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CONFIDENTIAL

January 10, 1983

To: Members of the Executive Board

From: The Secretary

Subject: Argentina - Staff Report for the 1982 Article IV Consultation and Request for Stand-By Arrangement

Attached for consideration by the Executive Directors is the staff report for the 1982 Article IV consultation with Argentina and a request from Argentina for a stand-by arrangement. Draft decisions appear on page 33.

This subject, together with a request from Argentina for a purchase under the compensatory financing facility (document to be issued), has been tentatively scheduled for discussion on Monday, January 24, 1983.

Att: (1)

CONFIDENTIAL

INTERNATIONAL MONETARY FUND

ARGENTINA

Staff Report for the 1982 Article IV Consultation and Request for Stand-by Arrangement 1/

Prepared by the Western Hemisphere and Exchange and Trade Relations Departments

(In consultation with the Legal and Treasurer's Departments)

Approved by Eduardo Wiesner and Manuel Guitian

January 10, 1983

I. Introduction

The 1982 Article IV consultation discussions with Argentina were held in Buenos Aires during September 22-October 27, 1982. Discussions on the authorities' economic program and on a request for a stand-by arrangement in support of the program were initiated at that time, were continued in Washington in the second week of November, and were concluded in Buenos Aires during the period December 6-10, 1982. The Argentine representatives in these discussions included the Ministers of Economy and of Public Works and Services; the President of the Central Bank of the Argentine Republic; the Secretaries of Agriculture, Finance, and Industry; the Undersecretaries of Economy, External Trade and Domestic Marketing, and other senior officials.

The staff representatives in the first round of discussions were C. Brachet (Head-WHD), H. Arbulu-Neira (WHD), K.B. Dillon (ETR), H. Puentes (EXR), L. Ramirez-Rojas (EP-WHD), B. Stuart (WHD), and A. Bitchakas (Secretary-WHD). Mr. Robichek joined them in Buenos Aires from October 17-27. This same team participated in the November discussions in Washington on which occasion the Argentine representatives also met several times with the Managing Director and Deputy Managing Director. The staff team that returned to Buenos Aires in early December included K.B. Dillon (Head-ETR), H. Arbulu-Neira (WHD) L. Ramirez-Rojas (EP-WHD), B. Stuart (WHD) and M. Greenleaf (Secretary-EXR). Mr. M. Teijeiro, Alternate Executive Director for Argentina, participated in all stages of the discussions.

1/ In accordance with suggestions made by Executive Directors concerning the documentation for Board discussion on country matters (EBM/81/52, April 9, 1981), this paper combines in one document material for the Article IV consultation and the presentation of a program to be supported by the use of Fund resources.

In the attached letter dated January 7, 1983, signed by the Minister of Economy of Argentina and the President of the Central Bank, the Government of Argentina requests a stand-by arrangement in an amount equivalent to SDR 1,500 million. In two memoranda attached to the letter, the Argentine authorities set forth an economic program for a 15-month period, the time the present Government is to be in office. Of the amount requested under the stand-by arrangement, SDR 745.7 million would come from ordinary resources, and SDR 754.3 million from borrowed resources. The Argentine authorities also will shortly request a purchase under the Compensatory Financing Facility in an amount equivalent to SDR 520.1 million, a request dealt with in a separate document circulated jointly with this paper.

Purchases under the requested stand-by arrangement would not exceed the equivalent of SDR 300.74 million until May 20, 1983, SDR 600.51 million until August 20, 1983, SDR 900.27 million until November 20, 1983, and SDR 1,200.04 million until February 20, 1984. A waiver of the condition in Article V Section 3(b)(iii) of the Articles of Agreement is required.

In early 1983, Argentina purchased the balance of its reserve tranche and the Fund's holdings of Argentine pesos stand at present at 100 per cent of Argentina's quota of SDR 802.5 million.1/ Full utilization of the requested stand-by arrangement would raise the Fund's holdings of pesos as of March 31, 1984 to 186.9 per cent of quota under tranche policy (Table 1). Including the purchase that is to be requested under the Compensatory Financing Facility, Argentina's total use of Fund credit would rise to 251.7 per cent of quota.

Argentina is a participant in the Special Drawing Rights Department and has received allocations totaling SDR 318.4 million. Current holdings are zero. Further information on Argentina's relations with the Fund is presented in Appendix I.

It should be noted that the letter from the Minister of Economy and the President of the Central Bank indicates that, by the end of 1983 or early 1984, and should Argentina's then newly-elected authorities so request, the present Administration would be prepared to arrange for preliminary contacts between those authorities and the Fund staff with a view to facilitating continued Fund support of Argentina's economic and financial stabilization effort.

1/ Argentina has had nine stand-by arrangements with the Fund. The last one expired on September 15, 1978, and no purchases were made thereunder.

Table 1. Argentina: Projection of the IMF Position Under Tranche Policy and Compensatory Financing Facility 1/

	Outstanding December 31, 1982	Operations in 1983 Jan.-Apr.	May-July	Aug.-Oct.	Nov.-Dec.	Operations in 1984 Jan.-Mar.	Outstanding Mar. 31, 1984
		(In millions of SDRs)					
Purchases							
Stand-by	--	300.7	299.8	299.8	299.8	299.9	1,500.0
Ordinary resources	--	200.5	136.3	136.3	136.3	136.3	745.7
Enlarged access	--	100.2	163.5	163.5	163.6	163.6	754.3
Compensatory financing	--	520.1	--	--	--	--	
Repurchases		--	--	--	--	--	
Total holdings (end of period)		820.8	1,120.6	1,420.5	1,720.5	2,020.1	
Excluding compensatory facility		300.7	600.5	900.3	1,200.0	1,500.0	
		(In per cent of quota)					
Total holdings (end of period)		102.3	139.6	177.0	214.4	251.7	
Excluding compensatory facility		37.5	74.8	112.2	149.5	186.9	

Source: Fund staff projections.

1/ Partials may not add up to totals because of rounding.

II. Background and Recent Developments

1. Background

Argentina presently is in the midst of the most severe economic crisis it has experienced since World War II. Output stagnated in 1980, and since then there has been a cumulative decline in real GDP of 10 per cent (Table 2). With the recent sharp increase in factor payments abroad and the deterioration in the terms of trade, real per capita income is now at its lowest level in about ten years. Measured by changes in the wholesale price index, inflation accelerated from below 60 per cent during 1980 to 180 per cent during 1981, and about 310 per cent during 1982. (The rate of price increase reached an annual rate of 875 per cent in the third quarter of 1982.) Investment, real wages, and industrial employment have plummetted, and unemployment and underemployment are at their highest level in 10 years. There has been an almost fivefold increase in external debt since 1976, and the country faces a serious debt service problem. The cumulative overall balance of payments deficit amounted to US$12 billion in the period 1980-82, exceeding US$5 billion--or 6-1/2 per cent of GDP--in 1982 alone. In the past two years, there was extensive reliance on swaps and external bonds issued in lieu of payment for private sector foreign obligations; large payments arrears accumulated, and the Central Bank's freely disposable international reserves have fallen to a low level.

This deterioration in Argentina's economic and financial position cannot be attributed to a single set of factors. To some extent, it derives from inconsistencies in the formulation and/or implementation of what was intended to be a rigorous, orthodox, market-oriented policy in the period December 1978-March 1981.1/ (A banking crisis erupted in March 1980 as a number of financial institutions overextended themselves and were forced to rely heavily on Central Bank financial assistance when faced with deposit withdrawals; this crisis undermined confidence and played a role.) Subsequently, the weakening of Argentina's position owed much to the failed attempts during April-December 1981 at correcting the overvaluation of the peso and the current account balance of payments deficit--a failure attributable mostly to the lack of supporting domestic adjustment policies.2/

With the installation of a new administration in late December 1981, a systematic effort at redressing the situation was launched, which initially met with a measure of success. The exchange market, which had been split in June 1981, was reunified, and the peso was left to float more or less freely. At the same time, considerable austerity was introduced in wage, fiscal and monetary policy. As a result,

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1/ These policies and subsequent developments were reviewed at length in the Staff Report on the 1981 Article IV consultation with Argentina (SM/81/233, 12/2/82, and Supplement 1, 2/25/82) and in the accompanying report on recent economic developments (SM/81/239, 12/8/81).
2/ Ibid.

Table 2. Argentina: Selected Economic Indicators

(Percentage changes at annual rates)

	1978	1979	1980	Prel. 1981	Est. 1982	Projected 1983	Projected 1st Qtr. 1984
Gross domestic product							
In current market prices	148.6	168.6	102.5	93.5	187.9	254.4	103.6 1/
In constant 1970 prices	-3.4	7.1	0.7	-6.0	-4.3	5.0	5.0 1/
GDP deflator	157.3	150.7	101.1	105.9	200.8	237.5	93.9 1/
Prices and exchange rate 2/							
Consumer prices	169.8	139.7	87.6	131.3	215.0	168.2	131.3
Wholesale prices	143.3	128.9	57.7	180.3	310.0	158.6	131.3
Wholesale prices of domestic nonagricultural products	138.9	133.9	65.0	170.7	295.0	...	...
Exchange rate for commercial transactions 3/	69.7	62.6	24.2	287.4	494.5	...	...

Sources: Central Bank of Argentina; National Institute of Statistics; and Fund staff estimates.

1/ Percentage change from the fourth quarter of 1983, at annual rates.
2/ Percentage change during 12 months to end of period.
3/ In terms of pesos per U.S. dollar.

monthly inflation abated substantially from January to March 1982, and the balance of payments deterioration was arrested. There also were signs of a turnaround in expectations and recessionary trends appeared to be bottoming out. Efforts at restructuring the external debt through new eurosyndications and the retirement of short-term debts also proved successful, and the interest rate spread on new Argentine foreign borrowing narrowed as confidence in Argentina's economic management strengthened.

The improvement, however, was short-lived. The outbreak of hostilities in the South Atlantic on April 2, 1982 brought the adjustment effort to a halt. Fiscal policy remained generally restrained during the period of the conflict (with the immediate cost of the conflict being financed in part by emergency voluntary contributions, an increase in fuel prices, and a curtailment of nondefense expenditure), but the weakening of confidence led to heavy deposit withdrawals from domestic banks and monetary policy eventually was relaxed. Economic activity weakened again, partly in reflection of the disruption of external trade, and inflation regained momentum--to 15 per cent in June from an average of 6-1/2 per cent a month during February-May.

The float of the peso gave way to a policy of de facto fixed exchange rates, although the peso was devalued in May and depreciated gradually in June. Imports were restricted through the imposition of a ban on most consumer goods imports, the establishment of a system of U.S. dollar limits for each importer, and the introduction of a 180-day minimum financing requirement for most imports. All external payments were made subject to prior authorization by the Central Bank; the right to repatriate capital was suspended; and provisions were introduced whereby transfers relating to profits, dividends, royalties, and technical assistance payments could only be effected through the purchase of U.S. dollar-denominated bonds issued by the Government of Argentina (BONEX). These measures, however, failed to protect the balance of payments, which registered an overall deficit of almost US$2.7 billion in the second quarter of 1982--financed primarily by the accumulation of US$2.1 billion in payments arrears.

With the cessation of hostilities in late June 1982, the Administration was replaced by a new military-civilian government entrusted with the task of reviving the economy and of preparing for an orderly transfer of power to an elected government in the first half of 1984.

2. Recent economic developments

The view of the new Administration is that the mounting imbalances in the public finances during 1978-81 were directly responsible for the high real level of domestic interest rates (13 per cent on the average for the commercial bank lending rate in 1980 and 1981) and for Argentina's poor growth, price, and balance of payments performance. High real interest rates, in turn, had led to a string of corporate bankruptcies and to growing insolvency in the domestic banking system, which had necessitated bail outs by the Central Bank at great costs in terms of monetary expansion and inflation. For some time, this diagnosis had been widely shared in Argentina, and the authorities responsible for economic management during July and August of 1982 acted on it by radically altering economic policies.

Given the limited supply of resources after two years of severe recession and the perceived need to revive economic activity and improve the labor market situation, the view was taken that policies should engineer a large one-time transfer of resources from savers to debtors. The agricultural sector, whose relative position had been strengthened greatly from mid-1981 by the large exchange rate adjustments of that year, also was called upon to assist temporarily in alleviating the corporate and public sector's financial situation. The instrumentation of this policy of resource transfer was to rest, in the short run, on certain exchange and trade measures and on far-reaching adjustments in the mechanisms of financial intermediation.

On July 5, 1982, the foreign exchange market was split into a commercial market for trade transactions and a financial market for other permitted transactions. The rate in the commercial market was set initially at $a 20,000 per U.S. dollar, representing a 21 per cent devaluation of the peso from its last quotation on the unified market; thereafter, the commercial rate was adjusted daily (Chart 1). The financial peso was allowed to float for several weeks and was then pegged at about $a 39,000 per U.S. dollar. Restrictions on access to the financial market promptly gave rise to a parallel market in which the peso quotation for a time exceeded $a 60,000 per U.S. dollar.1/

In conjunction with the devaluation, taxes on agricultural exports were raised from 10 per cent to a range of 20-25 per cent, and taxes on other traditional exports were raised from a range of 0-5 per cent to 10 per cent. Tax rebates for promoted exports were reduced somewhat from a range of 5-14 per cent to a range of 0-10 per cent. The import restrictions which had been introduced on a temporary basis in the second quarter were formalized in July and, in addition, minimum financing terms of up to five years were introduced for capital goods imports.

The new economic team also introduced an array of measures intended to induce capital inflows or prevent capital outflows. Special schemes were put into place whereby the private sector could clear amounts in

1/ All payments through the financial market other than freight, insurance, loan amortization and interest, and certain other selected service payments continued to require prior authorization from the Central Bank. After August 6, these provisions were liberalized somewhat to permit automatically the transfer of pensions and, up to certain specified limits, the sale of exchange for foreign travel, medical treatment, and transfers to students and dependent family members abroad.

arrears at preferential exchange rates by bringing in an equivalent amount of funds under a swap contract with the Central Bank, or by accepting marketable U.S. dollar-denominated Government of Argentina bonds (BONEX) in lieu of foreign exchange. A new exchange rate guarantee scheme was also introduced for private sector loans, whether or not in arrears, registered with the Central Bank prior to the devaluation; to be eligible for this scheme, the debtor had to obtain a loan extension of at least one year. The guaranteed exchange rate was the predevaluation rate, indexed thereafter by the inflation differential between Argentina and the United States.

The private sector responded strongly to these various preferential schemes. During the third quarter, outstanding swaps increased by almost US$800 million, and approximately US$1 billion in arrears and other payments were cleared through sales of BONEX. Also, by the time the new exchange rate guarantee scheme was terminated in October, more than US$4 billion in guarantees on previously unguaranteed debt had been granted under this program.1/ These measures--which could give rise to a potentially massive domestic credit expansion and international reserve loss when these mechanisms are unwound in the future--enabled the authorities to reduce private sector arrears from US$1.6 billion in June to about US$600 million in September; at the same time, however, public sector arrears mounted, rising from US$500 million at the end of June to almost US$1.2 billion in September.

The modification of the exchange and trade system was paralleled by a major domestic financial reform aimed at: (1) reducing the real domestic debt of a private sector burdened with high debt to capital ratios; (2) discouraging short-term speculative financial operations (credit and deposit operations had been conducted within a range of 7-30 days in Argentina since late 1978) and encouraging financing of production and investment; and (3) defusing the potential for largely unchecked credit expansion inherent in the government guarantee of bank deposits.

All bank deposits outstanding on June 30, 1982 were made subject to a 100 per cent reserve requirement; banks were given rediscount facilities for an equivalent amount less their outstanding loans to the public sector (which were to be taken over by the Central Bank) to refinance outstanding personal or corporate loans over a five-year period ("basic" loan). In order to reduce such debts in real terms, the interest rate on the refinanced loans initially was set at 6 per cent a month, well below the prevailing inflation rate.

Meanwhile, with the help of an array of new financial instruments, the financial system was to be assured greater permanence of the funds that it attracted. These new instruments would be in accord with the

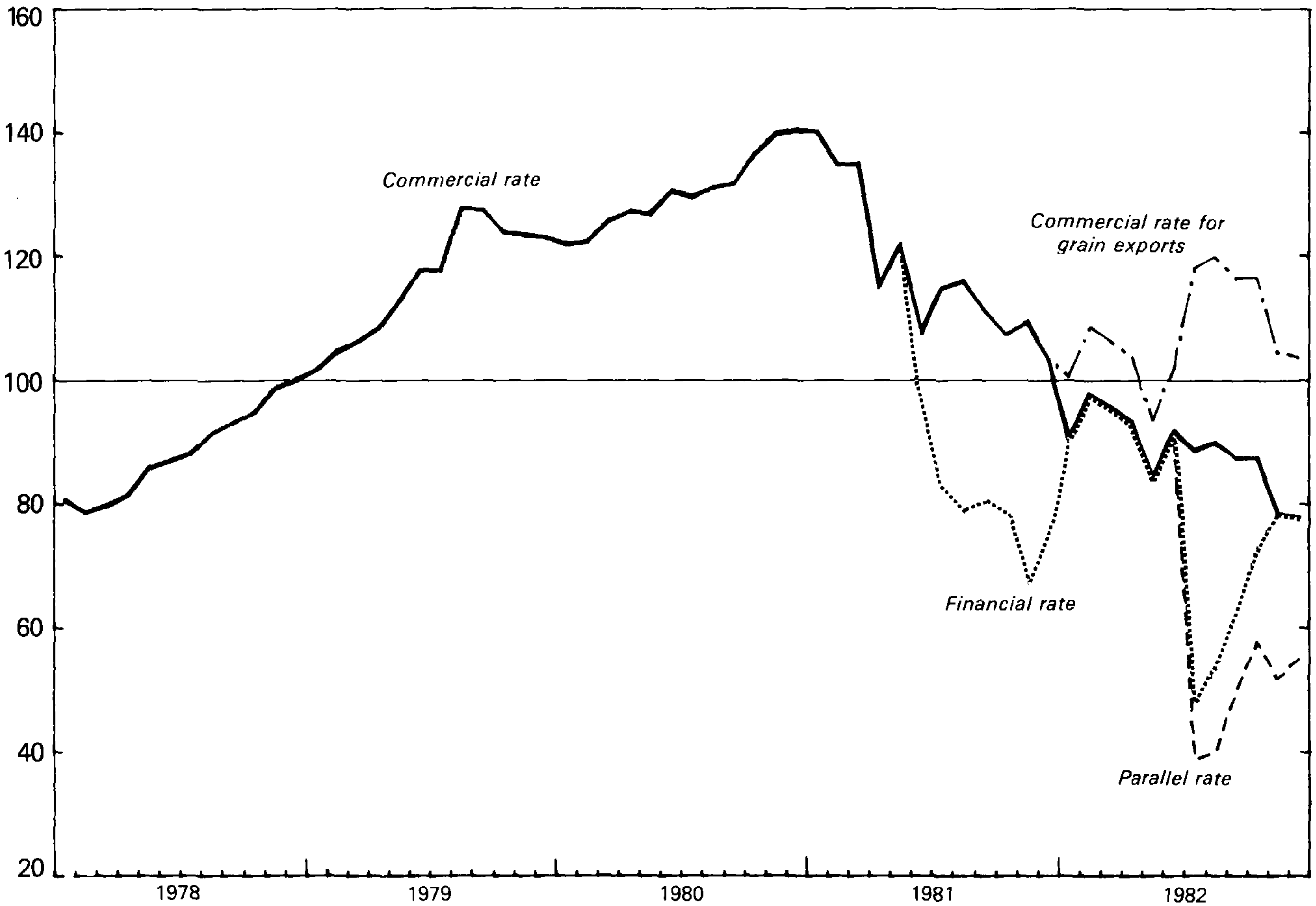
1/ These guarantees were in addition to those extended in the second half of 1981 (for the equivalent of US$5 billion) which began to come due in November-December 1982. Approximately US$1 billion of these loans were rolled over with guarantees during 1982.

