



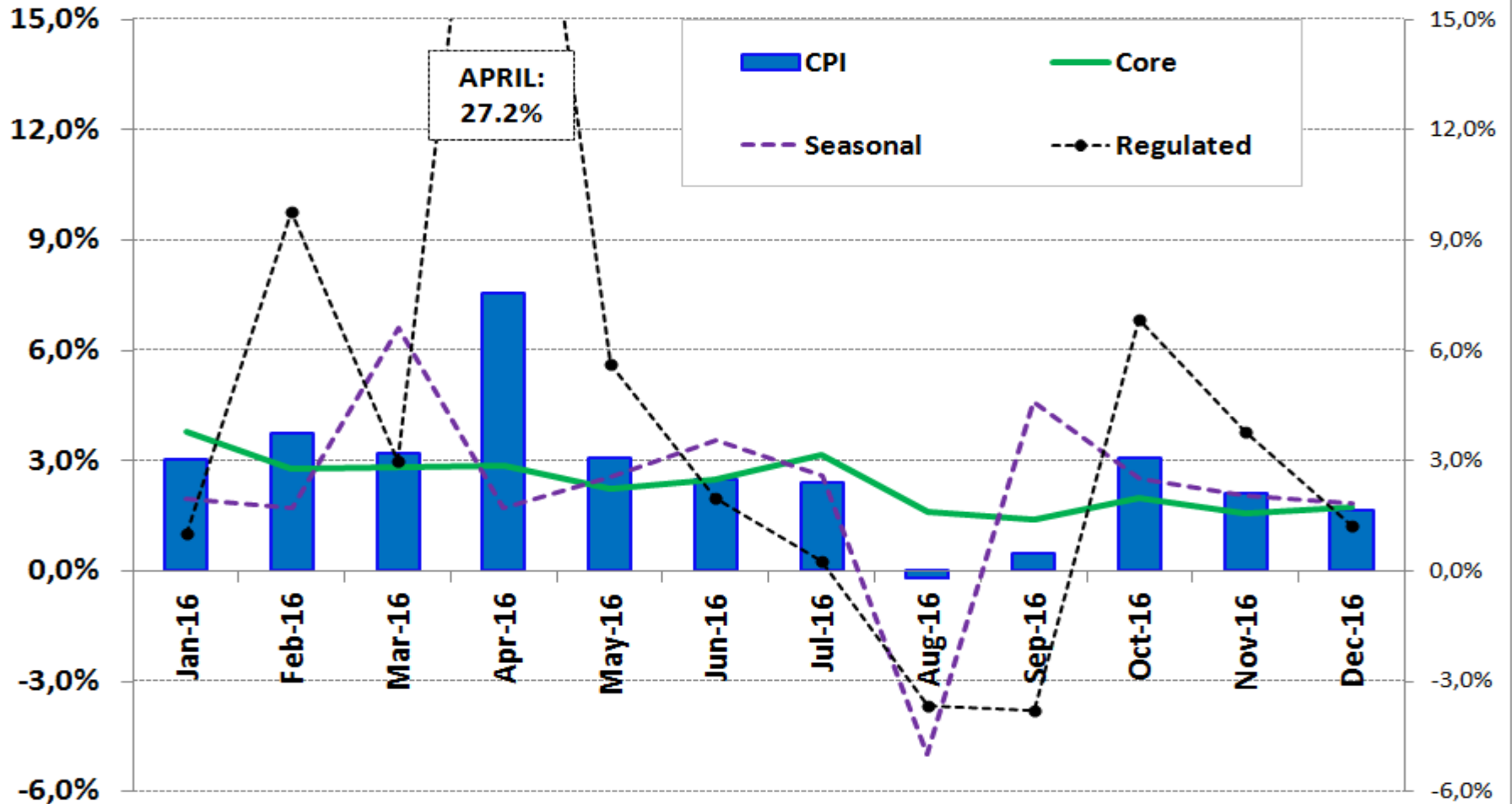
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Argentina: Disinflation and recovery
Juan Luis Bour, chief economist, FIEL

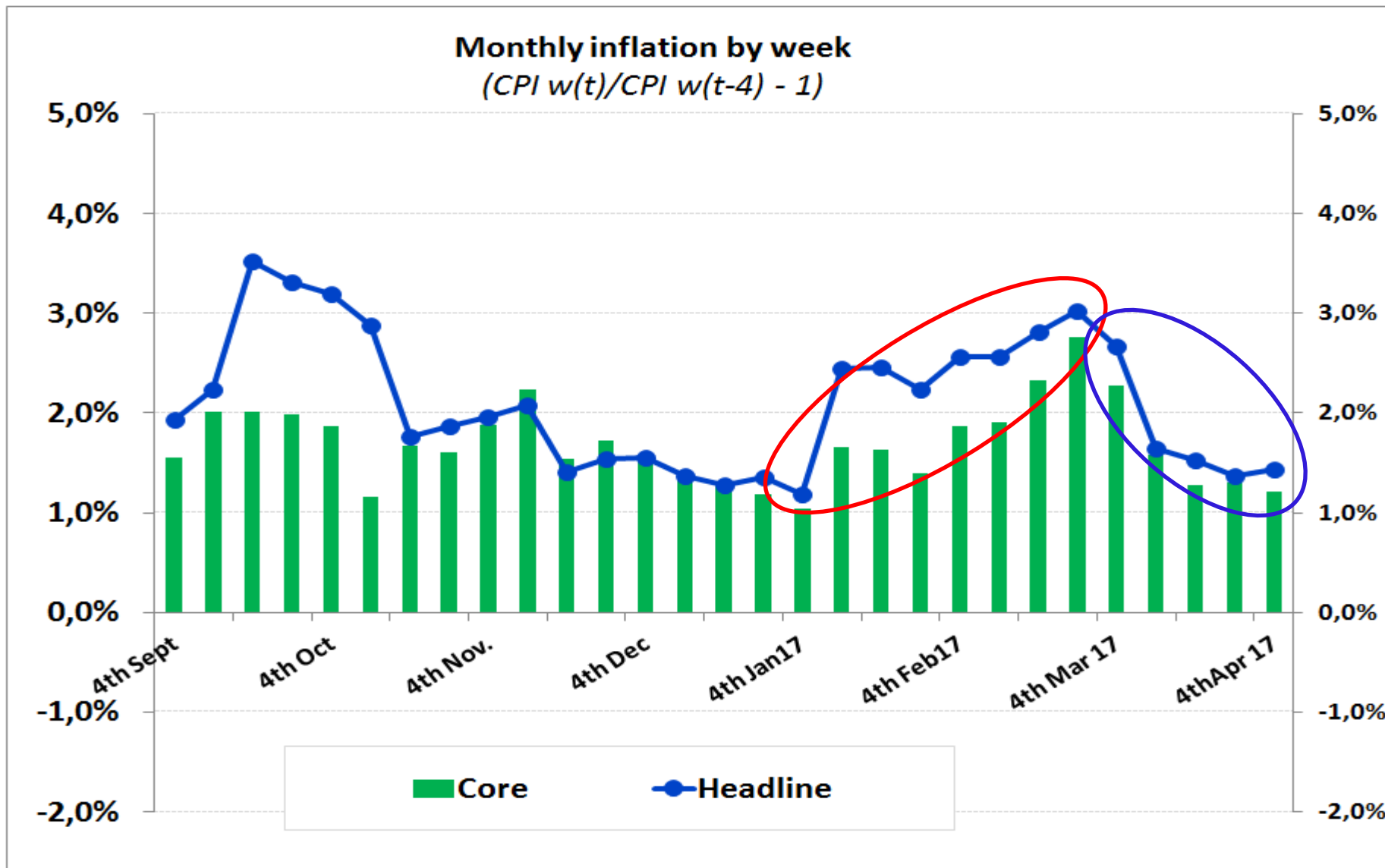
Council of Americas
New York, May 2nd, 2017

Inflation: high volatility during 2016

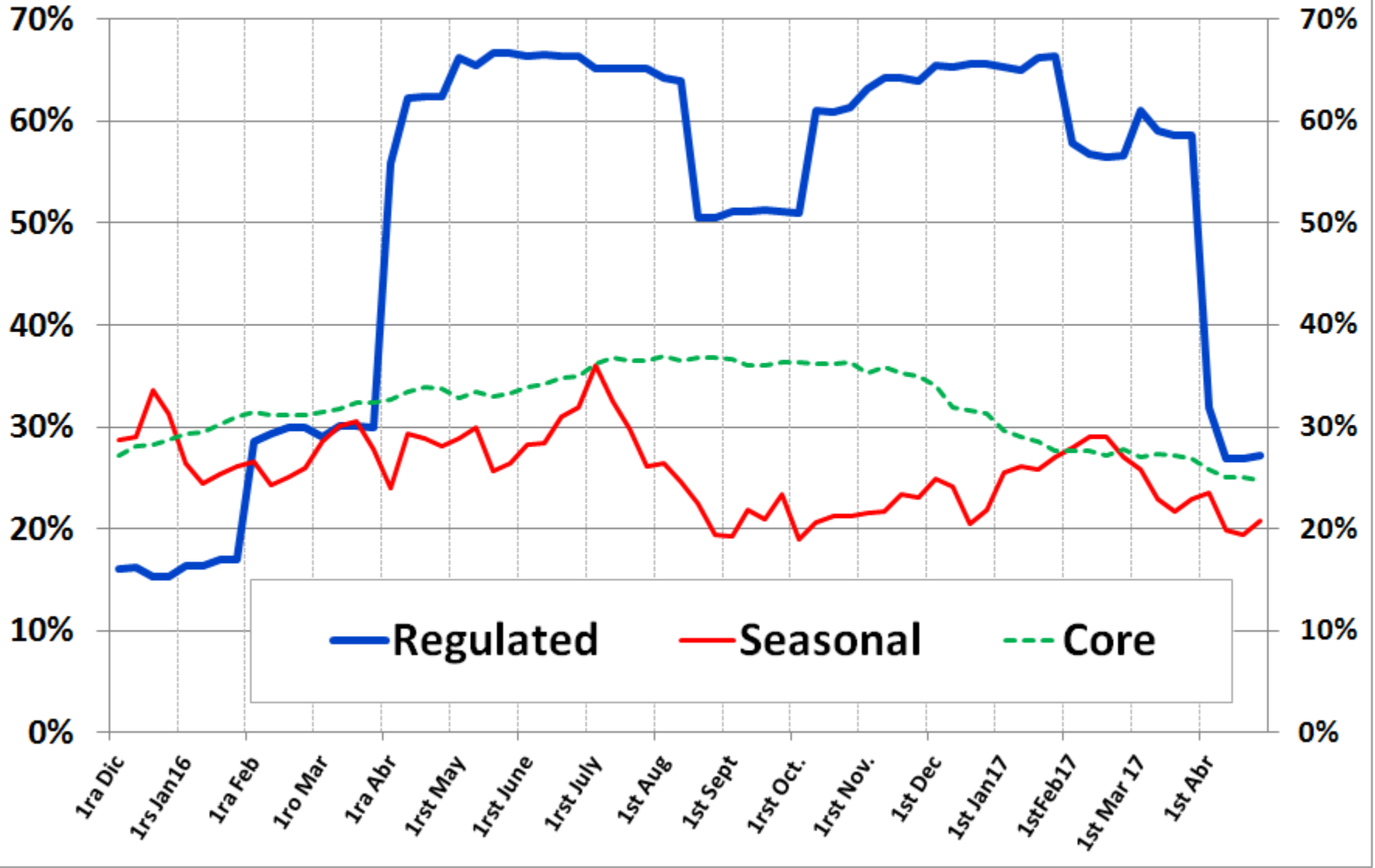
Monthly inflation in 2016: Total, Core, Regulated and Seasonal



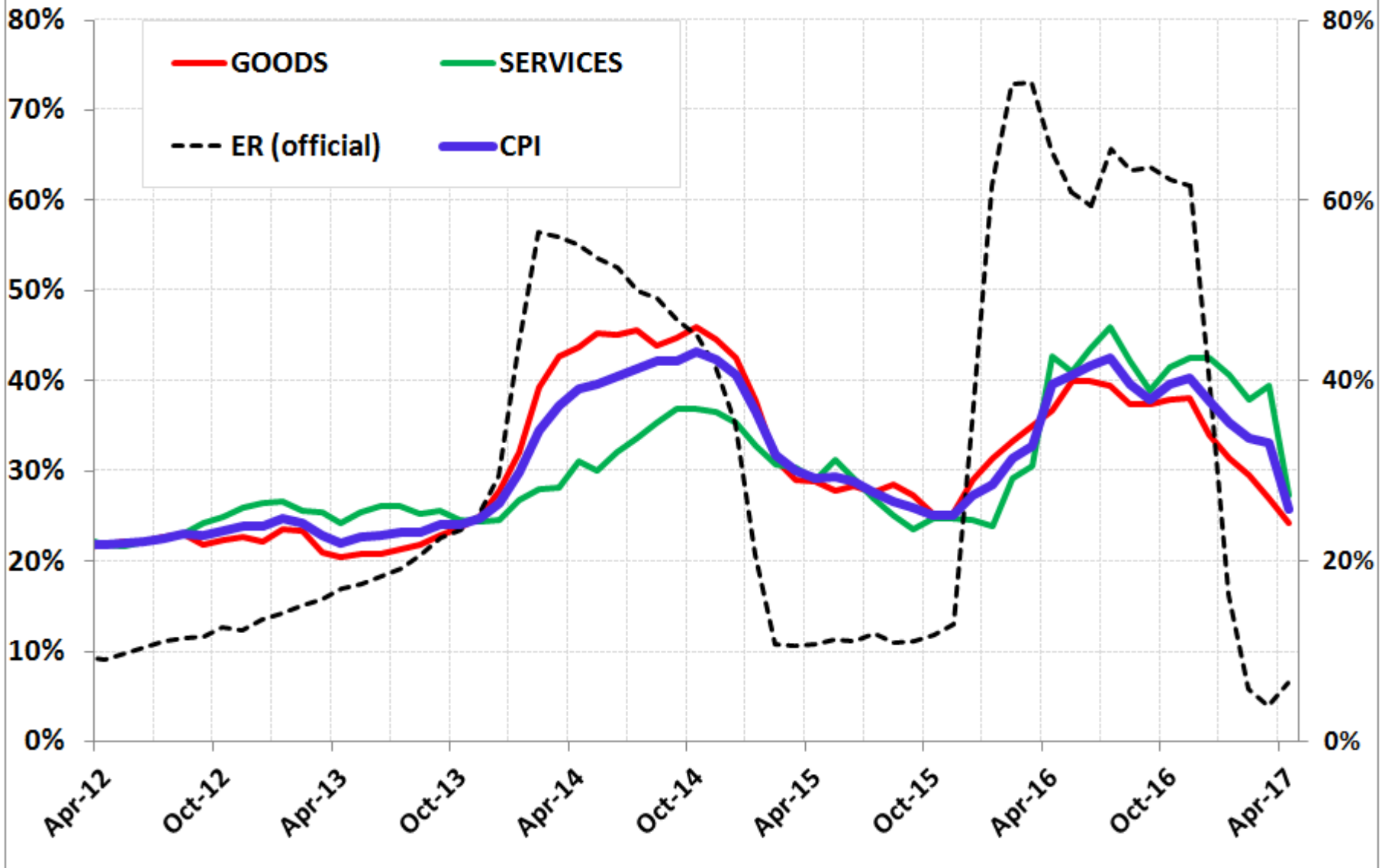
Acceleration in Q1 2017 followed by reversion in Q2



Annual % change in prices FIEL CPI (City of BA)

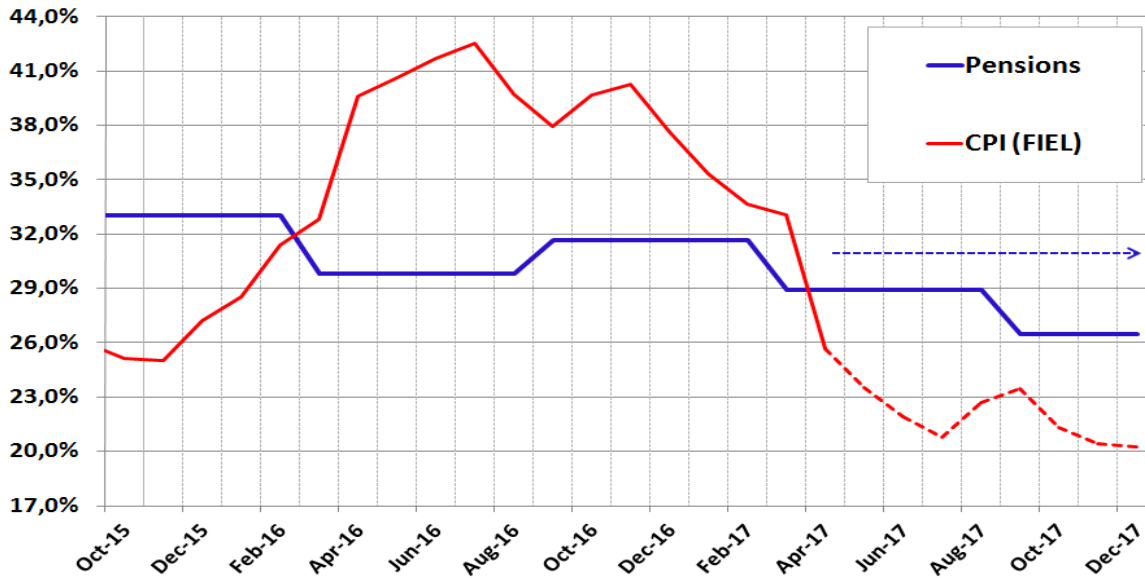


INFLATION (FIEL-CPI) and ER devaluation



Pensions and inflation

Year on year % change

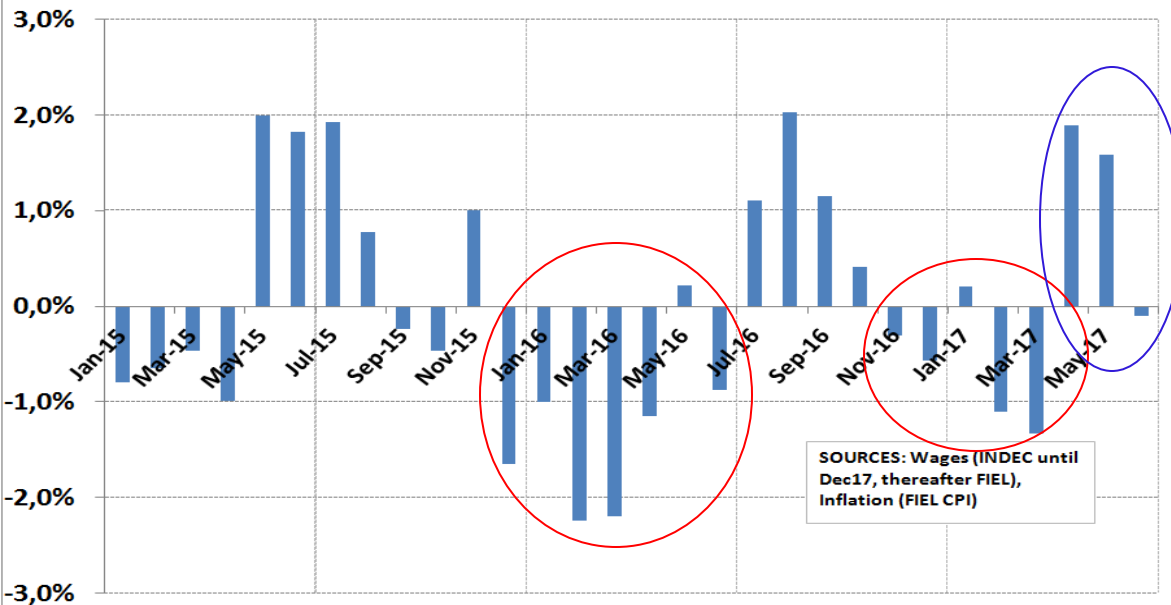


Pensions benefit from backward looking adjustments.

