

---

## Argentina

---

### 1. General trends

After plunging by 11% in 2002, Argentina's gross domestic product (GDP) surged by almost 9% in 2003 and continued to rise in the initial months of 2004. In 2003, despite a considerable upturn in consumption, the national savings rate remained at around 20%, which was similar to its 2002 level and higher than the average for the period 1993-2001. Gross fixed capital formation bounced back significantly, growing by 38.2% in the course of the year, after a cumulative slump of about 56% in the period 1998-2002. Goods-producing sectors, especially construction and manufacturing, played a major role in the recovery of economic activity.

In the external sector, merchandise imports rebounded strongly, rising by 54%, while exports were up by 14%, buoyed by favourable external prices. The trade account once again ran a sizeable surplus, as did the current account, even though the weakness of demand from Brazil hurt exports of more highly processed goods. Thanks to the economy's faster growth, employment rose significantly and unemployment fell from 20.4% to 14.4% between the first quarter of 2003 and the same period of 2004.

The cumulative inflation rate for 2003 was 3.7%; in the first few months of 2004 monthly inflation rates exceeded this figure, although they remained in the single digits. The national public sector's primary surplus rose to 2.3% of GDP in 2003 as a result of a sharp increase in tax receipts.

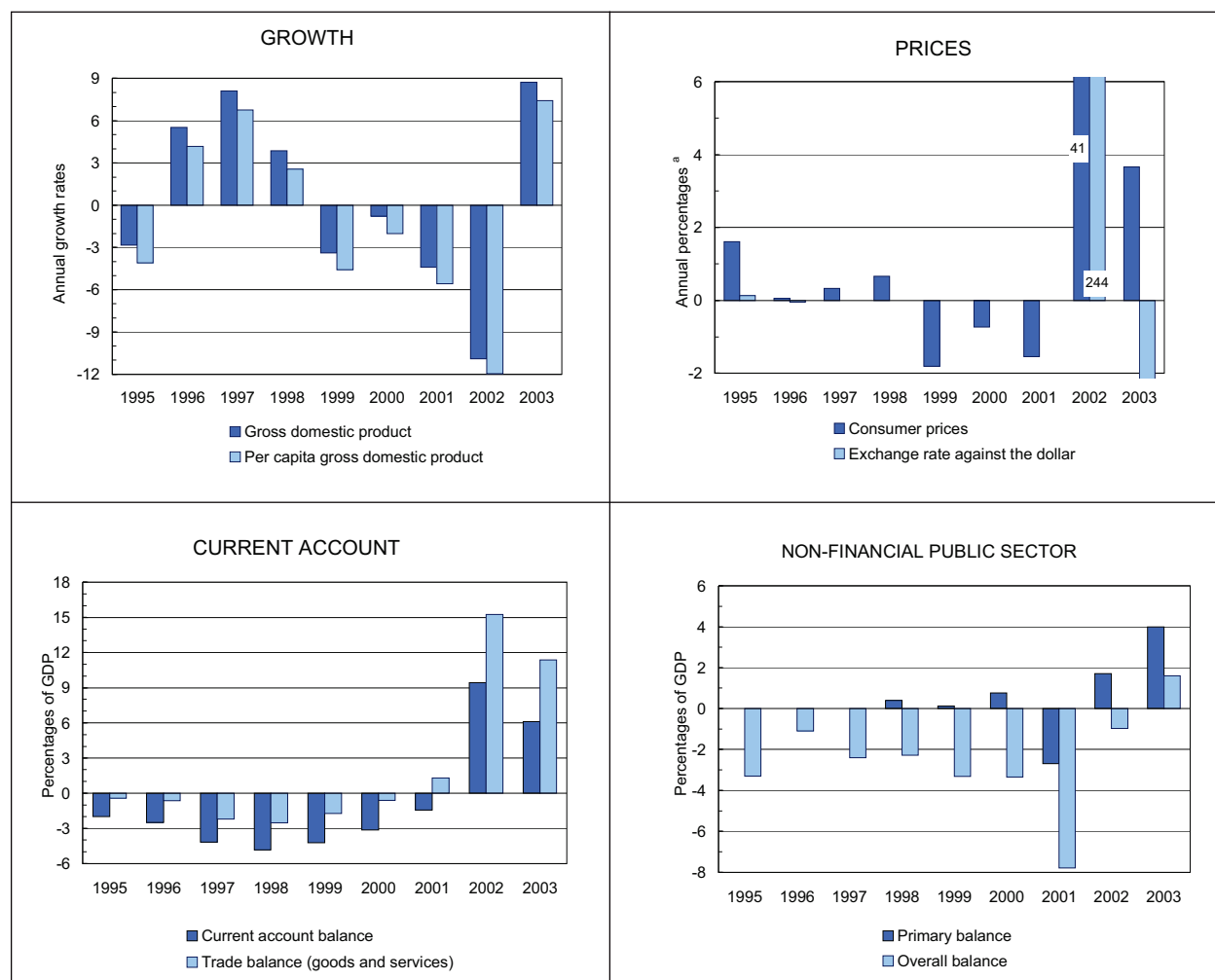
Argentina's relations with the International Monetary Fund (IMF) were strained at times, despite the country's good fiscal results, which even surpassed the established targets. In addition, the issue of restructuring public debt with private creditors remained to be settled. This represented a major element of uncertainty, but did not hold back the economic recovery. Likewise, the political

