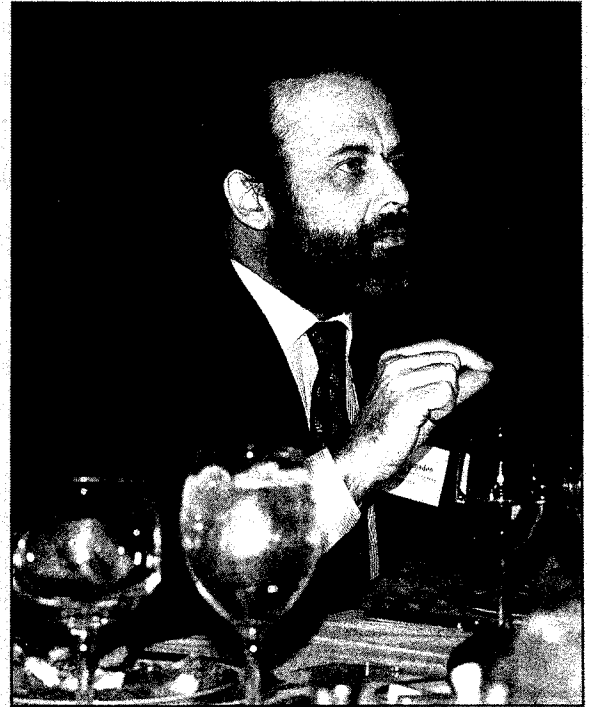


Carnegie Council Privatization Project

The Politics of Privatization in Argentina



No. 25



The Honorable
Eduardo Amadeo

Member, House of Representatives of
Argentina, and former President and CEO,
Banco de la Provincia de Buenos Aires

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The Honorable Eduardo Amadeo

I would like to describe four lessons from the privatization experience in Argentina. The first one is that when you try to defeat inflation or try to change the economic culture of a society, there's no silver bullet. In Argentina we have had long discussions about how to do it. Some people would come and tell us "if you apply this economic program or that economic program, it's proven, it has been written about, do it, and you will succeed in a couple of months or in a year." Our experience, ladies and gentlemen, is be patient, there is no silver bullet, don't believe in magic, it's a long, long process. Consultants who say that there is any one method are just trying to sell their skills. Our experience is that it's a very long process; inflation and the culture of state ownership are so deeply rooted in the behavior of the whole society that it takes years to change

the behavior, because it is not only a psychological problem, it's an economic problem. There are many people whose main way of life is related basically to that of the state and they are used to just collecting rent instead of making money with more productivity.

The second experience that we have learned from privatization in Argentina is that there's no perfect privatization at the beginning. At the beginning, many people were telling us that the process was not perfect, the company could be privatized in a different way, we were doing it wrong; we should stop and study it. In our case—particularly in our case, when we were in the middle of a terrible hyperinflation, with very serious problems and we had to manage the economy and manage the society—we couldn't stop. I do realize now that some of the privatizations were far from perfect; we're now having troubles with one of them. But you always have time to correct later on. The key point is that the process of privatization provides you

the most needed tool in order to keep both the economy and the politics working: it provides you confidence and trust from the people. Otherwise, if you don't have that tool, if you don't have that input, you cannot run the economy and you cannot run the country. So, if you wait until you have the perfect model, you're lost. There will always be time to correct the errors, but don't give up.

The third experience is that the most important cultural change generated by privatization is accountability. Again, when we consider that what we are discussing is not only an economic problem, but a major social and political problem, we realize that when citizens become accustomed

to social and political accountability, the process cannot be stopped. When people realize that they can exercise their most basic rights—such as calling and getting answered; getting a

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service; blaming a politician; or blaming someone who does not provide service, because now they are the real owners of the state apparatus—the process cannot be stopped, and this is a major outcome of privatization. For me, in fact, privatization equals accountability. The key political and social factor involved in privatization is accountability, and wise politicians should foster this process. You cannot stop it. Let me give you an example. In Argentina, because people want to know what's going on, we have been able to do something that has never been done before, which is evaluating our educational system. We were absolutely unable to do so before because the unions wouldn't allow it. It was a contradiction in itself. But now, the president has decided that the system is going to be evaluated and we all have the right to know what's going on in education. What's happening with the school down the street? What's happening with the school where my children are going? We have already produced the first evaluation, and this has pro-

duced a sort of revolution. In fact, this is a way of privatizing the educational system, even though we are not going to change it. Education in Argentina is still going to be public for time immemorial, but now the idea of accountability has reached the educational system because the citizens are demanding it.

