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AGENDA**

EBS/88/42

CONFIDENTIAL

February 26, 1988

To: Members of the Executive Board

From: The Secretary

Subject: Argentina - Use of Fund Resources - Compensatory Financing Facility

Attached for consideration by the Executive Directors is a paper on a request expected to be received from Argentina for a purchase equivalent to SDR 233.15 million under the compensatory financing facility. A draft decision appears on page 14.

This subject, together with the review of the stand-by arrangement for Argentina, will be brought to the agenda for discussion on a date to be announced.

Mr. Kaibni (ext. 7721) is available to answer technical or factual questions relating to this paper prior to the Board discussion.

Att: (1)

CONFIDENTIAL

INTERNATIONAL MONETARY FUND

ARGENTINA

Use of Fund Resources--Compensatory Financing Facility

Prepared by the Research Department and
the Western Hemisphere Department

(In consultation with the Exchange and Trade Relations, Legal,
and Treasurer's Departments)

Approved by Jacob A. Frenkel and S. T. Beza

February 26, 1988

The Managing Director has been informed that the Argentine authorities will shortly request a purchase equivalent to SDR 233.15 million (20.9 percent of quota) under the decision on compensatory financing of export fluctuations (Decision No. 6224-(79/135)). The request is being made with respect to a shortfall of SDR 1,351 million in merchandise exports estimated for the year ended December 1987. The proposed request is expected to be considered by the Executive Board concurrently with the staff report for the review under the stand-by arrangement. If approved, the proposed purchase would raise Argentina's outstanding purchases under the compensatory financing facility from 62.1 percent of quota to 83.0 percent of quota and the Fund's holdings of the member's currency from 324 percent of quota to 345 percent of quota. ^{1/} A waiver of the limitation in Article V, Section 3(b)(iii) of the Fund's Articles of Agreement is required and is being proposed.

This paper, which is being circulated in advance of the formal request from Argentina, includes five sections and two annexes. The sections deal with: (1) balance of payments position and cooperation with the Fund; (2) estimation of the export shortfall; (3) causes of the shortfall and earnings prospects; (4) repurchase; and (5) staff appraisal. Annex I analyzes the export shortfalls by reference to export developments and prospects for major commodities. Annex II summarizes Argentina's relations with the Fund.

^{1/} The outstanding amount relates to a CF purchase of SDR 275 million made in January 1985, with respect to a shortfall for the 12 months ended May 1984, and a CF purchase of SDR 518.8 million made in July 1987 with respect to a shortfall of SDR 865.4 million for the 12 months ended December 1986. Prior to Board consideration of the CF request, the Argentine authorities have indicated their intention to effect an early repurchase of SDR 103.1 million in respect of CF obligations falling due in the period to end-1988.

1. Balance of payments position and cooperation with the Fund

a. Balance of payments position 1/

The external current account deficit rose from SDR 2.4 billion in 1986 to SDR 3.4 billion in 1987, while the overall deficit widened from SDR 1.6 billion to SDR 3.1 billion (Table 1). The deterioration in the current account is more than explained by a reduction of SDR 1.4 billion in the trade surplus to SDR 380 million in 1987, which can be ascribed in large part to a substantial decline in export volumes reflecting weather-related damage to agricultural production. In addition, import growth was buoyed by the strength of domestic investment, while there was a further deterioration in Argentina's terms of trade. Interest payments were roughly unchanged in 1987 as a decline in international interest rates, on average, was offset by the rising level of net external indebtedness.

The balance on the capital account declined by SDR 480 million in 1987 to a surplus of SDR 283 million, mainly due to increased short-term capital outflows. Net direct investment fell sharply in 1987 in reflection of the purchase by Argentina of a major gas pipeline, but this transaction was largely financed by foreign borrowing. Capital inflows from international organizations rose sharply as World Bank lending operations were stepped up, but trade financing continued to generate net capital outflows.

In 1988, the overall balance of payments deficit is programmed to decline to SDR 1.8 billion, while the current account deficit would narrow to SDR 2.2 billion. The improvement on the current account would derive from a rise in the trade surplus from SDR 380 million in 1987 to SDR 1.6 billion in 1988. Exports are expected to recover strongly in 1988, as agricultural export volumes should rebound with the return to normal weather and as producers respond to the reduction in export taxes and to the real depreciation of the exchange rate in the latter part of 1987; a recovery in export prices is also expected for agricultural products. Import volumes are projected to decline slightly in 1988, as continued growth of nonfuel imports would be offset by a decline in fuel imports reflecting the government policies to boost domestic petroleum and natural gas production. The improvement in the trade balance would be somewhat offset by higher interest payments related to the increase in Argentina's external debt and a rise on average in world interest rates.

The surplus on the capital account is expected to improve by about SDR 140 million in 1988 to SDR 420 million. This rise would be largely explained by the effect of the transfer to the free exchange market of various service payments, which would involve the inflow of counterpart financing through the free exchange market. Direct investment also would rise sharply, in reflection of inflows associated with debt-equity

1/ Recent balance of payments developments are described more fully in the accompanying staff report being circulated for the second review of Argentina's stand-by arrangement.

Table 1. Argentina: Balance of Payments, 1984-88

	1984	1985	1986	Prov. 1987	Est. 1988
(In millions of SDRs)					
A. Current account	-2,333	-939	-2,437	-3,359	-2,221
Trade balance	3,437	4,513	1,814	380	1,612
Exports f.o.b.	(7,909)	(8,269)	(5,841)	(4,792)	(5,838)
Imports c.i.f.	(-4,472)	(-3,756)	(-4,027)	(-4,411)	(-4,226)
Services and transfers	-5,770	-5,451	-4,251	-3,740	-3,833
Nonfactor services (net)	(-200)	(-228)	(-488)	(-268)	(-170)
Profits and dividends	(-428)	(-419)	(-411)	(-429)	(-470)
Interest payments	(-5,402)	(-5,054)	(-3,658)	(-3,206)	(-3,387)
Interest receipts	(258)	(249)	(304)	(169)	(191)
Transfers	(3)	(--)	(2)	(-6)	(3)
B. Capital account <u>1/</u>	631	391	763	283	420
Direct investment	262	905	489	1 <u>2/</u>	716
Export financing	499	138	-49	213	-50
Import financing	-11	-938	-412	-609	-322
Loans from multilateral organizations	120	179	336	595	376
Other <u>3/</u>	-239	106	398	83	-301
C. Overall balance	-1,701	-548	-1,674	-3,076	-1,802
D. Financing	1,701	548	1,674	3,076	1,802
Change in assets (increase -)	-202	-1,843	480	859	-358
Arrears	917	-2,408	-1,001	30	-418
IMF position (net)	--	992	124	475	308
Official creditors	585	1,002	765	297	323
Commercial banks	--	3,049	1,029	962	501
Other liabilities <u>4/</u>	401	-244	278	453	1,445
Memorandum items:					
Gross official reserves end-of-year	2,690	4,223	3,505	2,182	2,544
Arrears, end-of-year	4,247	1,564	445	418	--
(In months of merchandise imports)					
Gross official reserves end-of-year	7.2	13.5	10.4	5.9	7.2

1/ Excludes from gross capital outflows the amortizations rescheduled with commercial banks and with other nonofficial creditors; the financing counterpart is likewise excluded from capital inflows.

2/ Includes US\$610 million in negative direct investment related to the purchase by Argentina of the COGASCO pipeline, which is largely compensated by foreign borrowing included in other capital.

3/ Includes the transformation of private debt with exchange guarantee into public debt, and errors and omissions.

4/ Includes valuation and other adjustments.

conversion, but this inflow would have an offset in the increased amortization of external public debt. Trade financing would continue to contribute to capital outflows, while on the basis of loans already signed or about to be agreed net lending from international organizations is expected to decline from the high level of 1987.

b. Cooperation with the Fund

The proposed request for a purchase under the compensatory financing facility may be approved only if the Fund is satisfied that Argentina has been cooperating with the Fund in efforts to find, where required, appropriate solutions for its balance of payments difficulties.

Under a stand-by arrangement with the Fund approved in December 1984 and in effect through June 1986, Argentina made considerable progress in bringing down the rate of inflation and in reducing external imbalances despite some slippages in policy implementation. A new arrangement with the Fund was approved in principle in February 1987 and came into effect in July 1987 after satisfactory arrangements had been made for financing the balance of payments in 1987. However, as a result of slippages in policy implementation and adverse exogenous developments it was necessary to amend the stand-by arrangement in December 1987. Key fiscal measures were approved by Congress in early 1988 and, upon the definition of policies for 1988, the authorities are requesting that the Fund complete the second review of the arrangement. 1/

Argentina maintains a complex system of trade and exchange controls that involves exchange restrictions and multiple currency practices that are subject to approval under Article VIII. 2/ The exchange restrictions include those evidenced by payments arrears on current international transactions, the suspension of foreign exchange sales for certain current transactions, and a minimum financing requirement for most imports. Multiple currency practices arise from the maintenance of two official exchange markets, from the requirement that the transfer abroad of profits and dividends be effected through the purchase of marketable Government of Argentina bonds denominated in U.S. dollars, and from a number of special programs for exports. In the light of these measures and the adoption of an economic program for 1988 that should permit further liberalization, the staff report on the review under the stand-by arrangement recommends that temporary approval be granted for the retention of those exchange restrictions and multiple currency practices other than those arising from external payments arrears, that are non-discriminatory.

1/ See the staff report for the review under stand-by arrangement (EBS/88/41, Supplement 1).

2/ A summary description of Argentina's exchange practices is provided in Appendix III of the staff report for the review under the stand-by arrangement.

External payments arrears have been reduced in recent years, and the Argentine authorities intend to eliminate them as external financing arrangements are made for 1988. However, pending the obtaining of such financing, the authorities' program envisages an increase in external payments arrears over the next few months, but through June 1988, they are not to exceed a specified limit. As described more fully in the accompanying staff report on the review under Argentina's stand-by arrangement, the staff is not recommending approval of the restriction that will give rise to external payments arrears.

2. Estimation of the export shortfall

The proposed CF purchase by Argentina is based on a shortfall estimated for the 12 months ended December 1987. Since actual export data are available only through June 1987, the staff, in cooperation with the authorities, has estimated the value of exports for the second half of the shortfall year. The calculation of the shortfall on the basis of partially estimated data for the shortfall year is made in accordance with paragraph 5 of the decision on compensatory financing of export fluctuations (Decision No. 6224-(79/135)).

After increasing by nearly 5 percent in 1985, the total value of Argentina's exports declined by 29 percent in 1986 and by a further 18 percent in 1987, the shortfall year. Export earnings are projected to recover by 22 percent in the first post-shortfall year and by 9 percent in the second post-shortfall year. On the basis of these annual movements, the export shortfall for the year ended December 1987 is calculated at SDR 1,324.6 million, far in excess of the proposed purchase of SDR 233.15 million (Table 2).

Table 2. Argentina: Estimation of the Export Shortfall

(In millions of SDRs)

	Years Ending December			Projected 1/	
	1985	1986	1987	1988	1989
Exports	8,269	5,841	4,792 <u>2/</u>	5,838	6,336
Shortfall			1,324.6		
Proposed purchase			233.15		

1/ Based on judgmental forecast of earnings given in Table 3.

2/ Data for July-December are estimated.

