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FEATURED Q&A

Is Argentina's Infrastructure Adequate for the Country's Needs?

Q The train crash that killed 51 people Feb. 22 in Buenos Aires was the country's deadliest rail disaster since the 1970s and the country's third fatal incident involving a train within six months. Argentina's economic growth over the past several years has led to other infrastructure breakdowns, including roads that are often clogged with traffic. Is Argentina's infrastructure inadequate for the country's transportation and economic activity needs? What should be done to improve the country's infrastructure? Has the government done an adequate job of providing oversight and encouraging investment?

A Miguel Kiguel, executive director of EconViews in Buenos Aires: "Argentina is facing a major challenge regarding investment in infrastructure. The needs are particularly significant in energy and public transportation due to the lack of adjustments in the utility and transportation rates since the 2001 crisis. Besides, there have been few incentives for oil and gas exploration and production as prices have remained well below international levels. At the end of last year, the government sent signals that it was ready to make adjustment in the rates, but that process came to a sudden stop following a train accident in which 51 people died. Perhaps it perceived that further increases would imply an implicit recognition of the failure of their policies. But that policy decision does not address the issue of who will invest in infrastructure. The utilities in charge of electricity and gas distribution and transportation are now facing negative cash flows and can barely maintain the service, let alone invest in new equipment. The recent expropriation of YPF makes things even worse, as it has introduced new uncertainty about property rights and the rules of the game. YPF represents around 30 percent of Argentina's total oil and gas production, and it does not have the financial resources to invest the $5 billion to $7 bil-

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Morales Seizes Operator of Bolivia's Electrical Grid

Bolivian President Evo Morales used celebration of International Workers' Day on Tuesday to announce the nationalization of the local unit of Spain's Red Eléctrica, which operates most of the South American country's power grid. See story on page 2.

Photo: ABI.

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NEWS BRIEFS

Peña Nieto Holds Strong Lead in Polls Ahead of Mexican Election

Enrique Peña Nieto, of the opposition Institutional Revolutionary Party (PRI), remains the frontrunner ahead of Mexico's July 1 presidential election with 38 percent support, according to a poll released Tuesday by **Consulta Mitofsky**, Reuters reported. Though his support was down 2.1 percent from the pollster's April 24 survey, he remains well ahead of Josefina Vázquez Mota, with 22 percent, and Andrés Manuel López Obrador, who reached 18 percent. The poll also found that the PRI and the Green Party, which is running on the same ticket, could win nearly 51 percent of congressional seats.

Iran, Venezuela Sign $130 Million Oil Deal

Iran and Venezuela signed an agreement to build a $130 million oil-platform yard, the *Tehran Times* reported Tuesday. According to an official of the Iranian Offshore Engineering and Construction Company, transporting equipment from Iran to Venezuela will pose the greatest difficulties.

Peru Boosts Banks' Reserve Requirements

Peru's central bank has increased reserve requirements for commercial banks in an effort to moderate the country's rate of credit expansion, state-run news agency Andina reported Tuesday. The central bank increased the rate on the country's average reserve requirement by a half point. The central bank is also increasing a marginal requirement from 25 percent to 30 percent and extending a 60 percent requirement for foreigners who hold debt with maturities of three years or less.

