Argentina:
The 30 Years Crisis

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"Argentina has a story to tell the world: a story which is about the importance of fiscal discipline, of structural change and of monetary policy rigorously maintained."

-Michael Camdessus
Managing Director,
International Monetary Fund
10/1998

1. Introduction

A. Introduction & Brief Literature Review

Through a little mental math, I recently realized that an Argentine friend of mine was roughly 14 years old when her country's economy crashed in 2002. What was it like, I asked her, to live through the crisis?

Her response was, "which one?"

Like my friend, it seems that much of the literature divides the Argentine economic implosions of the last 30 years into separate events. A great deal of literature emerged in the early 1990s analyzing the hyperinflation that first hit in 1988. Some of these works consider the newfound stabilization under market reform led by Carlos Menem. For example, William Smith's piece "Hyperinflation, Macroeconomic Instability, and Neoliberal Restructuring in Democratic Argentina," details the spectacular failures of President Raúl Alfonsín, and he foresees the potential of "continuity…maybe even irreversibility of the *menemista*" Argentine miracle.[1] In fact, compartmentalizing Argentine economic development was nothing new for Mr. Smith: he had previously authored a book on the Argentine political economy under authoritarianism, an episode that ended with the government of Alfonsín.[i]

A second batch of literature emerged following the 2002 crisis, and these works almost exclusively consider the rise and fall of convertibility: the legal peg of one peso to one dollar. Books such as *The Argentine Crisis at the Turn of the Millennium* edited by Flavia Fiorucci and Marcus Klein feature chapters called "From De la Rúa to Kirchner" – an example that highlights the compacted time frame of their evaluation. Similarly, International Monetary Fund (IMF) post mortems, such as the *The IMF & Argentina, 1991-2001 Evaluation Report*, their *Lessons From the Crisis in Argentina*, and Michael Mussa's unofficial *Argentina and the Fund: From Triumph to Tragedy* all pick up the story at the dramatic introduction of convertibility. Finally, there are examples such as Paul Lewis who wrote *The Crisis of Argentine Capitalism*

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[i] Other books that cover the Alfonsín-era crisis as independent of subsequent crises include *Remaking the Argentine Economy* by Felipe de la Balze, *Argentina: The Economic Crisis in the 1980s* by Keiler Studien, Roberto Cortés Conde's *The Political Economy of Argentina in the Twentieth Century*, among many others. See bibliography for full citation details. Of course, many of these works were composed prior to the breakdown of convertibility, but the point remains that the Alfonsín chapter is typically treated independently from the turn of the millennium chapter.

which covers through the Alfonsín years, only later to write *The Agony of Argentine Capitalism: From Menem to the Kirchners*, yet he never connects the Alfonsín era to the Menem era (one wonders which painful subject noun Lewis will use in any subsequent book titles should Cristina Krichner's economy fail).[ii]

B. Thesis Statement

This paper, however, considers the continuity of the crisis, suggesting that both Presidents Raúl Alfonsín and Carlos Menem not only faced similar sets of crises, but that they faced *the same* crisis, just at different points in time. In Part II of this paper, I consider how each one implemented very different plans yet they arrived at relatively similar results. I compare how both tried to tackle inflation, but neither could (or would) address the deep seated causes of the 30 Years Crisis.

In Section III, I argue that while both the Austral and Convertibility Plans sought primarily to address inflation, inflation was but a consequence of the true root problem: unsustainable debt. Under President Raúl Alfonsín, the debt was financed by Central Bank monetization that undermined *Plan Austral* price freezes. Under President Carlos Menem and Fernando de la Rúa, this debt was financed by external capital inflows (read: more debt), eventually undermining convertibility.

From this conclusion, the next logical question is why did foreign debt (not mathematically overwhelming in the 1990s[2], for example) become utterly unbearable. In Section IV, I argue that in both cases, the debt was unsustainable because the fiscal policy was irresponsible, and incapable of generating the requisite surpluses. This fiscal irresponsibility is the common trend throughout the 30 Years Crisis; this fiscal irresponsibility was behind the inflation and until this fiscal irresponsibly is addressed the results will always eventually be the same: capital flight, depreciated domestic currency and unsustainable (or no access to) external debt.

C. Overview: The 30 Years Crisis

In many ways, the characteristics of the economy inherited by Raúl Alfonsín in 1983 were similar to those inherited by Carlos Menem in 1989, and, for that matter, to those inherited by Eduardo Dulhalde in 2002. All three incumbents faced dangerously high

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[ii] Other titles that analyize the 2002 breakdown with little or no treatment of the Alfonsín-era include Julio Godio's *Argentina: En La Crisis Está la Solución,* Edward Epstein and David Pion-Berlin ed. *Broken Promises,* among others. See bibliography for full citations.

inflation, capital flight and unsustainable external debt. Of course, proponents of the military regime that ruled Argentina from 1976-1983 could persuasively argue that they themselves inherited two of these three: high inflation and capital flight from Juan Perón's disastrous final term as president (1973-1974). Thus, while policy responses differ significantly, the macroeconomic instability seems constant.

Perhaps 1969 can be used as the last time Argentina stood on truly stable ground. Following the Kreiger Vasena stabilization plan, inflation had dropped below 10%, and the government deficit stood at around 1% of GDP.[3] However, the early 1970s saw an emphasis placed on price and wage increases that destabilized the exchange rate. A series of devaluations kicked off inflationary expectations that would prove difficult to combat.[4] Price freezes aimed to correct these expectations, but these proved bureaucratic nightmares to enforce and could, in themselves, push inflation. For example, many firms expected a price freeze following Perón's return to office in 1973. Hoping to 'beat the freeze,' many quickly hiked prices not for reasons of supply and demand, but in order to lock in a higher price before the next round of fixing.[5]

Broken freezes and successive currency devaluations created short time horizons marked by a lack of credibility and unpredictability. Following a banking crisis in 1981 that forced the government to nationalize private external debt the military authorities announced another round of devaluation that Argentines interpreted as insufficient, and they speculated against it. As a result, Consumer Price Index (CPI) inflation spiked from 105% in 1981 to 165% in 1982, and reached a walloping 344% in 1983, the year Alfonsín assumed office. Meanwhile, by 1983 sovereign debt *interest payments* alone spiked to 10% of GDP up from 3.3% in 1980.[6] This external debt was exacerbated by capital flight which hemorrhaged out of Argentina. From 1971 to 1985 nearly US$41bn was siphoned out of the country.[7] With international investors no longer interested in financing Argentine debt, it was under these circumstances that Alfonsín would present his *Plan Austral* in 1985.

