

A country on a suicidal war path

By Fredrik Erixon - 19.04.2012 / 05:18 CET

Retaliation will not work with a government like Argentina's.

Yet again Europe finds itself in the unenviable position of having to develop strategies to deal with a populist and erratic government that has nationalised property owned by a European firm. This time, however, it is not Russia but Argentina that has expropriated property in a way that almost certainly violates international agreements that it has signed.

The move by Argentina's president, Cristina Fernández de Kirchner, to seize a controlling stake in the oil firm YPF – a subsidiary of the Spanish energy firm Repsol – came as a surprise. But it fits with the past decade's general trend of energy nationalisations in Latin America. And it follows hard on the heels of several other initiatives by the Argentine government to cut its dependence on foreign investors and close its market to foreign firms. The current president and her predecessor – her late husband Néstor Kirchner – have thrown Argentina back to an era of sordid Peronism, accompanied by belligerent economic populism.

Under their command, Argentina has buttressed a state-centred economy. Other companies have been nationalised and, following the government's confiscation some years ago of private retirement funds, the visible hand of the government can now be seen in many Argentine firms in which these pension funds had invested.

Kirchner has also jacked up import restrictions, styling protectionism as self-sufficiency. Last year, she introduced trade-balance requirements obliging companies to export as much as they import. That was a serious blow to companies such as BMW that are dependent on imports to build and sell cars in Argentina. As a result, foreign car-makers are now significant exporters of rice, peanuts and other agricultural products.

Unsurprisingly, foreign investors and firms are pulling out of Argentina in increasing numbers. This week's expropriation of Repsol's stake in YPF will only worsen the investment climate.

The diplomatic reaction from Spain and the EU should be firm. Repsol should file a case at an investment arbitration tribunal against the Argentine government for violation of the bilateral investment treaty (BIT) between Spain and Argentina. This treaty protects investors from hostile government actions, and it affirms investors' right to bring disputes against the state.

Argentina has been challenged by investors before. Indeed, Argentina has been one of the most frequent defendants at the World Bank's institute for arbitration in the past decade. Several parties have been awarded compensation from Argentina by arbitration panels.

Questions can no doubt be raised about the speed and effectiveness of investment arbitration: Argentina has been reluctant to pay these awards. Other countries have retaliated by suspending Argentine tariff concessions. The US, for example, did so in late March, in a case involving the US water company Azurix.

Yet tit-for-tat protectionism or retaliation outside the courtroom is not an effective strategy – especially not when directed against a government such as Argentina's. This week's nationalisation is not an isolated action, and behind the move is a general belief in irrational economic ideas. Such governments do not tend to respond to threats or incentives.

Calls have been made for the EU to follow the US's lead and suspend Argentina's tariff concessions under Europe's so-called generalised system of preferences (GSP), which reduces tariffs for developing countries.



CONFRONTATIONAL Cristina Fernández de Kirchner. REUTERS

But such a strategy is unlikely to pay off. It would take time for a suspension to be decided and take effect. The US government introduced the suspensions after an arbitration panel had ruled in favour of Azurix. It will take years before an arbitration panel has judged upon the expropriation of Repsol's stake in YPF. By then, the EU will have reformed its GSP scheme – and that reform, which is soon to be sealed, will graduate Argentina from preferential treatment.

“Never murder a man who is committing suicide,” Woodrow Wilson quipped about his opponent in the US presidential election in 1916. The same is true in this case. Retaliatory actions outside the courtroom will only serve to escalate deteriorating Europe's trade and investment relation to Argentina.

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