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Statement by the Honorable Axel Kicillof
Minister of Economy and Public Finance, Argentina

On behalf of Argentina, Bolivia, Chile, Paraguay, Peru, Uruguay

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Minister of Economy and Public Finance of Argentina
Speaking on behalf of the Southern Cone Countries of Latin America
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I. Where We Stand Today

Six years after the global financial crisis begun in 2008, "uncertainty" and “worrisome” are the best words to characterize the current prospects of the world economy. Global growth does not exhibit a firm recovery due to setbacks in the first half of the year. The World Economic Outlook (WEO) presents a substantial downward adjustment in its growth forecast for the global economy compared to the April 2014 report.

Even though financial indicators in many advanced economies have somewhat improved, this boost has not been translated to similar expansion in the real economy. Such apparent decoupling observed in advanced economies between financial indicators and those from the real economy should be closely followed up. In a very preliminary picture of the reality, it seems that through highly increasing public debt some countries have been able to halt economies from further deepening their serious financial conditions, but credit, investment, and economic activity continue to exhibit sluggish behavior.

In advanced economies (AEs), growth is expected to remain uneven across countries, downside risks have increased since the Spring Meetings in April, particularly those related to the geopolitical tensions, and the risks of stagnation and low potential growth which show the need of more active demand side measures. Indicators, in the United States (U.S.), show that a sustained recovery could be gradually gaining ground, but subject to risks. In any event, it seems that the normalization of U.S. monetary policy will follow a gradual path as previously expected. Growth in Japan is expected to remain modest. The situation in Europe shows that much more needs to be done in terms of active policies. The very low inflation in the euro area continues to reflect the considerable risk of deflation, which could affect unemployment, debt ratios and growth, among others.

In emerging economies, the pace of growth remains lower than expected and is becoming more country specific. Nevertheless, emerging market and developing countries (EMDCs) will continue to account for the lion’s share of global growth. The situation in China, which is an important reference for the global economy and emerging economies in particular, would reach, according to the WEO report, growth rates close or within the authorities’ targets. Several Latin American countries are exhibiting an economic slowdown after very high historical growth levels achieved in recent years and the prolonged slowdown, and difficulties and uncertainties in AEs.

As countries in our region continue their process of inclusive growth and development, they are dealing with ways to provide higher-quality public services. It is generally accepted that these reforms must be accompanied by a corresponding increase in permanent revenue mobilization in some countries. There is a healthy debate, of course, about how to go about this with due consideration to income distribution and fairness objectives.

Downside risks have increased. In advanced economies potential growth started to decline even before the onset of the crisis. Other regional geopolitical risks are added to this which can distort financial flows, commodity prices and supply chains. For emerging and developing countries, risks are related to the side effects of global financial conditions such as financial market volatility. At the same time, a prolonged period of slower growth in advanced and major emerging economies and persistent low inflation could mean, if realized, an important risk for EMDCs.

Other questions could be raised about risks and uncertainties on and the future of the global economy, in particular:

Unemployment, mainly among the young, continues to be unacceptably high in many countries. Long-term unemployment needs more active policy measures to avoid becoming endemic, particularly in many countries of the European Union. Also, efforts to create quality employment are important in many EMDCs and Low-Income Countries (LICs).

We are concerned how the systemic impact of the Argentine litigation will be dealt with in the U.S., International Fora and financial markets, and the effects it will have on Sovereign Debt Restructuring issues. The IMF has advanced proposals to improve contractual clauses to strengthen sovereign debt restructuring. This is necessary but will not be enough if a multilateral legal framework for the sovereign debt restructuring process, like the one being discussed in the UN, is not established.

We believe that the Fund has a responsibility to the so-called fragile members and their 800 million population.

II. Policy Priorities

The Managing Director's Global Policy Agenda (GPA)[1] takes stock of the policy priorities for the membership outlined in the last GPA (April 2014) in order to assess their implementation and suggest the policy priority for the next period. We agree with the message that "the key challenge is to buttress the recovery and make it more durable" and that "lifting the outlook for growth and jobs requires decisive policies". Raising growth involves more quality jobs, investment and productivity and how this is being achieved varies from country to country.

Structural Reforms

With regards to structural reforms in the Managing Director's document, it seems that they are the magical solution to everything without proof that countries have succeeded. It is also

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[1] IMFC/Doc/30/14/2, October 3, 2014

mentioned that problems have arisen because structural reforms were not applied in-depth. We believe that there are different views and approaches and the meaning, policies and scope behind structural reforms should be clarified to avoid misinterpretations. Besides, it is necessary to discuss how structural reforms, aimed at the long term, are related to the IMF's mandate.

Structural labor market reform is the best example of the above statement. The Fund's approach to labor market flexibility and structural reforms related to the labor market, public employment, minimum wages, wages as an adjustment variable, productivity achieved through wage reduction and the exclusion of labor migrations, should be reviewed. We are reluctant to accept that the Fund expands its work on labor market reforms because we do not agree that structural labor market reform (to make the labor market more flexible) is the way to solve unemployment problems and job creation. In addition, we reiterate that no meaningful work on this area should be initiated without relevant consultation with the International Labour Organization.

For example (*See the October 2014 Fiscal Monitor, Figure 2.1 Chapter 2, page 3*), Latin America and the Caribbean is the region where, during the crisis, unemployment hardly increased, and after the crisis there is a more noticeable drop in unemployment. It is our understanding that there were no structural labor market reforms in the region, but there were very high GDP growth rates after the crisis. Asia, with no structural labor market reforms, has the lowest unemployment rate, which was not affected by the crisis and, just after the crisis, unemployment was reduced a little bit more. Only in Europe and MENAP regions is unemployment still at the crisis level, while in other AEs the unemployment rate is now below its peak during the crisis but not yet at pre-crisis levels. For instance, in the U.S., a country which also received advice from the GPA document on structural labor market reforms, the unemployment rate is now at a six-year low. In turn, product market reforms are always linked to labor market reform but have reduced traction and less room in Fund documents. This reform should consider broadening consumer rights and preventing dominant positions.