CHART 1

ARGENTINA

REAL EFFECTIVE EXCHANGE RATE INDICES[1]

(Dec. 1978 = 100)



Sources: Central Bank of Argentina; and Fund staff estimates.

[1] Based on the monthly average of nominal exchange rates adjusted by price and exchange rate movements in Argentina's major trading partners. Increase in the index value represents an appreciation of the peso in real terms.

principle that short-term, government-guaranteed financial assets should neither be indexed nor pay positive real interest rates, while longer term deposits with freely determined interest rates would not benefit from the government guarantee. The intention was to make longer-term cost of living (COL)-indexed deposits an important financial asset and these deposits were given a government guarantee to make them more attractive. Accordingly, new deposits with maturities of up to 90 days carried fixed interest rates ranging from 2.5 to 5 per cent per month and were subject to a 100 per cent legal reserve requirement; they could be used as a basis for loans only in the amount that the Central Bank permitted ("additional" loans). In contrast, banks were free to on-lend deposits with maturities of more than 90 days at freely negotiated interest rates and to use one-year COL-indexed deposits to finance price-indexed loans.1/ Bank-by-bank limits initially were imposed on the quantity of deposits that could be accepted at freely determined interest rates. But, in the longer run, the intention was to release banks gradually from Central Bank control so that by the first quarter of 1984 (i.e., at the time power was to be transferred to the new government) about one half of bank deposit and credit operations would be at freely negotiated rates.

It was acknowledged that certain of the newly introduced schemes would bear a high cost in terms of inflation, but it was hoped that this strategy would permit a rapid reactivation of the economy. Also, the view was that if these policies were accompanied by prudent incomes policies and tight fiscal and Central Bank monetary programs, a progressive deceleration of inflation and strengthening of the balance of payments could be achieved.

In the event, none of the conditions required for the success of this strategy was met. In July, the minimum wage was raised sharply and there was a substantial increase in wages for government workers, followed by sizable flat peso increases for workers in the private and public sectors in August. Real money balances did not, as had been hoped, stabilize following an initial stock adjustment in response to the adoption of negative real interest rates. The growth of M4 2/ was 10 per cent in July and 3-1/2 per cent in August; in the same two-month period, the combination of corrective price and exchange rate adjustments, rapidly rising labor costs, and steadily eroding confidence in the domestic currency resulted in a jump of 48 per cent in wholesale prices (32 per cent in consumer prices).

On the balance of payments side, the differential between the most appreciated effective exchange rate (for grain exports) and the parallel rate remained very large (in a ratio of some 3 to 1); exporters retained shipments, and underinvoicing of exports and overinvoicing of imports became widespread. The hopes, therefore, that capital flight would

1/ Loan indexing could be based on one of seven different price indices at the option of borrowers.
2/ Money and quasi-money in local currency and Treasury bills.

abate and that 1982 would yield a surplus on goods and nonfactor services of the order of US$3.5 billion came increasingly to be questioned. Also, the authorities' renewed effort to obtain financing from the international capital markets came to naught. The reluctance of banks to lend to Argentina reflected to some extent the general cautiousness of the market at a time of growing strains in the international financial system. But it also stemmed from widespread uneasiness with Argentina's new domestic policies and from the as yet unresolved question of Argentina's servicing of debt to British creditors.

After two months, notwithstanding a mild rebound of domestic production, evidence became overwhelming that the policy experiment entailed much higher costs than had been foreseen; also, disagreements within the economic team on the future course of wage policy began to surface. Finally, the failure of the strategy pursued vis-a-vis the international capital market pointed to the need for a different type of approach.

Late in August, the present economic team came into office, and took a number of steps to regularize its relationship with foreign creditors. In a first step, priority was given to solving pending financial issues with U.K. creditors. The second step consisted of devising a program of economic adjustment and recovery for 1983-84 and of requesting Fund financial support for that program under an arrangement in the upper credit tranches. The third step was to negotiate short-term bridge loans with a group of foreign banks and, if possible, from the Bank for International Settlements to facilitate the prompt elimination of external payments arrears. The fourth stage, now underway, consisted of opening discussions with Argentina's foreign creditors with a view to refinancing the earlier bridging operations on a medium-term basis and restructuring the maturity profile of Argentina's public and private external debt.

However, the new economic team did not attempt to dismantle at once the economic policies which had been adopted in early July, and the interest rates, the exchange rate, and the exchange and trade system policies were adjusted only gradually. As a result, real money balances continued to decline, the balance of payments continued to record large deficits, and external payments arrears--which had been reduced somewhat between June and August--began to mount again. The mild revival of output that began in the third quarter appears to have continued in the fourth quarter but inflation remained above 11 per cent a month on the average, in reflection of large wage adjustments in September and October and expansionary financial policies. There was also an element of corrective inflation in the fourth quarter, as a result of the initiation of monthly rounds of adjustments in public sector tariffs and prices and the accelerated depreciation of the peso for trade-related transactions.

At the end of August, the exchange rates for the peso stood at about $a 24,000 and $a 39,000, in the commercial and financial markets, respectively, and the new team announced their intention to unify these markets gradually. While keeping the financial rate pegged at \$a 39,000, they accelerated the crawl of the commercial rate and, in mid-September, began applying a weighted average of the commercial and financial rates for trade transactions. As a result, the rate for trade transactions moved to \$a 33,800 at the end of October, a monthly rate of depreciation of about 11-1/2 per cent in terms of pesos per U.S. dollar. On November 1, the commercial and financial markets were unified at a rate of \$a 39,000; with this action, the real effective exchange rate for the peso (before export taxes) was restored to a level which historical evidence would indicate was broadly consistent with the attainment of the large trade surplus that is required if the authorities' overall balance of payments objectives are to be met. Since November 1, the exchange rate for the peso in the unified market has been adjusted daily and about in line with the rate of domestic inflation. Because of restrictions on transactions in the official market, activity in the parallel market has continued; the premium on the U.S. dollar in this market was about 50 per cent in December.

Corrective action in the area of monetary policy, however, was less decisive. The monthly interest rates charged on the "basic" and "additional" loans (unified in November into a single "consolidated" loan) were raised from 6 per cent a month to 8 per cent and then to 9 per cent, and regulated deposit rates were raised in line; however, interest rates remained below both the average rate of inflation and the pace of exchange rate depreciation. Even though banks began to capture COL-indexed deposits at a rapidly rising rate and the monthly interest rate on Treasury bills remained at 11 per cent a month, the rate of growth of peso-denominated financial assets continued to fall short of the rate of price increase, greatly complicating the task of monetary management.

This task was made all the more difficult by renewed heavy demand on Central Bank resources. The borrowing requirements of the public sector mounted owing to substantial wage adjustments for government employees and the launching in early October of an emergency public works program to combat unemployment. Also, the Central Bank incurred heavy losses on account of the special domestic debt refinancing schemes that had been introduced in early July 1982 and the payment of interest on commercial bank COL-indexed deposits that were redeposited in the Central Bank.1/ As a result, the growth of the Central Bank's net domestic assets far outpaced the increase in currency issue, resulting in a further loss of net official international reserves of about US\$1 billion in the last quarter of 1982.2/

1/ See section III, subsection 2 of the accompanying report on recent economic developments, and Appendix D to that report.

2/ This loss would have been far greater had not the Central Bank adopted emergency measures to offset the balance of payments impact of the exchange guarantees granted during June-December 1981 which began to mature from November 1982. For detail on these measures, see the accompanying report on recent economic developments, section II, and Appendix A to the same report.

III. The Adjustment and Recovery Program

The stated objectives of the Argentine program are to revive production in specific sectors of the economy, principally the hydrocarbon and export sectors, to restore balance of payments equilibrium and, once the spurt of corrective price adjustments now under way has worked its way through the economy, to achieve a major deceleration of inflation.

1. Prospects for output and prices

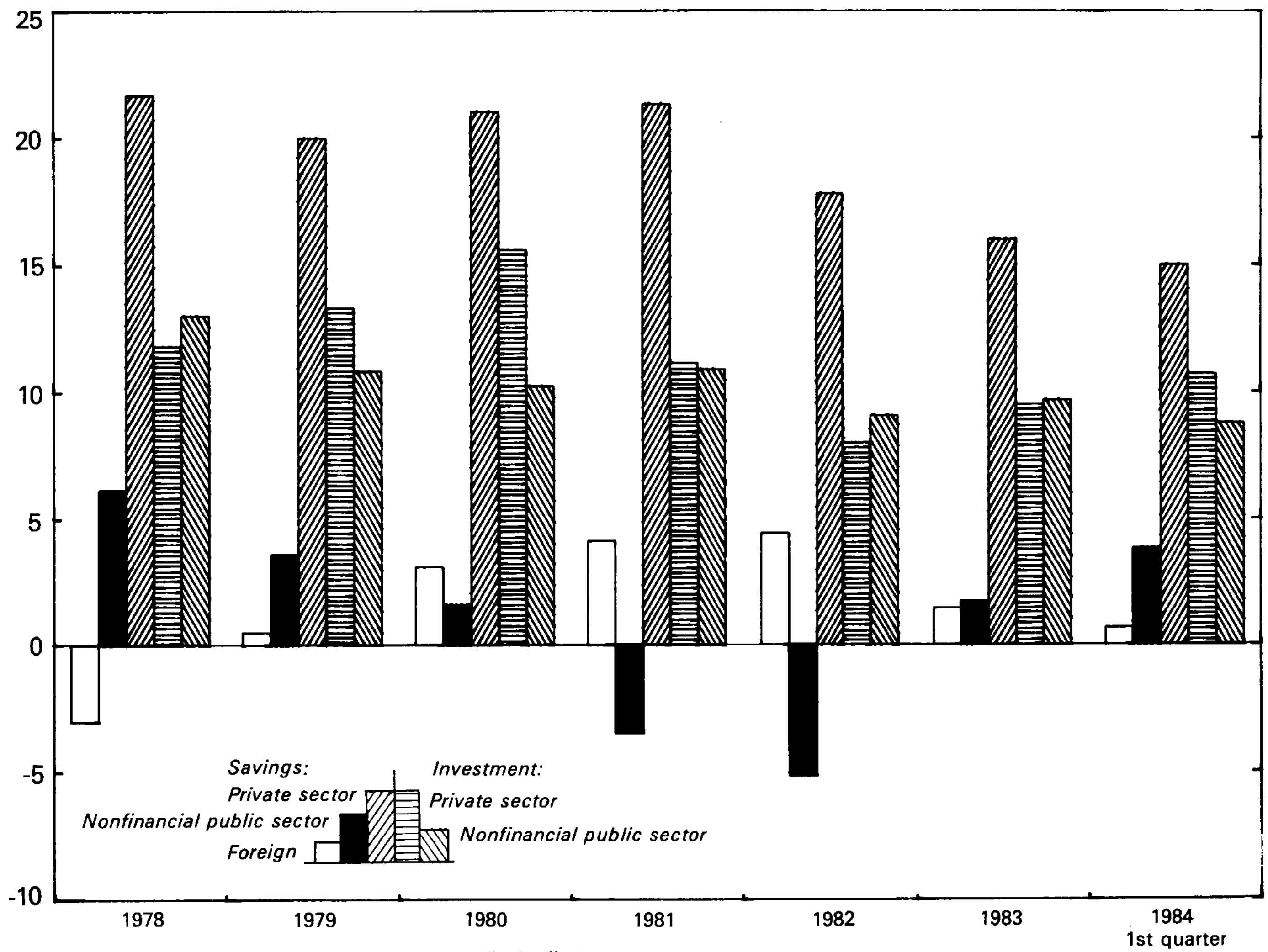
In all likelihood, the process of economic reactivation will be slow. Confidence was eroded severely during the past three years, and considerable time probably will be required before private capital is repatriated from abroad and investments in new productive facilities take place on any significant scale. Moreover, the relatively short political horizon of the current administration would not seem to be conducive to long-term planning, inasmuch as the ground rules for economic management beyond the first quarter of 1984 remain largely unknown.

The hope is, nevertheless, that the policy of financial restraint which is to be implemented will have a significant effect in reducing inflationary expectations while permitting a recovery of output of the order of 5 per cent in 1983. The authorities anticipate that adherence to external policies geared to a rapid growth of the nontraditional export sector will support the recovery, and they expect that the growth of farm income, which during the current crop year is being boosted by exceptionally favorable weather, also will make a contribution. No major recovery of private investment is projected for the near future, with much of the expected pickup in demand resulting mainly in greater use of existing capacity; however, as the public sector begins to lessen its demands on private savings, the hope is that private investment will begin to respond (Table 3 and Chart 2).

Only a modest rise in public investment (in relation to GDP) is foreseen, because of the prevailing internal and external financing constraints. Public investment is to be concentrated in labor intensive public works that call for limited use of imported inputs. Also, investment spending will, for the most part, be limited to maintenance work and to small or ongoing projects to avoid prejudging the investment priorities of the next administration.

An exception to this rule will be investment in the hydrocarbon sector, where prospects for turning Argentina from a net importer to a net exporter are promising. During the past two years, crude oil production has tended to stagnate owing to the low prices paid to the state oil company (YPF) and the private firms that produce under contract to YPF. To encourage production and new drilling, during the 18-month period which began in October 1982 the domestic price of oil products is to be raised by some 110 per cent over and above the increase in wholesale prices. A large part of this increase will result

CHART 2
ARGENTINA
SAVINGS AND INVESTMENTS



Sources: Central Bank of Argentina; Ministry of Economy; and Fund staff estimates.

- 12a -

Table 3. Argentina: Summary Macroeconomic Flows

(In per cent of GDP)

	1978	1979	1980	Prel. 1981	Est. 1982	Projected 1983	Projected First Quarter 1984
Foreign sector 1/							
Exports of goods and nonfactor services	11.8	9.0	6.9	9.5	13.6	19.0	19.5
Imports of goods and nonfactor services	-7.8	-8.8	-9.0	-9.7	-9.6	-13.8	-14.4
Factor services and transfers	-1.0	-0.7	-1.0	-3.9	-8.4	-6.7	-5.8
Current account balance	3.0	-0.5	-3.1	-4.1	-4.4	-1.5	-0.7
Net capital flows	1.9	4.5	1.4	1.0	-5.5	0.7	0.7
Financial loans to the nonfinancial public sector	2.1	1.2	1.9	4.8	-1.1	--	--
Other capital flows 2/	-0.2	3.3	-0.5	-3.8	-4.4	0.7	0.7
Valuation adjustment and SDR allocation	0.2	0.2	-0.1	-0.3	-0.2	--	--
Change in net international reserves of the Central Bank (increase -)	-5.1	-4.2	1.8	3.4	10.1	0.7	--
Nonfinancial public sector							
Savings	6.1	3.7	1.6	-3.4	-5.1	1.7	3.8
Capital expenditure	13.0	10.8	10.2	10.9	9.1	9.7	8.8
Overall balance	-6.9	-7.2	-8.6	-14.3	-14.2	-8.0	-5.0
Saving and investment							
Total investment 3/	24.8	24.1	25.7	22.0	17.1	19.2	19.5
Private sector	11.8	13.3	15.6	11.1	8.0	9.5	10.7
Nonfinancial public sector	13.0	10.8	10.2	10.9	9.1	9.7	8.8
Total saving	24.8	24.1	25.7	22.0	17.1	19.2	19.5
National saving	27.8	23.6	22.6	17.9	12.7	17.7	18.8
Private sector	21.7	20.0	21.0	21.3	17.8	16.0	15.0
Nonfinancial public sector	6.1	3.6	1.6	-3.4	-5.1	1.7	3.8
Foreign saving	-3.0	0.5	3.1	4.1	4.4	1.5	0.7

Sources: Central Bank of Argentina; Ministry of Economy; and Fund staff estimates.

1/ Balance of payments flows in U.S. dollars converted to Argentine pesos at actual average exchange rates.
2/ Includes direct investment, trade credits, trade related leads and lags, and errors and omissions.
3/ Public sector capital transfers to the private sector and extrabudgetary expenditure are included as public sector investment and subtracted from private sector investment as defined in the national accounts.

from higher taxes, part of which will be turned over by the Treasury to the state oil company to allow YPF to meet its own investment requirements and offer more remunerative prices to its private contractors. Prospects are even more encouraging for tapping the country's large natural gas reserves, most of which have been discovered since 1978. A first priority is to accelerate the substitution of gas for oil, thus releasing some heavy fuels for export. A second priority is to expand the natural gas-based fertilizer industry. In the longer run there exists the possibility of exporting to neighboring countries, and discussions have already been initiated with Brazil and Uruguay on the construction of transborder pipelines.

The authorities have emphasized that a sustainable recovery of output and real labor income will require the containment of inflation, and a substantial reduction in the rate of inflation is one of the key goals of the program. The aim is to reduce the rate of inflation (as measured by the wholesale price index) from 310 per cent during 1982 to 160 per cent during 1983 and to an annual rate of 85 per cent during the first quarter of 1984. The anti-inflation effort will be based on the pursuit of restrained financial policies, including some corrective price adjustments early in the program period to help strengthen the public finances. These measures will be supported by the flexible application of incomes and pricing policies, a reduction of waste and inefficiency in the public sector, a relaxation of barriers to international trade, and other measures designed to promote the efficient working of the economy. At the same time, care will be taken to safeguard the balance of payments through maintenance of an appropriate exchange rate policy.

