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Q&A- Peronists likely facing defeat in Argentinian elections; Peruvian strikes to hit copper investments: Mariana Zepeda, FrontierView



Argentina's Peronists face likely defeat in its upcoming midterm elections, which could potentially see the party move further left and jeopardize ongoing negotiations with the International Monetary Fund (IMF), **Mariana Zepeda, Latin America analyst at FrontierView**, told the Reuters Global Markets Forum on Friday, November 12.

Alternatively, President Alberto Fernández could maintain control of the party and commit to an agreement with the IMF and hopefully averting a crisis sparked by high inflation and a quickly weakening peso, Zepeda said.

She added that investments into the Peruvian copper industry could decline after a spate of recent labor strikes, and political and regulatory uncertainties.

Following are edited excerpts from the conversation:

Q: Could you run us through the lay of the land ahead of the Argentinian elections?

A: Absolutely! As many of you know, Argentina's midterm elections will be held on Sunday (Nov. 14), with a third of the Senate and about half of the lower house at stake. The results of the PASO midterm primaries in September, recent polling, and overall macroeconomic trends are pointing to a tough election for the ruling coalition.

Q: How is the huge rise in inflation and weakening peso playing into the election outlook? Is there a clear roadmap from any of the candidates on how to manage the situation?

A: It is definitely hurting the ruling coalition's chances in the elections. October inflation data was published yesterday, and it revealed that despite price controls and other measures the government has put in place to curb rising prices, inflation is still accelerating, eating into real wages and disposable income. The FX situation is tough as well - the government has tried to keep the official rate anchored, but the parallel rate (the dolar blue) is under significant pressure as the U.S. dollar continues to climb. Since their PASO defeat, the ruling coalition has leaned further into more interventionary policy in order to mitigate the impact of rising prices etc. on the population, but this is completely unsustainable given Argentina's low reserve position and lack of access to capital markets. The ruling coalition offers more of the same reliance on the printing presses to continue to fund government spending and try to address conditions on the ground.

Q: Who are the biggest challengers to the Peronists?

A: The main opposition, Juntos por el Cambio, is the coalition that President Mauricio Macri ran under previously, but some independent candidates have also become important challengers in local elections. Juntos por el Cambio's approach to addressing Argentina's economic ills is more broadly supportive of orthodox economic policies, and key candidates running under Juntos por el Cambio like Maria Eugenia Vidal have spoken out about working closely with the IMF to address macro and fiscal imbalances.

Q: If the Peronists suffer defeat, what kind of reckoning or policy shifts from them could be in store?

A: If the Peronists are defeated -- losing their Senate quorum and lower house plurality, which is the outcome that we are expecting at FrontierView -- the two most likely scenarios are that (a) more moderate Peronists like President Fernandez will lose political capital within the party, with VP Cristina Fernandez de Kirchner taking the reins of the coalition's economic policy and leaning into money printing, even higher spending, and more economic distortions, placing the IMF deal at risk and raising the likelihood of a debt and currency crisis in 2022.

Scenario B would have Fernandez keep the reins of his party, successfully keep his Finance Minister Martin Guzman at the forefront of negotiations with the IMF, and commit to implementing the IMF agreement, albeit with some pushback and continued uncertainty.

Q: Switching to Peru - what long term impacts, if any, do you see on the copper industry after the spate of strikes over the past few months?

A: That is an excellent question! Peru's copper industry and mining sector generally have faced extremely high levels of political and regulatory uncertainty since the election, not in the least because expropriation was on the ruling party's agenda. The Castillo government so far has behaved somewhat more moderately but renegotiating extractive sector concessions is still in the cards. The tepid response from the Castillo administration to these protests, coupled with already high uncertainty, is likely to depress investment in the industry. We expect still-high copper prices next year, though not as high as this year, so this could potentially impact Peru's ability to benefit from a high price environment, particularly if these protests continue to impact production, which has recovered slowly from the COVID-19 lockdowns.

Q: Do you think market and business worries after the election of Castillo were overdone given he has taken the more moderate route on a few issues so far?

A: I don't, I think there is still a lot of uncertainty. Castillo's policy stance and ideology have been hard to pin down, particularly since the decisions he's made about his government have not been entirely consistent, and he has spoken out publicly very little. Additionally, his recent shift toward the center lost him significant support from his party in Congress. Even though moderating enabled him to gain some support from the center-left, Peru Libre is still the largest bloc in Congress, and the right and center-right command an important part of the Congress too, so he is in a tough position politically. I wouldn't necessarily assume he is completely committed to taking the moderate route. It is a good signal that he has appointed a more moderate Congress, that he seems to have walked back from more radical viewpoints, and that he has selected a more moderate Finance Minister and kept on the head of the Central Bank, but the political environment has only gotten tougher, so he faces a lot of challenges ahead.

Q: What's your expectations from Peru's central bank, just after a series of rate hikes to curb inflation? How does this gel with the seeming desire from the government for continued spending?

A: The fact that Julio Velarde agreed to stay on is a positive signal for sure, and under him, the Central Bank seems committed to trying to curb rising inflation, though it is important to note that the policy rate was at 0.25% during the pandemic, so despite the hikes we are still in a very expansionary monetary policy environment. It is looking like we may see rates become more neutral midway through 2022, which is likely to create tensions between the government and the Central Bank. But Peru's fiscal position is certainly stronger than that of Argentina, for instance, so they have room for a bit more spending if needed before fiscal consolidation. It will be important to keep an eye on the tax reform too to see if the current spending situation will be sustainable!

Q: Any final thoughts for us?

A: 2022 is certainly going to be a fascinating year for Latin America, and we look forward to continuing to help our clients navigate challenging political and macroeconomic conditions in the region.

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