ARGENTINA

SYSTEMATIC COUNTRY DIAGNOSTIC (P164150)

September 12, 2018

International Bank for Reconstruction and Development
Argentina, Paraguay and Uruguay Country Management Unit
Latin America and Caribbean Region

The International Finance Corporation (IFC)
Latin America and Caribbean Department

The Multilateral Investment Guarantee Agency (MIGA)
Latin America and Caribbean Department

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List of Abbreviations and acronyms

<table>
<thead>
<tr>
<th>Abbreviation</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>ALMP</td>
<td>Active labor market policies</td>
</tr>
<tr>
<td>AMBA</td>
<td>Metropolitan Area of Buenos Aires (Área Metropolitana de Buenos Aires)</td>
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<tr>
<td>ANSES</td>
<td>National Social Security Administration (Administración Nacional de la Seguridad Social)</td>
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<tr>
<td>AUH</td>
<td>Universal Child Allowance (Asignación Universal por Hijo)</td>
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<td>BCRA</td>
<td>Central Bank of the Republic of Argentina (Banco Central de la República Argentina)</td>
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<tr>
<td>CABA</td>
<td>Autonomous Federal Capital of Buenos Aires (Ciudad Autónoma de Buenos Aires)</td>
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<tr>
<td>CEDLAS</td>
<td>Centro de Estudios Distributivos, Laborales y Sociales</td>
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<tr>
<td>ECD</td>
<td>Early Childhood Development</td>
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<tr>
<td>EPH</td>
<td>Permanent Survey of Households (Encuesta Permanente de Hogares)</td>
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<tr>
<td>EPHC</td>
<td>Continuous Survey of Households (Encuesta Permanente de Hogares-Continua)</td>
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<td>EU</td>
<td>European Union</td>
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<td>FAO</td>
<td>Food and Agriculture Organization</td>
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<td>FTA</td>
<td>Free Trade Agreement</td>
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<td>GCI</td>
<td>Global Competitiveness Index</td>
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<tr>
<td>GDP</td>
<td>Gross Domestic Product</td>
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<td>GHG</td>
<td>Greenhouse Gases</td>
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<td>GFS</td>
<td>Government Finance Statistics</td>
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<td>GMO</td>
<td>Genetically modified</td>
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<td>GP</td>
<td>Global Practice, World Bank</td>
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<td>GSURR</td>
<td>Global Practice for Social, Urban and Rural Development</td>
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<td>GVCs</td>
<td>Global Value Chains</td>
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<td>IDB</td>
<td>Inter-American Development Bank</td>
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<td>IFC</td>
<td>International Finance Corporation</td>
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<td>ILO</td>
<td>International Labour Organization</td>
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<td>IMF</td>
<td>International Monetary Fund</td>
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<td>IPs</td>
<td>Indigenous Populations</td>
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<tr>
<td>INDEC</td>
<td>National Statistical and Census Institute (Instituto Nacional de Estadística y Censos)</td>
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<td>LAC</td>
<td>Latin American and Caribbean region</td>
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<td>MERCOSUR</td>
<td>El Mercado Común del Sur</td>
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<td>MSMEs</td>
<td>Micro, Small and Medium Sized Enterprises</td>
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<td>NAFTA</td>
<td>North American Free Trade Agreement</td>
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<td>New HICs</td>
<td>New High-Income Countries</td>
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<td>NGO</td>
<td>Non-governmental organization</td>
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<tr>
<td>NREL</td>
<td>National Renewable Energy Laboratory</td>
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<td>NTMs</td>
<td>Nontariff measures</td>
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<tr>
<td>O*Net</td>
<td>Occupational Information Network Database Information Network database</td>
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<tr>
<td>OECD</td>
<td>Organization for Economic Co-operation and Development</td>
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<td>PISA</td>
<td>Program for International Student Assessment, OECD</td>
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<td>PIT</td>
<td>Personal Income Tax</td>
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<td>PPP</td>
<td>Purchasing Power Parity</td>
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<td>PPPs</td>
<td>Public-Private Partnerships</td>
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<td>PUAM</td>
<td>Universal Pension for the Elderly (Pensión Universal para el Adulto Mayor)</td>
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<td>R&amp;D</td>
<td>Research and Development</td>
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<td>RAP</td>
<td>Political Action Network (Red de Acción Política)</td>
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<td>RC</td>
<td>Routine Cognitive</td>
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<td>RER</td>
<td>Real Exchange Rate</td>
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<td>SEDLAC</td>
<td>Socio-Economic Database for Latin America and the Caribbean</td>
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<td>SCD</td>
<td>Systematic Country Diagnostic</td>
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<tr>
<td>Acronym</td>
<td>Description</td>
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<td>SITC</td>
<td>Standard International Trade Classification</td>
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<td>SMEs</td>
<td>Small and Medium Enterprises</td>
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<td>STI</td>
<td>Science, Technology and Innovation</td>
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<td>TTL</td>
<td>Task Team Leader</td>
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<td>TFP</td>
<td>Total Factor Productivity</td>
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<td>Trapped MICs</td>
<td>Middle-Income Trapped Countries</td>
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<td>UK</td>
<td>United Kingdom</td>
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<td>U.S.</td>
<td>United States of America</td>
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<td>WBG</td>
<td>World Bank Group</td>
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<td>WDI</td>
<td>World Bank’s World Development Indicators</td>
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<td>WDR</td>
<td>World Development Report</td>
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<td>WEF</td>
<td>World Economic Forum</td>
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<td>WHO</td>
<td>World Health Organization</td>
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<td>WTO</td>
<td>World Trade Organization</td>
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<td>WWF</td>
<td>World Wildlife Fund</td>
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Acknowledgments

The Systematic Country Diagnosis for Argentina is the result of a team effort of the Argentina Country Team of the World Bank Group. Members from all Global Practices and the International Finance Corporation (IFC) contributed to the preparation of the document in a collaborative process, through a large number of substantive inputs, participation in consultations, advice and feedback. In addition, the team benefited greatly from conversations with authorities, partners and stakeholders, throughout the preparation of the document. The report was completed at the beginning of August 2018 amid the continued economic turmoil that has hit Argentina. The focus of the report is on medium- to longer-term development challenges in Argentina, rather than contemporaneous macroeconomic developments.

This report has been prepared by a team co-led by María Ana Lugo (Senior Economist, Global Practice, GPV04), Giovanni Ruta (Senior Environment Economist, GEN04), and Emily Sinnott (Lead Economist and Program Leader, LC7), under the guidance of Jesko Hentschel (Country Director, LC7). The core team included Ignacio Apella (Social Protection Economist, GSP04), Agustin Arakaki (Consultant, GPV04), Laura Calderón (Consultant, GEN04), Julián Folgar (Research Analyst, GMF04), Fernando Giuliano (Economist, GMF04), and Marco Larizza (Senior Public Sector Specialist, GG016). On the IFC side the team consists of: Luciana Harrington (Strategy Officer, CCECE), Zeinab Partow (Principal Country Economist, CCECE), and Valeria di Fiori (Operations Officer, CLAAR). The team relied on the contributions and support of many colleagues, country office staff and consultants, included but not limited to the list below. The team gratefully acknowledges the overall guidance of Oscar Calvo-Gonzalez (Practice Manager, GPV04), Valerie Hickey (Practice Manager, GEN04), Pablo Saavedra (Country Director, LCC1C), LC7 program leaders Carole Megevand and Rafael Rofman, as well as LCR Chief Economist Carlos Vegh (LCRCE). The team also benefited from insightful comments and suggestions of the peer reviewers: Marianne Fay (Chief Economist, GGSCE), Luis-Felipe López-Calva (Practice Manager, GPV03), David Rosenblatt (Manager, DECSO).

**System Country Diagnostic (SCD) extended team**

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<tbody>
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<tr>
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<td>Kelly Alderson</td>
</tr>
</tbody>
</table>
# Table of Contents

**Acknowledgments** ...........................................................................................................................................i

**Executive Summary** .................................................................................................................................. viii

- Setting the Stage ...............................................................................................................................................viii
  - What sets Argentina apart? .......................................................................................................................... xi
  - A history of economic and policy volatility ................................................................................................. xii
  - Recent growth and shared prosperity trends .............................................................................................. xv
- Pathway to shared prosperity .......................................................................................................................... xviii

**Chapter 1. Setting the Stage**.......................................................................................................................... 27

- Introduction ....................................................................................................................................................... 27
- Falling behind .................................................................................................................................................... 28
- Argentina’s defining characteristics ................................................................................................................. 32
- Convergence postponed ................................................................................................................................. 36
- The Challenge going forward ......................................................................................................................... 43
- Pathway to shared prosperity .......................................................................................................................... 45

**Chapter 2. Growth** ........................................................................................................................................... 48

- Drivers of economic growth .............................................................................................................................. 48
- Pathway 1: Putting in place the institutional and macroeconomic fundamentals for growth ....................... 53
  - Macroeconomic stability: moving beyond boom-bust cycles .................................................................... 53
  - Expenditure and revenue policies to support growth .................................................................................. 57
- Institutions for growth ..................................................................................................................................... 62
- Pathway 2: Open, outward-oriented development model .............................................................................. 67
  - Creating financial capital ............................................................................................................................... 67
  - Creating the infrastructure to support growth ......................................................................................... 70
  - Creating an economy open to trade, competition and investment ........................................................... 75
  - Enhancing the capacity of firms to benefit from expanded markets ......................................................... 81

**Chapter 3. Toward a more inclusive society** .......................................................................................................................... 88

- Recent trends in poverty and shared prosperity and challenges ahead .......................................................... 88
- Pathway 3: Releasing constraints to productive inclusion ............................................................................. 97

**Chapter 4: Sustainability and investing in natural capital** ................................................................................. 114

- Overview of challenges and institutional context .......................................................................................... 114
- The role of natural capital in Argentina’s economy ......................................................................................... 116
- Pathway 4: Investing in natural capital and ensuring environmental sustainability ........................................ 120

**Chapter 5. Priorities for a sustained and inclusive growth** .................................................................................... 135

- Prioritizing reforms for shared prosperity ....................................................................................................... 135
- Prioritization process ....................................................................................................................................... 136
Priorities.................................................................................................................................................. 136
Knowledge and analytical gaps............................................................................................................... 145
References.................................................................................................................................................. 146

Annexes ...................................................................................................................................................... 159
Annex I: Poverty measurement in Argentina.......................................................................................... 159
Annex II: Profile of the Poor and Bottom 40.......................................................................................... 160
Annex III: Selected WBG Analytical Work ............................................................................................ 162
Annex IV: Data diagnostics for WBG client countries.......................................................................... 164
Annex V: Consultations.......................................................................................................................... 166
List of Figures
Figure 1. Argentina’s GDP per capita as a percentage of the average of rich economies, 1900-2016 ..........28
Figure 2. Change in GDP vs. total wealth per capita, 1995-2014 ..........................................................28
Figure 3. Argentina’s GDP growth rate, in percent, 1950-2016 ............................................................29
Figure 4. Years in recession as a percentage of total years, 1950-2016 ...............................................30
Figure 5. Land per capita, 2014 .............................................................................................................32
Figure 6. Forest cover change 1990-2014, in percent ........................................................................32
Figure 7. The top 1 percent income shares in Argentina, and other new world countries, 1916-2006 ........33
Figure 8. Average real wages, 1940-2006 ..............................................................................................33
Figure 9. Subnational inequality: Standard deviation of regional per capita (log) GDP, circa 2010, in percentage ..........................................................34
Figure 10. Provincial revenues as percentage of total revenues, 2015 ..................................................35
Figure 11. Correlation between current account as a percentage of GDP and GDP growth, 1950-2016 ....37
Figure 12. Real exchange rate index, 1950-2016 ..................................................................................37
Figure 13. Fiscal balance, Argentina, 1960-2016, in percent of GDP ........................................................38
Figure 14. Correlation between public expenditure and GDP, 1960-2016 ..............................................38
Figure 15. Policy volatility and convergence with the U.S. GDP per capita, 1940-2010 .........................39
Figure 16. Poverty and inequality in Greater Buenos Aires, 1974-2016 ..............................................41
Figure 17. Life expectancy at birth (years), 1960-2015 ..........................................................................41
Figure 18. Income poverty rate, circa 2016 ..........................................................................................42
Figure 19. Non-monetary dimensions, circa 2015 ...............................................................................42
Figure 20. Growth decomposition by decade, annual averages, 1961-2016, in percent .....................44
Figure 21. Labor productivity annual average growth rate, 1961-2016, in percent .................................44
Figure 22. Argentina’s economic transition ............................................................................................46
Figure 23. Growth decomposition by demand component, period annual averages, 1998-2017, in percent 48
Figure 24. Growth contributions by factor of production, period annual averages, 1998-2015, in percent 48
Figure 25. Change in value added per worker and change in employment by sector, 2004-2016, in percent ..........................................................................................................................50
Figure 26. Offshore wealth, 2007, in percent of GDP ............................................................................51
Figure 27. Product fitness for 2000 and 2015 .........................................................................................51
Figure 28. Correlation between product fitness and GDP per capita, 1995-2014, in logs ......................51
Figure 29. GDP annual growth rate, by sector, 2016 and 2017, in percent ............................................53
Figure 30. Correlation between cyclical component of real government expenditure and real GDP, 1961-2016 .........................................................................................................................54
Figure 31. Fiscal Procyclicality by level of government, 1961-2016 .........................................................55
Figure 32. Fiscal Procyclicality by sub-component, Federal Government, 1961-2016 ..........................56
Figure 33. Fiscal Procyclicality by sub-components, Provincial Government, 1961-2016 ..................56
Figure 34. Real exchange rate depreciation, 2004-2008, in percent .....................................................57
Figure 35. Nominal exchange rate depreciation and inflation, 2004-2008, annual averages, in percent .57
Figure 36. Public expenditure, general government, 1961-2016, in percent of GDP .......................58
Figure 37. Total expenditure increase, 2007-2016 by component, in percent of GDP .......................58
Figure 38. Public spending comparison on selected items, in percent of GDP, 2015 ...........................59
Figure 39. Pension expenditure in percent of GDP, and share of population older than 65 years of age, circa 2015 ..........................................................................................................................59
Figure 40. Tax burden, 2016, in percent of GDP ....................................................................................60
Figure 41. Direct tax composition, 2016, in percent ..............................................................................60
Figure 42. Income threshold where single taxpayers start paying income tax, measured as a multiple of the average wage, 2016 .............................................................................................................60
Figure 43. Argentina: Fiscal balance, in percent of GDP, 2002-2016 ....................................................61
Figure 44. Debt to GDP, in percent, 2018-2023 .....................................................................................61
Figure 45. Average annual inflation rate in comparator countries since 1960, in percent .................62
Figure 46. Fiscal balance and inflation tax, ...........................................................................................................................................................................62
Figure 47. Consolidated Regulatory Governance Score, 2016 ...........................................................................................................................................64
Figure 48. Congress Capabilities Index, Average 1994-2013 ...........................................................................................................................................64
Figure 49. Judicial Independence Index, Average 2001-2013 ...........................................................................................................................................65
Figure 50. Regulatory Enforcement Index, 2016 .......................................................................................................................................................65
Figure 51. Argentina: Low capital market depth for its income level ..................................................................................................................................68
Figure 52. Argentina: Banking soundness indicators ..................................................................................................................................................70
Figure 53. World Economic Forum’s Global Competitiveness Index Infrastructure pillar ranking, 2017 ............................................................................................................................................71
Figure 54. World Economic Forum’s Global Competitiveness Index quality of electricity ranking, 2007 and 2017 .....................................................................................................................................................71
Figure 55. Infrastructure investment as a percentage of GDP in Argentina by type, 2008-2015 ........................................................................................................................................................72
Figure 56. Infrastructure investment as percentage of GDP in regional peers, 2014 ............................................................................................................................................................................72
Figure 57. Logistics Performance Index, 2007 and 2016 .......................................................................................................................................................73
Figure 58. Trade openness (trade as a share of GDP), in percent, Argentina and select countries, 2016 .....................................................................................................................................................75
Figure 59. Export destinations, in percent of total exports, 1995-2016 .................................................................................................................................................76
Figure 60. Global value chain participation: Argentina vs. comparator countries, 2011 ........................................................................................................................................................................77
Figure 61. Inward FDI stock, in percent of GDP, 2016 .......................................................................................................................................................78
Figure 62. Sectoral composition of FDI inflows in Argentina, 2010-2015 .................................................................................................................................................78
Figure 63. FDI complexity and economic complexity index (ECI) in 2014: Argentina vs comparator countries ........................................................................................................................................................78
Figure 64. Product Market Regulation indicator, Argentina vs. comparator countries, 2013-2016 .....................................................................................................................................................79
Figure 65. Logistics cost index (2003=100), 2003-2014 .......................................................................................................................................................79
Figure 66. Management practices and impact of R&D on innovation, 2015 .......................................................................................................................................................84
Figure 67. Poverty and inequality in urban Argentina, 31 main cities, 2004-2016 ...........................................................................................................................................................88
Figure 68. Urban poverty (US$5.5 a day) by region, 31 main cities, 2004-2016 ...........................................................................................................................................................88
Figure 69. Annualized income growth for the average and the poorest 40 percent, Latin American Countries .............................................................................................................................................................89
Figure 70. Decomposition of per capita income growth per decile, by source of income ........................................................................................................................................................90
Figure 71. Labor market performance, 2004-2016 .................................................................................................................................................................91
Figure 72. Access to services, living context and school attendance, and level of education, 2016 ........................................................................................................................................................92
Figure 73. Maternal mortality (per 10,000 births) across provinces, 2013 ........................................................................................................................................................92
Figure 74. Informality rate among wage-employees, second semester 2016 .................................................................................................................................................95
Figure 75. Gender monthly labor income gap, contribution of characteristics and coefficients ..................................................................................................................................................95
Figure 76. Share of youth (15-24) not in employment, education or training, circa 2016 ........................................................................................................................................................95
Figure 77. Private sector industries with low labor productivity, share of the Gross Value Added at basic prices (GVAbp) and jobs creation, 2016 ........................................................................................................................................................95
Figure 78. Intensity of the tasks performed in a job, Argentina, 1998-2015 ........................................................................................................................................................97
Figure 79. Intensity of the task performed across deciles of hourly wage, Argentina, 2015 ........................................................................................................................................................97
Figure 80. Test scores in mathematics, 25th, 50th and 75th percentiles, selected countries (OECD average in shaded area), Program for International Student Assessment 2012 (PISA) ........................................................................................................................................................99
Figure 81. Share of children who attend school, by age, 2016 .................................................................................................................................................99
Figure 82. Share of students with below basic knowledge in math, by socioeconomic status, 2016 ........................................................................................................................................................99
Figure 83. Proportion of NDC related deaths under age 70, in percent’, 2010 .......................................................................................................................................................101
Figure 84. Risk factors of non-communicable diseases, Argentina. Circa 2015 .......................................................................................................................................................101
Figure 85. Account at a financial institution, percent of age 15+, 2017 ........................................................................................................................................................103
Figure 86. Debt ratios and kind of credit contribution, by annual remuneration level, July 2015 to June 2016 .......................................................................................................................................................103
Figure 87. Sprawl and agglomeration economies ........................................................................................................................................................105
Figure 88. Access to sewerage network: core urban areas vs. periphery, 2013 ........................................................................................................................................................105
Figure 89. Redistribution: reduction in the Gini coefficient through taxes and transfers, latest available year ..........................................................................................................................................................108
Figure 90. National poverty incidence, in percent, by age group, before and after transfer program .......110
Figure 91. Public pension expenditure relative to peers, in percent of GDP .............................................. 110
Figure 92. Ratio of net per capita public transfers between older adults and children .......................... 110
Figure 93. Projection of total expenditure on retirement benefits and pensions, 2010-2100, in percent of GDP ........................................................................................................................................ 110
Figure 94. Environmental Performance Index score, 2018 ...................................................................... 115
Figure 95. Argentina’s ranking across dimensions of Environmental Performance Index, 2018 .............. 115
Figure 96. Average annual forest vs. cropland and pastureland capital growth, 1995-2014 ................. 121
Figure 97. Forest cover, forest loss (1992-2015), and poverty by province (2010) ..................................... 122
Figure 98. Marine protected areas as percent of territorial waters (1990, 2000, 2014) ......................... 125
Figure 99. Average annual change in produced capital and natural capital, 1995-2014 ......................... 127
Figure 100. Matrix of vulnerability to climate change risks and readiness to act, 2016 ........................... 129
Figure 101. Matrix of capacity to act against climate risks and the economic readiness to accept investments for implementation. evolution between 1995-2014 ........................................................................................................ 129
Figure 102. Prioritization process ........................................................................................................... 136

List of Tables
Table 1. Argentina’s economic cycles, 1950-2016 ......................................................................................29
Table 2. Large depreciation episodes, 1950-2016, in percent ..................................................................37
Table 3. Economic policy making: an history of policy reversal ...............................................................39
Table 4. Simulation of per capita real income falling and increasing on official poverty and extreme poverty rates, 2017, second semester ..........................................................................................43
Table 5. Evolution of income per capita, 1870-1990 .............................................................................116
Table 6. Argentina’s world share and world ranking in production and exports of selected agricultural commodities, 2013-2016 ..................................................................................................................118
Table 7. Heat map with filters .................................................................................................................140
Table 8. Data and knowledge gaps ..........................................................................................................145

Boxes
Box 1. Middle income trap from above? Argentina and comparator countries ........................................31
Box 2. Vulnerability to shocks: potential impact on poverty rates ...........................................................43
Box 3. Summary of key policy shifts and structural reforms in 2016-2018 ..............................................47
Box 4. The notebooks (cuadernos) corruption scandal ...........................................................................67
Box 5. Argentine Wine: A case of export emergence .............................................................................84
Box 6. More than a third of Argentines are excluded from poverty statistics .........................................91
Box 7. Ni una menos ..................................................................................................................................112
Box 8. The potential of family farming for inclusive growth ..................................................................119
Box 9. Oil and Gas, and environmental compliance ...............................................................................133
Box 10. Setting incentives to promote inter-governmental cooperation: the Australian experience ......139
Box 11. SCD consultation process ........................................................................................................143
Setting the Stage

1. This report on the medium-term agenda to ensure growth and shared prosperity in Argentina comes at a time when the country is embarking on deepening structural reforms, while dealing with recent sudden financial market pressures that emerged in April 2018. The current Government came into office at end-2015 facing a difficult legacy of macroeconomic and structural imbalances. Significant progress has made since then by the administration on important reforms. However, continued macroeconomic imbalances—with a primary deficit of 4.2 percent of Gross Domestic Product (GDP) in 2017 and inflation of 24.8 percent at end-2017—combined with high external financing needs made Argentina vulnerable to increased emerging market turmoil at end-April, when the country experienced a large depreciation of the peso and a rise in country risk. In response to this, the Government requested an emergency credit line with the IMF in early May and accelerated some key reforms. The report was completed at the beginning of August 2018 amid the continued economic turmoil that has hit Argentina. The focus of the report is on medium- to longer-term development challenges in Argentina, rather than contemporaneous macroeconomic developments. This includes a substantial focus on macroeconomic policies to set in place the foundations for medium-term growth and shared prosperity by boosting jobs and productivity. Achieving macroeconomic stabilization is a precondition for creating a healthy and vibrant economy. But deep reforms in areas varying from enhancing domestic competition to developing capital markets to significantly improving when it comes to education outcomes, are necessary to ensure that the population benefits from a resurging private sector and renewed connection with the global economy. Learning from other countries experience in implementing structural reforms and gradually opening up their economies, like the Australian reforms from the early 1980s and Sweden’s in the 1990s, this is a long-term agenda and a strong societal consensus will need to develop to support the changes for reforms to endure. Not to be underestimated is the importance of ensuring a strong safety net to support those that may be hit by structural changes in the economy.

2. Argentina is rich in natural capital assets and has a historically strong middle class. Along with its 2.8 million square kilometers, its extraordinary fertile land makes Argentina one of the largest agricultural producers in the world. The beef and soy sectors apply among the world’s most modern practices and are leaders in breeding, agricultural machinery, and innovation. Argentina has vast natural resources in energy, with world class wind and solar potential, with the second highest shale gas and forth highest shale oil reserves in the world. In addition, Argentina has significant opportunities in some manufacturing subsectors and high-tech, innovative services. Argentina has a historically large and strong middle class. Social indicators are mostly good, and society deeply values education and knowledge as a means for potential mobility and status. Noted successes in research and innovation (four of the six most successful Latin American tech unicorn companies, with a value of over US$1 billion, are Argentine) makes the country a potential destination for high value-added industries.

3. Nonetheless, compared to its peers, Argentina’s long-run economic performance has been disappointing, impacting on the reduction of poverty and the increase in bottom incomes. Average long-run economic growth in Argentina has been only 2.7 percent—about half that of high performing countries in the region and less than a third of emerging countries in Asia. As a result, the country has consistently lost ground relative to rich economies, with a GDP per capita similar to the average of a group

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1 Shared prosperity requires that economic growth results in a sustainable increase in the living standards of the less well-off. The World Bank Group monitors progress in shared prosperity using the income growth of the population in the bottom 40 percent of the income distribution.

2 See Mander, 2016.
of rich economies by the beginning of the twentieth century, to only 38 percent of these rich countries’ economic output per person today (see Figure E 1). Given its secular decline from relatively high levels of income per capita, Argentina can be referred as a unique country that did not grow into, but fell into middle-income status, and remained there. Furthermore, 40 percent of its population is today still vulnerable to falling into poverty and growth has come at the expense of environmental sustainability (with 12 percent of forest loss between 2001 and 2014—double the world average). The lack of job creation in Argentina in recent years limited the significant progress made on poverty and shared prosperity in the previous decade, as the labor market deteriorated significantly since 2012.

Figure E 1. Argentina’s long decline from the top

Argentina’s GDP per capita as a percentage of the average of rich economies, 1950-2016


Note: Rich economies are the UK, the U.S., Norway, Switzerland, Australia, Denmark, Sweden, Germany, Canada and Netherlands.

4. The main explanation for this poor performance is Argentina’s unusually volatile macroeconomic environment, reflected in large swings in economic activity. During the period 1950-2016, Argentina has gone through 14 recessions (one or more consecutive years of negative growth), with an average duration of 1.6 years. As a result, the country spent roughly one-third of the time since 1950 in recession. This is the most time of any country in the world except the Democratic Republic of the Congo (Figure E 2), ranking with fragile states like Iraq and Syria and highly hydrocarbon dependent countries. Uruguay, a neighboring country affected by Argentina’s cycles and arguably subject to similar external shocks, spent less than one-fifth of the time in recession. Recessions not only occur often in Argentina, but they are deep. In an average recession cycle, Argentina’s GDP contracts 3.5 percent per year. The result is a relatively weak growth performance: Average long-run economic growth in Argentina has been only 2.7 percent, below that of its regional peers (3.7 percent), new high-income countries (3.9 percent, see Box 1 in the main report for a definition of this group), and OECD countries (3.2 percent).

5. Institutions have played a central role in shaping the policy-making process in Argentina and—consequently—the volatility in economic policymaking that has emerged. This report argues that economic policies are only the ‘proximate’ reason for Argentina’s decline in income relative to advanced economies. Economic policies are influenced by the quality of the institutions as the ‘rules of the game’ under which political and social actors interact. The way institutions function in Argentina has historically undermined the incentives to establish, enforce and sustain intertemporal agreements on the content and direction of economic policies. Specifically, there is a history of a lack of success of major political institutions—including the Executive, the Legislature, the Judiciary, and the state bureaucracy—in enforcing credible commitment and fostering cooperative behavior among actors that leads to policies that are either
too volatile (reflecting political opportunism and short-term calculations among actors—*cortoplacismo*) or too rigid (reflecting non-cooperative behavior and distrust among actors, forcing them to ex-ante rigid solutions to mitigate opportunistic behavior). These institutional features, which can be traced back to constitutional and electoral rules, as well as to a history of political instability, have limited the time horizon of policy decision makers, making longer-term structural reform programs difficult to get off the ground and sustain. Over the past years, important institutional reforms have commenced and an open dialogue about the need to foster and strengthen core institutions is taking place. The urgency to reform core institutions; foster functioning checks-and-balances between the legislative, executive and judiciary; and to ensure accountability of those holding office has recently been laid open by the widening *notebook (cuadernos)* scandal, involving fraud and corruption charges of public officials and a large number of private entrepreneurs.

**Figure E 2. Since 1950, Argentina spent one third of the time in recession**

![Graph showing years in recession as percentage of total years, 1950-2016.](image)

*Source:* Calculated based on data from the Conference Board’s Total Economy Database.

*Note:* The graph shows the number of years in recession as a percentage of total years, 1950-2016.

6. **Distributive conflicts between the federal and the provincial governments have been at the heart of Argentina’s political history, underlying the country’s structural challenges.** The stark economic inequalities among provinces and the structural features of the Argentina’s federal system imply that most provinces are highly dependent from the national government to finance their expenditures. In turn, presidents need to secure votes in Congress to implement economic policies. As a result, the policymaking process can be characterized as ‘deals’ or exchanges’ between president and governors whereby governors grant political support in exchange for fiscal transfers. Historically, these political economy dynamics have translated into a fiscal transfer system that tends to favor resource poor, but vote-rich regions to strengthen the national ruling coalitions, undermining efficiency in resource allocations. They have also weakened the functional role of the Congress as an institutionalized arena to discuss and define public policies, and created incentives for short-term policies that are often fiscally unsustainable and associated with long-term economic costs. Recent developments are encouraging as to a more fruitful dynamic emerging. The Fiscal Pact agreed between the National Government and 23 out of 24 provinces in November 2017 is an important step in coordinating fiscal policy at the national and provincial levels, and
the pledge to contain recurrent spending and public employment growth at the provincial level is core to avoiding a worsening of fiscal imbalances of the provinces in a time of high fiscal consolidation pressures.

What sets Argentina apart?

7. **Natural resource abundance.** Argentina is rich in natural capital, but underinvestment is holding back its potential. With 6.24 hectares per person, the country has one of the largest land endowments per capita in the world. Water is also abundant at the national level, though with wide regional variations. A favorable temperate climate makes Argentina’s land fertile for rainfed crop production and cattle. Argentina has one of the largest continental shelves and is rich in marine and coastal resources. It is also rich in renewable energy resources, including hydro, wind, solar and biofuels, which are largely untapped. Mineral and renewable resources are likely to play a growing role in the country’s economic future. Finally, natural diversity and landscapes attract international visitors, building a strong tourism sector that importantly contributes to GDP and job creation.

8. **An historically large middle class with unmet high-income country aspirations.** Between 1880 and 1915, the country benefited from an abundance of fertile land and the expansion of world trade, and land owners became increasingly wealthy, benefiting from land policy that facilitated land concentration. The massive influx of immigrants, especially from Europe, dramatically changed the social structure of the country. By 1914, a third of Argentines were foreign immigrants, a large share of which had non-manual work. Favorable international trade conditions after the Second World War, combined with industrialization and redistributive policies led to a real income increase and a rapid decline in inequality (the income share of the top 1 percent). By the mid-twentieth century, Argentina had a strong and educated middle class, at the time that the economy was in full employment, and many could enjoy a certain standard of living unheard before. These benign economic conditions for workers and the setting up of a welfare state, led to the expansion of middle class aspirations among this newly-enriched working class. In a context of full employment, the construction of a social welfare state in which most contributed, ensured health care and generous pensions for an increasing proportion of the population.

**Figure E.3. Argentina’s regions have very heterogeneous income levels**

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9. **An unequal federation marked by significant vertical fiscal imbalances.** Argentina is a very unequal federation, with areas as rich as developed nations, and provinces as poor as low middle-income countries. Argentina is a federal country comprising 23 provinces and the autonomous federal capital of
Buenos Aires (Ciudad Autónoma de Buenos Aires, CABA for its Spanish acronym). Heterogeneity across provinces in terms of income is very large. Figure E 3 compares the standard deviation of (log) GDP per capita across subnational governments. Argentina is a clear outlier among comparator countries. Many important expenditure responsibilities lie at the provincial level, such as basic health-care and education, while revenues are mostly collected at the national level. To help fund those expenditures, a portion of revenues is redistributed back to provinces through an automatic revenue-sharing scheme (“coparticipación”), and by discretionary transfers by the executive branch. While some degree of mismatch between expenditure and collection responsibilities is inevitable to guarantee the provision of relatively homogeneous services, in Argentina this is very large, with a sizable discretionary component. The need to provide homogeneous services across heterogeneous provinces generates perverse expenditure and revenue collection incentives, resulting in substantial fiscal challenges.

A history of economic and policy volatility

10. **Taken together, these three features of Argentina have combined in deleterious ways resulting in a long-term disappointing economic performance.** The high-income aspirations of a country with middle-class aspirations and the short-term considerations (cortoplacismo) of the political system combine to create enormous pressures to spend during booms. Often it is the booming agricultural sector that provides the high rents to the state to fuel these fiscal expansions. The large vertical imbalances of the federal system and the tendency of political and economic actors to reach agreements through short-term “deals” has undermined the ability of public institutions to enforce long-term commitment to reforms and to sustainable policies to use of the country’s rich natural assets to harness growth. This has frequently led to highly procyclical economic policies that amplify booms and busts. Successive crises have deepened this dynamic: growing impoverishment during downturns leads to high pressures to spend when economic conditions improve, and actors have over time lost their trust in the ability of the economy to deliver long-term stable growth, reducing their incentive to look beyond short-term gains. As a result, Argentina has failed to keep up with rich economies, and experienced an unusually volatile macroeconomic environment, reflected in large swings in economic activity.

11. **One of the main explanations behind Argentina’s disappointing macroeconomic performance lies its tendency to “live beyond its means”, an endogenous driver of its boom and bust cycles.** The country’s social demands and political pressures yield an equilibrium characterized by excessive aggregate spending (i.e. aggregate dissaving). The dissaving of the country as a whole is financed with savings from the rest of the world, reflected in a current account deficit. The tendency to overspend grows wider in booms, with procyclical policies that result in consumption and investment (both public and private) growing faster than income. On the external sector this is reflected in an increase in imports through two channels. First, imports rise due to an increase in the demand for imported consumption goods and production inputs. Second, a growing aggregate demand puts pressure on the market for non-tradable goods, increasing their relative price, a real appreciation that further increases imports. Since exports—mainly based on natural resources and held back by an extractive fiscal regime—usually fail to keep up with the rapid growth of imports, the current account deteriorates. This process usually comes to an end when the rest of the world refuses to continue to finance Argentina’s current account deficit, and usually results in a sharp depreciation of the currency, a spike of inflation, a large drop in real wages, and a deep recession that reverts the current account wiping out a large portion of the welfare gains in the expansion period. These boom and bust episodes in turn result in both underinvestment in natural capital (which takes time to reap rewards) and in extractive policies to generate short-term liquidity (generating the liquidation of assets and even illegal extraction). These cycles, sometimes referred to as “stop-and-go cycles” are illustrated in Figure E 4 showing

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\(^3\) CABA, the richest district of the country, has a GDP per capita of US$28,358, while Formosa, the poorest province, has a GDP per capita of US$3,704.
the correlation between current account balance and GDP growth. As the economy grows and the current account deteriorates, the external restriction starts to bind, and usually results in a sharp depreciation of the real exchange rate (RER). After a period of appreciation, the RER usually sharply depreciates, as shown by the spikes in Figure E 5. These large depreciation episodes triggered large contractions in economic activity. Defining large depreciation episodes as those where the exchange rate depreciates in one year by more than one standard deviation, there were five such episodes since 1950, that resulted in contractions in economic activity, usually large, with a decline on average of 5 percent per episode.

Figure E 4. Correlation between current account as a percentage of GDP and GDP growth

Sources: Data from Ferreres, Instituto Nacional de Estadística y Censos (INDEC), Central Bank of the Republic of Argentina (BCRA).
Notes: Each dot is a period of consecutive growth or contraction of economic activity, in percentage (x-axis), and the corresponding change in the current account balance, in percentage points of GDP (y-axis), all expressed in annual averages.

Figure E 5. Real exchange rate index

Source: BCRA.
Notes: A real depreciation of the peso is an increase in the index

12. Institutionally, these cycles are reflected in the large swings in economic policy throughout the country’s history. Among some of the most significant in the last quarter century: The country moved from a very rigid exchange rate regime (currency board established in 1991) to a managed float, then a dual exchange rate regime and has now a flexible exchange rate. Trade was to be gradually opened when Mercado Común del Sur (Mercosur) was created in 1991, but the strategy was left behind and reversed to the extent that in the 2000s an increased number of goods over time came to be subject to import controls. The privatization of public utilities in the 1990s, turned to nationalizations from the mid-2000s onwards and is now replaced by a focus on Public-Private Partnerships (PPPs). Argentina has moved from a “mostly free” economy in 1995 to a ‘mostly unfree’ one on 2017 (Index of Economic Freedom)—a situation that the aforementioned economic reforms are aiming to rectify by reducing the constraints to economic activity. Tax legislation has been enacted or modified over 80 times since 1988. Fiscal federal rules have been changed 14 times in the same period, and budgetary rules have been altered 16 times between 1992 and

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4 For an historical account of stop-and-go cycles, see for example, Diaz Alejandro (1970), or the more recent Gerchunoff and Llach (2007), Heymann (2007), Albrieu and Fanelli (2008), Gerchunoff and Rapetti (2016).
5 This does not include the most recent exchange rate depreciation episode in 2018.
6 The Index covers 12 freedoms, ranging from property rights to financial freedom, in 186 countries. According to the Index of Economic Freedom (2017), Argentina ranks 156 out of 186 countries.
2008. Historically, policy volatility has typified Argentina for longer than the last quarter of a century. Using a measure of policy stability based on presidential speeches during 1940-2016, Argentina and Venezuela are the countries that come out with the lowest policy stability using this measure, and in addition were the countries that most diverged in economic output from the U.S. over 1940-2010. Given this history, commentators today focus on the expectation that there is strong possibility that the current direction of economic policy may be reversed in Argentina if political power shifts.

13. Recurrent crises and successive policy swings resulted in worsening welfare conditions from the mid-1970s to early 2000s. Slow and unstable growth, deep political conflict, sweeping trade liberalization and labor repression in the mid-to-end seventies were associated with increasing poverty and inequality (Figure E 6). The hyperinflation, real depreciation and economic contraction of the 1980s, resulted in real wages declined even more, and rising labor informality, leading to rising levels of poverty. The following decade, while the economy was growing and inflation was under control, the sudden liberalization of trade along with an appreciated RER led to a rise in unemployment and informality, especially among unskilled workers, which in the absence of wide compensatory social protection programs and weak labor institutions led to a more unequal distribution of incomes and an increasingly segmented society between the have and have-not. This situation worsened toward the end of the decade, when a recession finally led to the end of the convertibility regime in 2001/02, accelerated inflation and poverty reached its highest level in Argentine history. After this deep crisis, employment conditions ameliorated, particularly for the less qualified. However, as macroeconomic unbalances accumulated, labor market improvements slowed and poverty stagnated.

![Figure E 6. Recurrent crises worsened welfare conditions since the 1970s](image)

**Source:** Data from Socio-Economic Database for Latin America and the Caribbean, SEDLAC (CEDLAS and World Bank), based on EPHC (Encuesta Permanente de Hogares-Continua).

14. The successive economic crises were also reflected in non-economic aspects of well-being. Life expectancy improvements slowed, diverging from New high-income countries (HICs) and OECD countries.

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7 Bonvecchi, 2010.
9 Altimir, 2001; Gasparini and Cruces, 2009.
11 Cicowicz, 2002; Galiani and Sanguinetti, 2003; Gasparini and Lustig, 2011.
ARGENTINA
Systematic Country Diagnostic

trends and, after thirty years, instead came closer to the performance of regional peers. The quality of Argentina’s education system, once seen as the top performer in Latin America, has eroded and converged to the median in the region. For instance, Argentina placed second in reading scores among third graders in Latin American and Caribbean Region (LAC) at the end of the 1990s (in UNESCO’s first regionally-comparable measurement), but fell to the LAC average in the latest round.\textsuperscript{12}

**Recent growth and shared prosperity trends**

15. The aftermath of the 2001/2002 crisis provided an opportunity to address the country’s recurrent macroeconomic imbalances and set the basis for long-term growth. The collapse of the Convertibility Regime and default on foreign obligations resulted in a massive real depreciation of the peso, a sizeable output gap, low wages, and a large fiscal surplus. In a context of expanding world demand and increasing commodity prices, the Argentine economy recovered vigorously, growing 5.9 percent, on average, between 2003 and 2011.\textsuperscript{13} But this was further fueled by expansionary fiscal and monetary policies to support high levels of private consumption (Figure E 7). The continued expansion of aggregate demand was met by increased intensity in the use of labor and capital, and by some productivity gains, mostly explained by a recovery from the large fall in 1998-2002 (Figure E 8).

16. By 2011, the demand-driven growth strategy showed signs of exhaustion, with macroeconomic imbalances becoming self-evident. General government expenditures had increased at an unprecedented pace, growing by over 11 percentage points of GDP between 2004 and 2011 to fuel mostly current expenditures on subsidies, pensions and wages. Increased tax pressure failed to keep up with expenditures, leading to a rapid deterioration in the fiscal position that turned a 3.3 percent surplus in 2004 to a 7.8 percent deficit in 2016. Growing fiscal imbalances put pressure on the RER and current account, which moved to deficit for the first time in almost a decade. Especially after 2011, to tackle external imbalances, the government turned to increasingly protectionist policies such as quantitative restrictions on foreign trade and foreign exchange markets, hurting productivity.

17. Macroeconomic imbalances grew wider in the years after 2011, following the deepening of the policies that generated them in the first place. In 2011-2015, private job creation almost stalled. Government expenditure continued to grow way beyond historical records, productivity collapsed, and the current account deficit widened. The lack of access to international credit markets translated into a growing monetization of fiscal deficits, which further fueled inflation. The economy thus entered an annual cycle of recessions and expansions, with real GDP a mere 2.5 percent higher in 2017 than in 2011, a fall if measured in per capita terms.

\textsuperscript{12}Cassasus et.al, 1998, 2014.
\textsuperscript{13}Geometric average, including the 2009 recession due to the international financial crisis.
With increasingly protectionist policies and a continuous real appreciation of the peso, the tradable sectors’ share of GDP fell. Export taxes, high import tariffs, low competition, discreitional import licenses, and quotas in currency markets, combined to reduce the share of tradable sectors in output, despite favorable commodity prices and external conditions. Industries that produce goods, such as agriculture or manufacturing, grew by less than half the rate of the service sectors in the 2004-2016 period (25 versus 57 percent). As a result, the share of goods-producing sectors in GDP (at producer prices) decreased by 12 percentage points from 44 to 32 percent. The share of services grew from 56 to 68 percent in the same period.14

The expansion of non-tradable sectors resulted in a misallocation of employment to low-productivity activities. High-growth sectors since 2004 are mostly non-tradable, such as construction, health services, or public administration. This is due to the continuous RER appreciation but also due to deliberate policies to protect some sectors perceived as being major contributors to job creation, especially for low-skilled workers. These high-growth sectors have also experienced low productivity growth, a sign that productivity in the high-employment growth sectors has failed to catch up with the influx of workers. Unless those sectors had relatively high productivity to begin with, which is not the case,15 this points to a misallocation of employment to low productive uses. The misallocation is a source and a result of low aggregate growth. Low growth results in low job creation, which in a context of a growing labor force (demographic bonus) leads to some sectors needing to absorb the growing labor force, typically public administration or public education. This vicious cycle generated a trap of low productivity, low job creation, and growing labor misallocation.