Economic News

Morales Seizes Bolivia's Power Grid From Spanish Company

Bolivian President Evo Morales on Tuesday seized the local unit of Spain's **Red Eléctrica**, the owner of approximately 85 percent of the South American country's power grid, *The Wall Street Journal* reported. "Long live the first of May and long live nationalization," said Morales, using a celebration of International Workers' Day to announce the expropriation in Cochabamba. "Today, as we pay homage to the workers and the Bolivian [citizens] that have fought for the recovery of natural resources and basic services, we are nationalizing the electricity transmission provider." Morales' announcement came just weeks after Argentine President Cristina Fernández de Kirchner seized control of her country's largest energy company, **YPF**, which is majority-owned by Spain's **Repsol**. Similar to Fernández's argument about YPF, Morales accused Red Eléctrica of not investing enough in Bolivia. "We regret the Bolivian government's decision, which was based on motives that are unknown to us," said Red Eléctrica spokesman Antonio Prada. "These actions go against the free market and the rule of law that should govern international investment." Spain's government owns approximately 20 percent of Red Eléctrica. A top Spanish government official told *The Wall Street Journal* that Bolivia has indicated that it will compensate the Spanish company for the nationalization. Since becoming president in 2006, Morales has used May Day to seize parts of the country's economy. Six years ago, he seized the country's national gas fields. Two years ago, he nationalized Britain's **Ruralec** in order to take control of most of the country's electricity generation. Red Eléctrica had more than 1.63 billion euros ($2.16 billion) of annual revenue last year. Its operations in Bolivia contributed only 1.5 percent of that revenue. Since acquiring the unit in Bolivia for about 92 million euros in 2002, Red Eléctrica has invested more than $60 million in the country, the company said.

> "Long live the first of May and long live nationalization."
>
> — *Evo Morales*

Political News

Alleged Rebel Says Colombia's FARC Is Holding French Journalist

The Revolutionary Armed Forces of Colombia, or FARC, is holding captive a French journalist who went missing on Saturday, a woman claiming to be a member of the rebel group told reporters Tuesday, BBC News reported. The woman identified herself as a member of the FARC's 15th division and read a statement she said had been issued by rebel commanders. "The 15th division informs the public that the French journalist, who was dressed in military clothes and captured in battle, is in our hands as a prisoner of war," said the statement. Roméo Langlois, who works for television channel France 24, vanished while reporting on soldiers' destruction of cocaine laboratories in Caquetá province. Rebels attacked, leaving two soldiers, a sergeant and a national police officer dead, CNN reported, citing Colombia's Ministry of National Defense. Six others were wounded. Colombian President Juan Manuel Santos has demanded Langlois' release. "We want to tell the FARC to release him as soon as possible," said Santos. "Among other things, because we understand he is hurt." Langlois was shot in the arm before his abduction, Defense Minister Juan Carlos Pinzón said Sunday. Santos also called on the FARC to keep the promise it made last

Langlois

File Photo: France 24.

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month to no longer carry out kidnappings. In related news, a helicopter carrying Colombian Air Force and police personnel crashed Monday, killing all 13 aboard, CNN reported. The crash happened near the country's Caribbean coastline in the municipality of Sabanagrande, the Air Force said. In a message posted to his Twitter account, Santos said, "We regret the accident of the Air Force helicopter crash ... Our condolences to the families of the patriotic heroes who died in this accident." Investigators are probing the cause of the crash, which happened as the helicopter was flying between Barranquilla and Caucasia.

Company News

Ecuador to Pay Petrobras $217 Million for Seized Assets

Ecuador's government has agreed to pay Brazilian state-run oil company **Petrobras** $217 million to compensate it for assets seized in 2010, Reuters reported Tuesday. Ecuador seized the assets after Petrobras refused to accept new terms that were part of Ecuador's move to boost government revenues from the oil sector. "We're talking about $217 million to be paid in two installments," Ecuadorean Energy Minister Wilson Pástor told reporters on Monday. Petrobras had been seeking $300 million after the expropriation and Ecuador last year offered approximately $168 million. Ecuadorean state-run oil company **Petroamazonas** now operates the assets, which accounted for a small fraction of Petrobras' production.

Ecuador seized the assets after Petrobras refused to accept new contract terms.

Featured Q&A

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lion a year that is necessary in the energy sector. The government is in a trap. It does not want to increase rates, but it does not have the financial resources to invest in infrastructure. It wants a public-sector YPF, but it needs the private sector to invest billions of dollars to increase gas production and take advantage of the large reserves of shale gas. In the meantime, it continues to send mixed signals and the situation will probably continue to get worse."

