
Small and medium-sized businesses in Argentina: Coping with economic crises

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Argentina is a country of 37 million people (2000 census), 93% of whom are of European descent. It occupies a large area of the lower part of South America (exhibit 1), extending approximately 3 000 kms from north to south. Argentina is the eighth largest country in the world in terms of area, occupying 2 780 080 square kms (or more than the combined areas of Mexico *and* the adjacent U.S. state of Texas). Its climate ranges from sub-tropical in the far north to sub-antarctic in Tierra del Fuego in the far south.

What is now Argentina had a relatively small native population when it was visited by Pedro de Mendoza in 1536. Following an earlier, failed attempt the Spanish established a permanent settlement in Buenos Aires in 1580 and this grew slowly. The Argentines declared their independence from Spain in 1816.

However the country was largely unsettled until the middle of the nineteenth century. Heavy immigration from Spain and Italy began in the 1860s. This immigration continued up until 1914 and, to a lesser extent, between the two World Wars and in the years since. (So many Italian immigrants (many of them from Genova) settled in Buenos Aires that the Spanish spoken by natives of the city has a decidedly Italian flavour).

English, Welsh and Scots settlers also arrived, though in much smaller numbers. British investment largely funded the growing Argentine economy (railways, meat-packing plants, etc.) in the late nineteenth and early twentieth century. The “most southerly ranch in the world”, in Argentinean Tierra del Fuego, is owned by a family of English descent.

Although few in numbers, the Welsh settled in remote Chubut Province in Patagonia and earned the gratitude of the Argentine government by irrigating the desert adjoining the coast to produce prize-winning wheat, settling a region of the Andes coveted by Chile and – in a 1902 referendum in this same Andean region – voting to be citizens of Argentina rather than Chileans.¹

With such a background of European settlement it is perhaps not surprising that Argentines tend to consider their country to be an outpost of European civilization in South America (cities such as Buenos Aires certainly have a European appearance). There is a tendency, among Argentines, to feel superior to some of their neighbours with mixed racial populations (such as Brazil, whose people are descendents of Portuguese and African settlers and the native American population). Well-to-do Argentines have traditionally shopped for their clothes in London; their Brazilian counterparts have preferred Paris. Despite Argentina’s long-lasting claim to the Islas Malvinas (Falk-

¹ The Welsh held the unique distinction of being the only European settlers in the Americas to have a perfect record in their treatment of the Indian population.

lands) and the war of 1982, the commercial and cultural links between Argentina and Britain remain quite strong.

At the start of the twentieth century Argentina had one of the highest per capita incomes of any developing country. Its prosperity was based primarily on its production, and export, of wheat, beef, lamb and soybean oil to Europe and other Latin-American countries, as well as the industry and adaptability of its European settlers. Argentina also possesses significant mineral wealth, including significant deposits of coal, gold, silver and copper. Moreover, during the past thirty years the country has become self-sufficient in oil and natural gas. Argentina, in addition, has a highly literate population and its doctor/patient ratio is one of the highest in Latin America.

Argentina survived both the Depression and the two World Wars remarkably well and its people still enjoyed a high standard of living in 1945, when World War Two ended.

Economic problems

Unfortunately, despite Argentina's substantial resources, Argentines have seen their living conditions worsen in many respects during the past half-century. This has been due, partly, to severe cyclical declines in world wheat and beef prices, together with (sometimes simultaneous) declines in the market prices of minerals. However, Argentina's economic decline has also been the result of the financial and social policies of various governments (both federal and provincial) since the end of World War Two. The Peronistas, who first came to power in 1945, provided the working classes with benefits that the state could not afford. Trade unions were given wide powers. In addition, an unnecessarily large and underemployed civil service developed.