transition that followed the elections did not significantly affect the economy's performance, nor did it alter the features of economic policy management.

The crisis of 2001-2002, which involved many macroeconomic, financial and fiscal factors, called the whole system of contracts into question. In the past few years, in the context of a struggling economy and a much higher real exchange rate, the adjustment of contracts (especially those denominated in dollars) has been a central issue. This process has kindled a number of debates and conflicts, some of which have died down, while others were still unresolved as of mid-2004.

Operations to convert dollar loans and bank deposits into pesos and the rescheduling of deposits raised a storm of controversy. Legal actions seeking to invalidate the "pesification" of deposits—which sometimes generated friction between the executive and judicial branches—concluded with a ruling in favour of the complainants, although the decision was limited in scope and did not cause significant financial disturbances. Resources began to flow back into banks, despite falling interest rates, with the result that restrictions on funds availability could safely be lifted. Credit, however, is recovering very slowly.

Figure 1  
**ARGENTINA: MAIN ECONOMIC INDICATORS**



**Source:** Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.  
<sup>a</sup> December-December variation.

The impact of the financial crisis was absorbed in part by the public sector, which accordingly issued a large amount of debt. The government met the servicing requirements of these new liabilities and of outstanding liabilities with multilateral institutions. The restructuring of privately-held debt is yet to be arranged, for an amount which, at the time of the default, was close to US\$ 80 billion. In September 2003 the government outlined an initial exit strategy, which involved substantial write-offs; in June 2004 it made a formal proposal –which included the recognition of interest accrued since the declaration of default– that was predicated on the assumption of a public-sector primary surplus on the order of 3% of GDP.

Meanwhile, non-bank corporate debt was the subject of various renegotiation processes, many of which concluded with agreements to extend maturities and, in some cases, to reduce interest or principal. Contracts for the provision of privatized services were another important issue.

The authorities avoided rate adjustments and made any increases contingent on agreements with suppliers, which included reviews of pre-crisis performance and the establishment of investment programmes. This issue was particularly important in 2004, when signs of a natural gas shortage affected domestic supply and exports to Chile.

## 2. Economic policy

### (a) Fiscal policy

Significant primary surpluses were generated as the economy picked up. Apart from the voluminous debt arrears and persistent structural problems that continued to weigh on fiscal policy, the public sector's cash transactions did not come under significant pressure, something that had not occurred for a long time.

In 2003 receipts of taxes levied by the national government were up by 50.6% in nominal terms, rising to 2.3% of GDP. The biggest proportional increase was in taxes on income and assets, while VAT receipts also rose sharply (by 37%). Social security revenues showed below-average growth (18%). In recent years, export duties and the tax on bank credits and debits—both of which, in principle, were imposed as temporary measures—have become important elements of the tax structure. Overall, taxes on foreign trade and on bank transactions accounted for about 21% of total receipts in 2003, which was somewhat higher than the 19.6% posted in 2002.