If the present program proves to be successful, toward the end of the 15-month program period the Argentine economy should be characterized by declining inflation, improved private sector confidence, and a markedly strengthened balance of payments position--at higher levels of exports and imports. With the sustained application of present policies in the medium term, a continued reduction of inflation and a gradual turnaround in private sector attitudes can be expected, which should result in a substantially better economic performance than in the past several years. Of course, continued attention will have to be paid to the need to limit the external current account and overall balance of payments deficits, and the extent of the improvement in the domestic economy will depend in good measure on external factors--the timing and strength of the world recovery, international interest rate levels and the behavior of Argentina's terms of trade. But, assuming moderately favorable developments in these areas, it should be possible for the Argentine economy to sustain rates of growth in the medium term that would be consistent with declining unemployment and a rising standard of living.

2. Fiscal policy

Crucial to the adjustment effort is the marked improvement of the public finances that is projected. The current account of the nonfinancial public sector is programmed to shift from a deficit equivalent to about 5 per cent of GDP in 1982 to a surplus of more than 1-1/2 per cent of GDP in 1983, and to one equivalent to more than 3-1/2 per cent of GDP at an annual rate in the first quarter of 1984 (Table 4 and Chart 3). This turnaround should ensure a reduction in the borrowing requirements of the nonfinancial public sector from over 14 per cent of GDP in 1982 to 8 per cent of GDP in 1983 and an annual rate of 5 per cent of GDP during January-March 1984; this would still allow for public investment to increase in 1983 to about 9-1/2 per cent from 8-1/2 per cent of GDP in 1982, the lowest level in 10 years, but it would drop back to 8-1/2 per cent of GDP in the first quarter of 1984. The improvement in the overall public finances is predicated on the first full year of application of the export and excise taxes introduced or raised in July 1982, on frequent adjustments of the tariffs, prices and fees for goods and services marketed by the public sector, on a strengthening of tax administration, and on a drastic curtailment of current outlays in the general government as well as of the state enterprises' operating expenses.

The rise in public sector revenues is to come mainly from tax and price increases. As an emergency measure, export taxes on nonpromoted exports were raised in steps from a range of 0-10 per cent in early 1982 to one of 10-25 per cent from July 1982. The yield of these taxes is estimated at about 1.2 per cent of GDP in 1982 and almost 2 per cent of GDP in 1983 (given present expectations of significantly higher production and export volumes in 1983 and notwithstanding continued low world prices). In addition, to regain the ground lost in the first half of 1982 when public sector tariffs de facto were frozen, tariffs are to be raised by 2.8 per cent a month in real terms on a weighted average basis (3.2 per cent in the case of petroleum derivatives) in the period October 1982-March 1984. Moreover, an additional 20 per cent increase in fuel prices (to accrue in full to the Treasury) is being implemented in four monthly stages beginning in late November 1982, and the authorities have indicated their intention to proceed with an additional 10 per cent increase should circumstances so require. Altogether, these measures are expected to boost general government revenue by some 2 percentage points of GDP in 1983 and the operating income of the public enterprises by about 1 percentage point of GDP.

A chronic problem confronting the Argentine authorities in their management of the public finances has been the extent of tax evasion. The latter is estimated at over 50 per cent in the case of the value-added tax, a reflection of a basic weakness in the tax auditing machinery. Moreover, charges for late payment or nonpayment of taxes have not been sufficiently high to deter evasion and late payment, and expectations of periodic tax amnesties have contributed to the delinquency

Table 4. Argentina: Public Sector Operations

(In per cent of GDP)

	1978	1979	1980	Prel. 1981	Est. 1982	Program 1983	Program First Quarter 1984
General government savings	4.8	4.7	2.9	-0.7	1.9	5.6	6.0
Revenue 1/	25.6	24.4	26.4	23.7	21.6	23.7	23.7
Expenditure 2/	20.8	19.7	23.5	24.4	19.7	18.1	17.7
State enterprises savings	4.2	1.9	2.0	2.8	2.9	4.2	4.8
Consolidated public sector savings	9.1	6.6	4.9	2.1	4.8	9.8	10.8
Capital expenditure	12.9	10.4	9.7	9.8	8.5	9.4	8.5
Public sector surplus or deficit (-)2/	-3.8	-3.8	-4.8	-7.7	-3.7	0.4	2.3
Interest treated as amortization 3/	3.0	3.0	3.3	5.5	8.5	8.1	7.0
Extrabudgetary expenditure 4/	0.1	0.4	0.5	1.1	0.6	0.3	0.3
Payments arrears	--	--	--	--	1.4	--	--
Financing	6.9	7.2	8.6	14.3	14.2	8.0	5.0
External (net)	2.0	1.7	1.4	4.4	3.0	...	...
Internal (net)	4.9	5.5	7.2	9.9	11.2	...	...
Memorandum items							
Total expenditure 5/	36.8	33.1	37.0	40.8	38.7	35.9	33.5
Total public sector savings 6/	6.1	3.6	1.6	-3.4	-5.1	1.7	3.8

Sources: Ministry of Economy; and Fund staff estimates.

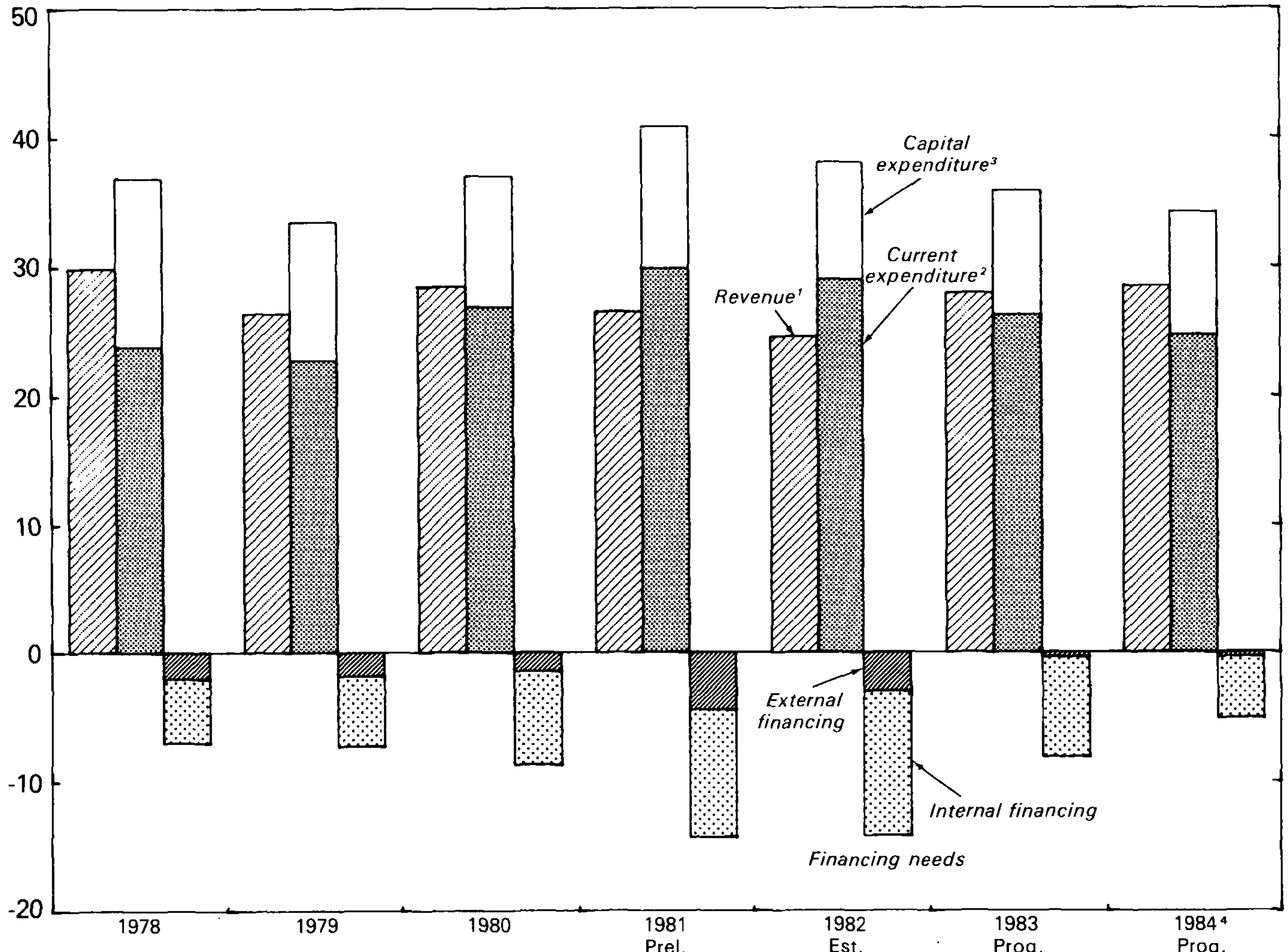
1/ Includes capital receipts.
2/ Excludes interest as amortization, extrabudgetary expenditure, and in 1982 payments arrears.
3/ In the Argentine accounts a part of nominal interest payments is treated as amortization.
4/ Mainly capital expenditure.
5/ Includes interest as amortization, extrabudgetary expenditure, and in 1982 payments arrears.
6/ Consolidated public sector savings minus interest as amortization and payments arrears.

CHART 3

ARGENTINA

PUBLIC SECTOR OPERATIONS

(As per cent of GDP)



Source: Ministry of Economy; and Fund staff estimates.

[1] Includes general government revenue and current account surplus of state enterprises.

[2] Includes interest treated as amortization in the Argentine presentation of public sector operations. 1982 also includes payments arrears.

[3] Includes extrabudgetary expenditure.

[4] First quarter 1984.

rate. An effort to increase the number of tax auditors and stiffen penalties is under way, but the effect of these measures can only be gradual.

On the expenditure side, the authorities are determined to exercise prudence as regards both the overall level of spending and its economic justification. In their view, austerity is dictated by the need not only to lower the public sector's borrowing requirements but also to reduce waste and inefficiency, which is deemed to have been one of the causes of the country's lackluster growth performance in the last 10-15 years.

Current expenditure of the general government is programmed to decline significantly in real terms, in reflection of the nonrecurrent nature of certain outlays made in 1982, of the decline in interest payments on the external debt, and of improved control over spending. In particular, the intention is to fill no more than one half of the positions left vacant by attrition; this should compensate in part for the modest recovery in real government remunerations which in principle is to take place over the course of 1983 if inflation abates at the rate anticipated by the program. Except for a brief period in the first half of 1982, the increase in the operating costs of the state enterprises has tended in recent years to outpace that in current outlays of the general government. As a means of enforcing greater discipline in the management of the state corporations, the authority of the State Enterprises' Central Office (Sindicatura General de Empresas) has been strengthened considerably and expectations are that the increased weight of this central authority will result in improved management control.

The performance criterion for fiscal policy is a set of cumulative quarterly limits on the borrowing needs of the nonfinancial public sector, measured as the sum of its net external borrowing, its net borrowing from the domestic financial system, and the net increase in private sector holdings of Treasury bills and bonds. The limits, which would imply a steady reduction in the ratio of the deficit to GDP to about 5 per cent by the first quarter of 1984, have been fixed at $a 105 trillion in the 3 months through March 31, 1983, at $a 218 trillion in the 6 months through June 30, 1983, at $a 326 trillion in the 9 months through September 30, 1983, at $a 445 trillion in the 12 months through December 31, 1983, and at $a 559 trillion in the 15 months through March 31, 1984. Given prevailing conditions in the international capital markets and the need for Argentina to give priority to a renegotiation of the maturity structure of her debt to private creditors, the program assumes no net borrowing from the international capital market by the nonfinancial public sector.1/ Net external financing would be

1/ For purposes of the program, the US$1.5 billion medium-term banking loan arranged in connection with Argentina's request for a stand-by arrangement is to be treated as a reserve liability of the monetary authorities.

limited largely to suppliers' credits, and the bulk of the financing requirements of the nonfinancial public sector would have to be covered from domestic sources.

3. Monetary policy

In order that sufficient domestic financing be made available in a setting of decelerating inflation, the sharp decline in real money balances which began in the second half of 1982 must be brought quickly to a halt. In recognition of this fact, the program assumes that the demand for financial assets will rise at a rate which is consistent with the projected decline in inflation, some recovery of real income, and a moderate decline in the income velocity of money. Specifically, M4 is projected to rise by 185 per cent during 1983 and at an annual rate of about 100 per cent during the first quarter of 1984. Attainment of such growth rates will require an interest rate policy designed to make domestic financial assets once again competitive with alternative domestic and foreign investments.

Accordingly, beginning in January 1983, the authorities have adopted a formula whereby regulated deposit and lending rates are to be set monthly on the basis of movements in a three-month moving average of the wholesale price index that would encompass the observed inflation of the previous two months and projected inflation for the current month. The regulated lending rate is to be set at least at the level indicated by the formula, while the rate for 30-day deposits is to be set within 1 percentage point below the lending rate. Interest rates payable on regulated deposits at more than 30 days are to be set in line with the 30-day rate. As the formula is based partially on estimated movements in prices, the authorities have indicated that they are prepared, in the course of any particular month, to compensate for any underestimation of actual inflation by adjusting legal reserve requirements or conducting their open market operations in such a way as to ensure that the targeted growth for M4 is being met.

More generally, the authorities intend to be flexible in their management of interest rates, as they believe that the ultimate test of the adequacy of their policy in this area is achievement of the balance of payments objectives and the gradual reconstitution of real money balances. Therefore, they intend to follow closely the behavior of freely negotiated rates on unregulated deposits which, together with the rate on Treasury or Central Bank bills, will be taken as an indicator of market sentiment; regulated rates will be adjusted to above the levels indicated by the formula, should circumstances so require.

Even if the objective for the growth of financial resources should be fully realized, the need to ensure overall balance of payments equilibrium will call for considerable restraint in domestic credit policies. Monetary management in 1983 and during the early months of 1984 will be under considerable pressure because of the heavy domestic borrowing requirements of the nonfinancial public sector. Credit accommodation to the private sector, therefore, will have to be kept very tight and below the anticipated growth in nominal GDP. A more substantial recovery of private sector activity than the modest one envisaged in the program thus would have to be financed by repatriation of private capital.

On present assumptions, a large part of the financing that will be made available to the private sector during the program period will be on account of a variety of Central Bank schemes introduced in July 1982. This "autonomous" expansion will arise mainly from (1) the automatic consolidation of interest due on the "consolidated" loan (formerly "basic" and "additional" loans); (2) the cost of indexing COL-indexed deposits captured by the banking system and redeposited with the Central Bank for lack of demand for price-indexed loans; or (3) whenever such COL-indexed deposits will finance investment loans to small and medium enterprises, the cost to the Central Bank of subsidizing up to 4 percentage points of the interest rate charged by banks on such loans.

The performance criterion for monetary policy is a set of ceilings on the net domestic assets of the Central Bank, defined as the difference between the Bank's currency issue and its net international reserve position, i.e., including liabilities to banks and other financial intermediaries as an offset to domestic credit operations. In this definition, the net domestic asset test captures all facets of credit expansion by the Central Bank. Given the simultaneous objectives of limiting the balance of payments deficit, and of reducing the rate of price increase, the growth of net domestic assets has been constrained as a percentage of the stock of currency at the end of 1982--to a maximum of 170 per cent through December 1983, and to a maximum of 220 per cent through the end of the first quarter of 1984--plus the targeted deficit in the balance of payments. Appropriate adjustments have been made in the quarterly distribution of these ceilings to take into account seasonal variations in the demand for money and the balance of payments.

4. Price and incomes policies

The authorities believe that reliance on market forces will best guarantee the efficient allocation of resources. A system of price agreements, and eventually of price controls, applicable to Argentina's largest industrial firms was introduced from July 1982. These controls were seen as necessary to prevent price overshooting on the part of firms with a dominant market position at a time when the effects of major corrective price and exchange rate adjustments were working their way through the economy. The controls have been administered flexibly, with authorization to increase prices granted once a month in the light of changes in costs, as well as the need to ensure an appropriate return on fixed assets. In October, the period for government review of firms' requests to raise prices was reduced from ten to seven days and the number of firms subject to price controls has been reduced; as the need for corrective price adjustments lessens and the tightening of domestic demand management begins to take hold, the authorities were confident that controls could be relaxed further and eventually eliminated.

A matter of concern to the Government has been the sharp deterioration in real labor remuneration since 1980 (Chart 4). Real wages in private employment and in the public sector declined by about 10 per cent in 1981; during the first six months of 1982, real wages in the private sector came down further by almost 25 per cent, while real wages in the public sector dropped even more. The authorities explained that, in an effort to prevent consumption from falling to unsustainably low levels, wages for government workers had been increased by an average of 23 per cent in July 1982, and the minimum wage had been raised by 40 per cent. In addition, there had been lump sum adjustments for all remuneration levels (in the public and private sectors) in August and September, and a further 40 per cent increase in the minimum wage in September. On average, nominal wages of industrial workers had risen by more than 15 per cent in both July and August, and by almost 30 per cent in September.

In October, wages were raised by 17 per cent, equivalent to the increase in the consumer price index in September. Remunerations of public sector employees were raised further by 10 per cent in November and by 14 per cent in December, and in addition, remunerations for the middle and upper echelons of the government salary scale were adjusted in November in part for the salary distortions introduced by the lump sum increases of the third quarter of the year. In December a general adjustment of 14 per cent for the private sector was decreed by the Government. Notwithstanding the substantial adjustment in the second half of the year, real wages in the public and private sectors are estimated to have dropped by a further 10 per cent in 1982.

The authorities have stressed that the salary adjustments of the second half of 1982 were dictated by the exceptional circumstances of that period. As a matter of policy, their view has been that the determination of wage levels in the private sector ought to be left to each firm in the light of its own financial position and of the labor market situation. Accordingly, in 1983 and early 1984, they would limit themselves to adjusting from time to time the basic conventional wages, paying due regard in the process to the need not to set these de facto wage floors to levels that might cause actual salaries to move on a path inconsistent with the intended deceleration of inflation.1/ More generally, the authorities observed that no lasting improvement in real income of labor could come from nominal wage adjustments alone and that the desired improvement in labor market conditions would only result from productivity increases and a recovery of output in the context of a deceleration of inflation.