Carlos Menem inherited a country suffering from very similar disaster symptoms. Attempts to overvalue the *Austral* currency (implicit in attempts to hold price freezes) in the *Plan Primavera* had been undermined by Central Bank monetization of debt. With expectations of further devaluation, speculators abandoned the Austral *en mass*, forcing the Central Bank to squander its dollar reserves in a futile attempt to defend the currency.[8]

When the Central Bank had to discontinue the sale of dollars, inflation spun out of control, with consumer prices rising 114.5% in the month of June, 1989 alone.[9] Inflation peeked in 1991, shortly after Menem assumed office, at a backbreaking 3,000%.[10] Thus, Menem faced essentially the same crisis as Alfonsín, just further down the road. Their attempts to rectify the situation, however would differ greatly. I address the philosophy, execution and downfall of each plan in turn.

2. Different Plans, Similar Results

A. The *Plan Austral* of 1985

Introduced in June 19th, 1985 President Alfonsín's *Plan Austral* is understood as a heterodox stabilization policy as it combined traditional measures of fiscal tightening with price and wage freezes. The plan placed a particular attention on curbing the inertia of inflation. Furthermore, the plan introduced a new currency, the *Austral* meant not only to chop zeros from the national unit of currency (one *Austral* was introduced at a rate equal to 10,000 pesos), but also to erase memories of inflation, and inflation expectations.[11]

Furthermore, the plan contained an explicit promise from the Central Bank to refrain from further money creation. To offset the lack of Central Bank credits, the plan introduced new and increased taxes on exports to boost public revenue.[12] The plan also emphasized limiting the fiscal deficit, but, as this paper will argue, external debt rendered such consolidation unrealistic. Scholar José Louis Machinea argues that Alfonsín's economic team was sufficiently sophisticated to understand the short term nature of such artificial price freezes,[13] but the government attempted to underscore their dedication to the freezes in the hopes of earning credibility.

B. The Convertibility Plan of 1991

Like Alfonsín, President Carlos Menem did not introduce the plan for which he would be remembered immediately. In fact, his initial *BB Plan* (named after the influence of industry titan Bunge & Born) featured similar approaches to that of Alfonín, namely price freezes followed by devaluations along with an attempt to improve tax intake to balance fiscal deficits. If the strategies seemed similar so did the results – hyperinflation struck again in 1990.

In 1991, however, Menem, and new Economic Minister Domingo Cavallo introduced a plan with a new kind of price freeze – a freeze on the price of the dollar. Whereas *Plan Austral* initially froze consumer prices, creating unsustainable market distortions, Menem and Cavallo liberalized markets eliminating bureaucratic measures previously in place to restrain hot money capital inflows.[14] Strong capital inflows would theoretically relieve the pressure of generating a current accounts balance in order to finance any fiscal deficit. As such, there would be less pressure to devalue the peso, now pegged (and likely overvalued) to the dollar. The *Austral Plan* failed because the government could not hold the price freezes. With capital inflows, Menem's currency price freeze would face less initial pressure.

Finally, The Convertibility plan featured fire sale privatizations of oil fields, steel mills, electrical power planes, railway lines, even the Buenos Aires subway; and these privatization were just the warm up act for the 1993 privatizations of the state oil company, Yacimientos Petrolíferso Fiscales, and the Social Security system.[15] These privatizations aimed to put Argentina inline with the Washington Consensus, and thus make the country more attractive to international investors. They also generated lump sum inflows, and in some cases, relived the government of consistent fiscal drains.

C. Initial Success

Both plans enjoyed initial success, especially in targeting inflation. Between June 1985 and March 1986, just after the announcement of *Plan Austral*, the Consumer Price Index (CPI) increased at a very manageable 3% per month.[16] The fiscal deficit shrank to 2.4% through the end of 1985. Instead of capital flight, demand for money increased through the second trimester of 1986, and Central Bank reserves increased by 67%.[17]

Whereas the *Plan Austral* held inflation in check for a matter of quarters, the Convertibility Plan stabilized the Argentinean economy for a matter of years. Inflation, 27% in February of 1991, had dropped to 2.8% in by May of that year. It would hover around zero from 1994 through most of 2001.[18]

International investors responded to the Convertibility Plan's efforts to attract inflows. Between 1989 and 1993, external investment totaled US$9.3bn, including just under US$1bn invested in private Argentine firms. Domestic and international confidence in the peg remained high as Menem paid off US$12bn of Alfonsín's debt and as the Argentine economy survived the Mexican Tequila Crisis of 1994. In fact, Menem's refusal to print money during the difficult months following the deterioration of the Mexican peso reassured investors of the Argentine commitment to convertibility.[19]

D. Shocks & Failure

Both plans aimed to stifle inflation and both succeeded in the short term (albeit much shorter in the case of the *Plan Austral* than in convertibility). Yet both plans proved unable to withstand trying shocks in the long run, and both ended in disaster. In the case of the *Plan Austral,* heterodox approaches never had a chance because Argentina's underlying macroeconomic conditions had collapsed, rendering price and wage freezes unsustainable. The fixed *Austral* quickly became overvalued making it impossible to generate the current account surplus required to finance foreign debt obligations. A widening gap between the price of wholesale tradable goods and retail domestic services made this overvaluation obvious to all, leaving the currency vulnerable to speculation.[20] In April of 1986, government officials relaxed the freeze and ushered in a 'flexibilization' phase that featured multiple revaluations. The return of inflation overwhelmed subsequent orthodox plans such as 1987's *Australito*.

