
Looking Forward for Argentina

After passing through three interim presidents in barely ten days, the Argentine Congress elected Eduardo Duhalde, the losing Peronist presidential candidate in the 1999 election, to fill the remainder of President de la Rúa's term. The new president immediately made two important decisions: he ratified the sovereign default announced by his short-lived predecessor (Rodríguez Saa), suspending debt-service payments to external creditors, together with a promise of future negotiations to reach a reasonable settlement; and he declared an official end to the Convertibility Plan and its one-to-one peg of the peso to the US dollar. Although the circumstances that led to these decisions were regrettable, by this stage there clearly was no viable alternative to either of them.

Unfortunately, the initial decisions of the Duhalde administration to try to maintain a dual exchange rate and to convert most bank loans, but not bank deposits, into pesos were based on political exigency rather than on sound economics. Within barely a month, economic reality forced the adoption of a unified floating exchange rate for foreign exchange transactions. The exchange rate for the conversion of dollar-denominated bank deposits, however, set a significantly higher value for such deposits than the market exchange rate applied for the conversion of dollar-denominated bank loans—implying huge capital losses and deep insolvency for Argentine banks. Also, a new bankruptcy law was passed that made it far more difficult for creditors to collect on defaulted claims, even if the debtor was potentially in a position to pay. And, a number of Argentine judges made use of an existing “economic subversion law” (dating back to Argentina's past governments and their efforts to suppress dissent) to pressure banks to release frozen deposits under threats of police action.

On a more positive note, the central government negotiated a deal with the provinces for a temporary reduction of transfers from the central government. But the deal involved the assumption by the central government of debts already issued by the provinces and failed to put an effective constraint on the provinces' authority to issue more debt, including debt that circulates as a money substitute. A budget for the central government that projected only a small fiscal deficit was proposed and passed by the Argentine Congress; but this budget was based on highly optimistic economic assumptions.

By mid-May 2002, some progress had been made by the Argentine authorities, including an agreement in principle between the president and provincial governors on a number of key issues. But the specific measures to implement these principles remained to be determined and enacted. Meanwhile, the economy minister, Remes Lenicov resigned when the Congress refused to adopt a key element of his plan to address the collapse of the banking system. All told, the efforts of the Argentine authorities continued to fall considerably short of a comprehensive, consistent, and credible program to achieve economic and financial stabilization and restore prosperity.

Recognizing the extremely challenging situation in Argentina, the international community, in particular the International Monetary Fund, should try to be as helpful as possible to the Argentine authorities in their efforts to stabilize the economy and put it on a path of sustainable growth. Most important, this can be done by making it clear that further meaningful financial assistance will be available to Argentina—on the condition that it develop and implement a consistent, responsible, and credible set of economic policies. This has been the central message of the international community, reinforced by the deliberations of the Fund's International Monetary and Finance Committee at its April 2002 ministerial meeting.

In accord with this approach, as the Argentine authorities make significant progress toward implementing their side of the bargain, it will be important that the international community, led by the Fund, be forthcoming concerning the support that they will be willing to supply and the specific conditions under which that support would be available. At the same time, it is essential to recognize that even with the best efforts of the Argentine authorities, backed by reasonable support from the international community, there is no assurance that stabilization and recovery will be achieved on the initial attempt. Indeed, the challenge is exceptionally difficult because the tragic collapse of the initially successful stabilization and reform efforts of the past decade have left the economy and the financial sector devastated. In addition, the government's credibility—even its legitimacy—has been seriously undermined by its failure to keep solemn commitments to its own citizens and to those who have invested in its economy and its securities. Undoubtedly, this critical prob-

lem has contributed to the delay in finding the political and social consensus essential for Argentina to move forward on the difficult measures necessary for stabilization and recovery. Unfortunately, delay and policy drift are only making the task more difficult.

