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Clausen's: Argentina

Vol 3



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THE WORLD BANK/INTERNATIONAL FINANCE CORPORATION  
OFFICE MEMORANDUM

*File - A*

DATE: October 10, 1986  
TO: Files  
FROM: Peter R. Scherer, Division Chief, LC2AR  
EXT: 76251  
SUBJECT: Meeting of the Argentine Delegation with Mr. Conable on  
September 27, 1986

The Minister of Economy of Argentina, Mr. Juan Vital Sourrouille, visited Mr. Conable on September 27, 1986. Mr. Sourrouille was accompanied by Messrs. Ramon Dabouza (National Director of Economic and Financial External Policy), Mr. Arturo O'Connell (Director, Central Bank) and Mr. Felix Camarasa (Alternate Executive Director). Also present from the Bank were Messrs. Knox, Husain, Gue, Sam and myself.

Welcoming Mr. Conable's appointment, Minister Sourrouille noted that Argentina had had a long tradition of cooperation with the Bank. The Government felt indebted to the staff of the Bank for the support it had been giving to Argentina.

The Minister emphasized that consolidating the democratic process was the Government's fundamental objective. Economic reform should therefore be seen in a political framework. Argentina's economic position was characterized by two main features: first, the legacy of an extended period of economic stagnation and falling real per capita income; and second, its isolation from the international economic system. Large fiscal deficits, conflicting domestic priorities and heavy debt service payments were of real but secondary importance. The resumption of economic growth was absolutely essential if the democratic process was to succeed in Argentina; a program that did not offer convincing prospects for sustained growth would make no sense. The Government's program was based on the principles of a mixed economy. Increasing investment was critical. At the very least, it must be at a level that compensated for depreciation of existing capital stocks; this has not been the case in the past. Financing increased investment was made all the more difficult by the sharp decline in the prices of Argentina's export products, in addition to the heavy burden of debt service payments.

Within the constraints set by the political environment in which it had to operate, the Government was directing its economic policies towards:

- (a) increasing the integration of Argentina's economy into the international trading system -- sustained growth would not be possible without structural change;

- (b) redefining the role of the public sector in the economy, including transfers of public enterprises to the private sector -- success in this endeavor would require a "cultural shift" in Argentina;
- (c) transforming the financial system -- the limited size of the current monetary base and the high cost of financial intermediation were inconsistent with the needs of a dynamic economy.

Proceeding with these reforms posed extraordinary challenges to the Government, and the Government was counting on the World Bank for substantial assistance.

Control of inflation was a sine qua non for successful structural reform; rationalizing the process of wage determination was fundamental in this respect. The current system, whereby the Government had to decide on the wage level, made no sense. However, establishing a functioning system of free collective wage bargaining was one of the thorniest problems associated with transition from the distorting regulations of the previous authoritarian regime to the free play of market forces under a democratic system. The Government has done just about everything it could to stabilize the economy. It had reduced the fiscal deficit from 12% to 3% of GDP within a single year, and had financed this deficit without monetary emission; GNP had grown by 5% in the year following adoption of the Austral Plan. Despite these successes, however, inflationary pressures had surfaced once more: causal factors were related to inelasticities in demand and supply adjustments, and not to fiscal and monetary policies which were firm and continue to be so.

The Government has learned the hard lesson: that price stability could not be achieved without vigorous structural change. Unfortunately, it took time to implement such change and still more time for it to have an effect. Meanwhile, stabilization was unattainable without growth; successful structural reform required a dynamic economy. Furthermore, changes in the operation of the economy had to be made carefully, in line with the rules of the democratic process. The Government needed the World Bank's support in cutting through what seemed to be a vicious circle; Bank financing of the structural reform program was of the highest importance for the Government. It had to be remembered that international institutions and developing countries worked with different timeframes: the latter needed funds more urgently than the international institutions might be able to supply them. The Argentine Government was now focusing its attention increasingly on the longer term and was therefore keenly interested in the greatest possible cooperation with the Bank.

The Minister extended an invitation from his Government to Mr. Conable to visit Argentina. He also expressed his Government's support for an increase in the Bank's subscribed capital.

Mr. Conable thanked the Minister for his comprehensive and thoughtful presentation. It had covered the ground very well and Mr. Conable therefore wanted to raise only one question, related to his previous professional interests: did the Minister expect that the tax amnesty would promote the return of Argentine flight capital? The Minister answered that the Government's tax reform program was closing most of the loopholes for tax evasion; combined with modernization of collection methods, the reform had yielded a 50% real increase in fiscal revenues. The tax amnesty was essentially intended to help speed up the tax reform; the Minister did not expect that it would bring back flight capital. The movement of flight capital was not determined by fiscal regimes, but rather by expected profitability, which in turn depended on favorable prospects of economic growth. Thus, while the tax package before Congress would lend credibility to the Government's program, it would not affect the decision-making processes of Argentines' who held capital abroad. Any Argentine could circumvent the tax rules by forming a company abroad and investing through that company in Argentina -- with no questions asked. The Minister expected that the creation of new debt instruments, including debt equity swaps combined with the transfer of additional foreign exchange, would be more important than the tax amnesty.

Mr. Knox mentioned that he was looking forward to the meeting with the Argentine delegation on Thursday in which he would like to follow up on specific issues. He reiterated that the Bank was prepared to expand its lending program to Argentina, with a lending target of US\$1 billion per year. Mr. Conable asked whether the Government would be able to control inflation. The Minister responded that he was confident the Government would succeed: recent adjustments in the stabilization program should lead to a decline in inflation to about 2%-3% per month by the end of the year. Preliminary figures for September were encouraging. Continuation of the Government's tight monetary and fiscal policy should produce the expected deceleration. Mr. Conable congratulated the Minister on the orientation of his policy and wished him best success.

cc: Messrs. Stern  
Knox  
Husain  
Sam  
Gue, LC2DR  
Picciotto, LCPDR  
Pfeffermann, LCNVP  
Aguirre-Sacasa, LCPDR  
Finzi, LCPDR  
Jennings, LCPDR  
Wessels, LCPDR  
Mirza, LCNVP  
Quijano, LCNVP  
Nankani, LC2DR  
Argentina Country Team

PRScherer:gc

ANNUAL MEETING BRIEF

push for Argentina  
to sign MIGA

Name of Country: Argentina

Date: September 10, 1986

Meeting with: Mr. Juan Sourrouille, Minister of Economy and Jose Luis  
Machinea, President of the Central Bank

Population: 30.6 m

Estimated Growth Rate: 1.6%

GNP per capita: \$2,130 (1985)

	(\$m)		(\$m)
Total Commitments to date:	2,642.8	FY86: Commitments:	544.5
of which:		Disbursements:	150.8
Bank (26 operations)	2,642.8	Amortization:	81.9
IDA	0		
Total Undisbursed:	1,275.0		
Lending Program FY87-88:	1,385		

<u>Summary Data</u>	<u>Average</u>		
	<u>1983-85</u>	<u>1986</u>	
GDP growth	0.5	2.9	Aid Group Meeting: None
Export growth	8.4	-2.7	Last Meeting: None
Import growth	-3.5	9.7	IMF Status as of June 30, 1986:
Current Account Deficit/GDP	-3.0	-3.1	December 1984 stand-by
Gross Debt Service Ratio	106.3	75.3	completed on a waiver in
Annual Inflation Rate	547.6	80.0	June 1986; a new stand-by
			is being prepared.

Background: The stabilization program is encountering difficulties; inflation has risen to almost 7% during July 1986 while the economy essentially remains stagnant. In response, the Government is adopting active incomes and tighter monetary policies combined with measures to strengthen exports and promote the repatriation of capital. The Government wants the Bank to play an increasingly important role in its efforts to mobilize external financing for economic growth. We have encouraged the Government to present an action-specific medium-term adjustment program as a framework for its negotiations with international lenders, including the Bank. Further expansion of Bank lending will depend on progress in reforms of the trade regime, the financial sector, the oil and gas sector and privatization.

Issues Likely to be raised by Delegation:

- Management of the Economy
- Cooperation with the Bank

Issues to be raised by Bank Management:

- Medium-Term Reform Program
- Trade Policy Loan
- Financial Sector Loan
- Privatization Loan
- Lending for Oil and Gas

Attachments

FIVE-YEAR LENDING PROGRAM: FY86-90 (FY86 actual)

Biographical Information

## Background

1. Economy. The Austral Plan, launched in June 1985, is running into difficulties, notwithstanding a good revenue performance (first semester results indicate a fiscal deficit of about 3.5% of GDP) and, until recently, restrictive monetary policies (essentially in line with IMF targets). Inflationary expectations may have been reignited by, inter alia, flexibilization of price controls, recent salary increases, reduction in beef supply and a fall in exports. The parallel exchange market has become more volatile (the premium has gone up as high as 20%). In response, the Government now is pursuing more active incomes (control of wages and prices) and tighter monetary policies. President Alfonsin has appointed Mr. Machinea (a close associate of Economy Minister Sourrouille) as President of the Central Bank to ensure that monetary policies are consistent with the stabilization program. Economic growth continues to be sluggish. It is unlikely that GDP will increase by more than 3% in 1986 (-4.5% in 1985) in spite of a recovery in industrial production, estimated at about 5% during the first semester. Unemployment has increased slightly to 6%. Recent increases notwithstanding, wages are still below 1985 levels. Private investment is declining further from already depressed levels (7% of GDP) and public investment (5% of GDP) cannot be expanded because of fiscal constraints. Following a 14% growth in 1985, exports are expected to decline by 3% this year. The Government has responded by accelerating the crawling peg and extending export promotion programs; it also has offered a tax amnesty for capital repatriation and swaps of public dollar denominated obligations for equity in export industries. In order to shore up external financing the Government intends to enter into a new stand-by with the Fund and to negotiate with the commercial banks rescheduling of 1986, and possibly 1987, maturities (US\$7 billion) together with a new money facility (we gather around US\$1.5 billion).

2. Bank Operations. Bank commitments have increased rapidly -- nil in FY84, US\$180 million FY85, US\$545 million FY86. Lending has been concentrated in the agricultural sector (reform of taxation and pricing) and the hydrocarbon sector (opening to the private sector, rationalization of price system, management of state oil company YPF). Disbursements lag behind commitments -- US\$74 million FY84, US\$131 million FY85 and US\$151 million FY86. Following a recent country implementation review with the Government, most of the constraints have been removed and the speed of disbursement has accelerated substantially. Significant progress in structural reforms would be a prerequisite for an expansion of future lending. The Bank has been helping the Government to prepare a medium-term reform plan and projections of associated external financing requirements that would provide the framework for Bank assistance and the Government's discussion with external lenders. We have encouraged the Government to finalize this plan quickly and to elaborate on its program for structural reform during the Annual Meeting. So far, progress in this respect has been slow, in part because of the Government's preoccupation with stabilization measures. The Government will have to overcome the opposition to structural change of entrenched and powerful interest groups. The private sector typically has fared better under inflation than it will do for some time in a more stable environment; the trade unions are concerned that their power will erode further under the proposed changes of labor and welfare legislation; public sector employees will have to work harder while still facing lower salaries or losing their jobs; and the military are losing influence and patronage. However, President Alfonsin has a clear political mandate and his economic team is among the very best Argentina has had for a long time.

### Issues Likely to be raised by the Delegation

3. Management of the Economy. Minister Sourrouille is likely to open the meeting with a summary of recent economic developments and to explain the measures the Government has taken and under consideration to counter rekindled inflationary pressures. You may wish to:

- commend the Minister for the Government's determination in pursuing the Austral Plan, especially its success in lowering the fiscal deficit, and encourage him to move as vigorously on the expenditure side as he has done on the revenue side; and
- ask the Minister about his assessment of the interplay between inflation and growth--where does he draw the line between efforts to stabilize prices and attempts to reactivate the economy, where does the inflationary danger zone begin that might jeopardize investor confidence--and his plans to lift price controls.

4. Cooperation with the Bank. The Government wants the Bank to play an increasingly important role in its efforts to mobilize external financing. Most likely, the Minister will reiterate his concern that expanded Bank lending should not be at the expense of additional funds from the commercial banks and request that the share of policy based lending be increased in view of tight budget constraints. You may want to respond that the Bank:

- is prepared to expand its lending. If all went well, commitments could reach close to US\$1 billion in CY87. This target is predicated on the adoption of substantial structural policy reforms, including progress in the most critical problem areas -- the trade regime, the financial sector, the energy sector and privatization -- and on commensurate commercial bank financing. The share of freely disposable policy loans could exceed 40% of total Bank lending;
- encourages the efforts of the Government to expedite disbursements of existing loans. One action is of particular importance: the promotion of Congressional approval of the new land tax for the release of the second tranche of the Agricultural Sector Loan (US\$170 million).
- the Bank stands ready to support the Government in its negotiations with the commercial banks and also the members of the Paris Club. However, a meaningful interaction of the Bank will require agreement on a medium term policy framework with the Government, an understanding on the Government's resource mobilization strategy and external financial requirements, and on progress in obtaining a new stand-by from the Fund.

#### Issues to be raised by Bank Management

5. Reform Policy Framework. We have reached a critical juncture in our cooperation with Argentina. Expectations for a further substantial increase in Bank lending can only be realized if the Government takes decisive action to resolve the structural constraints to Argentina's economic development. We have encouraged the Government to present an action specific medium-term adjustment program that would provide a framework for the Government's negotiations with international lenders, including the Bank. We have discussed with the Government possibilities to associate Bank lending with the most important components of structural reform.

6. Proposed Trade Policy Loan. This would be the second policy based sector loan to Argentina. Negotiations in early 1987 would require progress in (a) making the temporary admission scheme automatic and uniform; (b) reducing the list of imports requiring prior approval (de facto quantitative restrictions); (c) eliminating the remaining export taxes on manufactured products; and (d) maintaining a competitive exchange rate. You may want to emphasize to the Minister:

- that increasing Argentina's export competitiveness through a rationalization of the trade regime and an adequate exchange rate is a

sine-quo non to justify additional external borrowing in support of economic reactivation in the short term;

- the envisaged trade policy loan would be the cornerstone of the Bank's lending in FY87; delays cannot be compensated by other operations.

7. Proposed Financial Sector Loan. This would be the third policy-based sector loan. Bank staff has recently discussed with the Government the conclusions of a study of the financial sector. Government representatives have been receptive to the recommendations that would help reduce prohibitively high interest rates and operating costs of the financial system, phase out distortions and directed credit, eliminate Central Bank subsidies and enhance competition between and among private and public banks. You may want to mention to the Minister that:

- reform of the financial system (intermediation costs are close to 2% per month) is a logical sequence to the reform of the trade regime. To bring a sector policy loan to the Board in FY87, in which the Government is interested, would require expeditious agreement on a schedule of actions.
- processing of the proposed financial intermediary loans (Small and Medium Industries, Industrial Credit III) would depend significantly on progress with financial sector reform.

8. Proposed Privatization Loan. The Government has asked the Bank for assistance in the privatization program. Progress has been slow since the Government's announcement a year ago that it would privatize its stakes in the petrochemical and steel sectors. The reasons are political sensitivities associated with the enactment of the privatization law, to be submitted by the President to the Congress, and numerous changes in organization and government appointments. You may want to ask the Minister:

- is the Government prepared to spell out details of coverage and implementation of its privatization program?
- what role does the Minister expect the World Bank Group to play in the privatization process?

9. Proposed Lending for Oil and Gas. The Government has changed past policies by inviting private investment in oil and gas exploration, has rationalized prices, and is considering ways to induce more private participation in the exploitation of known oil reserves. The Bank has supported these reforms with sizeable lending. Considerable progress notwithstanding, the dominance of the state oil company (YPF) continues to constrain the efficient development of the sector. The Government has agreed to undertake, within 1986, a study of further policy reforms including the restructuring of YPF and the respective roles of private and public sector investors. Furthermore, the needed expansion of gas transmission infrastructure, a sector priority, is impeded by the dispute with a Dutch consortium (COGASCO) over Argentina's financial obligations related to a gas pipeline built by COGASCO under a toll contract. Negotiations are ongoing. You may want to mention to the Minister that:

- the timing and scope of our lending program in the sector will depend on the execution of the study (which has been unduly delayed) and on agreement on its recommendations and their implementation;
- cost-effective development of gas infrastructure and Bank participation in it, would require an expeditious solution of the COGASCO dispute.

## LATIN AMERICA AND THE CARIBBEAN REGION

COUNTRY: ARGENTINA  
 OPERATIONS PROGRAM: FY86-90  
 AS OF END AUGUST 1986

SECTOR			FY86	FY87	FY88	FY89	FY90	FY86-90
AGRICULTURE	PA036-AGR SECTOR-A	L	350.0	.0	.0	.0	.0	350.0
	PA065-AG CREDIT II-B	L	.0	.0	150.0	.0	.0	150.0
	PA061-AGR SECTOR II	L	.0	.0	.0	350.0	.0	350.0
	*SUB-TOTAL AGRICULTURE		350.0	.0	150.0	350.0	.0	850.0
EDUC + PHN	PA064-HEALTH DEV	S	.0	.0	.0	.0	40.0	40.0
	*SUB-TOTAL EDUC + PHN		.0	.0	.0	.0	40.0	40.0
ENERGY + POWER	PA047-REFINERY SUPP LOAN-A	M	116.0	.0	.0	.0	.0	116.0
	PA028-OIL & GAS PRIV-C	L	.0	150.0	.0	.0	.0	150.0
	PA042-POWER ENG-B	L	.0	14.0	.0	.0	.0	14.0
	PA048-SEGBA V-C	S	.0	.0	150.0	.0	.0	150.0
	PA051-PWR DISTRIBUT.-C	L	.0	.0	.0	150.0	.0	150.0
*SUB-TOTAL ENERGY + POWER		116.0	164.0	150.0	150.0	.0	580.0	
INDUSTRY + IDF	PA046-SML & MED SCALE IND-	L	.0	50.0	.0	.0	.0	50.0
	PA053-EXPORT PROMOTION-D	L	.0	.0	150.0	.0	.0	150.0
	PA056-FINAN SCTR LN-D	L	.0	.0	250.0	.0	.0	250.0
	PA058-PETROCHEM PRIVATIZ.	L	.0	.0	.0	150.0	.0	150.0
	PA055-SOMISA RESTR	L	.0	.0	.0	.0	50.0	50.0
	PA049-FINCIAL RSTRUCTURNG-	S	.0	.0	.0	.0	300.0	300.0
	PA063-TELECOMM TA	S	.0	.0	.0	.0	20.0	20.0
*SUB-TOTAL INDUSTRY + IDF		.0	50.0	400.0	150.0	370.0	970.0	
INFRASTRUCTURE	PA025-WATER SUPPLY-A	L	60.0	.0	.0	.0	.0	60.0
	PA024-BAHIA BLANCA PORT I-	L	.0	46.0	.0	.0	.0	46.0
	PA043-URBAN DEVT-D	L	.0	.0	75.0	.0	.0	75.0
	PA044-BAHIA BLANCA II-C	L	.0	.0	.0	150.0	.0	150.0
	PA057-WATER SUPPLY II-C	S	.0	.0	.0	150.0	.0	150.0
	PA060-TRANSPORT SCTR	S	.0	.0	.0	.0	150.0	150.0
*SUB-TOTAL INFRASTRUCTURE		60.0	46.0	75.0	300.0	150.0	631.0	
NON-PROJECT	PA041-T A I-A	L	18.5	.0	.0	.0	.0	18.5
	PA050-TRADE POLICY-B	L	.0	350.0	.0	.0	.0	350.0
	*SUB-TOTAL NON-PROJECT		18.5	350.0	.0	.0	.0	368.5
*TOTAL ARGENTINA		544.5	610.0	775.0	950.0	560.0	3439.5	
RESERVE	PA030-GAS DEVT - GDE-C	R	.0	250.0	.0	.0	.0	250.0
	PA027-INDUS CREDIT III-C	R	.0	.0	150.0	.0	.0	150.0
	PA066-YACYRETA II-C	R	.0	.0	150.0	.0	.0	150.0
	PA062-HOUSING FINANCE-D	R	.0	.0	.0	100.0	.0	100.0

LAC REGION, OFFICE OF THE PROGRAM COORDINATOR  
 08/29/86  
 MMC:SELMBA

## BIOGRAPHICAL INFORMATION ON VISITORS

ADOLFO CANITROT (age 55) is the right hand man of Mr. Sourrouille. As Secretary of Economic Coordination, he is second in the hierarchy of the Ministry of Economy. Mr. Canitrot's approach is pragmatic and straightforward; he says what is on his mind. Mr. Canitrot graduated as a Civil Engineer in 1955 and received a Ph.D. in Economics from Stanford in 1965. He has been a Research Fellow with the CEDES (a think-tank in Argentina), consultant to the United Nations, Professor of Macroeconomics at the University of Buenos Aires and Director of the journal "Economic Development" (Buenos Aires). He has collaborated with Minister Sourrouille since the first days of the Alfonsin government. Mr. Canitrot has taken personal responsibility for coordination with the Bank.

JOSE LUIS MACHINEA (age 40), has just been appointed as President of the Central Bank replacing Mr. Concepcion, a long-standing Radical Party member. Mr. Machinea is one of Mr. Sourrouille's closest collaborators; as Undersecretary of Economic Policy, he was responsible for the negotiations with the Fund. Mr. Machinea is a tough negotiator with an open mind and a constructive attitude. He is well-disposed towards the Bank; relations of Bank staff with him are very good. An economist by training, Mr. Machinea received his Ph.D. from the University of Minnesota where he was a student of Mrs. Krueger (1983). He worked with the Central Bank as an analyst and as a Manager of Public Finances and Economic Research from 1974 to 1982. Since 1983 he has been working with Mr. Sourrouille, first in Planning, as Undersecretary of Development Programming, and then in Economy, as Undersecretary of Economic Policy. He is married with two daughters.

MARIO S. BRODERSOHN (age 52) is Secretary of the Treasury. Mr. Brodersohn is one of the very few Radical Party members in the economic team. Mr. Brodersohn is a skillful negotiator; he is articulate and has a quick mind. Mr. Brodersohn has overall responsibility for negotiations with the commercial banks; he is credited for keeping a tight leash on the public budget. Mr. Brodersohn graduated with a degree in Economics from the University of Buenos Aires in 1956 and received a Ph.D. from Harvard in 1965. He has been Director of the Center for Economic Research of the Institute Di Tella, Professor of Economics at the University of Buenos Aires, consultant to the ONU, ILO, OAS and IDB, Visiting Fellow of the Brookings Institute, Research Associate of the University of California. Before moving to the Treasury, Mr. Brodersohn was President of the National Bank of Development (BANADE).

## ARGENTINA

### Biographical Information of Senior Officials

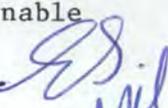
JUAN VITAL SOURROUILLE. Mr. Sourrouille, 46 years old, replaced Mr. Grinspun as the Minister of Economy in February 1985 in response to the rapidly deteriorating economic situation and the ineffectiveness of the policies then being pursued. Although an outsider to the mainstream of the Radical Party, the President chose him as his economic manager to undertake drastic economic reforms which were embodied in the Plan Austral. Mr. Sourrouille operates effectively in a low key fashion, backstaged by a strong economic team. He is reserved, a good analyst who has delegated a good deal of the day-to-day operations to his associates. Considered to be more of a technocrat than a politician, he has nevertheless gained support for his policies within the mainstream of the Radical Party. He is married with three children. Before being appointed Minister of Economy, Mr. Sourrouille was the Secretary of Planning of this Government. A respected academician, the Minister has a long experience in macroeconomics. He was Research Fellow of Harvard University and has worked as a consultant for the World Bank, ILO, IDB and the Economic Commission for Latin America (ECLA). In previous Governments he has served as Undersecretary of Economy and as Director of the National Institute of Statistics and Census. He has written several articles and books on the activities of multinationals in developing countries, development in Argentina and industrial policies. The World Bank published one of his studies, written in collaboration with Oscar Altamir, entitled "Measuring Levels of Living in Latin America: An Overview of Main Problems" (1980).

