

5th INTERNATIONAL WORKSHOP ON DEMAND-LED GROWTH: *CAPITAL FLOWS AND EXTERNAL CONSTRAINTS*

*A discussion about inflation in Argentina:
distributive conflict in a context of high financial
fragility*

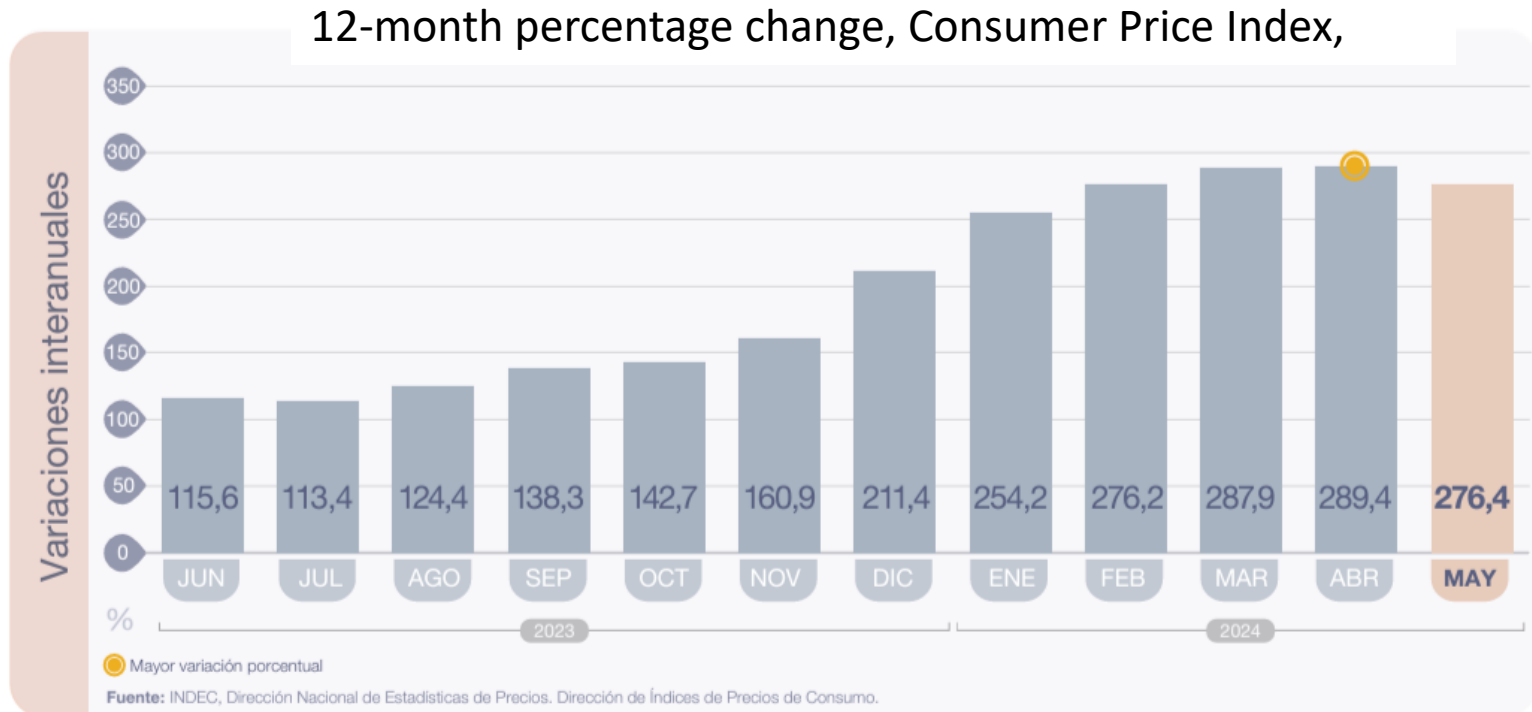
AN ALTERNATIVE VIEW ON INFLATION IN ARGENTINA IN THE
NEW MILLENNIUM: THE CHALLENGES OF THE CURRENT
SITUATION

ECONOMIA INTERNAZIONALE / INTERNATIONAL ECONOMICS

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I. Motivations:

- In contrast to most Latin American countries, Argentina (along with Venezuela) has experienced persistent inflation.



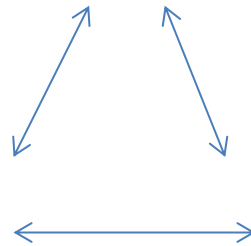
- Despite Argentina being the closest thing to an economic policy laboratory, it seems that most (media) economists agree that the cause of inflation is fiscal.

II. Objective:

- Inflationary processes in Argentina during the new century, especially in the last decade, can be explained by devaluations triggered by dynamics linked to the external sector, resulting from financial deregulation processes and inflows of external liabilities. In this scenario, conflict inflation manifests through a persistent exchange rate-wage spiral

FINALCIAL FRAGILITY + POLITICAL STALMATE

In an economy with structural current account deficits and a deregulated financial market, the result is greater instability.

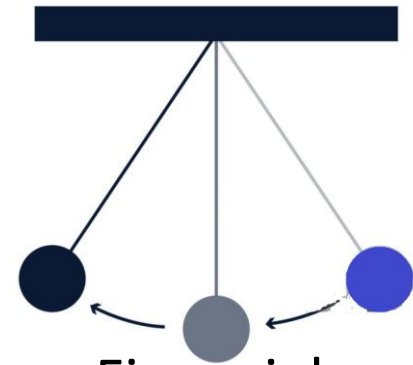


The exchange rate becomes so volatile that it fosters **unstable expectations and speculative price revisions**. In a conflictive society this dynamic is highly destabilizing, and foster inflation if wage claims are triggered.

III. Theoretical Foundations for Peripheral Economies

- Price-Taker economy; depreciation of the national currency increases the price level.
- Technical Dependence: Semi-Industrialized Productive Structure
- Financial Dependence:
- In Peripheral Economies, inflation driven by distributive conflict, $w - r$, is expressed through the Wage – Nominal Exchange Rate spiral.
- If any social group cannot impose its distributive aspirations on the rest of the society (Di Tella, 1968; Portantiero, 1974), price increases become persistent and widespread.
- It could result in an intense distributive conflict under “pendulum” governments that reflect a situation of political stalemate.

