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THEDIALOGUE

FEATURED Q&A

Is Argentina's Economy on the Right Track?

President Mauricio Macri met Wednesday with young entrepreneurs to discuss a new entrepreneurship law aimed at facilitating the registration of firms, providing fiscal incentives and more access to financing. // Photo: Government of Argentina.

Q Argentina suffered a setback when MSCI on June 20 declined to upgrade it to emerging market status, relegating it for at least another year to the index provider's list of frontier markets, which also includes Kazakhstan, Romania and Nigeria. MSCI's announcement came just a day after global investors piled into Argentina's sale of $2.75 billion in 100-year bonds, marking the first time a junk-rated sovereign has sold a so-called "century bond." How big a blow was MSCI's decision to the government of President Mauricio Macri, who has pushed for market-friendly reforms? How will MSCI's move affect Argentine businesses and the country's economy? Is investors' reaction to the "century bond" offering a strong vote of confidence in Argentina, or is it more a sign of investors' thirst for yield?

A Horacio Verbitsky, president of the Center for Legal and Social Studies in Buenos Aires: "The Financial Times asked its readership what they thought was the craziest thing in global markets. Of the 10,000 respondents, 69 percent said it was Argentina's 100-year bond. I don't think I have much to add. Argentina is obligated to pay an interest rate that is triple that of the market in 100 years. Among many of Argentina's poor negotiations, this one takes the cake. In a year and a half, the current government doubled the country's debt and grew the fiscal deficit, which in the long term is unsustainable, as Alex Werner, the director of the Western Hemisphere for the International Monetary Fund, has noted."

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TODAY'S NEWS

POLITICAL

Venezuela's Top Court Bars A.G. From Travel

Once considered an ally of President Nicolás Maduro, Attorney General Luisa Ortega has become the most vocal critic from within the government of his administration.

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BUSINESS

Brazil Regulators Reject Kroton-Estácio Deal

Officials at CADE voted 5-1 to reject the deal, effectively killing it, by deciding that the scale of the new business would have harmed the ability of smaller operators to compete with the new 1.5 million-student giant.

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POLITICAL

Leader of Brazil's Ruling Party in Senate Steps Down

Lobbing sharp criticisms at President Michel Temer, Brazilian senator Renan Calheiros announced he will no longer be the leader of the ruling PMDB party in the upper chamber.

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Calheiros // File Photo: Government of Brazil.

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POLITICAL NEWS

Venezuela Supreme Court Bars Attorney General From Travel

Venezuela's Supreme Court on Wednesday banned Attorney General Luisa Ortega from leaving the country and has frozen her assets ahead of a pre-trial hearing scheduled for July 4, CNN reported. President Nicolás Maduro called for the hearing to determine if Ortega committed unspecified "grave errors while in her position." Some media reports suggest the charges are related to the appointment of judges. Once considered an ally, Ortega has

Ortega // File Photo: Government of Ecuador.

become the most vocal critic of Maduro's administration within the government. Earlier this week, she criticized a Supreme Court decision to transfer some powers from the Attorney General to the country's Ombudsman's office. The decisions of the court "are not democratic, they dismantle the state," Ortega said, El Universal reported. In related news, Venezuelan authorities on Wednesday announced they had found the abandoned police helicopter used in a grenade attack on the Supreme Court building on Tuesday. The man authorities say piloted the aircraft, Oscar Pérez, has not been found. Rumors circulated that the government itself was behind the attack, designed as a ruse to justify a military crackdown. Meanwhile, opposition leaders have called for a march on the National Electoral Council headquarters in Caracas today to mark 90 days of protests. More than 70 people, both critics and supporters of Maduro, have died from injuries related to the protests.

Leader of Brazil's Ruling Party in Senate Steps Down

Brazilian senator Renan Calheiros on Wednesday announced he will no longer be the leader of the ruling PMDB party in the upper chamber, Reuters reported. Calheiros said he would not tolerate what he called President Michel Temer's "cowardly posture" in the face of corruption charges, Folha de S.Paulo reported. In a speech that lasted 15 minutes, Calheiros said he was freeing himself from "a heavy and unjust anchor." Analysts suggest the move is likely positive for proponents of a major labor reform bill going through Congress. A former Senate president, Calheiros has long opposed Temer's labor bill, and his decision to step down suggests he lacks support from a majority of fellow PMDB senators as the legislation moves through Congress, according to the report. A senate committee late yesterday passed key parts of the labor reform, Folha de S.Paulo reported. In related news, the driver of a car on Wednesday rammed the gate of the Brazilian president's palace in Brasília, BBC News reported. Security forces fired warning shots and the driver, who is underage, has been detained, a government statement said. Deep austerity measures put in place by the widely unpopular Temer administration have led to cuts in services, including the issuance of passports. In a statement late on Tuesday, the federal police said their decision to stop issuing new passports "stems from a dearth of funds earmarked to the activities of migratory control and the issuance of travel documents."