Isabella Alcañiz, assistant professor of government and politics at the University of Maryland: "Argentina's infrastructure deficits are a chronic problem that has remained unresolved for the past 50 years. As a result of great macroeconomic instability, both the private and public sectors have been unwilling to commit enough resources to satisfy basic needs in the areas of communications, roads and energy. A constant challenge is the high concentration of economic activity in the City of Buenos Aires and its metropolitan area (where the nation's main port is located). Key to solving the long-term investment problems in infrastructure is a working partnership between the federal and local governments to oversee and encourage investment. Yet, if the difficult relationship between the president and the mayor of Buenos Aires is any indication, such partnerships are politically difficult in a highly polarized environment. Problems between the national and local governments are readily observable in the failure to manage the system of public subways in Buenos Aires and the local police. To create the conditions for sustained infrastructure investment, Argentina needs to develop stable partnerships across government jurisdictions (national, provincial and local) as well as between public and private actors. Given the expropriation of Repsol's stake in YPF, the latter partnership does not seem very plausible in the current climate. But not all is bad news: after almost 40 years of planning and construction, in 2010 the administration of Cristina Fernández de Kirchner finally completed and inaugurated 250 miles of freeway connecting the cities of Rosario and Córdoba, the country's two major economic centers outside of Buenos Aires."

Claudio Loser, senior fellow at the Inter-American Dialogue and former head of the Western Hemisphere department at the International Monetary Fund: "February's train tragedy was a dramatic call for attention to the dire state of the public-service infrastructure in Argentina. Unfortunately, it also provides a warning about the consequences of the very recent expropriation and renationalization of oil producer YPF, the country's largest private company. Argentina does poorly in terms of the quality of its infrastructure. According to the World Economic Forum competition indicators, Argentina is positioned second to last in terms of quality among the seven largest Latin American countries, ahead of only Venezuela. Furthermore, it is behind the observed quality of other regions and countries, including 'newly industrialized countries,' East Asia as well as China and emerging Europe. This reflects years of underinvestment, service subsidization, power struggles among various sectors and a generally unattractive business environment. For example, the extremely powerful trucking union has been able to create conditions that make train transportation uneconomical. Moreover, the low profitability of passenger transportation (even with government transfers), and a lax, and most likely corrupt, supervisory framework has been a major factor explaining recent accidents. In addition to railways, road and port conditions are mediocre at best, electricity is characterized by erratic shortages and other services, including water and gasoline, have also been poor. The actions regarding YPF, with little investment capacity on the

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Featured Q&A

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part of the government, and in the context of mounting fiscal pressures, would suggest that Argentina is unlikely to see an improvement in its infrastructure, and thus growth will be difficult to sustain."

Franco Moccia, undersecretary of planning and management control for the City of Buenos Aires: "The prices of utilities, including energy and transportation, were not adjusted after the country's economic crisis and 2002 peso devaluation. Quotas and taxes were imposed on energy exports to keep local prices low and promote internal consumption. The populist model of promoting short-term consumption while ignoring long-term capacity building made sense as Argentina was getting out of the recession and had idle capacity. However, this was not sustainable as the economy started to grow steadily. When commodity prices began increasing in 2003, instead of creating incentives to build up infrastructure by improving local prices, the government kept the system paying subsidies to utility companies. By sustaining very low energy, utilities and transportation costs, consumption grew, investment disappeared and corruption in the assignment of the subsidies skyrocketed. Almost a decade later, Argentina has more than doubled subsidies to $20 billion as of 2011. Argentina has to change this failing infrastructure model right now. Subsidies need to fade down as market prices increase, in order to attract local and international investments in energy, transportation and utilities. This must be done before the growth of subsidies leads to fiscal collapse, energy imports lead to a trade deficit and infrastructure bottlenecks block economic growth. The February train cash can't be considered an accident. Paraphrasing Colombian writer Gabriel García Márquez, this is a 'chronicle of a death foretold' and an example that unsustainable policies not corrected on time are paid by the weakest segments of the population—those who should have been protected."

The Advisor *welcomes reactions to the Q&A above. Readers can write editor Gene Kuleta at gkuleta@thedialogue.org with comments.*

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The **Latin America Advisor** gets **answers** to the **questions** that informed executives are asking, every business day, so that you can rest easy.

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