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IV. ARGENTINA'S EFFORTS AT FINANCIAL RECOVERY AND IMPACTS OF THE CRISIS ON MERCOSUR AND FTAA TALKS

A. Introduction

Jon Mills

Adrian Makuc is a graduate of the University of Buenos Aires who has specialized in international economic relations in both public and private affairs. Since 1998 he is the national director of foreign trade policy in the Secretariat of Industry and Trade in the Ministry of the Economy. He has been engaged in multilateral and bilateral negotiations from that time.

B. *Perspectives on Argentina Today*

*Adrian Jorge Makuc**

The crisis we have today in Argentina is a general one. It is not only financial or economic. I will highlight the nature of the crisis, some background of how we did get to this point where we are at today, some comments about our process of economic reforms, and the liberalization we had in the 1990s, which are very important as a precedent to what is happening today. Finally, I will try to give you an idea of what we are confronting today basically.

The situation of Argentina is not an isolated problem. It is not a problem of Argentina as a country or within Argentine borders. It is a problem that has to do with what has been called in the last years or almost a lot of years by now, the "globalization process."

The globalization process affects many emerging countries, societies, and economies. It also has to do with the role of financial organizations and institutions at the world level. I think this puts on the table the issue of what is the responsibility of leading countries of a developed world, like the United States and the European Union, in shaping international relations? I think we have a great and complex world, interrelated in that many of those problems are of a different nature; not entirely economic, social, or political.

Today, there are wars. There are armed conflicts that are happening as you read this today. We have terrorism we see each morning. These phenomenas are not separated from my point of view; everything has a relation with everything. I do not think this is a simplification. Argentina faces a crisis of historic proportions, because it affects all the social, political, economical, and cultural situations in the status of the country. What the country needs is to find a way out of the crisis by building or rebuilding a social and economic structure, as well as a political

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superstructure to govern the society. We are under a provisional government today.

The provisional government of Argentina is composed of the same politicians that are under question by society; so everything is in a very unstable basis from this point of view. The way the civil society and its political representatives are going to define and agree on the minimum elements required to ensure future governance in terms of political, social, and economic stability is crucial. So I ask: What does Argentina want in terms of social, political, and economic structure? Unfortunately, if I had the answer to this question, I would not be presenting this Article. The problem is that many people in Argentina do not have a glint of an answer and that is worse because in the end I am only one citizen.

Argentina has a history and recent past as a closed economy, and as a society that has a very close relationship and cultural ties with Europe. At the same time, Argentina developed its economic ties with the United Kingdom first, and then the United States. On the basis of agricultural production, we prospered. We were one of the leading countries of the world. This is something that should be remembered today.

In 1910, one hundred years after our independence, Argentina was praised by the rest of the world because of all of its social and cultural achievements. Not the kings, but what they call the infantry from Spain visited the Argentine republic in 1910 to contribute to this anniversary of our revolution when we ousted the Spaniards in 1810. This is quite historical.

Since 1910, Argentina has become this closed economic society in order to develop after a very bad period in the last part of the 1970s and early 1980s. From the economic point of view, our relationship with the world needed to change and become interrelated so that we could have a liberalized economy. This, obviously, coincided with equalization, the internationalization of the economy in general, and the processes that were taking place in different developing countries — the so-called emerging economies of the 1980s. Therefore, we went into that trend.

Argentina changed with the changing government in 1989, in the middle of hyperinflation, in the middle of a financial crisis as well. Government changed in advance in July 1989, instead of December, because the president resigned, unable to deal with the situation. The new president, President Menem, took office and he remained there until 1999.

President Menem initiated a series of reforms. The biggest in terms of economic questions was the fixed relations from the national currency, the peso, with the dollar in 1991. It was a bad conversion from Spanish to English and the fixed exchange rate became 1 to 1. One peso to one dollar.

