



Argentina: Time for a Course Correction

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To paraphrase Baroness Margaret Thatcher, “The problem with populism is that eventually you run out of other people’s money.”

And populism in Argentina nowadays *is* running out of money, thus conforming to a cycle that has always been observed with populism everywhere it has been tried – especially in Argentina.

Eventually, it always runs out of the genuine tax resources, out of credit, out of the “savings” from not paying the bills, and out of usable international reserves, and then it loses credibility with local investors, the confidence of bank depositors, and the control of the streets necessary for the government to keep doing what it has been doing, which is:

- 1) Increasing government spending ever faster than revenues.
- 2) Maintaining key prices (like energy and public utilities) artificially low via controls or subsidies.
- 3) Keeping interest rates below the true pace of inflation.
- 4) Undermining property rights, including through the expropriation of private pension and other assets without compensation.
- 5) Leaning on the central bank to hand over more and more of its hard-currency reserves.

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- 6) Preventing cheaper imports from coming into the country, and forcing companies to export what they don't produce.
- 7) Stopping people from buying dollars, and saving or spending them as they wish.
- 8) Appeasing the labor unions by decreeing large wage increases, while letting companies increase most prices as much as the market will bear.
- 9) Bullying political opponents, intimidating the press, annoying your regional neighbors, and picking fights with the United States.
- 10) And last but not least, covering up the nature and scope of the problems that populism has created.

Add to the inherent, fatal flaws of populism as a development model an increasingly autocratic leader with narcissistic personality disorder and great ideological inflexibility, who has surrounded herself with an increasingly small circle of "yes" men and women, and you have all the ingredients for a movie with a very bad ending.

Indeed, the way things are going, I am certain that President Cristina Kirchner will not make it to the end of her term in office. Consider the following highlights of 2012:

- 1) She made a lot of political enemies, while at the same time losing many allies.
- 2) After several years of rapid economic growth, and despite record-high commodity prices, the economy stagnated, and it did because the business climate has been ruined.
- 3) The central bank expanded the money supply at an annual rate of nearly 40%, versus a pace of 20-30% prior to 2012, sowing the seeds for faster inflation this year.
- 4) Many companies have lost their international competitiveness and profitability, and they are no longer able to afford wage increases that keep up with true inflation, such that their workforce and labor unions are getting restless. There will be more strikes and demonstrations in 2013.
- 5) A real estate bubble that kept many people feeling rich has now been pricked, so many in the middle class are unhappy about the precipitous drop in property prices.
- 6) There have been a series of huge street protests against the government as well as episodes of supermarket lootings, and also fatal accidents involving mass-transit (railroads, mainly) due to poor maintenance, all in the context of rising street crime,

such the level of public insecurity and discontent has really increased. This explains the collapse of President Cristina Kirchner's popularity.

7) Access to and use of external finance by the public and private sectors has dwindled, the gap between the official and unofficial exchange rates has never been wider, Argentine bond prices are severely depressed, and the noose around Argentina is tightening – in terms of court judgments against it and negative attitudes at the IMF and at the U.S. State Department.

So the question is whether “Captain Cristina”, as her loyalists called her when she went to Mar del Plata to greet the returning *Fragata Libertad*, is at all capable of tacking the tall ship of state in a constructive direction. That is the \$60 billion question.



As things stand, she is sailing the vessel directly into the wind, but no tall ship can do that and get to where it wants to go. The ship has to be turned away at an angle and then it has to zigzag, sailing as close to the wind in one direction and then changing tack to have the wind blowing on the other side of the sails. It is by tacking continually that a tall ship can sail in the direction from which the wind is blowing.

I'm sure that if her late husband Néstor were in command of the ship of state he would be tacking continually, but Captain Cristina is a very different person. I think that her political ambition has blinded her, and I fear that she may end up like the real-life captain of the HMS *Bounty* replica. As you may have heard, for some unfathomable reason that captain decided last October to leave safe port and set sail straight into Hurricane Sandy, one of the biggest storm systems ever to hit the East Coast of the United States – and he ended up sinking the *Bounty* off of Cape Hatteras, and drowning with it. For Argentina's sake, I hope that I'm wrong and that Captain Cristina will soon learn how to sail the ship of state – and that means how to change tack.