Additional payments (not pictured here) account for 0.8% of GDP

Private Formal real wages

monthly % change



Wages: recovery in real terms since Q2 (lower inflation)

Inflation: summary

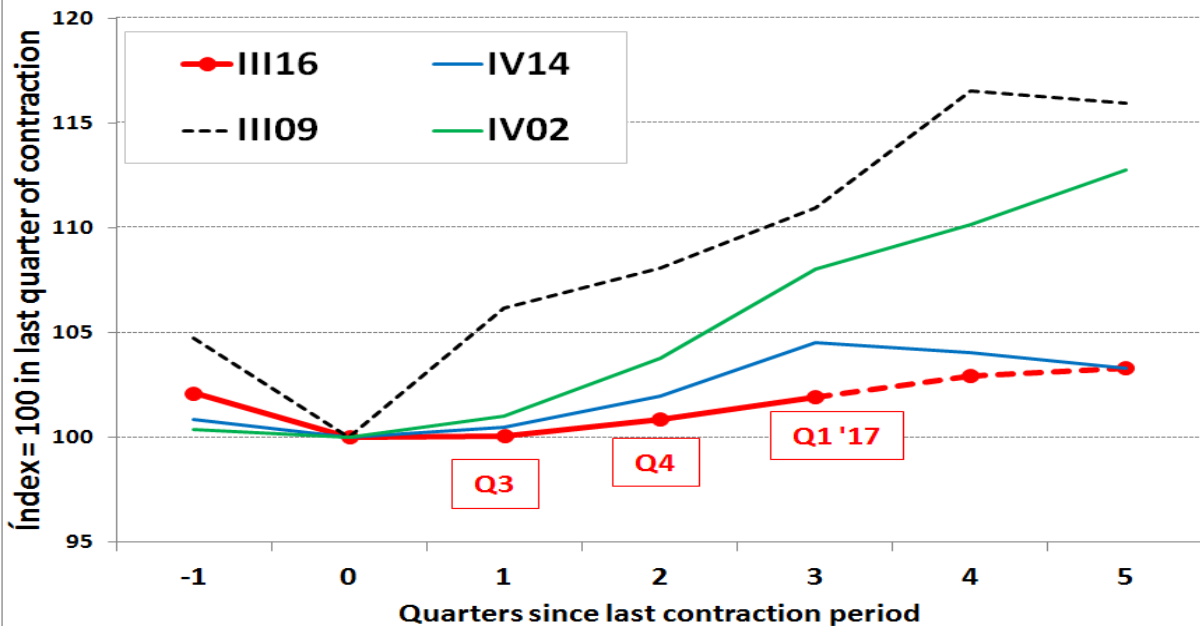
Inflation is on the path to converge to a monthly rate below or close to 1.3% for most of the rest of the year.

The average annual rate for 2017 will approach 24.7%, 13 percentage points below the average rate in 2016 (37.9%).

December rate (yoy) is expected to be 2-3 pp above the upper bound of Central Bank target (FIEL current estimate: 20%)

Inflation could pick up late in the year (after October) due to several factors, including tariff adjustments delayed in the first part of the year and an excess of monetary supply over demand (due to fiscal dominance and the strategy chosen to finance the deficit).

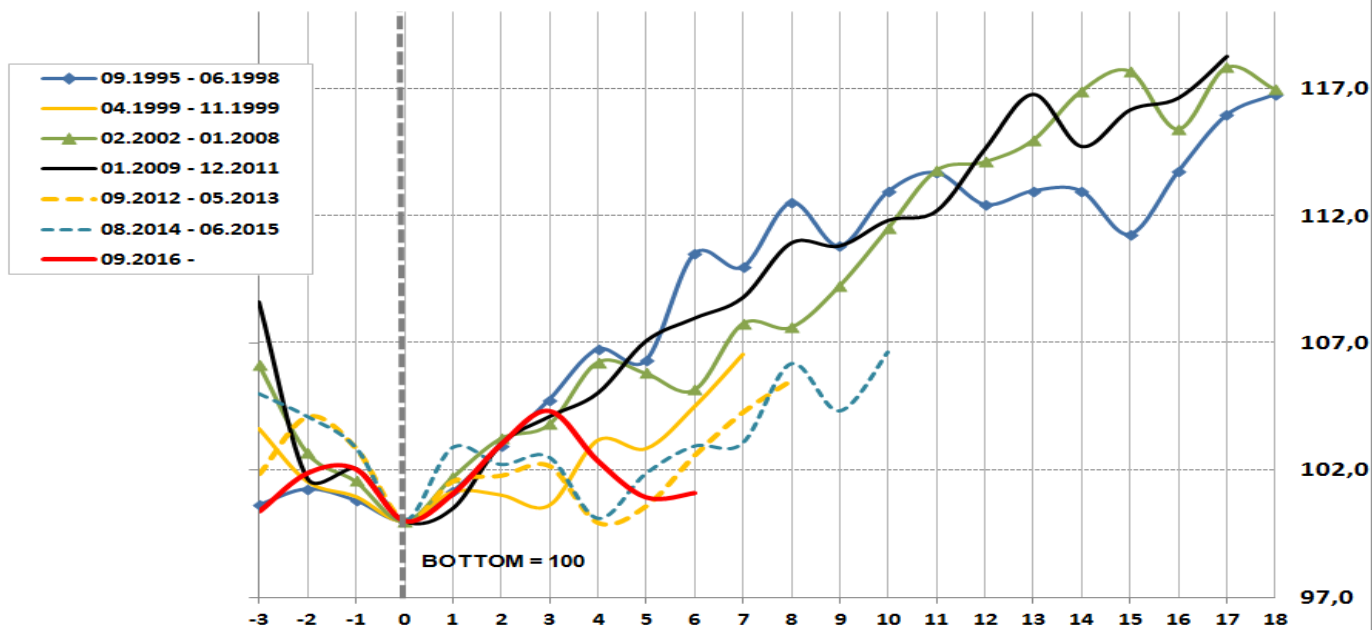
GDP: Speed of recovery from recessions



The real economy: a slow recovery

IPI (FIEL). Speed of recovery from bottom of recession

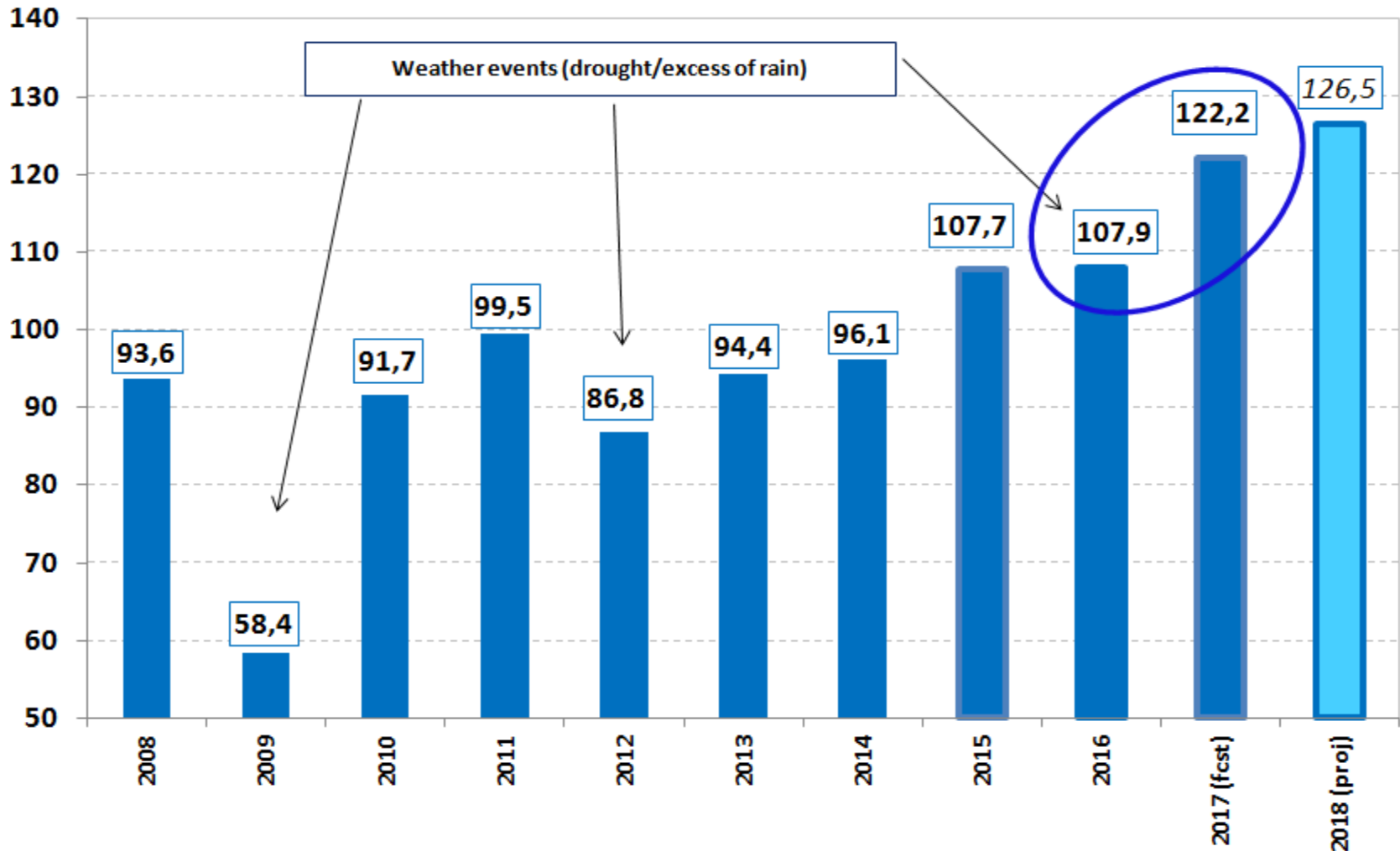
Number of months after end of recession (month=0)



Agriculture: major jump in production since harvest 2016/17

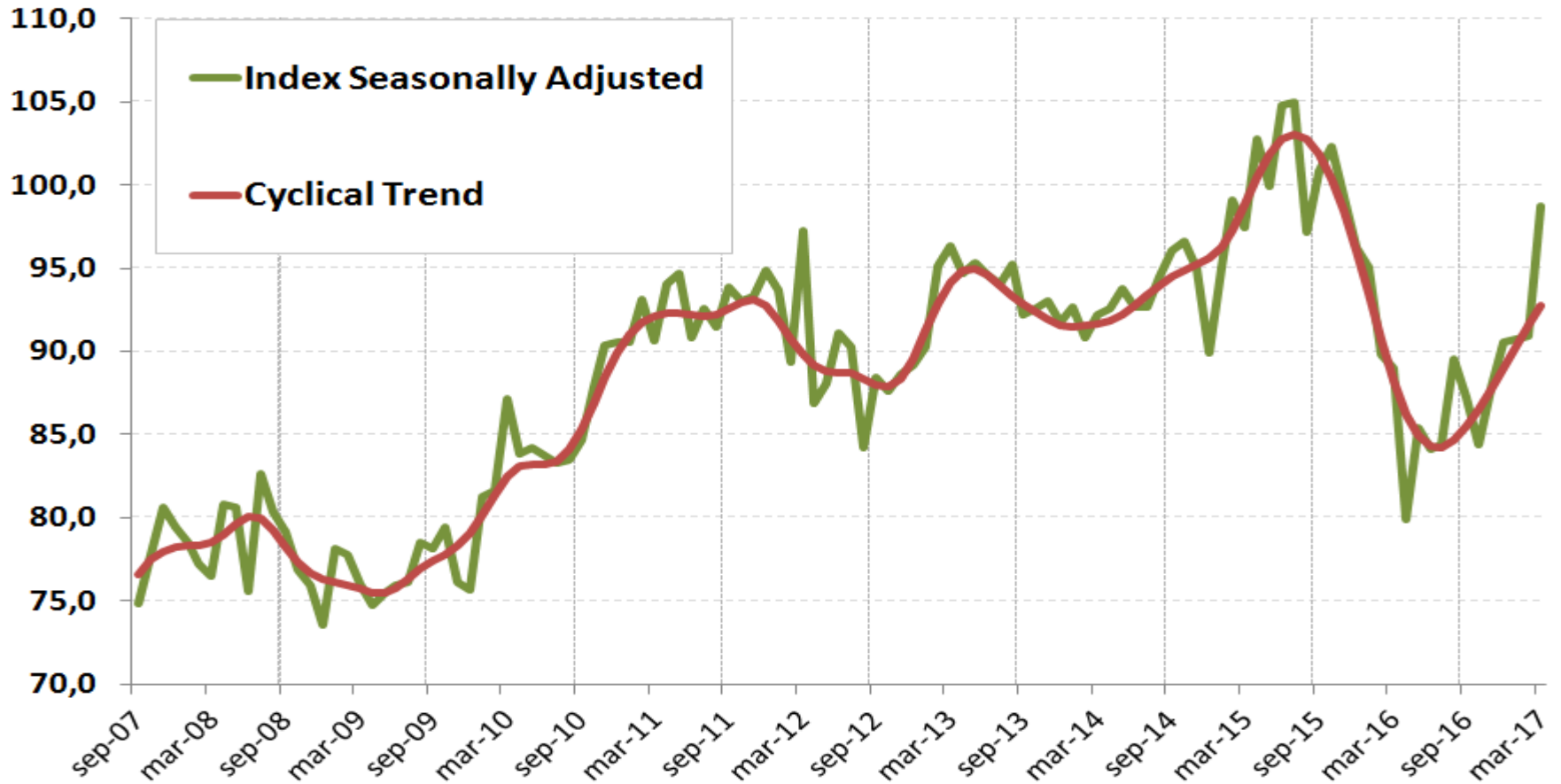
Expect strong growth to remain in next years.