The exchange rate was matched or paralleled with deregulation of the economy and privatization of state-owned enterprises. This opened the gates to attract as much foreign investment as possible because the economic model was based on free market — the conception that market forces are going to sort out everything and free competition was going to be the best way to modernize the Argentine economy or create new employment and in the end increase the welfare of all our population. In this conception, the idea of limits and regulations was not present. For example, in the case of public utilities, where monopolies were established but given to private companies, the regulations and limitations for the actions of the companies were not there. The public utilities contracts were made with the thought in how much profit the government was going to guarantee and how free the remittance was going to be for those profits abroad. However, this was not the responsibility of providing a good service on the part of the private companies. In the end, the conception was that there was a confidence in a free market that was going to end up in more positive than negative consequences.

By 1996, this was not so. At that time, we were developing integration in the region with other countries associated with Brazil, Uruguay, and Paraguay. We call it MERCOSUR, which was successful in 1991-1998 under the economic minister of Argentina, a star at the international level.

Mr. Cavallo went everywhere and everybody praised him as the representative of the economic success of Argentina. This success started to show problems after 1996 when Mr. Cavallo left us. He was no longer the economic minister, and the new economic minister had to start dealing with the negative consequences of this liberalization, deregulation, privatization process that started in 1991.

The new economic minister took a good part of 1998 and 1999 to adjust to the position. However, 1998 was the last time our economy grew. The recession that currently is going on in Argentina started at the end of 1998. Argentina has already had three and a half years of economic recession. Our GDP fell about 10-20% from that date, up to the end of 2001. Our fiscal problems started to grow at impossible levels and also did our foreign and our domestic debt, public debt, and private debt — mainly denominated in dollars.

When the new government took office at the end of 1999, they thought they could solve the fiscal problems by basically maintaining the fundamentals that the previous economic model had. This was compared of the convertibility, the fixed exchange rate, and all the other elements I very shortly and briefly have summarized to you. This conception was supported by foreign aid in terms of assistance from the financial institutions like the International Monetary Fund (IMF), the World Bank,

and the Inter-American Development Bank (IDB). At the same time, the government tried domestically to make efforts in limiting and restricting the fiscal deficit and basically to contain the growing social effects of this process seen by unemployment, which started to grow around 1997, and currently is at thirty percent of the population.

By the end of 2000, Argentina was developing social programs based on a poverty line to assist the poorer part of the population, which includes low income people who have an income, and other people who do not have an income because they are unemployed. If people are not able to satisfy their basic needs in terms of food, access to medicine, and the apparently elementary needs, they are considered under the poverty line. However, today we have forty percent of the Argentine population in this category.

In March 2001, the economy minister resigned and the minister that was so successful with the convertibility of 1991, Mr. Cavallo, came back to office. He tried to develop a lot of creative and imaginative ideas to save the original creation of the fixed exchange rate, the convertibility, deregulation, and the privatization of the economy. But unfortunately, he was not able to do that.

At the same time, we had a worsening social climate. I told you about unemployment. I told you about poverty. This was combined or growing, and there was a growing sensation in the Argentine population about the lack of credibility of the political class. Politicians are not at all credible in Argentina. When somebody comes to the podium and talks as a politician in Argentina, nobody believes him.

With this mistrust in the government, it is obviously a great problem to propose new projects to the population and to gain support for them. It is also a problem to present the needs of Argentina and expect assistance from abroad, because obviously if a politician in Argentina is not credible inside, he would not be credible outside.

The national government was not capable to gain support from society at the end of 2001. At the same time, capital investors were fleeing our country. We lost \$20 billion from our international reserves in the Central Bank, and \$17.5 billion was transferred from Argentina banks to foreign accounts throughout the world. Apparently, our economic minister was aware because many citizens could not get their money out of Argentina. Not that many citizens had much money, but what little savings they did have could not be put to an off-shore account.

