Don't Cry for Greece, Argentina

The Lessons from the Great Depression

By Omar G. Encarnación
Stiglitz and Paul Krugman, to money doctors at the International Monetary Fund (IMF), to the chattering classes in Europe and the United States, those looking for solutions to the Greek dilemma seem to be turning their gaze to the great depression that hit Argentina between 1998 and 2004. Lending credence to the Greek-Argentine comparison is that the structural causes and crushing consequences of the economic crisis in both countries bear striking resemblances. Indeed, anyone can be forgiven for mistaking one for the other.

After years of reckless borrowing and spending by corrupt and incompetent political administrations—all enabled by international financial institutions—the Argentine economy went into a free fall in 2001. With GDP tumbling by almost 30 percent (the same as in Greece) and unemployment skyrocketing to nearly a quarter of the population, millions of
Argentines were thrown into poverty. A run on the banking system forced the so-called *corralito*, or the government’s freezing of bank accounts, to prevent the country from running out of money. This, in turn, set off a wave of antigovernment demonstrations and riots across the nation that left 22 people dead and 200 injured. Hoping to defuse the situation, President Fernando de la Rúa fled the presidential palace by helicopter. He was the first of three presidents and at least five economic ministers who, in less than a year’s time, would try to fix the economy.

More than the crisis itself, though, it is Argentina’s robust recovery since the dark days that is enticing to students of the Greek economic crisis. By 2003, only a few years after the first period of economic contraction, the Argentine economy was roaring back. Between 2003 and 2012, the country achieved one of the longest periods of economic expansion in Argentine history, with GDP growth averaging 7.2 percent each year. In fact, for much of this period, Argentina was the fastest-growing economy in the Western Hemisphere, with its GDP expanding from $100 billion right after the crash in 2001 to $470 billion by 2014.

Alongside the economic expansion, Argentina’s debt-to-GDP ratio began to shrink dramatically, falling from a record 165 percent in 2002 to just 43 percent by 2012, lower than most developed economies (Germany’s ratio is 81 percent, France’s is 90, and the United States’ is 101). Moreover, the wrenching pain that citizens endured was mercifully short-lived. By 2005, household incomes had risen by almost 50 percent, helping lift millions of Argentines back into the middle class.
Unemployment, which at the peak of the crisis stood at about the same level as in Greece at the present time, fell to about seven percent by 2013.

So what about Argentina’s Lazarus-like revival can be applied to Greece? The short answer is: Not much. The reason is that the policy tools that worked like a charm in Argentina, such as an outright default on all foreign and domestic obligations, are not advisable for Greece (or probably for most nations). Those that Greece could potentially adopt, such as devaluing the local currency as a means of boosting exports (which for Greece would mean exiting the eurozone and restoring the drachma), cannot be expected to have the same results as in Argentina, given that the country lacks the vast natural resources that made Argentina’s lifesaving export boom possible.

Nonetheless, Argentina does hold some valuable lessons for Greece. Above all, the fact that Argentina managed to find its way back to economic growth without any external assistance offers a pointed rebuttal to the conventional wisdom about the role of international bailouts during debt-induced economic meltdowns.
DEFAULTING, DE-DOLLARIZING, AND DEPRECIATING

Argentina rebooted its economy after 2001 in three straightforward steps. First, after failing to secure a refinancing deal with the IMF and private lenders, Argentina defaulted on all of its debt obligations, including what it owed the IMF. This made Argentina’s 2002 default on a $95 billion sovereign debt the largest by any nation until Greece’s own $130 billion default in 2012. (The Greek default was soon reversed by a bailout from the European Central Bank and the IMF.) Argentina’s second step was to delink the value of the peso from the U.S. dollar—the “de-dollarization” of the Argentine economy—which entailed the forced conversion of all debts and savings (including private savings) into pesos. In the years leading to the crisis, Argentina had pegged its currency to the dollar as a last resort to cure the perennial problem of inflation. The third and last step was the depreciation of the peso with an eye toward reenergizing the economy by boosting exports.
Defaulting helped Argentina deal with its refinancing problems; it provided quick and meaningful relief in the country’s liquidity crisis. It also allowed Argentina to restructure its debt on its own terms—choosing which creditors to repay, when to repay them, and how much. The decision to default, however, was not a panacea. According to *The Economist*, Argentina managed to repay $9.5 billion to the IMF by 2006, and to reach agreements with 93 percent of creditors by 2012, by issuing new securities at a 65 percent loss. But the country remains mired in legal suits abroad over compensation disputes with those who have refused to accept Argentina’s terms and instead have taken their luck in the courts, mostly in New York. Several rulings have sided with the holdouts, including one from U.S. Federal Judge Thomas Griesa, who called Argentina’s decision to leave its creditors in...
the lurch “immoral.” The Argentine government has ignored the rulings and vows not to give in to the demands of what it calls “vulture funds.” To this day, the country understandably remains excluded from private credit markets—it is in the international equivalent of the doghouse.