The Prudent Level of International Support

In this situation, where the capacity of the Argentine authorities to deliver a consistent, responsible, and credible set of economic policies is likely to remain in substantial doubt, the international community must be prepared both to undertake some risks in supplying additional support and to act responsibly in controlling these risks. In this regard, key issues are how much support the Fund (and the international community) should be prepared to supply, over what period, and subject to what conditionality. The Argentine authorities undoubtedly want a very large amount of support to be provided very rapidly to help them to deal with the grave situation of the Argentine economy—subject to conditionality that recognizes immense economic and political difficulties of implementing a successful stabilization program. After all, if the Fund was prepared in 2000–01 to commit a large support package when the situation of Argentina was not as desperate as it is today, should it not be prepared to deliver the nondisbursed remainder of that package, plus a substantial augmentation?

Caving in to this type of argument would not be sound policy. A large support package was committed to Argentina in December 2000/January 2001 for a particular purpose: to give the Argentine authorities one last chance to implement policies that would avoid an economic and financial catastrophe. In keeping with this purpose, the level of support pledged to Argentina was well beyond the normal limits of Fund programs, and most of the support committed by the Fund was from the Supplemental Reserve Facility. This facility has a short maturity (repayment anticipated in one year and required in two years). As in other cases where the Fund has provided exceptionally large support, the idea was that a successful policy effort would enable the country to regain market access and rapidly repay the Fund. Unfortunately, in the case of Argentina, the policy effort failed.

Now, the situation is different. The Argentine economy is in far worse shape than it was in early 2001. But now Argentina does not face the threat of being cut off from private capital markets and the likelihood that this would induce sovereign default and a collapse of the Convertibility Plan. All of that has already happened. Hence, the large amounts of international support that were pledged to help avoid this outcome are no longer relevant. The issue is what level of assistance is appropriate now to

Table 4.1 Payments due to the IMF from Argentina, 2002–06

Payment category	2002	2003	2004	2005	2006
Principal due (millions of SDRs)	3,546	3,153	1,624	2,133	595
Interest and charges (millions of SDRs)	354	196	117	65	16
Total due (millions of SDRs)	3,900	3,349	1,741	2,198	611
Total due (millions of US dollars, at 1 SDR = \$1.25)	4,875	4,186	2,176	2,747	764

SDR = special drawing right

Source: IMF Web site: <http://www.imf.org>.

support the Argentine government's new efforts at stabilization in the country's present situation.

Several important factors must be weighed in answering this question. The Fund already has substantial support outstanding to Argentina—nearly \$14 billion. This amounts to 520 percent of Argentina's quota in the Fund, compared with a normal limit of 300 percent of quota for a member's total use of Fund resources. The already large level of Fund support for Argentina raises four concerns. First, as is indicated in table 4.1, Argentina is scheduled to make substantial repayments to the Fund during the next three years, and a default on these obligations would very seriously disrupt Argentina's relations with the international community. For the next year or two, however, it will clearly be very difficult for the Argentine government to secure the fiscal and foreign exchange resources to make scheduled repayments to the Fund (and other international financial institutions). Accordingly, it seems both reasonable and desirable for the Fund to extend sufficient credit to Argentina to finance the rollover of the repayments that are coming due to the Fund, provided that the Argentine authorities are making good-faith efforts to stabilize the situation.

Second, however, in extending additional credit (beyond rolling over scheduled repayments), the Fund has to take account of the fundamental responsibility to protect the temporary and revolving character of its support. When Fund support to a member is already very large, this is an important reason not to enlarge it further.

Third, in addition to protecting its resources, the Fund is also supposed to be governed by the general principle of "uniformity of treatment." Accordingly, a member that is already making much larger than normal use of Fund resources ought to be constrained in its use of additional Fund resources.

Fourth, even if the present efforts at stabilization in Argentina are highly successful, it is unlikely (especially in view of its sovereign default) that Argentina will rapidly reacquire voluntary access to private interna-

tional capital markets. Thus, in the best of circumstances, Argentina will likely need support from the Fund for some time. And if present efforts at stabilization fall short of success, the future need for Fund resources will be even greater. In this situation, it would clearly be imprudent to commit all of the additional resources that the Fund might make available to Argentina to support the 2002 stabilization effort.