The military government of 1976–1982 instituted a reign of terror and damaged Argentina's international image by executing its most vociferous opponents. Several successive Peronista and/or military governments, moreover, have used up valuable foreign exchange in their purchases of armaments designed to shore up their domestic power and confront Chile, the Argentine's historic rival. In 1982 the Galtieri military government seized the Islas Malvinas (Falkland Islands) from a small British garrison in order to deflect Argentinean public opinion from the country's domestic troubles. This resulted in Falklands War of 1982 and a humiliating defeat which brought a civilian government to power in Buenos Aires.



Exhibition 1: South America, Mercosur, Argentina

Protectionist and populist economic policies in the 1980s led to economic stagnation and hyperinflation. The Peronista Carlos Menem, who was elected president in 1989, abandoned the party's statist ideology in favour of market economics and liberalisation, resulting in a period of rapid growth. The Argentine peso was pegged to the U.S. dollar and, for a while, the economy improved. Argentina benefited, too, from its membership of the Mercosur trading bloc (Argentina, Brazil, Uruguay and Paraguay); trade between these four countries increased substantially between 1990 and 1995.

However, Menem's failure to deepen fiscal and structural reforms in his second term of office (1995–99) left the economy vulnerable to falling international commodity prices. Argentina's trade surplus widened in 2001. Fernando de la Rúa's centre-left government, which was unable to halt Argentina's economic decline, collapsed in December 2001 amid violent protests. Since then the country's economic situation has deteriorated still further, with a succession of governments attempting, vainly, to deal with the situation. International reserves have declined by almost one-half, to \$10.5 billion. The federal government of Argentina, in addition to state governments, is paying some of its bills using a growing number of what outside observers describe as "quasi-currencies" (bonds which look like banknotes and are used for everyday transactions).

In February 2002 the peso was disengaged from the U.S. dollar. Its value subsequently plunged to almost 3.50 pesos to the dollar. Beginning in December 2001, Argentines endured a five-month partial banking freeze which limited cash withdrawals to about \$500 a month. In early June it was estimated that consumer prices had risen by 21% since January. Unemployment reached 24% that same month.

In late April the Argentine government took the extraordinary step of closing the nation's banking system. As a result, as this paper is being written, bank doors are locked and ATMs are empty. The visits of upper and middle-class Argentines to nearby Uruguay to withdraw their money from Uruguayan banks (thus causing an economic crisis in Uruguay) has provoked an angry outburst from the president of the latter country and a deterioration in relations between the two close neighbours (The Economist, June 8, p. 34–35).

Foreign observers have become extremely critical of Argentina's seeming inability to set its house in order. As one recent commentator put it:

... the president, the governors of the national bank and the Congress are engaged in a political game in which each is trying to force the other to take responsibility for the unpopular measures needed to share out the costs of (the peso's) devaluation. The game itself adds to those costs by shovelling blame and burdens on to the (mainly foreign) banks. The longer the politicians bicker, the closer Argentine edges toward hyperinflation and another explosion on the streets.

The Economist, June 1, 2002, pp. 13–14

SMEs in Argentina

Argentine government statistics categorize SMEs as indicated in table 1.

Sector	Agriculture	Manufacturing/Mining	Retailing	Service
Micro Enterprises	\$ 150 000	\$ 500 0000	\$ 1 000 000	\$ 250 000
Small Enterprises	\$ 1 000 000	\$ 3 000 000	\$ 6 000 000	\$ 1 800 000
Medium Enterprises	\$ 6 000 000	\$ 24 000 000	\$ 48 000 000	\$ 12 000 000

Source: *Secretaria de la Pequena y Mediana Empresa y Desarrollo Regional, Buenos Aires, June 2002.*

Table 1: Net annual sales(turnover) sectors Agriculture Manufacturing/Mining, Retailing, Service

Corporate and individual income-tax rates in Argentina are both 35%. However, micro and small enterprises pay a “*monotributo*”, or a fixed sum which is payable monthly regardless of the total net sales (or lack of sales) achieved during that month. This payment becomes part of the total tax paid during prosperous times, i.e. it is *not* an additional tax. Presumably this tax is levied to discourage wealthy individuals from establishing small firms as tax-avoidance devices.