Government expenditure also expanded in 2003. Its real value had fallen considerably in 2002, reflecting the drop in the real value of wages and pensions. Primary expenditure amounted to 18.2% of GDP, more or less equalling its 2001 level. The expansion was concentrated in transfers to the provinces, as an automatic effect of dividing up a larger volume of tax receipts.

Despite the country's positive cash balances, public debt rose substantially in 2003. The national public sector's total liabilities at the end of the year approached US\$ 179 billion (compared to US\$ 137 billion at the end of 2002). Part of the increase was the result of accrual-basis accounting for back interest on the debt in default. The revaluation of euro-denominated liabilities and of price-indexed local-currency liabilities and the transfer of provincial-government debt to the national government also played a role. In addition, the authorities continued to issue bonds to savers in the financial system whose deposits had been rescheduled, and also issued securities to raise funds for reversing, with retroactive effect, the cutbacks that had been made in civil-service wages and retirement pensions, since those cutbacks had been overturned by a court decision.

In the first six months of 2004 tax collection continued to rise, exceeding its level of the year-earlier period by 43.5%, thanks in particular to VAT and profit-tax receipts. As a result, the government easily met the

primary surplus targets laid down in the IMF agreement, to the point where the figure set for the year as a whole had already been surpassed by May.

The distribution of taxes between the national government and the provinces is a matter of perennial debate in Argentina. As of mid-2004 negotiations on a new revenue-sharing system were still in progress. One critical element of the discussion was the level of resources to be assigned to the province of Buenos Aires. Meanwhile, the government presented a draft law on fiscal responsibility, whose provisions include limits on debt servicing that could affect the provincial governments.

### (b) Monetary and exchange-rate policy

In 2003 there was once again an excess supply of foreign exchange in the economy. Under the managed-float system, the nominal exchange rate went down by 20% in the first quarter of 2003 and then fluctuated moderately, reaching much higher levels by mid-2004.

The currency's tendency to appreciate was offset in part by the actions of the central bank, which partially sterilized the consequent monetary expansion by issuing bills of exchange. Meanwhile, the government arranged for the redemption of the quasi-money issued by the provincial governments as an emergency financial instrument. There was a significant expansion of the monetary base, both in the narrow sense (central bank deposits only) and in the broad sense (including quasi-money).

The demand for liquid assets continued to rise. Public holdings of cash and demand deposits increased rapidly, reaching historically high values as a percentage of GDP. The volume of deposits in savings banks also rose substantially. This stronger tendency to hold liquid assets denominated in local currency is related to expectations of low inflation and slight exchange-rate depreciation, as well as to low interest rates.

At the beginning of 2003 there was a large volume of deposits whose maturity had been rescheduled in 2002, and in the course of the year savers were able to gain access to these funds. A large proportion of the rescheduled certificates of deposit (CEDROs) were redeemed and some of those resources were placed in fixed-term deposits. As a result, the amount of such "voluntarily" withdrawn deposits increased considerably, although there was little change in the total amount of time deposits, including CEDROs. In any event, the

