

Economic Watch

Argentina

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Economic Analysis

Emerging Markets

Argentina

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The challenge of competitiveness

The automotive sector has driven manufacturing competitiveness since 2002, but there are questions about the future of Argentine competitiveness

- **Argentine exports grew at a good rate between 2002 and 2012, averaging 20.4% of GDP in the last decade, but they reached a ceiling in 2011**

They have grown since 2002 driven by a “competitive” real exchange rate, rises in labor productivity, and a major terms-of-trade shock, especially in primary goods, since industrial manufactured goods were the fastest growing exports by quantity, driven by the automotive industry. However, measured in current USD, they reached a ceiling in 2011 and have fallen in GDP terms over the last few years.

- **Several competitiveness indicators show Argentina as performing well in relative terms between 2002 and 2012, although with a certain impairment in its competitiveness in the last few years**

The Revealed Comparative Advantage shows that Argentina has a comparative disadvantage with the rest of the world in exports of non-basic manufactured goods, but a comparative advantage in basic manufactured goods, and has gained market share in its main manufactured products since 2002. By number of products exported, diversification has dropped slightly while by markets it has grown. Furthermore, it has increased the weight of exports of mid-range technology manufactured goods.

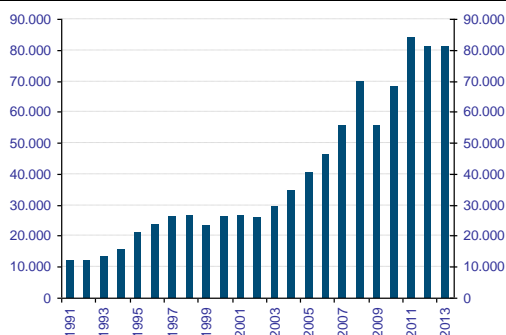
- **Sustained rises in labor costs and real currency appreciation, together with structural limits on competitiveness such as the lack of infrastructure and impaired business climate, are a concern for the future**

Real salaries have grown continually in Argentina since 2003, generating constant increases in labor costs (partially offset by productivity gains), and increasing inflation has meant that the real exchange rate has continued to appreciate. As well as these temporary factors there are other, structural, ones such as low infrastructure quality, impaired business climate, exchange rate restrictions limiting foreign investment and external borrowing, and conformism with Mercosur, as reflected in the absence of significant new trade deals. As a result, Argentina is facing the major challenges of improving the competitiveness of its economy and promoting exports in the next few years.

Does Argentina have a competitiveness problem?

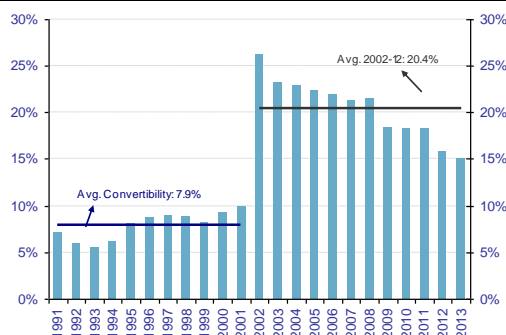
The Argentine economy has grown at an average rate of 5.1% between 2003 and 2013, a high rate of expansion both in terms of Argentina’s own history and in comparison with the rest of the world. Argentine exports were not excluded from this growth process, growing in dollar terms at a compound annual rate of 11% between 2002 and 2013 (Chart 1). This works out as an average of 20.4% of GDP over these 12 years, well above the average of 7.9% of GDP in the 11-year currency board period between 1991 and 2001 (Chart 2).

Chart 1
Exports (in current USD)



Source: Indec and BBVA Research

Chart 2
Exports (% GDP)



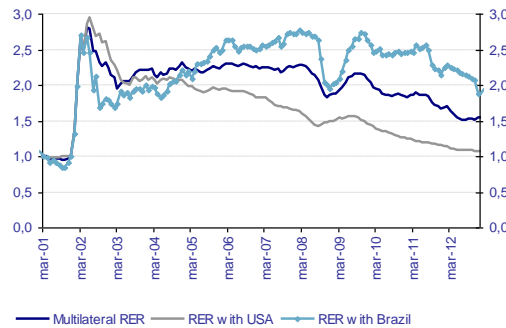
Source: Indec and BBVA Research

This growth in Argentine exports has been attributed by some analysts¹ to a more competitive real exchange rate. However, although it is true that after the currency board system collapsed at the beginning of 2002 the real exchange rate jumped to a more “competitive” (depreciated) level and stayed at those levels for around five years, rising inflation has gradually eroded these competitiveness gains via prices (Chart 3). As a result, exports measured in current dollars appear to have reached a ceiling in 2011 (Chart 1).

This has shown in the fall in exports-to-GDP ratio in the last few years (Chart 2), particularly in manufactured goods (basic and non-basic), although we also need to bear in mind the denominator effect (since GDP grew at a good rate over the period) and, more generally, in the gradual loss of the current account balance since 2002.

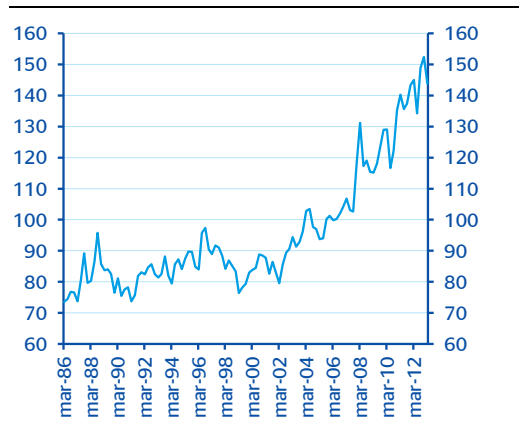
¹ Roberto Frenkel and Martín Rapetti (2008), “Five years of competitive and stable real exchange rate in Argentina, 2002–2007”, *International Review of Applied Economics*, Vol. 22, No. 2, March, pp. 215–226.

Chart 3
Bilateral real exchange rate with US & Brazil and real effective exchange rate (2001:12=1)



Source: BBVA Research

Chart 4
Terms of trade (2004=100)



Source: Indec and BBVA Research

What is more, if we consider export performance in terms of prices and quantities (Table 1), we see that from 2002 and up to 2012, the 12.2% compound annual growth of export value (+215% over the entire period) is accounted for, in the main, by an annual price hike of 9.6% (+149% in the whole period), while export quantities only went up by 2.4% (+27% over the period). By export category, Primary and Agro-related Manufactures essentially grew by the increases in the prices not in quantities, while Fuels and Lubricants had price rises but falls in their quantities over the period. The only category with similar growth in both prices and quantities was Industrial Manufactures. Thus it is clear that several external factors have also played an important role in Argentina's export performance and that the Terms of Trade favored Argentina a great deal between 2002 and 2012, rising 70% over the period (Chart 4).