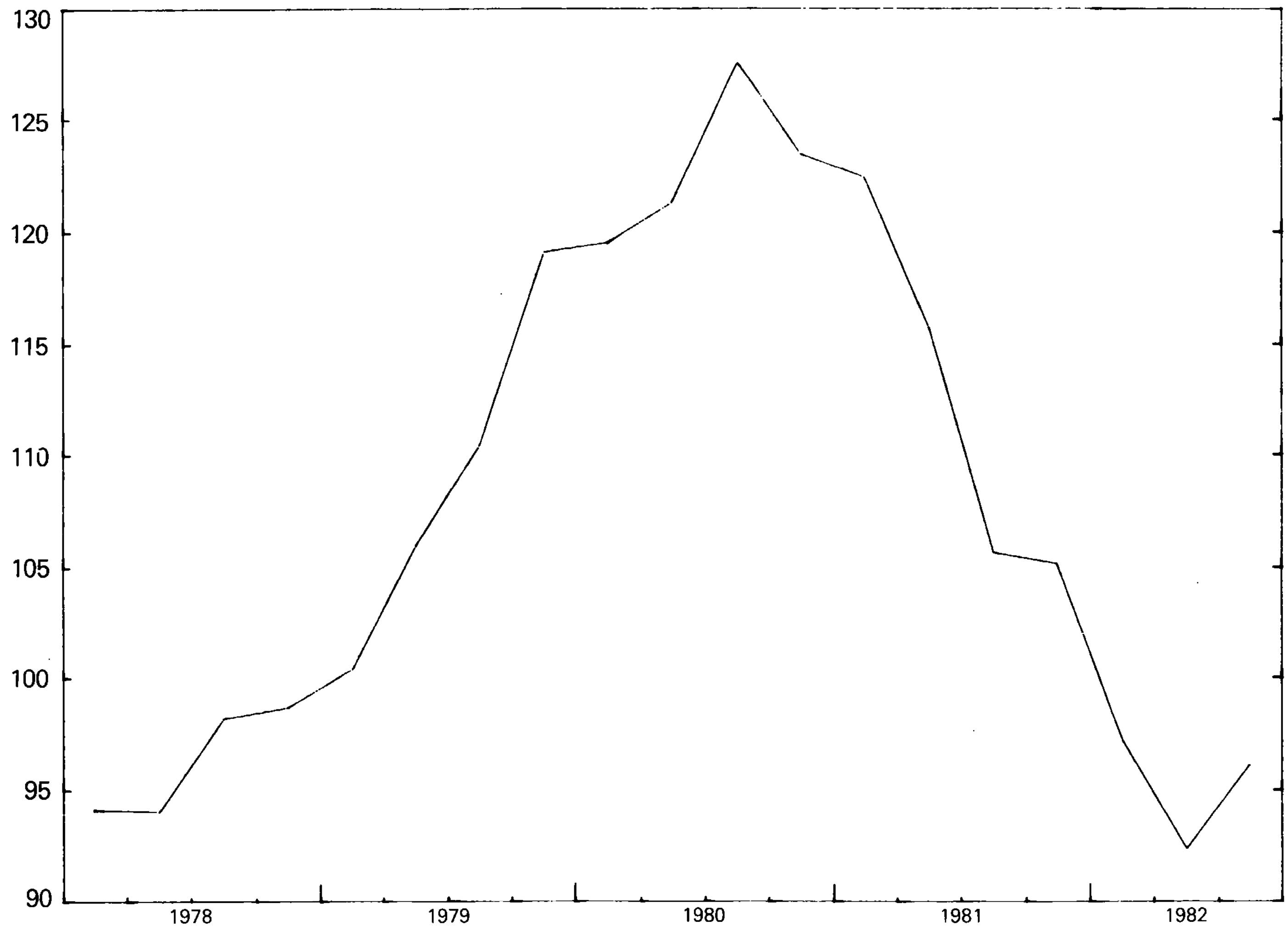
1/ Given the suspension of free collective bargaining since March 1976, the Government must by law set the basic conventional wages. There were substantial increases in these wages in November and December 1982, the first since October 1981; in December these wages were, in real terms, about 50 per cent below their level of October 1981. In recent years, these basic wages have become increasingly irrelevant, amounting to no more than 15-20 per cent of actual remunerations paid in October 1982 (around 25-30 per cent after the November and December corrections).

CHART 4

ARGENTINA

REAL WAGES IN MANUFACTURING[1]

(1976 = 100)



Source: National Institute of Statistics; and Fund staff estimates.

[1]Average monthly wages per worker (excluding year end bonuses) deflated by the consumer price index.

It is realized, however, that wage trends in the private sector and in state enterprises will be influenced in good measure by movements in government remunerations. Accordingly, from January 1983 wages for government employees will be adjusted no more frequently than quarterly, and the planned adjustment for the first quarter (12 per cent in February) represents a sharp decline in the rate of increase of nominal wages. Adjustments at the beginning of the next three quarters are to be about in line with the rate of inflation projected for the program period--i.e., are planned at 35 per cent, 31-1/2 per cent, and 28 per cent, respectively, for a total increase of 155 per cent for the year as a whole. To prevent a loss of qualified personnel in the Government, the restructuring of the government salary scale initiated in November 1982 in principle is to continue in 1983. However, only one third of this restructuring, or about the same proportion as in November 1982, is to be carried out in 1983, and only in quarterly installments to begin in April. With this adjustment, the government wage bill should be held to 7-1/2 per cent of GDP, only marginally up from its level in 1982 and still almost 3 percentage points of GDP less than in either 1979 or 1980.

5. External policies

a. Balance of payments

The program envisages a reduction in the overall balance of payments deficit from US$5.5 billion in 1982 to US$0.5 billion in 1983, a reduction equivalent to over 7 per cent of GDP (Table 5 and Chart 5), and aims at equilibrium for the first quarter of 1984. These objectives reflect the need to strengthen Argentina's creditworthiness after three years of mounting payments deficits. Some three quarters of the improvement in the overall balance of payments targeted for this year is expected to reflect a turnaround in the capital account. At the same time, the drop in international interest rates should reduce interest payments by at least US$600 million. An improvement of US$800 million (1 per cent of GDP) is expected on account of goods and nonfactor services; exports and imports are projected to grow substantially and a small improvement in the trade balance is projected.

Success in achieving the balance of payments targets depends critically on the authorities' ability to stem the outflow of short-term capital. Large short-term outflows were recorded in both 1980 and 1981 as the private sector wagered against the authorities' ability to maintain an overvalued exchange rate; in 1982 such outflows are estimated to have approached US$5 billion, reflecting the uncertainties surrounding events in the South Atlantic in the second quarter and the subsequent introduction of a policy of maintaining domestic interest rates at levels which were substantially negative in real terms. The authorities have indicated that it is their intention during the program period to take whatever actions are necessary with regard to interest rates and the exchange rate to bring this capital flight to a halt. It should be noted that the program assumes, conservatively, no new net

Table 5. Argentina: Summary Balance of Payments, 1978-83

	1978	1979	1980	1981	Est. 1982	Proj. 1983
	(In millions of U.S. dollars)					
Current account	1,833	-536	-4,768	-4,592	-2,230	-950
Merchandise trade	2,566	1,110	-2,519	-237	2,600	3,000
Exports, f.o.b.	6,400	7,810	8,021	9,143	8,100	9,500
Imports, c.i.f.	-3,834	-6,700	-10,540	-9,380	-5,500	-6,500
Services	-781	-1,681	-2,271	-4,333	-4,845	-3,950
Travel (net)	-307	-998	-1,447	-1,058	-91	--
Interest receipts	315	681	1,228	886	523	450
Interest payments	-720	-1,174	-2,175	-3,850	-5,031	-4,440
Other	-69	-190	123	-311	-246	40
Transfers	48	35	23	-22	15	--
Capital account	1,250	4,784	2,187	975	-3,160	450
Direct investment	274	265	788	904	270	365
Banking system 1/	-33	-175	-518	39	500	--
Trade finance 2/	-423	778	-115	-3,504	-2,405	85
Other public sector	1,388	1,222	2,957	4,535	-655	--
Other private sector 3/	44	2,694	-925	-998	-870	--
SDR allocation	--	73	74	70	--	--
Valuation adjustment 4/	166	132	-213	-363	-110	--
Change in net international (increase -)	-3,249	-4,453	2,720	3,910	5,500	500
	(As per cent of GDP) 5/					
Memorandum items						
Trade balance	5.3	1.9	-3.8	-0.4	3.8	3.9
Current account	3.8	-0.9	-7.2	-6.7	-3.2	-1.2
Overall balance	6.7	7.7	-4.1	-5.8	-8.0	-0.7

Sources: Central Bank of Argentina; and Fund staff estimates.

1/ Includes changes in Central Bank foreign assets not considered part of international reserves.

2/ Includes trade-related leads and lags, as well as identified trade credits.

3/ Includes errors and omissions.

4/ Changes in net international reserves due to exchange rate movements.

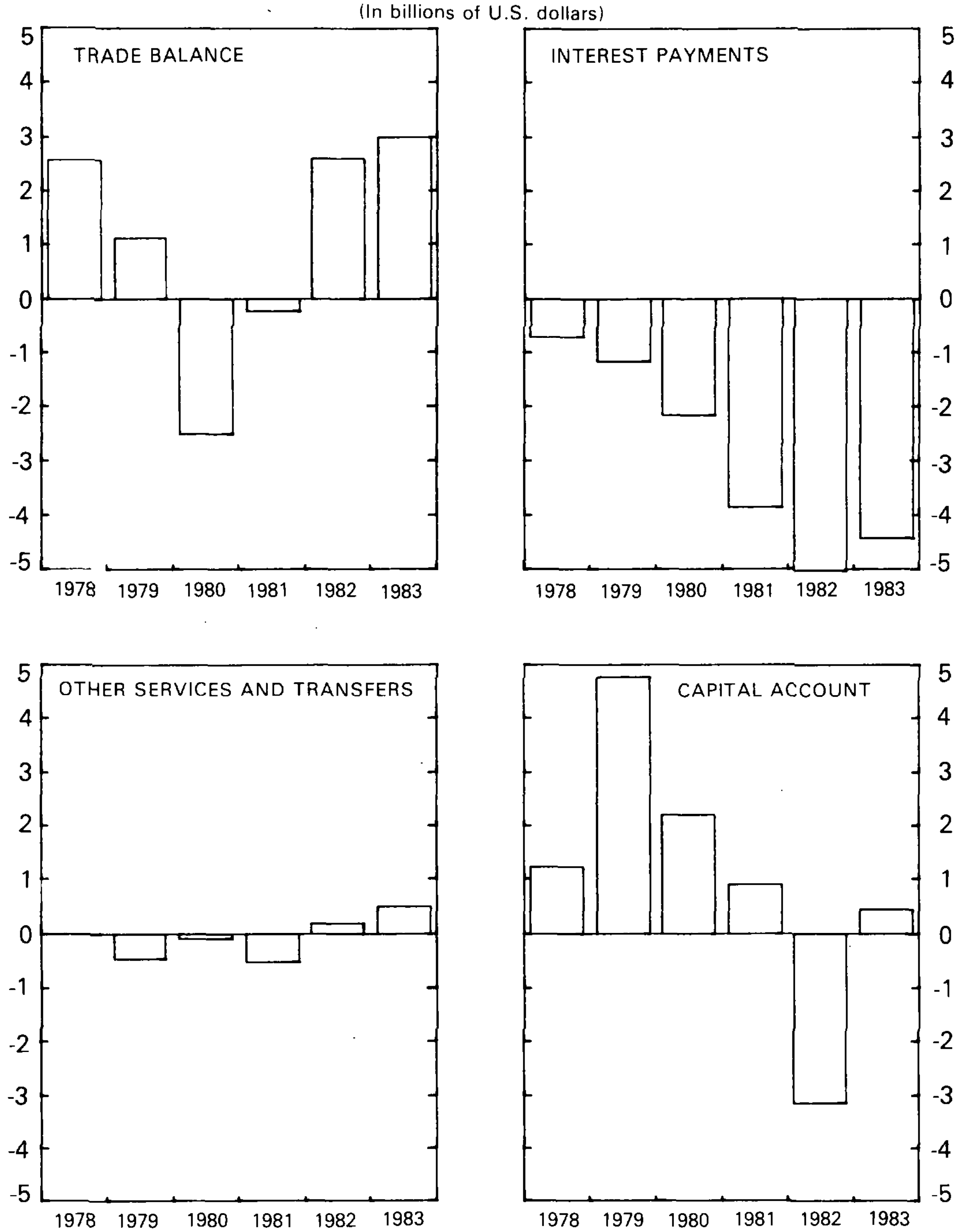
5/ Unlike in Table 3, for purposes of these calculations GDP has been converted to U.S. dollars using an exchange rate for the Argentine peso that would keep the peso/dollar exchange rate constant in real terms at its 1970 level.

CHART 5

ARGENTINA

MAIN COMPONENTS OF THE BALANCE OF PAYMENTS

(In billions of U.S. dollars)



Sources: Central Bank of Argentina and Fund staff estimates.

borrowing from international capital markets, other than a short-term "bridge loan" from commercial banks and a US$1.5 billion medium-term bank loan arranged in coordination with Fund financial assistance. These two loans are to be treated as reserve liabilities in the balance of payments, and the US$450 million net inflow projected above the line reflects only the reinvestment of profits and dividends and trade credits mandated under the legal minimum financing terms for capital goods and other imports.

Argentina's trade surplus is expected to increase only marginally in 1983, reaching US$3 billion, as both exports and imports rebound from the very low levels recorded in 1982. The export projections are examined in detail in the paper accompanying Argentina's request for a purchase under the compensatory financing facility; the main sources of expected export growth are a record grain crop and a marked expansion of nontraditional exports. Exceptionally favorable weather conditions have contributed importantly to the buoyant outlook for agricultural exports, and the sharp real depreciation of the peso and the unification of the exchange markets last November have substantially improved prospects for most categories of exports. Imports had surged during 1979-81 as the peso became increasingly overvalued and in 1982, the volume of imports declined by about 40 per cent; the imposition of import controls and difficulties encountered in opening letters of credit contributed to this decline but the timing of the adjustment indicates that the large depreciation of the peso in the first half of 1981 was by far the most important factor. For 1983, the program assumes an increase in import values of 18 per cent (in terms of U.S. dollars), an expansion which should be sufficient to accommodate both the projected expansion in real economic activity and a major liberalization of the import system.

Net outflows on account of nonfactor services declined from US$600 million in 1981 to almost zero in 1982, and a surplus of about US$400 million is projected for 1983. After three years of large net outflows, net receipts from tourism were positive in the last half of 1982, reflecting both exchange rate movements and the imposition of limits on the sale of exchange for tourism. Overall, the surplus on goods and nonfactor services is expected to increase from US$2.6 billion in 1982 to US$3.4 billion in 1983. Interest payments, while declining, will continue to impose a heavy burden; such payments exceeded US$5 billion in 1982 and are estimated at US$4.4 billion, or about 40 per cent of exports of goods and services, in 1983. These factors, taken together, imply a decline in the current account deficit from US$2.2 billion last year to US$950 million in 1983. If, however, the authorities are unsuccessful in their efforts to stem capital flight, a greater compression of the current account may be required.

b. External debt policies

As noted earlier, Argentina now faces a very serious debt service problem and efforts are under way to restructure the maturity profile of her external debt. The ratio of scheduled debt service payments to

Table 6. Argentina: Disbursed External Debt and Debt Service

	December				Aug.	Sept.
	1978	1979	1980	1981	1982	1982
(In millions of U.S. dollars)						
Total disbursed debt	12,496	19,034	27,162	35,671	34,060	...
By borrowing sector						
Public sector	8,357	9,960	14,459	20,024	20,385	21,420
Private sector	4,139	9,074	12,703	15,647	13,675	...
By maturity						
Medium and long term	9,849	13,703	16,877	26,077	27,071	...
Short term	2,647	5,331	10,285	9,604	6,989	...
Disbursed debt of public *sector, by type of creditor*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*
International organizations	13.1	12.9	7.8	6.0	5.9	5.6
Official creditors	5.2	4.7	2.6	1.9	1.7	1.6
Banks	55.5	55.1	71.0	67.4	64.7	64.2
Bond holders	13.6	14.7	10.1	18.7	21.8	22.9
Private firms	12.6	12.5	8.5	5.9	5.9	5.6

	1978	1979	1980	1981	1982
(In millions of U.S. dollars and in per cent)					
Debt service 1/	2,607	2,156	3,525	6,307	10,076
Amortization	1,887	982	1,350	2,457	5,045
Interest	720	1,174	2,175	3,850	5,031
Exports of goods and services	7,714	9,602	10,764	11,559	9,942
Debt service ratio	33.8	22.5	32.7	54.6	101.3

	1983	1984	1985	1986	1987
(In millions of U.S. dollars and in per cent)					
Debt service 1/	10,998	6,210	5,043	4,541	3,773
Amortization	6,558	3,508	2,903	2,870	2,500
Interest	4,440	2,702	2,140	1,671	1,273
Exports of goods and services	11,730	13,140	14,320	15,560	16,920
Debt service ratio	93.8	47.3	35.2	29.2	22.3

Sources: Central Bank of Argentina; and Fund staff projections.

1/ Includes amortization of loans with an original maturity of more than one year and all interest payments. Includes both public and private debt. Amortization numbers for 1982 reflect amounts due, rather than amounts actually paid. Amortization and interest payments for 1983 and beyond are based on the stock of debt outstanding as of the end of August 1982; no attempt has been made to take into account the impact of the rescheduling exercises for both private and public debt which are currently being undertaken.

exports of goods and services exceeded 100 per cent in 1982 and would exceed 90 per cent in 1983 in the absence of a restructuring of Argentina's debt (Table 6). At the end of August 1982, the medium- and long-term debt of Argentina totaled US$34 billion, excluding amounts in arrears. Scheduled amortization and projected interest through 1987 on that stock of debt are shown in Table 6. It is clear that a bunching of amortization payments and high interest rates have contributed heavily to Argentina's current difficulties, but projected service on debt already disbursed remains high for several years even assuming a drop in the average interest cost from 14 per cent in 1982 to 8-1/2 per cent in 1987. These large scheduled payments will need to be taken carefully into account in the current debt restructuring effort.