BUSINESS NEWS

Brazilian Regulators Reject $1.8 Billion Kroton-Estácio Deal

Brazil's antitrust regulator on Wednesday voted down Kroton Educacional's proposed $1.8

NEWS BRIEFS

Suriname Awards New Oil and Gas Contracts

A consortium made up of U.S.-based Exxon Mobil and Hess along with Norway's Statoil has been awarded an oil and gas production-sharing contract for Suriname's offshore Block 59 by the country's oil industry oversight agency, Staatsolie, Zaks reported Wednesday. Staatsolie has also reached an agreement with Statoil over Block 60. The companies are expected to sign their respective agreements by the second week of July.

Public Approval of Mexico's Cabinet Falls to New Low: Poll

Seventy-four percent of Mexicans disapprove of the performance of President Enrique Peña Nieto's cabinet, EFE reported Wednesday, citing a survey released this month by GEA-ISA. The cabinet's approval rating has fallen to its lowest level of popularity since the president's six-year term began at the end of 2012. When asked in the survey, How much do you believe President Enrique Peña Nieto?, only 3 percent responded, "a lot," while 58 percent responded, "not at all."

Ecuador Opposition Files Petition Against V.P. Glas

Opposition legislators in Ecuador on Wednesday called for political trial of Vice President Jorge Glas, El Universo reported. Fifty-nine legislators signed onto the petition against Glas, who they accuse of not preventing acts of corruption. Glas was vice president under former president Rafael Correa between 2013 and 2017 and now serves with President Lenín Moreno. He has been implicated in a corruption scheme involving millions of dollars in the oil sector and in the case of the Brazilian construction company Odebrecht, although a formal complaint has not been filed in court and he denies wrongdoing.

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billion acquisition of its biggest rival in the education business, Estácio Participações, Bloomberg News reported. In a six-hour meeting, government officials at the Administrative Council for Economic Defense, or CADE, voted 5-1 to reject the deal, effectively killing it, by deciding that the scale of the new business would have harmed the ability of smaller operators to compete with the new 1.5 million-student giant. CADE Counselor Cristiane Alkmin, who voted to approve the deal, had sought restrictions such as the sale of distance-learning unit Uniderp and the sale of Anhanguera assets, equivalent to 258,000 students. The deal, which is one of the largest ever voted on by CADE, would have created a company with a market value of some 30 billion reais ($9 billion) and about 20 percent market share, O Estadão de S.Paulo reported.

Alkmin // File Photo: Government of Brazil.

ECONOMIC NEWS

Pacific Alliance Summit Begins in Colombia

A three-day summit of the presidents of the Pacific Alliance economic bloc gets underway today in Cali, Colombia. Founded in 2011, the largely pro-trade and free-market group, composed of Chile, Colombia, Mexico and Peru, will open a new "associate state" category of membership, which will provide an intermediate category between the bloc's four founding members and its 52 observer states, which include countries like Australia, Canada, China, France, Germany, Japan, the United Kingdom and United States, EFE reported. "We are mainly focused on economic and trade integration, and we primarily partner up to achieve effective inclusion in Asian markets," Andriana Mendoza, a Colombian official, told the news service. The Summit will also include the IV Pacific Alliance Business Summit, a platform for 500 business representatives from both founding member and observer states. Pacific Alliance members account for 41 percent of the region's foreign direct investment and 35 percent of its GDP.