We agree that measures to increase investments, particularly in infrastructure, can boost growth, both in AEs and in EMDCs, including LICs. Investment in infrastructure plays a central role when talking about enhancing growth, job creation and development. In AEs they are needed to replace obsolete infrastructure, and in EMDCs to eliminate bottlenecks and support economic development. Regarding infrastructure investment, we are convinced of the leading role that public sector should have and which would be maintained, not only through public investment but through its central role as provider of guarantees and setting the right conditions for private sector investment. This, on the other hand, implies that the objective is also to attract private and external funding when rates of return demanded are deemed to be adequate. We are certain that benefits are enlarged and that the economy would benefit if there were a complementary relationship between the public and private sector, where the share of the (social) profits can be distributed fairly.

We strongly support policies, as implemented in the countries of our constituency, oriented to enhancing education, encouraging innovation, fostering financial inclusion and promoting alternative sources of funding for credit-constrained Small and Medium Enterprises (SMEs). Leveraging the expertise of other institutions of the United Nation would be welcome.

Fiscal Policy

We agree with the GPA that "enhancing the quality of expenditures and revenues is critical" and that "[s]trong, growth-friendly fiscal frameworks are needed" which concentrates on increasing domestic demand and investments. In this regard, there is a need to strike the right balance for fiscal policy going forward, taking into consideration the drivers of the fiscal balance in each economy and where the adjustment, if needed, will come from. In AEs the average debt-to-GDP ratio has stabilized, as mentioned above, but will remain around 100 percent of GDP at the end of the decade. The crisis that resulted as a consequence of the financial sector adventure increased the debt of AEs in the equivalent of one third of their total GDP, whereas for the U.S. the debt increased by US$ 7.2 trillion, which is equivalent to 41.6 percent of GDP. Efforts will be needed to sharply reduce this to avoid the fiscal consequences of a tighter financial market which could sharply increase the debt service.

In many AEs, the risk of a sluggish recovery, low inflation and reform fatigue requires a balance between supporting growth and employment creation, and fiscal sustainability. Though fiscal measures are said to be oriented to increase growth employment and competitiveness, in fact, in several countries the bulk of the adjustment impacts the population directly through increases in the consumption tax rate, expiration of exceptional unemployment benefits, spending cuts affecting public wages and social benefits, expenditure containments, and cuts in employers' social security contributions. At the same time, we are somewhat surprised about the omission in the IMF flagships to mention the reduction of subsidies in AEs as a way to enhance the achievement of fiscal consolidation, and we believe that the staff should not refrain from addressing this key issue with the same strength that energy subsidies are criticized in EMDCs.

Not less important are longer-term developments in AEs, such as the reduction in top marginal tax rates and a gradual shift from direct to indirect taxation. It is no surprise that these developments have coincided with a concerning increase in income inequality, which is particularly pronounced in the share of national income going to the top 1 percent of the population and in a reduction of the lower and middle class participation in total income. Taking functional distribution the same can be said about the reduction of the wage participation in total income; in some AEs the level of the minimum wage is astonishing low. Policies to cut the corporate income tax in several countries look like the equivalent of 1930s competitive devaluations; it is like a race to the bottom. It is also important to "level the playing field by helping combat tax evasion and tax avoidance by multinational corporations" (U.S. Secretary J.J. Lew in Cairns, Australia, 09/19/2014).

With regards to EMDCs, besides differences among countries, on average, the debt and deficits are reasonable, though their level is higher than pre-crisis levels. A recommendation of the Fund is to rebuild buffers to have more room for policies in view of possible tighter financial conditions and lower growth rates. LICs in general have reduced fiscal risks but in some countries the debt ratios have increased. Acute health problems due to the Ebola outbreak have impacted the finances of affected countries and financial support to finance much needed health-related issues in the affected countries is key. Other LICs face the challenge of development, and the provision of critical public services and infrastructure with the reduced available budget. In this regard, they are facing the need to strengthen fiscal management and increase revenues while prioritizing expenditures.

Monetary Policies

Expansionary monetary policy in AEs should be supported by demand, though QM has likely contributed to effervescent market conditions, while the IMF may not be granting adequate attention to other possible causes of these conditions, one of which could be the existence of moral hazard in sovereign and corporate debt markets. In the euro zone, mechanisms available for working out large debt overhangs remain unclear, with large write-downs yet to be assigned. As the Fiscal Monitor mentions, losses from excessive risk taking in financial markets incurred during the crisis were largely absorbed by the public sector, and the global regulatory reform agenda is far from complete. While banks around the world are better capitalized today thanks to improved regulations, there are likely gaps in the regulatory regime where moral hazard is again accumulating. These may be subtle and not linked to formal public guarantees, but represent important contingent liabilities if resolution mechanisms and bankruptcy regimes are unable to diffuse fears of systemic crises following large shocks.

Financial Sector Policies

The return to high leverage, compressed spreads, and low volatility, particularly among high-yield corporate and advanced economy government bonds, is worryingly reminiscent of the state of markets prior to the crisis. Increased portfolio investment in emerging economies has increased correlations across markets and may represent a shock amplification channel in the event of a sudden change in global risk sentiment. As always, emerging market policy makers must face changing external conditions with clear and flexible frameworks, strong domestic regulations that limit vulnerabilities, and sufficient buffers with which to face overreactions to large shocks. We agree that macro-financial measures should be the main policy tool for dampening financial excesses where they are identified, and support the urgent call to the international community to continue a decisive implementation of the global regulatory reform agenda.

In the reform of the financial system, progress has been made but important gaps still remain, such as in the areas of Over the Counter (OTC) derivatives that grew by 12 percent from 2102 to 2013 to a total of US$ 710 trillion (December 2013). Total OTC derivatives are equivalent to the astonishing figure of around 9 times the Gross World Product (GWP). Other gaps are related to cross-border resolution, reducing reliance on Credit Rating Agencies, and accounting standards and financial fragmentation also remains a concern.

The October 2014 GFSR has presented a timely chapter on shadow banking which highlights the type of multilateral surveillance that we value from the Fund: a cross-country analysis of a potentially large risk that could have important implications for financial stability, which is a source and conductor of spillovers between markets, and on which the current state of knowledge is limited. As feared, regulatory arbitrage is found to be an important driver of growth in shadow banking around the world. We welcome and support the call to improve data collection of non-bank financial intermediation, with a view to continue expanding the regulatory perimeter over time.

