

General Discussion: Lessons from the Stabilization Process in Argentina

Chairman: Thomas M. Hoenig

Mr. Hoenig: Since we are short on time, we will take just one question.

Mr. Lipsky: Mr. Cavallo, Argentine interest rates rose significantly following your recent resignation as Minister of Finance, suggesting that at least some investors are worried about the sustainability of the fixed peso/dollar rate under the Convertibility Plan. In such circumstances and considering the theme of this seminar—is there any policy action that the central bank could undertake in order to enhance the credibility and sustainability of the plan and thus lower interest rates? Or rather, is the bank essentially a passive captive of the actions of financial market participants and of the fiscal authorities?

Mr. Cavallo: There is nothing that the central bank can do to increase credibility, except perhaps one thing that Pedro Pou, the new president of the central bank, can do—and that is not to get involved in borrowing for the government. That is one thing that I particularly dislike from recent events. I was told that yesterday Pedro Pou went to New York instead of the Secretary of the Treasury or the other Secretary of Finance to borrow for the government. It is not good if the central bank, which is responsible for keeping the reserves and backing the currency, borrows for the government. That is the only thing that he can do—perform according to the law as the head of the central bank and take care of convertibility. Let the

government worry about financing the budget. That is the only advice I can give to the central bank. Now, the government can do a lot to bring down interest rates and reduce the currency risk. Particularly, it has to clarify what kind of policies it wants for the future. The appointment of Roque Fernandez as the new economic minister suggests that President Menem and the government want to continue exactly the same rules of the game and the same policies. That is the way the market read this decision the first week. Since the re-election of President Menem, let's say since May of last year, there has been a two-tier attitude in relation to the government. One attitude was evident in the speeches of President Menem and my actions and my proposals. And the other was evident in the decisions by the Peronist party in Congress and in suggestions made by the trade unions. It was argued that the attitude of the trade unions and of the Peronist party via the Congress was because of my personality, my political ambitions, and so forth. If that were true, it is perfectly good for Argentina that I am out of office. So the problem has been removed from the scenario. I am very happy to have helped resolve the problem. But now, that must be reflected in the attitude of the Peronist party through the Congress and the trade unions. If they continue to push the government for increased spending and changes in policies, that will be very bad for the country. It will be reflected in higher interest rates that will provoke another recession. If, on the contrary, President Menem does what I think he will finally do, because he is a very smart politician and he is a real political leader and a statesman, he will work hard to discipline his party and to have the Congress support the proposals by the Economy Ministry and the executive, of course, and not pay attention to what the trade union leaders have to say, because they are clearly defending vested interests. They have a crazy system of monopolies that generates a lot of corruption and a lot of inefficiencies, and they are just defending the system. So, if the government continues in the same line and there is support in Congress, interest rates should go down and the price of bonds should go up. If I were to bet on that, I would purchase Argentinian bonds, but you know that depends on everyone's confidence in the future.

Mr. Hoenig: Thank you very much, Domingo.