Agricultural production (Soybean, Corn, Wheat, Sunflower, Sorghum, Malting Barley)
In Million tons



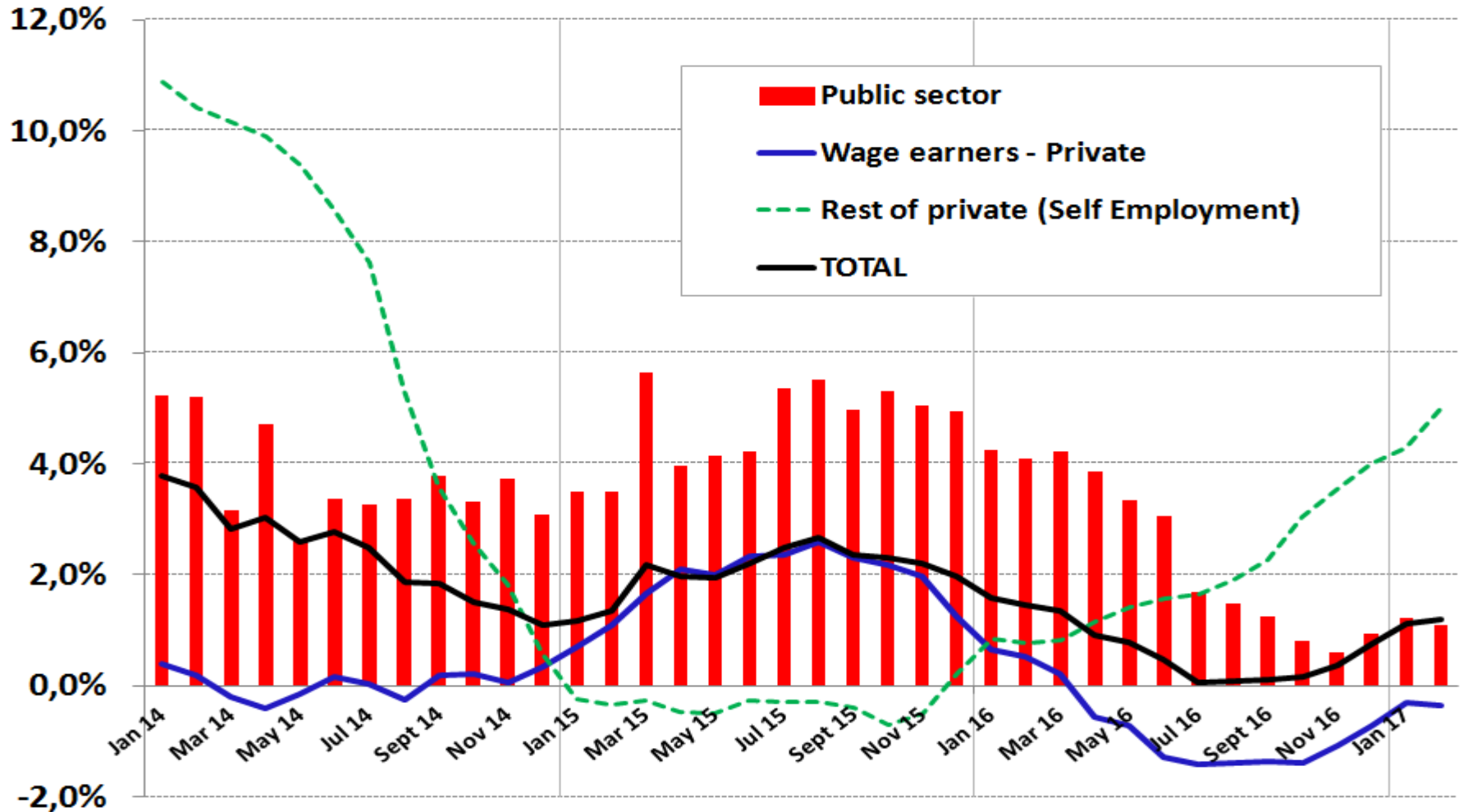
Public construction at full speed since 2nd Half 2016. Private works wake up in 2017: prices and real estate transactions go up

Construction activity (ISAC) Index 2015:100



Formal employment lags: moving to self employment

Formal employment Year on year % change



Perspectives: FIEL projections for 2017

Variable	<i>Unit</i>	2016	2017*
GDP	<i>% change</i>	-2,3	2,4
Gross Investment	<i>% change</i>	-5,5	6,0
Private Consumption	<i>% change</i>	-1,4	2,7
Inflation	<i>Average % ch</i>	37,9	24,7
	<i>December % ch</i>	37,7	20,0
Exchange rate	<i>\$/USD, Avge</i>	15,04	16,10
	<i>\$/USD, December</i>	16,10	16,80
LEBAC rate	<i>December Avge</i>	24,75	23,50

*Note: * forecast*

Sources: INDEC, C Bank, FIEL Macro Forecasts (FMF)



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Regulation of public utilities: achievements, drawbacks and challenges

Santiago Urbiztondo

Council of the Americas, New York, May 2, 2017

Initial context for Cambiemos (Dec-2015)

Counter-reform during K-administrations (2003-15):

- tariff freezing,
- cost-plus spiking fiscal subsidies,
- cross-subsidies,
- regulatory discretion, institutional degradation,
- investment contraction,
- late quality deterioration,
- spiking marginal costs,
- systemic energy crisis, reversed energy trade balance, etc.

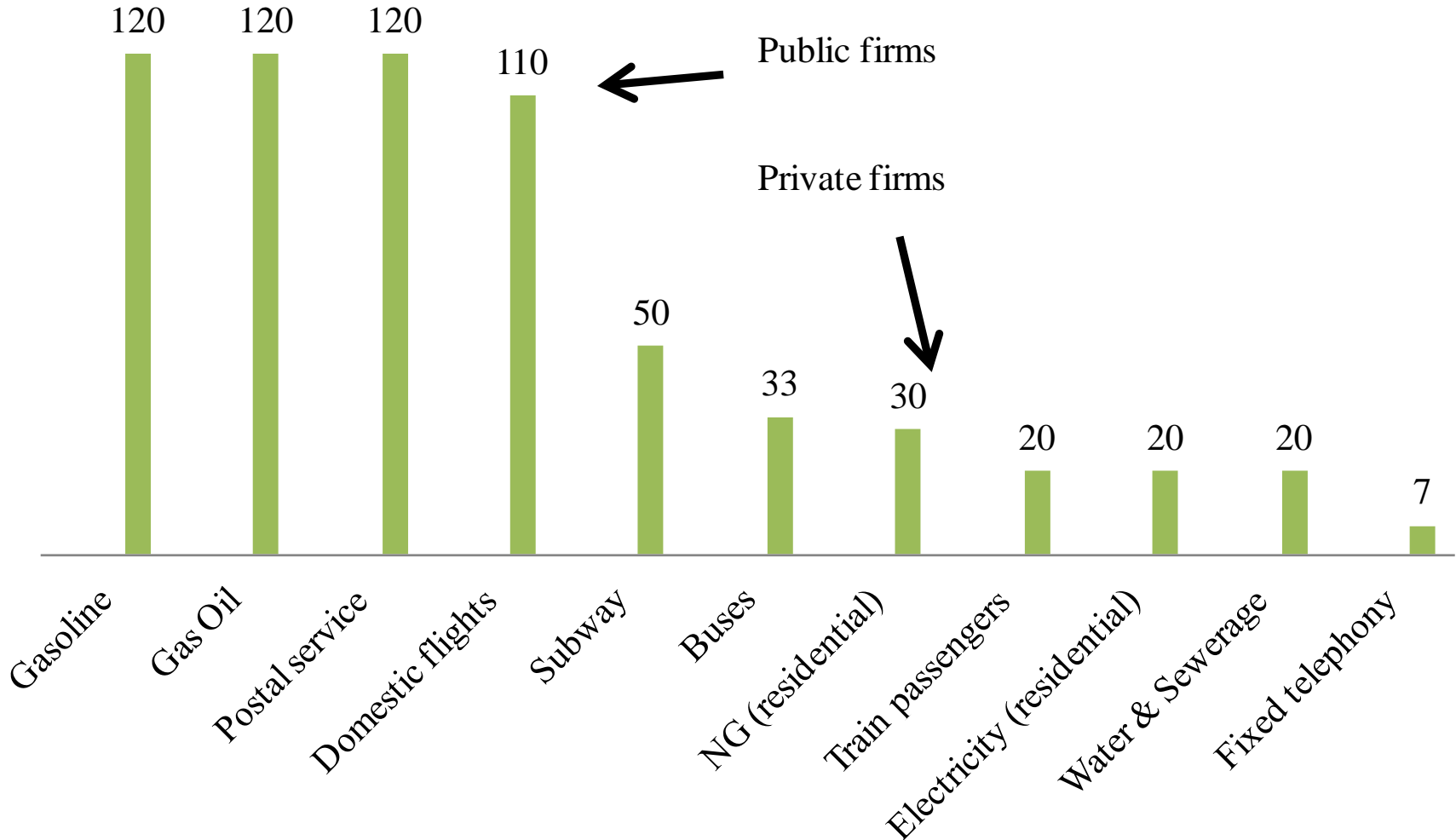
Overall task: Four dimensions of “normalization”

- reduce fiscal subsidies (higher tariffs)
- attract investment
- minimize distributive (& political) impact
- avoid inflationary shock

Initial context for Cambiemos (Dec-2015)

Real tariffs in 2015 (2001=100)

Source: based on sectorial information; retail deflator



The strategy adopted

Immediately:

- Deal with emergency in electricity sector (small scale emergency power additions), and renewable energy auctions
- Significant tariff & regulated wholesale price hikes in all public utility sectors, with focalized social tariffs for the poor
- Start normalization of energy T&D concession contracts through RTI (“integral tariff reviews”), within 1 year
- Start process to end intervention of ENARGAS

August 2016:

- Supreme Court ruled against NG residential price-hikes, requiring Public Hearings
- Higher than expected inflation & recession pushed for slower pace of price hikes & subsidy reduction

Revised strategy:

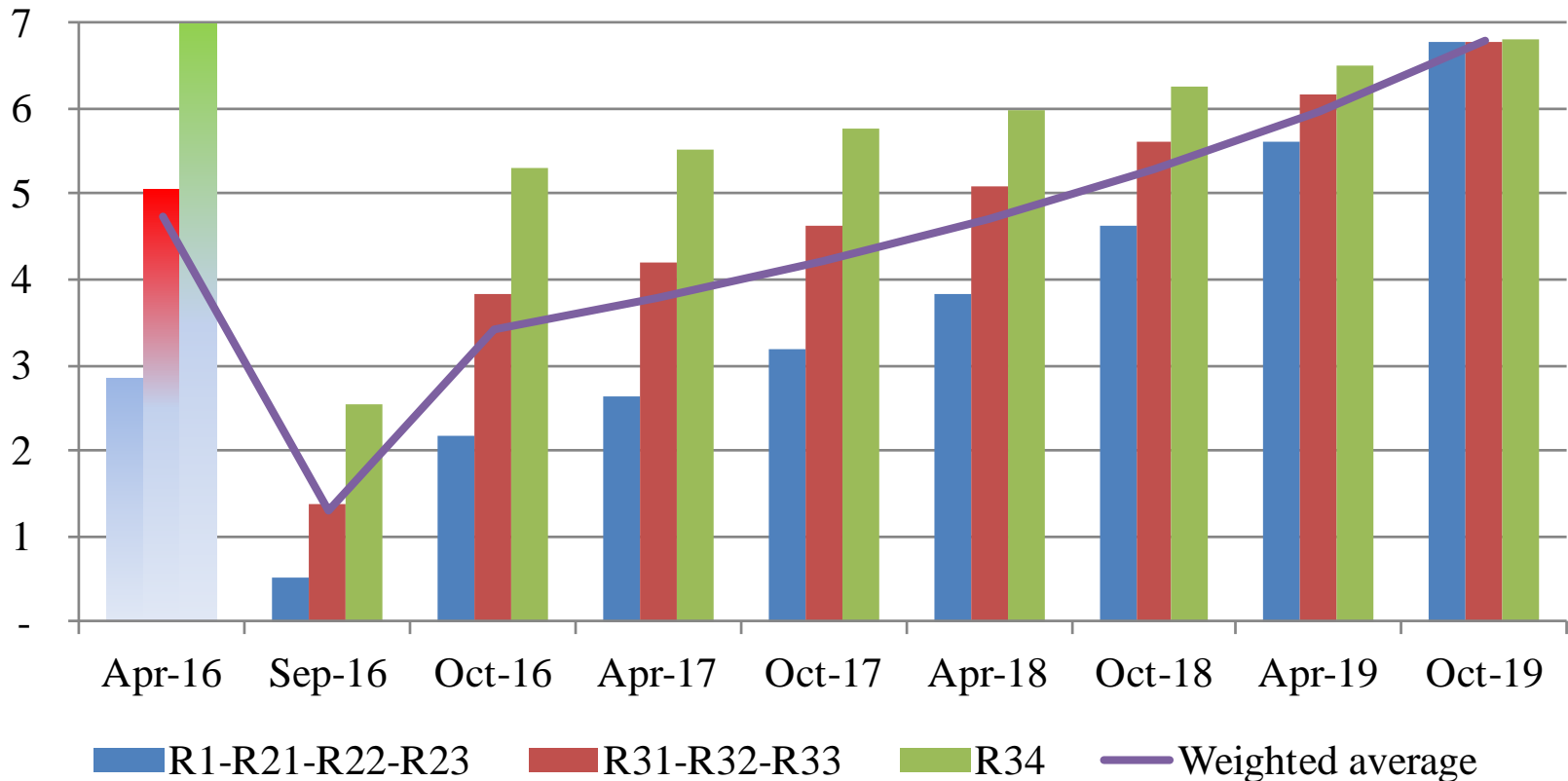
- Conduct Public Hearings, top maximum bill increases (400%), slow down price adjustments

•Achievements

Despite procedural mistakes (sidestepping Public Hearings), energy prices & tariffs are evolving towards actual opportunity costs (perhaps even more)

NG upstream prices for residential users: Values sanctioned in Apr-2016, and announced evolución post-Supreme Court ruling in Aug-2016