Policy Coherence

In a more interconnected world, international cooperation, coordination and coherent policies should tend to mitigate spillovers and stability risks, which in turn are expected to help support growth and increase employment. In this regard, cooperation and coordination are needed to deal with global imbalances, the stability of the international financial system and international taxation.

It was already pointed out that trade surplus economies should increase internal demand or change their composition towards internal consumption while trade deficit countries, the friends of the world economy, as were seen by the Bretton Woods Institutions' founders, should concentrate spending on physical and human capital, R&D, and technology. The Fund should thus continue its analysis on the multilateral consistency of policies and integrate the spillover risks in bilateral surveillance.

To provide stability to the international financial system the above-mentioned gaps should be addressed and the risk of dilution and inconsistencies across jurisdiction should be safeguarded. With regard to the membership, we concur with the commitments that need to be upheld, as mentioned in paragraph 15 of the GPA. The Fund should be consistent with the one-year old Financial Surveillance Strategy so as to ensure the effective operation of the international monetary system and support global economic and financial stability.

In strengthening the Fund, the governance of the institution should be the priority issue. The Fund's legitimacy and effectiveness should be enhanced while strengthening the multilateral and cooperative nature of the Fund. The 2010 reform package should be adopted swiftly because it represents the pre-crisis world economic situation (the data used was up until 2008), that is, the global situation six years ago. Moreover, if the continued reform of the quota and governance structure is key to the Fund's legitimacy and effectiveness, the stagnant process for the 15th General Review of Quotas (GRQ) puts forward the deepened democratic deficit of the institution and the need for a profound transformation of the Fund. The current governance of the institution does not represent the appropriate views and present weight of the whole membership in the world economy, particularly of EMDCs and LICs. If the 15th GRQ is expected to result in increases in the quota shares of dynamic economies, the definition of "dynamic" should be better discussed than it was in the 2010 quota reform.

We recognize the efforts the Fund has made on diversity issues, particularly on improving geographic and gender representation in senior and managerial positions but more has to be done and at a faster pace. Further progress should be achieved to promote the diversity of staff, particularly in regard to academic backgrounds, approaches and experiences.

We commend the efforts of the Fund to adapt to the future and we believe discussions should be continued on long-term trends, such as youth and aging, income distribution by country and at global levels, inclusive growth and environmental sustainability, among others, and how these issues can be considered within the Fund's mandate and its advisory and surveillance role.

Argentina

After a decade of sustained and inclusive growth, the challenge is to maintain and continue on the same path under an uncertain, worrisome, and stagnated external environment. In this context, active policies to boost the internal market and the aggregate demand are promoted. The Argentinean economy had experienced several decades characterized by macroeconomic instability and stop and go cycles. However, after the worst crisis in its history from 1998 to 2002, the country made a 180-degree turn starting a large structural transformation based on the active role of public policy. Between 2003 and 2013, Argentina's GDP had an average annual economic growth rate above 6.2 percent, the highest average growth rate in its economic history over such a long period, while per capita GDP increased by 63.1 percent during the same period. Most importantly, this has been achieved with socially inclusive growth, with a clear reduction in poverty, unemployment, and inequality, making Argentina's PPP GDP per capita one of the highest in Latin America and its Gini coefficient one of the lowest.

Argentina's economic resilience is due to prudent macroeconomic policies, despite the economic uncertainties in Advanced Economies, and strong domestic speculation. This policy is further buttressed by a strong domestic consumption based on the support given to employment policies, real wages and pension increases, enhancing job creation while promoting public and private investments, with low indebtedness levels of both the public and private sector and a solid balance of payments result, in the context of a managed floating exchange rate regime, and a robust financial sector supported by a sound macroprudential framework. The Ministry of Economy and Public Finance has focused on enhancing and guaranteeing income distribution to increase domestic demand and reorient private investments. In this regard, private consumption and investments increased in 2013 compared to 2012 by 4.3 and 3.0 percent respectively. Participation of investments in total GDP was 21 percent in 2013 among which the most dynamic sector was Research and Development which increased by 21.5 percent.

During the second quarter of 2014 GDP increased by 0.9 percent in relation to the previous quarter, ending two quarters of negative growth; 4Q13 and 1Q14 both with -0.5 percent. The accumulative figure for the first semester of 2014 compared with last year's first semester is on the positive side. These figures are closer to the Ministry of Economy and Public Finance of Argentina's GDP projection for 2014 of 0.5 percent than to the negative figure of -1.7

percent projected by the October 2014 WEO.[2] Today we are facing a slowdown in growth, mainly due to the contraction in activity in our major trading partners. However, taking into account GDP growth rates for the first two quarters of the year (0.3 percent and 0 percent on an annual basis), a projection of -1.7 percent could only be validated with two quarters of contraction deeper than 3 percent. Different expansionary fiscal policies pursued by the national government since early this year, coupled with wage increases achieved in joint negotiations, lead us to think that the WEO´s proposed projection for the remainder of the year is overly pessimistic.

Regarding the 2015 scenario, there is no reason to consider a downward revision in projections. The Argentine government has recently sent the draft budget for 2015 to Congress, which includes an increase of more than 2 percentage points in primary expenditure (in real terms), and, in particular, a social expenditure rise of almost 10 percentage points above the inflation rate. Moreover, these projections need to be complemented by the increase in the expected economic growth of our trading partners, which are in fact reported in the WEO.

We are concerned with the WEO forecasts, particularly regarding Argentina, where forecasts in one year for the following year's real GDP growth were off by an average of 5.0 percent points between 2000 and 2013. If the average of the Sept-Oct WEO forecasts for the same year is taken for the period 1998-2013 the forecasts were off by an average of 1.8 percent points, which is rather high considering that that the end of the year was just a few months away. Biases in the forecasts are rather interesting. Whereas optimistic forecasts are related to the period of Argentina´s programs with the Fund, pessimistic projections are seen when Argentina follows heterodox (and successful) economic policies. As previously stated, these forecasts are a concern. In a constructive way we tend to see this as further reason for the IEO recommendations for improving the Fund's forecasting methods. When forecasts for a particular economy are completely out of line persistently, the underlying model or accepted wisdom about that economy should be revised in order to add value to the forecast. This is what we ask to be done in this case.

On the other hand, as mentioned, an unfavorable external environment is putting negative pressure on growth. Exports fell by -6.4 percent in 2013 and 2014 growth prospects for Brazil, our main trade partner and a strategic ally, are less and less optimistic.