Thus, in retrospect, the price freezes of *Plan Austral* acted as a timeout might in sports. The plan briefly paused the action, but provided no long term solution or changes in trends. The country did not have the reserves to defend price controls, or the credibility to float them. Successive devaluation led to a speculative frenzy that in 1989 unraveled into hyperinflation.

The Convertibility Plan also offered a short term (and much more effective) answer to inflation, but again it did not solve the deeper macroeconomic instability that *generated* inflation, and was thus unable to withstand shocks. Returning to our sports analogy, if the *Austral Plan* was a short-lived timeout, Convertibility was a highly effective relief pitcher left in the game far too long. The plan seemed brilliant when GDP averaged well over 5%,[21] but the peg's firm veneer proved little match for the series of adverse shocks that struck in the late 1990s.

Argentina had no business being in a monetary union with the United States, and the following three major shocks demonstrated this: 1) The Brazilian devaluation of 1999, 2) A strengthening American dollar, and 3) An Argentine recession. Argentina may have avoided the worst of Asian Crisis contagion that spread throughout emerging markets between 1997 and 1998, but Brazil did not. When Brazil exercised their ability to devalue, suddenly

Argentine products became degrees more expensive for Brazil, a nation that previously received about 1/3 of Argentina's total exports. Brazil's devaluation also gave Argentina's neighbor an advantage in markets where the two competed such as beef and soy.[22] This price differential was exacerbated by an appreciating dollar, which meant an appreciating peso. These trends, along with a declining appetite for emerging markets investment led Argentina into persistent recession as the country posted negative quarterly GDP growth through the end of convertibility in 2002.

Under these conditions, the spread on Argentine bonds escalated to the point that, on April 1st, 2001, Economy Minister Cavallo (now in his second tour of duty) had to cancel an auction of $350 in Treasury notes because the yield topped 16.9%.[23] Given the importance of external financial inflows to the Convertibility Plan, once borrowing became prohibitively expensive, disaster seemed a matter of fate. In the following months a series of events raised grave questions about Argentina's ability to produce US$1 for every peso in circulation. These included requests for debt swaps, a 2001 Standard & Poor's downgrade in bond rating and the December 1st, 2001 *corrralito* that cut savers off from the bulk of their bank deposits.

Writing in 1991, scholar William Smith likened Convertibility to a "dramatic gamble…A high stakes poker game. If firms or individuals should fear that the government lacked the reserves to maintain the (peg) they could freely convert all their local currency into dollars, leaving Central Bank Coffers empty."[24] When domestic account holders, foreign investors and the IMF all called the Central Bank's bluff in late 2001 through early 2002, this is exactly what happened.

Like Alfonsín, President Fernando de la Rúa was forced to resign. Following a revolving door of presidents, Eduardo Duhalde assumed office, his country an international pariah due to debt default, a peso plunging against the dollar and anyone with the means trying to get their capital out of Argentina – not altogether different from the situation faced by Alfonsín in 1983 and Menem in 1989.

3. Beyond Inflation

A. Debt – The Achilles Heal

While the *Plan Austral* limited inflation only temporarily, Domingo Cavallo's Convertibility Plan stopped it dead in its tracks, and for this he was revered as a hero throughout Argentina.[25] However, as this section will demonstrate, a key factor for economic crisis throughout the period was the need to finance international debt, and this was not successfully addressed by either plan.

In the years leading up to both crises, Argentina accumulated significant international debt. Alfonsín entered office with Argentina already well over US$35bn in debt.[26] Under the import substitution model that prevailed from the close of World War II to the mid-1970s, Argentine investment was funded domestically by negative real interest rates: lenders subsidized borrowers, as interest on domestic loans was less than peso inflation.[27] During the military regime (1976-1983), however, three trends emerged: 1)Argentine savers, aware of this inflation tax, demonstrated an increased preference for dollars, 2)the military regime began to liberalize capital inflows, and the 3) "dollars suddenly began to flow in the country in big waves" in the form of international loans, and Argentine external debt increased exponentially.[28]

Only US$9.7bn in debt in 1976, external debt nearly quadrupled in the following eight years. On the public side, most of these funds went to projects such as military armaments that would not pay dividends greater than interest owed, let alone recoup the principal sum of the debt.[29] The Argentine private sector also took on external debt, according to Professor Joseph Halevi, at a greater clip than the public sector.[30] This private external debt would come back to haunt the Argentine public balance as a 1981 banking crisis forced the government to nationalize external private debt.[31]

In somewhat unfortunate timing, the two waves of Argentine capital liberalization coincided with periods of major developed world credit extension to emerging markets. The late 1970s witnessed billions of dollars of loans to the Argentine sovereign. In the 1990s, investment banks issued billions of dollars in emerging market sovereign bonds while emerging stock markets soared. In 1997, for example, with the Argentine debt-sustainability ratio already pushing credibility, Argentina received US$10bn in net external portfolio investment,[32] and J.P. Morgan and Merrill Lynch issued US$2bn in Argentine government bonds.[33]

Thus in the years proceeding the crises, both governments faced expanding external debt obligations. As mentioned, Alfonsín inherited US$35bn in external debt. By the time convertibility was announced in 1991, Argentine external debt topped US$60bn, including US$8bn in overdue interest payments.[34] How each government sought to finance this debt is illustrative of the nature and timing the subsequent crises.