In US\$/MMBTU. Source: MINEM



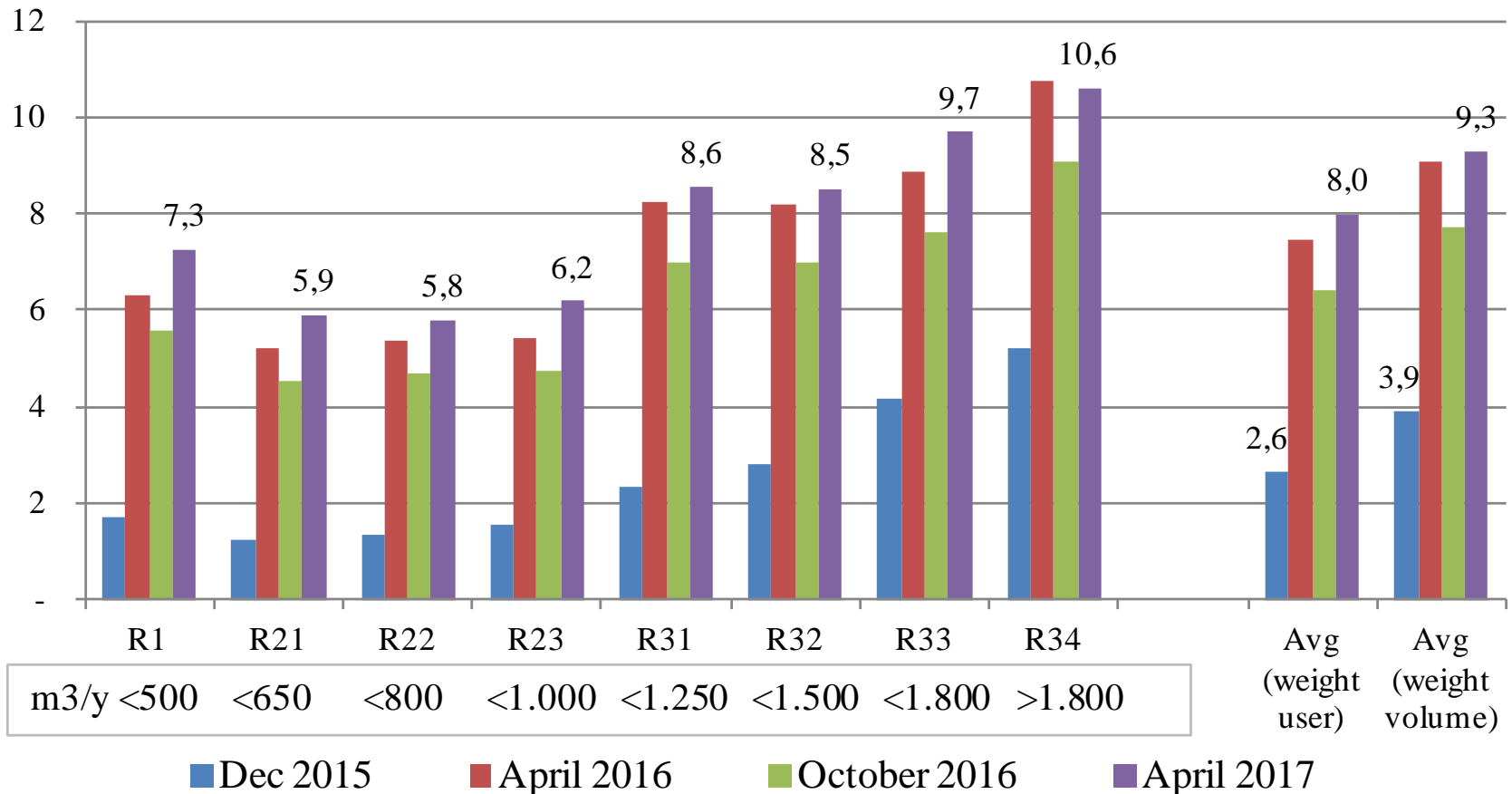
• Achievements

Today, T&D NG tariffs after RTI surpassed Apr-2016 hikes

40% average increase in T&D margins pending in 12 months

100% average increase in upstream prices pending in 2.5 years

Metrogas: Residential tariffs, before taxes, in US\$/MMBTU

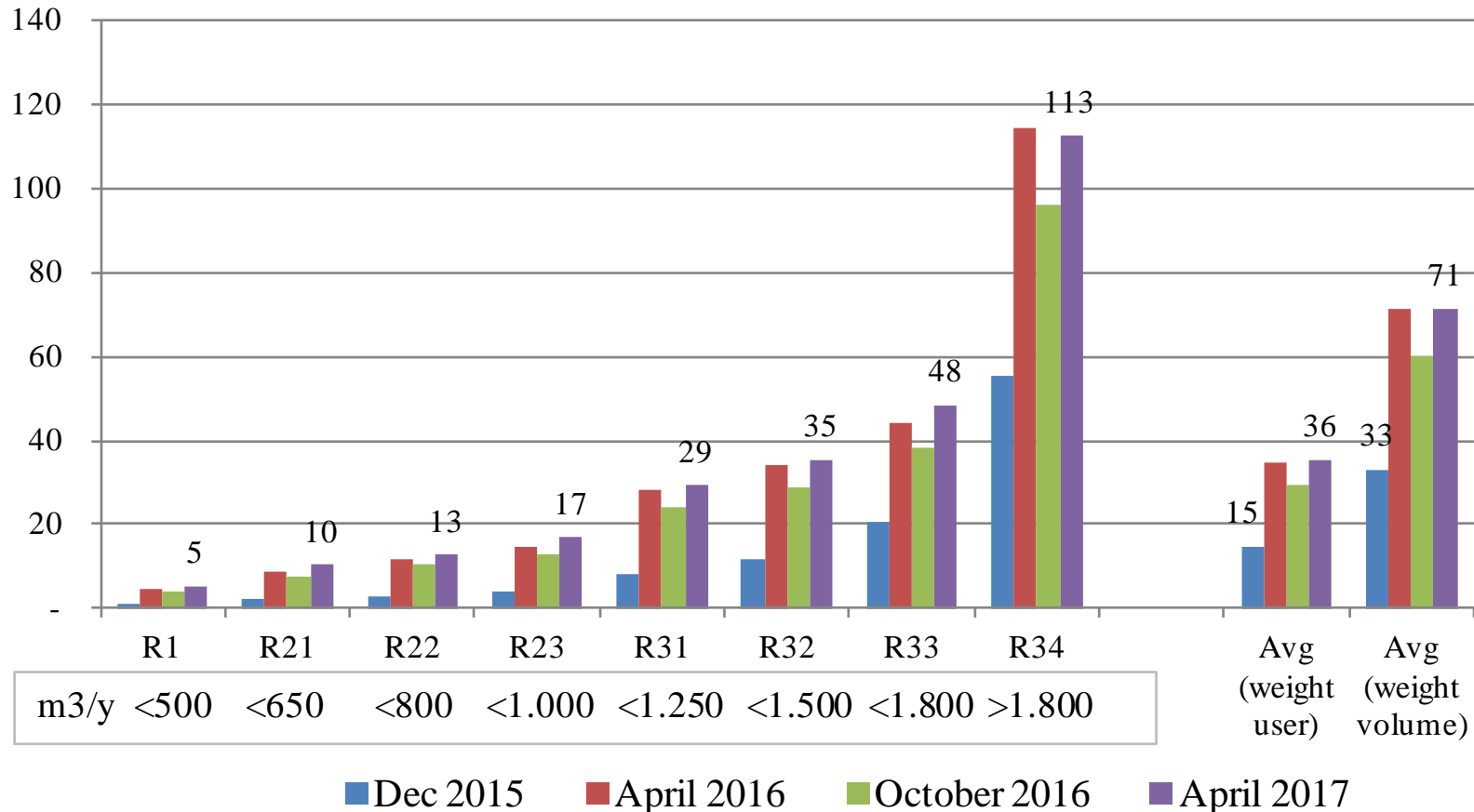


• Achievements

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- 40% average increase in T&D margins pending in 12 months
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Metrogas: Estimated Residential bills, before taxes, in US\$/month



• Achievements

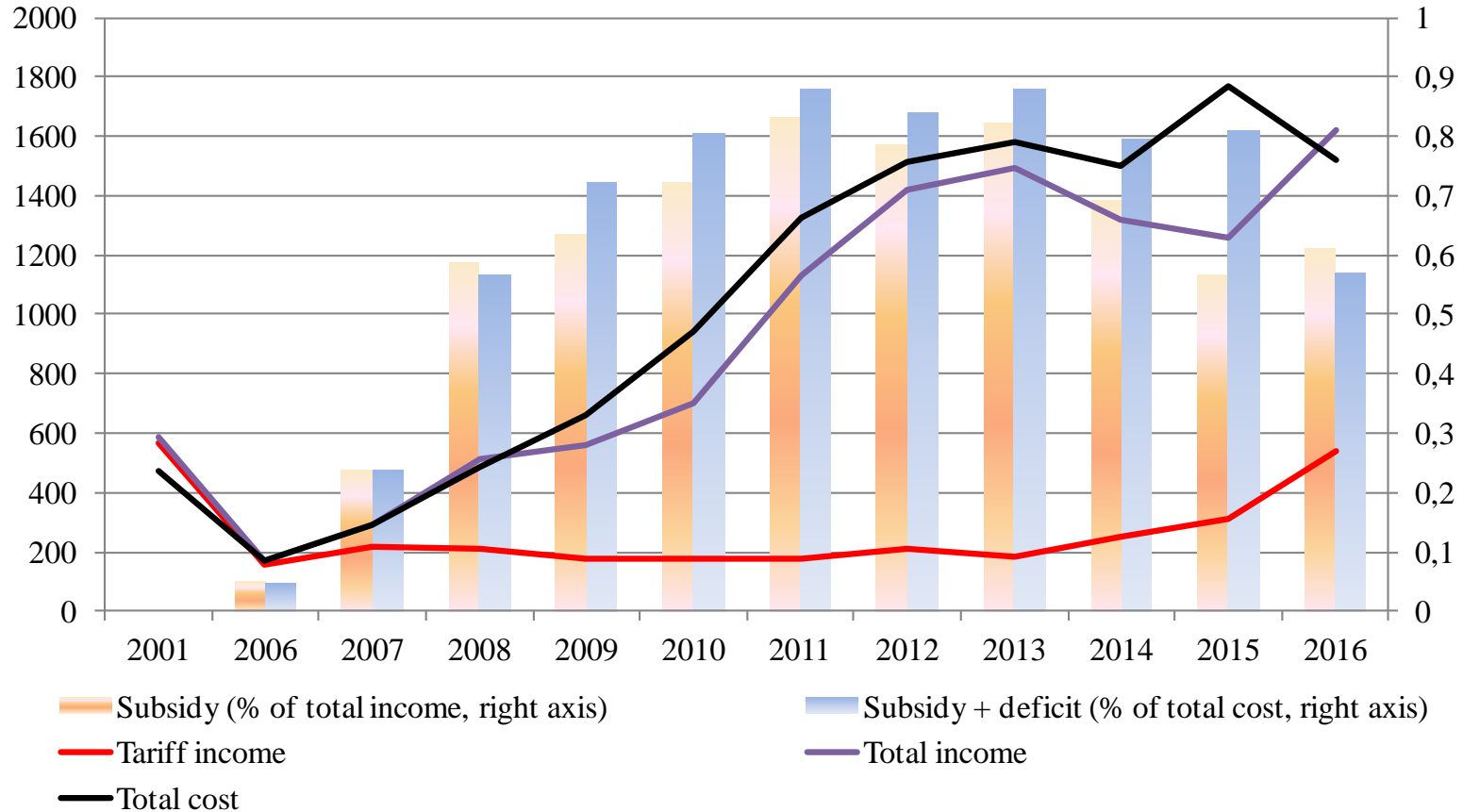
300% tariff hike in 2016 allowed 14% total US\$ cost reduction, eliminating AySA's deficit

In 2016, labor force up 3%, real wages constant, higher costs associated with tradable inputs

In 2017, AySA is receiving subsidies only for investment (with 27% yoy overall nominal fall)

AySA: Tariff income, subsidies, total income and total costs, 2001 & 2006-2016, in MM US\$

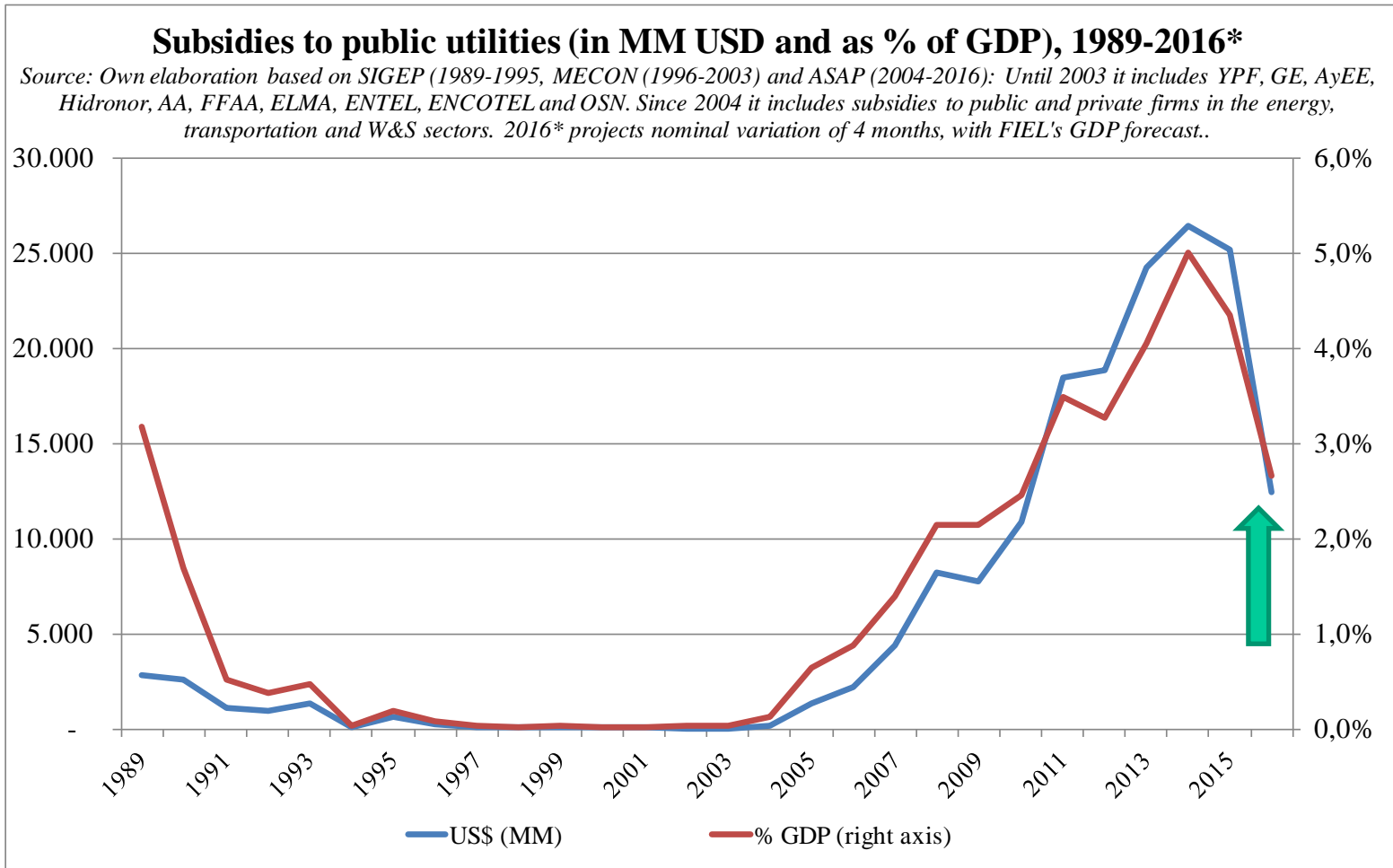
Source: Own elaboration based on AASA, ERAS & INDEC.



Impact on fiscal subsidies

Expectation / projection presented one year ago:

2016 (4-m): significant fall (50% in USD, 1.7 pp down, from 4.4% to 2.7% of GDP)
 2016 projected: final drop probably less, still around 1.5% of GDP



• Impact on fiscal subsidies

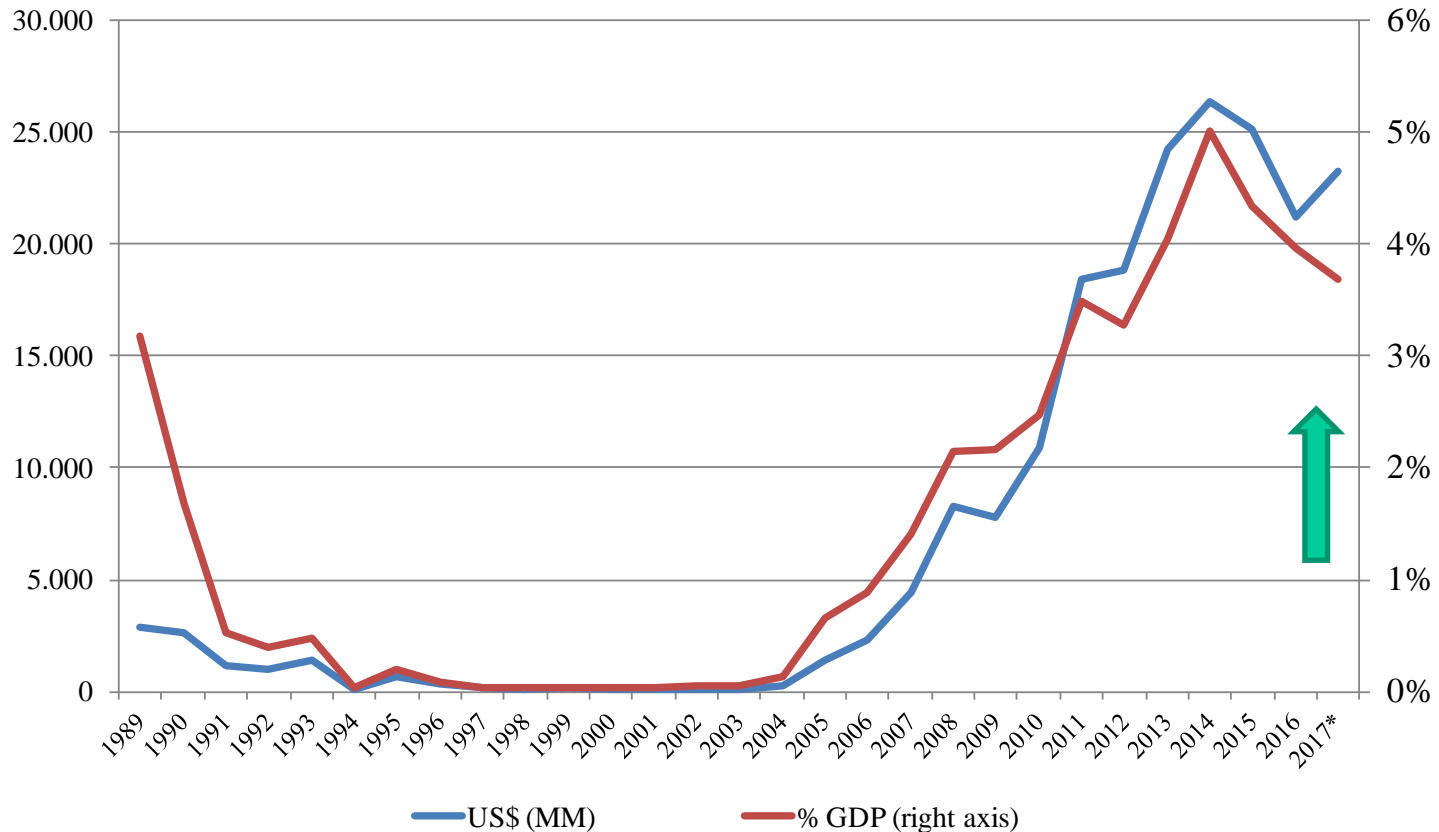
Reality / revised projections:

2016: less than 1% of GDP fall

2017 projected: no significant variation (higher tariffs OK, but also higher NG prices – imports and Plan Gas– & appreciated peso)

Subsidies to public utilities (in MM USD and as % of GDP), 1989-2017*

Source: Own elaboration based on SIGEP (1989-1995), MECON (1996-2003) and ASAP (2004-2017): Until 2003 it includes YPF, GE, AyEE, Hidronor, AA, FFAA, ELMA, ENTEL, ENCOTEL and OSN. Since 2004 it includes subsidies to public and private firms in the energy, transportation and W&S sectors. * Own estimation based on first quarter.