Equality is essential to promote and sustain economic and social growth. During the last decade, Argentina has strongly believed that equality is an important ingredient in promoting and sustaining economic and social growth. Since 2003, the creation of formal and quality employment, social inclusion and better income distribution are the key components of Argentina's growth model. During this period, the number of workers with a formal job, paying social security contributions, increased by 80 percent and the minimum wage grew to be among the highest in Latin America. The participation of wages in terms of total income, which was on average 40.2 percent in the period 1993-2001, increased to 51.4 percent in

[2] Page 83, GDP projections for Argentina and on Page 84, *"Argentina is projected to remain in recession in 2014–15".*

2013. The end result was a historical increase in living standards, which is reflected in the doubling of the middle class between 2003 and 2009, as found by a 2013 report by the World Bank.[3]

Economic and social growth goals are achieved through measures oriented to boosting economic activity and, at the same time, enhancing Argentina's social safety net. These measures are based on several programs, among others: the Universal Child Allowance; the Universal Pregnancy Allowance Program; "PRO.CRE.AUTO" the Credit Program for Car Purchasing; the National Program "Precios Cuidados" to provide predictability, stability and transparency to the price-setting mechanisms of consumer goods through price agreements; interest rate regulation to reduce financing costs; "Argentina Trabaja", "Ellas Hacen" with the aim of empowering women; "Manos a la Obra", the Food Security Plan (Seguridad Alimentaria) and the program Actions for Social Promotion and Protection, the Plan for Pension Inclusion, Plan Federal de Viviendas, and "PROCREAR", an innovative program to finance house construction and remodeling.

To deal with the hard core of poverty, the "Plan Ahí" has outreached small towns and poor neighborhoods. In addition, as part of the efforts to reduce income inequality and promote social inclusion, the Government recently launched the program "Prog.r.es.ar" (Programa de Respaldo a Estudiantes Argentinos - Program to Support Argentinean Students), aimed at including young people in the social protection system. The program encourages beneficiaries (young people who do not work or work informally or who have a salary lower than the minimum wage) to complete their studies and/or their professional training, thus increasing their chances of productively entering the labor force.

In order to create quality jobs, in June 2014 the law for Promotion of the Registered Labor and to Prevent Occupational Fraud was approved. Several policies were oriented to preserve the level of employment and support the rhythm of employment creation such as the Program of Productive Recovery (REPRO); the reduction of employer contributions for new workers; in August 2014 the Program Pro-Employment (PROEMPLEAR) to increase youth employment and several programs aimed to support micro, small and medium enterprises and cooperatives. In order to boost exports in the medium term, particularly of industrial manufactures, the Program to Increase and Diversify Exports (PADEX) was launched.

The minimum wage is planned to increase by 31 percent from September 2014 to January 2015 to be the highest in Latin America. Both, the defense of employment and the policies to increase the income of the vulnerable population have improved income distribution. The Gini Coefficient in 1Q2014 was 0.422 which is -17.6 percent below that of 2004. The income gap, that is, the per capita income of the richest 10 percent of the population compared to that of the poorest 10 percent, was reduced from 12.4 times in 2004 to 7.5 times in the second

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[3] Ferreira, Francisco H.G.; Messina, Julian; Rigolini, Jamele; López-Calva, Luis-Felipe; Lugo, Maria Ana; Vakis, Renos. 2013. *Economic Mobility and the Rise of the Latin American Middle Class.* Washington, DC: World Bank and Bussolo, Maurizio; Maliszewska, Maryla; Murard, Elie. 2014. *The Long-Awaited Rise of the Middle Class in Latin America Is Finally Happening.* Washington, DC, World Bank.

quarter of 2014. Moreover, the social security system has increased its coverage from 3,158,000 beneficiaries in 2003, which represented 66 percent of the elderly, to almost 6 million beneficiaries, reaching 94.3 percent of coverage. Expenditure on education has risen to more than 6 percent of GDP.

Finally, the recent implementation of a program for reallocation of subsidies, based on an income and wealth criteria, as well as on energy efficiency criteria, will allow the government to assign social spending more equally, guaranteeing the protection of the most vulnerable sectors of its population.

A vigorous and profitable financial sector is tackling the challenge of increasing credit.

During the 2001-2002 crisis in Argentina, the financial system almost collapsed. After more than twelve years, as shown in the FSAP, it is now solvent, liquid, well-regulated, profitable and capitalized. At the same time, the Central Bank of Argentina has a new charter, approved by law in 2012, which broadened its objectives and mandates, which currently include not only monetary stability, but also financial stability, employment, and economic development with social inclusion.

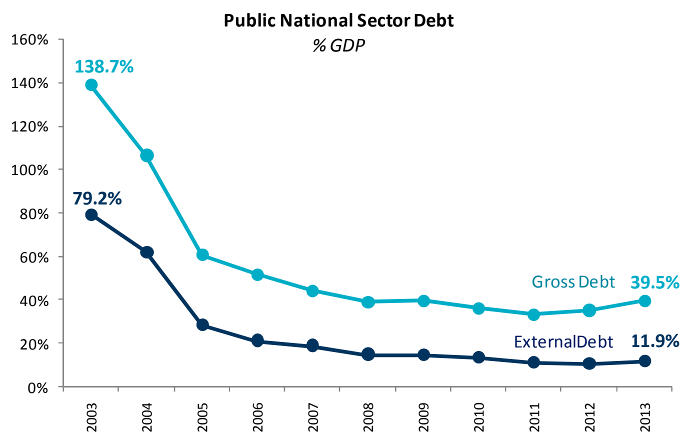
Furthermore, the government has implemented a range of policies to support the development of long-term financing for productive investments, particularly in infrastructure. Last December the Fund for the Argentine Economic Development (FONDEAR) was launched to broaden credit supply and make it more flexible. The program is oriented to projects in strategic sectors for the economic and social development to initiate activities with high technological content and to increase value-added generation in the regional economies. The Sustainability Guarantee Fund (FGS) has also contributed to the sustainable development of the real economy through financing long-term investment projects and recent regulatory initiatives aimed at increasing institutional private funding for those types of projects. Such is the case of subsection "K", which establishes that insurance companies must redirect a percentage of their investments to instruments financing productive projects which raised insurers' investments in these types of projects from less than 1 percent in 2011/2012 to 10.7 percent in 2013.

