

Slower growth, exchange restrictions bite



General Information

| | | |
|---------------------------|--|------------|
| GDP | USD446bn (World ranking 25, World Bank 2011) | |
| Population | 40.76 millions (World ranking 32, World Bank 2011) | |
| Form of state | Republic | |
| Head of government | Cristina FERNANDEZ DE KIRCHNER | (FPV - PJ) |
| Next elections | 2015, presidential | |



Strengths

- Natural resource base (agricultural, energy and minerals)
- Durable, democratic political system.

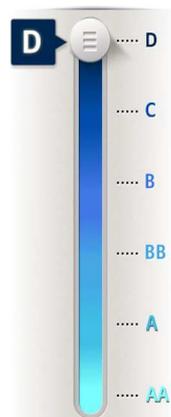
Weaknesses

- Unbalanced policy mix (high inflation and loose fiscal policy).
- Strong state interventionism, which has included expropriation of state energy company YPF and price controls clouds business environment.
- Import and capital controls.
- Lack of data transparency, particularly inflation, has brought formal censure from the IMF, threatening suspension.
- Lack of access to international financial support amid continued default to official creditors (Paris Club) poor relations with the IMF and the continued legal threat from debt "hold-outs".

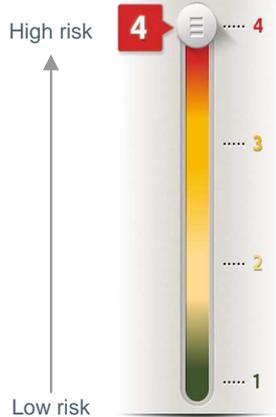
Country Rating

D4

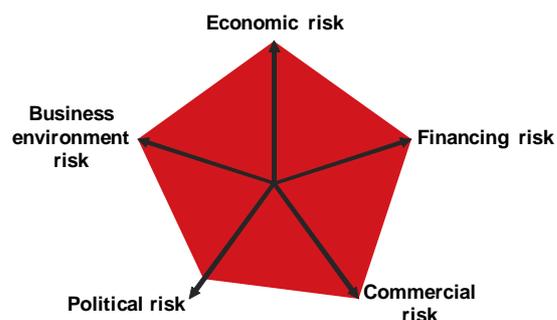
Country Grade



Country Risk Level

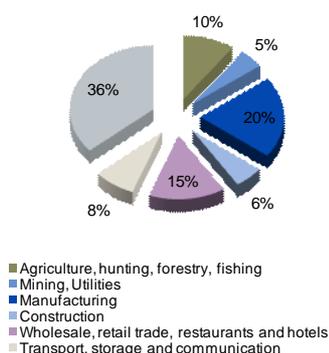


Risk Dimensions



Economic Structure

GDP breakdown (% of total, 2010)



Sources: Chelem, UnctadStat, IHS Global Insight, Euler Hermes

Trade structure (% of total, 2010)

By destination/origin

| Exports | Rank | Imports |
|---------------|-------|-------------------|
| Brazil | 21% 1 | 34% Brazil |
| China | 8% 2 | 15% United States |
| Chile | 6% 3 | 13% China |
| United States | 5% 4 | 6% Germany |
| Spain | 4% 5 | 3% Mexico |

By product

| Exports (% of total) | Rank | Imports (% of total) |
|--|-------|---|
| Feedstuff for animals (excluding unmilled cereals) | 13% 1 | 17% Road vehicles |
| Road vehicles | 12% 2 | 7% Petroleum, petroleum products and related and parts |
| Preparations | 11% 3 | 6% Telecommunication and sound recording apparatus |
| Fixed vegetable oils and fats, crude, refined or | 8% 4 | 5% Electrical machinery, apparatus and appliances, n.e.s. |
| Oil seeds and oleaginous fruits | 7% 5 | 5% |

Economic Forecast

| | Average 2000-08 | 2009 | 2010 | 2011 | 2012f | 2013f | 2014f |
|----------------------------|-----------------|------|------|------|-------|-------|-------|
| GDP growth (% change) | 3.9 | 0.9 | 9.2 | 8.9 | 1.9 | 2.0 | 2.5 |
| Inflation (% , end-year) | 9.6 | 7.7 | 10.9 | 9.5 | 10.8 | 12.0 | 11.8 |
| Fiscal balance (% of GDP) | -4.2 | -3.6 | -1.3 | -3.0 | -2.7 | -3.5 | -3.5 |
| Public debt (% of GDP) | 91.1 | 58.7 | 49.2 | 44.9 | 41.5 | 43.0 | 44.0 |
| Current account (% of GDP) | 2.6 | 3.6 | 0.8 | -0.1 | 0.4 | 0.4 | 0.2 |
| External debt (% of GDP) | 77.9 | 38.5 | 35.2 | 31.7 | 30.0 | 32.0 | 32.0 |

