

Argentina's Globalization Experiment

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The fall of Argentina's economy into complete disarray in the recent years can be traced to the failure of the government to compensate for failed globalization strategies that were implemented starting from 1991. Wishing to jump into the global ring, president Carlos Menem constructed a policy to keep inflation low and to make Argentina desirable to foreign investors. The national currency, the peso, was set by the government to be equal to the US dollar. This allowed investors to easily convert money into pesos to use in the Argentinian economy and gives them some assurances that the pesos they plan to make as profit will remain as stable as the US dollar, free from any dramatic inflation. However, from a geographic point of view, this plan of action is not sound. With pegging it's currency to such a strong economy as the United States, Argentina gives up local control of it's money. Without the ability to adjust exchange rates, economic crises become much more severe.

The problems with the linking of Argentina's currency with that of the US is the disparity between the two country's economic positions. The US is a economically strong, highly developed and very rich nation with little foreign debt compared to it's GDP of ten trillion dollars. Binding the peso to the dollar also binds Argentina to US currency policies. The internal currency changes of the US (i.e. changing interest rates) would affect Argentina in some ways without the direct link between the two country's currency. However, the US is not Argentina's largest trade partner, Brazil is. With the devaluation of Brazil's currency in 1999, Argentina's exports were far too expensive for Brazillians to purchase. Although imports were now cheap for Argentina, without more money provided by exports, debt continued to rise.¹ Argentina suffered several shocks throughout the 1990's, most notably the Mexican crisis in 1994, all which forced them to acquire more debt in order to keep the peso in line with the dollar.

The IMF solution to these problems during the 1990's was for Argentina to cut spending in order to balance the budget and pay off the debt. Unfortunately, this meant cutting government spending during a recession. This aggravated the recession and required even more loans. Government spending stayed at around 20% of the GDP during the 1990's, but the percentage of spending used to pay off the interest on the debt that the country carried increased from 6% in 1993 to 15% in 2000. The IMF supported the policy of tying the dollar of the peso to that of the dollar when Argentina started the plan in 1991, and generally support keeping exchange rates high.² It's solution to the large debt Argentina was experiencing did not address the problem. An increase in federal spending was not the cause of the problems, increased interest payments on existing debt was much more of an issue.

In the early 1990s, Argentina also engaged in a plan of privatizing most of it's public services: airlines, electric power, post office, water utilities and others. The privatization gave Argentina working capital to weather the various economic shocks like the United States increasing interest rates and Mexican devaluation in 1994; in effect they were selling off their businesses to private investors in order to fund the deficits caused by these economic shocks. By 1999, they had privatized all the services they were willing to privatize and so they had no other "emergency" sources of income to fall back on.

The direct cause of Argentina's current fiscal problems are caused by events they had no control of: a rise in US interest rates and bad economic downturns in foreign countries like Mexico, Brazil and Russia. However, these events would have had much less of an effect if the government had retained control of it's currency. Once it decided to stick with the policy of matching peso to dollar, the option to devalue it's own currency in order to cushion the

1 James E. Mahon Jr. and Javier Corrales, "Pegged for Failure? Argentina's Crisis." In Current History Feb. 2002

2 Mark Weisbrot and Dean Baker, "What Happened to Argentina?" (Center for Economic and Policy Research, 2002)

blows of economic problems.

Why did this policy continue even after it was clear (after the Mexican crisis) that it would not work in the long term, because of the increase of debt? The power of organized labor and the rest of the popular sector had been instrumental in electing Carlos Menem, in 1989 and who led the country for 10 years afterward. However, in power, he made alliances with the capitalist sector rather than with labor.³ To help the capitalist groups, Menem laxed labor laws and started the process of privatizing government services. The pegging of the peso to the dollar helped in the privatization process, since investors would be much more likely to invest in national utilities if they were sure that devaluation of the currency would not lessen their profits. The policies of privatization increased the disparity in incomes between the rich and the poor, with the rate of increase in income for the wealthiest 10% of people at more than twice the rate as that of the poorest 10% between the years 1991 and 1994. (13.7% and 5.3% respectively)⁴

The goals of globalization, to create a global marketplace with as few trade barriers as possible, seem to have failed in Argentina. This idea of free global trade often ignores problems with applying blanket policy to different localities. Even though money can travel instantly from the US to Argentina, the situations in the two countries may be very different, and in most cases, they are. There is no reason to believe that when the US Federal Reserve board raised interest rates in 1994 they were thinking of Argentina's economy, and Argentina should not expect a great consideration. With fixing their currency to the dollar, they effectively moved the power of their currency outside of their control: They could not get it back without serious economic repercussions. The capitalist sector is who benefits from the fixed prices; the state, located in a specific place, is not able to take advantage of the compression of space in a "global" economy.⁵ Argentina gave up all control of fine-tuning it's currency.

Foreign debt is a problem in most Latin American economies; companies need to worry about how to pay off the interest before they can even attempt to pay off the debt itself. This foreign debt is not new. However, in attempting to construct a more appealing place for economic development for foreign corporations and encouraging investment, they seem to have made a major mistake. The IMF, in continuing to give loans to keep the peso high, may have made things worse in the long run. Other countries who have let their currency devalue, such as Russia and Brazil, although they have suffered economic recession, have not experience the kind of hyperinflation that the IMF was so concerned about.⁶

As some call is heard for similar and even some more drastic "dollarization" schemes by neo-liberal think tanks including some in the IMF, countries must look at the outcome of Argentina and consider the risks of essentially losing internal monetary controls to a foreign entity (the US Federal Reserve Board) who will not be interested in devaluing their own currency to stem the tide of recession in a foreign country.

3 Fernando Javier Bosco, "State-society relations and national development: a comparison of Argentina and Taiwan in the 1990s" In *International Journal of Urban and Regional Research* 22 pp. 623-652: 632

4 Ruben M. Lo Vuolo, *The Retrenchment of the Welfare State in Latin America: The Case of Argentina*" In *Social Policy & Administration* Vol. 31 No. 4 Dec. 1997 pp. 390-409 (395)

5 Doreen Massey, "Power Geometry and a Progressive Sense of Place" In *Mapping the Futures*, (New York: Routledge) pp. 59-61: 61

6 Mark Weisbrot, "Don't Cry for the IMF, Argentina," *The Gazette* (Montreal, Canada), May 21, 2001: Editorial