In accordance with the authorities' determination to prevent a recurrence of debt servicing difficulties should access to the international capital markets be restored, the program contains a limit of US$2 billion on net new external borrowing by the public sector.1/ Also, to assist in the effort to improve the maturity structure of the external debt, the program includes a limit on the net increase in maturities on public sector debt falling due through the end of the first quarter of 1987. The effect of this subceiling is to ensure that no more than US$500 million of the US$2 billion overall increase in indebtedness permitted under the program will fall due within three years of the expiration of the proposed stand-by arrangement; quarterly limits require that this US$500 million net borrowing in the shorter maturity ranges be spread fairly evenly over the period of the proposed stand-by arrangement.2/ Also, to ensure that the restructuring of Argentina's external debt that is to be undertaken during the program period is not offset by new shorter-term borrowing, these quarterly limits will be adjusted downward for any net debt relief obtained through formal multicreditor debt rescheduling agreements.

c. Exchange and trade policy

The authorities have announced their intention to continue with the policy of adjusting the exchange rate about in line with increases in wholesale prices. They recognize, however, that given the deeply imbedded inflationary expectations in Argentina, the key to achieving the balance of payments objectives of the program is adherence to a flexible exchange rate policy.

Extensive restrictions on current and capital transactions were introduced in the course of the South Atlantic conflict, and were further intensified in its aftermath.3/ Also, despite the unification of

1/ Loans treated as reserve liabilities of the Central Bank for purposes of the stand-by program (e.g., the bridge loan and the medium-term bank loan) are excluded from these limits.

2/ For a description of how these limits are specified, see footnote 3, Table 7.

3/ For a description of Argentina's exchange and trade system, see Section II and Appendix A of the accompanying report on recent economic developments.

the commercial and financial exchange markets in November 1982, the system of export taxes and rebates gives rise to a multiplicity of exchange rates which range from 25 per cent below to 25 per cent above the official rate in the unified exchange market. Large external payments arrears on current transactions remain, which also constitute a restriction on current payments. Another restriction arises from the unilateral rescheduling in November 1982 of approximately US$4.5 billion in loans to the Argentine private sector for which the domestic borrower had obtained an exchange rate guarantee from the Central Bank under the scheme in operation during the second half of 1981.1/ The multiple currency practices and restrictions maintained by Argentina on payments and transfers for current international transactions are enumerated in Appendix IV of the present paper.

The authorities recognize that these restrictions result in an inefficient allocation of resources and that payments arrears have had a detrimental effect on the supply of imported inputs and the level of economic activity. Accordingly, their intention is to dismantle most of these restrictions over the course of the program period. Priority has been given to the elimination of payments arrears, which amounted to almost US$2-1/2 billion at the end of December 1982. Disbursement of the first tranche (US$600 million) of the US$1.1 billion bridge loan from a group of foreign commercial banks permitted a reduction in arrears in the first week of January 1983. The program calls for the complete elimination of arrears by the end of June 1983, which the authorities anticipate will be possible given the schedule of purchases from the Fund and the phasing of disbursements under the bridge loan and the US$1.5 billion medium-term banking loan.

With the arrears paid and the adjustment program taking hold, the authorities hope to be in a position to relax progressively the existing restrictions on the provision of foreign exchange for payments and transfers for bona fide current international transactions with a view to their complete elimination by the end of 1983, although measures intended solely to prevent disguised capital flight would be retained. A schedule for the phased elimination of the minimum foreign financing requirements for noncapital goods imports already has been established. Given Argentina's large payments arrears and the shortage of freely disposable foreign exchange, it has not been possible at this time for the authorities to set forth a precise schedule for the planned liberalization of Argentina's exchange and trade system and the elimination of remaining multiple currency practices. Accordingly, the program calls for a review of exchange policies with the Fund during the second quarter of 1983. This review has been made a performance criterion, and Argentina's access to Fund resources under the program after the second purchase will be made contingent on Argentina's reaching understandings with the Fund on the course of exchange system policy for the remainder of the program period.

1/ See item 2(d) in Appendix IV.

Most consumer goods imports have been effectively banned since May 1982, when a requirement of "prior study" was imposed on all applications for import licenses for goods on a long list of "nonessential" imports; such imports are estimated to have constituted between 10-15 per cent of total imports before this ban was imposed. This ban on nonessential imports remains in effect, and the May 1983 review will offer an opportunity to determine the extent to which it continues to be warranted. In conducting that review, due consideration will be given to eventual damages suffered by Argentina's neighbors on account of these prohibitions. The authorities also introduced in May 1982 (and implemented in July) a system of importer-by-importer and commodity-by-commodity U.S. dollar limits on imports. This system of U.S. dollar limits turned out to be both burdensome and unnecessary, given the reduced demand for permitted imports, and it was terminated at the end of October. In September, all outstanding import licenses for imports from Uruguay and Paraguay were cancelled because of suspected overinvoicing; subsequently, normal processing of such licenses was resumed after improved procedures for monitoring unit values had been established.

6. Performance criteria and review clause 1/

The program contains as performance criteria: (1) a quarterly balance of payments test limiting the deficit to US$500 million in 1983 (while allowing for seasonal variations) and requiring equilibrium in the first quarter of 1984 (paragraph 2 of the Memorandum of Understanding); (2) quarterly cumulative limits on the global borrowing requirement of the nonfinancial public sector, covering net borrowing from the domestic financial system, net placements of government paper outside this system, and net external borrowing (paragraph 3 of the Memorandum of Understanding); (3) a set of ceilings applicable at all times limiting the expansion of the net domestic assets of the Central Bank to the growth of its currency issue, constrained to the inflation target, plus the targeted balance of payments deficits (paragraph 4 of the Memorandum of Understanding); (4) a ceiling on the increase in the total disbursed external debt of the public sector as well as a complementary set of ceilings on the total principal payments falling due within three years of each quarterly test date; the latter limit is designed to permit the rollover of existing debt on a short-term basis, pending formal restructuring, but to require that new loans, whatever their final maturity, entail a net increase of not more than about US$500 million, in principal, falling due through the end of March 1987 (paragraph 5 of the Memorandum of Understanding); (5) the usual provisions regarding the exchange and import system (paragraphs 6 and 7 of the Memorandum of Understanding); a schedule for the phased elimination of the minimum financing requirement for imports and a commitment to terminate the system of special rebates for exports to new markets by February 28, 1983; (paragraph 6 of the Memorandum of Understanding); and a commitment to eliminate all current external payments arrears by June 30, 1983

1/ *Quantitative performance criteria are presented in Table 7.*

Table 7. Argentina: Stand-by Arrangement, Quantitative Performance Criteria for the period through March 1984

	1983				1984
	Jan.-Mar.	Apr.-June	July-Sept.	Oct.-Dec.	Jan.-Mar.
	(In trillions of Argentine pesos)				
Cumulative global borrowing needs of the nonfinancial public sector	105	208	326	445	559
Cumulative change in net domestic assets of the Central Bank of Argentina					
Change in currency issue of the Central Bank since December 31, 1982 plus indicated peso amounts:	9.7	15.0	4.9	11.7	24.3
With an upper limit of indicated percentage of December 31, 1982 currency issue plus indicated peso amounts (in per cent plus $a trillion)	40 plus $a 9.7	80 plus $a 15.0	130 plus $a 4.9	170 plus $a 11.7	220 plus $a 24.3
	(In millions of U.S. dollars)				
Cumulative change since December 31, 1982 in disbursed external debt of the public sector 1/	2,000	2,000	2,000	2,000	2,000
Increase, compared to December 31, 1982, in maturities of public sector debt falling due within three years of end of quarter 1/2/3/	600	1,200	1,800	2,400	3,000
Cumulative change in net international reserves of the Central Bank of Argentina 2/	-400	-220	20	-500	-500

Sources: Ministry of Economy; Central Bank of Argentina; and Fund staff estimates.

1/ Excludes reserve liability borrowings by the Central Bank.
2/ Limit tested at the end of each period.
3/ These limits are set for moving three-year periods and specify the maximum increase in maturities falling due within those three-year periods, compared to total maturities falling within three years of December 31, 1982. For example, total maturities falling due between March 31, 1983 and March 31, 1986, based on the stock of debt outstanding as of March 31, 1983, should exceed by no more than US$600 million total maturities falling due between December 31, 1982 and December 31, 1985, based on the stock of debt outstanding as of December 31, 1982. It should be noted that these limits are the sum of two components: (1) the net increase in maturities falling due within the period as a result of new borrowing, and (2) the impact of moving the period to which the limits apply. The US$3 billion limit for the full program period reflects approximately US$500 million in maturities falling due before March 31, 1987 as a result of new borrowing during the period of the stand-by arrangement plus approximately US$2,500 million in maturities falling due between December 31, 1985 and March 31, 1987 on debt already disbursed at the end of 1982. As specified here, these limits assume debt maturing in one period will be rolled over into the subsequent period; these limits will, however, be adjusted downward to reflect the net impact of any formal, multi-creditor agreements for rescheduling Argentina's debt.

(paragraph 8 of the Memorandum of Understanding); and (6) a special review clause requiring that understandings be reached on a schedule for the elimination of all other existing multiple currency practices and restrictions on current payments before the third (August) purchase can be effected (paragraphs 6 and 7 of the Memorandum of Understanding). All these performance criteria are referred to in paragraph 4 of the stand-by arrangement.

IV. Staff Appraisal and Proposed Decision

Argentina is faced with a severe economic crisis. In the last two years, output, real wages, and industrial employment have dropped sharply, and the unemployment rate is at its highest level in many years. Real per capita income is at its lowest level in ten years. Inflation has averaged over 150 per cent a year since 1975 and accelerated to about 310 per cent during 1982.

Even in the current world economic situation, not many countries confront imbalances of such magnitude, and it is unquestionably difficult to determine what policy mix holds out the greatest hopes of steering Argentina's economy onto a path of recovery and internal and external equilibrium. Furthermore, the present Administration is to be replaced by an elected government in the first half of 1984 and the difficulty of the adjustment effort is made all the greater by the short political horizon. The authorities, therefore, are to be commended for their determination to initiate such an adjustment, aware as they are that it is likely to produce results only slowly. Their margin of maneuver is constrained further by concern for maintaining as broad a consensus as possible on the speed and on the distribution of the burden of the adjustment. While this constraint rules out a shock approach to Argentina's problems, the authorities recognize that the marked intensification of financial imbalances in recent months owes much to the policies introduced by the previous economic team in July-August 1982 and that the policy course adopted at that time requires prompt and substantial correction.

The program presented by the authorities in support of their request for a 15-month stand-by arrangement has three main goals: a substantial improvement in the balance of payments, a marked reduction in inflation, and a recovery of the productive sectors of the economy. Its instrumentation centers on adjustments in the exchange and trade system, on the adoption of a prudent wage policy, on a substantial improvement in the public finances, and on a tightening of monetary policies.

With the unification of the exchange markets in November 1982, and the adoption of a policy of moving the exchange rate broadly in line with the rate of inflation, an important step has already been taken to eliminate distortions arising from the exchange system and to strengthen the competitiveness of the Argentine economy. It will be important for the exchange rate to be managed with considerable flexibility in the period ahead to ensure attainment of the balance of payments and other objectives of the program.

In October, the authorities abolished the importer-by-importer and commodity-by-commodity U.S. dollar limits on imports which had been imposed in May 1982, thereby re-establishing automatic licensing for all permitted imports. The system of special rebates for exports to new markets, a multiple currency practice, is being terminated; the resolutions implementing this change are to be issued before February 28, 1983. The staff welcomes these actions and urges the authorities, as Argentina's external position begins to strengthen, to move boldly in eliminating remaining multiple currency practices and in reducing restrictions on imports and on payments and transfers for current international transactions. Such actions should facilitate achievement of the targeted recovery in economic activity and exports.

The authorities already have established a schedule for the phased elimination of the 90-180-day minimum financing requirement for imports over the period of the stand-by arrangement. They also have committed themselves to eliminate all external payments arrears by June 30, 1983 and, thereafter, gradually to reestablish freedom for current payments and transfers. While the circumstances of late 1982 did not permit the setting of a precise timetable for further exchange and trade liberalization, the Government has committed itself to establish a schedule for the elimination of existing multiple currency practices and restrictions on payments and transfers for current international transactions within the context of the review with the Fund that is to take place in the second quarter of 1983.

A central component of the adjustment program is the abandonment in the early months of the program of wage indexing for government employees and the subsequent determination of wage adjustments on the basis of targeted future inflation. Another key element, which is closely related to wage policy, is the compression of the public sector financing requirement from more than 14 per cent of GDP in 1982 to 8 per cent of GDP in 1983 and to an annual rate of 5 per cent of GDP in the first quarter of 1984. The staff is of the view that a break with the wage policy of the past six months--which initially involved large nominal adjustments and subsequently monthly increases tantamount to indexing on past inflation--is indispensable not only because of the implications for the public sector deficit, but also because wage movements in government employment have a major impact on adjustments in the private sector. Indeed, adjustments in government remunerations in excess of those incorporated in the projected path would jeopardize the goal of slowing inflation and, with it, the entire program. The staff also welcomes the intention of the authorities to limit the degree of government intervention in the determination of private sector wage increases.

The targeted reduction in the public sector deficit involves a major effort but is clearly feasible. Its attainment will call for much determination on the part of the authorities in reining in the growth of government current spending and of the operating outlays of the state enterprises, especially if room is to be made for a modest recovery of public investment. Revenue growth in excess of the increase in nominal GDP is predicated on a full year's application of the export taxes adopted in July 1982 and, more importantly, on continued adjustments in public sector prices and charges--adjustments which on average should amount to no less than 80 per cent in real terms during the 18-month period ending March 1984. This includes a minimum of 110 per cent in real terms for fuel prices, a substantial part of which is to be realized by the end of February 1983.

The component of the adjustment program which may prove to be most difficult to implement--and the most controversial in Argentina's present circumstances--is the correction of interest rate and credit policy. Real money balances dropped precipitously in the second half of 1982 when real interest rates were sharply negative. The program envisages that the bulk of the public sector deficit will be financed domestically. There also is a need to accommodate some increase in credit to the private sector (a large part of which will be autonomous because of the subsidies involved in the domestic debt refinancing scheme introduced in mid-1982) if output is to revive. It is, therefore, crucial that interest rates be set sufficiently high to bring the acceleration in the income velocity of money to a halt and provide for a growth of domestic financial savings that at a minimum would be in line with the rise in money national income; indeed, the aim should be to try to achieve a growth of financial savings somewhat in excess of nominal income growth.

A formula based on a three-month moving average of past and projected inflation is to be used in setting regulated interest rates. If inflation declines steadily the use of this formula should result in interest rates which are slightly positive in real terms, but the possiblity exists that interest rates will remain negative in real terms, particularly on the deposit side. In any event, the staff notes that the formula only sets a floor for interest rates and that the authorities may well find it necessary to raise interest rates over and above the levels determined by the formula; this would be the case particularly if broad money should not rise as quickly as projected and thus affect the chances of achieving the balance of payments improvement targeted in the program.

With full adherence to the policy instrumentation of the program, the overall balance of payments improvement should be attained relatively easily. With deeply imbedded inflationary expectations, the deceleration of price increases is likely to be more elusive. Moreover, the requisite price, exchange rate and interest rate adjustments are bound to impart inflationary impulses in the early months of the year. The program should help to create the conditions for a revival of economic activity, but the extent of this revival depends on a number of other factors, including the speed at which confidence will be restored. Private entrepreneurs appear (with some reason) to be frustrated and disoriented by the frequent and abrupt changes in Argentina's economic strategies and, therefore, unlikely to react quickly to new economic policy orientations. They will probably need to be convinced that the corner has really been turned in improving Argentina's external and internal financial conditions before they repatriate capital and resume productive investment.

The program which the Argentine authorities have submitted to the Fund as the basis for their request for a stand-by arrangement undoubtedly will be difficult to implement. One reason is that it calls for perseverance with policies of restraint at a time when party politics and trade union activity are reviving in Argentina for the first time in eight years. Another reason is that the success of the program depends critically on world economic conditions and on the cooperation of foreign banks in providing debt relief and a measure of balance of payments support. Given the magnitude of the imbalances plaguing the Argentine economy, a medium-term program supported by the Fund with a financial arrangement of equal length would have been the appropriate framework for the requisite adjustment effort. Because of the limited political horizon of the present Administration, however, it was not possible to take that route. The 15-month program which it has submitted to the Fund is, in the staff's opinion, appropriate in Argentina's circumstances and merits Fund support with a stand-by arrangement for the maximum amount available to Argentina under existing Fund policies.

The following draft decisions are proposed for adoption by the Executive Board:

Stand-By Arrangement

1. The Government of Argentina has requested a stand-by arrangement for the period January --, 1983 to April --, 1984 for an amount equivalent to SDR 1.5 billion.

2. The Fund approves the stand-by arrangement attached to EBS/83/8.

3. The Fund waives the limitation in Article V, Section 3(b)(iii).

Article IV Consultation

1. The Fund takes this decision relating to Argentina's exchange measures subject to Article VIII, Sections 2 and 3, in the light of the 1982 Article IV consultation with Argentina conducted under Decision No. 5392-(77/63), adopted April 29, 1977 (Surveillance over Exchange Rate Policies).

2. The Fund welcomes Argentina's intention to eliminate progressively its multiple currency practices and restrictions on payments and transfers for current international transactions in the context of the adoption by Argentina of comprehensive policies for balance of payments adjustment, which are supported by a stand-by arrangement from the Fund. In the meantime, the Fund grants approval for the retention of the practices described in items 1(a)-(b) and items 2(a)-(e) of Appendix IV of EBS/83/8, until July 31, 1983.

Fund Relations with Argentina

Date of membership:	September 1956.		
Status:	Article VIII.		
Quota:	SDR 802.5 million.		
Fund holdings of Argentine pesos:	As of December 31, 1982	Millions of SDRs	Per Cent of Quota
	Total currency holdings	711.5	88.7
	Holdings from outstanding purchases	None	None
Special Drawing Rights Department (as of November 30, 1982):	Holdings (--) are zero per cent of net cumulative allocations of SDR 318.4 million.		
Transactions with the Fund:	Argentina has had nine stand-by arrangements, the last of which expired on September 15, 1978. Argentina made no purchase under that arrangement.		
Direct distribution of profits from gold sales (July 1, 1976-July 31, 1980):	US$69.9 million.		
Gold distribution:	376,565 fine ounces in four distributions.		
Exchange rate:	On July 5, 1982, the foreign exchange market was split into a commercial market for trade transactions and a financial market for other permitted transactions. The rate in the commercial market was set initially at $a 20,000 per U.S. dollar, representing a 21 per cent devaluation of the peso from its last quotation on the unified market and thereafter was adjusted daily; the financial peso was allowed to float for several weeks and was then pegged at about $a 39,000 per U.S. dollar. On November 1, 1982, the two markets were unified at a rate of $a 39,000 which represented a depreciation on that date of the exchange rate for commercial transactions of about 13 per cent. Since November 1, the unified exchange rate has been adjusted daily. On December 30, 1982 the exchange rate was $a 48,520 per U.S. dollar (buying) and $a 48,570 per U.S. dollar (selling).		
Last consultation (Article IV):	Discussions August 27-September 16, 1981 and January 18-27, 1982; consultation completed by the Executive Board on March 12 and 15, 1982 (SM/81/233 of 12/2/81 and Supplement 1 of 2/25/82 and SM/81/239).		