• Drawbacks

**Institutional reform: new ENARGAS directory with upstream NG
–not T&D or overall regulation– background dominance**

**Public Hearings seen as a non-substantial, formal, obstacle
(ENRE's RTI discussing firms proposals, deciding on
alternatives not debated)**

**Deepening cross-subsidies (besides social tariff) through
manipulation of cost measures (new electricity tariffs)**

**Extension of Plan Gas (higher prices on additional production)
only to non conventional NG in Neuquina basin (not
general, discriminates by region and technology, without
convergence plan & long-term market rule)**

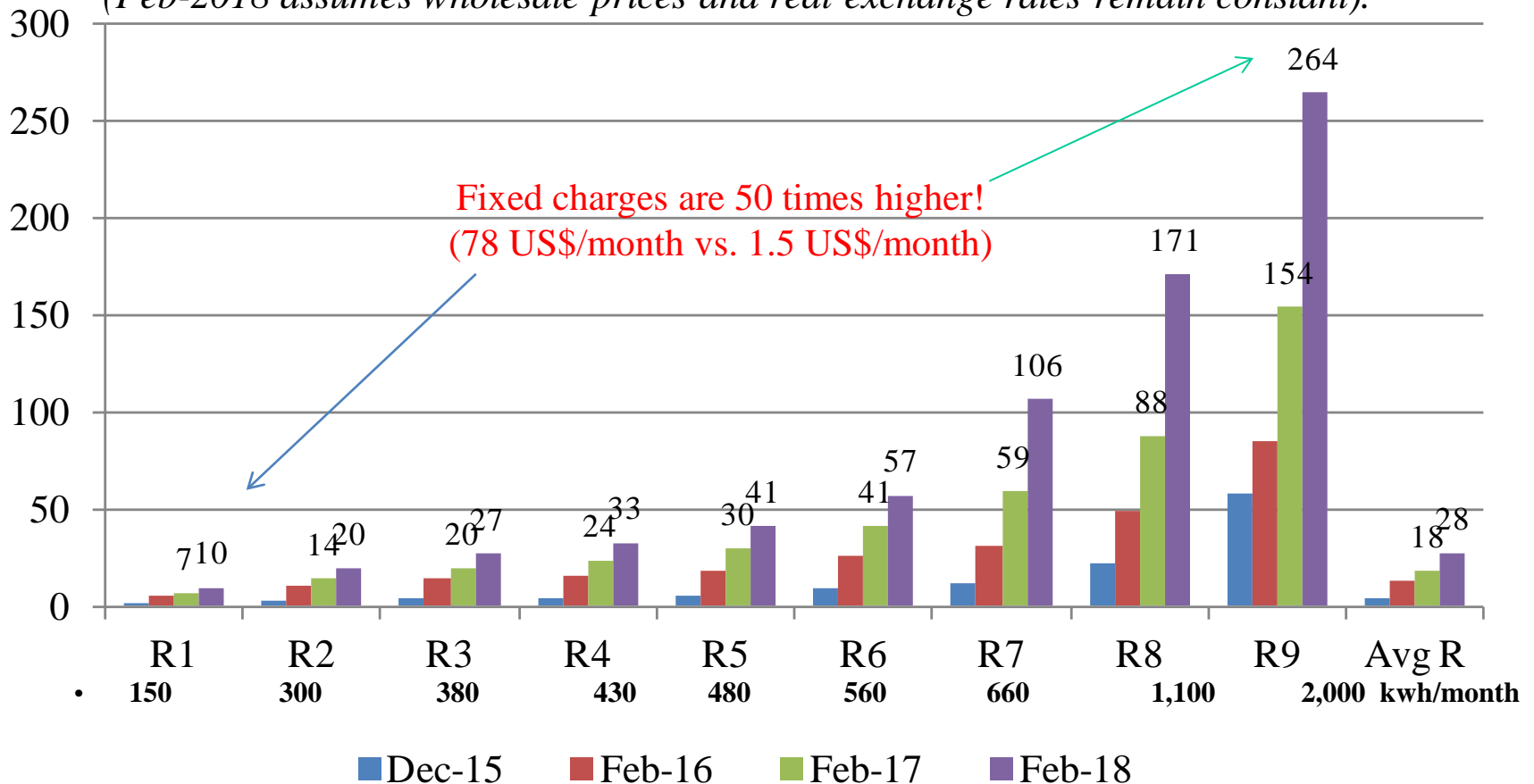
**No new contractual rules –to stop cost-plus subsidies– applying
to firms other than T&D NG and electric utilities**

• Drawbacks

Electricity tariffs after RTI: Deepening cross-subsidies (on top of social tariffs) through manipulation of cost measures, “designing” residential fixed distribution costs to induce rational use, in fact bypassing legal ban (new electricity tariffs)

Edenor: Estimated Residential Bills, before taxes, in US\$/month

(Feb-2018 assumes wholesale prices and real exchange rates remain constant).

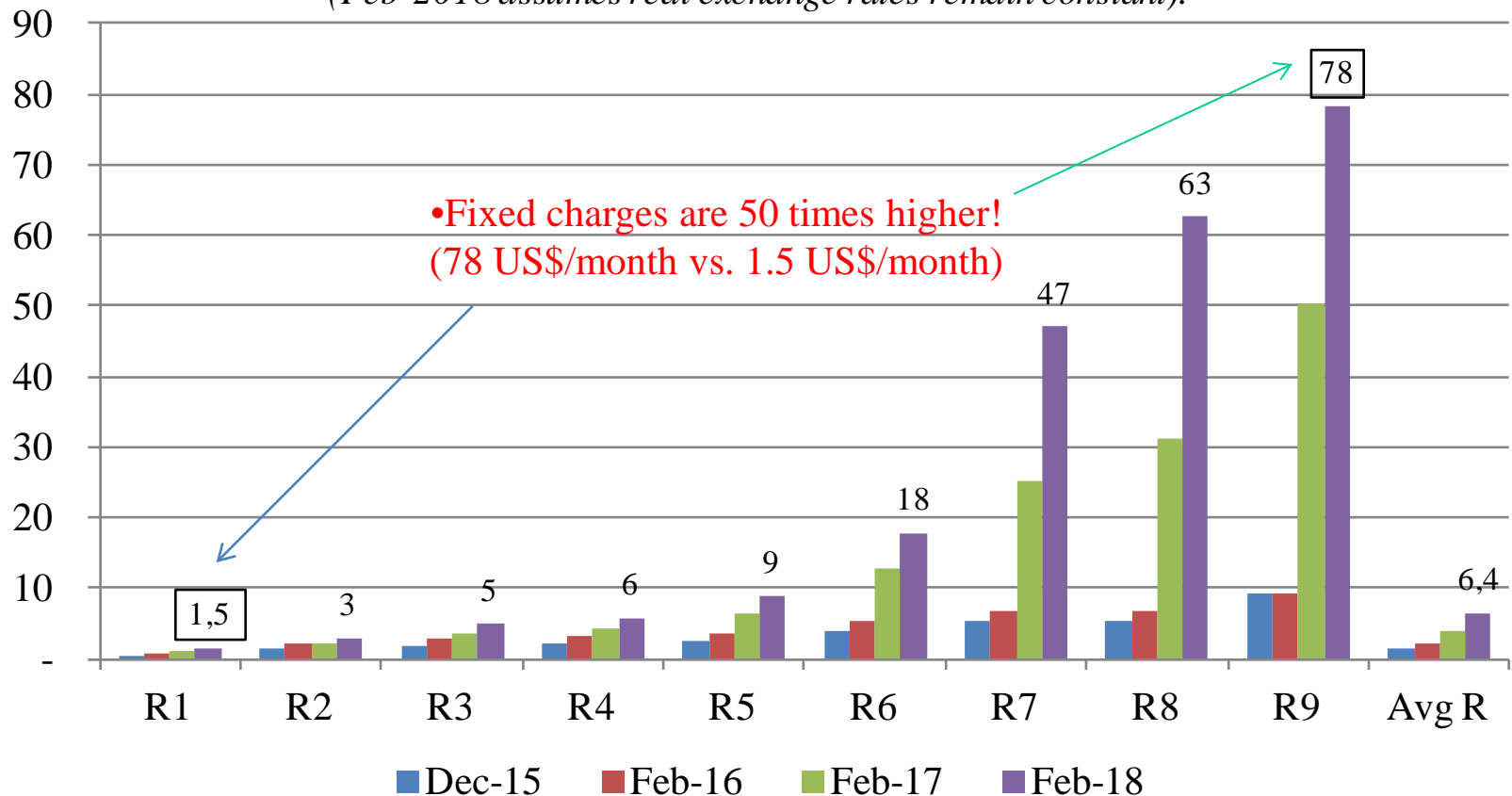


• Drawbacks

Electricity tariffs after RTI: Deepening cross-subsidies (on top of social tariffs) through manipulation of cost measures, “designing” residential fixed distribution costs to induce rational use, in fact bypassing legal ban (new electricity tariffs)

Edenor: Fixed Residential Charges, in US\$/month, Dec-2015 - Feb-2017

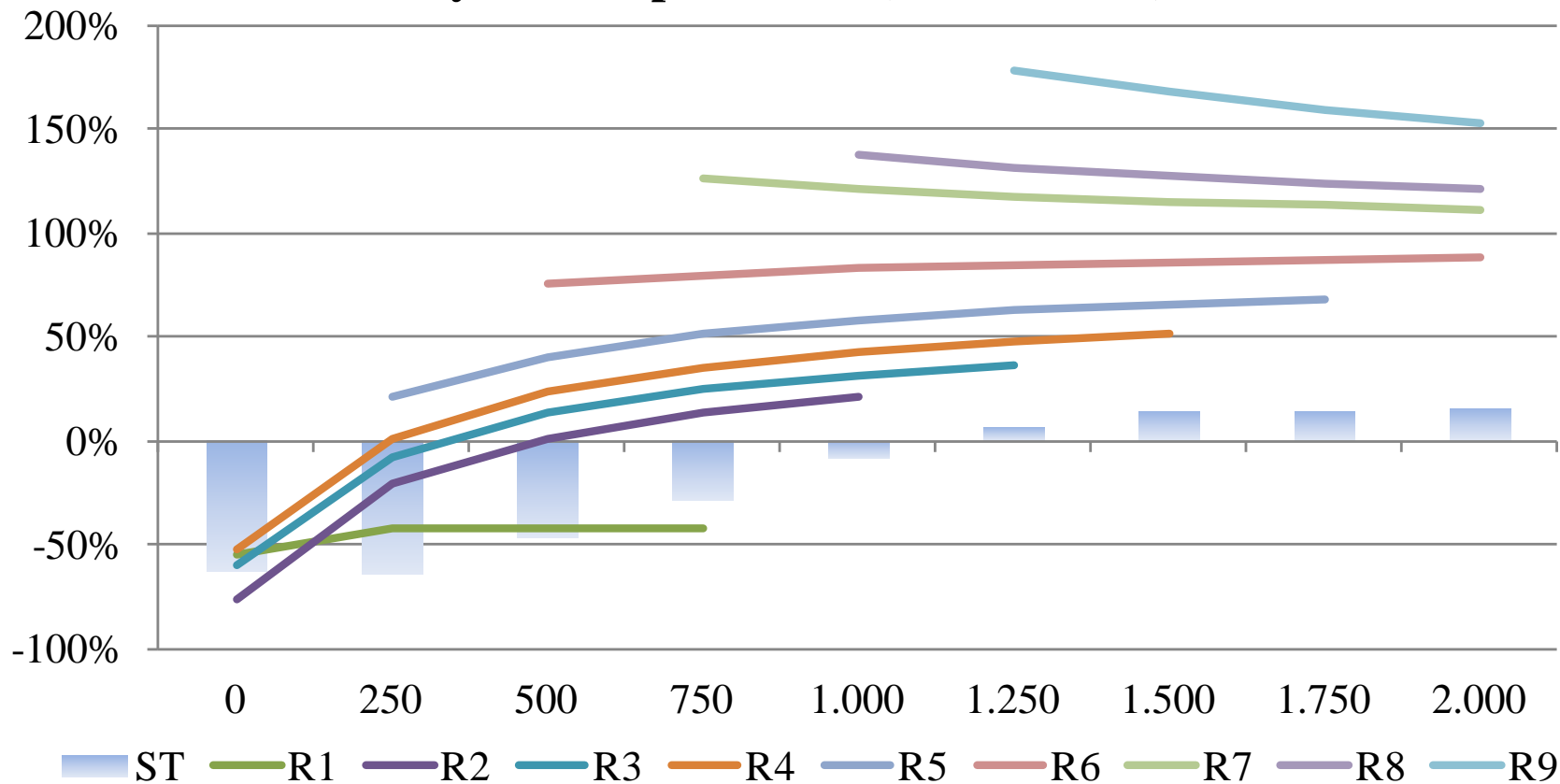
(Feb-2018 assumes real exchange rates remain constant).



• Drawbacks

Electricity tariffs after RTI: Deepening cross-subsidies (on top of social tariffs) through manipulation of cost measures, “designing” residential fixed distribution costs to induce rational use, in fact bypassing legal ban (new electricity tariffs)

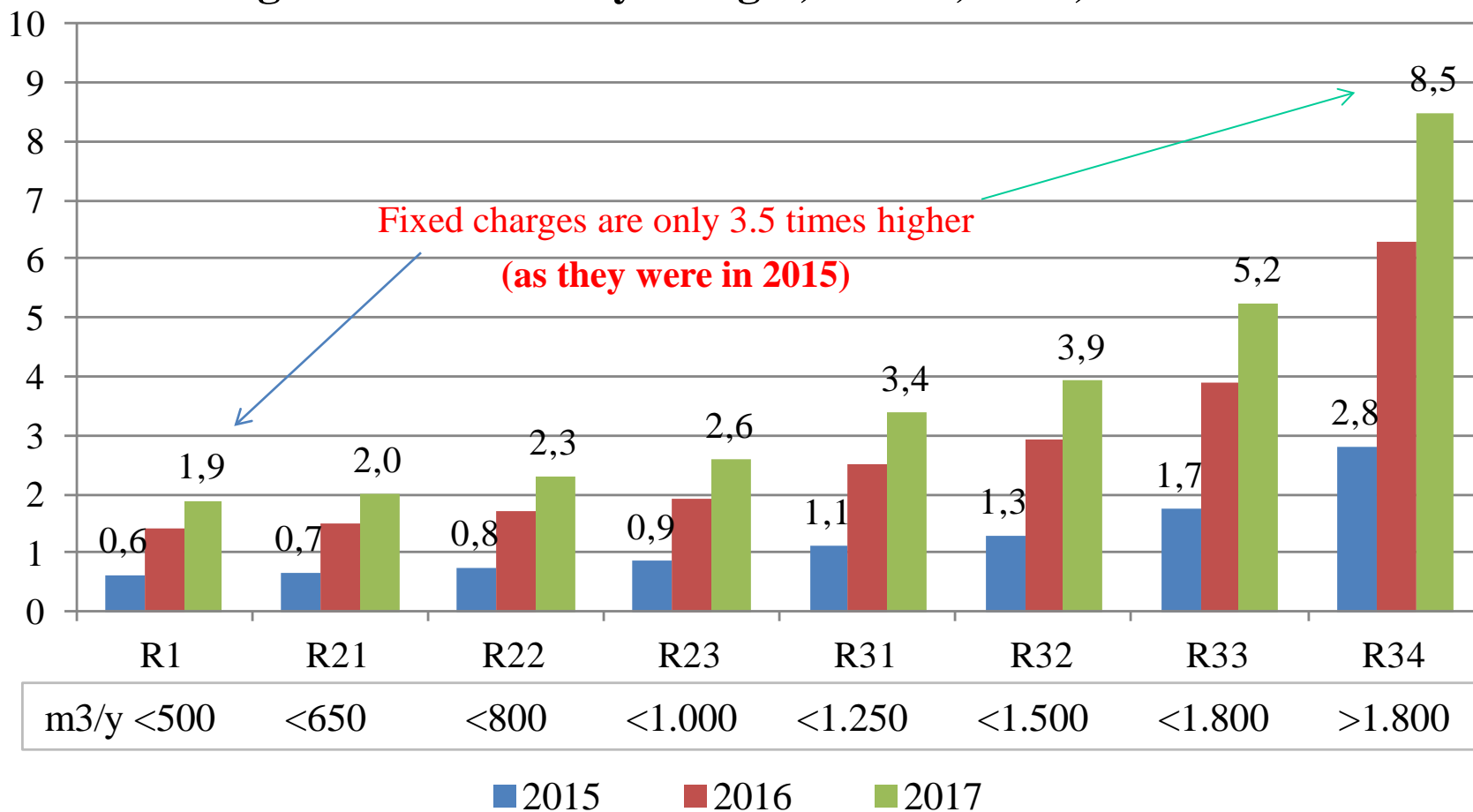
Edenor: Changes in US\$ Residential Tariffs, Dec-2001 to Feb-2017, by consumption level (kWh/month)



• Drawbacks

This manipulation did not occur in the NG RTI closed two months later by ENARGAS

Metrogas: Fixed monthly charges, in US\$, 2015, 2016 and 2017



•Challenges

New rules for price adjustments in competitive markets (energy) not announced yet:

Upstream NG & wholesale energy prices still set by the government, under cost-plus principle, approaching current marginal costs, without announcing long-term rule

New investments require knowledge of the rules that will govern them in the future, and paced convergence to unique competitive prices would be both credible and efficient

Need to clearly escape de facto cost-plus rule: raising tariffs without anchoring long-run costs will likely be excessive & deceiving

More generally, current efforts to cope with inherited “K counter-reform” need to be inserted into a new master-plan of consistent structural public utilities reforms