Argentina's last CF purchase of SDR 518.8 million (equivalent to 46.6 percent of quota) in July 1987 was in respect of a shortfall in merchandise export earnings for the 12 months ended December 1986, calculated at SDR 865.4 million. Ex post calculations based on actual data through June 1987 and estimated exports for the remainder of that year and revised projections for 1988 indicate that a shortfall of SDR 555.3 million was recorded for the year to December 1986. While the shortfall at the time of the last purchase was thus overestimated, the revised shortfall on the basis of present information indicates that Argentina was not overcompensated. The shortfall for 1986 was overestimated because the value of exports projected for both post-shortfall years, 1987 and 1988, were higher than now seems likely to be realized. Developments affecting exports in 1987, the first year of the projection period for the last purchase, which is also the shortfall year underlying the present CF request, are discussed in Section 3 below.

3. Causes of the shortfall and export earnings prospects

The overall export shortfall, estimated at SDR 1.3 billion, is mainly the result of a shortfall in agricultural products of SDR 959.5 million (Table 3); a sizable shortfall is also estimated for "other" products (SDR 248.2 million) with smaller shortfalls for petroleum products (SDR 70.4 million) and manufactured products (SDR 11.6 million).

The shortfall in total earnings reflects mainly lower volumes but there was also a significant shortfall in unit values. For commodities accounting for over 70 percent of total earnings (i.e. all exports excluding the broad category of "other" exports), the index of export volume in the shortfall year was 18 percent lower than the medium-term trend, while the index of export unit values was 11 percent lower (Table 4). This volume drop in 1987 was significantly larger than the modest decline of 1 percent envisaged in the projections made for that year at the time of Argentina's last CF purchase in July 1987. ^{1/} Although in mid-1987 it was clear that agricultural production had been reduced by abnormally high rainfall and flooding in the main cereal and oilseed producing areas in March, early April, and May 1987, the full severity of the damage was not known at that time. All cereal crops except wheat (which is harvested in December-January) were affected by the adverse weather, as were all oilseeds, and some other agricultural products, especially vegetables and cotton. The volume of cereals exported in 1987 is now estimated to have fallen by 31 percent (compared with the mid-1987 projection of a decline of 21 percent); that of oilseeds to have declined by 19 percent (compared with a projected increase of 1 percent); and that of other agricultural products to have risen by 10 percent (compared with a projected increase of 24 percent). The volume of some agricultural exports, especially cereals, tea, and sugar was also reduced by a smaller area planted for the 1987 crop because declining international prices for the third year in succession lowered returns to producers. The volume of sugar exports also fell because of a further reduction in Argentina's export quota to the United States.

^{1/} Projections for the year ended December 1987 were made in May/June 1987.

Table 3. Argentina: Export Earnings and Shortfalls By Major Commodities, 1982-89

	Years Ending December								Shortfall 1/	
	1982	1983	1984	1985	1986	1987 2/	1988 3/	1989 3/	Geo-metric	Arith-metic
----- (In millions of SDRs) -----										
Total exports	<u>6,906</u>	<u>7,330</u>	<u>7,909</u>	<u>8,269</u>	<u>5,841</u>	<u>4,792</u>	<u>5,838</u>	<u>6,336</u>	<u>1,324.6</u>	<u>1,423.2</u>
Agriculture	4,068	5,192	5,472	5,195	3,596	2,731	3,520	3,812	959.5	1,039.8
Cereals	(1,680)	(2,740)	(2,165)	(2,232)	(1,077)	(565)	(788)	(893)	(426.0)	(546.0)
Oilseeds 4/	(1,009)	(1,250)	(2,236)	(1,962)	(1,615)	(1,203)	(1,645)	(1,774)	(416.0)	(436.8)
Beef 4/	(614)	(468)	(319)	(318)	(336)	(392)	(418)	(432)	(-15.5)	(-12.8)
Other	(765)	(734)	(752)	(683)	(568)	(571)	(669)	(713)	(66.9)	(69.8)
Petroleum products	475	310	324	518	127	82	126	121	70.4	112.8
Manufactures	599	451	518	615	559	574	564	619	11.6	12.2
Other products	1,764	1,377	1,595	1,941	1,559	1,405	1,628	1,784	248.2	258.4
----- (Percentage changes) -----										
Total Exports		<u>6.1</u>	<u>7.9</u>	<u>4.6</u>	<u>-29.4</u>	<u>-18.0</u>	<u>21.8</u>	<u>8.5</u>		
Agriculture		27.6	5.4	-5.1	-30.8	-24.1	28.9	8.3		
Cereals		(63.1)	(-21.0)	(3.1)	(-51.7)	(-47.5)	(39.5)	(13.3)		
Oilseeds 4/		(23.9)	(78.9)	(-12.3)	(-17.7)	(-25.5)	(36.7)	(7.8)		
Beef 4/		(-23.8)	(-31.8)	(-0.3)	(5.7)	(16.7)	(6.6)	(3.3)		
Other		(-4.1)	(2.5)	(-9.2)	(-16.8)	(0.5)	(17.2)	(6.6)		
Petroleum products		-34.7	4.5	59.9	-75.5	-35.4	53.7	-4.0		
Manufactures		-24.7	14.9	18.7	-9.1	2.7	-1.7	9.8		
Other products		-21.9	15.8	21.7	-19.7	-9.9	15.9	9.6		

1/ Shortfall calculations may be affected by rounding of export data.

2/ Data for the last six months (July-December) are estimated.

3/ Projected.

4/ Includes products of relevant categories.

Table 4. Argentina: Value, Volume, and Unit Value by Major Commodities, 1982-89
(1987=100; In terms of SDRs)

	Value Share In Total Exports In 1987 (In percent)	Year Ending December								Shortfall In Percent Of Level In Shortfall Year 3/
		1982	1983	1984	1985	1986	1987 1/	1988 2/	1989 2/	
Value	71.0	151	175	185	185	126	100	124	134	31.1
Agriculture	56.9	149	191	200	190	131	100	129	140	35.1
Cereals	(11.7)	(299)	(487)	(384)	(396)	(190)	(100)	(140)	(158)	(75.5)
Oilseeds 4/	(25.0)	(84)	(104)	(186)	(163)	(134)	(100)	(137)	(148)	(34.7)
Beef 4/	(8.1)	(156)	(119)	(81)	(81)	(86)	(100)	(107)	(111)	(-3.7)
Other	(12.1)	(133)	(130)	(132)	(118)	(100)	(100)	(117)	(125)	(11.5)
Petroleum products	1.7	563	369	385	615	153	100	151	145	83.1
Manufactures	12.0	105	79	90	107	97	100	99	108	2.1
Volume		105	117	109	127	114	100	121	125	17.7
Agriculture		105	125	115	127	117	100	125	130	19.3
Cereals		(150)	(238)	(180)	(213)	(144)	(100)	(129)	(134)	(39.6)
Oilseeds 4/		(56)	(70)	(103)	(111)	(124)	(100)	(135)	(139)	(20.9)
Beef 4/		(178)	(133)	(83)	(90)	(96)	(100)	(109)	(110)	(0.7)
Other		(111)	(123)	(100)	(102)	(91)	(100)	(111)	(123)	(4.9)
Petroleum products		311	222	208	378	166	100	160	149	71.6
Manufactures		81	69	69	94	99	100	98	102	-1.4
Unit Value		144	150	170	146	111	101	102	107	11.3
Agriculture		142	153	174	150	112	100	103	108	13.3
Cereals		(199)	(205)	(213)	(186)	(132)	(100)	(109)	(118)	(25.9)
Oilseeds 4/		(150)	(149)	(181)	(147)	(108)	(100)	(101)	(106)	(11.2)
Beef 4/		(88)	(89)	(98)	(90)	(90)	(100)	(98)	(101)	(-4.3)
Other		(120)	(106)	(132)	(116)	(110)	(100)	(105)	(102)	(6.4)
Petroleum products		181	166	185	163	92	100	94	97	6.5
Manufactures		130	114	130	114	98	100	101	106	3.6

1/ Data for the last six months (July-December) are estimated.

2/ Projected.

3/ Negative shortfalls indicate an excess.

4/ Includes products of relevant categories.

In mid-1987 it also was expected that the volume of exports of petroleum products would decline by 31 percent in 1987 due to stagnant domestic production of crude oil and increasing domestic consumption associated with a higher level of economic activity. In the event, domestic consumption of fuel oil and gas oil increased faster than expected, owing to a temporary shortage of natural gas caused by unforeseen pipeline maintenance problems during the peak heating season (June-September), and the volume of petroleum products exports fell by 40 percent.

With respect to manufacturing, it was projected in mid-1987 that the index of export volume for "major" manufactures for which volume data are available 1/ would rise by 3 percent in 1987, mainly on account of the maintenance of a competitive exchange rate and the effect of government promotion programs and incentives, in particular, the Special Program for Exports (PEEX). 2/ In addition, over 70 percent of the value of the residual category of exports ("other" exports) consists of manufactured products--mainly chemicals, machinery, automobile parts, and textiles shipped to Latin American markets--for which volume indices are not available. In mid-1987, earnings from these other products were projected to increase by 15 percent for the year as a whole. However, although the real effective exchange rate depreciated by 7 percent in 1987, the export volume of "major" manufactures is estimated to have increased by only 1 percent, somewhat below the estimated market growth (Table 5), and the number of export contracts fulfilled under the PEEX proved to be much less than expected. The value of "other" manufactured exports is estimated to have risen by a similar amount, implying a decline in volume.

The decline in export volume of traditional commodities in the short-fall year may also be due, to a limited extent, to an under-recording of the volume actually exported as some exporters took advantage of the substantial premium that existed in the parallel foreign exchange market until the devaluation of the austral in October 1987. In the case of corn, for example, the discrepancy between availability and utilization of about 1 million tons may indicate that some corn may have been exported through unofficial channels. 3/

As noted above, the overall shortfall also partly reflected a short-fall in unit value. Although there was an upturn in the international prices of cereals, oilseeds and oils, and other agricultural products during 1987, Argentina's average unit values for these exports for the year as a whole were lower than in 1986 and were, respectively, 36 percent,

1/ The manufactures exports for which volume data are available are shown in Annex I, Tables 6 and 7.

2/ A description of the PEEX is provided in Section 3 of Annex I.

3/ Although it is not possible to determine precisely the amount of these unofficial exports, if the full amount of this difference of 1 million tons had been recorded and valued at the average unit price for 1987, recorded earnings in 1987 would have been raised by SDR 56 million.

Table 5. Argentina: Growth in Exports and
Underlying Factors, 1984-89

(Change in percent)

	Years Ending December				Average 1988-89 2/
	1984	1985	1986	1987 1/	
Export growth 3/					
Value	6	--	-32	-21	18
Volume	-7	17	-10	-13	15
Unit price	13	-14	-24	-9	3
Agricultural exports					
Value	5	-5	-31	-24	22
Volume	-8	10	-8	-15	18
Unit price	14	-14	-25	-11	4
Manufactured exports					
Value	14	19	-9	3	2
Volume	--	36	5	1	--
Unit price	14	-12	-14	2	2
Underlying factors					
1. Market growth					
Real GDP in trading partners	4.0	3.3	3.5	2.9	3.1
Non-oil import volume of trading partners	9.0	6.6	5.0	2.2	3.9
2. Competitiveness indicator					
Changes in real effective exchange rate 4/ (-depreciation)	16.5	-11.5	0.1	-7.3	...

1/ Estimated.

2/ Projected.

3/ Based on the value and volume of exports which account for 71 percent of total export earnings; value and unit price are in SDR terms.

4/ As measured by changes in the Information Notice System index of the trade-weighted effective exchange rate adjusted for relative price movements, period average.

21 percent, and 12 percent below their average values in the two pre-shortfall years. These declines reflected an excess of supply over utilization on world markets. The unit values of petroleum products and manufactures were higher in 1987 than in 1986, but were still 18 percent and 5 percent below their respective preshortfall year averages. By contrast, the unit value of beef and beef products was 11 percent higher in 1987 than in 1985-86.