Table 1
Exports annual average growth in value, price and quantities between 2002 and 2012

| | Total | Primary Products | Agro-related Manuf. | Industrial Manuf. | Fuels & Lubricants |
|-------------------|--------------|-------------------------|----------------------------|--------------------------|-------------------------------|
| Prices | 9,6% | 10,1% | 9,8% | 6,7% | 16,2% |
| Quantities | 2,4% | 3,1% | 2,9% | 6,6% | -10,5% |
| Value | 12,2% | 13,7% | 12,9% | 13,7% | 4,0% |

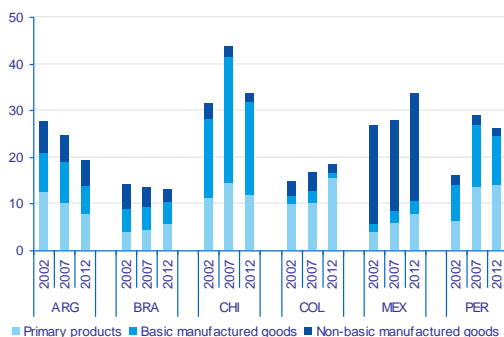
Source: Indec and BBVA Research

Given all this, the question is: how has Argentina's competitiveness fared in the last few years? And, with an eye to the future, does the country have a competitiveness problem, in particular in the manufacturing sector? In this Economic Watch we will try to provide some answers to these questions.

Argentina in its regional context ²

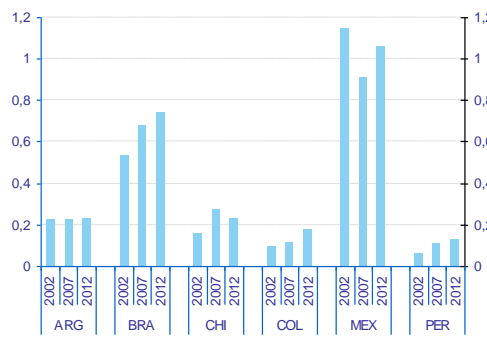
Latin America's economic growth in the last decade (3.7% average YoY), significant in historical terms and in comparison with other regions, has been accompanied in many countries of the region by the appreciation of real exchange rates, higher wages and tax raises. This has caused increasing concerns about a possible loss of manufacturing competitiveness in the region's economies. However, the weight of primary product exports as a proportion of GDP increased in practically all countries between 2002 and 2012, to a large degree because of historically high raw material prices, but this raw material push has not been able to generate a significant increase in the exports-to-GDP ratio in the last decade, with the exception of Peru and Mexico. This occurred mainly because the weight of non-basic manufactured goods (less intensive in primary resources) has fallen in all countries apart from Mexico (Chart 5). In terms of basic manufactured goods exports, more intensive in primary resources, their weight in GDP has dropped in some countries (Argentina, Brazil and Colombia) and increased in others (Chile, Mexico and Peru), although in all cases it has gone up in absolute terms at high rates since 2002. Where we certainly can see gains across the board throughout the decade is in the country shares in the world market, given that most countries in the region have kept or increased their participation in world exports between 2002 and 2012 (Chart 6). Given all this, an analysis of competitiveness in Latin America in the last few years is an important exercise.

Chart 5
Latin America: Exports (% GDP)



Source: WITS and BBVA Research

Chart 6
Latin America: Total Exports/World Exports (%)



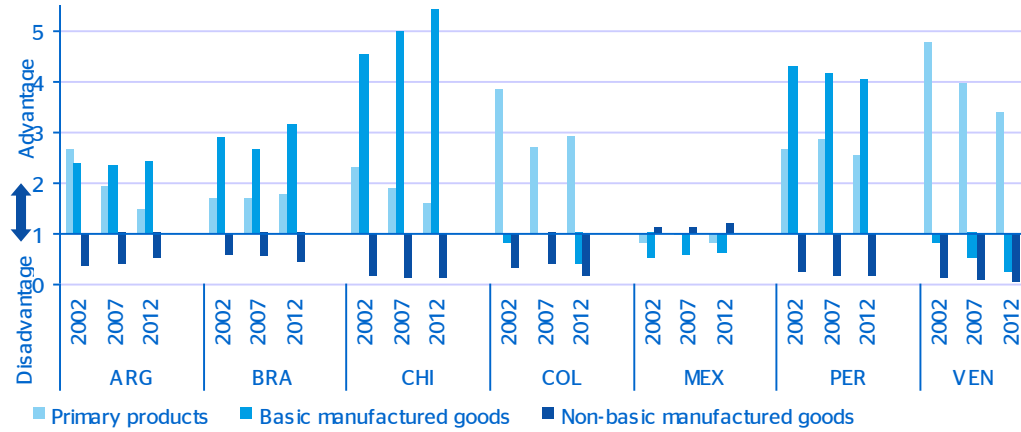
Source: WITS and BBVA Research

One way of answering this question is by analyzing the Revealed Comparative Advantage (RCA), a standard competitiveness indicator which is calculated as the ratio between the participation of a given sector in a country's exports and the participation of this same sector in world exports. Thus, an RCA above 1.0 indicates that the country has a relative advantage in this sector, since its weighting in the country is higher than the world average. This indicator shows (Chart 7) that all the countries in the region, with the exception of Mexico, have a comparative disadvantage in exports of non-basic manufactured goods; in basic manufactured goods exports, on the other hand, performance is more varied, with some countries having a comparative advantage (Argentina, Chile, Peru and Brazil), and others with a relative disadvantage (Colombia and Mexico).

² This section is based on Working Paper Nº 14/10 by BBVA Research "Competitiveness in the Latin American manufacturing sector: trends and determinants", March 2014, available in <http://www.bbva.com/BBVAResearch/KETD/ketd/ing/nav/geograficas/latinoamerica/index.jsp>.