The shared prosperity process in 2004-2011 was mainly driven by the recovery in labor incomes (Figure E 9). Family incomes grew largely due to the positive performance of labor income, particularly among the poorest households, recovering from the crisis as well as a continued job creation after 2007. During this period, employment grew at 2.2 percent rate per year, driven by wage-earners primarily in large but also small firms. This increase in employment and shrinking of the skill wage gap is

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14 Shares in current prices. In constant 2004 prices, the share of the service sector increased 5 percentage points.
15 The sectors with highest value added per worker in 2004 were mining and oil, fishery, and financial intermediation, in that order.
associated with the commodity boom which increased demand for low skill workers,\textsuperscript{16} in addition to the recovery of idle capacity right after the crisis, and a consumption growth model with a macroeconomic scheme which favored national firms.\textsuperscript{17} Government transfers became especially important for families in the lower deciles and contributed to the reduction of extreme poverty.\textsuperscript{18} Pensions were an essential source of additional family income—in particular, among the vulnerable—due to a pension fund moratorium, which led to a coverage rate doubling among elderly in the bottom quintile from 40 to 80 percent.\textsuperscript{19} In addition, the phasing out of the Jefas y Jefes de Hogar Desocupados program (launched to address the 2001/02 crisis) was reversed with the creation of the universal family allowance program (Asignación Universal por Hijo, AUH) in 2010, reaching 15 percent of households by 2016.

Figure E 9. Shared prosperity over 2004-2011 was mainly driven by the recovery in labor incomes

Figure E 10. Over 2011-2016, family incomes stagnated, due to a contraction in labor incomes compensated only partially by pensions and public transfers

Decomposition of per capita income growth per decile, by source of income

2004-2011

2011-2016

Source: Data from SEDLAC (El Centro de Estudios Distributivos, Laborales y Sociales (CEDLAS) and World Bank), based on Argentina's Continuous Permanent Household Survey (Encuesta Permanente de Hogares-Continua, EPHC).

21. Over 2011-2016, family incomes across the whole distribution remained stagnant, due primarily to a contraction in labor incomes, compensated only partially by pensions and public transfers (Figure E 9). The meagre 1.1 annual employment creation was driven mainly by public employment and self-employment, whereas wage employment in large firms remain almost at the same level. This slowdown in job creation reflects the limitations of a demand-driven development strategy, in a context of less favorable terms of trade than in the previous years, which resulted in the decline in labor productivity. Manufacturing contracted by 6 percent between 2011 and 2016, and the main employment gains came from the expansion of services (including the public sector) and commerce. Rising inflation also reduced the real value of wages (8.7 percent in the five years over 2011-2016), with the largest losses seen among self-employed and small-firm wage employees.

\textsuperscript{16} Fernandez and Messina, 2017; Messina and da Silva, 2017.
\textsuperscript{17} Beccaria et al, 2005.
\textsuperscript{18} Bustos and Villafañe, 2011; Salvia et al., 2015.
\textsuperscript{19} Rofman and Olivieri, 2012; Rofman et al., 2015.
22. Despite improvements in the past 15 years, Argentina faces significant challenges in terms of poverty and shared prosperity. According to official estimations, 30.3 percent of Argentines living in urban areas are poor and 6.1 percent are unable to meet basic food needs (2016, second semester). Measured at US$5.5 per capita per day in 2011 PPP (the upper-middle income country poverty line), the poverty rate in Argentina is around a third of the average level in Latin America. However, it is still higher than in the New HICs and OECD countries (fifty percent and almost two and a half times, respectively). Today, two million people live in informal settlements lacking property rights and basic services, which contrasts with the emergence of enclosed neighborhoods, catering to the upper-middle income class and the rich. The country has reached high levels in access to improved water, and educational attainment, but is still far from the OECD standards in terms of infant mortality, the under-five mortality rate, and life expectancy. In addition, access to basic services such as education, health and piped water or sewerage networks varies largely across provinces and across economic background. With a third of jobs being informal, economic opportunities are limited for youth – particularly among young women with low levels of education.

Pathway to shared prosperity

23. The development model that Argentina needs to move to centers on achieving sustained growth by opening up the economy and putting in place the conditions for private sector-led growth. The transition to new sources of growth for development in Argentina then involves a large and wide-ranging set of policy reforms (see Figure E 11 for an illustration of the transition needed). The government has already made progress along several of the areas identified (see Box E 1 for further details). These policy reforms can be grouped along four pathways where progress is critical for sustainable growth and an expansion of shared prosperity. Without sound macroeconomic management that brings price stability and a fiscally sustainable path, the transition to a new development model will flounder: Pathway 1 concerns putting in place these fundamentals for growth. Economic growth in Argentina has come to rely on domestic demand and largely on the expansion of government spending. The country has begun the move to a more open, outward-oriented development model. Pathway 2 looks at the supporting policies that are necessary. Low investment, very undeveloped capital markets and large physical investment needs have to be tackled. Reducing barriers to trade is only part of the story: the economy has to open up to domestic and international competition, and the highly-concentrated market power that some firms enjoy has to be reduced. For success, a larger group of firms will have to build the capacity to export and compete in a more competitive domestic market. Chapter 2 of the report describes Pathways 1 and 2.

24. Argentina has begun to implement this reform agenda to transform its economy, while dealing with the unwinding of macroeconomic imbalances and preventing a rise in poverty due to the transition. In December 2015, the Government faced the challenge of large macroeconomic imbalances, substantial distortions to economic activity, and a weakened institutional framework: large fiscal deficits, monetization of the fiscal deficit, and high inflation, were accompanied by price controls, large and regressive subsidies, trade restrictions, and the rationing of foreign currency. Credit and capital markets were extremely thin, and investment low. Reforms were put in place to eliminate foreign exchange controls and move to a flexible exchange rate regime, to establish an inflation-targeting framework for monetary policy, to gradually reduce energy and transport subsidies, to regularize relations with creditors, and to improve official statistics. Structural reforms have also been put in place to strengthen productivity and competitiveness by removing distortions holding back private sector-led growth, including reducing export taxes and easing import controls, improving the institutional framework for competition and capital markets, launching an ambitious infrastructure investment program to be financed by Public-Private Partnerships (PPPs), and reducing the costs of doing business. At the same time, there has been a focus on strengthening the legal framework to fight corruption and increase public sector transparency – which will now need to be tackled with higher urgency given the notebook scandal revelations about a widespread fraud and corruption scandal in the adjudication of public works programs (see Box E 1 for further details on the reforms put in place over 2016-2018).
Box E 1. Summary of key policy shifts and structural reforms in 2016-2018

Normalization of International Relations


• After 15 years, Argentina returned to international capital markets with the largest single bond issuance in history for an emerging country (April 2016).

Main Reforms

• Monetary Policy: The Central Bank formally adopted an inflation-targeting regime with a floating exchange rate. In addition, it committed to gradually decrease financial assistance to the central government.

• Statistics: Since January 2016, the credibility of the National Statistical System was restored; as a result the IMF lifted its Declaration of Censure on Argentine official statistics (November 2016).

• Export and imports: Export taxes were eliminated, with the exception for soybeans, which were reduced and for which the Government announced a scheduled further reduction. An imports administration system replaced the mostly discretional licensing regime in place until 2015. Foreign exchange controls were lifted after four years.

• Subsidies: Energy, water and transport subsidies were reduced while keeping a social tariff for low income users in water and transport and creating a social tariff for residential electricity and natural gas consumers. Energy subsidies will continue to decrease gradually until they are eliminated by 2021, with the exception of social tariffs.

• Taxes: The PIT tax floor was raised and family allowances were expanded to reach 4.1 million children, up from 2.9 million. A successful tax amnesty program was implemented to encourage repatriation of undeclared funds held abroad, resulting in additional revenues of 1.6 percent of GDP. Recently, a capital gains tax was implemented for the first time.

• Pension System: Argentina’s pension system accounts for 40 percent of the national budget. In December 2017, Congress approved a change in the pension indexation formula in line with international practice, and put in place the Universal Pension for the Elderly (PUAM)

• Competition: A new Competition Law, which modernizes the regulatory framework for antitrust policy, including setting up a new authority with greater independence, introducing a leniency program for cartel-agreements (such as price-fixing), improved sanctioning rules for anti-competitive practices and a more efficient merger control system, was passed by Congress on May 9, 2018.

• Capital markets: A new Capital Markets Law, which modernizes the regulatory framework for capital markets, including by enhancing corporate governance, expanding the supply of financial assets, and targeting the widening of the domestic investor base, was passed by Congress on May 9, 2018.

• PPPs framework: Congress approved a new PPPs framework to help address the country’s existing infrastructure deficit and to stimulate private investment in key sectors of the economy such as infrastructure, housing, services, production, applied research and technological innovation (November 2016).

• Transparency: President Macri declared his target of placing Argentina among the top countries in the world in terms of transparency. These efforts include Access to Information Law that became effective in September 2017, the passing of the Corporate Criminal Responsibility Law to fight corruption in November 2017, ongoing reforms in procurement for public infrastructure and public procurement, and a renewed commitment for Open Government with the open data portal and the implementation of the second open government action plan.

• Fiscal pact: Long-standing disputes over transfers between the national government and the provinces were settled in a fiscal pact of November 2017. Provinces agreed to freeze current public expenditures in real terms and to decrease the burden of the highly distortive provincial turnover taxes.

• Public employment: The Government enacted a voluntary separation scheme at the federal level to rationalize the public wage bill (April 2018). The program targets older employees from the national administration and government agencies.

Reforms under discussion on Structural Agenda

• Labor Market Reform: Informal labor accounts for one third of salaried employed workers. The Government is discussing a labor market reform with the aim of providing incentives for formalization.
Box E 1 continued

• **Trade**: Argentina is one of the most closed economies in the world. Trade reform needs to be carefully designed since a significant portion of labor is employed in protected sectors. Trade discussions between Mercosur and the European Union (EU) have resumed. The Pacific Alliance accepted Argentina as an observer member.

• **Education**: Argentina has high school dropout rates, especially in secondary school, and low learning outcomes. The Government made important strides in moving evaluation to the center of debate, but further reforms are needed.

25. For the change to a new economic model to endure, growth will have to translate into better quality jobs, and the progress made on reducing poverty will need to continue. Pathway 3 (presented in Chapter 3) outlines the constraints that will have to overcome to ensure that people can be included in the dividends from a changed economic model. Success will entail bringing in more people to the labor market and increasing their productivity. Of concern, then is the evidence that the population is falling behind in relative terms on educational outcomes—not a good sign for a country that needs to reverse its lagging economic performance and expanding its middle class. Additionally, sustained and inclusive growth will require that everyone, irrespective of socioeconomic background or location, has access to quality services needed to accumulate assets. In the shorter term, it will be also important to enhance the extent to which social safety nets and active labor market policies can mitigate the negative social impacts of reducing market distortions and opening up to domestic and international competition in the transition period. Furthermore, integrating all of Argentina (and not just the richer areas) into the world economy will be important to expand the gains from opening up and making the economy more productive. Finally, pathway 4 (Chapter 4) outlines how protecting the environment and harnessing the value of nature for development will be essential to ensure the sustainability of economic growth.

![Figure E 11. Argentina’s economic transition](source: SCD team)

26. From the long list of constraints identified in this systematic country diagnostic (SCD), it was necessary to distinguish those that are the most critical to achieving sustainable and inclusive growth (Chapter 5). To prioritize among the constraints to growth and shared prosperity, the report uses the following criteria: (i) Impact on the twin goals—this filter looks at the potential impact of removing a constraint on reducing poverty and increasing the welfare of the bottom 40 percent; (ii) Complementarities—this filter assesses the degree to which an opportunity identified in one area might have positive impacts on other priority areas given that there are strong connections across a number of the challenges and addressing one set of constraints might also trigger or be a condition for progress in other areas; and (iii) preconditions—
this filter identified those constraints that need to be tackled as a precondition for achieving sustainable and inclusive growth.

27. **Priorities are organized in two categories, including cross-cutting institutional factors needed to enable growth and thematic priorities.** Cross-cutting enablers are ‘drivers of success’ for the more traditional thematic priorities. Enablers can magnify the effects of other reforms and their impacts on growth, inclusion and sustainability over the long-term. They tend to be institutional in nature. The architecture of Argentina’s political and economic institutions plays a fundamental role as the underling determinant of policy outcomes. Moving toward a sustainable and inclusive development model can therefore be proven difficult without addressing some of the more pressing institutional challenges and governance constraints. The design and successful implementation of policies—in any sector or at any level of government—is, to a large extent, determined by the strength of the institutions and the coordination across levels. This section introduces the set of cross-cutting institutional factors to enable growth, which have emerged from the analysis and consultation process across most of the areas, and the sector-specific list of priorities identified.

**Cross-cutting institutional factors to enable growth**

28. **Strengthening the independence and efficiency of accountability institutions to ensure law enforcement and reduce corruption.** Transitioning toward a sustainable and inclusive development model will prove difficult without addressing some of the pressing and fundamental institutional challenges and governance constraints, including the need to ensure an impersonal application of rules (from the ‘rule by law’ to the ‘rule of law’). The experience of many countries shows that constitutional constraints become self-reinforcing when power in the system is distributed evenly and powerful elites and the political ‘system’ accept the law’s limitations.\(^20\) For this transition to happen in Argentina, further efforts are needed to ensure better contract enforcement, an independent judiciary, and stronger accountability institutions across all levels of government to be able to prosecute and sanction corrupt behavior. Over the past years, Argentina has made important strides in strengthening accountability and anti-corruption efforts: new or overhauled laws have been passed or are being discussed in the areas of corporate criminal liability, access to information, ethics and integrity, plea bargain and asset recovery; and accountability mechanisms have been strengthened significantly, such as those of the Anti-Corruption Office. In part, the revelations surrounding the cuadernos scandal—which are gaining in force and scale on a daily basis as this report is finalized—are fruits of such strengthened institutions. But this can only be a beginning of the necessary deep-rooted changes.

29. **Supporting decision making based on evidence using high quality data and information systems could contribute to reaching consensus and advance reforms.** Good and comprehensive quality data and information systems are necessary for the diagnosis, design, implementation and monitoring and evaluation of key policy areas. Yet, the challenges in information across sectors are large, and the sharing practices even within different sectors of government can undermine policy making. But in addition, transparency reforms and open data initiatives can also promote rational decision making based on best available evidence. Further efforts are needed to promote the reuse of these data and the dissemination of information to increase public scrutiny. In a context of often politicized debates on where and how allocate scarce public resources, evidence-based policymaking can help bridge the ideological divide and support a rational debate about policy goals and strategic priorities. By centering on expected outcomes and rigorous assessment of the impact of public policies, an evidence-based approach can help government focusing policymaking on effectiveness of social interventions and efficiency in use of resources. This approach can contribute to mitigate polarization among political and economic actors and increase the chances of bipartisan agreement.

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30. Making federalism work by promoting cooperative behavior across governmental levels will be central to ensure successful implementation of policies. As indicated above, the need to provide homogeneous services across heterogeneous provinces generates perverse expenditure and revenue collection incentives, resulting in substantial fiscal challenges. Historically, the policy instruments and processes used to negotiate these distributitional tensions between the national and provincial governments, (including “participaciones” to provinces, public transfers, pensions, subsidies, and taxation) have proven harmful for Argentina to achieve its long-term development objectives. Moreover, in many cases, the decision-making and implementation is decentralized to a variety of regulatory agencies, without appropriate coordination mechanisms, and thus leads to increased fragmentation and undermines the capacity of the Federal Government to guide implementation. There is therefore an urgent need to make federalism work in Argentina by promoting a more cooperative behavior in which national, state, and local governments interact cooperatively and collectively to solve common problems. To this end, stronger central coordination would assist in making government actions more coherent and aligned with the overall strategic priorities and orientation of the country’s development agenda. Coordination of policies can be improved also promoting reforms (such as those needed in education) that create incentives for subnational governments to improve public spending efficiency and comply with national policy guidelines and regulations, similar to the existing ones used in the health sector (Plan Sumar).

Thematic priorities

31. Inclusive and sustainable growth will require progress on both equity and productivity fronts, as well as ensuring macroeconomic stability and enhance environmental sustainability. The analysis done as part of the SCD process identified a large set of economic priorities from which twelve have been considered to be core. These priorities have been also assessed in terms of their impact on the twin goals, their complementarity with the rest of the priorities and in terms of their role as essential preconditions to the successful achievement of the remaining priorities. These have been largely confirmed through the systematic consultation with national and international experts.

32. The prioritization exercise suggests two tiers of priorities. Reforms included in the first tier are of first-order relevance, very important across the three filters. These include a sound macroeconomic management, better infrastructure, improved quality and relevance of education, and increased efficiency of spending. Improved fiscal policy for growth and equity can be pooled in the first-tier group, though with slightly lesser impact on twin goals. A second tier is headed by closing the gap in the provision of basic infrastructure services, important across the three dimensions, and the other priorities that have varying degrees of importance across the three filters.

First-tier reforms

33. These reforms are led by sound macroeconomic management, which is also key in the short-run, given current financial distress. This reform builds from the diagnosis that macroeconomic mismanagement and frequent economic policy reversals have been a source and outcome of successive boom and bust cycles and welfare swings. This is tightly linked to an improved fiscal policy for growth and equity, as a sound macroeconomic management also entails a rebalancing of fiscal policy to reduce economic distortions and have an expenditure and tax policy that better supports growth and equity. Public expenditure needs to move to a sustainable level in relation to economic output. Given the size of current fiscal imbalances, a fiscal consolidation is essential to stabilize public debt. Cuts to subsidies and other inefficient government programs need to continue, while long term the aim should be to increase the share of spending going on growth-enhancing measures, such as priority public investment projects. The tax system needs to be redesigned to reduce the weight of distortionary taxes and to broaden the tax base. This should include a clear definition of expenditure responsibilities across different levels of government and a
sound intergovernmental fiscal transfer system to ensure the efficient and equitable provision of public services, and improved subnational revenue-collection incentives.

34. **Enhancing infrastructure is also seen as an objective of first-order importance.** The quality of Argentina's infrastructure stock is deteriorating and this poses a challenge to competitiveness. Infrastructure investment is historically low, with a very low participation of private sector financing, and unlikely to grow much owing to limited fiscal space. Moreover, logistics performance indicators are generally lagging. Good infrastructure and lower logistic costs are key to Argentina's ambitions in terms of growth. While financing is a key bottleneck, more focused national and territorial goals, and efficient strategies can substantially reduce financing needs. In addition, upstream reforms will enable Argentina to both improve spending efficiency and attract private financing on better terms—whether through PPPs or commercial borrowing by public enterprises. Efforts to improve public investment institutions and frameworks—notably budgeting and procurement systems—should enable the country to substantially stretch the resources it already allocates to infrastructure. An improved framework for infrastructure planning, financing and investing will be a key driver of competitiveness.

35. **Improving the quality and relevance of education is identified as a first-tier reform related to fostering an inclusive economy.** School readiness and early literacy skills are low, despite relative high coverage. A focus on quality will also call for strengthening teacher careers, in terms of the training curriculum and but also consolidating the network of training institutes, as well as creating the conditions to attract and motivate teachers to perform. Recent reforms establishing annual standardized testing of students’ learning outcomes, enforcing the communication of results to schools, and pre-service teachers’ evaluations should contribute toward focusing the system on quality, although teacher evaluations are still pending. In fact, teachers’ unions resistance to education are generally focused on changes in teachers’ professional development. In addition, it will be essential to revamp secondary education focusing on developing critical basic cognitive and (21st century) soft-skills, in line with *Secundaria 2030*.

36. **Increased efficiency in the provision of health and education while ensuring equal quality for all will also contribute to an inclusive economy.** With respect to increased efficiency in health and education, completion rates are low, learning outcomes are poor, and health outcomes high and unequal across provinces. Unequal access to quality services and inefficiencies reflect highly fragmented systems with lack of coordination mechanisms across systems and subnational entities. Increasing efficiency will require making policies that are increasingly guided by evidence to help identify cost-savings initiatives, and a solid system of monitoring and evaluation. In health, efficiency could be substantially improved by establishing an appropriate model of care, where: (a) several providers including a main primary care provider work together in an integrated, coordinated manner to provide care for an individual (with integrated information systems), and where: (b) there is an emphasis on actively expanding effective coverage at the primary care level. As a result of these efforts, the health system would indeed be better placed to strengthen the prevention and control of the burden of non-communicable diseases, especially in the context of an aging population. This also calls for the reduction of common risk factors associated to these diseases, such as unhealthy diets (particularly among children, where obesity is high), physical inactivity and a tobacco use and alcohol abuse.

Second-tier reforms

37. **This group of very relevant reforms with a slightly lower level of priority is led by closing the gap in the provision of basic infrastructure services.** Broad disparities in basic services, informal settlements and connective infrastructure across regions and within large agglomerations persist. Access to safely managed water and sanitation services varies significantly across regions and between the core and the peripheries of large cities. There are 4,000 informal settlements in the country. Closing basic infrastructure service gaps, investing in connective infrastructure and strengthening local capacity will be
key for the convergence of living standards and for linking populations to economic opportunities. This will require enhancing integrated planning across different sectors, as well as widening the financial options and develop clear mechanisms to set up transparent systems of fiscal transfers across different levels of government.

38. A closely related priority refers to the development and deepening of financial and capital markets and household access to credit, which could be thought of as access to basic financial services. Argentina’s very shallow financial markets reflect a gap in mechanisms that could better support growth, infrastructure, housing, and enterprise development for the private sector. Households have limited access to credit for productive investment and asset accumulation, particularly for the more vulnerable. Poorer people rely on personal loans or credit cards, with high interest rates. Expanding credit and mortgage markets will be essential. The new legal frameworks are encouraging, but substantial regulatory and institutional roll-out measures are needed to ensure that financial and capital market products can operate in an enabling environment and that the government works with the private sector in developing new and innovative instruments to promote long-term finance for productive purposes, and to generate new asset classes of financial instruments that can be more transparently priced and traded.

39. Two reforms directly linked to the open-economy development strategy stand-out for their impact on the twin goals and complementarities: an increased integration into the global economy, and reduced barriers to competition and lower logistic costs. Key trade policy actions include lowering tariffs and non-tariff measures (NTMs) in priority sectors, unilaterally reducing NTMs in input products, removing nonautomatic licenses to increase predictability and boosting regional integration agreements to increase market access. Competition and trade authorities can further coordinate to harmonize technical standards with trade partners. To improve investment policy, Argentina can revise the incentives framework, introduce effective policies to promote linkages with local suppliers, and set up comprehensive regulatory improvement and simplification mechanisms. Jointly among competition and investment promotion authorities, the government can open-up key sectors to investment. On the competition and logistic side, Argentina can continue strengthening its anticartel enforcement, implement the recently overhauled merger control framework, strengthen pro-competition sector regulation in key sectors such as telecommunications and transport, and implement competitive neutrality principles to ensure that public and private operators compete on a level playing field. The competition authority will need to be well resourced, prioritize its engagements and actions, and achieve technical independence.

40. Two priorities on natural capital and environmental sustainability stand out. On the one hand, fostering climate smart growth for the short and the long-term relates to the climate impacts that are rapidly coming to the fore of Argentina’s lives and economic activities. While appropriate adaptation policies in key sectors including agriculture, water, energy, and health can help deal with impact in the present, a more systemic approach can offer more robust outcomes. By the end of this century, under an extreme emissions scenario, the projected warming could reach an average change of about 3.5°C in the north of the country, relative to present-day conditions. This will produce important social, economic and environmental impacts that will require strong policy shifts. Priorities to adapt to climate change involve proper costing of climate action; contingency planning; and a closer integration between the mitigation and adaptation agendas.

41. On the other hand, harnessing natural capital endowments through policies and investments stresses the need to leverage natural resources for growth in a sustainable way. Natural capital in Argentina includes agricultural soils and pastures; water; forests; fisheries; strong winds and solar potential; and subsoil assets (oil, gas, coal, and minerals). Some assets, particularly forest ecosystems and fisheries, are under significant pressures. Argentina has lost 21 percent of its forest cover in less than 25 years. At the same time, fish stocks have suffered from overexploitation due to the lack of a national management plan for sustainable and responsible fishing with a long-term vision. Yet, these resources, along with the strong
renewable energy potential can be important sources of economic rents, jobs and sustainable livelihoods. Unleashing the potential of natural capital requires breaking with the extractive policies of the past and consolidating a policy framework that attracts private sector investments. Policies, incentives and enforcement are also required to ensure that the open access that characterizes many natural assets, such as forests, land and fisheries, does not give way to illegality and degradation. Finally, a more sophisticated demand for greener attributes in global value chains is already emerging and Argentina has much to gain from developing information mechanisms in support of labels and practices that encourage the thriving green businesses throughout the country.

42. **Finally, an item that will become increasingly important as the population ages: the need for a social consensus to ensure pensions are sustainable.** Pensions are fundamental for protecting the income of the elderly population, as poverty rates would be substantially higher in the absence of the recent reforms that expanded coverage. Two-thirds of the moratorium goes to the three poorest deciles. But with already 11 percent of GDP accounted for by pensions, the mid-term sustainability is not currently guaranteed given the demographic transition and the current rules. There is a need to consider options that balance the high levels of generosity (which has recently increased with the Historical Reparation (Reparación Histórica) that recalculated and adjusted benefits retroactively and going forward), with the broad coverage while ensuring future sustainability. This is particularly important as the Government is starting discussions on a future pension system reform. In this sense, the December 2017 parametric reform will help make the system more sustainable by changing the pension indexation mechanism to one that ties benefit changes more closely to changes in prices (and up to a minor extent to changes in wages). Nonetheless, in addition it would be desirable to broaden the agenda to revise all the parameters and components of the system, both contributory and non-contributory.

43. **Moving along the reform path will not be easy.** The forces that caused political and economic volatility in the past still linger and are likely to influence the future. Just as this SCD was about to be completed, high devaluation pressures forced Argentina’s government to increase its focus on short-term macroeconomic stabilization priorities. Without broad-based support and appropriate safeguards for the vulnerable, the reform process might stall. The proposed reforms can however face a different fate than previous reform efforts in that they seek to put a comprehensive package of policies in place to tackle at the same time: growth challenges, inclusion concerns and the potentially large scope for productivity improvements and natural capital-based growth.

44. **A key element for government actions will be sequencing.** While all the priorities are identified as fundamental for sustainable and inclusive growth, the sequencing of reforms is essential for success. It is undeniable that ensuring macroeconomic stability, for instance, is not only a precondition for other priorities, but its failure can undermine most of the progress achieved in other dimensions. Improving the quality of social spending and investing in human capital are priorities that will see their fruits in the medium and long run, but today’s inaction will prove costly. Within some of the priorities, sequencing of specific measures is also fundamental, as is the case of prioritizing the deepening of domestic competition prior to successfully integrating the country into the global economy. International experience of implementing large structural reforms reveals substantial potential gains; however, prior experience has also shown that proper sequencing and monitoring are essential to success. Comprehensive reform programs to deepen competition and open up the economies to trade and investment in Australia, Mexico, and Sweden took a decade or more to put in place. In addition, appropriate interinstitutional coordination, at the federal level and between the national and subnational governments, as well as public-private dialogue, is required to achieve early wins, and consolidate the reform process. Finally, improving infrastructure spending appears as not only a precondition, but also as having strong complementarities with other policies identified.

45. **Some of these reforms are already underway, but there is a risk that the present context will mask the sense of urgency of key structural reforms whose outcomes are seen in the longer term.**
Continuing with the reform process is crucial before inequalities and vulnerabilities increase under the pressing fiscal challenges, and before the opportunity to embed the results of a decade of successful growth fades away. Sustaining a long-term commitment to policy reform on behalf of politicians, the private sector and the population at large is challenging given the complexity and extensiveness of the reform agenda. Clearly communicating the gains and potential longer-term impact can help, as will political dialogue around interventions to minimize social conflict and generate the political capital needed. Over time, results achieved in these areas may serve to build political support and shift incentives.
Chapter 1. Setting the Stage

Introduction

1. This report on the medium-term agenda to ensure growth and shared prosperity in Argentina comes at a time when the country is embarking on deepening structural reforms, while dealing with recent sudden financial market pressures that emerged in April 2018. The current Government came into office at end-2015 facing a difficult legacy of macroeconomic and structural imbalances. Progress has made since then by the administration on important reforms. However, continued macroeconomic imbalances—with a primary deficit of 4.2 percent of GDP in 2017 and inflation of 24.8 percent at end-2017—combined with high external financing needs made Argentina vulnerable to increased emerging market turmoil at end-April, when the country experienced a large depreciation in the peso and a rise in country risk. In response to this, the Government requested an emergency credit line with the IMF in early May and accelerated some key reforms. The report was completed at the beginning of August 2018 amid the continued economic turmoil that has hit Argentina. The focus of the report is on medium- to longer-term development challenges in Argentina, rather than contemporaneous macroeconomic developments. This includes a substantial focus on macroeconomic policies to set in place the foundations for medium-term growth and shared prosperity by boosting jobs and productivity. Achieving macroeconomic stabilization is a precondition for creating a healthy and vibrant economy. But deep reforms in areas varying from deepening domestic competition to developing capital markets to beating the best when it comes to education outcomes, are necessary to ensure that the population benefits from a resurging private sector and renewed connection with the global economy. Learning from other countries experience in implementing structural reforms and gradually opening up their economies, like the Australian reforms from the early 1980s and Sweden’s from 1990, this is a long-term agenda and a strong societal consensus will need to develop to support the changes for reforms to endure. Not to be underestimated is the importance of ensuring a strong safety net to support those that may be hit by structural changes in the economy.

2. Argentina is rich in natural capital assets and has a historically strong middle class. Along with its 2.8 million square kilometers, its extraordinary fertile land makes Argentina one of the largest agricultural producers in the world. The beef and soy sectors apply among the world’s most modern practices and are leaders in breeding, agricultural machinery, and innovation. Argentina has also vast natural resources in energy, with the second highest shale gas and forth highest shale oil reserves in the world. In addition, Argentina has significant opportunities in some manufacturing subsectors and high-tech, innovative services. Argentina has a historically large and strong middle class. Social indicators are mostly good, and society deeply values education and knowledge as a means for potential mobility and status. Noted successes in research and innovation (four of the six most successful Latin American tech unicorn companies, with a value of over US$1 billion, are Argentine) makes the country a potential destination for high value-added industries.

3. Nonetheless, compared to its peers, Argentina’s long-run economic performance has been disappointing. Average long-run economic growth in Argentina has been only 2.7 percent—about half that of high performing countries in the region and less than a third of emerging countries in Asia. As a result, the country’s income per capita fell from being 70 percent of that of the U.S. in 1914 to only 33 percent today. Furthermore, 25 percent live in poverty and another 20 is still vulnerable to falling into poverty while growth has come at the expense of the environment (with 12 percent of forest loss between 2001 and 2014—double the world average). The lack of creation of good quality jobs in Argentina in recent years limited the significant progress made on equity in the previous decade. While inequality as measured by the Gini Index

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21 See Mander (2016).
decreased by over 20 percent between 2004 and 2013, outpacing the reduction in the LAC region (5 percent), progress has since stalled.

**Falling behind**

4. **Argentina fell into middle-income status, failing to keep up its high-income peers of the early twentieth century.** Since the mid-twentieth century, Argentina has consistently lost ground relative to rich economies, and has now joined a group of middle-income countries failing to catch-up with more developed peers, usually referred to as middle-income trapped countries (see Box 1). Argentina’s GDP per capita was similar to the average of a group of rich economies by the beginning of the twentieth century, but has now dropped to 38 percent of these rich countries’ economic output per person (see Figure 1). Given its secular decline from relatively high levels of income per capita, Argentina can be referred to as a unique country that did not grow into, but fell into middle-income status, and remained there.

**Figure 1. Argentina’s GDP per capita as a percentage of the average of rich economies, 1900-2016**

![Graph showing Argentina's GDP per capita as a percentage of the average of rich economies, 1900-2016.](image)

**Figure 2. Change in GDP vs. total wealth per capita, 1995-2014**

![Graph showing change in GDP vs. total wealth per capita, 1995-2014.](image)

**Source:** Data from Maddison Project Database, version 2018. Bolt, Jutta, Robert Inklaar, Herman de Jong and Jan Luiten van Zanden (2018)

**Note:** Rich economies are the UK, the U.S., Norway, Switzerland, Australia, Denmark, Sweden, Germany, Canada and Netherlands.

5. **Poor GDP growth has reinforced itself through slow capital accumulation.** Sustained long-term economic growth requires investment and maintenance of assets, measured comprehensively to include produced capital, natural capital, human capital and net foreign assets. Recent estimates of comprehensive wealth show that Argentina’s poor GDP performance has been on par with the country’s total wealth evolution. The average annual growth rate, between 1995 and 2014 of wealth per capita has been around 1 percent.

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22 The ten economies were chosen under the following methodology: from the top 15 richest economies in 1950, 1985 and 2015, we selected the ten richest economies repeated on the three sample-years (excluding small island states and OPEC countries). These are the UK, the U.S., Norway, Switzerland, Australia, Denmark, Sweden, Germany, Canada and Netherlands.
percent, that is, slower than for most of its peers, except for Mexico (0.2 percent) and Turkey (nil; Figure 2). It has been much lower than Chile (4.3 percent), Peru (4.2 percent) and Uruguay (4 percent). What this means is that slow growth reinforced itself via slow accumulation of total wealth.

6. The main explanation for this poor performance is Argentina’s unusually volatile macroeconomic environment, reflected in large swings in economic activity (Figure 3). During the period 1950-2016, Argentina has gone through 14 recessions (one or more consecutive years of negative growth), with an average duration of 1.6 years. As a result, the country spent roughly one-third of the time since 1950 in recession. This is the most time of any country in the world except the Democratic Republic of the Congo (Figure 4), ranking with fragile states24 like Iraq and Syria and highly hydrocarbon dependent countries. Uruguay, a neighboring country affected by Argentina’s cycles and arguably subject to similar external shocks, spent less than one-fifth of the time in recession. Recessions not only occur often in Argentina, but they are deep. In an average recession cycle, Argentina’s GDP contracts 3.5 percent per year (Table 1). The result is a relatively weak growth performance: Average long-run economic growth in Argentina has been only 2.7 percent, below that of its regional peers (3.7 percent), new high-income countries (3.9 percent, see Box 1 for a definition of this group), and OECD countries (3.2 percent).

Figure 3. Argentina’s GDP growth rate, in percent, 1950-2016

Table 1. Argentina’s economic cycles, 1950-2016

<table>
<thead>
<tr>
<th></th>
<th>Expansions</th>
<th>Recessions</th>
</tr>
</thead>
<tbody>
<tr>
<td>Number of events</td>
<td>14</td>
<td>14</td>
</tr>
<tr>
<td>Average duration (years)</td>
<td>3.3</td>
<td>1.6</td>
</tr>
<tr>
<td>Average annual GDP change (in percentage)</td>
<td>6.7</td>
<td>3.5</td>
</tr>
</tbody>
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Source: Calculations based on World Bank’s WDI dataset.
What lies behind Argentina’s volatile behavior? In order to answer this, the next sub-section will introduce those three aspects that are on the base of this dynamic, which are: natural resources abundance, historically large middle class with unmet high-income country aspirations, and an unequal federation marked by a significant vertical imbalance. The following sub-section will show, with a long-term perspective, how these three characteristics have interacted, resulting in Argentina’s high volatility. Finally, the last sub-section will emphasize the recent history, mainly over the last decade and a half.
Box 1. Middle income trap from above? Argentina and comparator countries

Given its secular decline from relatively high levels of income per capita, Argentina can be referred as a unique country\(^1\) that did not grow into, but fell into middle-income status, and remained there. Following Felipe (2012),\(^2\) middle-income trapped countries (Trapped MICs) are defined as those who remained in the middle-income range for more than 20 years.\(^3\) The countries other than Argentina that fall into this definition are Algeria, Brazil, Mexico, Romania, South Africa and Bulgaria. Among Trapped MICs, Argentina is the country that has been the richest by far in the past (see Figure B1.1). Argentina is also the country that spent the most time as a middle-income country, 53 years, over 1960-2016, compared to an average of 36 years among Trapped MICs.

Although Argentina’s relative decline in GDP per capita is shared with Latin American peers, some countries have managed to diverge from this trend. Chile, in particular, has managed to grow rapidly in recent decades, and Uruguay also now is classified as a new high-income country (New HICs). Argentina remained the richest economy in the southern cone until the late 1990s, when first Chile and later Uruguay overtook it. Both Chile and Uruguay are now classified as New HICs following Felipe (2012): countries that took less than 20 years to move from the upper-middle-income range to the high-income range and have registered a 3 percent GDP per capita growth on average since they passed the middle-income threshold. By contrast, Argentina’s GDP per capita average growth rate is 1.3 percent since it last entered the upper middle-income range (1964-2016) (see Figure B1.2). Lower average growth in Argentina is due partly to higher economic volatility characterized by longer time periods spent in recession compared to other countries (for further discussion see Section 2.1).

Figure B1.1 Argentina’s and Trapped MIC’s GDP per capita as percentage of the average of rich economies, 1960-2016

![Figure B1.1](image)

Figure B1.2 GDP per capita in Argentina and New HICs, in 2016 PPP US$

![Figure B1.2](image)

Sources: Data from the de Hoyos’s Total Economy Database, November 2017, WB (2017) and Felipe (2012).

Three comparator groups are used in the SCD: (i) New HIC countries will be used as the set of structural peer countries for comparison purposes (Chile, Czech Republic, Korea, Malaysia, Poland, Slovak Republic, Turkey, and Uruguay); (ii) Argentina will also be benchmarked against the largest LAC economies (Brazil, Chile, Colombia, Mexico, Peru, and Venezuela) plus Uruguay; and (iii) OECD economies—a group of countries that Argentina aspires to join in the near future.

Notes: \(^1\) More recently, Venezuela also fell from high-income country status.
\(^2\) GDP per capita in PPP (constant 2016 US$) was used to create the income measure to rank countries. Income thresholds are the same as in WB (2017a).
\(^3\) There is an extensive literature on the Middle-Income Trap concept, first introduced by Gill and Kharas in 2007 (see World Bank (2017a) for a survey). World Bank (2012), for example, showed that only 13 of 101 middle-income economies in 1960 had graduated to high income by 2008.
Argentina’s defining characteristics

Natural resource abundance

8. Argentina is rich in natural capital, but neglect and underinvestment hold back its potential. With 6.24 hectares per person, the country has one of the largest land endowments per capita in the world (Figure 5). Water is also abundant at the national level, though with wide regional variations. A favorable temperate climate makes Argentina’s land fertile for rainfed crop production and cattle. Argentina has one of the largest continental shelves and is rich in marine and coastal resources. It is also rich in renewable energy resources, including hydro, wind, solar and biofuels, which are largely untapped. Finally, natural diversity and landscapes attract international visitors, building a strong tourism sector that importantly contributes to GDP and job creation. Renewable natural assets are not the only resource: mineral and renewable resources are likely to play a growing role in the country’s economic future. The country has world class gas and shale oil potential. Yet, Argentina’s development model has been depleting large portions of its natural capital base. For example, between 1990 and 2014, driven in large part by the expansion of industrial-scale agriculture, Argentina lost 21 percent of its forests, a loss considerably higher than the one experienced by peers (Figure 6). This has resulted into a private gain at often high public costs (in the form of increased flooding and reduced environmental services). Moreover, soils are highly compromised, as it is estimated that 37.5 percent are affected by hydraulic and wind erosion. Also, the most productive areas (Pampa Argentina), are vulnerable to increasing trends of hydrological extremes, mainly floods. The Province of Buenos Aires alone, source of 25 percent of grain and meat production in the country, had more than 1 million hectares flooded in 2001, and again in 2015, with hundreds of millions of dollars in losses. On the marine side, naturally rich fish resources have declined through overfishing.

![Figure 5. Land per capita, 2014](image1)

**Figure 5. Land per capita, 2014**

![Figure 6. Forest cover change 1990-2014, in percent](image2)

**Figure 6. Forest cover change 1990-2014, in percent**

*Source: Data from Faostat.*

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23 Of course, agriculture is not just a source of negative externalities. Positive externalities and benefits arise from the fact that Argentina is key relevant player in global food security, while innovation in agriculture and food systems provide important global public goods.

24 Casas and Albarracin, 2015.
An historically large middle class with unmet high-income country aspirations

9. By the mid-twentieth century, Argentina had a strong and educated middle class, at the time that the economy was in full employment, and many could enjoy a certain standard of living unheard before. Between 1880 and 1915, the country benefited from an abundance of fertile land and the expansion of world trade, and land owners became increasingly wealthy, benefiting from a land policy that facilitated land concentration. The massive influx of immigrants, especially from Europe, dramatically changed the social structure of the country. By 1914, a third of Argentines were foreign immigrants, a large share of which had non-manual work. Favorable international trade conditions after the Second World War, combined with industrialization and redistributive policies led to a real income increase and a rapid decline in inequality (the income share of the top 1 percent) (Figure 7). These benign economic conditions for workers and the setting up of a welfare state, led to the expansion of middle class aspirations among this newly-enriched working class. In a context of full employment, the construction of a social welfare state in which most contributed, ensured health care (through the trade union’s obras sociales) and generous pensions for an increasing proportion of the population. Social security revenues as a share of GDP rose from 1.3 percent in 1943 to 6 percent in 1955, real wages almost doubled from early 1940 to early 1970s (Figure 8) and old-age coverage increased three-fold (from 12.6 percent in 1950 to 44.5 percent in 1970).

Figure 7. The top 1 percent income shares in Argentina, and other new world countries, 1916-2006

Figure 8. Average real wages, 1940-2006

Source: Reprinted from Alvaredo (2010).

Source: Reprinted from Beccaria et al. (2005), based on Llach and Sanchez (1974) and authors’ calculations.

10. But the successive policy and economic shifts that led to declining real wages and the de-formalization of wage employment since the mid-1970s, hit workers and deepened the segmentation of the society. The periods of negative economic growth, combined with high rates of inflation and increasing unemployment, severely impacted the once aspiring middle classes (the “new urban poor”) and

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26 Estimates per occupation put the size of the middle class at 30 percent by 1914 (Adamovsky 2016).
27 Alvaredo, 2010.
29 The first estimate using of Ferreira et al. (2013) definition of the middle class (as those with per capita income between US$10 and US$50 per day), puts the size of this group in Greater Buenos Aires in 1974 as reaching almost 80 percent of the population.
the already poor, leading to a surge in inequality. The share of incomes received by the top 1 percent grew from 7.4 in 1973 to 12.4 in 1997 to 16.7 in 2004.\textsuperscript{30} Between 1980 and 1990, workers lost 38.8 percent of their income, and the fall was even higher for those in middle class occupations.\textsuperscript{31} The new poor had education levels and family structures closer to the middle class, but low income and a lack of social security akin to the structurally poor. As unemployment and informality increased, a higher proportion of families lost their health and old-age insurance, increasing the duality of society between the formal-protected and informal-unprotected groups. After the 2001/2002 crisis, economic growth and job creation was accompanied by an expansion in health and old-age insurance to the wider population, as well as in social safety nets. However, labor markets remain highly segmented, with a third of workers not contributing to the social security system.

\textit{An unequal federation marked by a significant vertical imbalance}

\textbf{Figure 9. Subnational inequality: Standard deviation of regional per capita (log) GDP, circa 2010, in percentage}

\textit{Note:} Last available data between 2001 and 2010. Argentina data for 2005
\textit{Source:} Data from Gennaioli et al. (2014).

