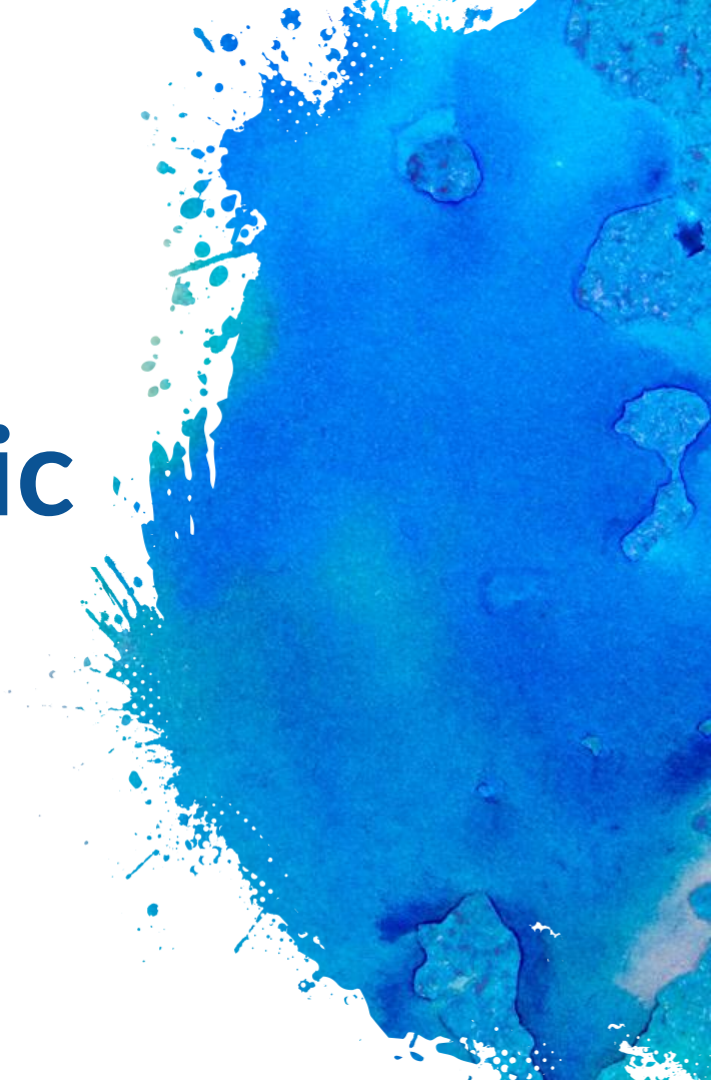


Argentina's economic crisis 1998-2002

EE452

International Monetary Economics
Semester 2 Academic Year 2018



Agenda

- Introduction
 - Hyperinflation 1983
 - 1991 Convertibility Plan & Washington Consensus by Carlos Menem
- Crisis
 - Factors crisis
 - What did Crisis do?
 - IMF Roles
- Recovery



The background features a vibrant, abstract composition. On the right side, there are various shades of blue and teal, with some darker, almost black, organic shapes that resemble ink splatters or biological cells. On the left side, there is a large, bright white area with a textured, halftone-like pattern. A prominent white brushstroke, resembling a thick line of paint, runs diagonally from the top left towards the center, separating the white textured area from the blue-toned area.

Introduction

Introduction of the crisis

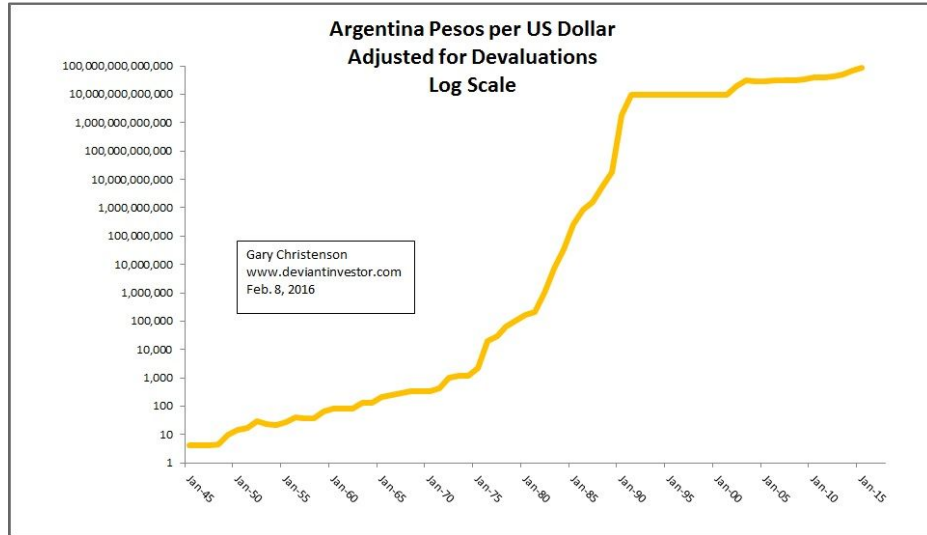
- In the beginning of 20th Century, Argentina was one of the wealthiest countries in the world.
 - Argentina's experienced many years of **Military Dictatorship** until 1983
- Foreign debt increased to \$45 Billion, industrial production decreased by 20%, real wage fall by 36% of their purchasing power and unemployment of 5%
- Election of president, **Raul Afonsin** introduced new currentcy "**Argentine Austral**" to stabilize the economy
- The plan collapsed in 1987, left with increased amount of debt, real wage decreased and **Hyperinflation**

