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ARGENTINA'S PATHWAY THROUGH FINANCIAL CRISIS

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## **Abstract**

Political support for Argentina's currency board rested on distributing the early gains from ending hyper-inflation and the spending made possible with access to external credit. When these gains were exhausted and external shocks left the peso overvalued, neither Argentina's political system nor its economy could adjust. The needed adjustment went well beyond simple fiscal tightening: it required deciding who would incur the financial losses associated with the deep contraction needed to correct a real over-valuation in a heavily indebted economy. By 2000, Argentina faced the prospect of further economic contraction, a banking crisis and an external sovereign debt crisis. Even if none of the three crises was avoidable, preemptive action might have made one or more of them less severe. Yet preemption was a political orphan – no political constituency in Argentina argued to bring some pain forward for a chance of less pain down the road, and the IMF and G-7 preferred continued financing to the political risk of supporting a new macroeconomic strategy.

## Introduction

Between 1999 and 2001, Argentina's economic slump transformed itself into a deep financial crisis. Two theories for Argentina's economic malaise dominated the policy debate. One held that Argentina was suffering from a crisis of confidence. Another held that the crisis was mostly fiscal. Both theories were too simplistic. They ignored the central importance of an overvalued currency and the heavy use of the dollar to denominate domestic financial contracts. They also failed to recognize the extent to which the Convertibility System (Argentina's currency board arrangement<sup>1</sup>) had become an organizing device for Argentina's politics – not just an anchor for monetary policy – and how access to external financing had provided the critical glue that held together the political economy of the currency board.

Argentina's political system was unwilling to act pre-emptively to reduce the scale of what in many ways was an unavoidable crisis. At no time was there a political consensus to incur the costs of exiting Convertibility immediately to avoid a bigger, deeper and more costly exit further down the road. Yet there was equally no consensus to shrink Argentina's economy and drive down wages and prices to make the economy compatible with the constraints of the currency board, particularly once those constraints started to bite in the face of reduced capital inflows. Argentina preferred to hope that its difficulties were temporary, drawing on IMF financing, spending its own reserves and then resorting to increasingly desperate attempts at clever financial engineering to postpone a payments crisis.<sup>2</sup>

Ironically, default and devaluation did not end Argentina's internal political paralysis. A desire to avoid probable losses transformed into an inability to allocate losses already incurred. All the major players initially hoped that someone else would get stuck with the bill. At the end of the day, only some got compensated for their losses – though the denouement of Argentina's crisis has been as protracted as its build-up.

This paper is organized into four sections. The first section traces the evolution of Argentina's crisis. The second section looks at the key decisions that defined how the crisis unfolded, paying particular attention to internal political forces that made alternative policy directions unattractive during the initial stages of Argentina's crisis as well as the decision to resolve Argentina's domestic debt crisis through pesification and compensation. The third section looks at who has borne the costs of Argentina's crisis. We conclude by examining the constraints Argentina's political institutions imposed on its approach toward crisis management.

## I. Crisis dynamics

Argentina experienced three conceptually different crises:

- *An economic crisis.* Brazil's devaluation and the tightening of external capital markets that followed Russia's default combined to push Argentina into recession in 1999. Argentina did not emerge from this recession until late in 2002: output stalled in 2000, fell sharply in 2001, and then collapsed in early 2002 after Argentina's devaluation and default.

- *An external sovereign debt crisis.* As Argentina's economy cooled, external investors lost interest in Argentina's government bonds, leaving the government dependent on domestic banks, domestic pension funds and the IMF for financing.
- *A domestic banking crisis.* Argentina experienced a series of a domestic bank runs in 2001. After default and devaluation, the banking system was in shambles, and required extensive restructuring.

These three crises were tightly interlinked.<sup>3</sup> The series of shocks Argentina experienced in the late 1990s – reduced market access following Russia's default, the growing competitive challenge from Brazil after its devaluation, and the slump in soybean prices – called for a real depreciation of the peso.<sup>4</sup> Breaking the dollar peg institutionalised in Convertibility would have allowed the exchange rate to adjust – but at the cost of bankrupting many firms and the government, since the peso value of their dollar debts would balloon. The alternative was slow deflation, which strangled growth, reduced tax revenues and risked the same outcome – bankruptcies throughout the private sector, and perhaps the government as well.<sup>5</sup> With no growth and no market access, the government turned to the banking system for financing to buy off domestic constituencies, increasing the risk of a domestic banking crisis.

Argentina did not experience a sudden, sharp crisis like Mexico or Korea. Rather Argentina found itself in a downward spiral, with a steadily shrinking real economy and persistent political tension that led successive groups of creditors to lose confidence.

**Table 1: Fiscal and public debt indicators<sup>6</sup>**

	Interest payments on debt (% of GDP)	Implicit interest rate	Primary balance	Debt to GDP	RER adjusted Debt to GDP
1991	2.8	8.6	-0.4	28%	28%
1992	1.6	6.2	1.4	24%	24%
1993	1.4	5.0	1.2	28%	28%
1994	1.6	5.1	-0.1	29%	29%
1995	1.9	5.4	-1.0	32%	32%
1996	2.1	5.6	-1.3	35%	35%
1997	2.3	6.1	0.2	38%	39%
1998	2.6	6.4	0.6	41%	46%
1999	3.4	7.1	-1.6	48%	63%
2000	4.1	8.0	0.3	51%	71%
2001	5.4	8.7	-1.4	62%	95%
2002	2.4		0.9	151%	
2003	2.4		2.4	149%	

#### *Growing difficulties raising new external financing*

Despite its economic slump, Argentina continued to import more than it exported, ran a significant current account deficit and required ongoing access to external financing. In 1999 and 2000, as bond spreads rose, sophisticated institutional investors became increasingly reluctant to buy new Argentine bonds.<sup>7</sup> For a short while, Argentina could still tap less sophisticated retail investors in Europe.<sup>8</sup> However, by the end of 2000 Argentina was losing access to the retail market as well. Private inflows all but dried up after a political scandal forced the vice-president to resign. Argentina looked to the IMF for emergency financing and the IMF responded with a \$15 billion loan – dubbed “*blindage*” (shield). In

this program, the IMF – unusually – agreed to defer fiscal consolidation until after 2001, in part to answer criticism that the tax hikes from a relatively tight fiscal policy contributed to Argentina's inability to grow during the course of 2000.<sup>9</sup>

However, it soon became clear that Argentina would have trouble meeting even these less demanding fiscal targets. In the spring of 2001, President De la Rúa chose an orthodox economist, Ricardo Lopez-Murphy, to replace Jose Luis Machinea as Economy Minister. Lopez-Murphy demanded the authority to cut budgets to reflect falling revenues, the rest of the government balked, De La Rúa did not back Lopez-Murphy, and Lopez-Murphy resigned.

