Institutional Determinants of the Argentinean Crisis: A Systemic Approach

Guillermo Cardoza
Julián Díaz
Adriana Ángel

ABSTRACT. The explanations given for the Argentinean crisis are fragmentary and center almost exclusively on the causal relationships among economic variables. This study builds on the interpretations that various economists have presented regarding the Argentinean crisis. Based on identified factors, a conceptual approach is used to expose the systemic and dynamic nature of the crisis and to permit an analysis of the interrelationship among the economic, political and institutional factors that triggered it.

The article contends that in addition to economic and financial factors, the Argentinean crisis was aggravated due to: (1) institutional frailty, inadequate political management, and lack of transparency, which led to increasing instability and uncertainty; and (2) institutional weakness and obsolescence, which hindered reform consolidation and juridical standards for guaranteeing property rights and adherence to contracts. The article also maintains that the solutions to the crisis required the coordinated actions of different economic and political agents within the framework of a new social pact.

Guillermo Cardoza is Professor, Instituto de Empresa, C. Pinar 7, Madrid 28006, Spain.

Julián Díaz is a PhD student, Universidad Carlos III de Madrid, c/ Madrid 126, Getafe (28903), Madrid, Spain.

Adriana Ángel is Adjunta vicedecanato de claustro, Instituto de Empresa, C. Serrano 105, Madrid 28006, Spain.

RESUMEN. Las explicaciones dadas sobre la crisis argentina están fragmentadas y se centran casi que exclusivamente en la relación fortuita de las variables económicas. Este estudio utiliza como base las interpretaciones presentadas por diversos economistas sobre la crisis argentina. Basándose en factores identificados, utiliza un enfoque conceptual para exponer la naturaleza sistémica y dinámica de la crisis, y permitir el análisis de la interrelación entre los factores económicos, políticos e institucionales que la provocaron.

Este articulo aboga que además de los factores económicos y financieros, la crisis argentina se agravó debido a: (1) la fragilidad institucional, una administración política inadecuada y la falta de transparencia, que aumentaron la inestabilidad e incertidumbre; y (2) la debilidad institucional y el anacronismo que obstaculizan la consolidación de la reforma y estándares jurídicos necesarios para garantizar los derechos a la propiedad y adherencia a los contratos. El artículo también defiende que las soluciones para la crisis exigen acciones coordinadas entre los diferentes agentes económicos y políticos dentro del marco de un nuevo pacto social.

RESUMO. As explicações fornecidas para a crise argentina são fragmentadas e concentramse quase que exclusivamente nas relações causais de variáveis econômicas. Este estudo aprofunda as interpretações que vários economistas apresentaram a respeito da crise argentina. Baseados em fatores identificados, é utilizada uma abordagem conceitual para expor as naturezas sistêmica e dinâmica da crise, e para permitir a análise do inter-relacionamento entre os fatores econômicos, políticos e institucionais que a provocaram.

Este artigo advoga que além dos fatores econômicos e financeiros, a crise argentina foi agravada devido a: (1) fragilidade institucional, gestão política inadequada, e falta de transparência, a qual majorou a instabilidade e a incerteza, e (2) debilidade institucional e anacronismo, impedindo a consolidação da reforma e de padrões jurídicos para garantir os direitos de propriedade e a adesão a contratos. O artigo também sustenta que as soluções para a crise demandam ações coordenadas dos diferentes agentes econômicos e políticos no contexto de um novo pacto social.

KEYWORDS. Emerging markets, Argentinean crisis, institutional determinants, competitiveness

> I believe that the lesson we got from the Argentinean crisis is that perhaps we had forgotten somewhat to separate the laws, norms, rules and institutions from the control of sustainability that the economic program required. As a result, we believe that it is extremely important to make evident the simultaneity in which people must give respect to institutions, fulfillment of contracts, respect for rules, respect for norms, and the quality and sustainability that the economic program has already undertaken.
>
> Speech by the Argentinean Minister of Economics,
> Roberto Lavagna, 4/2003.

INTRODUCTION

Studies on the Argentinean crisis of 2001 have centered almost exclusively on the interrelations among economic variables. For example, Feldstein (2002) cites the fixed exchange rate and the elevated level of external debt as the main factors responsible for the crisis.[1] Schuler (2002) presents evidence that dismisses the appreciation in Argentina's real exchange rate as the main reason. According to the author, the true causes are found in the growth rate of the foreign public debt during the 1990s, as well as the increase in taxes implemented in 2000 by President De la Rua. This increase contributed to decreased domestic demand and aggravated the recession, which had started towards the end of 1999.

In the opinion of Perry and Servén (2002), deflationary adjustments to the external shocks within a fixed exchange rate system coupled with elevated public debt, fiscal weakness and frailty in the financial sector[2] combined to bring about greater vulnerability to external shocks in Argentina. These authors maintain that the instability introduced by these factors generated a vicious cycle characterized by overvaluation of the peso,[3] increased unemployment, reduced aggregate demand, and the consequent economic stagnation. Specifically, they emphasize that the political decision to fix the exchange rate to the dollar within the framework of the Convertibility Plan increased the external shocks' impact on the overvaluation of the dollar and the devaluation of the Brazilian real, and limited possibilities for introducing adjustments.[4]

Similarly, Calvo, Izquierdo and Talvi (2003) assert that the rise in the real exchange rate in Argentina not only diminished the competitiveness of its exports, but that it also hid fiscal and financial problems and, as a result, postponed the adoption of corresponding measures.[5] For his part, Musa (2002) contends that the adherence to convertibility and the inability of Argentinean authorities to maintain a responsible fiscal policy were the principle causes of the crisis.

It is apparent that the explanations for the crisis given by economists fundamentally center on the study of causal relationships among macroeconomic variables. These partial focuses exclude an analysis of the role of institutional[6] and political factors and do not recognize the systemic nature of the crisis. As such, they lead to searches for short-term solutions. This is particularly valid in the case of the Argentinean crisis of 2001-2002. Although elements described by the economic models mentioned were present,[7] institutional deficiencies and poor political management intensified the crisis and a new conceptual framework is required to explain it. The contagion of the neighboring countries,[8] whose economies are also characterized by political and institutional instability, requires delving into the analysis of the Argentinean crisis in order to extract policy lessons for the public and private sectors.

Based on contributions from the authors cited, this article develops a conceptual systemic framework, which is valuable for studying the relationships and feedback mechanisms that are established among the decisive factors behind the Argentinean crisis. With this purpose in mind, and after a brief description of the Convertibility Plan and its macroeconomic results, the third part describes the economic factors that led to the crisis. The fourth section identifies the political and institutional factors responsible for the severity of the crisis, and the last part summarizes the main political elements and formulates recommendations for public and private sector leaders.

The methodology utilized to support the principal argument is based on statistical techniques of multiple regressions applied to the available data for the different institutional variables that are considered in the study. The majority of the information comes from the results of polls developed for the World Competitiveness Report, published by the World Economic Forum (WEF) in 2003. However, it is necessary to point out that only in the last few years has information on the quality of the institutional frameworks been compiled, so it is difficult to quantify the process and, consequently, the results must be interpreted with care.

THE CONVERTIBILITY PLAN AND MACROECONOMIC EVOLUTION

As a result of Argentina's weak situation due to hyperinflation in 1989, President Alfonsín resigned his position six months before the end of his term and was replaced by president-elect Carlos S. Menem, who after unsuccessful attempts to apply free market ideas, named Domingo Cavallo as Minister of Economics.[9] The new minister took a series of measures at the start of 1991 that constituted the basis for the Convertibility Plan,[10] launched on April 1 of the same year.[11]

The plan was successful, though not all the reforms that had been announced were implemented.[12] Argentina soon achieved significant monetary and fiscal results, along with real growth in its GDP. First, a large reduction in inflation was achieved, falling to levels similar to that of developed countries. The fiscal deficit was kept at minimal levels, not only due to the extraordinary influx of revenues for privatization,[13] but also due to the elimination of some of the roots of corruption and causes of the deficit. As a result of these reforms, between 1991 and 1998 the Argentinean economy registered elevated growth rates in real gross domestic product, reaching an accumulated increase of 42% during that period.

The implementation of the Plan resulted in greater economic stability, which reduced uncertainty among local economic agents, curbed the flight of capital, and attracted new foreign investors. Consequently, domestic credit increased, which, combined with the elimination of inflation and the reduction of country risk, produced lower interest rates and higher investment and consumption growth rates. As will be seen in section 3.3, an inflow of foreign direct investment (FDI) further contributed to strengthening the productive investment process.[14]

THE ARGENTINEAN CRISIS: A SYSTEMIC APPROACH

As the introduction indicates, the studies that describe the crisis in Argentina have principally centered on an analysis of economic factors. We also saw in the previous section that although the Convertibility Plan was initially successful, its results were short-lived and could not guarantee the sustainability of the economic model.

