1-16-2002

The Argentine Economy - We Should Care What Happened

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January 16, 2002

Cornhusker Economics

Cooperative Extension

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Market Report	Yr Ago	4 Wks Ago	1/11/02
Livestock and Products, Average Prices for Week Ending			
Slaughter Steers, Ch. 204, 1100-1300 lb Omaha, cwt	$78.55	$62.84	$66.07
Feeder Steers, Med. Frame, 600-650 lb Dodge City, KS, cwt	94.83	83.60	89.36
Feeder Steers, Med. Frame 600-650 lb, Nebraska Auction Wght. Avg	96.50	90.52	93.01
Carcass Price, Ch. 1-3, 550-700 lb Cent. US, Equiv. Index Value, cwt	121.04	103.89	102.79
Hogs, US 1-2, 220-230 lb Sioux Falls, SD, cwt	37.00	32.00	37.50
Feeder Pigs, US 1-2, 40-45 lb Sioux Falls, SD, hd	*	44.80	*
Vacuum Packed Pork Loins, Wholesale, 13-19 lb, 1/4" Trim, Cent. US, cwt	110.20	91.40	103.70
Slaughter Lambs, Ch. & Pr., 115-125 lb Sioux Falls, SD, cwt	72.00	55.00	60.95
Carcass Lambs, Ch. & Pr., 1-4, 55-65 lb FOB Midwest, cwt	154.00	128.60	130.27
Crops, Cash Truck Prices for Date Shown			
Wheat, No. 1, H.W. Omaha, bu	3.44	2.98	3.13
Corn, No. 2, Yellow Omaha, bu	1.93	1.94	1.93
Soybeans, No. 1, Yellow Omaha, bu	4.55	4.21	4.24
Grain Sorghum, No. 2, Yellow Kansas City, cwt	3.65	3.62	3.66
Oats, No. 2, Heavy Minneapolis, MN , bu	1.27	2.29	2.19
Hay, First Day of Week Pile Prices			
Alfalfa, Sm. Square, RFV 150 or better Platte Valley, ton	115.00	115.00	115.00
Alfalfa, Lg. Round, Good Northeast Nebraska, ton	67.50	77.50	75.00
Prairie, Sm. Square, Good Northeast Nebraska, ton	100.00	105.00	105.00

* No market.

Argentina is a country known to many Nebraskans as a kindred prairie-based producer of beef, corn, soybeans and wheat -- a friendly but tough customer for some of our agricultural inputs, a competitor in world agricultural markets. The collapse of the Argentine economy is therefore of some interest to Nebraskans. What happened, and what does it mean for us?

The administration's view of the problems there, as expressed by Treasury Secretary O'Neill months ago, seemed to be that the country hasn't tried to develop its export sector, was fiscally irresponsible and that no additional international funds should be provided until these things change. The Argentine export sector is actually about the same size as for the U.S. (9-10% of GNP there vs. 10-11% here), and although Argentine external debts have been growing, external debt as a fraction of GNP was growing but not unusual and they had not defaulted on payments.

Argentine politics are a critical part of this story. At mid-century, when per capita incomes were comparable to those in the U.S., a military coup by Juan Peron ushered in a brand of nationalistic populism with protectionist and anti-U.S. sentiments. For forty years the economy was hampered by slow growth and bouts of hyperinflation, and politics was plagued by coups. The Peronists continued to be the majority party, but after 1990 a new faction wrested control of the party and under President Menem and economic minister Cavallo, the economy was opened to greater world trade and investment, national industries were privatized and the peso was pegged to the dollar at one-to-one. The convertibility between dollars and pesos was a crucial element in establishing the confidence necessary for economic investment and growth.

Prosperity ensued. Between 1993 and 1998, annual growth rates were dramatic: GDP 3.8%; imports from the U. S. 10%, total imports 12%; agricultural exports 15%, total exports 13%; and foreign direct investment 19%.

But in 1999 and 2000 the volume and prices of exports fell (primarily those to Brazil, the largest trading partner) and GNP began to fall, in a recession that continued to worsen through 2001. Government receipts fell while expenditures did not, with public budget deficits increasing to around 3% of GNP. This relatively modest level of deficit spending (the deficits were a lower fraction of GNP than in the U. S. during later years of the first Bush administration and early Clinton years) did not pull the country out of recession, but it did increase foreign debt at the rate of 8-10% per year at a time when international investors were skittish and their interest rates were rising. Given the clumsiness of fiscal policy in combating recession, it would have been desirable to loosen monetary policy (as the U. S. Federal Reserve has done dramatically in the past year). But monetary policy was bound in the straightjacket of convertibility, a pillar of the policy reform that was strongly supported by the international financial community. Furthermore, the international financial community began to demand a balanced public budget as a condition of further loans, which exacerbated the recession and left the government no macroeconomic policy tools other than gimmicks to re-instill the confidence of consumers and investors. The gimmicks didn't work. The government did not generate enough revenue to meet its international and domestic obligations (even though the latter had been reduced substantially), international lenders stopped providing additional loans and the government froze personal bank accounts to stanch a surge of cash flowing out of the country.

Chaos followed when, some say with the encouragement of the original populist factions of Peronism, the public expressed its dismay and disgust by demonstrations and strikes that forced the exit of President De la Rua and Cavallo (a fate shared by the other two non-Peronist governments of the past half-century). The populist faction of Peronism emerged in control by early January, with new President Duhalde promoting a return to earlier policies such as suspension of payments to foreign lenders in favor of promises of job creation at home, abandonment of peso-dollar convertibility in favor of a two-tiered exchange rate, continued freezing of bank deposits and involuntary conversion of dollar deposits to peso deposits. Appeals to the IMF for new loan advances have continued, however, and it seems likely that the IMF will belatedly loosen its purse strings to provide the liquidity necessary for economic recovery.

With a devalued peso, Argentine agricultural exports will be cheaper on the world market, making it a tougher competitor for Nebraska agricultural products. The $15 million of Nebraska goods that Argentina has been importing annually will diminish drastically because of their higher cost in devalued pesos. Nebraska investors in TIAA-CREF and other funds that hold Argentine bonds will take a capital loss due to the devalued bonds. And not least, the U.S. will receive much less political support from a populist-oriented Argentine government for our foreign policies such as those in the Balkans, in the campaign against terrorism and in promotion of western hemisphere trade agreements. Most of these unfortunate consequences could have been avoided with a little more visionary policy of international financial support for our friends and allies.

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