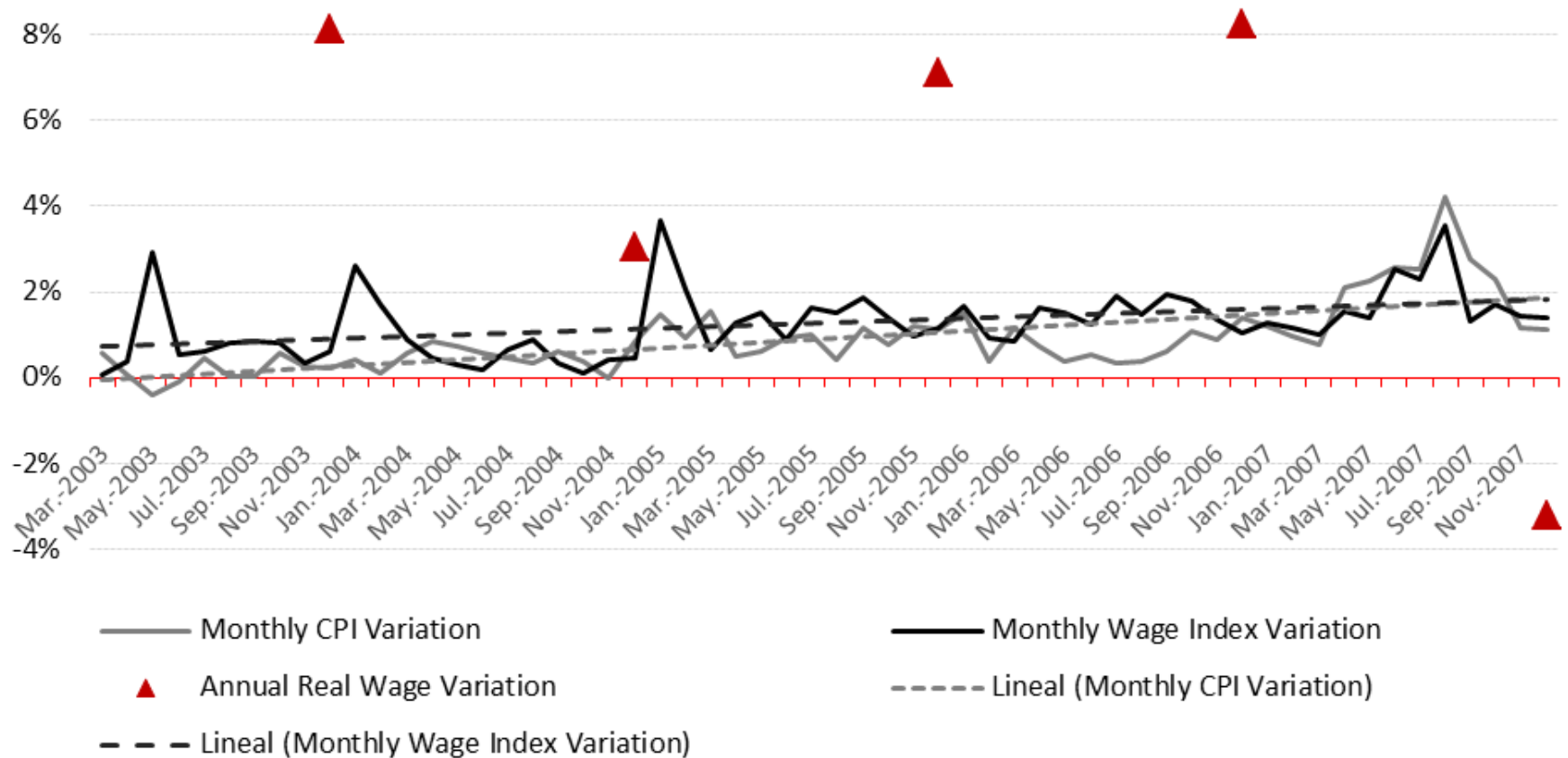
IV. THE INFLATIONARY PROCESS IN ARGENTINA (2002-2023) IN LIGHT OF THE CLASSICAL STRUCTURALIST TRADITION:



4.1. The Period 2003-2015: Exchange Rate Stability, Low Financial Openness, and Negative Interest Rate Differential:

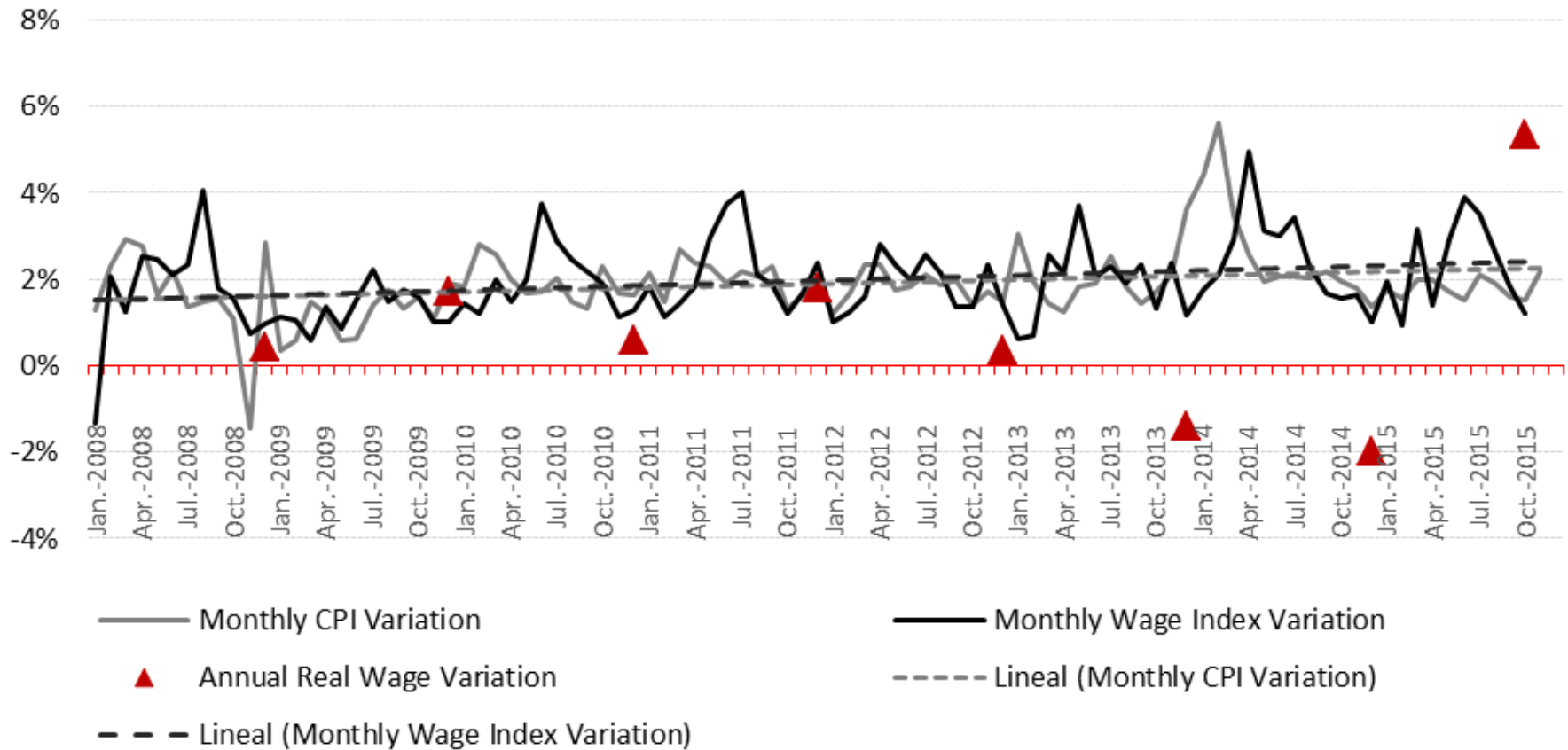
- Relaxation of the external constraint for almost a decade
- The governments implemented a series of progressive policies to boost spending and improve the labor market situation
- *The rise in nominal wages above the general price dynamics characterized much of the first term period (i.e., March 2003 – March 2007), resulting in positive annual variations in real wages*