Public Deficit, Foreign Debt and Falling Investment: Causes of Stagnation

In 1995 the process of selling public companies was completed at the same time that a strong drop in tax collection occurred due to a recession caused by the "tequila" effect.[15] The fiscal situation continued to worsen due to two additional factors. The first was related to public pension system reform in 1994, which introduced various new elements into the design of the Social Security System. In effect, taxes collected by the federal government were reduced, because worker contributions began to be administered by private entities. The social security contributions that employers made were gradually reduced from 33% of the nominal salary in January 1993 to 16.5% in March 1995. The reduction in total social security contributions between 1995 and 2000 totaled 10 billion dollars (Roca, 2001).[16]

The second factor that aggravated the fiscal problem was the massive transfer of revenues from the central government to the provinces. From the start, the decentralization model did not work, as the provincial governments knew that the resources to cover their expenses would be provided by the central government as a last resort. Therefore, they lacked the incentive to maintain an adequate level of fiscal discipline and collection. As Saieght and Tomassi (1999) explain, such an effect is exacerbated when the macroeconomic forecast looks favorable, since provincial governments tend to increase public spending in anticipation of an increase in funds from the national government.

Table 1 shows the evolution of the fiscal deficit for the federal government at a consolidated level (provinces included). The provinces' deficit increased over the period, arriving at 2.5% of the GDP in 2001. It can also be observed that during this period Argentina had to resort to public debt in order to cover the growing fiscal deficit.

As Diagram 1 suggests, the combination of these factors led the Argentinean economy into a vicious cycle that brought about a deep recession.[17] The recurring and growing fiscal deficit forced the government to increase its debt positions in domestic and foreign capital markets. In turn, the rise in debt increased amortization and interest payments (debt services), which reduced the governments' (both federal and provincial) ability to invest in the infrastructure necessary to develop private activity. Table 2 shows the evolution of these variables.

Additionally, and as is also indicated in Diagram 1, the demand for funds in the domestic capital market on the part of the government reduced the credit supply for the private sector.[18] Domestic interest rates were raised, forcing private companies to resort to borrowing from abroad.

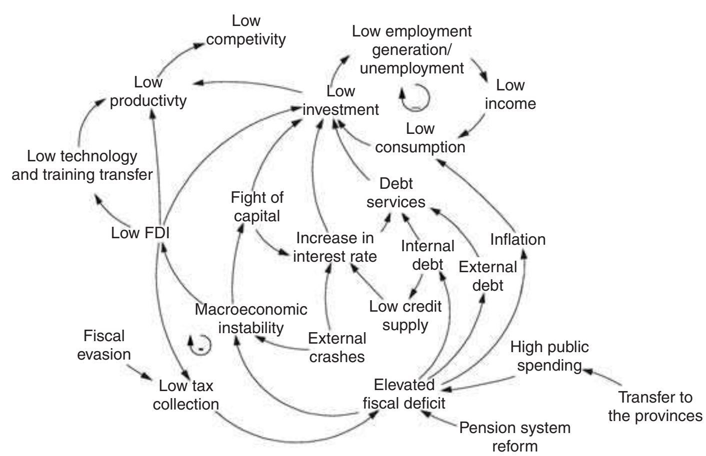
The consequences of this vicious cycle are obvious. The fall in investment generated a reduction in aggregated demand, and thus in profit. Additionally, the employment level dropped, thereby reducing income, which was accompanied by a drop in both consumption and

TABLE 1. Fiscal Deficit, Public Debt, Growth, and Unemployment

	1993	1994	1995	1996	1997	1998	1999	2000	2001
GDP (1)	5.7	5.8	–2.8	5.5	8.1	3.9	–3.4	–0.5	–4.5
Federal Deficit (2)	**0.4**	**–0.9**	**–1.9**	**–2.8**	**–1.4**	**–1.8**	**–3.0**	**–2.2**	**–3.9**
Consolidated Deficit (2)	–0.3	–1.9	–3.1	–3.6	–2.4	–2.5	–4.7	–3.6	–6.4
Consolidated Public Debt (2)	**32.8**	**35.1**	**39.2**	**39.8**	**38.1**	**41.3**	**47.4**	**50.8**	**64.1**
Gross Domestic Investment (2)	18.6	20.0	17.9	18.5	20.1	20.7	18.7	17.2	15.5
Domestic Savings (2)	**14.6**	**15.1**	**15.7**	**15.7**	**15.3**	**15.0**	**13.7**	**14.0**	**13.6**
Total Consumption (2)	5.3	5.0	–3.6	5.9	7.9	2.1	–2.1	–0.1	–5.1
Unemployment (2)	**9.6**	**11.5**	**17.5**	**17.2**	**14.9**	**12.9**	**14.3**	**15.1**	**16.4**

(1) Percentage change with respect to the previous year.
(2) Percentage of GDP.
Source: CEPAL(2002)(www.eclac.cl/estadisticas), and Krueger (2002) (www.imf.org/external/np/speeches/2002/071702.htm)

DIAGRAM 1. Economic Factors in the Argentinean Crisis: A Systematic Focus



savings (see Table 1). Furthermore, the economic deceleration meant reduced tax collection, which added to fiscal evasion, further increasing the deficit and public sector's financial requirements. This point, as suggested in Diagram 1, reinforced the dynamics of the vicious cycle, leading to a larger drop in productive investment.

TABLE 2. Primary Non-Financial Variable in the National Public Sector

	1995	1996	1997	1998	1999	2000	2001	2002
Total Public Expenditures (1)	25.6	25.4	25.2	25.8	28.5	28.2	29.8	26.63
Loans from Local Financial Sector to Public Sector (2)	**10.72**	**11.00**	**10.47**	**13.88**	**18.38**	**24.53**	**43.54**	**81.25**
Public Services Debt (3)	1.9	2.1	2.3	2.6	3.4	4.0	4.8	2.63
Public Investment (4)	**6.22**	**–**	**6.35**	**6.19**	**5.01**	**4.58**	**4.40**	**3.61**
Active Interest Rates (5)	–	10.48	12.64	110.82	13.45	16.86	49.96	78.83

(1) Percentage of GDP. Includes financial operations.
(2) Percentage of the total borrowed from the financial sector measured in December of each year.
(3) Internal and external debt service as a percentage of GDP.
(4) Percentage of primary public expenditures.
(5) Measured each year through December with the exception of 2002 whose value corresponds to the month of August.
Source: Ministry of Economy of Argentina Republic, Statistics Report (www.mecon.gov.ar).

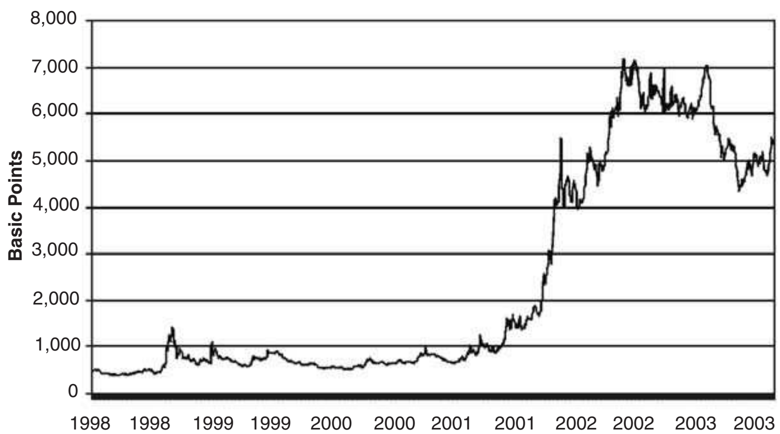
External Shocks, Overseas Financing and Unemployment

During the 1990s, there was a high availability of funds in the international capital market. This gave Latin American countries, whose domestic savings rates were low, a source for both public and private financing. However, access to this financing diminished due to several external shocks. The first was the Asian crisis of 1997. One year later the Russian crisis unfolded when the government of that country defaulted on part of its short-term internal debt. Lastly, in January 1999, Brazil devalued its currency in light of its inability to continue supporting its fixed value in relation to the dollar.

As Diagram 1 suggests, the worldwide macroeconomic instability significantly reduced the funds available to emerging countries, and as a result, interest rates increased. In Argentina's case, the reduction of foreign funds combined with a deteriorating fiscal situation–among other factors[19]–led to an increase in country risk, also due to the contagion effect. Figure 1 shows the evolution of the country risk[20] of the bonds issued by the government of Argentina.

As Figure 1 shows, from 1998 on, the spread ascends rapidly, arriving at values of more than 7,000 basis points at the end of 2002. This increase meant greater debt services (see Table 2),[21] which also in turn represented a greater financial burden for the public and private sectors.

FIGURE 1. Sovereign Country Risk of Argentinean Sovereign Bonds



Source: Adapted from J.P. Morgan, Emerging Countries Indicators (2003).

This brought about an increase in interest rates, and created an additional reduction in productive investment, which then led to a drop in employment. In effect, as Table 1 indicates, near the end of the last decade, unemployment was above 14% of the active economic population, and then reached 16.4% near the end of 2001.

