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Averting Disaster in Argentina: The Case for Economic Freedom

James M. Roberts

The irresponsible economic policies pursued by the government of Argentina in the wake of its sovereign debt default in 2001, and its debt restructuring offer in 2005, provide a vivid case study of the root causes of Argentina's steadily declining scores in the annual *Index of Economic Freedom* published by The Heritage Foundation and *The Wall Street Journal*.

In late December of 2001, Argentina declared a default on its massive sovereign debt—the largest such default in world history. In 2005, the country presented bondholders with its final offer, a "take-it-or-leave-it" debt-swap proposal for bonds with an original face value of $81 billion. The offer required bondholders to agree to a 70 percent reduction, the largest sovereign debt "haircut" on record. Holders of bonds amounting to about 76 percent of the national debt—many of them state-owned banks and other entities of the Argentine government with little say in the decision—agreed to the swap. The remaining 24 percent—"holdout" bondholders—who rejected the offer include more than half of Argentina's foreign creditors.

The country's left-wing government, led first by Peronist Party leader Néstor Kirchner (president from 2003 to 2007) and now by his wife, President Cristina Fernández de Kirchner, has used revenues from commodities exports to finance the same sort of populist policies that have kept General Juan Peron and his political progeny in power in Argentina more or less continuously since the 1940s with a simple but economically destructive formula: wasteful welfare state handouts, a swollen bureaucracy to redistribute wealth, and powerful closed-shop trade unions protected from foreign competition, all generously lubricated with corruption.

Although Argentina had made an impressive economic recovery after the disastrous 2001–2002 crisis, the Kirchners thumbed their noses at conventional economic wisdom, imposing price controls and a 21st-century version of Juan Peron's "Import Substitution" industrialization policy, as well as essentially lying about the true levels of inflation that their polices have created. Not only does an artificially low inflation figure overstate real gross domestic product (GDP) growth, it also permits the government to make lower interest payments to bondholders based on a consumer price index (CPI)-linked formula.

The Kirchners have also toed the party line of their only major benefactor—hard-left socialist president of Venezuela Hugo Chavez—and so they are rejecting advice on market-friendly economic reforms from the International Monetary Fund (IMF). In a cynical move in 2005, the government of Argentina repaid more than $9 billion in low-interest loans from the IMF ahead of schedule, greatly helped by revenue from high-interest bonds the Argentine government sold to Chavez (inflicting the resulting higher interest payments on Argentina's beleaguered taxpayers).

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With Argentina's loans paid off, the IMF has less leverage over the Kirchner government. Chavez is using Venezuela's oil wealth as a weapon to undermine the IMF, which he accuses of being a tool of the Western imperialist powers (led by the United States).

At long last, the Kirchners' luck appears to be running out. The economy is slowing and the Kirchners are finding it increasingly difficult to convince people in Argentina and around the world that the inflation figures reported by their government statistical office (INDEC) are correct. Although INDEC maintains that inflation in Argentina is running at an annual rate of 9 percent, most knowledgeable observers place the real figure at 30 percent—and growing.

Meanwhile, facing declining government revenues due to the economic slowdown they created, and the need to continue government handouts to their urban-poor political base, the Kirchners attempted to raise the already heavy taxes on exports of agricultural commodities, especially soybeans, in March 2008. That set off an unprecedented rebellion by Argentina's farmers that has hurt the country's image around the world and shredded Cristina's domestic approval rating. This has fueled concern that if the Kirchners do not address the debt issue (with the attendant rising inflation and low private-sector investment levels) and Argentina's economy slows, Argentina could be *en route* to another crisis and default as experienced in 2001.

Rule of law, secure property rights, transparent government, and vigilance against state corruption are among the most important measurements used to calculate the annual rankings of 179 countries in the *Index of Economic Freedom*. Argentina's score plummeted from 70.9 in 1998 (ranking 19th-freest economy in the world of 156 countries scored) to 55.1 by 2008 (ranking 108th of 162 countries). The Kirchners' Peronist government has callously disregarded these freedoms in a classic case of an assault by a leftist-populist regime on the property rights of both Argentine citizens as well as foreign investors and bondholders.

The Kirchners' aggressive and antagonistic attitude toward the holdouts (refusing until only recently to even consider re-entering negotiations), as well as their collusion with Hugo Chavez in his campaign against the world financial system, poses a grave threat to global prosperity and threatens to undermine established and time-tested international lending norms, ultimately to the detriment of all developing nations. Hundreds of U.S. companies operate in or export to Argentina, employing tens of thousands of people, whose futures have been jeopardized by the Argentine government's refusal to settle with the holdouts.

The country's investment climate has been damaged. This past August, Standard & Poor's cut Argentina's foreign-debt rating from B+ to B, which is five grades below investment grade and places Argentina into the same category as Belize and Burkina Faso, far behind neighbor and rival Brazil (which achieved investment grade in 2008). This lower rating will raise the cost of borrowing for Argentine businesses and make Argentina less competitive in the global economy.

The Kirchners must correct the deficiencies described in the *2008 Index of Economic Freedom*, for the good not only of their own citizens, but of all South America. The Argentinean government must also be honest about the true rate of inflation and cease efforts to manipulate the value of the peso. The government of Argentina has an obligation to its citizens to reach an agreement with all external creditors so that it can regain full access to world financial markets.

As a leader of the globalized economy and the international financial institutions that have ensured prosperity for billions of people over the past 50 years, the United States has a special responsibility to prevent abuse of that system by Argentina or other rogue nations.

The U.S. Administration should insist that the IMF, the Inter-American Development Bank, and the World Bank withhold any future lending to Argentina until Argentina adopts free-market and good-governance reforms addressed in the *Index of Economic Freedom*.

The U.S. Congress should hold hearings on the threat to both the U.S. economy and the world financial system if more sovereign debtors were to follow the bad example of Argentina and repudiate their debts. Congress should also investigate possible legislative remedies to prevent abuse of the legal system by sovereign debtors.

—James M. Roberts is Research Fellow for Economic Freedom and Growth in the Center for International Trade and Economics (CITE) at The Heritage Foundation.

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In late December of 2001, Argentina declared a default on its massive sovereign debt—the largest such default in world history.[1] In 2005, the country presented bondholders with its final offer, a "take-it-or-leave-it" debt-swap proposal for bonds with an original face value of $81 billion.[2] The offer required bondholders to agree to a 70 percent reduction, the largest sovereign debt "haircut" on record. Holders of bonds amounting to about 76 percent of the debt—many of them state-owned banks and other entities of the Argentine government with little say in the decision—agreed to the swap. The remaining 24 percent—"holdout" bondholders—who rejected the offer include more than half of Argentina's foreign creditors.