2003-2007



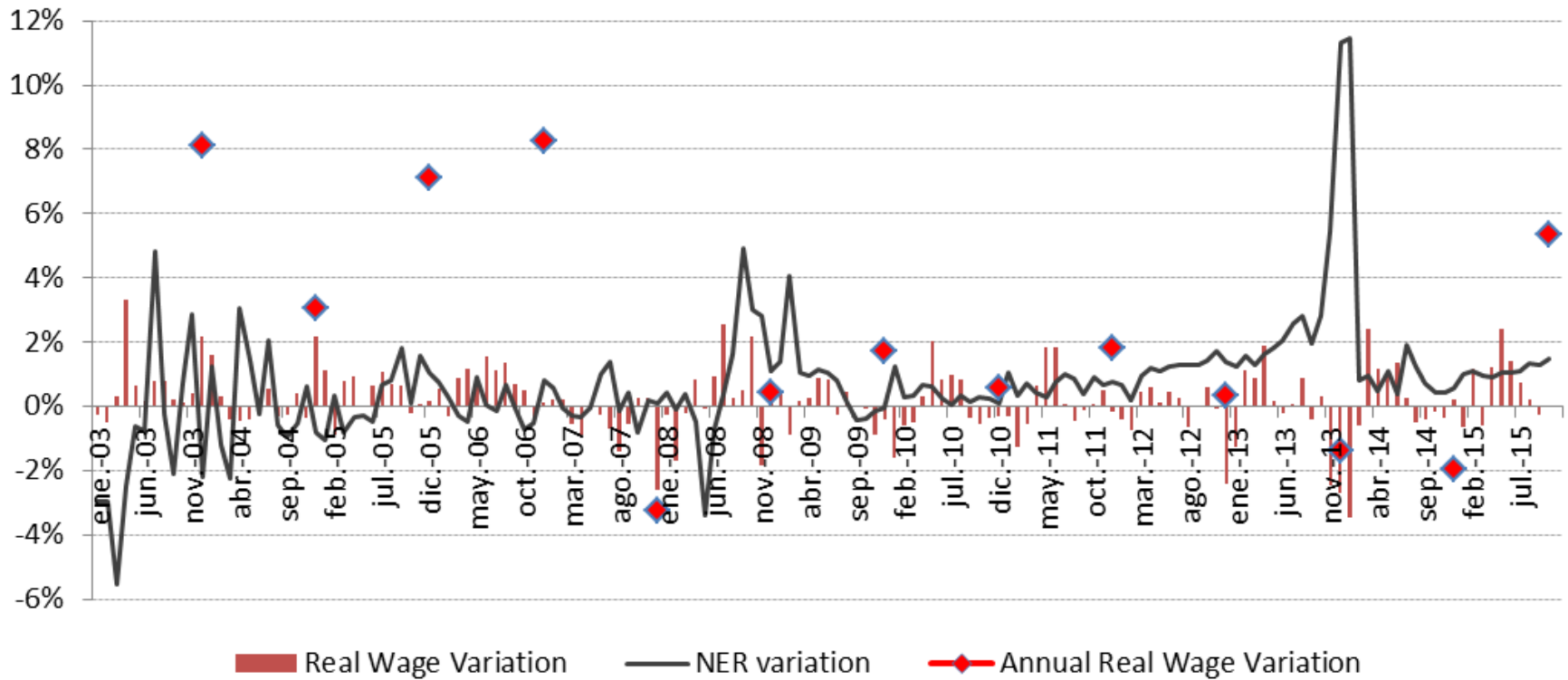
Particularly, from 2003-2007, the strengthening of the labor market explained not only the wage and income distribution performance during this period but also the dynamic of prices. Since the end of 2005, the rising nominal wages began to be gradually transferred to prices, generating a sustained inflation process

2008-2015: the reinstatement of the political stalemate

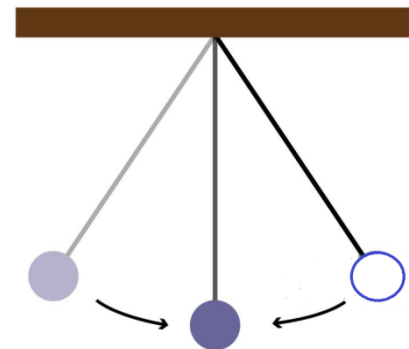


- The reduction of this gap between the trends of inflation and nominal wages is attributed, on the one hand, to the restoration of a scenario of political stalemate.
- On the other hand, the rise in international prices and then the restrictions on exchange rate markets emerge as crucial factors in devaluations and inflation expectations

2003 - November 2015

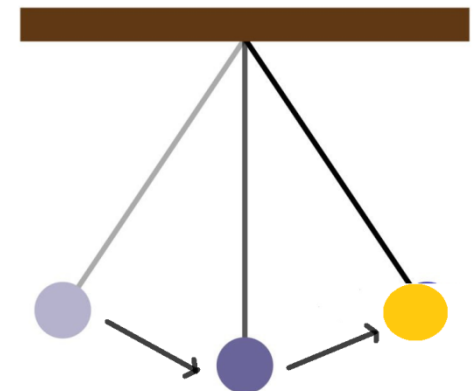
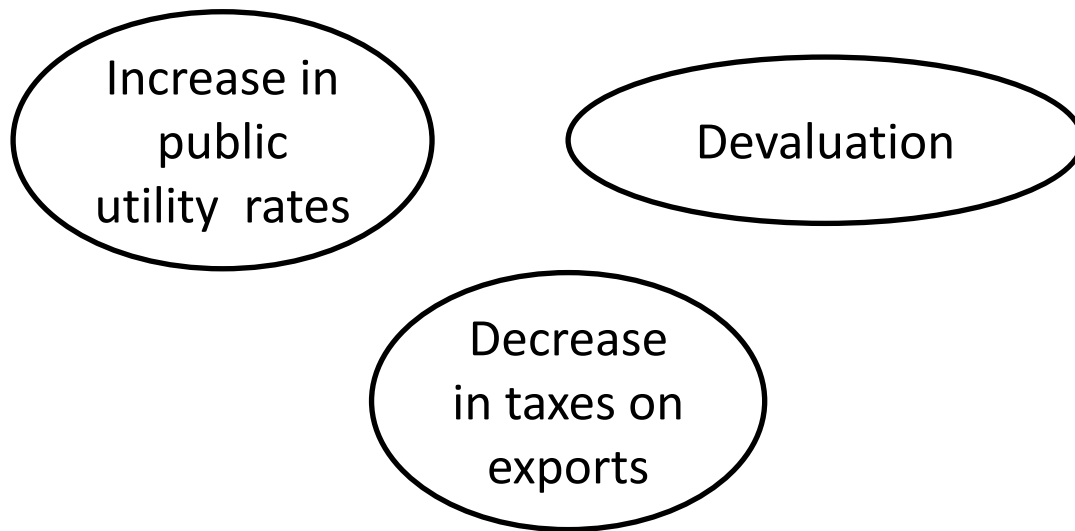


