Appendix 2

Argentina and the IMF Prior to 1991

Argentina entered the decade of the 1990s having experienced a dismal economic performance over a prolonged period of time. From about 1975 through 1990, the country was plagued by high inflation and general economic stagnation. Inflation seldom fell below 100 percent; there were bouts of hyperinflation, notably in 1985 and 1989–90. Real GDP in 1990 stood 6 percent below the level in 1974. Over this period, the general stance of economic policy was inward-looking and interventionist, although there were occasional attempts to adopt more market-oriented policies.

All-out crises erupted twice during the 1980s. Early in the decade, the mounting fiscal imbalances led to high real interest rates, a string of corporate bankruptcies, growing insolvency in the banking system, and a loss of confidence. An overvalued exchange rate had created a large cumulative balance of payments deficit, causing a serious debt service problem and an eventual loss of market access. Inflation accelerated, and real GDP declined by almost 10 percent from 1980 to 1982.

Likewise, in early 1989, a failure to adjust the official exchange rate and public sector prices in the face of accelerating inflation led to a sharp deterioration in the public finances, an attack on the currency, and a substantial loss of foreign exchange reserves. A pickup in inflation in turn created a vicious circle of soaring public sector deficits and further inflation. A suspension of the official exchange market caused external commercial arrears to accumulate. A deep recession ensued, causing real GDP in 1989 to decline by 7 percent from the previous year. During the middle of this crisis, the ruling Radical party lost the national elections, and the administration of President Raúl Alfonsín yielded power to the opposition Justicialist (Peronist) party, five months ahead of schedule.

Over this period, a number of attempts were made to deal with chronic inflation and large balance of payments imbalances. After the mid-1980s, the gradualist approach of early attempts gave way to a more decisive, shock-therapy ("heterodox") approach, beginning with the Austral Plan of June 1985, which introduced a new currency unit, the austral, initially set equivalent to 1,000 pesos. When this failed, additional attempts were made, notably a policy package of October 1987 and the so-called *Plan Primavera* of August 1988.[1] A common feature of these later efforts was the use of wage and price controls, supported by a (temporary) fixing of the exchange rate. But supportive fiscal and monetary policies were not sustained, making the wage-price freeze and the fixed exchange rate untenable. Inflation returned with vengeance.

The new Peronist administration of President Carlos Menem, after taking office in July 1989, immediately designed a package of short-run and medium-term measures to stabilize the economy and to promote growth. The currency was devalued and then fixed at a substantially depreciated level, supported by the strengthening of the public finances. A major program of structural reforms was announced, consisting of an overhaul of the tax collection agencies, privatization of public enterprises, promotion of competition (including from foreign firms), and central bank independence. Two basic laws were passed by Congress: the Law of Reform of the State (authorizing the privatization or liquidation of public enterprises), and the Economic Emergency Law (including measures to improve public finances in the short run and structural reforms over the medium term). In October 1989, the authorities requested an SBA with the IMF, which they indicated would pave the way for a later extended arrangement.

[1]It was within the context of the *Plan Primavera* that a major dispute over Argentina emerged between the IMF and the World Bank in the summer and fall of 1988. Resisting pressure from the U.S. Government, the IMF Managing Director chose not to lend to Argentina because he viewed Argentina's fiscal policy as insufficient to assure lasting stability. The World Bank, on the other hand, went ahead with a package of loans totaling $1.25 billion on the basis of a "Letter of Development Policy," which "included a statement of the authorities' intentions with respect to fiscal policy that was more expansionary than the policy on which the Fund staff was insisting as a condition for the stand-by arrangement." Argentina's subsequent failure to meet the Bank's conditions, and the early collapse of the *Plan Primavera* in February 1989, vindicated the IMF's insistence on fiscal control. See Boughton (2001), pp. 520–24; also OED (1996), p. 18.