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AGENDA

EBS/87/17
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CONFIDENTIAL

July 7, 1987

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 which updates the shortfall calculations contained in EBS/87/17 (1/29/87) and recommends an augmented purchase by Argentina equivalent to SDR 518.765 million. A draft decision appears on page 8.

This subject has been added to the agenda of an Executive Board meeting scheduled for Friday, July 10, 1987.

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

Att: (1)

INTERNATIONAL MONETARY FUND

ARGENTINA

Use of Fund Resources--Compensatory Financing Facility

Prepared by the Research Department

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

Approved by R.R. Rhomberg

July 7, 1987

EBS/87/17, dated January 29, 1987, contained an analysis of an anticipated CF request by Argentina for a purchase of SDR 388.7 million (35 percent of quota) with respect to a shortfall of SDR 731.6 million in merchandise exports estimated for the year ended September 1986. The request was made under the early drawing procedure, with data estimated by the staff in cooperation with the authorities for the second half of the shortfall year. The request was approved in principle by the Executive Board at EBM/87/29 on February 18, 1987, and the decision was amended at EBM/87/33 on February 26, 1987. The amended decision set forth in EBS/87/17, Supplement 2 (2/25/87) provides, inter alia, that the approval of the CF request shall become effective not later than July 15, 1987 provided that Argentina continues to cooperate with the Fund.

Since that time, additional export data have become available and Argentina has effected a repurchase in respect of SDR 65.0 million in April and is in the process of effecting a further repurchase of a similar amount in respect of outstanding purchases under the CFF. With the latter repurchase, maximum access available to Argentina would be raised from SDR 388.7 million to SDR 518.8 million, which is the amount of the proposed purchase. This supplement examines the case for Argentina's request for a purchase of SDR 518.8 million on the basis of the most recent information concerning actual and projected exports. The proposed purchase is equivalent to 47 percent of quota and, if approved, it would raise outstanding purchases under the CFF from 36 percent to 83 percent of quota, and the Fund's holdings of the member's currency from 273.3 percent of quota to 319.9 percent of quota. A waiver of the limitation in Article V, Section 3(b)(iii) is required and is being proposed.

1. Estimation of the export shortfall

The latest actual data on merchandise exports are available through September 1986. The staff in cooperation with the authorities has estimated exports for the last three months of 1986, so that the shortfall year ended December 1986 is within the standard period of about six months

between the end of the shortfall year and time of request. 1/ The calculation of the shortfall is based on partly estimated data in accordance with paragraph 7 of Decision No. 6224-(79/135). 2/

After rising by 8 percent in 1984 and 5 percent in 1985, export earnings fell by 29 percent in the shortfall year. Earnings are expected to fall further in the first post-shortfall year (by 7 percent) but to recover in 1988, rising by 21 percent. On the basis of these movements, a shortfall for the 12 months ended December 1986 is estimated at SDR 865.4 million (Table 1). This compares with a shortfall for the year ended September 1986 estimated at SDR 731.6 million as reported in EBS/87/17 (1/29/87), using estimated data from April-September 1986. 3/ The estimated shortfall is larger on a December year basis because the rate of decline (of 20 percent) in earnings in the shortfall year, when measured from the average of the two preshortfall years, was greater than the corresponding rate of decline (of 15 percent) on a September year basis using estimated data for April-September 1986.

Table 1. Argentina: Estimation of the Export Shortfall, 1984-88

(In millions of SDRs)

	Years Ending December				
	1984	1985	1986 <u>2/</u>	Projected <u>1/</u>	
				1987	1988
Exports	7,909	8,269	5,838	5,424	6,535
Shortfall			865.4		
Proposed purchase			518.8		

1/ Based on judgmental forecast of earnings given in Table 2.

2/ Data for the last three months (October-December) are estimated.

1/ Under established procedures, there should be a delay of not more than approximately six months between the end of the shortfall year and the date of consideration of the request by the Executive Board. This requirement has been interpreted flexibly in the past, and the staff considers that it is satisfied in this case by a shortfall year ended December 1986.

2/ Exports for the period October-December 1986 are estimated at SDR 400 million per month compared with SDR 515 million per month during the first nine months of the shortfall year and SDR 554 million per month during the period October-December 1985.

3/ The shortfall for the year ended September 1986 on the basis of actual data for April-September and the same projections made at the time is SDR 831.2 million.

