

THE WALL STREET JOURNAL

Tuesday, May 28, 2002

COMMENTARY

Argentina Doesn't Need the IMF

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The current crisis in Argentina has brought widespread suffering and a massive economic decline. Officials of the International Monetary Fund are now in Argentina negotiating the conditions under which they would provide a major new loan. Since Argentina already owes the IMF \$15 billion, more than five times its "quota" and therefore far above the Fund's normal borrowing limit, it is reasonable to ask whether a further exception should be made for Argentina.

Much of the press commentary and policy discussion assumes that Argentina desperately needs outside funding and that such funds would have a substantially favorable effect on the outlook for the Argentine economy. I disagree. I can see no way in which an IMF loan of \$10 billion the amount that is widely mooted would help Argentina deal with its fundamental problems or its short-term crisis.

Argentina got into the current crisis because it had an overvalued currency (the peso was tied one-to-one to the dollar) and excessive budget deficits financed by borrowing dollars from abroad. The currency overvaluation has already been eliminated by the collapse of the peso now worth about one-third of its previous value and the shift to a floating exchange rate. While future Argentine governments may continue to run large budget deficits, there is little risk that foreign lenders will continue to finance them.

Several reasons for providing a loan to Argentina are put forward by

advocates, including enabling the country to meet its immediate obligations to creditors and to bolster the reserves of the central bank. True, the IMF loan would temporarily increase the amount that Argentina could pay to its private creditors, but it would finance only a very small part of those obligations and would do nothing to reduce the debt write-down that will eventually be necessary. As for bolstering reserves, the government has accepted the idea of a floating exchange rate and should not be encouraged by an IMF loan to try to preserve the peso's value.

Some advocates of an IMF loan assert that the funds could be used to revive the banking system. There is no doubt that fixing the banking system is critical for recovery. Eventually, the government must replace the substantial bank assets that it destroyed by allowing dollar loans to be repaid in pesos, or it must permit banks to repay depositors with some form of longer-term bonds. In either case, an IMF dollar loan is irrelevant since what the banks need is not dollars but pesos, which the government can provide without help from the Fund. And Argentina's foreign exchange reserves and current trade surplus mean that it doesn't need IMF help to finance imports.

If there is no good economic reason for the IMF to lend money to Argentina, why is it so eager to do so? One reason is that Argentina has interest and principal payments of \$4.9 billion that are due to the IMF this year. By withholding that amount from any gross loan that it now makes, the IMF could maintain the fiction that its borrowers do not default on their loans. That claim is important to the IMF's ability to get funds from the U.S. and other industrial governments. Since lending just \$5 billion to Argentina would make this slight of hand obvious, the IMF wants to lend more. Putting the extra funds into Argentina's central-bank reserves would

also make it easier for Argentina to repay the \$4.2 billion that is due to the Fund in 2003.

A second reason that the IMF favors a loan to Argentina is that it would break the Fund's traditional policy of requiring debtor countries to reach an agreement with their creditors before the Fund would extend any new credit. This policy of "not lending into arrears" increases the leverage of the creditors in any negotiation. The IMF has been eager to shift the balance of power in favor of the debtors, as its recent proposals for some form of international bankruptcy procedure indicates. Giving a loan to Argentina in the near future would be a step in that direction.

A loan to Argentina would also allow the IMF to impose wide-ranging conditions on the Argentine government. Many of the policies that the IMF now demands would be sensible things that the Argentines themselves know should be done and that they would do even without IMF conditionality. Making these changes appear to be forced by the IMF only weakens the public's confidence in the government and increases the risk of instability. Policies that appear to be accepted under duress would also be easier for future Argentine governments to undo.

Of course, some of the policies demanded by the IMF would not otherwise be adopted by the Argentine government. It is not clear, however, that the IMF proposals are better than what the Argentinians would choose for themselves. The Fund's policy demands range from constitutional changes in the relation between the central government and the states to detailed aspects of tax and spending policy. I have serious doubts about the ability of an IMF team to select the changes that make the most sense in the context of local conditions. The Fund's repeated mistakes during the run-up to the crisis provide no reassurance about the appropriateness of its current advice.

It would be far better for the IMF to be an adviser that must persuade by its arguments rather than an aid-giver that can demand policy changes in exchange for financial help. Surely that is the way that Argentina or any other democratic government deserves to be treated.

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