China Open to Free Trade Agreement With Mexico

China's ambassador to Mexico, Qiu Xiaoqi, said on Wednesday that his country is willing to negotiate a free trade agreement with Mexico, state news agency Xinhua reported. "Mexico is China's second-largest trading partner in Latin America, and China is Mexico's second-largest trading partner in the world. This is a highly important relationship and we have great interest in deepening and broadening these ties," said Qiu. "I think any agreement to make trade easier is very worthy." The diplomat noted that, while China is willing to discuss the topic with the Mexican government, no discussions have been held so far. There is no difficulty from China's side," he said. Mexican officials have been seeking to diversify trade ties in the face of pressure from the United States under President Donald Trump to renegotiate the North American Free Trade Agreement, with talks planned later this year. Earlier this month, Ford Motor said that it would build its next-generation small car in China rather than in the United States or Mexico. The decision underscores the potential for China to export more vehicles for sale to American buyers, and the reluctance of domestic automakers to invest in additional production in Mexico, the New York Times reported. [Editor's note: See related **Q&A** in the April 17 issue of the Advisor.]

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Daniel Artana, chief economist at Fiel in Buenos Aires: "MSCI's decision was mildly negative to the economy, because positive news will be postponed for another year. But it does not have in itself the power to derail the modest economic recovery that is taking place right now. I do not think that the 'century bond' will create by itself a virtuous circle. Argentina already has access to international financing, but at high interest cost compared to its neighbors, and this will not be changed by the placement of the bond, at least in the short run. In any case, investors seem to be in a 'wait-and-see mode' to move ahead another step in the reduction of the country risk premium. This would require a positive political outcome for the ruling party in the October mid-term elections, and that that will encourage the government and the opposition to move ahead in the structural reform agenda."

> **"Investors seem to be in a 'wait-and-see mode' to move ahead another step..."**
>
> **— Daniel Artana**

Carolina Costa Hurtado, director at McLarty Associates: "The decision by the influential MSCI benchmark equity index to keep Argentina downgraded to the 'frontier market' category for at least another year came as a surprise, as many expected the country would be lifted to 'emerging status,' given President Macri's pro-business reforms and austerity measures since assuming office 18 months ago. But MSCI claims it is still too early to determine that the pro-market reforms are 'irreversible,' and more time is needed before a reclassification. The markets reacted immediately after MSCI's

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announcement: the Argentine peso fell to its weakest level ever, and Argentina's benchmark Merval stock index dropped nearly 5 percent, its largest daily decline since mid-January. While MSCI's decision is a blow to investors' confidence and hinders Argentina's access to inflows from foreign investors, a greater risk to President Macri's governability is Argentine consumers, whose patience with his program of economic policy adjustment is wearing thin. The continued perception among Argentines is that the reforms are not delivering expected economic progress rapidly. As such, President Macri faces increased domestic pressure to demonstrate economic success and manage intricate political and social forces ahead of the October 2017 legislative elections. His reform agenda greatly depends on the outcome of these elections, and the results will signal how he will proceed moving forward. In the meantime, President Macri will continue to face many challenges and unexpected market reactions, such as MSCI's announcement, as he continues his efforts to deliver sustainable economic growth to Argentina."

Juan Cruz Díaz, managing director, and Megan Cook, political risk specialist, at Cefeidas Group in Buenos Aires:

"MSCI's decision was a significant blow to the government. Emerging-market designation would have sent a strong signal to the international community about the robustness of the economic reforms implemented by Macri's government, allowed Argentine companies to raise capital more easily and strengthened the peso via increased foreign inflows. Most analysts and government officials had expected Argentina would be upgraded. This assumption was factored into the pricing of an unexpected 100-year bond issuance that occurred shortly before MSCI's decision was announced (these bonds have been rarely issued, especially by sovereigns that have so recently exited default).The oversubscribed 'century bond' offered attractive enough returns to entice investors looking for a more long-term play. However, MSCI's decision about Argentina's status has a greater impact on equity markets than bond markets. After having risen nearly 25 percent in recent months on anticipation of an upgrade, Argentina's benchmark Merval stock index fell several percentage points on the announcement. Argentina will now have to wait another year before MSCI's decision can be reconsidered. Although the country meets the criteria to be considered an emerging market, MSCI expressed concern that 'the irreversibility of the relatively recent changes still remains to be assessed.' Political risk and uncertainty continue to weigh heavily on foreign investment decisions, especially in light of the upcoming midterm elections in October. In particular, the return of former President Cristina Fernández de Kirchner to politics as a candidate for Senator in Buenos Aires Province has spooked investors. They are concerned that a good showing by her recently formed electoral front could herald a return to the economic policies that led Argentina to be designated a frontier market during her presidency in 2009, or could seriously complicate the Macri administration's efforts at future reforms."

> **"Political risk and uncertainty continue to weigh heavily on foreign investment decisions."**
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> **— Juan Cruz Diaz and Megan Cook**

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