Table 2. Argentina: Export Earnings and Shortfalls by Major Commodities, 1981-88

	Years Ending December									Shortfall 1/	
	1981	1982	1983	1984	1985	1986 2/	1987 3/	1988 3/		Geo- metric	Arith- metric
(In millions of SDRs)											
Total exports	7,754	6,906	7,330	7,909	8,269	5,838	5,424	6,535	865.4	957.2	
Agriculture	4,905	4,022	5,177	5,447	5,163	3,547	2,973	3,622	491.8	603.7	
Cereals	(2,407)	(1,681)	(2,740)	(2,165)	(2,233)	(1,069)	(648)	(1,006)	(205.9)	(355.2)	
Oilseeds 4/	(980)	(1,010)	(1,252)	(2,236)	(1,963)	(1,610)	(1,357)	(1,602)	(116.9)	(143.5)	
Beef 4/	(628)	(567)	(451)	(295)	(286)	(286)	(320)	(304)	(11.3)	(11.6)	
Other agriculture	(891)	(764)	(734)	(751)	(682)	(581)	(648)	(711)	(91.0)	(93.5)	
Petroleum products	512	475	310	324	518	108	76	176	80.9	132.1	
Manufactures	673	700	539	613	743	640	673	798	50.1	53.4	
Other products	1,663	1,707	1,304	1,526	1,846	1,543	1,703	1,939	160.3	168.0	
(Percentage changes)											
Total exports		-10.9	6.1	7.9	4.6	-29.4	-7.1	20.5			
Agriculture		-18.0	28.7	5.2	-5.2	-31.3	-16.2	21.8			
Cereals		(-30.2)	(63.0)	(-21.0)	(3.1)	(-52.1)	(-39.4)	(55.3)			
Oilseeds 4/		(3.1)	(24.0)	(78.6)	(-12.2)	(-18.0)	(-15.7)	(18.0)			
Beef 4/		(-9.7)	(-20.5)	(-34.7)	(-3.1)	(0.3)	(11.6)	(-5.0)			
Other agriculture		(-14.2)	(3.9)	(2.3)	(-9.3)	(-14.7)	(11.6)	(9.7)			
Petroleum products		-7.1	-34.9	4.6	59.9	-79.1	-29.9	131.7			
Manufactures		4.0	-23.1	13.7	21.2	-13.8	5.2	18.6			
Other products		2.7	-23.6	17.0	21.0	-16.4	10.3	13.9			

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

2/ Data for the last three months (October-December) are estimated.

3/ Projected.

4/ Includes products of relevant categories.

2. Causes of the shortfall and prospects for export earnings

The causes of the total export shortfall of SDR 865.4 million are mainly the same as reported in the previous paper. The major component of the aggregate shortfall is a shortfall of SDR 491.8 million in agricultural exports, which reflects shortfalls in both volume and unit value (Table 3). The volume of cereals exports in 1986 was 26 percent below its average level in the two preshortfall years. Wheat production in 1986 was severely affected by heavy rainfall in November 1985 in the major growing areas. The volume of rice and sorghum exports also declined in 1986 reflecting a return to normal yields after bumper crops in 1985. The average unit value of cereals exports in the shortfall year was more than one-third lower than in the two preshortfall years. This was due to the sharp decline in the international prices for all major cereals, brought about by the glut of these commodities on world markets.

Other agricultural exports experiencing declining volume in the shortfall year were beef and beef products, which lost market share owing to intensified competition from the EC; fruits and vegetables, tea, and cotton, where output was affected by adverse weather; and sugar, related to a reduction in the United States' sugar import quota. Although the volume of exports of oilseeds and their derivatives rose slightly in 1986, this was more than offset by a fall in unit values for the entire sector of 25 percent. The unit values of wool and tea also declined in the shortfall year in line with the movement of international prices.

A shortfall in petroleum products exports estimated at SDR 80.9 million also reflects shortfalls in both volume and unit values. The volume of exports of fuel oil, gas oil, and hydrocarbons fell by more than two thirds in 1986 due to a restructuring of refinery operations toward the production of lighter fuels, which reduced the availability of fuel oil for export, and an upturn in domestic consumption. The unit values of petroleum product exports as a group fell by 41 percent in 1986 as a result of the sharp decline in international oil prices.

The shortfall in exports of manufactured products estimated at SDR 50.1 million resulted entirely from lower unit values; the unit values of electronic, aluminum and steel products exports fell in response to higher world output and the slow growth of demand. The volume of most manufactures exports continued to rise in 1986 after experiencing rapid growth in 1985. Leather products exports benefited from the higher availability of hides, and electronic and steel products exports were boosted by additions to capacity. Assisting the volume growth of manufactures exports was the improvement of external competitiveness; year-on-year, the real effective exchange rate was virtually unchanged in 1986 after depreciating by 14 percent in 1985.

