

## Don't Cry for Me Argentina

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In November last I was in Argentina, the country of Evita Peron, for a Liberty Fund colloquium on whether commercial banks should back deposits with 100 percent ready money to avoid runs when confidence falters. What I have come to think about fractional reserve banking I will leave for a later column. Today, my topic is almost as distressing as that of banking crises, for it deals with the future of Argentina and other Latin American countries that follow the same populist path as that perpetually ailing country.

On my way to the city of Rosario where the colloquium was going to take place, I was told that the official rate of exchange was nothing short of extortionate. Foreign trade is the soul of Rosario. It is at the center of one of Argentina's most productive agricultural regions: soya, corn and other cereals, and formerly large amounts of beef are exported to the world through some twenty private ports on the river Paraná. (I say 'formerly' because the Argentine government has been trying to fight inflation by stopping meat exports to lower the local price of beefsteaks: the result, Uruguay has now more cattle than Argentina.) It could not be so difficult to find some establishment in Rosario where I would be quoted a price for my dollars that would take into account the galloping inflation.

The hotel concierge offered me the stingy amount of 8.50 pesos per U.S. dollar, which would make what I bought or spent in Argentina prohibitively expensive. I objected, "But that is the official rate; could you not give me the black market one?" Very correctly, the concierge answered that the only rate they were allowed to offer was the official or 'white' rate. I could get a better price ("Don't say 'black market rate,' but 'blue rate,' please.") at a small restaurant some blocks away. I walked to that establishment where the owner offered me 11 pesos per U.S. dollar—nearly thirty per cent more than the official rate. I suppose I could have bargained for more, but I was content with having both sides profit. In any case, the white and blue colors by which Argentinians call the official and the parallel rate piqued my curiosity and I decided to learn more about this multicolored currency.

The first step was to distinguish the official currency rates from those quoted on other more or less shady markets. The legal rate for 'white' dollars was indeed the overvalued one the hotelier had quoted me. However, to say that one *can* buy dollars even at this distorted rate is disingenuous, because the authorities will only grant permission to do so if they consider the buyer a person of sufficient means. Two months ago, a grandfather took the federal government to court because he had been denied

permission to buy US\$10, which he wanted to give his grandson. The President of Argentina, Cristina Fernández Kirchner, had the cheek to mock him in a television fireside chat for being such a miserly grandfather.

This is not the end of it. Since all real estate transactions in Argentina are conducted in U.S. dollars, one is permitted to purchase dollars from one's bank at the semi-official 'azure rate' of 10.71 pesos per U.S. dollar, on condition the notary avers that they are being invested in property. When tourists pay with a foreign credit card, the shop-keeper or the hotelier applies the 'gold' rate of 11.56. And when a soya exporter brings back the sums obtained with his exports he will only be paid 5.53 pesos per U.S. dollar, and that after the deduction of a profit tax of forty per cent. So the state exploits people who do not trust the local currency and want to sell their goods for dollars.

For more on these topics, see the EconTalk podcast episode [Foreign Exchange](#) by Jeffrey A. Frankel and in the *Concise Encyclopedia of Economics* and "[Why Private Banks and Not Central Banks Should Issue Currency, Especially in Less Developed Countries](#)", by Lawrence H. White and George Selgin, April 9, 2000, Library of Economics and Liberty.

This public policy has given rise to a lively *black market* (excuse me). Just before Christmas the illegal price for 'blue' dollars at exchange shops was 12.87 pesos. If one lived in Buenos Aires, one could buy so-called 'green' dollars at the better rate 13.07 pesos. Why 'green'? The dealers who pay this rate stand planted, so to speak, in Calle Florida in the country's capital city, and the ever humorous *porteños* call them 'arbolitos', or 'little trees'—hence green. Finally, if you badly need dollars to import parts for your car factory or tires for your tractors, the inexhaustibly inventive Argentinians have found another, though more risky way, of supplying them, by purchasing state bonds for pesos and selling them for dollars on Wall Street—at the 'grey' rate of 11.47 per cent.

