

## Argentina's Economic Revolution

By Domingo F. Cavallo<sup>1</sup>  
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The last few years represent a turning point in Argentina's national history. Two years ago, when President Menem assumed office after six decades of increasing state intervention in the economy and isolation from the world, the country was facing a dramatic economic crisis. Economic instability and social turmoil struck at the same moment, overturning the old order and the old thinking, and an opportunity arose to overhaul economic policy completely. That opportunity was not lost.

Looking back over the past century of Argentina's history, it is clear that the need for such a change was itself a tragedy. In the second half of the nineteenth century and the early twentieth century Argentina enjoyed great prosperity and stability. The fall from grace dated from only 60 years ago.

The foundation for that earlier period of well-being was set in place in 1853 when the country adopted a constitution similar to that of the United States. In the succeeding years, Argentina's economy became well integrated into the world system trade, capital flows and payment. The government confined itself to providing roads, railways and other physical infrastructure and to establishing and operating appropriate institutions such as the judicial system. Entrepreneurship and wealth creation were seen as entirely private activities. With few exceptions, such as the 1980 Crisis, the macroeconomic environment was a benign one and the period from 1870-1930 enjoyed political and macroeconomic stability and steady growth.

This began to change in 1929. A military coup brought to power a group intent on using the machinery of government to benefit particular groups within the country. They were followed by a succession of civilian and military governments that were either misguided or weak. They presided over a 60-year virtual hiatus in Argentina's economic developments.

Tariff barriers were raised to provide protection from foreign competition. Government boards were set up to regulate all aspects of commerce in many industries, setting prices for produce, goods and services. In some cases, the boards became large and centralized bureaucracies, collecting and distributing fees on their industries and thereby exercising considerable power over all aspects of business. Each such arrangement then stood to justify similar arrangements in other sectors, to the benefit of other groups in the economy. Intervention thus became widespread.

In the 1930s, farmers and professionals were among the first to be regulated in this manner. Later, in the 1940s President Peron raised the labor unions to become a countervailing force. And thereafter economic issues concerning large corporation, the professions, farmers and organized labor were settled politically rather than through the marketplace. When the economy suffered as a result, it became the national habit to blame outsiders, an attitude that justified progressively greater isolation.

In 1983, things began to change. The country suffered a major economical and political collapse after its defeat in the Malvinas War. The military lost all credibility as a force for sound

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government, which made a return to democracy inevitable. So when President Alfonsín was elected to power, it was clear that a change in regime was needed, politically and economically.

But he remained a prisoner of the ideas of statism and interventionism that had governed Argentina's economy for the prior half century. Additionally, the Peronist opposition was too strong to give him a great deal of leeway to enact and implement effective reforms. This deadlock, combined with Argentina's continuing economic decline in the mid-1980s, reinforced the national tendency to blame the rest of the world for Argentina's problems.

An important part of Alfonsín's intellectual inheritance was that an expansionary monetary policy was pro-growth: a philosophy that, when put into practice, had previously caused tremendous economic dislocations and this time proved disastrous. Inflation accelerated to a point where it was running at 200% a month at the time his government fell. As a result, the case for reform that had been strong at the beginning of Alfonsín's presidency became overwhelming when Carlos Menem assumed office. Clearly the prevailing statist wisdom was wrong. Moreover, in the intervening period, the governments of Eastern and Central Europe had turned away from communism. This had a profound effect in Argentina and undermined the credibility of proposals for anything other than a restoration of a free market economic system.

Although President Menem was initially viewed as a populist and regarded with some skepticism, his commitment to the people was of the broadest philosophical nature. He was not chained to any particular economic formula and was, therefore, free to adopt a program of radical pro-market economic reform. There was, however, one beneficial exception to the President's agnosticism on economics: his early and strong commitment to returning Argentina to the family of nations and the international economic system. He was particularly eager to learn from the experience of other countries and paid a good deal of attention to the success of Mexico and Chile in the Western Hemisphere as well as to the earlier reforms in Spain and Portugal.