Chart 7

Indicator of Revealed Comparative Advantage (RCA) by groups of products



Source: WITS and BBVA Research

If we look at the Revealed Comparative Advantage data for Argentina more closely by sector (Table 2), the revealed relative advantage is apparent and the high percentage of the total exports in some primary sectors (animal and plant products), some Manufactured goods of Agricultural Origin (Fuels, Hides and Skins), as well as the growth in Revealed Comparative Advantage and the weight in total exports of “Transport equipment” between 2002 (RCA: 0.51, when it showed “relative disadvantage” and represented 6% of exports) and 2012 (RCA: 1.56, now showing “relative advantage” and representing nearly 13% of all exports).

Table 2

Argentina: Revealed Comparative Advantage, % of total exports and annual growth, by sectors

| Argentina | RCA | | | % of total exports | | | Annual growth* | |
|--------------------------|------|------|------|--------------------|------|------|----------------|---------|
| | 2002 | 2007 | 2012 | 2002 | 2007 | 2012 | 2002-12 | 2007-12 |
| Animal products | 3.4 | 4.1 | 3.4 | 7.0 | 6.9 | 5.5 | 8.5 | -0.6 |
| Vegetable products | 9.6 | 12.2 | 9.6 | 24.5 | 30.8 | 28.2 | 12.9 | 2.3 |
| Food | 5.0 | 6.4 | 6.7 | 15.0 | 16.9 | 18.7 | 13.8 | 6.3 |
| Mineral products | 2.4 | 1.8 | 1.6 | 1.8 | 2.6 | 3.0 | 16.9 | 6.7 |
| Fuels | 2.0 | 0.9 | 0.5 | 18.4 | 11.8 | 8.4 | 3.0 | -2.7 |
| Chemicals | 0.6 | 0.6 | 0.9 | 5.6 | 5.6 | 7.7 | 14.9 | 11.0 |
| Plastics and rubber | 0.8 | 0.6 | 0.6 | 3.2 | 2.7 | 2.4 | 7.9 | 1.6 |
| Leather and furs | 4.0 | 3.4 | 2.4 | 3.4 | 2.1 | 1.3 | 1.3 | -4.8 |
| Wood products | 0.5 | 0.6 | 0.5 | 1.9 | 1.7 | 1.0 | 4.7 | -5.9 |
| Textiles | 0.3 | 0.3 | 0.2 | 1.6 | 1.0 | 0.8 | 4.4 | -0.2 |
| Footwear and Headgear | 0.1 | 0.1 | 0.1 | 0.1 | 0.1 | 0.1 | 11.5 | 0.0 |
| Stone and glass | 0.2 | 0.2 | 0.8 | 0.4 | 0.4 | 2.9 | 34.7 | 51.9 |
| Metals | 1.0 | 0.5 | 0.5 | 6.0 | 4.7 | 3.5 | 5.6 | -1.5 |
| Machinery and electrical | 0.1 | 0.1 | 0.1 | 3.1 | 3.2 | 2.6 | 9.3 | -0.2 |
| Transport equipment | 0.5 | 0.9 | 1.6 | 6.0 | 8.6 | 12.9 | 20.2 | 12.8 |
| Rest | 0.2 | 0.1 | 0.1 | 1.5 | 0.8 | 0.4 | -1.3 | -7.8 |

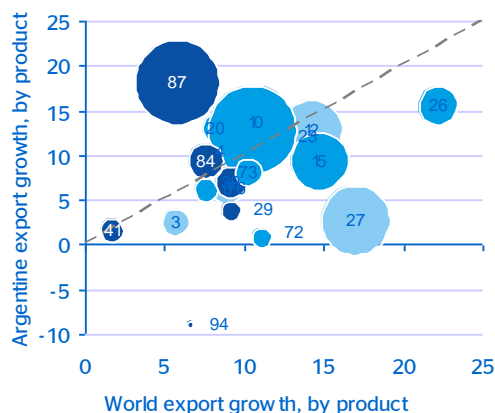
* Compound YoY annual growth rate

Source: WITS and BBVA Research

Another relevant competitiveness indicator is the loss or gain of world share the country has experienced in the different products it exports. In order to assess it, the growth rate in exports of a product in the country is compared with the average growth of that product. The data show that Argentina has gained market share in its principal manufactured goods products in the decade between 2002 and 2012, although there has been a degree of impairment in the last five years, with

the main exception of transport equipment - the country's main non-basic manufactured good - which has continued gaining world share (Chart 8). In comparison, we also show the case of Brazil (Chart 9), a country where exports have grown above world averages in the vast majority of products.

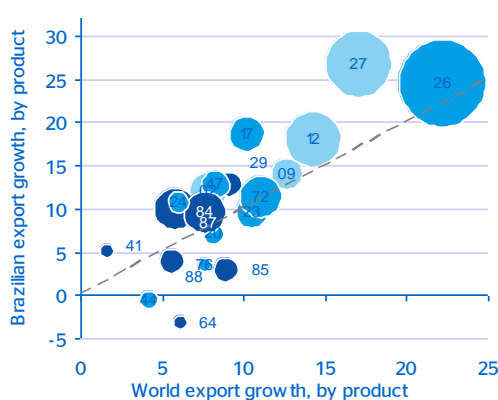
Chart 8
Argentina: main exported products, YoY growth (%) between 2007 and 2012*



* The bubble size shows the share of the product (identified by two HS 2002 classification digits) in the country's exports and colors classify the products by: ● Primaries, ● Basic manufactured goods, ● Non-basic manufactured goods. Above the 45° line, product exports have grown more in the country than in the world and the country has increased its share of world exports.

Source: WITS and BBVA Research

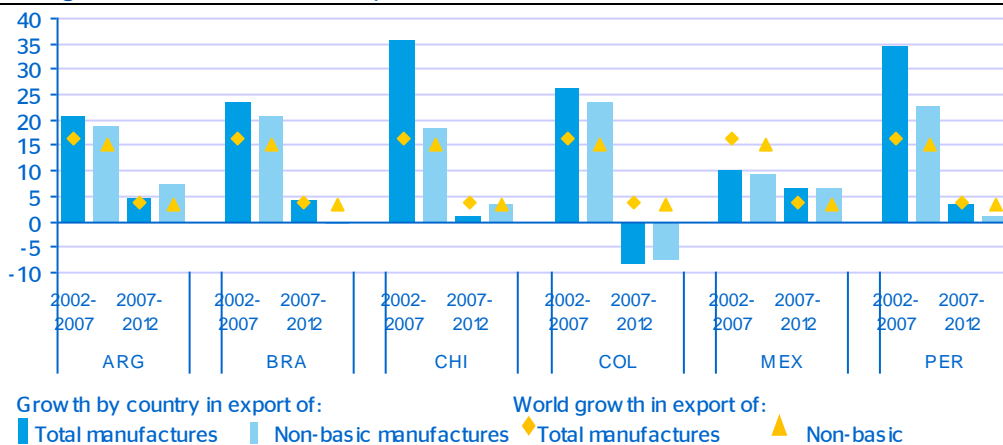
Chart 9
Brazil: main exported products, YoY growth (%) between 2007 and 2012*