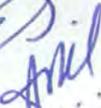
JOSE LUIS MACHINEA. Mr. Machinea, 40 years old, has just been appointed as President of the Central Bank replacing Mr. Concepcion, a long-standing Radical Party member. Mr. Machinea is one of Mr. Sourrouille's closest collaborators; as Undersecretary of Economic Policy, he was responsible for the negotiations with the Fund. Mr. Machinea is a tough negotiator with an open mind and a constructive attitude. He is well-disposed towards the Bank; relations of Bank staff with him are very good. An economist by training, Mr. Machinea received his Ph.D. from the University of Minnesota where he was a student of Mrs. Krueger (1983). He worked with the Central Bank as an analyst and as a Manager of Public Finances and Economic Research from 1974 to 1982. Since 1983 he has been working with Mr. Sourrouille, first in Planning, as Undersecretary of Development Programming, and then in Economy, as Undersecretary of Economic Policy. He is married with two daughters.

## OFFICE MEMORANDUM

**DATE:** August 29, 1986

**TO:** Mr. B. Conable

**THROUGH:** Mr. Stern 

**FROM:** A. David Knox 

**EXT:** 75901

**SUBJECT:** Visit of Argentine Delegation

1. Deputy Economic Minister Adolfo Canitrot, Central Bank President Jose Luis Machinea and Finance Secretary Mario Brodersohn will call on you at 4:00 p.m. on Wednesday, September 3. The visit essentially is of a courtesy nature. The delegation will have met with us over lunch to discuss the Government's medium-term reform program and Bank financial assistance. We shall brief you on the outcome before your meeting with the delegation. The delegation will have talked to Mr. Mulford before the meeting with you; it will see Mr. Volcker and Mr. de Larosiere on Thursday.

2. The visit comes on the heels of a "retreat" of the economic team in which it mapped out strategies for putting the Austral Plan back on track and the change in the management of the Central Bank. The removal of Mr. Concepcion as Central Bank President is a significant development. By overriding a prominent Radical Party member and most loyal political ally, President Alfonsin has given carte blanche to Economy Minister Sourrouille and his technocrats. It is now up to the Minister to demonstrate that it is possible to reactivate the economy with price stability. In order to accomplish this feat, he will have to obtain additional external financing for Argentina.

3. We expect that the delegation will present a new stabilization package and a program of medium-term structural adjustment to the international financial community as a first step to shore up requisite external resources. We understand that the Government's adjustment program is based on the reforms outlined in our Medium-Term Adjustment Paper (MTAP) for Argentina which I had discussed with the authorities back in February of this year. It has taken the administration some time to prepare the political grounds for action programs and to produce a version that has its imprimatur. The MTAP contains concrete proposals for improvements in the incentive system for the private sector and the efficiency of the public sector.

4. We expect that the delegation will focus its presentation on reforms in the trade regime and financial sector; these reforms could constitute the basis for Bank sector loans. In respect of trade reform, the Government is considering to eliminate most restrictions of the temporary admission regime and the taxes on industrial exports, in conjunction with accelerated currency depreciation. A course for the elimination of quantitative import restrictions and their replacement by

tariffs has not yet been decided. This is a very sensitive political issue in view of the disastrous results of a trade liberalization program under one of the previous military regimes. In respect of financial sector reform, the Government has indicated that it would strengthen the supervisory functions and ability of the Central Bank, simplify the regulatory framework, improve the performance of the public banks and promote a restructuring of the private banks. We have told the Government that progress in opening up the economy (Argentina traditionally has pursued inward-looking protectionist policies) and increasing the efficiency of the banking system (average operating costs over deposits are 1.7% per month) are prerequisites for the expected expansion in Bank lending. The proposals of the Government, if acted upon, are promising.

5. Following is a summary of recent economic developments. The Austral Plan, launched in June 1985, is running into difficulties, notwithstanding a good revenue performance (first semester results indicate a fiscal deficit of about 3.5% of GDP) and, until recently, restrictive monetary policies (essentially in line with IMF targets). Inflationary expectations may have been reignited by, inter alia, flexibilization of price controls, recent salary increases, reduction in beef supply and a fall in exports. The parallel exchange market has become more volatile (the premium has gone up as high as 20%). Economic growth continues to be sluggish. It is unlikely that GDP will increase by more than 3% in 1986 (-4.5% in 1985) in spite of a recovery in industrial production, estimated at about 5% during the first semester. Unemployment has increased slightly to 6%. Recent increases notwithstanding, wages are still below 1985 levels. Private investment is declining further from already depressed levels (7% of GDP) and public investment (5% of GDP) cannot be expanded because of fiscal constraints. Following a 14% growth in 1985, exports are expected to decline by 3% this year. The Government has responded by accelerating the crawling peg and extending export promotion programs; it also has offered a tax amnesty for capital repatriation and swaps of public dollar denominated obligations for equity in export industries.

6. A copy of the Bank's Five-Year Lending Program for Argentina and biographical information on the visitors is attached.

Attachments

PRScherrer:md

## LATIN AMERICA AND THE CARIBBEAN REGION

COUNTRY: ARGENTINA  
 OPERATIONS PROGRAM: FY86-90  
 AS OF END JULY 1986

SECTOR			FY86	FY87	FY88	FY89	FY90	TOTAL
AGRICULTURE	PA036-AGR SECTOR-A	L	350.0	.	.	.	.	350.0
	PA065-AG CREDIT II-B	L	.	.	150.0	.	.	150.0
	PA061-AGR SECTOR II	L	.	.	.	350.0	.	350.0
*TOTAL SECTOR AGRICULTURE			350.0	.0	150.0	350.0	.0	850.0
EDUC + PHN	PA064-HEALTH DEV	S	.	.	.	.	40.0	40.0
ENERGY + POWER	PA047-REFINERY SUPP LOAN-A	M	116.0	.	.	.	.	116.0
	PA028-OIL & GAS PRIV-C	L	.	150.0	.	.	.	150.0
	PA042-POWER ENG-B	L	.	14.0	.	.	.	14.0
	PA048-SEGBA V-C	S	.	.	150.0	.	.	150.0
	PA051-PWR DISTRIBUT.-C	L	.	.	.	150.0	.	150.0
*TOTAL SECTOR ENERGY + POWER			116.0	164.0	150.0	150.0	.0	580.0
INDUSTRY + IDF	PA046-SML & MED SCALE IND-	L	.	50.0	.	.	.	50.0
	PA053-EXPORT PROMOTION-D	L	.	.	150.0	.	.	150.0
	PA056-FINAN SCTR LN-D	L	.	.	250.0	.	.	250.0
	PA058-PETROCHEM PRIVATIZ.	L	.	.	.	150.0	.	150.0
	PA055-SOMISA RESTR	L	.	.	.	.	50.0	50.0
	PA049-FINCIAL RSTRUCTURNG-	S	.	.	.	.	300.0	300.0
	PA063-TELECOM TA	S	.	.	.	.	20.0	20.0
*TOTAL SECTOR INDUSTRY + IDF			.0	50.0	400.0	150.0	370.0	970.0
INFRASTRUCTURE	PA025-WATER SUPPLY-A	L	60.0	.	.	.	.	60.0
	PA024-BAHIA BLANCA PORT I-	L	.	46.0	.	.	.	46.0
	PA043-URBAN DEVT-D	L	.	.	75.0	.	.	75.0
	PA044-BAHIA BLANCA II-C	L	.	.	.	150.0	.	150.0
	PA057-WATER SUPPLY II-C	S	.	.	.	150.0	.	150.0
	PA060-TRANSPORT SCTR	S	.	.	.	.	150.0	150.0
*TOTAL SECTOR INFRASTRUCTURE			60.0	46.0	75.0	300.0	150.0	631.0
NON-PROJECT	PA041-T A I-A	L	18.5	.	.	.	.	18.5
	PA050-TRADE POLICY-B	L	.	350.0	.	.	.	350.0
*TOTAL SECTOR NON-PROJECT			18.5	350.0	.0	.0	.0	368.5
*TOTAL COUNTRYNAME ARGENTINA			544.5	610.0	775.0	950.0	560.0	3439.5

## BIOGRAPHICAL INFORMATION ON VISITORS

ADOLFO CANITROT (age 55) is the right hand man of Mr. Sourrouille. As Secretary of Economic Coordination, he is second in the hierarchy of the Ministry of Economy. Mr. Canitrot's approach is pragmatic and straightforward; he says what is on his mind. Mr. Canitrot graduated as a Civil Engineer in 1955 and received a Ph.D. in Economics from Stanford in 1965. He has been a Research Fellow with the CEDES (a think-tank in Argentina), consultant to the United Nations, Professor of Macroeconomics at the University of Buenos Aires and Director of the journal "Economic Development" (Buenos Aires). He has collaborated with Minister Sourrouille since the first days of the Alfonsin government. Mr. Canitrot has taken personal responsibility for coordination with the Bank.

JOSE LUIS MACHINEA (age 40), has just been appointed as President of the Central Bank replacing Mr. Concepcion, a long-standing Radical Party member. Mr. Machinea is one of Mr. Sourrouille's closest collaborators; as Undersecretary of Economic Policy, he was responsible for the negotiations with the Fund. Mr. Machinea is a tough negotiator with an open mind and a constructive attitude. He is well-disposed towards the Bank; relations of Bank staff with him are very good. An economist by training, Mr. Machinea received his Ph.D. from the University of Minnesota where he was a student of Mrs. Krueger (1983). He worked with the Central Bank as an analyst and as a Manager of Public Finances and Economic Research from 1974 to 1982. Since 1983 he has been working with Mr. Sourrouille, first in Planning, as Undersecretary of Development Programming, and then in Economy, as Undersecretary of Economic Policy. He is married with two daughters.

MARIO S. BRODERSOHN (age 52) is Secretary of the Treasury. Mr. Brodersohn is one of the very few Radical Party members in the economic team. Mr. Brodersohn is a skillful negotiator; he is articulate and has a quick mind. Mr. Brodersohn has overall responsibility for negotiations with the commercial banks; he is credited for keeping a tight leash on the public budget. Mr. Brodersohn graduated with a degree in Economics from the University of Buenos Aires in 1956 and received a Ph.D. from Harvard in 1965. He has been Director of the Center for Economic Research of the Institute Di Tella, Professor of Economics at the University of Buenos Aires, consultant to the ONU, ILO, OAS and IDB, Visiting Fellow of the Brookings Institute, Research Associate of the University of California. Before moving to the Treasury, Mr. Brodersohn was President of the National Bank of Development (BANADE).

5. As part of the conditionality for the proposed supplementary loan, we are seeking confirmation from the Government and YPF of their decisions regarding the streamlining and containment of YPF's expenditures for 1986, a more priority-oriented financing plan for balancing YPF's 1986 budget, in conjunction with Treasury contributions, and establishment of a mechanism for Government-Bank review and approval of future work plans and budgets of YPF. In particular, our concerns are that: (a) YPF's investment program for 1986 focuses on containing the extent of YPF's exploration drilling and on production at those oil fields which are consistent with a medium term strategy to maintain the country's petroleum self sufficiency and reasonable reserve levels; (b) YPF adopts measures to reduce investment and operating costs, and would apply sound principles of financial discipline, notably by placing greater emphasis on meeting current financial obligations than the financing of investment; (c) Treasury contributions to YPF's cashflow are timed so as to permit the company to be more prompt in meeting its debt service obligations as well as payments to suppliers and contractors; and that (d) the Government assumes the responsibility for the servicing of YPF's external debt. The Ministry of Economy and YPF have agreed to an arrangement which would meet the last point.

6. In your meeting, we suggest that you express the hope that the arrangements for the proposed supplementary loan will assist YPF to achieve greater financial order and stability for its operations, and that the recapitalization of YPF will help restore its financial viability. It would be very useful also to stress the importance of encouraging the private sector to expand its role in oil and gas activities.

HNissenbaum/Martaza:md

1-21-86

Argentina - when can't  
they comment on  
our people? heading  
towards frontera.  
Mexico - frontera + frontera + frontera etc.  
Trade policy, frontera + frontera etc.  
2<sup>nd</sup> will com. (Bols.)

Canada

Jamaica (medicine  
term frontera).

Rostromil - when the delay?  
conditioned and our  
coming up w/ 2 sectors.

Judge  
Dick

Brazil ★  
Tant fund  
Jamaica  
1-29-86

THE WORLD BANK

Office of the President

January 17, 1986

Tom:

Re your meeting on Tuesday, January 21 at 3:15 p.m. with Jacques, Richard Erb, and Ernie. The idea is to discuss mechanisms to ensure that the country specific medium-term assessments by the Bank and the Fund are reasonably consistent. The hope is that such a mechanism could operate early enough in the process before inconsistent views become cast in cement. The discussion will focus on the work we have underway for Argentina and Mexico.

Ernie is coming in at 2:30 p.m. on Tuesday to discuss your approach to the meeting. Attached is the Argentina Country Study by Shahid's shop (MC discussed it last Monday, January 13). The study for Mexico is not yet finished

Attachment

*Early contacts!  
Don't let too many  
the financial parameters*

*1) what countries?*

*2) audience is the Country Study*

*3) what about medium term*

*4) appropriate - desirable - necessary*

*5) appear on World Economic Outlook*

*How much growth?*

*Domestic Savings!*

*external financing*

*system of*

*things*

# OFFICE MEMORANDUM

For MC Consideration  
Mr. Clausen

Jan. 13/86  
E-1227

OPS/MC86-01

January 7, 1986

CONFIDENTIAL

TO: Members of the Managing Committee

FROM: Ernest Stern, SVPOP *ES*

SUBJECT: Argentina - Baker Initiative Country Study

DECLASSIFIED  
JAN 05 2017  
WBG ARCHIVES

Attached is a paper on Argentina, which spells out the approach to a growth-oriented debt strategy for that country. Based on a 4% rate of growth through 1990 and a reduction in the interest to GNP ratio to 3% by 1992, the paper identifies macro-economic policy actions which are required, as well as the actions in the principal sectors.

The debt service ratio declines gradually but remains high for a decade. Per capita consumption will grow, but slowly, at about 2% after 1989. A base case scenario is also shown. This base case is the continuation of the current stabilization program, not the previous set of policies. Growth is less, the interest/GNP ratio declines more gradually, and per capita consumption grows at less than 1%.

We plan to follow a similar methodology for the other country studies. These are not, of course, plans. They are scenarios for discussion with the government as an input to formulating plans. What it shows, however, is that debt work-outs are feasible while maintaining a reasonable rate of growth, although financial discipline to hold down consumption and accelerate savings will be required for an extended period.

cc: Mr. Southworth

*1-21-86*  
*what are the constraints?*  
*200 vs 300*  
*unbalanced -*  
*T in gamma -*  
*balance*  
*on restricting the*  
*gov. IBCD is more*  
*flexible about that*  
*annex*



CONFIDENTIAL

December 22, 1985

ARGENTINA: BAKER INITIATIVE COUNTRY STUDY

I. Initial Conditions

DECLASSIFIED

JAN 05 2017

WBG ARCHIVES

Economic Performance

1. Argentina's economy has been adversely affected by a poor political milieu and inappropriate economic management since the early 1950s. Over the last decade, abrupt shifts and inconsistencies in policies weakened Argentina's productive capacity and exacerbated structural imbalances. Economic mismanagement led to an increase of the country's external debt, which, as a share of GDP, has multiplied almost seven-fold (from 10% to 67%) during the last decade. Interest payments on the external debt now absorb about 40% of gross domestic savings compared to less than 5% in the early 1970s. While the external debt increased, domestic production declined. In 1985, real GDP per capita was 13% below its 1974 level. Investment declined to 13% of GDP, from an average of 21% during the early seventies.

2. The productive sectors, particularly manufacturing, are beset by thorny structural and financial problems. More than 40% of capacity in the construction industry now stands idle. Significant underutilization of capacity also exists in many manufacturing industries; and most firms also lack sufficient working capital. Financial intermediation is costly and inefficient, interest rates are high in real terms, and oversized banking institutions are suffering severe difficulties. Argentina's self-sufficiency in oil has deteriorated as the ratio of oil reserves to annual output has declined. Proven reserves of gas have increased, but the processing and transport infrastructure to exploit them is deficient.

3. Unfavorable changes in the external environment during 1979-82 further aggravated domestic problems. Argentina suffered external shocks equivalent to 4% of GNP owing primarily to deteriorating terms of trade and high interest rates. This situation was compounded by a deterioration in export competitiveness and a rapid increase in imports as the peso became increasingly overvalued. The policy response was primarily to resort to additional external borrowings. This was accompanied by some contraction of economic activity. The unfavorable external shocks and the poor policy response were further compounded by the South Atlantic war and subsequent political instability.

Stabilization Efforts

4. A democratic Government took office in 1983. The Alfonsin administration confronted a difficult situation: the economy was in poor shape following the 1982 military adventure, inflation was running at close to 20% per month, the fiscal deficit was about 16% of GDP, and the external debt exceeded US\$45 billion. Nevertheless, most social groups greeted the new Government with strong expectations for an improvement in their living standards. The Government first used a gradualist approach to tackle Argentina's problems, but with little success. There was a modest gain in real output led by real wage increases but, in order to finance a seemingly

chronic public sector deficit, the Government was obliged to resort to domestic financing, which produced a steady increase in inflation. The Government entered into a stand-by agreement with the Fund but was unable to meet the agreed targets. As the economy came perilously close to complete chaos, the Government changed gears and moved to shock treatment in mid-June 1985 with the Plan Austral and then reached agreement with the Fund on revised targets.

5. The Plan's main features were: (a) introduction of a temporary wage-price freeze to be supervised through spot-checks. However, before that a number of critical prices were adjusted. These included various public sector prices and an 18% devaluation; (b) a drastic cut in the overall public sector cash deficit, with the purpose of reducing it from 12.5% of GDP in the first half of 1985 to 2.5% in the second half of 1985. This was to be accomplished by increasing tax revenues, reducing real wages, and from falling interest payments resulting from lower inflation. The Government committed itself not to resort to Central Bank credit and to finance the deficit through capital inflows; and (c) a monetary reform introduced a new currency, the Austral, pegged to the U.S. dollar at a fixed rate.

6. The initial results have been impressive: monthly inflation has fallen from about 30% in May to 6% in June and about 2% per month on average during July-November; the overall public sector cash deficit has been cut down to slightly above 3% of GDP in the second half of 1985 without Government recourse to Central Bank credit; the deficit of the current account of the balance of payments has been reduced from 3.5% of GDP in 1984 to an estimated 2% of GDP in 1985. However, the stabilization program is encountering difficulties. First, the Government has been unsuccessful in containing the spending of some public enterprises and provincial governments. Unless additional measures are taken, the public sector deficit will exceed the Fund targets. Second, interest rates, although lower, now stand at 3% per month and discourage private investment. Third, the deficit in the current account of the balance of payments is expected to widen again in 1986, primarily because of continued deteriorating terms of trade and recent floods which have hampered agricultural production.

## II. Objectives of the Medium-Term Program

7. In the design of a program for the medium-term recovery and development of the economy, it is important to recognize that the continuation of the Plan Austral is a necessary precondition for any program. Thus, even a base case scenario will require a continuing series of policy steps building upon and strengthening the program initiated in mid-1985. In laying out the scenarios of the medium-term program, three objectives have been established. First, recovery of Argentina's growth performance to the traditional 4-1/2%. Second, that a modest but steady improvement in real per capita consumption is a necessity for the social and political maintenance of the consensus behind any economic program. Third, that the ratio of debt to exports must be brought down to levels where the normal role of foreign capital in the Argentine economy can be reestablished.

8. Real per capita consumption has been declining for some time and in 1985 was lower than any time in the past 15 years. With interest payments on foreign debt currently absorbing almost 40% of savings and 7% of

GDP, it will be difficult to find much scope for improvements in real consumption. Nevertheless, the base case scenario explores the costs of providing a steady but modest improvement of 1% per year within a 3% real growth rate, while the high case explores the possibilities of accelerating this to 2% per year within the next decade in the context of a 4-1/2% real growth rate. On the external side, the objective is to reduce the burden of debt from its current high ratio of 5 times exports to more manageable, but still high levels of roughly 3 times exports by 1990, with the further objective of approaching ratios significantly below this during the following decade. Finally, it should be emphasized that the magnitude of the difficulties that the economy is currently experiencing is such that the differences between the base case--maintenance of the Plan Austral--and the high case--maximum effort--are fairly small in terms of results until 1989-90.

### III. Implications of the Objectives of the Medium-Term Program

9. In assessing the implications of the objectives of the medium-term program, two key structural characteristics of the economy must be explicitly recognized. First, the economy is a relatively mature one with relatively small increases in population and labor force which, over the past half century, it has never exhibited the high growth rates characteristic of more normal developing countries. Thus, it would be unrealistic to expect growth rates of GDP to exceed 5% over a sustained period, even under conditions of maximum policy efforts. The second factor is the immense size of the external debt, equivalent to two-thirds of GDP and five times the size of exports. Even under the Plan Austral the economy does not generate enough surplus on the balance of payments to cover the interest on its debt. Thus, any program, even under the best of policy conditions, will require net lending to Argentina (either as fresh money or as capitalization of interest) for at least the next 3-4 years.

10. It is also important to point out that in our judgement it is necessary that the Plan Austral, in itself a bold and significant policy effort, be maintained, except for the wage price freeze, which should be phased out during 1986. Thus, we have taken this as our base case rather than setting forth the very dismal scenario that would emerge if we were to extrapolate the performance of the 1980-84 period, which would involve a stagnation in real growth, a continued decline in real per capita consumption, a highly protected and inefficient domestic economy, continued high debt to export ratios, and, in all likelihood, continued political instability. Thus, there is perhaps a less striking difference between our base and high cases than in other countries where similar analyses have been made.

11. Investment in Argentina has in recent years been an extremely low share (13%) of GDP and has been characterized by inefficiency with high ICORs. The program for the future does not call for massive new investments across the board, but rather selective investment in key areas, both public and private, with a focus on increased efficiency. Thus, it is projected that in the base case investment might productively be increased to about 15% of GDP by 1990 and about 17% by 1995 with private sector investment (currently 60% of the total) increasing about twice as fast as

public. In the high case, the ratios to GDP are only slightly higher (16% and 18%) but the ICORs are significantly lower as policy reforms, for example in the energy sector, are implemented allowing a significantly more efficient use of capital stock.

12. Roughly 40% of domestic savings is now being used to pay interest on external debt. Even under the best of policies it is not likely that this can be reduced to less than 20% before 1990. Saving itself, under either scenario, should show a modest improvement in its share of GDP in response to measures to reduce the public sector deficit and encourage private sector savings. The latter could be supported by the financial sector reform as well as by the improved investment climate generated by the policy package.