Aggregate earnings are projected to increase by 22 percent in 1988 and by a further 9 percent in 1989. The projected improvement in 1988 reflects to a large extent the expected recovery of agricultural exports from the weather-related depressed levels in the shortfall year. By 1989 this recovery is expected to be complete and further growth dependent on the continued implementation of the adjustment strategy, which is likely to result in export growth beyond that conservatively projected at present. Even after this recovery, earnings would still be below the level recorded in any year from 1981 to 1985. The recovery in earnings is expected to come mainly from a recovery in volumes; an average annual rate of growth in export volume of 15 percent is projected, largely reflecting the increased availability of cereals and oilseeds associated with a return to normal weather conditions. The production of oilseeds will also be augmented by a shift in land use away from cereals in 1988, but higher international prices for most cereals and oilseeds resulting from an anticipated tightening of global markets should increase the area planted and production of both cereals and oilseeds in 1989. More favorable weather conditions should assist in raising the volume of wool, tea, and cotton exports in 1988-89, while a higher volume of beef exports will be made possible by an expected decline in domestic consumption. A further increase in the volume of marine products exports is based on marketing agreements signed with the U.S.S.R. and Bulgaria.

The volume of petroleum products exports is expected to recover significantly in 1988 because natural gas will be substituted for fuel oil and gas oil in heating and electricity generation, thereby releasing these products for export, and a refinery upgrading program scheduled to be completed by mid-1988 will make more hydrocarbons and other lighter grade products available. A small decline in the volume of petroleum product exports in 1989 is anticipated owing to rising domestic consumption. For manufactured products for which volume data are available, a small decline in the volume in the first post-shortfall year is expected to be followed by a small increase in 1989 as a result of greater reliance by the authorities on the maintenance of a competitive exchange rate, rather than on special incentive schemes. 1/

1/ For Argentina's "other" manufactured exports, the average annual rate of growth of 11 percent projected for 1988-89 implies an average annual volume growth of 9 percent, assuming that unit values move in line with the projected development of the UN index of prices of manufactured goods exported by industrial countries.

The recovery of earnings is also expected to come in part from an average annual rate of growth of 3 percent in unit values based on the expected development of international prices. The recovery of prices of cereals, oilseeds, beef, marine products, wool, sugar, tea, and cotton which began during 1987 is expected to continue in 1988-89 due to a tightening of global markets. Manufactured goods prices, which increased throughout 1987, are also expected to rise modestly in 1988-89. The unit values of petroleum products, however, are projected to decline somewhat in 1988 and to partially recover in 1989, broadly in line with the expected movement of international crude oil prices.

4. Repurchase

In accordance with paragraph 7 of the compensatory financing decision, the Argentine authorities are expected to represent that they will make a prompt repurchase in respect of any outstanding part of this purchase if the amount purchased on the basis of partly estimated data (i.e., estimates for the 6-month period (July-December 1987) exceeds the amount that they would have purchased on the basis of actual data for the entire shortfall year. The amount to be repurchased would be equivalent to the excess of the actual purchase over the amount that could have been purchased on the basis of actual data for the entire shortfall year.

5. Staff appraisal

The Argentine authorities are expected to request a purchase of SDR 233.1 million (21 percent of quota) under the compensatory financing facility in respect of a shortfall calculated at SDR 1,324.6 million for the 12 months ended December 1987. Data for the shortfall year are partly estimated and, in accordance with paragraph 7 of the compensatory financing decision, the request is expected to include a representation that Argentina will make a prompt repurchase of the amount, if any, by which the proposed purchase exceeds the amount that could have been purchased on the basis of actual, rather than estimated, data for the entire shortfall year. If approved, the proposed purchase would raise Argentina's total purchases outstanding under the facility to 83 percent of quota.

Both the overall deficit and the current account deficit rose sharply in 1987. The deterioration in the current account was due entirely to a sharp reduction in the trade surplus, largely attributable to a substantial decline in export volumes, but also reflecting some import growth. The balance on the capital account was also sharply lower, mainly due to increased short-term capital outflows, resulting in an overall deficit nearly double that of 1986. The current account deficit is expected to narrow in 1988 as a result of a projected rise in the trade surplus, largely associated with a recovery in exports. Even though the surplus on the capital account is also expected to improve, a large overall deficit remains in prospect for 1988.

The staff also considers that the requirement of cooperation that applies to purchases in the upper CF tranche is met by the performance under the stabilization program in support of which the Fund approved a stand-by arrangement in July 1987. The review of performance under this arrangement is to be considered concurrently with the CF request. The request for a compensatory financing purchase is expected to include the statement that Argentina will cooperate with the Fund in an effort to find, where required, appropriate solutions for its balance of payments difficulties.

Following a modest increase in 1985, Argentina's export performance deteriorated sharply in 1986 with the total value of exports falling by 29 percent. There was a further decline by an estimated 18 percent in the shortfall year (1987). In the first post-shortfall year, exports are expected to stage a recovery of about 22 percent with a further increase of some 9 percent in prospect for 1989. The improvement in 1988 largely reflects the expected resurgence of agricultural exports from the depressed weather-related levels in 1987. The current projection for 1989 may be viewed as being somewhat conservative, as there is considerable scope for further improvement as the adjustment strategy proceeds. On the basis of these movements, a shortfall of SDR 1,324.6 million is calculated for calendar year 1987 which comprises shortfalls for all major export categories. The main component of the shortfall is agricultural products (SDR 959.5 million), which accounted for about 57 percent of exports in the shortfall year. Smaller shortfalls are calculated for petroleum products (SDR 70.4 million), manufactures (11.6 million), and "other" exports (SDR 248.2 million).

The shortfall in agricultural exports is the result of shortfalls in both volume and unit value, although volume developments predominate. Underlying the volume shortfalls in the agricultural sector, particularly for all cereal crops (except wheat) and oilseeds, was abnormally high rainfall and flooding in the main growing areas particularly in March and early April 1987. The volume of petroleum products exports was also sharply lower in the shortfall year as domestic consumption rose, following a temporary shortage of natural gas as a result of unforeseen pipeline maintenance problems, and growth in manufactured exports was less buoyant than anticipated. As noted, in addition to these volume effects, the shortfall was also a result of a continued weakness in world market prices for many of Argentina's major agricultural exports. Export unit values in the shortfall year for agricultural products as a whole were 23 percent lower than the average of the two preshortfall years; the decline was particularly severe for cereals (36 percent) and oilseeds and oils (21 percent).

In 1988, the first post-shortfall year, aggregate export earnings are expected to recover by 22 percent, to be followed by a 9 percent increase in 1989. Underlying this improvement is an expected recovery in export volumes, which should rise by about 15 percent per year. Agricultural output is expected to rise as weather conditions return to normal, and also because global markets are expected to tighten with higher prices

leading to an increase in planted area. Petroleum product exports should also increase as natural gas is substituted for fuel oil in heating and electricity generation. The outlook for manufactures is less buoyant, although some growth is anticipated as a result of the maintenance of a competitive exchange rate. As regards export unit values, prospects are for some improvement in the prices of agricultural products, particularly cereals as the glut in world supply is expected to be reduced.

In view of the above, the staff considers that Argentina's request for a purchase under the compensatory financing decision meets all the requirements set forth in that decision. Accordingly the following draft decision is proposed for adoption by the Executive Board after a duly authenticated request has been received.

1. The Fund has received a request from the Government of Argentina for a purchase equivalent to SDR 233.15 million under the decision on compensatory financing of export fluctuations (Decision No. 6224-(79/135) adopted August 2, 1979, as amended).
2. The Fund notes the representations of Argentina and approves the purchase in accordance with the request.
3. The Fund waives the limitations in Article V, Section 3(b)(iii).

Analysis of Export Shortfalls by Reference to Developments
and Prospects for Major Categories 1/

1. Agricultural exports

Agricultural exports, including marine products and processed products of primary origin, had a 57 percent share in total export earnings in 1987. The shortfall for this group of commodities is estimated at SDR 959.5 million (Table 6), reflecting shortfalls in both volume and unit value; the index of export volume in 1987 was 19 percent below its medium-term trend, while the index of unit value was 13 percent lower (Table 7). Large shortfalls are estimated for cereals (SDR 426.0 million) and oilseeds and oils (SDR 416.0 million) the major categories of agricultural exports, and a smaller shortfall (SDR 66.9 million) for "other" agricultural products; a small excess (SDR 15.5 million) is estimated for beef and beef products.

a. Cereals

The main cereal exports are wheat, and its by-product bran, corn, sorghum, and rice. The combined shortfall for cereal earnings (SDR 426 million) reflects shortfalls in both volume and unit value, but the contribution of volume is significantly larger. With the exception of wheat, which is harvested in December and January, the volume shortfall results mainly from lower supply caused by abnormally high rainfall and flooding in the cereal-producing provinces in March and May 1987. The unit value shortfall reflects declining international prices during 1985-86 and most of 1987, as well as the expected continuation in the two post-shortfall years of the upturn in prices which occurred in the final quarter of 1987.

(1) Wheat and bran

The area sown to wheat declined by 17 percent in 1984/85 and by a further 5 percent in 1985/86 (crop years ending March) because producer returns were adversely affected by falling international prices. Wheat production, however, declined by 4.9 million tons (36 percent) in 1985/86 because of flooding and disease caused by heavy rainfall in November 1985 at the maturation stage of crop development. ^{2/} Although domestic consumption remained fairly stable, the availability of supplies for export was reduced by a low stock carryover from 1984/85, and the volume of exports in 1986 fell by 5.6 million tons (58 percent). With global supply again exceeding utilization and intensified competition from other major exporters, international wheat prices declined sharply in 1986, and Argentina's average unit value fell by 28 percent, so that earnings were 70 percent lower than in 1985.

^{1/} All references to value, volume, and unit value movements in the shortfall year 1987 are estimates; data for July-December have been estimated by the staff in cooperation with the authorities.

^{2/} Wheat is planted in July-August and is harvested in December-January.