Source: WITS and BBVA Research

If we analyze manufactured goods products (basic and non-basic) for the region as a whole (Chart 10), most countries had growth rates above the world average in the first half of the decade, and below or practically the same in the second, which suggests competitiveness gains in the first few years and subsequent deterioration. An important exception to this generalized behavior is Mexico, whose manufactured goods exports grew less than world averages up to 2007 and more in the final years. If we restrict the comparison to non-basic manufactured goods (less intensive in natural resources), we also see growth rates above world averages in most countries in the first period and under world averages or similar in the second, between 2007 and 2012.

Chart 10
Annual growth (%) of manufactured exports: Latam vs. world



Source: WITS and BBVA Research

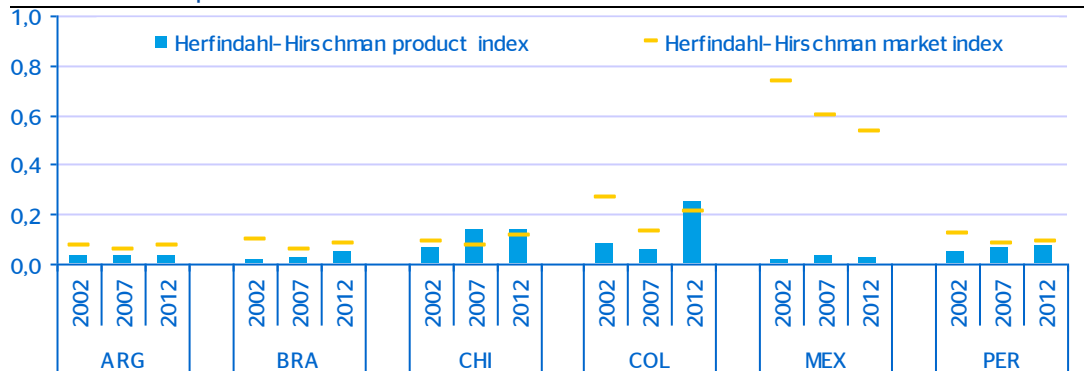
World growth in products and markets making up a country's portfolio is also an indicator of growth potential in exports. In this, a country's exports are better oriented if it sells products for which demand is growing worldwide to economies which are experiencing strong growth. In the case of Argentina, it has lost market share in those products with greater world growth and has, on the other hand, gained share in exporting those with more modest growth, a trend which has significantly sharpened in the last five years. On the contrary, in Brazil, Chile and Peru those products with the biggest share in their country portfolio have grown strongly around the world in the last ten years, although in Chile this orientation has gone significantly off-track in the last five years.

When it comes to export diversification since 2002, Chart 11 shows the performance of the Herfindahl-Hirschman (HH)³ indexes for products and markets in 2002, 2007 and 2012. There export products' diversification has been reduced in all countries between 2002 and 2012, although in some the fall has been small, amongst them Argentina and Mexico, whilst in others, such as Colombia, Brazil and Chile, the drop-back has been more significant.

Market diversification, on the other hand, has gone up in all countries, with the sole exception of Chile, although diversification by market remains particularly low in Mexico because of the intense trading relationship it has with the United States.

Chart 11

Concentration of products and markets

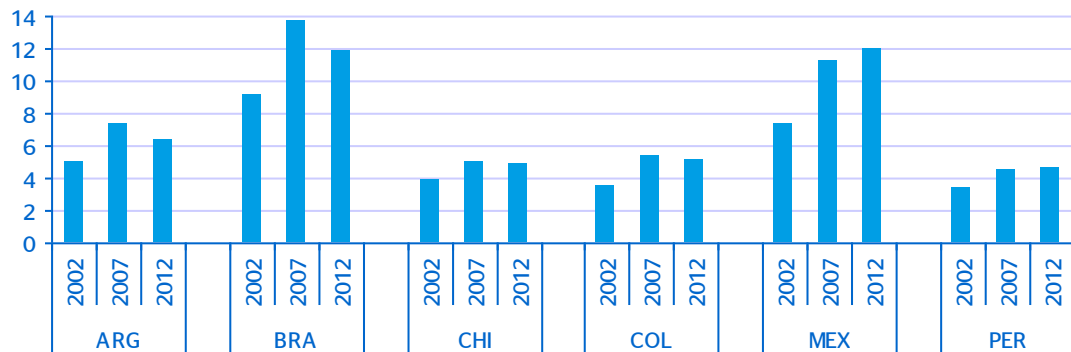


Source: WITS and BBVA Research

This improvement in market diversification is also visible - with some differences - in Market Penetration Index (Chart 12), since most countries have managed to export to a higher proportion of all those markets which are buyers of the products in its portfolio, although there are still significant differences between countries, with Brazil and Mexico those which most exploit their products' export potential.

³ An index close to one indicates a high concentration in the export portfolio of few products or destinations, while a zero index means that the portfolio is perfectly diversified.

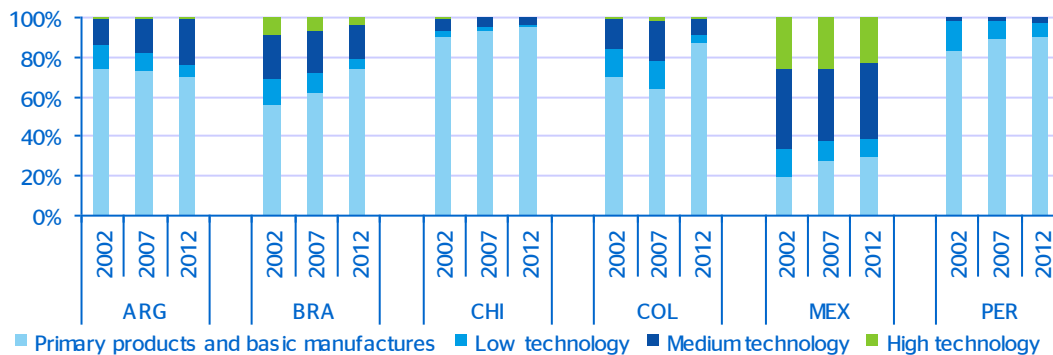
Chart 12
Market Penetration Index



Source: WITS and BBVA Research

Finally, we analyze the technological sophistication of exports around the region in Chart 13. This shows that the proportion of the most sophisticated manufactured goods (medium and high tech)⁴ in total exports fell in most countries between 2002 and 2012, principally because of strong growth in the export of raw materials, as we explained above. Argentina and Peru are the only countries in which the weighting of more sophisticated manufactured goods has gone up in total exports, although this increase has only occurred with medium-tech goods, and not high tech products.

