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### IMF Press Release: IMF Approves Extension, for Fourth Year, of EFF Credit to Argentina

International Monetary Fund (IMF)

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**PRESS RELEASE** NO. 95/18

## Press Release: IMF Approves Extension, for Fourth Year, of EFF Credit to Argentina

April 6, 1995

The International Monetary Fund (IMF) today approved a request by the Government of Argentina to extend to a fourth year the extended Fund facility (EFF) credit for Argentina, and to increase the amount by SDR 1,537.1 million (about \$2,407 million), to a total of SDR 4,020.25 million (about \$6,295 million), to support the Government's economic policies over the next 12 months. Together with the undrawn amount of SDR 278.05 million (about \$435 million) under the third year of the EFF credit, a total of SDR 1,046.6 million (about \$1,639 million) is immediately available to Argentina, and the rest, SDR 768.55 million (about \$1,203 million), will be disbursed in three equal, quarterly installments. The IMF approved the three-year EFF of SDR 2,483.15 million (about \$3,888 million) on March 31, 1992 in support of Argentina's medium-term economic and financial program (see Press Release No. 92/27).

### Background

Over the past four years under the Convertibility Plan adopted in March 1991, Argentina has substantially consolidated its stabilization efforts and made considerable progress in the area of structural reform. Under this plan, Argentina pegged the peso to the U.S. dollar, allowed the U.S. dollar to be used for most transactions, eliminated indexation, and prohibited the Central Bank from providing domestic credit beyond certain limits. The fiscal accounts were kept in approximate balance, and extensive structural reforms were implemented in the fiscal, monetary and trade areas, including opening up the economy to competition, deregulation and privatization. Real economic growth averaged more than 7 percent a year between 1991 and 1994, boosted by large capital inflows, and inflation dropped from very high levels to less than 4 percent in 1994. There was, however, an increase in the external current account deficit, which was mainly financed by private capital inflows.

The program for 1994, which was supported by the EFF, aimed at a further reduction in inflation and a lowering of the external current account deficit on the basis of a strengthening of fiscal policy. In the event, however, although economic growth was more robust than programmed, fiscal policy was weaker than expected as a result of a faster-than-programmed reduction in employer social security contributions, as well as expenditure overruns, mainly in pensions. The

authorities responded to the deteriorating fiscal situation by adopting a series of remedial measures in the second half of 1994.

Argentina experienced large capital outflows in early 1995 in the wake of the Mexican crisis. These were reflected in a substantial decline in both the Central Bank's international reserves and its monetary liabilities between end-December 1994 and end-March 1995, a tightening of bank liquidity, a surge in interest rates, and a sharp fall in asset prices. Parts of the banking system experienced difficulties, and bank deposits declined during this period. The authorities decided in early March to take strong action to reinforce the public finances and to provide resources for restructuring the weakened financial system by creating two Trust Funds to provide lender- of-last-resort facilities. The authorities also decided to seek large-scale international financial support, including an extension of the EFF, to rebuild international reserves and to finance the Trust Funds.

### The 1995 Program

The 1995 program, supported by the EFF extension and augmentation and including the measures already taken, aims to restore liquidity in the financial sector, raise domestic savings, and re-establish confidence in the Government's ability to defend the fixed exchange rate that is at the heart of the Convertibility Plan. The program assumes a slowdown to 2-3 percent in the rate of economic growth, and inflation of 3 1/2 percent. In the face of reduced private capital flows, the current account deficit is projected to narrow to 2 percent of GDP.

In the light of Argentina's limited access to foreign capital, the authorities have taken decisive action to generate an overall surplus in the nonfinancial public sector. These measures, which amount to some 2 3/4 percentage points of GDP on a full-year basis, mainly consist of a temporary 3- percentage point increase in the value-added tax rate to 21 percent; varying increases in import duties; a broadening of the tax base; a reform of the wealth tax; a unification of employer social security contributions rates across sectors; and improvements in tax administration. Expenditure cuts, mainly on current outlays, have also been made. The monetary program for 1995 foresees a reversal of the decline in bank deposits during the remainder of the year.

### Structural Policies

The 1995 program envisages further steps in the areas of privatization, labor market reform, and bankruptcy law that would build on the reforms undertaken over the past four years. In the area of privatization, the authorities intend to sell outright, or sell operating concessions for, a number of hydroelectric dams, nuclear power installations, and petrochemical plants, which is estimated to raise \$1 billion, as well as shares in other enterprises valued at some \$1.4 billion. Legislation has recently been passed with a view to enhancing labor market flexibility, which is central to addressing the problem of unemployment and improving Argentina's international competitiveness.

### The Challenge Ahead

The Challenge Ahead The decisive measures taken by the authorities, shortly ahead of national elections, demonstrate their full commitment to the basic objective of maintaining the Convertibility Plan that has served the country well. These measures should be adequate to re-establish financial stability, restore confidence, and ensure the program's success.

Argentina joined the IMF on September 20, 1956, and its quota<sup>1 (#1)</sup> is SDR 1,537.1 million (about \$2,407 million). Argentina's outstanding use of IMF credit currently totals SDR 2,821 million (about \$4,417 million).

## Argentina: Selected Economic Indicators

	1991	1992	1993	1994*	1995**
	<i>(percent change)</i>				
Real economic growth	8.9	8.7	6.0	7.1	2.0–3.0

Consumer prices (end of period)	84.0	17.5	7.4	3.9	3.6
	<i>(percent of GDP)</i>				
External current account balance (deficit –)	–0.2	–2.8	–2.9	–3.7	–2.0
Overall balance of the nonfinancial public sector, including privatization (deficit –)	–0.8	0.7	2.1	0.1	1.5
Gross official reserves (months of imports)	8.6	8.6	9.7	9.3	9.1

Sources: Argentine authorities; and IMF staff estimates.

\*Preliminary.

\*\*Program.

\*\*\*On the basis of revised official data published on April 4, 1995.

1. A member's quota in the IMF determines, in particular, the amount of its subscription, its voting weight, its access to IMF financing, and its share in the allocation of SDRs.

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