My fourth reflection about why privatization has been so important and so useful in my country is that there is a direct relationship between privatization and microeconomic equilibrium with improvement in the welfare conditions of low and middle class sectors. This is a discussion that's taking place now in Latin America and in some other places of the world. Has privatization been good or bad for the poor people? Has it worked or not? (Please refer to the chart on page 4.) It's very clear that what has happened with the macroeconomic improvement in the situation in Argentina and the situation of the poorest people is that stabilization has clearly improved the relative situation of the poor. Privatization has assured the provision of basic services to all of the population, and this is a key factor in improving the welfare situation of the poor people so they can have water, electricity, gas, etc. In my country, the difference between someone living in downtown Buenos Aires, in one of the most affluent neighborhoods of the capital city, and another person living 20 kilometers from downtown, is not only that they may have different jobs, but when the utility companies were in the hands of the state, people had different services, meaning that in the poorer areas they had no water, no sewage, no gas, and no electric-

ity, and that was one of the key welfare differences. So we found that there is a direct relationship between privatization and welfare. Over the next five years, thirteen million people will have full coverage of water and sewage; something which never happened before in seventy years of having a state-owned water company. So this is a major factor and also it can be used as a major political tool because you can offer people the right of access to basic services. Let me now describe what's happening in Argentina today.

"In my country, the difference between someone living in downtown Buenos Aires, in one of the most affluent neighborhoods in the capital city, and another person living 20 kilometers from downtown, is not only that they may have different jobs, but when the utility companies were in the hands of the state, people had different services, meaning that in the poorer areas they had no water, no sewage, no gas, and no electricity."

Argentina today is an example that the application of the aforementioned policies can be not only a source of economic success but also of political success. Argentina's growth had been, literally, zero between 1977 and 1990. In 1991 our growth was 9 percent; in 1992 it was 7 percent; last year it was 6 percent; and this year we again expect it to be between 5 percent and 6 percent. So, something has really changed in Argentina. Inflation was 5 percent, on average, through last year, and for the last two months it has been zero. The situation of the poor people has improved enormously. Talleyrand said that in politics it's more important to be successful than to have reason. It's a bit cynical, but in my country it seems that we have had both reason and success with these sorts of policies.

What's the next step? We are now facing the need to reform our social and welfare system. We have concentrated all of our efforts in reforming the economy and the functioning of the political system, and now we have to reform the administration of social programs. We have the resources; never before has Argentina spent more money on social affairs than it is now. This year's budget is the largest social budget in Argentinean history, and if to that you add the monies that we have been paying to pensioners—we used the entire proceedings of the sale of the petroleum company YPF to pay the debt of pensioners, which was over three billion dollars—it's a very large amount of money. But our management of those monies is, frankly speaking, very poor, because we do not have the proper technology and, as I said before, if privatization equals accountability, then we're



Dr. Amadeo speaks with Brian O'Neill, senior vice president, Chase Manhattan Bank, as Meredith Brown, partner, Debevoise & Plimpton, looks on.

The Decrease of Poverty in Argentina

Period	Percent under the line of:		
	Indigence	Poverty	
	Households	Households	People
May 1988	6.4	22.6	29.9
October 1988	7.8	24.2	32.4
May 1989	6.3	19.7	25.9
October 1989	12.7	38.3	47.4
May 1990	9.1	33.7	42.6
October 1990	5.0	25.3	33.8
May 1991	3.8	21.8	28.8
October 1991	2.4	16.3	21.6
May 1992	2.4	15.1	19.3
October 1992	2.6	13.7	17.8
May 1993	2.9	13.6	17.8

Percent of households and people under the line of poverty and indigence in greater Buenos Aires. May 1988–May 1993.

Notes:

1.) The line of indigence is the cost of a typical household food basket. The poverty line is approximately double the indigence line.

2.) The calculation is based on incomes reported in households surveyed by INDEC (the national census bureau). These incomes are generally underestimated by 20 percent, therefore the percentages in the table are overestimated by 20 percent and must be considered as a trend over time.

Source: Executive Committee for the Study of Poverty in Argentina and INDEC (census bureau).

not being accountable to the people in this respect, because it's still too bureaucratic. All social policies are being run by a huge structure based on bureaucrats. What we have to do is make social policies more efficient and more accountable and by this we expect to make them closer to the people.