Chart 13
Technological classification of exports



Source: WITS and BBVA Research

In summary, the weight of manufactured goods in total exports has fallen in the region, but this is mainly accounted for by the boom in raw materials, since manufactured goods exports have grown in most countries more than the world average. Even so, the region in general continues to suffer a relative disadvantage in exporting this type of products, and little technological sophistication in the same, apart from Mexico. There is, however, a differentiation if we divide the period into two parts: while in general there are world share gains between 2002 and 2007, suggesting competitiveness

⁴ We have used the Lall (2000) classification, "The Technological structure and performance of developing country manufactured exports, 1985-98". Oxford Development Studies, No. 28, vol. 3, pp. 337-369.

improvements, afterwards there have been impairments or loss of competitiveness. The rest of the document analyses the idiosyncrasies and specifics of Argentina which have affected the competitiveness of its manufacturing sector.

Argentina: sustained increase in labor costs, partly offset by productivity gains

Real wages have grown steadily in Argentina since 2003. As a result, the Argentine industry has registered continued rises in the unit labor cost in pesos in the last decade, at an annual average of 12% since 2002 (Chart 14), pushed by the constant increase in wages as measured in current pesos (Chart 15). If, on the other hand, we look at wages measured in USD in the Industrial sector (Chart 15), their rise was partly offset by the depreciation in the nominal rate of exchange. As a result, Industrial wages measured in dollars have gone up by an average annual rate of 5.3% between 2002 and 2012, well below the increase in Industrial wages measure in pesos.

One also needs to factor in that this process has taken place *pari passu* with average productivity growth of 5.1% between 2002 and 2012. So, the relative labor cost measured in pesos, i.e. the unit labor cost adjusted by productivity growth, went up by an average of 6% YoY since 2002 (Chart 14). Although this annual average increase is substantial, we should remember that the base year for comparison, 2002, was a year when there was a major macroeconomic crisis in the country after the traumatic exit from convertibility, and as such the unit labor cost was at rock bottom, having fallen by 38% that year over 2001, so that a good part of the increased labor cost in the industry since 2002 is merely recovering the level lost during the crisis.

The change in the industry's export ration is consistent with these figures, since in the last few years 23% of Industrial production has been exported (Chart 16), but the trend is a gradual decline since 2006, in line with the mentioned rise in unit labor costs. In their turn, the share of imported inputs shows a gradual upward trend in recent years, consistent with real currency appreciation (Chart 3).

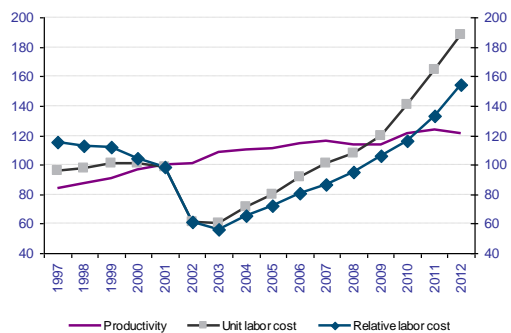
Nevertheless, it needs to be pointed out that this average behavior hides differences between sub-sectors within the industry. If we consider this information broken down into the 21 Industrial sub-sectors, the industry which fell most over the decade was the manufacture of radios, televisions and communication equipment, with an average increase in the physical production of 23% a year between 2002 and 2012⁵; followed by the manufacture of "automotive vehicles, trailers and carparts" (mainly saloon cars), which grew by 11.9%. In fact, these sectors are those which account for Argentina's relatively good performance in terms of the RCA indicator (Table 2). In particular, the automotive sector represented nearly 13% of Argentine exports in 2012, suggesting that this sector is mainly responsible for the increase in the RCA and in the country's market share of manufactured goods. Furthermore, since more than 80% of vehicle exports go to Brazil, a good part of the Argentine manufacturing sector's competitiveness improvement is a result of its preferential access to the Brazilian market and to the competitiveness gains over Brazil, which can be seen in the changes in the bilateral REE with Brazil (Chart 3). On the other side of the sub-sector spectrum, the least dynamic between 2002 and 2012 was "transport equipment manufacture" (tankers, locomotives, aeroplanes) which 1% over the period; it was followed by "tobacco product creation", which grew by an average of a mere 1% a year over the period; and by "leather and footwear", which increased by just 3.5% on average.

In terms of productivity by sub-sectors, most growth came from manufacturing "radio, TV and communications equipment" (+198% between 2002 and 2012; +11.6% YoY, Avg.) and in "Leather and Footwear" (+169%; +10.4% YoY, Avg.), while in "automotive vehicles, trailers and spare parts" productivity growth was more modest (+58%; +4.7% YoY, Avg.), bolstering the argument that a good

⁵ This is due mainly to the stimulus that production and trading of this type of goods receives in the Tierra del Fuego Free Zone.

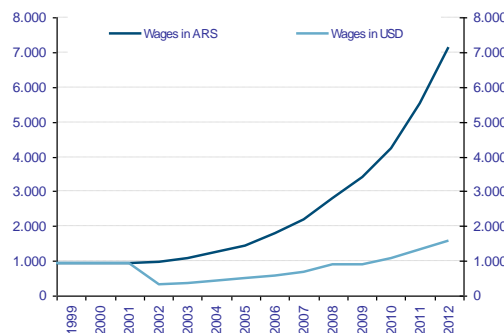
part of this sound export performance is down to the preferential access Argentina has to Brazil because of Mercosur.

