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MACROCOSM

Argentina: A Victim of Foreign AIDS

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Do cry for **Argentina**. Overnight confirmation that the peso/dollar fix is finally being jettisoned will almost certainly begin an extended period of high and rising inflation -- if not outright hyperinflation, plunging standards of living and political and social unrest in Argentina. The initial effort to limit the devaluation to 40% looks like a very short-term fig leaf for a government that has given the market no reason to believe that it will stand behind the peso at any level. In all likelihood, the throwback Peronistas that have taken power will offer no more than a token defense of the exchange rate if it requires spending a significant portion of their remaining $12 billion in dollar reserves. Moreover, with tax revenues collapsing along with the economy, before long the temptation will probably prove irresistible to run the printing presses to cover the budget shortfall. Historically, that's been the favorite Argentine recipe for hyperinflation

Among the more disturbing and exasperating aspects of this depressing event has been the wrongheaded interpretation of the roots of the crisis that has attained the status of accepted wisdom. Reading accounts of the Argentine smashup in various media outlets, one could easily conclude that the Argentines were done in by their desire to maintain a stable value for their currency and to undertake various market reforms -- including free trade, deregulation and privatization. The implication is that while these may be worthy policy objectives for the U.S. and other First World industrialized economies, they are the kiss of death to developing Third World countries that lack the maturity to abide by the rules of participation in the global market.

The propagation of this twisted version of reality provides a very convenient out for some of the major institutions of Western capitalism whose fingerprints are all over the sad Argentine spectacle. Start with **Fed Chairman Alan Greenspan**, whose super-tight monetary policies of the late 1990s were directly transmitted to Argentina through its one-to-one peg with the U.S. dollar. While the U.S., with its long contract lengths and extended maturity of debt, can absorb such deflationary errors gradually over time, countries like Argentina have no such luxury. The Argentine price level has been falling for three years, and the accumulating burden of the currency's real appreciation negatively impacted not only the country's external competitiveness but increasingly squeezed domestic debtors and resulted in falling tax revenue.

The country's deteriorating budget picture, of course, did not escape the sharp eye of the **IMF**, which the Argentines had been forced to abide for a number of years under various lending programs. Almost overnight, a bad situation became considerably worse, as the IMF austerity medicine of tax hikes and budget stringency had the predictable disastrous results. Under IMF mythology, balanced-budget austerity is intended to restore confidence among foreign creditors that their debts will be repaid. In the IMF medicine kit, there is no room for policies intended to boost tax receipts and reassure creditors by encouraging growth. Now, the poor Argentines will serve as another object example of the miserable consequences of IMF prescriptions which invariably fail due to this blind spot. TM

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