De-dollarization allowed Argentina to return to some kind of economic normalcy relatively quickly; for example, the government reopened the banks and started paying pensions and payroll. The move was not without considerable headaches, though. It caused widespread discontent and social unrest, since the conversion entailed the loss of almost half of the value of saving accounts, pensions, and other assets. In particular, de-dollarization represented a massive setback for the Argentine middle class, which for the first time had savings in what everyone assumed were dollar-guaranteed banking accounts. For this reason, many Argentines regard the 2001 economic crash as a worse calamity than the hyperinflation of the late 1980s. During this period, inflationary pressures led to food riots, including a deadly one in Rosario in 1989 that forced the government to declare a state of emergency for 30 days.
Depreciating the peso by some 300 percent in 2002 increased Argentina’s competitiveness relative to other countries in ways that a reduction in nominal wages could have never achieved (at least nowhere near as fast) and brought a massive influx of cash into state coffers as Argentine products such as grain, beef, soybeans, and wines became considerably cheaper than before the crash. Additionally, the country became a haven for tourists. Argentina’s European-styled capital city, Buenos Aires, historically Latin America’s most expensive and glamorous city, became one of its cheapest; tourists, especially from neighboring Brazil and Chile, flocked to vacation spots such as Patagonia and Bariloche.

DEBATING THE ARGENTINE MODEL

Stiglitz, Krugman, and other economists of that caliber have weighed in about the pros and cons of Greece following in
Argentina’s footsteps. They have concluded that there is much merit to the Argentine model. Upon closer inspection, however, most aspects of the Argentine model are simply not transferable, starting with a default—a brazen option that can be entertained only by countries with natural resources comparable to Argentina’s. In fact, defaulting is something of a national addiction for Argentina. According to *The New York Times*, since 1806 the country has done so seven times, including, most recently, last year. The habit is encouraged by the country’s paradox of plenty. That is, the enormous natural wealth in petroleum, minerals, beef, and other agricultural products that allows the country to get back into the good graces of domestic and foreign creditors with comparative ease and to survive without much external help.

For Greece, whose debt is twice as large and whose economy is half the size, defaulting is simply not an option. Greece’s former finance minister, Yanis Varoufakis, all but acknowledged this point when remarking to *The New York Times* that the idea that Greece should default and emulate Argentina is “profoundly wrong.” One key issue is Greece’s entanglement in the eurozone and its relations with its partners in the European Union, which have come to the country’s rescue with two massive bailouts so far: in 2010 and 2012. A third bailout, negotiated earlier this month in the sum of 86 billion euros, remains to be finalized. Another problem is Greece’s inability to make it on its own. Unlike Argentina, Greece depends on imports for most of its core necessities, including petroleum, chemicals, and pharmaceuticals. It is hard to imagine how Greece could operate as an Argentine-style economic renegade, even for a short period of time, without unleashing catastrophe.
Time out from the eurozone—a period long enough to revive the economy through a debt-restructuring program, a depreciated local currency, and foreign aid—is a more realistic option for Greece. This proposal, inspired by Argentina’s de-dollarization of its economy after 2001, is what Krugman, Stiglitz, and many other economists are recommending. But a short-term Grexit is easier said than done, at least when compared with the relative ease with which Argentina managed to delink itself from the dollar. Argentina did not abandon one currency and restore another, since the country never gave up its national currency. It had simply pegged the peso’s value to the dollar, a policy decision that could be easily reversed. Moreover, the de-dollarization of the Argentine economy did not require Argentina to abandon or sever its regional trading arrangements, especially Mercosur.
Greece is in a starkly different situation. Whereas Argentine business contracts prior to the crisis were written in pesos and remained in pesos during the debt restructuring, Greece’s were written in euros. Switching to the drachma or another currency would likely trigger a sea of bankruptcies, as companies would be forced to honor a debt burden denominated in euros with a considerably weaker currency. Moreover, there is the rarely discussed severe psychological blow that Greece’s exit from the eurozone, however short, would entail. Being part of the common currency and the EU is seen by Greece as the country’s top economic and political achievements of the postwar years—the most compelling evidence that the country had made it as a modern, First World nation. Unsurprisingly, it was the complexity and uncertainty surrounding a possible Grexit that forced the Greeks into accepting the harsh terms of the third bailout, which includes accepting more austerity measures and privatizing some $50 billion of state assets.