Table 1  
**ARGENTINA: MAIN ECONOMIC INDICATORS**

	1995	1996	1997	1998	1999	2000	2001	2002	2003 <sup>a</sup>
<b>Annual growth rates<sup>b</sup></b>									
<b>Gross domestic product</b>	-2.8	5.5	8.1	3.9	-3.4	-0.8	-4.4	-10.9	8.7
<b>Per capita gross domestic product</b>	-4.1	4.2	6.7	2.5	-4.6	-2.0	-5.6	-12.0	7.4
<b>Gross domestic product, by sector</b>									
Agriculture, livestock, hunting, forestry and fishing	5.6	-1.2	0.5	8.7	2.5	-1.7	1.1	-2.3	6.7
Mining	16.4	4.5	0.7	-3.8	-3.3	6.7	4.7	-3.7	3.7
Manufacturing	-7.2	6.5	9.2	1.8	-7.9	-3.8	-7.4	-11.0	15.8
Electricity, gas and water	7.4	4.1	8.2	7.6	3.6	6.6	1.1	-3.0	6.9
Construction	-12.2	8.4	16.6	8.7	-7.9	-9.3	-11.6	-33.4	34.3
Wholesale and retail commerce, restaurants and hotels	-7.5	7.9	10.9	3.4	-6.9	-2.4	-7.8	-16.8	11.1
Transport, storage and communications	1.7	6.9	11.2	8.9	-1.3	1.7	-4.6	-7.9	8.3
Financial institutions, insurance, real estate and business services	-0.9	6.1	7.3	7.0	-0.5	1.3	-4.4	-9.6	-1.1
Community, social and personal services	0.6	2.3	4.0	1.5	1.9	1.7	-0.1	-3.3	2.8
<b>Gross domestic product, by type of expenditure</b>									
Consumption	-3.6	5.0	8.1	3.5	-1.3	-0.5	-5.2	-12.8	7.0
General government	0.8	2.2	3.2	3.4	2.6	0.6	-2.1	-5.1	1.5
Private	-4.4	5.5	9.0	3.5	-2.0	-0.7	-5.7	-14.4	8.1
Gross fixed capital formation	-13.1	8.9	17.7	6.5	-12.6	-6.8	-15.7	-36.4	38.1
Exports (goods and services)	22.5	7.6	12.2	10.6	-1.3	2.7	2.7	3.1	6.4
Imports (goods and services)	-9.8	17.5	26.9	8.4	-11.3	-0.2	-13.9	-50.1	37.6
<b>Percentages of GDP</b>									
<b>Investment and saving<sup>c</sup></b>									
Gross domestic investment	18.5	19.6	20.9	21.0	17.9	17.5	15.6	10.8	14.2
National saving	16.5	17.1	16.6	16.1	13.6	14.4	14.0	19.6	19.8
External saving	2.0	2.5	4.2	4.9	4.2	3.2	1.7	-8.7	-5.7
<b>Millions of dollars</b>									
<b>Balance of payments</b>									
Current account balance	-5 175	-6 822	-12 240	-14 530	-11 966	-8 937	-3 906	9 627	7 941
Merchandise trade balance	2 357	1 760	-2 123	-3 097	-795	2 452	7 385	17 236	16 292
Exports, f.o.b.	21 162	24 043	26 431	26 434	23 309	26 341	26 543	25 709	29 375
Imports, f.o.b.	18 804	22 283	28 554	29 531	24 103	23 889	19 158	8 473	13 083
Services trade balance	-3 417	-3 527	-4 363	-4 433	-4 106	-4 274	-3 953	-1 688	-1 546
Income balance	-4 669	-5 503	-6 218	-7 406	-7 463	-7 470	-7 770	-6 498	-7 425
Net current transfers	554	448	463	406	397	355	432	576	620
Capital and financial balance <sup>d</sup>	2 863	10 080	15 571	18 620	13 978	7 761	-17 553	-25 339	-17 153
Net foreign direct investment	4 112	5 348	5 507	4 965	22 257	9 517	2 005	1 413	-296
Financial capital <sup>e</sup>	-1 249	4 732	10 064	13 655	-8 279	-1 757	-19 559	-26 751	-16 857
Overall balance	-2 311	3 258	3 331	4 090	2 013	-1 176	-21 459	-15 712	-9 212
Variation in reserve assets <sup>f</sup>	82	-3 875	-3 293	-3 436	-1 186	403	12 083	4 516	-3 581
Other financing <sup>g</sup>	2 229	617	-38	-654	-826	773	9 376	11 196	12 793
<b>Other external-sector indicators</b>									
Real effective exchange rate (index: 2000=100) <sup>h</sup>	113.1	116.3	114.3	109.9	99.8	100.0	95.9	228.1	212.4
Terms of trade for goods (index: 1997=100)	91.8	99.6	100.0	95.4	90.4	99.9	99.4	98.3	106.8
Net resource transfer (% of GDP)	0.2	1.9	3.2	3.5	2.0	0.4	-5.9	-20.2	-9.1
Total gross external debt (billions of dollars)	99	111	125	142	145	147	140	134	146
Total gross external debt (% of GDP)	38.2	40.6	42.7	47.5	51.2	51.5	52.2	131.5	112.2
Net profits and interest (% of exports) <sup>i</sup>	8.5	7.3	8.9	8.9	7.5	9.9	2.9	-1.2	3.1