Macroeconomic Instability, FDI and the Flight of Capital

Argentina was one of the main recipients of FDI flows into Latin America during the 1990s. During the 1990-1994 period, it received an annual average of US$2.99 billion, which increased between 1995 and 1998 to US$6.78 billion. The largest flow was reached in 1999, when foreign investment hit a value of US$23.15 billion.[22] Spain stood out among the countries that exported capital, with investments during the period of 1992-2001 reaching $26.3 billion (Chislett, 2003). However, this flow began to diminish due to the perception of risk that foreign investors had because of greater economic instability, the continued deterioration of the fiscal situation, and the start of the recession in 2000 (see Table 1). FDI flows fell to US$5 billion in 2001, representing barely 6.5% of the FDI received by Latin America that year (J.P. Morgan, 2003).

Additionally, as Diagram 1 suggests, Argentina saw itself affected by a strong reduction in the supply of private credit, principally caused by a very sizeable flight of capital.[23] This massive exit of funds also contributed to an increase in domestic interest rates and, consequently, the level of productive investment was reduced.

This situation was aggravated towards the end of 2001.[24] A drop in deposits led to lower liquidity in the banking system, an increase in active interest rates and, consequently, lower availability of credit for the private sector. Afterwards, declarations of default were made and the end of convertibility was announced. On December 20, 2001, President de la Rúa resigned. During the next two weeks, various governments followed and the game rules for national and foreign investment were changed, a fact which increased uncertainty for economic agents.[25]

As Diagram 1 indicates, the retreat of foreign capital, together with the acceleration in the flight of domestic capital, diminished the amount of productive investment, which reduced the aggregated employment demand and income, intensifying the recession in the Argentinean economy.[26]

The combined effect of these factors was reflected in an increase in poverty,[27] underemployment and unemployment, and emphasized the trend of increased inequality that had escalated without interruption since 1993 (Perry and Servén, 2002). Diagram 1 offers us a global view of the crisis from the economic standpoint, showing the interrelationship established between the diverse factors present. Nevertheless, the explanation of the crisis is still incomplete, in as much as the influence of political and institutional factors have not yet been taken into account. The next section tackles the analysis of these elements.

POLITICAL AND INSTITUTIONAL FACTORS IN THE CRISIS

In the previous sections, the effects of the Convertibility Plan were described and the relationships established among the economic factors–which partly explain its failure towards the end of the 1990s–were defined. As the systemic analysis illustrated, aside from the external shocks and withdrawal of capital flows, the remaining factors of the Argentinean crisis were domestic. In this section, it is argued that the crisis escalated due to different political and institutional factors, whose origins can be traced to the contemporary history of the country.

The Institutional Framework: Populism, Clientelismo and Public Spending

Since the beginning of Juan Domingo Perón's first term in 1946, Argentina has been led by governments that to a greater or lesser extent have received their principal electoral support from nationalist populist policies.[28] As Diagram 2 shows, this phenomenon, also present in other Latin American countries, was supported in, public expenditures, *clientelismo*[29] and favor-seeking behavior, among others. As such, the populist regime tried to legitimize itself through: (1) high public spending policies; (2) the granting of public positions in exchange for votes and support, and (3) the granting of generous contracts, perks and subsidies to different societal sectors close to the regime.

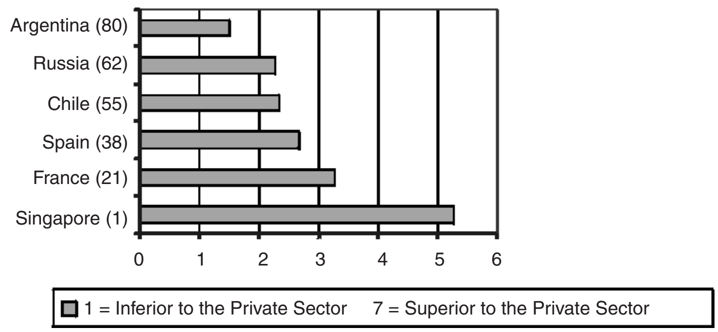
Clientelismo took on immense importance in Argentina with the return to democracy in 1983. In effect, during the 1983-1999 period, the number of political party members grew 270% (United Nations, 2002). One of the consequences of the hyperactivity in the political market was a substantial rise in the number of political positions. According to Krueger (2002), in 1999, 12% of the labor force in all of Argentina worked in the public sector, while in other countries, like Mexico and Brazil, the levels maintained were lower–4.5, and 7.3%, respectively.

Additionally, *clientelismo* practices had a negative impact on public administration efficiency, given the low levels of training and the non-existence of productivity incentives. As Figure 2 illustrates, competency among public employees was clearly lower than what was observed among private sector workers–much lower than in countries like Spain and France.[30]

Argentinean governments have frequently been accused of favoring corporations or individuals linked to the party in power. As Figure 3 shows, in the opinion of businessmen, favor-seeking on the part of certain sectors of the Argentinean society is a habitual practice in the country. In particular, Argentina's poor performance is noted in comparison to countries like the U.S. and Japan.

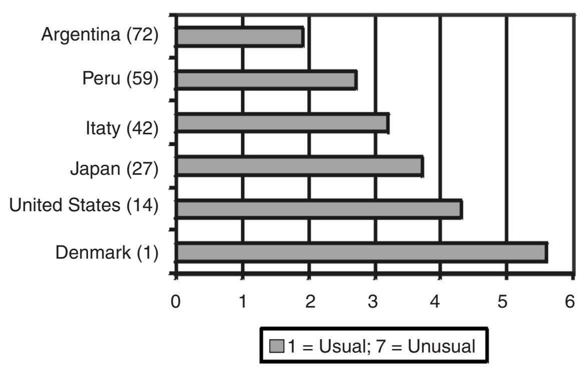
It is important to note that public expenditures in Argentina have grown over the last 40 years. While in 1960 consolidated public spending, as a percentage of GDP, was 18%, its value rose to 25% around 1980 and to over 30% at the end of 1999 (Bulacio, 2000). The rapid growth in public spending–primarily during the 1990s–has been closely related to the increase in spending on public sector wages, which has already been indicated as a very common practice in populist regimes.[31]

FIGURE 2. Competency Among Public Employees (2002)



Source: Own elaboration based on World Economic Forum (2003).

FIGURE 3. Rent Seeking Practices (2002)



Source: Own elaboration based on World Economic Forum (2003).

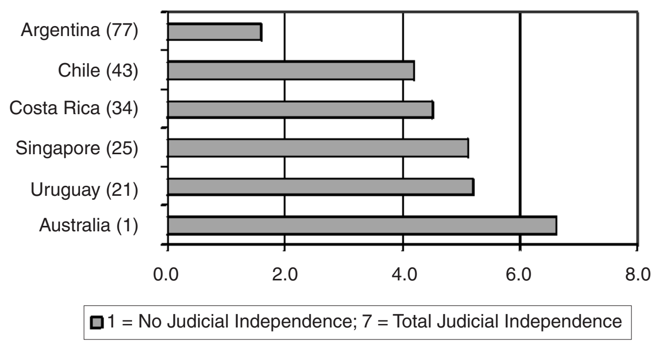
Thus, a relationship is observed between the institutional and economic factors within a country.

Populism, Judicial Dependence and Corruption

In order to protect the interests of political organizations, trade unions and corporate management close to its populist regimes, an institutional framework was adopted in Argentina that looked to maintain the *status quo*.

A clear example of this was the lack of independence of the judicial power in Argentina. In Figure 4, we can observe that in comparative in-

FIGURE 4. Independence of the Judicial Power with Respect to the Government (2002)



Source: Own elaboration based on World Economic Forum (2003).

ternational terms, Argentina is among the judicial systems most dependent on political power (WEF, 2003). Evidence of this is the fact that the populist rule, in both the central government and the provinces, has proceeded to remove and to choose judges based on their ideological affinity and on their disposition to defend the interests in the game.[32]

Another result of the interdependence between politics and judicial power is the limited transparency in government decision-making. Argentina placed poorly in the surveys done by the World Economic Forum on governmental transparency (WEF, 2003). As Figure 5 illustrates, Argentina was last among the 80 countries in the study.

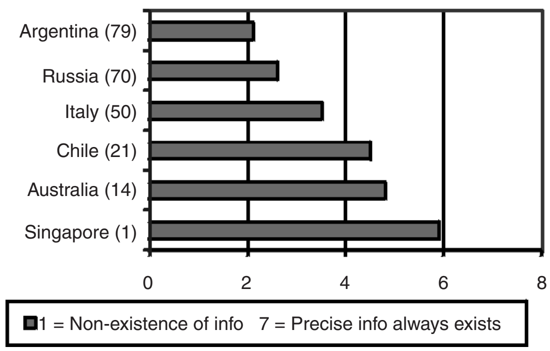
As Diagram 2 suggests, judicial power dependence, coupled with the weakness of the judicial framework and the lack of transparency and accountability, created a climate ripe for impunity and corruption[33] in both the public and private sectors.[34]

To summarize, as Diagram 2 indicates, the weakness in the institutional framework has generated a growing perception of uncertainty and distrust with both domestic and foreign economic players, not only around the government and political parties, but also toward other institutions such as the courts, banks and private companies.[35] Another result of this dynamic, shown in Diagram 2, has been the loss of legitimacy for political organizations in Argentina.