\section{11. Argentina is a very unequal federation, with areas as rich as developed nations, and provinces as poor as low middle-income countries.} Argentina is a federal country comprising 23 provinces\textsuperscript{32} and the autonomous federal capital of Buenos Aires (CABA for its Spanish acronym). Heterogeneity across provinces in terms of income is very large. CABA, the richest district of the country, has a GDP per capita of US$28,358 (higher than that of Spain), while Formosa, the poorest province, has a GDP per capita of

\textsuperscript{30} Alvaredo, 2010.
\textsuperscript{31} Kessler and Di Virgilio, 2008.
\textsuperscript{32} According to the 1853 Constitution, each province has its own constitution, generating different institutional designs and administrative structures.
US$3,704 (below that of Guatemala).\textsuperscript{33} To visualize such internal discrepancies in development levels, Figure 9 compares the standard deviation of (log) GDP per capita across subnational governments. Argentina is a clear outlier among comparator countries, with a standard deviation 30 percent higher than regional peers, 81 percent higher than new high-income countries,\textsuperscript{34} and 134 percent higher than the average OECD country.

**Figure 10. Provincial revenues as percentage of total revenues, 2015**

\[ \text{Source: Data from Ministry of the Treasury.} \]

12. **The need to provide homogeneous services across heterogeneous provinces generates perverse expenditure and revenue collection incentives, resulting in unique fiscal challenges.** Many important expenditure responsibilities lie at the provincial level, such as basic health-care and education, while revenues are mostly collected at the national level. To help fund those expenditures, a portion of revenues is redistributed back to provinces through an automatic revenue-sharing scheme (“coparticipación”), and by discretionary transfers by the executive branch. While some degree of mismatch between expenditure and collection responsibilities is inevitable to guarantee the provision of relatively homogeneous services, in Argentina this is very large, with a sizable discretionary component. In 2016, the average province collected only 37 percent of its revenues, and in only six provinces own tax collection represented more than 50 percent of revenues. Although, on average, transfers do serve redistributive purposes, with poorer provinces receiving a larger share of their revenues from the federal government, there are also large deviations (see Figure 10). The revenue-sharing arrangement is the source and outcome of a very unique political economy, where governors continuously lobby for transfers from the federal government, and the federal government needs the support of governors to pass laws in the Senate. As a result, many important decisions are negotiated on a short-term basis, resulting in a pro-expenditure, anti-tax collection bias at the sub-national

\textsuperscript{33} Values for 2005 (the latest year for which provincial GDP is available) in PPP constant 2014 US$ (Gennaioli et al., 2014).

\textsuperscript{34} For an explanation on the choice of comparator countries, please refer to Box 1.
level. While other federal countries like Brazil, Colombia and Mexico also show high levels of expenditures decentralization, Argentina’s larger heterogeneity and high degree of vertical fiscal imbalances make it an outlier.35

Convergence postponed

13. **Taken together, these three features of Argentina have combined in deleterious ways resulting in a long-term disappointing economic performance.** The high-income aspirations of a country with middle-class aspirations and the short-term considerations (cortoplacismo) of the political system combine to create enormous pressures to spend during booms. Often it is the booming agricultural sector that provides the high rents to the state to fuel these fiscal expansions. The large vertical imbalances of the federal system and the tendency of political and economic actors to reach agreements through short-term “deals” has undermined the ability of public institutions to enforce long-term commitment to reforms and to sustainable policies to use of the country’s rich natural assets to harness growth. This has frequently led to highly procyclical economic policies that amplify booms and busts. Successive crises have deepened this dynamic: growing impoverishment during downturns leads to high pressures to spend when economic conditions improve, and actors have over time lost their trust in the ability of the economy to deliver long-term stable growth, reducing their incentive to look beyond short-term gains. As a result, Argentina has failed to keep up with rich economies, and experienced an unusually volatile macroeconomic environment, reflected in large swings in economic activity.

14. **One of the main explanations behind Argentina’s disappointing macroeconomic performance lies its tendency to “live beyond its means”, an endogenous driver of its boom and bust cycles.** The country’s social demands and political pressures yield an equilibrium characterized by excessive aggregate spending (i.e. aggregate dissaving). The dissaving of the country as a whole is financed with savings from the rest of the world, reflected in a current account deficit. The tendency to overspend grows wider in booms, with procyclical policies that result in consumption and investment (both public and private) growing faster than income. On the external sector this is reflected in an increase in imports through two channels. First, imports rise due to an increase in the demand for imported consumption goods and production inputs. Second, a growing aggregate demand puts pressure on the market for non-tradable goods, increasing their relative price, a real appreciation that further increases imports. Since exports—mainly based on natural resources and held back by an extractive fiscal regime—usually fail to keep up with the rapid growth of imports, the current account deteriorates. This process usually comes to an end when the rest of the world refuses to continue to finance Argentina’s current account deficit, and usually results in a sharp depreciation of the currency, a spike of inflation, a large drop in real wages, and a deep recession that reverts the current account wiping out a large portion of the welfare gains in the expansion period. These boom and bust episodes in turn result in both underinvestment in natural capital (which takes time to reap rewards) and in extractive policies to generate short-term liquidity (generating the liquidation of assets and even illegal extraction). These cycles, sometimes referred to as “stop-and-go cycles” are illustrated in Figure 11 showing the correlation between current account balance and GDP growth.36 As the economy grows and the current account deteriorates, the external restriction starts to bind, and usually results in a sharp depreciation of the RER. After a period of appreciation, the RER usually sharply depreciates, as shown by the spikes in Figure 12. These large depreciation episodes triggered large contractions in economic activity. Defining large depreciation episodes as those where the exchange rate depreciates in one year by more than one standard

35 Tommasi et al., 2001.
36 For an historical account of stop-and-go cycles, see for example, Diaz Alejandro (1970), or the more recent Gerchunoff and Llach (2007), Heymann (2007), Albrieu and Fanelli (2008), Gerchunoff and Rapetti (2016).
deviation, there were five such episodes since 1950, that resulted in contractions in economic activity, usually large, with a decline on average of 5 percent per episode (Table 2). \footnote{This does not include the most recent exchange rate depreciation episode in 2018.}

**Figure 11. Correlation between current account as a percentage of GDP and GDP growth, 1950-2016**

![Correlation diagram](image)

*Sources: Data from Ferreres (2005), INDEC, BCRA.  
Notes: Each dot is a period of consecutive growth or contraction of economic activity, in percentage (x-axis), and the corresponding change in the current account balance, in percentage points of GDP (y-axis), all expressed in annual averages.*

**Figure 12. Real exchange rate index, 1950-2016**

![Real exchange rate index](image)

*Source: BCRA  
Notes: A real depreciation of the peso is an increase in the index*

**Table 2. Large depreciation episodes, 1950-2016, in percent**

<table>
<thead>
<tr>
<th>Year</th>
<th>RER Depreciation</th>
<th>GDP Growth Rate</th>
</tr>
</thead>
<tbody>
<tr>
<td>1975</td>
<td>81</td>
<td>-0.6</td>
</tr>
<tr>
<td>1981</td>
<td>78</td>
<td>-5.4</td>
</tr>
<tr>
<td>1982</td>
<td>137</td>
<td>-3.2</td>
</tr>
<tr>
<td>1989</td>
<td>61</td>
<td>-6.9</td>
</tr>
<tr>
<td>2002</td>
<td>153</td>
<td>-10.9</td>
</tr>
<tr>
<td>Average</td>
<td>102</td>
<td>-5.4</td>
</tr>
</tbody>
</table>

*Source: Calculations based on data from Ferreres, BCRA.  
Note: A large depreciation is defined as a depreciation above one standard deviation.*

15. **Fiscal policy is a key factor behind Argentina’s tendency to overspend.** The equilibrium is usually driven by—or channeled through—its public sector, which runs chronic fiscal deficits and conducts procyclical policies. On average, the consolidated (federal plus provincial) fiscal deficit since 1960 was 4.2 percent of GDP, with only five years (from 2003 to 2007) of fiscal surplus (see Figure 13). The surplus years were not the result of counter-cyclical policies, but an anomaly as the consequence of a massive crisis, a decade long default, and extraordinarily high commodity prices. In fact, Argentina failed to join a group of LAC countries that, despite a history of procyclical fiscal policies, where able to conduct counter-cyclical
policies in the twenty-first century (see Figure 14). One of the main sources of procyclicality is the inability of the political system to manage the country’s so-called distributional conflict, a situation where the demands by different interest groups (unions, businesses, professional councils, etc.) exceed the available resources, with the corresponding pressures over fiscal policy. The unequal federalism contributes to this distributional conflict, this time between provinces and the national government. The macroeconomic consequences of procyclical fiscal policies and the resulting fiscal imbalances are varied, but three mechanisms are of first order importance. First, procyclical fiscal policies contribute to the real appreciation process described above, both on the real side (i.e. increased public expenditure puts pressure on the markets for non-tradable goods, raising their relative price), and on the financial side (the inflow of borrowed dollars appreciates the nominal exchange rate). Second, the need to finance increasing fiscal deficits fuels Argentina’s recurrent debt problems. Third, fiscal deficits are the main cause of Argentina’s chronic inflation problems, as the monetary authority continuously acts as a lender of last resort to the Federal Government.

Figure 13. Fiscal balance, Argentina, 1960-2016, in percent of GDP

![Figure 13. Fiscal balance, Argentina, 1960-2016, in percent of GDP](image)

**Source:** Data from Ministry of the Treasury

Figure 14. Correlation between public expenditure and GDP, 1960-2016

![Figure 14. Correlation between public expenditure and GDP, 1960-2016](image)

**Source:** Reprinted from Vegh et al, 2017

16. Institutionally, these cycles are reflected in the large swings in economic policy throughout the country’s history. Among some of the most significant in the last quarter-century: The country moved from a very rigid exchange rate regime (currency board established in 1991) to a managed float, then a dual exchange rate regime and has now a flexible exchange rate. Trade was to be gradually opened up when Mercosur was created in 1991, but the strategy was left behind and reversed to the extent that by 2012 import controls were put in place. The privatization of public utilities in the 1990s, turned to nationalizations from the mid-2000s onwards and is now replaced by a focus on Public-Private Partnerships (PPPs). Argentina has moved from a “mostly free” economy in 1995 to a ‘mostly unfree’ one on 2017 (Index of Economic Freedom). Tax legislation has been enacted or modified over 80 times since 1988. Fiscal federal rules have been changed 14 times in the same period, and budgetary rules have been altered 16 times between 1992 and 2008. Table 3 gives an overview of policy reversals across varied areas between the 1990s and the 2000s. Historically, policy volatility has typified Argentina for longer than the last quarter of a century.

38 See Heymann and Navajas (1989) for a classic exposition.
39 The Index covers 12 freedoms, ranging from property rights to financial freedom, in 186 countries. According to the 2017 Index of Economic Freedom, Argentina ranks 156 out of 186 countries.
40 Bonvecchi, 2010.
Using a measure of policy stability based on presidential speeches during 1940-2016, Argentina and Venezuela are the countries that come out with the lowest policy stability using this measure, and in addition were the countries that most diverged in economic output from the U.S. over 1940-2010 (Figure 15). Given this history, commentators today focus on the expectation that there is a strong possibility that the current direction of economic policy may be reversed in Argentina if political power shifts.

**Table 3. Economic policy making: an history of policy reversal**

<table>
<thead>
<tr>
<th>1990s</th>
<th>2000s</th>
</tr>
</thead>
<tbody>
<tr>
<td>Founding Member of WTO (1995)</td>
<td>Import restrictions (“G3” complaint filed at WTO) (2012)</td>
</tr>
<tr>
<td>Privatizations: e.g. Telephone, airline, road concessions (1990); Railway concessions (1991); Water and sanitation concession, electricity companies (Edenor, Edesur), gas company (1992); Oil company (YPF) (1993); Postal service (1997); Provincial banks and provincial enterprises (various)</td>
<td>Nationalizations: e.g., Airline (2008); Railway (2015); Water services in GBA (2006); Oil company (YPF-Repso) (2012).</td>
</tr>
<tr>
<td>Price deregulation</td>
<td>New Supply Law (2014)</td>
</tr>
</tbody>
</table>


**Figure 15. Policy volatility and convergence with the U.S. GDP per capita, 1940-2010**


*Note:* This Figure shows the cross-country correlation between long-term growth and policy volatility during the 1940-2010 period. Long-term growth is measured as the percentage point change of the GDP per capita of each country (as a percentage of the GDP per capita of the US). Policy volatility is measured as the percentage point change of the share of the top three topics in the presidential speech of the initial year. The topics were selected by an Latent Dirichlet Allocation model using pooled data of all the countries, and using a 10 percent minimum threshold to discard topics with low frequencies.

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17. In turn, successive crises lead actors to lose their trust in the ability of the economy to deliver long-term stable growth, reducing their incentive to look beyond short-term gains. It increases volatility as growing impoverishment during downturns leads to high pressures to spend when economic conditions improve. This also implies that growth patterns become increasingly reliant on changes in factor accumulation and utilization rather than higher productivity (a shift in the production function). Since 1960, the contribution of total factor productivity (TFP) has been erratic, decreasing in three of the last six decades for an average of zero growth, compared to a 0.6 percent average annual growth rate in OECD countries and New HICs. The contribution of capital, large in the 1960’s and 1970’s has been decreasing: the capital-to-GDP ratio fell by on average 15 percent since the 1980s. Stagnant TFP, coupled with a strong decline in the capital intensity ratio resulted in relatively low labor productivity growth, as low as 2 percent on average in the 1980s (see Chapter 2 for a discussion on productivity trends).

18. Recurrent crises and successive policy swings resulted in worsening welfare conditions from the mid-1970s to early 2000s. Slow and unstable growth, deep political conflict, sweeping trade liberalization and labor repression in the mid-to-end seventies are associated with increasing poverty and inequality (Figure 16). The hyperinflation, real depreciation and economic contraction of the 1980s, resulted in real wages declined even more, and rising labor informality, leading to rising levels of poverty. The following decade, while the economy was growing and inflation was under control, the sudden liberalization of trade along with an appreciated RER led to a rise in unemployment and informality, especially among unskilled workers, which in the absence of wide compensatory social protection programs and weak labor institutions led to a more unequal distribution of incomes, and an increasingly segmented society between the have and have-nots. This situation worsened toward the end of the decade, when a recession finally led to the end of the convertibility regime in 2001/02, accelerated inflation and poverty reached its highest level in Argentine history. After the drastic crisis, employment conditions improved, particularly among the less qualified. However, as macro imbalances accumulated, labor market improvement slowed down, and poverty stagnated.

19. Despite improvements in the past 15 years (see chapter 3 for details), Argentina still faces significant challenges in terms of poverty and shared prosperity. According to official estimations, 30.3 percent of Argentines living in urban areas are poor and 6.1 percent are unable to meet basic food needs (2016, second semester). Measured at US$5.5 per capita per day in 2011 PPP (the upper-middle income country poverty line), Argentina’s poverty rate is significantly lower than that of its regional peers (Figure

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42 As a result, real appreciation during the “stop and go” cycles is not offset by productivity gains, making the RER much more volatile.
43 Moreover, the positive contribution of TFP to growth for Argentina in the 2001-2010 period is likely overestimated given the effect of the commodity price super-cycle on measured TFP.
44 Due to data limitations for the whole period, capital is not adjusted by capital utilization, so its contribution could be overestimated, as shown in BCRA (2017a).
45 While data for Argentina is not available, Brandt et al (2017) suggest that the poor performance of TFP may be lower than indicated. The authors show that TFP growth, after accounting for natural capital as a factor of production, is sometimes overestimated in times of natural resource booms.
46 Altinir, 2001; Gasparini and Cruces, 2009.
48 Cicowicz, 2002; Galiani and Sanguinetti, 2003; Gasparini and Lustig, 2011.
49 Latest official poverty estimations for 2017 (semester) show that poverty rates for the 31 agglomerations have declined to 4.8 percent for extreme poverty and to 25.7 percent for total poverty. While comparisons across time - beyond 2016- are challenging, experts estimate that these rates are the lowest in the past 15 years. To maintain time comparability with international statistics, we choose to report in the main text the 2016 figure.
ARGENTINA

Systematic Country Diagnostic

18). However, it is still higher than it was 40 years ago, and is now fifty percent higher than in the new HICs countries, and almost two and a half times than in OECD countries. In addition, a substantial proportion of the population is vulnerable to poverty should they be hit by economic shocks (see Box 2).

20. Although Argentina managed to reach OECD standards in some dimensions of well-being, successive economic crisis affected performance in other cases. The country has reached similar levels in access to improved water, but is still far from the OECD standards in terms of infant mortality, the under-five mortality rate, and life expectancy. Life expectancy improvements decelerated, diverging from New HICs and OECD countries trend and, after thirty years, instead becoming similar to the performance of regional peers (Figure 17). The quality of Argentina’s education system, once seen as the top performer in Latin America, has eroded and converged to the median in the region. For instance, Argentina placed second in reading scores among third graders in LAC at the end of the 1990s (in UNESCO’s first regionally-comparable measurement), but fell to the LAC average in the latest round.50

Figure 16. Poverty and inequality in Greater Buenos Aires, 1974-2016

![Poverty and inequality in Greater Buenos Aires, 1974-2016](chart.png)

Source: Authors’ calculation based on data from SEDLAC (Cedlas and World Bank), based on EPHC.

Figure 17. Life expectancy at birth (years), 1960-2015

![Life expectancy at birth (years), 1960-2015](chart2.png)

Source: Data from the World Bank’s WDI.

Note: For groups of countries, simple averages are presented.

Figure 18. Income poverty rate, circa 2016

Source: Data from INDEC for official estimates, and WDI-SEDLAC for internationally comparable estimates.
Note: For groups of countries, simple averages are presented.

Figure 19. Non-monetary dimensions, circa 2015

Source: Data from the World Bank’s WDI.
Note: For groups of countries, simple averages are presented.
Box 2. Vulnerability to shocks: potential impact on poverty rates

At the end of March 2018, INDEC announced the new estimates for poverty and extreme poverty, showing relatively large declines, surpring some observers. Most of the complementary indicators -both from the labor market and the main public transfer- were consistent with this improvement, and thus, qualitatively this was to be expected. Overall employment increased (faster for informal and independent workers), and wages in the formal sector grew at a higher pace than the value of poverty baskets (27 vis-à-vis 22 percent). Similarly, the total amount of pensions, family allowances and AUH grew faster than inflation. Still, a decline from 2016 to 2017 of 4.6 percentage points in poverty rates from 30.3 to 25.7 percent were larger than expected. In part, this is the result of the shape of the distribution relative to the poverty threshold. By the second semester of 2016, a sizeable share of Argentines had incomes very close to the poverty line (Figure B2.1). On average, a 10 percent increase in real household income was enough to move down the poverty rate 5 percentage points.

The other side of the coin is that nowadays a relatively large fraction of households is vulnerable to falling back into poverty even with slight changes in economic conditions. For instance, inflation usually has a higher impact on people in the lower tail of income distribution as the purchasing power of the poor tend to be more affected than those at the top resulting in increased poverty and inequality. If real incomes of families living just above the value of the basic basket of goods and services (poverty threshold) were to decline, the direct impact on the poverty rate would be sizeable. Estimates suggests that if prices grew 5 (10) percent faster than per capita household incomes, the official poverty rate will increase by 2 (4.5) percentage points relative to the last observed rates (2017, second semester). In this context, having a well-targeted cash transfer program with efficient delivery mechanism, such as the AUH, can potentially allow the government to respond quickly to mitigate the impact of a negative shock among the most vulnerable families.

The Challenge going forward

21. The opportunity for Argentina to develop is there: a closed economy, the country has large parts of the non-agricultural sector locked in low productivity and, currently, non-competitive activities. The divide between the two Argentina’s—globally competitive firms and workers enjoying rich country conditions contrasted with a large part of the population with low skills, poorer life quality, often in the informal sector, that is much more vulnerable—puts at risk the country’s convergence. Investing effectively in people so they can take up better quality jobs, and ensuring access to better services and social

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51 Easterly and Fischer, 2001; Panigo et al, 2017
protection is critical to narrowing these divides. The country can piggy back on its natural capital base. But rather than adopting extractive policies, it can create the conditions for nature-based industries that sustainably exploit the country’s fertile lands, forests, renewable energy sources and touristic assets.

22. **The long-run decline in relative GDP per capita has been mirrored by a lack of gains in aggregate and labor productivity.** Growth patterns have become increasingly reliant on changes in factor accumulation and utilization rather than higher productivity (a shift in the production function). The contribution of TFP has been erratic, negative in three of the last six decades (see Figure 20), for an average of zero growth since 1960, compared to a 0.6 percent average annual growth rate in OECD countries and New HICs. The contribution of capital, large in the 1960’s and 1970’s has been decreasing. Stagnant TFP, coupled with strong decline in the capital intensity ratio resulted in relatively low labor productivity growth, as seen in Figure 21, as low as 2 percent on average in the 1980s.

![Figure 20. Growth decomposition by decade, annual averages, 1961-2016, in percent](image)

![Figure 21. Labor productivity annual average growth rate, 1961-2016, in percent](image)

**Sources:** Data from BCRA and the Conference Board’s Total Economy Database

23. **Increases in labor and capital accumulation and utilization are a must for income convergence with advanced economies.** The labor force is not projected to shrink due to aging until the 2040s. But there is an opportunity to increase the current participation rate of women, youth and those with low skills. However, there are worrying indications that skills are falling behind relative to new HICs and OECD peers, and there is no time to waste in putting a priority on improving educational outcomes and building a culture of learning in the workplace. Investment is critical to support growth, currently it is around 16 percent of GDP, well below the new HICs, where investment is on average close to 24 percent of GDP. The severe underdevelopment of domestic capital markets limits the ability to invest: in Argentina loans to the private sector are only 14.4 percent of GDP versus the LAC average of 42.7 percent.

24. **Although there is space for growth based on capital accumulation and job creation, increasing productivity will be critical for convergence to advanced country income levels.** A requisite for

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52 Moreover, the positive contribution of TFP to growth for Argentina in the 2001-2010 period is likely overestimated given the effect of the commodity price super-cycle on measured TFP.

53 Sources: Competition data taken from the World Economic Forum (2017). Investment data is from the World Bank’s World Development Indicators for 2016, and domestic capital market development data is from the IMF’s International Financial Statistics (IFS) for 2015.
productivity growth is to achieve macroeconomic stability by establishing a macroeconomic and institutional setting that allows for a reduction of the primacy of fiscal policy. Reducing economic distortions and increasing domestic competition is required to reallocate resources across sectors: investors rank Argentina 137th out of 138 countries in openness to domestic and foreign competition. Integration into global markets would spur on productivity growth by creating conditions and incentives for better functioning of markets and more efficient use of resources. Argentina stands out for how much it is closed off from the global economy: it is the fourth most closed economy in the world, with total trade to GDP just ahead of Sudan, Pakistan and Brazil and only one free trade arrangement (FTA) in place. Continuous productivity gains, the ultimate driver of sustained shared prosperity, cannot be achieved in such a closed setting. On the structural side, there is also a large productivity agenda in improving firm management practices, and innovation investment and adaption. A precondition for this is to ensure the country has a highly skilled (and malleable) labor force.

25. The duality of the economy presents a challenge to ensure all households gain from an opening up of the economy, and is an obstacle to productivity growth itself. Close to a third of workers are informal, meaning they are more vulnerable to income shocks due to not qualifying for social insurance. Informality also means that workers are less likely to benefit from employer-provided training. Workers being excluded from the formal economy also presents a challenge to the political support for transition to an outward-looking growth model, with a social contract being more likely to form if there is a growing middle class with clear gains from change. There is also a dual economy for agricultural producers and firms engaged in services and manufacturing, with highly productive enterprises that can compete globally alongside low productivity producers and firms. Finally, there are big differences between the capacity of geographical areas across Argentina to benefit from exports, investment and increased domestic competition.

26. But this is not enough, as sustaining shared prosperity over time will require productive and sustainable use of the country’s assets. First is human capital. Enhancing equity of opportunities will be key to guarantee that nobody is left behind in the transition to the new development model. As mentioned above, this is particularly challenging given the dual nature of the Argentine economy, and will require active policies, where investment in human capital needs to be at a central stage. But the country also needs to invest in a more sustainable use of traditionally underinvested natural capital, such as forests, renewable energy and tourism resources. Investment in the country’s nature-based comparative advantage can generate employment and rents. This should include, but is not limited to, the acknowledgment of the negative effects of deforestation, aquifer depletion, and the state of depletion of a large share of agricultural soils, the most important source of rents for the country. Effective management of the adverse consequences of global warming and its heterogeneous social and geographical impact will need to play a greater role.

Pathway to shared prosperity

27. The development model that Argentina needs to move to centers on achieving sustained growth by opening up the economy and putting in place the conditions for private sector growth. This diagnostic identifies four pathways where progress is critical for sustainable growth and an expansion of shared prosperity. Without sound macroeconomic management that brings price stability and a fiscally sustainable path, the transition to a new development model will founder: Pathway 1 concerns putting in place these fundamentals for growth. Economic growth in Argentina has come to rely on domestic demand and largely on the expansion of government spending. The country has begun the move to a more open, outward-oriented development model. Pathway 2 looks at the supporting policies that are necessary. Low investment, very undeveloped capital markets and large physical investment needs have to be tackled. Reducing barriers to trade is only part of the story: the economy has to open up to domestic and international competition, and the highly-concentrated market power that some firms enjoy has to be reduced. For success, a larger group of firms will have to build the capacity to export and compete in a more competitive domestic market.
For the change to a new economic model to endure, growth will have to translate into better quality jobs, and the progress made on reducing poverty will have to continue. Pathway 3 outlines the constraints that will have to overcome to ensure that people can be included in the dividends from a changed economic model. Success will entail bringing in more people to the labor market and increasing their productivity. Of concern, then is the evidence that the population is falling behind in relative terms on educational outcomes—not a good sign for a country that needs to reverse its lagging economic performance and expanding its middle class. Additionally, sustained and inclusive growth will require that everyone, irrespective of socioeconomic background or location, has access to quality services needed to accumulate assets. In the shorter term, it will be also important to enhance the extent to which social safety nets and active labor market policies can mitigate the negative social impacts of reducing market distortions and opening up to domestic and international competition in the transition period. Furthermore, integrating all of Argentina (and not just the richer areas) into the world economy will be important to expand the gains from opening up and making the economy more productive. Finally, pathway 4 outlines how protecting the environment and harnessing the value of nature for development will be essential to ensure the sustainability of economic growth. The policy priorities are outlined in the final section. The transition to new sources of growth for development in Argentina then involves a large and wide-ranging set of policy reforms (see Figure 22 for an illustration of the transition needed). Many reforms in these areas have already started (see Box 3 for further details).

Figure 22. Argentina’s economic transition

<table>
<thead>
<tr>
<th>OLD DEVELOPMENT MODEL</th>
<th>TRANSITION</th>
<th>NEW DEVELOPMENT MODEL</th>
</tr>
</thead>
<tbody>
<tr>
<td>Growing macro and fiscal imbalances</td>
<td>Enabling factors</td>
<td>Sound macro and fiscal framework</td>
</tr>
<tr>
<td>Closed economy</td>
<td></td>
<td>Open economy</td>
</tr>
<tr>
<td>Limited financial and physical capital</td>
<td></td>
<td>Deepened capital markets and logistics</td>
</tr>
<tr>
<td>Low competition, innovation and productivity</td>
<td></td>
<td>High competition, innovation and productivity</td>
</tr>
<tr>
<td>Public sector as driver of jobs</td>
<td></td>
<td>High competition, innovation and productivity</td>
</tr>
<tr>
<td>Low quality services and inefficient social spending</td>
<td></td>
<td>Private sector as driver of jobs</td>
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<tr>
<td>Expanded social safety net</td>
<td></td>
<td>High and equal quality services and efficient social spending</td>
</tr>
<tr>
<td>Extractive and unsustainable use of natural capital</td>
<td></td>
<td>Strengthened social policy spending</td>
</tr>
<tr>
<td>Growth fundamentals</td>
<td>Social and productive Inclusion</td>
<td>Inclusive and climate resilient green growth</td>
</tr>
<tr>
<td>Open development model</td>
<td>Environmental sustainability</td>
<td></td>
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</tbody>
</table>

Source: SCD team
Box 3. Summary of key policy shifts and structural reforms in 2016-2018

Normalization of International Relations

• After 15 years, Argentina returned to international capital markets with the largest single bond issuance in history for an emerging country (April 2016).

Main Reforms

• **Monetary Policy**: The Central Bank formally adopted an inflation-targeting regime with a floating exchange rate. In addition, it committed to gradually decrease financial assistance to the central government.
• **Statistics**: Since January 2016, the credibility of the National Statistical System was restored; as a result the IMF lifted its Declaration of Censure on Argentine official statistics (November 2016).
• **Export and imports**: Export taxes were eliminated, with the exception for soybeans, which were reduced and for which the Government announced a scheduled further reduction. An imports administration system replaced the mostly discretional licensing regime in place until 2015. Foreign exchange controls were lifted after four years.
• **Subsidies**: Energy, water and transport subsidies were reduced while keeping a social tariff for low income users in water and transport and creating a social tariff for residential electricity and natural gas consumers. Energy subsidies will continue to decrease gradually until they are eliminated by 2019, with the exception of social tariffs.
• **Taxes**: The PIT tax floor was raised and family allowances were expanded to reach 4.1 million children, up from 2.9 million. A successful tax amnesty program was implemented to encourage repatriation of undeclared funds held abroad, resulting in additional revenues of 1.6 percent of GDP. Recently, a capital gains tax was implemented for the first time.
• **Pension System**: Argentina’s pension system accounts for 40 percent of the national budget. In December 2017, Congress approved a change in the pension indexation formula in line with international practice, and put in place the Universal Pension for the Elderly (PUAM).
• **Competition**: A new Competition Law, which modernizes the regulatory framework for antitrust policy, including setting up a new authority with greater independence, introducing a leniency program for cartel-agreements (such as price-fixing), improved sanctioning rules for anti-competitive practices and a more efficient merger control system, was passed by Congress on May 9, 2018.
• **Capital markets**: A new Capital Markets Law, which modernizes the regulatory framework for capital markets, including by enhancing corporate governance, expanding the supply of financial assets, and targeting the widening of the domestic investor base, was passed by Congress on May 9, 2018.
• **PPPs framework**: Congress approved a new PPPs framework to help address the country’s existing infrastructure deficit and to stimulate private investment in key sectors of the economy such as infrastructure, housing, services, production, applied research and technological innovation (November 2016).
• **Transparency**: President Macri declared his target of placing Argentina among the top countries in the world in terms of transparency. These efforts include Access to Information Law that became effective in September 2017, the passing of the Corporate Criminal Responsibility Law to fight corruption in November 2017, ongoing reforms in procurement for public infrastructure and public procurement, and a renewed commitment for Open Government with the open data portal and the implementation of the second open government action plan.
• **Fiscal pact**: Long-standing disputes over transfers between the national government and the provinces were settled in a fiscal pact of November 2017. Provinces agreed to freeze current public expenditures in real terms and to decrease the burden of the highly distortive provincial turnover taxes.
• **Public employment**: The Government enacted a voluntary separation scheme at the federal level to rationalize the public wage bill (April 2018). The program targets older employees from the national administration and government agencies.

Reforms under discussion on Structural Agenda

• **Labor Market Reform**: Informal labor accounts for one third of salaried employed workers. The Government is discussing a labor market reform with the aim of providing incentives for formalization.
• **Trade**: Argentina is one of the most closed economies in the world. Trade reform needs to be carefully designed since a significant portion of labor is employed in protected sectors. Trade discussions between Mercosur and the EU have resumed. The Pacific Alliance accepted Argentina as an observer member.
• **Education**: Argentina has high school dropout rates and low learning outcomes. The Government made important strides in moving evaluation to the center of debate, but further reforms are needed.
Chapter 2. Growth

Drivers of economic growth

29. The aftermath of the 2001/02 crisis was an opportunity to address the country’s recurrent macroeconomic imbalances and set the basis for long-term growth. The collapse of the Convertibility Regime and default on foreign obligations resulted in a massive real depreciation of the peso, a sizeable output gap, low wages, and a large fiscal surplus. In a context of expanding world demand and increasing commodity prices, the Argentine economy recovered vigorously, growing 5.9 percent, on average, between 2003 and 2011. But this was further fueled by expansionary fiscal and monetary policies to support high levels of private consumption (see Figure 23). The continued expansion of aggregate demand was met by increased intensity in the use of labor and capital, and by some productivity gains, mostly explained by a recovery from the large fall in 1998-2002 (see Figure 24).

30. By 2011, the demand-driven growth strategy showed signs of exhaustion, with macroeconomic imbalances becoming self-evident. General government expenditures had increased at an unprecedented pace, growing by over 11 percentage points of GDP between 2004 and 2011 to fuel mostly current expenditures on subsidies, pensions and wages. Increased tax pressure failed to keep up with expenditures, leading to a rapid deterioration in the fiscal position that turned a 3.3 percent consolidated surplus in 2004 to a 7.8 percent deficit in 2016. Growing fiscal imbalances put pressure on the real exchange rate and current account, which moved to deficit for the first time in almost a decade. To tackle external imbalances the government turned to protectionist policies such as quantitative restrictions on foreign trade and foreign exchange markets, hurting productivity.

31. Macroeconomic imbalances grew wider in the years after 2011, following the deepening of the policies that generated them in the first place. In 2011-2015, private job creation almost stalled.

\[ \text{Figure } 23. \text{ Growth decomposition by demand component, period annual averages, 1998-2017, in percent} \]

\[ \text{Figure } 24. \text{ Growth contributions by factor of production, period annual averages, 1998-2015, in percent} \]

Source: Data from Ministry of Treasury, and the World Bank’s WDI.

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54 Geometric average, including the 2009 recession due to the international financial crisis.
Government expenditure continued to grow way beyond historical records, productivity collapsed, and the current account deficit widened. The lack of access to international credit markets translated into a growing monetization of fiscal deficits, which further fueled inflation. The economy thus entered an annual cycle of recessions and expansions, with real GDP a mere 2.5 percent higher in 2017 than in 2011, a fall if measured in per capita terms.

32. **With increasingly protectionist policies and a continuous real appreciation of the peso, the tradable sectors’ share of GDP fell.** Export taxes, high import tariffs, low competition, discretionary import licenses, and quotas in currency markets, combined to reduce the share of tradable sectors in output, despite favorable commodity prices and external conditions. Industries that produce goods, such as agriculture or manufacturing, grew by less than half the rate of the service sectors in the 2004-2016 period (25 versus 57 percent). As a result, the share of goods-producing sectors in GDP (at producer prices) decreased by 12 percentage points from 44 to 32 percent. The share of services grew from 56 to 68 percent in the same period.55

33. **The expansion of non-tradable sectors resulted in a misallocation of employment to low-productivity activities.** The high-growth sectors since 2004 are mostly non-tradables, such as construction, health services, or public administration. This is due to the continuous real exchange rate appreciation but also due to deliberate policies to protect some sectors perceived as being major contributors to job creation, especially for low-skilled workers. These high-growth sectors have also experienced low productivity growth, (see Figure 25), a sign that productivity in the high-employment growth sectors has failed to catch up with the influx of workers. Unless those sectors had relatively high productivity to begin with, which is not the case,56 this points to a misallocation of employment to low productive uses.57 This misallocation is a source, but also a result of low aggregate growth. Low growth results in low job creation, which in a context of a growing labor force (demographic bonus) leads to some sectors needing to absorb the increase in the labor force, typically public administration or public education. This vicious cycle generates a trap of low productivity, low job creation, and growing labor misallocation.

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55 Shares in current prices. In constant 2004 prices, the share of the service sector increased 5 percentage points.

56 The sectors with highest value added per worker in 2004 were mining and oil, fishery, and financial intermediation, in that order.

57 A full assessment on the extent of resource misallocation in Argentina is not possible due to serious data limitations, so these findings should be taken with caution. For example: (i) value added per worker is an imperfect proxy for marginal productivity, especially for sectors such as public administration, (ii) sectors are defined rather broadly (with no disaggregation within manufacturing for instance), (iii) 2004 is not the best baseline year, etc. Nevertheless, Figure 25 illustrates an important point: the reallocation of workers to more productive sectors will be key to ignite productivity growth.
Figure 25. Change in value added per worker and change in employment by sector, 2004-2016, in percent

Notes: Bubble size represents employment in 2016. Includes formal and informal employees. Source: Calculations based on INDEC data.

34. **Low capital depth and shallow financial markets are another source of low productivity.** Since 2004, the capital-output ratio is on average 15 percentage lower than in the 1980-2004 period. This reflects the permanent negative shock of the 2001/02 crisis on credit markets, and its impact on investment: the private-credit to GDP ratio fell from an average of 22 percent in the two decades prior to the crisis to an average of 13 percent since.58 Lack of trust in the domestic financial system is also reflected in the fact that Argentine residents held a large share of their wealth offshore. Wealth held abroad by Argentine residents is estimated at 35 percent of GDP, the fourth largest among large economies, after major oil-exporting countries (see Figure 26). President Macri put in place a tax amnesty for the disclosure of undeclared assets that lasted from July 2016 to March 2017. Assets worth over a fifth of GDP were declared (US$116.8 billion). This did not induce nationals to repatriate these assets: about US$93 billion of the assets disclosed are continuing to be held offshore.

58 WDI (2017).
35. **In a challenging macroeconomic environment, the productivity and productive capabilities of Argentina’s firms barely improved over the past two decades.** According to the World Enterprise Surveys for 2010 and 2017, labor productivity at the firm level fell an average of close to 6 percent in those years. Moreover, an economic fitness analysis, which measures the underlying capabilities that support a country’s productive structure, shows Argentina has experienced fitness losses in several mid and high-complexity industries (such as electrical equipment, transportation and petroleum/coal processing). Since 2000, Argentina’s fitness has increased only marginally and in very few sectors (mainly in metal products and plastics, see Figure 27). On the GDP-fitness plane, Argentina’s position is close to that of Russia and Brazil (see Figure 28). Due to the high correlation between economic fitness and GDP, diversification and capability upgrading in the areas of strongest fitness such as chemicals, crops, animal products and food/beverages provide potential opportunities for further GDP growth.

**ARGENTINA**

Systematic Country Diagnostic

Figure 26. Offshore wealth, 2007, in percent of GDP

Sources: Data from Alstadsæter, Johannesen and Zucman (2017).

Note: All countries with a GDP of greater than US$200 billion in 2007.

Figure 27. Product fitness for 2000 and 2015


Figure 28. Correlation between product fitness and GDP per capita, 1995-2014, in logs

36. **With Argentina in need of more firms exporting, innovating and diversifying their production, recent policy measures are starting to have impact.** More than 80 percent of firms in Argentina are micro and small firms. However, most formal employment is generated by the few large firms. The Argentine economy is characterized by a high concentration of production, both geographically—in Buenos Aires Province, the Autonomous City of Buenos Aires (*Ciudad Autónoma* de Buenos Aires, CABA), Santa Fe, Cordoba, and Mendoza—as well as in terms of production sectors, with retail businesses, agriculture and light manufacturing accounting for the bulk of production. Although the total number of firms has slightly declined since 2013, net firm creation for all sizes of firms has been positive for the last two years. Firm entry has exceeded firm exit across the firm size distribution. Although few firms manage to grow sustainably—after five years existing, most micro, small, and medium sized firms continue to be classified in the same category—the “graduation rate” of firms into higher firm size categories has increased continuously over the last three years. This slow recovery is mirrored by the small proportion of fast-growing firms, those that generate most new private employment. Since 2006, the number of exporting firms has fallen. Only during the last two years has this trend stopped and started to reverse with exports increasing on both the extensive margin (new firms entering) and the intensive margin (more exports by existing exporters). Exporting firms are the only type of firms seeing an increase in employment according to the World Bank’s latest Enterprise Survey (2017).

37. **For a successful transition to a new development model, Argentina needs to generate the macroeconomic conditions and conduct the structural transformations to allow firms to thrive.** Macroeconomic conditions include sound fiscal and monetary policies to reduce volatility, and expenditures and revenue policies to promote growth, which include important institutional reforms. New sectors and firms can emerge as sources of sustained growth provided barriers to investment, trade and competition are removed. Recent growth has come mainly from services, agriculture and fishery, and construction, which is growing at the fastest pace in a decade (Figure 29). Imports of machinery and capital goods have been growing. Employment growth is coming mostly from tourism—in hotels and restaurants.

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Pathway 1: Putting in place the institutional and macroeconomic fundamentals for growth

Macroeconomic stability: moving beyond boom-bust cycles

38. The use of fiscal and monetary policies as a buffer rather than as an amplifier of economic shocks is of first order importance to avoid boom-bust cycles. Macroeconomic mismanagement in the form of procyclical fiscal and monetary policies have been a main driver of Argentina’s excessive macroeconomic volatility. Procyclical international capital flows and low domestic financial market depth exacerbate the problem. These repeated boom-and-bust episodes have been accompanied by big changes in the economic context and shifts in policies, undermining confidence in the long-term performance of the economy and the credibility of policy makers.

39. Fiscal policy in Argentina has been highly procyclical throughout its history, even within LAC, a procyclical region. Over the last 60 years, LAC countries and most developing economies have had procyclical fiscal policies (see Figure 30). Argentina is amongst the most procyclical economies in LAC (fifth), above the regional average. Fiscal procyclicality usually results from the combination of political pressures to spend in good times and the inability of emerging economies to borrow in bad times.

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See, for example, Buera et al (2011).
40. In contrast to most of its LAC peers, Argentina’s fiscal policy has become even more procyclical in the last 15 years. Most LAC countries improved fiscal management in the last 15 years, as countries learned from experience and implemented sounder fiscal policies in the context of favorable external conditions. While more than 90 percent of LAC countries carried out procyclical fiscal policies during 1961-1999, 60 percent continued to do so between 2000-2016. Furthermore, though still positive, the average LAC correlation coefficient went down from 0.24 to 0.13 after the year 2000. This was not the case of Argentina, where the correlation between (the cyclical component of) GDP and government expenditure increased from 0.35 to 0.72. The increase in fiscal procyclicality is true even excluding the 2001/02 crisis and its aftermath. Overall, Argentina became the second most procyclical country in LAC since 2000, after Venezuela. If the analysis takes into account fiscal multipliers, the procyclicality of fiscal policy becomes even more worrisome. Although there is no agreement about its magnitude in developing and emerging economies, there is evidence that long-run fiscal multipliers are as large as 1.3 or 1.4 in closed economies like Argentina.\footnote{Long-run multiplier estimates of Ilzetzki, Mendoza, and Vegh (2011) using a Structural Vector Autoregression Approach (SVAR).} This implies that procyclical fiscal policies amplify greatly the economic cycle.

41. Federal expenditure drove the increase in fiscal procyclicality, but it is still higher at the provincial level. Fiscal procyclicality at the provincial level is high but has remained relatively stable before and after the 2001/02 crisis (see Figure 31). All provinces have procyclical public expenditures except for Neuquen, rich in hydrocarbons. Although there are reasons to believe that sub-national governments should be less countercyclical than the federal government, who ultimately bears the burden of macroeconomic stabilization,\footnote{See for example Musgrave and Musgrave (1989); Oates (1972, 1999).} fiscal procyclicality at the provincial level is very high. This is to a large extent a result of the institutional design: significant spending decentralization processes in the 1970s and 1990s resulted in large vertical imbalances, funded by procyclical revenue transfers from the federal government. The narrow
access to alternative financial sources translates procyclical transfers at the federal level into procyclical policies provincial level. The overall increase in fiscal procyclicality has, however, been driven by federal government expenditures, whose correlation coefficient more than doubled from 0.24 in 1961-1999 to 0.49 in 2006-2016.