Cuadro 1 (concluded)

	1995	1996	1997	1998	1999	2000	2001	2002	2003 <sup>a</sup>
<b>Average annual rates</b>									
<b>Employment</b>									
Labour force participation rate <sup>j</sup>	42.0	41.5	42.2	42.2	42.6	42.6	42.5	42.4	42.9
Open unemployment rate <sup>k</sup>	17.5	17.2	14.9	12.9	14.3	15.1	17.4	19.7	15.0
Visible underemployment rate <sup>k</sup>	12.0	13.2	13.2	13.5	14.3	14.6	15.6	19.3	17.1
<b>Annual percentages</b>									
<b>Prices</b>									
Variation in consumer prices (December-December)	1.6	0.1	0.3	0.7	-1.8	-0.7	-1.5	41.0	3.7
Variation in wholesale prices	5.8	2.1	-0.9	-6.3	1.2	2.4	-3.4	113.7	2.0
Variation in nominal exchange rate (December-December)	0.1	0.0	0.0	0.0	0.0	0.0	0.0	243.7	-13.9
Variation in average real wage	-1.1	0.6	0.3	0.0	2.9	2.3	-0.8	-13.9	-1.8
Nominal deposit rate <sup>l</sup>	...	...	7.0	7.6	8.3	8.5	16.3	39.3	10.5
Nominal lending rate <sup>m</sup>	...	...	9.2	10.6	11.0	11.1	26.5	53.0	19.1
<b>Percentages of GDP</b>									
<b>Non-financial public sector<sup>n</sup></b>									
Current income	...	...	...	24.4	25.2	25.9	24.5	24.7	27.6
Current expenditure	...	...	...	24.6	27.2	27.8	30.8	24.8	24.5
Current balance	...	...	...	-0.2	-2.1	-1.9	-6.3	-0.1	3.1
Net capital expenditure	...	...	...	2.5	1.2	1.5	1.5	0.9	1.4
Primary balance	...	...	...	0.4	0.1	0.8	-2.7	1.7	4.0
Overall balance	-3.3	-1.1	-2.4	-2.3	-3.3	-3.3	-7.8	-1.0	1.6
Public debt of NFPS and central bank	26.0	27.2	34.5	37.6	43.0	45.0	53.7	137.3	139.9
Domestic	...	...	8.9	9.8	13.1	15.2	20.9	50.0	59.8
External	26.0	27.2	25.6	27.8	29.9	29.8	32.8	87.3	80.0
<b>Money and credit<sup>o</sup></b>									
Domestic credit <sup>p</sup>	23.4	24.6	25.6	28.6	32.2	32.8	32.9	41.5	34.4
To the public sector	3.7	5.4	5.5	5.9	7.2	8.5	9.9	24.8	23.0
To the private sector	19.7	19.2	20.1	22.7	25.0	24.2	23.0	16.7	11.5
Liquidity (M3)	20.4	22.7	25.6	29.2	32.8	33.7	33.4	29.2	28.4
Currency in circulation and local-currency deposits (M2)	12.0	13.0	14.8	16.3	17.0	16.6	14.7	25.3	27.1
Foreign-currency deposits	8.4	9.7	10.8	12.9	15.9	17.1	18.7	3.9	1.3

**Source:** Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.

<sup>a</sup> Preliminary figures. <sup>b</sup> Based on figures in local currency at constant 1993 prices. <sup>c</sup> Based on figures in local currency at current prices. Gross domestic investment does not include changes in stocks. <sup>d</sup> Includes errors and omissions. <sup>e</sup> Refers to the capital and financial balance (including errors and omissions), minus net foreign direct investment. <sup>f</sup> A minus sign (-) denotes an increase in reserves. <sup>g</sup> Includes the use of IMF credit and loans and exceptional financing. <sup>h</sup> Annual average, weighted by the value of merchandise exports and imports. <sup>i</sup> Refers to net investment income as a percentage of exports of goods and services as shown on the balance of payments. <sup>j</sup> Economically active population as a percentage of the total population in urban areas. <sup>k</sup> Rates of unemployment and underemployment are percentages of the economically active population in urban areas. <sup>l</sup> Fixed-term deposits, all maturities. <sup>m</sup> 30-day loans to leading firms. <sup>n</sup> Accrual basis. <sup>o</sup> The monetary figures are annual averages. <sup>p</sup> Refers to net credit extended to the public and private sectors by commercial banks and other financial and banking institutions.