Sources: IHS Global Insight, National sources, Euler Hermes

Economic Growth

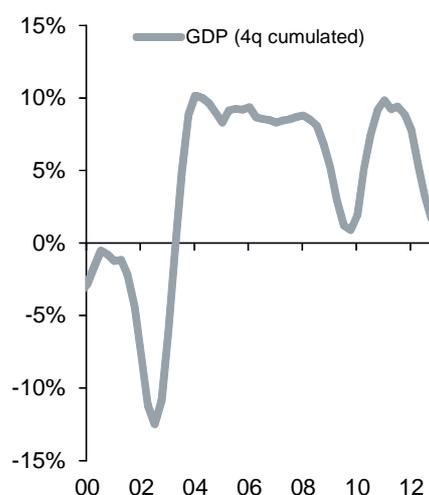
Growth slows sharply....

Frequently disastrous economic policies and political instability have led to volatile growth over an extended period, oscillating between boom and bust, despite a rich endowment of agricultural resources. Exports are mainly primary products and value-added goods from the agricultural sector, along with energy, and are concentrated on neighbouring countries, especially Brazil and Chile. Exports of soya and products account for 20-25% of total exports. Consequently, the economy is vulnerable to changes in commodity prices. Growth slowed sharply in 2012 to an estimated 1.9% (8.9% 2011) hit by drought, tight import controls, a fall in investment and a moderation of consumer spending.

...and only a modest pick-up in 2013-14

Growth is likely to pick up moderately in 2013 and 2014, reflecting a stronger harvest and recovery of demand growth in Brazil, but only to 2.0% and 2.5% respectively as the economy will remain constrained by import controls and weaker investment confidence.

GDP growth (y/y, 4 qtrs cumulated %)



Sources: IHS Global Insight, Euler Hermes

Economic Policies

Policies are increasingly heterodox and piece-meal interventionist (for example, the renationalisation of YPF). Inflation is high, fiscal policy loose and import and capital controls are in place. Moreover, there is little to suggest a change of approach from the current government or a strong response in terms of policy adjustment, if pressures were to increase.

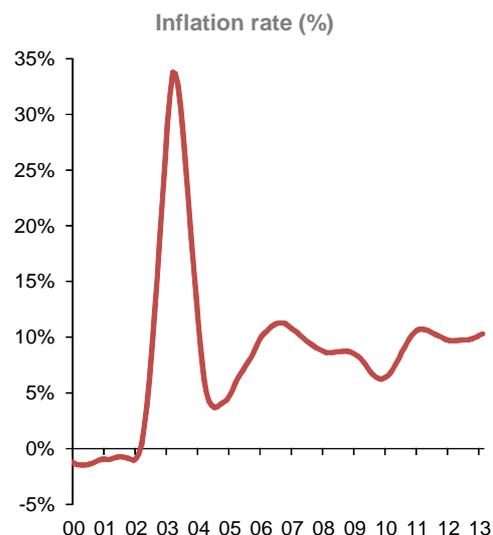
High inflation...

The central bank has little or no independence and legal restrictions on central bank financing to the public and private sectors have been removed. Money supply and domestic credit are still expanding strongly and the central bank continues to provide a large part of government financing. Real interest rates are negative. The result is high inflation, which was 10.8% y/y according to official data, though these are widely thought to be significantly underestimated with private estimates of observed inflation in the mid-20s. Moreover, failure to address data weaknesses, particularly inflation, has led to a formal censure by the IMF, which could lead to suspension later this year if not resolved. Official inflation is likely to accelerate to 12.0% by end-2013 and remain high in 2014

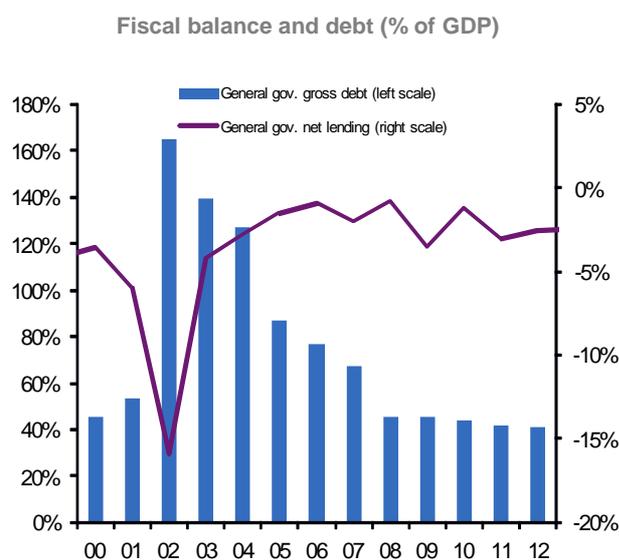
Exchange rate depreciation was relatively modest in 2010-11, but was accelerated in 2012 to improve competitiveness, as tighter controls on FX transactions stabilised FX reserves.