B. Financing Sovereign Debt in the 1980s

A major reason that the Austral Plan proved incapable of providing long term stabilization was that the Argentine government and Central Bank had to service outstanding international debt obligations denominated in hard currency. The Alfonsín government sought to satisfy these requirements by maintaining large current account surpluses, which in turn would generate the requisite hard currency to meet debt demands. However, this strategy entailed a devalued peso, such that the international demand for exports exceeded the national demand for imports. Furthermore, the ability of the cash strapped government to then purchase the hard currency from importers depended on monetary expansion. Unfortunately, both the devaluation of the peso and monetary expansion forced by the need to service sovereign debt undermined the integrity of price fixing schemes associated with the *Plan Austral*.

Large devaluations executed just before Alfonsín's ascension to office generated significant hard currency inflows in the form of a current account surplus. After posting a trade deficit of US$287m in 1981, the devalued currency generated a US$3.3bn surplus in 1983.[35] However, maintaining such surpluses required a currency at least at market value, if not *undervalued*. Thus the artificial fixed rates established by the *Plan Austral* led to the deterioration of the trade surplus, which dwindled from US$4.9bn in 1985 to $975m in 1987. Shortly thereafter, in April of 1988, Argentina was forced to suspend interest payments on debts to commercial banks.[36]

Unable to pay external debt due to the current account deficit, the government was forced to again devalue, in process challenging the credibility of any subsequent freezes. The initial success of the plan was undermined almost the moment Minister of the Economy Juan Sourrouille announced the relaxation of rigid price controls. His attempt to reestablish rigidity some months later served only to perpetuate a lack of credibility in the future of exchange rates.[37]

By January of 1989, as Central Bank financing of public debt spiked alongside an increasing total stock of private debt, further currency devaluation seemed inevitable – the only question was when? With the cost of staying "too long in austral-denominated instruments (being) financial ruin," Argentineans abandoned the domestic currency and hyperinflation struck.[38]

Furthermore, the ability of the cash strapped government to purchase any trade surplus generated hard currency from importers depended on monetary expansion. Simply put, just because Argentina realized a trade surplus did not mean this cash flowed directly to the government. More often then not, the hard currency earned by private firms went "to dollar savings accounts abroad."[39] The government could not generate a large enough fiscal surplus to purchase the foreign exchange, nor could it raise the money on international capital markets (See Figure 1 for a graph of the governments dwindling international reserves). Thus, it turned to the Central Bank for the extension of credits to satisfy interest payment.[40]

Rather than straightforward money printing, the Central Bank of Argentina initially attempted to support sovereign debt deficits by raising the reserve requirements of Argentine banks. This move forced banks to park more of their assets in Central Bank coffers, expanding the capital available to the state. These "forced investments"[41] carried generous spreads – spreads that spiked when capital markets were liberalized in 1987. Already running a large quasi-deficit,[42] the spike in interest the Central Bank now owed to other banks was simply unsustainable, and the Central Bank began printing money to pay its own interest.

By January of 1989, as Central Bank financing of public debt spiked alongside an increasing total stock of private debt, further currency devaluation seemed inevitable – the only question was when? With the cost of staying "too long in austral-denominated instruments (being) financial ruin," Argentineans abandoned the domestic currency and hyperinflation struck.[43] The World Bank reports that during the bout of hyperinflation in the second quarter of 1988, the quasi-fiscal deficit topped out at an "unprecedented 25.3% of GDP."[44]

The needs to devalue the peso and expand the monetary base to service sovereign debt sunk the price fixing schemes central to the *Plan Austral*. As will be seen, under Menem's convertibility the supposed excesses of monetary policy were eliminated. However, the root conundrum remained: how to generate the fiscal surplus required to service outstanding, dollar denominated international debt.

C. Financing Sovereign Debt in the 1990s

Monetary Policy under Convertibility is easier to explain: There was none. In apparent reaction to the traumatizing experience of hyperinflation of the late 1980s, the hard peg handcuffed any Central Banking authority over the monetary base. The currency broad rendered devaluation illegal, and pesos were not to be issued for public consumption unless they were backed by dollar reserves or part of exchanges for dollars.[45]

Given this monetary limitation, the IMF concluded in its 2004 post-mortem, "debt needed to be kept sufficiently low in order to maintain the effectiveness of fiscal policy as the only tool of macroeconomic management and the ability of the government to serve as the lender of last resort."[46] Argentine debt, however, both expanded and became significantly more expensive throughout the 1990s. By 1997, debt accumulation began to consistently outpace GDP growth.

Argentina had successfully stifled inflation, but the key question remained: how to finance this debt. Devaluation, as executed in the 1980s to generate a current account surplus was no longer an option. In fact, given the "strong" peso, Argentina ran a consistently negative current accounts balance in the years of convertibility – a deficit that was exacerbated after the 1998 Brazilian devaluation.[47]

Therefore, if debt could not be financed through monetary policy or through trade surplus, the fiscal position of Argentina became key. Unfortunately, fiscal stability has not historically been Argentina's strong point (see Section IIIF.). By 1997 the IMF still believed that certain fiscal actions would leave Argentina with a relatively manageable 34% Debt/GDP ratio in 2000. However, this scenario required 5% annual GDP growth and certainly did not take into account the series of adverse shocks discussed in Section II.[48]

How then was Argentina to finance its debt? Why, by more debt, of course. As journalist Paul Blustein wrote, the continued appetite for Argentine bonds (driven by investment bank reports of dubious impartiality) allowed Argentina to finance billions of dollars in debt.[49] When the markets balked, Argentina financed its debt through IMF loans. When the IMF punted in December 5th of 2001, Argentina faced an economic crisis every bit as horrifying and destabilizing as the hyperinflation of 1988.

Thus, convertibility may have halted inflation in its tracks, but inflation may have just been a symptom of a deeper problem that lurked throughout the 30-year crisis: the inability to generate the fiscal surpluses required to sustain debt-led growth.

