Emerging Markets: Cry for Me, Argentina Argentina’s relationship with foreign investors in its energy industry has historically been rocky. The government in 1955 canceled international oil contracts signed by a previous president, Perón, in 1952. The next president signed new contracts in 1958, which were nullified in 1963 by a different president. Foreign oil companies were then invited to return in 1966, expelled in 1973, and again encouraged to enter after 1976. Not surprisingly, many foreign investors shied away from this country.

Since the 1990s, the pro-market reform policies that were centered on trade liberalization, deregulation, and privatization have brought more stability. More foreign investors showed up. In 1993, YPF, the formerly state-owned oil giant, was privatized. In 1999, Spain’s Repsol bought 57% of the shares of YPF and became its controlling shareholder. Although Argentina suffered from the government’s default on its $155 billion public debt (a world record at that time) in 2002, and the country has struggled to recover since then, Repsol’s operations have been relatively smooth—until recently.

In 2012, Argentina again was engulfed in a major crisis. Given the severe trade deficit, the government, under President Cristina Fernández de Kirchner, unleashed a series of radical measures to curb imports. Importers of foreign cars were required to find export buyers of Argentine wines; otherwise, port authorities would not release their cars. Foreign print publications, including magazines and newspapers, were held at the Buenos Aires airport unless subscribers went there to pay a highly unpopular additional fee—an import tax or tariff of sorts. In addition to making the life of Argentine firms and citizens harder, Fernández also targeted foreign direct investors. Specifically, Repsol was singled out as a high-profile target for nationalization (or expropriation). Repsol’s alleged wrongdoing was that it failed to boost oil and natural gas production needed to keep up with rising local demand. In 2003, when Néstor Kirchner, Fernández’s late husband and predecessor, took office, Argentina was a net energy exporter. Ten years later, Argentina imported 15% more than its energy production, resulting in more than $10 billion of cash outflows. The government argued that the largest producer, YPF, which contributed 45% of the country’s energy production, was responsible for this mess. In Fernández’s own words in her announcement:

If YPF’s policy continues—draining fields dry, no exploration, and practically no investment— the country will end up having no viable future, not because of a lack of resources but because of business policies.… Our goal is for YPF to be aligned with the interests of the country. When corporate interests are not aligned with national interests, when companies are concerned only with profits, that’s when economies fail, which is what happened globally in 2008 and what happened to Argentina in 2002 In the words of a Congressional leader, who participated in the debate on the YPF renationalization bill submitted by the president: All oil companies that operate in Argentina, Repsol and the rest, have to work in the public interest, which in this case means energy self-sufficiency for Argentina.… Repsol invested little in Argentina. But it was YPF and Argentine oil that financed Repsol’s growth around the world.

Fernández framed the YPF renationalization as central to fulfill her campaign pledges to tighten the interventionist policies in order to rescue the economy. YPF was an iconic symbol of national pride, and the cash-strapped government would love to have its revenues, estimated at $1.3 billion a year. Fernández’s measures were popular with ordinary Argentines. Many of them blamed free market reforms such as privatization of the 1990s to be a cause of the economic devastation of the 2000s. Not surprisingly, the YPF renationalization bill passed Congress by a landslide. In May 2012, Fernández signed the measure into law and formally (re)nationalized— for the time being without compensation—Repsol’s assets, which according to Repsol would be valued at more than $9.3 billion.

Outraged, both Repsol and the Spanish government protested, but there was little they could do. Argentina had little FDI in Spain, while Spanish FDI in Argentina’s highly regulated banking, telecommunications, and utilities industries could suffer if tensions were to escalate between the two countries. In retaliation, Spain quickly moved to limit imports of biofuels from Argentina, which annually exported $1 billion to Spain. Spain also threatened to initiate complaints to the World Trade Organization, called for EU-wide boycotts of Argentine products, and took the case to the World Bank’s International Center for Settlement of Investment Disputes (ICSID). In response, Fernández said:

This president is not going to respond to any threats … because I represent the Argentine people. I’m the head of the state, not a thug.

Argentina might indeed be defiant, because it already had a very bad record at ICSID, whereby one-quarter of all ICSID cases had been brought against Argentina (thanks to its 2002 default). While renationalizing YPF brought more revenues and helped the president gain more popularity, according to the Economist, “it is a disaster for Argentina.” In the short run, the fight over the valuation of the firm already began in negotiations between Argentina and Repsol. In the long run, such expropriation has grave ramifications far beyond the oil industry and beyond foreign investors from Spain (Argentina’s largest foreign investor). In fairness, Fernández also nati country’s private pension funds and (re)nationalized the flagship airline, Aerolineas Argentinas. So, she did not just target foreign investors such as Repsol. Nevertheless, foreign investors entertaining largescale entries in the rapidly growing Latin American region are likely to be lured more strongly by Brazil, Chile, and Mexico, as opposed to risking their capital in a country known to be a global rulebreaker.