The detonator in December 2001 was when the public was denied access to their bank accounts. At the beginning of December 2001, there was a prohibition for anybody to get their money from their bank. This prohibition was called *coralito* or little corral. The corral was the bank account. You had been corralled in your bank account in terms of disposing

of money. Why do I think this was denied? Because the social crisis was there. It was very big and probably would have exploded because of something else. But what made the government resign? The president resigned in December 2001. I think it was people in the streets. What people were in the streets? It was not only poor people, low income people, but also marginal people coming to the center of downtown Buenos Aires, our capital city. That was almost everybody, because everybody had money in the banks. As President Juan Domingo Peron, a very famous old Argentine politician once said, the most sensitive vice that we have is our pocket. Unfortunately, this prohibition resulted in demonstration, demonstration clashing with police, and police repression which led to the death of twenty people.

After that, President de la Rúa resigned. The resignation of the President helped to calm things down and opened a new process. The new process was, according to our constitution, that after a President resigns, if there is no vice president, then the Congress has to reunite in assembly and elect a new president.

We elected a transitional president that lasted one week. Unfortunately, he thought he could not last or stay in office only on a provisional basis, so he pretended to be in on an indefinite basis. This president had to resign because the provincial governors, the Congress, the opposition party, and all the parties represented in Congress did not give him any more support after the first week. On New Year's Eve, he went to his province in San Luis, and he sat down in his house and he gave a speech to the nation and said, "Well, I'm resigning." He said "I am giving here to the armed forces officer that is with me, my letter of resignation to take to the national capital." That was original.

He went there, secluded himself in his province like a big landlord and just told all the thirty-seven million Argentinians, "You can do whatever you want." The Congress assembly elected a new president on January 2, 2002 and that man is the president we have today — Mr. Duhalde.

Now, we are in a transition period where this president has already scheduled elections for September 2003. We have a new economic program trying to restructure our economy to assist with trying to cover the basic social needs on the basis of savings made internally in Argentina domestically, national fiscal policy and provincial fiscal policies. Lowering the deficit, but ensuring social assistance to the poor, to the basic needs of these people that are under the line of poverty today.

This government has also promised that it would put forward in Congress a political reform bill so as to build again, or rebuild the credibility of politicians in Argentina. From the economic point of view, we have after these last years of recession basically made a growing foreign debt (public

and private), as well as domestic debt denominated in dollars. Our GDP fell about twenty percent since the end of 1998, and so did the production of goods and services in Argentina.

Investment fell roughly forty percent. The per capita GDP fell fifteen percent. Our fiscal deficit in total amounts to something like seven percent of GDP, which in dollars means we have a GDP today with the devaluation that occurred at around \$120 billion. So this deficit must be on the order of \$7 billion.

Our bank deposits fell. We lost about \$20 billion of reserves from our Central Bank. Obviously, this means the end of the convertibility scheme, the fixed exchange rate, or currency board as somebody denominated it in 1991. The basic conditions of convertibility were no longer there in December 2001: There was no access to bank deposits in dollars. There was no change from peso to dollar on a one to one basis and the state went on default of its public debt denominated in dollars.

The basic elements of convertibility have disappeared. Convertibility was abandoned. We have to restore competitiveness of Argentine production.

We have to find a way of restructuring our debt (public and private) denominated in dollars and see if we can pay that debt sometime in the future. Obviously, we have a balance of payments problem. What are the current economic authorities in this provisional government doing? The basic guidelines of the government are:

- 1) A free market economy;
- 2) No state intervention in the economy;
- 3) A free exchange rate that is floating today with some Central Bank interventions in the market;
- 4) The goal of financial recovery and working on the basis of domestic efforts, but also seeking assistance from international organizations like the International Monetary Fund. This assistance we are seeking is obviously based in a domestic effort in terms of fiscal deficit reduction, with a restricted monetary policy to prevent price inflation which is already happening in Argentina; and
- 5) The enforcement of structural reforms that change the political environment and ensure access to education and medical aid to the population in Argentina.

Government has promised to respect private contracts with privatized companies which are public services like electricity, gas, or energy in general. The case of our water company is different because it was subject to another model of privatization and that is a concession for a period of time. The question is that the private contracts with these firms that today are providing public services are being reviewed and the tariffs have been frozen for the time being for four months ending by the month of April 2002.

