Political and Economic Context: Overview

Largely owing to its history, Argentina is an unusual country in the Latin American context (Resico M., 2010 & 2015). It has a past as an upper-middle-income country with a large middle class and has been shaped by a large inflow of European immigrants. To achieve this, it experienced two main milestones in the 19th century: the Declaration of Independence in the first half, not to mention the commitment that gave rise to the National Constitution of 1853 in the second half of the century, which is consistent with the elitist style of the times. Notwithstanding, its transition from an enlightened and restricted democracy to a broader one that assimilated first the middle class and then the working class included the first coup d’état in 1930. This event had profound consequences in terms of the ensuing political, economic and social instability.

Thus, twentieth-century Argentina (1930-83) was characterized a high degree of polarization, marked by political instability lurching between democratic governments with a populist bias and de-facto restrictive governments that rejected and conditioned the democratic game. Two sides emerged, each adopting an opposing economic policy. On the one hand, there was an interventionist side focused on the domestic market, while on the other, there was a more open-minded side which relied more on export activity. Both sides benefited different sectors of a heterogeneous productive apparatus, leading, in turn, to high volatility in the economic cycle, characterized by pro-cyclical policies.

Despite the return to democracy and formal respect for the Constitution under President R. Alfonsín (1983-89), the dichotomies in economic policy remained, together with a certain implicit detachment from legality. Recently, Argentina has continued to show an unresolvable polarization of views and interests in the political system impeding the generation of equitable and sustainable development. The history of the 20th century with its many coups d’état, an attempt at unilateral constitutional reforms (1949), coupled with political and economic instability, shows a weakenedARGENTINA FACING THE COVID-19 CRISIS: BETWEEN POLITICAL DIALOGUE AND POLARIZATION

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1 Argentina exemplifies a contrast between its natural and human resources and the scarcity of social capital, which feeds a political culture that alternates between ideological polarization and a pragmatism bordering on illegal conduct. Some point out that the abundance of resources, instead of being a facilitating factor, may have functioned as a factor of underdevelopment of social and institutional capital (as can be seen in the literature on the “curse” of natural resources). This fits with Acemoglu, Robinson’s (2012) distinction between “extractive and inclusive” institutions.

2 Oversimplifying: agricultural sector versus industrial sector. For an elaboration on these topics, see Diamond M. (1983) and O’Donnell G. (1977).
awareness of a common and respected framework for the development of institutions based on broad consensus and consistent medium and long-term state policies.

In the economic field, a hyperinflationary crisis occurred in 1989, due to the collapse of the interventionist and closed model, and raising the poverty level to 47%. With President C. Menem (1989-99) a market-oriented and open-minded model was established based on privatizations. This brought significant growth and modernization. Notwithstanding, in addition to destroying the production fabric with no reconversion, it was dependent on the inflow of short-term capital. A fixed exchange rate (“convertibility”) provoked recession and unemployment to absorb international fluctuations. As capital outflows intensified at the end of the 1990s, a profound crisis ensued in 2001-02 during the President F. de la Rúa administration (1999-2001).

The result was a severe contraction (unemployment stood at 22% and poverty at 58%), and the country defaulted on its debt payments. The E. Duhalde administration (2002-03) dramatically adjusted the exchange rate. This, together with a substantial improvement in the terms of trade, caused a significant reactivation with a fiscal and current account surplus. However, despite growth and certain social improvements, subsequent administrations (N. and C.F. Kirchner 2003-15) gradually ended up squandering this opportunity1. Active monetary and fiscal policies were strengthened, resuming the fiscal deficit, and incurring a negative current account, leading back to inflation and exchange controls4. Eventually, this led to economic stagnation, with a reduction in savings, declining investments and escalating capital flight. Despite its vast clientelist system, growing interventionism in addition to poor government results social polarization exacerbated, and the party in office lost the 2015 elections5.