13. The exchange rate established in the June 1985 measures represented a more than competitive parity for the Austral. While there has been a modest domestic inflation since that time, the currency has not, in the opinion of the IMF, yet moved to a non-competitive position. It is expected, however, that during the period covered by our projection, the authorities will take the required policy measures, including--if necessary--periodic adjustments of the exchange rate in order to maintain the approximate competitiveness of the currency that existed during the latter half of 1985.

14. The key to Argentina's recovery and to the reduction of the heavy debt burden is the performance in the export sector. This is made all the more difficult by the relatively small degree of openness of the economy; exports are currently only 14% of GDP. In addition, the current weak position of the commodities that make up most of Argentina's exports does not augur well for rapid improvements in earnings in the short-run, even with maximum productive efforts by the country itself. Given that beef, wheat, soybeans, and sorghum are key commodities, it is unlikely that after 1985-86 improvement in production there will be more than 2-3% long-run real growth in exports. In the high case, full implementation of our policy recommendations in agriculture, trade, and more importantly in the energy sector, could result in real growth of exports in the 5% range.

15. On the import side the projections imply different assumptions on opening up the economy and, thus, on the share of GDP, given a competitive exchange rate and the phasing out of import restrictions. Under the base case, because of the necessity to have a modest improvement in per capita consumption, total external debt rises until 1992; in the high case this peak takes place until 1990, when the country begins to pay its debt. In the high case, the projection also assumes that there will need to be a significant opening up of the economy, and in particular, an acceleration of the value of capital goods imports, reflecting a capital deepening.

16. External debt, including short term, is currently just under US\$50 billion. The debt service ratio, including short-term interest payments, is currently over 100% of exports. Not only does this debt present a serious impediment to the resumption of normal international financial relations for Argentina, but it also represents a heavy burden on domestic resource mobilization. At the present time, the interest payments on all of Argentina's debt are over US\$5 billion, while the resource surplus on

the trade account is only slightly above US\$3 billion. Thus, not only must exports grow, but efforts need to be made to reduce the size of the debt in relation to the economy. The implication of the current situation is that as there is an insufficient resource surplus to pay interest on the debt at least for the next two to three years, Argentina will have to arrange for lending to cover this requirement. Reschedulings, whether officially or de facto, will be required throughout the rest of the 1980s with the possibility of some potential for repayment of commercial bank lending during the 1990s.

17. The projections are based on the assumption that all debt to commercial banks as of the end of 1985 is serviced on interest with amortization being fully rolled over, and all other debt is fully serviced including all new debt from commercial banks. When the projections reach the point that all such payments can be made without fresh borrowing, the surplus is assumed to accumulate in reserves. At that point four choices will be available to the Argentine authorities by 1992 in the base case and by 1990 in the high case to: (i) repay principal on pre-1986 commercial bank borrowing; (ii) increase imports with a view to accelerating growth; (iii) increase imports so as to improve consumption levels; and (iv) accumulate foreign exchange reserves and earn interest on them. There is no clear-cut case for preferring any one of these alternatives. It is quite probable that increased investment in the Argentine economy, beyond the point where growth is in the 4-1/2% range, would not increase growth further, but rather lead only to increased inefficiency in the use of capital. Repaying the principal of the pre-1986 commercial bank debt is certainly possible, but would only be desirable if it would enhance Argentina's creditworthiness. Increasing reserves is not an end in itself, it simply increases the resources available to be spent and the temptation to spend them on large projects. If higher consumption levels than those projected in the above analysis are politically necessary, then the external resource requirements to effect full recovery will be higher. Finally, the authorities could certainly use the resources to increase consumption even earlier than projected, which while certainly attractive, could lead to increased inflationary pressures on the non-tradeable sectors of the economy. Clearly, the authorities, when the time comes, will utilize a mix of the four alternatives; the point is that this should be done in a careful and balanced fashion. The purpose of the present exercise is to indicate at what point in time such an option might be available rather than to specify exactly what choices should be made. Thus, the choice of repaying debt has been adopted in our projections on a purely notional basis.

V  
↓  
Choices  
N.B.

18. In recent years, Argentina has been characterized by high fiscal deficits and, as stabilization was set in place, by very low ratios of money to GDP--M1 to GDP was as low as 3% and will probably finish 1985 at about 6%. The dilemma facing the authorities is how to increase the availability of money in the economy without raising inflationary pressures. Accordingly, the money expansion must be very modest and in both scenarios we have assumed that the policy packages are consistent with an expansion of the money to GDP ratio to 10% of GDP over the next four years. The fiscal deficit will be very difficult to reduce over the short run given

the high debt servicing burden placed on public finances and the structural problems in state enterprises, particularly YPF (Yacimientos Petroliferos Fiscales). We have thus assumed that the deficit can be reduced to 3% of GDP during 1986, but that in the base case it will fall no further. In the high case the policy reforms, particularly in YPF, should allow a further drop to 2% of GDP, but this, we believe, is a reasonable and attainable long-run structural ratio of the deficit.

#### IV. Policies, Institutions, and Priorities

19. Argentina has the potential to reverse the current recessionary trends in economic activity and gradually achieve respectable growth rates while reducing its debt to exports ratio. Fulfillment of this potential in a high case scenario is predicated on the adoption of comprehensive policy reforms.

NOTE

20. In a first stage, the Government has put into place a comprehensive program to stabilize prices, reduce the fiscal deficit and strengthen the external accounts. The next hurdle that needs to be overcome is the transition from a wage and price freeze (where, in effect, not all prices and wages have been frozen) to a regime of price flexibility. To proceed on this course without once again destabilizing the economy, the Government needs to undertake measures which should permanently reduce the fiscal deficit and avoid using Central Bank credit to finance it, so as to create an environment for breaking medium-term inflationary expectations as it implements a concerted and gradual phasing out of the freeze. Such a phasing out should be done gradually and with sufficient support from producers, retailers and trade unions to avoid a rekindling of inflation.

21. The Government has stated its intention to address the root causes of Argentina's economic woes through comprehensive medium-term program of structural reforms. At the moment though it is still seeking its way, the elements for an integrated program have not yet been put together. It is considering to eliminate most quantitative restrictions on imports and replace them by tariffs. It is also planning to reduce state participation in the industrial and petroleum sectors. Further, it has indicated interest in Bank support for the privatization of its petrochemical holdings in the Fabricaciones Militares complex. However, the Government is moving only slowly in opening up petroleum exploration and exploitation for the private sector; likewise, in telecommunications, it has decided to entrust the expansion of the seriously defective telephone network to a public sector company (ENTEL) that has been unable to operate the existing systems satisfactorily. The Government needs to act on several fronts simultaneously: improve the incentive system for the private sector, define a policy for the public sector, streamline public expenditures, eliminate distortions in the financial sector, and strengthen the infrastructure required to support exports. The following paragraphs summarize our judgment on the relative importance of the policies and measures required to achieve the objectives mentioned above.

22. The Government should give first priority to eliminating export taxes and quantitative import restrictions. As of October 1984, the average import tariff was about 23%. A comprehensive trade policy reform,

including lower rates of effective protection only seems feasible once the economic recovery is well under way. Meanwhile, a gradual process of rationalizing the trade regime should support a concerted major drive to promote industrial exports. We have estimated that such a program, which could be supported by Agricultural Sector, Trade Policy and Export Promotion Loans, could generate incremental foreign exchange earnings of about US\$1.2 billion from agricultural exports and of US\$1.3 billion from industrial exports by 1990; however, this would require new offsetting fiscal measures.

23. Policy reforms in oil and gas are crucial for the high case scenario to materialize. The Government has indicated its intention to allow for a broader role of the private sector, both foreign and local, in the development of Argentina's hydrocarbon resources. However, it has been slow in defining specifics and in taking concrete action. Key among the requirements for the promotion of gas and oil developments are more attractive and stable incentives for the private sector, award of attractive new exploration and exploitation contracts, limitation or elimination of convertibility risk, access to domestic credit (i.e., "apex" financing arrangements) and rationalization of the price structure of hydrocarbon products in line with economic costs. There are also possibilities to enhance the participation of the private sector in the gas transportation and distribution system. We have estimated that Argentina has the potential to export around 70,000-120,000 barrels per day amounting to US\$0.6 to US\$1.0 billion of crude oil/petroleum (at US\$24 per barrel) products by 1990. Moreover, annual investment requirements during 1986-90 of about US\$1 billion for petroleum and US\$0.5 billion for gas cannot be met by the public companies. At the same time YPF is the single major source of the public sector deficit, because it keeps for itself the taxes it collects for the Central Government, since its expenditures are much larger than its revenues. Bank lending in support of rational hydrocarbon development policies could include Refinery, Supplemental Oil and Gas Sector (policy-based), Gas Pipeline and Oil and Gas Private (project financing) Loans.

24. Eliminating the existing distortions which do not allow capital markets to operate efficiently will be a key to stimulating investment for capacity expansion. However, because of the risks of a financial crisis involved in a comprehensive financial sector reform, the needed reform has to proceed in stages. First, real interest rates could be reduced sharply if longer-term inflationary expectations were to be broken. A fall in real interest rates would also become possible by removing present surcharges, shifting the burden of reserve requirements to sight deposits with very low requirements on time deposits, and reducing controls to direct credit. The Government would also need to strengthen the supervisory role of the Banking Superintendency. In particular, the Government should not give preferential treatment to government banks. Second, the Government should initiate a program to restructure the sector through mergers and acquisitions by means of increasing minimum capitalization requirements and temporary fiscal measures to promote consolidation. However, the Government needs to proceed with caution, perhaps first concentrating on public sector banks, particularly the provincial banks that are inefficient and close them down. A proposed Financial Sector Reform Loan has tentatively been included in our program.

25. A framework for reforming the public sector should include the medium-term role of the public sector in the productive areas; namely, to both restructure (oil and gas, railways and telecommunications) and privatize public sector enterprises (petrochemicals and steel). Moreover, its share of public sector investment in total investment should gradually decrease. The public sector should not have preferential access to credit. Budgetary policy should be such that only transfers for equity take place and that operating losses of enterprises or the public banks not be financed by either the Central Bank or the budget, except on a temporary basis. At the same time, the public sector should have freedom to set its prices within certain regulatory limits for monopolistic services. Finally, enterprises should be managed as commercial entities, including policies over wages, recruitment and dismissals. A proposed Technical Assistance Loan would assist in formulating the above framework.

26. In the context of implementing the reform of the public sector, the Government also has to place emphasis on reorganizing its own house. The thrust of this effort should be to reduce public sector employment (through attrition) and to improve the efficiency of public sector enterprises including adequate cost recovery policies. Analytical work to improve the efficiency of public enterprises [especially YPF, ENTEL, Railways, SOMISA (steel)] has been initiated. Preliminary results indicate that restructuring (technical, financial and organizational/management) of these enterprises could lead to major gains in their efficiency and competitiveness, while at the same time strengthening public sector finances. The Bank could support restructuring, which would be a lengthy and difficult endeavor through sector loans in transport, energy and enterprise specific loans for SOMISA and ENTEL.

27. Similarly, the Government will need to prepare and review carefully the priorities of a medium-term public investment program. Our recent review of a preliminary investment program has indicated the following priorities in the transport and energy sectors, which account for about half of public sector investment: (i) improvement of port services; (ii) reconstruction/maintenance/graveling of high-traffic roads; building of feeder roads for the main export corridors; (iii) enhanced oil recovery/liquid extraction and gas gathering projects, acceleration of oil and gas pipeline construction; (iv) reinforcement of power transmission/distribution lines. The Government has to strike a better balance between new investment and maintenance; to introduce uniform investment criteria; define priority projects; and establish a central review for all public investment projects. In this connection, a central project processing/monitoring unit would go a long way in helping to implement the criteria and investment priorities that are agreed upon. As regards investment financing, improvements in tax administration and rationalization of public tariffs should be undertaken simultaneously with the elimination of earmarked funding (special funds) which are not conducive to efficient resource allocation. The Bank could support government efforts in this context through Technical Assistance, Bahia Blanca Ports I/II, Yacyreta supplemental, Power Distribution and Transport Sector Loans.

## V. Scenarios

28. This section is a description of the type of evolution of the economy that we expect to see under the two different policy scenarios. The differences in the scenarios are essentially a matter of degree in timing and intensity of implementation of policy reforms, which would condition, again as a matter of degree, a return of confidence and, consequently, direct private investment (both domestic and foreign). As was pointed out earlier, the base case requires the maintenance of the Plan Austral and thus needs a significant degree of continued policy action on the part of the authorities. As noted, a true base case would imply a return to the chaotic and disastrous policies of the early 1980's and would be characterized by escalating debt, high inflation, declining per capita consumption, and stagnant GDP. The Plan Austral represents a bold repudiation of these policies on the part of the Argentine people and an implicit assertion that the Plan, even with its present and future sacrifices represents a minimum acceptable state of the economy.

29. The central sequence of policy actions and responses in the economy centers on the necessity at first on increasing exports as rapidly as possible so as to address the overriding balance of payments and debt constraints. Thus the policies in the immediate future are aimed at exportables and at the incentives to export. As the economy has a moderate degree of unutilized capacity in most sectors, the initial thrust will be on pricing. To this end the agriculture policies are directed at a reduction in export taxes and a reformation of credit policies. Similarly in the manufacturing sector where trade policy reform is an early priority. In both these sectors there is enough capacity that it will be several years before new investments need come on stream. In order to effect this however, it will be necessary for a reform of the financial sector to have taken place, ideally by early 1987, so as to lower the real cost of capital to investors while simultaneously increasing the incentives to savers. A second key to the recovery will be the oil and gas sector. Here the country has a substantial potential, not only for natural gas, but also for petroleum. In the short-run the issues can best be addressed by the encouragement of the private sector in the industry, by allowing the private sector into the exploration and development phases, by reducing part of YPF's investment program (drilling and exploitation) and giving the private sector the responsibility to undertake it, and by encouraging technical developments in the extraction of existing wells. Finally, there are issues that affect the fiscal strength of the country including an early start on attaining adequate pricing in natural gas, power, and water and sewerage, improved planning, the scaling down of the public investment program, and monitoring of public sector investment. This latter program should not only be aimed at allowing the private sector greater participation in productive sectors, but also in focussing the investment of the public sector in key infrastructural areas (such as ports and transport corridors).

30. In the high case scenario, a very significant policy measure concerns the building of gas pipelines and this requires an early settlement of the COGASCO issue. This policy initiative will allow a dramatic change in the energy accounts of the balance of payments, by allowing the gas associated with petroleum deposits to be taken off and thus allowing a substantial increase in petroleum output. In addition this scenario will

require high levels of private investment in the sector. In both cases, it would be necessary to improve extraction from existing wells, private sector participation in exploration and development and moderate private sector investment. In the agricultural sector, while the base case would only envision export taxes being dropped to the May 1985 level, the high case would phase out most of them and would focus on public investment in the transport infrastructure between the producing areas and the ports. In the trade field, the base case will require policy actions. The high case assumes a significant opening up of the economy and may require further improvements in the competitiveness of the exchange rate, but will certainly require coherent and stepped-up efforts on export promotion and improved management and recapitalization of enterprises. In the base case scenario, adequate pricing policies will be required in the power sector. In the high case scenario, the power sector will require expanding the transmission and distribution network and the completion of ongoing power generation projects (including Yacyreta) based on adequately projected demand requirements. Finally the distinguishing characteristic of the high case scenario will be the expanded and enhanced role that the private sector must play in the economy. Private investment must double in real terms within the next seven years. This can only take place with a coherent and productive environment for the private sector coupled with an efficient financial system.

## VI. Action Program

31. The policy reform proposals included in the high case scenario should be implemented on the basis of annual action programs. This section outlines in detail the annual action program for 1986. A summary of the annual action programs for 1987-90 is outlined in the attached Policy Matrix (Annex I). These of course would be reviewed and modified to take into account the results of the implementation of each annual action program and changes in the external environment. Discussion of the policy requirements under the base and high case scenarios for 1986-90 is included in Section V above. A summary discussion of sector policies is included in the attached Sector Policies (Annex II).

### 1986 Action Program

32. The 1986 program would focus on: (a) agreement on a medium-term macroeconomic program; (b) preparation of a medium-term public sector investment and financing plan and external borrowing programs; (c) adoption of revenue and expenditure measures required to meet the targets under the Government's stabilization program; (d) gradual phase-out of the wage and price freeze; (e) exchange rate measures to maintain Argentina's international competitiveness as required; (f) improvement of the effective exchange rate in agriculture; (g) gradual elimination of about half of all import prohibitions and quantitative restrictions; (h) improving the administrative mechanisms of trade management; (i) facilitate financing for exports; (j) initiate support of export services as part of export promotion; (k) initiate reforms in the financial sector, and (l) introduce measures which will produce a structural reform in the operation of enterprises in the energy sector. More specifically, this would require the implementation of a number of sectoral actions.

33. Agriculture: (i) removal of the temporary increases in export taxes imposed in June 1985 (see para. 36 for offsetting revenues); (ii) removal of the temporary increases in import tariffs on agricultural inputs imposed in June 1985 and redesignation of tractors and agricultural machinery from the "prohibited" to the "free" classification for imported goods; and (v) initiation of studies to promote exports and improve efficiency in the sector.

34. Trade: (i) import liberalization through the elimination of most import licensing requirements: (a) reclassification of about 50% (2,000) tariff positions from prohibited to free and partial replacement by tariffs; and (b) reclassification of about 50% (650) tariff positions from prior consultation to free and partial replacement by tariffs; (ii) achievement of free trade status for export industries, through the reform of the temporary admission regime for imported inputs, along the following lines: (a) simplification of administrative procedures; (b) guarantee of automatic access for any products; (c) coverage of indirect exporters; (d) extension to capital goods used for export production; and (e) extension of the tax reimbursement scheme to exports processed under the temporary admission regime; (iii) simplification of export procedures, eliminating all unnecessary interventions by public sector agencies; and (iv) preparation of terms of reference for studies needed to support the adjustment process: (a) study of tariff protection with a view to actions that will reduce tariff dispersion; and (b) study on the indirect tax content of exports, with a view to actions to rationalize the system of tax rebates to exports, as well as strengthening it vis-a-vis trading partners that might be tempted to impose countervailing duties; (v) removal of the exclusive linkage of pre-shipment financing with dollar-indexed or dollar deposits; (vi) facilitate financing (pre- and post-shipment) by banks; and (vii) develop a common integrated data base on markets and products for exporters.

35. Financial System: (i) lowering reserve requirements; (ii) reduce controls to direct credit; (iii) preparing a program for rebuilding of the financial sector; and (iv) strengthen the supervisory role of the Banking Superintendency.

#### Public Sector

36. Fiscal System: (i) identification of alternative sources of fiscal revenues and taking appropriate measures as needed to maintain the fiscal deficit at levels commensurate with the ceilings of the Government's stabilization program (estimated at about 3% of GDP for 1986); (ii) satisfactory progress on a program for preparation and implementation of federal land tax; and (iii) tax administration: (a) initiate the improvement of information flow by unification of taxpayer identification for each separate tax collecting entity; phase out expensive visit system in favor of distribution of information on cross-compliance; increase penalties for evasion; and concentrate audit efforts on VAT; (b) eliminate tax amnesties; and (c) focus excise tax collection on commodities where the Government has direct control over the collection.

37. Public Enterprises: (i) decision to restructure and privatize; (ii) initiate reduction of employment through attrition; (iii) introduce

managerial accountability and cost accounting; (iv) initiate real tariff increases in electricity and water supply enterprises; (v) minimize coal investments; (vi) postpone major hydroelectric projects (Yacyreta); (vii) cancel the expansion of the petrochemical production capacity in Bahia Blanca, of the SOMISA new sheet steel rolling mill and the shipyards expansion; and (viii) establish clear criteria for public enterprise management on a commercial basis.

38. Energy: (i) reduction of YPF budget deficit (from projected US\$1.1 billion to US\$0.4 million) through: (a) cuts in the investment program. Cut proposed program of US\$1 billion to US\$600 million (with the private sector undertaking these investments) by reducing exploration and production activity from a proposed 130 exploration and 850 production wells to 50 exploration and 250 production wells, focussing on high-yielding fields and secondary recovery projects making maximum use of existing shut-in wells and well repairs. New oil production contracts with private companies would supplement YPF's production efforts. Continue infrastructure investment, mainly refinery conversion, which should be completed on time and could not be farmed out to the private sector at this stage; (b) cuts in the operating budget. Establish action plan to achieve operating cost reductions estimated at about US\$0.3 billion through savings due to reduced drilling activity (US\$0.2 billion) and efficiency improvements (US\$0.1 billion); and (c) introducing a monitoring mechanism. Establish independent monitoring body reporting to the Ministry of Economy which supervises YPF's budget programs on a continuous base and approves/countersigns major decisions/expenditures; (ii) private sector oil exploration and production: (a) new private oil production contracts. Establish action plan to farm out explored areas to local and foreign oil companies under production contracts. Achievable private sector investment estimated at US\$200-300 million annually; (b) private oil exploration contracts. Complete first bidding round for 32 areas (of 164 already defined areas) for new risk contracts by February 1986. Complete second round for another 30 areas during 1986. Estimated investment possibilities: about US\$200 million annually once drilling phase of awarded contracts starts; and (c) financing of private sector operations. Allow export of crude oil or petroleum products for limited recourse financing schemes. Improve disbursement procedures for World Bank funds managed by BANADE. Utilize IFC funds as matching funds to mobilize additional on-lending loans from commercial banks; (iii) YPF organization improvement: (a) Establish action plan to implement accounting and financial management systems to allow cost control by activity and clarify accountability of YPF managers; and (b) institute a high-level government committee to prepare options and approaches to restructure YPF and to introduce workable competition in the petroleum sector; (iv) gas sector: (a) begin Northern Pipeline expansion with clear schedules and budget provisions; (b) prepare transmission pipeline expansion program (Central West and new Western Pipeline); (c) resolve the COGASCO dispute in 1986; and (d) introduce new financing schemes such as limited resource financing guaranteed by petroleum export revenues; and (v) power sector: continuation of real tariff increases.

39. Water and Sewerage: Continuation of real tariff increases.

VII. Difficulties in Implementing Policy Reform

40. The proposed policy reform program outlined in the preceding sections constitutes a major task. With the exception of privatization, the proposed policy reforms in the agriculture, trade, energy and financial sectors are necessary for the high case scenario to become viable.

41. The reform of agricultural sector policies will be criticized by the conservative agricultural producers who are dead set against a land tax. Within the Government, at a time of great fiscal stringency, the Secretary of the Treasury is justifiably uneasy about the elimination of taxes that are very easy to collect (export taxes) and their replacement by a new tax that may prove harder to collect (the land tax).

42. Trade policy reform is an extremely sensitive area. The previous import liberalization attempt was a bitter disappointment: entire industries disappeared, industrial employment declined in absolute terms, and small and medium scale industries were particularly hard-hit; and the country had nothing to show for it. Thus, any effort perceived as reviving the "Martinez de Hoz policies" would be doomed to failure now. For this reason, the proposed program of policy reforms focuses on achieving free trade status for export industries, shying away from a comprehensive tariff reform that would decrease the already low average effective protection and its dispersion. This would be a way of maintaining the dialogue open on an issue whose sensitivity might diminish in a few years. Proceeding differently--that is to say, raising the issue of decreases in average effective protection at this point--would be extremely counterproductive. Business and labour leaders would present a united opposition front. The better investment climate that the Government is painfully trying to reconstruct would deteriorate sharply and the Bank's policy dialogue would be seriously jeopardized. Yet it must be recognized that so long as the import regime remains restrictive, additional external financing under the Baker proposal or repatriation of Argentine assets now held abroad might have inflationary consequences.