The government understands that public investment, particularly in infrastructure, is a key tool for development, regional integration, employment creation and improving the living standards of the population. Public investment is currently focused on roads and highways, railways, logistics and transportation, shale oil and natural gas, electricity, communications, education, health and housing. This enhanced role of the state has strongly encouraged private investment. In the second quarter of 2014 investment reached 19 percent of GDP, 3.6 percent more than in the first quarter.

A sustainable public debt path

Since 2003, after the country's worst financial crisis that led to default, Argentina implemented a set of measures aimed at progressively normalizing and reducing public debt and creating a sustainable repayment capacity. These measures involved a successful debt restructuring process that reached a substantial level of acceptance—more than 92.4 percent of the eligible debt.

There was an important debt reduction process carried out by the government in recent years. In this regard, the gross public debt (national sector) in terms of GDP dropped from 138.7 percent in 2003 to 39.5 percent in 2013. Moreover, the external public debt fell from 79.2 percent in 2003 to 11.9 percent in 2013, while the total stock of the external debt (public plus private) was reduced from 30.5 percent of GDP in September 2012 to 27.0 percent in September 2013, reaching the lowest ratio in the last 18 years.

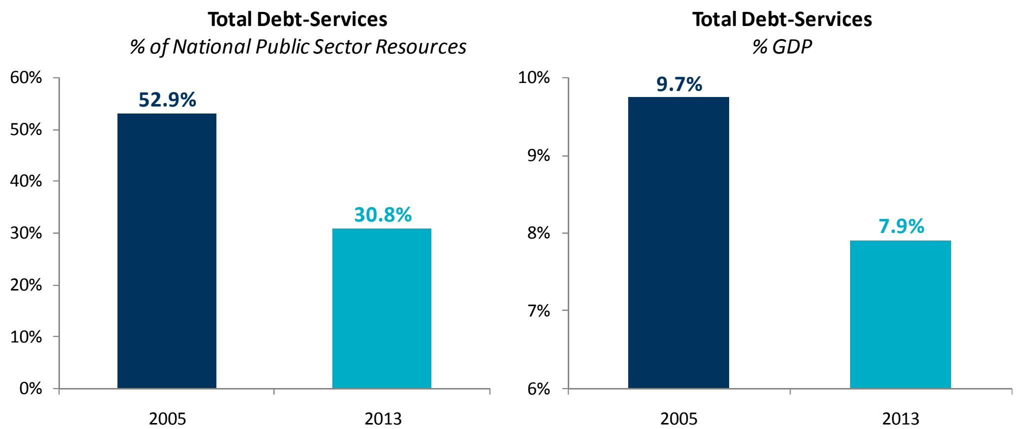


Source: Ministry of Economy and Public Finance

The reduced external public indebtedness in terms of GDP allowed the stock of international reserves to represent around 40.6 percent of the public external debt in January 2014, whereas in 1992-2000, the period of the so called "Argentine miracle" and the currency board, this relation was 33.4 percent.

At the same time, debt-services (principal plus interests) have significantly reduced since 2005. In terms of total national public resources, total services dropped from 52.9 percent in 2005 to 30.8 percent in 2013. GDP services decreased from 9.7 percent in 2005 to 7.9 percent in 2013.

Despite these efforts, Argentina is still facing an extraordinary challenge posed by the predatory speculative funds known as "vulture funds", who have not accepted and continue to refuse the restructuring offer. Argentina today continues to litigate and do not have any qualms about harming the rights of those majority creditors who accepted Argentina's exchange offers in 2005 and 2010. This disruptive strategy from the vulture funds, which consist mainly on blocking the rightful flow of funds to bona fide 92.4 percent of creditors that accepted the debt restructuring, is made possible because of the lack of an adequate international legal framework for sovereign debt restructuring. This new framework as has now been proposed to be established by the United Nation General Assembly in September 2014.



Source: Ministry of Economy and Public Finance

Several countries, international institutions (including the IMF) and prestigious experts are convinced of the disastrous potential consequences of upholding the vultures' views in court. They are aware that vulture actions may affect the financial world, particularly the sovereign debt market, and consequently have warned about the need to limit the damage that these strategies can generate. In this case, Argentina has received the support of other countries such as Brazil, Mexico, and France who sent "amicus curiae" to the Supreme Court in USA, as did several private banks, investors and academics.

Argentina has demonstrated its commitment to work together on the bilateral agenda with the IMF. Our relations with the Fund have involved technical assistance to develop the new CPI on a national basis (launched in February 2014) and the improvement of GDP figures. Also, the ROSC on the three key standards of financial regulation has been completed; the country is sharing all relevant information and statistics through the SDDS, and the FSAP was completed and discussed by the IMF Board last year. The Argentine Congress also approved the 2010 Quota and Governance Reform of the IMF. Argentina has also ended disputes with several corporations at the International Centre for Settlement of Investment Disputes (ICSID) of the World Bank and an agreement was achieved with the Paris Club and the first payment of the debt was already made. An agreement to compensate the company Repsol for the public sector's increased share in the company was approved by Congress. All these, together with the significant reduction in debt levels already achieved, are expected to generate favorable conditions to encourage FDI inflows. This will be particularly important in energy projects, such as Vaca Muerta, one of the largest world reserves of shale oil and natural gas.

Policy challenges and future endeavors

By the end of 2013, the economy was facing, as its main problem, a fall in international reserves and considerable pressures in its foreign exchange market, leading to a depreciation of the exchange rate in January 2014. After that, the government implemented a set of measures, including a rise in interest rates, and made conditions for access to local foreign exchange market more flexible. The strategy was successful in stalling the drop in reserves and reducing excessive volatility in the exchange market. Moreover, in order to avoid an excessive pass through from depreciation to prices, the authorities implemented temporary price agreements and monetary and fiscal measures.

On the structural front, Argentina is facing important challenges. Many of them are, to a large extent, a result of fast growth itself (as in the case of energy or infrastructure), but also as a consequence of the natural increase in the aspirations of the population and the need to improve competitiveness, to increase the complexity and regional integration of production and to stimulate the diversification of exports. Reform priorities will remain focused on the areas of growth, investment, employment and social inclusion.