**Figure 31. Fiscal Procyclicality by level of government, 1961-2016**

Source: Calculations based data from on Ministry of Treasury.

42. **Recurrent transfers have been the main driver of the increase in fiscal procyclicality, while pensions and wages have historically been the most procyclical sub-components of fiscal policy.** At the federal level, pensions are not only the biggest expenditure item in the budget, but also the one that contributed the most to fiscal procyclicality since 1961 (Figure 32). However, the increase in procyclicality in the last decades has been driven by wages, capital expenditure, and especially transfers (mainly energy and transport subsidies). At the sub-national level, the dynamics was more uniform across expenditure items (Figure 33). Nonetheless, recurrent transfers to municipalities (mainly to finance municipal wages) not only is the most important contributor to provincial procyclicality, but also the one that increased the most after the year 2000.
Monetary policy has also been an amplification mechanism for macroeconomic shocks. Argentina has the third most procyclical monetary policy in LAC. The main source of monetary procyclicality in Argentina has been fiscal procyclicality, with the Treasury using the Central Bank as a regular source of financing for its continuous deficits, as will become clear in the next subsection. However, monetary policy has also been an independent source of macro instability. The 2004-2008 period of fiscal surplus is a good example of procyclical monetary management not driven by fiscal considerations. In that period, countries of South America were subject to similar real appreciation pressures due to the commodity price boom. Real exchange rates appreciated to a similar order of magnitude across countries, 11.6 percent on average (see Figure 34). Depending on monetary policy, real appreciation can materialize either through a nominal exchange rate appreciation, or an increase in domestic inflation. All countries except for Argentina took the first path, which resulted in single-digit inflation (5.1 percent on average). Argentina, on the other hand, used monetary policy to prevent the peso from appreciating in nominal terms. As a result, real appreciation was met by a large increase in prices, 14.6 percent on average (see Figure 35).

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The RER is defined as $e \equiv \frac{E P^*}{P}$, where $E$ is the nominal exchange rate (LCU per US$), $P^*$ is the U.S. CPI, and $P$ is the domestic CPI. A real appreciation is a decrease in $e$.
44. **Macroeconomic management to tap Argentina’s unusually volatile cycle is thus a precondition for sustainable growth.** Argentina needs to build fiscal space in good times to be able to run countercyclical fiscal policies in bad times. To this end, the role of automatic stabilizers in the federal budget should be heightened, and institutional arrangements such as the establishment of sovereign wealth funds could be evaluated once fiscal pressures ease. At the provincial level, the procyclicality of public expenditure is tied to the nature of transfers to provinces from the federal government. The recently enacted Fiscal Pact, which increases provincial financial autonomy and establishes spending rules at the provincial level is an important step. Alternatives such as the establishment of a countercyclical fund across provinces could help them share risks to smooth-out regional shocks. On the monetary side, a consensus on the importance of an independent monetary authority is a prerequisite for countercyclical monetary policies.

**Expenditure and revenue policies to support growth**

45. **An improved fiscal framework is needed to reduce economic distortions and better support growth.** A significant growth in the size of the public sector such as the one experienced in Argentina in the last decade has economic effects that go beyond fiscal sustainability concerns. First, it increases real appreciation pressures, which results in a reallocation of resources away from traded and into non-traded, often unproductive, sectors. Second, it crowds out the private sector, increasing the returns to rent-seeking activities and diverting effort and talent from more productive endeavors. In a resource-constrained environment, it also diverts financing from the private sector, given the large returns that can be made on sovereign bonds. Third, given the relatively high level of informality, increased fiscal pressure on the formal sector becomes substantial, which limits the amount and scope of potentially profitable projects and might reduce incentives toward formality. Moreover, larger public expenditure did not translate into a more efficient provision of public services or better infrastructure. It instead concentrated on current expenditures such as pensions or energy subsidies, which do little to enhance productivity and, in the case of subsidies, can disrupt the functioning of strategic sectors. On the revenue side, the large increase in the tax burden was not based on a sound and progressive expansion of the tax base but relied heavily on emergency and distortionary taxes.

46. **The public sector in Argentina expanded at an unprecedented pace over 2006-2016, due to an expansion in public employment and wages, and spending on pensions and subsidies.** While Argentina’s overall public sector has represented historically around 26 percent of GDP—the period average over 1961-
2006—expenditure to GDP reached 41.2 percent in 2016. Public spending grew 15.2 percent of GDP between 2006 and 2016 (see Figure 36). This expansion, was concentrated on current spending (rise of 15.4 of GDP), capital expenditure (remaining at about 3.7 percent of GDP, just 1 percent higher than the 1990s average) did not benefit from this expenditure boom. The large rise in public spending is due to a large increase in public employment and wages (increase of 4.1 percent of GDP), a strong increase in pensions (social security spending rose by 4.5 percent of GDP) and a significant increase in energy and transport subsidies (transfers to private sector increased by 3.8 percent of GDP) (see Figure 37). Pension spending rose due to an expansion in coverage—the incorporation of non-contributory pensioners to the system for an almost universal coverage—and to the introduction of an automatic indexation mechanism in 2009 that resulted in large increases in real earnings for pensioners.

![Figure 36. Public expenditure, general government, 1961-2016, in percent of GDP](image)

![Figure 37. Total expenditure increase, 2007-2016 by component, in percent of GDP](image)

**Source:** Calculations based on data from Ministry of Treasury.

**Source:** Calculations based on data from Ministry of Treasury.

47. **After a large expansion in the last decade, Argentina’s public spending on salaries and social security benefits is higher than most of comparators:** the wage bill in Argentina is close to 12 percent of GDP, almost double the regional and new HIC average, and higher than the OECD average. Expenditure on social security, which increased due to an expansion in pension coverage and a generous new indexation scheme, is higher than regional and new HIC averages, but still below OECD levels (see Figure 38). Pension spending as a share of GDP (11.3 percent) is among the highest in the world, higher than in much “older” countries like Japan and Bulgaria (see Figure 39), and has almost doubled in the past decade.
### Figure 38. Public spending comparison on selected items, in percent of GDP, 2015

<table>
<thead>
<tr>
<th>Item</th>
<th>ARG</th>
<th>Regional</th>
</tr>
</thead>
<tbody>
<tr>
<td>Wage Bill</td>
<td>11.7</td>
<td>6.8</td>
</tr>
<tr>
<td>Social benefits</td>
<td>6.9</td>
<td>8.3</td>
</tr>
</tbody>
</table>

### Figure 39. Pension expenditure in percent of GDP, and share of population older than 65 years of age, circa 2015

**Sources:** Data from Ministry of Treasury, IMF and OECD.

**Source:** Data from Ministry of Treasury, IMF and OECD

#### 48. The tax burden also increased substantially, reaching OECD levels, though relying heavily on indirect taxes.

The tax burden in Argentina reached 31.5 percent of GDP in 2016, higher than regional peers, but similar to new HIC and OECD peers (Figure 40). Taxes rose by more than 10 percentage points of GDP between 2001 and 2016, based on the introduction of new “emergency” taxes (e.g. export duties and a financial transaction tax), the economic recovery and higher rates (e.g. social security contributions and the provincial turnover tax). Unlike OECD countries and to a lesser extent, new HIC peers, Argentina relies heavily on indirect taxes, including the distortive provincial transaction tax and financial transactions tax, and has a narrow tax base. Argentina stands out for having low personal income tax (PIT) revenues compared to the OECD average and new HICs (Figure 41) due in part to generous treatment of personal deductions and the proliferation of simplified tax regimes, and a very high non-taxable income threshold—compared to the average wage, the minimal taxable income level is much higher than in OECD countries (see Figure 42). Broadening the tax base and reducing special regimes and exemptions, while shifting the structure toward higher direct taxes and less indirect distortive ones, are the key tax challenges faced by the country looking forward. The recent tax reform of December 2017 aims to reduce the weight of distortive indirect taxes over time and to decrease the burden of social security contributions for lower income workers.

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64 Taxes on goods and services are higher than all its peers both in relative (i.e. they represent 46 percent of overall tax revenues compared to 33 percent in OECD) and in absolute terms (14.5 percent of GDP against 10.7 percent of GDP in OECD).

65 See Gomez Sabaini and Morán (2012).
Figure 40. Tax burden, 2016, in percent of GDP

Figure 41. Direct tax composition, 2016, in percent

Note: PIT: Personal Income Tax; CIT: Corporate Income Tax.
Sources: Data from IMF’s Government Finance Statistics (GFS), and OECD database

Figure 42. Income threshold where single taxpayers start paying income tax, measured as a multiple of the average wage, 2016


49. A similar story took place at the subnational level. Overall provincial expenditures increased substantially (by 40 percent) in the last decade, only partially matched by own revenue growth, thus putting additional pressure on the transfer system to close the fiscal gap (given the lack of access of provinces to financial markets). Likewise, provincial tax schemes shifted toward distortionary taxes, such as the Turnover Tax (Ingresos Brutos in Spanish), which generates internal trade barriers as the tax rate is heterogenous among provinces, and increases domestic prices and discourages exports by being a cascade sales tax.

50. Fiscal consolidation is still essential to stabilize public debt. The federal government’s gross public debt in 2017 is estimated to be around 57.1 percent of GDP (excluding intra-public-sector debt, the ratio goes down to 29.4 percent of GDP). Given the size of current fiscal imbalances, a fiscal consolidation is essential to stabilize public debt. The overall fiscal deficit reached 6.5 percent of GDP in 2017: of which, 6.0 percent of GDP corresponds to the central government deficit, while 0.5 percent of GDP is due to subnational governments (see Figure 43). In May 2018, President Macri announced that Argentina would start
talks with the IMF to secure a precautionary credit line. The announcement took place following a 5 percent fall in the peso at the beginning of the day, and growing worries of a continued run on the currency. The timeline for reducing the fiscal deficit was also made more ambitious, with the 2018 target reduced from 3.2 to 2.7 percent of GDP. As of the beginning of August 2018, for 2019 the target was set at a 1.3 percent of GDP primary deficit, reaching a 0.2 percent of GDP surplus in 2020. The planned fiscal consolidation effort should yield a declining federal public debt-to-GDP ratio after 2018. The peso depreciation in 2018 is expected to increase the public debt-to-GDP ratio to 65 percent. But implementation of the Government’s fiscal program would make public debt converge toward 53 percent of GDP by 2023. However, there are risks to debt sustainability. The standard DSA stress test shows that under a real exchange rate shock (50 percent real depreciation with 0.25 pass-through) debt could jump to 81 percent of GDP, above the high-risk threshold. Thus, given that almost 70 percent of public debt is denominated in foreign currency, a peso depreciation is a large risk. Debt is also vulnerable to a growth shock (negative growth in 2019 and 2020), as the parameters of the stress test would take it to 70 percent of GDP (see Figure 44).

51. **A sound fiscal policy is also necessary to solve Argentina’s chronic inflation problem.** Since 1945, the year when chronic inflation started, Argentina has seen double digit inflation (or more) in 61 years (out of 73). This includes three hyperinflation episodes between 1989 and 1990 (see Figure 45 for a cross-country comparison starting in 1960). Only between 1994 and 2001, did Argentina experience consistently low inflation, the cost of which was having a strict currency board regime. For the most part, inflation can be explained by the subordination of monetary policy to fiscal policy. Figure 46 shows the evolution of the fiscal balance and the inflation tax, both as a share of GDP. Both series are close mirrors of each other, except for the currency board years, where monetary policy was limited to defending the peso-dollar parity.

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67 The inflation tax refers to the penalty for holding cash due to inflation. This is seen as a tax, as it ultimately represents a transfer of real resources to the State, who has monopoly power over money printing, the ultimate cause of inflation. It is computed as the inflation rate times the stock of money in the economy (as measured by M1, which is cash holdings and demand deposits of the public).
The inflation tax is on average 3.3 percent of GDP, reaching peaks of 11 percent in 1975 and 9.5 percent in 1989.

**Figure 45. Average annual inflation rate in comparator countries since 1960, in percent**

<table>
<thead>
<tr>
<th>Year</th>
<th>Regional</th>
<th>New HICs</th>
<th>OECD</th>
<th>ARG</th>
</tr>
</thead>
<tbody>
<tr>
<td>1944</td>
<td>41.3</td>
<td>23.3</td>
<td>5.0</td>
<td>63.8</td>
</tr>
</tbody>
</table>

**Figure 46. Fiscal balance and inflation tax, in percentage points of GDP, 1944-2013, in percent**

Sources: Data from the World Bank’s WDI, Treasury Department, INDEC, and calculations based on BCRA.
Note: These averages exclude hyperinflation episodes in Argentina, Brazil and Perú.

52. **The composition of public expenditure in Argentina and its chronic fiscal deficits are detrimental to growth.** The country needs to reduce the fiscal deficit to limit external vulnerabilities, crowd-in private investment, help relative prices adjust in favor of tradable sectors, and allow for an independent, anti-inflationary monetary policy. At the same time, it is important to protect the vulnerable from the adverse impacts of fiscal consolidation. Over time, the country needs to gradually re-balance its expenditure profile to increase the share of investment to support its productive and welfare needs. On the revenue side, a reduction of overall tax pressure should include a re-balancing of the tax system to rely more on direct taxes such as the PIT and move away from distortionary and regressive taxes such as the financial transactions tax and a provincial turnover tax levied on sales that is levied at each stage in the supply chain without any tax credits for tax paid at earlier stages of production (*impuesto sobre los ingresos brutos*). Reform of the tax structure or indeed a reduction in tax pressure are, however, challenges that can only be faced once an elimination of the fiscal deficit has been achieved.

**Institutions for growth**

53. **Moving toward a new growth model based on greater economic diversification and productivity requires a different set of institutions.** According to the World Development Report (WDR) 2017 *Governance and the Law*, although it is possible for economies to start growing without substantive changes in the nature of governance, sustaining growth over time is difficult without addressing fundamental institutional challenges. Indeed, the historical experience of countries that “escaped” the middle-income trap and converged toward high-income economies suggests that a range of institutional reforms (i.e. strengthening the role of check-and-balances institutions, promoting greater independency and competition in the media market; curbing corruption through effective anti-corruption reforms; etc.) were instrumental to create a level playing field among firms, enable contract enforcement and more efficient resource allocations, ultimately contributing to long-term growth and productivity gains.
54. Power asymmetries and vested interests, however, may prevent the adoption and implementation of reforms needed to enable the transition to a new economic model. In Argentina, a range of priority policy and institutional reforms are instrumental to move the country on a path toward greater diversification and productivity. Such reforms are expected to alter the bargaining influence and preferences of political and economic actors, creating winners and losers. In the face of these changes, interest groups, currently benefiting from the status-quo, have incentives to oppose new economic conditions and thus prevent efficiency-oriented reforms from happening, leading to a low-equilibrium that undermines the growth potentials. These political economy constraints may be particularly binding in Argentina because actors who gained during an earlier or current growth phase may be powerful enough to block institutional changes that threaten their positions and resist the switch to a new growth model based on firm entry, competition, and innovation. The notebook scandal, which started to unfold at the beginning of August 2018, offers the country an opportunity to examine past institutional failures in-depth and to put its governance institutions on new and more robust foundations, ensuring that a functioning, empowered system of checks-and-balances exists.

55. Historical legacies of institutional instability tend to reproduce a low-level equilibrium where the incentives of policymakers and interest groups are dominated by short-term considerations (cortoplacismo) and opportunistic behavior. For a large part of the twentieth century, institutions of a variety of types have consistently failed to take root in Argentina, and the country experienced a level of institutional instability remarkable even by regional standards. Between 1930 and 1983, 12 presidents were removed by extra-constitutional means and successive military coups led to radical institutional reversals and U-turn in economic policies. Since 1928, only four elected presidents completed their full term in office; two of them rewrote the Constitution to prolong their presidencies, and another one tried to amend it to allow the President to run for a third term. Indeed, Argentina’s history of instability has left an imprint on how political and economic actors interact, fostering a culture of non-compliance with formal laws and procedures and recurrent efforts to circumscribe, manipulate and change rules and policies whenever they are perceived to harm short-term interests of powerful actors.68

56. Distributive conflicts between the federal and the provincial governments have also undermined the ability of institutions to enforce long-term commitment to policy reforms and induce the coordination and cooperation needed to carry them out. The stark economic inequalities among provinces and the structural features of the Argentina’s federal system (vertical imbalance) imply that most provinces are highly dependent from the national government to finance their expenditures. In turn, presidents need to secure votes in Congress to implement economic policies. As a result, the policymaking process can be characterized as ‘deals’ or exchanges’ between president and governors69, whereby governors grant political support in exchange for fiscal transfers. The governors’ political support is provided through the electoral channel (by mobilizing votes during presidential elections); and the legislative channel70 (by securing votes from provincial legislators for the President’s policy agenda and projects in the House and the Senate)71. Moreover, agreements are often achieved through informal channels, undermining the legislative and oversight functions of the Congress72—whose performance is weak in comparative

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70 Due to the closed-list proportional electoral system, governors control the candidate selection process and the nominations for congressional elections, to the point that political careers of individual politicians are often structured and decided at the provincial level (Jones 2002; Jones and Hwang 2005). Consequently, “president need to negotiate not only electoral but also legislative support with governors” (Gonzales and Mamone 2015: 55).
71 De Luca, 2008; Spiller and Tommasi, 2008.
72 In the WDR 2017 terminology, this refers to “deal-based” versus “rules-based” elite bargains.
As a result, Argentina’s rulemaking process often lacks transparency and there is little space for engagement with key stakeholders and beneficiaries on the proposed content of laws and regulations (Figure 48). The political economy of the budget process in Argentina illustrates this point, showing how Congress plays only a marginal role relatively to other more influential players. Moreover, the historical tendency of both civilian and military governments to replace Supreme Court justices with political loyalists have weakened the judiciary performance, including its ability to enforce laws and sanction non-compliance. Finally, political interference in the public administration have undermined the development of a professional bureaucracy, leaving Argentina with weak cooperation and coordination mechanisms among government agencies as well as across levels of government. Consequently, laws and regulatory practices are often enforced in a decentralized and fragmented manner, with different sectors of the public administration operating under different regulations and overlapping responsibilities. In turn, this institutional environment allows opportunities for inefficiencies and rent-seeking behavior.

**Figure 47. Consolidated Regulatory Governance Score, 2016**

<table>
<thead>
<tr>
<th>Country</th>
<th>Score</th>
</tr>
</thead>
<tbody>
<tr>
<td>Argentina</td>
<td>0.8</td>
</tr>
<tr>
<td>Turkey</td>
<td>0</td>
</tr>
<tr>
<td>Peru</td>
<td>1</td>
</tr>
<tr>
<td>Chile</td>
<td>2</td>
</tr>
<tr>
<td>Slovak Republic</td>
<td>3</td>
</tr>
<tr>
<td>Czech Republic</td>
<td>4</td>
</tr>
<tr>
<td>Brazil</td>
<td>5</td>
</tr>
<tr>
<td>Poland</td>
<td>6</td>
</tr>
<tr>
<td>Colombia</td>
<td>7</td>
</tr>
<tr>
<td>Malaysia</td>
<td>6</td>
</tr>
<tr>
<td>Mexico</td>
<td>5</td>
</tr>
<tr>
<td>Korea, Rep.</td>
<td>4</td>
</tr>
</tbody>
</table>

**Figure 48. Congress Capabilities Index, Average 1994-2013**

Source: Data from Global Indicators of Regulatory Governance.

Source: Data from Franco Chuaire and Scartascini (2014).

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73 Hallerberg; Scartascini and Stein, 2009; Bonvecchi 2008; Rodriguez and Bonvecchi, 2006.
74 Spiller and Tommasi, 2008.
75 The score captures good regulatory management practices in three core areas: publication of proposed regulations, consultation around their content, and the use of regulatory impact assessments. Each core area has multiple sub-components included in the overall score.
57. This opportunistic and non-cooperative behavior has implications for economic activities. On the one hand, the expectations that certain policies might not endure has inhibited firms’ propensity to invest and take advantage of otherwise favorable conditions. The failure of trade reforms to change industrial behavior during the 1990s illustrates this point. On the other hand, the tendency of governments to react to economic shocks through various redistributive mechanisms (subsides, public expenditures, fiscal transfers and taxation of export-oriented sectors) further contributes to undermine capital-intensive investments as economic actors expect their profits to be confiscated to address short-term budgetary needs.

58. The institutional weakness of the state apparatus has created a social environment where perceptions of corruption continue to permeate public affairs. Argentina ranks 85 out of 175 countries on the 2017 Corruption Perception Index. Both the Global Competitiveness Index (GCI 2017-2018) and the World Bank 2017 Enterprise Survey report corruption as one of the most problematic factors for doing business in Argentina, with 13 percent of firms having to pay bribes to secure government contracts (slightly below the regional average of 14.4 percent). These perceptions tend to correlate with public opinion surveys: about 41 percent of respondents in Argentina report the level of corruption as increasing over the previous 12 months, and believe the Government is doing a bad job at fighting corruption; and 16 percent report having paid a bribe to a public official to get access to basic services (Transparency International 2017).

59. Over time, endemic corruption can generate significant economic and social costs, undermining citizens’ trust in public institutions. The challenges related to corruption in Argentina are quite broad, they extend through all of the areas measured by the World Economic Forum’s Global Competitiveness Index, taking in ethics, corruption and undue influence (for example judicial independence, diversion of public funds, public trust in politicians, irregular payments in public contracts, and favoritism in the decisions of government officials), and with notable weaknesses when compared to peers within the

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76 The Regulatory Enforcement indicator does not assess which activities a government chooses to regulate, nor does it consider how much regulation of a particular activity is appropriate. Rather, it examines how regulations are implemented and enforced. To facilitate comparisons, this factor considers areas that all countries regulate to one degree or another, such as public health, workplace safety, environmental protection, and commercial activity.

77 Acuna (1991) shows that export promotion policies did not produce the expected changes in investment decisions by industrial firms due to the uncertainty of the duration of the policies (quoted in Spiller and Tommasi 2003). This is consistent with the general argument that "it is not trade liberalization per se, but credible trade liberalization that is the source of efficiency benefits" (Rodrick 1989).

78 https://www.transparency.org/whatwedo/publication/global_corruption_barometer_people_and_corruption_latin_america_and_the_car
region in the areas of irregular payments in tax collection and ethical behavior of businesses. By facilitating the inefficient allocation of scarce resources, corruption can undermine private investments and competitiveness in the international market. Besides its economic effects, corruption puts the legitimacy of state institutions into question: according to the latest Latino barometer survey, only about one third of respondents trust the government. While this is in line with regional and global trends, it is nevertheless worrying as it can undermine the social contract between the state and the citizens. 79

60. The current administration is putting in place important changes in the legal framework to promote transparency, fight corruption and strengthen public integrity. In 2016, the Government approved the State Modernization Plan (Decree 434/2016). The plan, which is to be implemented by the recently created Ministry of Modernization, aims to achieve a public administration at the service of citizens within a framework of efficient, effective, and good-quality service delivery. The same year the Congress approved a Right of Access to Information Law (Law 27,275), which entered into force on September 27, 2017. Until its enactment, Argentina was one of the few Latin American countries which did not have a law in this area, together with Bolivia, Costa Rica, and Venezuela.80 The Government has also relaunched an open data policy, which it had timidly begun with the incorporation of Argentina into the Open Government Partnership in 2012. Continuing these efforts is critical to institutional reform.

61. The recent corruption scandal, such as that of the notebooks, provide an opportunity to deepen institutional reforms by tackling key historic and structural causes of corruption, including strengthening the independency and efficiency of judiciary and oversight institutions. As the fight against corruption continues and large-scale investigations are revealed to the public (see Box 4), Argentina should remove all obstacles in the way towards reducing corruption effectively and demonstrate a sustained long-term commitment to the reform agenda, following the experience of neighbor countries like Brazil.81 Some of these obstacles are a historically low level of anti-corruption enforcement; a judiciary still perceived as inefficient and corrupt due to opacity in judge appointments and instances of political interference;82 the lack of credible entities, in the administrative jurisdiction, with the mandate, independence and capacity to monitor, detect, investigate and sanction unethical behaviors or corruption practices within the public administration; the lack of a corporate compliance culture among private firms, as well as public integrity laws delimiting the use of public funds by civil servants; and the substantial legislative and economic

79 According to the Edelman Barometer for example, in 2017 only 41 percent of citizens globally trust their governments.

80 Access to public information in Argentina was regulated at the national level through a Presidential decree (Decree 1172 from 2003), which—later reformed by Decree 79/2017—remains in effect until the new law’s entry into force.


82 The latest (2017-2018) Global Competitiveness report ranked Argentina 100 out of 138 in judicial independence (3.2 score).
differences among the various provincial jurisdictions that would ultimately be in charge of applying the federal laws.

**Box 4. The notebooks (cuadernos) corruption scandal**

From August 1, 2018 a large-scale corruption investigation was revealed, dominating the news and attention ever since. On August 1, the Justice Department detained five former officials and several businessmen that are accused of having participated in massive bribery schemes associated with public works during the Kirchner administration. The amount of former public officials and business men implicated continues to grow. The case is based on information of bribe amounts, names, address, dates and places that were recorded in notebooks (cuadernos) by a driver of the former Ministry of Planning.83 Many businessmen called to testify used plea bargains related to the “Repentance Law” (Law 27,304), sanctioned in late 2016. The detailed information recorded in the notebooks reveals the magnitude of the corruption and rent-seeking behavior of public and private sector elites involved in public contracts in Argentina, where public biddings were allegedly guaranteed to specific companies in exchange of bribes. While the investigations are still unfolding, they are likely to impact future public contracts, such as the PPPs under way, since four out of six active PPPs involve companies that are mentioned in the investigation.84

**Pathway 2: Open, outward-oriented development model**

Creating financial capital

62. **Low investment is one factor constraining inclusive and sustainable growth.** Argentina’s investment rate is lower than its regional neighbors, comparable peers, and even compared to its own historical records. Investment to GDP was 16 percent in 2016, below the regional average (20 percent) and significantly below the average among upper-middle income countries (32 percent). It is also four percentage points below the investment rate for 2007, the highest reached in the last decade. Foreign direct investment is also low, accounting for about 2 percent of GDP in 2016, below the regional average and the average for upper-middle income countries (3.6 and 2.4 percent of GDP, respectively). Public investment is low averaging 2.5 percent in the last decade. Infrastructure investment strongly relies on public investment (more than 80 percent), and is much lower in Argentina (at 2.7 percent of GDP) than the highest infrastructure investors in Latin America, which invest more than 5 percent of GDP with strong private sector participation.85 Low private and public investment has led to a declining capital stock.

63. **Argentina’s financial and capital markets are shallow versus comparator countries, thus limiting firm activity and private financial investment in key sectors such as infrastructure.** Private bank credit is extremely low at under 14 percent compared to the 44-45 percent average for the LAC region: this the lowest among the LAC-7 economies, among which Mexico and Peru are closest at 24 and 37 percent respectively—and Haiti’s share is higher than Argentina’s at 17.5 percent of GDP. The domestic equity market capitalization represents less than 12 percent of GDP versus comparator countries which are closer to 40 percent and the regional average of 35 percent; and private bond market issuances stand at under 1 percent of GDP, much lower than comparators (see Figure 51). For investor markets in infrastructure, for example, a key challenge will be attracting foreign investors given the large sums needed in sectors typically seen as risky. Incentives will be needed both from a regulatory point of view to facilitate entry into capital

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85 Fay et. al., 2017.
markets, as well as in terms of credit enhancement instruments to increase the perceived credit quality of such investments to ensure private finance.

Figure 51. Argentina: Low capital market depth for its income level

Private Credit, 2016, as percentage of GDP

Stock Market Capitalization, 2016, as percentage of GDP

Therefore, deepening capital markets and expanding access to finance to enterprises and households is key to mobilizing new capital in the economy. Investment and the allocation of capital are inadequately supported by financial intermediation given the smallness and risk averseness of capital markets and financial institutions, respectively—particularly for a country of Argentina’s income level. The financial sector is extremely limited compared to its peers, both regional and OECD, translating to low financing for infrastructure, housing, small and medium enterprises (SMEs) and the corporate sector. In addition, the financial sector is highly concentrated with low rates of banking penetration: the five largest banks own 50 percent of total loans and only 50 percent of the population has access to a bank account. Only 3 percent of MSMEs have adequate access to financial products with 50 percent being either unserved or underserved. Given the low base, there is substantial potential for the Argentine market to unlock financing for several sectors if the credit and capital markets are developed with appropriate instruments to transition from a high inflation to a stable environment. Housing is the main investment assets for households, but lending for residential housing amounts to less than 1 percent of GDP thus contributing to a housing deficit and depressed household investment.

In terms of financial sector stability, the relatively small banking sector remains very well-capitalized with low non-performing loans (NPLs) (see
Figure 52). However, given the recent rise in market volatility that began in April 2018, it is important to ensure contingency plans exist, and have risk mitigation measures in place. With high interest rates maintained to stem inflation, this could generate increased debt servicing stress on enterprise creditors of banks and therefore, banks need to be prepared. A review by financial supervisory authorities of their forward-looking systemic prudential measures would be useful to identify any banks that could have shortfalls in loan-loss provisions if borrower defaults were to rise. Stress testing by BCRA is critical, including looking at several scenarios that could develop and cause systemic liquidity stress in the system. In parallel, continued improvements in the financial payments and settlement systems would help to identify if any significant gaps in execution exist.
Overall, there is a huge potential for the financial market in Argentina to grow and bring more resources from the private sector to add to investment, growth and equitable development. Some of the key constraints initially identified to unlock this potential, include the: (i) review of regulatory and cost requirements for the entry of foreign investors given the funding levels needed, (ii) procedures, regulations and public listing requirements for the streamlined issuance of market securities, (iii) management of risks such as inflation to be mitigated in order to develop sustainable mortgage loan and securities markets, (iv) untapped identification of revenue and value capture opportunities in the infrastructure project market, (v) suboptimal development of risk mitigation mechanisms to protect PPPs concessionaries and creditors in the infrastructure finance area, (vi) lack of sufficient development of individual retail and e-finance banking products to broaden the scope of access to financial services across the country, (vii) dearth of approaches to augment SME finance potentially through innovative instruments and pooling of risks, and (viii) lack of development in the life insurance and private pension markets to increase individual saving safety nets while generating demand for long-term market investment instruments. The tackling of these constraints and the development of new policies and instruments will be a priority to ensure that the government can increasingly rely on the private sector to participate in an economic revival of Argentina.

Creating the infrastructure to support growth

The quality of Argentina’s infrastructure stock is deteriorating and this poses a challenge to competitiveness. The country faces important challenges related to both the quality of infrastructure and the level of investment. Argentina ranks 81 among 152 countries in the infrastructure pillar of the World Economic Forum’s (WEF) Global Competitiveness Index, well behind the regional leaders such as Chile (36) and Mexico (45) and all structural peers (Figure 53). From 2007 to 2017, Argentina has declined in the WEF rankings of overall infrastructure quality perception, falling 26 places from 80th to 106th. Although this is worse than most regional and structural comparator countries that have also fallen, perception of quality improved in 2016 and 2017 both in relative and absolute terms. Ageing infrastructure

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86 Indicator 2.01 Quality of overall infrastructure as per GCI of the World Economic Forum (2018).
is taking its toll on competitiveness, with Argentina ranking 96 and 113 out of 144 in terms of road and electricity quality infrastructure (Global Competitiveness Index, 2017). Bottlenecks in the transport infrastructure—essential to connect enterprise to markets and people to jobs—poses serious challenges, particularly for the Northwest of the country. The great distances that separate the Northwest region from the ports and the country’s main centers of consumption is a key driver for elevated transport costs which calls for provision of high quality transport assets and efficient provision of ancillary services. The average cost of transporting one ton of cargo from the Northwest to the country’s main ports of Rosario and Buenos Aires averages US$73 per ton, which is between 15 and 20 percent higher than in other regions of the country. In electricity, one of the main challenges is related to transmission as the country does not count with the adequate transmission lines. The WEF GCI quality of electricity rank for Argentina dropped from 95 (in 2007) to 113 (in 2017; see Figure 54).\textsuperscript{87}

\textbf{Figure 53. World Economic Forum’s Global Competitiveness Index Infrastructure pillar ranking, 2017}

\textbf{Figure 54. World Economic Forum’s Global Competitiveness Index quality of electricity ranking, 2007 and 2017}


\textsuperscript{87} With respect to ICT the Argentina’s performance is comparable to structural peers and is relatively strong compared to regional peers, as shown by the ITU ICT Development Index, in which the country scored 6.9 out of 10 in 2017 (and is ranked 51 in the World), while structural peers scored 7.0 on average, and regional peers scored 5.7 on average.
69. **Infrastructure investment in Argentina is very low and there is limited room for increasing public investment.** Argentina’s infrastructure investment rate has been low historically, hovering around 2 percent of GDP (Figure 55) and is much lower compared to the highest infrastructure spenders in Latin America (e.g., Honduras, Panama, Nicaragua) which invest more than 5 percent of GDP with strong private sector participation. It is also lower than the one for its regional peers (Figure 56) and for structural peers. Traditionally, it has strongly relied on the public sector (about 76 percent on average between 2008 and 2014). To make the situation more challenging, the country also has limited room to increase public investments. This is true for most of the region, but faster-growing economies, such as Chile, Colombia, Paraguay, and Peru are likely to fare better in terms of fiscal space for infrastructure than slower-growing ones, such as Argentina, Brazil, and Ecuador. Things are made difficult also by the fact that primary expenditures play an important role in Argentina’s fiscal situation. Moreover, given that even PPPs depend heavily on government support, limitations to public finance also imposes constraints on private finance for infrastructure.

![Figure 55. Infrastructure investment as a percentage of GDP in Argentina by type, 2008-2015](image1)

![Figure 56. Infrastructure investment as percentage of GDP in regional peers, 2014](image2)

Sources: Data from CAF, Inter-American Development Bank (IDB) and ECLAC. INFRALATAM database.

Note: latest year with data available for private is 2014

70. **Logistics performance indicators are generally lagging compared to peers.** At 27 percent of GDP, logistics costs are the second highest in Latin America and nearly three times higher than the average for OECD countries. According to the World Bank’s Logistics Performance Index (LPI), Argentina performs similarly to regional peers, but its performance has not improved in the past years (Figure 57). As a result, in worldwide scale it fell from position 45 in 2007 to 66 in 2016. Some of the factors impacting logistics performance include: (i) a heavy reliance on road transport, representing 95 percent of cargo movements; (ii) deficiencies in road infrastructure, including lack of capacity of trunk roads and low levels of road maintenance, particularly in provincial and municipal networks; (iii) the high cost of domestic logistics; (iv) a lack of standardization in maritime and air transport; (v) a complex tax system; and (vi) a lack of trained logistics personnel.

Sources: CAF, IDB and ECLAC. INFRALATAM database.

Note: latest year with data available for Uruguay 2012

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88 Structural peers also tended to invest more than Argentina in infrastructure. According to estimates from the structure Hub, which provide slightly higher estimates relative to the CAF, IDB and ECLAC INFRALATAM database (presented in the figure), the average investment in infrastructure as a percentage of GDP between 2007 and 2015 in Argentina was 2.47 percent, which is below the averages for Turkey (2.51 percent), South Korea (3.21 percent), Malaysia (3.93 percent), and Poland (4.32 percent).


91 World Bank, 2017f; Argentina Transport Engagement Strategy.
transportation services; (iv) the restriction in the capacity of waterways and the national port system; (v) the weaknesses in trade procedures and practices, particularly in international border crossings and ports; (vi) infrastructure deficiencies in international border crossings with key neighboring countries including Chile and Brazil; and (vii) the increased costs of urban logistics in the main metropolitan areas in the country.

![Figure 57. Logistics Performance Index, 2007 and 2016](image)

*Source:* Data from World Bank’s WDI.

### Tackling the challenges in infrastructure

71. **Better spending is a key element of improving the status of infrastructure and this heavily depends on better planning between national and provincial levels of Government.** Argentina’s federal structure poses unique challenges to planning, i.e. expenditure responsibilities are not accompanied by an equivalent transfer of tax powers and fiscal decentralization is modest, and infrastructure is not immune. The system for “coparticipación federal” has tried to solve the problem and approximately 60 percent of the provinces’ resources come from Nation to province transfers. To address this situation, it will be important to set clear planning priorities and develop a more transparent multi-sectoral methodology to prioritize and select public infrastructure investments. Special attention is required for the logistics network, particularly key corridors and critical exit nodes (such as the ports in the Buenos Aires metropolitan area and Rosario) and major border crossings. Further developing multi-modal transport networks is also key. From the organizational side, infrastructure planning and execution is diluted at different layers of government and several other agencies. In the case of water, for example, provinces tend to wait for investments made by federal government, without fixing their utilities performance issues. Construction of new water treatment plant is prioritized over measures to reduce non-revenue-water (where physical and commercial losses are huge). Argentina would benefit from a more comprehensive and strategic planning approach that covers both expansion plans as well as maintenance and improvement of existing infrastructure. This would also involve a stronger territorial development approach that places emphasis on the dimensions of economic geography. A solid national infrastructure policy should also take into consideration the role played by the provinces and municipal governments and a coordination of national and subnational resources and priorities.

72. **Better governance in the infrastructure sectors is also key, particularly when it comes to regulatory autonomy.** Argentina is particularly challenged by the coordination of regulation between the National Government and provinces. In the power sector, for instance, electricity regulation at the distribution level is a provincial responsibility. This explains the dispersion in final electricity prices around the country. Argentina has a lower than average performance in the autonomy index, following closely
behind El Salvador. Regulatory governance has distinct effects on utilities’ performance indicators. Argentina can aspire to regulatory bodies with greater levels of autonomy and transparency. The main focus would be in tackling the “regulatory” autonomy that includes clarity in their responsibility regarding particular issues (tariffs, service quality, consumer complaints, companies’ investment plans, wholesale market, anticompetitive behavior, technical standards), and powers to enforce its decisions. The main challenge is, and will always be, how to find this balance between rationality and politics. Agencies also present significant gaps in terms of the transparency of appointments. This aspect should call the attention of regulators and service providers, as a fully professionalized bureaucracy is the last guarantee against undue political influence in regulatory matters.

73. **Improving the mechanisms to leverage private sector financing is an important step in increasing investment and the Government is looking at PPPs as a vehicle to address the infrastructure gaps.** The Government has improved the PPPs framework to make it more favorable to private investors with the implementation of the new PPPs law approved by the Congress in 2016. This is supported by a new capital markets law to support the development of new long-term financial investment instruments was approved in May 2018. The Government has announced an ambitious US$26 billion investment program with 60 projects to be financed by private capital. The plan includes investments in capacity and road safety of the national highway network, upgrading existing airports and ports, and the construction and expansion of the rail network, including freight. This is in addition to a large power generation program with the aim of increasing the country’s power generation capacity, including renewable energy, by about 20 gigawatts (GW) by 2025. However, private sector financing of a large investment program remains challenging, particularly given the amount of financing and the limited capacity of the domestic capital market to supply the necessary equity and debt. In the water sector, the lack of definition of roles and responsibilities between provinces and federal government is one of the key bottlenecks in moving forward transactions in a context in which operators do not generate tariffs to recover even operations and maintenance costs. The financial structures will need to find risk allocations consistent with the appetite of investors even if this comes at the cost of limiting the potential benefit of the PPPs scheme, at least in the first set of projects until a track record is set and more risk can be shared among sponsors and financiers.

74. **Good infrastructure and lower logistic costs are key to Argentina’s ambitions in terms of growth.** While financing is a key bottleneck, more focused national and territorial goals, and efficient strategies can substantially reduce financing needs. In addition, upstream reforms will enable Argentina to both improve spending efficiency and attract private financing on better terms—whether through PPPs or

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92 Andres, et. Al. (2007). It should be noted that although the data from the study dates from 2007 the regulatory situation in the region has not changed dramatically, so these indices should provide a relatively accurate indication of the current situation.

93 See for example, Andres, et. al (2008). The World Bank. These estimates for Latin America show that a one standard deviation change in the formal regulatory governance components had a large effect on improving labor productivity (15.9 percent) and reducing the frequency of interruptions (13.8 percent) and residential tariffs (19.0 percent). A one standard deviation improvement in formal autonomy and the characteristics of the agency in terms of setting tariffs was associated with higher labor productivity (11.4 percent) and a reduction in the average duration of interruptions (17.2 percent). It was also associated with a 42.8–49.3 percent reduction in operational expenditure, with consequent improvements in the cost recovery ratio.

94 Among other aspects, it promotes the use of specialized funding vehicles to allow increased private investment in infrastructure projects, a legal regime allowing contestability at both the local and international levels, and regulations facilitating funding of infrastructure through the capital markets. The Ministry of Finance also created a PPPs Unit (Subsecretaría de Participación Público Privada, SPPP) that provides guidance and clearance on the gateway process and advises on the financial structuring.

commercial borrowing by public enterprises.\textsuperscript{96} And efforts to improve public investment institutions and frameworks—notably budgeting and procurement systems—should enable the country to substantially stretch the resources it already allocates to infrastructure. An improved framework for infrastructure planning, financing and investing will be a key driver of competitiveness, an issue to which this SCD turns in the following pages.

Creating an economy open to trade, competition and investment\textsuperscript{97}

75. The Argentine economy is poorly connected with the world economy and particularly closed to trade. Argentina’s trade flows, as a share of its GDP, have fallen by almost half over the last decade, dropping from 40.4 percent in 2006 to 26.3 percent in 2016, which is slightly above the level experienced in 1998 (23.3 percent) and Argentina is the fourth most closed economy in the world after Pakistan, Brazil and Sudan (see Figure 58).\textsuperscript{98} From 2010-2016, average trade openness, measured by trade as a share of GDP, was only 29.1 percent. Trade in services, as a share of GDP, is lower than in all neighboring countries. Integration to global value chains (GVCs)—i.e. global trade in parts and components rather than end products—is limited. Argentina’s average import tariff was 13.6 percent in 2015, well above the level of comparator countries. Nontariff measures (NTMs) further restrict trade flows, with effects similar to those of tariffs as high as 34 percent. Countries around the world participate, on average, in about 14 free trade agreements each; Argentina is a signatory to only one.\textsuperscript{99} Product market regulation, as measured by the OECD-World Bank Group (WBG) Product Market Regulation database,\textsuperscript{100} imposed barriers to trade facilitation that are more restrictive than in other LAC countries. As of January 2018, import licenses for around 1,300 tariff lines were still not subject to automatic approval.

**Figure 58. Trade openness (trade as a share of GDP), in percent, Argentina and select countries, 2016**

![Image of trade openness chart]

\textit{Source: Data from the World Bank’s WDI dataset.}

\textsuperscript{96} Fay et. al., 2017.
\textsuperscript{97} This chapter is based on World Bank (2018a) and Martínez Licetti et al. (2018a)
\textsuperscript{98} All values from the World Bank’s World Development Indicators (WDI) database.
\textsuperscript{99} See World Bank (2018a) and Martínez Licetti et al. (2018) for a comprehensive assessment of Argentina’s trade, investment, and competition position and reform agenda.
\textsuperscript{100} The OECD-WBG PMR data are part of the WBG’s Markets and Competition Policy Database.
The potential medium-to long-term gains from integrating into the global economy are substantial. Reforms to eliminate an import licensing system that required preapproval for each incoming shipping load is expected to boost GDP by at least 0.14 percent over a period of three to five years compared to baseline projections, as per Computable General Equilibrium (CGE) simulations.\(^{101}\) Removing all export taxes would expand GDP by at least 1 percent over a period of three to five years compared to baseline projections.\(^{102}\) A MERCOSUR-EU FTA would boost Argentina’s exports to the EU by 80 percent by 2030, relative to the baseline. These impulses would not dissipate over time, but bring permanent gains to the economy.