Argentina--Basic Data

Area and population	
Area (continental)	2,792,000 sq. kilometers
Population (mid-1981)	28.1 million
Annual rate of population increase (1976-81)	1.5 per cent
GDP at market prices (1981) 1/	SDR 57,292 million
GDP per capita (1981 est.)1/	SDR 2,039

	1979	1980	1981	Est. 1982
Origin of GDP		(per cent)		
Agriculture	13.5	12.5	13.9	14.9
Manufacturing	26.0	24.9	22.3	22.0
Construction	7.0	7.4	7.2	6.0
Transportation and communications	11.0	11.0	11.2	11.2
Commerce	14.1	14.4	14.0	13.4
Other	28.4	29.8	31.4	32.3
Ratios to GDP				
Exports of goods and services	9.0	6.9	9.5	13.6
Imports of goods and services	8.8	9.0	9.7	9.6
General government revenue	24.4	26.4	23.7	21.6
General government expenditure	28.7	31.9	34.3	29.0
External public debt (end of year)1/	17.3	22.0	29.6	32.6
Saving	23.6	22.6	17.9	12.7
Investment	24.1	25.7	22.0	17.1
Money and quasi-money (end of year)	37.2	35.0	37.9	27.0
Annual changes in selected economic indicators				
Real GDP per capita	5.5	-0.8	-7.3	-5.6
Real GDP	7.1	0.7	-6.0	-4.3
GDP at current prices	168.6	102.5	93.5	187.9
Domestic expenditures (at current prices)	178.9	107.4	89.8	175.8
Investment	160.8	116.2	65.5	124.4
Consumption	185.2	104.6	98.0	190.3
GDP deflator	150.7	101.1	105.9	200.8
Wholesale prices (annual averages)	149.3	75.4	109.6	258.0
Consumer prices (annual averages)	159.5	100.8	104.5	159.2
General government revenues	161.5	113.3	73.5	162.8
General government expenditures	157.8	119.2	107.6	143.7
Money and quasi-money	188.2	90.1	109.8	105.0
Money	140.9	97.6	69.7	165.2
Quasi-money	210.3	87.4	125.0	87.7
Net domestic financial assets 2/	182.6	106.9	132.1	133.8
Credit to public sector (net) 2/	14.0	15.9	46.0	41.6
Credit to private sector 2/	144.0	81.6	88.7	88.0
Merchandise exports (f.o.b., in U.S. dollars)	22.0	2.7	14.0	-11.4
Merchandise imports (c.i.f., in U.S. dollars)	74.8	57.3	-11.0	-41.4

General government finances	1979	1980	1981	Est. 1982
	(billions of Argentine pesos)			
Revenues	34,921	74,474	121,187	339,460
Expenditures	41,060	90,023	186,871	455,411
Overall deficit (-)	-6,139	-15,549	-57,684	-115,951
External financing (net)	436	-125	9,619	-9,000
Internal financing (net)	5,703	15,674	48,065	124,951
Balance of payments	(millions of U.S. dollars)			
Merchandise exports, f.o.b.	7,810	8,021	9,143	8,100
Merchandise imports, c.i.f.	-6,700	-10,540	-9,380	-5,500
Interest payments (net)	-493	-947	-2,964	-4,508
Other services and transfers (net)	-1,153	-1,302	-1,391	-322
Balance on current and transfer accounts	-536	-4,768	-4,592	-2,230
Financial loans to nonfinancial public sector	1,222	2,957	4,535	-655
Other capital flows 3/	3,694	-983	-3,923	-2,615
Allocation of SDRs	73	74	70	--
Change in net official reserves (increase -)	-4,453	2,720	3,910	5,500

International reserve position	Nov. 30 1981	Dec. 31 1981	Nov. 30 1982
	(millions of SDRs)		
Central Bank (gross)	2,989.4	3,001.4	2,981.9
Central Bank (net)	2,774.6	2,709.0	2,370.5
Central Bank and Treasury (net)	2,759.1	2,694.8	2,360.0

1/ GDP in dollars or SDRs is derived by converting GDP in Argentine pesos using the U.S. dollar/peso exchange rate that would maintain this exchange rate at its real 1970 level.

2/ Effective flows in relation to the adjusted stock of liabilities to the private sector.

3/ Includes direct investment, trade credits, trade related leads and lags, and errors and omissions.

Argentina: Main Targets, Assumptions, and Elements of the Financial Program

I. Targets

1. A reduction in the overall deficit of the nonfinancial public sector (relative to GDP) to no more than 8 per cent in 1983, and 5 per cent in the first quarter of 1984, compared with deficits of over 14 per cent in 1981 and 1982.

2. A level of public sector savings (relative to GDP) of over 1-1/2 per cent in 1983 and over 3-1/2 per cent in the first quarter of 1984, compared with a negative level of 5 per cent in 1982.

3. Some remonetization of the economy following the sharp decline in real money balances in the second half of 1982. During the program period, money balances (broadly defined) are projected to rise about 5 per cent faster than the projected growth in nominal GDP.

4. A substantial moderation in the rate of inflation. Wholesale prices are projected to rise by 160 per cent during 1983, compared with about 310 per cent during 1982; during the first quarter of 1984, it is projected that wholesale prices will rise at an annual rate of about 85 per cent.

5. A reduction in the overall balance of payments deficit from US$5.5 billion (8.0 per cent of GDP) in 1982 to no more than US$500 million (0.7 per cent of GDP) in 1983 and a target of overall balance of payments equilibrium in 1984, with external payments arrears, as well as balance of payments support loans from foreign banks and certain other balance of payments support operations, treated as reserve liabilities of the Central Bank.

II. Assumptions

1. Real GDP is projected to rise at an annual rate of about 5 per cent in 1983 and the first quarter of 1984, reflecting a substantial increase in agricultural output and higher production of nontraditional exports.

2. Buoyed by a record grain harvest, the volume of exports is projected to rise considerably faster than the growth of Argentina's export markets and a slight improvement in the terms of trade is projected; on the basis of these assumptions, a substantial rise in import volumes would still be consistent with a slight improvement in the trade balance in 1983.

3. The three-month London Interbank Offered rate is assumed to average 10-1/2 per cent throughout the program period. However, this decline in LIBOR compared to 1982 will be partially offset by higher spreads on both public and private sector borrowing.

4. Net capital inflows of US$450 million are projected for 1983 and US$120 million for the first quarter of 1984. Trade-related financing and reinvestment of profits and dividends are assumed to account for all of the net inflow in 1983 and for US$45 million of the net inflow in the first quarter of 1984. Net financing from the international capital markets is, therefore, assumed to be zero in 1983 and US$75 million in the first quarter of 1984; the bridge loan and the US$1.5 billion medium-term loan that have been arranged by the international banks in conjunction with the proposed stand-by arrangement are treated as Central Bank reserve liabilities and, therefore, not included in these capital account estimates.

III. Main Elements of the Program

1. Public sector policies

a. The main discretionary measures behind the improvement in the nonfinancial public sector's overall balance are an improvement in tax administration; the continued implementation of the scheduled increases in public sector tariffs, which was begun in October 1982 (plus an additional 20 per cent real increase in fuel prices between November 1982 and February 1983); a break, in the first quarter of 1983, with the policy of indexing salaries of government workers to past inflation, and the establishment of a quarterly rather than monthly timetable for government wage adjustments; a limit on government hiring and strict control of current spending by the government and public enterprises. Government revenues also will benefit in 1983 from increases in export and excise taxes in the second half of 1982.

b. The increase in public sector saving that is projected permits an increase in public sector investment (relative to GDP) in 1983, while public sector investment (relative to GDP) would drop back to its 1982 level in the first quarter of 1984. Capital spending is to be concentrated in labor intensive projects with little import content and generally will involve small and ongoing projects so as not to prejudge the investment program of the incoming administration.

c. Cumulative quarterly limits have been placed on the total borrowing requirement of the nonfinancial public sector, defined to include external borrowing, net borrowing from the domestic financial system, and the net increase in the private sector's holdings of Treasury bills and bonds.

2. Money and credit

a. With effect from January 1, 1983, regulated interest rates will be set on the basis of a moving average of the rate of increase in wholesale prices for the previous two months and the projected rate of price increase for the current month. The rate of interest for loans will be set equal to the moving average of the rate of inflation, and the rate of interest on 30-day regulated deposits will be set within 1 percentage point below the lending rate. This formula sets a floor to regulated interest rates; these rates will be managed flexibly with a view to achieving the targeted improvement in the overall balance of payments and the projected increase in domestic financial savings.

b. The growth in the net domestic assets of the Central Bank will be limited to the growth in currency issue plus specified peso amounts for each quarter which are consistent with the overall balance of payments target, with an upper limit defined in terms of the currency issue for end December 1982; specifically, over the 15-month period from end 1982 to end March 1984, the increase in net credit of the Central Bank will be limited to currency issue plus $a 24.3 trillion, or 220 per cent of currency issue at end December 1982 plus $a 24.3 trillion, whichever is lower.

c. Notwithstanding the remonetization of the economy and the substantial reduction in the deficit of the nonfinancial public sector that has been projected, the financial program implies that credit to the private sector will be sharply constrained. A recovery in private sector activity greater than the one envisaged in the program would thus require a repatriation of private capital.

3. Wages

Wage policy is to be geared to the achievement of a significant deceleration of inflation. The Government is to abstain from intervening in the process of wage determination in the private sector. In the Government, wage indexing is to be discontinued in the first quarter of 1983, with only one adjustment, of 12 per cent, to be granted in February. From the second quarter, wage raises will be granted quarterly and at rates consistent with the decline in the rate of inflation which is being sought.

4. External sector

a. Exchange rate policy will be managed flexibly to ensure the attainment of the balance of payments objectives of the program: as a minimum, the exchange rate will be adjusted to offset domestic inflation. Interest rate and exchange rate policy will be coordinated in order to stem capital flight and facilitate the attainment of the balance of payments objective without undue compression of the current account.

b. The system of special rebates for exports to new markets, a multiple currency practice, will be terminated by February 28, 1983; all external payments arrears will be eliminated by June 30, 1983; and the minimum financing requirements for imports other than capital goods are to be eliminated according to a schedule which is a performance criterion under the stand-by arrangement. All other multiple currency practices and restrictions on payments and transfers for current international transactions are to be eliminated according to a schedule to be established during the May review with the Fund. Freedom for current payments and transfers is to be established by no later than December 31, 1983. The standard clause on restrictions and multiple currency practices is included as a performance criterion.

c. As adjustment proceeds, import restrictions are to be relaxed with a view to rationalizing the structure of protection and improving resource allocation. The May 1983 review will encompass a discussion of trade policies.

d. The net increase in the external indebtedness (excluding official reserve liabilities of the monetary authorities) of the public sector over the period of the stand-by arrangement is to be limited to US$2 billion; borrowing from all sources and of all maturities is covered by this limit. Also, to assist in the effort to improve the maturity profile of the external debt, the program includes a limit on the net increase in maturities of the public sector debt falling due before the end of the first quarter of 1987. The purpose of this subceiling is to ensure that no more than US$500 million of the US$2 billion overall increase in the public sector's indebtedness will fall due within three years of the expiration of the proposed stand-by arrangement.1/

1/ For a description of how this subceiling has been specified, see footnote 3, Table 7.

Argentina: Exchange and Trade System

A detailed description of the exchange and trade system maintained by Argentina is provided in Appendix A to the paper on recent economic developments that accompanies this report. A list of selected changes introduced in the exchange and trade system over the course of 1982 is provided in that same appendix.

The exchange system currently in effect in Argentina involves the following multiple currency practices and restrictions on payments and transfers for current international transactions subject to Fund approval under Article VIII, Sections 2 and 3 of the Articles of Agreement.

1. Multiple currency practices

Argentina maintains a system of rebates for certain exports which is implemented through the exchange system. These rebates are set as a percentage of the export value, and the exchange proceeds must be surrendered as a condition for payment of the rebate. In the general case, the rebates are paid to the exporter by the intervening bank at the time the exchange proceeds are surrendered or the letter of credit is discounted.

a. Rebate rates of 5 or 10 per cent presently apply to certain promoted exports. In addition, exports originating in and shipped through ports located in specified less developed regions of Argentina are eligible for rebates of 5 to 9 per cent. The Argentine authorities have committed themselves, pending the review with the Fund in May 1983, to continue to operate this system only within the existing range of rates.

b. Argentina also maintains a system whereby special rebates of 5 per cent are provided for fixed periods for exports to new markets.

2. Exchange restrictions

a. An exchange restriction arises from the existence of arrears on current payments and transfers. Total external payments arrears amounted to US$1,976 million at the end of November 1982.

b. Sales of exchange to effect the transfer of profits, dividends, royalties, and payments for technical assistance have been suspended since April 20, 1982.

c. Prior Central Bank approval is required for the sale of exchange to effect certain transfers and payments related to services. Such approval is required for sales of exchange beyond certain specified limits for foreign travel, foreign study, family remittances, and foreign medical treatment. In the present circumstances, such authorization is not automatically granted for all bona fide current payments and transfers.

d. The sale of exchange is not currently permitted for the repayment of foreign loans for which the domestic borrower obtained an exchange rate guarantee during 1981. These loans had a minimum maturity of 540 days and, in some instances, were related to current trade finance. The foreign creditor must reschedule such loans, either by accepting a U.S. dollar-denominated Government of Argentina debt instrument, or by renegotiating the loan directly with the domestic borrower according to minimum terms established by the Central Bank of Argentina.

e. Minimum foreign financing terms of between one and five years have been established for imports of capital goods valued at more than US$50,000.

f. Minimum foreign financing terms have been established for most imports other than capital goods as follows:

(i) Goods on the "negotiated" list shipped from and originating in member countries of the Latin American Integration Association (LAIA) may be paid for against shipping documents;

(ii) Other goods shipped from and originating in LAIA, as well as goods shipped from and originating in the member countries of the Central American Common Market, Cuba, Haiti, Panama, or the Dominican Republic are subject to minimum financing terms of 90 days; and

(iii) Imports from all other countries are subject to minimum financing terms of 180 days.

In view of the discriminatory nature of this restriction, Fund approval has not been requested.

Argentina maintains an additional multiple currency practice related to capital transactions. The Central Bank of Argentina has undertaken foreign exchange swap arrangements with private domestic borrowers; the premia charged for such swap arrangements are set well below the recent or expected rate of depreciation of the peso and, therefore, these arrangements cannot be deemed to be reasonably related to normal forward exchange operations. As of the end of 1982, approximately US$1.3 billion of such swap arrangements were outstanding.

The Argentine authorities have undertaken to terminate the system of special rebates for exports to new markets by February 28, 1983; to eliminate all payments arrears by June 30, 1983; to eliminate the 90- to 180-day minimum financing requirement for noncapital goods imports according to a schedule which is a performance criterion under the proposed stand-by arrangement; and to eliminate all other multiple currency practices and restrictions on payments and transfers for current international payments according to a schedule on which understandings are to be reached during the May review. Freedom for current payments and transfers is to be established by no later than December 31, 1983.

Stand-By Arrangement - Argentina

Attached hereto is a letter with annexed memoranda dated January 7, 1983 from the Minister of Economy and the President of the Central Bank of the Argentine Republic requesting a stand-by arrangement and setting forth the objectives and policies that the authorities of Argentina intend to pursue for the period of this stand-by arrangement.

To support these objectives and policies the International Monetary Fund grants this stand-by arrangement in accordance with the following provisions:

1. For the period from January --, 1983 to April --, 1984 Argentina will have the right to make purchases from the Fund in an amount equivalent to SDR 1,500 million, subject to paragraphs 2, 3, 4, and 5 below, without further review by the Fund.

2. (a) Purchases under this stand-by arrangement shall not, without the consent of the Fund, exceed the equivalent of SDR 300.74 million until May 20, 1983, the equivalent of SDR 600.51 million until August 20, 1983, the equivalent of SDR 900.27 million until November 20, 1983, and the equivalent of SDR 1,200.04 million until February 20, 1984.

(b) None of the limits in (a) above shall apply to a purchase under this stand-by arrangement that would not increase the Fund's holdings of Argentina's currency in the credit tranches beyond 25 per cent of quota or increase the Fund's holdings of that currency resulting from purchases of borrowed resources beyond 12.5 per cent of quota.

3. Purchases under this stand-by arrangement shall be made from ordinary and borrowed resources in the ratio of 2 to 1 until purchases under the arrangement reach the equivalent of SDR 300,937,500 and then from ordinary and borrowed resources in the ratio of 1 to 1.2, provided that any modification by the Fund of the proportions of ordinary and borrowed resources shall apply to amounts that may be purchased after the date of modification.

4. Argentina will not make purchases under this stand-by arrangement, other than the initial purchase equivalent to SDR 300.74 million that it may request not later than within 15 days of the effective date of this arrangement, that would increase the Fund's holdings of Argentina's currency in the credit tranches beyond 25 per cent of quota or increase the Fund's holdings of that currency resulting from purchases of borrowed resources beyond 12.5 per cent of quota:

(a) during any period in which the ceiling on the net domestic assets of the Central Bank described in paragraph 4 of the Memorandum of Understanding annexed to the attached letter has been exceeded; or

(b) during any period in which the data at the end of the preceding calendar quarter indicate that

(i) the cumulative overall balance of payments targets described in paragraph 2 of the Memorandum of Understanding annexed to the attached letter have not been met, or

(ii) the limit on the cumulative borrowing needs of the nonfinancial public sector described in paragraph 3 of the Memorandum of Understanding annexed to the attached letter has been exceeded, or

(iii) the cumulative limit on the outstanding disbursed external debt of the public sector described in paragraph 5 of the Memorandum of Understanding annexed to the attached letter has been exceeded, or

(iv) the limits on total maturities falling due within 36 months of the end of each calendar quarter described in paragraph 5 of the Memorandum of Understanding annexed to the attached letter have been exceeded, or,

(c) during any period after February 28, 1983 in which the system of special rebates for exports to new markets has not been terminated, or

(d) during any period after March 31, 1983 in which the schedule for the phased elimination of the minimum foreign financing requirements for imports, as set out in paragraph 6 of the Memorandum of Understanding annexed to the attached letter, has not been adhered to, or

(e) during any period after June 30, 1983 in which external payments arrears persist or reappear, or

(f) during any period after July 31, 1983 in which understandings between Argentina and the Fund on a schedule for the elimination of existing multiple currency practices and restrictions on payments and transfers for current international transactions have not been reached, or

(g) during the entire period of this stand-by arrangement, if Argentina

(i) imposes or intensifies restrictions on payments and transfers for current international transactions, or

(ii) introduces or modifies multiple currency practices except as referred to in paragraph 7 of the Memorandum of Understanding annexed to the attached letter, or

(iii) concludes bilateral payments agreements which are inconsistent with Article VIII, or

(iv) imposes or intensifies import restrictions for balance of payments reasons.