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We know this is a problem everywhere; I remember what President Clinton said a couple of weeks ago in his State of the Union Address when he proposed going back to the fundamentals of the American society, going back to the community, going back to the family, going back to Tocqueville, in a way, to correct social problems. So successful social policy is a problem everywhere. Our next challenge in Argentina, therefore, is to make the administration of social welfare more accountable and more efficient. For those of you who work with countries that are involved in this process of privatization, my suggestion would be try to make the administration of social services more efficient now. In some Eastern European countries lots of effort is being devoted to the privatization of state-owned enterprises, but, if we in Argentina were starting over again, we would probably put much more emphasis on making more efficient

the administration of social affairs at the very beginning because it would ease the political process.

Let me make a final comment. I have read with certain consternation during the last weeks some comments coming from Latin American politicians saying that people have had enough with conservative economic policies. The newly elected president of Costa Rica, Mr. Figueres, said last week that enough is enough, and he blamed adjustment policies for the poverty, economic problems, and social problems in his country. I by no means want to interfere in Costa Rican affairs, but you will see that sort of declaration in a number

of places—people blaming adjustment policies for the social problems in their countries—and frankly speaking, this is completely wrong. If you are going to blame anyone or anything for what's happening in terms of poverty in Latin America, economic adjustment is not the problem; it is the situations that were inherited. It's clear, by any professional standard, that the worst enemy of poor people is inflation, and bad adjustments have been the main reason for poverty on our continent in the last ten to twenty years. I think the answer to poverty in our countries is, first, better economic policies, then more resources for social welfare and better social policy; not the other way around. We cannot go back to previous economic policies because that would be a disaster; we would lose all that we have worked so hard to accomplish. ■

Questions and Answers

Q What progress have you made on the new pension system in Argentina?

A Let me first begin with some psychological aspects of it because people are dealing now with this issue in East European countries. Whenever you touch the future of the people, they get very scared about what's going on, so that's one of the main reasons why you have to be extremely careful in how you explain it to the people. That's one of the main reasons why it has been so difficult for us and it took so long to go ahead with pension reform. For us this is a major component of not only the privatization process, but of the future of our economic program. The first reason this is so deals with the way the monies of the pension-

ers are going to be managed. The experience of Argentina is that whenever there is any money saved anywhere in the state apparatus, you end up losing it. For example, there could be an earthquake and you need a couple of billion dollars. Where are those billions of dollars? There, in the pension plan, so you put your hand in the till. There's really no chance of having savings inside the state and not losing them for any number of reasons. So our experience is that the future of the pensioners is in danger unless you are able to move those savings into a system that cannot touch them. Second, in the long run we expect a substantial increase in savings and the overall savings rate. But more than the increase in the overall savings rate, what we expect in the near future is

an improvement in the quality of investments made with that money, and that's very important, because you introduce a huge amount of money being managed with long-term objectives and professionally managed savings. The savings rate could increase a couple of points, but what's going to improve enormously is the degree of professionalism with which those funds are going to be administered. What we finally got through Congress was not exactly the same thing that we introduced, because we did not have a Party majority at that time, but still, we are convinced that the program will work in the long run.

One point for those of you who are dealing with this in East Europe: I have some blame to place with my former colleagues—bankers—which has to do with the fears of the people. One of the things that was difficult to manage in political terms and in terms of communications was that banks were putting too much emphasis on publicity, with commercials saying that this was going to be extremely useful in improving the situation of the financial markets. Pensioners therefore said, "But we don't care what's happening with the *financial markets*. I'm 68 years old, I



(Left to right) Dr. Amadeo; Bruce Nussbaum, editorial page editor, *Business Week*; Martín Blumenthal, financial manager, *Techint, Inc.*; and Gonzalo de Las Heras, executive vice president, *Banco Santander*.

want to keep my pension, what I care is what's going to happen with *my funds*." We had long discussions with bankers about putting too much emphasis on financial markets versus the future of the people and we had some trouble discussing this with them. I have to mention it because I was a key actor in that discussion, and if I would give a recommendation to someone who is going to deal with it, it's to make sure that the old people—or young people, those who are going to be

pensioners in the future—feel comfortable with their future.

Q Has capital flight been brought to an end and is there a positive capital flow into Argentina now?