The success at the polls of President M. Macri (2015-19), and his coalition “Cambiemos” (Let’s change) was an unprecedented event in national politics6. The new administration’s main commitment was to accept the financing of the pervasive social security net, and proposing a gradualist reform of the state. The government quickly regained confidence by freeing up the foreign exchange rate and the financial market7. Activity and employment slowly picked up, but after the success of the mid-term elections, the administration suffered a drastic economic setback when an attempt to call for a broad political agreement failed to materialize8. The lagged exchange rate (to contain inflation) stepped up the increase in the current account deficit. Coupled with lenient measures to regulate foreign exchange flows, a sudden reversal of external financing occurred induced a pronounced devaluation. This resulting a spiral of mistrust combined with rising inflation and feeble growth brought about a recession. The government failed to reverse the trend, despite taking an unprecedented loan from the IMF and sharp plans to cut the fiscal deficit. The economy went into recession with high inflation, which, in

3 A policy with high doses of clientelism was promoted at the social level. This improved economic indicators for a while, but then they fell again as inadequate policy design, coupled with inflation, made achievements unsustainable. The poverty rate, which had dropped to 25%, ended 2015 at 32%.
4 Consolidated national public spending went from 23.3% of GDP to 41.2% in 2015 (excluding interest on debt).
5 From then on, the polarization of values and political and economic ideas was called the “crack” or the “divide”.
6 Center-right forces resumed the democratic path of Álvaro Alsogaray (UCEDE party). He was an advisor to President Menem (1989-99), who took office with a discourse contrary to the one he later applied.
7 Taxes on exporters were also reduced and utility rates were updated.
8 The government adopted the following objectives: to reduce poverty, combat drug trafficking, and unite Argentines.
addition to increasing poverty (36% end of term), turned independent voters to align with the alternative party in the elections held in late 2019. The opposition coalition “Frente de Todos” (FdT), led by former president C. F. de Kirchner, forged an alliance between her sector and the traditional Peronist faction, anointing a moderate candidate, A. Fernández. The opposition candidate won the elections and the transfer of power was carried out in an exemplary manner. Invoking dialogue and consensus-building, the new president also called for the union of Argentines, the reactivation of the economy, and the renegotiation of the bulky foreign debt.

The Impact of the Pandemic and the Measures Implemented

This context, described above, has been impacted by the Covid-19 pandemic. Just as in several countries, initial controls were first adopted at airports and borders, and then public events and classes were cancelled. On March 19, “social, preventive and compulsory isolation” was decreed, except for essential activities. At the beginning, the contagion curve rose slowly, but the strict quarantine had a strong impact on economic activity. Of special concern were slums, and a strategy was designed for these neighborhoods that consisted of measures to try to reduce entrance and exit flow. The government met and coordinated measures with the opposition. These were initially received with high levels of adherence by the population, which served to buy vital time to prepare the healthcare system and prevent its collapse.

A series of social and economic measures were introduced to prevent workers from losing their jobs and companies from going bankrupt, as well as for protecting businesses and commercial networks. To that end, social support schemes were expanded. Two main tools were added: the “emergency family income” for the unemployed and for informal workers (reaching 9 million people), and the “labor and production assistance program,” easing the burden of payroll taxes for employers and granting subsidies to pay a portion of employees’ salaries in the affected sectors of the private economy. Likewise, maximum prices were fixed by decree for essential goods and services, a rent freeze was enforced, and loans were granted to individuals and SMEs in financial distress. Measures also included the deferment of tax debts and the rescheduling the due dates for utility payments.

To fund such aid, the country found itself with limited fiscal capacity due to its macroeconomic weakness and its level of indebtedness. In April, the government presented its first offer to restructure the public foreign debt in private hands, amounting to some USD 66,137 million, part of a total debt representing 90 percent of GDP. The main source of financing for such aid was the issue of money by the Central Bank (BCRA), implying a risky exchange rate and inflationary tensions. Despite the public policy efforts, the economic crisis reached unprecedented dimensions and GDP fell by 19.1% year-on-year in the second quarter.