Hyperinflation 1989



Result of Hyperinflation Problem

- Rapid loss in currency value
- Income poverty rates increased from 27% in 1980 to 47% in 1989



Source: Deviant investor

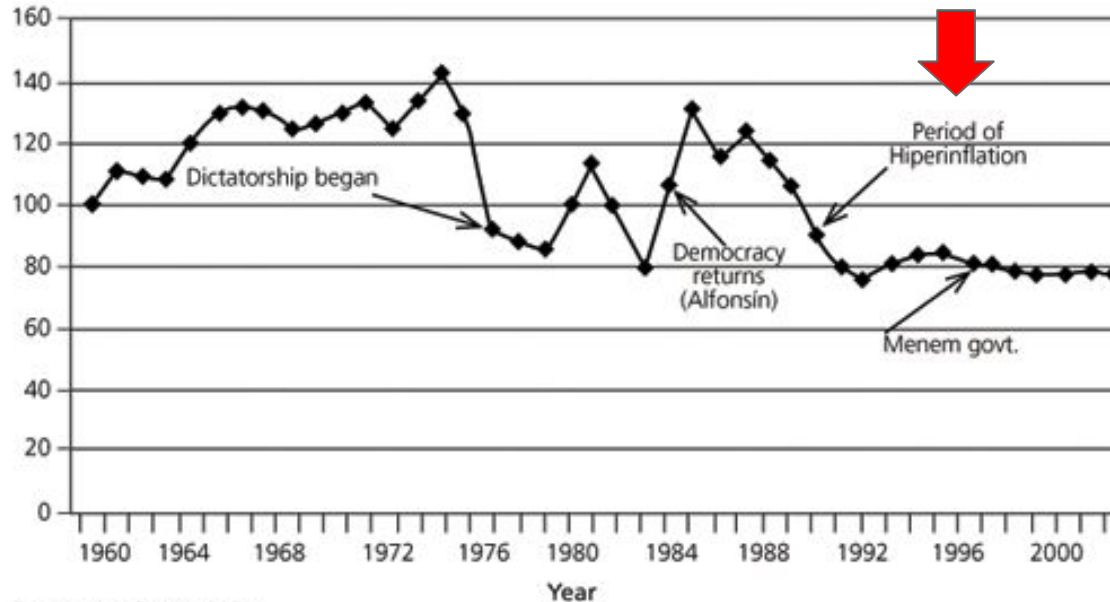


Source: World Bank

Result of Hyperinflation Problem

- Prices skyrocketed and minimum real wage floored

Figure 2: Industrial Real Wages 1960-2002 (1960=100)



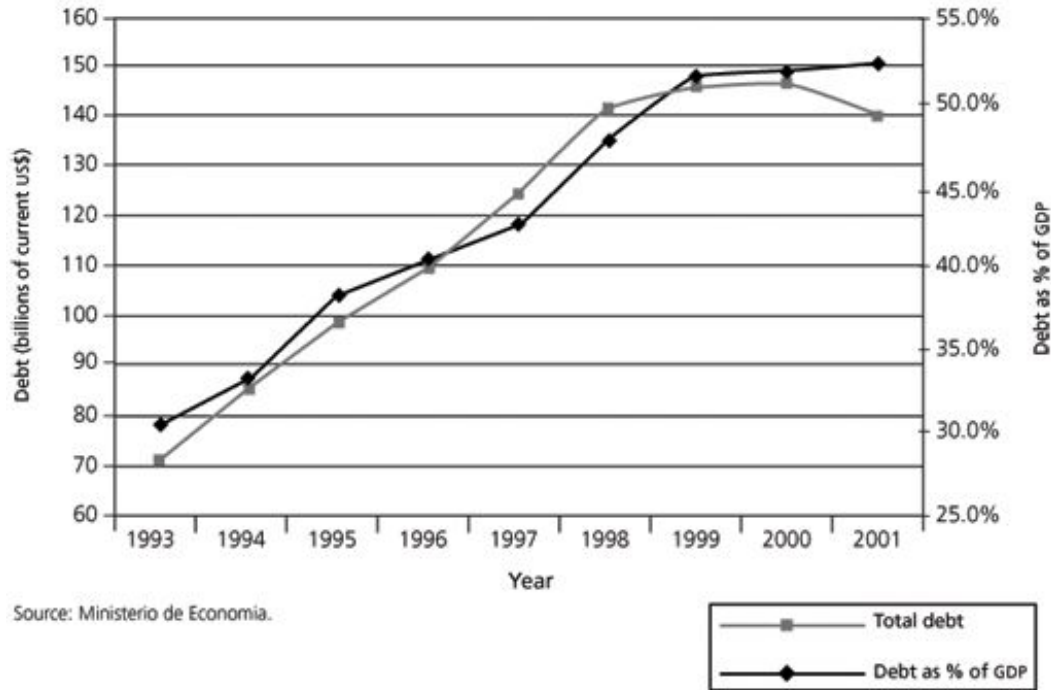
Source: Inigo Carrera, 2000.

