently, the *estancias* are attracting travelers interested in experiencing traditional working ranches. For the modern tourist from the developed world, adventure sport activities have also been thrown in.



This gaucho is part of a distinct sub-culture developed around Argentina's cattle ranches, much like the cowboys of the American West. Cattle farming brought prosperity to the country in the 19th century, and remains an important industry even today.

Gauchos were wanderers or nomads roaming the plains of South America, who later settled down to run the organized farms that came up to feed the European demand for leather and later, beef. As overseas demand for meat and leather waned after the First World War, the farms went into a decline. Political instability within the country held back the revival of the Argentinean livestock industry during the second half of the last century.

Firm demand and higher prices for meat products in recent years reinvigorated the estancias and exports picked up, including to the U.S., until the global economic slowdown led to slower shipments. Though Argentina remains the third largest beef exporter globally, the gap with leader Brazil has widened. Unfavorable government policies, like the 2006 ban on beef exports to fight domestic inflation, remain the biggest challenge for the industry. The beef export ban was later replaced by a quota system which continues to restrict export volumes. Lower domestic prices have led to an increase in domestic consumption since the export restrictions and Argentineans, who devour more than 150 lbs of beef on average every year, remain the biggest consumers of beef in the world.

Mendoza – Argentina's Napa valley

When Wine Spectator, one of the most influential voices in the wine industry, rated an Argentinean wine 95 out of a possible 100, wine aficionados were not surprised. South American wines have been in the forefront of the 'new world wine' wave. Among South American origins, Chile has been the major exporter, but Argentina is fast catching up.

Argentina is often called the sleeping giant in the global wine market. The country boasts of the greatest land area suitable for wine growing, most of it in the Andes mountain valleys. High-altitude growing imparts uniqueness to Argentinean grapes, like Malbec and Torrontes, an attribute which many vinerias in the region have now started exploiting. Yet, though it is the fifth largest wine producer in the world, it exports only 10% of its production.

Mendoza, in west-central Argentina, is the undisputed wine capital of the country. With more than 800 wineries, the region accounts for nearly 80% of total wine production. Mendoza has vineyards at altitudes as high as 1,400 meters above sea level.



From near obscurity a decade back, Argentinean wines now occupy pride of place among New World wines and are enjoyed the world over.

Annual wine exports from Argentina now exceed \$600 million and the U.S is the biggest customer, accounting for nearly 30% of exports by value. It takes, many years to develop superior wines and the relatively improved political and economic conditions compared to the past should encourage

Argentinean winemakers to take a longer term view and increase investment in vineyards. With demand for wine growing globally, the Argentinean wine industry holds a quite a bit of promise.

Political instability and restrictive policies hinder economic growth

Argentina's journey from one of the richest countries less than a century ago to a nation currently struggling to measure up to its fast growing neighbors in Latin America is a story of misguided government policies and wasted opportunities. Blessed with copious natural wealth, relatively thin population density, strong social infrastructure and a long history of agricultural and industrial development, it may seem improbable that consistent growth still eludes the Argentinean economy. However, recurrent political instability throughout its modern history prevented the development of sound economic policies. During the intermittent spells of political calm, the development policies and programs were overtly populist, and did more harm in the long term.

The first wave of development happened towards the second half of the 19th century when increased export demand led to the establishment of immense livestock ranches and commercial farms. Large scale migration from Europe before the Great War ensured a steady supply of labor, essential for farm development. The country subsequently expanded its export basket to include corn and wheat, which eclipsed meat exports by the first quarter of the 20th century.

Large capital inflows, initially from Britain and subsequently from the U.S., facilitated the modernization of the farm sector and industrialization in the country. In the absence of domestic capital and credit, foreign investments financed the development of the meat packing industry and the railway network. Meanwhile, increased urbanization pushed up domestic consumption which became the primary driver of economic growth.



Argentina's hydro-electric potential is vastly under-exploited and may hold the key to the country's future energy security.

Foreign investment flows dried up after the Second World War and the Peron government, which came to power after the War, nationalized most of the economy. These policies remained for the next several decades and stifled long term economic growth. To make matters worse, the second half of the 20th century was a period of heightened political instability in Argentina. Several governments were brought down in military coups and the uncertain environment hampered the overall development of the country. After political stability returned in 2003, the country saw average growth of close to 9% for the next few years. However, Argentina was one of the worst hit in South America by the global recession in 2008 and the recovery came slower and weaker than most of its neighbors.