De La Rúa then turned to the architect of Argentina's 1991 Convertibility Plan, Domingo Cavallo. Cavallo rejected calls for severe fiscal tightening, arguing that technical changes in the operation of Convertibility could provide a de facto monetary easing and jumpstart growth.<sup>10</sup> Lopez-Murphy had wanted control over the spending ministries and did not get it; Cavallo wanted control of the central bank and got it. Central Bank President Pedro Pou was forced out when he resisted Cavallo's efforts to encourage bank lending by loosening reserve requirements.

Cavallo convinced the IMF to continue lending despite the missed fiscal targets and initiated an ambitious \$30 billion voluntary government debt swap (the *mega canje*) in June 2001. The swap deferred near-term principal and some interest payments. It proved to be a tactical success but a strategic failure. It attracted higher levels of participation than many had expected, but what little breathing space Argentina did buy was extremely expensive.<sup>11</sup> To many, the government's willingness to pay so much for so little in the swap signalled desperation.<sup>12</sup>

Market dynamics changed for the worse. A failed Treasury bill auction led Cavallo to reverse his fiscal policy course: the government announced that it had lost access to credit and therefore had to run a zero-deficit policy. This led to a deposit run, concentrated rationally on the banks most actively involved in financing the government – two state banks and one Argentine-owned private bank.<sup>13</sup> Cavallo was forced to play his last card: he audaciously announced that the IMF would speed up and substantially augment its next disbursement, even though he had yet to secure commitment from Fund management or the US Treasury.<sup>14</sup> Cavallo's bluff worked – the announcement helped to stem the run, and Argentina got more money. The \$15 billion IMF program was increased to \$23 billion, including \$6 billion made available immediately to supply emergency financing to the banking system.

However, the economy continued to contract, government revenues continued to fall, and the pace of deposit withdrawals picked up again after Peronist opposition won congressional and provincial elections in October.<sup>15</sup> In November, Argentina converted domestically held international bonds into domestic loans: the loans carried a lower interest rate, but at least in theory, were backed by revenues from the financial transactions tax.<sup>16</sup> But efforts to cut spending, including interest spending, lagged falling revenues. Many provinces resorted to paying their workers with IOUs marketed as quasi-currencies. The federal government itself started issuing a quasi-currency, Lecops, to cover shortfalls in revenue transfers to the provinces. McDonald's started selling Lecopburgers.

In December, growing pressures on the banks led the government to restrict access to sight deposits (*corralito*), and then to time deposits (*corralón*). Argentina's financial standstill quickly turned into a full-blown political crisis. Riots followed the bank holiday, resulting in several deaths and the resignation of Cavallo and President de la Rúa. De la Rúa's successor declared default on Argentina's external debt. After another change of government, the new government of Eduardo Duhalde formally devalued the peso, introduced exchange controls, and issued a decree that converted domestic financial contracts from dollars into pesos.

### *Financial stabilization and economic recovery*

The crisis reached its nadir in the spring of 2002. Economic activity plummeted, poverty rates surged, the financial system remained frozen, and the peso briefly fell to four to a dollar. Duhalde's new government – and a new economic team led first by Jorge Remes Lenicov and then by Roberto Lavagna – eventually managed to achieve a degree of financial stabilization without the IMF. Central bank intervention to the tune of \$3 billion, capital and exchange controls that locked the utilities' domestic cash balances in the banks and above all, responsible fiscal policy combined to stop the peso's free fall. Government revenues were plunging, but it generally spent only what it took in, avoiding the need to print money and laying the groundwork for the eventual stabilization of the peso.<sup>17</sup>

By mid-summer of 2002, the real economy started to rebound, driven both by higher revenues from exports and import substitution. Stabilizing the banking system took more time. The deposit freeze was never watertight: frozen deposits could, for example, be used to pay peso debts and the courts ordered additional deposits to be released from the freeze. However, once both the peso and the economy had stabilized, the government was able to lift the freeze in stages without triggering a renewed run. By the end of 2002, all sight deposits were freed.

This started a new phase of Argentina's crisis – a phase marked on the one hand by a strong domestic recovery and on the other hand by demands for compensation for financial losses incurred during the crisis, deliberations on how to allocate these enormous losses among various domestic constituencies, and negotiations – of a sort – with Argentina's external creditors.

## **II. How Political Constraints, Market Pressures and Institutions Shaped Key Decisions**

### *Key Argentine decisions*

Argentina made three key decisions during the course of its crisis. The first was to seek IMF assistance in fall of 2000 to support the currency board and a relatively accommodative fiscal policy. The second decision, made by Cavallo after markets closed in the summer of 2001, was to push off bond maturities and seek more IMF money, instead of exiting the Convertibility and initiating a real debt restructuring. The third key decision, taken after the IMF left the scene, was to restructure public and private domestic debts through pesification.

### *Seeking IMF financing*



Neither Argentina's decision to seek IMF financing to back the Convertibility in late 2000, nor the IMF's decision to support Argentina are a surprise. The IMF had a long and close relationship with Argentina. IMF financing helped Argentina through the bank run that accompanied the 1995 Tequila Crisis. A smaller IMF program followed in 1996-98, and then a non-disbursing "precautionary" program from 1998 onwards.

While IMF programs are often viewed as a major constraint on a country's macroeconomic freedom, the opposite was generally true in Argentina. Private external financing, unlocked in part by the availability of backup IMF funds and IMF endorsement of Argentina's policies, generally helped to loosen the constraints of a strict currency board. Indeed, in many ways the entire political economy that sustained Convertibility hinged on access to external financing, whether from private capital markets or the IMF.

Argentina's long history of financial instability is rooted in an enduring gap between the federal government's ability to raise money and the demands on the government for spending, including the demand for transfers to Argentina's politically powerful provinces. This gap was closed by borrowing from the central bank in the 1980s, leading to persistent inflation and eventually to hyper-inflation.<sup>18</sup> Convertibility, along with the Brady restructuring, anchored a classic "liberalize, privatise and stabilize" package that sought to break this political and economic constellation. A currency board, at least in principle, required that all pesos be backed one to one by hard currency reserves, and thus precluded central bank financing of the government. (In practice, Argentina allowed some of the monetary base to be backed by the government's own dollar-denominated bonds rather than true reserve assets. It also kept more reserves on hand than required just to back the pesos in circulation, providing an additional source of flexibility.)