Institutional Framework and Macroeconomic Evolution

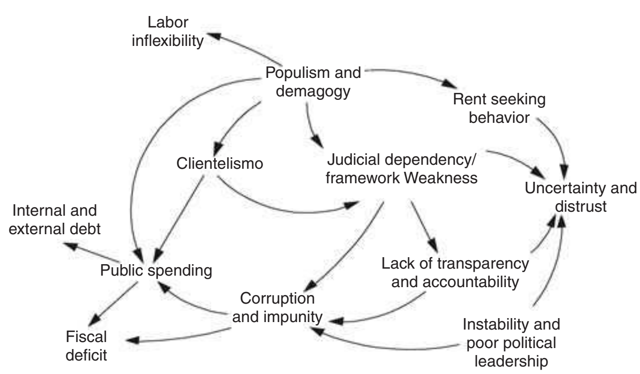
The institutional framework described in the previous sections was kept invariable during the 1990s, the period of enforcement of the Con-

FIGURE 5. Transparency into Government Acts (2002)



Source: Own elaboration based on World Economic Forum (2003).

DIAGRAM 2. Institutional Dynamics and the Crisis in Argentina



vertibility Plan. The lack of fit between the existing framework and the objectives pursued by the plan, on one hand, and the resistance to adopting a new institutional framework, on the other, created significant barriers for the economic and political reforms. As Diagram 2 suggests, the institutional and political factors indicated also shaped the evolution of the Argentinean economy during the 1990s, and were decisive in the unfolding of the crisis. As will be analyzed in the next sections, the populist practices based on *clientelismo*, the weakness of the judicial system and corruption were also responsible for:

1. introducing inflexibility into the labor market,
2. contributing to worsening the deficit through increases in public spending, and
3. resulting in declines in both the domestic and foreign productive investment flows required to maintain economic growth.

Populism, Labor Market Rigidities and Employment

With respect to the labor structure, the overall strategy of the populist governments and the labor unions under their influence consisted in unions being granted the power to negotiate sector agreements in matters such as employment conditions and wages. As Figure 6 shows, in the mid-1990s, over 72% of employed Argentineans were protected by collective bargaining agreements–a much higher percentage than in other countries. In addition, the populist governments offered improvements to workers through the promulgation of employment protection laws, which, together with the centralized negotiation of labor agreements, introduced major rigidities into the labor market.

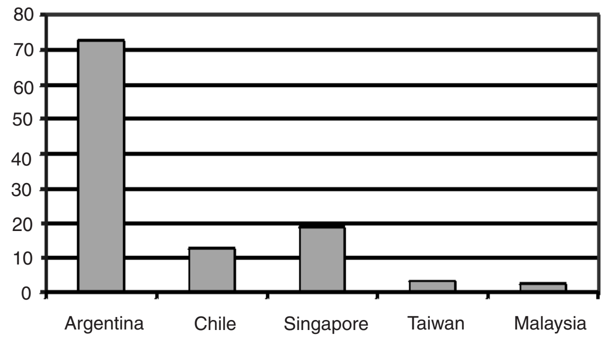
These labor market rigidities impeded:

a. short-term wage rate adjustments, when confronted with fluctuations in labor supply and demand,
b. maintenance of an employment growth rate in the long-term, since the high costs of firing discouraged firms from creating employment (OECD 2000), and
c. resistance to the negative effects that domestic and external shocks had on the employment level (Phelps and Zoega, 2001).

Judicial Dependence, Corruption, Instability and Uncertainty: Their Impact on FDI and the Domestic Credit Supply

As Diagram 3 indicates, the combined effect of limited property rights protection, corruption,[36] instability and uncertainty led to loss of confidence among the economic players in the judicial-legal framework, and, consequently, the flight of capital and a drop in both direct and indirect foreign investment. Additionally, the government's nonfulfillment of contractual obligations, identified as "obsolescing bargaining" by Vernon (1971), affected foreign economic agents' decisions on investing in Argentina.[37]

FIGURE 6. Proportion of Employees Covered by a Collective Work Contract (1995)



Source: Márques and Pages (1998)

Figure 7 shows the relationship between FDI and property rights protection. As can be observed, the relationship is positive, with a partial correlation of 0.25.

In addition, Diagram 3 shows how the supply of domestic credit,[38] directly influenced by the institutional variables indicated, also affected productive investment levels. The analysis of the domestic capital stock development shows that between 1990 and 2000 Argentina experienced a massive flight of capital.

In other words, when faced with general distrust and lack of guarantees for recouping credit, economic agents prefer to abstain from investing, and as the case of Argentina demonstrates, they choose to withdraw their capital. This leads to a reduction in credit supply and a drop in the productive investments that the economy requires to generate employment and maintain the growth rate of its product.

In fact, Figure 8 illustrates how a lack of confidence in the political leadership also contributed to reducing domestic credit supply in the country (positive correlation of 0.553).[39]

With the intention of investigating the relationship between quality in the judicial environment and the reduction in domestic credit supply that Argentina experienced, an analysis was also done between domestic credit and two variables: (a) level of property rights protection, and (b) degree of judicial independence. Figures 9 and 10 show that a positive relationship was found (0.692 and 0.614, respectively), which verifies that the deterioration in property rights protection and the weakness of the judicial framework also explain, at least partially, the reduction in

DIAGRAM 3. Crisis in Argentina (2000-2001): A Systemic Approach

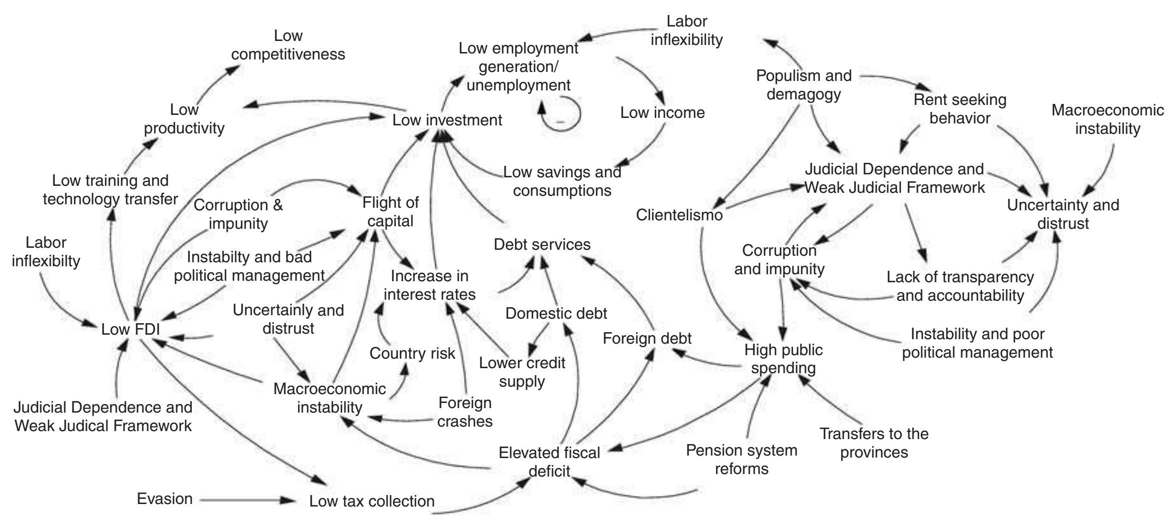
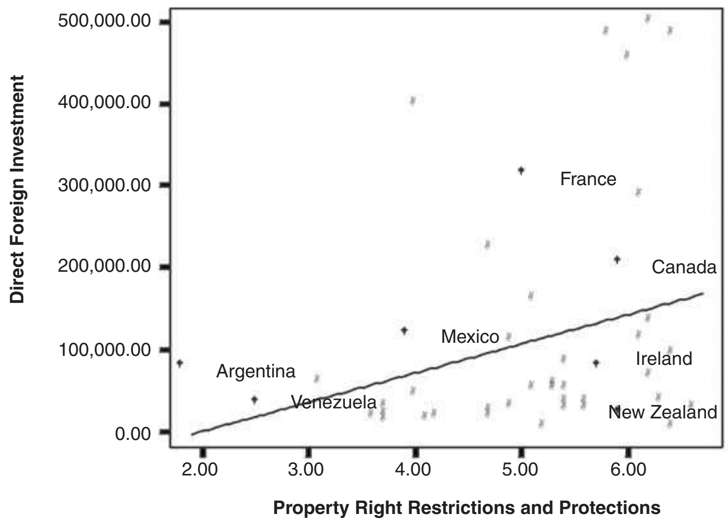
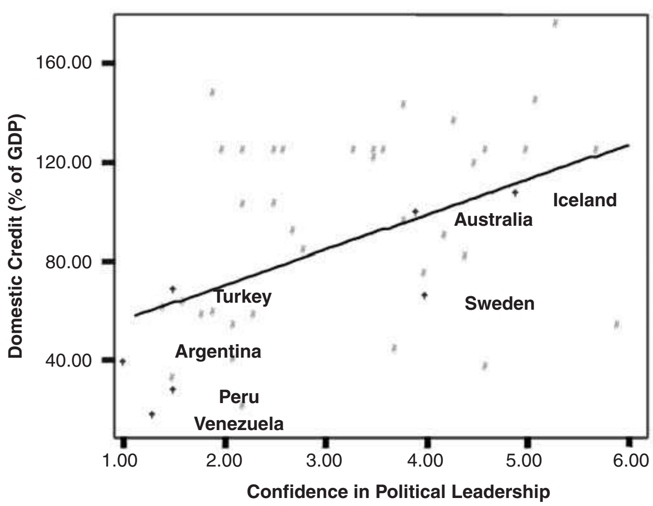