A shortfall in the residual category of exports--"other" exports--estimated at SDR 160.3 million, reflects shortfalls in respect of the agricultural and petroleum product components that were partly offset by

Table 3. Argentina: Value, Volume, and Unit Value by Major Commodities, 1981-88
(1986=100; In terms of SDRs)

	Value Share in Total Exports In 1986 (In Percent)	Years Ending December								Shortfall in Percent of Level in Shortfall Year
		1981	1982	1983	1984	1985	1986 ^{1/}	1987 ^{2/}	1988 ^{2/}	
Value	<u>71.8</u>	<u>144</u>	<u>123</u>	<u>142</u>	<u>151</u>	<u>152</u>	<u>100</u>	<u>85</u>	<u>106</u>	<u>15.6</u>
Agriculture	60.7	139	115	146	155	147	100	84	103	14.5
Cereals	18.3	225	157	256	202	209	100	60	94	18.9
Oilseeds and oil- seed products	27.5	61	63	78	139	122	100	84	100	7.3
Beef and beef products	4.9	219	198	157	103	100	100	112	106	4.1
Other agriculture	10.0	157	139	128	138	127	100	113	126	20.1
Petroleum products	1.9	470	437	284	296	476	100	70	161	73.8
Manufactures ^{3/}	9.2	108	112	85	97	115	100	96	113	3.9
Volume		<u>98</u>	<u>95</u>	<u>108</u>	<u>102</u>	<u>119</u>	<u>100</u>	<u>99</u>	<u>121</u>	<u>7.8</u>
Agriculture		95	92	112	105	117	100	99	121	8.0
Cereals		130	104	164	124	148	100	79	125	12.6
Oilseeds and oil- seed products		42	49	60	86	92	100	101	112	-2.2
Beef and beef products		194	208	165	100	104	100	116	108	5.4
Other agriculture		128	135	136	121	132	100	124	142	23.0
Petroleum products		263	235	161	149	281	100	69	148	33.7
Manufactures ^{3/}		84	85	72	72	98	100	103	117	-3.2
Unit Value		<u>147</u>	<u>129</u>	<u>131</u>	<u>148</u>	<u>128</u>	<u>100</u>	<u>86</u>	<u>88</u>	<u>7.5</u>
Agriculture		146	125	130	148	126	100	85	85	6.1
Cereals		173	151	156	163	141	100	76	75	5.5
Oilseeds and oil- seed products		145	129	130	162	133	100	83	89	9.7
Beef and beef products		113	95	95	103	96	100	97	98	-1.2
Other agriculture		123	103	94	114	96	100	91	89	-2.4
Petroleum products		179	186	176	199	169	100	101	109	29.9
Manufactures ^{3/}		129	132	118	135	117	100	93	97	7.3

^{1/} Data for the last three months (October-December) are estimated.

^{2/} Projected.

^{3/} Excluding leather products and electronic products; growth of value of manufactures exports in 1987 and 1988 is understated by comparison with Table 3.

an excess in the manufactures component. ^{1/} The causes of the shortfalls in the agricultural and petroleum products components are the same as those noted above for other products, primarily the decline in international commodity prices and weather-related reductions in output.

The pattern of export growth now projected for 1987 and 1988 is significantly different from the projections on a September year basis reported in EBS/87/17 that were made in January 1987. The projected decline in earnings of 7 percent in the first post-shortfall year is larger than the 4 percent decline expected previously. The downward revision in exports reflects the heavy rainfall and severe flooding which occurred in Buenos Aires province--the main cereal and second largest oilseed producing area--at the end of March and early April 1987. ^{2/} As a result, the projected volume of exports of corn, soybeans, and sunflowerseeds in 1987 has been lowered significantly. Exports of fresh, frozen, and chilled beef will also be constrained by livestock losses, and by a recent outbreak of foot-and-mouth disease. Assuming that normal weather conditions return in 1988, a recovery in the output of cereals and oilseeds will enable their export volume to attain about the levels that were projected on a calendar year basis at the time of preparation of EBS/87/17. The volume of exports of processed beef and manufactured goods is expected to grow rapidly in both post-shortfall years under the influence of special export promotion programs and incentives and the maintenance of a competitive exchange rate. These assumptions underpin the projected average annual rate of growth of export earnings in 1987-88 of just over 1 percent, because further declines in the unit values of all major export groups except for petroleum products are expected on average in the two post-shortfall years.

3. Repurchases

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 of SDR 518.8 million if the amount purchased on the basis of partly estimated data (that is, estimates for the 3-month period October-December 1986) exceeds the amount 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.