Chart 14
Industry: average product, unit labor cost and relative labor cost (by worker, 4Q01=100)



Source: Indec and BBVA Research

Chart 15
Industry: wages in pesos and in dollars 1999-2012



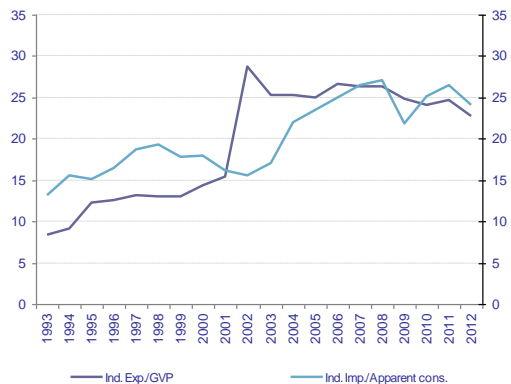
Source: Indec and BBVA Research

Positive shock in the terms of trade, especially for primary goods

Terms of trade have given a powerful positive shock to the Argentine economy since 2002 (see Chart 18), given that it accumulated 70% growth to 2012 – an annual growth rate of 5% – reaching record series highs in 2012. By sub-periods, over these 10 years the terms of trade grew at an annual rate of 4.5% from 2002 to 2006 (inclusive), and by 6.2% annually from 2007 to 2012. Clearly, this growth in terms of trade has had a major wealth effect for the country, and has been a driving factor in Argentine exports, since the increase in export prices over import prices has offset part of the increase in costs we mentioned above.

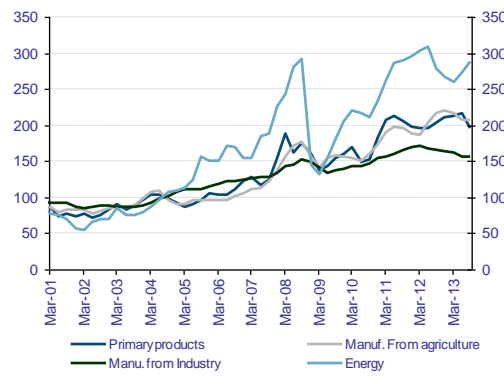
However, it should be pointed out that the main sectors to suffer a positive price shock in their exports were primary products (commodities) and energy (fuels and lubricants), while Industrial manufactured goods went through substantially lower price rises (see Chart 17).

Chart 16
Industry: exports coefficient and import penetration



Source: Indec and BBVA Research

Chart 17
Price of export products by sector (2004=100)



Source: Indec and BBVA Research

What is more, since 2002 exports have been subject to a “retention” duty (export rights) such that part of the price increase in export goods does not reach producers (see Chart 18). This fact is key if we are to understand the impact of the increase in export prices on the performance of exports. Quotas for these export rights vary from 5% in the case of most manufactured goods, 15% for meat and hides, and up to 30-35% for most agricultural commodities, while hydrocarbon exports have a special scheme which sets a “benchmark value” as the cap for what the exporter can receive (for example, USD70 for a barrel of oil).

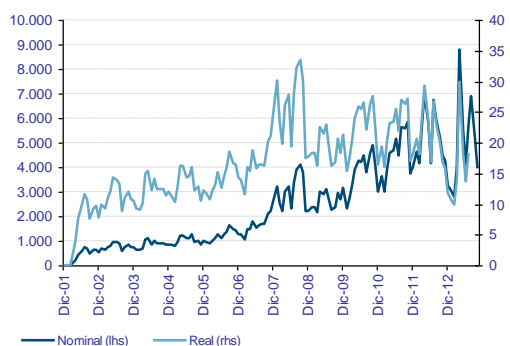
Exchange rate appreciation in real terms since 2007 harmed exports

The effective multilateral real exchange rate in Argentina since 2002 has behaved in two clearly differentiated ways, which exactly match the periods used in this paper. Between 2002 and 2006 (inclusive), after the major nominal and real depreciation which meant the end of the currency board in January 2002 (the nominal exchange rate sank from 1 ARS/USD in December 2001 to 3.80 ARS/USD in July 2002, leaving the REER 150% higher than in December 2001), the real exchange rate remained depreciated in historical terms, given that price growth was low in this five-year period compared to the leap in the exchange rate. That is, the pass-through of the exchange rate to prices was very low in these first five years.

To the contrary, in the second five-year period (2007-2012), inflation gradually rose and started gaining ground over the exchange rate. Thus, Argentina’s real effective exchange rate appreciated continually between 2007 and 2012, standing in December 2012 only 50% higher than its December 2001 level. This final period coincided with that of relative stagnation in Argentine exports, which suggests that the appreciation in the real effective exchange rate has been an important factor in this performance. However, it also needs to be borne in mind that, as we discussed in Section 2, this is also the five-year period of the global crisis in which, as well as Argentina, other countries in the region such as Chile went through significant falls in the contribution of exports to their GDP, suggesting that global factors account for part of this deterioration.

Chart 18

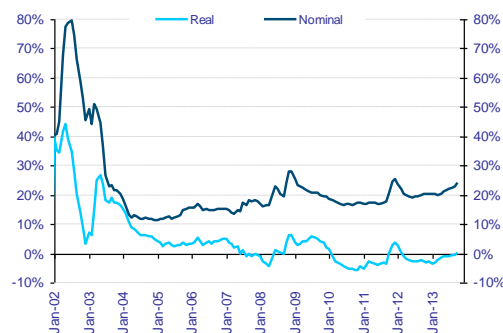
Nominal export duties (in ARS bn) & real export duties (by CPI deflator)



Source: Ministerio de Economía, Indec and BBVA Research

Chart 19

Monthly interest rates (nominal & real, in %)



Source: BCRA and BBVA Research

We should point out that the real appreciation of the Argentine currency has been attenuated by the nominal appreciation in the currencies of Argentina’s principal trading partners and the inflation they experienced as well. This can be seen, for example, if we compare the bilateral (with the US) real exchange rate change with that of the multilateral real exchange rate (see Chart 17). In particular, what happened with inflation and the exchange rate in Brazil, Argentina’s principal trading partner, has been key in this differential performance, which meant that the Argentine peso depreciated continuously between 2002 and 2008 (see Chart 17). This has had a positive influence on exports to its giant

neighbor, especially automotive exports. Since 2009 onwards, after the high volatility of bilateral RER at the end of 2008/beginning of 2009, the Argentine peso appreciated gradually against the real although, as above, less than the aggregate of its trading partners.