FIGURE 7. FDI Stock and Property Right Protections (2001)



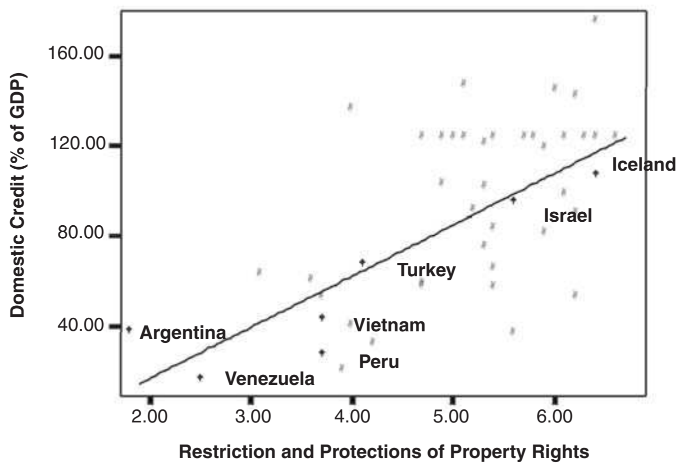
Source: Own preparation based on World Economic Forum (2003).

FIGURE 8. Domestic Credit and Confidence in the Political Leadership (2002)



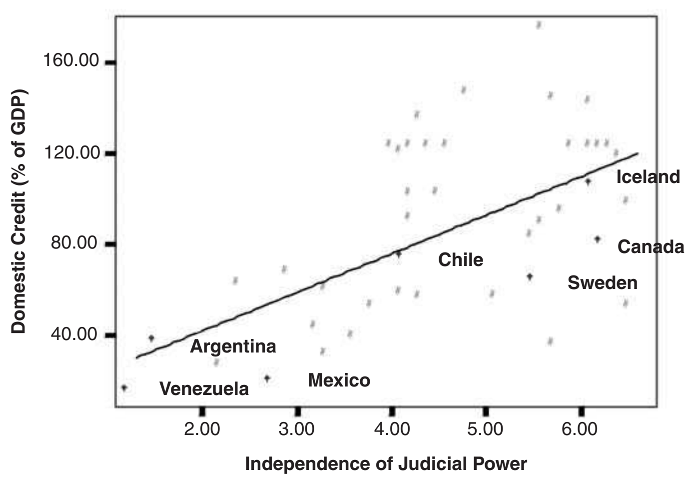
Source: Own preparation based on World Economic Forum (2003).

FIGURE 9. Domestic Credit and Property Rights Protections (2002)



Source: Own preparation based on data form WEF (2003).

FIGURE 10. Domestic Credit and Judicial Power (2002)



Source: Own preparation based on data from WEF (2003).

the domestic credit supply that the country experienced during the last years of the 1990s.

It is clear that the lack of judicial independence and the inability to enforce adherence to contracts and norms that govern financial transactions explain the massive withdrawal of bank deposits and the consequent rupture in the payment chain–essential elements in the functioning of any modern economy.

To summarize, Figure 11 allows us to take into account the relationship that exists between the lack of confidence in the economic situation, the reduction in direct and indirect foreign investment, and the flight of domestic credit.[40] This figure shows that confidence and FDI are variables that tend to move in tandem. It is clear that at the end of the 1990s, an inverse relationship existed between confidence and the flight of capital.[41]

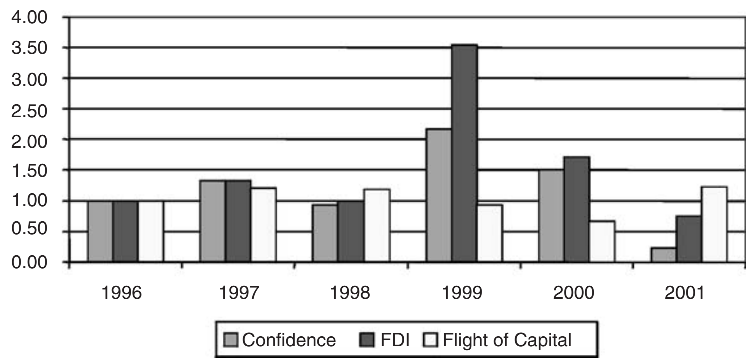
As is suggested on the left of Diagram 3, instability and inadequate political management led to corruption and uncertainty, accelerated the flight of capital and discouraged foreign investment. The combination of these factors resulted in a reduction in the resources available for productive investment, an increase in the cost of capital and with it a fall in product growth rate, intensifying the recession.

FDI and Credit Supply: Their Impact on the Economic Growth Rate

Diagram 3 shows that the dynamics that were established between the institutional, economic, and political factors drove the Argentinean economy into a vicious cycle of low investment, low employment generation, low income levels, and as a result, falling levels of domestic consumption and savings–key factors for economic growth. In other words, the systemic analysis allows verification of the fact that the institutional problems were also present in the Argentinean economic crisis, since they conditioned the behavior of economic agents.

In order to reinforce our argument, various multiple regressions were done between the average GDP growth rate during the period of 1997-2001 and a series of institutional variables. The results are noted in Annex 1. With the exception of the government acts transparency variable, all the other institutional variables appear to influence growth significantly. Furthermore, the positive sign of the institutional variables reinforces the argument supported in this work: the greater the institutional quality, the greater the economic growth.[42] This coincides with the evidence contributed by previous works.[43]

FIGURE 11. Economic Uncertainly, FDI, and Flight of Capital



Source: Own construction based on Lationobarómetro (2002) and BID (2002).

In the second part of this work we have held that the formal and informal institutions inherited by the populist regimes:

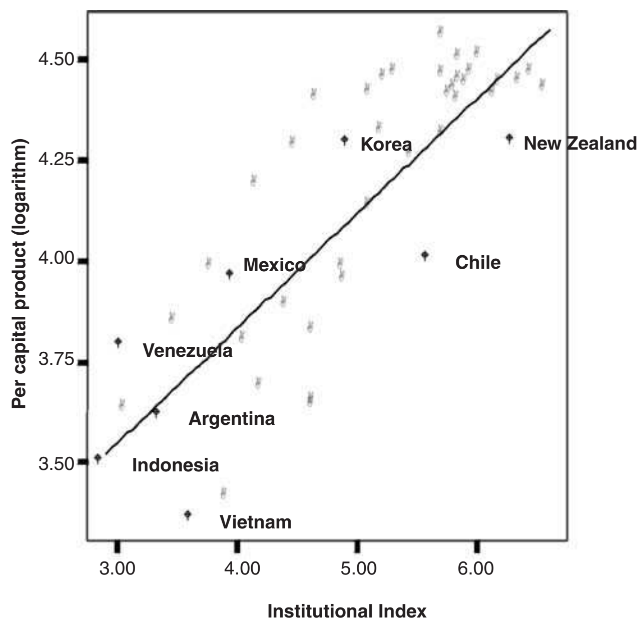
1. conditioned the rhythm and the results of free market reforms in Argentina;
2. generated great uncertainty towards and distrust of the economic players;
3. contributed to intensifying the Argentinean crisis and made it harder to resolve.

The deterioration and frailty of the political-institutional framework played a key role in the evolution of the crisis, and it is therefore necessary to take into account these factors in making a better diagnostic and designing sustainable solutions.

In a manner of concluding, Figure 12 shows that a clear relationship exists between the degree of institutional development[44] and gross domestic product per capita for the collection of selected countries (positive correlation of 0.818).

In the next section, some lessons are extracted from the Argentinean crisis for the parties responsible so that they may design, execute and evaluate development policies, as well as for the domestic and foreign companies that operate in emerging economies that are characterized by instability and uncertainty.

FIGURE 12. Institutional and Economic Development (2002)



Source: Own preparation based on data from WEF (2003).

CONCLUSIONS

In addition to the domestic and foreign factors indicated in the literature, towards the end of 2001 the Argentinean crisis was aggravated by weaknesses in the institutional structure and political instability. As was described in the preceding section of this work, institutional frailty and poor political management increased instability and uncertainty, and impeded development of a timely and adequate response during the different stages of the crisis.