The country's current left-wing government, led first by Peronist Party leader Néstor Kirchner (president from 2003 to 2007) and now by his wife, President Cristina Fernández de Kirchner, has used revenues from commodities exports to finance the same sort of populist policies that have kept General Juan Peron and his political progeny in power in Argentina more or less continuously since the 1940s with a simple but economically destructive formula: wasteful welfare state handouts, a swollen bureau-

Talking Points

- The Kirchner government has pursued irresponsible economic policies since Argentina's 2001–2005 sovereign debt default and restructuring, as illustrated in Argentina's steadily declining scores in the annual *Index of Economic Freedom*.
- The Kirchners' stance on debt reflects their collusion with Hugo Chavez to undermine the global financial system, posing a grave threat to world prosperity.
- The Argentinean government should follow through on its announced intention to repay debts both to the Paris Club and to private bondholders and correct the deficiencies detailed in the *2008 Index of Economic Freedom*.
- The Bush Administration should make debt repayment a policy priority to strengthen U.S. relations with Latin America and improve financial freedom and investor confidence throughout the region.
- Congress should hold hearings on the threat to both the U.S. economy and the world financial system if more sovereign debtors were to follow Argentina's example and repudiate their debts.

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cracy to redistribute wealth, and powerful closed-shop trade unions protected from foreign competition; all generously lubricated with corruption.

Although Argentina had made an impressive economic recovery after the disastrous 2001–2002 crisis, the Kirchners pulled off several years of economic growth with smoke and mirrors. They thumbed their noses at conventional economic wisdom, imposing price controls and a 21st-century version of Juan Peron's "Import Substitution" industrialization policy, as well as essentially lying about the true levels of inflation that their polices have created. Not only does an artificially low inflation figure overstate real gross domestic product (GDP) growth, it also permits the government to make lower interest payments to bondholders based on a consumer price index (CPI)-linked formula.

The Kirchners have also toed the party line of their only major benefactor—hard-left socialist president of Venezuela Hugo Chavez—and so they are rejecting advice on market-friendly economic reforms from the International Monetary Fund (IMF). In a cynical move in 2005, the government of Argentina repaid more than $9 billion in low-interest loans from the IMF ahead of schedule, greatly helped by revenue from high-interest bonds the Argentine government sold to Chavez,[3] inflicting the resulting higher interest payments on Argentina's beleaguered taxpayers. With Argentina's loans paid off, the IMF has less leverage over the Kirchner government.

Chavez is using Venezuela's oil wealth as a weapon to undermine the IMF, which he accuses of being a tool of the Western imperialist powers (led by the United States). Chavez is pushing the creation of a South American competitor for the IMF—the "Bank of the South" (Banco de Sur)—which he hopes to dominate through Venezuelan oil wealth and use to advance his regional political ambitions.[4]

At long last, the Kirchners' luck appears to be running out. The economy is slowing and the Kirchners are finding it increasingly difficult to convince people in Argentina and around the world that the inflation figures reported by their government statistical office (INDEC) are correct. Although INDEC maintains that inflation in Argentina is running at an annual rate of 9 percent, most knowledgeable observers place the real figure at roughly 30 percent[5]—and growing.

Meanwhile, facing declining government revenues due to the economic slowdown they created, and the need to continue government handouts to their urban-poor political base, the Kirchners attempted to raise the already heavy taxes on exports of agricultural commodities, especially soybeans, in March 2008. That set off an unprecedented rebellion by Argentina's farmers that has hurt the country's image around the world and shredded Cristina's domestic approval rating. "Concerns are growing that as the nation's economy slows, if Kirchner doesn't deal with mounting debt, rising inflation, sagging investment, and limited resources to pay for subsidies, then Argentina may be on the way to an economic crisis and [another] debt default."[6]

Hundreds of U.S. companies operate in or export to Argentina, employing tens of thousands of people[7] whose futures have been jeopardized by the Argentine government's long-standing refusal to settle with the holdouts. The country's investment cli-

1. J. F. Hornbeck, "Argentina's Sovereign Debt Restructuring," Congressional Research Service *Report for Congress*, October 2004, at *http://fpc.state.gov/documents/organization/39301.pdf* (September 19, 2008).
2. Ashley Seager, "Argentina Says Debt Default Is Over," *The Guardian*, March 4, 2005, at *http://www.guardian.co.uk/business/2005/mar/04/argentina.internationalnews* (September 19, 2008).
3. Christopher Swann, "Hugo Chavez Exploits Oil Wealth to Push IMF Aside," *International Herald Tribune*, March 1, 2007, at *http://www.iht.com/articles/2007/03/01/business/imf.php* (September 19, 2008).
4. Alexei Barrionuevo, "Bank of the South, Championed by Venezuela, Begins to Take Form," *International Herald Tribune*, October 22, 2007, at *http://www.iht.com/articles/2007/10/22/business/bank.php* (September 19, 2008).
5. Santiago Mosquera, "S&P Downgrades Sovereign Risk Rating for Argentina," *Global Insight*, August 13, 2008.
6. Charles Newberry, "Hard Times for Argentina," *Business Week Online,* August 5, 2008, at *http://www.businessweek.com/bwdaily/dnflash/content/aug2008/db2008084_082921.htm* (September 19, 2008).

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mate has been damaged.[8] This past August, Standard & Poor's cut Argentina's foreign-debt rating from B+ to B,[9] which is five grades below investment grade[10] and places Argentina in the same category as Belize and Burkina Faso, far behind neighbor and rival Brazil (which achieved investment grade in 2008).[11] This lower rating will raise the cost of borrowing for Argentine businesses and make Argentina less competitive in the global economy.

Impartial rule of law, government transparency, and vigilance against state corruption are among the most important measurements used to calculate the annual *Index of Economic Freedom*. The Kirchners' Peronist government has callously disregarded them all—as demonstrated by Argentina's steadily declining scores—and this has been well illustrated by their attitude toward the bond-debt-swap holdouts. It is a classic case of an assault by a leftist-populist regime on the property rights of both domestic and foreign bondholders.

The Kirchners' aggressive and antagonistic attitude toward the holdouts (refusing until only recently even to consider re-entering negotiations) threatens to undermine established and time-tested international lending norms, ultimately to the detriment of all developing nations. As a leader of the globalized economy and the international financial institutions that have ensured prosperity for billions of people over the past 50 years, the United States has a special responsibility to prevent abuse of that system by Argentina or other rogue nations.

The U.S. Administration should insist that the IMF, the Inter-American Development Bank, and the World Bank withhold any future lending to Argentina until Argentina adopts free-market and good-governance reforms addressed in the *Index of Economic Freedom*.

The U.S. Congress should hold hearings on the threat to both the U.S. economy and the world financial system if more sovereign debtors were to follow the bad example of Argentina and repudiate their debts. Congress should also investigate possible legislative remedies to prevent abuse of the legal system by sovereign debtors.