Table 6. Argentina: Export Earnings and Shortfalls By Major Commodities, 1982-89

	Years Ending December								Shortfall 1/	
	1982	1983	1984	1985	1986	1987 2/	1988 3/	1989 3/	Geo-metric	Arith-metic
(In millions of SDRs)										
Total exports	6,906	7,330	7,909	8,269	5,841	4,792	5,838	6,336	1,324.6	1,423.2
Agriculture	4,068	5,192	5,472	5,195	3,596	2,731	3,520	3,812	959.5	1,039.8
Cereals	1,680	2,740	2,165	2,232	1,077	565	788	893	426.0	546.0
Wheat and bran	675	1,450	957	1,153	366	288	409	453	180.3	245.8
Wheat	(612)	(1,379)	(900)	(1,116)	(335)	(268)	(378)	(429)	(170.7)	(237.2)
Bran	(63)	(71)	(57)	(37)	(31)	(20)	(31)	(24)	(8.0)	(8.6)
Corn	530	751	726	754	555	217	307	349	178.9	219.4
Sorghum	460	518	440	292	130	53	61	80	46.6	70.2
Rice	15	21	42	33	26	7	11	11	7.9	10.6
Oilseeds	1,009	1,250	2,236	1,962	1,615	1,203	1,645	1,774	416.0	436.8
Soybeans	386	301	828	573	416	192	366	390	173.6	195.4
Soy oil and meal	224	430	726	651	678	665	893	942	91.0	100.8
Peanuts	18	29	37	44	50	38	33	38	2.2	2.6
Sunflower oil and seeds	254	352	492	575	394	241	286	330	107.7	124.2
Linseed oil and meal	127	138	153	119	77	67	67	74	11.8	13.8
Beef 4/	614	468	319	318	336	392	418	432	-15.5	-12.8
Other agriculture	765	734	752	683	568	571	669	713	66.9	69.8
Vegetables and fruit	235	186	177	214	198	179	181	197	14.4	14.8
Beans	(53)	(49)	(66)	(77)	(86)	(38)	(43)	(43)	(16.1)	(19.4)
Fresh fruit	(182)	(137)	(111)	(137)	(112)	(141)	(138)	(154)	(-5.3)	(-4.6)
Wool	168	135	159	128	104	103	98	99	2.9	3.4
Marine products	171	155	154	145	187	209	303	317	13.4	23.2
Minor agricultural products	191	258	262	196	79	80	87	100	21.5	28.4
Petroleum products	475	310	324	518	127	82	126	121	70.4	112.8
Fuel oil	264	173	207	279	55	30	48	27	26.9	57.8
Gas oil	137	60	46	134	27	10	35	48	26.0	40.8
Hydrocarbons	74	77	71	105	45	42	43	46	10.3	14.2
Manufactures	599	451	518	615	559	574	564	619	11.6	12.2
Tanned leather	258	239	285	275	291	272	271	289	7.5	7.6
Tannin	60	45	40	40	35	29	27	27	2.2	2.6
Aluminum ingots	62	48	74	102	66	77	33	33	-20.7	-14.8
Steel pipes and plates	207	106	108	178	154	184	224	260	12.6	16.0
Synthetic rubber	12	13	11	20	13	12	9	10	0.3	0.8
Other products	1,764	1,377	1,595	1,941	1,559	1,405	1,628	1,784	248.2	258.4

Table 6 (Concluded). Argentina: Export Earnings and Shortfalls By Major Commodities, 1982-89

	Years Ending December						
	1983	1984	1985	1986	1987 ^{2/}	1988 ^{3/}	1989 ^{3/}
	(Percentage changes)						
Total Exports	6.1	7.9	4.6	-29.4	-18.0	21.8	8.5
Agriculture	27.6	5.4	-5.1	-30.8	-24.1	28.9	8.3
Cereals	63.1	-21.0	3.1	-51.7	-47.5	39.5	13.3
Wheat and bran	114.8	-34.0	20.5	-68.3	-21.3	42.0	10.8
Wheat	(125.3)	(-34.7)	(24.0)	(-70.0)	(-20.0)	(41.0)	(13.5)
Bran	(12.7)	(-19.7)	(-35.1)	(-16.2)	(-35.5)	(55.0)	(-22.6)
Corn	41.7	-3.3	3.9	-26.4	-60.9	41.5	13.7
Sorghum	12.6	-15.1	-33.6	-55.5	-59.2	15.1	31.1
Rice	40.0	100.0	-21.4	-21.2	-73.1	57.1	---
Oilseeds	23.9	78.9	-12.3	-17.7	-25.5	36.7	7.8
Soybeans	-22.0	175.1	-30.8	-27.4	-53.8	90.6	6.6
Soy oil and meal	92.0	68.8	-10.3	4.1	-1.9	34.3	5.5
Peanuts	61.1	27.6	18.9	13.6	-24.0	-13.2	15.2
Sunflower oil and seeds	38.6	39.8	16.9	-31.5	-38.8	18.7	15.4
Linseed oil and meal	8.7	10.9	-22.2	-35.3	-13.0	---	10.4
Beef ^{4/}	-23.8	-31.8	-0.3	5.7	16.7	6.6 ^a	3.3
Other agriculture	-4.1	2.5	-9.2	-16.8	0.5	17.2	6.6
Vegetables and fruit	-20.9	-4.8	20.9	-7.5	-9.6	1.1	8.8
Beans	(-7.5)	(34.7)	(16.7)	(11.7)	(-55.8)	(13.2)	(---
Fresh fruit	(-24.7)	(-19.0)	(23.4)	(-18.2)	(25.9)	(-2.1)	(11.6)
Wool	-19.6	17.8	-19.5	-18.8	-1.0	-4.9	1.0
Marine products	-9.4	-0.6	-5.8	29.0	11.8	45.0	4.6
Minor agricultural products	35.1	1.6	-25.2	-59.7	1.3	8.7	14.9
Petroleum products	-34.7	4.5	59.9	-75.5	-35.4	53.7	-4.0
Fuel oil	-34.5	19.7	34.8	-80.3	-45.5	60.0	-43.8
Gas oil	-56.2	-23.3	191.3	-79.9	-63.0	250.0	37.1
Hydrocarbons	4.1	-7.8	47.9	-57.1	-6.7	2.4	7.0
Manufactures	-24.7	14.9	18.7	-9.1	2.7	-1.7	9.8
Tanned leather	-7.4	19.2	-3.5	5.8	-6.5	-0.4	6.6
Tannin	-25.0	-11.1	---	-12.5	-17.1	-6.9	---
Aluminum ingots	-22.6	54.2	37.8	-35.3	16.7	-57.1	---
Steel pipes and plates	-48.8	1.9	64.8	-13.5	19.5	21.7	16.1
Synthetic rubber	8.3	-15.4	81.8	-35.0	-7.7	-25.0	11.1
Other products	-21.9	15.8	21.7	-19.7	-9.9	15.9	9.6

^{1/} Shortfall calculations may be affected by rounding of export data.

^{2/} Data for the last six months (July-December) are estimated.

^{3/} Projected.

^{4/} Includes products of relevant categories.

Table 7. Argentina: Value, Volume, and Unit Value by Major Commodities, 1982-89
(1987=100; In terms of SDRs)

	Value Share In Total Exports In 1987 (In percent)	Years Ending December								Shortfall In Percent Of Level In Shortfall Year 3/
		1982	1983	1984	1985	1986	1987 1/	1988 2/	1989 2/	
Value	71.0	151	175	185	185	126	100	124	134	31.1
Agriculture	56.9	149	191	200	190	131	100	129	140	35.1
Cereals	11.7	299	487	384	396	190	100	140	158	75.5
Wheat and bran	6.0	235	504	333	402	127	100	142	157	62.6
Wheat	(5.6)	(229)	(515)	(337)	(417)	(125)	(100)	(141)	(160)	(63.7)
Bran	(0.4)	(315)	(354)	(282)	(186)	(153)	(100)	(155)	(119)	(39.3)
Corn	4.5	245	347	335	348	256	100	142	161	82.7
Sorghum	1.1	875	985	837	554	246	100	117	153	89.4
Rice	0.1	220	294	600	479	377	100	154	154	112.0
Oilseeds	25.0	84	104	186	163	134	100	137	148	34.7
Soybeans	4.0	201	157	432	299	217	100	191	204	90.8
Soy oil and meal	13.9	34	65	109	98	102	100	135	142	13.9
Peanuts	0.8	48	77	98	117	133	100	86	101	6.2
Sunflower oil and seeds	5.0	106	147	205	239	163	100	119	137	44.7
Linseed oil and meal	1.3	190	208	230	179	117	100	100	110	18.2
Beef 4/	8.1	156	119	81	81	86	100	107	111	-3.7
Other agriculture	12.1	133	130	132	118	100	100	117	125	11.5
Vegetables and fruit	3.8	129	103	97	118	109	100	101	110	7.4
Beans	(0.8)	(139)	(128)	(175)	(203)	(227)	(100)	(115)	(115)	(43.5)
Fresh fruit	(3.0)	(126)	(96)	(77)	(95)	(78)	(100)	(97)	(108)	(-4.9)
Wool	2.2	164	132	155	125	102	100	96	96	3.3
Marine products	4.4	82	74	74	69	89	100	145	152	6.2
Minor agricultural products	1.7	236	336	328	239	102	100	108	124	26.7
Petroleum products	1.7	563	369	385	615	153	100	151	145	83.1
Fuel oil	0.6	876	573	685	923	181	100	160	89	88.5
Gas oil	0.2	1,354	593	454	1,326	270	100	344	472	257.2
Hydrocarbons	0.9	178	183	170	252	108	100	102	109	24.8
Manufactures	12.0	105	79	90	107	97	100	99	108	2.1
Tanned leather	5.7	95	88	105	101	107	100	100	106	2.8
Tannin	0.6	209	157	140	141	122	100	94	94	8.7
Aluminum ingots	1.6	81	62	96	132	86	100	42	42	-27.5
Steel pipes and plates	3.9	113	58	58	97	84	100	122	142	7.1
Synthetic rubber	0.2	102	113	92	170	110	100	81	87	5.7

Table 7 (Continued). Argentina: Value, Volume, and Unit Value by Major Commodities, 1982-89
(1987=100: In terms of SDRs)

	Years Ending December								Shortfall In Percent Of Level In Shortfall Year 3/
	1982	1983	1984	1985	1986	1987 1/	1988 2/	1989 2/	
Volume	105	117	109	127	114	100	121	125	17.7
Agriculture	105	125	115	127	117	100	125	130	19.3
Cereals	150	238	180	213	144	100	129	134	39.6
Wheat and bran	96	240	165	217	99	100	134	134	31.0
Wheat	(91)	(244)	(166)	(230)	(96)	(100)	(132)	(135)	(31.5)
Bran	(163)	(188)	(157)	(30)	(139)	(100)	(158)	(113)	(-5.7)
Corn	134	168	141	181	189	100	128	135	42.7
Sorghum	514	511	402	316	189	100	106	128	52.0
Rice	176	250	391	329	332	100	147	147	88.2
Oilseeds	56	70	103	111	124	100	135	139	20.9
Soybeans	143	109	236	224	196	100	174	180	68.9
Soy oil and meal	27	45	72	76	99	100	138	138	7.5
Peanuts	39	65	68	91	106	100	92	106	-1.2
Sunflower oil and seeds	60	93	85	127	148	100	113	121	20.8
Linseed oil and meal	95	124	119	93	76	100	99	106	-5.8
Beef 4/	178	133	83	90	96	100	109	110	0.7
Other agriculture	111	123	100	102	91	100	111	123	4.9
Vegetables and fruit	91	94	88	108	86	100	104	108	0.8
Beans	(115)	(124)	(139)	(153)	(175)	(100)	(115)	(115)	(28.8)
Fresh fruit	(85)	(86)	(74)	(96)	(62)	(100)	(101)	(106)	(-8.6)
Wool	117	113	118	104	109	100	107	113	6.5
Marine products	97	78	53	62	85	100	120	140	2.4
Minor agricultural products	186	320	225	194	93	100	112	124	20.2
Petroleum products	311	222	208	378	166	100	160	149	71.8
Fuel oil	451	315	306	490	186	100	171	94	71.1
Gas oil	683	328	239	818	233	100	370	497	222.8
Hydrocarbons	135	136	135	205	137	100	106	108	26.3
Manufactures	81	69	69	94	99	100	98	102	-1.4
Tanned leather	84	80	84	98	110	100	106	110	4.7
Tannin	196	131	109	109	111	100	100	100	3.9
Aluminum ingots	83	50	66	123	93	100	44	44	-26.0
Steel pipes and plates	58	50	44	72	84	100	108	115	-5.6
Synthetic rubber	75	79	58	121	92	100	79	75	-8.0

Table 7 (Concluded). Argentina: Value, Volume, and Unit Value by Major Commodities, 1982-89

(1987=100: In terms of SDRs)