In the electoral context, and with the deterioration of confidence, the Macri government restored exchange controls.
In a Latin American context marked by social crises in countries like Bolivia, Chile, Ecuador, Colombia.
The Program “The Neighborhood takes care of the Neighborhood”. The slums, locally known as “villas,” have a higher population density, the majority of people work in informality, and have high rates of unmet basic needs.
FE, Emergency Family Income, and Labor and Production Assistance Program, ATP.
Fiscal packages announced as % of GDP El Salvador 11.1, Chile 5.7, Peru 4.8, Brazil 4.6, Argentina 3.9, Panama 3.7, Average LA 3.2, Honduras and Guatemala 2.5, Colombia 1.7, Mexico 1.1, and Uruguay 0.7. Source: ECLAC (2020).
It is estimated that for the period January-September there was an issue equivalent to 5.5% of GDP.
which was the highest drop in history, with a decline across 16 sectors of economic activity.\(^{16}\)

Although there was consensus on the need to establish an early quarantine, there was also criticism of certain aspects of its implementation including restrictive freedoms and the economic cost of such a measure, in addition to its long duration. Since the beginning of May, a new strategy was deployed to detect and isolate cases in the AMBA region (Metropolitan Area of Buenos Aires). On May 10, the lockdown was extended, expanding exceptions and empowering regional authorities (except for AMBA) to permit more activities, provided that the protocol was enforced. From then on, the number of infections kept growing. The AMBA region reached its peak in August, when the healthcare system faced the maximum demand; however, a plateau in case numbers started to be observed.\(^{17}\) Meanwhile, in the provinces, which had enjoyed greater flexibility, cases have gone up again, with peak figures expected at the time this study was concluding.\(^{18}\)

After the first measures, taken largely in consensus with the opposition, the government rose sharply in popularity.\(^{19}\) It was expected that this popularity would continue by promoting a heralded Economic and Social Council in the hopes of institutionalizing dialogue and fundamental consensus, not only with the opposition but also with the main socio-economic actors, in efforts to strengthen the cohesion of actions, and to pave the way for regaining confidence in the economy and its recovery (Resico M., 2020). Notwithstanding, in a context in which both the Judiciary and Legislative powers were operating at a distance due to the pandemic, the government promoted a series of actions and laws that compromised the consensus that had been previously achieved, and managed to deteriorate the relationship with the opposition, and jeopardize both its popularity and the incipient recovery.\(^{20}\)

This new stage began on June 8 with a decree that proposed the expropriation of Vicentin, a company that was under receivership due to bankruptcy.\(^{21}\) The measure unleashed a public demonstration against what was seen as a measure of unjustified interventionism.\(^{22}\) Then the government heightened the conflictive situation by launching a highly controversial Bill of Judicial Reform with the aim of modifying the organization and competency of the Federal Judiciary, coupled with other complementary measures.\(^{23}\) These initiatives included the Telework Law at the end of July, and a

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\(^{16}\) The largest decreases were reported for hotels and restaurants, -73.4%, and for social and personal community activities -67.7%.

\(^{17}\) Deaths from Covid-19 per 100,000 inhabitants LAC as of August 2020: Peru 63.2, Chile 53.3, Brazil 66.4, Mexico 39.4, Panama 37.2, Ecuador 34.2, Colombia 23.4, Argentina 9.2.

\(^{18}\) There were successive extensions of the “compulsory isolation,” or lockdown, the current one is in force until October 11.

\(^{19}\) Starting in August, the measures were complemented with a provincial financial emergency program, and multiple programs that promote specific sectors such as construction, access to ICTs, support for entrepreneurship and job training in popular neighborhoods, assistance to tourist providers, family and peasant agriculture, etc., while continuing with the social assistance programs ATP and IFE.