Likewise, the obsolescence of the institutions in power conditioned the rhythm and the results of free market reforms in Argentina. Furthermore, the weakness of the judicial framework added to the lack of transparency and accountability, creating an environment conducive to corruption. This, in turn, impeded the securing of property rights and adherence to contracts.

The data and calculations have shown a high correlation between institutional frailty, credit supply, and economic growth. The increase in uncertainty and the loss of confidence deters FDI, and leads to a massive outflow of capital, along with a drop in domestic credit supply, and, consequently, a reduction in resources available for productive investment. These factors plunged Argentina into a vicious cycle of distrust, political instability, unemployment and economic recession.

Argentina's case also illustrates another interesting problem that will require greater investigation in the future. The transition to the new political and economic model has been made difficult by a lack of adjustment between the formal institutions and the informal institutional frameworks that govern the economic and social relationships. While the creation of these formal institutions has implicated, in principal, changes in labor, finance, education, and trade legislation, the informal institutions (traditions, practices, etc.) have required more time to adjust. This imbalance has created a paradoxical situation: the institutional platform has been prepared–at least formally–but individuals and groups have continued operating using informal institutions acquired during previous regimes.

In summary, the dynamics described indicate that the crisis in Argentina is of a systemic and multidimensional nature and establishes the need to tackle the analysis from an integrated perspective that allows better understanding of the interrelationship between the economic, political and institutional factors that unfolded. Only under circumstances of understanding the multiple relationships established between the factors/key variables and the role that the different economic and political agents play will a better diagnostic be developed, along with a political framework that allows the designing of viable and sustainable solutions to the crisis.

NOTES

1. Feldstein (2002) indicates that the low domestic savings rate and elevated public spending were the direct causes of Argentina's indebtedness.

2. One of the greatest weaknesses of the Argentinean financial system is related to elevated credit granted to the public sector, which constitutes 26.4% of banks' debt portfolio.

3. De la Torre et al. (2002) have estimated that around 2000, the real exchange rate in Argentina was overvalued by 50%.

4. According to Perry and Servén (2002) and De la Torre et al. (2002), from the beginning, President de la Rúa's government fell into the trap of low growth, high debt, overvalued currency, and a fixed exchange rate.

5. Among the problems mentioned by Calvo, Izquierdo and Talvi (2003) are: the dollarization of corporate and government liabilities, which made the country more vulnerable to depreciation in the exchange rate and the low proportion of goods traded abroad as a percentage of GDP.

6. Institutions are created to: (1) structure and coordinate political, economic, and social relationships among the members of a certain society and which are therefore essential for economic development (Williamson, 1985; North, 1991), and (2) reduce the uncertainty in exchanges derived from imperfect information that economic players possess (North, 1993, 1995). Market efficiency depends on their quality and functioning.

7. Argentina exhibited an elevated fiscal deficit and had a fixed exchanged rate, and, additionally, investors' expectations for the floating of the exchange rate and the devaluation that followed produced a massive outflow of capital, reduced the international reserves and pressured interest rates.

8. Between July and August of 2002, Uruguay suffered the "contagion effect" of the Argentinean crisis with a restriction on the withdrawal of bank capital and uncertainty around the viability of certain financial institutions.

9. The previous Economic Minister, Herman González, had to resign after another hyperinflation event occurred in January 1991.

10. The Currency Board, the monetary component of the Plan, was based on one-to-one parity between the peso and the U.S. dollar, entrusting to the Central Bank the responsibility of guaranteeing this conversion with reserves denominated in foreign currencies in an amount equal to 100% of the monetary base. This restriction on the reserve composition could be relaxed in certain circumstances, permitting that 80% of the monetary base was backed with dollars, while the remaining 20% was composed of national government debt titles.

11. Among the measures promised by the Menem administration were: privatization of state companies, government reform, opening of the economy to the foreign flow of goods and services, fiscal discipline, labor reform, and economic deregulation.

12. Beyond privatization, the national government structures as well as those of the provincial states–principally the latter–were not greatly modified. In addition, labor reform only introduced minor modifications, without offering solutions to the inflexibilities of the labor market. For a description of the labor market in Argentina and other Latin American countries, see Márquez and Pages (1998).

13. The government sold more than 250 companies, mainly in the sectors of telecom, gas, oil, rail, air, and electricity, receiving more than US$30 billion (Espert, 1996). According to Krueger (2002), during the 1992-1994 period, the average consolidated public deficit was situated at around 0.9% of the value of the GDP.

14. In addition, FDI not only generated tax revenue, but also created direct and indirect jobs. For example, the FDI stock from Spanish business alone generated 11% of the total tax revenue in Argentina around the year 2001, and in turn gave direct employment to 70,000 workers (FUCAES, 2002).

15. Tax collection during 1995 was 5.2% lower than what was registered in 1994 (Ministry of Economy of Argentina Republic, Economic Report, 1996).

16. Roca (2001) also estimates that this amount represents approximately 25% of the public debt generated during the same period.

17. As a consequence of the recession that began in 2000, the total tax collected dropped by almost 11% between the years 1998 and 2001 (Krueger, 2002).

18. Between 1993 and 1998, both domestic credit to the public sector and to the private sector increased to 68% and 72%, respectively. However, for the period between 1998 and 2001, while internal credit to the public sector was reduced by 5%, credit to the private sector was reduced by 35% (Ministry of Economy of Argentina Republic).

19. The drop in the international price of Argentinean product exports, along with the rigidity of the exchange system tied to the dollar, are the factors commonly cited in the literature. For a more extensive explanation, see Fanelli (2002).

20. The literature addressing "country risk" recognizes the effect of the fiscal situation on the level of country-risk. See Eaton and Stiglitz (1986) for a comprehensive review of the literature.

21. In mid- 2001, 32% of the public debt was composed of debt with floating interest rates (Pontoni, 2002).

22. These values represented 16.7%, 12.25%, and 25.58%, respectively, of the FDI received by Latin America (Paiva Abreu, 2002).

23. The process of the flight of capital reached its highest point in 2002, when $13.5 billion left the country, which represented 16% of the GDP (Blázquez and Sebastián, 2004).

24. First, as noted by Perry and Servén (2002), the Minister created an import tax and subsidized exports. This decision increased doubts about the support for convertibility, since it had broken the basic contract of one to one peso-dollar parity for trade transactions, and it raised the prospect that it could also be broken for financial transactions. Second, on November 30, 2001, Cavallo imposed a withdrawal restriction on savings account holders' deposits, a measure known as the *corralito*.

25. In effect, among other measures, the peso was devalued, an asymmetrical *pesificación* was declared, taxes for oil exports were fixed and charges for public services were frozen. The tax on profits was increased as well as the tax on assets (Schuler, 2002).

26. The default of the Argentinean government affected not only foreign holders of public debt, but also domestic holders–mainly banks and the Pension Fund Administration. In June of 2001, domestic public debt represented approximately 40% of the total public debt (Pontoni, 2002). This fact brought about additional reductions in income, investment, savings and consumption.

27. According to the National Institute of Statistics and Census of Argentina (INDEC, 2002), 35.9% of the population in May 2001 was found living below the poverty line. In October of the same year, the level rose to 38.3%.

28. For a description of this populist phenomenon in Argentina, see also Auyero (2000).

29. Clientelismo is an old political practice in Argentina that looks for electoral support through the granting of public administration positions. It is based on the contracting of an agent (*puntero*, according to Argentinean political terminology), charged with hiring and mobilizing members in parties' internal elections. Thus, the politician with the greatest backing of votes within the party is chosen to represent the party in the general elections, obliging him or her to repay the support received through positions in public offices or within the party itself.

30. As an example, note that the opening of a new company in Argentina required 60 more days of bureaucratic procedure, in comparison to the number of days required in Canada (Djankov et al., 2002).

31. Krueger (2002) indicates that public spending in wages increased from 7.63% of GDP in 1991 to 9.87% in 2001.

32. Since the presidency of Perón, five of the seventeen presidents (in a period of 50 years) during their term have appointed all the members of the Supreme Court of Justice. The average duration of justices' positions in Argentina is 3.7 years, compared to 12.5 years in the U.S.A. or 9.6 years in Australia (Spiller and Tommasi, 2000).

33. According to studies on the perception of corruption done annually by *Transparency International*, with the exception of the periods 1988-1992 and 1980-1985, when it obtained averages of 5.91 and 4.94, respectively, Argentina has had marks of four points or less (0 = total corruption, 10 = without corruption).

34. In addition to judicial dependence, and perhaps as a consequence of it, a clear judicial ineffectiveness is observed related to restricting and adhering to property rights in Argentina. Economic agents, according to the WEF survey, share this opinion. The managers polled placed Argentina last in this variable.

35. Towards the end of 2001, the distrust of Argentinean society towards its institutions was above the Latin American average. In response to the question "Would you say that you have much, some, little or no confidence in . . .?" the total of the "little" and "none" responses was above or equal to 90% for political parties, the government, banks, national congress, and judicial power, and about or equal to 80% in relation to municipal administrators and private companies. In 1996, 34% of those surveyed expressed satisfaction with the democracy; around 2002, the percentage had fallen to 8% (Latinobarómetro, 2002).