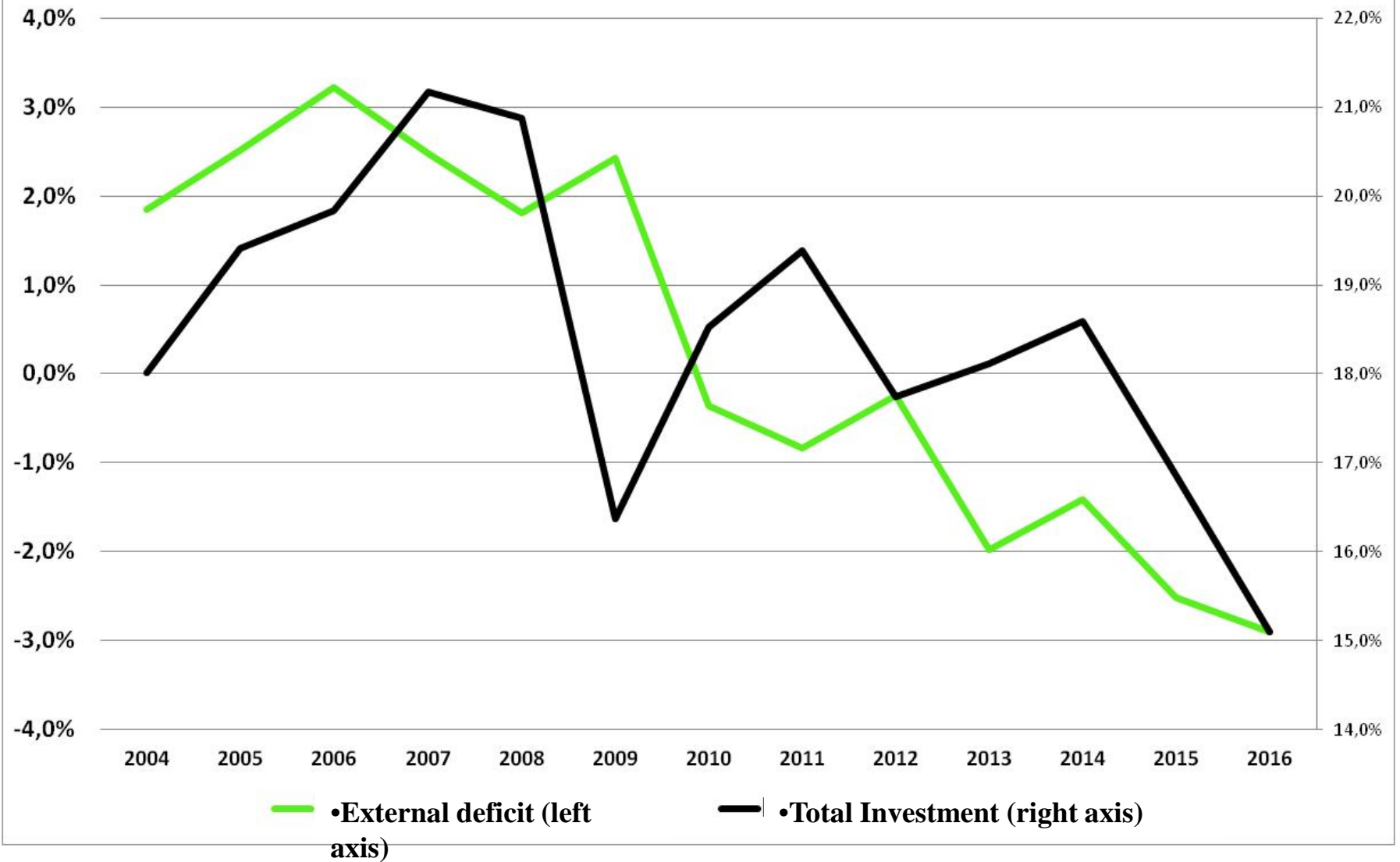
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Fiscal and External Challenges

Daniel Artana

May 2017

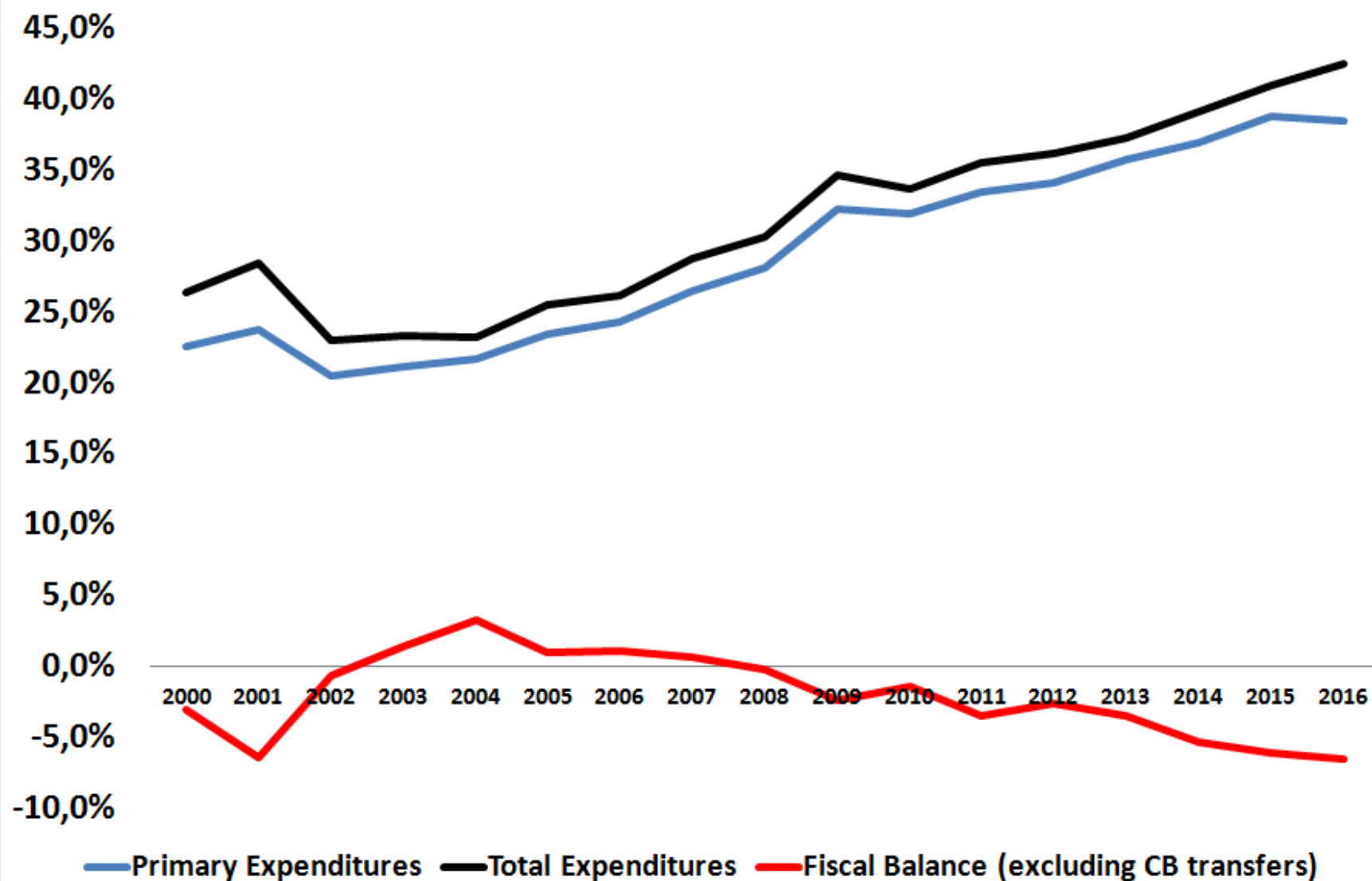
External Deficit and Investment (% of GDP)



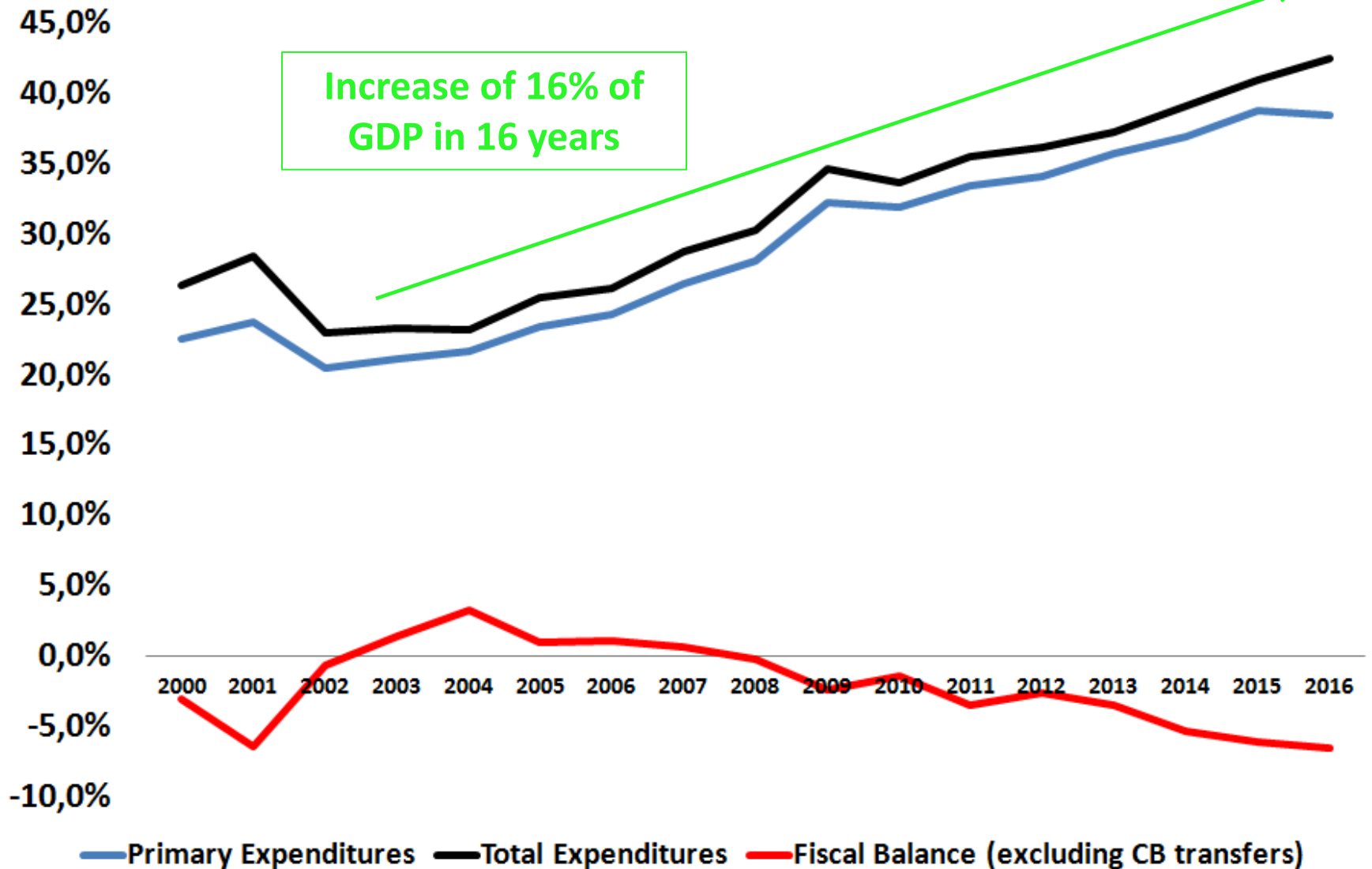
Large portfolio capital inflows in Q1 2017

TOTAL SOURCES	18,2	TOTAL USES	18,2
Foreign Direct Investment	0,7	Argentines' savings in foreign currency	4,8
Capital inflows for government & private sector	18,5	Accumulation of Reserves at the CB	11,5
Other	-1,1	Current account deficit	1,9
		o/w Tourism	2,7

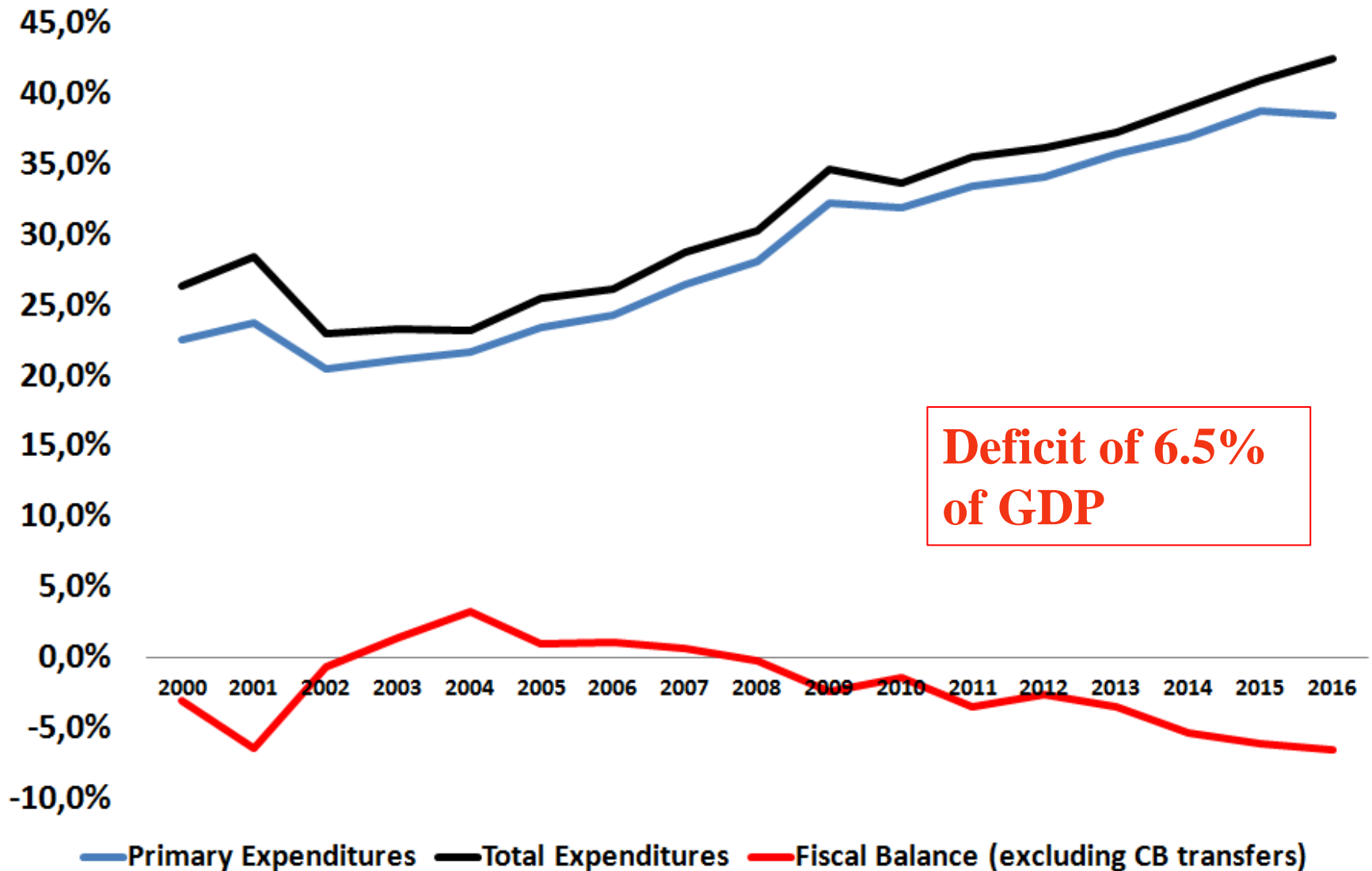
Argentina. General Government Expenditures and Fiscal Balance (% of GDP)