\(^{20}\) The Merval stock market indicator, at the end of March reached 22,000 points, then it recovered and reached its highest level in early August around 50,000. GDP drop 2nd quarter: -19.1% year-on-year, -16.2% compared to 1st quarter. Industrial production recovered 12.3% in May and 16.5% in June, (-6.9% year-on-year), construction, which fell by 80% in April, recovered 113.6% in May and 37.5% in June (still -13% year-on-year), automotive production fell to 0 in April while in July it went back to last year’s indicators. Inflation fell by 1.5% in April and May, and rose to 2.2 and 1.9% in June and July. Unemployment was 13.1% in the 2nd quarter, + 2.5% year-on-year.

\(^{21}\) A major company of national capital in the agro-industrial sector.

\(^{22}\) Seeing that it would fail to generate the necessary majorities in Congress where the decree was to be confirmed, the government backed down looking for alternatives to the situation. The initial decree was revoked at the end of July.

\(^{23}\) This proposal was interpreted, both by the opposition and by part of the population which organized several demonstrations, as an attempt to achieve impunity for high officials of the Kirchnerist administration, in addition to questioning its high cost and lack of opportunity in the context of the crisis.
decree declaring the information and communication technology (ICT) sector an essential service in early August. Furthermore, a law was proposed for a solidarity contribution by the owners of large fortunes, consisting of a one-time contribution. With these initiatives, which caused breaks of varying degrees in the consensus with the opposition against a backdrop of several announcements of foreign companies leaving the country, the question that hovers is concerned with the cost in terms of the deterioration of the investment climate.

In this context, economic signs point to awaningrecovery. The Merval index, which reached its highest level in August (around 50,000 points), fell back to pre-pandemic values, reaching around 40,000 points in mid-September. After the peak of expansion in May and June, activity continued to rise, but at a slower pace. The economic activity estimate was -7.4% year-on-year in June; industrial production grew by 2.1% on a monthly basis in June and July following double-digit growth in the previous two months and a progressive recovery of activity is recorded in most sectors. On the other hand, inflation accelerated again and was 2.7% in August (18.9% year-to-date); while unemployment in the second quarter amounted to 13.1%. After the initial dire situation, state spending started to decrease (it was announced that 70% of companies stopped requesting the assistance program), and revenues began to recover. In early September, three months after its first offer, the government achieved 99% adherence in the restructuring of the foreign debt with the private sector. This result strongly decompressed the maturity profile until 2024, by approx. USD 41.5 billion. However, there has been a distinct lack of confidence, especially considering that since the beginning of the current recession the balance of trade has shown positive balances and the Central Bank reserves continued their systematic descent, forcing the government to expand exchange restrictions.

At the conclusion of the drafting of this study, the Minister of Finance presented the 2021 Budget Bill to Congress. In it, he defended the need for a “transition program” with priority given to the reactivation of economic activity with macroeconomic stability and fiscal sustainability, and he justified the new intervention in the foreign exchange market as an exceptional emergency measure. The plan foresees GDP growth of 5.5% for 2021 in line with consumption, and aims at a primary fiscal deficit of 4.5% (financial 6%).

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24 We should add to this the phenomenon of “land grabs” by poor people in the province of Buenos Aires, and other parts of the interior, which not only reveals a complex structural problem, but also a certain inertia on the part of the government regarding the defense of private property.

25 The rebound in the construction sector also slowed, with activity rising 6.8% in July following further gains in May and June. Automotive production grew 21.2% monthly in August. Cement shipments climbed 6% monthly in August, and August energy consumption returned to near pre-pandemic levels.

26 Since 2007, private formal salaried work has been practically growing, representing just over a quarter of the economically active population in working conditions (5.8 and 21 million). Informal salaried workers (almost 7 million), the public sector (3.2 million) and self-employed (1.9 million).

27 According to estimates, savings of around USD 32 billion would be achieved for the country. Total public debt reached USD 324 billion in May, and represented 90.2% of GDP at the end of 2019.

28 President Fernández maintained a monthly ceiling of USD 200 for saving and expenses abroad (“lock”) that had been established by Macri, and added a country tax of 30%. On December 10, 2019, the day Fernández took office, the official exchange rate was ARS 63 to the US dollar, while the informal exchange rate was ARS 69.50. As of September 25, 2020, the official exchange rate was ARS 79.75 to the US dollar, while the informal exchange rate was ARS 145. Since the beginning of the recession, the balance of trade has reported positive balances at the end of 2018.