Paradoxically, the quick success of the reform package and the funds it brought made the fundamental political bargain that underlay Argentina's reform program less rigorous in practice than in theory<sup>19</sup> (Starr, 1997). Stabilization brought an economic boom, and a booming economy meant growing revenues, allowing the state to reward political supporters and to buy off potential opponents. Privatisation – even less than perfectly clean privatisation – generated substantial one-off revenues. By the end of the decade, most major utilities were in private, and often foreign, hands. The apparent success of the reform project and changes in global markets combined to open new sources of market financing to the government.

The government initially could use the gains from macroeconomic stabilization to reward supporters and to buy off opponents to its other liberal reforms – a general pattern that Dani Rodrik has emphasized.<sup>20</sup> But after the first gains from ending inflation had been spent, Argentina's government relied more and more on access to external capital markets to generate the resources to lubricate Argentina's political system. Eventually, Argentina had tapped out those markets – forcing the political system to change. Joyce Chang, JP Morgan's head of emerging market research, observed: "Menem's authority was very much influenced by his ability to provide goods in exchange for favors. Once privatization proceeds were exhausted, the power of the executive branch was severely weakened. By the time De la Rúa took office, there was relatively little in the way of goods to distribute to political leaders. Menem was in the position to "give and splurge" while De la Rúa was left with the task of attempting to "take back and save."<sup>21</sup>

Argentina's President can exert considerable control over the federal legislature and even over the federal judiciary, but far less control over power provincial governors. In

recent years, some of the President's institutional authority has been delegated to a strong economy minister.<sup>22</sup> But, the institutional power of the economy ministry hinged in no small part on its ability to deliver external financing, whether from the privatization of state assets or from the international bond market. So long as sufficient external financing was available, the economy ministry accommodated domestic spending pressures and the current account deficits associated with rapid growth never triggered the currency board's automatic adjustment mechanism. This meant a delicate balancing act: to tap the markets, the economy ministry needed to sell Argentina as a model of financial prudence, even though the financing obtained on the back of such promises was needed to pay for the spending ministries' priorities.

**Table 2: Access to Domestic and External Financing**

\$ billion

Year	Net private external financing	Net financing from the bonds market	Net financing from the IMF and MDBs	Increase in bank deposits
1995	13.2	2.4	3.8	-2.9
1996	11.5	10.0	1.1	8.9
1997	14.5	8.4	0.4	13.1
1998	16.8	11.6	2.3	8.9
1999	3.4	2.8	1.3	5.5
2000	1.3	-0.8	1.4	3.7
2001	-6.4	-9.2	10.6	-19.8
The fat years: 96-98	42.8	30	3.8	30.9
The lean years: 99-00	-1.7	-7.2	13.3	-10.6

Source: Government of Argentina (external debt statistics) and BCRA.

Revising these political bargains when revenues started shrinking and external financing disappeared was hard. In general, Argentina opted to tap new sources of financing rather than make fundamental changes. In 1999, both President Menem and Buenos Aires Governor Eduardo Duhalde turned to the banks to finance public spending associated with their duel for the Presidency.<sup>23</sup> The election of a third candidate, Fernando de la Rúa of the Radical party, did not alter Argentina's political economy. The Peronists controlled the federal senate and the main provincial governments, and had no desire to provide political cover for unpopular spending cuts. Imposing cuts by decree would have threatened De la Rúa's political position further: most constituencies, including the provincial governors, wanted protection from a deflating economy, not a program of shared sacrifice.<sup>24</sup> Market commentary at the time often criticized De la Rúa's political weakness and indecision, without observing that the structural basis of strong executive leadership disappeared along with access to external financing. That was particularly true since the ability "to provide goods in exchange for favors" (in the words of JP Morgan's Chang) became more important, not less important, to Argentina's political system when different parties controlled different parts of the government.

When IMF endorsement could no longer bring in private external financing, it was eminently logical for Argentina to seek the funds it needed from the IMF itself. In Argentina's case, the political costs of asking the IMF to finance the status quo were smaller than the costs of the alternatives. Economically, IMF funds enabled Argentina to finance budget deficits and provided the external inflows needed to avoid a sharp monetary tightening and more rapid deflation. Politically, IMF involvement was sold as part of a package that would allow Argentina to maintain stability and resume growth with limited sacrifice.

It is a bit more surprising that the IMF went along with a program that, at least initially, relied on its financing to support slightly looser fiscal policy.<sup>25</sup> After all, the IMF typically argues that currency pegs needed to be backed with rigorous fiscal policy to eliminate pressures for central bank financing. However, at the end of 2000, IMF staff and management – and for that matter the G-7 and most market participants – were torn between two competing analyses of Argentina's troubles. Some believed the core problem was with Argentina's profligate public finances, or with the exchange rate. But others saw the problem as the markets' temporary unwillingness to finance Argentina after Russia's default, augmented by fear of the official sector's interest in bond restructuring. They argued that tight fiscal policy in 2000 had prevented Argentina from growing, and that growth would unleash a virtuous circle of market confidence, lower interest rates and new inflows.<sup>26</sup> Their hand was strengthened by widespread criticism that the IMF's tight fiscal conditionality had aggravated Asia's crisis.<sup>27</sup> The split within the IMF combined with Argentina's reputation as a bastion of market reforms to give its policy makers more room to manoeuvre.

#### *Turning to Cavallo and yet more IMF financing*

The failure of the initial IMF package to restore growth – along with Argentina's failure to meet the program's fiscal targets -- provided an obvious point for all parties to reassess their strategy, as did Argentina's request for yet more financing in the summer of 2001. Argentina could have sought external financing to back a different set of policies, including a pre-emptive debt restructuring and/or a change in exchange rate regime. Instead, Argentina opted to turn to Cavallo, and to use Cavallo's reputation to secure one last injection of IMF liquidity. For all the attention generated by Cavallo's deviations from classical economic orthodoxy -- introducing special import tariffs and a financial transactions tax; talking of pegging to both the euro and the dollar -- Cavallo continued the core policies of his predecessors. He remained committed to the currency board, refused to initiate a coercive restructuring to reduce Argentina debt burden and eventually adopted an orthodox policy of fiscal tightening.

Even as Argentina's economy slipped further into recession and popular support waned for the sacrifice Convertibility implied, there was no political consensus in Argentina to abandon Convertibility. Perhaps more accurately, at no point in time was there consensus around an alternative to Convertibility – some wanted to float, others wanted to dollarize, yet others wanted to devalue and dollarize. In face of a deteriorating economy, the only consensus inside Argentina was to seek more IMF financing and to spend its remaining reserves to defend the status quo.