43. The major reforms proposed in the energy sector are likely to provoke opposition from several sectors. Drilling contractors which now execute about half of YPF's annual drilling program, will vehemently oppose any cuts that jeopardize their service contracts. This would be supported by provincial governments in oil-rich areas if reduced state production activity resulted in a loss of royalty payments and reduced employment of workers in the oil service industries. These concerns could be addressed by awarding a substantial amount of production contracts to private sector firms, which would shift risk and financing burdens to the private sector. In particular, foreign firms would be able to service capital more easily and could improve production efficiency more quickly than local firms. Moreover, any privatization of oil production, introduction of more competition or the restructuring of YPF, are likely to encounter resistance from YPF's management, unions, and political forces within the Radical Party (traditionally supporting public sector dominance of oil and gas activity). This could be addressed by the creation of new private sector jobs through the increase in private sector activity and by improving performance incentives within YPF. Basically, however, these groups will have to be convinced that the proposed policy reforms will

improve the Government's fiscal deficit and the balance of payments prospects.

44. The reforms proposed in the transport sector will receive strong opposition from the Transport Secretariat (within the Ministry of Public Works and Services) which does not concur with policy recommendations originating from development institutions. In addition, major changes in the railways will be difficult, given that these inevitably will require a massive reduction in personnel.

45. Financial sector reform is likely to be resisted by the owners and managers of those financial institutions that are least likely to survive and by the public sector-owned provincial banks. Since restructuring will unavoidably imply the closing down of some institutions and branches, it must be expected that, the banks' employees unions will agitate to defend their members' jobs. Pressure will be applied on the Government to absorb the redundant employees (about 30,000) which it will not be in a position to employ.

46. Privatization efforts in all sectors are likely to be resisted, even by some groups within the Radical Party. The issue is complicated, moreover, by the administration's reluctance to antagonize the armed forces unduly, and the fact that some of the more obvious privatization cases are the Defense Ministry's steel and petrochemicals industries. Even in the event that privatization could take place, the availability of buyers and lack of financing could pose a serious constraint to divestiture.

#### VIII. Monitoring of Policies

47. The Bank would follow the Colombian model to monitor the progress of the Government's medium-term program. However, different from the Colombian case, we would expect that the Government enter into formal standby agreements with the Fund. Such monitoring would be implemented through yearly assessments of a medium-term macroeconomic and public sector investment programs. This would include the adoption and direction of policies to ensure the programs' future viability. Consideration of policy based loans which would include specific agreements on agricultural, trade, energy and financial sector policies and public sector reforms, and on a successful implementation of the above mentioned programs. We would push to reach an agreement with the Government on the above before we present a proposed Trade Policy Loan to the Board. We would also include in the programs specific agreements on the adjustments of prices of public utilities to appropriate levels, together with corrective actions on the overall economic program as required, and actions to increase the role of the private versus the public sector, including foreign investment. On the basis of the above, we would undertake regular supervisory exchange of views with the Government. The Bank's yearly assessment of the macroeconomic program would take into account the IMF's review of its stand-by agreement with the country, particularly as it relates to targets on net international reserves, the fiscal deficit, total credit of the Central Bank, net credit of the Central Bank to the public sector and the level of public sector debt on a quarterly basis. The Bank's overall assessment would incorporate the IMF's view on progress with respect to achieving and

maintaining export competitiveness in the current stand-by, and in subsequent ones, to be negotiated once the current one expires in March, 1986. As part of this process, we will propose to the Government that it prepare and send to the Bank two reports on a yearly basis, summarizing the status of implementation of the medium-term program to be agreed with the Government. The first status report would also serve as a basis for a mid-term review. These reviews would also form the basis for the release of the tranching under new policy based lending.

#### IX. Stabilization: Relationship with the IMF

48. The principal aim of our relationship with the Fund will be to develop an operationally effective understanding before their next stand-by negotiation (March 1986). The purpose of the proposed relationship will be to: (a) agree on a medium-term framework necessary for the country to become creditworthy and resume real economic growth; (b) agree on a stabilization approach that is compatible with growth objectives; (c) receive their input and support to ensure that the Government's medium-term investment program will be financially viable; (d) define the respective roles in monitoring; and (e) incorporate the IMF's view in progress with respect to stabilization and maintenance of export competitiveness in the Bank's overall assessment of the adequacy of the Government's medium-term macroeconomic program. Consistency between stabilization and medium-term growth will be essential, and thus the Bank's and Fund's programs should be worked out concurrently. The IMF would be responsible for the stabilization aspects of the medium-term program; the Bank would be responsible for the growth and efficiency aspects (Section VIII above). Continuous consultations would take place to ensure that stabilization and growth objectives are compatible with each other. In this connection, Fund/Bank consultations would also focus on the stabilization issues to be covered by Fund missions and on the issues which Bank economic missions and policy based lending operations would cover. The Fund's expertise in the fiscal area would be sought to complement our analyses regarding the introduction of new taxes in our policy based lending and for the supervision of the tax policy and tax administration activities in the proposed Technical Assistance Loan.

#### X. Financing Requirements

49. Given the above objectives, policies, and constraints, it is estimated that between 1985 and 1990, even with the best achievable policy package, the Argentine economy will require net flows (excluding IMF and direct foreign investment) of some US\$8.7 billion, the bulk of which would have to be concentrated in the 1985-87 period. With the more modest policy package the flows would be more in the range of US\$9.5 billion. It is envisioned that this would require gross disbursements of about US\$18 billion and commitments of about US\$14-15 billion in either case. The Argentine economy itself has not been characterized as one with large trade deficits. The country's indebtedness increased during 1979-82, mainly because of a misguided policy experiment which was followed by a huge capital flight and because of an unfortunate military action. For this

reason Argentina may develop the capability to repay its external debt if policies appropriate to fully utilize the country's potential are implemented, provided the Government does not opt for substantially higher consumption levels. In the base case, longer maturities for fresh money from the commercial banks would be required as compared with the high case where such borrowings could be repaid over a shorter period of time. In the base case, some 60% of the net flows would have to come from the commercial banks, concentrated mainly in the early years of the program. In the high case, the commercial banks' share would be somewhat lower (about 50%) as the potential to service the debt fully would appear sooner (1988 as compared the base case (1990)). World Bank commitments for 1986 would amount to about US\$630 million in both cases, since the level of commitments would be significantly firmed-up. From 1987 onwards, commitments would average US\$500 million per year in the base case; and in the high case, US\$800 million in 1987 and US\$900 million per year during 1988-90. In the base case the World Bank share of debt outstanding and disbursed would be under 4% while in the high case, the World Bank share would go up to 5%.

ARGENTINA - PROPOSED MEDIUM-TERM ADJUSTMENT AND GROWTH PROGRAM

High-Case Scenario

- Main Goals: (1) To restore and sustain real economic growth of 4% on average during 1986-90, and 4.4% during 1991-95.  
 (2) To expand exports in real terms by 5.4% on average during 1986-90.  
 (3) To maintain a sound balance of payments position, consistent with a reduction in the debt to exports ratio from 5% in 1985 to 3% in 1990.

Note: \* indicates actions to be implemented in one year; — indicates actions covering several years.

Area	Policy Objectives	Recent Actions Taken by Government	Further Measures Recommended	Proposed Timing				
				1986	87	88	89	90
<b>A. TRADE, INDUSTRY AND AGRICULTURE</b>								
1. Exchange Rate Policy	Maintain international competitiveness	Crawling peg devaluations during first half of 1985; 18% devaluation in June 1985; continuing depreciation of the real exchange rate vis-a-vis major trade partners	Maintenance of competitive exchange rate policy through periodic adjustments which are equal to the difference between domestic and international inflation.	—	—	—	—	—
	Improve the effective exchange rate in agriculture	Export tax on wheat reduced from 26.5% to 15% (September 1985); smaller reductions in other commodities	Phased reduction of export taxes on agricultural commodities by 1988 to no more than 50% of the rate in force on May 1, 1985; by 1990 to 5% of agricultural exports; and by 1991 complete elimination.	—	—	—	—	—
	Improve the effective exchange rate in industry	Export taxes on agroindustrial exports eliminated (August 1985)	Full rebates on direct and indirect taxes paid by exporters.					*
2. Import/Export Regime	Eliminate prohibitions and quantitative restrictions		Phased elimination of most import licensing requirements: (i) reclassification of 4,000 (100%) tariff positions from prohibited to free list and partial replacement by tariffs (ii) reclassification of 1,300 (100%) tariff positions from prior approval to free list and partial replacement by tariffs (iii) redesignation of tractors and agricultural machinery from the prohibited to free list.	—	—	—	—	*

Area	Policy Objectives	Recent Actions Taken by Government	Further Measures Recommended	Proposed Timing				
				1986	87	88	89	90
3. Export Incentives	Provide inputs for exporters at world prices  Reduction of import tariffs  Improve the administrative mechanism of trade management  Provide export support services and adequate and timely information		Reform of the temporary admission regime for imported inputs:					
			(i) guarantee of automatic access to any input;					*
			(ii) gradual coverage of first-line suppliers of exporters;					*
			(iii) gradual extension to capital goods used for export production					*
			Removal of the temporary increases in import tariffs on agricultural inputs imposed in June 1985					*
			Preparation of studies needed (i) to rationalize the import tariff structure					—
			(ii) to rationalize the structure of tax rebates for exports					—
		Implementation of recommendations of above studies					—	
		Simplification of export procedures, unification of agencies authorized to review and approve export applications					—	
		Formation of a joint organization to provide institutional support for marketing, storage, quality guarantee, legal assistance, lobby. Development of an integrated data base.					—	
4. Export Financing	Expand available resources		Removal of the exclusive linkage of pre-shipment financing with dollar-indexed or dollar deposits; and encouragement of joint financing by banks					*
			Review the level of financing subsidies.					—

Area	Policy Objectives	Recent Actions Taken by Government	Further Measures Recommended	Proposed Timing					
				1986	87	88	89	90	
			Allowance of export plans by firms as a basis to determine the amount of Central Bank credit lines for financing.						*
			Broadening risk coverage of exporting firms.						*
5. Agricultural marketing	Provide marketing infrastructure		Provision of market places and information for non-traditional agricultural products.						—
	Expand transport and storage facilities		Promotion of private sector participation.						—
6. Agricultural Credit	Financing increases in production.		Increase availability of short- and long-term credit.						*
<b>B. FINANCIAL SYSTEM</b>									
1. Interest Rates	Reduce real costs of financing for investments.		Lowering reserve requirements on time deposits and sight deposits.						—
2. Sector Restructuring	Create a healthier financial sector.		Increasing minimum capital requirements for financial institutions.						—
			Temporary stock purchasing to facilitate adjustment and consolidation.						—
			Institutionalization of deposit and employment insurance systems.						—
			Prepare a program for rebuilding of the financial sector.						*
			Removal of the 2% ISSBE (Institute of Social Services for Bank employees) surcharge and its coverage by alternate fiscal measures.						*
			Removal of the ORM (a device to reallocate differential reserve requirements).						*
			Elimination of credit subsidies.						*
			Reduce controls to direct credit.						*
			Strengthen the supervisory role of the Banking Superintendency.						*

Area	Policy Objectives	Recent Actions Taken by Government	Further Measures Recommended	Proposed Timing				
				1986	87	88	89	90
<b>C. FISCAL SYSTEM</b>								
1. Tax Structure	Broaden the corporate tax base	Inclusion of rural properties to capital gains tax	Include profits on the sale of property					*
	Improve the buoyancy of tax system, shift the burden to direct taxation		Elimination of most industrial incentive exemptions from VAT.					—
			Focusing excise taxes on commodities where Government has direct control over the collection				*	
	Eliminate anti-export bias of the tax system		Introducing a federal land tax as export taxes are phased out					*
2. Tax Administration	Improve the effectiveness of tax administration		Unification of tax payer identification for each separate tax collecting entity					—
			Phasing out expensive visit system in favor of distribution of information on cross-compliance					—
			Increased penalties for evasion and tax delinquency					—
			Concentrating audit efforts on VAT					—
			Elimination of tax amnesties					

Area	Policy Objectives	Recent Actions Taken by Government	Further Measures Recommended	Proposed Timing					
				1986	87	88	89	90	
<b>D. PUBLIC SECTOR</b>									
1. Central Govt., Public Enterprises and Investment	Definition of medium-term public/private sector roles		Decision to restructure and privatize public enterprises.	*					
	Improve efficiency of operations	A commission for the privatization of a group of public enterprises has been established.	Establish clear criteria for public enterprise management on a commercial basis.	*					
	Eliminate bottlenecks constraining trade expansion	A set of studies to guide public sector reform has been initiated.	Reduction of public employment through attrition.				_____		
			Wage differentiation and productivity bonuses.				_____		
			Introduction of managerial accountability and cost accounting.				_____		
	Phase-out public sector investment in non priority areas		Phasing out the production of goods and service lines.				_____		
			Phasing divestiture of those enterprises that are not producing a true public good and/or service.				_____		
		Elimination of budgetary support to enterprises and of preferential credit.				_____			

Area	Policy Objectives	Recent Actions Taken by Government	Further Measures Recommended	Proposed Timing				
				1986	87	88	89	90
2. Energy Sector	Mobilize and allocate resources to priority investments	National Development Council (CONADE) was reestablished to redirect public investment	Elimination of earmarked funds for non-priority projects.			*		
			Allocating to enterprises a higher percentage of tariffs paid by users, as the Treasury rebuilds its own revenue sources; continuation of real increases in water and electricity tariff revenues; and preparation of a medium-term public sector investment program and financing plan and external borrowing program.					
	Better use of energy resources	Major cuts and postponements in several energy projects	Government decision on the expansion of the gas transportation system through private participation Solution of the COGASCO dispute.			*		
	Enhance the private sector's role and improvement of oil export possibilities	A five-year investment program for the sector is being prepared	Award new exploitation and exploration contracts for oil and gas to private firms.			*		

Area	Policy Objectives	Recent Actions Taken by Government	Further Measures Recommended	Proposed Timing				
				1986	87	88	89	90
			Provision of safeguards against the risks of convertibility for foreign investors.	*				
	Improve the operations of state oil and gas companies		Reduction of investment and operating costs, financial strengthening and streamlining of organizational structures, accounting and control systems, preparation of the restructuring options for YPF.		_____			
	Mobilize potential financial resources		Adjustment of the price of natural gas taking its long run opportunity cost as a guide.		_____			
	Promote energy conservation		Adjustment of the price of diesel as a function of the gasoline price, preparation of the deregulation of oil and petroleum products.	*			_____	
			Design and implementation of an energy conservation program including price and taxation aspects.				_____	
			Reviews of the energy efficiency of the power sector and of the possibilities for conversion and savings.				_____	
			Minimization of coal investments and postponement of major hydroelectricity projects.	*				

Area	Policy Objectives	Recent Actions Taken by Government	Further Measures Recommended	Proposed Timing				
				1986	87	88	89	90
3. Transport Sector	Reduce deficits  Provide adequate facilities for export trade		Assurance of adequate cost recovery in ports, channel dredging, and railroads and the introduction of road user charges.	—	—	—	—	—
			Strengthening of transport planning and intermodal coordination.	—	—	—	—	—
			Consolidation of agencies working in the same sector.	—	—	—	—	—
			Railways: Overhauling company, cutting uneconomic lines, providing bulk freight, improving maintenance, elimination of electrification schemes.	—	—	—	—	—
			Highways: Better maintenance of main traffic corridors, concentration on feeder roads with higher traffic.	—	—	—	—	—
			Ports and Maritime Transport: Deregulation of offshore storage/shipping, containerization, tugboat services.	*	—	—	—	—
4. Restructuring	Restructuring to improve efficiency and competitiveness of basic industries		SOMISA: cut costs, balance production lines and strengthen management/administrative practices.	—	—	—	—	—
			ENTEL: improve operation and managerial efficiency.	—	—	—	—	—
5. Privatization	Programs for privatization of public enterprises		Petrochemicals: (i) identify potential investors;	—	—	—	—	—
			(ii) negotiate the sale price value of assets;	—	—	—	—	
			(iii) define the vehicle of transfer of assets to private investors.	—	—	—	—	

SECTOR POLICIES

1. This section identifies the major sectoral features that are necessary for policy reform to resume and sustain medium-term growth in Argentina. The purpose of the policy framework is to identify factors that have constrained growth, define policy objectives to eliminate such constraints, recommend specific policy changes, and indicate the possible effects of the proposed policy changes.

2. There are two major constraints for the resumption of sustained growth in Argentina: (a) the underlying distortions in the economy and (b) the inefficiencies in the operation of the public sector. Elimination of these constraints requires improving the incentives system necessary for a more intensive use of resources to increase production and exports, and undertaking a series of actions to improve the efficiency of the public sector. Carrying out these tasks will require the removal of distortions in the trade regime, the phase-out of the price freeze, restoration of domestic financial markets, the strengthening of the tax system and an overall improvement of the machinery of government, notably, sound public investment screening mechanisms, requiring public enterprises to operate like commercial entities, and defining an adequate framework for an expanded private sector role. Thus, this section is divided into two parts. Part I deals with the incentives system necessary for the resumption of growth and focusses on the elimination of distortions, reformation of domestic financial markets, and increasing the effectiveness of the tax system. Part II deals with improving the efficiency of the public sector, and focusses on the public sector investment program, with special emphasis on the energy and transport sectors which comprise over half of the public sector investment program. It also examines the possibilities of restructuring and privatization of public sector industrial enterprises as a means to help reduce the Government's financial burden and public sector deficits, and to increase industrial efficiency, competitiveness and exports.

I. IMPROVING THE INCENTIVES SYSTEM

AGRICULTURE

A. Analysis

3. The agricultural sector has been growing below potential as a result of pricing policies that have: (a) depressed domestic prices for outputs through export taxes; and (b) artificially raised the costs of some key farm inputs through import tariffs and quantitative restrictions. As a consequence, most farmers have opted for low-risk; lower-input technologies which led to a significant underutilization of production and export potential. Also, the inadequacy of transport, storage, information and marketing facilities has raised the final costs of agricultural products and discouraged the production of new commodities.

4. The total agricultural sector credit portfolio in each of the last few years has been less than 50% of the portfolio registered in 1980. The economic uncertainty has negatively affected the demand for investment credit. In the case of short-term production credit, inadequate supply by the Banco de la Nacion and provincial banks has been a constraining factor. The Government's stabilization program has restricted credit further. Yet, maintenance of the growth of the agricultural sector will require substantial increases in both production and investment credit.

5. Policy objectives in agriculture should focus on: (a) reducing export taxes on agricultural products, providing alternative sources of fiscal revenue to compensate for the export tax reduction so as to maintain the overall fiscal deficit at satisfactory levels; (b) rationalizing import laws and regulations on agricultural inputs, (c) strengthening marketing efforts; and (d) providing sufficient credit resources to the sector.

#### B. Policy Recommendations

6. Specific changes recommended include:

- (a) phased reduction of export taxes on agricultural commodities. The timetable of such an export tax reduction should include by: (i) January 1986, the removal of temporary increases imposed in June 1985; (ii) end-1986, the reduction of export taxes to no more than 70% of the rates in force on May 1, 1985; (iii) January 1988, the reduction of export taxes to no more than 50% of the rates in force on May 1, 1985; (iv) January 1990, the reduction of export taxes to 5% of the FOB value of agricultural exports; and (v) January 1991, complete elimination;
- (b) introduction of a federal land tax and of alternative tax provisions to compensate for the revenue losses resulting from the export tax reduction program;
- (c) removal of the temporary increases in import tariffs on agricultural inputs imposed in June 1985;
- (d) redesignation of tractors and agricultural machinery from the "prohibited" to the free imported;
- (e) marketing policies should be geared to: (i) promote the participation of the private sector, especially cooperative organizations, marketing; and (ii) provide marketing infrastructure to promote the development of new agriculture commodities; and
- (f) make adequate resources available to financial institutions to meet the demands for both long-term and short-term credit in the sector.

### C. Potential Results

7. The policy reforms would stimulate increases in agricultural production and exports by: (i) increasing domestic producer prices, bringing them closer to international prices and improving benefit-cost ratios for investment and production inputs; (ii) reducing the subsidy from producers to consumers; and (iii) improved marketing and increased credit. The introduction of a production-neutral federal land tax substituting for production-negative export taxes would represent a structural change in Argentina's taxation system.

### MANUFACTURING

#### A. Analysis

8. Argentina's manufactured exports have been influenced substantially by the overall trade regime, which has, in the last five decades, been largely protectionist, creating a strong inward-looking bias in the economy. Industrial export promotion has been generally seen as secondary to import-substituting industrialization. As a number of incentives and disincentives for different products were introduced, a multiplicity of effective exchange rates emerged, with exports of traditional goods receiving the lowest rates. The system ultimately succeeded neither in eliminating the anti-export bias in the highly protected industries nor in sustaining the traditional manufacture and agriculture. The incentives regime was rendered particularly inadequate during the 1977-81 import liberalization attempt. Argentina's manufacturing sector is still badly shattered by that unfortunate import liberalization experience, adopted concurrently with a revaluation of the domestic currency.

9. The present tariff regime has been in place since January 1984. As of October 1984 (the last date for which detailed information is available), the range of tariff duties was 0-38%, with an average rate of 22.8%. The average tariffs for the major sectors of the economy were, in fact, quite close to that mean, and they point to little dispersion of average tariffs across major economic sectors: in the agriculture and mining sectors, they are, respectively, 19.9% and 25.2%, while in the manufacturing sector, 22.9%

10. Manufacturing has the potential for export-oriented output growth, with attendant foreign exchange earnings and employment creation. The sector lacks a clear development strategy, institutional support and consistent policy signals. The main issue is how to redress the strong anti-export bias built onto the complex systems of tariff and non-tariff protection while maintaining an exchange rate adequate enough to restore export competitiveness. Policy objectives in manufacturing should focus on the implementation of an outward looking development strategy by introducing reforms to reorient the economy towards export promotion. This should include: (a) phased elimination of import prohibitions and quantitative restriction, and of export restrictions; (b) reorientation of export policies so as to reduce the discretionary element and provide automaticity and uniformity of access to incentives and foreign exchange in order to provide free-trade status for export industries; (c) improvement of the administrative mechanisms of trade management; and (d) preparation of

studies on tariff protection and rationalization of the system of tax rebates to exports as a basis for further policy reforms.

B. Policy Recommendations

11. Specific changes recommended include:

- (a) the gradual elimination of most import licensing requirements as follows: (i) reclassification of about 4,000 (100%) tariff positions from prohibited to free and partial replacement by tariffs; and (ii) gradual reclassification of about 1,300 (100%) tariff positions from prior consultation to free and partial replacement by tariffs.
- (b) achievement of free trade status for export industries, through the reform of the temporary admission regime for imported inputs as follows: (i) simplification of administrative procedures; (ii) guarantee of automatic access for any input; (iii) coverage of indirect exporters; (iv) extension to capital goods used for export production; and (v) extension of the tax reimbursement scheme to exports processed under the temporary admission regime;
- (c) simplification of export procedures, eliminating all unnecessary interventions by public sector agencies;
- (d) preparation of the following studies needed to support the adjustment process: (i) tariff protection, with a view to reducing tariff dispersion; and (ii) the indirect tax content of exports, with a view to rationalizing the system of tax rebates to exports, as well as to strengthen it vis-a-vis trading partners that might be tempted to impose countervailing duties;
- (e) extension of export financing: (i) removal of the exclusive linkage of pre-shipment financing with dollar-indexed or dollar deposits; (ii) facilitating joint financing by banks; and (iii) reviewing the level of financing subsidies; and
- (f) establishment of an export assistance and information system: (i) allowance of export plans by firms as a basis to determine the amount of Central Bank credit lines for financing; (ii) broadening risk coverage of exporting firms; (iii) formation of a joint organization to provide institutional support for marketing, storage, quality guarantee, legal assistance, lobby; and (iv) development of a common, integrated data base.