29 It proposed a counter-cyclical behavior with fiscal sustainability, gradually reducing the needs of BCRA monetary financing, a greater share of public lending in pesos, and stability of the real exchange rate.

30 The 2021 Budget foresees a GDP growth of 5.5% in line with private consumption, and investment is expected to grow by 18.1%; exports by 10.2%; and imports by 16.3%. It aims at a primary fiscal deficit of 4.5% of GDP and a financial deficit of 1.5%. The forecast includes an inflation rate of 29% and an official exchange rate of ARS 102.4 to the US dollar by December 2021, as well as a trade surplus balance of USD 15,087 million.
Scenarios: Between Dialogue and Polarization in an Unstable Context

The health scene continues to have a level of high alert, but there is a possibility that the decline in the indicators of AMBA infections will continue. It would be expected that the dynamics in the provinces will follow this pattern. Likewise, it will be necessary to continue being alert, through more focused and efficient detection and isolation, especially regarding the possibility of a second outbreak in a society that is rather unwilling to remain in self-confinement. Finally, it will be crucial to have the vaccine, the production of which is expected to begin in the first half of 2021.

The socio-economic situation continues to be very serious. The country continues to be mired in the Pandemic, with growing poverty projections. According to the survey of private estimates carried out by the Central Bank, an annual contraction of 12% is expected, the deepest recession ever reported, combined with inflation of 37.8%, which is high in a recession. In any case, the recovery of the economy is already underway - the same projections foresee a growth for 2021 of 5.6% with a higher inflation of around 47%.

A step further in aligning the situation could come from the need to negotiate an agreement with the IMF to restructure a debt of approx. USD 52 billion issued by that organization, since it will require agreeing on a macroeconomic program. In any case, we understand that, leaving aside the possibility of exogenous events, the structuring of future scenarios will depend mainly on the evolution of the economy, together with the ordering effect of politics that the next midterm elections, scheduled for late 2021, involve.

The government’s strategy is to prioritize recovery, especially as the election period approaches, betting more on fiscal and monetary activism than on confidence and the business climate. But this is precisely why it runs the risk of unleashing higher inflation. Although the Minister of Finance has been explicit in terms of achieving a “sustainable” reactivation, political will to take greater risks in the governing coalition cannot be ruled out. A more volatile flank, which is the exchange rate, will also depend on the government’s macroeconomic policy, as well as on the signals given as to its political orientation. An abrupt devaluation with an inflationary jump would have a high cost not only on economic recovery, but also on the electoral possibilities of the ruling party.

President Fernández seems to have missed an opportunity to maintain the moderate profile that was essential for winning the elections for him and which increased his popularity at the onset of the Pandemic. His contrasting measures are understood by reference to the need to instill cohesion in his politically and ideologically heterogeneous coalition. Notwithstanding, this very contrast amplifies uncertainty, which, in turn, undermines the business climate and erodes public approval. An economic recovery without “too much” inflation would not only be favorable, but also would increase the chances of success for his

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31 As of September 25, there were 691,235 infected people and 15,208 deaths.
32 The government announced on August 12 that the mAbxience pharmaceutical company will produce the Oxford and AstraZeneca vaccine.
33 From an already high current value of more than 35% of the population.
34 Activity -12%, inflation 37.8% annually to December 2020, BCRA (2020).
35 The exchange rate is at risk of a fall in Central Bank reserves due to a shortage of foreign exchange due to high demand arising from uncertainty and inflation expectations, and low supply, because of the wide range between the official and market dollars.
36 At closing, the BCRA reserves amounted to USD 42,226M, although the “freely available” reserves are a fraction.
coalition in the upcoming elections and mean that it is still possible the shift towards radicalization could be reined in next year. Nevertheless, as long as radicalized sectors bring their influence to bear in shaping the agenda, polarization will increase, making it increasingly harder to reach political agreements to reverse the crisis.