Though Argentina's economy has performed below par for the last several decades, its strengths and potential for growth are evident. It is largely self sufficient in food and energy. Only a small portion of its land area is under cultivation or livestock farming, which can be expanded with supportive government policies. Argentina relies heavily on

natural gas which accounts for the bulk of domestic energy consumption. The country has the third largest reserves of natural gas in South America, but output has stagnated because of underinvestment. Most of Argentina's electricity demand is met by gas-fired thermal plants and hydroelectric plants. With only 20% of its hydroelectric potential exploited, the country can meet much of its future electricity demand by increasing investments in new hydroelectric plants.

Policy inconsistency and concerns about poor economic governance have long affected investor perceptions about Argentina and have restricted capital inflows into the country. Successive Argentinean governments have always been ready to indulge their domestic constituencies at the cost of consistent economic policies that are crucial to ensure long-term growth. Extended

periods of political instability have also contributed to the country's poor record in economic management, as the government turned more populist to gain political advantage. Efforts to build and nurture independent economic institutions were undermined by politically expedient decisions for short-term gains. In the most recent of such instances, the country's central bank chief was forced to resign for resisting the government's decision to utilize part of the exchange reserves for debt servicing. Unless Argentina can build investor confidence in its economic institutions by freeing them from political pressures, it will continue to lag its regional competitors like Brazil in the ability to attract foreign capital.

The debt default that initially helped, but hurt later

Sovereign countries usually do not refuse to honor their debt obligations. Defaulting countries will be shut out of global credit markets and raising external finance will be extremely difficult in the future. Even then, Argentina did not have much of a choice but to default on its debt repayments to international creditors in 2001. The government's finances were so bad that it could not have made the repayments even if it wanted to, as the IMF refused to provide additional loans. At over \$90 billion, it remains the biggest ever sovereign debt default in history.

Three years later, Argentina offered to pay its creditors 30 cents to a dollar on total debt, which had increased to \$103 billion including interest. More than three-fourths of the investors accepted the offer, as they saw no other way out, though some investors held out and challenged the settlement in U.S. and European courts. Though at a painful cost to its creditors, the debt restructuring helped Argentina significantly. As the total external debt declined after the default, lower demand on government finances for debt servicing helped improve fiscal health and supported economic growth.

However, the debt default and the recovery suits filed by the remaining creditors made it impossible for Argentina to raise money from international financial markets. Before the global recession, when domestic tax revenues were buoyant, this was not a major concern for the Argentinean government. But as the economy slipped, government finances also suffered and the fiscal deficit soared.

As the country's debt servicing needs are set to rise in the coming years, and domestic sources are unlikely to meet the requirements fully, Argentina may have to raise funds from the international markets. To this end, the Argentinean government has made a new offer to the holders of defaulted bonds. If the new proposal is accepted by a majority of the bond holders, Argentina's long exile from international financial markets will end. The government's controversial plan to set aside a part of its foreign currency reserves for debt repayment is aimed at reassuring international investors and encouraging them to subscribe to new bond issues.

Trade ties that bind, though often fractious

South American countries have deep economic relationships among themselves and hence their economic cycles often follow the same trends. For instance, Brazil, South America's largest economy, accounts for 31% of Argentinean imports and 19% of exports. Bilateral trade between Brazil and Argentina now exceed \$30 billion annually. Neighboring country Chile is the fourth biggest importer of Argentinean goods, with a 7% share.

A decade ago, trade between South American countries was even more important, which led to the formation of the regional trade group Mercosur. However, increasing demand for minerals and farm products in other parts of the world has led to a decline in the importance of trade within the Mercosur group. In the case of Argentina, exports to other Mercosur countries have steadily declined over the last decade. China has emerged as Argentina's second biggest trading partner, followed by the U.S. Though the Mercosur member countries are now less reliant on each other for trade, total trade in absolute terms within the group continued to expand until the 2008 global economic decline. As the regional economies emerge out of recession, growth in trade between them should also revive.