Source: researchgate.net

Result of Hyperinflation Problem

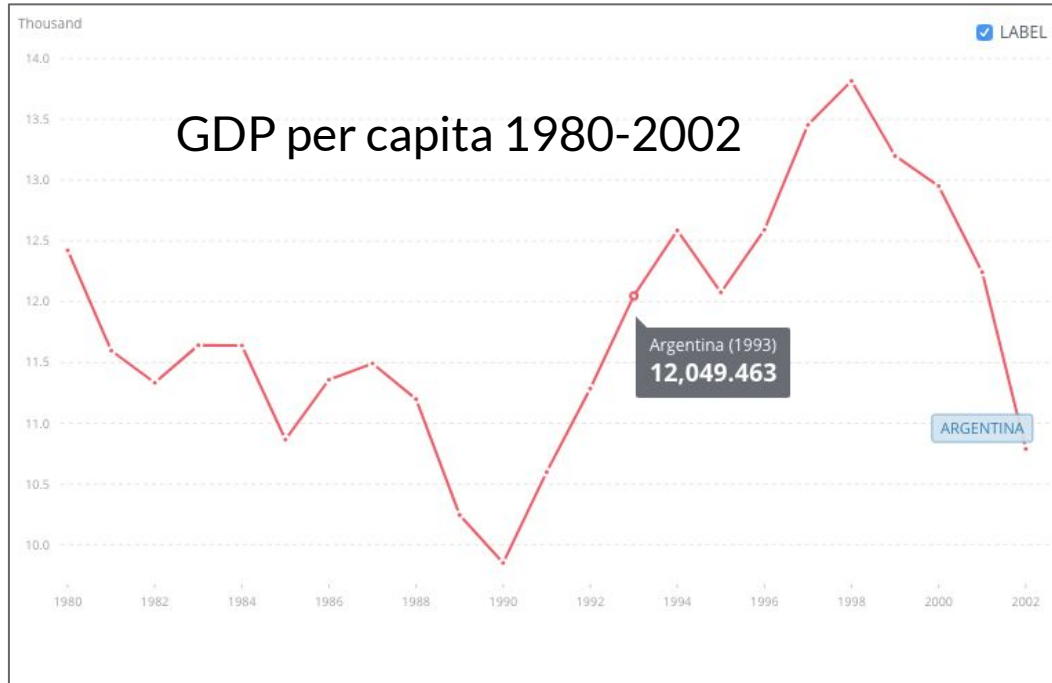
- Unserviceable debt

Figure 3: Argentina's foreign debt (1993-2001)



Result of Hyperinflation Problem

per capita GDP had fallen by over 20%.