C. Potential Results

12. The following projections for 1986-90 reflect the potential impact of the proposed policy changes, predicated on the basis of a timely implementation and supported by massive export promotion efforts and by improved management and recapitalization of enterprises in the private sector: (a) exports of manufacturing goods are projected to grow on average by about 4.9% in real terms during 1986-90, from 0% in 1985; (b) imports of goods are projected to grow on average by about 4.7% in real terms on average during 1986-90, from a drop of 3% in 1985; and (c) the current account

deficit of the balance of payments is projected to fall from an estimated US\$2.2 billion in 1984 to an estimated US\$2.1 billion in 1986 and turn into surplus of US\$1.2 billion in 1990.

### FINANCIAL SYSTEM

#### A. Analysis

13. The efficiency of the financial system will be a key element in the speed and effectiveness of the recovery in Argentina. Once the economy has reached capacity in the productive sectors, the availability of credit at realistic interest rates will be the key to stimulating investment in future productive capacity. The financial sector, having been severely battered over the past decade, is in a poor position to provide the type of efficient service that the economy is going to need. It is currently characterized by substantial overexpansion, poorly run banking institutions, almost inexistent supervision by the Banking Superintendency, and by intermediation spreads of as much as 4% real per month reflecting not only an overall scarcity of funds, but more importantly, substantial inefficiencies in the system itself. Even with more normal levels of money supply in the economy, it is estimated that financial institutions would need spreads of 1.5% to 2% per month to break even. In effect, the system has operated like an oligopoly, despite the large number of participant institutions, protecting the least efficient ones and guaranteeing large economic rents to the more efficient ones. Analysis of the sector also indicates that low productivity is not confined solely to small institutions and that a policy of encouraging mergers will not, in itself, solve the problem. Other factors working to increase interest rate spreads include the 2% surcharge used to finance the Institute of Social Services for Bank Employees (ISSBE), the CRM (a device to reallocate the burden of differential reserve requirements) and various mechanisms to direct credit.

14. The goal of the reform of the financial sector should be to eliminate distortions and allow the market to define the spreads between the deposit rate and the lending rate. The increased monetization of the economy will then be reflected in declining interest rates.

#### B. Policy Recommendations

15. While a return to more normal levels of money supply in relation to GDP will certainly help to create a more healthy financial sector, there are a number of specific policy measures that must be taken within the sector itself:

- (a) restructuring of the sector by means of (i) increasing the minimum capitalization required for financial institutions; (ii) temporary fiscal measures to encourage consolidation; and (iii) a program aimed at public as well as private banks and at large as well as small;
- (b) removal of the ISSBE surcharge and its coverage by alternate fiscal measures;

- (c) removal of the CRM, recognizing that its allocative function has never worked efficiently;
- (d) shifting the bulk of reserve requirements on sight deposits with a very low requirement, say 10%, on time deposits;
- (e) elimination of credit subsidies.
- (f) reduce controls to direct credit; and
- (g) strengthen the supervisory role of the Banking Superintendency.

C. Potential Results

16. The above reforms should be sufficient for the market to function, lowering real intermediation spreads and allowing the development of an interest rate structure that would attract deposits while not discouraging investment in new plant and equipment. The restructuring of the banking system is bound to be gradual, however, and the economic and political costs of required adjustments may be high.

TAX ISSUES

A. Analysis

17. Argentina's basic tax structure is sound and appropriate for its level of development, including taxes on income, wealth, and value added. The revenue generated by the tax system, however, has been characterized in recent years by high volatility. Poor tax administration and widespread leakages through exemptions have led to a serious deterioration of government tax revenues. Total taxes collected are less than 20% of GDP. Income taxes amount to only 1.5% of GDP, and the value added tax (VAT) yields, in spite of the 18% rate, only 3.5% of GDP. Customs and excises are too high a share of revenues for a country of Argentina's level of development and create significant distortions both on the supply and on the demand side of the economy.

18. Policy objectives in the tax area should focus on increasing the yield from the existing structure through better administration of income, value added, and wealth taxes. There is strong evidence that tax administration has been hampered by poor information, frequent tax changes, repeated amnesties, and by penalty interest rates substantially below the taxpayer's cost of capital. Argentina's goal should be to raise tax revenue within the existing tax structure with emphasis on the elimination of tax exemptions and loopholes.

B. Policy Recommendations

19. Specific changes recommended include:
- (a) taxes on foreign trade: to be significantly phased out for agricultural exports;
  - (b) property taxes: introduce a production-neutral federal land tax, including an accurate cadastre;



- (c) tax administration: (i) unification of taxpayer identification for each separate tax collecting entity; (ii) phasing out of expensive "visit" system in favor of distribution of information on "cross compliance"; (iii) concentration of audit efforts on VAT; (iv) sharply increased penalties for evasion; (v) penalty interest for delinquency to be set significantly above taxpayers' cost of capital; and (v) elimination of amnesties;
- (d) income taxes (corporate): to be left largely as is except to: (i) broaden tax base; and (ii) include profits on the sale of agricultural properties;
- (e) wealth taxes: (i) to be extended (due to run-out in 1985) as is; and (ii) to eliminate deduction of 50% of assessed value of agricultural property;
- (f) taxation on goods and services: (i) turnover tax to remain unchanged; and (ii) in VAT eliminate most of exemptions given for industrial incentives purposes; and
- (g) excise tax: (i) not to be broadened; and (ii) focus on commodities where government has direct control over the collection (e.g., gasoline).

### C. Potential Results

20. The overall target would be for tax revenues to gradually reach 25% of GDP by 1990, a level which would be adequate to allow for real increases in public services and an increasing contribution of government savings to investment.

## II. IMPROVING THE EFFICIENCY OF THE PUBLIC SECTOR

21. A framework for reforming the public sector should include the medium-term role of the public sector in the productive areas; through restructuring and divesting public enterprises. Public sector's share in total investment should also gradually decrease. Public enterprises should not have preferential access to credit. Budgetary policy should be such that only transfers for equity take place and that operating losses of enterprises not be financed by either the Central Bank or the budget. Finally, enterprises should be managed as commercial entities, including policies over wages, product prices, recruitment and dismissals.

### PUBLIC SECTOR INVESTMENT AND FINANCING

#### A. Analysis

22. Since 1977, public investment has declined by 60% in real terms. In recent years, the Government has encountered difficulties cutting current expenditure and has resorted to sharp cuts in investment. The cuts have been made haphazardly, and essential services have deteriorated. The critical areas where deterioration has reached a scale to constrain the expansion of trade are the following.

- (a) Port services are not adequate for an expanded volume of grain exports. The bottlenecks are likely to become even more serious if exports continue to expand.
- (b) Exploration and exploitation of hydrocarbon resources have fallen behind the country's estimated potential. As soon as the economy recovers, consumption will increase and the country may face the danger of becoming an importer of hydrocarbons.
- (c) Roads feeding main transport corridors are either lacking or have deteriorated seriously. The agricultural export potential (especially fruits/vegetables) is not being fully exploited because of high transport costs/quality deterioration resulting from incomplete/bad feeder roads.
- (d) The telecommunications network is inadequate to meet the needs of business and residential users. Waiting lines for telephone installation stretch to 5-7 years, raising operating costs significantly.

#### B. Policy Recommendations

23. Policy reforms are extremely difficult to achieve in this sector. Some of the proposals outlined below have been previously recommended, as far back as 25 years ago. Specific changes proposed include:

- (a) rapid completion of dredging and the reconstruction of hinterland services at the Bahia Blanca port; and encouragement of private sector to build river ports;
- (b) concentration of YPF's (the State Oil Company) resources on oil exploitation and liquid extraction, gas gathering and enhanced oil recovery projects; and accelerating the projects of oil and gas pipeline construction, particularly those for Formosa oil fields and for Lujan de Cuyo;
- (c) increased emphasis on road reconstruction and maintenance and gravel surfacing on roads with more than a minimum (e.g., 100) average daily traffic; shifting railway transport operations to bulk freight with unit trains over a basic network of 16,000 km; emphasis on railway track renewal and bridge/culvert repairs; and
- (d) encouragement of private sector participation in the provision of telephone services.

24. The public investment budget will continue to be tight in the foreseeable future. At the same time, average public tariffs for users have already reached--with the exception of water supply and electricity--a level above which Argentine producers' international competitiveness could be negatively affected. Therefore, priority investments should increasingly have to be financed from increasing productivity, revenue sharing and cuts on non-priority investments. These are highly desirable but difficult to achieve.

- (i) productivity increases: (i) reduction of public employees through attrition; (ii) provision of adequate wage differentiation and production incentives; (iii) reinforcement of managerial accountability and introduction of cost accounting in public enterprises; (iv) cutting uneconomic production lines and transport losses; and (v) restructuring of some enterprises to expose them to competition;
- (ii) revenue sharing: (i) elimination of earmarked funds for non-priority projects; (ii) allocating to enterprises a higher percentage of tariffs paid by users, as the Treasury rebuilds its own revenue sources; and (iii) real increases in water and electricity tariff revenues;
- (iii) actions on non-priority investments: (i) in the energy sector minimization of coal investments and postponement of major hydroelectricity projects; (ii) in road transport, reduction of investments in upgrading/capacity, and decreases in "strategic" roads with very low traffic and in new paving; (iii) in railway transport, elimination of new electrification schemes, and reduction of investments in passenger traffic; (iv) in maritime transport slowing down the expansion of the merchant fleet; and (v) in industry, cancellation of the expansion of the petrochemical production capacity in Bahia Blanca, of the new sheet steel rolling mill by SOMISA, and of the expansion of shipyards.

## ENERGY

### A. Analysis

25. Falling proven oil reserves and heavy reliance on petroleum as the primary energy source jeopardize Argentina's self-sufficiency in liquid fuels. Substantial new drilling is needed to maintain production in order to avoid imports. Proven and potential reserves of gas are almost twice as important as those of oil, but increased use of gas (including its possible export) is constrained by the limited transport infrastructure. Rationalization of oil and gas development requires more attractive and stable incentives for the private sector, clarification of the latter's role vis-a-vis the Government's, bringing absolute as well as relative prices of hydrocarbon products more in line with the economic cost of fuels, and strengthening public sector agencies in the energy sector, notably their financial condition and planning framework.

26. The Government's past efforts in the oil and gas sector focussed on exploration and production of oil to assure self-sufficiency and substitution of relatively abundant gas for liquid fuels. Energy conservation received little attention. The petroleum sector has the potential not only to assure the country self-sufficiency in oil but also to produce significant surpluses for export. At the same time, it has the potential to contribute significantly to reducing the overall fiscal deficit. It would be possible to continue to substitute gas for liquid fuels if a significant expansion of gas transmission infrastructure can be achieved during the next three to four years. Over the medium and longer term, Argentina's oil and gas reserve base could be expanded and important energy conservation efforts should be supported.

27. Policy objectives on oil and gas should focus on the following areas: (a) developing the infrastructure for oil and gas transport; (b) defining an adequate framework for an expanded private sector role; (c) rationalizing price structures and taxation; (d) financial and institutional restructuring of major public enterprises in the energy sector; and (e) launching of an energy conservation program.

B. Policy Recommendations

28. Specific changes recommended include:

- (a) infrastructure: (i) government decision on the expansion of the gas transportation system (and corresponding gas gathering, treatment, and distribution through significant private sector (local and foreign) participation. Specifically, whether to expand the Central-West pipeline or to construct a new pipeline from Neuquen via Bahia Blanca to Buenos Aires; and (ii) solution of the COGASCO dispute would also be an integral part of this decision;
- (b) private sector role: (i) encourage private sector participation by awarding new exploitation and exploration contracts to private firms which have the financial and managerial capabilities to supplement YPF's efforts in order to expand oil and gas reserves; and (ii) limit or eliminate convertibility risks (i.e., exports of products as guarantee for foreign currency obligations) and facilitate access to domestic credit (i.e., "apex" financing arrangements to support private sector borrowing needs);
- (c) public enterprises: strengthen financially YPF and gas del Estado and reorganize their accounting and control systems;
- (d) pricing and taxation: (i) adjust the price of natural gas, taking its long-run opportunity cost as a guide; (ii) adjust the price of diesel as a function of the regular gasoline energy equivalent; (iii) review the level and structure of prices of other energy products; (iv) review relationship with energy conservation incentives; and (v) review the costs and benefits of the existing structure of taxation of the energy sector with a view to increasing efficiency; and
- (e) conservation: (i) design and implement an energy conservation program including pricing and taxation aspects; and (ii) study of the energy efficiency of the power sector and of the possibilities for end-user conversion and savings.

C. Potential Results

29. Official reserve estimates assume that only 19% of the oil in the ground may be recovered. This appears low by international standards. It may well be that a recovery rate of around 25% or more is possible. This would increase proven reserves from around 370 million cubic meters to over 600 million cubic meters of oil and would allow exports of crude oil or petroleum products of around 70,000 - 100,000 barrels per day amounting to US\$0.6 - 1.0 billion (at US\$24 per barrel). New resource discoveries combined with energy conservation efforts should allow Argentina to maintain self-sufficiency in energy use for the next two or three decades.

30. Over the next five years, annual investments of US\$1 billion or more would be required in the petroleum sector and around US\$500 million in gas transmission and distribution. Under the foreseeable constraints on government investment funds, neither YPF nor GdE will be able to finance such programs on their own, nor would they have the capacity to implement them. However, by involving the private sector and by using new financing instruments such as limited recourse financing and funds from international development banks, implementation of such investment programs would be feasible even in the present environment of tight public investment funds. The efficiency of these undertakings could be significantly improved by restructuring YPF and by deregulating the present pricing policy framework in the petroleum sector. YPF's investment program which was already reduced from a high of US\$1.8 billion in 1980 to about US\$900-1000 million (including dry wells) in 1985 could be further reduced to around US\$600 million by the late 1980s. Offering areas for exploration to private sector firms could reduce investment needs for YPF by US\$100-200 million per annum. New exploration contracts could decrease YPF's investment requirements for production and provide the capacity to achieve the export targets mentioned above before the end of the decade. US\$200-300 million of investments per year appear to be an achievable target for private sector production activities.

#### TRANSPORT SECTOR

##### A. Analysis

31. Public enterprises in the transport sector are an important drain on the Treasury's financial resources on account of their operating deficits and their investment programs. At the same time, their efficiency has an important bearing on the profitability of export-oriented domestic production and on reducing the cost of bringing imports into the country.

32. The sector is beset by bottlenecks and idle capacity which go side-by-side as a result of poor resource allocation and disinvestment, serious deterioration of infrastructure, poor maintenance, and obsolescence of rolling stock and fleet. There is little intermodal coordination; responsibilities of transport agencies are unclear, and the roles of the public and private sectors remain largely undetermined. Funds are earmarked for specific modes of transport or institutions without taking into account demand and rate of return criteria. Planning systems, staffing and information are inadequate. The Ministry of Public Works and Services lacks systematic information on project preparation and monitoring. There has been a major loss of experienced and trained staff while underemployment of lower level personnel has increased.

33. Policy objectives in transportation should focus on: (i) measures necessary to allow public enterprises to operate like commercial entities, including increased prices for public services, and adequate cost recovery; and (ii) policies to improve sector planning, investment follow-up, reduce public sector investment requirements through increased private sector participation, and deregulate and privatize transport sector activities.

##### B. Policy Recommendations

34. Policy reforms are extremely difficult to achieve in this sector. Some of the proposals outlined below have been previously recommended as far back as 25 years ago.

- (a) increased prices of public sector services to ensure adequate cost recovery in, ports dredging, and railroads, and the introduction of road user charges;
- (b) improvement of efficiency of operation of the railways. Since this is an area where all previous efforts have failed, it would represent a major task. It should include: (i) reduction of manpower (currently 108,000), closure of uneconomic lines, generation of operation/line-specific economic information to allow the assessment of the merits of expenditure programs; (ii) an overall reduction of the 1986-90 investment expenditures by 60%; and shifts in investment priorities: from passenger traffic to bulk freight (using unit trains over a basic network of 16,000 km); from the expansion of rolling stock (limiting purchases to replacement needs) and new electrification schemes to track renewal and bridge and culvert repairs; and to investments to control of operations, including the coordination of broad-gauge lines;
- (c) improvement of efficiency of operation of maritime and air transport. This should include: (i) reduction in total investment expenditure; introduction of a toll system to cover major reequipment costs; efficiency improvements of import dredging operations; and elimination of legal obligations to buy from domestic shipyards; and (ii) shifts in investment priorities from the expansion of the merchant fleet to dredging and port support services and elevators, and from a possible air fleet standardization investment to the improvement of air traffic control systems;
- (d) strengthening of MOSP planning and follow-up including the restoration of national transport planning as part of the global public investment planning mechanism, and the elimination of earmarked funds. In most road transport, priorities need to be shifted (i) from upgrading/capacity increases to reconstruction (current investment projects allocate 73% and 26%, respectively, to the former and the latter); (ii) from projects that are not likely to yield acceptable rates of return (due to expected traffic levels below minimum), that are allocated 52% of total investment expenditure, to higher traffic corridors; and (iii) from new paving projects with expected average daily traffic (ADT) of less than 100 to gravel surface projects with higher ADT;
- (e) initiation of institutional reforms such as consolidation of port agencies and urban rail authority, and agreement on studies to implement action programs in the sector; and
- (f) deregulation and privatization in areas of offshore storage/shipping facilities, containerization, tugboat service, and highway maintenance.

### C. Potential Results

35. Action on the above areas would result in a more efficient and less costly transport operation in support of Argentina's export promotion efforts. At the same time, the negative effects on the overall public sector deficit will be significantly reduced.

## RESTRUCTURING AND PRIVATIZATION

### A. Analysis

36. Restructuring and privatization of public sector industrial enterprises provide a further means to help reduce the Government's financial burden and public sector deficits and to increase industrial efficiency, competitiveness and exports. These are important areas of policy consideration because future growth possibilities of the economy may hinge critically on the ability of the Government to keep down public sector deficits, which otherwise could lead to uncontrollable upward pressures on inflation, interest rates and/or taxes.

37. Policy objectives in restructuring and privatization should focus on: (a) restructuring of public sector enterprises which often have large potential for cost reductions or which, through their linkages, could have a significant impact on the efficiency and competitiveness of other parts of the industrial sector as well as the rest of the economy; and (b) privatization of select state-owned enterprises.

### B. Policy Recommendations

38. ~~Specific actions recommended include:~~

(a) technical, financial and organization/management restructuring of selected public enterprises or subsectors to improve the efficiency and competitiveness of basic industries. The most significant benefits from restructuring can be expected in steel (mainly SOMISA) and telecommunications (ENTEL). Systematic restructuring/rationalization should focus on improvements in: (i) organizational structures and management and administrative processes, including the degree of the enterprises' autonomy and the nature of their relationship with the Central Government; (ii) balancing and/or modernization of existing production lines; (iii) production management techniques (e.g., inventory and other working capital management, appropriate balance between production capacity and size and composition of work force; (iv) financing; and (v) pricing/cost recovery techniques;

(b) mounting a comprehensive program for privatizing public enterprises especially in the productive sectors (e.g., petrochemicals) which should include: (i) the identification of potential local and foreign private sector investors who would be interested in the purchase of state-owned assets; and (ii) the determination of vehicle of transfer of assets to private investors, e.g., stock market, international competitive bidding, etc.

### C. Potential Results

39. Benefits of restructuring/privatization programs are likely to be significant for other productive subsectors through cost reductions and efficiency components, as well as through linkage and potential impacts on competitiveness. In the near term, the efforts toward privatization could

help reduce the public sector deficit and support the Government's stabilization objectives. In the longer term, through better exploitation of the benefits of private initiative and entrepreneurship, they could also lead to significant efficiency improvements in many segments of the economy, help stimulate direct foreign investment, and facilitate export development.

Table 1: ARGENTINA - Summary of Key Macroeconomic Aggregates, 1978-1985

(percentages)

	1978	1979	1980	1981	1982	1983	1984	Estimated 1985
GDP Growth Rate	-3.4	6.7	0.7	-6.2	-5.2	3.1	2.0	-3.0
Debt/Export Ratio <sup>1/</sup>	1.62	2.0	2.5	3.1	4.6	4.8	4.7	4.7
Interest/Export Ratio <sup>2/</sup>	1.69	14.6	20.4	33.0	51.6	56.8	55.8	50.6
Total Debt/GDP <sup>3/</sup>	23	28	31	40	63	61	62	69
Interest Payments/GDP <sup>4/</sup>	2.4	2.1	2.5	4.3	7.0	7.2	7.0	7.0
Debt Service Ratio <sup>5/</sup>	38	24	31	43	65	71	64	61
Terms of Trade	78	83	94	107	92	88	93	89
Import Growth Rate <sup>6/</sup>	-4.9	45.4	45.4	0.4	-41.2	-2.4	1.5	-5.3
Export Growth Rate	12.2	-3.0	-4.9	5.9	-2.4	11.5	-1.2	11.6
Current Account Balance	1,833	-537	-4,767	-4,714	-2,357	-2,461	-2,492	-1,280

1/ Total debt including short-term/exports goods and NFS; absolute ratio.

2/ Total interest payments to exports goods and NFS.

3/ Total debt including short-term/GDP.

4/ Total interest payments/GDP.

5/ Total interest and amortization on MLT divided by exports of goods and non factor services.

6/ Real growth rates in 1970 prices.

Table 2.A: ARGENTINA - Projections of Key Variables, 1985-1994, Base Case Scenario  
(percentages and 1985 U. S. Dollars)

	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994
GDP growth rate	-3.0	2.7	3.5	3.3	3.3	3.2	3.3	3.3	3.4	3.4
GDP/capita	2,049	2,066	2,101	2,131	2,163	2,194	2,225	2,257	2,292	2,328
Debt/Exports	4.8	5.0	5.0	4.5	4.1	3.7	3.3	3.3	2.8	2.5
Total Debt Outstanding and Disbursed (billions)	48.6	50.1	51.6	52.4	53.2	53.2	53.6	52.6	51.0	48.7
Debt/GDP	69	69	69	68	66	64	62	59	55	50
Interest Payments/GDP	7	6	6	5	5	4	4	4	3	3
Debt Service ratio (exclud. short term)	61	67	50	44	43	42	43	39	39	38
Public Investment a/	2,451	2,426	2,523	2,624	2,729	2,839	2,952	3,070	3,193	3,321
Public Investment/GDP	4.9	4.8	4.8	4.8	4.8	4.9	4.9	5.0	5.0	5.0
Private Investment a/	3,827	4,264	4,596	4,964	5,356	5,774	6,207	6,672	7,173	7,711
Private Investment/GDP	7.7	8.4	8.7	9.1	9.5	9.9	10.3	10.8	11.2	11.6
Public Savings/GDP	6.9	7.9	8.2	8.8	9.0	9.3	9.6	10.0	10.2	10.5
Private Savings/GDP	12.2	10.6	11.1	10.9	11.1	11.1	11.1	11.1	11.2	11.4
Exports Growth Rate	11.6	-3.0	6.7	3.0	3.4	2.4	3.0	3.0	3.5	3.6
Exports/GDP	15.1	14.2	14.7	14.6	14.6	14.5	14.5	14.4	14.5	14.5
Imports Growth Rate	-5.3	4.8	3.8	3.7	3.7	3.7	4.0	4.0	4.1	4.1
Imports/GDP	8.6	8.8	8.9	8.9	8.9	9.0	9.0	9.1	9.1	9.2
Consumption/Capita Growth Rate	-5.2	1.5	0.7	1.0	1.0	1.0	1.0	1.0	1.0	1.0
GNP Growth Rate	-2.8	3.3	4.0	4.1	3.6	3.7	3.8	3.6	3.7	3.8
GNP/Capita	1,898	1,926	1,967	2,012	2,048	2,086	2,128	2,165	2,206	2,249

a/ In thousand billions of 1984 pesos.