^{1/} In the shortfall year, manufactures comprised about 70 percent of the value of "other" exports, agricultural products about 25 percent, and petroleum products about 5 percent.

^{2/} Over 800 mm of rain fell in the province in March/April, which is the amount which normally falls in the area in one year.

4. Staff appraisal and proposed decision

The Argentine authorities are expected to request a purchase of SDR 518.8 million (47 percent of quota) under the compensatory financing facility which would raise Argentina's total purchases outstanding under the facility to 83 percent of quota. Last February a purchase of SDR 388.7 million, representing maximum access available at the time, was approved in principle by the Executive Board at EBM/87/29 (2/18/87), and the decision was amended at EBM/87/33 (2/26/87). Larger CF access is currently available through scheduled repurchases of outstanding CF purchases that took place since last February. (Argentina made a repurchase of SDR 65 million in April and is expected to have completed a repurchase for a similar amount by the time of Executive Board consideration of the request for a CF purchase). Accordingly, the authorities are expected to make a request for a purchase of SDR 518.8 million (47 percent of quota) which would raise outstanding CF purchases to the maximum of 83 percent of quota.

In accordance with the amendment adopted by the Executive Board on February 26, 1987 the approval in principle of the CF purchase was to become effective "on the date when the stand-by arrangement set forth in EBS/87/5...becomes effective, or in any event not later than July 15, 1987, provided that Argentina continues to cooperate with the Fund." Over the past several months the Argentine economic program that was presented to the Executive Board on February 18, 1987 did not unfold as had been planned. However, the Argentine authorities have in recent weeks been actively negotiating measures that would allow a completion of the review of the stand-by arrangement that had been approved in principle on that date. The Argentine authorities' letter of intent describing the revised program is expected to be issued shortly. In light of this development and given that satisfactory arrangements for the financing of Argentina's balance of payments which have been made, an Executive Board discussion is scheduled for July 23, 1987 in order to complete the review and to consider the coming into effect of the stand-by arrangement. On the basis of the policies that Argentina is adopting, the staff considers that the requirement of cooperation for the proposed purchase under the compensatory financing facility has been met.

The staff paper supporting the approval in principle of the request EBS/87/17, (1/29/87) was based on a shortfall of SDR 731.6 million for the 12 months ended September 1986, calculated by using estimated data for the last six months of the shortfall year. Since that time, additional data have become available, thereby requiring a re-examination of Argentina's request to purchase the proposed amount on the basis of updated calculations. Actual data on merchandise exports are now available through September 1986, and the staff in cooperation with the authorities has estimated exports for the last three months of 1986.

On the basis of the updated calculations, a shortfall for the year ended December 1986 is estimated at SDR 865.4 million, or well in excess of the proposed purchase of SDR 518.8 million. As the calculations are based on partly estimated data, in accordance with paragraph 7 of the

compensatory financing decision, the authorities' request for purchase 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.

The causes of the estimated shortfall of SDR 865.7 million for the year ended December 1986 are mainly the same as the factors responsible for the shortfall for the year ended September 1986, as described in EBS/87/17. The unit values of major agricultural exports comprising cereals, oilseeds and oilseed products, wool, tea, and tobacco, declined sharply in 1986 because of an increase in world supply of these commodities. The unit value of petroleum products exports also fell sharply in line with the movement of international oil prices, and the unit values of most manufactured goods exports were adversely affected by the combination of higher world output and the sluggish growth of demand. As "other" exports consist mainly of minor manufactured goods, the shortfall in this category is also largely attributable to declining unit values. Adverse weather conditions were responsible for a decline in the volume of exports of wheat, tea, cotton, and fruit and vegetables.

Earnings are projected to decline further in the first post-shortfall year largely because of the impact on agricultural exports of abnormally heavy rainfall in the main cereal and oilseed producing areas in March/April 1987. Moreover, an upturn in unit values of most agricultural exports is not expected until the second post-shortfall year. A return to normal weather conditions is expected to enable the volume of agricultural exports to increase strongly in 1988, and the volume of manufactured exports is projected to rise in both 1987 and 1988 because of increases in capacity, the improvement of their competitiveness, and the impact of special export promotion programs and incentives.

The staff believes that the proposed request for a purchase of SDR 518.8 million by Argentina will meet all the requirements of the CF 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 by the Government of Argentina for a purchase of SDR 518.765 million under the Decision on Compensatory Financing of Export Fluctuations (Executive Board Decision No. 6224-(79/135), adopted August 2, 1979).
2. The Fund notes the representations of Argentina and approves the purchase in accordance with the request.
3. The Fund waives the limitation in Article V, Section 3(b)(iii).