Throughout its economic and social history, Argentina has learned the hard way that the state must play an active role to achieve a steady, sustainable and inclusive path of economic growth and that the development process should be focused on people and the improvement of their living standards. It is the state who cares for the vulnerable people, the workers, the pensioners, the poor, the consumers, women, the youth and children. Growth has been sustained and social indicators have improved considerably. Due to the structural transformation of the economy since 2003, Argentina is now in a very good position to address the development challenges ahead. The main objectives for the future will be strengthening, broadening and continuing with these endeavors.

Bolivia

Despite the international scene still being marred by uncertainty, **Bolivia** expanded notably in 2013 as a result of its economic policy derived from the application of the economic, social, communitarian and productive model. Bolivia's growth is third in the region—second in South America—explained mainly by the expansion of domestic demand. In 2013 **Bolivia** marked an important milestone in its economic history as it reached its highest growth in the past 38 years (6.8 percent), continuing the strong and stable economic performance observed since 2006. The evolution of the manufacturing industry, hydrocarbon, financial services, transport, communication and public administration services explained this dynamism. Public investment amounted to $ 3,780.7 million in 2013, aiming to develop the productive sector, strengthen the country's infrastructure, and support with greater resources education and health. As an example of structural transformation, Bolivia ventured into the satellite era putting the Tupac Katari satellite into orbit, which will make communications more efficient.

In 2013 **Bolivia** continued its process of industrialization. In August 2013, the liquid-hydrocarbon separation plant at Rio Grande (Tarija) was launched to supply the domestic Liquefied Petroleum Gas (LPG) market and to export to Paraguay. In addition, the country has continued with the implementation of other important projects, such as the liquid-hydrocarbon separation plant at Gran Chaco, the urea and ammonia plant, and the lithium industrialization project, among others.

The external accounts still show a positive performance. Last year the level of exports reached a new record of $ 12,162.7 million. The trade balance achieved a positive balance of $2,809.7 million and the authorities expect that the current account will stay positive at the end of 2014. Net foreign direct investment registered a new record of $ 1,749.6 million, above the levels registered from 1993 to 2002. The flow of foreign investment went mainly to hydrocarbons (69.8 percent), manufacturing (15.1 percent) and mining (7.4 percent). Net international reserves reached a new high ($ 14,430.1 million); a figure without historical precedent which, as a percentage of GDP, is the largest in the region. Such strong level of international reserves allowed the administration of President Morales to better support the output base and promote productive projects that contribute to economic development and food security. Indeed, in July the Central Bank of Bolivia (CBB) transferred $ 600 million as a non-refundable contribution to the Fund for Industrial and Productive Revolution (FINPRO), and in September FINPRO borrowed $ 600 million from the CBB.

The exchange rate policy kept its objective of avoiding excessive volatility, which is reflected in a stable demand for foreign currency and no expectations of sudden movements in the exchange rate while preserving the competitiveness of the economy. The authorities intend to keep the exchange rate in line with its fundamentals noting that its recent stability is a result of the response to the post-global crisis juncture and it does not indicate a change of the exchange rate regime, which is a crawling peg.

The prudent exchange rate policy along with the macroeconomic stability has deepened the "bolivianization" of financial intermediation. Bolivian currency-denominated deposits and loans reached 77.3 percent and 88.7 percent respectively in 2013, while the indicators of solvency, profitability and portfolio quality recorded favorable levels for the financial institutions, which is a reflection of the strength of the national financial system. The promulgation of the new financial services law indicates a milestone in the history of the national financial legislation, breaking the trend marked by the old law of banks and financial institutions. Under this new regime, the State performs two main functions: i) regulating the financial sector; and (ii) getting directly involved in the financial system. In 2013, the positive performance of the financial system highlights the record level of deposits and credits. Deposits closed with a growth of 16.2 percent in 2012, while micro-credit and housing credit stimulated the expansion of the loan portfolio at a growth rate of 19.2 percent. Loans to productive sectors increased 14.7 percent, driven by loans to manufacturing industry, construction, agriculture and livestock. In addition, the degree of regional loan concentration decreased. The banking system is strong and shows a comfortable expansion, an increasing capital adequacy ratio and decreasing non-performing loans.

In 2013 there were inflationary pressures through the second half of the year as the consumer price index increased, due mainly to the hike of prices of tomatoes, potatoes and chicken, explained by adverse climate conditions such as drought and frost that affected crops, followed by some degree of speculation. The Government rapidly approved measures that were compelling to reverse the increase in commodity prices namely: i) a temporary deferral of tariff assessment for the import of tomatoes, ii) an increase in import quotas of potatoes and tomatoes and iii) the regulation and control of the price of chicken which has proven successful to abate inflation in conjunction with the monetary policy. In fact, the CBB gradually reduced the liquidity of the financial system by increasing the supply of monetary regulation instruments, allowing moderated increases in interest rates. These gradual increases preserved the dynamism of economic activity. Inflation in 2013 ended up at 6.5

percent, a rate within the range envisaged by the authorities (3.8 percent to 6.8 percent). For 2014, inflation should be smaller than in 2013.

For the eighth consecutive year, **Bolivia** recorded a surplus in the fiscal accounts; the overall result of the Non-Financial Public Sector reached 0.7 percent of GDP, attributed to the increase in oil revenues and taxes, and the proper control of current expenditures. Similarly, the National Treasury (TGN) recorded a surplus of 1.9 percent with a new record of revenues as a consequence of the dynamism of the economy and the implementation of tax measures. Autonomous departmental governments, autonomous municipal governments and public universities benefited from higher income transfers and royalties, which increased by 19.4 percent compared to 2012. In 2013, the sustainability of external public debt continued being the main objective of public debt management. The debt-to-GDP ratio registered 17.3 percent, below common international standards and for the third consecutive year, the domestic debt saw a significant decrease of 5.3 percent. The resources of 2012 and 2013 sovereign bond issues were entirely earmarked for enhancing the national road network. It is also remarkable that the National Treasury issued, for the first time in Bolivia's history, a series of 50-year maturity domestic bonds, generating a reference for long-term private sector financial investment

In 2014 **Bolivia** has continued to follow its model of state-led economic development. The Government strategy aims to reach a sustained growth with a more equal income distribution and further reducing the poverty rate, relying on the nationalized sectors (hydrocarbons, electricity and telecommunications) and a significant expansion of public investment. However, the indebtedness associated with it will not put the sustainability of external debt at risk. The fiscal stance may result in a small deficit but there is up-side risk associated with international prices, while monetary policy will continue to support the economy's liquidity needs and, at the same time, control inflation. The authorities are confident that the growth rate for this year will be around 5.7 percent, as the economy is being stimulated decisively.