	Years Ending December								Shortfall In Percent Of Level In Shortfall Year 3/
	1982	1983	1984	1985	1986	1987 1/	1988 2/	1989 2/	
Unit Value	144	150	170	146	111	101	102	107	11.3
Agriculture	142	153	174	150	112	100	103	108	13.3
Cereals	199	205	213	186	132	100	109	118	25.9
Wheat and bran	245	210	202	185	128	100	106	117	24.0
Wheat	(252)	(211)	(203)	(181)	(130)	(100)	(107)	(119)	(24.5)
Bran	(193)	(188)	(180)	(620)	(110)	(100)	(98)	(105)	(47.7)
Corn	183	207	238	192	135	100	111	119	27.9
Sorghum	170	193	208	175	130	100	110	120	24.6
Rice	125	118	153	146	114	100	105	105	12.9
Oilseeds	150	149	181	147	108	100	101	106	11.2
Soybeans	141	144	183	133	111	100	110	113	12.9
Soy oil and meal	126	144	151	129	103	100	98	103	6.0
Peanuts	123	118	144	129	125	100	93	95	7.3
Sunflower oil and seeds	177	158	241	188	110	100	105	113	19.7
Linseed oil and meal	200	168	193	192	154	100	101	104	25.4
Beef 4/	88	89	98	90	90	100	98	101	-4.3
Other agriculture	120	106	132	116	110	100	105	102	6.4
Vegetables and fruit	142	110	110	109	127	100	97	102	6.5
Beans	(121)	(103)	(126)	(133)	(130)	(100)	(100)	(100)	(11.6)
Fresh fruit	(148)	(112)	(104)	(99)	(126)	(100)	(96)	(102)	(4.1)
Wool	140	117	131	120	94	100	90	85	-2.9
Marine products	85	95	140	111	105	100	121	109	9.0
Minor agricultural products	127	105	146	123	110	100	96	100	5.4
Petroleum products	181	166	185	163	92	100	94	97	6.5
Fuel oil	194	182	224	188	97	100	94	95	12.8
Gas oil	198	181	190	162	116	100	93	95	10.7
Hydrocarbons	132	135	126	123	79	100	96	101	-1.2
Manufactures	130	114	130	114	98	100	101	106	3.6
Tanned leather	113	110	125	103	97	100	94	96	-2.1
Tannin	107	120	128	129	110	100	94	94	4.6
Aluminum ingots	98	124	145	107	92	100	95	95	-2.3
Steel pipes and plates	195	116	132	135	100	100	113	123	13.4
Synthetic rubber	136	143	159	140	120	100	103	116	15.0

1/ Data for the last six months (July-December) are estimated.

2/ Projected.

3/ Negative shortfalls indicate an excess.

4/ Includes products of relevant categories.

Although the rate of export duty on wheat was reduced from 15 percent to 5 percent for the 1986/87 crop, the less favorable international price outlook for wheat viz-a-viz soybeans induced a further 12 percent decline in the area planted to wheat. Improved weather conditions resulted in a lower incidence of crop losses so that the decline in harvested area was smaller (9 percent), and the average yield recovered sufficiently to raise wheat output by 0.3 million tons (3 percent). Export volume increased by 0.2 million tons in 1987, as stocks were largely depleted, but international prices continued to fall under the influence of intensified competition for markets mainly by the United States and the EC. ^{1/} Argentina's average export unit value declined by a further 23 percent, and earnings fell by 20 percent. Shortfall year earnings of SDR 268 million were 56 percent lower than average earnings in 1985/86.

Although the export duty on wheat was eliminated for the 1987/88 crop, the persistence of low international prices resulted in a further decline of about 1 percent in both area planted and harvested. Excellent growing conditions led to an improvement in yield to the second highest on record, and output rose by 12 percent. With increased availability, the volume of wheat exports is expected to rise by 1.3 million tons (32 percent) in 1988, and assuming normal weather conditions for the 1988/89 crop, export volume is projected to increase by a further 3 percent in 1989. International wheat prices turned upward in the final quarter of 1987 in response to strong demand from the U.S.S.R. and lower availability in the EC (related to adverse weather) and in Australia (because of smaller planted area), as well as in Argentina. Global utilization of wheat is expected to exceed supply in 1987/88 for the first time since 1980/81, and the market is expected to tighten further in 1988/89. Argentina's average unit value is projected to increase by 8 percent per year in 1988 and 1989. Average earnings in the two post-shortfall years are expected to be 50 percent higher than in 1987. A shortfall of SDR 171 million is estimated for wheat.

Earnings from bran are less than 10 percent of the value of wheat exports, and similar actual and projected price and volume developments to those for wheat are responsible for the shortfall of SDR 8 million estimated for bran.

(2) Corn

The output of corn, which is harvested later than wheat, in the second quarter of the year, was not severely affected in the preshortfall year by the adverse weather of November 1985. However, shortfall year production was reduced sharply by torrential rains and flooding in March/April 1987, at the beginning of the harvest. Buenos Aires province, which produces over 40 percent of corn output, received over 800 mm of rain in March; this amount is normally received in a year. The rainfall

^{1/} In 1987, the United States made substantial sales of premium quality wheat under the export enhancement program at prices between US\$85 and \$90 a ton, compared with domestic U.S. prices ranging from \$95 to \$115 a ton.

was also well in excess of normal in other producing areas. Heavy rainfall in May again affected the harvest. With the area planted to corn for the 1987 crop already 5 percent lower than in the previous year because of declining international prices and low producer returns, the adverse weather increased crop losses so that area harvested fell by 14 percent and lowered the yield of the remaining crop. Production fell by 3.2 million tons (25 percent). Domestic consumption of corn rose by 0.3 million tons in 1987 because weather damaged corn of non-export quality was fed to cattle, and export volume fell by 3.5 million tons (47 percent). ^{1/}

Favorable growing conditions in the other major corn-producing countries, especially the United States, China, and Brazil, contributed to an excess of global output over utilization in 1986/87 (year ended September) for the third successive year and global stocks reached a record 33 percent of annual utilization. As a result, international prices continued to decline, and Argentina's average unit value fell by 26 percent in 1987. Earnings were 61 percent lower than in 1986, and 66 percent lower than average earnings in 1985/86.

The sharp drop in export volume in 1987 may, to some extent, also reflect smuggling of corn to Uruguay to take advantage of a more favorable exchange rate; there is some circumstantial evidence to this effect, including a statistical discrepancy between corn availability and recorded utilization of 1 million tons in 1987. Although it is impossible to quantify the amount of illicit exports with precision, if an additional 1 million tons had been recorded at customs in 1987, shortfall year earnings would have been raised by SDR 56 million to SDR 273 million.

The global market for corn is expected to tighten appreciably in 1988-89 because of lower acreage planted in the United States and the EC and a drought-affected 1987 crop in Thailand. Argentina's unit value is projected to increase at an average annual rate of 10 percent in line with the development of international prices. Argentine production is also projected to fall in 1988 (by 3 percent), as a recovery of yield under normal weather conditions is expected only to partly offset a further 10 percent reduction in harvested area; land has been switched into soybean production which is anticipated to be more profitable. The elimination in February 1988 of the 15 percent export duty in effect in 1987 will improve producer returns, and a 5 percent increase in output is projected for 1989, entirely reflecting higher acreage. Export volume is projected to increase at an average annual rate of 20 percent, as a more competitive exchange rate should assist in keeping exports within official channels. On this basis, average earnings in the two post-shortfall years are projected to be 51 percent higher than in the shortfall year and the shortfall for corn is estimated at SDR 179 million.

^{1/} The projections for Argentina's previous CF purchase in July 1987 took into account the impact of the abnormally high rainfall on corn production, and the export volume projection for 1987 was reduced at that time from 7.9 million tons to 4.7 million tons. The current estimate for 1987 is 3.9 million tons.

(3) Sorghum

Sorghum is used almost entirely as animal feed, and as the prices of higher quality substitutes have declined sharply, external demand (mainly from Japan) has been reduced and the area planted to sorghum in Argentina was cut back by 45 percent between 1985 and 1987, being switched mainly to sunflowerseed production. The heavy rainfall in March also affected production in 1987, which declined by 25 percent, and the volume of exports was almost halved compared with 1986. Similarly to the prices of other grains, the average unit value fell by 23 percent in the shortfall year, and earnings were 73 percent below their average level in 1985-86.

A recovery in earnings is projected in the two post-shortfall years based only on higher unit value in 1988 and on both increased volume and unit value in 1989. Unit values are expected to increase by 10 percent per year being supported by higher prices for other feedgrains, and this, in conjunction with the elimination of the 15 percent export duty at the beginning of March 1988, should provide sufficient incentive to increase the area planted to sorghum and stimulate exports in 1989. Average earnings in 1988-89 are projected to be one-third higher than in the shortfall year, and a shortfall of SDR 47 million is estimated for sorghum.

(4) Rice

The production of rice in Argentina is very small in relation to the other cereals; the area sown is less than 5 percent of the area planted to wheat. In response to an excess of global supply over utilization since 1983/84, international prices for rice declined each year until mid-1987 when the late arrival of the monsoon in Southeast Asia caused heavy crop losses in India and Thailand. Prices then rose by 25 percent between the second and fourth quarters of 1987. In Argentina, the declining profitability of rice production has resulted in land being shifted gradually to other uses. In 1987, however, output was severely affected by heavy rainfall and flooding at the harvest, and the volume of rice exports fell by 70 percent. Moreover, most shipments were made before the turnaround in prices in the second half of the year, and the average unit value declined by 12 percent. As a result, shortfall year earnings were 76 percent below average earnings in 1985/86. International prices are expected to rise further in 1988 and to be 5 percent higher than in 1987, year-on-year. This, in turn, should induce some increase in the area planted to rice in 1988, and assuming normal weather, export volume is projected to rise by 47 percent and to stabilize in 1989. Average earnings in 1988/89 are expected to be 57 percent higher than in 1987, and a shortfall of SDR 8.0 million is estimated for rice.

b. Oilseeds and oilseed products

Oilseeds and oilseed products, as a group, accounted for 44 percent of agricultural export earnings in the shortfall year. These commodities replaced cereals as the main agricultural export sector in 1986 and accounted

for more than twice the value of cereal exports in the shortfall year. A shortfall of SDR 416.0 million, or 31 percent of the overall shortfall, is calculated for the group. Shortfalls are calculated for all commodities in the group, with large shortfalls for soybeans (SDR 173.6 million), sunflowerseed oil and seeds (SDR 107.7 million), and soybean oil and meal (SDR 91.0 million). Smaller shortfalls are calculated for linseed oil and meal (SDR 11.8 million), and peanuts (SDR 2.2 million).

Argentina is a major producer and exporter of oilseeds, especially soybeans and sunflowerseeds and their respective derivatives. 1/ Oilseed production has expanded rapidly since the 1970s, reflecting increased area under cultivation and substantial improvements in average crop yields. This has been accompanied by sharp increases in the production and exports of oilseed products, partly stimulated since mid-1982 by differential export taxes favoring exports of oilseed products over seeds. However, these taxes have been lowered recently in response to weaker world prices for oilseeds and oilseed products and are expected to be reduced further during 1988. 2/ Crushing capacity has expanded rapidly to over 38 thousand tons daily in 1986 3/ and is estimated to have increased further in 1987, albeit more slowly than in recent years.

(1) Soybeans and soybean products

Earnings from soybean exports have declined for three consecutive years. After falling by 31 percent in 1985 and 27 percent in 1986, soybean exports are estimated to have declined by a further 54 percent in the shortfall year. The reductions in earnings reflect consecutive declines in both unit value and volume.