This political choice reflects a key economic reality: all other policy options implied higher short-term costs. Default – or even a successful pre-emptive restructuring – would have traded more short-term pain for potential long-term gains.<sup>28</sup> A default meant losing

access to domestic and external credit, and immediately moving into fiscal and external balance. Moreover, about half of Argentina's \$90 billion in bonds were held domestically, so reducing the value of the government's debt would reduce the financial wealth of those Argentines who had invested in the debt – banks (and ultimately bank depositors) and pension funds as well as wealthy Argentines with offshore accounts. Realistically, any sovereign restructuring would have brought on a banking crisis, a run on the peso and collapse of Convertibility.

It is at least conceptually possible that Argentina could have abandoned Convertibility, let the peso float, conducted a coercive but not draconian debt restructuring and still avoided a complete collapse of domestic confidence and extreme overshooting in the exchange rate (the "Uruguay option").<sup>29</sup> But avoiding complete collapse is not the same as avoiding large costs. Like the other options, floating sooner held few political rewards in the near term.

A wide swath of the Argentine society, including the big winners from the 1990s reforms, had extensive dollar denominated debts and thus a financial stake in dollar parity. Disinflationary pegs usually result in real appreciation of the currency, as inflation only falls with a lag. In Argentina, the dollar's steady rise after 1995 contributed to even further real appreciation of the peso – raising even further the potential cost of abandoning the peg for Argentina's dollar debtors. This may explain why in Argentina, the noisy opposition to fiscal consolidation was not matched by a debate about the costs of Convertibility. Political analysts argue that support for currency stability traditionally comes with trade integration, as exporters and importers demand a stable currency – though not necessarily strong -- currency to facilitate commerce.<sup>30</sup> Yet, Argentina's overall trade was limited, and its trade with the dollar zone was particularly small. Demand for a stable exchange rate came from the non-tradeables sector, which, ironically, was heavily foreign-owned. Firms and households in this sector had borrowed in dollars during the post-convertibility boom, and wanted a stable and strong peso to facilitate access to new dollar financing or to facilitate repayment of existing dollar debts.<sup>31</sup>

Since the short-term losses from devaluation to dollar debtors would far outweigh the short-term gains to exporters, it is no surprise that the tradeables sector lacked the clout necessary to take on the currency peg. The solution that Argentina eventually found to the domestic dollar debt dilemma – converting domestic loans into pesos, issuing compensation bonds to the banks, and servicing these new bonds ahead of defaulted external debt – was too radical for the government, or the IMF, to contemplate until the crisis really bit.

### *Why did Argentina get more money in the summer of 2001?*

Recent accounts of decision making in Washington demonstrate that both the IMF and many G-7 finance officials had serious doubts about the wisdom of providing additional financing to Argentina in one last attempt to bolster the currency board in the summer of 2004. Paul Blustein reports that at an internal staff discussion, the optimists in the IMF thought the augmentation had a less than 20% chance of succeeding. IMF management nonetheless supported Argentina's request for an augmentation. In part, this reflected the IMF's institutional aversion to forcing a change in its member's currency regime. The IMF likes to define its role as advising member countries on the policies needed to make their own choice of exchange rate regimes work, not as choosing exchange rate regimes for its members. Telling a country that it had to let its currency fall and suffer the consequences of

a disruptive default was more than the IMF could stomach. Above all, though, Blustein's work reveals that the IMF was willing to go the extra mile and provide Argentina with extra financing largely try to inoculate itself from blame for Argentina's eventual nasty crisis. If Argentina failed, it would be the fault of the Argentines, not the fault of the IMF. The IMF's reputation might suffer less if Argentina failed to live up to a demanding program of adjustment than if the IMF failed to provide financing.

But the IMF does not act on its own, and its shareholders share in the responsibility for the outcome in Argentina. The Clinton Administration was more inclined than the IMF to believe that some exchange rate regimes were not viable. However, Clinton's last Treasury Secretary, Larry Summers, was a lame duck when Argentina's crisis broke. A truly bold course – like pushing Argentina off its chosen exchange rate regime or making debt restructuring a condition for IMF financing – would have reverberated throughout the region. Such policy (or for that matter, a policy providing Argentina with a Mexico-style mega-bailout) would have required the sort of sustained US leadership that Summers could not put on the table. It was also probably impossible to build political support for such an approach without a smaller loan first to try to rebuild confidence in the currency board.

After blessing an unprecedented bailout for Turkey (a critical strategic ally in a critically important region) in the spring of 2001, the new Bush Administration had a clear opportunity in Argentina to break from the “jumbo” packages of the Clinton era and show that fear of contagion would not drive policy. The head of the Bush National Economic Council Larry Lindsey and Treasury Secretary Paul O'Neill did not agree on much, but both had indicated that they opposed IMF bailouts that had little chance of working.<sup>32</sup> However, the Bush Administration was not monolithic. The foreign policy team did not want to create the impression that the Administration was turning its back on Latin America, and the White House may have worried that Argentina's collapse would set back the Administration's efforts to create a hemisphere-wide free trade zone.<sup>33</sup>

As governor of Texas, George W. Bush had backed the Clinton Administration's bailout of Mexico. O'Neill had specifically praised Robert Rubin's Mexico experiment as a “success” in his confirmation hearings. Some in the Administration may have seen in Argentina potential for Mexico-style success that justified the multibillion-dollar gamble.

But the chances that a large loan would allow Argentina to escape a restructuring and default were far lower than in Mexico. Argentina had far more debt than Mexico. Its government debt to GDP ratio was far higher, as were its external debt to GDP and external debt to export ratios. Argentina also had much higher degree of “informal” dollarization than Mexico, particularly in the banking system. That complicated any exit from Argentina's tight dollar peg.<sup>34</sup> Worse yet, no one in the Administration stepped up with a comprehensive plan and insisted that the international community and the crisis country coalesce around this plan, as Rubin and Summers had done in Mexico. The administration neither wanted to be perceived as turning away from Argentina, a pro-market Latin friend in need, nor wanted to take responsibility for developing a real and potentially costly solution. Instead, at the insistence of Paul O'Neill, it included \$3 billion in the August IMF package, ostensibly to back a voluntary debt restructuring, even though this amount was patently insufficient catalyze a meaningful market solution.<sup>35</sup> Similar divisions were replicated inside the rest of the G-7. Many economic and financial policy makers believed that Argentina could not be saved; however, European political leaders were reluctant to block a multilateral support package that had US backing.