...Fiscal surplus eroding

The primary fiscal surplus has fallen sharply and the overall deficit moved into deficit in 2011 (-1.7% of GDP) increasing to an estimated 2.7% of GDP in 2012. Public expenditure has risen as a proportion of GDP from 23% in 2007 to 31% in 2011. Revenues should pick up somewhat in 2013 and the deficit should be contained to -3.5% of GDP. The public debt-GDP ratio is just over. The government has resorted to direct intervention to provide funding, via re-nationalisation of the pension system, borrowing from state banks, and transfer of FX reserves from the central bank and will need to continue to use these sources in the absence of access to international financial markets.



Sources: IHS Global Insight, Euler Hermes



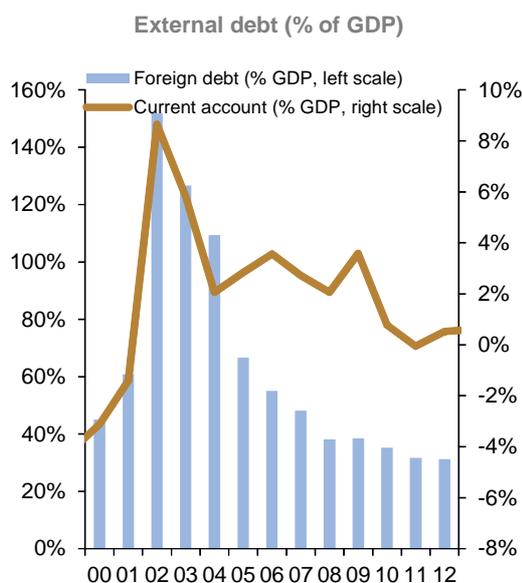
Sources: IHS Global Insight, Euler Hermes

Import controls maintain the current account balance...

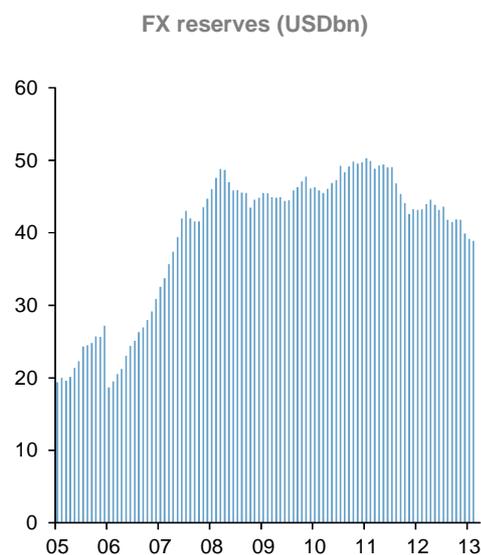
Tightening of import controls has halted the erosion of the trade surplus and the current account and rough balance or small surplus is likely to be maintained through 2013-14, though absent a rise in commodity prices import controls will need to be maintained and the external balance remains highly sensitive to commodity price changes. Recent actions, including the re-nationalisation of YPF, place considerable uncertainty over FDI inflows. FX reserves fell prior to the tightening of controls over foreign exchange transactions in 2012 but have since stabilised. FX reserves provide more than 5 months import cover but do not fully cover estimated external debt payments (ST and MT principal) falling due in 2013.

...External debt faces legal challenges

External debt ratios are moderate, following debt reduction after earlier default. The external debt-GDP ratio at end-2011 was 32%, the external debt-exports of goods and services (XGS) ratio 140% and interest payments due-XGS just under 5%. There are still arrears on external debt, however, and there has not as yet been an agreement on debt owed to Paris Club creditors while the private sector debt has been restructured, there are still 'holdouts'. Indeed a key short term issue is a ruling on a legal challenge in the US that is pending at the end of February, which could result in a technical default, if the ruling goes against Argentina and Argentina refuses to pay the 'holdouts'. The government also still lacks access to international financial support.



Sources: IHS Global Insight, Euler Hermes



Sources: IHS Global Insight, Euler Hermes

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