The Argentine Monetary Crisis

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Outline

• Financial History and why the crisis happened.
• What happened during the crisis and what was done?
• What is going on today? The Remedy?
• Future outlook and the lessons we learned.
Financial History and why the crisis happened.
- 1930’s
  Argentina’s Economic Boom
- 1940’s
  Start of Military Rule
- 1972-1974
  Government Returned to Civilian Rule
  Life of Juan and Isabel Peron
• 1975-1983
  – Dirty War
  – Inflation to Impeachment
  – Military back to Power (stabilization)
  – Currency Depreciation
  – Generals Videla, Viola, Galtieri
  – Hyperinflation
  – Falkland Islands disaster, a resignation
  – Victory for the Radical Party (Alfonsin)
• 1985-1988
  – IMF intervention and demands
  – Introduction of Austral
  – Some inflation
  – Return of hyperinflation
  – Menem wins presidency
• 1991-1993
  - New Argentine peso
  - April: Peg to $US
  - Formation of Mercosur
  - Soaring Unemployment
• 1994-1996
  – Interest rate hike in US
  – The Tequila Crisis
  – Heightening interest burden
  – Some market recovery
• 1997
  - East Asian Financial Crisis
  - Slide of Thai Baht
  - Worried investors
  - $US overvaluation
  - Interest payments now in CA
• 1998
  – Financial crisis in Russia

• 1999
  – Financial crisis in Brazil (real collapses)
  – de la Rua becomes President
  – aid seeked from IMF
• 2000
  – Tax increases
  – IMF agreement
  – Government budget cuts
  – Multilateral assistance package by IMF
2001
- IMF augmentation
- Minister of Economy resignation
- Voluntary debt restructuring
- Exchange rate price change
- Cavallo’s plan
- Unions strike
- “Zero-deficit” law announced
• 2001 (continued)
  – IMF reaction to “zero-deficit” law
  – Provincial bonds as scrip to pay salaries
  – Debt swap
  – Run on banks
  – Protests begin
  – IMF withholds payment
  – Announcement on foreign debt repayment
• 2001 (continued)
  – Unemployment at 18%
  – Supermarket looting
  – Rioting from protests, leaving several dead
  – Cavallo resignation
  – de la Rua resignation
What happened during the crisis and what was done?
3 Main Periods

- November 2001-December 2001
- January 2002
- February 2002- November 2002
November 2001-December 2001

- Presidents Meet
- Declining Reserves
- Bank Restrictions
- Strikes and Looting
- Mass Resignations & Market Closures
- New Economic Plan
- Resignation
January 2002

- New Government
- Bank Policies
- IMF Extension
- Meeting With US and IMF
February 2002-November 2002

- Supreme Court Ruling
- Export Tax and Other Policies
- Suspension of Activity
- Protests
- Early Elections
- Default
What is going on today?  
The Remedy?
Argentina’s Re-emergence into Financial Markets

• January 2003
  – IMF approves new $6.6bn loan program

• April 2003
  – Nestor Kirchner wins Presidential Elections with 22% of vote
  – Pledges to take a tougher stance with creditors and IMF
• June 2003
  – IMF begins negotiations for new 3-year deal
• September 9
  – Argentina misses $2.9bn payment to the IMF
• September 10
  – IMF agrees to roll-over $12.3bn in debt payments and Argentina makes payment
• September 22
  – At the annual Dubai conference Argentina asks its private creditors to write-off 75% of the money they are owed
Argentina Today

• January 2004
  – IMF disbursed $330m to Argentina
  – IMF gave positive review of year’s progress

• March 2004
  – Argentina made a $3.1bn payment to IMF on-time, after threatening to delay again
  – IMF agrees to released $3.1bn loan to Argentina without delays similar to December
• In the fourth quarter of 2003 Argentina’s GDP grew 11.3%
• Overall, GDP grew 8.7% in 2003
• The unemployment rate is down to 15.6%
• The inflation rate has fallen to 15.7% from 41% at end of 2002
What Next?

- Restructuring debt
- Argentina owes almost $100bn in private debt
- Needs to negotiate in “good faith”
- Kirchner wants creditors to write-off 75% of debt
3-Year Economic Program

• Goal: establish sustained growth, reduce widespread poverty, reduce debt, maintain low inflation, and strengthen the banking system and investment environment through:
  – Utility Company Reform
  – Fiscal Policy
  – Structural Fiscal Reform
  – Monetary Policy
  – Banking Reform
  – Legal Framework
Future outlook and the lessons we learned.
## Economic Data (1)

<table>
<thead>
<tr>
<th></th>
<th>1999</th>
<th>2000</th>
<th>2001</th>
<th>2002</th>
<th>2003</th>
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</thead>
<tbody>
<tr>
<td><strong>GDP Growth</strong></td>
<td>-3.39</td>
<td>-0.79</td>
<td>-4.41</td>
<td>-11.3</td>
<td>8.7</td>
</tr>
<tr>
<td><strong>Inflation (%)</strong></td>
<td>-1.17</td>
<td>-0.94</td>
<td>-1.07</td>
<td>25.87</td>
<td>15.7</td>
</tr>
<tr>
<td><strong>Unemployment (%)</strong></td>
<td>13.03</td>
<td>14.55</td>
<td>16.4</td>
<td>18.8</td>
<td>15.6</td>
</tr>
</tbody>
</table>
## Economic Data (2)

<table>
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<th>1999</th>
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<th>2002</th>
<th>2003</th>
</tr>
</thead>
<tbody>
<tr>
<td>Public Debt / GDP (%)</td>
<td>42.99</td>
<td>45.04</td>
<td>53.76</td>
<td>111.5</td>
<td>132.9</td>
</tr>
<tr>
<td>CA Balance / GDP</td>
<td>-4.2</td>
<td>-3.12</td>
<td>-1.69</td>
<td>8.6</td>
<td>5.7</td>
</tr>
</tbody>
</table>

--From the Economist Intelligence Unit and United Nations--
Future Outlook

• GDP Growth:
  – 2004: 4.9%
  – 2005: 3.5%

• Inflation:
  – 2004: 6.3%
  – 2005: 6.2%

-- From the Economist Intelligence Unit
Economic situation

- GDP will not return to 1998 level until 2005.
- Inflation continues rising.
  - CA surplus may be erased by inflation
- Fiscal policies remain weak.
Policy-making

• Short term:
  – Monetary policy
  – Tax rates
  – Banking system
  – Foreign debt
Policy-making (continued)

• Long term:
  – Rule of Law
  – Tax strategy
  – Government spending
  – Labor
  – Health care
What might go wrong?

- With hindsight:
  1. Weak fiscal policy
  2. Unfavorable external environment and shocks.
  3. Unsustainable debt dynamics.
Exchange Rate and Shadow Exchange Rate

\[ S = b^H + \lambda w \]

\[ S = b^H \]

ATTACK
What we have learned?

1. Focus more closely on debt dynamics.
2. Currency board are not necessarily as durable.
3. Emerging market countries may need to be more conservative.
4. Making it easier for countries to exit from unsustainable debt dynamics. (A sovereign debt reconstructing mechanism?)
Other Issues

• Would a different exchange rate policy help to avoid the crisis?
  – A floating exchange might help avoid the crisis, but
  – Floating exchange rate is associated with high inflation, extreme depreciation, and economic stability in history.
Thank you!