Beyond these concerns related to the scale of the Fund's existing support for Argentina, there are other important reasons why further extensions of official financial support should be kept within reasonable limits. In particular, approval of a new Fund-supported program while Argentina is in default on its sovereign obligations to private creditors would constitute "lending into arrears" to Argentina's private creditors. As a consequence of its default, Argentina will effectively receive a substantial flow of "exceptional financing," equal to the interest and principal payments that it is not making to its private foreign creditors. By lending into arrears, the Fund (on behalf of the international community) would recognize the need for, and signal official support of, this exceptional financing in the present circumstances of Argentina. But in so doing, the official international community must also insist that Argentina do its best to service these claims once the situation improves.

Indeed, official lending into the arrears of private creditors is necessarily a balancing act. Official support that assists in the stabilization of Argentina and in its more rapid return to economic prosperity will also increase the amounts that Argentina's private creditors are likely to receive on the obligations now in default. On the other hand, as the preferred creditor, the Fund (and other suppliers of official support) will surely and rightfully insist that their claims be fully serviced, and this potentially diminishes the resources available to meet the claims of Argentina's private creditors. Though the responsibility of the Fund is not to maximize returns to private creditors, it cannot serve the important interests of all its members in an efficiently functioning international financial system by ignoring the legitimate concerns of private creditors.

Moreover, in the case of Argentina, it is essential to recognize that the inability to control the appetite for public-sector borrowing was not only the primary cause of the present catastrophe, but it has also been a critical defect of Argentine public policy for decades. Thus, it would be perverse to believe that massive new public borrowing—this time from the Fund and the official international community—is the right way to resolve the present crisis. Official support is surely needed, but moderate levels of support ought to be sufficient. From the Fund, net new annual support (in addition to rolling over scheduled repayments) up to the normal limit of 100 percent of the Fund quota would supply about \$2.7 billion, and net new money from the World Bank and the Inter-American Development Bank might raise the total of net new money to \$4–5 billion.

On top of this, one should take some account of the “extraordinary financing” of \$8–12 billion that Argentina will derive from deferral of payments of interest and principal on foreign debts. In addition, there will be revenue from money creation that will probably far exceed the limit of 3 billion pesos proposed in the government’s budget. And it is reported that Argentina still has \$12–14 billion in reserves, a modest part of which could be used to help finance the budget. Adding all of this up, the amount of financing is quite substantial for the government of a country whose GDP may be only about \$150 billion (at the average exchange rate likely to prevail during 2002).

Bifurcated Conditionality

In considering the conditionality that should be applied in connection with new official financial support for Argentina from the Fund and other international financial institutions, it might be useful to distinguish between the conditionality appropriate for a rollover of existing support and the conditionality relevant for the extension of net new support. Under such a bifurcated system, conditionality appropriate for only a rollover of existing support would be somewhat more relaxed than usually applied; whereas conditionality applied for the extension of net new support would be at least as rigorous as that usually applied.

Under bifurcated conditionality, disbursements under an agreed-on program would proceed at the level of rollover plus significant new support only if the Argentine authorities were determined and generally successful in efforts to meet the program’s objectives. If performance fell short of this rigorous standard, but the Argentine authorities were making good-faith efforts to implement the program, then disbursements could continue at the level of rollover of existing support. (Of course, if policy performance was clearly inadequate, disbursements would be interrupted until a new program, with appropriate prior actions, could be agreed on.)