As a result of poor integration, export products and destinations are undiversified and concentrated in relatively low value-added goods. Concentration has persisted and even increased in terms of products and destinations since 1995 reflecting barriers to entry into new markets. Vegetables, foodstuffs and wood represent more than 60 percent of Argentina’s export basket and this proportion has been increasing since 2010. The top exports are soybean meal (17.6 percent), corn (7.4 percent), soybean oil (7.2 percent), and soybeans (5.7 percent). Export destinations are also concentrated in a few countries (see Figure 59). Argentina has somewhat limited integration into GVC, the 21st century mode of trade whereby a country does not need to produce an entire export good, but rather produces an input as part of the production process (Figure 60). Argentina is more likely to be the seller (forward GVC participation) due mostly to its export of agricultural commodities that are used as an input in production in other countries (for instance, the use of soy in processed soy products). The country is less likely to buy inputs from other countries to produce higher value-added exports (backward GVC participation).\(^{103}\)

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\(^{101}\) World Bank, 2018a.

\(^{102}\) The potential fiscal implications of this measure also need to be taken into consideration.

\(^{103}\) Forward GVC participation is measured as the share of Argentina’s value added embodied in foreign countries’ gross exports. Backward GVC participation is measured as the share of foreign value added embodied in Argentina’s gross exports.
Figure 60. Global value chain participation: Argentina vs. comparator countries, 2011

Source: Data from World Bank (2018a) based on data from OECD/WTO TiVA dataset.
Note: Countries are ranked by backward participation ratios.

78. Much needed foreign direct investment is low and has not contributed to developing more complex export products. The FDI stock in Argentina amounts to only 16.1 percent of GDP compared to 44.9 percent in new HICs and 43.1 percent in the region in 2016104 (see Figure 61). Weak FDI inflows and stock exacerbate Argentina’s already low rate of overall investment, which is critical for narrowing its infrastructure gap. Even so, FDI inflows have been quite diversified across sectors with chemicals (15 percent), mining (11 percent), and financial (10 percent) sectors accounting for the largest individual shares (Figure 62). Other, smaller sectors also contribute to a substantial portion of FDI inflows including food and beverages (8 percent), communication (7 percent), automotive, machinery and equipment, and wholesale. The challenge, however, lies in ensuring that FDI translates into higher economic and export complexity. FDI complexity itself in Argentina is low, -0.39, below the global average and below other Latin American countries (i.e., Brazil, Costa Rica) with similar economic complexity index (ECI) standings (Figure 63). Unsophisticated, unprocessed products—primarily in the agricultural sector—still dominate Argentina’s export basket leading to a relatively low ECI (Argentina’s ECI is -0.502, 72th country in the ranking in 2014).

104 Represents the simple average for each country grouping.
78. In addition to low import competition, many markets feature government interventions that further curb domestic competition and distort the level playing field. According to OECD-WBG PMR data, Argentina has both the most restrictive product market regulation in the region and more restrictive regulations than other countries of similar size and income levels (see Figure 64). Argentine state-owned enterprises (SOEs) operate in 17 sectors without a clear set of rules that guarantee competitive neutrality relative to private investors. These and other direct government interventions in the market (such as the price control system) can distort the level playing field.

79. Lack of pro-competition regulation in enabling sectors holds back firm competitiveness. Regulatory design in key service input markets is limiting contestability in communications technologies. For instance, regulatory asymmetries explicitly prohibit participation in certain segments of the
telecommunications industry, preventing the provision of converged and better-quality services (companies that offer pay television by subscription can offer telecommunications services, but not vice-versa). Delays in spectrum assignment processes and the absence of rules to protect competitive neutrality have prevented mobile operators from connecting more people at faster speeds. Between 2000 and 2015, there were no auctions for assigning spectrum. Currently, only 40 percent of broadband connections in Argentina provide speeds above 4 megabits per second, compared to 67 percent of top performers in the region. Successive government interventions in all segments of the energy industry have contracted energy supply and affected the reliability and prices of energy services. The regulatory set-up does not enable price signals to attract investment in electricity generation. SMEs lost, on average, 2.4 percent of sales due to outages, which is double the amount in comparator countries.

81. **Firms struggle, in particular, with high-cost, low-quality transport and logistics services, owing in part to rules that do not induce local providers to operate efficiently.** Logistics costs in Argentina, at 27 percent of GDP, are the second highest in Latin-America and nearly three times higher than the average for OECD countries; and have grown by 40 percent in real terms since 2003 (see Figure 65). It performs more poorly on the Logistics Performance Index than would be expected from its per-capita income. It also underperforms on specific logistic indicators compared to regional peers. For example, the average lead time to import or export in Argentina is seven days, compared to four days for the average LAC country. In part, the underperformance and high costs of logistics services reflect inappropriate sectoral regulations. For instance, road cargo transport regulations allow truck drivers and transporters to negotiate jointly salaries applicable to all market participants, including those unaffiliated with the respective associations. Such joint negotiation may facilitate or even constitute collusive behavior. In addition, operators that transport their own cargo and exert competitive pressure on public road freight services face distortive rules: they receive only a 30 percent discount on tolls, while public road freight providers receive a 100 percent exemption. In the case of railway networks, and given the vertical connections between majority shareholders and cargo rail transport end-users, regulators and the competition authority could, for example, collaborate to ensure effective third-party access regulations are in place where appropriate.

82. **The new competition authority, to be set up in 2018, will need to actively enforce anti-cartel policy, implement effective merger control and competition advocacy.** Government interventions that
restrict competition often enable anti-competitive practices by firms, such as price-fixing cartels. While mature competition agencies detect five or more of such anti-competitive agreements per year, Argentina has recently sanctioned the first cartel in many years, and after detecting only two in the entire decade before. The competition law passed by Congress in May 2018 will help consolidate initial reform progress by setting up a new and more independent competition authority, separating the investigation and ruling functions, increasing thresholds for merger notification, creating a leniency program for cartels, and strengthening the competition advocacy function of the authority.

83. **More effective competition policy can benefit Argentine consumers who pay significantly higher prices for key food products that are sold in relatively concentrated domestic markets.** Overall, households in Argentina spend 28 percent of their overall consumption on food products, more than the 14 percent in comparator countries. Between 2010 and 2015, the most important food products cost, on average, almost 50 percent more in Argentina than in international peer countries and 35 percent more than in Pacific Alliance countries.105 This is generally consistent with information on the relatively high concentration in these product markets, and the Competition Authority has already selected several of these for market investigations.106

84. **More effective competition will further be able to reignite productivity as an engine of inclusive growth.** Increasing competition in the manufacturing sector would increase the annual growth rate of labor productivity by 7 percent, on average, with all else being equal. Reducing the regulatory restrictiveness of competition in the Argentine service sectors (such as energy, transport, professional services, and telecommunications) would translate into an additional 0.1 percent to 0.6 percent growth in annual GDP, with all else being equal.

85. **Beyond the empirically well-established gains from integrating into the global economy, the current global trade landscape also opens specific opportunities for Argentina.** First, trade in intermediate goods has grown faster than trade in final goods, with FDI as a catalyst for GVCs. Building on existing capabilities in specific market segments (such as auto and food processing), Argentina can attract FDI in these sectors while strengthening linkages with local suppliers in order to reorient the production structure and integrate into GVCs and/or Regional Value Chains (RVCs). Second, services trade now represents 20 percent of global trade. Argentina can leverage comparative advantages in services to increase FDI and exports (for example, in knowledge-based service sectors). Unlike the goods sector, exports of services are already more diversified than in comparator countries with 49.7 percent of total service exports represented by ICT, professional and other services, 18.3 percent transport, and 31.6 percent travel. Third, information communications technology (ICT) tools can facilitate cross-border e-commerce and the participation of smaller and new entrants in global markets by boosting their ability to reach a sufficient scale. Retail e-commerce in Argentina grew by 50 percent between 2010 and 2015, much faster than in peer economies, but Argentina’s share in world retail e-commerce is one-fifth that of Australia and Brazil. This points to untapped potential.

86. **The gains from integrating into the global economy for inclusive growth will depend on the degree to which domestic markets encourage firms to operate efficiently and price competitively.** Ensuring that the gains from trade opening are shared across the economy relies on firms being able to enter, invest and compete, and having access to competitively priced and high-quality inputs. Firms that already operate or seek to invest in Argentina have faced challenges across all four conditions, and the solutions to these challenges lie in all three policy areas (trade, investment, and competition) across the four conditions.

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105 World Bank, 2018a.
106 The level of concentration is only one indicator of the intensity of competition. Further analysis undertaken at specific stages of the supply chain would contribute to identifying specific barriers and constraints that might be affecting competition.
No one policy alone can ensure that these conditions are fulfilled and firms can integrate into the global economy. Rather than sequencing reforms among policy areas, this report suggests sequencing specific reform options within each policy area so as to advance in all three areas simultaneously. If producers and retailers can exercise market power, they may fail to pass on reduced input costs to consumers. For example, in India, there is evidence that input tariff declines were offset by firms raising markups by 11 percent, on average. Similar results have been found after Mexico’s tariff decline due to the North American Free Trade Agreement (NAFTA).  

87. **Priority policy actions in trade, investment and competition, can be complemented by improvements in institutional resources and capacities.** Key trade policy actions include lowering tariffs and NTMs in priority sectors, unilaterally reducing NTMs in input products, removing nonautomatic licenses to increase predictability; and boosting regional integration agreements to increase market access. Competition and trade authorities can further coordinate to harmonize technical standards with trade partners. To improve investment policy, Argentina can revise the incentives framework, introduce effective policies to promote linkages with local suppliers, and set up comprehensive regulatory improvement and simplification mechanisms. Jointly among competition and investment promotion authorities, the government can open up key sectors to investment. To boost competition policy, Argentina can continue strengthening its anticartel enforcement, implement the recently overhauled merger control framework, strengthen pro-competition sector regulation in key sectors such as telecommunications and transport, and implement competitive neutrality principles to ensure that public and private operators compete on a level playing field. Each of the respective institutions for trade, investment and competition policy will need to be well resourced, prioritize its engagements and actions, and achieve greater technical independence.

**Enhancing the capacity of firms to benefit from expanded markets**

88. **For Argentina to successfully integrate into the global economy, as well as external obstacles, such as trade barriers, changes within firms will be needed to improvement productivity.** Since 2006, the productivity of all firms has fallen. Reversing this process will involve further reforms to improve the external conditions firms face. But improving productivity also requires improvements within firms, including higher rates of technological transfer, ICT adoption, and innovation, as well as improvements in the managerial quality of Argentinian firms.

89. **New firms and entrepreneurs face significant barriers at all stages of the firm life-cycle, preventing efficient reallocation of resources from low productivity to high productivity uses.** Trade liberalization, the elimination of red-tape and continued efforts to improve the business climate, together with increased investment in infrastructure and new laws to promote competition and facilitate financing, are poised to pay off provided macroeconomic stabilization is achieved. For its income level, Argentina stands out for its poor performance in international surveys of the environment for conducting business: it ranks 92nd out of 137 countries in the World Economic Forum’s GCI and 117th out of 190 countries in the World Bank’s Doing Business Survey. The evidence also points to a lack of competition in input markets as being particularly problematic: Argentina ranks close to the bottom in the world in GCI pillars related to the efficiency of markets, both for final goods and services and for factors of production. In a survey conducted by the World Bank over 2017-2018 of business owners and top managers, the biggest obstacles to enterprise growth in Argentina are reported as high tax rates, labor regulations, and political instability. However, the effects of barriers differ by type of firm: larger firms perceive labor regulations, 

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107 De Loecker et al., 2016; Santamarina, 2017.
109 World Bank, 2018d.
business licenses, and corruption as the worst obstacles to doing business, whereas smaller firms perceive
tax rates and tax administration as well as access to finance as worse obstacles than do large firms.⁸¹⁰

90. **Argentina’s firms invest too little in innovation, and creating an innovation ecosystem connecting researchers, businesses, and government will be essential to enhance their productivity and capacity to export.** The country invested 0.6 percent of GDP in Research and Development (R&D) in 2014, higher than the average of regional peers (0.5 percent), but much lower than the New HICs average (1.3 percent) in improving productivity. The country’s Science, Technology and Innovation (STI) system will have to play a crucial role. Forty percent of (formal) manufacturing firms did not perform any innovation-related activity, and only 13 percent of manufacturing firms have a R&D department. Business investment in R&D is 0.06 percent of GDP and Argentina performs worse than the average of the OECD on competences to innovate and skills for innovation. Argentina falls below OECD average public R&D spending/GDP, as well as on publications in top journals, and universities among the top 500.¹¹¹ Indicators of private innovative activity also lag significantly behind OECD comparator countries, with low business spending on R&D, no top 500 corporate R&D investors, and low patenting and trademark activity (OECD 2014). Facilitators of innovative entrepreneurship, such as sources of venture capital and access to broadband internet and other ICT infrastructure, are likewise scarce, as well as skills in science and engineering where Argentina performs better than other Latin American countries, but still far behind the average OECD country. Argentina performs close to the average of the OECD on indicators of networks, clusters and transfers, including international co-authorship and international co-invention. Building on these strengths, the innovation system will require more private sector financed innovation and better knowledge transfer between academia and firms capable of commercializing new scientific and engineering breakthroughs.

91. **To take full advantage of R&D, Argentina should also invest in complementary factors, such as physical, human, and importantly managerial capital.** Argentina’s challenges with respect to human and physical capital are known, and are discussed in Chapter 3 and Section 2.3, but the importance of managerial ability at the firm level is often overlooked. Management quality has a dual impact on productivity: a direct effect through a more efficient use of factors of production and an indirect effect by increasing the probability of innovating. Figure 66 for example, shows the correlation between the impact of R&D on innovation and good management practices across countries.¹¹² Argentina lags with respect to best managerial practices, and this negatively affects the efficiency of R&D and the scope of technological absorption. Also, it makes much more challenging the creation of a vibrant export sector, where firms face the challenge of developing and producing products, and having marketing and distribution practices tailormade to capture new external markets. There are success stories in Argentina. Firms have managed to remain at the global frontier despite macroeconomic volatility and microeconomic distortions. Firms in the oilseed complex, for example, collectively became the first exporting-sector of the country thanks to the adoption of direct sowing techniques, and is now a world-leader in the field.¹¹³ In addition, this led to the creation of new subsectors along the value chain, such as biodiesel, where Argentina is the top world exporter, and to the development of synergies with knowledge-intensive sectors such as bio-tech.

92. **Box 5. Argentine Wine: A case of export emergence**

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⁸¹⁰ Business owners and top managers in 991 firms were interviewed from March 2017 through March 2018 as part of the World Bank’s Enterprise Survey (2017).

¹¹¹ OECD, 2017.

¹¹² Cirera and Maloney, 2017.

Until the early 1990s the vast majority of wine production in Argentina was dedicated to the domestic market and no wine was specifically adapted to be sold abroad. After knowledge of how to make new-world wines spread throughout the sector, exports increased dramatically rising from US$25 million in 1993 to US$806 million in 2017 (Figure B5.1 shows the increase in constant US$ 2010 million terms). During the same period the number of countries to which Argentina sold its wines rose from 45 in 1993 to 115 in 2008. By 2008, Argentina had become the tenth largest exporter of wine in the world, capturing slightly over 2 percent of the world market. How did Argentina do it?

**Finding 1:** Consistent exporters adopt a markedly different set of business practices. They also exhibit a common mindset about the importance of adopting these practices and a discourse that suggests that they are mutually complementary.

**Finding 2:** An export pioneer, defined as the first individual to implement the set of export business practices outlined above, was also the first to become a consistent exporter. Export pioneers have a knowledge advantage about foreign markets to which they were previously exposed.

![Figure B4.1 Argentina: Wine Exports, in US$ 2010 million, 1960-2016](image)

*Source:* Data from DESA/UNSD, United Nations Comtrade database.

Artopoulos et. al (2011) find that export emergence can be distilled to two critical factors:

In Argentina, the export pioneer was Nicolás Catena Zapata, the first Argentine wine producer to systematically adopt the practices outlined above, achieving consistent sales of new-world wines to developed countries. His winery was also the only one to achieve unabated export growth to the OECD from 1994 to 2006.

Zapata had taken control of his family winery in 1963 while doing a PhD in Economics at Columbia University. He traveled back and forth from New York to Mendoza, the center of wine production in Argentina, on a regular basis during his studies. Zapata’s efforts to develop a new world wine made in Argentina began after he returned from a three-year stay at the Department of Agriculture and Resource Economics at U.C. Berkeley in the early 1980s, where was a visiting professor. During this time, he visited wineries in Napa Valley, befriending winemakers that had developed and mastered new-world winemaking techniques. One of the most important acquaintances he made was Robert Mondavi, one of the leaders of the new-world wine revolution in California. According to Zapata, his decision to undertake this transformation was not based on a detailed economic analysis of potential markets, but rather on a desire to emulate the success he had witnessed in the U.S.

In the 1990s, the Argentine economy underwent economic liberalization reforms, enabling wineries to upgrade equipment allowing for new-world production techniques. Argentina’s soil is particularly well-suited to meeting a variety of demands in terms of taste because it can accommodate up to 28 different grape varieties. However, despite conducive economic and geographical conditions, consistent exporters had to take the next step and adapt production techniques to the specific demand tastes and export requirements of foreign markets.

Artopoulos et al. affirm that export business practices are radically different from those that prevail in the domestic market, involving adapting products to foreign demand and establishing information channels to keep up to date about its evolving patterns. Export business practices also require upgrading production processes to improve...
quality, complying with the requirements of foreign distributors such as rigorous expectations in terms of quality consistency and timely delivery, as well as other specific requirements like packaging and back-office procedures. Finally, export businesses need to establish and maintain long-term relationships with foreign distributors to secure up-to-date information about foreign markets.

**Policy implications**: Artopoulos et al. suggest that public policy that seeks to promote high-wage jobs should include export development policies that promote the diffusion of export business practices. Policy makers could, for example, promote conferences through business associations and educational institutions designed to facilitate the transmission of explicit and tacit knowledge from emerging pioneers to potential followers.

*Source*: Based on Artopoulos et al. (2011).

93. presents a case study of the emergence of Argentina’s wine industry, which despite the barriers to innovation and growth documented above, has managed to become world class.

**Figure 66. Management practices and impact of R&D on innovation, 2015**


**Box 5. Argentine Wine: A case of export emergence**

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**Figure B4.1 Argentina: Wine Exports, in US$ 2010 million, 1960-2016**

![Figure B4.1](image.png)

*Source: Data from DESA/UNSD, United Nations Comtrade database.*

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**Policy implications:** Artopoulos et al. suggest that public policy that seeks to promote high-wage jobs should include export development policies that promote the diffusion of export business practices. Policy makers could, for example, promote conferences through business associations and educational institutions designed to facilitate the transmission of explicit and tacit knowledge from emerging pioneers to potential followers.

*Source: Based on Artopoulos et. al (2011).*
94. **The skills gap is not limited to managerial skills, but also affects the capacity of firms to efficiently fill vacancies with the right profile of workers.** According to a recent Manpower Survey, 59 percent of firms have difficulty finding the right skills to fill vacancies.\(^{114}\) The skills gap is wider in Argentina than in comparable countries with 20.8 percent of the labor force having tertiary education, compared with 32 percent in the OECD, and only 12 percent of students in secondary education enrolled in vocational programs, compared to 25.8 percent in the OECD. Recent data from the unmet labor demand survey (\textit{Encuesta de Demanda Laboral Insatisfecha}) reveals persistent shortfalls in the skills required by firms when hiring, especially for operatives.\(^{115}\) Incentives to upskill in Argentina are also lower than in other Latin America countries: earnings premiums for tertiary education are 48 percent compared with 55 percent in the OECD and as high as 133 percent in Colombia and 105 percent in Mexico.

95. **The dual nature of the Argentine economy is a major limitation for reaping the benefits of expanded market access.** Alongside the highly-productive clusters described above lie a myriad of firms characterized by their low dynamism, that need high levels of protection to survive. Many of these firms operate in the informal economy, limiting their ability to generate quality jobs and take advantage of improved business conditions. These firms sometimes employ a disproportionate share of the labor force, especially low-skilled, and any negative shock to them can have significant effects on the more vulnerable portions of the population. The inefficiencies of such firms, usually clustered in particular sectors, spread to the rest of the economy through higher prices for key inputs, such as computer equipment for example, generating a vicious cycle of low productivity and low growth. The dual nature of the Argentine economy manifests itself in the extent of informality and the differential effects on different populations. Informality is a lot higher for young, female, and low-skilled workers.

96. **Argentina’s firms have a big opportunity to take advantage of an opening up of the economy to upgrade their products, technologies, and business processes.** Since the potential returns increase with the distance to the frontier,\(^{116}\) Argentina’s lackluster productivity performance opens the door for large returns from innovation and technological transfer investments. Given the large externalities involved, however, this is not a passive process where the opening-up of the economy will naturally bring Argentina to the global productivity frontier, but one that needs an active commitment by public and private actors. First, there is a need for macroeconomic stability and policy predictability. Second, a reduction in government red tape—particularly to ease firm entry and the efficient exit of low productivity enterprises—getting rid of the barriers to competition, and over time reducing the burden of distortionary taxes\(^{117}\) are important for decreasing costs to facilitate business activity. Third, supportive government policies can help foster innovation and competition, and develop an export sector through policies that promote the diffusion of export business practices. Fourth, deepening the financial sector with a larger variety of financial instruments will be required to allow firms benefit from opportunities to innovate and build on existing capabilities.\(^{118}\) Fifth, Argentina needs to ensure education and skills attainment compares well with the best in the OECD from basic education onwards to position itself for high wage, differentiated export production.

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\(^{114}\) OECD, 2017.

\(^{115}\) In Argentina, the largest skill gap is for operatives (average 40 percent from 2010-2015), followed by professionals (36.8 percent), and finally technical labor (23.1 percent). In terms of years of experience, the largest gaps are for workers with no experience (36.5 percent), 3-5 years’ experience (32.3 percent), and 1-2 years’ experience (27.4 percent) (OECD, 2017).

\(^{116}\) See Griffith et al., 2004.

\(^{117}\) Argentina comes in 169th in ease of paying taxes in the Doing Business 2018 rankings.

\(^{118}\) The capital markets law (\textit{Ley de Financiamiento Productivo}) passed by Congress in May 2018 can contribute by fostering financial innovation and a growing Fintech sector offering new sources and methods of SME finance, such as factoring and crowdfunding, together with new simpler corporate forms such as the Simplified Corporation (\textit{Sociedades por Acciones Simplificada}, SAS), will be important complements for the innovation ecosystem.
Chapter 3. Toward a more inclusive society

Recent trends in poverty and shared prosperity and challenges ahead

98. After the severe economic crisis at the turn of the century, Argentina experienced remarkable inequality and poverty reduction since 2004, followed by a persistent slowdown of progress since 2011. Although the urban poverty rate and Gini index fell between 2004 and 2016 (from almost 26 percent to slightly almost 8 percent and from 0.48 to 0.42, respectively), two different phases can be clearly identified: strong improvement in welfare levels and equality which coincided with a strong recovery up to 2011, and stagnant or slightly worsening welfare indicators with slower overall economic growth from 2011 to 2016 (Figure 67, Figure 68). These dynamics reflect the significant improvement combining a fast post-crisis recovery in the first four years and a solid improvement since 2007, and later slowdown of shared prosperity. As discussed previously, the slowdown reflects the fact that the rapid growth and poverty reduction in the first period came had-in-hand with an unsustainable growth model that started to show its limits, in the second period.

Figure 67. Poverty and inequality in urban Argentina, 31 main cities, 2004-2016

Source: Data from SEDLAC (CEDLAS and World Bank), based on EPHC (2nd semester). Due to comparability challenges, poverty rates are based on the $5.5 a day poverty lines (in 2011 PPP), which is closer to the current official extreme poverty line

Figure 68. Urban poverty (US$5.5 a day) by region, 31 main cities, 2004-2016

Source: Data from SEDLAC (CEDLAS and World Bank), based on EPHC (2nd semester). Due to comparability challenges, poverty rates are based on the $5.5 a day poverty lines (in 2011 PPP), which is closer to the current official extreme poverty line

99. Although poverty was reduced in almost all the Latin-American countries, Argentina’s performance stood out in both phases but for different reasons. Argentina reduced poverty at a rate higher than in other countries between 2004 and 2011, but at a slower pace during the period 2011-2016. For instance, poverty rate dropped 17 percentage points in Argentina, 15.3 in Brazil, 11.6 in Chile, and 11.1 in Uruguay in the first period, while it contracted 1.1 percentage points in Argentina, 3.9 in Brazil, 6.0 in Chile, and 2.2 in Uruguay in the second period. This difference is related to shared prosperity developments. Pre-2011, Argentina was among the best performers with incomes of the B40 growing at almost 9.5 percent annually, and among the worst performers in 2011-2016, when incomes of the B40 and the average did not grow at all (Figure 69).

119 Welfare data is based EPH survey, that covers only the main urban areas (31 agglomerations), representative of only 61 percent of the total population of the country. See Box 6 on the representativeness of the household survey and the implications for the excluded populations.
100. Welfare changes for the bottom 40 in 2004-2011 were mainly driven by the recovery in labor incomes (Figure 70). Family incomes grew largely due to the positive performance of labor income, particularly among the poorest households, recovering from the crisis as well as a continued job creation after 2007. During this period, employment grew at 2.2 percent rate per year, driven by wage-earners primarily in large but also small firms (Figure 71). This increase of employment and shrinking of the skill wage gap is associated with the commodity boom which increased demand for low skill workers, in addition to the recovery of idle capacity right after the crisis, and a consumption growth model with a macroeconomic scheme which favored national firms. Fast earnings growth also reflected the strengthening of labor market institutions.

Figure 69. Annualized income growth for the average and the poorest 40 percent, Latin American Countries

![Graph showing annualized income growth for the average and the poorest 40 percent, Latin American Countries](image)

Note: Argentina is marked in red. Regional peers are marked in green.
Source: Data from SEDLAC (CEDLAS and World Bank).

101. During this period since 2004, disadvantaged groups saw some improvements in their situation. While female employment grew faster than male employment and the (uncontrolled) gender earnings gap narrowed from 68 to 76 percent, relative to the total population, female labor force participation rate has ceased to grow in the last fifteen years. As a result, it currently lags behind other LAC countries and is the second lowest among peer countries. Fast economic growth, increased earnings and expansion of social assistance might be behind this general slowdown, though child care difficulties and preference against hiring women with children may also play a role. During this period, the informality rate among wage-employees was also reduced considerably as a result of both formal job creation and formalization of

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120 Fernandez and Messina, 2017; Messina and da Silva, 2017.
121 Beccaria et al, 2005.
122 Lopez-Calva and Lustig, 2010; Gasparini and Lustig, 2011.
125 Latinobarometro, 2015.
existing jobs, but it stagnated around one thirds in the last few years. Despite this, the unconditional wage gap remained almost at the same level during the whole period, and conditional wage gap persisted.

102. In addition, government transfers became especially important for families in the lower deciles during 2004-2011 and, hence, they contributed to extreme poverty reduction. Pensions were an essential source of additional family income—in particular, among the vulnerable—due to the pension moratorium passed in 2005. Pension coverage among the elderly increased reaching almost 95 percent and doubled from around 40 to 80 percent for those in the bottom quintile, giving generous starting pensions to new beneficiaries. The decline of families receiving social transfers following the phasing out of the Jefas y Jefes de Hogar Desocupados program (launched to address the 2001/02 crisis) was reversed with the creation of the AUH in 2010, which reached 15 percent of households by 2016.

128 Bustos and Villafañe, 2011; Salvia et al., 2015.
129 Rofman and Olivieri, 2012; Rofman et al., 2015.
130 The AUH is a non-contributed cash transfer program for all families with school-age children in which neither parent is contributing to the social security program (informal workers, unemployed or inactive). The conditional part of the transfer is based on school attendance, medical check-ups and vaccinations of the kids, as well as pregnancy check-ups.
Despite the significant reduction over the last 15 years, income poverty is still high in Argentina. The urban poverty rate—measured at US$5.5 per capita per day in 2011 PPP—is around 8 percent. This upper-middle income country poverty line is similar to the official extreme poverty line, but significantly lower than the official poverty line. According to this last threshold, three out of ten people...
would be considered poor in the second semester of 2016. Poverty is concentrated regionally in three areas—the two Northern regions and Greater Buenos Aires—where around 70 percent of the poor live. Additionally, its incidence is twice as high among children aged 0 to 14, with one in four children being poor and among recent migrants (see Annex II). Today, two million people live in informal settlements lacking property rights and basic services, which contrasts with the emergence of enclosed neighborhoods where a large portion of the rich live. Finally, information is missing on the living standards of a large share of the population, which is a big concern (Box 6).

105. Access to basic services and resulting social outcomes are determined by place of residence and family background, limiting intergenerational mobility. Access to education, health and piped water or sewerage networks varies widely across provinces (Figure 72). For instance, the Northwest region has an average of 0.04 health centers and 0.09 schools per 1000 population, against the national average of 0.14 and 0.19 per 1000 population respectively. Infant mortality declined at a faster rate in poorer provinces than in richer ones, but coverage for control and prevention of chronic diseases is still significantly better in richer provinces. Children under five in the poorest provinces in the north, such as Formosa, are almost twice as likely to die, and maternal mortality rates in La Rioja and Formosa are six to seven times higher than in the City of Buenos Aires (Figure 75). In addition, children living in poor households are three times more likely to be out of school and live in households with no safely managed water or sanitation; and poor elderly people are two and a half times more likely to live in a precarious dwelling and without safely managed water and sanitation (see Annex II).

Figure 72. Access to services, living context and school attendance, and level of education, 2016

Figure 73. Maternal mortality (per 10,000 births) across provinces, 2013

Source: Data from SEDLAC (CEDLAS and World Bank), based on EPHC.

Source: Argentine Ministry of Health.

106. Indigenous populations (IPs) are particularly vulnerable. A larger share of IPs lives in precarious slum-like conditions (24 percent), compared to non-indigenous people (13 percent). In the cities, 79 percent of IP have access to water and 47 percent to sewerage, compared to 84 percent and 53 percent, respectively, of non-indigenous people. IPs also lag behind non-indigenous when it comes to access to health and

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131 Using national poverty lines, half of children are considered poor. The discrepancy arises because the national poverty line is significantly higher than the one used to make international comparison. The $5.5-a-day line used in this present text is closer to the national extreme poverty line.


133 World Bank, 2017d.

134 Sources: Dirección de Estadísticas e Información de Salud, Ministerio de Salud, Argentina; Global Burden of Disease.
education. Among IPs, 53 percent has some kind of health insurance, which compares to 64 percent of non-IPs. In education, while there are no significant differences on average in school enrolment or attainment among IP and non-IP populations, starker gaps emerge for specific groups. For example, a rural, indigenous woman is considerably less likely to finalize primary or secondary school as compared to a non-indigenous rural woman; while an urban non-indigenous woman is almost four times more likely to finish secondary school.

**107. Labor informality is one of the main challenges today.** At around 30 percent among wage-employees, informality is still high, especially among less educated women (A large proportion of 15-to-24 years old are not employed or in school, particularly affecting young girls and in the poorest regions of the country). One in five young adults are not in employment, education or training (NEET) and almost a quarter of women, one of the highest rates among peer countries (Figure 76). Within the country, these numbers are particularly worrisome among the Partidos of Greater Buenos Aires, where 23 percent for young people are NEET and 28 percent of women. Associated with this high and higher incidence among women is the fact that adolescent fertility rate (births per 1,000 women ages 15-19) is at 63.8, three times as high as in the OECD. Dropping out from school before finishing upper secondary levels, youth lack the necessary skills to secure a formal sector job and settle, instead, with informal unstable employment. Indeed, among the youth that have wage employment, 56 percent are informal (Figure 77).

**108. Going forward, the labor market needs to recover lost momentum as a force to reduce poverty and inequality.** Employment rates, particularly among men and youth, ceased to grow and slightly declined since 2011. As mentioned in chapters 1 and 2, not only more jobs are required, but also labor productivity needs to grow. Two out of three jobs belong to low productivity industries, in sectors such as social and personal services, restaurants and hotels, or construction (Figure 77), in which the informality rate is high.

**Figure 74. Informality rate among wage-employees, second semester 2016**

**Figure 75. Gender monthly labor income gap, contribution of characteristics and coefficients**

**109.** Except for Patagonia, more than half of women with less than complete secondary is informal, a proportion that reaches 70 percent in the northern regions of the country. Informal wage-earners not only have less perks, but also earn lower salaries. The unconditional wage gap between formal and informal jobs was around 42 percent in 2016, a difference that does not disappear even after controlling for relevant characteristics.

**110. Labor market outcomes for women are particularly disappointing.** At 46.6 percent, the female participation rate in Argentina is the third lowest among all peer countries, and significantly lower than the average in OECD countries (54.2 percent). The participation gap between women and men is particularly large among the less educated workers (31 percentage points), a difference that closes to 9 percentage points for those who finished university degrees. Important levels of informality—especially among less educated (A large proportion of 15-to-24 years old are not employed or in school, particularly affecting young girls and in the poorest regions of the country). One in five young adults are not in employment, education or training (NEET) and almost a quarter of women, one of the highest rates among peer countries (Figure 76). Within the country, these numbers are particularly worrisome among the Partidos of Greater Buenos Aires, where 23 percent for young people are NEET and 28 percent of women. Associated with this high and higher incidence among women is the fact that adolescent fertility rate (births per 1,000 women ages 15-19) is at 63.8, three times as high as in the OECD. Dropping out from school before finishing upper secondary levels, youth lack the necessary skills to secure a formal sector job and settle, instead, with informal unstable employment. Indeed, among the youth that have wage employment, 56 percent are informal (Figure 77).
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![Figure 74. Informality rate among wage-employees, second semester 2016](image)

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112. **and reduced opportunities to access better paying jobs, combined with the limited access to affordable child care services, are among the reasons behind this gap.** Women earn less than men, even controlling for a set of relevant variables. Women earn on average 34 percent less than men, and the difference is driven by the fact that they are more typically employed in jobs that are worse paid (more informal, part time, and in low-paid activities) as opposed to being paid differently for the same job (Figure 75).

113. **A large proportion of 15-to-24 years old are not employed or in school, particularly affecting young girls and in the poorest regions of the country.** One in five young adults are not in employment, education or training (NEET) and almost a quarter of women, one of the highest rates among peer countries (Figure 76). Within the country, these numbers are particularly worrisome among the Partidos of Greater Buenos Aires, where 23 percent for young people are NEET and 28 percent of women. Associated with this high and higher incidence among women is the fact that adolescent fertility rate (births per 1,000 women ages 15-19) is at 63.8, three times as high as in the OECD. Dropping out from school before finishing upper secondary levels, youth lack the necessary skills to secure a formal sector job and settle, instead, with informal unstable employment. Indeed, among the youth that have wage employment, 56 percent are informal (Figure 77)

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135 Beccaria, Maurizio y Vázquez, 2017.
136 Based on Mincer equations and Oaxaca Blinder decompositions.
137 WHO
138 De Hoyos et al, 2016.
Figure 74. Informality rate among wage-employees, second semester 2016

Source: Calculations based on data from SEDLAC (CEDLAS and World Bank). SI is secondary incomplete, SC secondary complete, UI university complete, and UC university complete.

Figure 75. Gender monthly labor income gap, contribution of characteristics and coefficients

Source: Calculations based on data from EPHC 2016 (second semester). The figure presents the results of Oaxaca-Blinder decomposition for three types of workers: formal sector, informal sector and all workers.

Figure 76. Share of youth (15-24) not in employment, education or training, circa 2016

Source: Calculations based on data from SEDLAC (CEDLAS and World Bank), based on EPHC, and International Labour Organization (ILO)

Figure 77. Private sector industries with low labor productivity, share of the Gross Value Added at basic prices (GVAbp) and jobs creation, 2016

Source: Calculations based on data from National Accounts.
Note: Low productivity industries are those whose labor productivity is lower than 66 percent of the average private sector in the economy.
115. **In the short run, the transition toward an outward oriented high-productivity model may bring about challenges for employment.** Theoretically, the lowering of tariffs and barriers to external competition will lead to a reallocation of labor from less to more productive sectors with consequent welfare gains at the aggregate level. While conditions are different from the liberalizations of the 1990s (in terms of the speed of the process), Argentina’s past experience opening the economy highlights the need to ensure that adequate social protection policies are in place, to ease the transition. Estimates for alternative opening models (considering the employment characteristics of affected sectors) suggest that, in the short run, skills mismatches may result in increased unemployment. Also, skill wage premium might rise as trade openness might affect labor intensive industries negatively but provide a premium to higher value-added services. In addition, given the relatively low level of formalization of both affected and expanding sectors, there might be a pressure toward informalization.  

116. **Beyond this, the demographic transition will increasingly put pressure on the economy.** Argentina is currently at a very opportune stage of its demographic transition, and yet, the country risks not taking full advantage of it. Both the demographic as well as the economic dependency ratios are at a historical minimum. Until the aging period starts in the 2040s (when the dependency ratio starts to grow), it is necessary to ensure that the greatest portion of the active population can generate savings. Estimates suggest that aging alone could represent a drag on growth of up to 0.2 percentage point in the next 30 years. However, policy measures and socioeconomic forces could outweigh the demographic trends. Increasing female labor force participation to match that of men in 15 years would increase per capita growth on average by 1 percentage point per year in the next 15 years, and still reach 0.3 above the baseline after 30 years, more than compensating the demographic effect. In addition, increasing the proportion of workers that contribute to the social security system (which now stands at a third among wage employees), particularly among the youth, will be essential.

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141 The dependency ratio is defined as the ratio between the number of children and elderly (under 15 and over 65 years old) and the working-age population (aged 15 to 64).

142 Calculations based on Bloom et al. (2010), INDEC and UN Population estimates.
Technological change—which may be accelerated by trade openness—could deepen inequality in the medium and long run, unless accompanied by complementary investments in human capital, institutional reforms and public policies. Automation would displace part of the labor force, particularly those who perform routine tasks. During the past twenty years, in Argentina, as well as in other parts of the world (U.S., Germany, Eastern and Central Europe, and Latin America), technological change has been reflected in a shift from jobs that are highly intensive in routine manual (RM) tasks toward a greater intensity in cognitive tasks (Figure 78). This new scenario may cause labor market polarization, with an increase demand for high-earning cognitive work as well as for low-earning non-routine manual (NRM) occupations, accompanied by a reduction in demand for routine tasks with medium earnings (Figure 79). In this context, there is a clear challenge for public policy associated with the need to train and reassign low-skilled workers to tasks that are less susceptible to automation, that is, those that require an intensive use of creative and social intelligence.

Pathway 3: Releasing constraints to productive inclusion

Argentina still faces challenges to ensure that everyone is able to contribute and benefit from a successful transition to a sustainable high productivity/high wages model. As the labor market represents the main source of incomes for the largest part of the population, positive employment dynamics—including an increasing formalization rate—is core for continued household welfare increases. Ensuring that the population has adequate levels of human capital is essential for job creation (WDR, 2013). Yet, the sharp spatial and socioeconomic differences in access and quality of services limits Argentines ability to accumulate crucial assets needed for taking equal advantage of available opportunities and breaking with duality, as well as for transitioning toward a more competitive economy. Behind these differences lie fragmented social service systems, worsened by a federalist structure with unequal capacity to deliver services and with limited compensation mechanism at the disposal of the State. As a result, investment in children and youth is deficient, undermining the chances for social mobility. In addition, the excessive

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143 Apella and Zunino, 2017.
geographic concentration of economic prosperity means that opportunities in the lagging areas are scarce, and that agglomeration economies are not fully exploited. Finally, the relatively generous welfare system, more akin to those of OECD countries (although more heavily biased toward the elderly) is at odds with a less progressive tax structure, typical of economies to which the middle class aspires to emulate. Despite its generosity, the system might be neither sufficiently prepared to protect the losers of the transition nor providing cost-effectively quality social services, particularly for children and the youth, to compensate for the prevailing gaps across groups and across the country.

**Investing in human capital**

119. **In the short term, the underperformance in educational outcomes, despite the reasonably high spending levels, may hinder the country’s ability to increase productivity and respond to changing demands.** Learning, much more than attainment, has been found to be associated with economic growth.\(^{144}\) Although coverage of formal education and public expenditure (at 6 per cent of GDP) are high in Argentina, completion rates remain low and quality is lagging. More than half of the relevant-age students do not finish secondary education,\(^{145}\) and the rate of enrolment falls significantly after 15 years of age (particularly for boys) (Figure 81). Internationally comparable test score data shows that Argentina underperforms relative to its peers both at the primary and secondary level. Almost four out of ten students have the lowest performance in reading tests by the third grade. By age 15, two-thirds of children are not able to solve basic math problems, and half cannot interpret basic texts. The median Argentine performs in mathematics is an equivalent of 2.5 years below the average of OECD countries (Figure 82).\(^{146}\) More worrisome, test scores results have stagnated at the same time as spending was increasing, pointing toward increase inefficiencies as well as to long-term effects in terms of future incomes.\(^{147}\) Estimates suggest that Argentina could raise its average growth rate by two-thirds if were able to increase its cognitive skills to match those in peer countries.\(^{148}\)

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\(^{144}\) Hanushek and Woessmann, 2008.

\(^{145}\) World Bank, 2015b.

\(^{146}\) According to PISA scales: 41 points in Mathematics are equivalent to having an additional year of formal education.

\(^{147}\) World Bank, 2015b.

\(^{148}\) Calculations based on OECD (2010) and OECD (2018). OECD (2010) presents a model of economic growth on workers’ cognitive skills (C), years of schooling (S) and initial GDP (\(GDP_0\)), estimated OECD countries database. Cognitive skills are proxied using the average PISA test score between math and science. The resulting equation is \(g^{PE} = −3.54 + 1.74C − 0.30 GDP_0 + 0.025S\). This means that one standard deviation change (100 PISA points) raises per capita GDP by 1.74 percentage points. Applying this model to Argentina assumes that the relationship between covariates and per capita growth is similar to the average of OECD countries.
Figure 80. Test scores in mathematics, 25th, 50th and 75th percentiles, selected countries (OECD average in shaded area), Program for International Student Assessment 2012 (PISA)

Source: 2018 WDR, based on PISA 2012. OECD countries are in green. The green lines represent the interquartile range of OECD countries.

120. Quality is deficient at all levels of the educational system, and early deficiencies accumulate over time. School readiness and early literacy skills are low hampering children’s educational development in later years, and perpetuating inequalities across generations. While coverage of Early Childhood Education (4-5) and the first cycle of primary education are high, quality remains low, as expressed in low test scores in early grades. Ensuring children are off to a good start by improving school readiness and early literacy is key to create a strong platform for later years.

Figure 81. Share of children who attend school, by age, 2016

Figure 82. Share of students with below basic knowledge in math, by socioeconomic status, 2016

Source: Calculations based on data from SEDLAC (CEDLAS and World Bank).