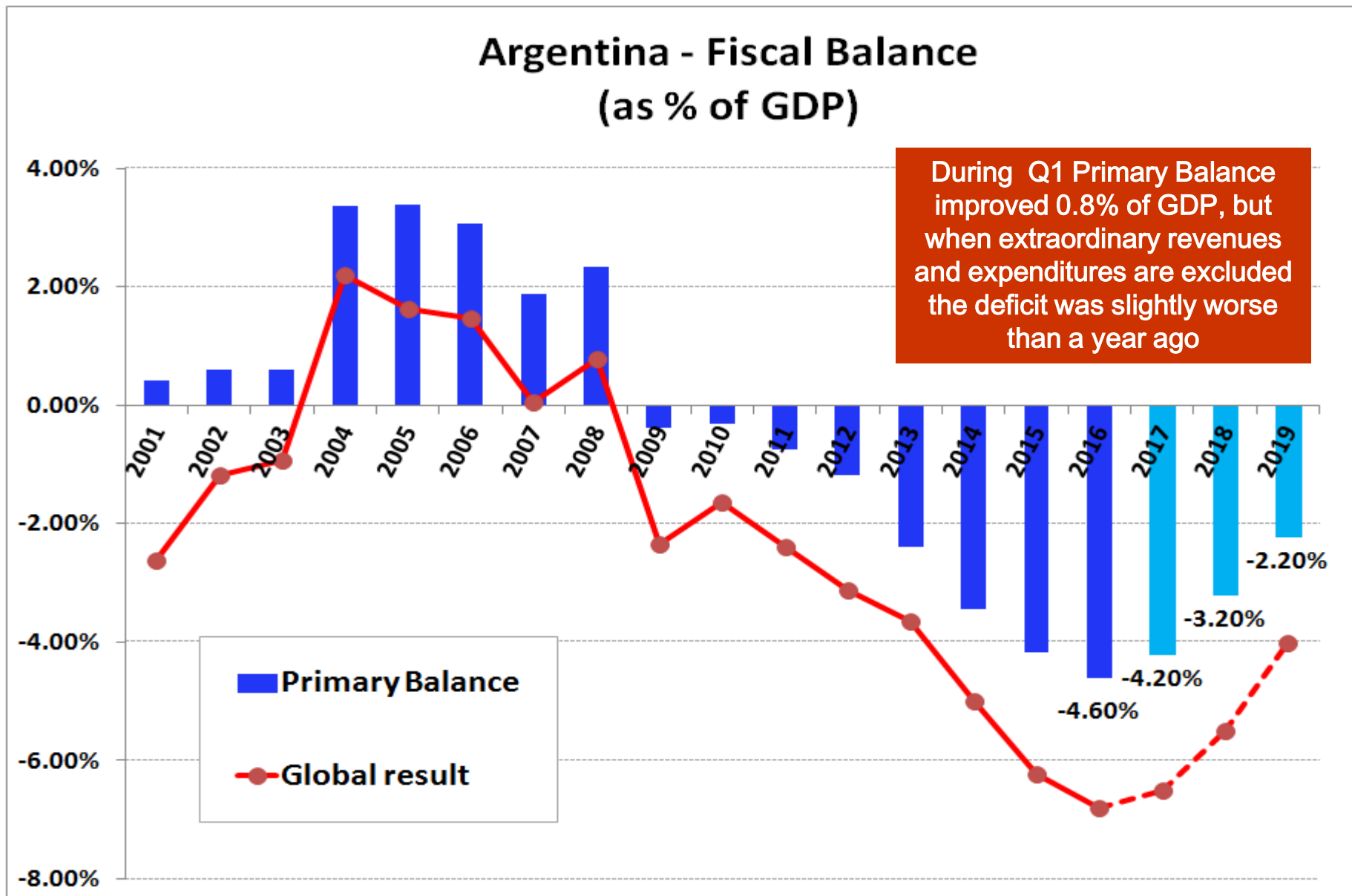
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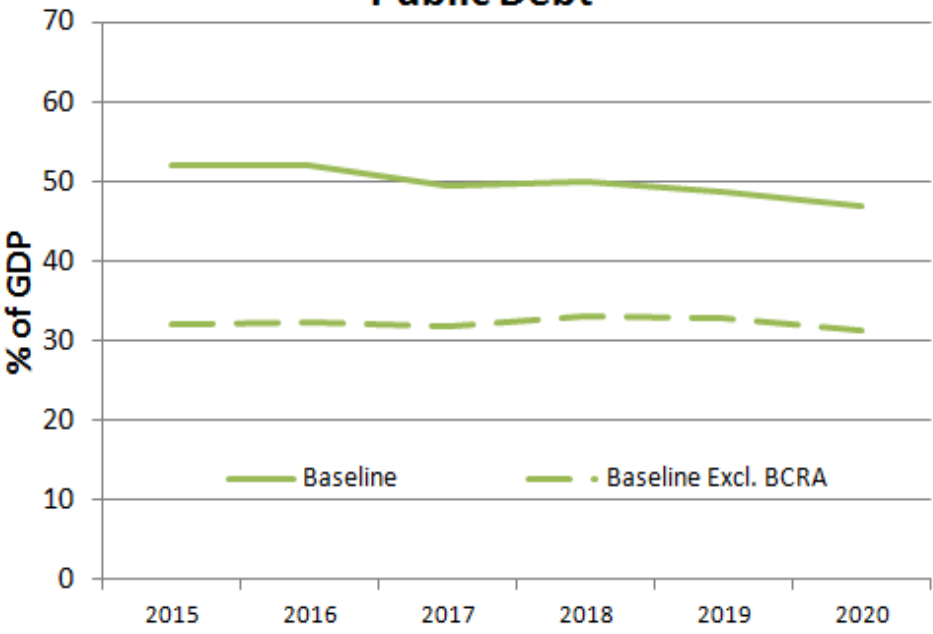
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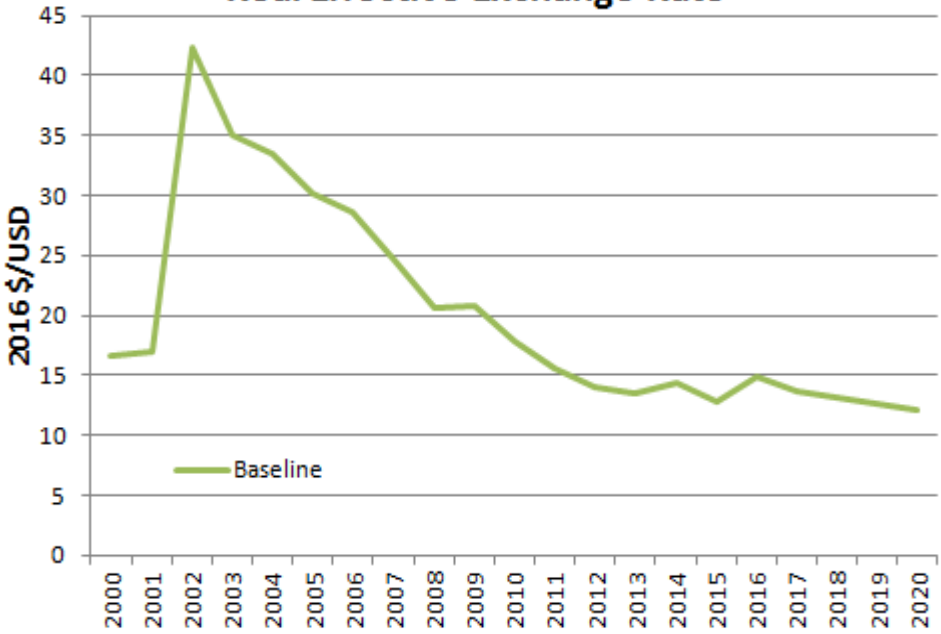
•A gradual program to reduce the fiscal deficit

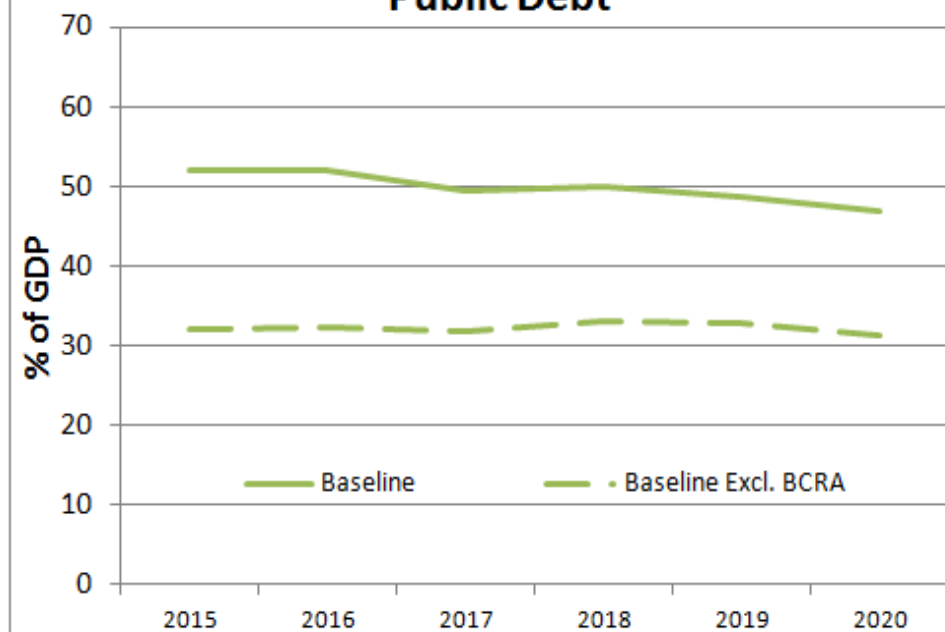
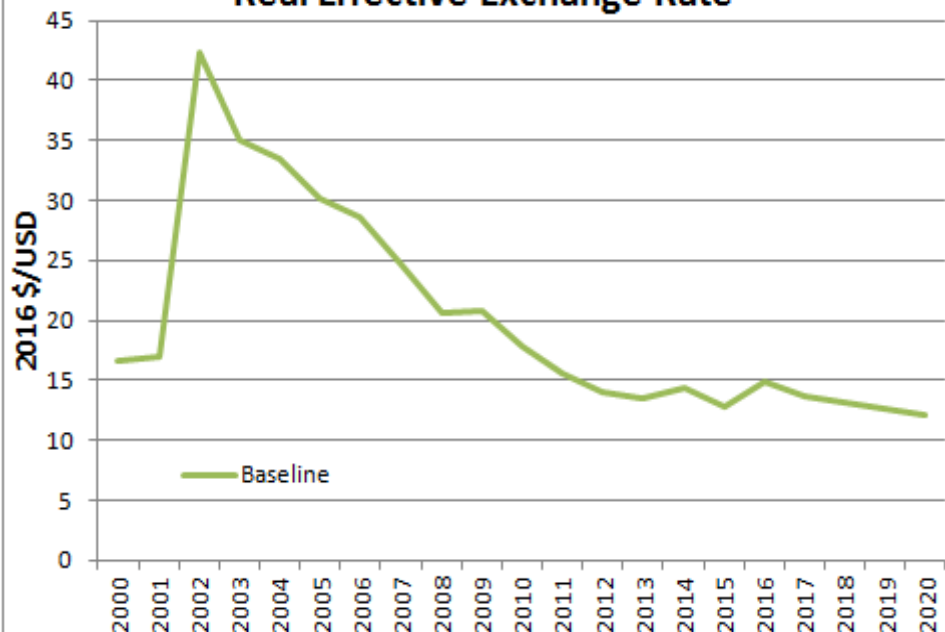
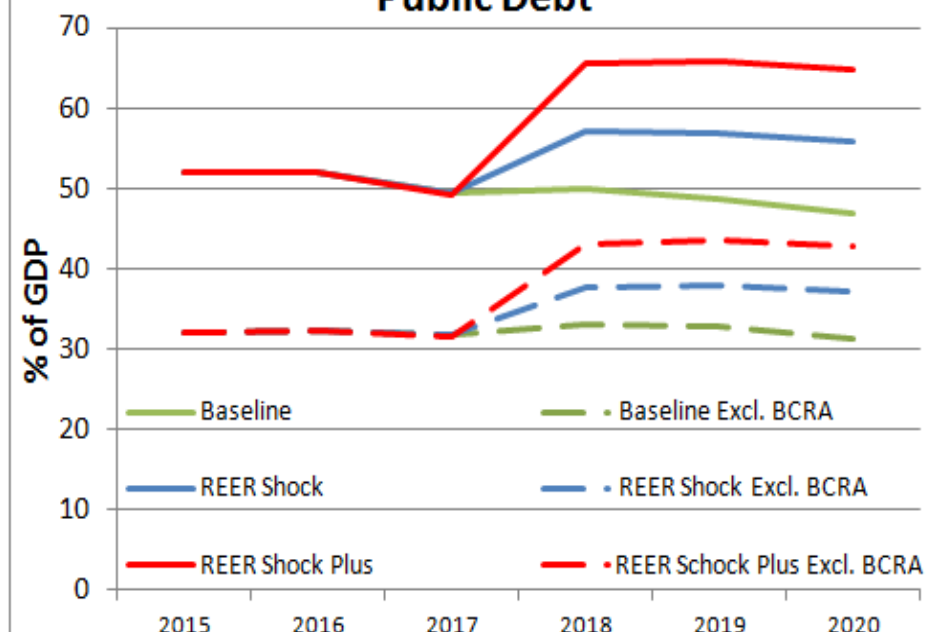
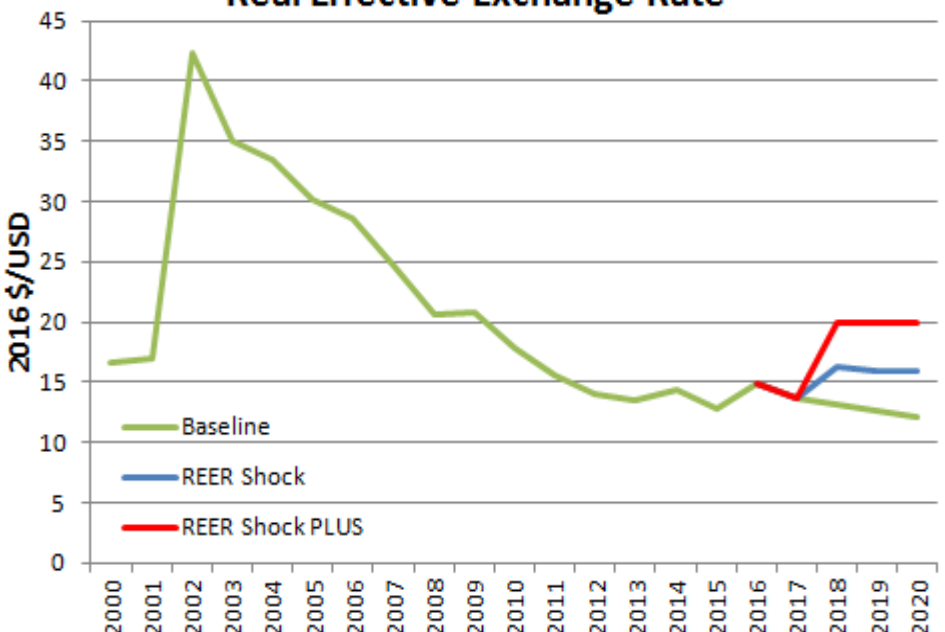


Public Debt

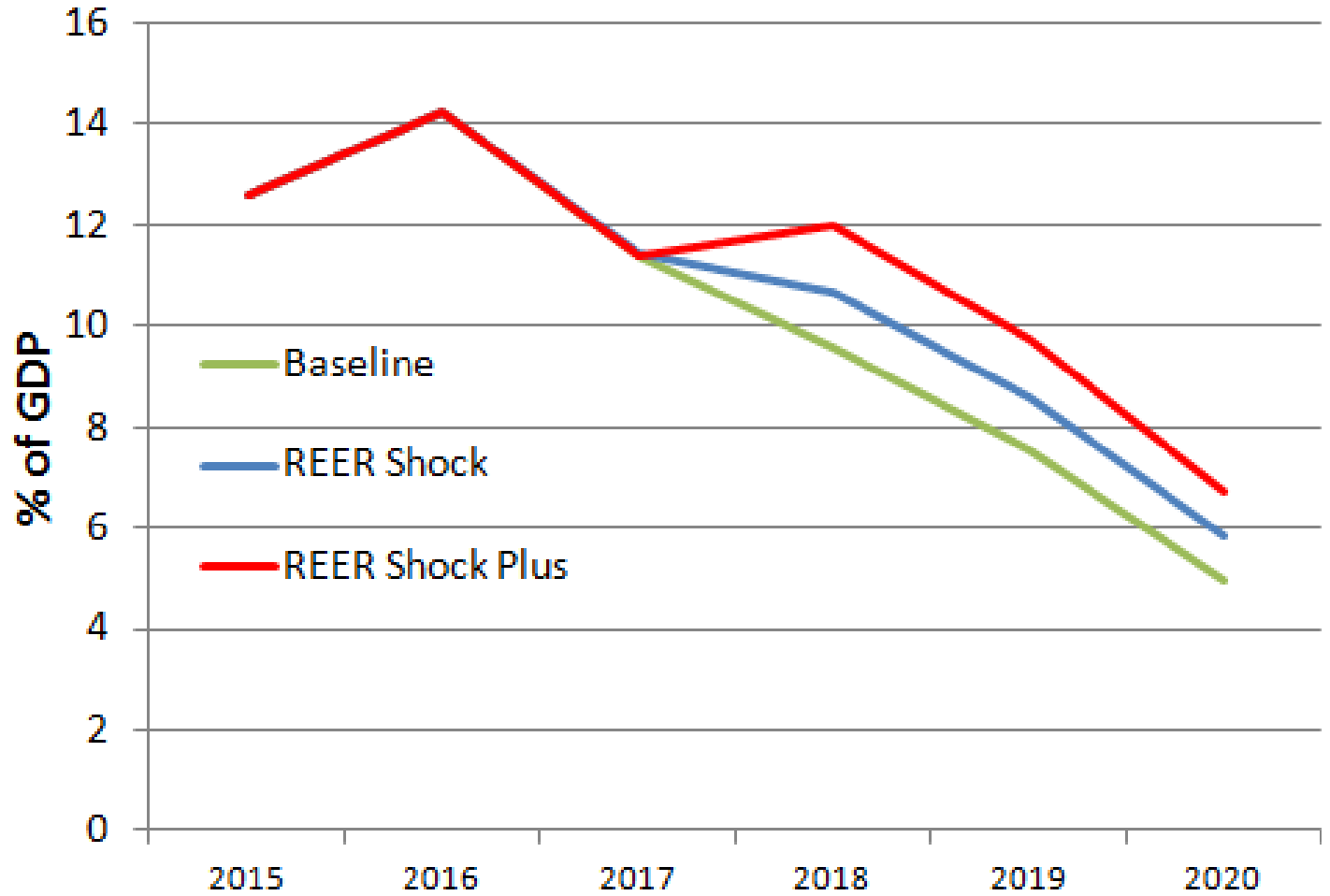


Real Effective Exchange Rate



Public Debt**Real Effective Exchange Rate****Public Debt****Real Effective Exchange Rate**