4. Government Irresponsibility & The Unsustainable Debt

Thus far this paper has demonstrated that various economic stabilization plans aimed primarily to counter inflation could not offer long term stability. In the first part of Part III, I argue that the true root of both crises was unsustainable foreign debt, and plans that focused on inflation would not eradicate the root cause of the crisis. If this is the case, the logical next question is why were successive Argentine governments unable to finance foreign debt? In this final section I will argue that ingrained government irresponsibility – demonstrated by hubris and fiscal profligacy - overruled any allusions to fiscal consolidation presented in the various stabilization plans.

A. Hubris & The Great Panacea

Perhaps in line with Argentine infatuation with individuals as saviors, every leader that succeeded Perón seemed to think that their existence alone, or their general theories alone, would be enough to eventually calm the Argentine economy, presumably without facing the pain of fiscal austerity. Beginning with the military's assumption of power, scholar Roberto Conde writes, "As they saw it their mere presence would be the necessary condition to end the recession…and start on the road to sustained growth."[50] Similarly, Alfonsín coined a popular phrase prior to assuming the presidency in 1983, "with democracy, you eat, you get educated and you get cured." Scholar Adolfo Canitrot suggests that the slogan implied, "first, that the economic crisis stemmed from the moral perversity of the authoritarian regime; and second, that that democracy would be sufficient to overcome the economic crisis."[51]

For Carlos Menem, the great panacea was market liberalization and privatization, which he tried (vainly) to couch in Perónist terms, stating in 1991, "to liberate our country from its backwardness, what is required is not to be less of a Perónist, but more of a

Perónist," by which he must have meant more power focused on one individual as he distanced himself from his party and ruled increasingly by decree.[52]

Finally, as the Argentine economy began to show stress in 1999, President Fernando de la Rúa and the Argentine Congress' response was to award sweeping powers to returning Minister of Economy Domingo Cavallo and wait for another magic trick from a man "voracious and insatiable (whose) ambition could save the country."[53] To be sure, all of these figures also issued economic plans. Nevertheless, the belief that their sheer existence could solve the fiscal problem shielded them from facing tough fiscal decisions that would have helped Argentina manage its foreign debt.

B. Paying for Populism

It would be easy to blame Argentine fiscal irresponsibly on populism, and at times it seems the word is used as a catchall explanation for Argentina's woes. This section considers populism as an explanation for fiscal irresponsibility with an important caveat: by the time Alfonsín and Menem entered office, the effects of Perónist populism were deeply ingrained into the Argentine economy. Under Perón's Corporate State, an endless array of key industries had already been nationalized. Others enjoyed "easy credit, high protective tariffs, and a variety of subsidies."[54] These industries were over-employed, inefficient drains on the public budget. As a result in the 1980s, 83% of Argentines lived in urban areas, and 87% were employed in non-agricultural professions.[55] Any fiscal consolidation that threatened these workers would be very painful to Argentina's bloated public sector. Thus, it is too easy to say that populism alone prevented Alfonsín and Menem from reigning in public spending. But any attempt to adjust the existing structure was either viewed as political suicide (in the case of Alfonsín), or would lead to a stiff recession, as occurred following Menem's reforms.

It would not be easy to unwind the corporatist economy. In a telling passage referring to the era of military rule (1976-1983), Conde writes that the military eschewed fiscally austere measures that could "cause unemployment, and lead to more upheaval and workers to joining those involved in political violence."[56] This argument suggests that even a military government that ruled by brute force and terror feared the consequences of fiscal contraction.

If the military government worried about imposing fiscal reforms, one can understand if Alfonsín's government "did not think it was strong enough…to overcome the iron opposition" of government unions opposed to fiscal austerity.[57] Despite the pressing need to finance the external budget, Alfonsín could not face down

> the ruling elites…in control of government owned enterprises; business sectors that benefited from government subsidies or inflated sales to the public sector, or who made money from minimally productive businesses that could only have survived in the shelter of strong protectionist and interventionalist polices; corrupt officials who got rich from the system, and many more.[58]

The refusal to do so led to deteriorating fiscal conditions and it rendered external debt unsustainable, thus undermining various variations of the *Plan Austral* which aimed at curbing inflation.

Perhaps we would expect Menem's experience to disprove the populist interpretation. After all, he bucked the corporatist trend, privatizing many of the nation's most vital industries. However, Menem would pay the price of trying to dismantle an economy based on public employment. Lacking the political framework, global sophistication and competitiveness, many of Argentina's key private firms went bankrupt in the 'Menem Decade,' and this was a factor in the recession that began in 1999.[59]

Furthermore, populism, to the extent that the term refers to politicians bending and placating to popular will, may explain Menem and de la Rúa's stubborn unwillingness to consider easing off convertibility. The quarters of high growth between 1996 and 1997 may have offered the opportune time for such a transition. But Menem had already parlayed the success of convertibility into a second (previously unconstitutional) presidential term. Not only did the payouts required to win political support for this constitutional amendment challenge pledges of fiscal austerity, but it also opened the door for a potential third Menem term and decreased the likelihood that he would modify the very popular convertibility plan.[60]

The dogged allegiance to convertibility stifled the current account balances with a negative effect on fiscal accounts. According to Lucas Llach, even after privatization wages constituted a disproportionate share of the government's bill, so the overvalued peso was a drain on the government balance.[61] Tax reductions meant to subsidize struggling exporters also limited government revenue intake.[62]

Furthermore, while the privatizations provided short term fiscal relief, the overall fiscal pressures inherent to populism remained. Argentina ran fiscal *deficits* every year of convertibility except 1993.The fiscal situation was further deteriorated by Menem's election year spending in 1998, and the inability to rain in provincial government spending, most notably in the province of Buenos Aires which itself spent US$10bn in 1998.[63] Rather than using the boom years to generate a fiscal surplus, the Menem government financed expansionary fiscal policy with more debt. It was government spending that drove the 10% increase in government debt from 1992 to 1998.[64]

All told, Menem made headlines for his liberalizing economic policies, but the underlying populist structure of the Argentine economy, along with Menem's own tendency towards populist fiscal spending partially explains the inability to fiscally consolidate, despite advantageous national growth statistics that should have made the debt manageable.