36. For an extensive study on the impact of corruption on the rate of growth, see Murphy, Séller and Vishny (1993) and Mauro (1995).

37. According to evaluations by Cornelius et al. (2002), insecurity and instability, among other factors, impeded the arrival in Argentina of at least US$14.15 billion between the years 1990 and 1999. In addition, a poll taken on Spanish business leadership indicated that corruption, judicial insecurity, bureaucracy and political instability are likewise among the major obstacles to investment in Latin America (BID, 2004).

38. It is necessary to clarify that the domestic credit supply consists not only of the domestic capital that forms part of the local financial system, but also of the foreign capital invested in fixed and variable financial instruments (investment portfolios).

39. Brunetty, Kismko, and Weder (1998) also found a direct and positive impact between the credibility of public organizations and private productive investment.

40. Confidence in the future evolution of the economy is an index set by Latinobarómetro. Foreign direct investment and flights of capital are expressed in flows, and are taken from De Soto (2001). All measurements have been standardized in line with 1996 for the purpose of facilitating interpretation.

41. The high value of FDI registered in 1999 is due to the sale of Argentine state petroleum YPF to the Spanish oil company Repsol.

42. And vice versa as well: the greater the economic growth, the greater the institutional development. This relationship is not the focus of this article's study, but can be found in Huber, Rueschemeyer and Stephens (1993).

43. See, for example, Barro (1991) and Sachs and Warner (1997). For his part, Levine (1999) holds that a higher quality in institutions leads to greater financial development, and hence, greater economic growth.

44. The index of institutional development proposed by the World Economic Forum (2003) is a combination of different institutional indicators.

BIBLIOGRAPHY

Arellano, J. (2002). International competitiveness and education in Latin American and the Caribbean countries, in: J. Vial & P. Cornelius (Eds.), *The Latin American Competitiveness Report*, New York, Oxford University Press.

Auyero, J. (2000). "The logic of political clientelism in Argentina: An ethnographic account," *Latin American Research Review*, Vol. 55, No. 3, pp. 399-422.

Barro, R. (1991). "Economic growth in a cross section of countries," *Quarterly Journal of Economics*, Vol. 106, No. 2, pp. 407-443.

BID (2004). *La percepción de los inversores de los riesgos regulatorios e institucionales en América Latina*, Washington: Publicaciones IFM.

Blázquez, J., & Sebastián, M. (2004). El impacto de la crisis argentina sobre la economía española, Real Instituto Elcano, Documento de Trabajo DT no. 11/2004.

Bonifacio, J., & Falivene, G. (2002). Análisis comparado de las relaciones laborales en la administración pública latinoamericana, *CLAD*, 8, pp. 1-34.

Brunetti, A., Kisunko, G., & Weder, B. (1998). "Credibility of rules and economic growth: Evidence from a worldwide survey of the private sector," *The World Bank Economic Review*, Vol. 12, No. 3, pp. 353-384.

Bulacio, J. (2000). La ley de Wagner y el gasto público en Argentina, unpublished paper, Universidad Nacional de Tucumán, Argentina, http://www.aaep.org.ar/espa/anales/resumen_00/bulacio.htm

Calvo, G. (2002). Política económica en aguas borrascosas: vulnerabilidad financiera en economías emergentes, Universidad del CEMA, Documento de Trabajo No. 178.

Calvo, G., Izquierdo, A., & Talvi, E. (2003). Sudden stops, the real exchange rate and fiscal sustainability: Argentina's lessons, NBER Working paper No. 9828.

Cardoza, G., Flores, J., & Soto, J. (2001). Competitividad internacional en México, América Latina y Asia del Este, *Mexican Academy of Sciences. . . .*

Cardoza, G. (1997). "Learning, innovation and growth in East Asia and Latin America," *Science and Public Policy*, Vol. 24, No. 6, pp. 377-393.

CEPAL (2001). *Inversión extranjera en América Latina y el Caribe*. Informe 2000, Comisión Econômica para América Latina.

CEPAL (2002). *Anuario Estadístico de América Latina y el Caribe 2001*, Comisión Económica para América Latina.

Chang, R. & Velasco, A. (1998). The Asian liquidity crisis, NBER Working Paper No. 6796.

Chemark, J.M. (1992). "Political risk analysis: past and present," *Resources Policy*, Vol. 18, No. 3, pp. 167-178.

Cornelius, P., Hall, T., & Kurtzman J. (2002). "Opacity, foreign direct investment, and economic growth," in: J. Vial and P. Cornelius (Eds.), *The Latin American Competitiveness Report*, New York: Oxford University Press.

De La Torre, A., Levy Yeyati, E., & Schumkler, S. L., (2002). Argentina´s financial crisis: Floating Money, sinking banking, NBER conference "The Argentina crisis," 17 July 2002.

De Soto, H. (2001). *Competitividad: El motor del crecimiento*, Washington: Publicaciones IFM.

Della Paolera, Gerardo, & Ortiz, J. (1995). Dinero, intermediación financiera and nivel de actividad en 110 años de historia económica argentina, Universidad Torcuato Di Tella, Working Paper No. 36.

Diamond, D. & Dybig, P. (1983). "Bank runs, deposit insurance, and liquidity," *Journal of Political Economy*, Vol. 91, No. 3, pp. 401-419.

Djankov, S., La Porta, R., López-de-Silanes, F., & Shleifer, A. (2002). "The regulation of entry," *Quarterly Journal of Economics*, Vol. 117, No. 1, pp. 1-37.

Eaton, J., and Stiglitz, J. (1986). "The Pure Theory of Country-Risk," *European Economic Review*, Vol. 30, No. 3, pp. 481-513.

Eichengreen, B. (2001). "Toward a new financial architecture: A practical Post-Asia agenda," *Asean Economic Bulletin*, Vol. 18, No. 2, pp. 240-242.

Eichengreen, B., & Rose, A. (2001). "The empirics of currency and banking crises," *NBER Reporter*.

EL PAÍS (2002). "La desaparición de Argentina sigue su curso," 14 de abril.

Espert, J.L. (1996). Política fiscal durante la convertibilidad: 1991-1995, Consultora Espert & Asociados, Mimeo.

Fanelli, J. (2002). "Crecimiento, inestabilidad y crisis de la convertibilidad en Argentina," *Revista de la CEPAL*, Vol. 77, No., pp. 25-45.

Feldstein, M. (2002). "Argentina's fall," *Foreign Affairs*, Vol. 81, No. 2, pp. 8-14.

Flood, R. & Garber, P. (1984). 'Collapsing exchange rate regimes: Some linear examples," *Journal of International Economics*, Vol. 17, No. 1-2, pp. 1-13.

FUCAES (2002). Las inversiones españolas en la Argentina (Buenos Aires, Cámara Española de Comercio de la República Argentina).

Guido, P. & Lazzari, C. (2002). "Desempleo encubierto en las provincias," *Política Pública*, 6, pp. 1-10.

Hall, P., & Soskice, D. (2001). *Varieties of capitalism: The institutional foundations of comparative advantage*, Oxford: Oxford University Press.

Huber, E., Rueschemeyer, D., & Stephens, J. (1993). "The impact of economic development on democracy," *Journal of Economic Perspectives*, Vol. 7, No. 3, pp. 71-86.

INDEC (2002). Informes Estadísticos (Buenos Aires, Instituto Nacional de Estadísticas y Censos de Argentina).

J.P. Morgan (2003). Indicadores de países emergentes (J.P. Morgan).

Kaufmann, D., Kraay, A., & Mastruzzi, M. (2003). Governance matters III: Governance indicators for 1996-2002, Policy Research working paper No. 3106.

Kritz, E. (2002). Poverty and the labour market in the Argentine crisis 1998-2002, World Bank Poverty Update Background No. 4.

Krueger, A. (2002). Crisis prevention and resolution: Lessons from Argentina, speech to NBER conference on "The Argentina Crisis," Cambridge, MA, (July 17), http://www.imf.org/external/np/speeches/2002/071702.htm

Krugman, P. (1979). "A model of balance of payments crises," *Journal of Money, Credit, and Banking*, Vol. 11, No. 3, pp. 311-325.

Krugman, P. (1999). Balance sheets, the transfer problem and financial crisis, Mimeo, http://web.mit.edu/krugman/www/FLOOD.pdf

Latinobarómetro (2002). Informe de opinión 2002 (Latinobarómetro).

Levine, R. (1999). "Law, finance, and economic growth," *Journal of Economic Intermediation*, Vol. 8, No., pp. 8-35.