A Absolutely. Capital flight has been reversed. In fact, every country that defeated deep inflation immediately ran into huge trade deficits, and at the same time no country emerged from a hyperinflationary situation without foreign aid. In the 1930s and 1940s that was in the form of help from America and European countries. The only way we can defeat inflation now is with private capital, and private capital is entering Ar-



Attending a private dinner for Dr. Amadeo are (left to right) Alan Stoga, *Kissinger Associates*; Ingrid O'Neill; and Brian O'Neill, *Chase Manhattan Bank*.

gentina for a number of reasons. We have a booming emerging market; operations on the stock exchange have multiplied many times. For me the key indicator is how low the risk of investing in Argentina is now. We are now getting money from the international market at an absolutely international rate and for a very long period. So, capital flight does not exist any longer and it's exactly the other way around.

Q I wonder if you could give us your views on handling potentially troublesome labor unions and how to keep opposition to privatization from translating into opposition to foreign investment?

A It has to do with what I said before about the idea of accountability and how citizens feel with a new situation. President Menem has been betting all the time and winning every single bet. He made the reforms because he felt that what

he was doing was providing him with a new political base each time. People were supporting him. In fact, President Menem and President Peron have been the only two presidents who have won their third legislative elections. It's a tradition in Argentina that you win the first two and you lose the third one, and in 150 years only those two presidents have won three consecutive legislative elections.

What happened in Edesur the other day is no longer a political problem. Ten years ago a discussion of that sort could easily have become a major political issue, but now it's just a problem of some people in a certain company. The overall majority of the country does not follow their position and that's because the privatization process has been so successful. Again, that is why my recommendation is to keep on trying, don't stop, use privatization as a political tool. When you start the process and you keep on doing it, it's a major political tool that will allow you to go ahead with the next steps. Our labor unions are now broken. They are divided and because of things such as what happened in Edesur, I don't envisage any major problem with foreign investment in Argentina, not only in the near future, but in the long-term future as well.

Q When your government looks at the Indian uprising in Chiapas, Mexico, do you draw any lessons; do you see Chiapas as any kind of a forewarning?

A I have two comments on that. First, the problems posed by the Indians in Chiapas almost seem a discussion from a hundred years ago. They are asking for land and to have their most basic rights respected. Let me refer to the experience that we had last month in Argentina in a province called Santiago del Estero, which some people have cited as an example that our economic model failed and that we are having serious political troubles. For those of you who are familiar with Argentina, you probably know that Santiago del Estero is not the poorest province in the country. We have some provinces in Argentina that have almost no hope; they consist of little more than just stones and the people can hardly find any productive activity. The residents live mostly from money received from

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the central government. Santiago del Estero does not fall into that category; they have some good productive sectors, such as cotton and cattle raising. However, we had a very serious riot there and you know what happened? People started by burning the government house. Then they burned the Congress. Then they burned the houses of all elected political officers from both parties—the governor, the vice governor, the congressmen, the mayors, and then they also tried to burn the house of the bishop. Incidentally, there are 56 priests in Santiago del Estero, and they were all getting salaries from the government, so in the minds of the people priests were sort of like politicians; they were all in the same bag. People were just fed up with the corrupt political class of Santiago del Estero. For example, an average legislator in Santiago del Estero receives three times the salary I get as a national legislator. Santiago del Estero, therefore, is not a case of problems with economic adjustments, it's a case of bad social management on the part of the politicians. The question is why did people riot in Santiago del Estero and why has that not happened in any other province? I think it is because the economic adjustment was much more difficult because there was bad management from the political classes in Santiago del Estero, and I think this is the key challenge for the political class in Latin America. The economies are doing very well, the macroeconomics of Latin America in the 1990s are doing far better than in the 1980s. The points are, one, are we going to be able to reform our welfare systems in order to make them more efficient and have better use of the available resources, and, two, are we going to have incorrupt exemplars, capable of feeling what the people need, being close to the people, representing the people the way they want to be represented, and being accountable to the people?

I think that this is the new demand of the 1990s of the political class in Latin America. So I wouldn't think that the better functioning of the economies of Latin America have been responsible for what's happening in Chiapas. I think people are demanding other things. People are demanding better political classes and better management of social welfare.

Q Could you comment a little bit on the repercussions for Brazil and MERCOSUR of Argentina's success, and the contrasting chain of events in Brazil?

A We in Argentina feel very concerned with what is happening in Brazil, and I say this with due re-

spect and due care for our brothers and for their sovereignty. We had important expectations on the association with Brazil through MERCOSUR, but Brazil is currently unable to adjust its economy and its politics. We are still going to bet on MERCOSUR; we think it's our key strategic possibility for joint development in a world where areas are more important than countries. We have to wait. We have to see what happens with the next election, whether they can overcome this difficult situation, but we want to go ahead with MERCOSUR, because it's a strategic bet for their future and for ours.

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