Argentina's Ongoing Debt Crisis

One of the wealthiest countries in the world a hundred years ago, "Argentina suffered during most of the 20th century from recurring economic crises, persistent fiscal and current account deficits, high inflation, mounting external debt, and capital flight."[12] Though Argentina's most recent military dictatorship was finally overthrown in 1983, three of the democratically elected presidents since then have left office early and another served only in a caretaker capacity. In fact, during the 2001 debt default, Argentina went through five presidents in two weeks.[13]

Early Reforms Sank into the Morass of Peronist Party Corruption. After the Cold War, Argentina and other Latin American governments wanted to repair their economies damaged by the "lost decades" of the 1970s and 1980s, when Argentina and many other countries in the region were ruled by dictatorships and bedeviled by hyperinflation.[14] By the time Carlos Menem was elected president of

7. U.S. Department of State, "2008 Investment Climate Statement: Argentina," at *http://www.state.gov/e/eeb/ifd/2008/101776.htm* (September 19, 2008).
8. Travel Document Systems, "South America: Argentina—Economy," 2007, at *http://traveldocs.com/ar/economy.htm* (September 19, 2008), and U.S. Department of State, "Background Note: Argentina," February 2008, at *http://www.state.gov/r/pa/ei/bgn/26516.htm* (September 19, 2008).
9. Drew Benson, "Argentina's Debt Rating Cut to B by Standard & Poor's," *Bloomberg*, August 11, 2008, at *http://www.bloomberg.com/apps/news?pid=20601087&sid=aRz9NR9W52wU&refer=home* (September 3, 2008).
10. Drew Benson and Eliana Raszewski, "Argentina Weighing Plans to Swap Defaulted Debt," Bloomberg, September 22, 2008, at *http://www.bloomberg.com/apps/news?pid=newsarchive&sid=a.nu2tUmZQeA* (September 25, 2008).
11. Standard and Poor's Sovereign Credit Ratings at *http://www2.standardandpoors.com/portal/site/sp/en/us/page.topic/ratings_sov/2,1,8,0,0,0,0,0,0,3,0,2,0,0,0.html* (September 24, 2008).
12. Central Intelligence Agency, *The World Factbook,* "Argentina," at *https://www.cia.gov/library/publications/the-world-factbook/print/ar.html* (September 19, 2008).

Argentina in 1989, inflation was raging at a rate of at least 250 percent—per month.[15] Menem and other Latin leaders implemented the "Washington Consensus," a series of policy steps needed for an economy to enter the modern world—macroeconomic discipline, microeconomic liberalization, and participation in the global economy.[16]

Menem's sweeping market-based policies and his attempt to end 50 years of statism through an ambitious privatization program[17] led to increased investment and growth with stable prices. Inflows of foreign direct investment (FDI) to Argentina were among the highest in Latin America through most of the 1990s.[18]

To break the back of hyperinflation in 1991, President Menem adopted a Currency Board exchange rate mechanism and imposed peso–dollar parity. The government pegged the Argentine peso to the U.S. dollar at a 1:1 exchange rate through a strict "convertibility" law.[19] "While convertibility defeated inflation, over time the rigidity that it imposed on exchange rate policy, combined with lack of fiscal discipline and poor governance, undermined Argentina's export competitiveness and created chronic deficits in the current account of the balance of payments, which were financed by massive borrowing."[20]

In addition, unfortunately, neither Peronist Menem nor his successor, Fernando de la Rúa of the Radical Party, followed through on reforms needed to make Argentina's historically rigid and anti-free-market labor laws more investor friendly, nor did they reduce regulatory burdens on business, strengthen the judiciary, or reduce impediments to trade. They withheld their wholehearted support for the U.S.-led negotiations for a Free Trade Area of the Americas (FTAA) agreement.[21] Even more significantly, widespread corruption in the Menem and De la Rúa administrations undermined confidence in the government and hampered economic growth. The absence of deeper reforms caused new investment flows to slow, unemployment to rise, and "eventually, the [2001 debt] crisis [to] hit."[22]

2001: The Largest Sovereign Default in World History. In 1998, the domino effect of the Asian financial crisis "precipitated an outflow of capital that gradually mushroomed into a four-year depres-

13. December 10, 1999–December 21, 2001: Fernando de la Rúa
December 21, 2001–December 23, 2001: Ramón Puerta (acting)
December 23, 2001–January 1, 2002: Adolfo Rodríguez Saá (interim)
December 31, 2001–January 2, 2002: Eduardo Camaño (acting [for Rodríguez Saá to January 1, 2002])
January 2, 2002–May 25, 2003: Eduardo Duhalde
(Source: Rulers.org, "Argentina," at *http://www.rulers.org/rula2.html#argentina* (September 11, 2008).)
14. Mark Falcoff, "Are We Heading for Another 'Lost Decade?'" American Enterprise Institute *Latin American Outlook*, February 1, 2002, at *http://www.aei.org/publications/pubID.13595/pub_detail.asp* (September 19, 2008).
15. Carmen M. Reinhart and Kenneth S. Rogoff, "The Forgotten History of Public Debt," April 17, 2008, p. 21, at *http://www.economics.harvard.edu/faculty/rogoff/files/Forgotten_History_Of_Domestic_Debt.pdf* (August 15, 2008).
16. John Williamson, "The Washington Consensus as Policy Prescription for Development," speech at the Practitioners of Development Seminar Series, World Bank, Washington, D.C., January 13, 2004, at *http://info.worldbank.org/etools/BSPAN/PresentationView.asp?PID=1003&EID=328* (September 19, 2008). See also Juan Forero and Peter S. Goodman, "Chávez Builds His Sphere of Influence," *The Washington Post*, February 23, 2007, p. D1, at *http://www.washingtonpost.com/wp-dyn/content/article/2007/02/22/AR2007022201875_pf.html* (September 19, 2008).
17. U.S. Department of State, "2008 Investment Climate Statement: Argentina."
18. U.S. Department of State, "Background Note: Argentina," at *http://www.state.gov/r/pa/ei/bgn/26516.htm* (September 19, 2008).
19. International Monetary Fund, Independent Evaluation Office, "The Role of the IMF in Argentina 1991–2002," July 2003, at *http://www.imf.org/External/NP/ieo/2003/arg/#2* (August 19, 2008).
20. U.S. Department of State, "2008 Investment Climate Statement: Argentina."
21. U.S. Department of State, "Background Note: Argentina."
22. Ana I. Eiras, "Argentina: No Aid Without Reform," Heritage Foundation *Backgrounder* No. 1537, April 17, 2002, at *http://www.heritage.org/Research/LatinAmerica/BG1537.cfm*.