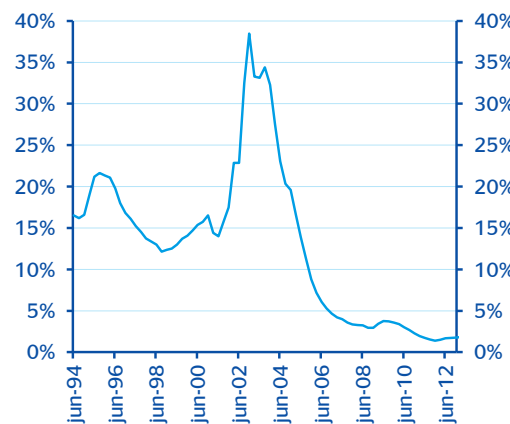
Low borrowing costs, although the recent exchange system limits foreign investment

In the decade we are looking at, borrowing costs for firms in Argentina stayed fairly low. Although in nominal terms the active interest rate for companies was on average 22.8% between 2002 and 2012 (see Chart 24), in real terms the average was 5.4% over the ten years. What is more, since 2007 and until 2012 (both inclusive) the average real rate for firms was negative, at -0.5%, because of the spike in inflation (and inflation expectations) in this period in a context of relatively stable nominal interest rates over this period.

Therefore, Argentine firms have borrowed at negative real rates for a good part of the last decade, meaning that borrowing costs have not been a burden. In fact, the rate of non-performing loans has remained at all-time lows for the last 5 years (see Chart 25), a sign of this context of persistently negative real rates for Argentine firms, together with major product growth in the last decade.

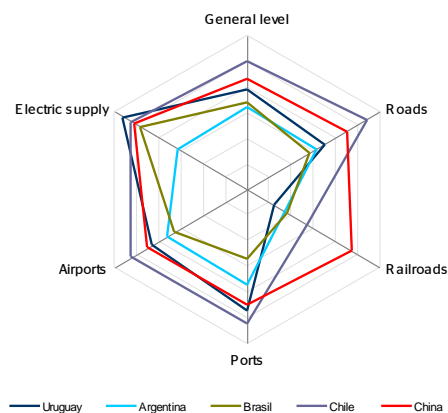
A negative recent factor in this area is the foreign exchange system that has been in force since 2011, which is closing off access for Argentine firms to foreign lending, and has truly stifled direct foreign investment inflows.

Chart 20
Default rate for the non-financial private sector (as % of total credit to that sector)



Source: BCRA and BBVA Research

Chart 21
Quality of infrastructure (year 2012)



Source: World Bank and BBVA Research

Conformism with Mercosur; no new trade deals signed

The country's main trading agreement is the Southern Common Market (Mercosur in the Spanish acronym) it forms with Brazil, Uruguay, Paraguay and, recently, Venezuela, which has been key for the development of the automotive segments, which is the main Industrial manufacture exported by Argentina. Mercosur's main Industrial protection mechanism is the Common Foreign Duty (AEC in the Spanish acronym) applied by the member countries to extrazonal products, and which has helped to develop the internal market and intrazonal exports. However, in the case of the automotive sector, as well as the existing AEC duty of 35% for the final vehicles, there are agreements on the minimum regional content of parts in the final car produced in each member country and on the establishment

of the Free Trade zone. For example, the last negotiation conducted in 2008 concluded with the setting of an asymmetric “flex” for five years (subsequently extended in 2013), which sets out the relationship between imports and exports with a value that indicates the maximum amount of dollars that can be imported for each dollar exported, and which gave Argentina greater protection. Goods included in this scheme include goods produced by other sectors which are used in automotive production (rubber, plastic, etc.). So, this special protection scheme for the automotive sector, together with AEC duties and the appreciation of the Brazilian real, has stimulated the Argentine automotive sector’s exports to Brazil a great deal.

However, this positive aspect of Mercosur, which enables sectors to develop within the protection of the AEC, also has the cost of capping competitiveness gains that member countries might have if they were to compete head on in the international market. Furthermore, as happened with the other Mercosur countries, belonging to the shared market has brought with it a degree of conformity and there has been no active search for further trade deals with other extrazonal countries. Thus, Argentina has not signed important trade agreements in the last few years: this has, to an extent, limited local firms’ export capacity. This could change if the negotiations for the postponed trade agreement between Mercosur and the European Union, relaunched in 2010, go forward: this seeks to liberalize trade, by reducing existing commercial (tariff) barriers for nearly 90% of the commercial sectors active between the two blocks, over a period of between two and ten years (depending on the product). The agreement would also include a chapter on investment, seeking a level playing-field in each country for the companies in both trading blocks.

Poor infrastructure and difficulties in doing business

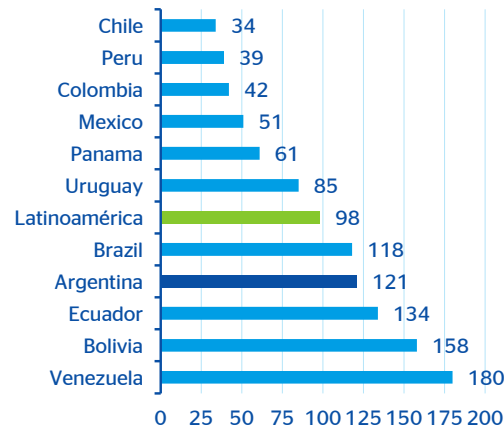
The quality of its infrastructure is an area where Argentina clearly has room for improvement, since in general it is below other countries in the region such as Brazil and Chile, or other regions such as China (see Chart 21). After a major overhaul of its infrastructure in the nineties, in the last decade the country has suffered continuous deterioration of the same (ports, railways, etc.), which has had a definite impact on the country’s “non-price” competitiveness.

Evaluations of its business environment are not positive about Argentina, either. In the World Bank’s latest Doing Business ranking, Argentina comes 121st out of 189 countries evaluated (see Chart 22), and in the lower group of Latin American economies, below Chile (34), Mexico (51) and Brazil (118). By sections, Argentina’s worst score is for the time and procedure required in getting a construction permit (181st out of 189 countries), starting a business (155) and paying taxes (152). It achieves its best scores in contract execution (49), getting a loan (71) and having electricity connected (77). Clearly the evaluation of these structural factors does not help Argentina, and some of the reasons for stagnation in the country’s export performance are to be found in these obstacles, once other issues such as price rises and the exchange rate appreciation stop impacting.

When it comes to export costs, these have gone up from USD1,350 per container exported in 2005 to USD1,650 in 2012 (see Chart 23), although this increase was below that of other countries in the region such as Brazil and Colombia. If we bear in mind the time it takes in Argentina to export, this has stayed at 13 days in the last few years, similar to the time for other countries in the region (see Chart 25).