After falling by 7 percent to 6.5 million tons in 1984/85 (crop years ended September), soybean production increased to 7.1 million tons in 1985/86 and is estimated to have remained at about that level in 1986/87. Despite these record levels of production, the volume of soybean exports declined by 17 percent between 1984 and 1986 or from 3.1 million tons to 2.6 million tons, as a result of the diversion of an increasing proportion

1/ In 1986/87 (October-September), Argentina was the fourth largest producer of soybeans, after the United States, Brazil, and China, the third largest exporter of soybeans and soybean oil, and the fourth largest exporter of soybean meal. In the same year, Argentina also was the second largest producer of sunflowerseeds, after the U.S.S.R., and the world's largest exporter of sunflowerseed oil, accounting for nearly 39 percent of world trade.

2/ Between March and December 1986 the export tax on soybeans was reduced from 32.5 percent to 15 percent and the taxes on soybean oil and meal, which are levied at the same rate, were reduced from 19 percent to 3 percent. Effective April 1, 1988, the export tax on soybeans is expected to be lowered to 11 percent.

3/ Assuming a crushing year of 320 days, crushing capacity reportedly has been estimated at 12.2 million tons.

of soybeans to domestic crushing. 1/ Unit values for soybeans declined by 27 percent in 1985 and 17 percent in 1986, reflecting the decline in world market prices. Export receipts from soybean products (soybean oil and meal) fell by 10 percent in 1985 but recovered by 4 percent to SDR 678 million in 1986. The volume of both oil and meal exports increased in both years. However, the individual unit values for soybean oil and meal respectively averaged 42 percent and 16 percent lower in 1985-86 than in 1984. World market prices for vegetable oils declined sharply from the record levels recorded in 1984 as a result of the strong recovery of world production and the rise in accumulated stocks to unprecedented levels. Between 1984 and 1986, the world market price for soybean oil, in terms of dollars, declined from an average annual level of \$725 a ton to \$342 a ton, the lowest level since 1973. The decline in world market prices for soybean meal is attributable to weak demand as a result of increased use of alternative feeds.

In the shortfall year, earnings from soybean exports are estimated to have fallen by 54 percent, reflecting a 49 percent decline in volume to 1.3 million tons and a 10 percent decline in the average unit value. 2/ The decline in volume, despite nearly record production of 7.0 million tons, reflects to a large extent an estimated further increase in the proportion of soybeans diverted to domestic crushing. The authorities estimate the volume crushed at 5.0 million tons (72 percent of production), compared to 4.5 million tons in the previous year. After taking into consideration the estimated export volume of 1.3 million tons and small increases in stocks and seed requirements, there is unidentified use of soybeans of over 0.4 million tons. 3/ Rising domestic beef prices in 1987 have probably encouraged increased consumption and production of poultry and hogs, and increased use of balanced concentrate rations. Increased crushing is reflected in a 2 percent rise in the volume of soybean oil exports 4/ but the volume of meal exports is estimated to have remained unchanged at the previous year's level. The decline in the combined value of soybean product exports in the shortfall year entirely reflects lower earnings from soybean oil as a result of lower world market prices. Partly reflecting an expected substantial increase in the demand for vegetable oil imports by India because of the country's drought-reduced groundnut crop, soybean oil prices rose sharply during the fourth quarter of 1987. However, for the year as a whole, world market prices in terms of SDRs were 11 percent lower than in 1986.

1/ In 1985/86, 63 percent of soybean production was crushed, compared to 56 percent in 1984/85 and 49 percent in 1983/84.

2/ World market prices for soybeans increased by about 4 percent in terms of U.S. dollars in 1987, but declined by over 6 percent in terms of SDRs.

3/ The authorities have suggested that the soybean crush may be underestimated due to on-farm crushing by poultry and hog farmers in order to prepare balanced feed.

4/ The small increase in the volume of soybean oil exports may be attributable to increased domestic consumption because of the smaller sunflowerseed crop.

In the two post-shortfall years, earnings from soybean exports are projected to average SDR 378 million annually, nearly twice as high as in the shortfall year. Assuming average yields, production is projected to rise to 8.7 million tons in 1987/88 and 8.8 million tons in 1988/89, as a result of the expansion of soybean plantings from 3.7 million hectares in 1986/87 to an estimated 4.2 million hectares in 1987/88 and a projected 4.3 million hectares in 1988/89. The expanded plantings would to some extent displace certain cereals and other oilseeds because of poor returns to producers of these crops. Allowing for 71 percent of projected annual production to be crushed, the volume of soybean exports in the two post-shortfall years is projected to average 2.3 million tons per year, about 77 percent higher than in the shortfall year. The average volume of soybean oil exports is projected to increase by 40 percent, while the average volume of soybean meal exports is projected to increase by 37 percent. Unit values for soybean oil exports are expected to be 13 percent higher, on average, than in the shortfall year, while unit values for soybean meal are expected on average to be 4 percent lower. On the basis of these movements, the combined value of soybean and soybean product exports in the two post-shortfall years is projected to be 51 percent higher on average than in the shortfall year and about 12 percent higher than the average level in the two preshortfall years.

(2) Peanuts

Export earnings from peanuts, after increasing by 19 percent and 14 percent in 1985 and 1986, respectively, declined by 24 percent in the shortfall year. The rise in earnings in the two preshortfall years is entirely attributable to higher volume, as the area planted to peanuts, especially confectionary nuts, expanded in that period, while unit values, in terms of SDRs, declined in both years. The decline in earnings in the shortfall year reflects a 20 percent drop in unit value, in line with the movement of world market prices and a 6 percent decline in volume; nevertheless, volume was about 2 percent above the average level in the preshortfall period.

Earnings from peanut exports in the post-shortfall period are expected to average about 7 percent below the shortfall year. Export unit values and volumes are projected to average 1 percent and 6 percent lower, respectively, than in the shortfall year.

(3) Sunflowerseed and oil

After declining by 32 percent in 1986, export earnings from sunflowerseed and oil fell by an additional 39 percent in the shortfall year. The 1986 outcome was entirely attributable to a 41 percent drop in unit value; volume rose by 17 percent reflecting a 21 percent increase in production to a record level of 4.1 million tons, as a result of increased area under cultivation.

Export earnings from sunflowerseed oil fell by 41 percent in the shortfall year. This is attributable to a 14 percent decline in unit value, reflecting lower world market prices and a 32 percent decline in volume. The decline in volume reflects reduced sunflowerseed production due mainly to lower area planted, but also to reduced yields. The area planted to sunflowerseed declined by 40 percent in 1986/87 as land was switched from sunflowerseed to soybean production because of substantially lower returns. The average yield declined by 5 percent as sunflowerseed plantings were delayed because of lack of adequate soil moisture, and germination and growth were subsequently hindered by very dry or extremely wet weather. Prior to harvesting a major share of the Pampas crop, four days of heavy rainfall followed by several days of dry weather caused severe crop losses. Severe flooding also caused crop losses in western and northwestern Buenos Aires province, a large producing area.

In the post-shortfall period, earnings from sunflowerseed oil are projected to average SDR 231 million, 37 percent higher than in the shortfall year. Export unit value is projected to average 13 percent higher than in the shortfall year, while volume is expected to increase by 18 percent in 1988 and 6 percent in 1989. This reflects higher levels of production as a result of increased area under sunflowerseed cultivation. Producers are switching from sorghum production, with a lower rate of return than sunflowerseeds. Most of the sorghum produced in the northern Pampas is grown on marginal land which is not suitable for soybean production, and sunflowerseeds are considered the next best alternative. Sunflowerseed production is expected to increase from 2.2 million tons in 1986/87 to an average of 2.9 million tons annually in 1987/88-1988/89.

Only a small share of sunflowerseed production is exported as seed. In the shortfall year, earnings from sunflowerseed exports represented 30 percent of the combined earnings from sunflowerseed and sunflowerseed oil. After increasing by 60 percent in 1986, earnings from exports of sunflowerseed declined by 33 percent in the shortfall year to SDR 72 million. The reduction is entirely attributable to a 34 percent decline in volume, as unit values increased by only 2 percent in terms of SDRs. In the post-shortfall period, earnings are projected to average about 6 percent higher than in the shortfall year, as higher export volumes are expected to more than offset a slight decline in average unit value.

(4) Linseed oil and meal

Linseed oil and meal exports together represent only about 1 percent of total export earnings. The combined value of these exports declined by 22 percent in 1985, 35 percent in 1986, and an estimated 13 percent in the shortfall year.

In the shortfall year, all of the decline in combined earnings from these products is attributable to linseed oil. Inadequate domestic prices caused Argentine farmers to reduce area planted to flaxseed in 1987, but improved yields nevertheless caused production of flaxseed and

its derivative products, linseed oil and meal, to increase. The volume of linseed oil exports rose by 37 percent, but earnings from linseed oil declined by 29 percent owing to a 48 percent decline in unit value resulting from a sharp decline in world market prices. ^{1/} In the post-shortfall period, earnings from linseed oil exports are expected to average 22 percent higher than in the shortfall year, as volume and unit value are expected to average 10 percent and 12 percent higher, respectively.

Export receipts from linseed meal, after declining by 11 percent in 1986, increased by 4 percent in the shortfall year, reflecting a 28 percent increase in volume, as unit value declined by 19 percent. On average, the value of linseed meal exports in the post-shortfall period is projected to be about 10 percent lower than in the shortfall year, reflecting projected declines in both unit value and volume.

c. Beef and beef products

Fresh beef is exported mainly to the EC, Israel, and Brazil because North American markets are closed to countries, including Argentina, which are not free of foot and mouth disease. Processed beef is exported to a large number of countries. In carcass weight equivalent, processed beef has a larger share of total exports, but fresh beef has a larger value share, in large part reflecting the export of prime beef to the EC under quota.

The cattle cycle entered the liquidation phase in 1984 because declining international prices caused by competition from the EC in other Latin American, Middle Eastern, and African countries and price controls in the domestic market lowered producer returns. Although the volume of exports rose by 8 percent in 1985 (reflecting higher shipments of processed products) and by a further 7 percent in 1986 (reflecting an increase in the Hilton quota in the EC), these increases were insufficient to absorb the high rate of slaughter, and apparent domestic consumption increased from 76 kg per head in 1984 to 82 kg per head in both 1985 and 1986. Although the number of cattle slaughtered fell by 5 percent in 1987, lower domestic consumption enabled the volume of beef exports to increase by 4 percent. Higher processed product exports more than offset a 14 percent decline in fresh beef exports. This shift in composition reflected the strong performance of small- and medium-sized export firms under the special incentive program for exports (PEEX). International prices for beef firmed considerably in 1987 because of the start of herd rebuilding in the United States and lower availability in the EC following the depletion of the intervention stockpile in 1986. Argentina's export earnings rose by 17 percent in 1987 to a level 20 percent higher than average earnings in 1985-86.

^{1/} In 1987, world market prices for linseed oil declined by 25 percent, in terms of U.S. dollars, and 32 percent in terms of SDRs, as world production of flaxseed and linseed oil increased by 15 percent and 14 percent, respectively.

Although the rate of slaughter is expected to decline slightly in the two post-shortfall years as the cattle cycle enters the rebuilding phase, a modest rise in export volume (averaging 6 percent a year) will be made possible by lower domestic consumption. Price controls on cattle were lifted in February 1988 and higher domestic prices are expected to restrain consumption. International prices are expected to rise modestly in U.S. dollar terms in 1988-89 as herd rebuilding in the major producing countries continues, but are expected to show little change in terms of SDRs. On average, earnings in 1988-89 are projected to be 8 percent higher than in 1987. Because of the deceleration in the rate of growth of earnings projected for the post-shortfall period compared with that in the shortfall year, an excess of SDR 15.5 million is estimated for beef and beef product exports.

d. Other agricultural products

Earnings from exports of other agricultural products, consisting of vegetables and fruit, wool, marine products, and minor agricultural products, accounted for 12 percent of total exports in the shortfall year. Two successive years of weather related reductions in export volume and adverse movements in world market prices caused earnings from this group of commodities to decline by 17 percent to SDR 568 million in 1986 and to remain at virtually the same level in the shortfall year 1987. A return to normal weather conditions in the two post-shortfall years and a modest improvement in world market prices are expected to contribute to a recovery in earnings to pre-1986 levels. A shortfall of SDR 66.9 million, calculated for this group, is due to both volume and price factors.