Comparing Argentina's Debt Restructuring

	Largest Sovereign Debt Defaults		Acceptance Rate History		Most Severe Sovereign Debt Default "Haircuts"	
Country	Amount (Billions)	Date	Year	Rate	Year	Rate
Argentina	$82.30	November 2001	2005	76%	2005	70%
Russia	$73.00	November 1998	1998–2000	98%	1998–2000	61%
Ukraine	$2.70	September 1998	1998–2000	99%	1998–2000	56%
Pakistan	$0.75	December 1998	1999	99%	1999	31%
Ecuador	$6.60	August 1999	2000	97%	2000	27%

Source: Vivian Z. Yue, "Sovereign Default and Debt Renegotiation," New York University, November 2006, at *http://www.econ.nyu.edu/user/yue/Yue_2006.pdf* (September 19, 2008); Barry Eichengreen, "Restructuring Sovereign Debt," p. 5, at *http://www.econ.berkeley.edu/~eichengr/research/journaleconomicperspectivesaprileditsep22-03.pdf*; and Federico Sturzenegger and Jeromin Zettelmeyer, "Haircuts: Estimating Investor Losses in Sovereign Debt Restructurings, 1998–2005," IMF Working Paper WP/05/137, July 2005, p. 59, at *http://www.imf.org/external/pubs/wp/2005/wp05137.pdf*.

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sion, culminating in a financial panic in Argentina in November 2001."[23] By early December, the financial and political crisis came to a head. Private capital fled the country and the government—drowning in debt—stopping interest payments on government-issued bonds to tens of thousands of individual investors, pension funds, and financial institutions (in Argentina and abroad).

On December 20, 2001, amidst bloody riots, President De la Rúa resigned.[24] At the end of the month, the government defaulted on roughly $82 billion in privately held debt and over $6 billion in "Paris Club" debt to official government creditors (including approximately $360 million owed to the U.S. government). It was "the largest sovereign debt default in history,"[25] and it rattled the world's already jittery financial markets.

The legislative assembly elected Peronist Eduardo Duhalde on January 1, 2002, to complete De la Rùa's term. Duhalde quickly abandoned the peso's 10-year-old convertibility link with the dollar, a move that was followed by a sharp currency depreciation and rising inflation. "While the [currency] board was operating, most contracts in the [utilities and transport] sector[s] were written in U.S. dollars; when the peso was devalued, the government decided to void most of these agreements,"[26] an act of bad faith and a harbinger of things to come.[27] As a result of the voided contracts, for instance, "multi-year price freezes on electricity and natural gas rates for residential users stoked consumption and kept private investment away, leading to restrictions on industrial use and blackouts [by] 2007."[28]

The 2003–2005 Restructuring Plan: Repudiating a $20 Billion Debt. After a new president, Peronist Néstor Kirchner, took power in 2003, the government presented a "take-it-or-leave-it"[29] debt-swap proposal to its foreign and domestic creditors.

23. U.S. Department of State, "2008 Investment Climate Statement, Argentina."
24. Lucia Newman, "Argentina Teeters on Possible Economic Collapse," CNN.com/WORLD, December 21, 2001, at *http://archives.cnn.com/2001/WORLD/americas/12/20/argentina/* (August 21, 2008).
25. U.S. Department of State, "Background Note: Argentina."
26. Economist Intelligence Unit, "2008 Country Commerce Report," at *http://www.eiu.com/index.asp?layout=displayIssueArticle&issue_id=193595604&article_id=423595627* (September 1, 2008).
27. U.S. Department of State, "Background Note: Argentina."
28. CIA, "The World Factbook: Argentina."
29. Ashley Seager, "Argentina Says Debt Default Is Over," *The Guardian*, March 4, 2005, at *http://www.guardian.co.uk/business/2005/mar/04/argentina.internationalnews* (September 26, 2008).

The swap (which was slightly sweetened in June 2004) amounted to a 70 percent reduction of the face value of the original bonds, which creditors would be forced to exchange for "three new bonds—Par, Quasi-Par and Discount—for a maximum estimated face value of $21.8 billion, plus a coupon linked to GDP growth [which the government pledged to maintain at 2.7 percent]."[30]

By 2005, bondholders accounting for a total of 76 percent of Argentina's defaulted debt accepted the government's offer of about 30 cents per one dollar of original debt. Many of these bondholders were Argentinean state-owned banks and government-controlled pension funds, which had little recourse after the Kirchners pressured them and threatened legal consequences if they refused to sign off on the debt-swap deal. Even so, the 76 percent acceptance rate was very low compared with other recent sovereign restructurings.

The acceptance rate for international creditors, however, has been estimated at only about 50 percent. And those foreign holders of more than $20 billion in bonds, the "holdouts" who refused to accept a 70 percent haircut in the 2003–2005 restructuring—which many called a "buzz cut"—are suing for full repayment.[31]

The Argentine Government's Contempt for Bondholders. Until very recently[32] the government of Argentina has refused even to engage with the holdouts, among which are several hedge funds, along with a number of pension funds as well as individual investors from Germany, Italy, and elsewhere. After rejecting the Argentine government's initial 2003 offer, the holdouts sued the Argentinean government in U.S. federal courts, an act that an irritated President Néstor Kirchner branded "genocide."[33] Kirchner also scoffed when Rodrigo de Rato, managing director of the IMF, requested that the Argentinean government be more respectful to the holdouts and treat its creditors with respect. Hans Humes, an asset manager who represents investors holding about $40 billion worth of defaulted debt, observed that Néstor Kirchner's behavior was proof that "Argentina is just trying to bully people into accepting an unacceptable offer."[34]

The intransigence of the Argentinean government toward the holdouts, while perhaps attractive politically for the Kirchners vis-à-vis their supporters, has been costly to the government in other ways. Argentina's reputation among global investors has deteriorated, and "the latent threat of [attachment of assets by creditors] prevents [the government of Argentina] from accessing international capital markets"[35] and thereby raises its borrowing costs. Until recently, the continuing refusal by the government to negotiate with the holdouts was causing the default to look more and more like a repudiation. Very few countries have taken such a hard stance in the past and those that have done so (for example, Zimbabwe[36]), have done incalculable damage to their reputations and their investment climates.