### Argentina's plight

This welter of prices for the national currency may seem anecdotal, but in truth it is a symptom of the dire situation of Argentina's economy and polity. Economists call all this toing-and-froing the 'shoe-leather cost' borne by ordinary citizens who try to minimize the burden of inflation. The government prints too much money and tries to force individuals to accept the devalued pesos willy-nilly; the long suffering individuals then look for ways to get rid of this funny money for the highest value that can be got; the hope is to invest one's savings in a currency that does not melt like snow on the high peaks of the Andes in summer.

Since exchange rates are in the end related to the purchasing power of the respective currencies, the first thing to be asked is the rate of inflation in Argentina. The concept of a cost of living index, by which inflation is usually measured, is itself an abstraction, since every person buys a different basket of goods and therefore sees the value of money change differently. Despite this, many countries calculate inflation with the help of a weighted average rate of consumer price increases. Unfortunately, there was no such a thing as a well calculated inflation rate for Argentina. Some provincial governments do calculate the rate in their territory; others did in the past but have given

up. The government, after demoting the Statistical Office to the rank of a mere bureau within the Ministry of Economics, finally started compiling a national price index in February 2014. The Minister of Economy, the young Keynesian Axel Kicillof, has set the inflation rate for the present year at 24 per cent, while the opposition parties in the Argentine Congress claim it is above 41 per cent. Public opinion tends to believe the pessimists, if one can call Kicillof's rate optimistic. Whichever figure is right, inflation will in the end have the effect of stopping economic growth.

The question to be asked at this point is, why are prices climbing so fast? As [Milton Friedman](#) used to say, "Inflation is always and everywhere a monetary phenomenon". The National Bank of Argentina must be creating an excessive money supply. This usually happens when the government cannot cover its expenses with its tax intake. And in fact, Argentina shows a large and increasing budget deficit. Public debt becomes more and more expensive to issue and the public starts to suspect that in the end the government will have recourse to 'print' the money it needs to spend.

From 2001 up to 2007 Argentina's public accounts showed a surplus. But public expenditures have been going up relentlessly since 2002, especially to pay for an increasing number of public employees and to defray the costs of ever more generous social services. There has been an attempt to finance these growing expenditures by applying fiscal pressure: the take has gone up from around one fifth of GDP in 2002 to one third in 2014, an increase of 11 percentage points in twelve years. When the product of taxes and Social Security contributions started to falter in 2007, the budget deficit came back. It is now at more than 6 per cent of GDP and growing. So the government issued debt. The figure stands at over 38 per cent of GDP, which sounds small in comparison with the debt of developed countries. But such is the plight of poor nations—and the curse of rich nations which seem to be able to bear debts greater than their GDP. The late clashes of the Argentinian State with its foreign creditors show that the present budget deficit is simply not sustainable.

The irony of this situation is that the deterioration has coincided with ten very favorable years with regard to agricultural, mineral and oil prices: from 2007 to 2013 the terms of trade for Argentina improved by 75 per cent. Despite this, the basic balance of payments is now in growing deficit and the official exchange rate keeps falling despite the Central Bank having spent \$25 billion from its reserves in propping up the peso. The terms of trade advantage has thus been squandered. During the presidency of Nestor Kirchner and the first term of the Presidency of his wife, Cristina Fernández Kirchner, growth and populist redistribution seemed to go hand in hand. [Joseph Stiglitz](#) even spoke of an "Argentinian model" to be imitated in other progressive developing nations and especially by Europe. Now the rate of growth expected for Argentina in 2015 is minus 4.5 per cent.<sup>1</sup> Good old Stiglitz, always backing the wrong horse!