Source: <https://data.worldbank.org>

**1991 Convertibility Plan and
Washington Consensus by
Carlos Menem**



First Plan : Washington Concensus by Carlos Menem

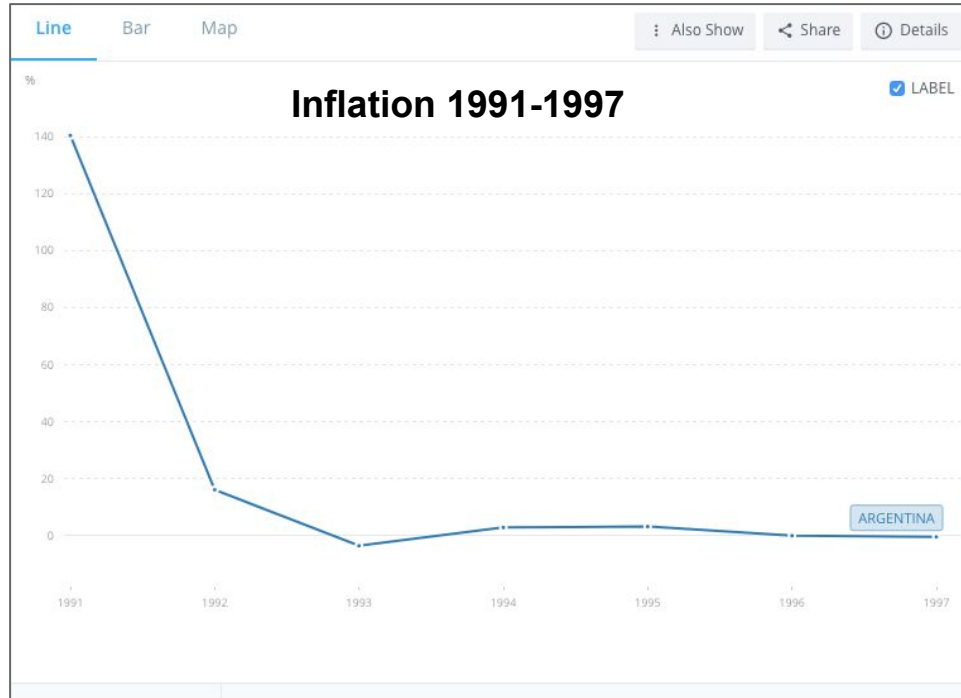
- Plan for Economic stabilization and Liberalization
- The reforms included the privatization of state owned enterprises
- Lower trade barriers and state reform
- Encouraged foreign investment and infused the country with cash to finance its fiscal deficits
- Reduce tarriff

Second Plan : Convertibility Plan of 1991

- Fixed the Argentine peso one-to-one to the US Dollar
- Argentines could now freely convert their pesos into dollars.
- The regime intended to stabilize the peso, encourage both foreign and local investment, and foster sustained economic growth.
- Limitation : Lack of independent monetary policy, Central Bank cannot act as a lender of last resort

Effect of the regime between 1991-1997

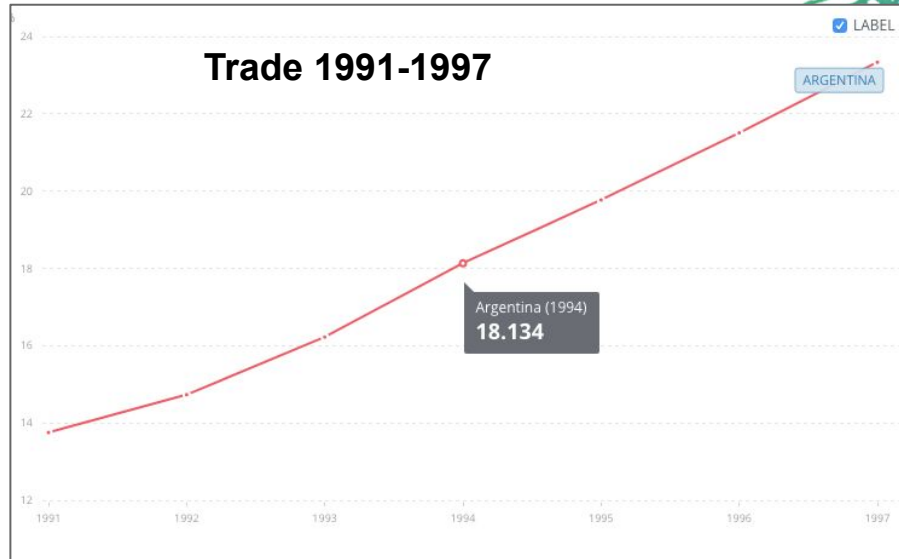
- Had successfully brought down from more than 3,000% in 1989 to 3.4% in 1994.



- Achieve high world prices of primary products

Effect of the regime between 1991-1997

- International trade also increased dramatically
- Imports increased from US\$11.6 billion in 1991 to US\$32.3 billion in 2000. Likewise, exports also increased from US\$12.1 billion in 1991 to US\$30.7 billion in 2000.



The background is an abstract composition of textures. On the left, there is a large white area with a fine, dotted pattern. This transitions into a diagonal band of teal and light blue. The right side of the image is dominated by a deep, vibrant blue with organic, marbled patterns and some darker, almost black, spots. The word "Crisis" is centered in the white area on the right, written in a clean, sans-serif font.

Crisis

Factors causing the crisis

- Fixed exchange rate between peso & USD (Peso convertible)

- × international exchange rate was fixed at 1 peso = 1 US dollar
- × When US dollar appreciate >> Argentina would suffer from trade deficit
- × Peso exchange rate was higher than it should be (Overvalued)

- Excessive borrowing and corruption (Carlos Menem)

- × high national debt



Factors causing the crisis

- Fall in government revenue

- × Lower exports due to appreciation of US dollar and Mexico and Brazil crisis
- × Tax evasion and money laundering
- × Brazil devalued its real in 1999

- Contrationary policies from IMF's instructions

- × decrease government spending



What did the crisis do?