30. Martin Krause and Aldo Abram, "CIIMA/ESEADE Study on Foreign Direct Investment," Centro de Investigacion y Instituciones Mercados de Argentina (CIIMA) (Argentine Institutions and Markets Research Centre at ESEADE business school), Buenos Aires, October 2007.
31. Krause and Abram, "CIIMA/ESEADE Study on Foreign Direct Investment." See also David Bosco, "The Debt Frenzy: Vulture Funds," *Foreign Policy*, July 1, 2007, p. 36.
32. Drew Benson and Lester Pimental, "Citigroup, Barclays Propose Debt Plan to Argentina," Bloomberg, September 22, 2008, at *http://www.bloomberg.com/apps/news?pid=newsarchive&sid=a9QrJOnYJ0F0* (September 24, 2008).
33. Joshua Goodman, "Economy Minister Plays Down Fears Over Argentina's Isolation," *Financial Times*, February 14, 2004, at *http://search.ft.com/ftArticle?queryText=genocide+Argentina+Kirchner+bondholders+++&y=3&aje=true&x=10&id=040214000169&ct=0* (September 19, 2008).
34. Lester Pimentel and Daniel Helft, "Argentina May Reverse Stance on Debt," *International Herald Tribune*, February 22, 2007, at *http://www.iht.com/articles/2007/02/21/bloomberg/BXTK.php?pass=true* (September 19, 2008).
35. *Ibid*.
36. "Business Briefing," *The San Diego Union-Tribune*, September 10, 2003. See also Thomas M. Woods and Brett D. Schaefer, "Africa Must Confront the Growing Crisis in Zimbabwe," Heritage Foundation *WebMemo* No. 1970, June 26, 2008, at *http://www.heritage.org/Research/Africa/wm1970.cfm.*

Unfortunately, Argentina has a long history as a deadbeat in world financial markets. In fact, the Paris Club, representing developed countries' official government creditors, was invented to deal with a sovereign debt default by Argentina—in 1956. [37]

The Kirchners' Cookbook: Subsidized Beef Served with Heavy Inflation. The Kirchners' strategy has been to exploit record-high commodity prices to finance their leftist-populist policies and keep the peso artificially low. In the process they have overheated the economy and stoked exports and inflation.[38]

To deal with the high inflation their policies have generated, the Kirchners have simply denied that it is high and maintain the fiction that inflation in Argentina is relatively moderate. They imposed a new set of methodologies and ordered INDEC's statisticians to abandon best practices. Criticism of INDEC's figures has increased "as public and private estimates of price increases diverge ever further."[39] Recent estimates by private-sector analysts "put observed inflation closer to 30 percent."[40] Not only does an artificially low inflation figure allow the Kirchners to overstate real GDP growth, but it also permits the government to make lower interest payments to domestic bondholders because the interest calculation is based upon a formula using Argentina's CPI.

The Kirchners have used other tricks to hide inflation or attempt to depress it. They have imposed wage and price controls and have gone so far as to ban exports of world-famous Argentine beef in order to flood the domestic market and drive down the prices of beef (a staple food in Argentina).[41] In 2006, "President Néstor Kirchner banned beef exports in an effort to keep rising beef prices from pushing the country's [CPI] out of control."[42]

These efforts to tamp down inflation artificially and provide protection to local industry from competition from imports have succeeded in the short run. According to Morgan Stanley analyst David Volberg, "the peso has actually weakened nearly 2% annually against a basket of its main trading partners, although it should be strengthening because of strong terms of trade and steady economic growth."[43]

Luck is Running Out for the Kirchners. As *The Economist* noted recently, since the economy recovered in "mid-2002….it has seemed to defy economic gravity. [Argentina under the Kirchners has] violated many standard economic prescriptions: it has shunned the IMF and shafted private bondholders; kicked out foreign companies and set up new state-owned ones…. Yet over the past six years, Argentina's economy has grown at an annual average rate of 8.3%—faster than any other big economy except China."[44]

Although the farmers benefited initially from increased agricultural exports as a result of the government's weak peso policy, the Kirchner government began to look at those export revenues as a golden goose. When (now-former) Finance Minister Martín Lousteau attempted to raise taxes on agricultural exports to 44 percent earlier this year (the third increase in six months), the farmers revolted, staging strikes and blocking shipments of food,

37. Krause and Abram, "CIIMA/ESEADE Study on Foreign Direct Investment."
38. James M. Roberts, "Argentina Farmers Strike: Refusing to Foot the Bill for the Kirchners' Populist Politics," Heritage Foundation *WebMemo* No. 1938, May 27, 2008, at *http://www.heritage.org/Research/LatinAmerica/wm1938.cfm.*
39. Roque Planas, "Argentine Public Dubious of Inflation Numbers," *World Politics Review*, August 20, 2008, at *http://worldpoliticsreview.com/Article.aspx?id=2586* (September 19, 2008).
40. Mosquera, "S&P Downgrades Sovereign Risk Rating for Argentina."
41. Matthew Craze, "Tougher Cattle Threaten Argentine Beef Exports," *International Herald Tribune*, August 31, 2007, at *http://www.iht.com/articles/2007/08/30/bloomberg/bxbeef.php* (September 19, 2008).
42. Dow Jones Newswires, "Govt Official: Argentina Uses Any Excuse to Stop Beef Trade," May 8, 2006.
43. Daniel Volberg and Gray Newman, "Argentina: Policy Dilemma," Morgan Stanley, June 24, 2008, at *http://www.morganstanley.com/views/gef/archive/2008/20080624-Tue.html#anchor6568* (September 25, 2008).
44. *The Economist*, "Clouds gather again over the Pampas," August 21 2008, at *http://www.economist.com/world/americas/displaystory.cfm?story_id=11966983* (September 19, 2008).

both for export and to Argentine cities. Although the farmers demonstrated peacefully, the government at times responded with police brutality and its usual populist weapon—Communist rent-a-mobs (*Picateros*).[45]

After months of fruitless negotiations between the government and the farmers over the level of export taxes, the legislature finally resolved the impasse in a close vote that reflected great political courage by Cristina Kirchner's vice president, Julio Cobos.[46] The Kirchners were defeated by the senate's decision to overturn the tax increase, but that means that now government revenues will drop and Argentina's debt-to-GDP ratio will deteriorate. Debt levels are rising—currently 56 percent of GDP (67 percent if the debt owed to the haircut holdouts is included), compared with 54 percent in 2001 at the time of the default. Some economists in Argentina have raised the spectre of another default on the horizon.[47]

The Economist reports that Argentina may be reaching that turning point:

> A slowdown, long predicted by the Kirchners' opponents, is at hand. When compared with the same period last year, retail sales (measured by volume) are down 10% to 15%. On Calle Florida, Buenos Aires's main shopping street, almost every block has at least one vacant shop front. Employment in the private sector is still growing, but at half last year's rate, according to Nicolás Bridger of Prefinex, a consultancy. Meanwhile, inflation has taken off.[48]

British journalist Ambrose Evans-Pritchard reports that Argentina still looks safe on paper, but he notes that "the yield spread on inflation-linked peso debt has ballooned to 1230 basis points. They are priced for the dustbin. The world's biggest exporter of soybeans—and number two in corn—is riding the food boom, even if at war with its own farmers. The trade surplus is $12 billion. Foreign reserves are more than $50 billion. Yet the default premium is soaring anyway."[49] Evans-Pritchard reports speculation by University of Maryland economics professor Carmen Reinhart that the Kirchners are manipulating the inflation figures to "engineer a partial default on [Argentina's] domestic debt."[50]

Bondholders Win in U.S. Courts, and Then Lose. The holdouts have been aggressive in trying to force the Kirchners to pay their debts. Dozens of class action and individual lawsuits have been filed against the Republic of Argentina in the Federal District Court for the Southern District of New York. All of the federal cases were heard by U.S. Circuit Judge Thomas Griesa, who has consistently ruled in favor of the holdouts in the first instance.[51] Many more claims have been brought by Argentina's creditors in Europe before the International Centre for Settlement of Investment Disputes (ICSID)—and in Argentina's own courts.