POLITICAL STATEMALE + EXTERNAL CONSTRAINT



4.2. The Period 2016-2019: Exchange Rate Instability and Financial Opening

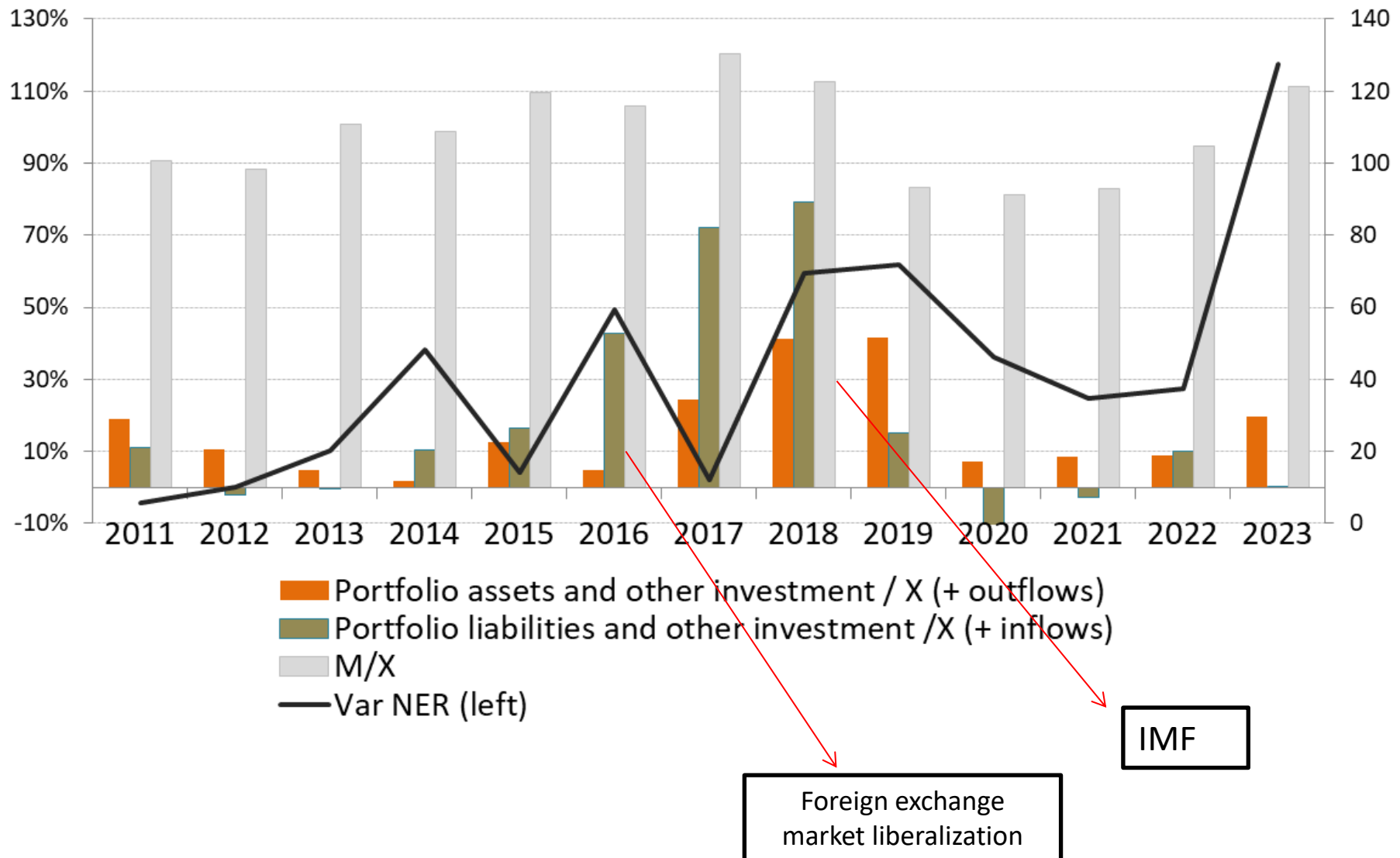
- The major problem of financial fragility that Argentina is currently experiencing has been generated in this period.
- From December 2015 to July 2016, the nominal exchange rate grew by 62%, electricity and gas prices rose by an average of 207%, and water service prices increased by 283%.



