

Confidence in Argentina takes a knock

by Jason Mitchell

YPF nationalization deters foreign investment; Even core agricultural sector affected

M&A activity in Argentina has dried up and the investment by Mexican billionaire Carlos Slim in YPF, the Argentine integrated oil and gas company, should not be seen as a vote of confidence in the country's economic performance, according to experts. On June 14, Slim, the world's richest man, acquired an 8.4% stake in YPF. The Argentine government has tried to portray that as a signal that foreign confidence in the country has returned. In mid-April, the government nationalized 51% of YPF, which had been majority owned by Spanish oil and gas company Repsol. However, the Argentine government has exaggerated Slim's commitment, because most of his recent investment has been non-voluntary. He ended up inheriting the YPF stake because of his support for Argentine conglomerate Grupo Petersen. Essentially, it was collateral that backed credit to the company, which helped it to amass a 25.6% equity interest in YPF. Following YPF's nationalization, the government cancelled the dividend payments to Petersen – which had been used to finance the loans – and the Eskenazi family, owners of Petersen, was forced to default on them. The 8% stake then fell into Slim's hands. Experts say that since the YPF nationalization foreign direct investment in Argentina has dried up. "The nationalization was an earthquake for M&A activity in Argentina and business confidence generally," says Fausto Spotorno, head of research at Buenos Aires-based economic consultants Orlando Ferreres and Associates. "M&A activity is really bad. There is none." Andres Azicri, a director at Buenos Aires-based financial consultants Elypsis, says: "The nationalization move reduced foreign confidence in the country, and there is a real issue about the rule of law. The business climate is not very friendly for foreigners. There are very few acquisitions being made, and those that are taking place are by locals who are more used to how Argentina operates." For the year to June 20, 70 transactions have been announced in the country, valued at a total of \$7.43 billion, according to Dealogic. For the same period last year, 80 deals were announced, valued at \$4.28 billion; for the same period in 2010 there were 64 deals valued at \$5.27 billion. This year's figure has been skewed by the Argentine state's \$4.78 billion acquisition of the majority stake in YPF. In May, Grupo Petersen purchased a 10% stake in YPF. Overall, announced deals last year amounted to \$6.49 billion with a total of 165 transactions, compared with \$9.2 billion in 2010 (134 deals) and \$2.3 billion in 2009 (68 deals).

Experts say that the overall business climate in Argentina has deteriorated this year, with inflation hovering around 25% and the pace of economic growth slackening. The government has been adopting increasingly protectionist methods to try to defend domestic producers but that has led to deteriorating relations with Brazil, Latin America's economic powerhouse and Argentina's neighbors.

Victor Hugo Rodriguez, chief executive of LatAm Alternatives, a Miami-based hedge fund consultancy focusing on Latin America, says: "Perception is everything and unfortunately Argentina's sovereign and corporate debt became very illiquid after the YPF event. It is a very distressed market. It's not easy even for participants with a lot of knowledge of the market. The country could be a very long-term investment because at the end of the day Argentina may still present some opportunities." Azicri adds: "No foreign company really wants to invest in the energy or oil-and-gas sectors in Argentina. They are all heavily subsidized by the state so that the prices to the final consumer are lower. But this leads to very low profitability. A natural step would be to nationalize these industries as well." He adds that the government is considering nationalizing the country's gaming industry. Even the agricultural sector – traditionally the backbone of the Argentine economy – is suffering. According to investors, banks will no longer accept assets such as farms and ports used by agricultural exporters as collateral for loans out of fear that the state might nationalize them. During the past six months, a parallel market for the dollar – as in Venezuela – has developed. Officially, there are 4.5 pesos to the dollar but up to six pesos can be obtained on the black market. "People's inflation expectations are anchored to the parallel exchange rate," says Azicri. "That has become the equilibrium price of the dollar, rather than the official one. That could spell trouble for Argentina, as it's really an agricultural country and doesn't have the oil that Venezuela has."