Nonetheless, Argentina has managed to evade these adverse rulings by shuffling its domestic assets. Creditors have been unable to execute their judgments against the country because it moved anything that might be attached from the United States and has hidden the rest in protected accounts, such as those held by its central bank. Seeking relief and with no other recourse, the creditors appealed their enforcement action to the Second Circuit in 2007 but lost on a fairly basic issue: They had sued the wrong entity (the central bank instead of the Republic). The court hinted, however,

45. Author's notes from interviews with eyewitnesses during a visit to Buenos Aires, Argentina, March 25–April 2, 2008.

46. *The Guardian*, "In Blow to President Kirchner, Argentine Senate Rejects Export Tax," July 17, 2008, at *http://www.guardian.co.uk/world/2008/jul/17/argentina?gusrc=rss&feed=worldnews* (September 19, 2008).

47. Jude Webber, "Argentine Debt Raises Spectre of 2001 Crisis," *Financial Times*, June 13, 2008, at *http://www.ft.com/cms/s/0/2cc8e12a-38e2-11dd-8aed-0000779fd2ac.html* (September 19, 2008).

48. *The Economist,* "Clouds Gather Again over the Pampas." See also "Argentina: Uncertain Outlook," *Latin Business Chronicle*, September 8, 2008, at *http://www.latinbusinesschronicle.com/app/article.aspx?id=2723* (September 19, 2008).

49. Ambrose Evans-Pritchard, "Argentine Alert as Inflation's Spectre Stalks Half the World," *The Daily Telegraph*, June 3, 2008, p. 4, at *http://www.telegraph.co.uk/money/main.jhtml?xml=/money/2008/06/02/ccview102.xml* (September 19, 2008).

50. *Ibid.*

that they might have better luck simply alleging fraud, that Argentina was abusing the law "to play a shell game to deprive creditors of their legitimate remedies."[52] The creditors have not yet indicated whether they will pursue this line of attack.

Effects of Default Still Felt—In Argentina and on Main Street, USA

Argentina's economy is slowing, but real GDP growth for 2008 is still forecast to be 6 percent,[53] although it is unclear how much that figure has been manipulated by erroneous INDEC inflation figures. Nevertheless, there are growing problems related to the default that will negatively affect growth and hurt the average Argentinean: "mounting debt, rising inflation, sagging investment, and limited resources to pay for subsidies"[54]

An analyst for Morgan Stanley predicts that the risk of a wage-price spiral will increase in Argentina due to default-related inflation. "We suspect that wage negotiations are a key risk…and that…labor demands [for] wage growth [will] further spur inflation and risk an economic downturn as both supply and demand pull back."[55]

Lost: $6 Billion in New Foreign Direct Investment in Argentina. There are at least 450 U.S. companies operating in Argentina with more than 150,000 employees.[56] As noted above, those workers' futures were jeopardized by the Argentinean government's refusal, to date, to settle with the holdouts, which has damaged the country's investment climate.[57] At a recent meeting a panel of distinguished economists lamented Argentina's long trail of broken promises. They estimated that the country has failed to attract approximately $6 billion in foreign direct investment every year since the 2001 default. Much of that FDI has flowed instead into Argentina's more stable and prosperous neighbors, especially Brazil and Chile. "One problem lies in a history of broken contracts, debt defaults, and weak institutions. Another is the expectation of economic crises and investors' focus on short-term gains. Economic damage has also resulted from price controls, export bans, and the waning credibility of the INDEC National Statistics Institute, in addition to Argentina's still-defaulted Paris Club debt and litigation by holdouts from a 2005 sovereign restructuring."[58]

Why the Default and Restructuring is Significant to U.S. Taxpayers and Workers. Argentina has borrowed more than $25 billion over the years from the Inter-American Development Bank (IDB). Nearly 300 IDB loans were funded in part by American taxpayers, since the U.S. government funds almost one-third of the IDB's capital.[59] A default by Argentina on IDB loans would, ultimately, have to be paid by the American taxpayer.

51. Various filings with the United States Circuit Court for the Southern District of New York, e.g., 1-12-07 Amended Judgment—Laura Rossini et al. v. Republic of Argentina and Province of Buenos Aires, at *http://www.heritage.org/Research/LegalIssues/upload/1-12-07Amended.pdf*; 8-16-06 Complaint Teachers Insurance and Annuity Association of America (TIAA) v. Republic of Argentina, at *http://www.heritage.org/Research/LegalIssues/upload/8-16-06ComplaintTIAAvARG.pdf*; 1-5-07 Amended Judgment—Carlos Alberto Martinez et al. v. Republic of Argentina, at *http://www.heritage.org/Research/LegalIssues/upload/1-5-07AmendedMartinezVArgentina.pdf*; 2007_05_14 12 Judgment-J Griesa (Teachers Ins v. Arg 06 CV 6221 SDNY), at *http://www.heritage.org/Research/LegalIssues/upload/2007_05_14JudgmentTeachersVSDNY.pdf*; and 3-30-07 Judgment—Agostino Consolini et al. v. Republic of Argentina, at *http://www.heritage.org/Research/LegalIssues/upload/3-30-07JudgmentConsoliniVArgentina.pdf*. [Note: These PDFs have been scanned and made available through Heritage Foundation URLs.]
52. EM Ltd. V. Republic of Argentina, 473 F.3d 463, 480 n17 (2nd Cir. 2007).
53. Economist Intelligence Unit, "Argentina: Country Forecast Summary," *EIU ViewsWire Select,* August 22, 2008.
54. Newberry, "Hard Times for Argentina."
55. Volberg and Newman, "Argentina: Policy Dilemma."
56. U.S. Department of State, "2008 Investment Climate Statement, Argentina."
57. Travel Document Systems, "South America: Argentina—Economy," and U.S. Department of State, "Background Note: Argentina."
58. Hilary Burke, "Argentina Lost $6 Bln/Yr Foreign Investment—Study," Reuters, October 2, 2007, at *http://www.reuters.com/article/bondsNews/idUSN0242416320071002* (September 19, 2008).