When Argentina is prevented from purchasing under this stand-by arrangement because of this paragraph 4, purchases will be resumed only after consultation has taken place between the Fund and Argentina and understandings have been reached regarding the circumstances in which such purchases can be resumed.

5. Argentina's right to engage in the transactions covered by this stand-by arrangement can be suspended only with respect to requests received by the Fund after (a) a formal ineligibility, or (b) a decision of the Executive Board to suspend transactions, either generally, or in order to consider a proposal, made by an Executive Director or the Managing Director, formally to suppress or to limit the eligibility of Argentina. When notice of a decision of formal ineligibility or of a decision to consider a proposal is given pursuant to this paragraph 5, purchases under this arrangement will be resumed only after consultation has taken place between the Fund and Argentina and understandings have been reached regarding the circumstances in which such purchases can be resumed.

6. Purchases under this stand-by arrangement shall be made in the currencies of other members selected in accordance with the policies and procedures of the Fund, and may be made in SDRs if, on the request of Argentina, the Fund agrees to provide them at the time of the purchase.

7. The value date of a purchase under this stand-by arrangement involving borrowed resources will be normally either the 15th day or the last day of the month, or the next business day if the selected day is not a business day. Argentina will consult the Fund on the timing of purchases involving borrowed resources.

8. Argentina shall pay a charge for this stand-by arrangement in accordance with the decisions of the Fund.

9. (a) Argentina shall repurchase the outstanding amount of its currency that results from a purchase under this stand-by arrangement, in accordance with the provisions of the Articles of Agreement and decisions of the Fund, including those relating to repurchases as Argentina's balance of payments and reserve position improves.

(b) Any reductions in Argentina's currency held by the Fund shall reduce the amounts subject to repurchase under (a) above in accordance with the principles applied by the Fund for this purpose at the time of the reduction.

(c) The value date of a repurchase in respect of a purchase financed with borrowed resources under this stand-by arrangement will be normally either the 6th day or the 22nd day of the month, or the next business day if the selected day is not a business day, provided that the repurchase will be completed not later than seven years from the date of purchase.

10. During the period of the stand-by arrangement Argentina shall remain in close consultation with the Fund. These consultations may include correspondence and visits of officials of the Fund to Argentina or of representatives of Argentina to the Fund. Argentina shall provide the Fund, through reports at intervals or dates requested by the Fund, with such information as the Fund requests in connection with the progress of Argentina in achieving the objectives and policies set forth in the attached letter and annexed memoranda.

11. In accordance with paragraph 5 of the attached letter, Argentina will consult the Fund on the adoption of any measures that may be appropriate at the initiative of the Government or whenever the Managing Director requests consultation because any of the criteria in paragraph 4 above have not been observed or because he considers that consultation on the program is desirable. In addition, after the period of the stand-by arrangement and while Argentina has outstanding purchases in the upper credit tranches, the Government will consult with the Fund from time to time, at the initiative of the Government or at the request of the Managing Director, concerning Argentina's balance of payments policies.

Buenos Aires, Argentina
January 7, 1983

Mr. Jacques de Larosiere
Managing Director
International Monetary Fund
Washington, D.C. 20431
U.S.A.

Dear Mr. de Larosiere,

1. Annexed are (1) a Memorandum of the Government of the Republic of Argentina on Certain Aspects of its Economic Policy for the period through March 1984; and (2) a Memorandum of Understanding setting out certain operational guidelines for the conduct of this economic policy from January 1983 through April 1984. The memoranda describe the measures that Argentina already has taken and still has to take in order to correct economic imbalances and to ensure economic growth on solid and stable foundations.

2. In support of this 15-month program, we request herewith a stand-by arrangement with the International Monetary Fund in an amount of SDR 1,500 million, including access to the Fund's borrowed resources. We believe that our request for Argentina's maximum access to Fund resources permissible under existing policies is fully justified given the exceptional circumstances of our country and the pronounced deterioration in international capital market conditions which not only affect Argentina but the entire world. Moreover, believing as we do that the process of full economic recovery and restoration of financial stability will not be completed by the time the present Government leaves office, we would like to ensure that the authorities who will succeed it will have the opportunity to establish, if they desire, new financial relations between Argentina and the Fund. To this end the Government is prepared to arrange preliminary contacts prior to March 1984 between representatives of the Fund and the authorities in charge of the next government.

3. The Government of the Republic of Argentina intends to enter into discussions with the international financial community to secure a restructuring of its public and private external debt and attaches great importance to any assistance the Fund could lend in this exercise, as well as in efforts to obtain new external financing.

4. The annexed Memorandum of Understanding covers the principal economic targets and policy undertakings for the period of the requested arrangement. The Government of the Republic of Argentina understands that if, for any reason, any of these targets or policy undertakings are not observed in the period to the end of the arrangement, Argentina will not request any purchase under the arrangement that would raise the Fund's holdings of Argentina pesos beyond the first credit tranche

and 12.5 per cent of quota, until after reaching understandings with the Fund regarding the circumstances in which such purchases might be resumed.

5. The Government of the Republic of Argentina believes that the policies set out in the annexed Memorandum on Certain Aspects of its Economic Policy and further elaborated in the annexed Memorandum of Understanding are adequate to achieve the objectives of its program but will take any further measures that may become appropriate for this purpose. The Government will consult with the Fund in accordance with the Fund's policies on such consultations, about the progress made in the implementation of its program and any policy adaptations that may be appropriate for the attainment of its objectives. The first such consultation with the management of the Fund in May 1983 will include a review of trade and exchange policies.

Yours sincerely,

Julio Gonzalez del Solar
President of the Central Bank
of the Republic of Argentina

Jorge Wehbe
Minister of Economy

Annexed (2): Memorandum of the Government of the Republic of Argentina on Certain Aspects of its Economic Policy
Memorandum of Understanding

MEMORANDUM OF THE GOVERNMENT OF THE REPUBLIC OF ARGENTINA ON CERTAIN ASPECTS OF ITS ECONOMIC POLICY

I. Objectives and Strategies for Economic Recovery

1. The Argentine economy is in a severely depressed state and plagued with acute imbalances. The rate of inflation remains high and real wages have declined sharply. Real GDP growth, uneven during 1976-79, came to a halt in 1980 and was negative in 1981-82. Output now barely is at its level of six years ago, and real per capita income is at its lowest level in a decade. Unemployment approached 6 per cent in mid-1982 and underemployment has risen sharply.

2. The exchange rate policy pursued until March 31, 1981 led to an overvaluation of the peso and caused heavy external current payments imbalances which were financed by foreign borrowing on an increasing scale and on ever shorter terms. From that time on, attempts were made to correct these imbalances by an adjustment of the real exchange rate, which did reduce the deficit to some extent, but the lack of supporting domestic policies and waning confidence caused the overall balance of payments deficit to grow in the remainder of 1981. After a brief improvement in early 1982, the overall imbalances intensified during the second quarter of the year, when Argentina's access to international financial markets was interrupted, shipping routes were altered, and payments arrears began to accumulate. Argentina's external debt now exceeds US$36 billion, about one half of which falls due in 1983. The overall balance of payments deficit incurred in 1981 and 1982 combined is estimated at US$9 billion, which has reduced the disposable international reserves of the Central Bank to an extremely low level. Internally, wholesale prices rose by 180 per cent during 1981 and by about 310 per cent during 1982, reaching an annual rate of increase of 495 per cent in the second half of last year.

3. Notwithstanding heavy foreign borrowing, private and public investment stagnated during 1978-80 and dropped sharply in 1981-82 with the intensification of the economic recession. Gross fixed capital formation is estimated to have been only 17 per cent of GDP in 1982, compared with 25 per cent of GDP in the mid-1970s. Moreover, certain public investments in the last six years were in sectors yielding low, and in certain cases, negative rates of return.

4. The revival of the economy and the reduction of unemployment, therefore, have been the Government's priority economic objectives. The strategy has been divided into two stages: with the help of an emergency public works program, efforts were initially directed to reactivating activities that are heavily labor-intensive and make little use of imported inputs. Because of budget constraints, however, this program has been limited to the resumption of work on certain projects, the speeding up of others, and maintenance work. The second stage will involve increased capacity utilization (now at some 60 per cent on the average in

manufacturing), particularly in sectors that can generate quick and substantial increases in foreign exchange earnings. In pursuit of this objective, public investment will be directed primarily to the development of the energy sector, where prospects for achieving such increases are promising.

5. It will take more than a year to bring the economy back on a path of satisfactory and self-sustaining growth. With the plant and equipment now in place, an excellent fine grain crop this year and good prospects for the coarse grain harvest, it would be reasonable to expect an output growth of the order of 5 per cent in 1983. The attainment of higher growth rates beyond 1983 is certain to call for more capital formation in the public and private sectors which, in turn, will require concerted efforts to mobilize domestic savings. To this end, corrective measures are being taken to raise prices in the public sector to levels that cover costs and finance a reasonable part of investment. Also, adjustments have been made in the exchange and interest rates in order to encourage savings, improve resource allocation, and stimulate productive activity.

6. Present world economic conditions would not seem to favor a rapid recovery of the external sector. Nevertheless, the adoption of policies designed to stimulate both traditional and nontraditional exports is being given priority. The limited size of Argentina's domestic market prevents industries from taking full advantage of economies of scale; it is, therefore, necessary to move ahead with a steady and aggressive policy of export growth, the success of which will depend in good part on an improvement in international economic conditions and a reduction in protectionism, especially in the industrial countries. The Government intends to adopt policies that will encourage the development of an efficient, export-oriented industrial sector that will offer improved employment opportunities. Recent experience also demonstrates that Argentina's payments difficulties cannot be resolved by reliance on external borrowing alone--a course which in good measure has been the cause of these difficulties--but must be dealt with by increasing earnings from international trade in goods and services. This is the policy presently being followed by utilizing fully the existing productive capacity of exporters with traditional markets and by offering incentives to the development of new export lines and markets. The importance of maintaining steady trading relationships is being given due weight in the formulation of exchange rate and other policies affecting the export sector.

II. Economic Management

7. It is believed that energy development and conservation can contribute to output and employment growth and provide relief to the balance of payments. Argentina so far has been a small importer of oil and gas. Efforts now are being made to turn the country gradually into a net hydrocarbon exporter notwithstanding a likely rebound in domestic consumption as economic activity picks up. Until 1982, low domestic

retail prices were a major obstacle to higher production. Measures have been taken to remedy this situation and encourage conservation, primarily the adoption since November 1982 of a schedule of monthly adjustments in domestic fuel prices (including a special 20 per cent real increase between November 1982 and February 1983) which should result on average in a 7.9 per cent real price increase per month during the period through February 1983 and in one of 3.2 per cent per month in the period through March 1984. Should it prove necessary for fiscal or other reasons, consideration would be given to increasing fuel prices by another 10 per cent in real terms in the course of 1983. Moreover, negotiations have been resumed with firms under risk contracts to guarantee them remunerative ex-well prices and thus encourage new drillings and increased production. Prospects for an increase in natural gas production and exports are even more encouraging. Major discoveries since 1978 have raised estimates of commercially recoverable gas reserves to M^3 600 million. This level should be sufficient to allow for an important substitution of gas-fired for liquid fuel-fired thermal power generation, for the development of a local fertilizer industry--which in turn would help save foreign exchange and increase yields in agriculture--and possibly for exports to neighboring countries.

8. The determination of prices should in normal circumstances be left to market forces in order to prevent distortions in resource allocation. Circumstances in the second quarter of 1982 caused a delay in exchange rate adjustments, which unavoidably led to the imposition of trade and payments restrictions. In July, the exchange rate was adjusted and public tariffs were raised. This caused the authorities to adopt a system of price agreements, and eventually price controls, for the 725 leading industrial firms in order to avoid excesses in pricing on the part of those firms which enjoy dominant market positions. Adjustments are permitted only once a month, but the controls are administered with utmost flexibility, taking due account of cost movements and permitting efficient enterprises to achieve reasonable rates of return on their investment. It is the Government's intention to relax these price controls progressively as the stabilization program takes hold and inflation subsides. An increased availability of imports as external payments arrears are eliminated and trade restrictions are lifted will play an important role in this respect.

9. Argentina's situation from the second quarter of 1982 on called for a rapid and sizable reduction in the level of imports and, to effect this adjustment, quantitative restrictions on imports were imposed. Nonessential imports were banned in May, and in August import quotas restricting imports by firm and by type of merchandise to 70 per cent of the annualized U.S. dollar value of each category of imports during the period July 1981-April 1982 were established. Recognizing that this system produced distortions, acted as a break on economic recovery to the extent that it reduced the supply of imported inputs, raised domestic prices, and was no substitute for an enduring balance of payments adjustment, the Government in November dismantled this import quota system. The Government intends to liberalize the remaining

import restrictions when the availability of foreign exchange permits. The temporary suspension in September 1982, because of suspected over-invoicing, of imports from Paraguay and Uruguay included in the LAIA negotiated list was lifted in October-November 1982 after import applications were resubmitted, reviewed, and declared import values adjusted in cases of demonstrable excesses.

10. The authorities are of the conviction that a sharp deceleration of inflation is a precondition for an improvement in real labor remunerations. The economic program has been designed to slow domestic price increases to an annual rate of about 85 per cent in the first quarter of 1984. Attainment of this objective will require a drastic reduction of the growth of nominal demand in the economy. To ensure that the restraint in money demand growth will mainly affect the rate of price increase while allowing for a recovery of domestic output and employment, the Government will act with prudence in determining the frequency and size of wage adjustments.

11. Real wages fell precipitously in the first half of 1982 and in June reached one of their lowest levels in a decade. To prevent an excessive contraction in real per capita consumption, large pay hikes, either in the form of flat peso increases or of increases proportional to pay levels were granted from July 1982 on. These large nominal wage adjustments resulted in some recovery of real labor remuneration levels, particularly in the construction sector where real wages had contracted sharply owing to the severity of the recession in that sector, but was limited in other industries. It is recognized, however, that large nominal wage hikes can have but a very short-lived impact on real labor remunerations while they may trigger an uncontrollable wage-price spiral. More generally, the Government believes that it should abstain from intervening in the process of wage determination in the private sector, and that wage levels are best left to the decision of each enterprise in the light of its own economic conditions and of the labor market situation. In this regard, the Government would expect the anticipated revival of economic activity in 1983 to bring about an improvement in real labor remuneration of around 5 per cent on the average and would hope that this improvement will be reflected primarily in employment gains. Until free collective bargaining is reinstated with the next administration, the Government will continue (as required by law) to set minimum and basic conventional wages, even though these have been of little practical relevance in recent years, accounting as they did for only a minor portion of wages and salaries actually paid. Basic conventional wages had remained unchanged since October 1981 and, in November 1982, a long overdue adjustment was made. In proceeding with the adjustment of these implicit wage floors in the future, the authorities will be mindful of not raising them to the point where they would cause actual remunerations to move at a rate inconsistent with the intended deceleration of inflation and recovery of output and employment.

12. This said, it is recognized that the pattern for wage adjustments in the private sector will be set in large measure by the policy of remuneration pursued in the public sector. The wage bill of the general government dropped from more than 10 per cent of GDP in 1979 and in 1980 to below 7.5 per cent of GDP in 1982, reflecting in part the freeze imposed on public sector remunerations during the first half of the year and the adoption of flat pesos increases in the third quarter. To the extent permitted by the need to compress sharply the borrowing requirements of the public sector, current budget plans for 1983 imply a real increase in the remunerations of public employees of 5 per cent. In addition, in order to retain qualified medium- and high-level civil servants their salary scale will be partially restructured so as to correct the distortions in salary levels introduced by the flat peso increases of July-September 1982. Such selective increases will be quarterly commencing on April 1, will be kept during 1983 to one half of the full contemplated restructuring and will be subject to the availability of budgetary resources consistent with the fiscal program. The restructuring process will be completed in 1984. Altogether, the government wage bill would be held to no more than 7.5 per cent of GDP, a level significantly below that recorded in 1980 and 1981. Although wage developments in the public enterprises in principle follow the pattern of those in the private sector, the Government will monitor carefully the behavior of remunerations in the state enterprises and bring appropriate pressure to bear on these enterprises to ensure that the remunerations they pay remain in line with those for government employees.

13. There has been a marked deterioration in the public finances since 1977, particularly in the last two years. Public sector expenditure rose to about 40 per cent of GDP, to a large extent because of mounting interest payments on the internal and external debt and notwithstanding a drop in capital spending. Meanwhile, government revenues declined, affected as they were by rapidly changing economic conditions, modifications in the tax system and widespread tax evasion. Savings of the public sector fell sharply, from a high of 10-1/2 per cent of GDP in 1977 to around minus 3-1/2 per cent of GDP in 1981 and to minus 5 per cent of GDP in 1982. The overall borrowing requirements of the public sector, which in 1977 had been compressed to 4-1/2 per cent of GDP, widened steadily thereafter to a high of 14-1/3 per cent of GDP in both 1981 and 1982. Consequently, the public sector not only preempted a growing share of domestic financial savings, but also borrowed heavily abroad.

14. The Government is committed to prudent financial management and thereby to strengthening the confidence of the private sector, where expectations are markedly influenced not only by the size of the public sector deficit but also by the magnitude and composition of public spending. There also is a need for relieving pressures on the domestic financial market in order to free savings for the revival of output in the private sector.

15. Accordingly, the net borrowing requirements of the public sector will be kept to 8 per cent of GDP in 1983 and to 5 per cent of GDP in the first quarter of 1984. In order to raise public investment somewhat from its depressed level in 1982, the bulk of the improvement in public finances will have to come from a turnaround in public sector savings from sharply negative levels in 1981 and 1982 to over 1 per cent of GDP in 1983. To achieve this objective, government revenue will be raised by 2 percentage points to over 23-1/2 per cent of GDP, largely on account of the increase in fuel taxes. At the same time, current government spending will be held to 21-1/3 per cent of GDP, or 2 percentage points less than in 1982. The operating costs of public enterprises will be kept under close watch, and tariffs will be increased substantially. With effect from October 20, 1982, a schedule of monthly adjustments in public sector tariffs was established, a schedule that aims at a weighted average increase of 2.8 per cent a month (excluding the special 20 per cent real fuel tax increase of November 1982-February 1983) over and above the increase in the wholesale price index. Altogether, the objective is to seek an improvement in the savings rate of public enterprises of the order of 1-1/3 per cent of GDP in 1983.