*Key decisions in 2002: pesification*

By the end of 2001, Argentina could not avoid devaluing the peso and defaulting on its external debt. A bank holiday was no more avoidable: the banking system lacked dollars, and the government did not have nearly enough dollar reserves – even after breaking convertibility – to back all dollar deposits.<sup>36</sup> But Argentina did not have to pesify – or to pesify asymmetrically, with deposits and loans converted into pesos at different rates. In the event, it chose to convert most debts to financial institutions at 1:1, indexing future payments to increases in peso wages and the consumer price index, and to convert deposits at 1:1.4, indexing future payments to increases in the consumer price index. The government eventually issued new low-coupon bonds to compensate banks for the 40% difference in conversion rates.

The policy of pesification and compensation demonstrates the difficulties of allocating the losses intrinsic in a major financial crisis. The final outcome reflected the political limits on the scale of losses that a democratic government could impose on depositors, and the economic constraints that limited the scale of the losses the government could impose on the banks. Since the banking system ended up with more losses than could be imposed on either the banks' owners or on depositors, the government made up the difference, in part at the expense of its remaining creditors.

The political imperative to help depositors regain access to their frozen deposits is not hard to understand. Citizens wanted their money back. The economic constraints are harder to grasp. The populist policy of asymmetric pesification initially pushed enormous paper losses onto the banks' owners. But there is no way to force a bank's owners to lose more money than they had put up in capital. It soon became clear that the government would either have to pick up some of the tab, or, in the words of one policy maker, accept the keys to every bank in Argentina and tell the depositors that they could not get their money back – a politically untenable outcome.

There clearly needed to be a way of restructuring the banking system's assets as well as its liabilities, and some aspects of that restructuring needed to be done quickly. Keeping deposits frozen during the lengthy process required to restructure the banking system's assets on a case-by-case basis was neither politically nor economically viable. After the devaluation, almost all firms, households and individuals with dollar debts would have been effectively bankrupt and stopped paying.<sup>37</sup> However, no bankruptcy regime is designed to function effectively when insolvency is the norm rather than the exception. No matter what their formal legal rights, the banks neither had the capacity to assume control over all technically insolvent firms nor the ability to monitor the behaviour of this many debtors. Experience in East Asia suggests that extended periods of non-payment and protracted restructuring negotiations dissipate value.<sup>38</sup> Across-the-board reduction in the debts of small firms and households allow scarce workout resources to be devoted to the biggest and most important cases.

Across-the-board pesification has proved to be a qualified success: it instantly restructured domestic contacts and restored payment flows, it made it possible to unfreeze deposits relatively rapidly and, by resolving the internal payments crisis, it helped lay the basis for Argentina's current recovery. Nonetheless, pesification has many flaws. Initial decisions on conversion rates and indexation were arbitrary; many details were poorly thought through. This laid the ground for seemingly continuous renegotiation of the terms of

the restructuring. Influential large dollar debtors reportedly lobbied hard to extend a solution initially meant to cover only mortgages and other small loans to cover Argentina's biggest firms as well.<sup>39</sup> Pesification was especially advantageous for large borrowers with export revenues, as the devaluation increased the peso value of their exports while pesification kept the peso value of the domestic dollar loans from rising commensurately, and firms with little foreign-law debt. The biggest winners of all were Argentina's farmers: their dollar debts were pesified just before the harvest brought in an influx of dollar revenue. Those who benefited the most from their initial decision paid down their pesified debts quickly; those who lost sought compensation.

While we believe that some form of across-the-board restructuring that limited the increase in the real debt burden of most borrowers was necessary, it is reasonable to ask if domestic debtors should have picked up more of the cost of crisis, leaving less to be borne by other stakeholders. One to one pesification and indexation effectively kept the real debt burden of domestic firms without external revenue constant. Given the scale of economic contraction, any solution that was substantially less favourable to debtors risked leading to more non-performing loans – and the deadweight losses associated with more widespread bankruptcy. On the other hand, it might have been possible to do something that was more targeted, and offered less relief to Argentina's biggest firms that had the greater capacity to weather the crisis.<sup>40</sup>

### **III. Who Paid?**

In 2001, Argentina used its substantial reserves and IMF funds to buy time in the hope its troubles would pass. In the process, it dug itself into a deeper hole and in our view, increased the scale of the resulting crisis.<sup>41</sup> As a result of this strategy, most Argentines incurred larger losses than they might have. But it is important to be clear. No strategy would have avoided large losses. Argentina's exchange rate was substantially overvalued, and correcting the real overvaluation required a fall in the real income of most Argentines. Most domestic Argentine financial assets were dollar-denominated claims on borrowers who had no way of earning enough dollars to pay their debts in full. This implied a domestic restructuring that would substantially reduce the real value of domestic financial assets. The need to realize such losses was hidden so long as Argentina sustained the 1 to 1 peg, but would become apparent as soon as the peg collapsed. Yet postponing the collapse only increased the scale of the eventual losses.

But even if delay increased losses overall, some benefited from it. The \$16 billion of domestic depositors who fled the banking system in 2001 and parked their funds abroad were the biggest beneficiaries of delay.<sup>42</sup> The real domestic value of their assets increased substantially after the devaluation. The banks' short-term external creditors that cut their exposure by \$8 billion benefited as well. Some external bondholders – notably those holding the \$6.5 billion that came due in 2001 – clearly benefited from the delay, as did the investment banks that collected fees from Cavallo's mega-swap.

Big losers include all those who provided additional financing to Argentina in 2001: the IMF, which provided roughly \$10 billion in net new financing; those with accounts in Argentine pension funds, and all Argentines who kept money in the banking system whose best assets financed the deposit outflow, leaving a lower quality portfolio to back the remaining deposits. Beyond 2001, it is far harder to say who has paid the cost of Argentina's decisions to abandon convertibility, default and pesify.

But some winners and losers are emerging. Winners include Argentina's exporters and import competing industries, particularly the booming agricultural sector. The tradeables producers gained from the devaluation, and, if they had borrowed locally in dollars, also gained from pesification. Indeed, relative to most alternative scenarios, all those who borrowed dollars under Argentine law won – so long as they were not hurt disproportionately by other government decisions. The compensation bonds issued to cover the costs of asymmetric pesification were a subsidy that Argentine taxpayers granted to bank borrowers as well as to bank depositors.

The clear losers are Argentina's external bondholders. Argentina's post-crisis debt issuance has diluted the value of their future claim on Argentina's revenues. Those who accepted Argentina's offer agreed to, in aggregate, reduce the face value of their claims by about 50%, and to accept relatively low coupon payments for a long time (the new bonds issued in the exchange were worth about 32 cents on the original dollar at market discount rates).<sup>43</sup> Argentine taxpayers are another likely loser – they will be paying off the domestic debts Argentina incurred in the crisis for a long time.