Argentina's default has also hurt the pension funds of American teachers and other workers in the non-profit sector. The Teachers Insurance and Annuity Association of America (TIAA-CREF) lost $100 million, not including lost interest and penalties, when Argentina's government defaulted—a big hit to the pension funds of teachers and college professors across the U.S.[60] The artificially low peso has hurt U.S. soybean farmers. When the farmers were on strike in Argentina, U.S. soybean exports rose. But when Argentina, the world's largest producer of soybeans, returned to full production and began exporting soybeans again at artificially low peso prices, "soybean demand from U.S. processors fell 6.7 percent."[61]

Economic Freedom: Argentina's Sinking Scores

Impartial rule of law, secure property rights, transparency in government, and vigilance against government corruption are among the most important measurements used to calculate the annual ranking of 179 countries in the *Index of Economic Freedom* published by The Heritage Foundation and *The Wall Street Journal*. Argentina's *Index* score plummeted from 70.9 in 1998 (ranking 19th freest economy in the world out of 156 countries scored) to 55.1 by 2008 (ranking 108 out of 162 countries).[62]

The structural problems in Argentina's economy are outlined in the *2008 Index of Economic Freedom*, which reports low scores on property rights, labor freedom, freedom from corruption, and especially financial freedom. The Kirchners' manipulation of the official government inflation index allows them to reduce interest payments on government bonds. The interest payments are calculated using a formula that includes the CPI. Thus, the Argentinean government's use of an artificially low inflation figure in the formula in practice results in the theft of a portion of the interest payments it owes to bondholders (the difference between the interest owed if the higher—true—inflation figure were used versus the lower interest payment resulting from using the artificially lower CPI figure), thereby violating their property and legal rights.

Argentina in the *2008 Index of Economic Freedom*. The 2008 edition of the *Index* noted that the 2001–2002 foreign debt crisis remains unresolved, and local capital markets are not healthy for entrepreneurs. Argentina scored only 55.1 out of a possible 100, with zero being "least free" and 100 indicating "most free." Its low rank even in the Western Hemisphere, 23rd of 29 countries, reflects how far behind Argentineans are from those they consider peers: Canada, the U.S., and Chile.

Compared to the typical country, Argentina has only one economically favorable institution: relatively small government in terms of expenditures. Most advanced economies are cutting their corporate tax rates, but Argentina's top corporate and income tax rates are 35 percent. Yet tax revenue as a percentage of GDP is low, as is expenditure, as a result of tax avoidance and evasion. Property rights, labor freedom, and freedom from corruption are low, but financial freedom is especially problematic. Political interference with an inefficient judiciary hinders foreign investment, and popular and official obstructions of due process make international courts preferable to Argentine courts. A brief look at some of the defects in the Argentine system detailed in the 10 *Index* freedoms for Argentina confirms these findings:[63]

59. Inter-American Development Bank, "Argentina and the IDB," 2008, at *http://www.iadb.org/countries/home.cfm?id_country=AR&Language=English* (September 19, 2008).
60. U.S. District Court for the Southern District of New York, TIAA vs. Republic of Argentina, ECF Case # 06 Civ.6221, "Complaint," August 15, 2006.
61. Jeff Wilson, "U.S. Soybean Use Falls as Supplies from '07 Crop Fall" *Bloomberg*, September 15, 2008, at *http://www.bloomberg.com/apps/news?pid=newsarchive&sid=agfH.J0EzVQY* (September 25, 2008).
62. The Heritage Foundation and *The Wall Street Journal*, *2008 Index of Economic Freedom*, Past Scores Data, at *http://www.heritage.org/research/features/index/downloads.cfm.*
63. Kim R. Holmes, Edwin J. Feulner, and Mary Anastasia O'Grady, *2008 Index of Economic Freedom* (Washington, D.C.: The Heritage Foundation and Dow Jones & Company, Inc., 2008), pp. 83–84, at *http://www.heritage.org/index/countries.cfm.*

Business Freedom. "Inconsistency and lack of transparency persist…. Regulations are often applied inconsistently."

Trade Freedom. "Extensive non-tariff barriers…to constrain trade, protect domestic industries, and maintain price controls for some goods include import and export controls, tariff escalation, import and export taxes, reference pricing, burdensome regulations, restrictive sanitary rules, subsidies…. While the customs process has been improved, many delays continue."

Fiscal Freedom. "Argentina has high tax rates."

Key Statistics on Argentina

Population	39.1 million
Gross Domestic Product (Purchasing Power Parity)	$469 billion
GDP Growth	8.5%
5-year compound annual growth	4.6%
Per-capita income	$11,985
Unemployment rate	14.1%
Inflation (Core Price Inflation)	8.8%
Foreign Direct Investment inflow	$4.8 billion

Sources: World Bank, *World Development Indicators Online 2008*; International Monetary Fund, World Economic Outlook Database April 2008; U.S. Central Intelligence Agency, *The World Factbook 2008*; United Nations Conference on Trade and Development, *World Investment Report 2007*.

Table 2 • B 2191 heritage.org

Government Size. "The state's role in the economy has grown in recent years, and structural budgetary weakness persists. The energy and transport sectors are particularly dominated by the public sector."

Monetary Freedom. "Official government figures for inflation show it to be relatively high, averaging 9.4 percent between 2005 and 2007. Credible unofficial figures report the true rate of inflation was raging at an annualized rate of at least 25 percent in 2008. The government regulates prices on numerous goods and services, including electricity, water, retail-level gas distribution, urban transport, and local telephone services. It also establishes price agreements with producers and sellers."

Investment Freedom. "Investors are obliged to keep foreign currency earnings in the country for a period of at least 180 days. In June 2005, the government further tightened capital controls by increasing the minimum holding period for capital inflows and establishing that some capital inflows are subject to a 30 percent unremunerated reserve requirement to be deposited in a local bank for 365 days. …The most significant deterrent is legal uncertainty concerning creditor, contract, and property rights. The flow of capital is restricted, and repatriation is subject to some controls."

Financial Freedom. "Argentina's banking system remains significantly dominated by the state's presence. The largest bank is state-owned and serves as the sole financial institution in parts of the country. Argentina remains unable to gain full access to international capital markets, however, because of the government's outstanding debt."

Property Rights. "The executive branch influences Argentina's judiciary, and independent surveys indicate that public confidence remains weak. Courts are notoriously slow, inefficient, secretive, and corrupt. Many foreign investors resort to international arbitration. An important violation of property rights is the 'piquete,' by which protestors take over private business, causing extensive losses with no effective punishment by the police or the government." The government's manipulation of official statistics for inflation has caused domestic bondholders to lose billions in interest payment because of the effect of the lower inflation figures on the formulas for domestic debt re-payments.