- Stagnant economy
- Rapid government deficit and large public debt
- Increasingly high interest rates
- Borrowing contract with IMF led to restrictive policies
 - Reduced government budget
 - Lower benefit of social security
 - Lay off government employees
- Loss competitiveness in exports
- High unemployment and riot

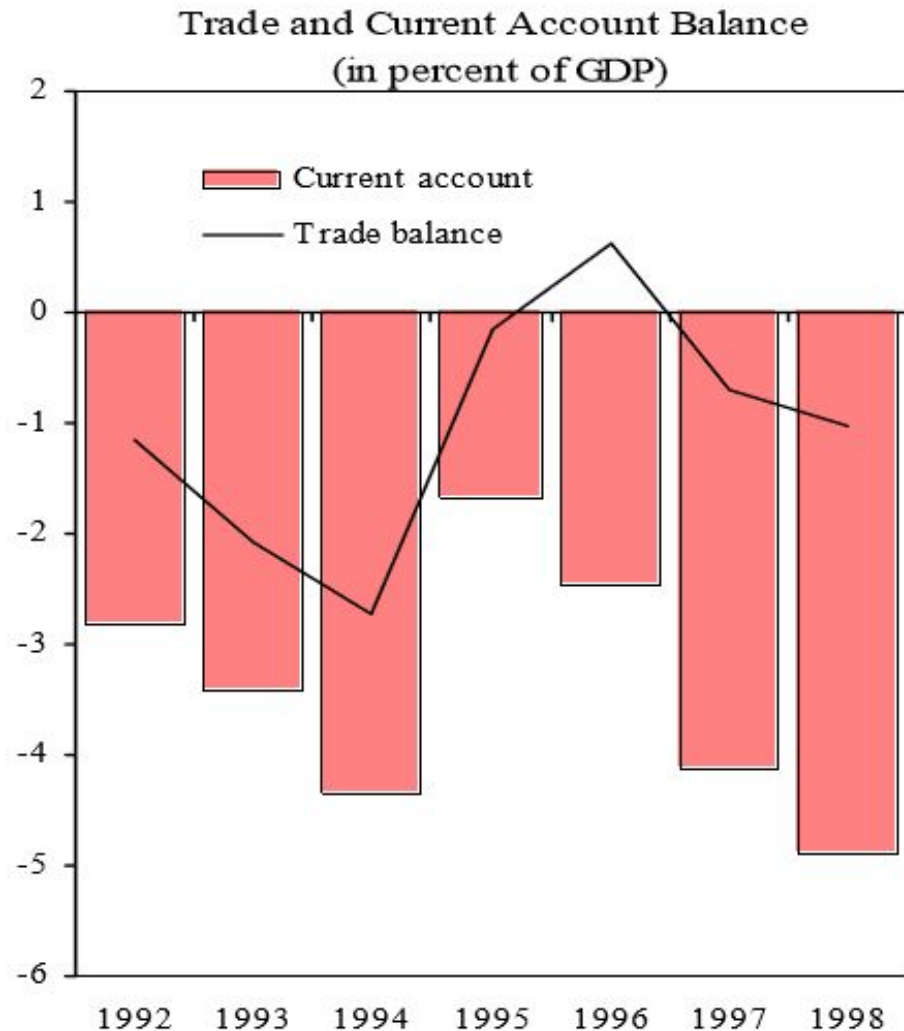


How did it 'start'?

Before the crisis set in, Argentina already had significant current account deficit.

This in itself was not a red flag, especially when putting the convertible plan into the account.

Source: IMF, World Economic Outlook



There were even early concerns about huge conversion from peso to dollar when dollar reserve was still plentiful.

The government even promised to use contractionary monetary policy (lower money supply & raise interest rate) to counter this.

So what happened?...

To simply put...they were too optimistic.



The government did not incline to push the interest rate high enough in response to economic weaknesses and situations.

Deficit and Debt remained high and rising...creating more nervousness about the long term exchange rate.

Adding that with external shocks and crises

... the red flag became crimson...



Result?

- Uncompetitive exports
- Excessive outflows
- Piled-up external debt

And eventually led to a complete distrust in the economy...



Uprise and Riots

The continuously aggravated situation evoked unsettling premonitions among the population and created discontent on the government.

When displeasing policies were enacted, their patience was exhausted.

- Fernando De la Rúa's tax increase policy in January 2000
- A spending cut policy in May 2000
- Domingo Cavallo's tax increase policies in 2001
- National partial deposit freeze in December 2001 (Withdrawing is limited to \$250/week to prevent bankrun)



High debt and borrowing cost

Loss in competitiveness
Instability in economy
Political conflict



...lead to...

Higher risk!!!

Therefore... Interest rates for borrowing rose!

Added with the tax increase policies in 2000 and 2001, confidence in government finance was reduced. Said policies resulted in unmet revenue goals, leading to further loss of confidence...

In July 2001, Argentina's credit rating was reduced, resulting in a higher interest rate since investors feared the possibility of a default.