Reasonable people may also disagree about the impact of many of Argentina's decisions:

- Domestic bank depositors certainly believe that they are among the losers, even though they did better in the restructuring than Argentina's other creditors.<sup>44</sup>
- Domestic bank owners decry asymmetric pesification and court injunctions (*amparos*) that hurt their banks. But compensation bonds and regulatory forbearance have helped. Locally owned banks also clearly benefited from the regulatory leeway to value compensation bonds at par. Most foreign banks had to value them at a discount.
- Regulated utilities condemn the price freeze even as they gained from the pesification of their domestic debts. Domestic energy firms were hit especially hard as their prices remained frozen while world energy prices rose.
- Argentine workers saw their real wages fall – particularly if measured in dollar terms. But some fall in Argentines' real incomes was inevitable even if convertibility had survived. Urban poverty rates rose steadily during the 1990s recession, reaching 38% before the devaluation. Poverty surged following the devaluation, peaking at 58% in October 2002, before falling back to 48% toward the end of 2003. But with the peso so overvalued, if Argentina had continued to adjust through deflation, real incomes would have fallen in any event over time. The depreciation brought forward the increase in poverty that was bound to accompany Argentina's external adjustment. Unless Argentina redistributed national income towards the poor, the large overall fall in its national income was bound to bring a large increase in poverty.

The poor were not hurt directly by Argentina's default (they had little savings in the banking system), but rather by the rise in unemployment and the increase in the price of basic necessities. In many ways, the difficulties of the urban poor are the mirror image of the gains of many farmers. Basic foodstuffs are a tradeable good priced in dollars: farmers gained substantially from higher peso prices for their products after the devaluation while the urban poor were hurt. In this context, using the proceeds from the export tax to pay a subsidy to the poor (the "heads of household" program) can be viewed as a way of redistributing gains from the devaluation to help those hurt the most.<sup>45</sup> But overall, the government's perilous finances constrained its ability to ease the suffering of Argentina's vulnerable population. Before the default, the government had to squeeze all domestic spending just to free up more resources to cover rising interest payments. After the default, the government could not suspend



domestic interest payments without imposing further losses on bank depositors, and it could not print money without creating inflation, which disproportionately hurts the poor. Without access to credit, the government had to finance all spending out of tax revenues, further constraining its ability to provide major transfers to Argentina's poorest. Overall government spending on the poor increased after Argentina's default and devaluation, but the rise did not keep pace with growing poverty, so spending per poor person fell.

## IV. Conclusions

No easy crisis path was open to Argentina in 2001: defaulting and devaluing faster might have reduced the overall losses, but these would have been large in any event. Nonetheless, the IMF got both the economics and politics wrong by continuing to support Argentina's attempts to cling to its peg and avoid a restructuring through 2001.

In 2001, the IMF bet that Convertibility would succeed, or, at a minimum, that the IMF's continued support of Argentina would be better for the IMF politically, even if it did not work economically. However, the IMF underestimated the extent to which it would be blamed for backing a failed system and helping Argentina dig itself into a deeper hole. In early 2002, wary of backing another failure, the IMF refused to lend to Argentina, and effectively bet that Argentina's attempt to stabilize the peso, the domestic banking system and the government's finances would fail. But the IMF ended up betting wrong twice: Duhalde's economic team, led by Economy Minister Roberto Lavagna, stabilized the financial system and the real economy – admittedly after an enormous loss of financial wealth and a steep fall in output -- without the IMF. By the summer of 2002, the relationship between the IMF and Argentina had changed for good: Argentina's policy makers now looked at the IMF as just another creditor to be satisfied at the lowest possible cost, not as a partner or trusted advisor.

And yet Argentina, not the IMF, bears prime responsibility for digging itself into an ever deeper hole throughout 2001. The only political consensus inside Argentina was to spend Argentina's own reserves and to seek new money to support the status quo. It is striking that Argentina opted to use all its potential sources of flexibility going into 2001 – the banking system's liquid reserves, the pension system's free cash flow, Argentina's capacity to borrow from the IMF, Argentina's relationship with the US government -- not to develop a way out of its economic and political trap, but rather to mount an extended, painful and ultimately futile last-ditch defence of Convertibility.

**Figure 1: Constraints facing Argentina (end 2000)**

	<b>External constraints</b>	<b>Internal constraints</b>
<b>Economy</b>	Currency board Strong Dollar (v. euro, emerging currencies) Weak real External debt (government & private sector) Dependence on int. bond market Small export base Dependence on commodity exports	Currency board Dollarized banking system Dollarized domestic debt Domestic gov. debt Labour market rigidities Rigid utility contracts Small revenue base/ inefficient taxation Shrinking revenues Provincial revenue sharing

<b>Political System</b>	Mercosur	Coalition government Fiscal federalism Opposition governors Opposition-controlled Senate
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**Figure 2: Sources of flexibility (end 2000)**

	<b>External</b>	<b>Internal</b>
<b>Economy</b>	International reserves IMF financing	Liquid banking system Financing from pension system
<b>Political System</b>	Relationship with IMF Bush Administration focus on Latin America (pre-9/11)	Economists with domestic and external political capital (Lopez-Murphy, Cavallo)

The IMF cannot prevent a country from squandering its own reserves. However, the IMF is under no obligation to lend a country additional reserves. The lack of local “ownership” may well be a good reason for the IMF to withhold funding – the authorities are unlikely to implement policies in which they do not believe. However, the presence of local “ownership” should not be used by the IMF to absolve itself of responsibility for key choices. Political elites don’t always have incentives to use the IMF’s funds wisely. Sometimes, they have strong incentives to use the IMF’s funds to gamble for resurrection, no matter how small the odds of success.

No one in Argentina wanted to “own” the painful steps it had to take to escape from the trap created by extensive dollar debts and an overvalued exchange rate. The same can be said of the U.S., the other G-7 and the IMF. As 2001 came to a close, both the IMF and the U.S. doubted whether Argentina’s rescue would work. The IMF initiated a series of internal papers exploring alternatives. But rather than help Argentina develop a plan B, they focused on avoiding responsibility for the messy decisions Argentina would have to take after its devaluation and default. Argentina made its share of mistakes. But the international community’s criticism of Argentina should be tempered by a recognition that when a regime it had endorsed and financed came under stress, most players far preferred Argentina to make mistakes on its own than to make mistakes following the advice of the IMF, the U.S. or the G-7.