There were a total of more than 40000 micro, small and medium-sized businesses in Argentina at the time of the last census. The Argentine federal government does not, unfortunately, break down enterprises by size (with the partial exception of farms which are listed only by acreage) in its census for the year 2000. However, table 2 lists the distribution of grants, to the various Argentine provinces, from the Federal Government of Argentina’s National Fund for Micro, Small and Medium-sized Enterprises (FONAPyME), in 2001.

<i>Region</i>	<i>% of Total Funds</i>	<i>Pesos</i>
Metro Buenos Aires	21.32	3 198 000
Santa Fe	8.68	1 302 000
Codoba	8.62	1 293 000
Chaco	4.84	726 000
Entre Rios	4.74	711 000
Tucuman	4.62	693 000
Mendoza	4.05	607 500
Santiago del Estero	4.01	601 500
Salta	3.72	558 000
Corrientes	3.61	541 500
	<i>68.21</i>	<i>10231 500</i>

Source: FONAPyME, Buenos Aires.

Table 2: Distribution of grants

Since this fund is disbursed to SMEs which submit proposals to increase their productive capacity, introduce new products, create value-added products and increase the number of their employees and/or increase Argentine exports, logic would suggest that these funds (which totaled 15 000 000 pesos in 2001) are distributed primarily to the

Manufacturing/Mining sector, though fruit and vegetable packers (in the Agricultural sector) would be eligible for funds under the right circumstances.

Table 2 indicates that, of Argentina's 24 provinces, Metropolitan Buenos Aires alone received over 20 percent of all funds; the ten most populous states combined (42 percent of the total number) received more than two-thirds of the budget. This is not surprising since there is likely to be at least some correlation between total population and the number of small and medium-sized provincial enterprises that have been formed to provide goods and services to consumers, either directly or indirectly (as would be the case with small wholesale firms).

The effects of the economic crisis on Argentina's SMEs

It will have become quite obvious by now that owners/operators of Argentine SMEs have been severely affected by the country's economic crisis. When withdrawals of savings from banks are limited or, even more seriously, prohibited (which, as has been indicated already, occurred for a short time recently) it is clear that the entire economy of any country will inevitably grind to a halt. Both individuals who are still employed and individuals who are not in the work-force, or unemployed, become concerned only with survival.

Examples follow from three representative sectors of the economy (the retailing sector, the tourist industry and the construction industry). As we have noted, the Argentine Census of 2000 does not provide separate data by firm size. However, figures published in April 2002 (*before* the economic situation worsened still further) indicate that retail sales in Argentine shopping malls were 22% *below* those of a year earlier. Many small stores in shopping malls have disappeared; one Argentine consumer refers to "whole galleries" (rows) of stores which have gone out of business.

A great many corner grocery stores are currently surviving the crisis (and their continued competition with large grocery chains such as the French-owned Carrefour) by remaining open seven days a week, closing at 10 p.m. even on Sunday nights.

Before the current crisis, dry cleaning was an important small business in Argentina because Argentines have traditionally worn woolen clothes. Dry cleaning has now become an unnecessary luxury; Argentines are wearing nylon jackets to avoid dry cleaning costs. The result is that a great many dry cleaning establishments have failed.

In the tourist industry (a sector of increasing importance in efforts to improve Argentina's international trade deficit), the effects of the World Trade Center bombing on September 11, 2001 caused some American (and, to a lesser extent, other foreign) tourists to curtail their plans to travel to other countries, Argentina included.

However, the owners of small family hotels and similar establishments have been affected far more seriously by a fall in their *domestic* market. This is due to growing Argentine unemployment (and the resultant insecurity of those still employed) together with the effects of the *corralito*, or "little fence" (the earlier partial freeze, mentioned previously, on bank deposits) which took effect on December 1, 2001. (This freeze made it impossible for the majority of Argentines to afford travel even *within* Argentina after they had withdrawn funds from their bank to pay for everyday expenses).