“Debt Trap”

High Debt → Loss in Confidence → Higher interest rate → **EVEN MORE DEBT!!!**

This inevitably led to a government default in December 2001...

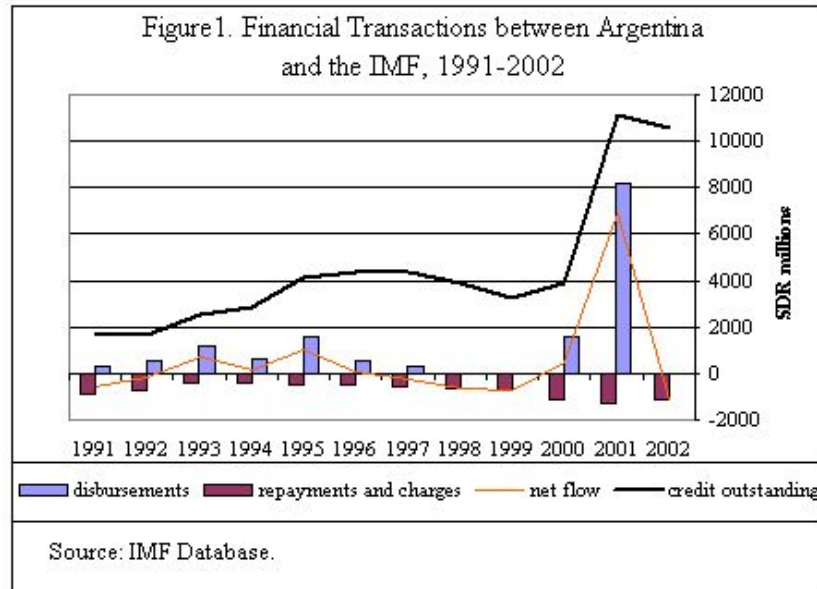
And **the BIGGEST sovereign debt default** at the time at that.

(A whopping \$155 Billion default...)



IMF role

- Engaged in Argentina since 1991 “Convertibility plan”
- IMF supported program **but fail**
- provide extensive technical assistance(TA) during the period(Fiscal,monetary and banking areas)



Source: International Monetary Fund

The background features a complex, abstract composition. On the left, there is a large, bright white area with a fine, dotted or halftone texture. This transitions into a vibrant blue field on the right, which is layered with various textures, including what appears to be a marbled or watercolor-like pattern. The word "Recovery" is printed in a clean, white, sans-serif font, centered horizontally in the blue section.

Recovery

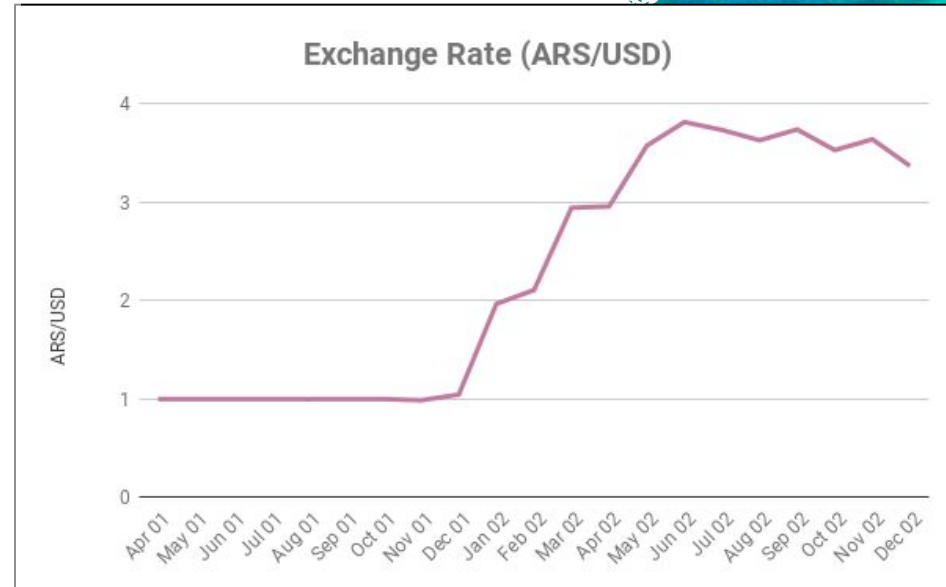
Recovery

- **Prevent capital outflows**
 - by freezing bank accounts for 12 months
- **Pesofication**
 - Converted dollar loans to Peso
- **Imposition of export taxes**
 - on the main exports of the country
- **Debt renegotiation**
 - pointing towards a substantial debt reduction
- **Encouraged Import substitution and accessible credit for businesses**