5. Conclusion:

This paper has argued that the Argentine economic events of the 1970s to year 2002 were part of a 30 year battle against inflation, capital flight and foreign debt. The paper reviewed two major efforts to address these conditions, namely the *Plan Austral* and the Convertibility Plan. Both set inflation as their main target, and the two proposed quite different methods to combat it. Yet they both failed. While both could contain inflation in the short term, neither could find a longstanding solution for financing international debt, mostly due to an inability to maintain fiscal order.

In some sense, the thirty year span fits because it encompasses Argentina from the death of Perón to the epic 2002 collapse. But in another sense, the time span is arbitrary. Argentine fiscal woes have led to defaults since the time of Hipólito Yrigoyen,[65] and there is no definitive reason to believe that this chapter in Argentine history has passed.

Under current President Cristina Fernández Kirchner (2007 -), fiscal spending has again become a primary strategy to woo voters and maintain support. She has expanded pensions and increased welfare benefits. Her fiscal expansion is supposedly being financed by strong commodity prices and redistributive taxes levied against agricultural exporters. But, just as the models Alfonsín, Menem and de la Rúa used to expand fiscal spending proved unsustainable, so might this one. Commodity prices are historically finicky, and the European Sovereign Debt Crisis threatens every day more than the next to drag the world economy into a second recession.

Such a recession could put downward pressure on Chinese and developed world demand for Argentine exports. Meanwhile, inflation is estimated at over 20%,[66] and by the state's own admission, capital is flowing out of the country at a pace of US$2bn per month. The current account – the same current account expected to finance fiscal expansion – is dwindling. The fact that Argentina recently issues laws restricting the exchange of dollars for pesos[67] does not exactly smack of confidence.

Whether the Argentine economy unwinds into another period of crisis remains to be seen. However, it is unfortunate that now 35 years since the demise of Juan Perón, Argentine leaders continue to promote economic models that claim long term growth can be achieved without fiscal responsibility.

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[1] William Smith. "Hyperinflation, Macroeconomic Instability, and Neoliberal Restructuring in Democratic Argentina." In Edward Epstein ed. *The New Argentine Democracy*. (Westport: Praeger, 1992), 51-52

[2] International Monetary Fund, *The IMF and Argentina, 1991-2001*. (Washington, D.C., International Monetary Funds, 2004), 26.

[3] Kieler Studien. *Argentina: The Economic Crisis in the 1980s*. (Germany: J.C.B. Mohr Tubingen, 1985), 8.

[4] Studien, 9.

[5] Roberto Cortés Conde. *The Political Economy of Argentina.* (New York: Cambridge University Press, 2009) 249.

[6] Conde, 268.

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[8] Smith, 39.

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[15] Lewis, (*The Agony),* 54.

[16] Heyman, 286.

[17] Smith, 28.

[18] International Monetary Fund, 11.

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[21] As it did between 1991 and 1997, except for four quarters during the Tequila Crisis.

[22] Blustein, 59-60.

[23] Padma Desai, *From Asia to Argentina: Financial Crisis, Contagion and Containment*. Princeton: Princeton University Press, 2003, 209.

[24] Smith, 50.

[25] Blustein.
[26] Paul Lewis. *The Crisis of Argentine Capitalism.* (Chapel Hill: The University of North Caroline Press, 1990), 478.
[27] Canitrot. "Economic Policy Under Conditions of High Uncertainty: The Case of Argentina in the 1980s," 243.
[28] Canitrot, 244.
[29] Joseph Haveli. "The Argentina Crisis," *The Monthly Review Vol 53, Issue 11.* (April, 2002). Available online at http://monthlyreview.org/2002/04/01/the-argentine-crisis.
[30] Haveli.
[31] Conde, 274.
[32] International Monetary Fund, 12.
[33] Bluestein, 30.
[34] Smith, 51.
[35] Conde, 275.
[36] Smith, 36.
[37] William C. Smith, 30.
[38] Mario Damill and Roberto Frenkel. "Hiperinflación y establización. La Experiencia Argentina Reciente," in Gui,kkermo Rozenwurcel ed. *Elecciones y Política Económica en América Latina*. Buenos Aires: Editorial Tésis S.A.
[39] Canitrot, 243.
[40] Conde, 275.
[41] The World Bank, 180.
[42] The quasi-balance refers to transfers between the public and private sector that are not reflected in budgetary quotes, but can have a significant (if hidden) effect on macroeconomic footing. For further explanation see: Robert Tchaidze. "Quasi-Fiscal Deficit in Nonfinancial Enterprises." *IMF Working Paper, WP/07/10*, 2007.
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[44] The World Bank, 180.
[45] Jorge Schvarzer. "The Costs of the Convertibility Plan: The Economic and Social Effects of Financial Hegemony," in Edward Epstein & David Pion-Berlin ed. *Broken Promises: The Argentine Crisis and Argentine Democracy*. (New York: Rowman & Littlefield Publishrers, Inc, 2006), 73.
[46] The International Monetary Fund, 4.
[47] International Monetary Fund, 19.
[48] Blustein, 49.
[49] Bluestein, 48.
[50] Conde, 255.
[51] Canitrot, 80.
[52] Javier Corrales. *Presidents Without Parties: The Politics of Economic Reform in Argentina and Venezuela in the 1990s*. (Pennsylvania: Pennsylvania State University Press, 2002), 173.
[53] Bluestein, 119.
[54] Paul Lewis, 2010., 21
[55] Lewis, 493.
[56] Conde, 254.
[57] Balze, 69.
[58] Balze, 69.
[59] Lewis, 2010, 108.
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[61] Lucas Llach. "A Depression in Perspective: The Economics and the Political Economy of Argentina's Crisis of the Millennium," in Flavia Fiorucci and Marcus Klein ed. *The Argentine Crisis at the Turn of the Millennium*. (Amsterdam: Aksant, 2004), 52.
[62] Llach 53.
[63] Blustein, 53.