Efforts are being made by member countries to strengthen Mercosur, through further liberalization of trade between member countries, improving market access, and trade agreements with other countries. More countries may be added to the group, which currently has five full members and five associate members. After the formation of the Mercosur Parliament next year, observers feel the trade block can develop along the lines of the European Union template.



The recession affected demand for luxury goods and shopping malls like this one in Buenos Aires are attracting fewer visitors. However, retailers are hopeful that the mostly urban population will again throng the shopping centers as the economy revives.

However, the relationship between countries in the region has often turned fractious and has led to trade disruptions. Most recently, a trade dispute between Argentina and Brazil caused a sharp decline in bilateral trade. To protect domestic manufacturers hurt by the global recession, the Argentinean government imposed restrictions on imports and Brazil responded by preventing Argentinean trucks carrying farm produce from entering their territory. Realizing that trade disputes are harmful to the interests of both nations, Brazil and Argentina have agreed to resolve the problems and promote more trade and economic integration.

Candies to online auctions

Most Americans wouldn't suspect that the candies they crave for are probably made in Argentina. They could be, as the largest Argentinean confectionery group is a leading supplier to large American retailers and a contract manufacturer for some well-known American brands. With a history of more than 50 years, Arcor Group has manufacturing plants in five countries and sells its products in more than 120 countries across the globe. It manufactures more than 1,500 different products and launches over a 100 new products every year.

Such success stories in non-traditional businesses are rare in Argentina, where commodity businesses thrive. Like neighboring Brazil, Argentina is a significant producer and exporter of farm products which remain the mainstay of the economy. Exports include soybean, vegetable oils, and cereals. Higher international food prices contributed significantly to the country's economic growth, until the 2008 global recession led to weak export demand. To make it worse, the Argentinean government imposed export taxes on several farm products to improve their domestic availability and control inflation. This policy led to widespread protests by farmers and farm produce exports suffered. More recently, the global economic recovery lifted demand for agricultural produce, and prices became more remunerative. Increased revenues from farm produce exports, especially soybeans, will likely drive the country's economic prospects.

As well, Argentina is a large exporter of copper and gold concentrates. Other mineral resources include lead, zinc, tin, iron ore, and manganese. American and Canadian companies have a large presence in the domestic mining industry. The upstream oil industry in Argentina was dominated by a state-owned firm, which was later privatized and subsequently merged with a Spanish oil company to become Repsol-YPF.

With changing global trends, Argentinean businesses are also evolving. Good education standards have helped the country emerge as a favored destination for outsourcing, largely comprised of call centers offering services in Spanish. Several global technology companies, including Microsoft, IBM and, HP, have back-office operations in Buenos Aires now. More recently, the country is attracting outsourced creative work, including graphic design and

entertainment software. Such service businesses are estimated to have created tens of thousands of jobs and now generate annual revenues of billions of dollars.

Yet, the enterprise which should represent Argentina today and inspire its young citizens is a



Commemorating the 400th anniversary of the founding of Buenos Aires, El Obelisco or The Obelisk was built in a mere 31 days. As the most recognizable monument in the city, the Obelisk stands tall as an icon of Argentina's many rebirths and revivals. Argentina - vivacious, full of possibilities, and always hopeful.

young technology company. Its founder was still in business school when he volunteered to chauffeur a well-known investor, in order to make a pitch for venture capital to start his own business. His company, MercadoLibre, is now the largest online auctioneer in Latin America and is listed on the NASDAQ. MercadoLibre has more than 25 million registered users, spread across 12 countries in the region. If Argentina can build the right economic environment for more firms like MercadoLibre to thrive, the country's below par economic performance will be history.

Young, vibrant, adventurous, and full of life – that is the image the world had of Argentina. Unfortunately, the reality behind that colorful mask has often let the country and its citizens down. To bury the disappointments of the past and regain its glory days, the country has to work hard, strengthen its institutions, and rebuild confidence. However, unlike in the past, Argentina may not get several more opportunities for revival and growth. With several countries in the region quickly recovering from the global recession and now starting to grow at a good pace, Argentina cannot afford to fall behind. If it does, the country risks that the label of a perennial laggard will forever remain. 🌐

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