Adoption of this form of bifurcated conditionality, however, would be an important departure from the principles, policies, and practices that govern conditionality (at least in the Fund) and might set precedents for cases beyond Argentina. Hence, it is important to weigh the potential benefits and defects. On the positive side, such bifurcated conditionality would recognize the very great difficulties confronting the Argentine authorities and would seek to avoid the serious problems that would arise if Argentina went into default on its obligations to the Fund or other international financial institutions. Also, it would be consistent with the Fund’s sanctioning Argentina’s deferral of debt service on its external private credits by lending into these arrears, if the Fund also recognized the implications of Argentina’s very serious situation for its near-term ability

to repay support previously extended by the Fund. It would recognize, however, that the Fund (and the other international financial institutions) have a clear obligation to protect their resources by requiring rigorous conditionality for further extensions of support, taking account of the substantial support that has already been extended to Argentina.

On the negative side, introduction of bifurcated conditionality in the Argentine case could imply a significant weakening of the tool of conditionality and could be seen as a violation of the principle of uniformity of treatment. Under the long-standing practices of the Fund, each new extension of Fund support is subject to conditionality during the period when that support is being disbursed, whether or not the member has payments due to the Fund arising from past support. Once disbursements cease, conditionality no longer applies, aside from the obligation of the member to make scheduled payments of interest and principal to the Fund. In seeking Fund support, all members stand on essentially the same footing, with no special preference given to members that already have outstanding support.

In contrast, under bifurcated conditionality, members with already outstanding support (especially large outstanding support) would appear to have an advantage in getting new support from the Fund, at least up to the level of the rollover of their already outstanding support. Moreover, under the principles implicit in bifurcated conditionality, the Fund and other international financial institutions would presumably have less leverage over members with already large outstanding support. Under the present system, such members have to earn the rollover of already outstanding support by accepting standard conditionality. Under bifurcated conditionality, members with large outstanding support would have more of a presumption in their favor in requesting rollovers of that support. For the Fund, this could mean a greater problem of some members making large and prolonged use of Fund resources—contrary to the principle that use of Fund resources should be temporary. For other international financial institutions that rely on borrowing in private credit markets for their financing, an apparent weakening of conditionality could mean higher financing costs, which would have to be passed on to all members using the resources of these institutions.

To put these concerns in proper perspective, however, it is essential to recognize that Argentina is a very special case in terms of the severity of its present crisis. The combination of sovereign default, collapse of the Convertibility Plan, virtual destruction of the domestic financial system, an exceptionally prolonged and deep decline in economic activity, and collapse of public confidence in government and the rule of law are—fortunately—not the concomitants of most the situations where members call upon the Fund for its support. Accordingly, the relevance of the Argentine case as a precedent for how conditionality should and will be handled in other cases may not be that great.

Requirements for Stabilization and Recovery

What should be the elements of the policy program that might be supported by moderate net new financing from the international community? Six elements can be delineated. First, the program should be based on realistically optimistic economic assumptions—on assumptions that presume success of the stabilization effort relative to Argentina’s presently dire situation, but not on the absurdly optimistic assumptions in the government’s recent budget. Even if stabilization efforts are successful and the downward economic spiral flattens out by midyear, Argentina’s real GDP will likely fall 10 to 15 percent in 2002. The value of the peso has already (in mid-May) dropped below 30 US cents and is almost surely headed lower.

Indeed, even if a credible stabilization program were put in place at midyear and rigorously implemented, it is hard to see how the value of the peso at the end of 2002 could be kept above 20 or 25 US cents. Although the general increase in domestic prices (in pesos) would likely lag well behind the increase in the peso price of the dollar, nevertheless, domestic inflation on a December-to-December basis would appear to be headed over 200 percent. This may be an imprudently large number to admit explicitly in a Fund-supported program; but there is no point in denying that inflation in Argentina during 2002 is likely to be very high—even if hyperinflation in the thousands of percent is successfully avoided.