The Argentine economic crisis, with its wildly fluctuating peso exchange rate, together with the attendant political unrest, has also discouraged visitors from other Latin American countries. In January 2002 (in the middle of the summer in the Southern Hemisphere) some tourist establishments reported declines of over 60% in net revenue. (It is important to note that this was the situation *before* the Argentine government's closure of the banks and the freezing of *all* assets in May 2002). Most travel agencies have closed down and/or have declared bankruptcy.

Many upscale restaurants have closed because the great majority of their former patrons can no longer afford to eat "out". (Middle-class Argentineans are currently said to be existing on rice and pasta). Small corner cafes are surviving so far because they are still attracting some business; whereas a middle-class Argentinean might previously have enjoyed three of four coffees a day at two or more of his/her neighbourhood cafes, he/she is now more likely to have three coffees a *week*.

The construction industry, too, has been crippled by Argentina's economic and political crises. If we put ourselves in the position of the owner-manager of a hypothetical small construction firm who has recently contracted to add an extra room on to a middle-class home, we can visualize the situation which confronts him. He has probably received an initial "down payment" from the head of the family, and will have used these funds to pay for some of the materials to be used and to pay his workmen. In all probability, however, the family is unable to make a second down payment to the builder because it has to use its limited, and rapidly dwindling, funds to pay for its food and other basic necessities.

This, of course means that, very soon, the builder will have no funds to buy fixtures for installation in the half-completed new room – nor will he have funds to continue to pay his workmen. He will, moreover, find it increasingly difficult to obtain funds on credit, either because he may already be heavily indebted to his bank and/or because Argentine banks and other credit institutions will be increasingly reluctant to make loans in the present situation. All work on the half-completed room will cease. (In Argentina *no* construction whatsoever is taking place as this paper is being prepared).

It will have become clear to the reader by now that the worsening crisis in Argentina has affected all social-economic classes except the very rich. (An Argentine authority recently stated that 18 million Argentineans (almost 50 percent of the total population) are currently "living below the poverty line"). In Rosario, Argentina's second largest city and, under normal circumstances, a busy port and meat-packing centre, observers have reported that "the middle classes are moving into working class residential areas because they can no longer afford to live in their former homes. The working classes are moving into the slums." A recent survey of a class of 30 eleven-year-old children, attending a school in a traditionally working-class of an Argentinean city revealed that 24 of them (80 percent) had not had breakfast.

Traditionally the urban poor (as in many other countries) have been saved from starvation because they have been fed by Catholic and other charities, and by government. This continues to be the case. However in recent months, for the first time, many middle-class Argentineans have been seen at these soup-kitchens. More recently still, upper-middle-class Argentineans have established "barter groups" in which urgently-

needed items, including food, are obtained via the exchange of some sometimes cherished household possessions (Christian Science Monitor, April 30, 2002, 1, 7).

It is now customary for middle class Argentines to go to their bank (in which their salary is often automatically deposited) on pay-day and withdraw, in cash, their *entire* salary because they no longer trust their banks. Many middle-class people stopped using their ATM or credit cards some time ago.

One may well ask how *any* Argentinean SMEs and their owners are even surviving the present economic and political situation. To begin with, entrepreneurs in Argentina have had some experience in coping with the various economic crises of the past and have performed various ways of coping. Many owners of small and medium-sized enterprises who are still in business appear, at least in part, to be operating on a barter basis – both as small businesspersons and as consumers in their own right.

This would appear, logically, to be somewhat more feasible in smaller communities where there is a greater feeling of community and, perhaps, greater access to the agricultural sector. (Unfortunately the poorer segments of the population cannot even afford the cost of transportation to the countryside.)

Until economic and social conditions improve, transactions by surviving SME owner-operators (involving both purchases and sales) are likely to be limited to urgently needed items. Unquestionably, some Argentine SMEs will not survive the present crisis. Nevertheless, Argentines are a resilient people. Even though the present crisis is far more severe than any other in living memory, many Argentine SMEs *will*, somehow, survive. Regrettably, however, some will have been dealt a death-blow.

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