121. In addition, access to quality education is highly unequal across socioeconomic groups and place of residence, limiting mobility across generations. Students from poorer background are six times more likely to have low educational attainment in science than those from richer background, a difference
that is twice as high as in advanced economies.\textsuperscript{149} What is more, Argentina is the Latin American country in which the socioeconomic status of the family most influence learning outcomes.\textsuperscript{150} Primary school students from a poor background are over three times more likely to perform below the basic standard in math than those from a richer background, and these differences worsen as the child progresses in the educational system (Figure 82).\textsuperscript{151}

122. Finally, the education system does not adequately prepare students for entering higher education or the labor market. Low completion rates reflect, in part, the fact that the secondary model has limited relevance given current skills needed, lowering the benefits of remaining in school and restricting future insertion in high-productivity jobs. In addition, the limited quality of basic education has resulted in high-school graduates that are poorly prepared for higher education, which in turn translates into low completion rates and high time-to-degree indicators. Indeed, Argentina ranks poorly among the countries in the region in terms of these two indicators.\textsuperscript{152} The rapid expansion of higher education over the past 10-15 years disproportionally benefited students from the left-tail of the distribution. However, many of these students are the first-generation in their families that access higher education and are poorly informed about higher education programs and returns, and are particularly academically unprepared for higher education, limiting the equalizing effects of the expansion in coverage. Global evidence suggests that indeed, in this context, the increased access might translate mostly into poor completion rates and low—and in some cases even negative—returns to higher education. True equality of opportunity requires not only to improve access to tertiary education but also to support strong remedial and developmental programs and, more important and cost-effective, to level the playing field in early and basic education.

123. Improving learning will require a combination of measures at all levels of the educational system. Improving the quality of early childhood education (ECD) and early math and literacy interventions could have a substantial effect on improved learning outcomes and completion rates later on. A more direct focus on learning calls for strengthening teacher career and professional development, improving both in-service and pre-service training (including the reorganization of thousands of atomized institutes into fewer high quality centers with stringent standards) to attract the best candidates to the teaching career and to motivate teachers to perform. Revamping secondary education by supporting a switch from a paradigm of acquiring encyclopedic knowledge to one prioritizing critical basic cognitive skills and skills for the 21\textsuperscript{st} century (including socio-emotional skills) and re-thinking the role of universities would be critical to be able to compete in the economy of the future. This is the cornerstone of the ongoing flagship reform of the secondary model in Argentina, \textit{Secundaria 2030}.\textsuperscript{153}

124. In addition, enhancing the efficiency of the educational system will call for reassessing the allocation of resources both at the macro (ministry) and micro (school) levels. At the macro level, education policy should be progressively guided by evidence-based decision making that help to identify

\textsuperscript{149} OECD, 2017.
\textsuperscript{150} Ferreira et al, 2013.
\textsuperscript{151} Aprender, Ministerio de Educación y Deportes, Argentina.
\textsuperscript{152} World Bank, 2017
\textsuperscript{153} See https://www.educ.ar/recursos/132104/marco-para-la-implementacion-de-la-escuela-secundaria-2030. The so called “Secundaria del futuro” is to be based on a competence approach, comprising six basic competences: (i) problem solving; (ii) critical thinking; (iii) learning to learn; (iv) team cooperation; (v) communication, and (vi) commitment and responsibility. The document also includes achievement for objectives each cycle of schooling, and on project-based teaching and integration of areas and subjects as well as general guidelines for re-organization of learning, teaching, academic regime, and training and mentoring. Regarding teachers, the project promotes concentration of teaching hours in one school, more time for institutional planning and the creation of stable teaching teams. Implementation will be gradual, and each province will follow its own planning.
cost-effective initiatives that should be scaled-up and/or expanded (or not). This also requires a solid monitoring and evaluation system, and strong management skills for second-level and intermediate government officials. At the micro level, global evidence identifies school principals’ management skills as a priority area of intervention.

125. **Non-communicable diseases and injuries are becoming increasingly important, particularly among men, and can limit further increases in productivity.** Nowadays, Non-Communicable Diseases (NCDs) and injuries have become the main burden of disease, potentially generating large productivity losses caused by worker absenteeism, disability and premature deaths. Among men, 42 percent of all NCD deaths are among those under 70 years old (while the proportion among women is 27) (Figure 83). Indeed, significantly more adult men than women are likely to be overweight, have high blood pressure, and smoke, despite being slightly more active physical (Figure 84). In addition, being obese and overweight is increasing among children\(^{154}\) and Argentina now tops the regional ranking for those under five.\(^{155}\) Yet, a large share of the premature NCD burden can be prevented or controlled through a reduction of common risks factors associated with these diseases, such as unhealthy diets, physical inactivity and a tobacco use and alcohol abuse. Preventative care is particularly deficient among the more vulnerable population, which are more likely to be exclusively covered by the public health system. Indeed, those patients are less to have cervical cancer screening (60 vis-à-vis 72 percent of the rest of the population), receive mammographs among women aged 50-70 (48 versus 66 percent), and have a high blood pressure control test (71 versus 82 percent). A shift of resources toward prevention and treatment of non-communicable diseases will be required.\(^{156}\)

![Figure 83. Proportion of NDC related deaths under age 70, in percent\(^{\dagger}\), 2010](image1)

![Figure 84. Risk factors of non-communicable diseases, Argentina. Circa 2015](image2)

**Source:** Data from WHO.

126. **Despite improvements in the past 15 years, there are large inequalities in health outcomes across income levels, migration status, and geographic location.** In addition to differences in basic infrastructure services (such as water and sanitation), differences in health outcomes reflect the coexistence

\(^{154}\) Almost 40 percent of school-aged children is overweight or obese (Source: *Programa Nacional de Salud Escolar 2016* (PROSANE), Ministry of Health), which is more than 15 percentage points higher than in OECD countries (Source: OECD Health at a Glance, 2015).

\(^{155}\) Pan American Health Organization (PAHO)/WHO

\(^{156}\) World Bank, 2017d. To address this issue, the Argentine Government developed and initiated the implementation of the National Strategy for the Prevention and Control of NCDs and Injuries 2009.
of a fragmented system in which those that have access to the contributory social health insurance are able to access more effective services, at least for prevention and control of chronic diseases, than those who rely on the public system. Given that access to different health systems is associated with labor market status, there is a strong relationship between socioeconomic status and services provision: while overall over two thirds have access to the contributory social or private insurance systems, less than 30 percent among those the poorest quintile do so.\textsuperscript{157}

127. Reducing these spatial and socioeconomic differences in a federal country with a fragmented social system might be achieved by creating incentive mechanism to enhance coordination and harmonization of standards across providers, as well as by strengthening the existing compensatory instruments. One such example is the experience with the Plan Nacer/Sumar Program, whose objective was to improve health outcomes (particularly maternal mortality, child morbidity and mortality). The program implemented “a public insurance strategy and a pay-for-performance scheme in order to solve agency relationships between the Nation and the provinces, and between the provinces and the health facility networks, in turn. By means of such instruments, the idea was to align the priorities of every involved institutional decision-maker and to generate incentives that operate on the teams of healthcare facilities”.\textsuperscript{158} The impact evaluation of the program showed that it reduced coverage gaps across provinces and improved health outcomes for vulnerable pregnant women and children living in the poorest regions of the country.\textsuperscript{159} The program was successful in increasing the use and quality of prenatal care services and the probability of receiving the tetanus vaccine. As a result, Plan Nacer beneficiaries have seen a reduction in the probability of a stillbirth by 26 percent and the probability of low birth weight by 7 percent.

\textit{Improving people’s access to markets}

128. Access to financial services in Argentina is low, limiting people’s ability to accumulate assets. Less than half of Argentines report having an account at a bank or another type of financial institution, and only 37 percent among those in the bottom 40.\textsuperscript{160} While higher than in other Latin American countries -such as Colombia, Mexico or Peru-, such access is still too low when compared with New HIC where, on average, more than 70 percent of adults do so (Figure 85). In addition, while women are more likely to access to financial institutions than men (50 against 45 percent), and equally likely to borrow money from formal channels, 71 percent of women consider that it would be impossible to raise with emergency funding, vis-à-vis 51 percent among men.

\textsuperscript{157} Source: based on EPH 2016 (INDEC).
\textsuperscript{158} “Monitoring and Evaluation (M&E) in a P4P Health Program in Argentina: a mechanism to provide datasets to assess the use and quality of health services, the health status of the population and the “fine-tuning” of the Health Reform Strategy: The case of Plan Nacer /SUMAR Program in Argentina (2004-2015)
\textsuperscript{159} Gertler et al., 2014.
\textsuperscript{160} Source: Global Findex Database 2017, https://globalfindex.worldbank.org/
129. **Access to credit (including to mortgages) is scarce and varies largely depending on income, reinforcing existing inequalities.** On average, one in five borrowed from a financial institution, while only one in ten did so among the poorest 40 percent. In addition, while poorer people tend to rely on personal loans and closed card systems issued by non-financial institutions, a high proportion of the credit taken by richer people is through a mortgage (Figure 86). As a result, the better-off can borrow higher amounts of money and can refund it a longer period, but also interest rates charged are lower. On average, only 7.8 percent of Argentines have outstanding mortgage loans (and lower than 5 percent in the B40), limiting families’ possibility of owning their own home.

130. **Not only households, but also firms face difficulties in obtaining finance, particularly small firms which make up the brunt of employment and job creation.** Improving access to finance, particularly to small firms, is fundamental to increase its productivity. Yet, according to the Enterprise Survey (2010), 15 percent of the firms in Argentina identify access to finance as the biggest business environment obstacle, behind tax rates (19.6 percent), and 43.5 percent consider it a major constraint compared to 28.4 and 26.5 for the LAC average and all other countries in the sample, respectively. Among female-led firms, the proportion that consider finance a major constraint is even higher, at 57 percent. Lack of finance is substantially worse for small business, and the reported gap between small and large firms is wider than that reported in Latin America (1.5 times higher) and all the countries in the sample (3.5 times higher). The differences in access to finance across gender is stark: while 52 percent of firms managed by a man have a bank loan or line of credit, only 25 percent of women led firms do. Similarly, 15 percent of investments in male headed firms come from banks, compared to 4 percent of investments in firms with a female top manager.

131. **People’s access to employment opportunities is also constrained by transport efficiency.** In Greater Buenos Aires, the average number of jobs per worker accessible within a one-hour commute depends on the level of income: around richer downtown Buenos Aires it is significantly larger than in the Partidos of Greater Buenos Aires. This means that those living in one of the poorest areas in Argentina have less

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162 Quirós and Mehdiratta, 2014.
jobs opportunities, or that they need to spend more time travelling to have the same amount of labor opportunities. The difference based on income is, in part, related to the available means of transport across economic groups. While most of the users of subway (metro) are high income, less well-off individuals tend to use a combination of railway and buses. This is both the result of the territorial coverage of each means of transport -there are no subways outside the city of Buenos Aires – as well as its affordability -subways are the most expensive means, whereas trains are the cheapest. As buses and railways need more time than subways to cover the same distance and given that jobs are scarcer in poorer areas, these users spend more time traveling, reducing their spare time for other activities.

132. **Women in more vulnerable neighborhoods are specially constrained in their use of public transportation due to issues of security and social norms.** Preliminary results of a recent study carried out in Buenos Aires on women’s mobility barriers and facilitators show that in neighborhoods such as Villa 31 and Ejercito de los Andes, security issues influenced women’s decision on their selection of public transport modes and time to travel, which led in several occasions to longer travels. For instance, because of insecurity, some buses, that should be traveling inside the neighborhoods, preferred to use alternative routes far away from the predefined bus stops, increasing users’ exposure to additional security risks. In addition, social norms influences travel behaviors for women. Those with young children prefer to work in their communities to be closer to their children, limiting their options in terms of economic opportunities. Moreover, even when their children reach adolescence, mothers prefer to stay near home to ensure their kids do not get involved in criminal activities, which are more prevalent in these vulnerable neighborhoods. Finally, the study shows that even if some of the barriers to increase women’s mobility depend of the transport sector, such as providing safe and alternative forms of transportations, others need a multi-sectoral effort (such as child care provision).

*Making cities livable, inclusive and productive*

133. **Today, Argentina has a system of geographically diverse cities and persistent lagging regions where significant differences in access to basic services prevail.** The proportion of households with unmet basic needs (NBI) in the Northern regions of the country is 15.9 percent compared to a national average of 9.1 percent. The rapid convergence across provinces in the access to basic services in the past four decades such as safely managed source of water has not been seen in terms of sanitation. In the case of access to water, while the lowest proportions of households are found in Northeastern provinces (Chaco, Formosa, Santiago del Estero), the coverage still reaches 75 percent among them -vis-à-vis 99 percent in the city of Buenos Aires. But in the case of sanitation, the coverage gap is particularly striking: less than a fourth of households in provinces such as Chaco, Misiones and Santiago del Estero are connected to a sewer, another 60 percent has basic sanitation, leaving behind between 9 to 21 percent of households with unimproved sanitation services. In the rest of the provinces, the latter figure is less than 6 percent. These conditions increase families’ sanitary and environmental risks, worsening even more their social vulnerability, and increasing their exposure to illnesses such as respiratory disease, diarrhea and iron deficiency.

The population growth in urban areas has not been accompanied by adequate investments in infrastructure and services, leading to growing informal settlements, sprawl, congestion, pollution,
crime, exacerbating social exclusion. Agglomerations in Argentina have experienced high and increasing levels of sprawl, with the sprawl index\(^\text{166}\) increasing from 1.4 in 1990–2001 to 2.3 in 2001-2010 (Figure 87). In many cases, this has resulted in low-density, fragmented and spatially segregated cities, characterized by isolated high-income gated communities and low-income informal settlements marginalized in the city’s peri-urban areas. The spatial inequality that arises is reinforced by failures in housing and transportation policies. As a result, growth opportunities are being lost: evidence indicates a negative and statistically significant effect of sprawl on economic density. A denser city would also reduce the cost of basic infrastructure provision, contributing to reduce territorial disparities. In places such as the services Metropolitan Area of Buenos Aires (Area Metropolitana de Buenos Aires, AMBA) or Santa Rosa, access to sewage network is almost universal at the core of the agglomeration, but it is below 60 percent for the peri-urban areas (Figure 88).\(^\text{167}\) The rise in the quantitative housing deficit between 2001 and 2010 has led to an increase of informal settlements. It is estimated that 17 percent of the population lives in one of the 4,000 vulnerable settlements in the country, mostly located in peri-urban areas.\(^\text{168}\) Whereas barriers to housing finance have been a binding constraint over the past decades, Argentina also faces supply-side constraints that limit access to affordable housing. Finally, air pollution in cities such as Buenos Aires (factors of six), Cordoba (factor of three) and Mendoza (factor of two) are a multiple of the WHO recommended threshold.\(^\text{169}\)

Figure 87. Sprawl and agglomeration economies

Figure 88. Access to sewerage network: core urban areas vs. periphery, 2013


\(^{166}\) The sprawl index measures the increase in the built-up area relative to a benchmark where the urban built-up area would have increased in line with population growth. In Argentina, this is measured in 26 agglomerations. The sprawl index is equal to zero when both population and the urban built-up area are stable over time. It is greater (or smaller) than zero when the growth of the urban built-up area is greater (or smaller) than the growth of population, that is, the city density has decreased (or increased). \(^{166}\) Muzzini et al., 2017.

\(^{167}\) Refers to Barrios Populares, defined by the government as at least 8 families grouped, where more than half of the population does not have the land title or regular access to two or more basic services (water network, electrical network with meter and/or sewerage network). Relevamiento Nacional de Barrios Populares. December 2016. Jefatura de Gabinete de Ministros. http://datos.gob.ar/dataset/barrios-populares-argentina

\(^{169}\) World Bank, 2016a.
134. Climate change and environmental degradation pose a growing challenge to Argentine cities. Urban flooding is recurrent in AMBA, particularly for those living in the outskirts. A recent study estimates that 236,000 people in the three main basins around AMBA cannot cover the basic consumption basket of goods and services, making them highly vulnerable to impacts of flooding. The recurrent flooding in the Autonomous City of Buenos Aires (CABA) has a negative impact on the livelihood of its 3 million inhabitants and its more than 2 million daily commuters—who come to the city to work, study, and access health institutions. Disruption of transportation systems has a considerable negative impact on the livelihood of particularly those living in the outskirts (it has been estimated that from the total commuters 47 percent belong to the lower quintiles of income). Over time, many natural runoff systems have been covered up or "tubed" and are now blocked, increasing the risk of flooding. The combination of urban flooding and riverine flooding increases the risk manifold. In recent years, more than 200 housing developments have been built in the floodplains of the Parana Delta near Buenos Aires. These constructions prevent the natural runoff of water that would cushion the impact of floods, increasing the risk of urban flooding in the metropolitan area. Solid waste management is also an important problem, with approximately 4 million inhabitants without regular collection services, particularly in slums (14.3 percent not covered). Open dumps remain the most common mode of disposal in Argentina, particularly in poorer communities: nearly 90 percent of the municipalities dispose their waste in open or semi-controlled dumps without adequate sanitary controls.

135. Lack of integrated planning in urban areas has prevented efficient and sustainable urban growth, limiting the potential of cities to contribute to the country’s long-term prosperity. While in development, there is not yet a national framework to guide urban development. Provincial governments usually have weak regulatory frameworks to oversee municipal land use planning. Municipalities are responsible for land use planning, but they typically do not use all available planning tools to guide development of their territory partly because many of them lack capacity or incentives to update land use regulations. The limited responsibilities delegated by provinces to municipalities often prevent municipalities from integrating land use planning with transport systems and from carrying out long-term planning for public works, for which responsibilities are fragmented across tiers of governments. Successful urban policies are typically integrative of a wide range of sectors. Integrated planning across different sectors is critical to: (i) ensure that investments have a greater impact at the city-level enhancing inclusive economic growth; (ii) optimize scarce resources to ensure that long-term objectives and sequencing are coordinated across sectors; and (iii) optimize impacts on poverty and inequality. Enhancing coordination of urban policies at the municipal and metropolitan level and promoting sustainable growth through improved housing policies and urban mobility will be essential to improve the livelihoods of the urban poor. A more equal provision of basic services such as water, wastewater infrastructure and drainage would require widening and strengthening the financing options, such as developing clear mechanisms to set up a

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171 In April 2013, CABA experienced one of the heaviest storms recorded in nearly 50 years, resulting in key transportation routes being submerged and mass-transit system shutdowns. Power outages lasted for as long as 15 hours in many neighborhoods and up to several days in a few others. Direct damages and losses of this event amounted to US$300 million. In addition, fiscal impacts (subsidies and tax exemptions) of severe weather events are important—the events recorded in April 2012 and April 2013 were estimated to result in a US$49 million budget impact. Logistics disruptions also had a negative impact on the overall economy.
172 World Bank, 2016a.
173 The Government of Argentina is currently working on the “Política Nacional Urbana y del Hábitat” but it is not yet implemented.
transient system of fiscal transfers to provinces (with an opportunity, for example to design them with “performance based” criteria). 174, 175

**Strengthening social protection for a more inclusive society**

136. Argentina’s fiscal system is one of the most redistributive among developing countries and some of new high-income economies. The difference in the Gini coefficient between the market income and the disposable income in Argentina is larger than countries such as Chile, Mexico, Turkey or Korea, but still lower than most OECD countries (Figure 89). 176

137. The large redistributive capacity is largely due to a strong social transfer system (especially pensions), against limited labor policies, regressive energy subsidies and low direct taxation relative to peers. Argentina’s social security system is a combination of contributory and non-contributory systems. Pensions, family allowance and unemployment insurance are partially funded through payroll contributions (from employees and employers), although general revenues are often needed to cover the deficit. The reforms since the mid-2000s toward the extension of benefits to the uncovered population through the non-contributory family allowances (AUH), the two pension fund moratoria and the new non-contributory pension represent an increasing burden to the system. 177 Yet, these transfers substantially reduce poverty and inequality, even to a larger extent than other countries in the region. Unemployment benefits play a small role in reducing poverty and inequality since its coverage is limited (around one-tenth of unemployed, mostly non-vulnerable) and the benefit is low. While subsidies to energy consumption and transfers remain sizeable and regressive, with more than half going to the richest quintiles though the recent reforms toward reducing these subsidies while creating a social tariff to protect the most vulnerable should improve its incidence. 178 Direct taxes are close to Latin American averages but significantly lower than OECD countries. An extremely high-income tax threshold (at 5 times the average income) and low levels of compliances, combined with a poorly progressive but high social security contributions (at 35 percent) in a context of high informality, result in a limited redistributive impact of direct taxation. 179

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174 Muzzini et al., 2017.
175 This is key in the AMBA context, where managing water within administrative boundaries of municipalities often impedes a more integrated management of water considering the basin, and ignores the upstream-downstream links. This requires better institutional coordination (concept of integrated urban water management).
176 Lustig (2017) and OECD (2017) both present international comparable estimates of the size of redistribution, and in most cases, the rankings are similar.
177 The pension fund moratoria allowed workers with insufficient years of contribution to declare their work history in the informal sector, but gain access to a pension which includes a penalty related to the non-contributed years. In 2016, a universal non-contributory pension system was installed to avoid the need for future moratoria. The pension received is equivalent to 80 percent of the minimum contributory pension benefit.
179 OECD, 2017.
138. **Non-contributory transfers (especially, AUH) play an important role protecting the most vulnerable, but 0.5 million children out of 13 million are still excluded from the benefit.** Conceived to universalize the family allowances to families that do not contribute to the formal system, the AUH turns out to be effective in reaching the most vulnerable, with no substantial negative impact on labor participation.180 With a fiscal cost of approximately 0.5 percent of GDP (one of the highest in LAC), the AUH reaches 3.9 million children and distributes over 80 percent of its transfers to the bottom 40 percent of families.181 Given the size of the transfer (equivalent to a child’s food basket), AUH is insufficient to lift families out of poverty—only a tenth of beneficiary families were able to do it.182 In addition, 4 percent of all children are currently not covered by either the contributive or the non-contributory family allowance system. Coverage gaps are due to different factors, including delays or lack of necessary documentation, the non-compliance of co-responsibilities and the coexistence of non-traditional household arrangements, that might disproportionally affect those that are most excluded in the society.183 Larger efforts are needed to solve administrative problems and to better understand their household socioeconomic situation of the uncovered population to better design policies to close the gap.

139. **Because of the limited and weak policies directed to central ages, the social protection system might be not sufficiently prepared to deal with the transition to an outward high-productivity model.** Active labor policies remain limited and spending on these programs is well-below the OECD average (0.05 vis-a-vis 0.15 percent of GDP). The unemployment insurance is the main instrument available to help cope with the loss of employment. Yet, it has limited coverage, particularly for workers in sectors that are likely to lose, where formality is low, and has relatively low benefit, due to the lack of indexation. Active labor market policies (ALMP), on the other hand, have the potential to help retrain and reallocate (through

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180 Maurizio and Monsalvo (2017) do not find any significant effect of perceiving AUH on labor force participation or hours worked. On the other hand, Garganta and Gasparini (2017) do find a positive impact on wages of informal workers and a small negative impact on hours worked, particularly among vulnerable women (primarily, secondary workers) but the effect, while significant, is not large. Yet, the authors do find evidence of a significant disincentive to formalization of new workers while no informalization of current formal employees. Both studies use non-experimental techniques given that no randomization of the program was done. They differ, however in the control group use, with the former potentially underestimate the impact and the latter overestimate them.


182 Estimates suggest that an additional 2.4 percent of GDP would be needed to lift the recipient families out of poverty (official definition) and another 0.85 percent for the poor non-recipients.

183 Davolos and Beccaria, 2017.
intermediation services) some of those affected by the shift. In the last years, ALMP have shifted toward the provision of training and intermediation services against direct employment. Examples include Red de Oficinas de empleo, Programa Jóvenes con Más y Mejor Trabajo (both from the Ministry of Labor), and PROGRESAR (from the social security administration, ANSES). Nevertheless, the absence of a single institution to oversee and coordinate these ALMPs, as seen elsewhere in LAC, becomes more evident in a landscape where private training providers co-exist with training centers run by trade unions or directly provided by governments at different levels of public administration. The incidence of the private sector in labor intermediation is even more pronounced than in the case of training. The profit seeking nature of these (non-policy) actions impose additional barriers (search costs) to labor mobility.

140. Enhancing interinstitutional coordination of active labor market policies will be essential to prevent low coverage and administrative inefficiency given by the multiplicity of institutions implementing these programs. In addition, a consolidation of a national labor training policy would facilitate national surveys of employment demand providing systematic information on what skills businesses need and on the relevance of socio-emotional skills both for the more employable population and for those most difficult to place (i.e. young people who are not studying or working) and would enable curricula and skills certification to be demand-oriented. While such interventions are not a panacea, they are often more effective when they combine the various components of such programs (classroom training, internships, development of social and emotional skills, etc.). In terms of intermediation, the use of digital technologies may reduce costs both due to competence as well as length of search periods for open vacancies. Yet, it is unclear whether these technologies may have a differential impact along the whole range of labor qualifications (higher for more qualified workers).

141. Finally, pensions are fundamental for protecting the income of the elderly population, but its spending is large and the demographic change will put additional pressure on its fiscal sustainability, maintaining coverage and adequacy. It is estimated that two-thirds of the pension moratorium go to the poorest three deciles of the income distribution (OECD, 2017). Yet, with more than 11 percent of GDP going to the pension system, Argentina spends a higher proportion of its social public spending to the elderly through the pension system than its peers resulting in differential gaps between the lifecycle deficit curves and the net public transfers (Figure 90 and Figure 91). This is the result of a high level of coverage, as well as due to pension benefit levels that are above its peers. The demographic transition process toward an older population structure will put pressure on the social security and health/long-term care system for the elderly and its fiscal sustainability. Currently, older adults benefit much more than do children from net per capita public transfers; however, the family allowance program means that this imbalance is much less than exists in other countries (Figure 92). Estimates, based on National Transfer Accounts calculated for 2010, indicate that future pension expenditure is projected to reach 15 percent of GDP by the 2050s (Figure 93).

142. A pension reform that ensures inclusion and equity, while balancing the fiscal burden will not be straightforward. One option would be to consider a system that combines a universal non-contributory scheme, which provides a basic benefit to all senior citizens who do not reach the minimum required contributions, and a contributory pillar proportional to the number of years of contributions and labor income level. On top of these, a voluntary scheme can also reduce the burden to the system, while incentivizing savings. Other reforms include the flexibilization of the retirement age to generate financial incentives that

184 Recent reviews on active labor market policies in Latin American countries show that they are particularly effective in increasing formalization, while results on increasing the probability of employment or higher earnings are more mixed. Retraining tends to be more effective than help with job search or private sector employment incentives. Results are also better when directed to youth than older workers (Busso et.al 2017, McKenzie 2017, Escudero et al 2016).

185 WDR 2013 Jobs.
motivate the delay of the retirement, even more among those workers with higher productivity. As an important step, Congress passed an adjustment to the current indexation scheme in December 2017.

Figure 90. National poverty incidence, in percent, by age group, before and after transfer program

Sources: Calculations based on data from SEDLAC, EPH-C 2016, extending Rofman and Apella (2015).

Notes: Poverty rates are calculated excluding each transfer, in a cumulative manner. AUH: Universal child benefit, PLM: Pension lower than the minimum, UI: unemployment insurance, AF: family allowance.

Figure 91. Public pension expenditure relative to peers, in percent of GDP

Sources: Data for Argentina, Brazil, Chile, Colombia, Mexico, and Uruguay: Ministry of Finance. Argentina includes Provincial expenditure. Rest of the countries from OECD’s Pension at a Glance (2015).

Figure 92. Ratio of net per capita public transfers between older adults and children

Source: Comelatto (2015).

Figure 93. Projection of total expenditure on retirement benefits and pensions, 2010-2100, in percent of GDP


Note: Projections are based on the estimation of National Transfer Accounts for 2010, when public expenditure on pensions had reached 9.1 percent, which is several points below current estimates. Hence, the figure should be taken to represent pension spending trends, rather than levels.
Creating social capital to curve crime and violence

143. Homicide rates remain low relative to the region but the incidence of crime is among the highest, and citizen’s security remain a high priority for citizens and governments at national and provincial level. At 6.5 homicides per 100,000 inhabitants, the homicide rate is one of the lowest in Latin American countries—where it reaches around 26 homicides per 100,000 in Brazil or Mexico—though it is three times higher than in New HIC and OECD countries (2.7 and 2.0 per 100,000, respectively). On the other hand, the proportion of people affected by any sort of crime (included assault, attack or other crime) is one of the highest in the region. While on average victimization rate in LAC is around 43 percent, it reaches 47.1 percent in Argentina. Young men particularly bear a disproportionate share of the risk of committing crimes, with important repercussions for their life trajectories and society as a whole. Violence against women and girls is on the rise, negatively affecting women’s opportunities for development. The latest Victimization Survey (2017) provides some sex-disaggregated data, showing that men and women report similar levels of having been victims of non-violent crime, while more women (12.7 percent) than men (9.3 percent) report having been victims of violent crime. In terms of perceptions, 85 percent of Argentines declare that insecurity in their cities is a serious or very serious problem (particularly among women), and less than half feel safe walking around their own neighborhood. Importantly, around 45 percent believe that insecurity has worsened where they live.

144. Among factors that affect people’s increased sense of insecurity is the fact that the identification of drugs selling points increased considerably during the period 2010-2015. The percentage of people who answer that drugs are sold in their neighborhood rose from 30.2 percent in 2010 to 46.8 percent in 2015. Even though this pattern was observed across different type of neighborhoods, the rate grew faster in slums and low-class neighborhoods. While the prevalence was around 25 percent in high-class neighborhoods, it reached 80 percent and 65 percent in the informal settlements and vulnerable neighborhoods, respectively.

145. On the other hand, the majority of crimes are not reported to the authorities mainly due to public mistrust. Around two out of three crimes against people were not reported, and half of them were not reported because victims do not trust authorities. Among those that reported the crime, more than half are unsatisfied with the way the authorities handled the report. Most often, the victim felt that the authorities were not sufficiently interested in the case. Comparing to other countries in the region, four out of five people believe that protection against crime is not ensured or, at least, not satisfactorily. This is more than ten points higher than in countries such as Brazil, Mexico or Colombia.

146. Although data on gender-based violence (GBV) is scarce, the few figures known show an alarming situation, mainly for women who lack economic autonomy. More than sixty thousand phone

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186 UNODC
187 Jaitman, 2017. The victimization rate is defined as the percentage of the population that claim to have been assaulted, attacked, or the victim of a crime in the past 12 months.
188 INDEC (2017).
189 Bonfiglio, Rival and Rodriguez Espinola (2016) based on Encuesta de la Deuda Social Argentina, UCA.
190 People are considered crime victims when they have been victims of a violent theft, pickpocketing, fraud, bank fraud, physical aggression, threat, sexual harassment, or was asked for a bribe by a public agent. Source: INDEC (2017).
192 The UN Declaration on the Elimination of Violence against Women (1993) defines GBV as any act that “results in, or is likely to result in, physical, sexual or psychological harm or suffering to women, including threats of such acts, coercion or arbitrary deprivations of liberty, whether occurring in public or in private life.” As it generally impacts
calls were made to the free phone line specifically created to provide information, orientation and support to women victims of GBV in its first two years of operation (2013-2014). In 2016, around 100,000 cases of GBV were registered, and in most cases (98.4 percent) the perpetrator was the partner. In fact, the Argentine Supreme Court reported 254 women victims of femicide, of which 164 were killed by their partner or ex-partner in 2016. An overwhelming majority of cases of GBV are related to domestic violence and to repeated situations of violence already registered in the system. Women survivors of intimate partner violence find that one of the main obstacles to removing themselves from the situation is the lack of economic autonomy, as many times their only source of economic support is the perpetrator himself. For example, half of the women who reported living in a relationship in which violence is prevalent, were not working or having any source of independent income. Box 7 summarizes the recent Ni una menos movement to protest against gender-based violence in Argentina.

Box 7. Ni una menos

Ni una menos means "Not one [woman] less" in Spanish, comes from a phrase coined by the Mexican poet and activist Susana Chávez in 1995: "Ni una muerta más", used during protests against female homicides in Ciudad Juárez. Chávez was assassinated in 2011, and the phrase became a "symbol of struggle".

In Argentina, the “Ni Una Menos” movement began in 2015 to protest against gender-based violence and stop femicides (see www.niunamenos.com.ar). The movement was started by a group of Argentine female artists, journalists and academics, and spread across Latin America. A May 2015 protest became massive when the body of Chiara Paez (14) was found beaten to death and a few weeks pregnant, buried underneath her boyfriend’s house. By June, the request for female safety was present in huge demonstrations in front of the Argentine Congress. Following this, street demonstrations also sprung up in other countries in the region such as in Chile, Peru, Bolivia, Paraguay, Uruguay, El Salvador, Guatemala, Mexico and Spain, giving the movement a greater international momentum. Ni una menos was able to establish in public and political agendas themes such as femicide, gender gaps and roles, harassment, legality of abortion, and sex worker and transgender rights.

147. Different institutions collect data on GBV, but there is an important challenge in integrating and harmonizing the information, and the reporting rates are presumed to be underestimated. Institutions that collect data include the Supreme Court of Justice, the police, the Observatory of Femicide “Adriana Marisel Zambrano”, and the National Institute of Statistics and Censuses. There are several challenges in collecting accurate and complete data on gender-based violence. Under-reporting is a serious issue: many sources of information on GBV depend on the reporting of the episode, which may not occur due to the victim’s lack of confidence, economic autonomy, trust in authorities, or knowledge about reporting processes. From the service providers’ side, problems include the lack of knowledge and clear protocols...
on accounting for what activities constitute an act of violence, and harmonized variables and institutional coordination that would allow for a more systematic, integrated collection of data at a national level.
Chapter 4: Sustainability and investing in natural capital

Overview of challenges and institutional context

148. This Systematic Country Diagnostic (SCD) stresses the importance of fiscal, environmental, and social sustainability aspects of the Argentina's growth and poverty reduction efforts. Achieving the twin goals of reduced poverty and shared prosperity in the short-term, but only at a cost of sacrificing those same goals in the future, is a trade-off Argentina does not want to make. Therefore, sustainability analysis must reconcile the short and the long term, and must take into consideration both current and future generations. Fiscal and social sustainability have been at the core of the discussion on the growth and inclusion pathways. This chapter identifies natural capital as a key driver of sustainability in the efforts to achieving the twin goals over the longer-term. It focuses on three key sets of issues: (i) management of natural capital; (ii) achieving climate smart development; (iii) addressing diseconomies originating from pollution. As will be shown in the next pages, the three defining characteristics set out in Chapter 1, resource abundance, aspirations of the middle class and unequal federation, play out through the degradation of key assets such as land, forests and fisheries, and by producing diseconomies and poor environmental quality in sprawling urban centers.

149. Argentina faces several environmental and climate change related challenges that must be addressed to sustain inclusive economic development and job creation in the future. Natural resources are facing severe pressures from anthropogenic activities, that constitute a threat to the sustainability of the development model that the country has followed. Soil-degrading agricultural practices, over-exploitation of fish resources, water degradation and pollution are putting at risk productive assets and affecting people’s quality of life. Deforestation and habitat fragmentation is driving loss of biodiversity and reducing forest resources at alarming rates; intensive agriculture risks depleting soils; pollution of air and water threaten human health; ineffective solid waste management affects quality of life; increased frequency and intensity of climate impacts pose severe risks by accentuating the effects of ecosystem degradation such as floods and severe droughts; and pollution due to untreated effluents, groundwater depletion in water stressed areas, or impacts from glacial retraction are degrading water resources. Furthermore, adequate Environmental Impact Assessment (EIA) framework and capacities to mitigate risks from investments are weak.

150. The federal system imposes complexities in natural capital management. Management of natural resources in Argentina takes place within a complex legal and institutional architecture. Provinces retain sovereignty over the management of natural resources in their territories and over enforcement, and the role of the federal government is to inform decision-making by proposing guidelines and standards for provincial level policy formulation and implementation. In fact, the Argentine National Constitution vests the Congress with the power to enact rules setting forth “minimum standards for environmental protection”. The Federal Council of Environment (COFEMA), or in the case of water issues the Federal Hydrological Council (COHIFE), serves as a space to discuss environmental issues and find solutions in a coordinated way. However, the COFEMA does not hold formal power to ensure compliance or with resources to carry out its mandate, which has historically hindered its ability to promote sustainability and avoid environmental degradation in provinces and municipalities. Meanwhile, there is lack of a strong information system

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In the case of water, the resources cannot be effectively managed at the basin level. There are basin councils in specific cases, but the fact that provinces have the legal jurisdiction over the resource adds a layer of complexity. Current conflicts on Rio Atuel between Mendoza and La Pampa, related to water scarcity, have reached the supreme
about the state of the environment that informs decision making and allows to plan, monitor and enforce regulations. This is reflected in the lack of clear priorities at the federal level.

151. As a result of these challenges, Argentina’s environmental performance is low in relation to countries with a similar level of income and worse than its regional and structural peers’. The Environmental Performance Index (EPI), covering environmental health (which measures threats to human health), and ecosystem vitality (which measures natural resources and ecosystem services), ranks Argentina 74th (with a score of 59.30) among 180 countries in terms of overall environmental performance, below most of its peers except for Malaysia (which ranks 75th with a score 59.22), Chile (84th; 57.49) and Turkey (108th; 52.96; See Figure 94), and it ranks worst in terms ecosystem vitality (133th among 180; Figure 95). In addition, although overall environmental performance improved in recent years, it improved less than in most of regional peers. Argentina went from 80th to 74th, whereas Mexico climbed 24 places, going from 96th to 72nd, Uruguay climbed 25 places, going from 72nd to 47th) and Colombia climbed 13 places, going from 55th to 42nd.

Figure 94. Environmental Performance Index score, 2018

Figure 95. Argentina’s ranking across dimensions of Environmental Performance Index, 2018

Source: Data from Yale CELP (2018). Environmental Performance Index 2018.
Note: Current scores are based on most recent year of data available, and Baseline applies to data roughly one decade prior.

152. A key achievement, in recent years, is the establishment of an on-par relationship between environment and other sectors in the national executive, and this will be instrumental in tackling key priorities identified in the SCD. The Ministry of Environment and Sustainable Development (MAyDS) court. There are also conflicts in El Salado river basin, between Santa Fe and Buenos Aires, La Pampa, related to flooding.

198 The 2018 Environmental Performance Index (EPI) scores 180 countries on 24 performance indicators across ten issue categories covering environmental health, which measures threats to human health, and ecosystem vitality which measures natural resources and ecosystem services. These metrics provide a gauge at a national scale of how close countries are to established environmental policy goals.
replaced the Secretary of Environment and Sustainable Development in 2015. With this elevation in status, on taking power the Administration sent a clear signal on the importance to mainstream sustainability considerations into different sectoral plans and policies at the state level in a more efficient way. The SCD identified several environment-related priority issues. These include: (i) forest, land and natural capital depletion; (ii) the increasing severity and frequency of extreme events (including the likely impact of climate change in worsening future disasters and economic conditions in key development sectors); and (iii) pollution management, including the low capacity to manage risks in the oil, mining and infrastructure sectors. These issues have both short-term and long-term aspects, and they threaten Argentina’s achievement of poverty reduction and shared prosperity in the longer time frame. To illustrate this, this section will analyze the relationship between these various environmental sustainability issues and the twin goals.

The role of natural capital in Argentina’s economy

153. **Argentina has abundant natural capital, but there is still important scope to turn it into an engine of sustained growth and employment creation.** Natural capital has been a key driver of growth in the past. By the second decade of the twentieth century, Argentina had increased its income per capita by 190 percent, compared to 1870, reaching levels above those of Italy, Portugal and Spain. The country’s comparative advantage in beef and wheat, and its trade openness, contributed to this performance. However, while growth continued in some resource-rich countries over the later decades of the twentieth century, Argentina’s performance diminished. While in 1870, Argentina had a level of income similar to Finland, Norway, Sweden and Canada, by 1990 its income was between two and three times lower (Table 5). While there is a large literature showing empirically the so called “resource-curse”, which shows how natural capital-rich developing countries have grown more slowly than other developing countries, some authors have stressed how “natural resources are neither curse nor destiny”.

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<th>Table 5. Evolution of income per capita, 1870–1990</th>
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154. **Natural capital in Argentina includes agricultural soils and pastures; water; forests; fisheries; strong winds and solar potential; and subsoil assets (oil, gas, coal, and minerals).** Conservative estimates suggest that renewable natural capital, captured in the value of agricultural land, forest land and protected areas (thus excluding, given lack of data, many other resources such as fisheries) represents about 10 percent of Argentina’s total wealth. This puts Argentina on the top quartile of the list of regional and structural peers, following Turkey (26 percent), Peru (16 percent) and Brazil (15 percent). Moreover, Argentina has more than 20,000 m^3/capita of water availability, making it a water rich country. The majority of the population lives in water abundant areas (but there are important agricultural activities in water scarce areas, thus vulnerable to inefficient water management and climatic variability). Of course, natural capital also includes non-renewable resources such as oil, gas, coal and minerals. Insufficient data on potential

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199 The most influential article in this literature is probably Sachs and Warner (1995).
200 Lederman and Maloney (2007)
201 Lange et al (2018). The numbers for Argentina likely underestimate the value of pasture land, given the relative importance of cattle production compared to poultry, eggs, milk and pork. Rental rates used to estimate pasture land are based on a world average of these factors across the dataset.
future rents for Argentina, particularly related to the shale oil and gas reserves in Vaca Muerta, in Neuquén province, do not allow a similar comparison for total natural capital.

155. Soil productivity and abundant water underpin agriculture, a traditional driver of economic growth. Argentina has taken advantage of its abundant fertile land to develop a strong agriculture sector that has historically represented a key engine of growth for the country. While growth in the country has slowed down in the second half of the twentieth century, Argentina is among the top countries in the world ranking for production and exports on key commodities such as soybeans, soybean oil, lemons and limes, maize and wine (Table 6). Agriculture value added contributed on average 7.5 percent to the GDP between 2010 and 2016, and food exports represented on average 55.4 percent of merchandise exports in the same period, significantly higher than the contribution of agriculture to its peers’ economies. The agroindustry value chain contributes significantly to employment with 1 out of 6 jobs. The primary sector represents 46 percent of jobs in the agroindustry sector, followed by commercialization (26 percent), agro-processing (16 percent) and Transportation (12 percent). With respect to value chains, wine, fruits and vegetables, and industrial crops contribute 32 percent of the total jobs in agriculture; extensive crops and oilseeds, which have experienced the fastest growth rates, represent 35 percent; meat and dairy contribute 23 percent and 9 percent respectively; agricultural machinery contributes 1 percent. Little is known about the state of family farming, but evidence suggests that it plays an important role in agricultural employment as 53 percent of the sector’s employment comes from family farming (see also Box 8). Family farmers, if better integrated into value chains, could contribute to economic growth and rural job creation. They can play a significant role in tackling some challenges of the food system in Argentina, such as obesity, which is endemic among the poor, insufficient provision of fresh fruits and vegetables in domestic markets, huge food waste and losses, to give a few examples. In addition, there is an untapped potential for locally-grown food, an agenda where family farming systems can take center stage.

156. Forests and fisheries are also a potentially abundant source of rents but their contribution to the economy is limited. Argentina’s forestry potential remains largely unexploited. Despite its 1.2 million hectares of plantations and 50 million hectares of primary forest, silviculture, timber extraction and related services only contribute 0.2 percent of GDP (2 percent of the agriculture sector). Since at least 1990, Argentina has been a net importer of timber. Although the area under forest plantation has been increasing, the sector is much less developed than in Brazil or Chile. Fisheries are also a potentially valuable source of rents. With a surface area of 1 million km², Argentina has one of the largest continental shelves and is rich in marine and coastal resources. Both fisheries and forests are affected by open access, the so called “tragedy of the commons”, and high levels of illegality. Fish endowments, for example, have suffered from overexploitation due to the lack of a national management plan for sustainable and responsible fishing with a long-term vision. In 2017, fish represented 3.2 percent of total exports. Forests have also been under threat, as shown in the next section.