(1) Vegetables and fruit

Earnings from exports of vegetables and fruit declined by 10 percent in the shortfall year wholly because of a 56 percent fall in earnings from exports of beans; earnings from exports of fruit increased by 26 percent in the shortfall year. The volume of bean exports declined by 43 percent in the shortfall year because of a decline in bean production due to heavy rainfall and severe flooding. The unit value of bean exports fell by 23 percent due to weather-related quality problems. As production and exports recover with a return to normal weather conditions in the two post-shortfall years, earnings from bean exports are expected to recover at an annual average rate of 9 percent. A shortfall of SDR 16.1 million is calculated for bean exports.

After declining by 18 percent in 1986 due to the incidence of late frosts and unseasonal rains, earnings from fruit exports increased by 26 percent in the shortfall year because a 21 percent decline in export unit value was more than outweighed by a 61 percent recovery in export volume. All the main categories of fruit, namely apples, pears, and citrus fruit shared in the recovery in export volume. Earnings are projected to increase at an annual rate of 2 percent in the post-shortfall period on account of a continuing increase in export volume. An excess of SDR 5.3 million is calculated for fruit exports.

(2) Wool

Argentina is a relatively small producer of mainly fine quality merino and fine crossbred wools. Earnings from wool, which account for about 2 percent of total exports, declined by 1 percent in the shortfall year. Export volume declined by 8 percent because of a lower wool production resulting from a fall in forage availability due to climatic factors. World market prices for fine wool increased sharply in the shortfall year because of exceptionally buoyant demand from buyers in Japan, China, and Eastern Europe. Argentina's wool export unit value, however, increased by only 6 percent in the shortfall year because the quality of the wool clip was adversely affected by poor weather conditions. A return to normal weather conditions is expected to lead to a recovery in export volume in the two post-shortfall years. Export unit values on the other hand are expected to decline in the two post-shortfall years because global consumption is likely to be curtailed by the high prices prevailing in 1987. Based on these movements, a shortfall of SDR 2.9 million is calculated for wool exports.

(3) Marine products

Marine products, consisting mainly of fish and shrimp, accounted for 4 percent of total export value in the shortfall year. Earnings from marine product exports increased by 29 percent in 1986 and by a further 12 percent in the shortfall year because of an increase in Argentina's catch, resulting from controls on foreign fishing fleets operating off the coast of Argentina. In addition to the EC, the United States and Japan, which have traditionally been the largest outlets for marine product exports, Argentina has recently concluded fishing agreements with the U.S.S.R. and Bulgaria. These agreements have already resulted in substantial increases in the volume of lower valued fish exported to these countries. As a result of a continuing increase in exports, especially to Eastern Europe, the volume of exports in the two post-shortfall years is projected to continue to increase at an annual rate of 19 percent in the two post-shortfall years. Export unit values are projected to increase at an annual rate of 10 percent over the same period. On the basis of these movements, a shortfall of SDR 13.4 million is calculated for marine product exports.

(4) Minor agricultural products

This group of products consisting of sugar, tobacco, tea, and cotton accounted for only 2 percent of total exports in the shortfall year. Earnings in the shortfall year from the group as a whole were virtually unchanged from the previous year with lower earnings from sugar and tea largely offset by sharply higher earnings from cotton and to a lesser extent from tobacco. The volume of sugar exports, which has been declining for a number of years because of low world market prices, declined further in the shortfall year largely because of a reduction in Argentina's quota in the United States sugar market. Similarly, the volume of tea exports which has also been declining for a number of

years because of low international prices and reduced profitability, declined further in the shortfall year as production continued to fall. Although cotton production, which had been decimated by adverse weather in April 1986, was again adversely affected by rainfall in April 1987, a recovery in production to levels substantially lower than in 1985 caused the volume of cotton exports to double in the shortfall year. Movements in export unit values of most of these commodities were generally in line with movements in world market prices. In the post-shortfall period, earnings from this group of commodities are projected to increase at an annual rate of 5 percent as weather conditions return to normal and export volumes recover in conjunction with a modest projected recovery in prices. A shortfall of SDR 21.5 million calculated for this group of commodities is due largely to volume factors.

2. Petroleum products

Argentina is close to self-sufficiency in petroleum. About 90 percent of output is consumed domestically and the remainder is exported as refined products. The petroleum fields are relatively old, however, and about one third require the application of secondary and tertiary recovery methods to maintain present production levels (injection of water or gas to maintain wellhead pressure). Argentina also produces natural gas which accounts for 26 percent of total primary energy demand (compared with 49 percent for petroleum). Argentina's policy has been to increase the substitution of natural gas for petroleum in power generation and large industrial applications, thus freeing petroleum for export; the main impediment to this policy has been a lack of infrastructure to move gas from remote fields to major consumers in coastal regions.

Exports of petroleum products, which include residual fuel oil, gas oil (including diesel), and hydrocarbons (mainly ethylene), are estimated to account for about 2 percent of total exports in the shortfall year. Earnings for petroleum products fell by 76 percent to SDR 127 million in 1986 and are estimated to decline by another 35 percent to SDR 82 million in the shortfall year. The main causes of the decline in 1986 were a fall in production of crude petroleum, due to the depletion of older fields, and a low rate of application of secondary recovery methods, and a sharp decline in unit value associated with the collapse in international prices for crude petroleum and products. In the shortfall year the decline in earnings was mainly attributable to a sharp increase in domestic consumption of petroleum products caused by a temporary shortage of natural gas during the peak heating season. Earnings are expected to recover in the post-shortfall period by about 50 percent to an average level of SDR 123 million, due entirely to a recovery in export volumes. The completion of maintenance on existing natural gas pipelines and the commissioning of a new pipeline by mid-1988 is expected to result in an increase in the availability of natural gas for domestic consumption and permit the greater release of petroleum products for export. Based on these movements, a shortfall of SDR 70.4 million is estimated for petroleum products.

a. Fuel oil

Fuel oil accounts for about one fourth of Argentina's total production of refined products and about one half of its product exports. Fuel oil is consumed domestically in electric power plants (including hydroelectric plants during peak periods) and in large industries, both of which possess the capability of switching between fuel oil and natural gas. Substitution of gas for oil is expected to accelerate following completion of expansion of the northern gas pipeline (to 476 from 300 million cubic feet per day) in June 1988. At the same time completion of upgrades to the Plata and Lujan de Cuyo refineries is expected to facilitate the reprocessing of about 4 million tons of fuel oil into lighter products for domestic use and export.

The volume of fuel oil exports fell by almost half in 1987 to 0.4 million tons, due principally to higher domestic consumption that resulted from a shortage of natural gas. Consumption of all petroleum products rose by 22 percent to 13.3 million tons for the period January-September 1987, compared with the same period the year before, while gas consumption fell by 10 percent to 10.0 million tons of oil equivalent. The immediate cause of the gas shortage was maintenance and repair difficulties during the year. A second factor affecting export volumes of fuel oil was the general decline in crude oil production which resulted from the depletion of older fields and a low rate of application of secondary recovery methods. 1/ Production fell by 6 percent to 22.0 million tons in 1986, and by about 3 percent to 21.2 million tons in the shortfall year. Increased domestic consumption and lower crude production led to the importation of refined products for the first time since 1985, of an estimated 1.6 million tons, during the peak heating months of April-October 1987. 2/

Earnings from fuel oil are expected to recover in the post-shortfall period, by an average annual rate of 13 percent, due entirely to a recovery in export volumes. The conversion of some industries to natural gas following the addition of more pipeline capacity is expected to release significant amounts of fuel by 1989; however exports of fuel oil are expected to fall to 0.4 million tons, since almost all fuel oil production will be used in the enhanced refineries to produce lighter grade products. Export unit values, which have moved in line with international prices for fuel oil, are expected to remain flat at about US\$173 a ton in the post-shortfall period, but to decline by 3 percent in SDR terms. A shortfall of SDR 26.9 million is estimated for fuel oil.

1/ While an estimated 35 percent of the production from Argentina's existing fields could benefit from the application of secondary and tertiary recovery methods, only about 12 percent were being worked on that basis.

2/ To satisfy contract obligations with Paraguay, exports of fuel oil took place in the off-peak months, the first and fourth quarters of 1987.

b. Gas oil

Gas oil is also a substitute for natural gas in small-scale electricity generation. As with fuel oil, export volumes of gas oil fell sharply in the shortfall year by 57 percent to 76,000 tons, due principally to lower gas availability which led to higher domestic consumption and imports of gas oil. Volumes are expected to recover to an average level of 330,000 tons in 1988-89 with a return to more normal consumption and some increased production of gas oil from fuel oil. The implementation of contract incentives in mid-1987 to promote more secondary recovery by foreign companies, and the development of the Hidra field which will add 1.3 million tons of crude per year by 1990 or sooner, are also expected to result in some increased production of crude oil in general, and gas oil in particular. A shortfall of SDR 26.0 million is estimated for gas oil.

c. Hydrocarbons

Hydrocarbons are chemicals (ethylene, benzene, toluene, and xylene) that are made from petroleum products and natural gas. The value of exports for this category declined by 7 percent to SDR 41.8 million in 1987, on account of sharply lower volumes (which declined by 27 percent) that were mitigated somewhat by higher unit values (which rose by 40 percent in U.S. dollar terms). Less gas availability and higher domestic consumption of petroleum products meant that less input was available for hydrocarbon production. A worldwide contraction in capacity and improved demand have resulted in an improved outlook for hydrocarbon prices, which are expected to grow at an annual rate of 4 percent in U.S. dollar terms. Export volumes, however, are not expected to recover to their preshortfall period levels, since hydrocarbons will be increasingly used to produce plastic products (included in "other" exports). A shortfall of SDR 10.3 million is estimated for hydrocarbons.

3. Manufactures

Manufactured products for which volume data are available accounted for 12 percent of total export earnings in the shortfall year. A small shortfall of SDR 11.9 million is estimated for this group.

The volume of manufactured exports as a group rose by about 1 percent in the shortfall year, as large increases in export volumes of aluminum ingots, steel products, and synthetic rubber were mostly offset by declines in those of tanned leather and tannin. Increased capacity utilization in 1987 permitted exports of aluminum ingots to rise by 8 percent and those of synthetic rubber by 9 percent. The export volume of steel pipes and plates increased by 19 percent as domestic production of steel products rose sharply as a result of significant additions to capacity realized in 1986. In contrast, the export volume of tanned leather fell by 9 percent in the shortfall year because of the shortage of hides on account of a lower rate of cattle slaughter. Finally, the volume of tannin fell largely due to lower exports to Brazil.

The overall index of unit values of manufactured exports rose by 2 percent in the shortfall year reflecting the combined effect of strong recoveries in the prices of aluminum ingots and tanned leather and declines in the prices of tannin and synthetic rubber. The unit value for steel products as a group was unchanged over the previous year basically reflecting sluggish economic growth in industrial countries, and still remained considerably below the average for the two preshortfall years. A 9 percent increase in the prices of aluminum ingots reflected an upsurge in international prices of aluminum in the face of strong world demand and diminishing stocks, while higher prices of hides raised the unit value of tanned leather products. A 17 percent decline in the prices of synthetic rubber reflected in part a shift in world demand from synthetic to natural rubber for manufacture of hygiene products. Prices of tannin fell in the shortfall year as a large surplus of tannin persisted in the world market. With both volume and unit values increasing at modest rates, the value of manufactured exports rose by 3 percent in the shortfall year and remained below the average earnings in the two preshortfall years.