### The legacy of General Peron

But who is this Cristina Kirchner? What is the origin of her world-view, now shared by other populists in Latin America and in the European Union? Why does she hail back to 'Peronism'? The only thing the advanced world seems to know about this congeries of ideas and endeavors is the musical *Evita*. The heroine of this show is Eva Duarte de Peron, Evita for her fans. A second rate actress who suffered the poverty of an illegitimate child, she seduced her political hero, Juan Domingo Peron, who married her

in 1945 when he was running for President. In 1946 he won the election with her decisive help. She never held a government post but took as her own the social policy of the Government during Peron's first stint as head of the country. Her very personal mixture of glamour and sentimentalism caught the imagination of the masses. With the proceeds of the National Lottery she funded hundreds of hospitals, schools, and homes for the aged around the country and personally doled out help to the needy. Attributed to her is the saying, "every need is a right". She was mainly responsible for giving Argentinian women the vote. The "shirtless", or "descamisados" as she called them in Spanish, revered her. I quite remember the delighted surprise felt by the people of the dour Spain of General Franco when she visited us: a bejeweled beauty spectacularly clad in her furs, able to show heartwarming sympathy to the toiling women and men in factories and fields. She died at the early age of thirty-two. Her adoring followers tried to have her canonized by the Church. Her embalmed body suffered a fate worthy of the magical realism of a Latin-American novel: when Peron was overthrown in a coup her body was whisked to Italy, then to Madrid to the home of her exiled husband, then to a crypt in the presidential palace, finally to be buried in the tomb of her family in Buenos Aires.<sup>2</sup>

Cristina Kirchner is ever trying to become Evita; her ideology is still that of Peron. The general, an admirer of Mussolini in his years as a military attaché in Rome, raised the political banner of resistance to the U.S. hegemon in Latin America and tried to define a middle way between capitalism and socialism for his country. His aim was to create a just society, hence the name "Justicialismo" he gave his ideology. That implied nationalism, industrial protection, trade-unionism, and an all-encompassing welfare state.

The figures of Peron and his Evita are the incubus of Argentinian politics, ever present never exorcized. In one form or another Peronism has been in government in the Argentine provinces and in the federal government since 1945, except during the periods of military dictatorship. After Fidel Castro took over Cuba, Peronism found a growing echo in large parts of Latin America, where a number of countries now seek independence (from the US) and socialism (of the 21st century) by joining an organization called ALBA,<sup>3</sup> founded by the late Hugo Chavez of Venezuela.

When Argentina was rich

Between 1860 and 1930 Argentina became the star of Latin America, not only economically but also culturally and in terms of political stability. The economic historian Mauricio Rojas<sup>4</sup> relates how the city and port of Buenos Aires grew to be the metropolis we can still admire today, despite the decadence of the last eighty years. The extermination of the Indians of the Pampas in 1879-80 left the land free to be engrossed by a very small number of powerful landowners, who in effect ruled the republic until the crisis of 1930. They were the class that the Peronists would contend with in the second half of the 20th century. The development of steam transport, both by rail and by ship, opened a huge market for the wool, wheat, and beef Europeans craved. Argentina also opened its shores to poor immigrants of Italy and Spain, who mostly went to the cities and started shops and small industries. Exports were the mainstay of landowner prosperity, consumer industry the supplier of the urban middle class. The value of real exports multiplied 13 times from 1865 to 1914. Industrial production and the railways

also expanded—so that the average yearly growth of the Argentine economy from 1869 to 1914 was more than six per cent.

However, far from being an ultra-liberal economy and a paradise of free trade, protectionism gathered strength all through the last quarter of the 19th century, as Dr. Rojas shows. Strangely for an economy whose engine was foreign trade, there were continuous tariff hikes, despite the complaints of exporters who faced retaliation. Local wheat and maize producers obtained a tariff to protect them from foreign competition. This was also the case with refined cane sugar. Especially after 1900 local consumption industries were able to hide behind a tariff wall, which reinforced the tendency in Argentina towards shallow industrialization concentrated on finished goods. Argentina was lucky to be at the receiving end of long term foreign capital investment in railways, port facilities, urban equipment, and trade services but growing anti-foreign capital rhetoric lay the ground for expanded protectionism. Oil was the special point of contention and Standard Oil became the whipping boy of nationalism. As ever, foreign capitalists were portrayed as leeches sucking excessive profits from a subject country.