Notes:

1. Debt includes public and publicly guaranteed, private non-guaranteed and short term debt.
2. Exports and imports include that of goods and non-factor services.

Table 2.B: ARGENTINA - Projections of Key Variables, 1985-1994, High Case Scenario

(percentages and 1985 US dollars)

	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994
GDP growth rate	-3.0	2.6	4.3	4.6	4.8	4.4	4.3	4.3	4.4	4.4
GDP/capita	2,049	2,066	2,117	2,176	2,241	2,297	2,355	2,412	2,474	2,537
Debt/Export	5.1	4.8	4.4	3.9	3.4	2.9	2.8	2.6	2.4	2.2
Total Debt Outstanding and Disbursed	48.6	50.1	51.9	52.5	52.6	53.2	53.9	54.3	54.8	55.2
Debt/GDP	69	65	60	54	48	42	38	34	29	25
Interest Payments/GDP	7	6	6	5	5	4	4	3	3	3
Debt Service Ratio (exclud. short term)	61	67	49	41	39	40	45	43	48	36
Public Investment <sup>a</sup> /	2,451	2,426	2,596	2,765	2,931	3,092	3,246	3,409	3,579	3,758
Public Investment/GDP	4.9	4.8	4.9	5.0	5.0	5.1	5.1	5.1	5.2	5.2
Private Investment <sup>a</sup> /	3,827	4,264	4,690	5,253	5,830	6,413	6,991	7,550	8,154	8,806
Private Investment/GDP	7.7	8.4	8.8	9.4	10.0	10.5	11.0	11.4	11.8	12.2
Public Savings/GDP	6.9	7.9	9.2	9.8	10.0	10.3	10.6	11.0	11.2	11.5
Private Savings/GDP	12.2	10.6	10.1	10.3	10.9	11.0	11.1	11.0	11.2	11.3
Exports Growth Rate	11.6	-3.0	8.6	6.3	6.7	4.1	4.6	4.3	5.2	5.1
Exports/GDP	15.1	14.2	14.8	15.0	15.3	15.3	15.3	15.3	15.4	15.5
Imports Growth Rate	-5.3	4.8	9.3	5.8	6.2	6.0	5.9	5.6	5.5	5.5
Imports/GDP	8.6	8.8	9.2	9.3	9.5	9.6	9.7	9.9	10.0	10.1
Consumption/Capita Growth Rate	-5.2	1.5	1.5	1.75	2.0	2.0	2.0	2.0	2.0	2.0
GNP Growth Rate	-2.8	3.3	4.9	5.6	5.2	4.9	5.0	4.7	4.8	4.8
GNP/Capita	1898	1925	1985	2059	2127	2193	2261	2324	2393	2464

<sup>a</sup>/In thousand billions of 1984 pesos.

## Notes:

1. Debt includes public and publicly guaranteed, private non-guaranteed and short term debt.
2. Exports and imports include that of goods and non-factor services.

Table 3.A.1: ARGENTINA - Projections of Commitments, 1985-1990: Base Case

(in millions of US dollars)

	1985	1986	1987	1988	1989	1990	TOTAL
World Bank	240	630	500	500	500	500	2,870
IDB (or other multilateral)	400	400	300	200	200	200	1,700
Bilateral Official Exp. Credit							
Suppliers' Credits	1,100	1,200	900	800	800	700	5,500
Commercial Banks	2,992	1,865	1,334	727	929	209	8056
TOTAL	4,732	4,165	3,034	2,227	2,229	1,409	18,056

Table 3.A.2: ARGENTINA - Projections of Disbursements, 1985-1990: Base Case

(in millions of US dollars)

	1985	1986	1987	1988	1989	1990	TOTAL
World Bank	146	478	462	470	425	400	2,381
IBD	236	470	157	189	192	196	1,440
Bilateral/Official Exp. Credit							
Suppliers' Credits	695	826	375	375	325	275	2,871
Commercial Banks	2,992	1,865	1,334	727	929	209	8,056
TOTAL	4,069	3,639	2,328	1,761	1,871	1,080	14,748

Table 3.A.3: ARGENTINA - Projections of Repayments, 1985-1990: Base Case

(in millions of US dollars)

	1985	1986	1987	1988	1989	1990	TOTAL
World Bank	116	149	161	159	178	198	961
IDB	76	100	35	50	68	118	447
Bilateral							
Official Exp. Credit	143	249	168	222	388	413	1,583
Suppliers' Credits							
Commercial Banks	765	982	—	—	—	466	2,213
TOTAL (including IMF)	1100	1480	364	431	634	1195	5204

Table 3.A.4: ARGENTINA - Projections of Net External Flows, 1985-1990: Base Case

(in millions of US dollars)

	1985	1986	1987	1988	1989	1990	T O T A L
World Bank	30	329	301	311	247	202	1,420
IDB	160	370	122	139	124	78	993
IMF	702	400	-150	0	-300	-300	652
Bilateral							
Official Exp. Credit	552	577	207	153	-63	-138	1,288
Suppliers' Credits							
Commercial Banks	2,227	883	1,334	727	929	-257	5,843
Direct Foreign Investment (net)	214	246	285	330	384	447	1,906
TOTAL (incl. IMF and DFI)	3,885	2,805	2,399	1,660	1,321	32	12,102

Table 3.B.1: ARGENTINA - Projections of Commitments, 1985-90: High Case

(in millions of US dollars)

	1985	1986	1987	1988	1989	1990	T O T A L
World Bank	240	630	800	900	900	900	4,370
IDB	400	400	500	500	500	500	2,800
Bilateral )							
Official Exp. Credit )	1,100	1,200	700	500	400	400	4,300
Suppliers' Credits )							
Commercial Banks	3,423	1,859	1,293	0	0	0	6,575
TOTAL	5,163	4,089	3,293	1,900	1,800	1,800	18,045

Table 3.B.2: ARGENTINA - Projections of Disbursements, 1985-90: High Case

(in millions of US dollars)

	1985	1986	1987	1988	1989	1990	T O T A L
World Bank	146	478	600	670	670	600	3,164
IDB	236	470	157	189	192	196	1,440
Bilateral )							
Official Exp. Credit )	695	826	375	325	275	247	2,743
Suppliers' Credits )							
Commercial Banks	2,992	1,865	1,293	432	303	0	6,885
TOTAL	4,069	3,639	2,425	1,616	1,440	1,043	14,232

Table 3.B.3: ARGENTINA - Projections of Repayments, 1985-90: High Case

(in millions of US dollars)

	1985	1986	1987	1988	1989	1990	T O T A L
World Bank	116	149	161	159	178	198	961
IDB	76	100	35	50	68	118	447
Bilateral )							
Official Exp. Credit )	143	249	168	222	388	413	1,583
Suppliers' Credits )							
Commercial Banks	765	982	0	0	0	805	2,552
TOTAL (including IMF)	1,100	1,480	364	431	634	1,534	5,543

Table 3.B.4: ARGENTINA - Projections of Net External Flows, 1985-90: High Case

(in millions of US dollars)

	1985	1986	1987	1988	1989	1990	T O T A L
World Bank	30	329	439	511	492	402	2,203
IDB	160	370	122	139	124	78	993
IMF	702	400	-150	0	-350	-300	-602
Bilateral Official Exp. Credit)	552	577	207	103	-113	-166	1,160
Suppliers' Credits )							
Commercial Banks	2,207	883	1,293	432	303	-805	4,333
Direct Foreign Investment (net)	269	214	246	285	330	384	1,728
TOTAL (including IMF and DFI)	3,940	2,773	2,457	1,470	1,136	-107	11,019

Table 4.1: ARGENTINA - Projections of Debt Outstanding and Disbursed, 1985-90: Base Case

(in millions of US dollars, end of period)

	1985	1986	1987	1988	1989	1990	Change 1984/1990
World Bank	579	985	1,286	1,597	1,844	2,046	1,420
IDB	1,104	1,465	1,587	1,726	1,850	1,928	993
IMF	1,800	2,200	2,350	2,350	2050	1750	652
Bilateral							
Official Exp. Credit	5,535	6,112	6,319	6,472	6,409	6,271	1,288
Suppliers' Credits							
Commercial Banks	35,860	37,174	38,391	39,118	40,047	39,790	5,843
Total Medium & Long Term DOD	44,878	47,936	49,933	51,263	52,200	51,785	10,196
Short Term Debt	5,005	4,500	4,000	3,500	3,004	3,175	-3,395
TOTAL	49,883	52,436	53,933	54,763	55,204	54,960	6,801

Table 4.2: ARGENTINA - Projections of Debt Outstanding and Disbursed by Source, 1985-90: High Case

(in millions of US dollars, end of period)

	1985	1986	1987	1988	1989	1990	Change 1984/1990
World Bank	579	985	1,424	1,935	2,427	2,829	2,203
IDB	1,104	1,465	1,587	1,726	1,850	1,928	993
IMF	1,800	2,200	2,310	2,310	2,050	1,750	652
Bilateral							
Official Exp. Credit)	5,535	6,112	6,319	6,422	6,309	6,143	1,160
Suppliers' Credits )							
Commercial Banks	35,860	37,174	38,350	38,782	39,085	38,280	4,333
Total Medium & Long Term DOD	44,878	47,936	50,030	51,175	51,721	50,930	9,341
Short Term Debt	5,005	4,500	4,000	3,500	3,165	3,383	-3,187
TOTAL	49,883	52,436	54,030	54,675	54,886	54,313	6,154

## ANNEX IV

COUNTRY: ARGENTINA  
 FY86-FY90 PROPOSED LENDING PROGRAM - PROJECT DETAIL  
 NOVEMBER 27, 1985

## High Case

MANAGING UNIT	PROJECT / STATUS	PLAN/ACT. APPRAISAL		US\$ Million	
			DEPARTURE		BANK
<b>FY86</b>					
LC2PB	PA041-TAI-B	L	11/85		20.0
LCPWS	PA025-Water Supply-B	L	02/85		60.0
LCPAC	PA036-Agric. Sector-C	L	05/85		350.0
LCPEN	PA042-Power Eng.-B	M	11/85		10.0
FY86 Totals: Lending Amount					440.0
Number of Projects					<u>3</u>
<b>FY87</b>					
LCPT1	PA024-Bahia Blanca I-C	S	12/84		40.0
LC2PB	PA050-Trade Policy-C	L	06/86		350.0
EGYD2	PA047-Refinery Supp Ln-S	M	11/85		110.0
LCPI2	PA046-Sm. & Me. Ind. B	L	06/86		100.0
EGYD2	PAO -Oil & Gas Private D	L	06/86		100.0
FY87 Totals: Lending					700.0
Number of Projects					<u>4</u>
<b>FY88</b>					
LCPI2	PAO -Financial Sector D	S	06/86		350.0
LCPEN	PA051-Power Distrib. D	L	09/86		150.0
LCPI2	PA046-Export Promotion C	S	06/86		200.0
EGYD2	PAO-Gas Pipeline D	L	09/86		200.0
FY88 Totals: Lending Amount					900.0
Number of Projects					<u>4</u>
<b>FY89</b>					
LCPI2	PA027-Industrial Cr.III-D	S	03/87		150.0
LCPI2	PAO-Financial Sector II D	L	07/87		350.0
EGYD2	PA028-Oil & Gas Infrast.D	S	06/87		100.0
LCPI2	PAO -Trade Policy II D	L	06/87		350.0
FY89 Totals: Lending Amount					950.0
Number of Projects					<u>4</u>
<b>FY90</b>					
INDD3	PAO -SOMISA Restruct. -D	S	06/87		50.0
LCPEN	PA051-SEGBA V C	S	06/88		150.0
LCPWS	PAO Water Supply D	L	06/89		80.0
LCPI2	PA053-Export Promot. II-D	S	06/88		100.0
LCPURB	PAO Housing D	L	06/89		75.0
LCPURB	PAO Market Town Impr.-D	L	05/88		75.0
LCPTR	PAO Transp. Sector II-D	L	06/89		350.0
FY90 Totals: Lending Amount					880.0
Number of Projects					<u>7</u>
TOTAL LENDING AMOUNT					<u>3,870.0</u>
NUMBER OF PROJECTS					<u>22</u>

## Reserve Projects:

<b>FY87</b>					
LCPAC	PAO -Agric. Sector II C	L	09/86		350.0
<b>FY88</b>					
LCPTR	PAO -Bahia Blanca II C	L	09/86		160.0
LCPEN	PAO -Yacyreta	C	09/86		200.0
<b>FY89</b>					
LCPTR	PAO -Transport Sect. I-D	S	06/86		350.0
LCPI2	PAO -Financial Restruc.D	L	06/87		100.0
<b>FY90</b>					
INDD4	PA055-ENTEL Restruct. -D	S	06/88		150.0

THE WORLD BANK  
Washington, D. C. 20433  
U.S.A.

A.W. CLAUSEN  
President

December 20, 1983

Dear Mr. President:

It was a pleasure meeting you yesterday and having the opportunity to personally congratulate you on your appointment as Alternate Governor for Argentina on the Board of Governors of The World Bank. I enjoyed our conversation and discussion vis-a-vis the Bank and its role in Argentina.

On behalf of the Executive Directors, Officers and Staff, I welcome your appointment and look forward to your participation in the affairs of the Bank.

Warm regards.

Sincerely,



Senor Dr. Enrique Garcia Vazquez  
Presidente  
Banco Central de la Republica Argentina  
Reconquista 266  
1003 Buenos Aires, Argentina

BC: Mr. Zalduendo  
BCC: Mr. Lerdau  
Mr. Adams

ETSANIDAD:hh

December 15, 1983

Dear Mr. Minister:

It is indeed good to know that you have been appointed Governor for Argentina on the Board of Governors of The World Bank. Congratulations!

The Executive Directors, Officers and Staff join me in extending to you a warm welcome. We look forward to your participation in the affairs of the Bank.

On a personal note, I hope to have the opportunity of greeting you here in Washington in the near future.

Sincerely,



A. W. Clausen

Su Excelencia  
Senor Bernardo Grinspun  
Ministro de Economia  
Hipolito Yrigoyen 250  
1310 Buenos Aires, Argentina

✓ cc: Mr. Zalduendo  
Mr. Lerda  
Mr. Adams

ETSANIDAD/ek

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Box!

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OF

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TO:

BERNARDO GRINSPUN, BARMIENTO 670, PISO 8,  
BUENOS AIRES, ARGENTINA. THANK YOU FOR YOUR LETTER OF NOVEMBER 18,  
1983. I AM PLEASED TO INFORM YOU THAT WE HAVE MADE ARRANGEMENTS  
TO RELEASE DR. JUAN EDUARDO BARRERA FROM HIS CONSULTING CONTRACT  
WITH US EFFECTIVE DECEMBER 2 WHICH I UNDERSTAND IS IN ACCORD WITH  
HIS PLANS. PLEASE ACCEPT MY CONGRATULATIONS AND MY BEST WISHES  
FOR THE HEAVY RESPONSIBILITIES YOU WILL BE UNDERTAKING AS  
MINISTER OF ECONOMICS. REGARDS, A.W. CLAUSEN, PRESIDENT,  
THE WORLD BANK.

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NOT TO BE TRANSMITTED

CLASS OF SERVICE: **CABLE**

TELEX NO.:

DATE: **11/23/83**

SUBJECT: **Mr. J.E. Barrera**

DRAFTED BY:  
**GSKajj/jh**

CLEARANCES AND COPY DISTRIBUTION:

cc: **Mr. Scherer, LC2**

AUTHORIZED BY (Name and Signature):

**A.W. Clausen, EXC**  
DEPARTMENT:  
**Office of the President**

SECTION BELOW FOR USE OF CABLE SECTION

CHECKED FOR DISPATCH

**WORLD BANK**

**OFFICE OF THE PRESIDENT**

Nov. 23, 1983

Gautam:

The swearing-in ceremony for Mr. Barrera is December 10 so we need to respond quickly. I am leaving Monday, so need your counsel as soon as possible.

Tom

Bernardo Grinspun

Buenos Aires, November 18<sup>th</sup>, 1983

Mr. A. Clausen  
President of the World Bank  
1818 H St., N.W.  
Washington D.C.

Dear Mr. Clausen:

It is a real pleasure for me, as the Ministry of Economic of Argentina designated by president-elect Dr. Raúl Alfonsín to greet you at this historical moment for our country. I would also like to take this opportunity to express our wish and will to reinforce and, if possible expand the traditionally excellent relationship between that prestigious institution and the Argentine Republic.

In addition, I would like to introduce you to the handler of this note, Dr. Juan E. Barrera, who has been designated Secretary of Mining. Mr. Barrera is presently working as a Consultant for the Economic + Projections Department (EPD), Commodities Division.

As I would like to incorporate Mr. Barrera to the Cabinet as soon as possible, I would like and really appreciate if you can assist him in speeding up the details related to the termination of his present contract.

Yours, sincerely

B. Grinspun

File

THE WORLD BANK  
Washington, D. C. 20433  
U. S. A.

March 7, 1983

A. W. CLAUSEN  
President

Dear Mr. Minister:

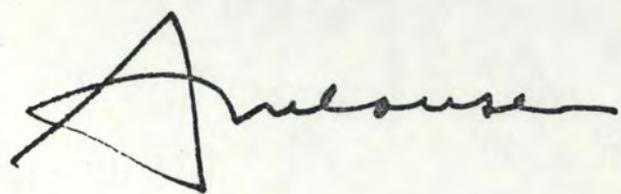
It was a great pleasure for me to see you and your associates here on February 9 and to receive, subsequently, your letter of February 14.

Regarding your request for an economic mission, I am pleased to inform you that we have started preparations to put such an economic mission together. Its task would be, on the one hand, to make recommendations for policy direction in areas critical to Argentina's economic development and, on the other, to frame recommendations to the Bank on the type of assistance that we could offer to Argentina that would be most suitable given the Government's policies and the country's economic situation. We are planning to have a report ready for discussion by the time the change in Government is expected to take place.

In response to your concern about the development of Argentina's foreign trade, we are exploring the possibilities of restructuring the existing Industrial Credit Loan to BANADE so as to permit exporters to obtain foreign exchange for importing production inputs and equipment. This should make it possible to expedite disbursements of this loan in the course of this year.

Let me assure you, Mr. Minister, that we will try our best to assist your country effectively in the present difficult circumstances.

Sincerely



Dr. Jorge Wehbe  
Minister of Economy  
Ministry of Economy  
Buenos Aires  
Argentina

217

To be ready today 3/4

Copies to Mr. Stern + Mr. Ardito - Barkha (to prepare reply)

Follow R1

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2/28-

(THIS IS NOT AN OFFICIAL TRANSLATION)

Washington, D.C. February 14, 1983

Dear Mr. Clausen:

As a follow-up to the cordial meeting we had on Wednesday 9th last, I thought it opportune to summarize the main subjects discussed in order to facilitate further action.

We talked, Mr. President, about the difficult balance-of-payments situation that my country is facing and the steps that have been taken in regard to the servicing of the external debt. As you are aware, we have the decided support of the International Monetary Fund, of commercial banks in many countries and that of many governments.

We have concurred with you on the necessity of expanding the Argentine foreign trade as a way to attain great part of a genuine solution through an increase in imported goods, utilization of idle productive capacity and a rise in the employment level.

This is a difficult task taking into consideration the serious and prolonged recession that the world economy is experimenting. We have been encouraged by the fact that you share our concern for maintaining a sustained growth, for promoting new operative modalities, and for easing some requirements in view of the aforementioned economic situation.

Under these circumstances, and bearing in mind the fact that you have expressed your desire to cooperate with my country and to facilitate the initial steps to be taken by the constitutional government, we have requested the assistance of the Bank to carry out the following new activities:

1. To negotiate a loan for a significant amount to develop foreign trade;
2. To increase the amount allotted for Argentina in the Lending Program of the Bank in order to carry out operations in new sectors (foreign trade and housing for low-income sectors of the population); and
3. To send a mission to prepare a study of the Argentine economy and its most relevant problems.

2-14-83 Follow for reply for my signature

In view of the cordial relations that my country maintains with the Bank, and in the light of the spirit of the conversation we held, I hope that you will set up guidelines so that your staff and mine may agree on the modalities to be followed to undertake these tasks as soon as possible.

With the assurances of my highest consideration, I am,  
Mr. President,

Sincerely yours,

(signed)

Jorge Wehbe

*Ministro de Economía*

Washington, D.C., 14 de febrero de 1983.

Estimado Sr. Clausen:

Después de la cordial reunión mantenida con usted el miércoles 9 me parece oportuno reseñar los temas principales de la misma con el propósito de facilitar las acciones siguientes.

Hemos comentado con usted, señor Presidente, la difícil situación de balance de pagos por las cuales atraviesa mi país y los pasos ya dados para ordenar el servicio de la deuda externa. Como es de su conocimiento hemos contado con el apoyo decidido del Fondo Monetario Internacional, de la banca comercial de muchos países y de distintos gobiernos.

Asimismo hemos coincidido con usted, en la necesidad de aumentar el comercio exterior argentino ya que este camino brindará gran parte de una solución genuina a través del aumento de bienes importados, utilización de la capacidad productiva ociosa, y aumento del nivel de empleo.

El logro de estos objetivos en momentos en que la economía mundial atraviesa una seria y prolongada recesión es, sin duda, una tarea difícil. Nos ha alentado saber que el señor Presidente comparte la preocupación por sostener el crecimiento, promover nuevas modalidades operativas y aún reducir algunas exigencias dada la situación económica señalada.

## *Ministro de Economía*

Dentro de estas circunstancias y el deseo manifestado por usted de colaborar con mi país y , además, facilitar la actividad inicial del gobierno constitucional, hemos solicitado la colaboración del Banco para las siguientes nuevas actividades:

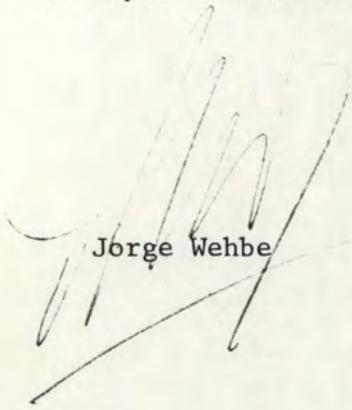
1° Obtención de un préstamo por una cantidad significativa destinado a desarrollar el comercio exterior;

2° Ampliación del monto asignado a Argentina en el Programa de Préstamos del Banco para poder encarar operaciones en nuevos sectores ( comercio exterior y vivienda para población de bajos ingresos ); y

3° Envío de una misión para preparar un estudio sobre la economía argentina y sus problemas más relevantes.