## Endnotes

<sup>1</sup> To be clear, Argentina's currency board was not a pure currency board any more than Hong Kong's currency board is a pure currency board. Argentina committed to maintain sufficient reserves to match its currency base – the basic idea behind a currency board. But it also allowed some of the “reserves” that backed the currency to be invested in Argentine dollar bonds rather than “classic” reserve assets. It also kept more reserves on hand than required to back the currency, which gave Argentina more flexibility than allowed in a classic currency board. It could, for example, lend its surplus reserves out to the banking system without necessarily contracting the monetary base. Schuler calls it a “currency board like system” or a pseudo-currency board. An orthodox currency board “does not hold significant domestic assets, does not engage in sterilized intervention, does not lend to the government and does not act as a lender of last resort to the banks.” See Schuler, Kurt. 2005. “Ignorance and Influence: U.S. Economists on Argentina's Depression of 1998-2002. *Econ Journal Watch*, August, volume 2, number 2.

<sup>2</sup> An Economist article at the end of 1997 contrasted Latin banking systems with Asian banking systems, suggesting Asians crisis economies would be well advised to follow the Latin model – exemplified in Argentina.

<sup>3</sup> Domestic banks financing is generally an imperfect substitute for external financing, since there is no net inflow from abroad. However, in 2001, the government loosened reserve requirements, allowing the banks to sell U.S treasuries and similar high quality external assets to increase their holdings of domestic government bonds, generating a capital inflow of \$2 billion.

<sup>4</sup> Perry, G. and Servén, L. (2003). *Argentina: What Went Wrong*. The World Bank: Washington, D.C. (May). The World Bank estimate that the peso was overvalued by roughly 40%, with roughly half the overvaluation explained by the dollar's appreciation. See also Independent Evaluation Office (2004), “The IMF and Argentina, 1991-2001,” Washington, DC: International Monetary Fund (September 30) and Mario Blejer (2003), “Managing the Financial Crisis in Argentina,” Powerpoint Presentation at the World Bank's “Practitioners of Development” Seminar series, Washington, DC: World Bank (October 22).

<sup>5</sup> Roubini, N. (2001). “Should Argentina Dollarize or Float? The Pros and Cons of Alternative Exchange Rate Regimes and their Implications for Domestic and Foreign Debt Restructuring/Reduction.” New York University (December 2), unpublished [www.stern.nyu.edu/~nroubini/asia/argentinadollarization.doc](http://www.stern.nyu.edu/~nroubini/asia/argentinadollarization.doc). Roubini emphasizes that the real exchange rate adjustment brought about by deflation increases the real burden of foreign-currency denominated debts in the same way as a nominal depreciation. Both reduce “peso” revenues (one through falling peso prices, one through changes in the peso/ dollar) while leaving dollar debts unchanged. Deflation, however, occurs more slowly – something that is both a blessing and a curse.

<sup>6</sup> From Perry and Servén (2003), *Op. Cit.* and International Monetary Fund (2003). *Argentina: Request for a Standby Arrangement and Request for an Extension of Repurchase Expectations*. Washington, D.C.: International Monetary Fund. (September).

<sup>7</sup> See, among others, Ades A. (2003), *Emerging Market FX and Bond Views*, Goldman Sachs, October 30.

<sup>8</sup> *Wall Street Journal*, January 13, 2004.

<sup>9</sup> The 2001 IMF program assumed that Argentina would retain access to captive domestic sources. However, the domestic banking system and pension systems were nowhere near large enough to provide all of the \$20 billion in bond financing the government needed.

<sup>10</sup> Cavallo reduced mandatory reserve requirements to free up bank credit (notably allowing the banks to invest \$2 billion of their mandatory reserves in a new government bond), introduced a set of tax subsidies to help firms facing competition from Brazil and signalled his intent to change the currency board from a pure dollar peg to a dollar-euro peg, but only when the euro reached parity with the dollar.

<sup>11</sup> The swap did not cover Euro denominated bonds, yet these bonds accounted for a large share of Argentina's near term external debt payments.

<sup>12</sup> See Roubini, N. and Setser, B. (2004). *Bailouts or Bail-ins*. Washington, D.C: Institute for International Economics for a more detailed critique. Also see Mussa, M. (2002). *Argentina and the Fund: From Triumph to Tragedy*. Policy Analyses in International Economics 67. Washington, D.C.: Institute for International Economics. March 25.

<sup>13</sup> Miles, V. (2001). "Argentine Banks, Why deposits hold the key". JP Morgan. July 23.

<sup>14</sup> See Mussa (2002), *Op. Cit.*, p. 40-46.

<sup>15</sup> Short-term lines fell from \$28 to \$20 billion during the course of 2001. World Bank (2003). *Global Development Finance*. Washington, D.C.: The World Bank.

<sup>16</sup> The government continued to tap local banks for financing, particularly those local banks which depended on support from central bank.

<sup>17</sup> Primary expenditures fell from 18.6% of GDP to 17.2% of GDP. Not paying interest on external debt helped, but was not the primary reason for Argentina's fiscal stabilization.

<sup>18</sup> Mussa, M. (2002), *Op. Cit.* Also see Hirschman, 1995.

<sup>19</sup> Starr, Pamela K. (1997), "Government Coalitions and the Viability of Currency Boards: Argentina under the Cavallo Plan," *Journal of Interamerican Studies and World Affairs*, Vol. 39, No. 2 (Summer 1997).

<sup>20</sup> Rodrik, D. (1996). Understanding Economic Policy Reform. *Journal of Economic Literature* 34(1) argues the "liberalize, stabilize, privatise" policy package typical of many "reform" programs of the early 90s used the large, broad-based gains from ending hyperinflation to help compensate the losers from other reforms, which often had ambiguous or negative distributional effects.

<sup>21</sup> Joyce Chang (2002). Brookings Trade Forum: 2002 Comments and Discussion on the Argentine Papers. Washington, DC: Brookings.

<sup>22</sup> Most Presidents have had a working majority in the legislature as well as the ability to use decree power to shift the power balance between the executive and the legislature. See Romero, L. A. (2002). *A History of Argentina in the Twentieth Century*. (trans. J. P. Brennan), University Park, PA: Pennsylvania State University Press.

<sup>23</sup> 1999 was the only year nominal non-interest spending sharply increased.

<sup>24</sup> The point can be extended even further. Many of Argentina's privatised utilities had the right to index their prices to the U.S. dollar and to increase their prices in line with U.S. inflation even as other prices in Argentina were falling. Neither the utilities nor Argentina's labour unions were volunteering to give up their hard-fought privileges.

<sup>25</sup> International Monetary Fund (2001). Argentina: Second Review Under the Stand-By Arrangement and Request for Augmentation—Staff Report. IMF Country Report 01/26. Washington, DC: International Monetary Fund. See also: International Monetary Fund (2003). "Lessons from the Crisis in Latin America." Washington: International Monetary Fund (October 9).