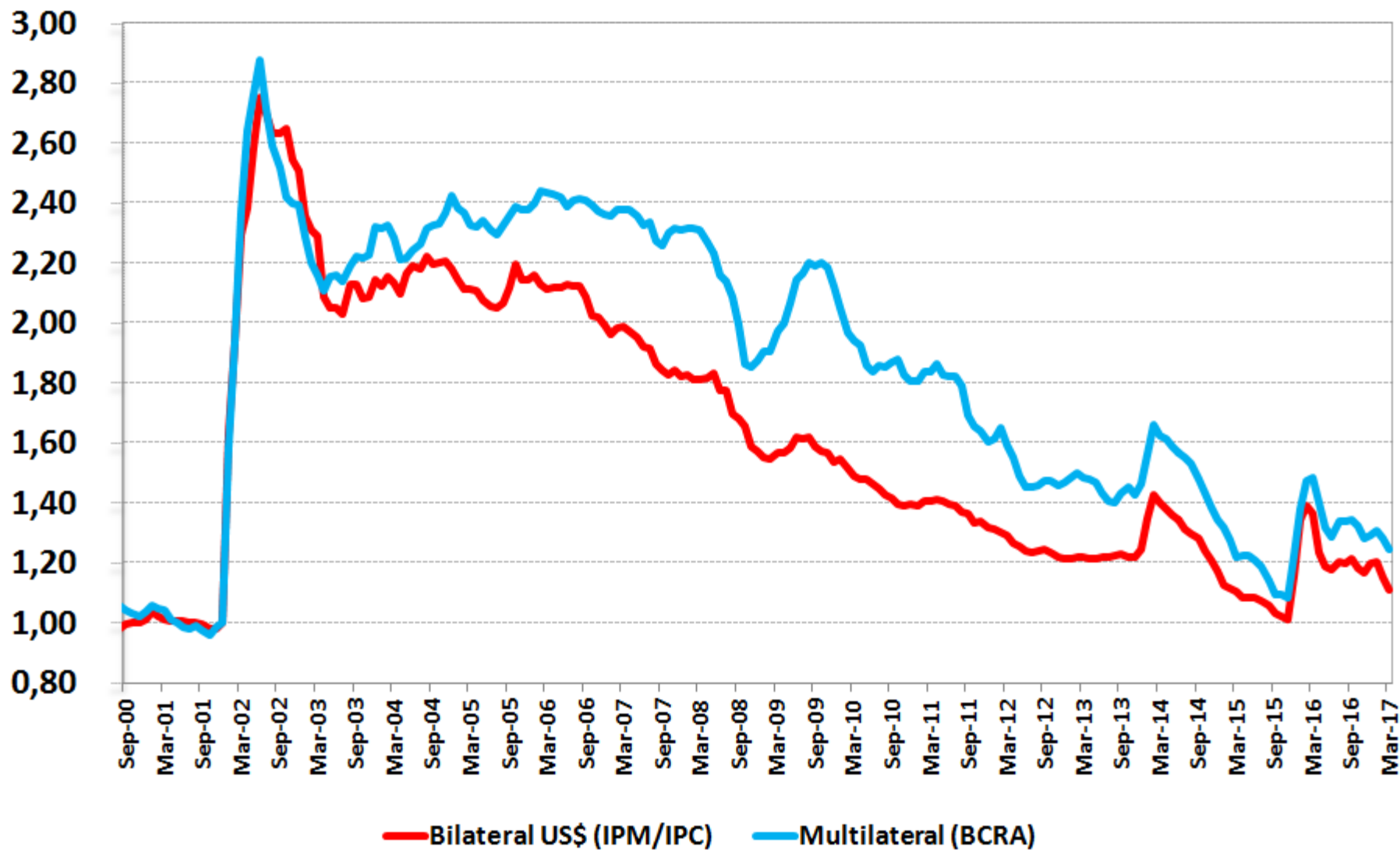
Gross Financing Needs



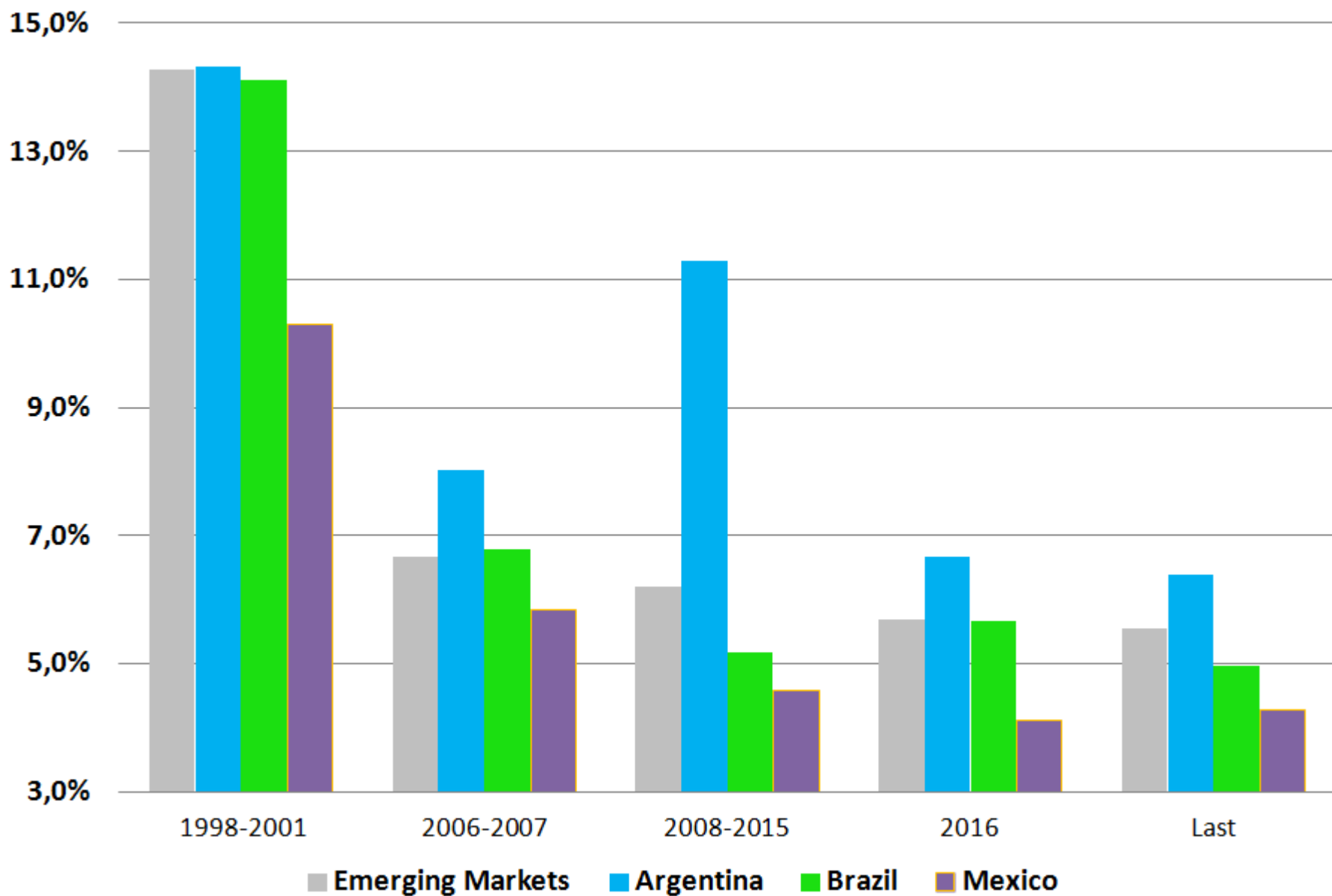
Note: Gross Financing Needs exclude Transitory Advances from the Central Bank. Non-transferable Notes amortize after 2020.

Bilateral and Multilateral Real Exchange Rate Arg\$ / Foreign Currency

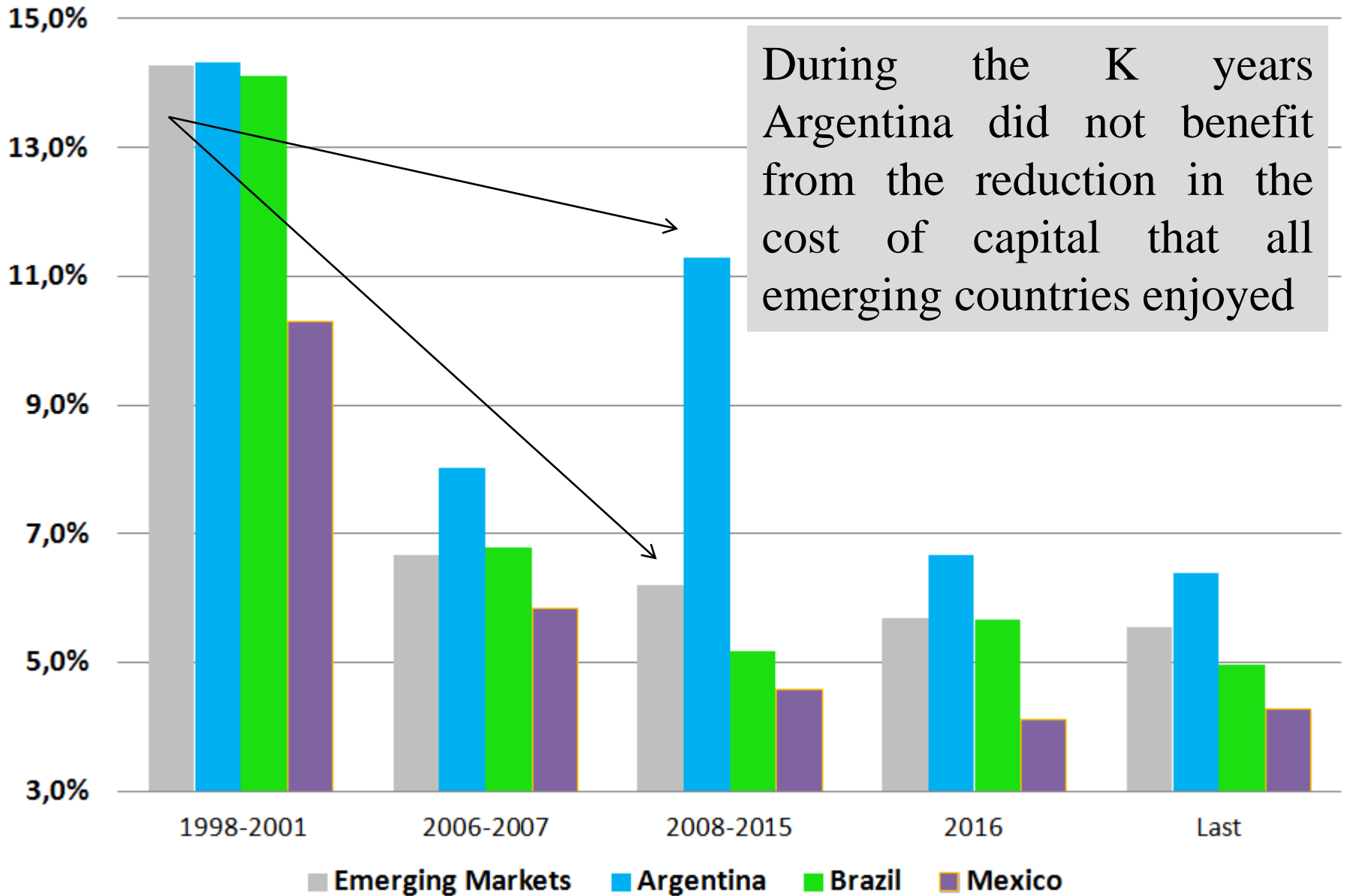
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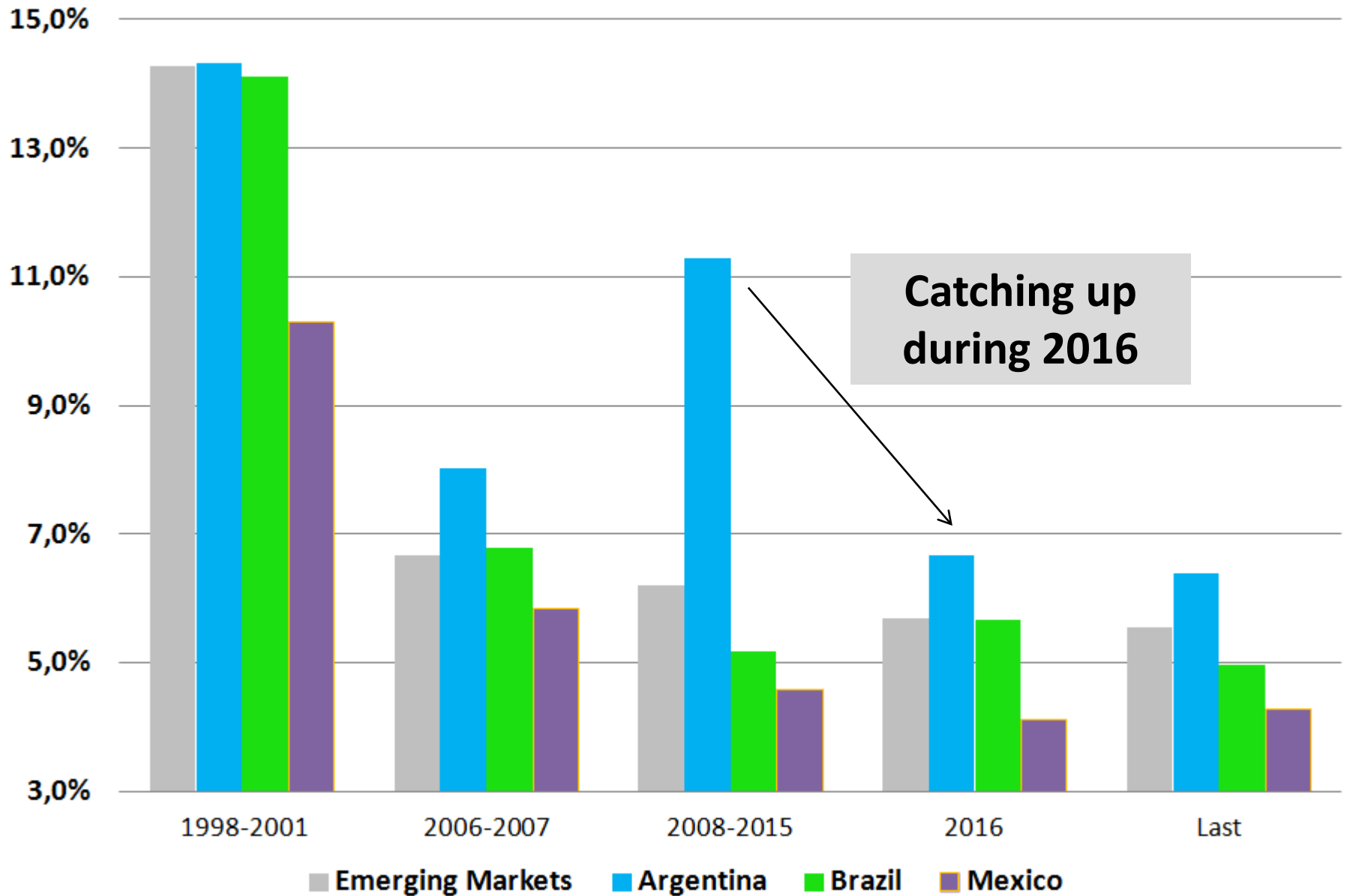
Cost of Capital for the Sovereign (10 yr US Treas + Embi) %



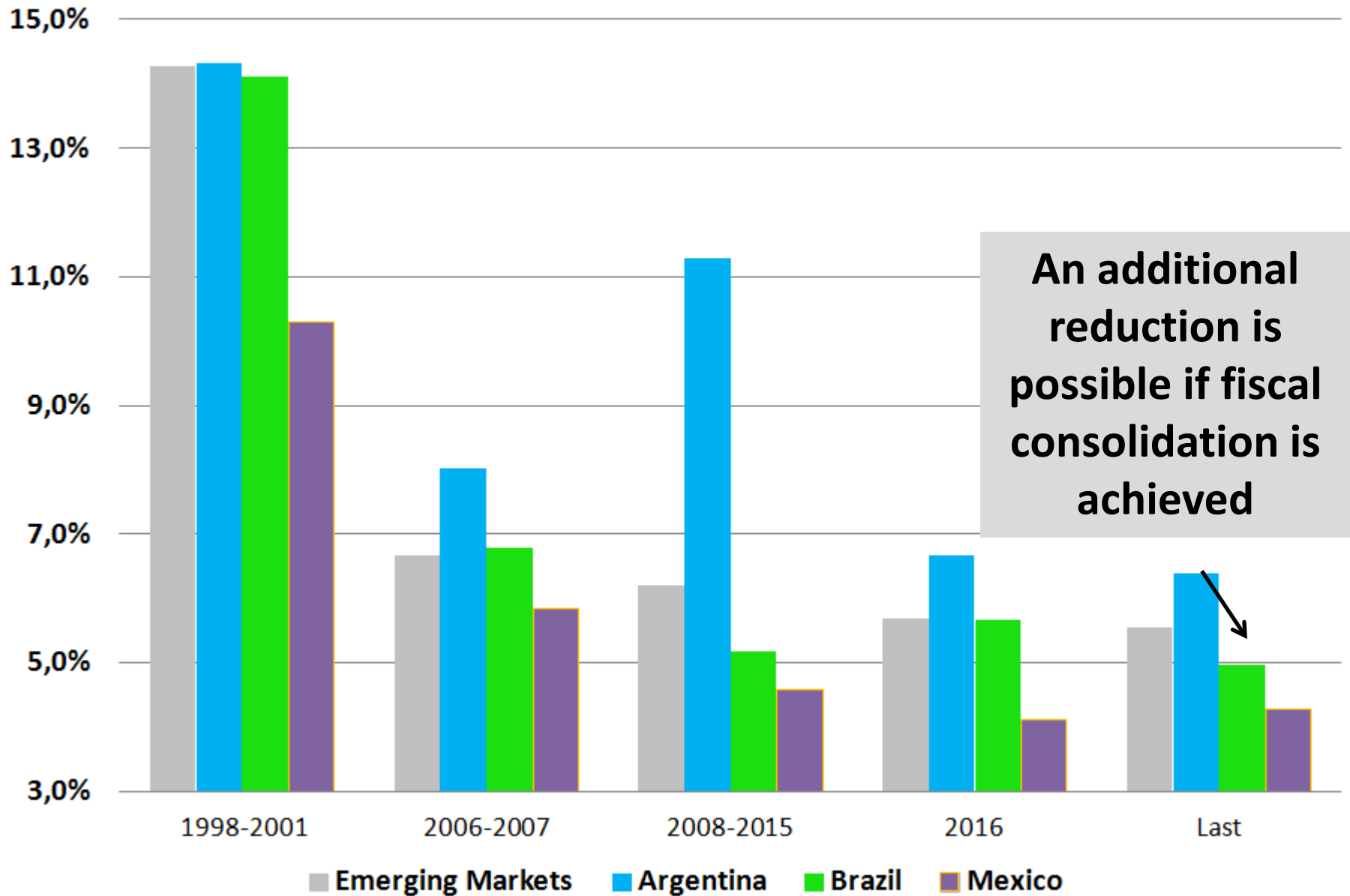
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The short-term and medium-term outlook

- **Upside**

- The international context is likely to be benign
- An additional reduction in the cost of capital
- The opportunities opened by the removal of distortions (e.g. multiple exchange rates, taxes on exports, unnecessary regulations)

- **Downside**

- Gradual improvement in fiscal accounts delays positive effects on the economy
- High costs in US\$
- Increase in investment constrained by current account deficit