Second, given plausible economic assumptions, the government budget needs to be realistic and needs to include measures that will reasonably assure that the deficit will be within the bounds of what can be financed without resort to money (or money-substitute) creation at rates that will generate hyperinflation. The Argentine government will derive significant fiscal benefit from deferral of interest and principal payments on its external debt.¹

Most debt service on the internal debt will need to be paid, however, if Argentine banks and pension funds that hold most of this debt are not to default on their obligations. Tax revenues are likely to be very low because of the economic collapse and very poor tax compliance—a problem that has been exacerbated by the general breakdown of respect for the government and for the rule of law. Also, there are likely to be substantial costs to the government from dealing with the mess it has created in the

1. Nonpayment of the interest on the external debt of perhaps \$3–4 billion counts as a budgetary saving because interest expense normally appears as a budget expenditure. Nonpayment of principal is also a cash saving to the government and reduces the need for government financing (and balance of payments financing), but does not count as a budgetary saving in normal accounting. Also to the extent that interest and principal payments are deferred rather than written off, there are future budgetary and cash flow implications for temporary nonpayment of external debt-service obligations.

Argentine banking system. And there will be the politically difficult but absolutely essential task of reining in the deficits of the provinces and terminating their discretionary authority to borrow, virtually without constraint, by issuing debt that circulates as a money substitute.

All told, this suggests that containing pressures for deficit financing within tolerable limits will be very difficult. Official external financing and use of some of Argentina's foreign exchange reserves can probably finance a modest general government deficit. However, the creation of money and money substitutes will likely occur to a significantly greater extent than the planned issuance of 3 billion pesos; and use of such financing will need to be accepted, provided that it is contained within limits that will not drive inflation beyond tolerable limits. This probably means that the Fund will have to accept a bigger budget deficit and a higher inflation rate than it normally likes to see for countries receiving Fund support. For the Argentine authorities, it means slightly more slack on fiscal policy than would usually be acceptable in a Fund-supported program, but with the recognition that the results of the stabilization effort are likely to be less satisfactory than the Argentine authorities would like to admit. The point is to have a program that has at least some chance of being successfully implemented—a program that is not virtually assured of collapsing with further damage to the Argentine government's already tattered credibility—a program on which the Argentine authorities will be required to deliver or face interruptions in the flow of international support.

Third, it is essential to establish a reasonable framework for monetary policy. The Argentine authorities have indicated that monetary policy (of the operationally independent Central Bank of Argentina) will be governed by an inflation target. This sounds like a reasonable policy for 2004 and beyond, after stabilization efforts have succeeded in restoring growth, in reducing inflation to moderate rates, and in resurrecting the Argentine financial system. (Mexico, for example, was able to move successfully to inflation targeting a couple of years after the tequila crisis. Brazil moved very rapidly to inflation targeting after the crisis of early 1999; but the crisis in Brazil was not nearly as catastrophic as the present crisis in Argentina.)

However, in 2002 and probably also in 2003, the Central Bank of Argentina will have great difficulty in controlling the supply of money and central bank credit, and the demand for domestic money is likely to be highly unstable. The central bank will simply not have the means to keep inflation within relatively narrow bounds of a preannounced target; and announcing that the objective of monetary policy is to keep inflation in the range of, say, 150 to 250 percent is not a meaningful prescription for an inflation target.

Rather, the objective of monetary policy should be to contain the initial inflationary surge from the collapsing value of the peso and then bring

the inflation rate down to more moderate levels during the course of the next two years. This will require that the central bank strictly limit the growth of its own credit to within boundaries agreed on for the Fund-supported program and, consistent with these quantitative limits, will generally imply interest rates on central bank credit be kept at levels that are generally positive in real terms. In addition, monetary policy will clearly need the support of fiscal policy to keep public debt issuance within tolerable limits and to lend credibility to the notion that monetary policy will not be completely dominated by the needs of public finance.

Fourth, exchange rate policy needs to be adapted to deal with the present crisis. The initial attempt of the Duhalde government to institute (for an interim period of several months) a dual exchange rate (with the rate for most trade transactions pegged at 1.4 pesos to the US dollar) was a serious mistake. Not only was this system doomed to collapse, as it did in a few weeks, but its inevitable collapse further undermined the government's limited credibility.