Price controls and poor intellectual property protection have made Argentina less attractive for FSI from multinational pharmaceutical companies. "A senior manager at U.S. firm Eli Lilly [says] that it was looking elsewhere for growth in the absence of robust patent laws and tolerance of copy drugs by the Argentine authorities."[64] Unsurprisingly, Argentina features prominently as one of the nine countries on the U.S. Trade Representative's Priority Watch List published in April 2008.[65]

Freedom From Corruption. "Corruption is perceived as widespread. Argentina ranks 105th out of

179 countries in Transparency International's *Corruption Perceptions Index* for 2007.[66] Foreign investors complain frequently about both government and private-sector corruption. Money laundering, trafficking in narcotics and contraband, as well as tax evasion plague the financial system."

Labor Freedom. "Argentina's labor market operates under restrictive employment regulations that hinder employment creation and productivity growth."

Other Indices Echo the *Index* Findings:

- *Forbes* "Best Countries for Business" report in 2008: Argentina ranked 92nd of 121 countries[67] versus 75th out of 144 in 2007.[68]
- World Bank *Doing Business 2009* report: Argentina ranked 113th of 181 countries,[69] down from 109th of 178 countries in 2008.[70]
- World Economic Forum (WEF) *Global Competitiveness Index*: Argentina dropped from 70th of 131 in 2006 to 85th of 131 in 2007.[71]
- Transparency International *Corruption Perceptions Index*: Argentina ranks 105th of 179 countries for 2007[72] versus 93rd of 163 countries in 2006.[73]

What Argentina and the U.S. Should Do

As a leader of the globalized economy and the international financial institutions that have ensured prosperity for billions of people over the past 50 years, the United States has a special responsibility to prevent further abuse of that system by Argentina and possibly other rogue nations. The U.S. government must also act to prevent further losses to the American taxpayer emanating from the Argentine default.

The Argentinean government should:

- Follow through on its recently announced intention to re-enter negotiations to repay debts to the Paris Club and private bondholders.
- Honor the commitments made by the government of Argentina at the time of the borrowing and repay the loans with full faith and credit.
- Take note of and implement the steps needed to correct the deficiencies described in the *2008 Index of Economic Freedom*.

The U.S. Administration should:

- Make debt repayment a policy priority in recognition of the importance of the strengthened U.S.

64. MarketWatch/Business Monitor International, "Argentina Pharmaceuticals and Healthcare Report Q3 2008," July 22, 2008, at *http://www.marketwatch.com/news/story/argentina-pharmaceuticals-healthcare-report-q3/story.aspx?guid=%7B7DF2B42C-7F50-466D-9C68-2AFBB5C1D84A%7D&dist=hppr* (September 19, 2008), Research and Markets, "Argentina Pharmaceuticals and Healthcare Report Q3 2008," *Business Monitor International,* July 2008, p. 68, at *http://www.researchandmarkets.com/research/f545f9/argentina%5fpharmace* (September 19, 2008).
65. Office of the United States Trade Representative, *2008 Special 301Report,* "Priority Watch List," April 2008, p. 35, at *http://www.ustr.gov/assets/Document_Library/Reports_Publications/2008/2008_Special_301_Report/asset_upload_file558_14870.pdf* (August 21, 2008).
66. J. Graf Lambsdorff, *Corruption Perceptions Index 2007*, Transparency International, 2007, at *http://www.transparency.org/policy_research/surveys_indices/cpi/2007* (September 26, 2008).
67. "Best Countries for Business," *Forbes*, June 26, 2008, at *http://www.forbes.com/lists/2008/6/biz_bizcountries08_Best-Countries-for-Business_Rank_4.html* (September 19, 2008).
68. "Capital Hospitality Index," *Forbes*, April 3, 2007, at *http://www.forbes.com/lists/2007/6/07caphosp_Capital-Hospitality_Rank_4.html* (September 24, 2008).
69. The International Bank for Reconstruction and Development/The World Bank, *Doing Business 2009*, "Economy Rankings," September 10, 2008, at *http://www.doingbusiness.org/economyrankings/?direction=Asc&sort=1* (September 11, 2008).
70. The World Bank and the International Finance Corporation, *Doing Business 2008* (Washington, D.C.: The World Bank, 2007) p. 6, at *http://www.doingbusiness.org/documents/FullReport/2008/DB08_Full_Report.pdf* (September 19, 2008).
71. World Economic Forum, *The Global Competitiveness Index 2007–2008*, 2007, at *http://www.weforum.org/pdf/Global_Competitiveness_Reports/Reports/gcr_2007/gcr2007_rankings.pdf* (September 19, 2008).
72. Lambsdorff, *Corruption Perceptions Index 2007*.
73. J. Graf Lambsdorff, *Corruption Perceptions Index 2006*, Transparency International, 2006, at *http://www.transparency.org/policy_research/surveys_indices/cpi/2006* (September 19, 2008).

relations with Latin America that would flow from the resulting improvement in financial freedom and investor confidence throughout the region.

- Hold Argentina accountable in all high-level contacts between U.S. and Argentinean government officials by emphasizing the need for the Kirchner government to settle with its international creditors.
- Insist that the IMF, IDB, and the World Bank withhold any future lending to Argentina until policy reforms outlined in the *2008 Index of Economic Freedom* are implemented.

The U.S. Congress should:

- Hold hearings on the threat to both the U.S. economy, for example, U.S. businesses and U.S. jobs affected by Argentina's economy, as well as the world financial system if more sovereign debtors were to follow the bad example of Argentina and repudiate their debts.
- Investigate possible legislative remedies to prevent abuse of the U.S. legal system by sovereign debtors.

Conclusion

The Kirchners should take note of and implement the steps needed to correct all of the deficiencies described in the *2008 Index of Economic Freedom*, for the good not only of their own citizens but of all South America. The government must also be honest about the true rate of inflation and cease efforts to manipulate the value of the peso. The government of Argentina has an obligation to its citizens to reach some sort of agreement with all external creditors so that it can regain full access to world financial markets.

Instead of perpetuating wasteful welfare-state handouts and income redistribution based on an unsustainable economic model, the Argentine government should look west and emulate the success that Chile has enjoyed from a combination of market-based economic reforms, privatizations, and limited government.

The Kirchners also should look north to Brazil, where fellow leftist and President Luiz Inacio Lula has been more successful governing than the Kirchners. Lula has called inflation a "degrading disease," preferring fiscal restraint and support for Brazil's central bank anti-inflation measures. As a result, Brazil has enjoyed much greater inflows of FDI and was recently awarded investment-grade foreign-debt rating.[74]

The Kirchners' collusion with Hugo Chavez in his campaign against the world financial system poses a grave threat to global prosperity. Their aggressive and antagonistic "take-it-or-leave-it" attitude threatens to undermine established and time-tested international lending norms, ultimately to the detriment of all developing nations in the form of higher borrowing costs.

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74. Webber, "Argentine Debt Raises Spectre of 2001 Crisis," *Financial Times.*