Dado las cordiales relaciones que mi país mantiene con el Banco así como el espíritu de nuestra entrevista, espero que usted disponga lo necesario para que nuestros funcionarios acuerden las modalidades de las operaciones en el más breve plazo posible.

Saludo al señor Presidente con mi mayor consideración.

  
Jorge Wehbe

Sr. A. W. Clausen  
Presidente  
Banco Mundial

Arg.

February 18, 1983

Dear Mr. Minister.

Thank you very much for your letter of February 9, 1983, giving us formal notification of your Government's decision to release in full the balance of Argentina's contribution to IDA6. We deeply appreciate your decision.

I express once again our thanks to you and your Government for your continued support to the Association.

Sincerely,



A. W. Clausen  
President

Su Excelencia  
Senor Jorge Wabbe  
Ministro de Economia  
Hacienda y Finanzas  
Hipolito Yrigoyen 290  
Buenos Aires, Argentina

cc: Mr. Eduardo Zalduendo  
Executive Director

copies to: Messrs. Qureshi, Mistry, Ikram, Van Puybroeck  
Mrs. De Santis

P.Samidia:dm

THE WORLD BANK/INTERNATIONAL FINANCE CORPORATION  
OFFICE MEMORANDUM

*Fate please*  
2/17/83

TO: Memorandum for the Record February 15, 1983

FROM: Peter R. Scherer, Division Chief, LC2DD

SUBJECT: Meeting of Mr. Clausen with the Argentine Delegation

1. Mr. Wehbe, the Argentine Minister of Finance, called on Mr. Clausen on Wednesday, February 9. The Minister was accompanied by Mr. Gonzalez del Solar, President of the Central Bank, Mr. Zalduendo, Executive Director World Bank and Mr. Zimmerman, personal advisor to the Minister. Messrs. Stern, Lerdaun and Scherer also participated.
2. Minister Wehbe commended the Bank for its recent initiatives to provide more effective assistance to the developing countries under present difficult economic and financial circumstances. He asked that Argentina be considered for a special assistance loan. Mr. Clausen was pleased about the positive Argentine response but cautioned on the possibility of a special assistance loan to Argentina. There was already a long queue of applicants and the Bank had to apply rather strict selection criteria in view of limited funds. The Minister indicated that he was aware of difficulties and the need to have a meaningful policy package accompany a quick disbursing loan. The President of the Central Bank asked that the Bank increase and diversify its lending program to Argentina. The Minister asked for Bank support in the social sectors, notably housing. Mr. Stern responded that while housing may be of highest priority for the Government, the Bank would have to assess carefully whether there was justification for support within the context of the Bank's overall assistance program to Argentina; usually, the Bank concentrated on low cost housing which, in Argentina, probably had a very small foreign exchange component. The Minister, while elaborating on the importance of stimulating and reorganizing the housing sector, clarified that this not necessarily was of the highest priority of the Government. Rather, he would like to see this matter analyzed by a Bank mission in the broader context of Argentina's development constraints and needs. The President of the Central Bank felt that a "basic" economic mission a la Chile, in which he had participated as a consultant, would be a most useful guide for the new authorities, expected to enter office a year hence. He mentioned social security, the financial sector, the fiscal system and regional development as areas for priority attention. Messrs. Clausen and Stern expressed support and promised that an effort would be made to arrange for such a mission within existing staff constraints.
3. The Minister was confident that Argentina would overcome its serious balance of payments problem; he explained that the stabilization program was proceeding on schedule and that the negotiations with the commercial banks were moving well. Agreements on fresh financing were essentially in place and no major problems were foreseen with the refinancing of the public debt falling due in 1983. The President of the

Central Bank was hopeful that co-financed loans could be excluded from the rescheduling; he mentioned that his team has had discussions on this matter with the Mexicans to define a common position. Mr. Clausen congratulated the Argentine delegation and expressed hopes that recent promising signals indicated the beginning of a turn-around in the economy. He was particularly pleased with Argentina's strong export performance. The Bank was supporting programs to strengthen exports but also provided financing for critically important imports to buttress international trade. The Minister again expressed Argentina's interest in a loan to help finance imports. He felt that, particularly in agriculture, increasing amounts of imported inputs would be required to sustain production growth. He closed by saying that the record harvest should be seen as an indicator of a more dynamic performance of the Argentine economic in the future.

cc: Messrs. Clausen, Stern, Barletta, Lerdau and Levy

R.1

Sent Orig. to Mr. Qureshi  
to handle  
2/16

228

Washington, D.C., February 9, 1983

Mr. A.W. Clausen  
President  
International Development Association  
Washington, D.C.



Dear Mr. Clausen:

I refer to Resolution No. 117 of the Board of Governors of the Association authorizing the Sixth Replenishment of the Association's resources.

The Government of Argentina has already waived, in respect of part of its subscription and contribution under the Sixth Replenishment, the limitations which are set forth in paragraph 11(a) and (b) of said Resolution as regards the use by the Association of such subscription and contribution for purposes of credit commitments.

The Government of Argentina hereby notifies the Association that it waives these commitment authority limitations under Resolution No. 117 in respect of its total subscription and contribution to the Sixth Replenishment, thus releasing the entire balance not yet so made available for purposes of credit commitments.

Yours sincerely,

Jorge Wehbe  
Minister of Economy  
of Argentina

1770

VRD  
2/16/83

ARGENTINA

Briefing Paper for Visit of  
Messrs. Wehbe and Gonzalez del Solar<sup>1/</sup>  
February 1983

1. Messrs. Jorge Wehbe, Minister of Finance, and Julio Cesar Gonzalez del Solar, President of the Central Bank, will visit the Bank on February 9, 1983. They are expected to discuss the present Argentine economic crisis and ask for an increase in the volume of World Bank lending, including quick disbursing assistance.<sup>2/</sup>

Political and Economic Developments

2. Argentina is struggling to complete the transition to a civilian regime and to reactivate the economy. When the Government of President Bignone took office in July 1982, the country was demoralized and in a gloomy political impasse. The armed forces were split over the responsibility of the Falklands defeat, the naming of the new President and the transition to civilian rule. General Bignone's interim regime has managed to take root and should remain in office until elections are held in October. He governs, however, with a fragile mandate and both the civilian camp, where moderates and leftists prevail, and the rightist military groups, regard his actions warily. Lack of a solid political basis notwithstanding, this Government has negotiated a Fund stand-by in a surprisingly smooth fashion and, so far, kept the stabilization program in place. Exchange rate, monetary and fiscal policies are on target; public sector prices and tariff increases have been above the levels agreed with the Fund.

3. The Bignone Government inherited a severe economic situation: industrial output was declining for the tenth consecutive quarter, coming down to a level equivalent to only 2/3 of its level five years ago. Industrial labor force had shrunk by 38%, bringing the overall unemployment rate to 6%. Real wages had declined 31% during the previous six months. The country was already in arrears on its payments to foreign commercial banks and faced massive defaults by the end of 1982.

4. For the last seven months, the Government has been trying to: (i) negotiate an orderly rescheduling of the country's external debt; (ii) contain the renewed inflationary pressure; and (iii) reactivate the economy. To date it has achieved some success, though additional efforts will be needed.

5. The agreements with the IMF, the commercial banks and the Bank for International Settlements have provided short-term debt relief. The IMF agreed to provide US\$2.2 billion for 15 months; a commercial bank

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1/ Biographical Data attached as Annex I.

2/ Current approved lending program for FY83-87 attached as Annex II.

bridge loan of US\$1.1 billion is being disbursed and BIS recently announced a US\$0.5 billion loan. Agreement has been reached on a fresh US\$1.5 billion medium term loan; the loan will be signed in March and disbursed throughout 1983. The Central Bank is now beginning to negotiate the rescheduling of the public external debt due in 1983 (US\$ 12.3 billion).

6. The initial inflationary surge, which reached an average 21% per month during the third quarter of 1982, reflected the effects of the financial measures and the large-scale devaluations (60% in three months). To absorb excess liquidity, the Treasury has introduced bonds with higher interest. While attempts at voluntary price controls have not been very productive, restrictive fiscal and monetary policies have finally brought the rate of inflation down to an average level of 10% per month. The IMF ceiling on the expansion of net domestic credit to the public sector should help reduce it further.

7. To reverse the recessionary trend, the Government introduced interest rate ceilings and established large rediscount schemes easing the industrial sector's liquidity problem which was also threatening the solvency of the financial institutions. A substantial part (estimated to be more than 40%) of industrial debt was written off by this subsidized credit. Firms have begun to rehire labor, but industrial investment is still lagging, primarily because of political uncertainty but also because of the shortage of foreign credit which makes importing intermediate inputs increasingly difficult. In its efforts to mobilize more foreign exchange for intermediate input imports, the Bignone Government has promised an incentive scheme (not yet announced) to induce the repatriation of Argentine capital abroad. The Government is also looking to other sources, including quick disbursing assistance from the Bank, to help finance imports of intermediate goods.

8. After two years of falling output and large current account deficits, GDP growth in 1983 is expected to be positive and the current account manageable. Although the officially targeted 5% growth may be optimistic, a 2% to 3% growth should not be difficult to achieve for an economy producing 11% below the GDP of 1979. The prospects for export growth in 1983 are good: the record wheat harvest and the realistic exchange rate policy will contribute to make this year's trade surplus even larger than that of 1982. The question whether growth will be severely constrained by balance-of-payments difficulties depends mainly on the success of the debt rescheduling discussions and on the maintenance of a realistic exchange rate policy. Overall, it appears that the economy is finally leading towards a more stable path with positive growth, reduced unemployment and lower inflation. However, a full-scale economic recovery in 1983 is not expected, as uncertainty about political developments is forestalling investments.

#### Bank Lending and Economic Program

9. The current FY83-87 Lending Program stands at US\$800 million of which US\$200 million is allocated for two loans in FY83-84. The Highway Sector Loan (US\$100 million, FY84S) has been appraised, but work is still being done to clarify the participation of the Provincial Governments in the loan. We hope to negotiate the loan in April and present it to the Board in June 1983. The Second Oil and Gas Development Loan (US\$100 million, FY84), whose appraisal began January 31, would assist

exploration and development activities of the state oil company, Yacimientos Petroliferos Fiscales (YPF).

10. Quick Disbursing Loan. Neither of the above loans would meet the Government's need for quick disbursing assistance. At most they would probably generate US\$10-20 million in disbursements in 1983. In addition, the ten on-going loans currently being disbursed will probably provide about \$120-150 million in foreign exchange to the Government (the higher figure assumes problems are resolved holding up progress in Yacyreta project, discussed below). The Government desires more Bank assistance than the above sources would provide. The delegation is expected to seek your approval for two quick disbursing loans in 1983 of US\$250 million each.

11. For the moment, there are strong reasons for skepticism regarding such a request. While the Government is considering a strengthening of the export law and liberalization of the temporary import admission regime, it has yet to put forward a coherent set of policies indicating how they intend to get the productive sectors of the economy moving again. Even assuming such policies could be drawn up rapidly, their implementation by an interim government may prove impossible. And the degree to which this government can give credible commitments binding its successors, seems quite limited.

12. Nonetheless, the Bank can somewhat increase its assistance to Argentina in the short-term by restructuring the Second Industrial Credit Project (US\$100 million loan of November 30, 1982). The loan, made to Banco Nacional de Desarrollo (BANADE) for industrial subprojects, could be modified to permit subloans for working capital, or creation of a revolving fund to allow subborrowers to import raw materials and spare parts. BANADE believes its subborrowers, mostly medium-sized private industrial companies, could utilize US\$50-60 million of our loan for this purpose in 1983. If we pursued this course, our total disbursements in Argentina could amount to about US\$200 million over the next twelve months.

13. The Bank's economic work program includes a mission in April 1983 to review trade policy and industrial sector performance. The mission will examine existing export incentives and possibilities for the rationalization of the trade regime as well as the Government's policy framework for industrial sector promotion, to determine if a case can be made in the Bank for supporting such initiatives with a Program Loan or Industrial Exports Credit. Technically, a loan of this nature could be ready by the end of 1983 and acted upon once the political situation had attained a reasonable amount of stability (that is, after an elected Government comes to office).

#### Issues

14. Yacyreta Hydroelectric Project (signed in November 1979; US\$210.0 million). The bid evaluation for the main civil works contract, received in November 1981, was found to be incompatible with ICB policies. The Bank suggested that the Government negotiate with the lowest evaluated bidder or rebid. In order to meet the Bank's views, the Government was bringing together the two lowest bidders to form a joint venture when the Falkland crisis and EEC economic sanctions forced a delay. In response to our pressure for a decision on the procurement

problem, the Argentines are again pursuing the joint venture concept along satisfactory lines, although they recently informed the bidders that they had to provide for a majority of the civil works to be performed by local contractors. We have advised the Government that such a restriction violates our procurement guidelines. (We now understand that the Paraguayan Government is holding out for a larger Paraguayan share whereas the Argentine members of the consortium would be satisfied with their part). The Government also needs to submit to us a new financial plan demonstrating their ability to meet Yacyreta's sizeable financial costs. Quick action on awarding the main civil works contract and preparing a financial plan is necessary for disbursements of the loan to commence this year.

15. Co-financing. The Argentine Government has told us that it intends to press again for exclusion of co-financed loans from the rescheduling of its commercial debt. It also has offered to discuss this matter with the Brazilian and Mexican Governments in an attempt to reach a common position among the three countries vis-a-vis the commercial banks. The Argentine Central Bank feels that active high level Bank intervention with the commercial banks is required to avoid rescheduling of the co-financed loans and wants to inquire about the Bank's position in this respect.

Attachments

BIOGRAPHICAL INFORMATION

Dr. Jorge Wehbe. Sixty-two year old Minister of Economy, Treasury and Finance since August 24, 1982, graduated from the Law Faculty of the University of Buenos Aires. He is the first Argentine to have been appointed Minister of Economy three times, having held the post in 1962 and 1972 respectively under short-lived governments. He has served as either the president or a director of four major Argentine banks, has taught financial law in local universities and has been long associated with the Argentine automobile industry.

Dr. Julio Cesar Gonzalez del Solar. Sixty-six year old President of the Central Bank since August 26, 1982, graduated from the Faculty of Economic Sciences of the University of Buenos Aires. He also has a PhD in economics from Harvard University. His latest appointment brings him back to the Central Bank where he first worked from 1935 to 1946, and served as vice president in 1959-61. He also has been an advisor to the Finance Ministry (1957-59); a consultant to the Guatemalan Government economic and financial authorities; a consultant to the Bank and an IMF staff member. Dr. Gonzalez del Solar has been active in Argentine private banking and industry over many years.

FIVE YEAR LENDING PROGRAM AS OF 12/31/82  
 RUN ON 01/03/83

ARGENTINA

MID-81 POPULATION: 28,137,000

GNP PER CAPITA: 2,560

	FY 83 - 84		IDA ALLOCATIONS		FY 83 - 87	
	IBRD	IDA	FY 81 - 83	FY 84 - 86	IBRD	IDA
REVIEW GROUP 12/06/82	200.0	.0	.0	.0	800.0	.0
CUR REV GROUP 12/06/82	200.0	.0	.0	.0	800.0	.0
LAC PROGRAM	200.0	.0	.0	.0	800.0	.0
AVG. ANNUAL PER CAPITA LENDING						
REVIEW GROUP		3.55				5.69
CURRENT REVIEW GROUP		3.55				5.69
LAC PROGRAM		3.55				5.69

FISCAL	YEAR	PROJECT NAME	RESERVE PROJECTS								
			BANK/IDA	SOURCE	FY 83	FY 84	FY 85	FY 86	FY 87	FY 88	
TH05	84S	HIGHWAY SECTOR		IBRD		100.0					
GI03	84	OIL & GAS DEVT II		IBRD		100.0					
TP03	85S	BAHIA BLANCA PORT		IBRD				155.0			
GI04	85	OIL & GAS CREDIT II		IBRD				150.0			
TRO3	85R	RAILWAYS III	125.0	IBRD							
WU01	86S	WATER SUPPLY & SEWERAGE		IBRD				195.0			
GI05	87	OIL & GAS DEVT III		IBRD						100.0	
DD05	88S	INDUSTRIAL CREDIT III		IBRD							100.0
GI06	88	OIL & GAS CREDIT III		IBRD							150.0
TP02	88R	PORTS II	150.0	IBRD							

## COUNTRY TOTAL

IBRD	.0	200.0	305.0	195.0	100.0	250.0
	0	2	2	1	1	2
IDA	.0	.0	.0	.0	.0	.0
	0	0	0	0	0	0
TOTAL		200.0	305.0	195.0	100.0	250.0
		0	2	2	1	1
OF WHICH 'S'		100.0	155.0	195.0		100.0
		1	1	1		1

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MID-81 POPULATION: 28,127,000

GDP PER CAPITA: 2,420

FY 83 - 87

IDR ALLOCATIONS

FY 83 - 84

1983 1984

FY 81 - 82 FY 84 - 84

1983 1984

800.0 800.0

.0 .0

200.0 200.0

.0 .0

.0 .0

200.0 200.0

.0 .0

.0 .0

200.0 200.0

2.52

2.52

2.42

2.52

2.42

2.52

CODE	YEAR	PROJECT NAME	BANK/PROJECT SOURCE	REVENUE				
				FY 83	FY 84	FY 85	FY 86	FY 87
1903	88	GR. PORTS II	1980					
1904	88	OT 1 GAS REFIN III	1980					
1905	88	INDUSTRIAL CREDIT III	1980					
1906	88	OT 1 GAS REFIN III	1980					
1907	88	WATER SUPPLY & SEWERAGE	1980					
1908	88	RAILWAYS III	1980					
1909	88	OT 1 GAS CREDIT II	1980					
1910	88	RAMPA CLAMPA PART	1980					
1911	88	OT 1 GAS REFIN II	1980					
1912	88	HIGHWAY 2000	1980					
				100.0				
					100.0			
						100.0		
							100.0	
								100.0
								100.0

COUNTRY TOTAL	TOTAL				
	1980	1981	1982	1983	1984
100.0	100.0	100.0	100.0	100.0	100.0
100.0	100.0	100.0	100.0	100.0	100.0
100.0	100.0	100.0	100.0	100.0	100.0
100.0	100.0	100.0	100.0	100.0	100.0
100.0	100.0	100.0	100.0	100.0	100.0
100.0	100.0	100.0	100.0	100.0	100.0
100.0	100.0	100.0	100.0	100.0	100.0
100.0	100.0	100.0	100.0	100.0	100.0
100.0	100.0	100.0	100.0	100.0	100.0

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1983 FEB - 8 PM 1: 38  
OFFICE OF THE PRESIDENT



## OFFICE MEMORANDUM

DECLASSIFIED

JAN 05 2017

WBG ARCHIVES

DATE: February 3, 1983

CONFIDENTIAL

TO: Mr. Yves Rovani  
FROM: Philippe Bourcier  
SUBJECT: Argentina and Colombia - Petroleum Projects

1. Following your request I have reviewed our past and current activities in Argentina and Colombia to determine if we may have given reasons to the US Ambassador for complaining that we were pushing our way into petroleum at the expense of the private sector.
2. In Colombia the secondary recovery project has been in abeyance since June 1980 when the Division's last mission visited Bogota.
3. In Argentina, the Oil and Gas Engineering Loan (1880-AR) is almost fully disbursed and is aimed at providing a better basis for private oil companies participation. The Oil and Gas Credit (2031-AR) supports private investment. The proposed loan to YPF which would support a slice of YPF's investment program is conditioned on satisfactory renegotiations of contracts with private companies and on a satisfactory setting of product prices. Both conditions are prerequisite to further investment in the private sector and should be looked upon favorably by oil companies. A pre-appraisal mission is currently in the field.
4. In both cases I do not see any ground for the claim made by Mr. Hoguet.

cleared with and cc. Mr. Bauer

PBourcier:mds

INTERNATIONAL MONETARY FUND  
THE WORLD BANK

Boards of Governors • 1982 Annual Meetings • Toronto, Ontario, Canada

MEMORANDUM FOR THE RECORD

Prior to August 9, 1982

Mail Address:  
JOINT SECRETARIAT  
IMF—WORLD BANK  
WASHINGTON, D. C. 20431 U.S.A.

Cable Address:  
INTERMEET  
WASHINGTONDC (USA)

Telex Addresses:  
(RCA) 248331 IMF UR  
(ITT) 440040 FUND UI  
(WUI) 64111 INTERFUND  
(TRT) 197677 FUND UT

After August 9, 1982

Mail Address:  
JOINT SECRETARIAT  
IMF—WORLD BANK  
P.O. BOX No. 4217  
STATION A  
TORONTO, ONT. M5W 1V9  
CANADA

Cable Address:  
INTERMEET  
TORONTO  
CANADA

Telex Address:  
06-218811  
INTERMEET TOR

FROM : E. Lerda

SUBJECT : Argentina - Meeting Between Mr. Clausen  
and Minister J. Wehbe

DATE : September 5, 1982

A meeting was held on September 4, 1982 in Toronto between Mr. Clausen and Minister of Economy Jorge Wehbe. Also present were Messrs. Gonzalez del Solar, Guillermo Blanco, Alberto Sola and Eduardo A. Zalduendo, as well as Messrs. Stern, Barletta and Lerda.

Minister Wehbe said that Argentina was fundamentally a solvent country which could and would honor its obligations. Mistakes had been made in the past and excessive debts falling due in the near future had been taken on, so that now help was needed to improve the maturity structure, but Argentina had a tradition of paying its debts which was not about to be broken. The program of payments that had to be worked out had to be such as to leave no doubt about Argentina's ability to comply with it in minute detail.

Mr. Clausen applauded this intention and agreed that the problem was basically a temporary liquidity squeeze, not a fundamental inability to service debt. But a program was needed, of course, to overcome even a temporary difficulty, and he asked the Minister what his plans were.

The Minister said that these included monetary, fiscal and financial measures which were being elaborated, as well as debt rescheduling in agreement with the commercial banks. These would include the U.K. banks; he was optimistic that an agreement would be reached. Eventually, he also would want to have an agreement with the IMF. He added that once the Bank of England removed its restrictions, the U.K. would receive net payments of some US\$300 million on official account that had already accumulated. The private Argentina funds blocked amounted to some US\$1.3 billion. The Minister stressed that he had consulted the major political leaders and had obtained general support for the approach outlined.

Continued on page 2 ....

A constitutional government would take office in the foreseeable future and it was his objective not to let them inherit an unmanageable situation.

In response to questions the Minister said that he attributed great importance to the prompt execution of the silos program, but said that what was needed were not large silos but on-farm silos, to avoid rail and shipping congestion.

He also said that early next year it would be possible financially to resume work on the Yacyreta project. He did not refer to the procurement issue.

Mr. Clausen stated his desire to be as helpful as possible in the solution of Argentina's serious difficulties, and the Minister praised the past help that Argentina had received from the Bank and stressed his appreciation for Mr. Clausen's forthcoming attitude.

c.c. Mr. Clausen's Office  
Mr. Stern's Office  
Mr. Ardito Barletta  
Mr. Scherer

**The World Bank**

1818 H Street, N.W.  
Washington, D.C. 20433, U.S.A.



With the compliments of  
**Alberto Sola**  
Alternate Executive Director

April 5, 1982

Attached please find the statement of the Minister  
of Foreign Relations of Argentina at the UN  
Security Council Meeting held on Saturday,  
April 2.

