Argentina Crisis

2001

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Financial Crisis

- Output/employment/fiscal/trade effects.
- Risk of default.
- Effects on future K-inflows.
- Banking sector issues.
- Social costs.
- Contagion effects
Default in Open Economies With K-Inflows

- Imports disrupted
  - Large Effects on Firms
    - Inputs availability affect input mix and production mix.
    - Financial Issues.

- Political backslash against free market and free trade.
Argentina
Some History

- Rich Natural Resources
- High Human Capital
- Reasonable Infrastructure
- Great Performer in early 1900’s.
- Closed economy/populist policies 1945-55
- Fiscal Problems, High Inflation, Macro Instability 70-80’s
Reforms in the 90’s

• Opening, Privatization, Financial Reform
• Currency Board (Convertibility Law 1991)
  – Fixed Peso/US dollar exchange rate
  – Pesos issued had to be backed by dollar reserves (fiscal discipline)
• Results:
  – End of Inflation
  – Great Performance 90-98
1999-2001
Deterioration and Crisis: What Went Wrong?

Combination:
- External Shocks
- Peso overvaluation relative to currencies of largest trading partners (from external shocks+currency board)
- Fiscal dynamics (too weak during upswing, problem of provincial budgets, political issues)
- Debt dynamics (unsustainable nature was not addressed)
- Self Fulfillment Pessimism?
External Shocks

- Mexico Crisis 1995 (Argentina recovered)
- Asian Crisis 1997 (↓ terms of trade)
- Russian Crisis 1998 (K-flows dried out)
- Brazilian devaluation January 1999
- Euro depreciation against dollar 2000
- World recession 2001

Country risk ok until January 1999
(similar to Mexico)
Fiscal issues/Debt

- Circumvention of currency board implicit fiscal discipline through the issuance of quasi-moneys by both provinces and federal government.
- Interest payment Brady Bonds negotiated in 90’s (↑ interest rate increased cost of servicing foreign debt).
- After Russian crisis: ↑ interest rate in new debt
- Declining tax revenues, ↑ debt
- Attempts to collect more (↑ taxes in midst of recession) may have backfired
1999-2001

- Declining output
- Increasing unemployment
- K-outflows
- Decrease in reserves
- Decrease in deposits in banking system
December 2001/Jan 2002

- December 2001: Frozen Deposits (corralito)
- Political Crisis
  - Change of 4 presidents
  - Riots, middle class protests
  - Society’s negative view of politicians ↑
- Default
- Devaluation/Currency board abandoned
- Pesification
- IMF wants to see a feasible plan before granting loans
Output Growth: One Aggregate indicator

LATIN AMERICA AND THE CARIBBEAN: GROSS DOMESTIC PRODUCT*
(Percentage variation with respect to the same quarter of previous year)

Source: ECLAC, on the basis of official figures.
*Includes Argentina, Brazil, Chile, Colombia, Mexico, Peru and Venezuela.
LATIN AMERICA AND THE CARIBBEAN: STOCK-MARKET PRICES AND CAPITAL INFLOWS

Source: ECLAC, on the basis of figures from the International Monetary Fund and the International Finance Corporation.
GDP growth

<table>
<thead>
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<th>Year</th>
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<td>1992</td>
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<tr>
<td>1993</td>
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<td>2001IV</td>
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Source: ECLAC, on the basis of figures from official sources and from the International Monetary Fund.
International Reserves and Total Deposits of Non Financial Private Sector in millions of dollars

Source: Centro de Economía Aplicada -UCEMA en base a datos del BCRA.