M3-to-GDP ratio –which, in the historical series, includes dollar deposits– had topped 30% by the end of the year.

The new deposits taken in by banks were used to rebuild liquidity –to levels well in excess of the legal requirement– and to pay off rediscounts. The volume of bank credit continued to shrink in 2003 but has recently begun to show signs of a very slow recovery, despite the limited level of supply and the weak demand for

financing. In April 2004 the central bank issued six-month bills of exchange (in pesos) at a rate of less than 3% per year (as against 21% a year earlier). The rate on bank deposits also fell considerably. Nevertheless, many economic agents continued to face tight restrictions on access to financing. In a market with these characteristics and where the asset position of financial entities is still uncertain, the question of how the banking system will be configured in the medium term remains open.

Table 2  
**ARGENTINA: MAIN QUARTERLY INDICATORS**

	2002				2003 <sup>a</sup>				2004 <sup>a</sup>	
	I	II	III	IV	I	II	III	IV	I	II
Gross domestic product (variation from same quarter of preceding year) <sup>b</sup>	-16.3	-13.5	-9.8	-3.4	5.4	7.7	10.2	11.5	11.2	...
Merchandise exports, f.o.b. (millions of dollars)	5 711	6 794	6 759	6 446	6 548	8 087	7 491	7 250	7 285	...
Merchandise imports, c.i.f. (millions of dollars)	2 071	2 157	2 292	2 470	2 500	3 328	3 705	4 281	4 626	...
International reserves (millions of dollars)	12 780	9 629	9 404	10 476	10 517	12 183	13 406	14 119	15 003	17 442
Real effective exchange rate (index: 2000=100) <sup>c</sup>	174.5	253.0	249.4	235.4	215.7	207.0	210.2	216.6	221.7	214.3
Unemployment rate	...	...	...	...	20.4	17.8	16.3	14.5	14.4	...
Consumer prices (12-month percentage variation)	7.9	28.4	38.5	41.0	31.7	10.2	3.5	3.7	2.3	4.9
Average nominal exchange rate (pesos per dollar)	1.91	3.25	3.58	3.51	3.15	2.85	2.88	2.90	2.91	2.90
Average real wage (variation from same quarter of preceding year)	0.7	-16.4	-17.5	-21.2	-19.4	0.0	5.4	9.2	16.1	14.2
Nominal interest rates (annualized percentages)										
Deposit rate <sup>d</sup>	9.4	60.8	62.0	25.1	18.8	14.2	4.8	4.1	2.5	2.4
Lending rate <sup>e</sup>	30.7	...	90.6	42.7	27.6	24.3	13.9	10.8	9.1	6.3
Interbank interest rate <sup>f</sup>	38.7	67.3	48.2	9.7	5.9	5.6	2.5	1.6	1.4	2.0
Sovereign bond spread (basis points)	5 013	6 791	6 629	6 358	6 167	4 505	5 421	5 583	4 862	5 063
Stock price index (in dollars, June 1997=100)	24.9	15.5	17.1	24.0	30.3	39.4	41.6	54.7	60.2	48.0
Domestic credit <sup>g</sup> (variation from same quarter of preceding year)	36.0	63.3	73.1	64.9	6.1	-12.3	-13.6	-7.5	-1.1	-0.2
Non-performing loans as a percentage of total loans <sup>h</sup>	...	...	...	12.7	...	18.7	18.8	13.4	11.4	...

**Source:** Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.

<sup>a</sup> Preliminary figures. <sup>b</sup> Based on figures in local currency at constant 1993 prices. <sup>c</sup> Quarterly average, weighted by the value of merchandise exports and imports. <sup>d</sup> Fixed-term deposits. <sup>e</sup> 30-day loans to leading firms. <sup>f</sup> Buenos Aires interbank offered rate (BAIBOR). <sup>g</sup> Refers to net credit extended to the public and private sectors by commercial banks and other financial and banking institutions. <sup>h</sup> Refers to total credit extended by the banking system.