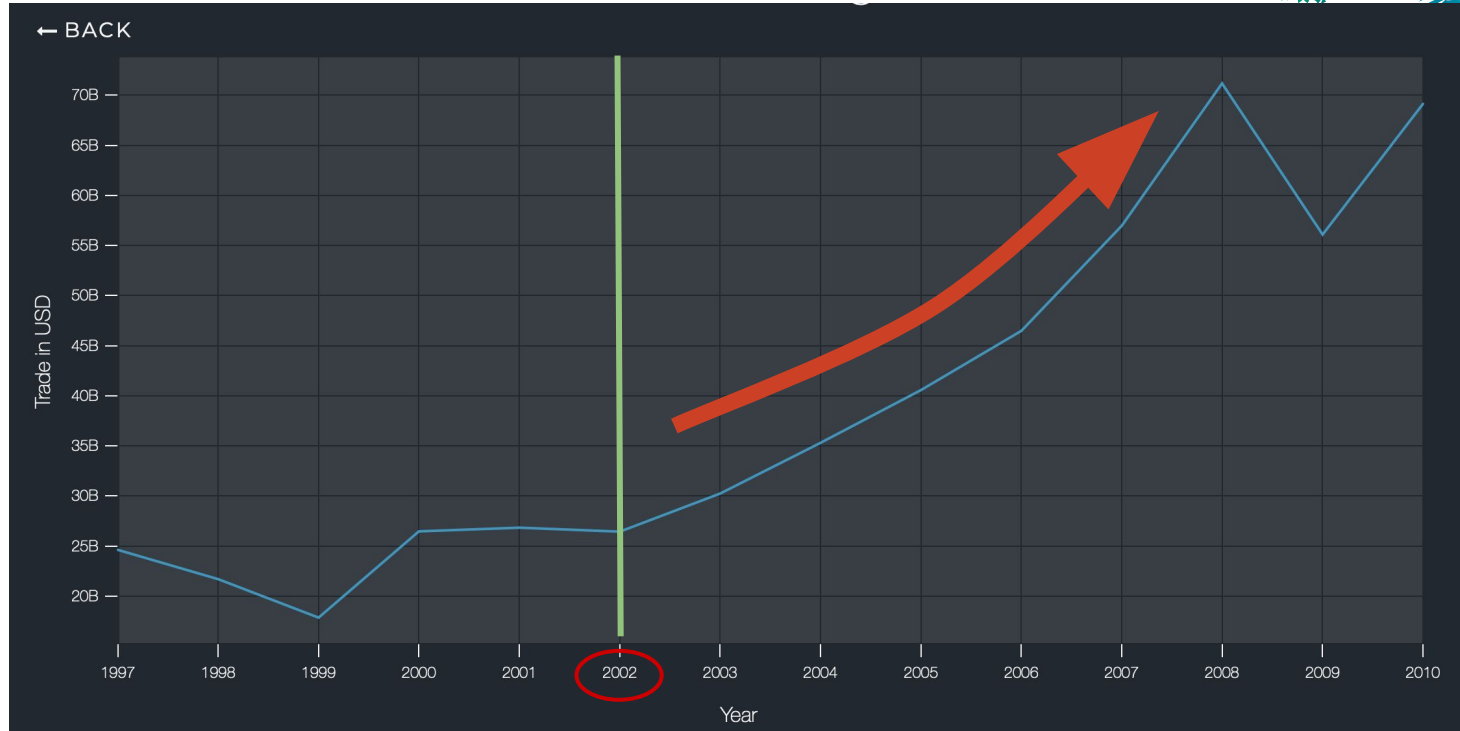
Recovery

- **Abandoned the “Convertibility Plan”** in January 2002
 - Caused **devaluation** in Argentina peso
 - Less importation
 - Export became more competitive
 - More domestic production