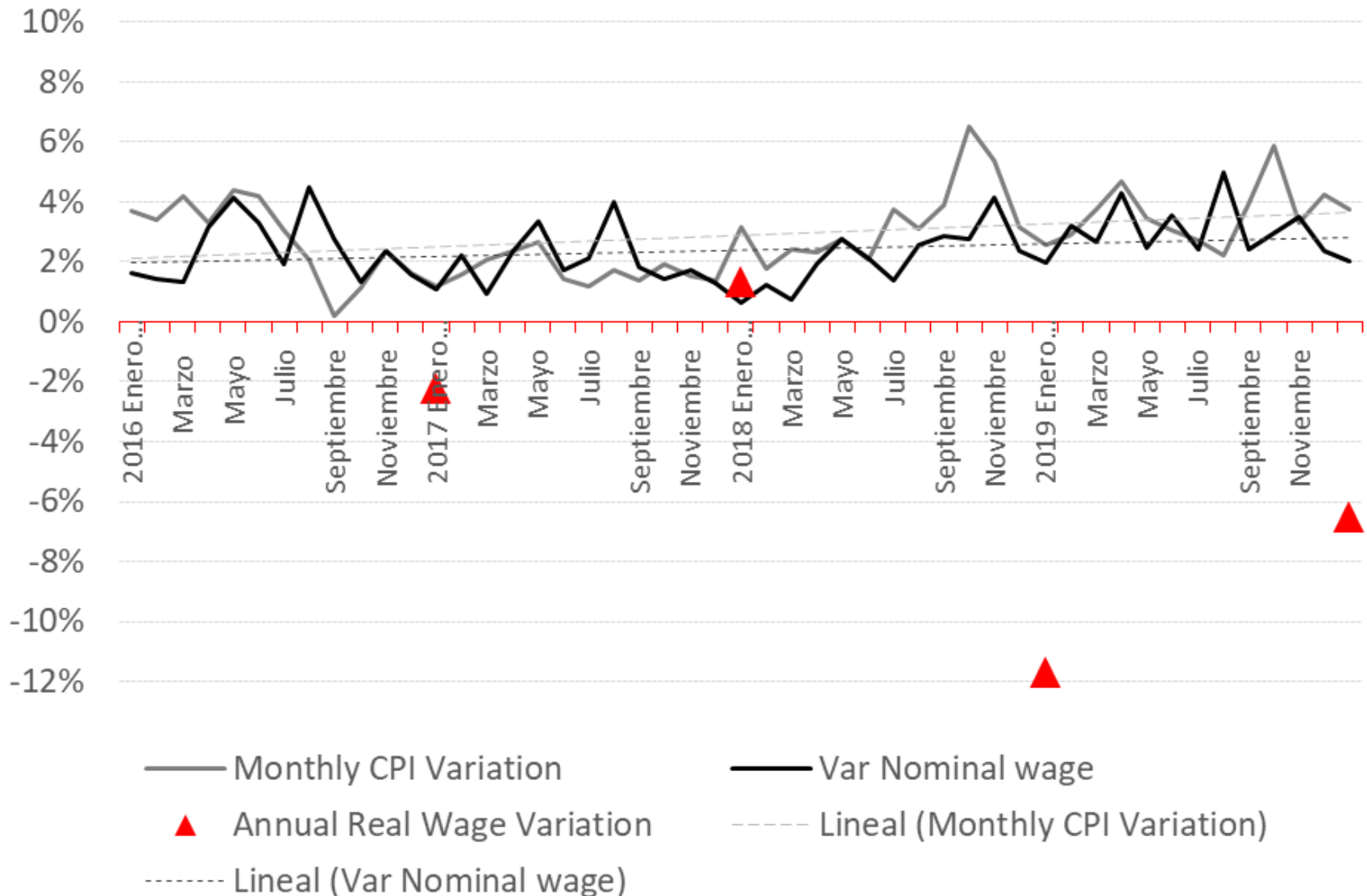
	Trade Account - Exports Ratio (%)	Current Account - Exports Ratio (%)	International Reserves - Imports Ratio (%)	Terms of Trade Index	Nominal Exchange Rate (quarterly average)	Inflation (%)	Interest Rate (BADLAR), deposits over \$ 1 M pesos
2002	53.9	29.9		86.4	3.44	25.9	5.1
2003	45.3	23.4	63.0	93.4	2.95	13.4	9.0
2004	29.9	7.7	60.4	100.0	2.94	4.4	10.1
2005	25.7	10.8	66.9	97.0	2.92	9.6	13.6
2006	24.7	13.9	61.0	101.3	3.07	10.9	12.4
2007	19.5	10.9	75.7	107.6	3.12	8.8	10.1
2008	17.2	8.1	70.2	120.6	3.16	8.6	13.4
2009	25.9	12.3	93.8	121.6	3.73	6.3	13.8
2010	15.6	-1.9	72.1	125.1	3.91	10.5	17.0
2011	10.1	-4.5	57.0	138.8	4.13	9.8	22.6
2012	12.6	-1.5	55.4	144.7	4.55	10.0	21.6
2013	1.1	-13.4	41.8	135.2	5.48	10.6	25.8
2014	3.5	-9.8	36.0	132.6	8.12	21.4	20.6
2015	-6.1	-23.7	41.4	126.3	9.26	21.5	34.4
2016	-5.65	-21.16	0.43	134.2	14.77	40.50	30.94
2017	-20.42	-42.00	0.55	130.2	16.55	24.80	26.22
2018	-12.55	-35.11	0.65	131.4	28.08	47.65	44.08
2019	16.75	-4.37	0.90	130.5	48.19	53.83	65.32
2020	18.77	4.17	0.81	131.3	70.62	36.14	39.65
2021	17.25	7.59	0.57	144.0	95.07	50.94	38.00
2022	5.28	-4.17	0.40	131.3	130.54	94.79	57.06

INFLATION DOUBLED.

- The deregulation of the financial sector and the erratic monetary policy led to a logic of speculative financing that worsened external vulnerability). Argentina increased its debt rapidly, mostly in foreign currency.



2016-2019: the price dynamics was characterized by the reduction of real wages and the redistribution of income towards ownership social groups, mainly the financial and export sectors.



Chronicle of a Crisis Foretold

However, several events in the early months of 2018 triggered the sudden stop:

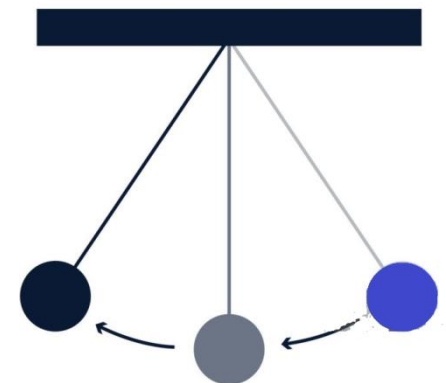
- reduction of the domestic interest rate;
- the increase in the U.S. interest rate;

Consequences:

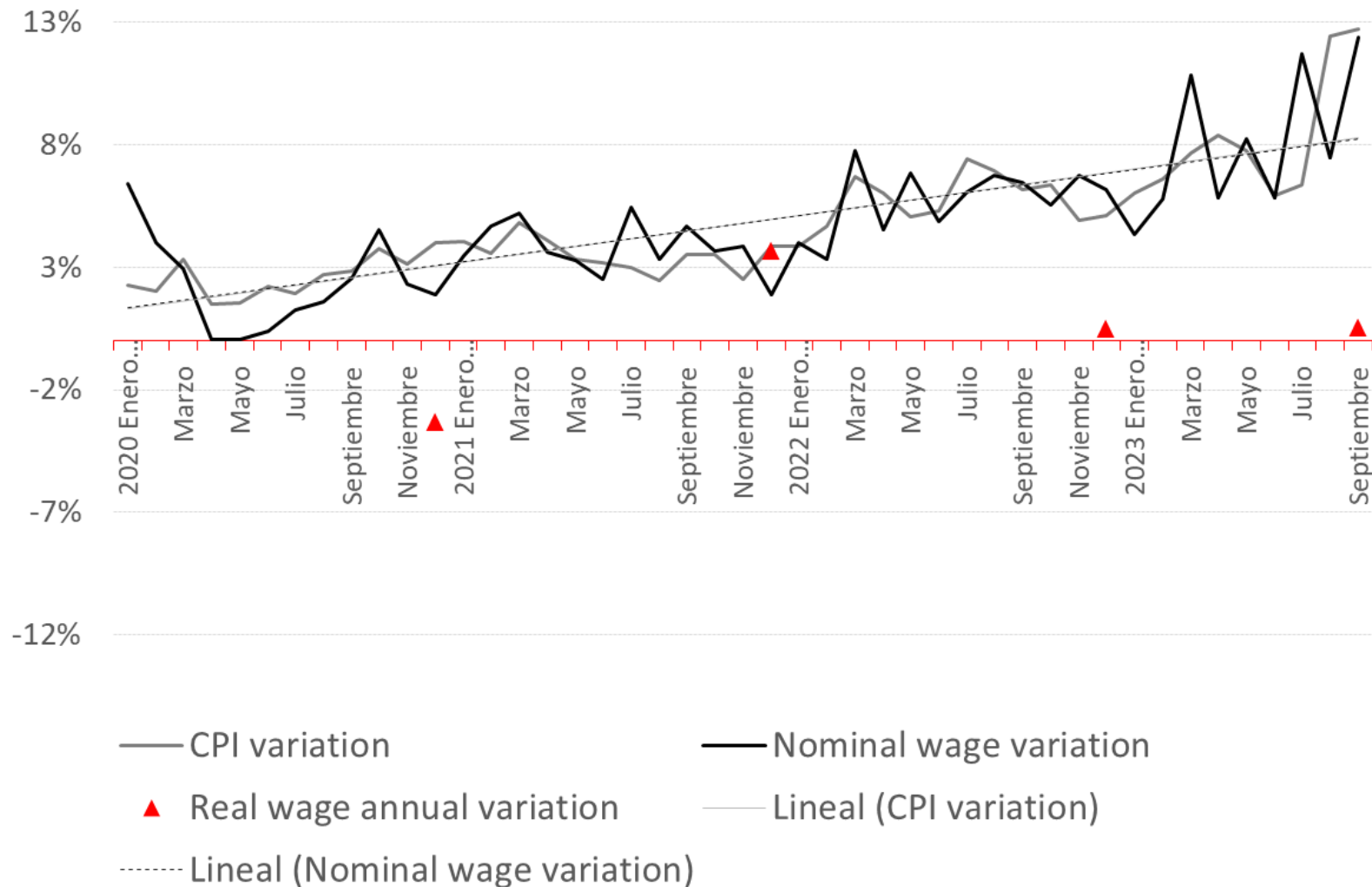
- The central bank lost 12% of its international reserves from February to June;
- Currency depreciated by 40% during this period;
- Argentina signed a stand-by agreement with the IMF in June 2018;
- The increasing exchange rate volatility quickly translated into a higher inflation rate, with peaks in September and October 2018, leading to a real wage decline of nearly 12%;
- After losing a third of foreign currency reserves between July and October and experiencing a defeat in the 2019 general elections, the government reintroduced exchange controls, stricter restrictions than those imposed in 2015.

