Companies fear radical turn in Argentina

By Benedict Mander in Buenos Aires

Hundreds rally in Buenos Aires over the Argentine debt crisis

When President Cristina Fernández confidently praised Argentina's financial system as “one of the most solid in the world” during a speech at the Buenos Aires stock exchange on Wednesday, some of the high-ranking executives present struggled to hide their incredulity.

Just the day before, at one point on the verge of tears, Argentina’s mercurial leader had nervously announced a plan to dodge a US court order to pay so-called “holdout” creditors in New York, after the ruling pushed the country into default last month for the second time in 13 years.

Economists say Ms Fernández had good reason to be nervous. They warn that the plan to use an Argentine state bank to make debt payments and to invite creditors to swap their foreign law bonds for new ones subject to Argentine law will only prolong Argentina’s isolation from international markets since its last default in 2001, and plunge the economy deeper into recession.

Many also cast doubt on whether the plan is even feasible. One of the holdout hedge funds, Aurelius Capital Management, said Argentina’s leaders had “chosen to be outlaws” with the plan. New York Judge Thomas Griesa on Thursday said it was “illegal”, although he stopped short of declaring Buenos Aires in contempt of court, “for the moment”.

Since the default, which was triggered by Judge Griesa’s decision to prevent Bank of New York Mellon from transferring interest payments to bondholders without also paying the holdouts at the same time, fears are growing that Ms Fernández is adopting an increasingly hardball strategy.

“The president has decided to stop being orthodox and is going all-out radical,” said one foreign executive in Argentina, referring to attempts over the past year to normalise relations with international creditors in order to regain access to external financing as central bank reserves plumbed record lows.

Those efforts, now apparently stymied by the default, included an agreement to compensate Spain’s Repsol with $5bn after expropriating its Argentine assets in 2012, and to pay a long overdue $10bn debt with the Paris Club of creditor nations.

The executive complained of a series of “scary” moves against the private sector.

These included threats to sanction a US-based company after it filed for bankruptcy and closed down its local operations, which Ms Fernández claimed was really an attempt
backed by the "vulture funds" to spread fear among the population.

Business groups are also up in arms over a so-called "supply" law being debated in congress that has been described as "retrograde" and "unconstitutional" by business leaders, who say it will enable the government to intervene in companies to control prices and profits.

Some observers even fear a conflict is brewing on the scale of Ms Fernández’s damaging clash with the farming sector in 2008.

But Hugo Haime, a pollster in Buenos Aires, says this combative atmosphere suits Ms Fernández, if she is to be seen defending the nation’s interests against an unpopular enemy, whether it is the "vulture funds" abroad, or the rich and privileged at home.

“This government feels most comfortable in permanent confrontation,” he said.

In particular, it enables Ms Fernández to shore up support among her most hardline supporters, whose backing in congress she will depend on not only as the campaign for presidential elections next year heats up, but also for the longer-term duration of her political movement and the protection of her legacy after her term finishes.

Carlos Germano, a political analyst, said Ms Fernández is also taking advantage of the conflict, especially with the holdouts, to distract attention from economic woes, with a deepening recession worsened by one of the highest inflation rates in the world and acute shortages of foreign exchange reserves.

Indeed, many economists expect a second devaluation this year, with the black market peso plunging to a record low of 14 to the dollar this week, compared with about 10 in January.

Concerns for the central bank’s autonomy intensified when interest rates were lowered after the default to stimulate the economy, rather than raised to prevent capital flight.

The government’s unorthodox economic management came under further scrutiny on Thursday when beef exports were suspended to combat inflation, despite dollar shortages.

“The government’s economic model is coming apart at the seams . . . They are trying to put the holdouts issue at stage centre to stop people from talking about what they really care about: not being able to pay their bills,” said Mr Germano, who says that although Ms Fernández has received a boost in support over her handling of the holdouts issue, it won’t last forever.

“She may be laughing now, but it will all end in tears,” he said.