<sup>26</sup> Gavin, M. (2000), "Argentina update: drowning in a cup of water," UBS Warburg, October 29.

<sup>27</sup> The Argentina and Asian crises, however, were not analogous. Most obviously, several Asian governments had little government debt going into their crisis, though they had large contingent liabilities as a result of weak banking systems.

<sup>28</sup> The political difficulty of selling such a restructuring scenario was compounded by the technical challenges to a pre-emptive restructuring created by the size and diversity of Argentina's external debt. Uruguay's bonded debt was roughly 1/20 the size of Argentina's, with a considerably less diverse range of holders and instruments.

<sup>29</sup> At the end of 2000, Argentina had \$27 billion in reserves and the banking system held an additional \$7 billion in cash and mandatory liquidity reserves in an offshore account. Argentina might have supplemented this \$34 billion pool of reserves with a \$15 billion loan from the IMF. That is almost \$50 billion – plus whatever resources the parent firms of foreign owned banks might have been willing to contribute to help back their local operations. Argentine banks had only \$49 billion in dollar deposits at the time, along with \$18 billion in short-term external liabilities and around 35 billion in peso-denominated deposits. See Lagos, Martin. 2002 (December). *The Argentine Banking Crisis 2001-02*. Buenos Aires: Argentine Banking Association and International Monetary Fund (2004). Debt-related Vulnerabilities and Financial Crises – an Application of the Balance Sheet Approach. July 1, 2004. Washington, DC: International Monetary Fund.

<sup>30</sup> Argentina's currency board never fit entirely comfortably with either economic or political models that seek to explain exchange rate preferences. Economically, it was clearly not an optimal currency area with the United States. Nor was it the small open economy that political theorists suggest favour a fixed currency to meet the demands of commercial

interests. See Frieden, J. (2001), *Political Economy of Dollarization: Domestic and International Factors* and Frieden, J. and Stein E. (2002), “The Political Economy of Exchange Rate Policy in Latin America: An Analytical Overview” in Frieden, J. (2002), *The Politics of Exchange Rates*.

<sup>31</sup> Liliana Rojas-Suarez has noted that Argentina’s banking system was in far worse health than most believed because of its extensive dollar lending to firms that lacked export revenues. She believes this stems from a regulatory mistake: Argentina’s central bank should have clamped down on banking lending (in dollars) to the non-tradeables sector back in 1998 or before, even if this crimped bank loan growth and overall economic growth. If the banking system had less exposure to the non-tradeables sector, exiting from the currency board at an earlier stage would have been somewhat less costly, and thus might have received more serious consideration. See Liliana Rojas-Suarez, Brookings Trade Forum: 2002, Comments and Discussion on the Argentine Papers, Washington, DC: Brookings, 2002.

<sup>32</sup> Suskind, Ron. *The Price of Loyalty: George W. Bush, the White House, and the Education of Paul O’Neill*. New York: Simon and Schuster, 2004.

<sup>33</sup> The size of the August augmentation should not be discounted. Almost all the \$8 billion was made available upfront, so Argentina ended up receiving far more net official financing in the second half of 2001 (under the Bush Administration program) than it received under the Clinton Administration program in the first half of 2001.

<sup>34</sup> Both Robert Rubin and Larry Summers believed Mexico’s exit from its peg was central to the success of the rescue package. See Rubin, Robert E., and Jacob Weisberg. 2003. *In an Uncertain World: Tough Choices from Wall Street to Washington*. New York: Random House.

<sup>35</sup> The Administration’s approach toward Argentina’s exchange rate regime was equally confused. O’Neill’s public statements suggested that Argentina needed to let its exchange rate float. In an iconic moment after Argentina floated, O’Neill’s chief deputy for international affairs, John Taylor, testified in Congress that he believed that Argentina should have dollarized – but that it was not his place to tell this to the Argentines.

<sup>36</sup> In August, it might have been possible to have closed down some locally owned banks without triggering a run on foreign-owned banks, so long as it was clear the foreign owners of foreign owned local banks were willing to back their local operations. By December, this option was clearly no longer viable.

<sup>37</sup> The prospect that a firm’s equity investors would lose control of the firm in the bankruptcy process is the key incentive for payment.

<sup>38</sup> Gelpern, Anna, “Systemic Bank and Corporate Distress From Asia to Argentina: What have we learned?” *International Finance* 7:1, 2004: 151-168.

<sup>39</sup> See Mario Blejer, 2002, “An interview with Mario Blejer,” Central banking Volume XIII.1 (August)

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<sup>40</sup> It should be noted that most large firms had external as well as domestic debts, and were not able to avoid bankruptcy in any case. In some cases (Telefonica), pesification of a firm's domestic loans effectively freed up resources that allowed the firm to offer a favourable deal to its external creditors.

<sup>41</sup> For a similar view, see Ricardo Hausmann and Andres Velasco, "Hard Money's Soft Underbelly: Understanding the Argentine Crisis," *Brookings Trade Forum* 2002. Washington, DC: Brookings, 2002.

<sup>42</sup> Argentines who always kept their savings abroad also won, but they would have "won" even if Argentina had moved more rapidly.

<sup>43</sup> Government of Argentina. 2005. Argentina Announces Results of Successful Exchange Offer (March 18). Buenos Aires: Secretariat of Finance, Ministry of Economy and Production. [www.mecon.ar](http://www.mecon.ar); Republic of Argentina, 2004, "Recent Restructuring Developments," SEC form 18-K/A (September), Buenos Aires: Secretariat of Finance, Ministry of Economy and Production. [www.mecon.ar](http://www.mecon.ar); Damill, Mario, Roberto Frenkel and Martin Rapetti. 2005. The Argentine Debt: History, Default and Restructuring. Buenos Aires: CEDES. August 2005 revision.

<sup>44</sup> Gelpern, Anna and Brad Setser. 2004. "Domestic and External Debt: The Doomed Quest for Equal Treatment," 35. *Georgetown Journal of International Law* 795 (Summer 2004).

<sup>45</sup> For a more detailed assessment, see World Bank (2003). *Argentina – Crisis and Poverty 2003: A Poverty Assessment*. Washington, D.C.: The World Bank. The World Bank's analysis though stops in mid 2002, and thus misses the gains the poor have enjoyed from the strong rebound Argentina experienced in 2003 and 2004. INDEC ([www.indec.mecon.ar](http://www.indec.mecon.ar)), Argentina's statistical agency, provides more recent data. The INDEC data looks at urban poverty. While Argentina's rural areas traditionally have been poorer than its urban areas, the end 2001 devaluation favoured rural tradable good producers, so it is not obvious that the recent crisis had a deeper impact on the countryside.

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