Earnings from manufactured exports are projected to fall by 1 percent in 1988 due mainly to sharp declines in exports of aluminum ingots and synthetic rubber, but to recover by 10 percent in 1989 aided mainly by strong growth in exports of steel products. Given the limited production capacity of the industry and the anticipated rise in domestic demand, the export volume of aluminum ingots is projected to fall by 56 percent to the lowest level in the 1980s and to stagnate at this level in 1989. The export volume of synthetic rubber is projected to decline by 21 percent in 1988 and by a further 5 percent in the following year due mainly to capacity constraints and rising domestic demand. In contrast, capacity is not expected to be a constraining factor for the other manufacturing industries, in particular steel products, for which the export volume is projected to increase by an annual average rate of 7 percent in the post-shortfall period. Greater availability of raw materials is expected to provide some volume growth to tanned leather, but the prospect of raising the export volume of tannin in the post-shortfall period is not favorable in view of a large surplus prevailing in the world market. The Government will continue to provide during 1988-89 a number of export promotion programs and incentives, including the Special Program for Exports (PEEX) in order to assist the growth of manufactured exports. 1/

Unit values in manufacturing, on average, are projected to rise by one percent in 1988 and by 5 percent in 1989, although for the first post-shortfall year price declines are forecast for tanned leather, tannin,

1/ The PEEX is a scheme whereby small- and medium-sized firms agree with the Government to raise exports by at least US\$2 million a year for five years, or by at least \$10 million at the end of five years. In return, firms receive dollar equivalent subsidies of up to 15 percent of the realized increase in exports. Other incentives to promote non-traditional exports include low-interest export financing, rebates of import duty and indirect taxes, and marketing assistance.

and aluminum ingots. The overall price of steel products is projected to rise in the post-shortfall period, mainly reflecting a change in the composition of steel pipe exports from oil pipelines to higher priced gas pipelines.

4. "Other" exports

"Other" exports, for which only value data are available, accounted for 29 percent of the total value of exports in 1987. A disaggregation of some of the individual products in this category is reported in Table 8; in 1987, the share of manufactures in "other" export earnings was 74 percent, that of agricultural products 24 percent, and that of petroleum products 2 percent.

The largest component of the overall shortfall in "other" products, estimated at SDR 248.2 million, is in agricultural products (SDR 101.0 million). Earnings from other agricultural products declined by 10 percent in 1987 to a level 37 percent below average earnings in 1985-86. The decline in the earnings of cereals (rye, barley, and oats), oilseeds (primarily rapeseed), and vegetables and fruit, reflected supply constraints caused mainly by the heavy rainfall in early 1987. In addition, the supply of dairy products for export was diminished because of low cattle numbers; 1987 was the fourth successive year of herd reduction. By contrast, sheep flock retention, in response to high wool prices, reduced the availability of meat for export. The projected recovery of agricultural earnings at an average annual rate of 15 percent in 1988-89 assumes higher international prices for cereals, oilseeds, sheepmeat, and dairy products, and increased supplies associated with a return to normal weather conditions.

The shortfall for other petroleum products (naphtha and solvents) is estimated at SDR 41.4 million. As with the decline in earnings of the major petroleum products discussed above, the 34 percent reduction in earnings in 1987 reflects increased domestic consumption of petroleum products which was caused by a shortage of natural gas. Earnings are projected to more than double in 1988 and to rise by a further 11 percent in 1989. The acceleration of growth in the post-shortfall period will be made possible by greater substitution of natural gas in fuel use, and by the scheduled completion of refinery upgrading by mid-1988 which will allow for the cracking of fuel oil to produce more light and middle distillate products.

The shortfall for other manufactured exports is estimated at SDR 88.6 million, consisting mainly of SDR 19.2 million for electronic products, SDR 16.5 million for ships, and SDR 11.9 million for chemical products. In the shortfall year, earnings from electronic exports fell by 28 percent partly as a result of a delay in removal of import tariffs by Brazil under the Accord signed in 1986, but such exports are projected to increase at an annual average rate of 14 percent in the post-shortfall period under agreements already signed under the Special Program for Exports. Earnings from exports of chemical products, which include plastics, pharmaceutical drugs and photographic materials, grew by 17 per-

Table 8. Argentina: Disaggregation of "Other" Exports, 1985-1989

	Years Ending December					Shortfall
	1985	1986	1987 <u>1/</u>	1988 <u>2/</u>	1989 <u>2/</u>	Geometric
(In millions of SDRs)						
Total "other" exports	<u>1,941</u>	<u>1,559</u>	<u>1,405</u>	<u>1,628</u>	<u>1,784</u>	<u>248.2</u>
Agricultural products	<u>583</u>	<u>472</u>	<u>333</u>	<u>400</u>	<u>420</u>	<u>101.0</u>
Cereals	<u>35</u>	<u>15</u>	<u>12</u>	<u>34</u>	<u>27</u>	<u>10.5</u>
Oilseeds and products	205	160	70	81	83	39.1
Seeds and beans	(102)	(81)	(8)	(14)	(15)	(18.8)
Oils	(84)	(50)	(41)	(51)	(60)	(14.3)
Oilseed meals	(19)	(29)	(21)	(16)	(8)	(-4.1)
Fresh fruits	9	12	15	20	21	-0.5
Fresh vegetables	17	22	17	16	20	1.4
Processed fruits and vegetables	70	38	46	63	82	11.5
Meat	63	61	38	45	50	12.1
Dairy products	16	19	14	15	20	2.4
Other agricultural products <u>3/</u>	169	146	120	126	118	14.5
Petroleum products	<u>213</u>	<u>57</u>	<u>38</u>	<u>78</u>	<u>86</u>	<u>41.4</u>
Manufactures	<u>1,145</u>	<u>1,029</u>	<u>1,035</u>	<u>1,149</u>	<u>1,278</u>	<u>88.6</u>
Leather products	<u>13</u>	<u>14</u>	<u>17</u>	<u>19</u>	<u>22</u>	<u>-0.6</u>
Electronic products	114	89	64	74	83	19.2
Aluminum products	0	24	30	96	97	-15.4
Steel wire	58	34	25	28	32	9.0
Other metal products	161	123	70	46	50	9.6
Chemical products <u>4/</u>	244	213	249	279	338	11.9
Machinery	149	146	151	153	165	2.0
Ships	137	75	15	14	14	16.5
Transport equipment	95	103	121	135	151	-1.2
Textiles	99	97	131	149	147	-8.6
Other manufactures	75	110	161	155	178	-31.5
(Percentage changes)						
Total "other" products		<u>-19.7</u>	<u>-9.9</u>	<u>15.9</u>	<u>9.6</u>	
Agricultural products		-19.0	-29.4	20.1	5.1	
Petroleum products		-73.2	-34.1	107.1	10.5	
Manufactures		-10.1	0.5	11.0	11.2	

1/ Data for the last six months (July-December) are estimated.

2/ Projected.

3/ Including live animals, honey, medicinal plants and flowers, bones, internal organs and skins, dried fruit, flours, herbal teas, spices, canned fish, seafood and fowl, and confectionary.

4/ Including plastics, pharmaceutical drugs, and photographic materials.

cent in 1987, aided in part by an increase in trade with Brazil, and such earnings are projected to increase at about the same rate in the post-shortfall period. Ships are normally exported with exporters receiving preferential export credits from the authorities, and as such financing became tighter, ship exports fell sharply in 1987. In the two post-shortfall years, ship exports are expected to stagnate at the current low level as exporters would be unable to receive additional export credits at preferential rates.

ARGENTINA - Fund Relations
(As of February 26, 1988)

I. Membership Status

- (a) Date of Membership: September 1956
- (b) Status: Article VIII

A. Financial Relations

II. General Department (General Resources Account)

(a)	Quota: SDR 1,113.0 million	Millions of SDRs	Percent of Quota
(b)	Total Fund holdings of australes	3,726.6	334.8
(c)	Fund credit	2,613.6	234.8
	Of which: credit tranches (ordinary resources)	775.7	69.7
	enlarged access resources	1,044.2	93.8
	compensatory financing facility	793.8	71.3
(d)	Reserve tranche position	--	--
(e)	Current Operational Budget: Not applicable		
(f)	Lending to the Fund: Not applicable		

III. Recent Stand-By or Extended Arrangements and Special Facilities

(a) Stand-by arrangements

Type of Arrangement	Amount (SDR million)	Duration	Amount Drawn (SDR million)	Status
SBA	1,113.0	July 23, 1987- Sept. 30, 1988	451.0	In effect
SBA	1,419.0	Dec. 28, 1984- June 30, 1986	1,182.5	Expired
SBA	1,500.0	Jan. 24, 1983- April 24, 1984	600.5	Canceled, Jan. 23, 1984
SBA	159.5	Sept. 16, 1977- Sept. 15, 1978	--	Expired

(b) Special Facilities: CFF

<u>Year</u> <u>Approved</u>	<u>Amount</u> <u>(SDR million)</u>
1987	518.8
1984	275.0
1983	520.1
1975	220.0

IV. SDR Department

- (a) Net cumulative allocation: SDR 318.37 million
- (b) Holdings: SDR 903 or 0.0 percent of net cumulative allocation (as of January 31, 1988)
- (c) Current Designation Plan: not applicable

V. Financial Obligations Due to the Fund

	<u>Overdue</u> <u>Financial</u> <u>Obligations</u>	<u>Principal and Interest Due</u> <u>(SDR million)</u>			
		<u>Feb.27-</u> <u>Dec. 1988</u>	<u>1989</u>	<u>1990</u>	<u>1991</u>
Repurchases	--	279.3	558.2	513.6	601.9
Charges and Interest including SDR and TF (provisional)	--	121.6	166.5	131.1	92.7
Total	--	400.9	724.7	644.7	694.6

B. Nonfinancial Relations

VI. Exchange Rate

On June 14, 1985, the austral (symbol: \$) replaced the peso argentino at a rate of one austral per 1,000 pesos argentinos. On October 14, 1987, Argentina introduced a freely fluctuating financial exchange market, which in effect replaces the extra-official parallel exchange market and in which all transactions not required to be channeled through the official exchange market may occur. The transactions to be conducted at the fixed official exchange rate include all trade-related capital transactions, all public sector transactions, all disbursements from international organizations, the amortization and refinancing of private sector loans disbursed prior to October 9, 1987, and the servicing of debt contracted through the official market. The official exchange rate was fixed at \$ 3.49 per U.S. dollar

(buying) and \$ 3.51 per U.S. dollar (selling) from October 14, 1987 to December 30, 1987; since then, the rate has been subject to frequent, small adjustments. On February 23, 1988, the official exchange rate was \$ 4.44 per U.S. dollar (buying) and \$ 4.47 per U.S. dollar (selling), while the free exchange rate was \$ 6.07 per U.S. dollar (buying) and \$ 6.12 per U.S. dollar (selling).

VII. Last Article IV Consultation

The 1987 Article IV consultation was concluded on July 23, 1987 (EBM/87/107).

VIII. Technical Assistance

A Fund panel expert has been assigned to Argentina by the Fiscal Affairs Department since June 1986 to implement the recommendations of a report prepared by the Fiscal Affairs Department on ways to improve the reporting of data in the Treasury and other parts of the public sector. The assignment was initially for a period of one year, but has been extended for an additional year. In 1987, a mission from the Fiscal Affairs Department visited Argentina to review the system for publishing periodic information on the government finances.