A unified floating exchange rate for the peso is the only reasonable option in present circumstances. Official intervention can be appropriate to counteract turbulence in the foreign exchange market; but intervention should not be consistently one-sided, should not attempt to defend any specific exchange rate, and should not be permitted to result in substantial losses of Argentina's official reserves. It must be recognized that given everything else that is happening in Argentina, the peso inevitably will depreciate very substantially (from its old parity) in real terms—and even more so in nominal terms.

As in other countries where exchange rate pegs have collapsed, depreciation will be “excessive” in the period following the collapse, and the real exchange rate will likely recover to more reasonable levels as the crisis abates. The principal policy tool to resist “overly excessive” depreciation is not large-scale official intervention, but rather the maintenance of sufficiently tight conditions on the supply of domestic credit. In addition, temporary controls on capital outflows may be useful, although such controls are distortive, tend to lose effectiveness over time, and afford opportunities for corruption.

Fifth, something needs to be done to clean up the horrendous mess in the Argentine banking system—for without a functioning banking system it will be very difficult to restore reasonable prosperity to the Argentine economy. In approaching this problem, it is essential to recognize that the responsibility for the mess lies entirely with the Argentine government—both past and present. Four actions of the Argentine government have made the Argentine banking system effectively insolvent and incapable of meeting the claims of depositors: (1) The government defaulted on its commitments to honor its own dollar-denominated debt, including substantial amounts of such debt held by Argentine banks. (2) The government reneged on its commitment to maintain the Convertibility Plan,

leading to a massive depreciation of the peso against the dollar. (3) The government mandated that dollar-denominated loans of Argentine banks were payable in pesos. (4) The government mandated that dollar-denominated deposits at Argentine banks be converted into pesos at an exchange rate for the peso much above that used to convert dollar-denominated bank loans.

It has already been argued that by no later than mid-2001, the first two of these actions had become unavoidable. The third action was a wise recognition of the fact that after the collapse of the Convertibility Plan most Argentine debtors would not be able to service their dollar-denominated loans from Argentine banks. The first three actions together effectively forced a massive write-down in the dollar value of the assets held by Argentine banks—a write-down that was unavoidable. If, instead of the fourth action, the dollar value of the liabilities (and capital) of Argentine banks had been converted into pesos (at the same one-to-one exchange rate as dollar-denominated bank loans), the banking system would have remained solvent.²

The Argentine government, however, lacked the political courage to tell the Argentine people the truth: that the US dollar value of their deposits in Argentine banks was being sharply reduced as a result of government actions. Instead, through the fourth action, the Argentine government sought to purvey the fiction that most of the dollar value of deposits could be preserved as the peso depreciated and to shift the blame for the losses of depositors from the government to Argentine banks.

Now, the Argentine public has, with good reason, lost confidence in the banking system and has little reason for confidence in the government or any of its promises. Moreover, the owners of Argentine banks who have effectively been robbed of all of their invested capital also have little reason to believe any promises of the Argentine government. This means that there is no incentive for these bank owners, or any who might succeed them, to put in new capital to refloat the banking system—that would simply be an invitation to be robbed again by the Argentine government.

One possibility would be for the international community to supply the resources (perhaps \$10 billion or \$15 billion) to recapitalize the Argentine banking system and lend its credibility to support renewed public confidence in that system. That, however, would be an unconscionable mistake. Beyond the general reasons why further international support for

2. This was the essence of the proposal made by Ricardo Hausmann (Personal View, *Financial Times*, October 30, 2001). It was widely recognized well before the event that the collapse of the Convertibility Plan would inevitably cause great problems for the Argentine banking system. The only sensible way to deal with these problems was to convert both dollar-denominated bank assets and dollar-denominated bank liabilities into pesos at the same one-to-one rate, and then allow the dollar value of both bank assets and liabilities to depreciate along with the dollar value of the peso.

