Crises, Reforms, and Reversals
in Argentina, Chile and Peru

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April 2014

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Before I begin with the motivation let me tell you a story...
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Balance of those decades and the decades after...
Figure: Peru: 1980-2013
Luck?

- Has success been luck?
Chile in Figures

Figure: Chile: 1980-2013
Argentina in Figures

Figure: Argentina: 1980-2013
Three common histories

- Argentina, Chile and Peru remarkably similar histories:
  - 50-70s era of classical Latin American populism
  - Crises followed: hyperinflation, GDP decline
  - Violent Transitions
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  1. Fiscal Discipline Reforms
  2. Privatization
  3. Social Security
  4. Central Bank Independence
  5. Others: market-based price systems, labor reform, tariffs
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- ...but Argentina is different
  - Why?
Reversals in Argentina

Carlos Saul Menem President
Peso-Dollar convertibility wave
Privatization wave
New Constitution and Pension Reform
National government absorbs provincial pension system deficit
Fernando de la Rúa took Presidency.
Devaluation and Default
Central bank non-zero borrowing limits
Kirchner, Nestor
Kirchner, Cristina
Debt Repatriation
Kirchner, Cristina
Closed the private block of pensions
Nationalization of YPF
New Central Bank Mandate
Inflation in Argentina

Figure: Argentina: Official and Unofficial (Internet) CPI index
Our Paper

- **Historical Narrative**
  - Study three parallel histories
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- **Review Descriptive Work of Reform Period**
  - Differences in reforms

→ Employ economic theory to interpret events systematically

Postulate:
Argentina’s inability to fix its political economy of budget deficits

Common theme in other countries...
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- **Postulate:** Argentina’s inability to fix its political economy of budget deficits
  - *Common theme in other countries...*
“Keeping books on social aid is capitalistic nonsense. I just use the money for the poor. I can’t stop to count it.”
- Attributed to Eva Perón. Circa 1950s.

“Placed in a historic transition, I will pay for loyalty to the people with my life.”

“My government policies have been described as liberal [i.e., free market] by certain individuals who like to label reality. I am sorry but you have the wrong label. My government and I are simply pragmatic. This means that I do not pay homage to theories, dogmas or myths. I am an agronomist, but I do not breed cows and I do not believe in sacred cows.”
Negotiations

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- **Fujimori in Peru:**
  - Shining Path
  - Fujimori shut’s down Congress
- **Menem in Argentina:**
  - Menem had to negotiate approval of reforms with Congress
  - Provincial Governments
    - No hard evidence
    - To understand this → Argentina’s political institutions
Popular Opposition in Chile

Figure: Chile: Worker Strikes
Electoral Rules

- **Chile:** Electoral Rules after 89 Constitution
  - Electoral districts with only two slots (similar to US)
  - Coalition formation
  - Municipal elections - same day
  - President appoints local governors
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- **Peru**: Electoral Rules *after 93 Constitution*
  - Regional Proportional Representation
  - Fragmented Unicameral Congress
    - Caudillo-based parties
    - One traditional party - APRA
  - Regional Governments - Low Budget, low participation
    - Limits on infrastructure investment
Electoral Rules

- **Argentina:** Electoral Rules after 94 Constitution
  - Kept Historical Strong Federalism
    - Local congress, constitutions etc. (US Model)
    - In charge of large fraction of spending
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  - Regions key for congressional campaigns (Spiller and Tomassi, 2003)
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    - At all steps of reforms
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  - Provinces can issue debt ⇒ bargaining instrument
Budget Assignment in Argentina

Figure: Argentina: Revenues and Expense Decomposition - 2004
Who determines budgets?

- Scartascini and Stein (2009)
  1. Proposal
     - Executive
     - Negotiations and Approvals
  2. Execution
  3. Performance Balance
Proposals

- Chile - *Strong Executive*:  
  - Proposes Budget  
  - Congress can only reduce individual accounts → no reassignments, increments  
  - Short approval period (30-60 days) → automatic approvals otherwise  
  - Explicit fiscal rules in recent years
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- **Argentina - .... is different**
Argentina - Nominally Strong Congress, but...
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- *De facto* powerful executive bargaining with...
- Powerful Provincial Governors
- Executive vs. Provincial Governors
Budget Proposals - Argentina

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- Mechanism - Spiller and Tomassi (2003):
  - Governors and local party leaders: propel congressional careers
  - Short lived congressional terms

- Tricky part, **not formal institution**
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- On the other hand...
Argentina - Manipulation by Executive

1. Forecast Manipulation
   - Extra surplus: assigned to Federal Accounts

2. Administration of Quota System
   - Tax Collection by Federal Government
   - Choice in timing delivery

3. Use of “Decretos Ley”
   - For emergency purposes
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Once Provinces have their shares
   - Hard to coordinate in Congress
   - **ex-ante:** credible commitments?
Checks and Balances

- Chile: Budget Office of Finance Ministry
  - Systematic Assessment of Performance
  - Punishment: determines spending ceilings following year
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Argentina: two audit and control institutions
- Abuelafia et al. (2009):
  - SIGEN (Executive’s office) ⇒ controlled
  - AGN (Congress’s office) ⇒ bargaining tool
Social Security

- Emergence of Safety Nets:
  - Similar historical evolution
  - Group by group
  - Emerge together with ability to tax

Fiscal Burden:
- Use of entitlements for political leverage

Eighties: Tanzi-Bresciani-Turoni effects for SS

Need to Reform:
- Temptation to use Funds
- Temptation to Promise entitlements

Privatization:
- Chile: national level
- Peru: parallel system
- Argentina: tranch system
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Transition from Pay-as-you-Go to Individual accounts

Chile
- Forced participation of new workers to private system
- Choice between private and public fund for pre-reform participants
- Incentive scheme to join private funds
- 96% by 1999

Peru
- Private System modelled on Chile
- Original failure to attract majority of pensions
- Majority switch to private system (76%) after incentive scheme
Argentina

- Public vs. mixed schemes
- Mixed schemes: pay-as-you-go up to limit
- Individual account, after-limit of contribution
- Reversed in 2008

Portfolio-Investment limits

- Subsidy to public debt - 2006 IMF debt repay
Social Security - Fiscal Burden

Figure: Argentina: Pension Self-Funding Deficit, Source: Centragolo and Jimenez (2003)
Privatization

- Arguments: - Free markets, no government intervention
  - Efficiency?
  - Revenue source to stop inflation quickly

- Argentina raising revenues explicit goal
- 91-94: Average Privatization Revenues 1% GDP
Efficiency or Fiscal Deficits?

Figure: Peru: Budget Deficits of GSE (% of GDP)
Privatization in Argentina

- Fiscal accounts needed those revenues...
Privatization in Argentina

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“I believe we should put a final end to the convertibility plan with a Central Bank that is not limited to preserve monetary stability, but that also preserves fiscal and production stability. A Central Bank that interacts with the real economy is what we need.”

Cristina Kirchner, 01/03/2012
Past Experiences...

- I don’t think I have to say much
- Sargent, Williams and Zha (2009)
  - Illustrate statistically how seigniorage financing is a risky (fragile) game
Conclusion

Figure: Argentina, Protests Against Inflation 04-10-14
Conclusion

- Pecking-order theory of populism funding
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- Pecking order $\Rightarrow$ reversal of reforms
- As revenues sources disappear, potential social unrest
- Argentina will see this cycle, let’s hope Peru is already on Chile’s side
Figure: Argentina: Pension Funding 1987 - 2001. Source: Centragolo and Jimenez (2003)
Figure: Peru: 1980-2013
Chile in Figures

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