### 3. The main variables

#### (a) Economic activity

In 2003 the recovery of economic activity that had begun in mid-2002 gained momentum. In the first quarter of 2004 GDP was 11.2% higher than it had been in the same period of 2003, bringing Argentina's GDP to a level 17.2% above the low point reached in the first quarter of 2002. However, GDP is still 16% lower than its peak level, recorded in the second quarter of 1998.

Domestic demand, which had trended steadily downward since 1999, grew substantially in 2003 (by 10.8%). Consumption rose by 7% and gross fixed capital formation made a strong comeback (38%). The investment rate rose gradually, starting from very low levels (10.5% of GDP in the first quarter of 2002) and approaching 16.5% of GDP in the first quarter of 2004. The upsurge in gross fixed investment in 2003 was due

to increases in both construction (35%) and investment in durable production equipment (45%), although in both cases expenditure remained far below the record levels posted in 1998. Despite the collapse of financing, private demand for real estate recovered significantly, probably as a result of portfolio restructuring among individuals who held external assets or withdrew funds from banks. The upturn in prices in relation to costs stimulated construction activity. The production of goods expanded substantially, especially in construction and manufacturing. The growth of basic services was robust (8%) but fell short of the growth of aggregate GDP, while activity in commerce, restaurants and hotels was up by 11.1%. Other services posted modest growth.

Agricultural activity expanded by about 7% in 2003, driven by a bigger harvest of grains, particularly soybeans, production of which was up by almost 16%.

Yields are expected to decline by about 8% in 2004 owing to bad weather conditions. Downturns have been observed most clearly in soybeans and wheat. The demand for beef increased, pushing up prices for cattle.

Crude oil production was down by 2% in 2003, while gas extraction increased by 10.4%. Investment in the gas sector declined, however, with a significant downturn in new well drilling. The supply capacity proved to be insufficient to meet higher demand, with the result that service to the domestic market was interrupted a few times and the supply of gas to Chile was restricted. This episode drew attention to the need to redefine the contractual and regulatory frameworks for the energy sector.

In 2003 output was up in most branches of industry, but different segments grew at different speeds. There were large jumps (of over 50%) in textiles and metalworking, which, starting from depressed levels, benefited from the recovery of domestic demand and relatively higher import prices. The growth of the construction materials segment kept pace with the strong upturn in demand. Intermediate goods-producing industries, such as the chemical and paper sectors, revived at a somewhat slower but still strong rate (10% to 20%). Growing at more moderate rates were the food and beverage industries, basic metal manufactures and the automotive industry. The upturn in automobile production became sharper over time, however, and was an important determinant of the industrial sector's aggregate growth in the initial months of 2004. In April the industrial production index was 1% lower than its average level in 1998, when the annual rate had reached a record high.

### **(b) Prices, wages and employment**

Labour demand bounced back in 2003. The employment rate in the major urban areas went up by 2.8 points between the first and fourth quarters of the year. The underemployment rate, meanwhile, went down slightly. Formal employment grew, as did employment as a whole; in September 2003 the number of contributors to social security was 7.5% higher than it had been a year earlier. The rate of informal employment, however, remained high.

Employment continued to increase briskly in the initial months of 2004; in May the variation was close to 7% compared to the same month of 2003. Manufacturing, commerce and services and construction were the main generators of employment.

The unemployment rate fell by almost six percentage points in the course of 2003, although it remained high at the end of the year, at 14.5%, with about 5% of the economically active population receiving public assistance.<sup>1</sup> In the first quarter of 2004 unemployment stood at virtually the same level as in the last quarter of 2003, although it was six points lower than it had been in the first quarter of that year.

Wages went up in 2003, albeit with sharp differences between sectors. The rise in formal private-sector compensation was influenced by the fixed-sum increases provided for by the authorities. In the first quarter of 2004 real wages were 14% higher than they had been in the year-earlier period (and 16% higher in the manufacturing industry). Wages rose faster among private-sector workers covered by social security than among workers without coverage and civil servants.

In 2002 lower levels of employment and real wages had led to an increase in poverty and indigence rates. These rates subsided in 2003, yet in the second half of the year 20.5% of the population of the main urban areas was classified as indigent and 48% of the total population was living below the poverty line.