4.3. 2020-2023: Impacts of External and Internal Shocks on Conflict-Driven Inflation

- Current account deficit
- The insufficient international reserves of the Central Bank, with strong financial restrictions.
- The need to address the restructuring and renegotiation of external debt, both with private creditors and multilateral credit organizations,
- the indebtedness with the IMF, which emerges as a potential auditor of the economic policy of the Peronist government
- COVID Pandemic.
- Ukraine war
- A severe drought between late 2022 and early 2023 exacerbated the critical shortage of international reserves



Jan-2020 / Sep 2023 NER rises 483%.



The Figure shows a growing inflation and wage variation trend. While this consolidates a pattern of increasing high inflation, it results in a stagnation of real wages (unlike the decline recorded in 2015-2019), characteristic of the political stalemate.

Unstable dynamics of expectation formation (Tavares and Belluzzo, 1984)

- Low central bank's ability to maintain exchange rate policy because of insufficient international reserves in the context of a conflictive society regarding income distribution.
- In a scenario of general election, the influence of devaluation expectations (and future prices) on inflation dynamics was exacerbated as these are constantly revised upward to hedge against potential future losses in a context of high nominal volatility.
- Gradual devaluations triggered wage demands that perpetuated an inflationary dynamic in a society in conflict over income distribution

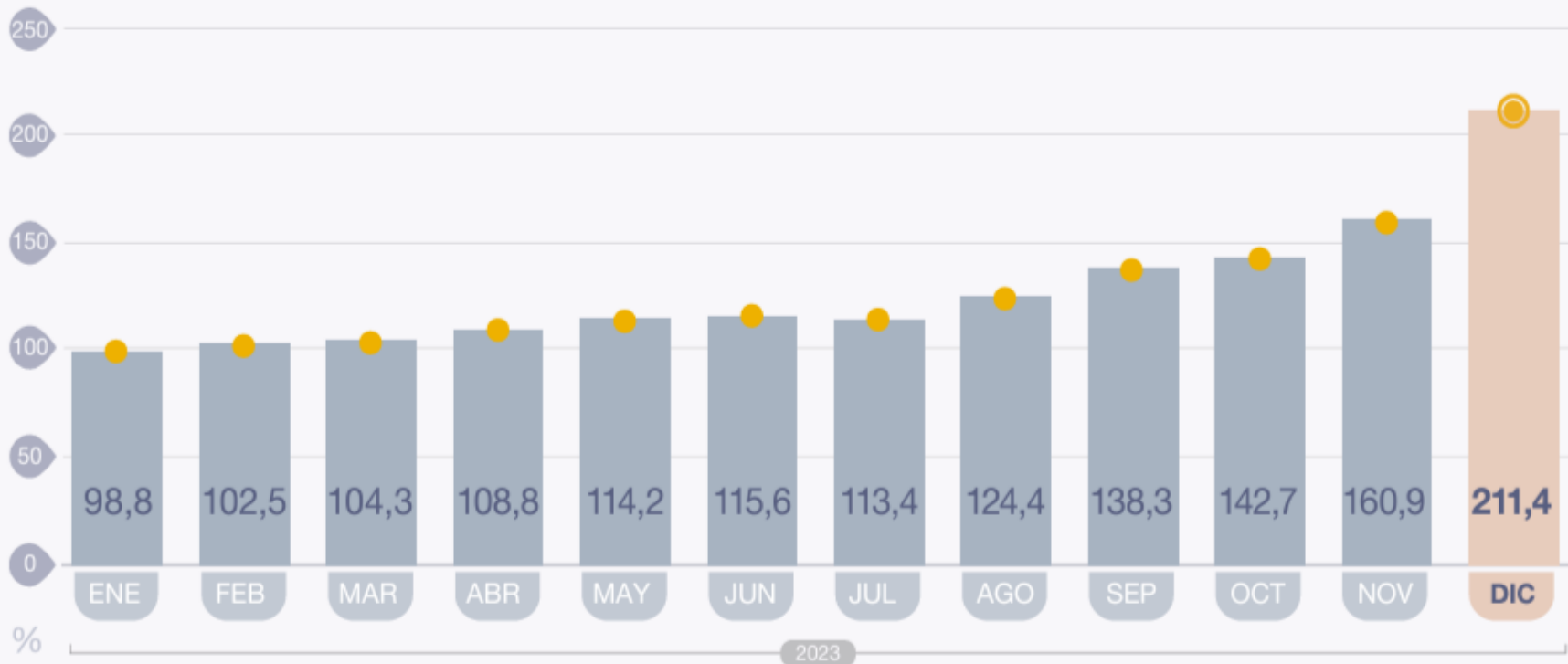
- The monetary authority raised interest rates to prevent the accumulation of external assets. These dynamics started an inflationary spiral involving a feedback mechanism between wages, interest, and exchange rates.
- Particularly in the end of the year, the process accelerated and the expected margin becomes unstable and challenging to predict:

"Supply prices, planned by producers, tend to be significantly exaggerated in an attempt to anticipate a potential devaluation of liquid capital. This dynamics leads to the overall supply price departing from the 'normality' conditions of production price within a capitalist enterprise" (Tavares & Belluzzo, 1984, p. 8).