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202 Food comprises the commodities in Standard International Trade Classification (SITC) sections 0 (food and live animals), 1 (beverages and tobacco), and 4 (animal and vegetable oils and fats) and SITC division 22 (oil seeds, oil nuts, and oil kernels).
205 Guardia and Tornarolli (2010). Boom agrícola y persistencia de la pobreza rural en Argentina. Documentos de Trabajo del CEDLAS; no. 98
### Table 6. Argentina’s world share and world ranking in production and exports of selected agricultural commodities, 2013-2016

<table>
<thead>
<tr>
<th></th>
<th>Production</th>
<th></th>
<th>Exports***</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>World Share %</td>
<td>World Ranking</td>
<td>World Share %</td>
<td>World Ranking</td>
</tr>
<tr>
<td>All crops</td>
<td>1.9</td>
<td>8</td>
<td>5.7</td>
<td>3</td>
</tr>
<tr>
<td>All agricultural products (crops,</td>
<td></td>
<td></td>
<td></td>
<td></td>
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<tr>
<td>processed crops, and primary</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>livestock)</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Apples*</td>
<td>1.1</td>
<td>15</td>
<td>1.9</td>
<td>12</td>
</tr>
<tr>
<td>Grapes*</td>
<td>2.3</td>
<td>12</td>
<td>0.6</td>
<td>18</td>
</tr>
<tr>
<td>Lemons and limes*</td>
<td>9.7</td>
<td>4</td>
<td>10.5</td>
<td>2</td>
</tr>
<tr>
<td>Maize*</td>
<td>3.8</td>
<td>4</td>
<td>16.2</td>
<td>3</td>
</tr>
<tr>
<td>Soybeans*</td>
<td>17.6</td>
<td>3</td>
<td>7.3</td>
<td>3</td>
</tr>
<tr>
<td>Sunflower seed*</td>
<td>6.3</td>
<td>3</td>
<td>1.6</td>
<td>10</td>
</tr>
<tr>
<td>Wheat*</td>
<td>2.5</td>
<td>12</td>
<td>1.5</td>
<td>13</td>
</tr>
<tr>
<td>Oil, soybean**</td>
<td>15.5</td>
<td>4</td>
<td>40.9</td>
<td>1</td>
</tr>
<tr>
<td>Oil, sunflower**</td>
<td>5.9</td>
<td>3</td>
<td>5.1</td>
<td>5</td>
</tr>
<tr>
<td>Wine**</td>
<td>5.1</td>
<td>6</td>
<td>3.1</td>
<td>9</td>
</tr>
<tr>
<td>Meat, cattle*</td>
<td>4.0</td>
<td>4</td>
<td>0.2</td>
<td>30</td>
</tr>
<tr>
<td>Meat, chicken*</td>
<td>1.8</td>
<td>11</td>
<td>2.9</td>
<td>9</td>
</tr>
<tr>
<td>Milk, whole fresh cow*</td>
<td>1.5</td>
<td>17</td>
<td>0.0</td>
<td>57</td>
</tr>
</tbody>
</table>

*Source*: Calculated based on data from FAOSTAT.

*Notes*: All shares and rankings based on physical units. * data for year 2016; ** data for year 2014; *** data for year 2013.
ARGENTINA  
Systematic Country Diagnostic

157. **Argentina’s rich renewable energy potential could also become an increasingly important source of growth.** These include hydro, wind, solar and biofuels. Although hydroelectricity accounts for over one-third of the energy mix, Argentina only uses 20 percent of its hydro generation potential. Wind resources are world class, especially in the southern Patagonia region where capacity factors exceed 45 percent and solar resources are abundant, with the finest resources in the northwestern region. In addition, the country is already one of the world-largest producers of biofuels. However, as of 2012, less than 10 percent of total final energy consumed came from non-conventional renewable sources, lower than most countries in the region. Progress toward adopting clean sources of energy is yet to take place. Installed capacity is 60 percent thermal, 34 percent hydro, 5 percent nuclear, and 1 percent wind. Solar represents 8 MW (0.02 percent).

158. **Argentina also counts on untapped non-renewable energy reserves, but their development needs to be weighed against important risks.** After a decade of declining production, the conventional energy sector received considerable interest after the discovery of the world's second-largest shale gas reservoir and fourth-largest shale oil reservoir in the Vaca Muerta basin. Authorities expect these to supply as much as 50 percent of Argentina’s natural gas needs by 2021, and 60 percent of its oil requirements by 2020. Such developments however carry important risks. Some of them are related to the management of potential (and still somewhat unknown) environmental and social impacts, for which a solid framework is still needed (see Box 9). In addition, at a time in which countries around the world transition to sustainable energy as a mean to keep global temperature rise to below 2 Celsius, Argentina could miss-out on the benefits of global technological shifts that allow a wider set of low-cost options for countries to tap on to strengthen

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207. Argentina spent about US$15 billion in 2016 to import gas via its 2 LNG import terminals and pipeline with Bolivia to meet the gap between its domestic gas demand and domestic production.
energy supply and extend access to energy.\textsuperscript{208} Moving forward, it will be important for Argentina to see oil and gas as part of a broader strategy for the energy sector to respond to increasingly pressing domestic and global challenges.

159. Finally, Argentina’s unique natural landscapes and protected areas system, can be a driver of tourism development. The country has a huge variety of climates and ecosystems ranging from the tropical and dry forests in the North to the tundra and polar ecosystems in the South. Some key landmarks include the Andes, with the highest mountain in the world outside the Himalayas, the Aconcagua, the Iguazú Falls, the humid Pampas and the Perito Moreno glacier. Argentina’s tourism represents 7.1 percent of exports of goods and services (and the first in terms of services) and it generates 5.4 percent of employment.\textsuperscript{209} However, the country’s tourist assets are likely under-utilized. At its current stage of development, the tourism sector is expected to grow at 2.5 percent per annum, which is significantly lower than the forecasted global average growth, at 3.9 percent.\textsuperscript{210} Key challenges include the scarce diversification in international markets with a high dependency on neighboring countries, with a bias toward low end markets.

160. Summing up, an engine of growth in the past, Argentina’s natural capital still holds great potential as part of broader efforts toward openness and competitiveness. In addition to agriculture, which has been a key driver of growth at the turn of the twentieth century, Argentina has large unexploited potential in forestry—including native forests and commercial plantations—, in fisheries, protected areas and unique landscapes potentially attracting a growing number of tourists internationally, renewable energy and mining. But the country needs to break with the extractive policies of the past and consolidate a policy framework that attracts private sector investments. Policies, incentives and enforcement are also required to ensure that the open access that characterizes many natural assets, such as forests, land and fisheries, does not give way to illegality and degradation. Finally, a more sophisticated demand for greener attributes in global value chains is already emerging and Argentina has much to gain from developing information mechanisms in support of labels and practices that encourage the thriving green businesses throughout the country. These recommendations are presented in more detail in the following section.

Pathway 4: Investing in natural capital and ensuring environmental sustainability

Unleashing the potential of natural capital

Challenges

161. Forest depletion is one of the fastest worldwide. Argentina’s success in developing a competitive and productive agriculture sector has come at a high cost in terms of ecological externalities. The effective adoption of agricultural technologies resulted in increased profitability and rapid expansion of cropland into forest lands and often pushing pasture production into forest and other higher value biomes. World Bank

\textsuperscript{208} Low carbon transition worldwide can affect fossil fuel dependent economies through the emergence of a global price for carbon—and the related imposition of border carbon adjustments—and by the country’s own locking-into diversification patterns that are highly dependent on fossil fuels. In the case of Argentina, both the oil and gas sector and an evolving renewable energy sector could be impacted. World Bank (2018, forthcoming) analyses the optimal strategies for fossil fuel dependent countries in light of the uncertain yet rapid evolution of climate negotiations and argues for a careful assessment of the macro-fiscal and structural risks and opportunities of a low carbon transition; and the development of economic strategies that are robust under climate negotiations uncertainty and that foster cooperation in international climate initiatives.

\textsuperscript{209} Data from the Plan Integral de Gestión 2016-2019, Ministerio de Turismo, Gobierno de la Nación.

comprehensive wealth estimates\(^{211}\) suggest that between 1995 and 2014, the positive change in agricultural land value has been paired with a negative change in forest land value (Figure 96). In other words, the country has been switching forest land with cropland. This contrasts with the results of Uruguay and Chile, which have managed to increase the value of both types of capitals over the same period. In physical terms, Argentina is losing its forest land at a faster pace than its peers: between 1990 and 2014 the country lost 21 percent of its forests (See Figure 6).\(^{212}\) Loss of forest results in the loss of biodiversity and key ecosystem services such as carbon sequestration, water provision and regulation, and pollination, which are crucial in sustaining food production, protection against floods and livelihoods. A recent estimate of the cost of ecosystem services due to land use cover change between 2001 and 2009, indicates that the cost ascends to US$80 billion, representing 15 percent of the country’s GDP.\(^{213}\)

**Figure 96. Average annual forest vs. cropland and pastureland capital growth, 1995-2014**

\[\text{Source: Estimated based on Lange et al., (2018).}\]

162. Deforestation and poverty are related phenomena, and even if a clear causality cannot be established, it is not possible to address one issue without taking the other into account. There is a positive correlation between the share of tree cover and unmet needs and between area of tree cover loss and unmet needs.\(^{214}\) Moreover, a comparison of 2010 census-based unmet needs data and tree cover loss between 1992 and 2015 shows that deforestation took place mainly in areas with high poverty rates and that the


\(^{212}\) In absolute terms as Argentina’s deforestation has been second only to Brazil’s in the LAC region.


\(^{214}\) Correlation coefficient between tree cover and unmet needs: 0.544 (p=0.000); Correlation coefficient between tree cover and unmet needs: 0.351 (p=0.000).
provinces with the highest share of rural poverty have also the highest deforestation (Figure 97). Data also shows that provinces with a high poverty reduction between 2001 and 2010 had predominantly high deforestation rates too. Agricultural expansion into marginal lands has also been accompanied by displacements of some of the most vulnerable people and forest dependent communities (e.g. indigenous and criollo in the Northern provinces) who lack secure land tenure. The fact that poverty reduction may be associated with forest loss in the short term is troubling as forest services may be important to sustain livelihoods over the longer term. But a true counterfactual does not exist. In fact, it is possible that controlling forest loss through sustainable forest management and providing better access to markets to forest dependent communities can contribute to poverty reduction. The government’s efforts to provide access to the Forest Fund to poor communities, even without perfect land tenure, is a step in the direction of better inclusion.

Figure 97. Forest cover, forest loss (1992-2015), and poverty by province (2010)

Source: Data from the World Bank’s HDD and INDEC (2010).

163. Inadequate land use practices, including deforestation, may increase the risk of flood occurrence, which in turn affects the poor the most. The world’s second largest reinsurer in the world Swiss-Re, ranks Argentina among the ten emerging economies with the highest flood hazard exposure. This exposure translates into significant losses: over the past two decades, estimated losses due to floods exceeded US$3 billion per year, equivalent to 0.7 percent of GDP in 2012. Some of the most severe impacts are felt in the agriculture and livestock sector, particularly in the Central and the Northern provinces: in 2017 about 20 percent of agricultural land and 80 percent of land dedicated to cattle ranching was affected by floods in the provinces of Buenos Aires, Córdoba, Santa Fe, La Pampa and Entre Ríos. In the province of Buenos Aires, between 2000 and 2011 floods caused nearly $4.5 billion in losses and affected 5.5 million people, with a particularly negative impact on poverty alleviation, economic development, and transit connectivity. The impact on poverty is large because poor people are exposed to hazards more often as

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215 The World Bank (2016). Argentina Country Environmental Analysis. Note that there are also areas in which there is high poverty prevalence and minimal deforestation, e.g. in the western part of the Northwest of Argentina, which confirms the complexity of the forest and poverty relationship.


they tend to live in high-risk areas, live in low quality houses that suffer more damage in case of flood, and lose more as a share of their assets when hit.\textsuperscript{218} In fact, this type of disasters can push people into poverty. The literature points to the effect of soybean monocrop on flooding.\textsuperscript{219} Moreover, deforestation and the replacement of perennial pastures for annual crops, combined with poor watershed and wetland management, reduces groundwater infiltration—though it may at the same time reduce evapotranspiration—increases erosion and run-off, usually increasing the risk of flooding in the presence of extreme weather events that are expected to become more frequent with climate change (see climate change subsection).\textsuperscript{220} As deforestation tends to occur in the upper watersheds of the main river basins, the water regulation capacity of ecosystems are affected and water run-off accumulates further downstream in higher volumes and at a faster pace, often creating floods. Data for Argentina is scant and no correlation can be established between deforestation and flood risk. However, a visual comparison between the spatial distribution of deforestation and flooding events suggests that higher riverine floods occur in regions where deforestation is higher.\textsuperscript{221} More detailed studies are needed to better assess the impacts of deforestation on flooding in Argentina and identify areas that might become vulnerable to flooding in the future as a result of land use changes.\textsuperscript{222}

164. **While the country has set a promising land use planning instrument, its implementation faces challenges.** In 2007, the Minimum Standard Natural Forest Protection Law (\textit{Ley de Presupuestos Mínimos de Protección Ambiental de los Bosques Nativos, 2007}) was setup to combat deforestation. This Law constitutes a federal compensation scheme in which provinces receive payment for protecting forest through territorial planning and enforcement. It established an innovative framework to control deforestation, promote land use zoning, implement sustainable forest management and strengthen collaboration between the national and provincial forest administrations. A Forest Fund was established to transfer public resources to provinces to promote sustainable use of forests and provide payment for environmental services. To date, all provinces have implemented land-use zoning but, although deforestation rates have decreased in recent years, forest loss remains high and about half of it is illegal. In addition, deforestation persists in areas zoned for conservation, often because clearing permits are granted in non-transparent ways. Law enforcement, which is largely the responsibility of provinces, however faces weaknesses: stronger control capacity and penalties for illegal deforestation, and transparency in the way that permits are granted need to be established. Enforcing the Forest Law also requires sufficient resources, as resources allocated for implementation and monitoring have been less that what is stipulated in the Law. In addition, a more efficient management of the Forest Fund, with broader access to different type of stakeholders, including small holders; and close coordination between national, provincial and local level stakeholders is required.

165. **Agriculture is also depleting its very resource base: soils.** Degradation of the Earth’s land surface through human activities is a systematic phenomenon that affects well-being of millions of people all over the world by exacerbating food and water insecurity, and the effects of climate change in the long run\textsuperscript{223}. In Argentina 75 percent of soils are characterized as arid and semi-arid, with high risk exposure to


\textsuperscript{219} See for example Nosetto et al (2012).


\textsuperscript{221} The World Bank (2016). Argentina Country Environmental Analysis.

\textsuperscript{222} In a study for Malaysia, Tan-Soo et al (2016) stress the importance of using disaggregated land-use data, controlling for potentially confounding factors, and applying appropriate estimators in econometric studies on forest ecosystem services. Their results do show that the conversion of inland tropical forests to oil palm and rubber plantations significantly increased the number of days flooded during the wettest months of the year.

\textsuperscript{223} Ibpes (2018). Summary for policymakers of the thematic assessment of land degradation and restoration
ARGENTINA Systematic Country Diagnostic

desertification processes, and soils are already highly compromised, as 81 percent of soils are considered degraded, and 40 percent affected by erosion. This represents a direct threat to maintaining high yields in the future and is already imposing significant costs to the economy. For instance, work on the economics of land degradation estimated that cost of land degradation on grazing land on milk and meat production was in 2007 about 11 percent of the livestock GDP.

166. Naturally-rich fish resources have declined through overfishing. Fish stocks have suffered from overexploitation due to the lack of a national management plan for sustainable and responsible fishing with a long-term vision. A proxy for weak marine resources management is the amount of marine protected areas (as a percentage of territorial waters; Figure 98). Argentina, with just under 9 percent has accumulated a delay compared to other countries in the region, such as Brazil (20 percent), Mexico (19 percent), Colombia (17 percent) and Venezuela (17 percent). Maximum allowable fish catch systematically exceeded levels of acceptable biological catch. There is a lack of monitoring and control systems; and an absence of selective fishing devices to avoid capture of juvenal fish. Patagonian hake (Merluza común) is the main species exploited and stocks were in crisis between 1986 and 2011, when the country lost about 60 to 80 percent of this resource. As a result, captured volumes have decreased in recent years, in part due to fishing restrictions that were set to address overexploitation and illegal fishing. Argentinian shortfin squid (calamari illex) and shrimp have now become important products that contribute large volumes to fish landings, and given the crisis in Patagonian hake stocks, some fishing firms have replaced this species by calamari and shrimp. In 2017, shrimp capture increased by 30 percent in relation to 2016.

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228 Ibid.
167. **Reversing natural resource depletion trends will require a combination of enforcement, incentives and institutional coordination between the national government and the provinces.** As noted earlier, renewable natural capital, including soils, forests, protected areas and fisheries can be an important engine of growth. But degradation is taking place at a fast rate. To reverse this situation, enforcement is key, particularly by the provinces, which hold control over natural resources management decisions. To foster collaboration between the national government and the provinces, it will be key to further develop information systems that are able to track performance on land use change, forest degradation and fishery management. Such information systems can be used in turn to feed performance-based systems for the channeling of resources, such as the ones in the national Forest Fund. A stronger information base on natural resource management will also be key to improve private sector decision making.

The role of policies, investments and markets

168. **Harnessing natural capital for growth requires appropriate policies and incentives.** The fiscal regime has been important in determining the fate of the nature-based sector. For example, Argentina’s agriculture sector has suffered from extractive rent policies (especially exchange restrictions, and taxes and quotas on agricultural exports) that reduced profitability and undermined incentives to invest in the sector. The results of these adverse policies were pronounced: despite a boom in global commodity prices, investment in the sector fell dramatically, and productivity growth slowed. From 2002 to 2013, the average productivity growth in Paraguay, Brazil and Uruguay was 30 percent higher than in Argentina, and in 2013 Food and Agriculture Organization’s (FAO) Agriculture Production Index was between 20 percent and 30 percent higher in these countries than in Argentina. Extractive rent policies affected particularly the beef and wheat production, which led to increases in the prices of beef and wheat-based products. Economic policies should also be climate-smart and help reduce vulnerability to weather-related risks. Climate change will likely pose important challenges to agriculture, particularly in the central part of the country, as it will increase water variability affecting flood intensity and water availability for agricultural production.

169. **Policies and institutions can also be used to encourage the sustainable management of natural capital by reducing the scope for free-riding.** The trade in forestry products is a case in point. While well-regulated cross-provincial trade in timber would benefit the country as a whole, each province may realize a gain by encouraging its own exports of timber. Provincial forest administration and control systems have

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**Figure 98. Marine protected areas as percent of territorial waters (1990, 2000, 2014)**

![Figure 98](image)

*Source: Data from the World Bank’s WDI dataset.*
evolved autonomously, resulting in great differences between forest management and timber transport regulations, creating the condition for the illegal harvest of timber and lost opportunities for the formal economy. If appropriately implemented, the Forest Law (Ley de Presupuestos Mínimos de Protección Ambiental de los Bosques Nativos, 2007) can unlock opportunities in Argentina’s forestry sector. A key line of action is the effective targeting of economic incentives. The Forest Law establishes a Forest Fund that is meant to provide incentives for provinces, firms and land users to adopt sustainable forestry practices. Translating the Forest Law into action requires broadening access to Forest Fund resources as well as close coordination between national, provincial and local level stakeholders to improve Fund performance.  

170. **Policies to deal with open access are crucial in the fisheries sector as well.** A more sustainable fishing model must be adopted. It is recommended that Argentina manages fisheries under an ecosystem based framework, as an integrated management strategy that takes into account all the components of the ecosystems and aims to align social and economic needs with the preservation of ecosystems. The first step in this direction would be to develop a national policy of sustainable fisheries management. In addition, the development and implementation of a legal framework for the sector is essential. It is also key that estimates of biological acceptable captures from the National Institute for Fisheries Research and Development (INDEP) are adopted by the National Fisheries Council (CNP), when setting maximum catch allowances, and to invest in fisheries research to be able to design and manage fish resources based on accurate information. Finally, the promotion of certifications can generate incentives to adopt sustainable fishing practices.

171. **In addition to good policies, harnessing natural capital for growth requires investment.** Traditional investments in produced and human capital, and the management of natural capital can go hand in hand. Figure 99 shows that countries that invest more in infrastructure tend (with some exceptions) to also invest more in the value of natural capital. The same relation holds between human capital and natural capital. This is a key element of the growth narrative in resource rich countries: to put natural capital to work, it is necessary to invest in access to markets, irrigation, technology and transport, among others. An example of this is agriculture. In addition to its favorable climatic conditions, Argentina has become a leader in technological development and adoption for the agricultural sector. This has resulted in both the intensification of production and expansion of the agricultural frontier, mainly driven by the expansion of genetically modified soybean crops in no tillage systems. Yet, Argentina has probably lagged behind in its true potential owing to the low level of investment. For example, the sector faces high transport and logistics costs (which account for approximately 35 percent of the Free on Board (FOB) price of a ton of soy).

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230 The recent Government of Argentina decision to remove restrictions requiring formal tenure to access Forest Fund resources has generated an opportunity to increase the share of fund resources flowing to poor communities (particularly indigenous and campesino) who were previously excluded due to their unclear tenure status.


232 Today Argentina produces 17 percent of world soybean and is the third major producer after the United States and Brazil.
172. Investments, public and private, can be crucial in boosting productivity in sectors that rely on natural capital goods and services. For example, Argentina could harness its soil and water abundance into a more sophisticated and sustainable agricultural sector. New Zealand is one of the countries that followed a growth strategy led by agricultural exports. New Zealand’s agriculture today is the most deregulated in the world and Government support is provided mainly through expenditures on general services such as agricultural research and biosecurity controls for pests and diseases. 233 Many initiatives in support of private sector investments in the sector have taken place over the years. The Primary Growth Partnership was launched in 2009 as a government-industry initiative to invest in significant programs of research and innovation. The Community Irrigation Fund was established in 2007 to assist rural communities in difficulty to address the water supply risks as part of New Zealand’s sustainability and climate change initiatives. Another example of the role of investments, particularly private, relates to the country’s renewable energy potential. The high dependency of the wholesale power market and electricity concessions on government transfers has increased the risk perception of investing in the sector. To address these barriers, the country has issued and is implementing the renewable energy Law 27,191 (year 2015), which has set ambitious mandatory renewable energy targets of 20 percent of overall electricity consumption by the end of 2025 and has mandated the creation of a Fund aimed at injecting funding and offering guarantees for renewable energy projects. The Ministry of Energy and Mining established the RenovAr program, releasing renewable energy Power Purchase Agreement (PPA) tenders, and developed a fund (FODER) designed to cover ongoing PPA payments (i.e. liquidity support), and payment obligations emerging from a “put option”. 234 Moreover, since 2017 large energy consumers are allowed to sign power purchase agreements (PPAs) directly with renewable energy producers. The Executive Resolution “Resolución 281-E/2017 on the Régimen del Mercado a Término de Energía Eléctrica de Fuentes Renovables” has built on the framework laid out by the Renewable Energy law 27191. In addition, the recently approved Law 27,424 for distributed generation allows consumers to produce their own electricity, and inject it back into the grid. The main challenge ahead is to maintain the momentum in the industry, while making sure the high quantity of ongoing tendering processes

233 OECD (2011).
and projects in the first stages of implementation get to financial closure, and are commissioned by the expected deadlines.

173. **Moreover, investments in restoration will be key to generate production, reverse trends in land degradation, but also to diminish the need for infrastructure.** Short-term gains from unsustainable land management practices often result in long-term losses, making the initial avoidance of land degradation an optimal and cost-effective strategy. Estimates show that the returns to taking action to stop land degradation and restore degraded land in Argentina is at least four times higher than the cost of action. Restoration efforts may help meet increasing demand for livestock and agricultural products and would simultaneously provide options to diversify farmer income, sequester carbon for improved soil health, and reduce soil erosion and desertification processes. The recently launched National Program to Restore Degraded Native Forests constitutes a move in the right direction to address degradation and its implementation will be key. Its implementation will require technical knowledge, extension services, incentives, and support land-owners to help overcome upfront costs. In addition, critical information and adequate baseline data on the state of soils is needed to further understand the magnitude of the issue, and to implement effective monitoring strategies and verification systems along value chains. These would allow consumers throughout supply chains to make better-informed commodity choices that reward responsible management practices.

174. **Finally, growth based on the principle of sustainable management of resources can be a great source of opportunity in global value chains.** An analysis of global value chains in Uruguay, which might also provide interesting insights for Argentina given the similar resource and comparative advantage patterns of the two neighbors, finds that there are important growth prospects and attractive price margins in the niches of sustainable beef, non-genetically modified (non-GMO) soy, and organic milk powder. Argentina could also gain by strengthening its international offer of adventure tourism and ecotourism, and explore the potential for exporting knowledge-based services (KBS), biotech and e-commerce services (all areas with low environmental footprint and in which Argentina has a competitive edge). Argentina’s private sector has already used sustainable practices as a key driver of trade competitiveness in sectors such as horticulture and wine making, among others. The public sector however has not kept pace and initiatives by the Ministry of Agriculture and the Secretary of Commerce have been narrowly focused. Going forward, it is important to develop environmental information data that would allow backing up the green attributes of export products (e.g. organic, ecological, bio, FAIRTRADE). Besides, developing niche markets on differentiated products may present new opportunities for regional economies and family farming.

**Pursuing climate smart growth**

175. **Across most of Argentina, average temperatures have shown an upward trend since the beginning of the last century, with an increase in the number of extremes and occurrences of heat waves during the most recent decades.** There has been a remarkable increase in precipitation over most of subtropical Argentina, especially since 1960. Although the climatic changes have favored agriculture yields in the last decades and the extension of crop lands into semiarid regions, it also induced desertification processes in productive areas and produced frequent heavy rainfalls and consequent flooding of rural and urban areas. In addition, glaciers in the Andean region have continued to recede and reduce river flows.

236 Bouza et al. (2016).
238 While here the focus is on agriculture, Argentina is also rich in tourist assets that are likely under-utilized. At its current stage of development, the tourism sector is expected to grow at 2.5 percent per annum, which is significantly lower than the forecasted global average growth, at 3.9 percent (World Travel and Tourism Council Report, 2017).
Climate impacts for the first half of this century might be dealt with timely adaptation policies in key sectors including agriculture, water, energy, and health. However, by the end of this century, under an extreme greenhouse gases (GHG) emissions and business-as-usual scenarios, the projected warming could reach an average change of about 3.5°C in the north of the country, relative to present-day conditions. Recurrent droughts and floods in the most productive areas of the country, will produce important social, economic and environmental impacts that will require strong policy shifts to satisfy household, industrial, and environmental water competing needs to ensure and sustain resilient growth.

176. **Argentina lags in terms of adaptation readiness.** Although Argentina is less vulnerable to climate change than most countries (it is ranked 40th out of 181 countries in terms of vulnerability)\(^{239,240}\) and it ranks similarly to its peers, the country is less ready than most of its peers to make effective use of investments for adaptation actions thanks to a safe and efficient business environment (Figure 100).\(^{241}\) In addition, Argentina’s performance to reduce vulnerability and increase readiness to deal with climate hazards has been worse than its peers’: for example, as Figure 101 shows, on the vertical axis, the vulnerability component related to the ability of society to reduce potential damage and to respond to negative consequences of climate events has improved (i.e. decreased) in recent years, but it has done it less rapidly than most of its regional peers; and when it comes to improve readiness, the country has not been able to improve its capacity to make effective use of adaptation at the pace its regional peers have (Figure 101).\(^{242}\)

**Figure 100.** Matrix of vulnerability to climate change risks and readiness to act, 2016

**Figure 101.** Matrix of capacity to act against climate risks and the economic readiness to accept investments for implementation. evolution between 1995-2014

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\(^{239}\) University of Notre Dame, 2018, *Notre Dame Global Adaptation Initiative (ND-GAIN)*, Online at [https://gain.nd.edu/](https://gain.nd.edu/)

\(^{240}\) Vulnerability measures the propensity to be negatively impacted by climate hazards and it depends on: exposure to hazards; sensitivity to hazards, and adaptive capacity.

\(^{241}\) The readiness indicator includes the investment climate, political stability, control of corruption, rule of law, regulatory quality, social inequality, ICT infrastructure, education, and innovation.

\(^{242}\) The adaptive capacity indicator includes: medical staff per 1000 people; access to improved sanitation facilities; protected biomes; engagement in international environmental conventions; quality of trade and transport infrastructure; percentage of paved roads; electricity access; and disaster preparedness.
177. Argentina has defined a target in terms of GHG emissions reduction and a set of adaptation needs that would allow it to contribute to combating climate change and its impacts. Through its NDCs and under the Paris Agreement, Argentina has committed not to exceed a net emission level of 483 million tons of (CO2 equivalent) by 2030. This is an ambitious target. It ought to be delivered with a series of economic targets focused on both adaptation and mitigation actions. These actions include roadmaps for the enhancement of renewable energy; climate smart agriculture; sustainable forest management; low carbon transport and waste management. Moreover, Argentina has reaffirmed the commitment to the 2030 Agenda for Sustainable Development which includes climate change. The targets can be achieved through substantial efforts from all sectors of society, but this will not be enough. Adequate integration of climate smart policies and means of implementation will need to be designed and followed through. Currently, Argentina has not costed out the actions needed to meet GHG emissions reduction commitments, nor the large set of adaptation measures that need to be implemented. Climate finance remains a key challenge for the country.

178. The ability of the country to sustain low carbon and resilient growth will need the removal of several binding constraints and alignment of national climate strategies and international commitments. First, it is important to encourage smart planning through access to climate research and information, awareness and early warning systems (EWS). The need for timely and accessible information on climate risks and impacts can transform the way vulnerable sectors do climate smart development planning. For example, access to short and medium forecast can allow small and medium size farms to take full advantage of years with favorable conditions for rain fed crop production and reduce risks in less favorable ones. Second, as Argentina fills its infrastructure quality gap, it will need to comply with low-carbon and resilience standards. If the right investment choices are not made today, the country will be locking into high-carbon infrastructure for the next 40 to 70 years. The public sector will have to take a leading role – but private sector solution providers will also have to step up to the plate. Third, managing risks through contingency planning, financial and risk sharing instruments will be needed to improve the ability of vulnerable populations to hedge impacts from recurrent risks and economic impacts. For example, agricultural insurance is limited or not accessible to medium and small farmers—although efforts to expand coverage are ongoing. Finally, there is important scope for integrating adaptation and mitigation agendas. The integration and coordination of existent climate change policies for both adaptation and mitigation in key sectors (energy, agriculture, AFOLU, transport, industry and waste) is a unique opportunity to accelerate both resilient and low carbon growth development in the country.

Managing pollution and the diseconomies of growth

179. Environmental degradation from pollution and waste has direct impacts on the economy due to health costs and loss of productivity. Most Argentineans live in urban areas and urbanization processes have created environmental externalities such as air and water pollution, and have led to unsanitary waste disposal practices. Without adequate management, pollution can off-set the economic gains from agglomeration. Air pollution, poor wastewater and waste management are an important threat to human health. According to the Lancet Commission on Pollution and Health, 8.4 percent of all deaths in Argentina in 2015 were caused by pollution in air, water and soil. While this is below the average for lower than upper-middle income countries (10.3 percent), it is higher than the average for high income countries (7.3 percent). The cost of air pollution on society was estimated at about 1.8 percent of GDP and annual costs from health effects related to inadequate household water, sanitation and hygiene in 0.4 percent of GDP in 2012. In rural areas the exploitation of mineral resources imposes important trade-offs: while it can

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243 It is important to note that the country is still missing an effective energy efficiency policy, that should complement the renewable energy policy currently under implementation.


contribute to GDP growth and generate important revenues, it carries risk and imposes environmental and social negative impacts.

180. **Poor air quality prevails in urban areas impacts on the population, especially the most vulnerable groups.** In 2015, 97.3 percent of Argentineans where exposed the levels of PM2.5 that exceeded the World Health Organization (WHO) guideline values, similar to exposure rates in structural peers (98.1), and higher than the in regional (79.8 percent) and in OECD countries (65.8 percent)\(^{246}\). In addition, modeling estimates from the CEA (World Bank, 2016a) indicate that air pollution in the main urban agglomerations is far above the WHO recommended thresholds, that Buenos Aires exceeds the levels of pollution of other cities by significant amounts, and that despite slight decreases in air pollution in large cities and acceptable levels in small cities, it is expected that increasing urban population and traffic will contribute to higher levels of pollution in the future.\(^{247}\) Today, Ischemic heart disease, lower respiratory infections and chronic obstructive pulmonary disease are among the four main causes of death in Argentina,\(^{248}\) and are all linked to poor air quality.\(^{249}\) The share of deaths caused by lower respiratory tract infection has increased by 25 percent between 2005 and 2016,\(^{250}\) by 11.6 percent in the case of COPD, and by 7 percent in the case of ischemic heart disease. Distributional impacts of air pollution are biased toward the poor, who tend to be more exposed to air pollution and are less aware of the possible negative consequences. Poor health due to air pollution impacts people’s productivity and their ability to work.\(^{251}\) For children, reduced productivity translates into educational underperformance, with long-term negative effects for economic performance\(^{252}\) and poverty alleviation. While information on air quality in Argentina remains limited, the available evidence points to increased use of vehicles and traffic congestions being the main sources of urban air pollution.

181. **Water pollution from domestic activities, industry and agriculture is increasing in many watersheds degrading the main source for water consumption.** Surface water is the main source of water for consumption and is vulnerable to pollution from discharges of untreated wastewater and/or domestic activities, industrial effluents or agricultural run-offs. There are 16.7 million people, or 42 percent of the urban population who do not have access to wastewater systems, and only 65 percent of municipal waste water is collected and only 12 percent is treated before disposal. Treatment levels for fecal effluents is less than 20 percent nationally, posing a clear health risk to people living nearby contaminated waters. Given that many regions of the country report high levels of arsenic in groundwater, increasing pollution of surface water is of particular concern. Although significant investments in wastewater infrastructure are being made by central and provincial governments, the WSS sector faces substantial sustainability challenges that can put these investments at risk.

182. **Pollution from increased use in agrochemicals is also a source of concern.** The shift toward industrial agriculture came with an increase in the use of fertilizers and herbicides, especially glyphosate,
and the use of agrochemicals rose by 1000 percent in the last 20 years.\textsuperscript{253} The use of glyphosate and other herbicides have carried important economic benefits especially through the promotion of zero-tillage agriculture, allowing to exploit Argentina’s comparative advantage for soybean production and establish its role in the modern global economy.\textsuperscript{254} However, glyphosate is classified as probably carcinogenic to humans and high concentrations of this agrochemical have been found in the Parana basin.\textsuperscript{255,256} Case-studies are increasingly warning about severe harmful effects of glyphosate on human health and the environment, Further investigation is required to assess the trade-offs of associated with GMO crops that heavily rely on agrochemicals.

183. To address pollution, improving information systems, strengthening monitoring capacities, stronger management and implementing target policies to the most pollutant sectors are key. In the case of water, current management of water resources is not grounded on good quality information about resource availability and use. This hinders the development of policies and planning instruments to manage water resources, address conflicts among users, protect the environment from pollution and reduce vulnerability to extreme weather events. In addition, lack of data hinders the capacity of regulators to monitor utilities’ performance and charge adequate tariffs for water use and water discharges. Stronger management, by means of building capacity in institutions, improving regulations is also key. There is also lack of air quality information. To address local air pollution, Argentinian cities can learn from other Latin American cities, that in the past two decades have begun to deal more seriously with this issue. They have strengthened their environmental institutions and upgraded their environmental measurement and monitoring systems, and they have imposed environmental standards to vehicles, fuel quality and industries. The recent launch of the Red Federal de Monitoreo Ambiental (Red FEMA), a data management system that aims to produce periodic and systematic information to facilitate monitoring of air, water, and soil quality at the province level is a move in the right direction that needs continuity to ensure that that all the provinces joined the system and use the information for decision making.

184. Inefficiencies in solid waste management directly affect citizen’s quality of life and livability in cities. An uncleanly and disordered environment affects health, livability, property values, attractiveness for business and tourism, and sense of security. The inclusion chapter described how many Argentineans still lack access to regular collection services and open dumps remain the most common mode of disposal. In addition, landfill organic waste (about 50 percent of total waste produced) is an important source of vector-borne disease and a significant cause of GHG emission.\textsuperscript{257} In addition, reuse and recycle rates are low with only 11 percent of total waste being recycled (vs. 46 percent in OECD countries) and most of the material is estimated to be recovered by mostly informal waste pickers (cartoneros).\textsuperscript{258} In CABA, despite having set up a “Zero Waste” plan that aims to reduce the amount of recyclable materials that is being sent to landfills by 2020,\textsuperscript{259} the ambitious target is still far from being met. However, there are important opportunities to reduce impacts of inefficient waste management and reduce GHG emissions: facilities that collect and

\textsuperscript{253} Data from FAO. FAOSTAT Database. Retrieved from Food and Agriculture Organization of the United Nations: http://www.fao.org/faostat/en/#data
\textsuperscript{258} Bioenergy consult (2018). Available at: https://www.bioenergyconsult.com/tag/argentina/
\textsuperscript{259} Ley 1854 Gestión Integral de Residuos Sólidos.
combust methane from landfills already exist in several landfills in the country and recycling and composting programs exist in many part of the country; increasing their capacity and increasing separation of waste at the source remain main challenges.

185. **Accelerating a transition toward a circular economy would enable a more efficient use of resources and improve livability, but this transition needs coordinated actions.** Solid waste management has followed an inefficient lineal model with low reuse and recycling rates that if improved could result in significant savings, social opportunities and environment benefits. MAyDS is currently promoting a circular approach for integral waste management, with the National Plan for Circular Economy, that set the guidelines for “Provincial Strategic Plans of Waste Management toward a Circular Economy”, an instrument that provinces must develop, with the participation of municipalities, to identify guidelines, actions and policies needed to improve waste management at the province level with a circular economy approach. The development of this plans is a step in the right direction to pursue a circular model in which the value of products and materials is maintained for as long as possible and waste and resource use are minimized, and which is expected to reduce the long-term costs related to dependence on landfills; provide substantial net materials savings, provide opportunities for innovation; and contribute to job creation.

186. **A key element to achieve environmental sustainability is to identify and assess the risks and impacts associated with investments and policies.** This is the role of Environmental Impact Assessment (EIA), when it comes to projects, and Strategic Environmental Assessment (SEA), when it comes to policies and programs. While the federal environmental framework requires that the relevant authorities (provinces and sectors) conduct EIAs for projects with significant impacts, there are no regulations at the federal level that establish minimum requirements for the use of this instrument across all provinces and sectors. Compared to international best practice, shortcomings include (i) lack of standardized criteria to evaluate risks and impacts; (ii) a lack of adequate screening to identify the projects that should be subject to EIA; (iii) limited public participation; and (iv) weak monitoring to ensure that the mitigation measures proposed by the EIA are implemented. As a result, EIAs have largely been used as procedural permitting tools to allow major projects to move forward, rather than as tools to guide project design through impact assessment and stakeholder buy-in. This needs to be fixed. It does not only pose a risk to the environment, but it also poses a risk to growth, as non-compliant projects can be attacked and eventually stopped by public outcry. Oil and gas developments, if not well managed from an environmental standpoint, can pose risks to the investments in the sector (Box 9). Minimum standards need to be established and capacities to enforce regulation at the provincial level need to be strengthened.

**Box 9. Oil and Gas, and environmental compliance**

*The current administration is focusing on rebuilding Argentina’s energy industry and seeks to capitalize on the nation’s enormous unconventional oil and gas potential.* So far, the government has made progress in amending the complex system of domestic oil tariffs and subsidies introduced by the previous administration. Local price distortions led to considerable underinvestment in the energy industry, which turned the country into a net energy importer despite its tremendous unconventional oil and gas resources. The rewards are large, considering that Argentina’s technically recoverable shale oil reserves come to 27 billion barrels, which is 60 percent of the country’s technically recoverable crude. The Vaca Muerta formation is ranked by the U.S. EIA as the second-largest unconventional oil and gas reserves globally. Argentina’s national (and largest) energy company YPF has committed to investing US$30 billion over the next five years to exploit the potential of Vaca Muerta. The company will attempt

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260 MAyDS. Plan Estratégico Provincial PEP para la gestión integral de residuos sólidos urbanos hacia una economía circular.

to match the U.S. shale oil and gas boom. Since YPF lacks its own expertise, capital and workforce, foreign investments are particularly important if Argentina is to realize its full energy potential.

These massive investments, if realized, must avoid undue harm to livelihoods and the environment. This is an area that is still full of unknowns. In fact, there are concerns that fracking may contaminate drinking water supplies with harmful chemicals, raising public health issues. Fracking may change local geology in a substantial way, leading to earthquakes. Moreover, fracking can be characterized by methane (a potent GHG) leakage, reversing one of the potential advantages of gas over ‘dirtier’ fuels, such as coal. More effective governance of social and environmental issues in unconventional oil and gas developments is needed. Some of the main challenges associated with new developments include, water use and management; surface planning to minimize disruption of other local productive activities; public disclosure of chemicals; air emissions and GHG from flaring and venting. Government must improve the coordination of the issuance of regulations and actions taken by energy and environmental authorities, particularly between federal and provincial levels. For example: (i) minimizing potentially negative environmental and social impacts of oil and gas operations on regional economies; (ii) harmonizing environmental regulations; (iii) planning infrastructure expansion; (iv) increasing local content of supply and services. Communities must have the proper engagement by new unconventional hydrocarbon developments.
Chapter 5. Priorities for a sustained and inclusive growth

187. The main objective of this study is to identify what are for Argentina the most critical factors constraining or driving growth, inclusiveness and sustainability. These constraints emerge from the analysis presented in the previous sections, based on recent evidence and studies carried out by the World Bank and other national and international institutions as well as the academic literature. In this chapter, the constraints are listed, and further distilled with the help of a prioritization exercise. This section also highlights areas where there are data and knowledge gaps (See Annex III).

Prioritizing reforms for shared prosperity

188. A prioritization and sequencing of reforms is critical given the broad reform agenda that Argentina faces. The country has embarked on the transition to become a more globally integrated, competitive economy. Such a shift implies a large reallocation of factors of production away from non-tradable, low-productivity sectors into more dynamic tradable sectors, which necessarily entails winners and losers in the short to medium term. The transition occurs when the Government is also tackling persistent macroeconomic imbalances and significant currency turmoil that make the country vulnerable to external shocks and domestic tensions. In this context, a careful design in terms of setting priorities and sequencing is key, as is putting in place social policies and sectoral plans to mitigate the adverse impacts of the economic reform program. Current Government policies are consistent with this approach, which not only protects the vulnerable, but increases the probability of a lasting social consensus developing in support of the reform program.

189. Argentina can take the lessons from its previous reform episodes. Many past reform efforts underestimated the importance of a proper sequencing, necessary complementary policies and/or the social costs of the transition. Without broad-based support and appropriate safeguards for the vulnerable, for example, the reform process might stall, and could even be reverted. The proposed reforms can, however, face a different fate than previous efforts in that they seek to put a comprehensive package of policies in place to tackle at the same time growth challenges, inclusion concerns, and the potentially large scope for productivity improvements and natural capital-based growth.