Chile

Following several years of strong growth, the Chilean economy has slowed markedly and is expected to grow by 1.75 to 2.25 percent this year. The slowdown stems from the end of the super cycle of high commodity prices due to a deceleration in China. As a result, prices of minerals have fallen and stabilized at lower levels, thus deteriorating the terms of trade for commodity-exporters throughout Latin America. Such lower price levels triggered a significant drop in investment in the mining sector from very dynamic growth rates in investment in recent years. Lower investment rates translated into a marked deceleration of demand in the early stages of this deceleration cycle, which has now broadened also into private consumption, particularly of durable goods. In this context of weaker demand, a credible policy framework has allowed the Chilean authorities to take decisive policy actions to support demand by making use of monetary and fiscal policies to achieve higher growth rates in 2015.

Monetary policy has provided a first line of defense to support domestic demand, as the Central Bank of Chile has implemented a loosening of the monetary policy stance by cutting the monetary policy rate by 175 basis points over the past year, from 5.0 to 3.25 percent. Monetary loosening, along with the global strength of the U.S. dollar, has lead to a marked depreciation of the peso that has contributed to a reduced current account deficit. Within the context of a free floating exchange rate, the exchange rate is indeed playing its buffer role, but pass-through has also put some degree of upward pressure on domestic prices. While inflation currently exceeds the central bank's target range, this is estimated to be a transitory phenomenon. Over the policy horizon, private inflation expectations remain well anchored at the midpoint of the central bank's target range, reflecting the credibility of the inflation targeting framework. Given the seven rate cuts already implemented in the last 12 months and the lag with which monetary policy operates, the authorities see limited space for further monetary accommodation, and will remain vigilant of risks to their price-stability objective.

Chile has ample fiscal space stemming from low public debt, significant resources in its sovereign wealth funds, and very favorable market access, as a result of the long-standing operation of a structural balance rule. The authorities are committed to using such available space for maneuver to support the domestic demand and ensure an inclusive and sustainable recovery. The government has recently presented the 2015 budget bill, with an overall increase in public spending of 9.8 percent, with increased spending on education, infrastructure investment and health care to support growth, while boosting the economy's productive capacity in the longer term. This expansionary fiscal stance remains anchored within the fiscal rule, and it has been announced that the budget will return to structural balance by 2018.

The government is in the process of implementing an ambitious agenda of reforms to taxation, education, and infrastructure that aims to make the economy more inclusive and productive. After a bipartisan agreement was reached in the Senate, the President signed into law the most important tax reform package in 20 years. The reform will raise structural revenue by 3% of GDP, allowing for an increase in spending on public education, health care and other social services, while also increasing public savings by returning the budget to structural balance. The design of the reform has sought to make the tax system more progressive by shifting the burden towards direct taxes, while maintaining adequate incentives for savings and investment.

Paraguay

After strong growth last year, the Paraguayan economy will continue to perform well, increasing by around 4 percent in 2014. While some sectors show some deceleration at the margin (mainly agriculture and generation of electricity by bi-national companies) the rest of the economy remains quite dynamic, growing on average by more than 5 percent on a yearly basis.

Some price pressures observed at the beginning of the year are now fading, after the timely monetary adjustment that started at end-2013. Since then, the Central Bank of Paraguay (CBP) has increased its policy rate by 175 basis points. The change in policy was crucial to anchor inflation expectations and avoid second-round effects coming from the adjustment in some administrative prices. Inflation is expected to reach just below 5 percent at the end of

2014 and since the formal implementation of the inflation-targeting regime in 2011, inflation has remained slightly under the 5 percent target.

Congress has recently approved a Fiscal Responsibility Law (FRL). The new fiscal framework will improve the quality of public outlays by putting strict ceilings on the amount of the annual deficit and on increases in current spending. A tax reform was also passed to broaden the tax base in the economy. The reform introduced a value-added tax on agricultural goods and an income tax for the agricultural sector, making it one of the most buoyant sectors in the last decade. Before the reform, this highly profitable sector was fully exempted from income taxes and benefited from value-added tax deductions. Finally, a program against tax evasion was implemented and, as a result, tax revenues are increasing by around 20 percent year-on-year, a percentage which cannot be solely explained by economic growth and new taxes.

The fiscal deficit is projected to reach about 1.5 percent of GDP in 2014; the limit set by the new FRL. While current spending has stayed under control (and will remain stable in real terms), capital spending will more than double its historical average. Given its productive capacity, the country lags behind in infrastructure. The government's aim is to reverse this juncture, not only using public resources (including those coming from international sovereign bond issuances) but also involving the private sector. A public-private partnership law, which was approved last year, will become a useful instrument to achieve this goal. The CBP is currently working on modernizing the country's financial legislation, which is needed to put Paraguay´s in line with international best practices. The banking sector now represents about 45 percent of GDP and it is the major source of credit for the productive sector. A healthy financial sector is a crucial element for the government's plans to achieve a more sustainable and inclusive growth path.

Peru

GDP grew 1.7 percent in 2Q2014, with a 3.1 percent increase of in non-primary sectors. The most dynamic sectors were commerce (4.4 percent) and services (4.9 percent). Domestic demand expanded by 2.2 percent, compared to 7.1 percent in 2Q2013. This result was due mainly to a decrease in investment.

In 2Q2014 the current account deficit increased to $3,738 million (7.3 percent of GDP), reflecting a temporary fall in the value of exports due to lower international prices (especially for copper and gold) and a smaller volume of gold exports.

The nonfinancial public sector surplus was 3.2 percent of GDP in 2Q2014, 0.9 percentage points lower than one year earlier. This performance was associated with higher general government current expenditures (0.6 percentage points) and with the fact that state-owned enterprises ran a deficit of 0.5 percent of GDP (from a surplus of 0.5 percent of GDP in 2Q2013).