Finally, there is no reason to believe that restoring the drachma, even a massively depreciated drachma, would have the same positive effect of the depreciated peso in Argentina. The reason for this is apparent: Greece is not, and will never be, the export juggernaut that Argentina is—or that Argentina has become since the economic crisis. Beyond the country’s natural resources, Argentina benefited from a phenomenon that is not likely to repeat itself anytime soon: the crisis had the auspicious timing of coinciding with the expansion of the Chinese and Brazilian economies, both of which had an almost insatiable appetite for Argentine exports throughout the 2000s.

By contrast, Greece’s economy is anchored in tourism and
shipping, and its main exports are fish and cotton. It is hard to imagine how any of this could turn into an export boom. Tourism could certainly grow as a consequence of a weaker currency. But the Greek tourism sector has already drastically reduced prices, hoping to drum up business. And as for increasing production of those things Greece can export, fishing is tightly regulated by the EU to prevent depletion of the oceans and unfair competition among EU members, and cotton does not demand premium prices in international markets. In short, the pain of exiting the eurozone for Greece would be more intense than the very painful process of de-dollarization in Argentina; and the gains would be considerably less significant.

BREAKING AWAY FROM ORTHODOXY

All that said, the Argentine example does contain lessons for Greece, starting with the importance of stable political leadership in the process of economic recovery. Since 2003, Argentina has been governed by essentially the same political administration, the husband-and-wife team of Néstor Kirchner (2003–2007), now deceased, and Cristina Fernández de Kirchner (2008–present) of the Peronist party. Their time in

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office, known in Argentina as “Kirchnerismo,” a present-day spin on “Peronismo,” is one of the longest stretches in power by a political force in Argentine history.

There is much to dislike about the Kirchners’ governing style—their no-holds-barred approach to handling their opponents and the press, corruption and nepotism, and naked political ambition. Even as she is readying to exit office this December, Fernández de Kirchner is widely thought to be plotting her return to power in 2019, which would be allowed under the Argentine constitution. But no one can question the political stability that the Kirchners have brought to Argentina, without which the country’s economic recovery would not have been possible, at least not as quickly. So dire was the political picture during the 2002 presidential election that Néstor Kirchner, then a little-known governor of the Patagonian province of Santa Cruz, won the presidency by default after former President Carlos Menem withdrew from the race.

Another lesson from Argentina is the need to lessen the suffering on society on the way back to economic stability, a point suggested by the Kirchners’ socioeconomic policies, which veered significantly from the neoliberal orthodoxy that prevails among international financial institutions. Rather than embracing austerity, the Kirchners have expanded the welfare safety net, as can be seen in the rise of social spending, from five to nine percent of GDP between 2002 and 2012. The aim of this spending goes beyond targeting poverty, which during the Kirchners’ time in office has been cut from 53 percent to 23 percent, and toward fighting inequality. Programs such as the
Universal Child Allowance target those in the lower-income social strata by providing the children and adolescents from unemployed families, or from families working in the informal sector, with the same benefits as the children whose parents are employed in the formal sector.

Finally, and most important, the Argentine great depression reveals that the path to economic recovery could well hinge on breaking the vicious cycle that bailouts seem to induce, in which debt begets dependency on foreign lenders, misery, and more debt. The cycle is hardly surprising, since external bailouts are generally more concerned with repositioning countries to repay their debt than with creating conditions that can restore economic viability. Lately, the criticism of such “rescues,” traditionally confined to critics of international financial institutions, is coming from one of those very institutions: the IMF. The multilateral organization, which has veto power over the third deal between Greece and its European creditors, has criticized its terms for failing to provide any debt relief, a long-standing demand of the Greeks. In the IMF’s view, the current deal is not sustainable and will likely deepen the crisis.

The IMF’s new thinking gives hope that one legacy of Greece’s pain will be a new international consensus on how to help nations get back on their feet after they suffer an economic broadside, one that provides aid and sustainability rather than more dependency and suffering.
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