On the other hand, the opposition is also divided between moderate and radicalized sectors. Those who have public service roles, including the Mayor of the City of Buenos Aires, and a better image need a more stable environment for their tenure. They also must agree to dialogue. But this need to keep a coalition of such contrasts united up to the next elections means keeping the most extreme polarized, liberal and conservative sectors in check. The latter feel that their own electoral possibilities are strengthened by hardening their discourse in the face of the government’s radicalization, while also foreseeing a more abrupt collapse of its economic measures.

What is encouraging, however, is that this diagnosis seems to be growing in scope, and there is a generational shift in the making that could be an opportunity. Both our diagnosis and our proposal are based on the Social Market Economy (SME) (Resico M., 2011 & 2012). This can be an adequate contribution since it provides a framework of liberal and social principles that can be agreed upon and provides an emphasis on consciously integrated economic institutions and policies to achieve an outperforming synthesis aimed at inclusive development.

SME is an approach that places production in the private sector, requiring a state framework that actively regulates economic activity, reducing uncertainties about the future, and understanding that it is necessary for the social dissemination of outcomes. It also suggests that demand-driven policy is possible while there is idle capacity in the economy. This implies avoiding the impulse to increase electoral spending and observing a technical perspective. If confidence is regained, and a certain stability is achieved, the economy could reactivate strongly, driving employment and in-

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37 At present, on the contrary, a diversion of federal funds was reallocated by decree from the City of Buenos Aires, whose mayor is from the opposition, to the province of Buenos Aires, whose governor is from the ruling party, accentuating the differences.
38 With deficits in terms of food, healthcare, education, informality, employability and associated urbanization.
39 The first part of the statement coincides with the thesis proposed by Olson M. (1982).
40 From the macroeconomic point of view, it means reestablishing fiscal consistency, reducing the tax burden, and building coherence between monetary and exchange policy. Also, finding a balance between the recovery of the domestic market and export incentives.
41 Potential exporting sectors: science and technology, healthcare, agricultural sector (added value, meat export) Other extractive products such as mining (energy and lithium). Buenos Aires, along with Bogotá, Mexico City, Santiago de Chile and Curitiba, are the main Startup systems in Latin America, bringing together human talent, performance, financing and market reach. Startup Genome (2020).
vestment. But the weakness of the required policies is rooted in institutional instability and the lack of consensus.

In SME, the institutions involved in the economic activity depend on the political system: a republican democracy with alternation, under the rule of law. Consensus on institutions and policies that aim for the common good is the path for all reasonable forces, so the real struggle is for unity in diversity. Therefore, it is necessary to manage, the resolution of differences in a cooperative way through an institutional mechanism, such as an Economic and Social Council, reformulating dysfunctional corporatism, and placing electoral competition in a context that encourages developing the elements that are central to the political and economic order need by the country for equitable and sustainable development.

References


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42 The weakness in the creation and respect of solid and reputable institutions permanently contaminates the economic activity with short-term and merely instrumental views. On the contrary, growth requires increased savings and investment, which calls for clear rules of the game and predictability.

43 This requires a State with a capable bureaucracy, respect for private property, defense of the competition, stability of fiscal relations with the provinces, non-polarized foreign relations, and regional and global economic integration. More stable macroeconomics, with public spending that can be financed, better tax conditions for investment, job creation and exports. With more and better competition (less monopoly, privilege and corruption) and competitiveness. Resico M. (2019).


Graph 1.

Elaboración propia en base a datos de Fundación Norte y Sur, Ministerio de Economía, INDEC, FMI. Estimaciones del resultado financiero 2020 basadas en el nuevo Presupuesto 2020 (-10,5%) y estimación de saldo en cuenta corriente por Abeceb (+4,9%)
Graph 2.

Elaboración propia en base a datos de Ministerio de Economía, INDEC, Ferreres, ODSA UCA, proyecciones de PBI de REM (2020: -12.5%) y de pobreza ODSA UCA (45%).

Author profile

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