In the Roaring Twenties the weakness of the Argentinian economy began to show. Agriculture needed foreign capital and better management. Industry was not ready to compete in the world either, turned as it was mainly towards the domestic market. Also, social tensions increased after World War I, in sympathy with a new spirit of confrontation fostered by the example of the Russian Revolution. The day of reckoning came on Black Friday 1929. Suddenly, the market for primary goods dried up. Industrial sectors could survive only by selling on the domestic market. The situation worsened with the sudden surge of protectionism among Argentina's customary clients. The Smoot-Hawley Tariff of 1930 caused immense harm in Argentina and around the world. The United States and other advanced countries have much to answer for the harm done to Argentina and more generally to economic freedom in the years after the Great Depression.

### Populism in the World

I need not spend much time in describing Peron's policies when he was elected President in 1946. They are those of Cristina Kirchner and of the other national-populist governments of Latin America today—only the present economic climate has changed radically and those dreams have turned into nightmares. Colonel Peron was pro-Nazi during World War II and maintained his anti-Americanism all through the fifties. As President, he set in motion a massive redistribution of income and property with forcible wage increases and a wide array of social benefits and entitlements. Docile trade unions became an instrument of state-power. Agricultural exports, except cotton, were centralized and monopolized under a State Trade Board. The profits from the primary goods trade monopoly were channeled towards an aggressive policy of industrialization, with state-controlled companies at the forefront. The domestic market expanded behind ever higher tariff walls. As a consequence of all these developments the weight of the state in society increased immensely.

As I went from pillar to post in search of a good price for my dollars I thought I saw Colonel Peron and dear Evita round every corner. Only those policies which looked so promising and patriotic half a century ago were in tatters in the fair land of Argentina. That is why I watch the development of populist movements in the world today with

some despair for our lack of conviction in the practice of capitalism. All this is our fault—Peron, Evita, Kirchner, Chavez, Evo Morales, the mild revolutionaries of southern Europe, the protectionists in the United States and the United Kingdom. Liberal democrats who pose as the standard-bearers of capitalism have promised the impossible: to keep our economies growing while resisting competition and guaranteeing an ever more generous welfare state. The recent crisis should have been an object lesson in the failure of our middle of the way policies. We in the advanced nations do not want to recognize that a huge state sector doling out generous supplies of money to keep private industry happy is simply unsustainable. Populism is our Dr. Frankenstein, who now has turned angry because he believes that the recent crisis was due to too little rather than too much Peronism.

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## Footnotes

[1.](#)

Source for the data is a presentation at Rosario by José Luis Espert, on November 10, 2014. See <http://www.espert.com.ar>.

[2.](#)

The entry in the *Encyclopedia Britannica* draws a fetching portrait of this political star. Tomás Eloy Martínez has written a masterly novel on the travels and adventures of her embalmed body, called *Santa Evita* (1997), where fiction becomes reality and long suffering Argentina is shown to have found her defining myth.

[3.](#)

ALBA is the acronym of the "Bolivarian Alliance for the Peoples of Our America", encompassing countries going from Cuba in the Caribbean to Ecuador and Bolivia in the Andes. It was founded to counteract ALCA, the U.S.-inspired "Free Trade Area of the Americas". The countries in ALBA are in close contact with MERCOSUR, the attempted customs union of the South of the Continent, whose principal members are Brazil and Argentina.

[4.](#)

Mauricio Rojas: *Historia de la crisis argentina*. (Cadafal and Timbro, 2001).