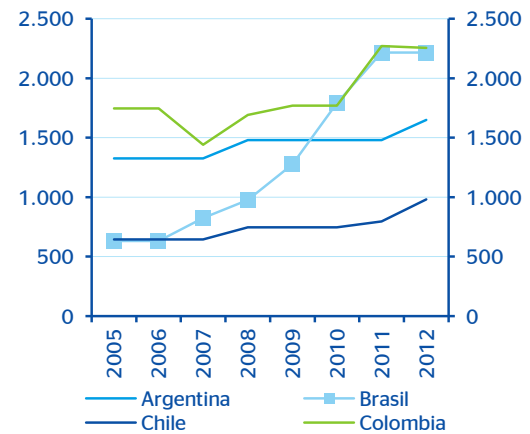
If we look at the logistical barriers to export in the World Bank’s International Trade Logistics Performance Index (see Chart 24), which evaluates areas such as the degree of competition and quality of a country’s logistics and the efficiency of its customs procedures, this shows that Argentina has a performance level similar to that of South America’s major countries, Brazil and Chile, and better than that of Colombia.

Chart 22
Doing Business index (positions in the 2013 ranking)



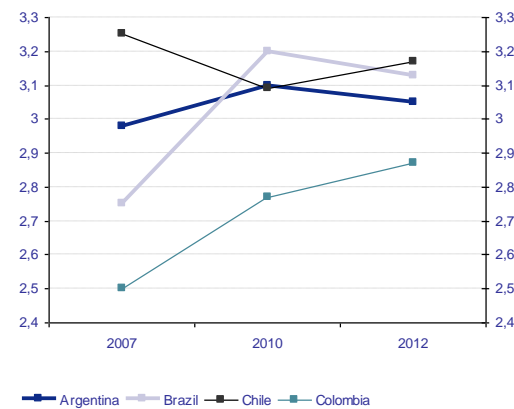
Source: World Bank and BBVA Research.

Chart 23
Cost to export (USD per container)



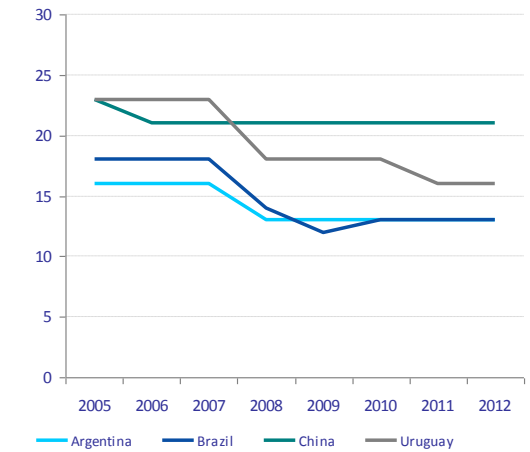
Source: World Bank and BBVA Research.

Chart 24
Logistics performance index for international trade (1: low; 5: high)



Source: World Bank and BBVA Research.

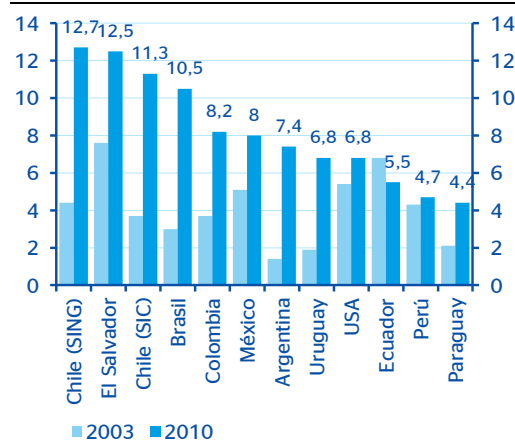
Chart 25
Time to export (days)



Source: World Bank and BBVA Research.

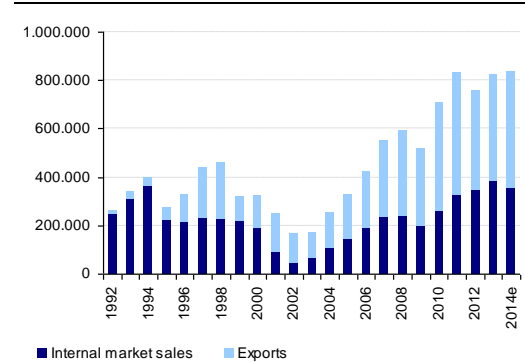
In terms of the price of electricity in Argentina, although it has gone up significantly since 2003, it is still cheaper than in most countries in the region, such as Brazil and Mexico (Chart 26).

Chart 26
Electricity price in selected countries
(USD/kWh)



Source: World Bank and BBVA Research.

Chart 27
Automotive demand (units)



Source: Adefa and BBVA Research.

Conclusions

Argentine exports in general, and manufactured goods in particular, have performed well in the decade we are studying in historical terms, although they have declined in terms of GDP throughout the period, partly as a result of the comparison with a very low GDP in the base year (2002). The RCA indicator and the comparison between the performance of Argentina's main export products with worldwide exports of these same products, as well as other international trade indicators presented in Section 2, show that Argentina's manufactured exports in aggregate terms did not lose competitiveness in the decade we are looking at. However, behavior is heterogeneous both by sectors and by five-year periods, with a few (but important) sectors with growth in RCA and global market shares (such as the automotive), and other sectors with gains in RCA and shares in the first five years, and losses in the second.

Compared with other export categories, Industrial manufactured goods were the fastest growing in quantity in the decade we are examining, while agricultural manufactured goods and primary products have grown basically due to price rises. However, exports in general, and manufactured goods in particular, lost momentum in the latter years. In these pages we identify some factors which help to explain this lack of dynamism. On the one hand, the continued increase in labor costs, in the general context of increasing inflation since 2003, although this is partially offset by productivity gains, had an increasingly negative impact on production and Industrial exports. The Argentine peso's real appreciation since 2007, the other side of the coin of the above-mentioned inflation, is also affecting exports negatively, despite the enormous shock of the terms of trade the country has been experiencing continually since 2002, especially for primary goods, on top of the current export tax scheme (retentions). The currency's real appreciation was reflected in the loss of the current account surplus in the second half of the period being studied. The low cost of borrowing for Argentine firms was a factor which helped export development, although more recently the current exchange system has been affecting alternative borrowing methods used by export companies, such as direct foreign investment inflows.

From a more structural point of view, there are many factors which are increasingly having a negative effect on Argentina's competitiveness in general, and on the Industrial sector in particular, which explains the loss of momentum that Industrial exports have suffered since 2007, and concerns that this trend will continue over the next few years.

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