[64] Christina Daseking, Atish Ghosh, Timothy Lane and Alun Thomas. *Lessons the Crisis in Argentina*. (Washington, D.C., International Monetary Fund, 2004), 5.

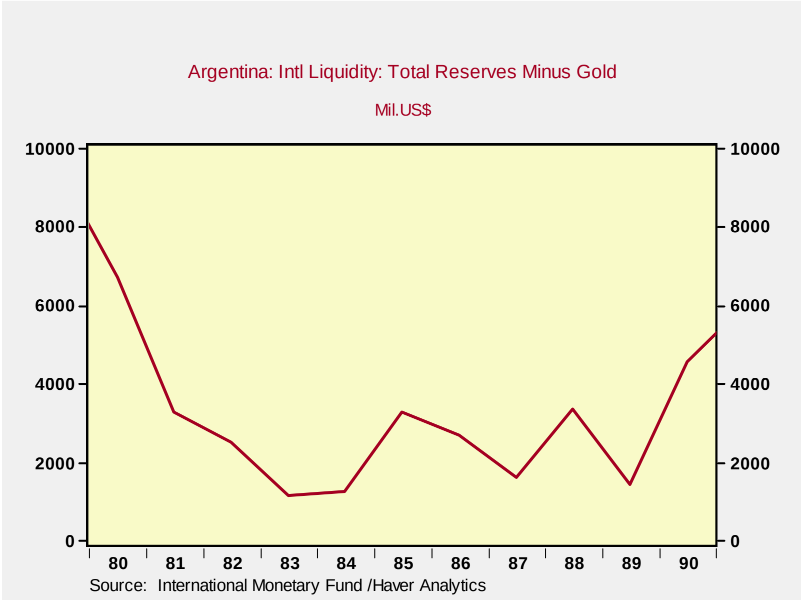
[65] See Smith, *Authoritarianism and the Crisis of the Argentine Political Economy*, 21.

[66] The Economist. "Argentina's Presidential Election: The Widow Takes it All." *The Economist* (October 22nd, 2011).

[67] The Economist. "Currency Controls in Argentina: Unfree Exchange." *The Economist.* (November 5th, 2011)

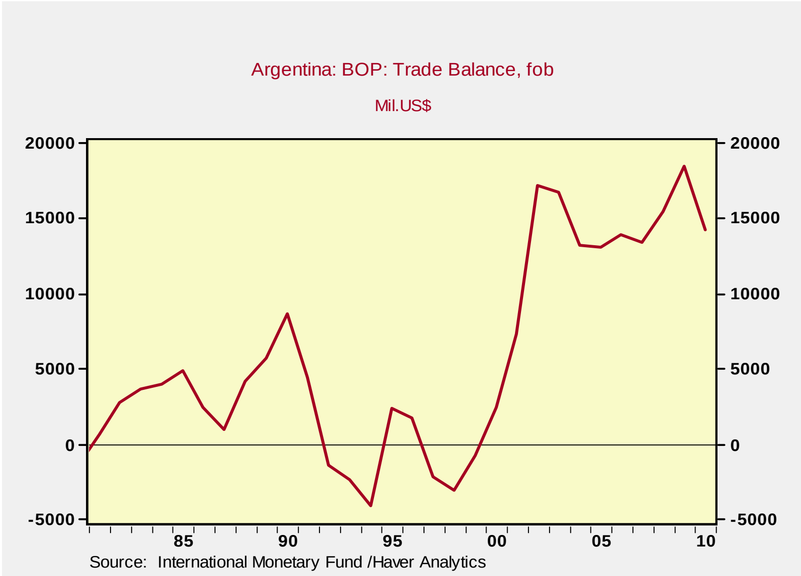
6. Appendix

Figure 1



Dwindling access to hard currency forced the Argentine government to monetize debt payments in the 1980s

Figure 2



Trade surpluses were unable to finance fiscal deficit in the 1980s, and even less so given the overvalued peso in the 1990s

Figure 3

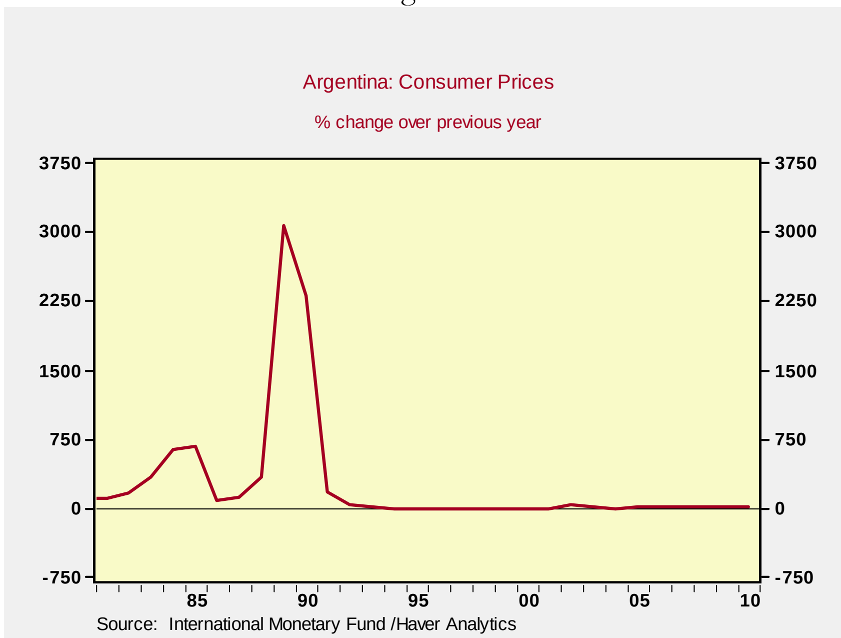
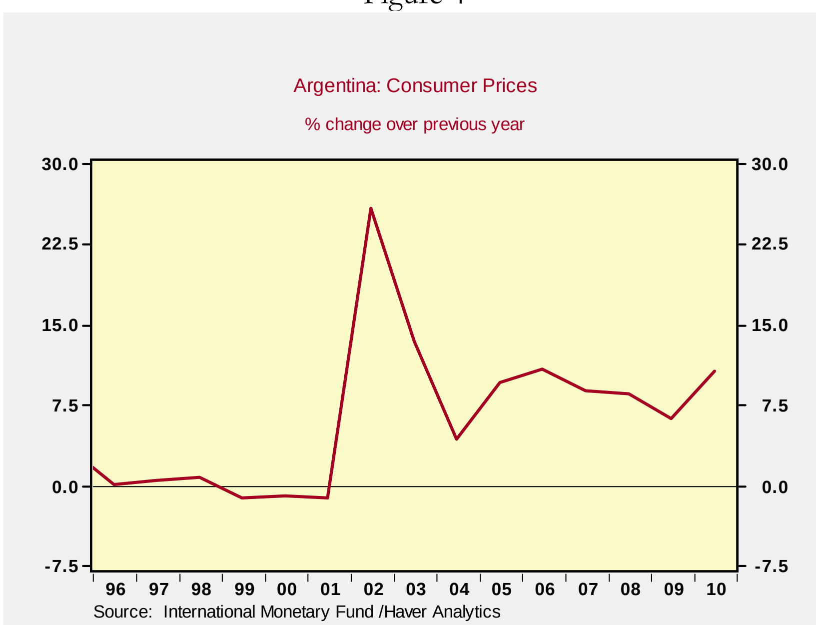