12-month percentage change, Consumer Price Index,

Diciembre de 2023 - Variaciones interanuales del Nivel general del IPC. Total nacional

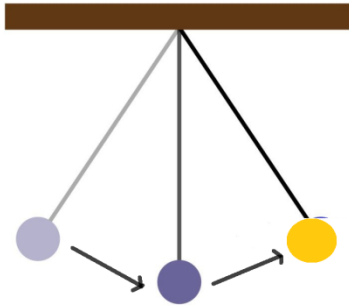
Variaciones interanuales



Fuente: INDEC, Dirección Nacional de Estadísticas de Precios. Dirección de Índices de Precios de Consumo.

4.4 December 2023....

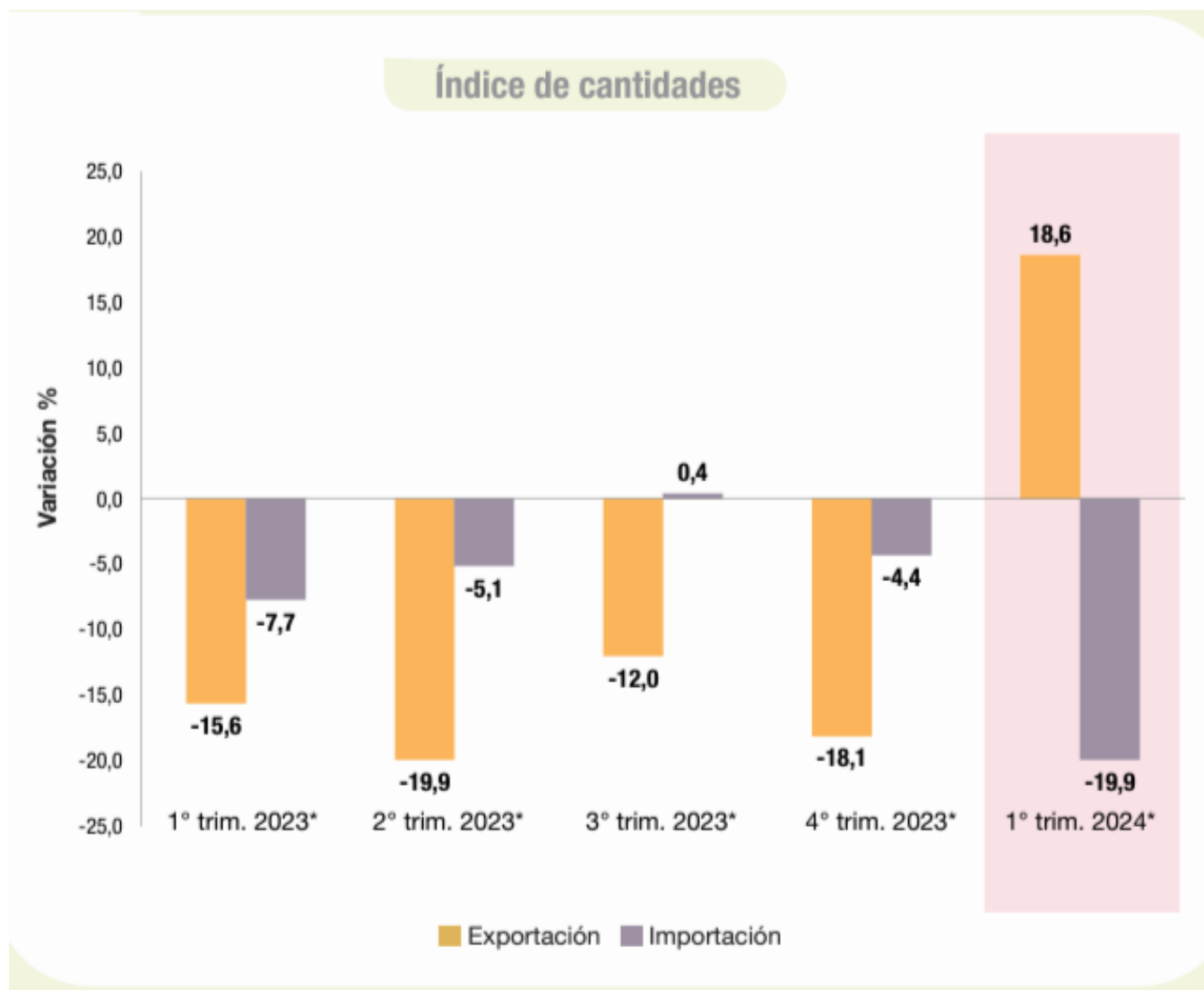
"the mole that destroys the State from within"



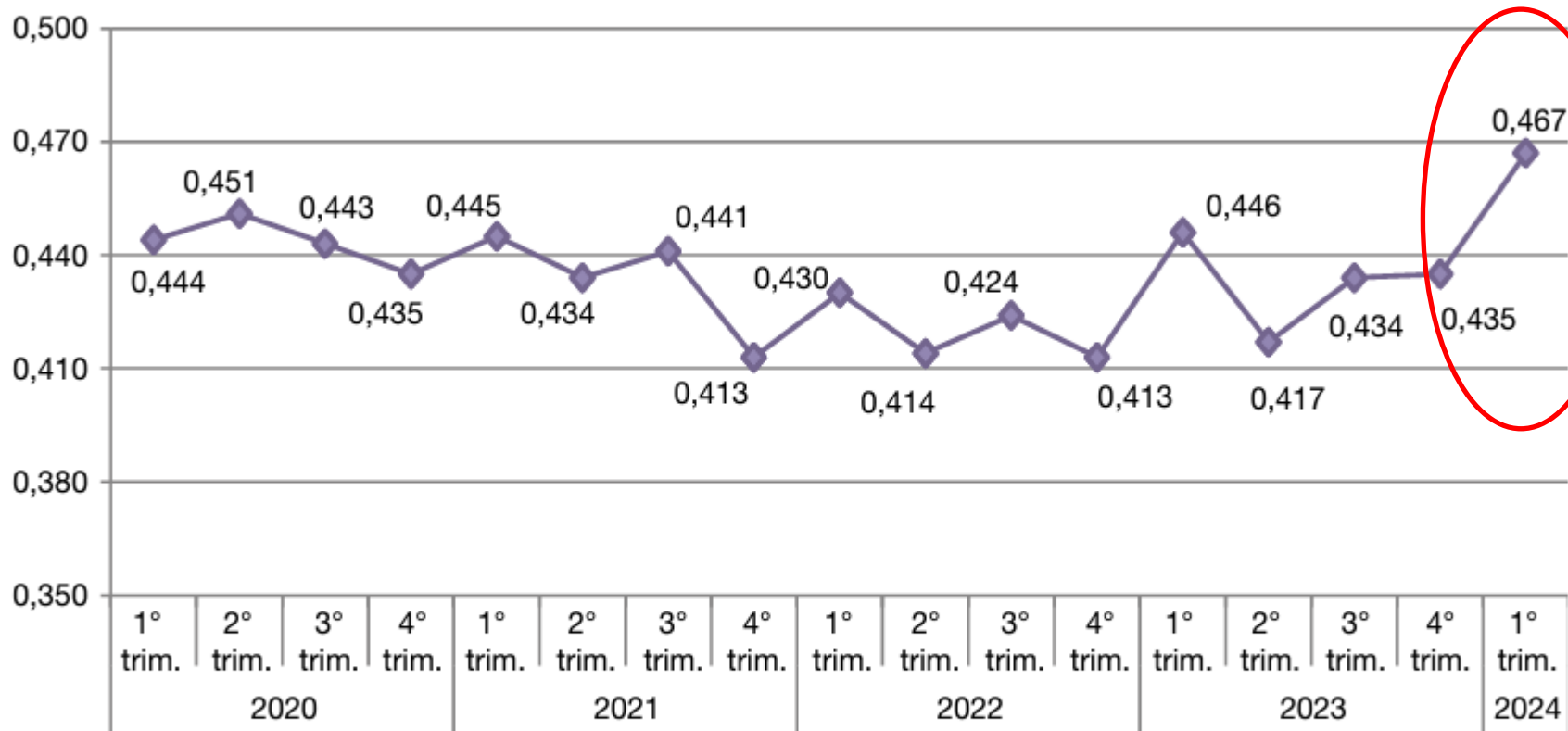
A new pendulum swing: the new president promised a drastic reduction in public expenditure, the elimination of the central bank, full economic liberalization, and dollarization.