The PRESIDENT (interpretation from French): The Security Council will now resume its consideration of the item on its agenda.

The first speaker is the Minister for Foreign Affairs of Argentina, His Excellency Mr. Nicanor Costa Mendez. I welcome him and invite him to make his statement.

Mr. COSTA MENDEZ (Argentina) (interpretation from Spanish): Perhaps the beginning of my statement may be considered repetitive, but I consider it none the less useful to state that the reason for the calling of these meetings lies in the Malvinas Islands, which is part of Argentine territory and which was illegally occupied by the United Kingdom in 1833 by an act of force which deprived our country of that archipelago.

The British fleet in 1833 displaced by force the Argentine population and the authorities which were exercising the legitimate rights that belonged to the Republic at that time as the heir to Spain.

Legally speaking, that act of force cannot give rise to any right at all, and politically the events of 1833 were one more reflection of the imperialist policy which the European States carried out in the nineteenth century at the expense of America, Africa and Asia. Hence, we can say today that this is a colonial problem in the most traditional sense of that political and economic phenomenon.

Since 1833, the Republic of Argentina has been claiming reparation from the United Kingdom for the great wrong done. The Republic of Argentina has never consented to that act of usurpation of its national territory, usurpation carried out by unacceptable and illegal means. All the successive Governments of Argentina, regardless of party or faction, have remained united and steadfast in their position during those 149 years of strongly protesting against that arbitrary occupation.

(Mr. Costa Mendez, Argentina)

No one can have the slightest doubt as to the historic role of the United Nations in the decolonization process. This is perhaps the area in which the United Nations has proved most fruitful, a task that it has carried out most effectively, one that has changed the course of international relations. Proof of this is that the original membership of 54 has increased to 157. Many of the young nations represented here in the Council have been freed from the colonial yoke, and their contribution to the organized international community is of such magnitude that I do not need to mention it - far less to emphasize it.

Of the 54 original Members 20 belong to the Latin American Group, and their decisive influence in the early days of the Organization must be recognized. That group of nations was very active in giving impetus to the decolonization process. The Latin American Group was, if we may say so, a champion of that cause, because it had suffered from the effects of colonization. We too had been colonies: we too had fought the hard struggles for national independence.

One of the last vestiges of colonialism on Latin American territory ended yesterday. The claims that my country has been making repeatedly since 1833 have enjoyed the support of the decisions of the world Organization, and of the individual assistance of these new nations just emerging from the colonial era.

Despite the Organization's efforts and my country's arduous and careful work, time passed and brought with it only continued frustration, resulting from the evasive tactics and time-wasting manoeuvres of Great Britain - and all that despite the many alternatives put forward by Argentina and despite the imagination and flexibility with which we approached negotiations.

Two days ago the Permanent Representative of my country made reference here to the willingness and readiness on our part demonstrated by the facilities offered in 1971 in terms of communications and other concessions to the inhabitants of the islands. Those 1,800 inhabitants, as the United Kingdom representative

(Mr. Costa Mendez, Argentina)

said yesterday would fit without difficulty into this chamber. They have been and are the subject of constant concern in Argentina, which has given them attention that I venture to say, with all due respect, they have not received from their "homeland". The Government of Argentina is always careful to respect individual rights and physical integrity.

Yesterday Argentina stated that its position did not represent any kind of aggression against the present inhabitants of the islands, whose rights and way of life - and I stress this - will be respected in the same way as those of the countries freed by our liberators. Troops will be used only when absolutely necessary and they will not in any way disturb the inhabitants of the islands; quite the contrary, they will protect the institutions and inhabitants, since they are part of us. This is a most solemn commitment by the Government of Argentina to the international community.

The United Kingdom has invoked the presence of the inhabitants of the Malvinas Islands as an excuse for its colonial presence in those islands. But I ask members: What, then, is the pretext for that presence in the South Sandwich or South Georgia Islands? I here, as the Times of London said in an editorial of 29 March last, "the only natives, according to the Commonwealth and Foreign Offices, were seals - and in the present state of international law seals do not enjoy the right to self-determination?"

In view of the fact that my country opened up communications, the British Government did not seem too concerned over the physical and historical isolation in which the inhabitants of the islands lived.

I shall not go into details about the change in the standard of living brought about by the facilities offered by Argentina. As the President of my country has said, we are ready to guarantee all the individual rights of the inhabitants. But we cannot allow anyone to use those 1,800 persons as something enshrined in international law as a "population".

(Mr. Costa Mendez, Argentina)

In previous statements the characteristics of that group of persons have been dealt with, but I must say again here that, to a large extent, those persons are officials of the British Government and a large number of them are employees of the Falkland Islands Company, a typical colonial firm - a complete anachronism: a colonial corporation of those who had letters patent from the eighteenth century, the trade branch of colonialism and imperialism; history offers various examples of this.

Those foreigners with interests there, with no right other than trade and colonial ones, are those who most strongly and systematically have prevented the British Government from taking action.

Of necessity, the recalcitrant attitude of the British Government that I have mentioned brought about tension and difficulties. More than once peace and security in the region were threatened by the persistent colonial presence.

We have already mentioned in another statement the Shackleton incident of 1976, an episode - and I wish to emphasize this although I am sorry to have to cite this - that supplies a fine example of the Inter-American Committee's resolution, which states:

"Threats to peace and security in the region, together with flagrant violations of international rules on non-interference, are constituted by the presence of foreign war ships in American waters, and also by the announcements made by the British Government concerning their dispatch of other vessels."

It would seem that this would apply equally well today.

The foregoing episode and the episode I have mentioned which was the immediate origin of the present situation are both covered in the statement made by the Permanent Representative of my country and the letter dated 1 April 1982 from my Government to the Security Council which has been circulated as document S/14940.

(Mr. Costa Mendez, Argentina)

That incident was serious, but was made even more serious by the United Kingdom because it sent warships to the region in a clear attempt at intimidation, which constituted a real threat to my country and to the continent. Hence the statement I have just read out about the Shackleton episode from the Inter-American Committee is still fully valid in 1982.

The military preparations and the despatch of warships to the region by the United Kingdom, to which I have already referred, explain and justify the actions taken of necessity by the Government of Argentina in defence of its rights.

Some delegations here have stated that my Government acted hastily. I leave it to the Council to judge, but I must point out that it seems difficult to describe my country as acting hastily when, with the greatest respect for peaceful solutions, it has borne with a situation of continued usurpation of its territory by a colonial Power for 150 years. Argentina has wisely, patiently and imaginatively negotiated on its long-standing claim but the United Kingdom has not given the slightest indication of being flexible nor made a single just proposal. Furthermore, we have been accused in this chamber of violating Article 2 (3) and (4) of the United Nations Charter. No provision of the Charter can be taken to mean the legitimization of situations which have their origin in wrongful acts, in acts carried out before the Charter was adopted and which subsisted during its prevailing force. Today, in 1982, the purposes of the Organization cannot be invoked to justify acts carried out in the last century in flagrant violation of principles that are today embodied in international law.

Throughout the years we have celebrated the excellent results of the irreversible march of history typified by decolonization and at the same time, while we were celebrating and taking part in that process, our frustration was growing because of the conviction that the United Kingdom was not ready to give up the territory it had usurped from Argentina. The accession of emerging peoples to international politics and the change in international society are a result of the historic process I mentioned at the beginning of my statement. This is a real force, and this real force in the world order was reflected in the

(Mr. Costa Mendez, Argentina)

establishment of the Non-Aligned Movement, which my country joined in 1973 and in which it takes part as an active member. That Movement promotes the eradicating of historical injustices, whether they be political or economic. Members of the Non-Aligned Movement, as our Permanent Representative has already said, have repeatedly recognized and acknowledged the justice of the Argentine claim and our country's sovereignty over the Malvinas Islands, the South Georgia and Sandwich Islands, they have already stated that the principle of self-determination does not apply in this case for special historical reasons I have already explained.

The representative of the United Kingdom said that he had doubts about being able to arrive at an agreement with the representative of my country as to the historical vicissitudes. That is possible, but it would seem difficult for us not to agree on the facts of history which are absolutely indisputable.

The Government of Argentina has not invaded any foreign territory, as the United Kingdom claims. As was stated very simply by the President of my country,

"Safeguarding our national honour and without rancour or bitterness, but with all the strength that comes from being in the right, we have recovered a part of our national heritage".

The same cannot be said of the United Kingdom Government vis-à-vis our country.

Apart from the case which concerns us today, in 1806 and 1807 British expeditionary forces attacked and temporarily occupied the city of Buenos Aires and its suburbs, a historical fact that may not be well known to everybody. On both occasions the British troops were repelled by the Argentine people. In 1840 and in 1848 the Government of Great Britain organized naval blockades against the Republic of Argentina, and, to abide by historical facts, it is rather strange to notice that another colonial power, France, whose representative was so quick to rally to the colonial position yesterday, was already associated in 1848 with these colonial ventures since it took part in the blockade that year that I have mentioned.

(Mr. Costa Mendez, Argentina)

All that is by way of providing the Council with the background. None the less, I want to mention something familiar to all members of the Council.

Yesterday France made reference to the Malvinas Islands and even mentioned them by their English name, ignoring the General Assembly decision which provides that in referring to the islands they shall be called the Malvinas Islands and the Falkland Islands - always using both names. The representative of France and all representatives of the French-speaking nations in the Organization cannot be unaware that the name Malvinas has its origin in the famous trip made by Bougainville from Saint Malo to the Archipelago; it became "Malouines", which was hispanized to "Malvinas".

(Mr. Costa Mendez, Argentina)

I dare not think that there may be ideological or political subtleties underlying this historical error of language, but I mention it because it is surprising.

I have made reference to something of which everyone is aware: the spirit of conciliation and the firm resolution of successive Governments of Argentina to seek by peaceful means a solution to our dispute with Great Britain. Furthermore, everyone is aware that on several occasions our Government has had to discourage sectors of the Argentine community that considered that the total lack of response from the British community made imperative the use of other means. Recent events have affirmed our presence in the islands, and we have offered every guarantee and safeguard so that the new state of peace may be maintained. We have again here told the British Government that we are ready and willing to negotiate and to hear its position. But we must make it absolutely clear in this chamber that any change or disturbance in the peace that may come about from now on in the area of the islands will be the sole responsibility of the United Kingdom.

There is something of which members may not be so aware. The Government of Argentina, after very lengthy negotiations, all fruitless in view of the reluctance of Great Britain, finally proposed a written paper to institutionalize the meetings and to structure the talks so that we could move forward to a peaceful, honourable and just solution. We thus handed the British Embassy a document before a meeting that was to be held on 4 February 1982 with the express, formal and pressing request that it should be answered on the occasion of the meeting. The British delegation, always cordial in matters of form, agreed to the meeting but gave no response to our presentation despite our urgent request. We called upon the meeting to set a date for the response. No date was agreed to. We asked that it should be before the end of March. We were told that they would think about it, but that it was not possible to give any date at that time.

I want to tell members that Argentina felt great discouragement, sadness, and frustration at hearing all that non-news. And yet, despite that recalcitrance, despite that inexplicable reluctance, the Government of Argentina offered a press release that we believed to be extremely important. I shall now read it out:

(Mr. Costa Mendez, Argentina)

"The representatives of Argentina and the United Kingdom, at a meeting in New York in February, have considered an Argentine proposal for the establishment of a system of monthly meetings with a pre-established agenda, the venue to be established beforehand, presided over by officials from the highest echelons. Such meetings will have the purpose of speeding up to the utmost the on-going negotiations to arrive at recognition of Argentine sovereignty over the islands and of thus obtaining substantial results within a time-limit which at this stage of the talks must of necessity be short.

"Argentina has negotiated with Great Britain with patience, honesty and good faith for more than 15 years within the framework mentioned in the relevant resolutions of the United Nations to arrive at a solution to the dispute over the sovereignty of the islands. The new system is an effective measure to arrive at a prompt solution.

"However, if this does not come about, if there is no response from the British side, Argentina reserves the right to put an end to the operation of such a mechanism and freely to choose the procedure it deems most fit in accordance with its interests."

This forewarning was given to the representative of Great Britain. There was not, and there has not been as yet, any reply except the presence of HMS Endurance in the Georgias and a note from Lord Carrington the terms of which I shall refrain from mentioning for various reasons.

I now wish to make reference to the draft resolution submitted by the United Kingdom. It speaks volumes that the terms are absolutely identical to those put forward more than 22 years ago in this same chamber in the case of Goa, when Portugal was hanging on to its colonial power, which consumed it and gave rise to a new Portugal. That resolution sought to deny India its territorial rights, just as an attempt is being made here to deny my country its proper rights. That draft resolution was thrown out by the Council because it was merely a defence, an expression of continuing colonialism.

(Mr. Costa Mendez, Argentina)

The United Kingdom is the only other party to this dispute. It is the only sponsor of the single draft resolution before the Council. This also is strange. In trying to deny us our territorial integrity and our right to it, the United Kingdom calls for the withdrawal of the Argentine troops which recovered the Malvinas for national sovereignty. If the United Kingdom took those islands through an illegitimate act of force, why has it not withdrawn in the last 149 years on the basis of the same principles that it is today invoking in order to avoid this conflict, which now seems to be of such deep concern to it?

Obviously I am at variance with the draft resolution submitted by the United Kingdom, but I wish to say that I am in agreement on one point. The Republic of Argentina is threatening nobody; the Republic of Argentina is not carrying out acts of aggression or hostility against anyone. It is of no interest to us to have any armed confrontation with anybody at all. We are ready to negotiate through diplomatic channels. I would say that again: we are willing to negotiate through diplomatic channels any differences we have with the United Kingdom except our sovereignty, which is not open to negotiation.

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(Mr. Costa Mendez, Argentina)

We have a clear conscience about our rights, and we shall maintain them with firmness and prudence until we arrive at a proper and peaceful settlement. It is useless to whip up emotions when there is clear justice, as in our case. Our policy, the policy of Argentina has, at all time been lofty, conciliatory and prudent - and there is no evidence to the contrary. I am sure that it will lose none of those attributes here.

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*Ministro de Economía*

BUENOS AIRES, January 25 th., 1982

Mr. A.W. Clausen  
President  
The World Bank  
Washington D.C. 20433  
U.S.A.

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Dear Mr. Clausen:

I thank you very much for your kind letter for my appointment as Governor for Argentina in the World Bank.

I look forward to work together with you and the staff of the World Bank, in matters of common concern as I did when I held the same office twenty years ago.

Sincerely,

*Roberto T. Alemann*

DR. ROBERTO T. ALEMANN

Copy sent to Barletta

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JAN 27 1982  
SECRETARIADO



Office of the Secretary of State

BUENOS AIRES, January 25th, 1952

Mr. A. W. Gissen  
President  
The World Bank  
Washington D. C. 20543  
U.S.A.

Dear Mr. Gissen:

I thank you very much for your kind letter for my appointment as Governor for Argentina in the World Bank.

I look forward to work together with you and the staff of the World Bank in matters of common concern as I did when I held the same office twenty years ago.

Sincerely,  
Dwight D. Eisenhower

OFFICE OF THE PRESIDENT

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JAN 13 1982

Dear Mr. Minister:

It is indeed good to know that you have been appointed Governor for Argentina on the Board of Governors of the World Bank. Congratulations!

The Executive Directors, Officers and Staff join me in extending to you a warm welcome. We look forward to your participation in the affairs of the Bank.

On a personal note, I hope to have the opportunity of greeting you here in Washington in the near future.

Sincerely,

A.W. Clausen

Su Excelencia  
Senor Dr. Roberto T. Alemann  
Ministro de Economia,  
Hacienda y Finanzas  
Hipolito Yrigoyen 250  
Buenos Aires, Argentina

cc: Mr. Blanco  
Mr. Lerdau  
Mr. Adams

HM Fleming:ets

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ROUTING SLIP

DATE

Dec. 17, 1981

FROM THE OFFICE OF THE  
REGIONAL VICE PRESIDENT

NAME

ROOM NO.

~~Mr. Skon~~

~~Mr. Clausen~~

~~A~~

APPROPRIATE DISPOSITION

NOTE AND RETURN

APPROVAL

NOTE AND SEND ON

COMMENT

PER OUR CONVERSATION

FOR ACTION

PER YOUR REQUEST

INFORMATION

PREPARE REPLY

INITIAL

RECOMMENDATION

NOTE AND FILE

SIGNATURE

REMARKS

Useful information

Update on the political  
change in Argentina.

~~Ernie~~

FROM

N. ARDITO BARLETTA

NOTE

December 17, 1981

Mr. Lerdau:

Re: ARGENTINA--Political Developments

1. As you know, the military Junta has removed General Viola from the Presidency. Subsequently, the entire cabinet submitted resignations but only those of Messrs. Camilion (Foreign Affairs), Liendo (Interior), Kuhl (Industry) and Urricariet (Public Works) were accepted. Admiral Lacoste (Minister of Welfare) will head a caretaker Government until December 22, when General Galtieri will be sworn in as President. The decision of the Junta marks the end of protracted negotiations with General Viola, whose political fortunes had been declining rapidly. The Junta had wanted Viola to step down for reasons of poor health. His hospitalization for heart ailments notwithstanding, Viola apparently felt that he was sufficiently fit to continue as President. He was unwilling to take the exit custom-made for him and conditioned his resignation on an explicit recognition of political causes underlying it. The Junta did not accept and finally ousted him without explanation. What may seem a trivial issue at first glance is of considerable importance to the military. They had wanted to uphold the principle that Presidents appointed by the Junta serve their full term as safeguard against political pressure to change the system.

2. General Galtieri has come out of the power struggle as undisputed strong-man. He was able to retire virtually all the senior Generals who might have challenged him and to appoint men of his confidence to key positions. General Galtieri will keep his present position as Commander in Chief of the Armed Forces. This arrangement, as replicate of the early Videla years, is intended to give him the necessary authority and credibility to get the house into order. People who know Galtieri have little doubt that he will make full use of his power; opinions are divided on whether he will do so judiciously. Galtieri is portrayed as a headstrong, short tempered and even tempestuous man. He is not afraid to take decisions nor wage a fight. In his speeches and statements, Galtieri has not impressed with analytical intelligence nor with eloquence. However, his closest advisors and confidants are reportedly men with solid professional formation, good mind and balanced judgment. Politically, Galtieri is characterized as a liberal, his traditional military mold notwithstanding.

3. The military apparently have been caught off guard by the premature change in the Presidency, planned to coincide with the anniversary evaluation of the Viola administration in March 1982. Galtieri decided to select his cabinet in a swoop, presumably to avoid the risks of an extended interim period. The selection process and the timing of program formulation will provide a good basis on which to forecast Galtieri's modus operandi and test his judgment. Should Galtieri concentrate on a few key appointments, he probably would give his ministers considerable freedom in the management of their portfolios. Should he announce his economic program early, he probably wants to demonstrate his capacity to get things done, thus distinguishing himself from his predecessor. In case he allows the time for

careful analysis, he is likely to put a premium on a well orchestrated performance to inspire confidence. Whatever his decision, Galtieri apparently believes, as do many Argentines, that the ambiguities and conflicting signals of the Viola administration have contributed in large measure to the present economic problem. To ensure clear and consistent guidelines that allow for predictability, he apparently has already decided on a reorganization of the economic cabinet. It is expected that the functions of the Ministries of Finance, Commerce, Industry and Agriculture and of the Presidential Planning Office will be centralized in a Ministry of Economy and that the public enterprises and agencies will be controlled through a Ministry of Public Works and Services.

4. The institutional change may signal not only a return to the practice but also to the economic strategy of the Videla administration. Galtieri is said to favor, with the broad support of the military, policies along the lines of the 1976 liberalization program. In particular, Galtieri is likely to press hard for a reduction in the participation of the public sector in the economy. At the same time he seems to favor a reduction in private sector subsidies and protection. This expectation is based to some extent on the dismissal of the ministers reportedly close to the Desarrollistas and on the list of candidates for Minister of Economy. Adalbert Krieger, Danino Pastore and Roberto Aleman are mentioned as leading contenders. Yesterday evening Messrs. Krieger, Pastore and Liziardo (Minister of Finance under Lanusse) were invited for a meeting with General Galtieri and his inner military circle. Messrs. Aleman, Klein and Alsogaray (Minister of Economy under Frondisi) have been invited for today. The pressure on Mr. Krieger to accept seems to be building up. He had been approached already twice before the present series of meetings. General Galtieri and the military apparently think that Mr. Krieger, because of his prestige within the private sector, has the best chance to get the economy back on even keel. I was told that Mr. Aleman had also been approached earlier. The invitation of Mr. Klein came as a surprise even to him. I think that Danino Pastore will end up as Minister of Economy. Mr. Krieger has strong personal reasons not to accept even though the formidable challenge may finally erode his resistance. Mr. Aleman apparently has put forward conditions that Galtieri and the military may find difficult to swallow. Mr. Klein's chances are small (sic!); the military were quite irritated by the mutual vitriolic attacks of Messrs. Sigaut and Liendo on the one side and Martinez de Hoz on the other following publication of his book. Whoever the final choice may be, the trend is towards a candidate of "corte liberal" with prestige and proven merit.

5. Galtieri is probably going to slow down somewhat the dialogue with the political parties and trade unions. This would be in line with the apparently widespread concern among the military at the overtures of General Liendo, the former Minister of Interior. On the other hand, expectations are that Galtieri will strengthen the participation of civilians in the economic cabinet, notably in the management of decentralized public agencies. Resolution of the economic problems will have priority for Galtieri. Only with a healthy economy, the military think the political question can be approached with any expectation for a reasonable outcome (stabilization of traditional parties and shift of votes from the Peronist groups). The public is calm and the financial exchange rate has remained stable (reportedly without Central Bank intervention), a notable difference to the frenzy accompanying the previous change of Government. Imports though are said to be picking up in expectation of a devaluation of the commercial rate, possibly through a free float. The prevalent feeling seems to be one of relief that the period of uncertainty has ended and of expectation that a strong Government will come in. Because of its advance billing as a Government of strength, the new administration may well be

Very good  
man  
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former MINISTER  
I know  
him  
well.  
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able to thwart pressure of individual interest groups and succeed where its predecessor failed.

7. A thorough assessment of the implications the change in Government will have on our operations in Argentina can only be made after the cabinet has been appointed and formulated its program. There is, however, ground for a few speculative thoughts. The reorganization to centralize economic management may help expedite decision-making and facilitate the resolution of problems confronting ongoing as well as proposed projects. The general orientation of economic policies may provide a rather propitious framework for Bank lending. The names mentioned for senior positions in the Ministry of Economy would seem to augur well for constructive cooperation. On the other hand, Yacyreta may get us off to a bad start. In case of disagreement, the award of the civil works contract may well become a test case for the quality of the Bank's dialogue with the Government. I understand that Galtieri has pressed personally in favor of Impregilo. Obviously, the relationship will depend to a large degree on Galtieri's position towards the Bank, his willingness to accept outside conditions and the degree of his interference in economic decision-making. On balance, I think it is not inconceivable that we may be able to operate in Argentina more efficiently than we have in the past - and I thought I had become a pessimist.

  
Peter R. Scherer

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Peter H. ...

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