Figure 4



Inflation was a traumatizing factor during the 30 years crisis. While the inflation of 2001-2003 seems to pale in comparison to that of the late 1980s, the devaluation of 2002 was devastating for families and firms that had borrowed in dollars under convertibility.

Figure 5

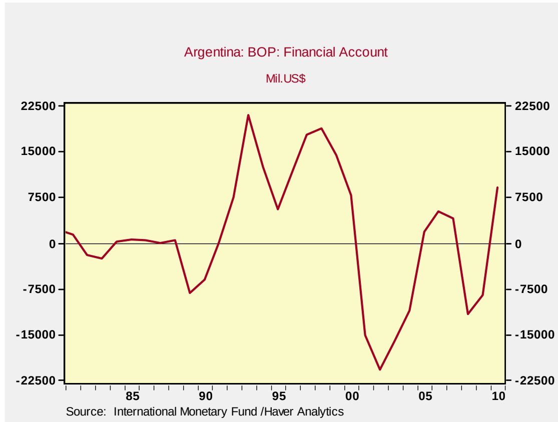


Figure 6

Figure 7

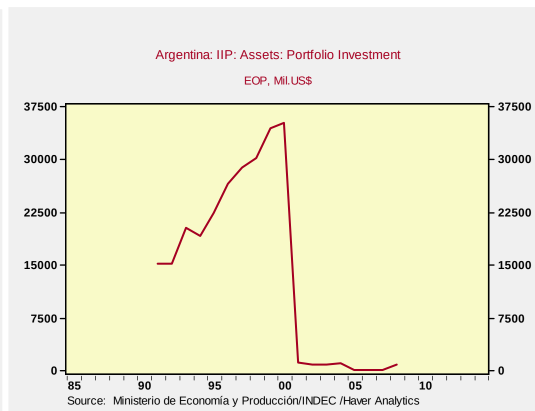
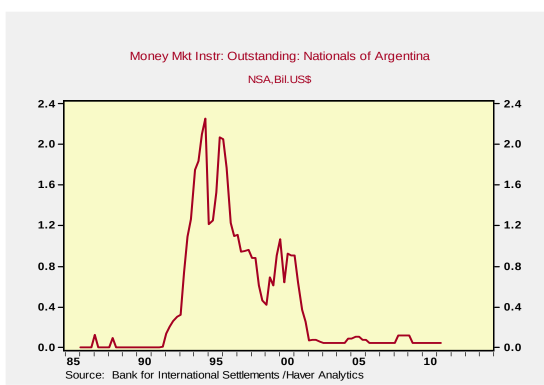


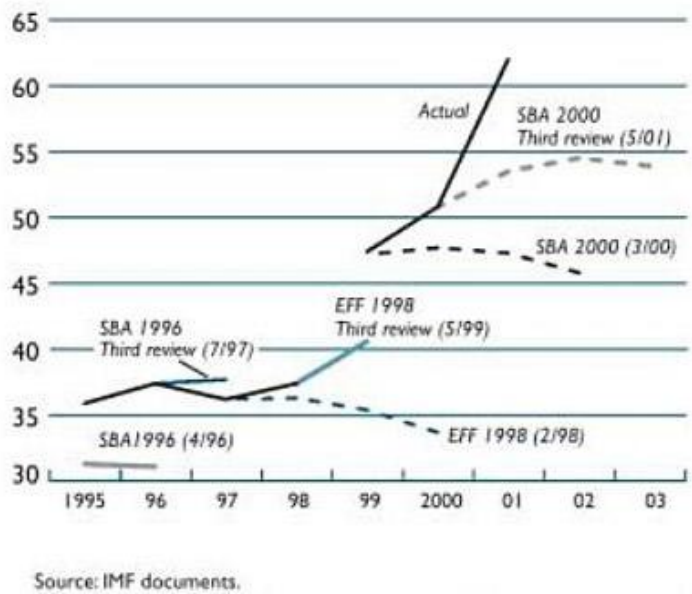
Figure 8



These graphs demonstrate the increasing reliance on international capital inflows to finance Argentina in the 1990s. Such flows can disappear just as fast as they build up.

Figure 9

% Debt to GDP Ratio:
Actual vs. IMF Expectations



Given the trade deficit and the Argentine recession, debt financing became a ticking time bomb for Argentina

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