The consumer price index (CPI) rose by 3.7% in 2003. Since movements in relative prices were fairly small, the general pattern remained similar to what it had been just after the devaluation. With regard to categories of goods and services, food prices rose somewhat faster than the overall CPI, as did the prices of private services, which had lagged behind in 2002. Conversely, public utility prices increased more slowly than the overall index. In the first six months of 2004 inflation picked up speed, accumulating 3.3% over the period. Given the steady rise in the level of demand and the prospect of adjustments in utility prices, this upturn in inflation is likely to continue, although the rate will probably remain moderate.

### **(c) The external sector**

In 2003 the current account surplus was lower than it had been in 2002 but remained at a high level, equivalent to 6% of GDP, even though the calculation includes debits from the income account to reflect unpaid interest on the external debt, once it is recorded on an accrual basis. The merchandise trade balance reached US\$ 16.292 billion, which was 5% lower than the 2002 figure. The increase in export earnings from services as a result of a hike in travel-industry revenues slightly reduced the deficit on the services trade balance, which,

<sup>1</sup> In 2003 the methodology for measuring household survey data was changed, with the result that 2003 data are not fully comparable to data from previous years. The new methodology yields higher rates of labour-force participation, employment and unemployment.

however, was lower than it had been in the period 1996-2001. The income balance showed a large deficit of US\$ 7.425 billion –which was bigger than the 2002 deficit but smaller than the one posted in the period 1998-2001– owing to the recording of the large amount of interest owed on the external debt and to a rise in profit and dividend payments.

One notable development was a sharp slowdown in capital outflows. The deficit on the capital and financial account fell to US\$ 2.639 billion, compared to US\$ 12.145 billion in 2002. This change mainly reflected a downturn in outflows from the non-financial private sector –from US\$ 13.19 billion to US\$ 4.285 billion– as a result of the country's brighter economic outlook. Meanwhile, foreign direct investment inflows were very meagre. There were delays in the servicing of substantial amounts of private-sector debt, although to a lesser degree than in 2002. Financial entities paid off external liabilities in the amount of some US\$ 3 billion, and the national government once again accumulated large arrears in its loan repayments. Disbursements from international institutions returned to their former levels, but the net value of loans and repayments and the net transfer of funds from those institutions were again negative. Reserves stood at US\$ 14.119 billion at the end of 2003, exceeding their year-end level of 2002 by US\$ 3.6 billion.

The upsurge in exports in 2003 was due to increases in both price (9.6%) and volume (4.4%). Although the hike in the export value of commodities and agricultural manufactures was most pronounced in the case of soy products, there was a general rise in the export values of the different components of these two groups (with the exception of dairy products, milled products and sugar and derivatives). Particularly strong increases were

observed in exports of cereals, meats, tea, mate and fish products. External sales of fuels and energy grew by 13%. Exports of industrial manufactures showed no net growth, as a drop-off in flows to MERCOSUR (and, to a lesser degree, in sales to the countries of the Latin American Integration Association (LAIA)) was offset by increases in exports to other destinations. Downturns were seen mainly in exports of motor vehicles, base metals and electrical machinery; in contrast, exports of chemicals increased.

During the year the relative importance of MERCOSUR as a destination for Argentine exports continued to decline rapidly, to the point where the MERCOSUR countries' share of those exports accounted for less than one fifth of the total, whereas it had reached more than a third in previous years. Conversely, the Asian countries' share expanded further, accounting for 17% of the total, mainly on the strength of sales of soy products to China.

Merchandise imports are still significantly lower than they were during the convertibility regime, even though they expanded by 54% in 2003. The upturn was especially strong in capital goods, imports of which doubled from the previous year's level but remained 40% lower than the 2001 figure. Imports of intermediate and consumer goods also grew substantially (by 43% and 54%, respectively).

Merchandise exports were up by 11% (7% in price and 4% in volume) in the first quarter of 2004 in relation to the same period of 2003, while imports jumped by 85%. This growth is almost entirely due to a rise in import volume, with capital goods and intermediate goods posting the biggest increases. In fact, those two categories account for 63% of the total increase in import value over that period.