Loser, C., & Guerguil, M. (1999). "Trade and trade reform in Latin America and the Caribbean in the 1990s," *Journal of Applied Economics*, Vol. 2, No. 1, pp. 61-96.
Mankiw, N., Romer, D., & Weil, D. (1992). "A contribution to the empirics of economic growth," *Quarterly Journal of Economics*, Vol. 107, No. 2, pp. 407-437.
Márquez, G., & Pages, C. (1998). Ties that bind: Employment protection and labor market outcomes in Latin America, conference "What is the employment problem in Latin America and how to deal with it?", Annual meeting of governors of the Inter-American Development Bank and the Inter-American Investment Corporation (Cartagena de Indias, Colombia).
Mauro, P. (1995). "Corruption and growth," *The Quarterly Journal of Economics*, Vol. 3, No., pp. 681-712.
Melconian, C., & Santangelo, R. (2003). *Recuperar la ilusión,* Buenos Aires: Editorial Atlántida.
Ministerio de Economía de la República Argentina (2003). Informes Económicos 1992-2002 (Buenos Aires, Ministerio de Economía de la República Argentina).
Montenegro, M. (2002). Fuga de capitales en Argentina y globalización, Mimeo, http://www.globalizacion.org/argentina/ArgentinaFugaCapitales.htm
Murphy, K., Shleifer, A., & Vishny, R. (1993). "Why is rent-seeking so costly to growth?", *American Economic Review*, Vol. 83, No. 2, pp. 409-414.
Mussa, M. (2002). *Argentina and the Fund: From triumph to tragedy*, Washington: Institute for International Economics.
N'Diaye, S. (2001). "The Role of Institutional Reforms," *Finance & Development*, Vol. 38, No. 4, pp. 18-21.
Neely, M. (1999). "Paper tigers? How the Asian Economies lost their bite," *The Regional Economist*, January, pp. 4-9.
North D. (1991). "Institutions," *Journal of Economic Perspectives*, Vol. 5, No., pp. 97-112.
North, D. (1981). *Structure and change in economic history.* New York: Norton.
North, D. (1993). The New Institutional Economics and Development, Mimeo Department of Economics, Washington University, St. Louis, http://econwpa.wustl.edu:8089/eps/eh/papers/9309/9309001.pdf
North, D. (1994b) "*Institutions matter*," Department of Economics, Washington University, St Louis. (Mimeo).
North, D. (1995). "Five proposition about institutional change," in J. Knight and I. Sened (Eds.), *Exploring Social Institutions* (pp.), Michigan: University of Michigan Press.
Obsteld, M. (1994) The logic of currency crises, Cahiers Economiques et Monetaires, 43, pp. 189-213.
OECD (2000). *Policies towards full employment*, Paris: OECD.
Paiva Abreu, M. (2002). "Basis for future competitiveness in Latin America and the Caribbean: Trade agreements and FDI attraction," in: J. Vial and P. Cornelius (Eds.), *The Latin American Competitiveness Report* (pp.), Oxford Economic Press.
Perry, G., & Serven, L. (2002). "La anatomía de una crisis múltiple: ¿qué tenía Argentina de especial y qué podemos aprender de ella?", *Desarrollo Económico*, Vol. 42, No. 167, pp. 323-375.
Phelps, E., & Zoega, G. (2001). "Structural booms: Productivity expectations and asset valuations," *Economic Policy*, (CEPR), Vol. 32, No., pp. 85-126.

Poirer, R. (1997). *Political risk analysis and tourism*, Pergamon: Elsevier Science.
Pontoni, A. (2002). El endeudamiento del sector público argentino, Mimeo, http: clubmacro.org.ar/infodeuda.htm
Roca, E. (2001). "La seguridad social en un contexto de precariedad laboral," Jornadas sobre *Precariedad Laboral, Vulnerabilidad Social, y Seguridad Socioeconómica*, Buenos Aires, Argentina.
Rodríguez, C. (1991). "The macroeconomic effects of public sector deficit: The case of Argentina," Universidad del CEMA, Documento de trabajo No. 76.
Rummel, R. & Heenan, D. (1978). "How multinationals analyze political risks," *Harvard Business Review*, Vol. 56, No. 1, pp. 67-76.
Sachs, J., & Warner, A. (1997). "Fundamental sources of long run growth," *American Economic Review*, Vol. 87, No. 2, pp. 184-188.
Saiegh, S., & Tommasi, M. (1999). "Why is Argentina's fiscal federalism so inefficient? Entering the labyrinth," *Journal of Applied Economics*, Vol. 2, No. 1, pp. 169-209.
Sanguinetti, J., & Tomassi, M. (2000). "La conducta fiscal de los gobiernos municipales en Argentina: Los decisivees económicos, institucionales, and políticos," Universidad de San Andrés, Argentina. (Mimeo).
Schuler, K. (2002). "Fixing Argentina," *Policy Analysis*, Vol., No. 445, pp. 1-37.
Shuyler, K. & Gabjem S., (2002). Argentina, dinero and moralidad, Revista Siete, 1st April 2002.
Spiller, P., & Tommasi, M. (2000). Los decisivees institucionales del desarrollo argentino: una aproximación desde la nueva economía institucional, Universidad Torcuato Di Tella, Documento de trabajo no. 33.
Sturzenegger, A. (1996). Contexto Macroeconómico in CAFJP (Eds.), *Jubilación Privada, Certidumbre Social, and Crecimiento Económico*, (Buenos Aires, Argentina).
The Economist (2002). Explaining Argentina's Economic Collapse, 28 February.
Transparency International (2003). Corruption Perception Indexes (1999-2002) (Transparency International).
United Nations (2002). Aportes para el Desarrollo Humano de la Argentina (Buenos Aires, United Natios).
Vernon, R. (1971). *Sovereignty at bay: The multinational spread of US enterprises*, New York: Basic Books.
Watkins, T. (2003). Argentine political economic history, Economics Department working paper, San José State University, http: www2.sjsu.edu/faculty/watkins/argent1.htm
WEF (2003). The Global Competitiveness Report 2002-2003, WORLD ECONOMIC FORUM, (Oxford University Press, New York).
Williamson, O. (1985). *The economic institutions of capitalism: Firms, markets, relational contracting*, New York: Free Press.
World Labour Report (1997-1998). Industrial Relations: Democracy and Social Stability, in: Organización Internacional del Trabajo (Eds.). World Labour Report.

APPENDIX

In this appendix, the different cross regressions presented in this paper are explained. Each one of them has as its dependent variable the average GDP growth rate during the period of 1997-2001. The independent variables are classified into two groups: on one side, economic variables; on the other, institutional variables.

Within these economic variables we include the investment rate as a percentage of GDP, and human capital is measured as the average number of years of schooling for the economically active population. The first variable controls the convergence effect that predicts the neoclassical model: the greater the level of investment as a percentage of GDP, *ceteris paribus,* the lower the growth rate of the product. The problem with this approach is that such a relationship does not apply to samples containing both developed and developing countries. In another words, and following Mankiw, Romer and Weil (1992), the neoclassical model predicts conditional convergence: each country converges to its own stationary state, which primarily depends on its level of human capital. As a consequence, the cross regressions include the measurement of human capital as a basic specification.

TABLE A1. Regression on the Average GDP Growth Rate (1997-2001)*

	1	**2**	**3**	**4**	**5**	**6**
Constant	3.045 (19.106)	3.276 (23.428)	3.109 (20.290)	3.286 (19.343)	3.211 (21.388)	3.319 (22.952)
Investment (% of GDP)	–0.012 (–2.241)	–0.013 (–2.441)	–0.012 (–2.302)	–0.013 (–2.220)	–0.013 (–2.283)	–0.017 (–2.807)
Human Capital	0.843 (5.523)	1.017 (7.641)	0.949 (7.025)	1.173 (8.273)	1.015 (7.326)	1.136 (9.107)
Index Institutional	0.128 (3.506)					
Judicial Independence		0.065 (2.758)				
Property Rights			0.098 (3.301)			
Gov't Transparency				0.040 (0.997)		
Absence of Rent Seeking					0.097 (2.588)	
Competency of Pub. Empl.						0.088 (1.832)
R square (adjusted)	0.827	0.810	0.822	0.780	0.806	0.792

*Between parentheses the value of statistic t is included.

APPENDIX (continued)

With respect to the institutional variables, the World Economic Forum defines these in the following manner:

- **Institutional Index:** an index composed of 37 different sub indexes, grouped into two large categories. The first is related to corruption, while the second is concerned with laws and contracts.
- **Judicial Independence:** measures the degree of independence of the judicial power with respect to the government.
- **Property Rights:** measures the degree of protection offered by the judicial system to financial assets and to the wealth of economic agents.
- **Government Transparency:** measures the quantity and quality of government information related to (1) its public policy decisions; (2) the changes that can take place as a result of these policies.
- **Absence of Favor Seeking:** measures the extent to which government decisions involving policies and contracts are independent of the individual and companies that are affected by the results of such policies.
- **Competency of public employees:** measures the efficiency level of public employees in comparison with what is observed in private sector employees. We assume that it is a proxy of *clientelismo*.

The sample that we have utilized in this work was obtained from the data contributed by the World Economic Forum (WEF) in its 2003 survey, consisting of 80 countries ranked according to the classifications reached in three different areas: Economic, Technical, and Institutional. Due to the inexistence of certain dates for some countries, we ended up utilizing a smaller sample consisting of 45 countries.

The software used for both the graphical analysis as well as the statistics was the program SPSS version 12.0