However, it did take time to assemble an economic team to carry through these reforms. The importance of this public management concept, of an "economic team," was not generally appreciated early on by the Menem administration. Responsibilities for the various ministries involved in economic management were distributed among the various political factions represented by the government. A beginning was made on privatization and on reducing public expenditures. But tax reform was not possible. It later became clear that coherence of views within the economic policy team was a precondition for the comprehensive reform that the country needed. Now, late in 1991, it can be said that public officials in all the major economic government departments share a common vision of the future.

Aside from privatization and budgetary reforms, Argentina has drastically reduced or eliminated tariffs and quantitative restrictions on most imports. By an act of Congress, it has transformed the Central Bank into what is virtually a currency board: the currency is now backed by either gold or foreign exchange. By making monetary policy virtually tamper-proof, the government has restored faith in the currency and people have begun to treat the austral as they used to treat the US dollar: as a store of value as well as a unit of account and means of payment.

At the end of October 1991, the President announced in a 122-article decree that he was dismantling the regulatory boards. Health, safety and environmental regulations would remain, but controls on such purely economic matters as opening hours, prices and fees would be settled in the marketplace, free from government interference.

It is extraordinary how attitudes have changed. Over the previous few months, every effort had been made to get Congress to disband one set of controls after another, but to no effect. Farmers would not tolerate deregulated farm gate prices, for fear that they would fall and that transportation companies would reap the benefits. The transportation lobby fought deregulation of agricultural transport services because, they argued; their truck tires cost four times as much as they would at world prices, which they blamed on import duties. One pressure group after another frustrated piecemeal reform, always citing the benefits that others enjoyed to justify their own restrictive practices.

The President judged that circumstances warranted enactment by decree and, as his government did away with restrictive practice in several industries at the stroke of a pen, it braced itself for an outcry of public condemnation. But none came. Instead, the press and the public at large hailed the decree as necessary and farsighted. Indeed, congressional leaders were so taken with the measure's popularity that they quickly pressed to ratify the decree with legislation of their own.

There was a potential public employment problem related to the disbanding of so many statutory agencies. But this was solved by reassigning employees of the old boards to the internal revenue and social security services where they are being drawn into an effort started at the beginning of 1991 to improve tax collection. Tax evasion used to be endemic. But, since that effort started, revenues have risen sharply as a share of GNP, due almost entirely to much stricter enforcement.

Argentina's reforms remain unfinished. There is great concern that inflation remains at one-and-a-half percent a month- down from %200, but still at a rate that will undermine competitiveness rapidly when a currency is virtually tied to the US dollar. And the privatization program is only half complete. Clear regulatory frameworks need to be established before several public monopolies can be privatized. For most of 1991, Congress and the trade unions opposed these.

But several critically important changes have already occurred:

Argentina has opened up again to the world. On the one hand, international examples of reform are now sought out; and, at a more practical level, trade and capital flows are once more substantially unrestricted;

Privatization and liberalization have reduced the intrusiveness of the state in the economy; and  
Politics is no longer the key to making money in Argentina's economy.

This last point deserves emphasis. Politics and economics are progressively being separated to the point where it seems safe to predict that future elections will be fought over who can implement a liberal economic program most effectively, rather than who can offer fundamental alternatives.

This extraordinary change in economic policies was possible only after combined economic and political crisis. Previous upheavals of one kind or the other had not been enough. But, the experience in 1989 of hyperinflation at home, the evidence of success and failure abroad, and the resultant intellectual bankruptcy of statism of both the left and the right created the opportunity for widespread and radical reform.

A new, broadly-based consensus has emerged in favor of free market economic policies. Based on this new consensus and the policies that have accompanied it, Argentina should now prosper as it did at the beginning of the twentieth century and enjoy many years of growth and prosperity well into the next.