- Devaluation
- Deregulation of the economy
- These caused a spike in inflation that was partially offset by:
 - Significant reduction in public spending -> recession -> imports reduction
 - Discipline of the working class

X (orange) and M (light purple) : variation of the quarterly quantities index compared to the previous year



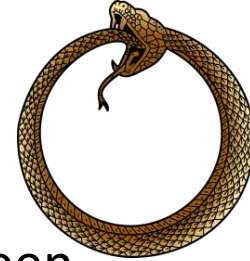
Coeficiente de Gini del ingreso per cápita familiar de las personas. Total 31 aglomerados urbanos.
Primer trimestre 2020-primer trimestre 2024



Nota: los resultados del tercer trimestre de 2020 no incluyen el aglomerado Ushuaia-Río Grande. En consecuencia, este informe refleja resultados que representan el 99,4% de la población de los 31 aglomerados urbanos cubierta habitualmente por la EPH (ver “Acerca de la cobertura geográfica” en el Anexo metodológico del informe técnico *Evolución de la distribución del ingreso. Tercer trimestre de 2020*).

Fuente: INDEC, Dirección de Encuesta Permanente de Hogares.

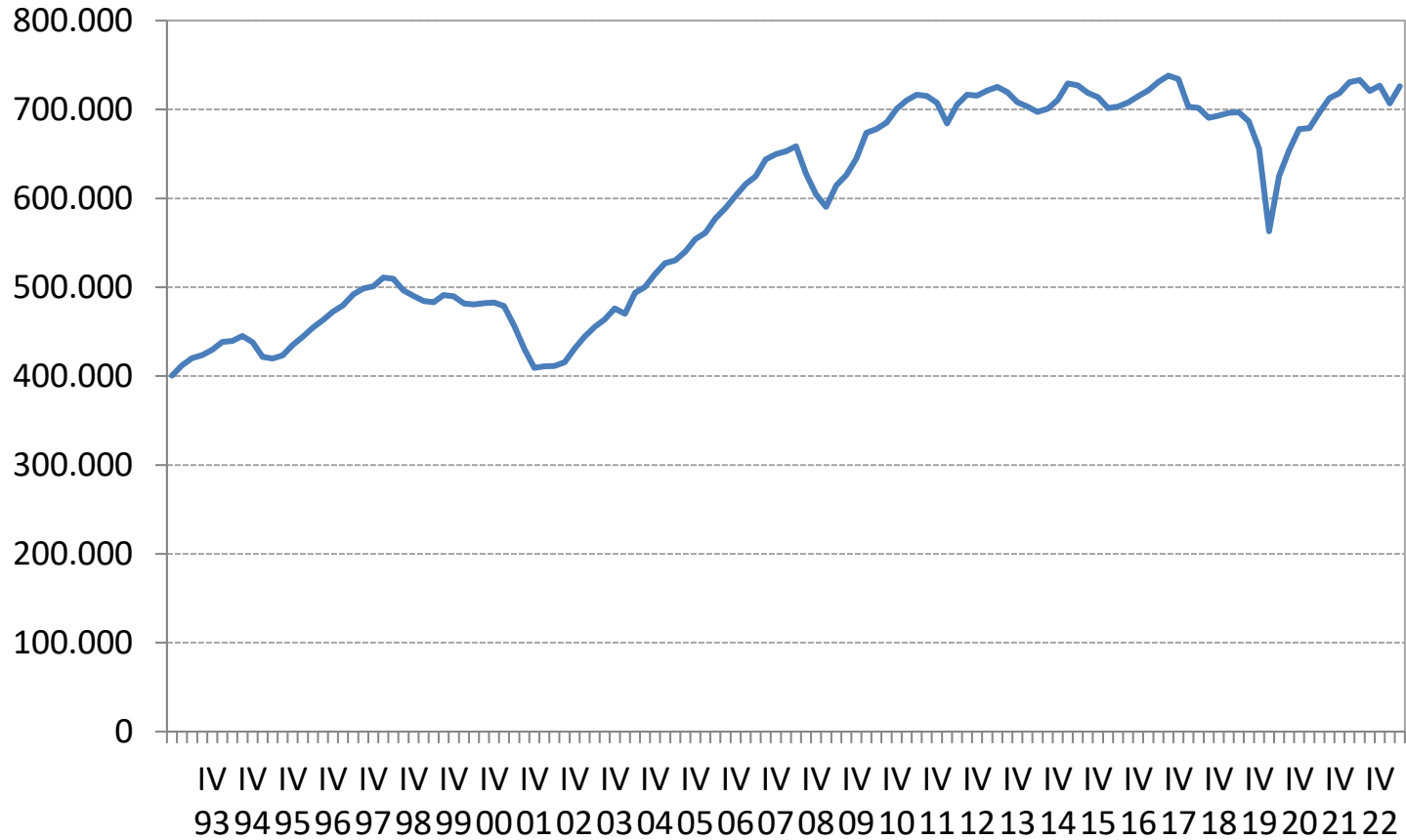
Lessons and final thoughts



- There is nothing special in theoretical terms about Argentina.
- The price dynamic is understood as the result of conflict between wage increases and devaluations in a price-taker economy open to trade and financial flows.
- Inflation performance can be explained by devaluations triggered by dynamics linked to the external sector, resulting from financial deregulation.
- In this scenario, conflict inflation manifests through a persistent exchange rate-wage spiral.
- Therefore, monetary authorities will seek to maintain foreign currency reserves to cope with capital outflows and mitigate devaluation expectations.
- For the latter objective, keeping domestic interest rates higher than international rates to cover the devaluation risk and implementing financial flow regulations are essential starting points. In this sense, price stability requires exchange rate stability.

Thanks for your attention!

GDP



Argentina: distribución personal y funcional del ingreso (1993-2022)