Argentina should be kept within reasonable limits, it is essential that the international community not lend its financial or moral support to bail the Argentine government out of a predicament that is so clearly the result of its own cynical misbehavior.

Rather, the burden must be on the Argentine government to find the bulk of the resources, within a tightly constrained budget, that are needed to recapitalize the banking system. This could probably be done most efficiently by supplying public funds to limit the losses of bank owners to no more than half or two-thirds of their invested capital, and by attempting to persuade them to supply some additional capital to help refloat the banking system. To help restore public confidence in the banking system, the government should also admit forthrightly the fundamental causes of the system's recent failure and seek to provide some assurance that similar mistakes will be avoided in the future. When the Argentine government has a responsible plan to address the problems in the banking system, the international community should consider providing some meaningful assistance to support that endeavor.

Sixth, the Argentine authorities need to signal their clear intention to pursue good-faith efforts to deal responsibly with their external sovereign debt and with a host of obligations to foreigners (such as contractual commitments to foreign investors in Argentine utilities) in which they are now in default. Two general principles should be recognized as governing how these problems will ultimately be resolved: (1) Argentina's foreign private creditors and other private holders of contractual claims on Argentina will need to recognize that in the ultimate resolution of their claims, they will not be made whole, but rather will need to share in the enormous economic losses being sustained by the Argentine economy in the present crisis. Private foreign investors in Argentina undertook risks when they made their investments, and generally they were promised rates of return that reflected these risks. As with all investors who undertake risks anywhere, when things turn out particularly badly, investors (including bond holders and others secured by contractual obligations) take losses. (2) The Argentine authorities must ensure that foreign investors in Argentina are treated "fairly" in the sense that they are not forced to accept disproportionately large losses. What constitutes fair treatment in individual cases will need to be a subject of negotiation and likely a matter of dispute. But treatment that falls substantially short of Argentina's reasonable best efforts to meet its external obligations across a broad front should not be that difficult to discern. The international community has the right and the obligation to insist, as one of the conditions for its support, that the Argentine authorities assiduously apply these principles in dealing with their external obligations.

Of course, the resolution of most of the private claims on Argentina will not occur quickly. Because of the dire state of the economy and of the government's budget, the resources to meet external claims are now very lim-

ited. And seeking to negotiate now how most external claims will be resolved on the basis of promises of what will be done when the economic and budgetary situations improve is unlikely to be very productive. The uncertainties for both sides in such bargains are simply too great to make any deal credible and mutually acceptable.

When the economic situation does stabilize and the Argentine economy moves forward into recovery, then the time for serious negotiations with external claimants will begin. At that stage, Argentina will not yet have regained voluntary access to private credit markets and will likely still be dependent on the Fund and the rest of the official international community for support (or at least for rollovers of past support). Thus, the international community will still have considerable leverage over the Argentine authorities; and, if necessary, it should be prepared to use this leverage to help assure that external claimants on Argentina are treated fairly.

This approach is consistent with—indeed, it is required by—the Fund’s fundamental responsibility to provide assistance to its members while simultaneously supporting the principles of a stable and efficient international financial system and safeguarding the temporary revolving character of its own resources. The exceptionally difficult circumstances confronting the Argentine authorities argue for Fund support to be as generous as possible, under appropriate conditionality.

Because outstanding Fund support for Argentina is already substantial, however, it is particularly important to assure that further extensions of support do not expose the Fund to undue risks. A strong policy program that is vigorously implemented by the Argentine authorities is the most important protection against these risks—because it is the indispensable requirement to restore stability and renew prosperity in Argentina. But the situation is so difficult that it is essential to recognize that, despite the best efforts of the Argentine authorities, success may not be achieved on the first attempt. As the unfortunate experience with the large disbursement of August–September 2001 clearly demonstrates, it would be a serious mistake to venture large amounts of whatever additional support the Fund might reasonably supply to Argentina on one-shot efforts that may fall well short of what is needed for sustainable success.