The government is trying to ensure the social assistance programs on the basis of domestic savings, the national and provincial budgets, and foreign assistance. At the same time, this means if the government is thinking of seeking assistance from abroad, it has to maintain foreign economic relations with the United States and Europe, obviously, in terms of ensuring some possibility of having assistance from IMF. Solutions to the problem include: trade and economic links with our partners in MERCOSUR; the integration process; our negotiations with other countries because we have to seek access to markets. Furthermore, if there is an economic recovery in terms of production of goods and services, domestic consumption may not be enough to ensure a stable recovery.

There are concerns about whether the government will be able to keep in place the social policy that promotes employment, which for the time being is ensuring a small subsidy for unemployed people, as well as food and medicine aid for many poor people. There is a legal reform also that has been promised on the basis of ensuring legal stability in Argentina. It should be serious. Finally, there needs to be a political reform where a great part is the cost of politicians. What does that mean? Cost to politicians means that a legislator in a province of Argentina was earning something like \$10,000. This was because of the fixed exchange rate, where pesos were equal to dollars on a one to one basis.

Argentina has trade negotiations going with the FTAA, and we are participating as part of MERCOSUR. There are two basic questions to keep in mind. Obviously, Argentine government officials, politicians, and in general the Argentine population have a responsibility of what it does with its country, and I include myself there. Today in this interrelated world, I think everyone should be responsible for what happens with a country such as Argentina. The world today cannot go on if there is not a mutual relationship between or among all of the countries. You cannot think about terrorism; you cannot think about environment; you cannot think about anything around the world if you think of countries isolated with no relations among themselves. This responsibility should be put forward by those countries which are in a better position to do that. The United States government cannot say that they are not worried with what

happens with Argentina. They should be worried because we are all interrelated in this world.

C. Questions and Answers

QUESTION:

In Brazil, there are price controls. Do you think there is an effort to control prices in Argentina?

ADRIAN JORGE MAKUC:

Yes, I think there are different kind of efforts being done. Food is being exported by Argentina, for example, the same as happened in Brazil, if there is a devaluation there is a translation of those higher prices in terms of dollars or translated to pesos to domestic prices. We have tried in the beginning to prevent that by imposing export duties so that the dollars that come into Argentina translated to pesos are less than what the price received is abroad. It was one general measure. It did not work. It is not working at least up to now. To give an example, oil prices have gone up to seventy percent, sometimes some companies one-hundred percent, so price controls for the time being have not been imposed. There are some ideas of controlling prices of pharmaceuticals, linking basic provision of pharmaceuticals as I have said before by medical aid systems or procedures for people who are not able to buy them. So there is a linkage in some cases for the provision of pharmaceuticals with their prices by means of government intervention. The other idea is based on a law we have in Argentina that maybe you have in Brazil as well, where there is a difficulty in the supply of a product because the law says that government has the right to seize the product if there is no guarantee of that product being supplied when in effect the product exists. This may be combined in some cases with price controls. It may happen in Brazil. It has happened in Argentina thirty years ago. For the time being, there is no price control as such in general terms.

QUESTION:

Do you feel Argentina will remain a democratic society? Also do you think the general Argentine population supports democracy?

ADRIAN JORGE MAKUC:

I feel that is a very important question. I may have implied there was a possibility of no survival of a democratic system in Argentina. If that was the case, it was not my intention. I think we have democracy in Argentina and we will keep under a democratic system because people believe in that system. Those who oppose, either civilian or military people, I think are very minor and restricted to small groups; I do not think that in general the

Argentine population wants nothing to do with losing the democracy they have today. In the middle of this crisis in December people started to gather together in neighborhoods in Buenos Aires, meeting together in popular assemblies to discuss what they could do on peaceful terms. Nobody was thinking about attacking or destroying anything. The discussions focused on what could be done when the politicians or authorities of the time before the resignation of President de la Rúa were not proposing anything that could be credible. If I take that into account, which also happens in internal provinces in Argentina, the fact of democratic discussions leading to direct participation in many cases, my belief is we will continue to have democracy with us, and I hope so.