190. Moving along the reform path will not be easy. The forces that caused political and economic volatility in the past still linger and are likely to influence the future. Just as this report was about to be completed, high devaluation pressures forced Argentina’s government to increase its focus on short-term macroeconomic stabilization priorities. Important reforms cannot be carried out if certain preconditions haven’t been met. Ensuring macroeconomic stability, for instance, is not only a precondition for other priorities, but its failure can undermine most of the progress achieved across other dimensions.

191. Some of the reforms identified in this chapter are already underway, but there is a risk that the present context will mask the sense of urgency of key structural reforms whose results are seen in the longer term. Continuing with the reform process is crucial, albeit the short-term focus in the country is, rightly so, on dealing with the macro-economic imbalances and the pressing fiscal challenges. Sustaining a long-term commitment to policy reform on behalf of politicians, the private sector and the population at large is challenging given the complexity and extensiveness of the reform agenda. Clearly communicating the gains and longer-term impact can help, as will political dialogue around interventions to minimize social conflict and generate the political capital needed. Over time, results achieved in these areas may serve to build political support and shift incentives.
Prioritization process

192. From the long list of constraints identified throughout the SCD, it was necessary to distinguish those that are the most critical to achieving sustainable and inclusive growth. To prioritize among the constraints to growth and shared prosperity, the report uses the following criteria:

- **Impact on the twin goals:** This filter looks at the potential impact of removing a constraint on reducing poverty and increasing the welfare of the bottom 40 percent.
- **Complementarities:** This filter assesses the degree to which an opportunity identified in one area might have positive impacts on other priority areas. There are strong connections across a number of the challenges and addressing one set of constraints might also trigger or be a condition for progress in other areas.
- **Sequencing:** This filter identified those constraints that need to be tackled before others, in order to achieve sustainable and inclusive growth.

In addition, a number of cross-cutting priorities come out of the analysis as needing to be in place for the reform program to succeed. These cross-cutting institutional factors needed to enable growth emerged out of several of the diagnostics on constraints.

193. The SCD prioritization criteria were applied throughout the prioritization process, which had five elements: (i) a diagnostic of growth, inclusiveness, and sustainability; (ii) an analytical benchmarking exercise combined with country knowledge and SCD filters; (iii) a description of the priority areas identified; (iv) a systematic prioritization exercise to identify opportunities within the priority areas; and (v) a description of the opportunities identified (Figure 102). The consultations resulted in broad agreement on the cross-cutting necessities, and also a number of priority areas albeit, there were some differences in view and approach.

![Figure 102. Prioritization process](image)

Priorities

194. Priorities are organized in two categories, including cross-cutting institutional factors to enable growth and thematic priorities. Cross-cutting enablers are ‘drivers of success’ for the more traditional thematic priorities. Enablers can magnify the effects of other reforms and their impacts on growth, inclusion and sustainability over the long-term. They tend to be institutional in nature. As highlighted in chapter 2, the architecture of Argentina’s political and economic institutions plays a fundamental role as the underling determinant of policy outcomes. Moving toward a sustainable and inclusive development model can therefore be proven difficult without addressing some of the more pressing institutional challenges and governance constraints. The design and successful implementation of policies—in any sector or at any level of government—is, to a large extent, determined by the strength of the institutions and the coordination across levels. This section introduces the set of cross-cutting institutional factors to enable growth, which
have emerged from the analysis and consultation process across most of the areas, and the sector-specific list of priorities identified.

**Cross-cutting institutional factors to enable growth**

195. **Strengthening the independence and efficiency of accountability institutions to ensure law enforcement and reduce corruption.** Transitioning toward a sustainable and inclusive development model will prove difficult without addressing some of the pressing and fundamental institutional challenges and governance constraints, including the need to ensure an impersonal application of rules (from the ‘rule by law’ to the ‘rule of law’). The experience of many countries shows that constitutional constraints become self-reinforcing when power in the system is distributed evenly and powerful elites and the political ‘system’ accept the law’s limitations. 262 For this transition to happen in Argentina, further efforts are needed to ensure better contract enforcement, an independent judiciary, and stronger accountability institutions across all levels of government to be able to prosecute and sanction corrupt behavior. Over the past years, Argentina has made important strides in strengthening accountability and anti-corruption efforts: new or overhauled laws have been passed or are being discussed in the areas of corporate criminal liability, access to information, ethics and integrity, plea bargain and asset recovery; and accountability mechanisms have been strengthened significantly, such as those of the Anti-Corruption Office. In part, the revelations surrounding the cuadernos scandal – which are gaining in force and scale on a daily basis as this report is finalized – are fruits of such strengthened institutions. But this can only be a beginning of the necessary deep-rooted changes.

196. **Supporting decision making based on evidence using high quality data and information systems could contribute to reaching consensus and advance reforms.** Good and comprehensive quality data and information systems are necessary for the diagnosis, design, implementation and monitoring and evaluation of key policy areas. Yet, the challenges in information across sectors are large, and the sharing practices even within different sectors of government can undermine policy making. But in addition, transparency reforms and open data initiatives can also promote rational decision making based on best available evidence. Further efforts are needed to promote the reuse of these data and the dissemination of information to increase public scrutiny. In a context of often politicized debates on where and how allocate scarce public resources, evidence-based policymaking can help bridge the ideological divide and support a rational debate about policy goals and strategic priorities. By centering on expected outcomes and rigorous assessment of the impact of public policies, an evidence-based approach can help government focusing policymaking on effectiveness of social interventions and efficiency in use of resources. This approach can contribute to mitigate polarization among political and economic actors and increase the chances of bipartisan agreement.

197. In addition, Argentina can establish institutionalized spaces for consultation and public deliberation to increase legitimacy of the proposed policy trajectories, and maximize compliance by all stakeholders involved in the reform process. The process whereby policies are adopted and implemented is as much important for success as the specific content of such policies. For this reason, the adoption of important policy and regulatory reforms across sectors should involve the creation of institutionalized spaces where multiple interest groups, business associations, and ordinary citizens can have a bigger say on the content of the proposed reform. The public nature of such spaces will be critical to reduce risks of capture, thereby re-balancing the influence of more powerful interest groups. The recent experience of subsidy reforms suggests that public deliberation and participation mechanisms can also be an effective—and legally enforced—mechanism to overcome polarization and increase support to highly-contested reforms, achieve early wins,

and mitigate adjustment costs. 263 This strategy is particularly relevant for regulations aiming at improving the business environment, as compliance is usually higher as result of the co-participation of various actors in the decision-making process.

198. Making federalism work by promoting cooperative behavior across governmental levels will be central to ensure successful implementation of policies. As indicated above, the need to provide homogeneous services across heterogeneous provinces generates perverse expenditure and revenue collection incentives, resulting in substantial fiscal challenges. Historically, the policy instruments and processes used to negotiate these distributional tensions between the national and provincial governments, (including “participaciones” to provinces, public transfers, pensions, subsidies, and taxation) have proven harmful for Argentina to achieve its long-term development objectives. Moreover, in many cases, the decision-making and implementation are decentralized to a variety of regulatory agencies, without appropriate coordination mechanisms, and thus leads to increased fragmentation and undermines the capacity of the Federal Government to guide implementation. There is therefore an urgent need to make federalism work in Argentina by promoting a more cooperative behavior in which national, state, and local governments interact cooperatively and collectively to solve common problems. To this end, stronger central coordination would assist in making government actions more coherent and aligned with the overall strategic priorities and orientation of the country’s development agenda. Coordination of policies can be improved also promoting reforms (such as those needed in education) that create incentives for subnational governments to improve public spending efficiency and comply with national policy guidelines and regulations, similar to the existing ones used in the health sector (Plan Sumar). While the institutional architecture that defines the nature of fiscal federalism in Argentina is hard to change in the short-term, the ‘fiscal pact’ recently signed on November 2017 by the Federal Government and 23 out of 24 provinces 264 suggests there might be opportunities to introduce incremental improvements in the inter-governmental fiscal transfer system, including the roll-out of federal guidelines on public financial management to better monitor expenditures and promote more efficient allocation of resources. In this sense, incentives could be provided for the provinces in the forms of results-based grant schemes and conditional transfers that reward efficiency in public spending, prudent fiscal management as well as compliance with federal guidelines, policy regulations and jointly agreed reform priorities. The Council of Australian Governments (COAG) may serve as an example for Argentina’s ongoing efforts to institutionalize rules-based forms of coordination and cooperation between the federal government and the provinces (Box 10).

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263 Subsidies to energy and transportation were introduced since 2006 to dampen the impact of rising prices and protect incomes of the poor and reached almost 5 percent of GDP by 2016. Families were paying on average between 15 and 20 percent of the total cost of the subsidized services, with a large proportion of the subsidies going to the middle class and the rich. After two months in office, the new Government announced that energy subsidies were to be phased out gradually until 2019, and a social tariff system was created to protect low-income households. A few months after the announcement, the Supreme Court ruled that the hike in gas prices were illegal and to be postponed until the Government organized public deliberation, as required by the constitution. These were held in September 2016, and the tariff change was passed a month later. Since then, new tariff increases for both piped gas and electricity were preceded by similar public deliberations with active participation of civil society (the last one took place in November 13-17, 2017).

264 The agreement addresses part of the long-lasting fiscal disputes between different levels of government in Argentina. This includes the implementation of fiscal rules, the gradual reduction of distortive taxes at the provincial level, the resolution of lawsuits against the Federal Government, political support to change the pensions indexation formula, and a partial redesign the revenue transfer system to compensate for the historical discrimination of the Province of Buenos Aires. The draft bill is expected to be sent to each sub-national congress for ratification.
Box 10. Setting incentives to promote inter-governmental cooperation: the Australian experience

The Council of Australian Governments (COAG), established in 1992, is the highest level intergovernmental forum in Australia, comprising the Prime Minister (chair), State Premiers, Territory Chief Ministers and the President of the Australian Local Government Association (ALGA). The role of COAG is to initiate, develop and monitor the implementation of policy reforms that are of national significance and which require coordination and cooperative action by Australian governments. Where formal agreements are reached, these may be embodied in intergovernmental agreements, including National Agreements and National Partnership Agreements. COAG has a strong record of driving reforms that have improved the lives of all Australians. For example, the package of economic reform policies linked to national competition policy in the mid-1990s left a legacy of a more competitive, efficient and flexible economy which has enabled Australia to meet key economic challenges in the last 20 years.265

Australia’s National Competition Policy (NCP) linked untied performance grants to states achieving certain regulatory reform objectives intended to promote economic growth. An important feature of the institutional framework was the use financial incentives — in the form of performance-based grants — made by the Australian Government to the States and Territories to ‘return’ the fiscal dividend from their implementation of agreed reform commitments. Prior to the scheduled payment of the transfer in each year, an independent body - the National Competition Council (NCC) - assessed whether each State had met the specified performance targets and provided recommendations for consideration by the Australian Government in terms of rewards or sanctions (reduction of the size of the grant to be transferred). The NCP is recognized as having made a significant contribution to Australia’s welfare, aligning the incentives of central and state government toward meeting jointly-defined reform commitments. The Australian experience also demonstrates that the grants involved need not be large, because the policy was based on an intergovernmental agreement and a mutually accepted settlement scheme rather than imposed from above.

Source: Parker (2009); Commonwealth of Australia (2009).

Thematic priorities

199. Inclusive and sustainable growth will require progress on both equity and productivity fronts, as well as ensuring macroeconomic stability and enhance environmental sustainability. The analysis done as part of the SCD process identified a large set of economic priorities from which twelve have been considered to be core. These priorities have been also assessed in terms of their impact on the twin goals, their complementarity with the rest of the priorities and in terms of their role as essential preconditions to the successful achievement of the remaining priorities. This assessment in presented in Table 7. These have been largely confirmed through the systematic consultation with national and international experts. Thematic priorities are grouped according to the pathways toward inclusive and sustainable growth: (a) putting the macro-economic fundamentals in place, (b) opening the economy, (c) fostering an inclusive economy, (d) investing in natural capital and ensuring environmental sustainability.

200. A proper sequencing of the reforms will be a key element for government actions. While the priorities identified in the table below are fundamental for sustainable and inclusive growth, the sequencing of reforms is essential for success. Macroeconomic instability, as mentioned before, is a basic precondition for the success of the reform effort. It is also undeniable that improving the quality of social spending and investing in human capital are priorities that will see their fruits in the medium and long run, but today’s inaction can prove costly. Within some of the priorities, sequencing of specific measures is also fundamental, as is the case of prioritizing the deepening of domestic competition prior to successfully integrating the country into the global economy. International experience of implementing large structural reforms reveals

substantial potential gains; however, prior experience has also shown that proper sequencing and monitoring are essential to success. Comprehensive reform programs to deepen competition and open-up the economies to trade and investment in Australia, Mexico, and Sweden took a decade or more to put in place. In addition, appropriate interinstitutional coordination, at the federal level and between the national and subnational governments, as well as public-private dialogue, is required to achieve early wins, and consolidate the reform process. Finally, improving infrastructure spending appears as not only a precondition, but also as having strong complementarities with other policies identified.

Table 7. Heat map with filters

<table>
<thead>
<tr>
<th>Priorities (12 highest out of 29)</th>
<th>Impact on twin goals</th>
<th>Complementarities</th>
<th>Sequentiality</th>
</tr>
</thead>
<tbody>
<tr>
<td>Ensure sound macroeconomic management</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Improve fiscal policy for growth and equity</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Improving infrastructure</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Develop and deepen financial and capital markets and household access to credit</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Increase integration into the global economy</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Reduce barriers to competition and lower logistic costs</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Improve the quality and relevance of education</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Increase the efficiency of spending in health and education while ensuring equal quality for all</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Close the gaps in the provision of basic infrastructure services</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Ensure pensions are sustainable</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Harness natural capital endowments through policies and investments.</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Foster climate smart growth for the short and the long-term.</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Note: The number of boxes next to each of priorities reflect the average importance of the priority for each of the filters, as derived from the analysis and confirmed by polling with internal and external stakeholders. □□□□ denotes that the priority is “very important” for the relevant filter; □□□□ denotes that the priority is “important” and that a high proportion of consulted stakeholders confirmed this; and □□□□ denotes that although the priority is “important”, but with a lower proportion of consulted stakeholders considering it so.

201. The prioritization exercise suggests two tiers of priorities. Reforms included in the first tier are of first-order relevance, very important across the three filters. These include a sound macroeconomic management, better infrastructure, improved quality and relevance of education, and increased efficiency of spending. Improved fiscal policy for growth and equity can be pooled in the first-tier group, though with slightly lesser impact on twin goals. A second tier is headed by closing the gap in the provision of basic infrastructure services, important across the three dimensions, and the other priorities that have varying degrees of importance across the three filters.
**First-tier reforms**

202. **These reforms are led by sound macroeconomic management, which is also key in the short-run, given current financial distress.** This reform builds from the diagnosis that macroeconomic mismanagement and frequent economic policy reversals have been a source and outcome of successive boom and bust cycles and welfare swings. In this context macroeconomic stability is a precondition for the actual unfolding of the reform agenda. This is tightly linked to an improved fiscal policy for growth and equity, as a sound macroeconomic management also entails a rebalancing of fiscal policy to reduce economic distortions and have an expenditure and tax policy that better supports growth and equity. Public expenditure needs to move to a sustainable level in relation to economic output. Given the size of current fiscal imbalances, a fiscal consolidation is essential to stabilize public debt. Cuts to subsidies and other inefficient government programs need to continue, while medium to long term the aim should be to increase the share of spending going on growth-enhancing measures, such as priority public investment projects. The tax system needs to be redesigned to reduce the weight of distortionary taxes and to broaden the tax base. This should include a clear definition of expenditure responsibilities across different levels of government and a sound intergovernmental fiscal transfer system to ensure the efficient and equitable provision of public services, and improved subnational revenue-collection incentives.

203. **Enhancing infrastructure is also seen as an objective of first-order importance.** The quality of Argentina's infrastructure stock is deteriorating and this poses a challenge to competitiveness. Infrastructure investment is historically low, with a very low participation of private sector financing, and unlikely to grow much owing to limited fiscal space. Moreover, logistics performance indicators are generally lagging. Good infrastructure and lower logistic costs are key to Argentina's ambitions in terms of growth. While financing is a key bottleneck, more focused national and territorial goals, and efficient strategies can substantially reduce financing needs. In addition, upstream reforms will enable Argentina to both improve spending efficiency and attract private financing on better terms—whether through PPPs or commercial borrowing by public enterprises. Efforts to improve public investment institutions and frameworks—notably budgeting and procurement systems—should enable the country to substantially stretch the resources it already allocates to infrastructure. An improved framework for infrastructure planning, financing and investing will be a key driver of competitiveness.

204. **Two first-tier reforms are related to fostering an inclusive economy: improve the quality and relevance of education, and increased efficiency in the provision of health and education while ensuring equal quality for all.** On the quality and relevance of education, school readiness and early literacy skills are low, despite relative high coverage. A focus on quality will also call for strengthening teacher careers, not only in terms of the training curriculum but also consolidating the network of training institutes, as well as creating the conditions to attract and motivate teachers to perform. Recent reforms establishing annual standardized testing of students’ learning outcomes, enforcing the communication of results to schools, and pre-service teachers’ evaluations should contribute toward focusing the system on quality, although teacher evaluations are still pending. In fact, teachers’ unions resistance to education reforms is generally focused on changes in teachers’ professional development. In addition, it will be essential to revamp secondary education focusing on developing critical basic cognitive and (21st century) soft-skills, in line with Secundaria 2030. With respect to increased efficiency in health and education, completion rates are low, learning outcomes are poor, and health outcomes high and unequal across provinces. Unequal access to quality services and inefficiencies reflect highly fragmented systems with lack of coordination mechanisms across systems and subnational entities. Increasing efficiency will require making policies that are increasingly guided by evidence to help identify cost-savings initiatives, and a solid system of monitoring and evaluation. In health, efficiency could be substantially improved by establishing an appropriate model of care, where: (a) several providers including a main primary care provider work together in an integrated, coordinated manner to provide care for an individual (with integrated information systems), and where: (b) there is an emphasis on actively expanding effective coverage at the primary care level. As a result of these
efforts, the health system would indeed be better placed to strengthen the prevention and control of the burden of non-communicable diseases, especially in the context of an aging population. This also calls for the reduction of common risks factors associated to these diseases, such as unhealthy diets (particularly among children, where obesity is high), physical inactivity and a tobacco use and alcohol abuse

*Second-tier reforms*

205. This group of very relevant reforms with a slightly lower level of priority is led by closing the gap in the provision of basic infrastructure services. Broad disparities in basic services, informal settlements and connective infrastructure across regions and within large agglomerations persist. Access to safely managed water and sanitation services varies significantly across regions and between the core and the peripheries of large cities. There are 4,000 informal settlements in the country. Closing basic infrastructure service gaps, investing in connective infrastructure and strengthening local capacity will be key for the convergence of living standards and for linking populations to economic opportunities. This will require enhancing integrated planning across different sectors, as well as widening the financial options and develop clear mechanisms to set up transparent systems of fiscal transfers across different levels of government.

206. A closely related priority refers to the development and deepening of financial and capital markets and household access to credit, which could be thought of as access to basic financial services. Argentina’s very shallow financial markets reflect a gap in mechanisms that could better support growth, infrastructure, housing, and enterprise development for the private sector. Households have limited access to credit for productive investment and asset accumulation, particularly for the more vulnerable. Poorer people rely on personal loans or credit cards, with high interest rates. Expanding credit and mortgage markets will be essential. The new legal frameworks are encouraging, but substantial regulatory and institutional roll-out measures are needed to ensure that financial and capital market products can operate in an enabling environment and that the government works with the private sector in developing new and innovative instruments to promote long-term finance for productive purposes, and to generate new asset classes of financial instruments that can be more transparently priced and traded.

207. Two reforms directly linked to the open-economy development strategy stand-out for their impact on the twin goals and complementarities: an increased integration into the global economy, and reduced barriers to competition and lower logistic costs. Key trade policy actions include lowering tariffs and NTMs in priority sectors, unilaterally reducing NTMs in input products, removing nonautomatic licenses to increase predictability and boosting regional integration agreements to increase market access. Competition and trade authorities can further coordinate to harmonize technical standards with trade partners. To improve investment policy, Argentina can revise the incentives framework, introduce effective policies to promote linkages with local suppliers, and set up comprehensive regulatory improvement and simplification mechanisms. Jointly among competition and investment promotion authorities, the government can open-up key sectors to investment. On the competition and logistic side, Argentina can continue strengthening its anticartel enforcement, implement the recently overhauled merger control framework, strengthen pro-competition sector regulation in key sectors such as telecommunications and transport, and implement competitive neutrality principles to ensure that public and private operators compete on a level playing field. The competition authority will need to be well resourced, prioritize its engagements and actions, and achieve technical independence.

208. Two priorities on natural capital and environmental sustainability stand out. On one hand, foster climate smart growth for the short and the long-term relate to the climate impacts that are rapidly coming to the fore of Argentine’s lives and economic activities. While appropriate adaptation policies in key sectors including agriculture, water, energy, and health can help deal with impact in the present, a more systemic approach can offer more robust outcomes. By the end of this century, under an extreme emissions
scenario, the projected warming could reach an average change of about 3.5°C in the north of the country, relative to present-day conditions. This will produce important social, economic and environmental impacts that will require strong policy shifts. Priorities to adapt to climate change involve proper costing of climate action; contingency planning; and a closer integration between the mitigation and adaptation agendas.

209. **On the other hand, harness natural capital endowments through policies and investments stresses the need to leverage natural resources for growth in a sustainable way.** Natural capital in Argentina includes agricultural soils and pastures; water; forests; fisheries; strong winds and solar potential; and subsoil assets (oil, gas, coal, and minerals). Some assets, particularly forest ecosystems and fisheries, are under significant pressures. Argentina has lost 21 percent of its forest cover in less than 25 years. At the same time, fish stocks have suffered from overexploitation due to the lack of a national management plan for sustainable and responsible fishing with a long-term vision. Yet, these resources, along with the strong renewable energy potential can be important sources of economic rents, jobs and sustainable livelihoods. Unleashing the potential of natural capital requires breaking-up with the extractive policies of the past and consolidate a policy framework that attracts private sector investments. Policies, incentives and enforcement are also required to ensure that the open access that characterizes many natural assets, such as forests, land and fisheries, does not give way to illegality and degradation. Finally, a more sophisticated demand for greener attributes in global value chains is already emerging and Argentina has much to gain from developing information mechanisms in support of labels and practices that encourage the thriving green businesses throughout the country.

210. **Finally, an item that will become increasingly important as population ages: the need for a social consensus to ensure pensions are sustainable.** Pensions are fundamental for protecting the income of the elderly population, as poverty rates would be substantially higher in the absence of the recent reforms that expanded coverage. Two-thirds of the moratorium goes to the three poorest deciles. But with already 11 percent of GDP going to pensions, the mid-term sustainability is not currently guaranteed given the demographic transition and the current rules. There is a need to consider options that balance the high levels of generosity (which has recently increased with the Reparación Histórica that recalculated and adjusted benefits retroactively and going forward), with the broad coverage while ensuring future sustainability. This is particularly important as the Government is starting discussions on a future pension system reform. In this sense, the December 2017 parametric reform will help make the system more sustainable by changing the pension indexation mechanism to one that ties benefit changes more closely to changes in prices (and up to a minor extent to changes in wages). Nonetheless, in addition it would be desirable to broaden the agenda to revise all the parameters and components of the system, both contributory and non-contributory.

**Box 11. SCD consultation process**

During the SCD preparation, the team carried out broad and intensive consultations both within the World Bank Group as well as with a large number of relevant stakeholders in the country to identify the key challenges and constraints, and crucial analytical pieces that can fit into the analysis. These consultations were carried out jointly between the World Bank and the IFC. Internal consultations in Buenos Aires and DC began during July-August 2017, and included the broader Argentina country team, the LAC Chief Economist office, the Environment Chief Economist Office, the GPs and the Country Management Unit (CMU). These continued throughout the preparation of the SCD, and in the last phase included several country team meetings for the internal prioritization exercise. A list of external participants can be found in Annex V.

External consultations were held in Argentina on several occasions. A first round took place in Buenos Aires during November and early December, with experts, civil society, private sectors and politicians. These discussions were crucial to validate the diagnosis and receive feedback on emerging priorities. Given the SCD’s emphasis on institutional constraints to development, the team organized a one-day closed-door
workshop on the political economy of institutional reforms in November 2017, targeting high-level politicians (including former Presidential candidates, Congressional representatives and provincial Ministers), the private sector (IFC clients NXTP, Vicentin, Afluenta, and CMF), and national academics (including institutional economists and political scientists). The meeting was chaired by the Country Director and facilitated by a local non-government organization (NGO, Fundación RAP, Red de Acción Política), and organized in two sessions. In the first session, the discussion aimed at validating and enriching the team’s preliminary diagnostics by identifying a long list of institutional reforms (20) needed to address the most important constraints to inclusive and sustainable growth. In the second session, a short list of reforms was prioritized according to their potential for economic impact and their political/social feasibility. Among the most impactful and likely reforms, the following were highlighted: addressing educational challenges, clarifying functions and responsibilities across levels of government and improving efficiency and transparency of national and sub-national expenditures. A second round of consultations took place in March 2018, with a selected group of cross-sectoral experts, to which the priorities were presented and validated.

A second round of consultations—held between April and May—involved presenting to external audience the set of constraints identified, to further validate the list of priorities and ensure the widest consensus around the proposed policy recommendations. These included, first, a meeting with three renowned academics, each asked to comment on the pillars of growth, inclusion and sustainability. Guiding the discussion pillar-by-pillar resulted in a wide discussion that went beyond the specific areas of interest of each of the guests, which proved helpful for the team in helping to bring the different elements together into a coherent story. In addition, a follow-up close-door event was carried out in collaboration with Fundación RAP, which included high-level politicians, members of the academia and the private sector. There was an overall consensus on the identified priorities. But importantly, there was strong support for the report’s emphasis on the institutional foundations as the necessary pre-conditions for successful implementation of the proposed technical priorities.
Knowledge and analytical gaps

211. The SCD also underlines critical knowledge gaps and areas for further research in Argentina. The most salient areas are described in the table below.

Table 8. Data and knowledge gaps

<table>
<thead>
<tr>
<th>Sector</th>
<th>Data and knowledge gaps</th>
</tr>
</thead>
<tbody>
<tr>
<td>Agriculture</td>
<td>- Characterization and trends of family farming.</td>
</tr>
<tr>
<td></td>
<td>- Economic complexity analysis for the sector.</td>
</tr>
<tr>
<td></td>
<td>- Analysis of the effect of land ownership on productivity growth</td>
</tr>
<tr>
<td></td>
<td>- Distributional implications of current policies for the sector</td>
</tr>
<tr>
<td>Education</td>
<td>- ECD assessments and detailed data on the quality of ECD is not available, as well as on teacher practices and school management skills.</td>
</tr>
<tr>
<td></td>
<td>- Detailed diagnostic of the sources of inefficiencies in the education sector and the identification of successful interventions to reduce school dropout in Argentina.</td>
</tr>
<tr>
<td>Environment and natural resources</td>
<td>- Understand causality between poverty and deforestation in rural area.</td>
</tr>
<tr>
<td></td>
<td>- Understand environmental and social impacts to oil and gas development.</td>
</tr>
<tr>
<td></td>
<td>- Air quality and health impact assessment with local epidemiology data. Cost of environmental degradation.</td>
</tr>
<tr>
<td>Health, Population and Nutrition</td>
<td>- Recent household survey to assess the health status of the population or the quality of the provision of health services provided</td>
</tr>
<tr>
<td>Growth, Macroeconomics and Fiscal Management</td>
<td>- Official, homogeneous and updated data on Provincial GDP.</td>
</tr>
<tr>
<td></td>
<td>- Firm-level microdata for productivity analyses.</td>
</tr>
<tr>
<td></td>
<td>- Access to administrative records the tax system (equity and efficiency issues).</td>
</tr>
<tr>
<td></td>
<td>- Full assessment of the monetary and fiscal frameworks under fiscal dominance.</td>
</tr>
<tr>
<td></td>
<td>- Full assessment of the monetary framework under</td>
</tr>
<tr>
<td>Poverty and Labor Markets</td>
<td>- Poverty and labor market household survey data for rural and small urban areas that will allow for national estimates currently non-existent</td>
</tr>
<tr>
<td></td>
<td>- Data and analysis of economic mobility across time for more than one-year period, and of economic mobility across generations.</td>
</tr>
<tr>
<td>Social Protection and Labor</td>
<td>- Data to estimate skill mismatch, linking type of skills demanded by the productive sector that can be matched to supply (labor force survey)</td>
</tr>
<tr>
<td></td>
<td>- Information on the type of task performed by workers in their occupation, and task content.</td>
</tr>
<tr>
<td></td>
<td>- Government social spending (national and provincial) cannot be analyzed by age group, considering not only cash transfers but also in-kind transfers.</td>
</tr>
<tr>
<td>Trade, Investment and Competition</td>
<td>- Analysis of productivity distributions within industries and the barriers to intra-industry reallocation.</td>
</tr>
<tr>
<td></td>
<td>- Firm level data that can be used for panel estimates and matching with household surveys, employment data, and trade data, is scarce.</td>
</tr>
<tr>
<td></td>
<td>- Innovation surveys discontinued in 2010 should be rebuilt.</td>
</tr>
<tr>
<td></td>
<td>- Better data on services, a dynamic sector, would allow for better policy formulation.</td>
</tr>
</tbody>
</table>
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ARGENTINA

Systematic Country Diagnostic


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158
Annexes

Annex I: Poverty measurement in Argentina

All the document’s data attributed to “SEDLAC (CEDLAS and the World Bank)” rely on a harmonized version of the urban-only household survey data from the *Encuesta Permanente de Hogares-Continua* (EPHC). The EPHC is collected by Argentina’s Instituto Nacional de Estadística y Censos (INDEC) on a continuous basis, and reported quarterly. The survey is representative of the 61 percent of the population, living in the 31 largest urban areas in the country. The harmonization undertaken by CEDLAS and the World Bank increases the comparability of household surveys among various LAC countries, allowing for internationally comparable indicators. Poverty rates are estimated using a US$5.5 per day, adjusted to USD in 2011 purchasing power parity.

Several issues had affected comparisons in official poverty rates over the years. First, they were under criticism from 2007 to 2013, primarily due to the consumption price index used to update the poverty line. Second, from 2013 to 2015, official estimates were not released. Third, although INDEC relaunched the publication of this indicator for the second quarter of 2016, it indicated that its value is not comparable with previous numbers, because of methodological changes, as well as changes related to the use of more up-to-date information on consumption patterns to define the poverty line. Finally, different changes related with the treatment of missing information on incomes and the projections of population growth were introduced in the EPH since 2003.

International poverty estimates (SEDLAC dataset) are able to overcome some of these difficulties. For the period 2007-2016 local inflation comes from private estimates. Yet, they do not address changes in the treatment of missing information on incomes and in the projections of population growth, which could affect poverty levels. However, differences in levels are not significant and, importantly, do not modify the trends of different indices.
Annex II: Profile of the Poor and Bottom 40

<table>
<thead>
<tr>
<th>Second semester, 2016. (31 largest cities)</th>
<th>Total</th>
<th>Poverty ($5.5-day line)</th>
<th>Shared prosperity</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>Poor</td>
<td>Non-poor</td>
</tr>
<tr>
<td><strong>Poverty rate and bottom 40</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Share of population</td>
<td>100.0</td>
<td>7.8</td>
<td>92.2</td>
</tr>
<tr>
<td>Share of the households</td>
<td>100.0</td>
<td>4.9</td>
<td>95.1</td>
</tr>
<tr>
<td><strong>Recent immigrants</strong></td>
<td>100.0</td>
<td>22.6</td>
<td>77.4</td>
</tr>
<tr>
<td><strong>Regions</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>GBA</td>
<td>100.0</td>
<td>7.2</td>
<td>92.8</td>
</tr>
<tr>
<td>Pampeana</td>
<td>100.0</td>
<td>8.8</td>
<td>91.2</td>
</tr>
<tr>
<td>Norte grande</td>
<td>100.0</td>
<td>9.1</td>
<td>90.9</td>
</tr>
<tr>
<td>Cuyo</td>
<td>100.0</td>
<td>9.1</td>
<td>90.9</td>
</tr>
<tr>
<td>Patagonia</td>
<td>100.0</td>
<td>3.0</td>
<td>97.0</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th><strong>Demographic characteristics of poor, non-poor and bottom 40</strong></th>
</tr>
</thead>
<tbody>
<tr>
<td>% of households with female head</td>
</tr>
<tr>
<td>% of households with 4 members or more</td>
</tr>
<tr>
<td>Average household size</td>
</tr>
</tbody>
</table>

**Dependency ratio**

- Children (aged 0 to 14) per adult (aged 15 to 64) | 0.4 | 0.9 | 0.3 | 0.7 | 0.2 | 0.1 |
- Elderly (aged 65+) per adult (aged 15 to 64)      | 0.1 | 0.0 | 0.2 | 0.1 | 0.4 | 0.1 |

**Age groups**

- Children (aged 0 to 14)                                | 22.4 | 41.4 | 20.8 | 34.6 | 14.2 | 6.8  |
- Adults (aged 15 to 64)                                 | 65.1 | 57.0 | 65.8 | 62.2 | 67.0 | 70.3 |
- Elderly (aged 65+)                                     | 12.5 | 1.7  | 13.5 | 3.1  | 18.8 | 22.9 |

*Source:* EPHC, 2016 second semester. Representative of 62 percent of the national population. For reference, the $5.5-per day line per person (in 2011 PPP) is closer national extreme poverty line, which is on average, around $4.6 per person per day. The national poverty line is on average for all regions, around $11.40 per person per day (2011 PPP).
<table>
<thead>
<tr>
<th>Second semester, 2016. (31 largest cities)</th>
<th>Total</th>
<th>Poverty ($5.5-day line)</th>
<th>Shared prosperity</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>Poor</td>
<td>Non-poor</td>
</tr>
<tr>
<td><strong>Assets and labor outcomes of the poor, non-poor; b40</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Access to basic services (% of HHs)</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Access to safely managed water</td>
<td>99.6</td>
<td>97.9</td>
<td>99.7</td>
</tr>
<tr>
<td>Access to safely managed sanitation</td>
<td>69.1</td>
<td>41.7</td>
<td>70.5</td>
</tr>
<tr>
<td>Less than 1.5 people per room</td>
<td>96.4</td>
<td>79.1</td>
<td>97.3</td>
</tr>
<tr>
<td>Precarious location</td>
<td>1.9</td>
<td>6.4</td>
<td>1.7</td>
</tr>
<tr>
<td><strong>School attendance</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Children (aged 3 to 5)</td>
<td>96.0</td>
<td>96.2</td>
<td>96.0</td>
</tr>
<tr>
<td>Children (aged 14 to 18)</td>
<td>85.2</td>
<td>76.9</td>
<td>86.4</td>
</tr>
<tr>
<td><strong>Coupled deprivations (% of its age-group)</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Children (aged 3 to 17) out-of-school and no safely managed water and sanitation</td>
<td>0.9</td>
<td>2.3</td>
<td>0.7</td>
</tr>
<tr>
<td>Youth (aged 18 to 25) not studying nor working</td>
<td>24.9</td>
<td>51.0</td>
<td>22.2</td>
</tr>
<tr>
<td>Elderly (aged 65+) in precarious dwelling and no safely managed water and sanitation</td>
<td>26.4</td>
<td>68.9</td>
<td>25.9</td>
</tr>
<tr>
<td><strong>Adult (25+)</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Below complete secondary</td>
<td>45.0</td>
<td>71.0</td>
<td>43.7</td>
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<tr>
<td>Complete secondary and above</td>
<td>55.0</td>
<td>29.0</td>
<td>56.3</td>
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<td><strong>Labor (aged 18+)</strong></td>
<td></td>
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<tr>
<td>Unemployment rate</td>
<td>8.0</td>
<td>30.6</td>
<td>6.9</td>
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<tr>
<td>Non-registered wage-earners (as % wage-earners)</td>
<td>32.1</td>
<td>77.2</td>
<td>30.7</td>
</tr>
<tr>
<td>Self-employed (as % employed)</td>
<td>17.7</td>
<td>23.0</td>
<td>17.5</td>
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</table>

**Source:** EPHC, 2016 second semester.
### Annex III: Selected WBG Analytical Work

#### Selected WBG Analytical Work

<table>
<thead>
<tr>
<th><strong>Existing Resources (World Bank reports)</strong></th>
<th><strong>Agriculture</strong></th>
<th><strong>Education</strong></th>
<th><strong>Energy and extractives</strong></th>
<th><strong>Environment and natural resources</strong></th>
<th><strong>Governance</strong></th>
<th><strong>Health, Population and Nutrition</strong></th>
<th><strong>Growth, Macroeconomics and Fiscal Management</strong></th>
<th><strong>Poverty and Labor Markets</strong></th>
<th><strong>Social Protection and Labor</strong></th>
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<tbody>
<tr>
<td></td>
<td></td>
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<td></td>
<td></td>
<td>- Argentina Development Discussion Notes: Social Protection and Labor in Argentina.</td>
<td></td>
<td>- Public Expenditure Review, 2016-</td>
<td>- 2013 WDR Jobs</td>
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<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>- LCR Regional Policy Report “Job creation and labor productivity”</td>
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</table>
| Social, Urban, Rural and Resilience | -Leveraging the potential of Argentinean Cities (2017)  
-2009 WDR "Reshaping economic geography"  
-Cities and Productivity LAC Flagship |
| Transport and ICT | -Argentina Transport Engagement Strategy (2017)  
-Project Appraisal Document: Northwestern Road Development Corridor Project (P163115).  
-Cirera, Maloney, 2017. The Innovation Paradox.  
-Brambilla and Tortarolo, Argentina chapter in regional study directed by Mark Dutz “Digital technology adoption, skills, productivity and jobs in Latin America”. |
| Water | -Diagnóstico de la Prestación de Servicios de Agua, Saneamiento y Electricidad en 10 Provincias del Norte Argentino. |
Annex IV: Data diagnostics for WBG client countries

Prepared by the Development Data Group (DECDG) of the World Bank

Country: Argentina

### Section 1: General Information about the Statistical System

**Legal status of NSO**

Agency of the Secretariat of Economic and Regional Planning in the National Ministry of Economy and Public Works and Services

**Statistical Legislation (latest)**

Statistics Law, 1968, 1993

**NSDS/Statistical masterplan**

Los lineamientos del Programa Estadistico Nacional 2007-2011

### Section 2: Micro data

<table>
<thead>
<tr>
<th>Type of census/survey</th>
<th>Latest (Year)</th>
<th>Second Latest (Year)</th>
<th>Representativeness</th>
<th>Data Accessibility</th>
<th>Optional Disaggregation (Y/N)</th>
<th>Sex</th>
<th>Regional</th>
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<td><strong>Censuses</strong></td>
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<td>2010</td>
<td>2001</td>
<td>National</td>
<td>External repository</td>
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<td>Agriculture Census</td>
<td>2008</td>
<td>-</td>
<td>-</td>
<td>-</td>
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<tr>
<td>Business/establishment census</td>
<td>2004-2005 (^{266})</td>
<td>-</td>
<td>-</td>
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<tr>
<td>Household Survey on income/consumption</td>
<td>2017 (^{267})</td>
<td>2016</td>
<td>Urban settlements (61% of total population)</td>
<td>External repository</td>
<td>Y</td>
<td>Y</td>
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</tr>
<tr>
<td>Household survey on education</td>
<td>MICS 4 2011-2012</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>Y</td>
<td>-</td>
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<td>Household survey on health</td>
<td>National Survey on Sexual and Reproductive Health (ENSSyR) 2013</td>
<td>MICS 4 2011-2012</td>
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<td>Labor force Survey</td>
<td>2017</td>
<td>2016</td>
<td>Urban settlements</td>
<td>External repository</td>
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<td>Enterprise Survey 2010</td>
<td>Enterprise Survey 2006</td>
<td>National</td>
<td>External repository</td>
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\(^{268}\) https://www.indec.gob.ar/bases-de-datos.asp?solapa=2
### Section 3: Macro data

#### Does the country subscribe to the IMF SDDS or participate in the eGDDS?

<table>
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<tr>
<th>SDDS</th>
<th>Periodicity</th>
<th>Country</th>
<th>SDDS</th>
<th>Perioricity</th>
<th>Country</th>
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<td>National accounts: GDP by Production and Expenditure at Current and Constant Prices.</td>
<td>Q</td>
<td>Q</td>
<td>1Q</td>
<td>NLT 1Q</td>
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<td>Consumer price index</td>
<td>M</td>
<td>M</td>
<td>1M</td>
<td>NLT 2W</td>
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<tr>
<td>Central government operations</td>
<td>M</td>
<td>M</td>
<td>1M</td>
<td>1M</td>
<td></td>
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<tr>
<td>Balance of payments</td>
<td>Q</td>
<td>Q</td>
<td>1Q</td>
<td>NLT 1Q</td>
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<tr>
<td>External debt</td>
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<td>Q</td>
<td>1Q</td>
<td>NLT 1Q</td>
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<tr>
<td>Merchandise trade</td>
<td>M</td>
<td>M</td>
<td>8W (4-6W encouraged)</td>
<td>3W</td>
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<tr>
<td>Production index</td>
<td>M</td>
<td>M</td>
<td>6W (1M encouraged)</td>
<td>NLT 1M</td>
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<tr>
<td>Employment</td>
<td>Q</td>
<td>Q</td>
<td>1Q</td>
<td>75D</td>
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<tr>
<td>Unemployment</td>
<td>Q</td>
<td>Q</td>
<td>1Q</td>
<td>75D</td>
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<tr>
<td>Producer Price Index</td>
<td>M</td>
<td>M</td>
<td>1M</td>
<td>3W</td>
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### Section 4: Compliance with WBGs core data standards

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<th>WBG Standard</th>
<th>Compliant (Y/N)</th>
<th>Actual yearly interval or %</th>
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<tr>
<td>Household survey of income or consumption</td>
<td>One every 3 years</td>
<td>Y</td>
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<tr>
<td>PPP price survey</td>
<td>One every 3 years</td>
<td>N</td>
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<tr>
<td>CRVS</td>
<td>80% of births registered</td>
<td>Y</td>
</tr>
<tr>
<td></td>
<td>60% of deaths registered with cause of death</td>
<td>N</td>
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### Section 5: Statistical Capacity Indicators (2017)

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<th>Open Data Barometer Score</th>
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<td>80.0</td>
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<tr>
<td>Source Data</td>
<td>Open Data Index Score</td>
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<td>90.0</td>
<td>60%</td>
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<td>Periodicity</td>
<td>Overall</td>
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<td>86.7</td>
<td>85.6</td>
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### Section 7: Data for country priorities

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<th>Available (Y/N)</th>
<th>Latest year</th>
<th>Issues</th>
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### Section 8: Data Gaps Identified and Recommended Actions

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<th>Major Data Gaps Identified</th>
<th>Recommended Actions</th>
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Annex V: Consultations

The SCD team conducted external consultations with specialists and stakeholders from the following organizations:

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<td>Universidad de La Plata (CEDLAS)</td>
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<td>Universidad del CEMA</td>
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<td>Universidad Di Tella</td>
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<td>Organización de Estados Iberoamericanos para la Educación</td>
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<td>Coalición Cívica</td>
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<td>Province of Córdoba</td>
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<td>Province of Salta</td>
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<td>Province of Santa Fe</td>
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</table>