Source : Wikipedia

Argentina Exportation



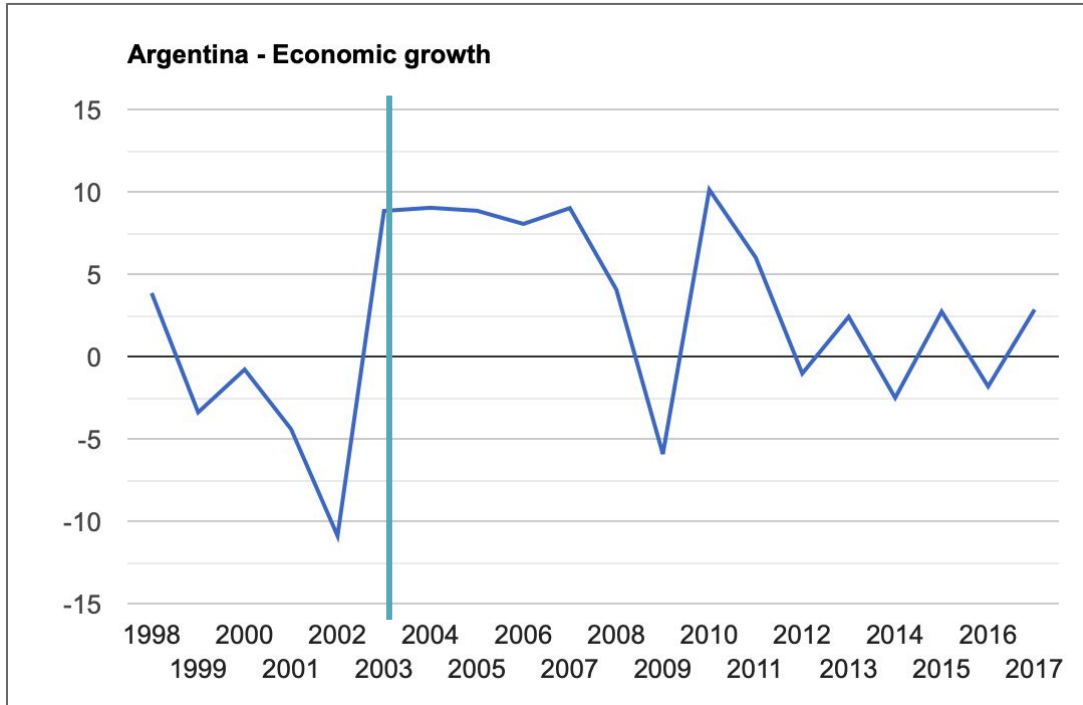
Source : OEC

Why didn't Argentina devalue peso sooner?

1. Fear the return of extreme inflation
2. Concerns about the possible high default of USD dominated debts
3. Prediction of USD depreciation



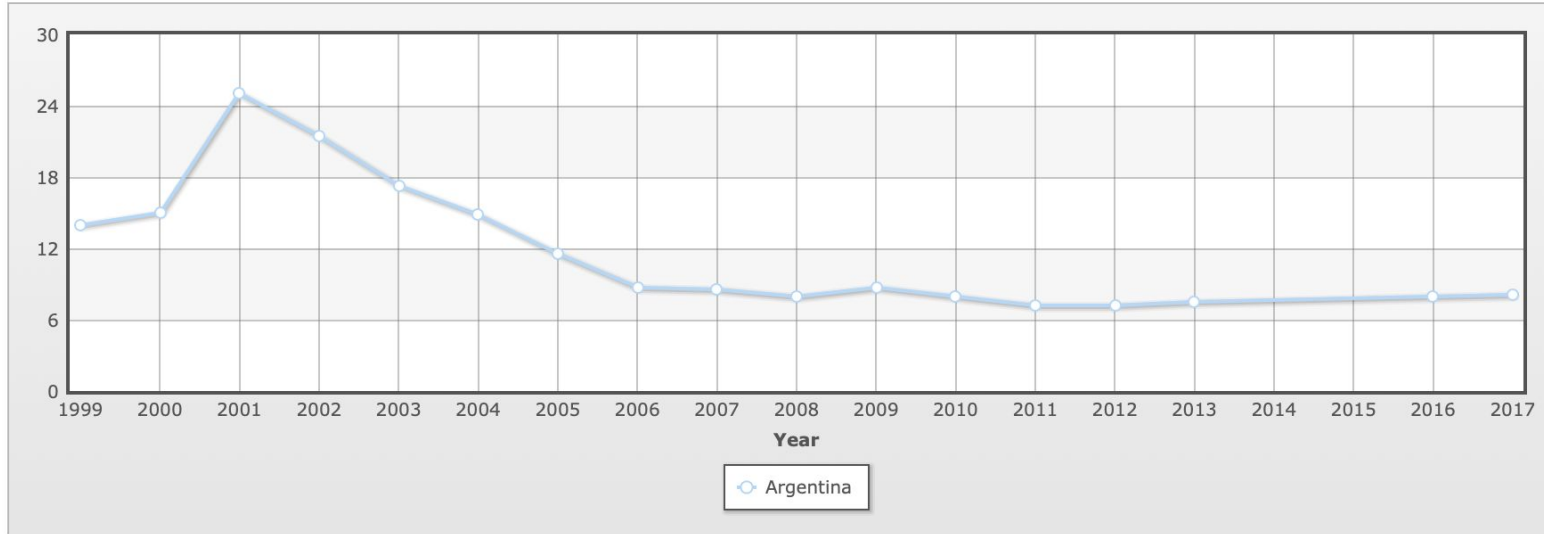
Economic Growth (%)



Source : The Globe Economy

Unemployment Rate

Unemployment rate (%)



Country	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2016	2017
Argentina	14	15	25	21.5	17.3	14.8	11.6	8.7	8.5	7.9	8.7	7.9	7.2	7.2	7.5	8	8.1



Q&A

Member

Nok	Jeamteerasakul	5904641155
Pantita	Sukumdhanakul	5904641189
Boonyaporn	Chamnankit	5904641197
Chirapak	Phromsri	5904641254
Nattacha	Lurpromchai	5904641650
Thita	Wongwan	5904641684