Inflation in September was 2.74 percent, within the target range fixed by the Central Reserve Bank of Peru (BCRP), reflecting mainly an increase in food and fuel prices, and in electricity tariffs. Inflation is expected to remain within the target range and decrease towards the central point of the range (2 percent) in 2015-2016.

In September the BCRP Board decided to reduce the reference interest rate from 3.75 percent to 3.50 percent, consistent with the expectation that inflation will converge towards 2 percent in the context of a weaker-than-expected business cycle. In line with expectations, 12-month inflation returned to the target range in August. Moreover, the BCRP has adopted measures to relax its reserve requirement policy, with an aim to ensure adequate bank liquidity and facilitate credit expansion in domestic currency. The most recent reduction (from 11.0 percent to 10.5 percent) became effective in October.

Uruguay

Solid institutions and sound policies are always important, but they are more noticeable in thorny times. Uruguay has recorded an impressive growth (annual average of 6 percent) over the last decade, even when during this period the gains of the country's terms of trade did not have at all the same magnitude as the rest of the countries in the region, as underscored by some IMF studies. However, perhaps the most telling years are 2009 and 2014. During the worst year of the global crisis, Uruguay's GDP was able to grow at 2.6 percent (compared with a contraction of 1.7 percent in Latin America and the Caribbean). Meanwhile, amidst a substantial regional slowdown (particularly in Uruguay's key partners), the country is showing a considerable dynamism in its economic activity, with a growth forecast close to 3 percent (compared with 1.3 percent for the region).

There are many indicators that reflect the traditional soundness of Uruguay's pillars. Among others, the country ranks first in the region on the Corruption Perception Index (Transparency International), Press Freedom Index (Reporters without frontiers), Democracy Index (Economist Intelligence Unit), while it is second on the Economic Freedom Index (Heritage Foundation) and Worldwide Governance Indicators (World Bank). Meanwhile, there have been major structural reforms waged over the last decade, which substantially strengthened a number of institutions. For instance, among others, profound reforms were undertaken in the public banks (*Banco de la República Oriental del Uruguay* and *Banco Hipotecario*) as well as in the Superintendency of Financial Services. These changes led to a critical transformation of the incentive structure, resulting in a sound financial system, manifested, among others, in a moderate increase of credit, very low non-performing loans, a small non-resident deposit level (particularly Argentinean deposits, once a source of vulnerability, are less than 10 percent of total deposits), and comfortable levels of solvency and liquidity. Likewise, there have been remarkable changes at the revenue administrations on which a recent IMF document ("Modernization of the Revenue Administrations in the period 2010-13") underscored the successful process observed in recent years. The huge decrease of tax evasion (for instance, VAT evasion declined systematically from 39.9 percent in 2000 to 13.4 percent in 2012) mirrors the magnitude of the improvements; these reforms have been accompanied by a drastic change in the tax system, which aimed at enhancing the efficiency of tax collection, increasing fairness, and creating an appropriate investment climate.

Investment, which was once Uruguay's Achilles' heel, has been exhibiting a remarkable performance over the past years, not only compared with the country's history, but also with regional developments. The level of investment relative to GDP significantly increased to somewhat more than 20 percent (average in the period 2005-13), while foreign direct investment went up from an almost negligible level to 5.7 percent. Most of the country's current account deficit is explained by the high level of FDI. Strong efforts in different areas have driven exports of goods and services to show a substantial diversification in terms of products and markets. A short time ago, many IMF studies, among others, underlined the existence of strong linkages between Uruguay and its neighbor countries. Many episodes in recent years (2014 being one of them) highlight the critical decoupling of Uruguay from regional developments, in a process that continues to deepen.

Considering the country's robust economic activity, it is not by chance that unemployment rates have been at record lows, and that real salaries have risen robustly although closely accompanying productivity increases. The considerable boost of domestic demand (growing somewhat above the country's GDP over the past few years) along with some external factors (currently, as has occurred in many emerging economies, there have been some pressures on the local currency, which is also consistent with Uruguay's flexible exchange rate system) have added to inflationary pressures. While it is under control, lessening inflation constitutes one of the authorities' priorities and, accordingly, the government has been displaying decisive policies, for instance through a contractionary stance of the monetary policy.

For some years over the last decade, external developments along with the country's attractiveness, have led Uruguay to accumulate an important amount of international reserves (currently at 33 percent of GDP) which, of course, constitutes a substantial financial buffer. At the same time, this kind of insurance has contributed to increasing the fiscal deficit (now, at somewhat above 3 percent of GDP). In perspective, Uruguay's fiscal position is solid and fully sustainable, which is reflected in the country's sound debt indicators. In this regard, it is important to note that gross public debt-to-GDP has declined more than 40 percentage points over the past ten years. More importantly, the net public debt-to-GDP ratio (under the current circumstances, is a much more appropriate indicator to assess the state and outlook of Uruguay's public finances) has decreased to 23 percent. Other indicators, such as the average time to mature the central government's debt (15 years), the debt composition by currency (52 percent of the debt was denominated in local currency in 2013, compared with less than 10 percent a decade ago; meanwhile, assets in foreign currency have overcome debt in foreign currency), and the negligible level of contingent liabilities further corroborate the drastic changes observed by Uruguay's fiscal accounts, which have been endorsed by a number of upgrades by rating agencies.

For a long time, the Uruguayan authorities have insisted on their concept of global stability, in the sense that it involves economic, political, and social factors; and that, in the same way, economic growth is a necessary but not a sufficient condition to reach their ambitious social targets. Uruguay's case demonstrates once again that growing and attaining an appropriate distribution can perfectly go hand in hand. Poverty rates have dramatically declined, for instance, from 24.2 percent (households) in 2006 to 7.8 percent, and the Gini Index has dropped from 0.46 to 0.38. Meanwhile, the authorities are introducing new initiatives towards reinforcing the process of inclusive growth, and one of them is the financial inclusion law. Inclusiveness and a further boost in the development of capital markets are headed in the same direction.

Macroeconomic stability and better distribution; appropriate rules and institutions to enforce them; development of capital markets and inclusiveness: Uruguay’s policies and structural changes point out one more case in which this kind of objectives are not only compatible but, especially, synergetic. The authorities are not complacent with the results; they just constitute further stimulus to keep facing the substantial challenges Uruguay will have in the short and medium-term.