16. The Government intends to strengthen the tax base. Following the exchange rate adjustments in July 1982, taxes on nonpromoted exports were raised as an emergency measure from a range of 0-10 per cent to one of 10-25 per cent. The potential effects of this decision on the farm sector were considered carefully and the conclusion was reached that its drawbacks would be more than outweighed by its fiscal benefits and its moderating influence on the domestic prices of tradeable goods. Moreover, the 1981/82 coarse grain crop had been harvested and the 1982/83 fine grain crop already had been planted. Altogether, it is estimated that this tax represented about 1.2 per cent of GDP in 1982 and that it would rise to 1.9 per cent of GDP in 1983. The Government recognizes, however, that this system of export taxes, combined with a system of automatic tax rebates for promoted exports, produces major distortions in resource allocation, and hence hampers the development of an efficient and dynamic export sector. It is intended, therefore, to simplify over time this system of export taxes and rebates. As a first step in that direction, the system of special rebates for exports to new markets is to be eliminated in February 1983, although rebates already approved under this system will be allowed to continue until their pre-established expiration dates.

17. Other tax revenues performed well in the second half of 1982. Value-added tax (VAT) collections increased strongly as nominal GDP growth accelerated and sales in the third quarter of the year surged. VAT rates for foodstuffs and medicines were lowered from 12 per cent to 8 per cent in September, compared with a 20 per cent standard rate for all other goods, to help mitigate the impact of inflation on low income groups. But the expectation is that the revenue thus foregone

will be partly, if not wholly, offset by the gradual recovery of production, imports, and sales and by a systematic effort at reducing tax evasion, now estimated at around 50 per cent in the case of the VAT alone. A growth of other government revenue is expected from the adoption of a tax moratorium and the impact of the ongoing adjustments in the domestic prices of petroleum derivatives and electricity.

18. The Government will observe austerity in its consumption spending through tight control over the growth of its wage bill and by keeping the increase in its outlays on goods and services below that in domestic prices. Although no dismissal from government employment can be envisaged in current economic circumstances, no more than one half of the positions vacated by attrition will be filled. With such prudent management of current spending and the anticipated increase in revenue, government savings should rise from minus 1.8 per cent of GDP in 1982 to 2-1/2 per cent of GDP in 1983.

19. Given the transitory nature of this Government, it would seem inappropriate to introduce major modifications in the size and overall priorities of the public investment program. Nonetheless, concern for economic reactivation dictates that in 1983 real public investment spending be raised by around 1 per cent of GDP from its level of 8.5 per cent of GDP in 1982, and care has been taken in the 1983 budget to concentrate such spending on labor-intensive projects with a large income multiplier effect. Projects with low economic returns and those of no immediate priority have been cancelled or postponed, except when breach of contracts involved higher costs than continuing with the project.

20. The financial system was substantially modified in July 1982 with the objective of alleviating the heavy domestic and foreign debt burden of enterprises resulting from large-scale borrowing during 1978-80. With these modifications, the real value of the private sector's debt to the financial system was reduced by 40 per cent from July through October. But the cost of this operation was high as the low level of real interest rates caused real domestic financial savings to fall sharply. Monetary policy therefore is being directed toward the reconstitution of real financial savings and the efficient allocation of financial resources.

21. A number of measures in this direction were taken in the latter part of 1982 as the interest rate structure established in July 1982 was gradually made more flexible. The maximum monthly interest rates payable on regulated deposits of 30 days were increased in steps from an initial level of 5 per cent per month in July to 7 per cent in September and to 8-1/2 per cent in November, and the rates on regulated deposits at longer terms were raised correspondingly. The rate of interest on the subsidized basic and additional loans was raised from the original 6 per cent a month in July to 8 per cent a month in September. That lending rate was raised further to 9 per cent a month in November, and new access to these loans was suspended from November 1, 1982. Also, regulations were issued in November 1982 to prevent maturing exchange guarantees granted during June-December 1981 from causing an undue Central Bank credit expansion and a loss of foreign exchange reserves.

22. With effect from January 1, 1983, the monetary authorities have adopted a policy whereby the key regulated deposit rates and the lending rate for loans financed from regulated deposits will be set at the beginning of each month on the basis of a three-month moving average of the wholesale price index--the observed increase in that index during the two preceding months and the projected increase for the current month. The lending rate will be set at least equal to that three-month moving average; the 30-day deposit rate will be set within 1 percentage point below that average and the rates on deposits of more than 30 days will be set in line with the 30-day rate. Recognizing that this formula is based on partially estimated data for the preceding month and projected data for the current month, the authorities are prepared during the course of each month to adjust minimum reserve requirements or to conduct their open market operations in such a way as to produce an interest rate on Central Bank absorption bills which will compensate for any significant underestimation of the current inflation rate resulting from the formula.

23. More generally, the authorities view the ultimate test of the appropriateness of interest rate policy to be the degree of success in achieving the balance of payments objectives and the targeted real increase in the financial assets of the private sector; they are prepared to adapt the formula for setting regulated deposit and lending rates to the extent that is necessary to meet these goals. In the short run, the results of the regular bill auctions and the movements in the rates on unregulated deposits will be used as indicators of the appropriateness of that formula, and regulated rates will be set above the levels indicated by the price formula if this appears necessary.

24. A major obstacle to economic recovery since the second quarter of 1982 has been the foreign exchange shortage. Two major reasons for this shortage were adverse movements in the leads and lags of import payments and surrender of export receipts and the drying up of external sources of finance at a time of heavy external debt service payments. From July 1982, another reason has been the emergence of a large differential between the commercial exchange rate applicable to merchandise transactions, the financial rate applicable to all other authorized transactions, and the rate in the parallel market which emerged as exchange restrictions were tightened. As a consequence, under- and over-invoicing became widespread, unrecorded border transactions increased, exporters withheld shipments, and a large portion of service receipts evaded official channels.

25. To avoid the continuation of these distortions in trade and payments flows the Government is determined to restore order in the foreign exchange market. While continuing with the daily depreciation of the commercial rate initiated in July 1982, the unification between the financial and commercial exchange rates was accelerated in September and October by introducing, and subsequently increasing, the mix of the two rates for trade transactions. The exchange markets subsequently were unified on November 1, 1982, for a 13-1/2 per cent peso depreciation for

trade related transactions, and since then the exchange rate has been adjusted about in line with the rate of domestic inflation. This policy will be applied with sufficient flexibility to meet the overall balance of payments objectives.

26. A parallel market will remain in existence so long as complete freedom of exchange transactions has not been restored. Moreover, the benefits in terms of resource allocation of a unified exchange rate are at least partly foregone by such payments restrictions as presently exist. Despite the drawbacks of exchange restrictions, the freeing of the capital account of the balance of payments has to be ruled out in Argentina's present circumstances, but it is the intention of the Government to phase out gradually restrictions on payments and transfers on current account. To this effect a program of gradual liberalization has been drawn up, which calls for a return to complete freedom for current payments by December 31, 1983, except possibly for limits on certain invisible payments to prevent disguised capital outflows. The 180-day minimum import financing requirement also will be reduced in steps and eventually eliminated.

27. Beginning in the second quarter of 1982 Argentina incurred large external payments arrears, of which US$2.5 billion remained outstanding at the end of December. The authorities are giving the highest priority to the total elimination of these arrears, in their determination to restore the normal flow of imports and Argentina's international creditworthiness.

28. The authorities have asked foreign banks to restructure Argentina's debt maturities. As already indicated, principal payments equivalent to about one half of the external debt of US$36 billion at the end of 1982 fall due in 1983. This debt amortization schedule obviously is unrealistic for a country with Argentina's level of income and export earnings. The Government trusts that the private international banking community will recognize this fact and respond positively to Argentina's request for debt relief. Should foreign banks be prepared to go further and resume lending to Argentina, the Government will observe prudent limits on its total external borrowing, especially in the shorter maturity ranges.

Government of the Republic of Argentina
January 7, 1983

Buenos Aires, Argentina
January 7, 1983

MEMORANDUM OF UNDERSTANDING

1. This Memorandum describes more concretely the key targets and policy undertakings of the accompanying Memorandum of the Government of the Republic of Argentina on Certain Aspects of its Economic Policy.

2. The overall balance of payments target for 1983 and for the 15-month period through the first quarter of 1984 is a deficit of no more than US$500 million. The intermediate targets are a deficit of no more than US$400 million for the three-month period through March 31, 1983; a deficit of no more than US$220 million for the six-month period through June 30, 1983; and a surplus of at least US$20 million for the nine-month period through September 30, 1983. For the purpose of these targets, the balance of payments performance will be measured by changes in the net international reserve position of the Central Bank of the Republic of Argentina. The Central Bank's net international reserve position will be defined as the difference between (a) the sum of its holdings of gold, SDRs, reserve position in the IMF, and all claims on nonresidents except discounted export letters of credit and credit lines granted to nonresidents; and (b) the sum of any outstanding external payments arrears and all other obligations to nonresidents, regardless of their currency denomination, any outstanding foreign currency swaps with residents, any loans obtained by public sector entities the foreign currency proceeds of which were surrendered to the Central Bank without the borrowing entity receiving the peso counterpart, any other balance of payments support loans, the cumulative net issue of external bonds (BONEX) against pesos for settlement by the private sector of outstanding external obligations (but excluding external bonds issued in settlement of foreign loans carrying an exchange rate guarantee by the Central Bank) and any debt to the IMF and the BIS. For the purpose of this definition, all foreign assets and liabilities will be expressed in U.S. dollars. All foreign assets and liabilities in other foreign currencies will be converted into U.S. dollars at the market rates of the respective currencies; gold will be valued at a fixed accounting rate of US$42 per fine troy ounce; and the Central Bank's SDR holdings and Argentina's IMF position, be the latter positive or negative, will be valued in SDRs converted into U.S. dollars at the basket valuation of the Special Drawing Right. The Central Bank's net international reserve position as of September 30, 1982, so defined, is shown in attached Table 1. However, for purposes of measuring balance of payments performance, the change in the net international reserve position will be adjusted for changes in the U.S. dollar value of assets and liabilities denominated in other foreign currencies. An adjustment factor will be calculated weekly as the difference between (a) the U.S. dollar value of such assets and liabilities as of the day before the end of each statistical week valued at market rates on that day and (b) that same stock of assets and liabilities valued at the market

rates on the day before the end of the preceding statistical week. The cumulative value of these weekly adjustment factors will be subtracted from the change in net international reserves of the Central Bank as measured at current market rates.

3. The cumulative global borrowing needs of the nonfinancial public sector will not exceed \$a 105 trillion from January 1, 1983 until March 31, 1983; \$a 218 trillion until June 30, 1983; \$a 326 trillion until September 30, 1983; \$a 445 trillion until December 31, 1983; and \$a 559 trillion until March 31, 1984. These borrowing needs will be defined as the sum of the net increase above their respective stocks on December 31, 1982 in (a) the external debt of the nonfinancial public sector, including short-term debt, foreign currency denominated Treasury bills and bonds (BONEX) (excluding BONEX issued against pesos) converted into U.S. dollars if denominated in another foreign currency (and properly adjusted for exchange rate movements) and all U.S. dollar values converted into pesos at the average exchange rate of the U.S. dollar during the calendar quarter of the transaction; (b) external bonds in foreign currency issued against pesos in settlement of foreign obligations carrying an exchange rate guarantee by the Central Bank, valued in pesos at the amount actually received by the Treasury on the date of each such transaction; (c) the net debt (credit minus deposits) of the nonfinancial public sector to the Central Bank of the Republic of Argentina (including external bonds issued against pesos other than those referred to in (b) above) and the rest of the domestic financial system, excluding any valuation adjustments for alterations in the external value of the Argentine peso in the pertinent foreign currency denominated accounts; and (d) net placement of Treasury bills and bonds with the nonfinancial private sector. For the purpose of these cumulative limits, the nonfinancial public sector will be defined as the Treasury, the Special Accounts, the decentralized agencies, the Social Security System, the provinces, the Municipality of Buenos Aires, and the public enterprises listed in attached Table 2.

4. The net domestic assets of the Central Bank of the Republic of Argentina will at no time during the first quarter of 1983 increase by more than the increase (or decrease by less than the decrease) in its banknote issue above (below) its base stock on December 31, 1982, plus \$a 9.7 trillion, but in no event by more than 40 per cent of the base stock, plus \$a 9.7 trillion; at no time during the second quarter of 1983 increase by more than the increase (or decrease by less than the decrease) in its banknote issue above (below) its base stock, plus \$a 15.0 trillion, but in no event by more than 80 per cent of the base stock, plus \$a 15.0 trillion; at no time during the third quarter of 1983 increase by more than the increase (or decrease by less than the decrease) in its banknote issue above (below) its base stock, plus \$a 4.9 trillion, but in no event by more than 130 per cent of the base stock, plus \$a 4.9 trillion; at no time during the last quarter of 1983 increase by more than the increase (or decrease by less than the decrease) in its banknote issue above (below) its base stock, plus \$a 11.7 trillion; but in no event by more than 170 per cent of the

base stock, plus $a 11.7 trillion; and at no time during the first quarter of 1984 increase by more than the increase (or decrease by less than the decrease) in its banknote issue above (below) its base stock, plus $a 24.3 trillion, but in no event by more than 220 per cent of the base stock, plus $a 24.3 trillion. For the purpose of this ceiling, the net domestic assets of the Central Bank will be defined as the difference between (a) its banknote issue and (b) its net international reserve position, defined as in paragraph 2 above, with the U.S. dollar value converted at all times into Argentine pesos at the Central Bank's accounting rate on December 31, 1982.

5. The outstanding disbursed external debt of the public sector will at no time during the period of the arrangement exceed by more than US$2 billion the stock of such debt outstanding on December 31, 1982. Furthermore, the total maturities falling due within three years of the end of each calendar quarter, based on the stock of debt outstanding as of the end of that calendar quarter, will not exceed the total maturities falling due within three years of December 31, 1982, based on the stock of debt outstanding as of that date, by more than US$600 million on March 31, 1983, by more than US$1.2 billion on June 30, 1983, by more than US$1.8 billion on September 30, 1983, by more than US$2.4 billion on December 31, 1983, and by more than US$3 billion on March 31, 1984. These limits on maturities falling due within three years of the end of each calendar quarter will be subject to a downward adjustment (even, if appropriate, to negative values) for (a) any net debt relief on maturities falling due within these periods obtained through multicreditor agreements involving a formal refinancing or rescheduling of the external debt of the public sector, and for (b) any increase in arrears on principal payments on public sector debt over and above the amount of such arrears outstanding on December 31, 1982. For purpose of these limits, the external debt of the public sector will be defined as all external obligations of the total public sector, including the official banks (the domestic offices of Banco de la Nacion, the National Development Bank, the Mortgage Bank, the National Postal Savings Bank, and the provincial and municipal banks), but excluding any increase in the stock of Argentine government bonds denominated in foreign currency but issued against pesos; any increase in the external obligations of the public sector treated as international reserve liabilities of the Central Bank as per paragraph 2 above; and any increase in the external debt of the public sector as the result of default by the private sector on a publicly guaranteed debt. External debt in currencies other than the U.S. dollar will be converted into U.S. dollars at the exchange rates prevailing on December 31, 1982.

6. During 1983 and through April 1984, the Government will not impose any new or intensify any existing restriction on payments and transfers for current international transactions, conclude any bilateral payments agreement inconsistent with Article VIII of the Articles of Agreement, or impose any new or intensify any existing import restriction for balance of payments reasons. During the second quarter of 1983 the Government will undertake, in consultation with the Fund, a

comprehensive review of the Argentine exchange and trade system and reach understandings with the Fund on a schedule for the elimination of existing multiple currency practices and restrictions on payments and transfers for current international transactions and of the consequent distortions. The Government will terminate the system of special rebates for exports to new markets by February 28, 1983, although rebates authorized before that date will continue in effect until their pre-established expiration dates. The Government will reduce the minimum foreign financing requirement for private imports, now at 180 days, to no more than 150 days by March 31, 1983, to no more than 120 days by June 30, 1983, and to no more than 90 days by September 30, 1983, and it will eliminate this requirement entirely by December 31, 1983.

7. During 1983 and through April 1984, the Government will not introduce or modify any multiple currency practice with the following exceptions: (a) any modification in a multiple currency practice which reduces the differential between the effective exchange rate applied for a given transaction and the official buying or selling rate for the peso in the unified exchange market; and (b) pending the completion of the review mentioned in paragraph 6 above, the continued operation of the existing system of export rebates within the existing range of rates, including the reclassification of exports within that range of rates.

8. All external payments arrears will be eliminated as quickly as possible and, in any event, by June 30, 1983. Once eliminated, foreign exchange will be provided freely at the official exchange rate for all bona fide current international payments. However, reasonable limits may be applied on the automatic allocation of foreign exchange for foreign travel and remittances in order to prevent disguised capital outflows.

9. The Government intends to initiate shortly discussions with its foreign creditors with a view to achieving a restructuring of Argentina's external public and private debt that would produce an amortization profile attuned to Argentina's repayment capacity.

Sincerely yours,

Julio Gonzalez del Solar
President of the Central Bank
of the Republic of Argentina

Jorge Wehbe
Minister of Economy

Table 1. Argentina: Net International Reserves as of September 30, 1982

(In millions of U.S. dollars)

Assets	3,304
Gold 1/	185
Foreign exchange	421
ALADI	140
Investment realizable in foreign exchange	2,310
SDRs	--
IMF reserve position	248
Liabilities	5,005
ALADI	62
Liabilities to IMF	--
Arrears	1,709
Swaps	1,156
BONEX against pesos 2/	1,464
Reserve loans from residents 3/	141
Other external obligations of the Central Bank in foreign currencies	473
Net international reserves	-1,701

1/ Valued at US$42 per fine troy ounce.
2/ Excludes external bonds issued against pesos in settlement of exchange guarantees issued by the Central Bank.
3/ External obligations of residents, the foreign currency proceeds of which were surrendered to the Central Bank without the borrowing entity receiving the counterpart in peso financing.

Table 2. Argentina: Selected List of Public Enterprises

Y.P.F.	Yacimientos Petroliferos Fiscales
Y.C.F.	Yacimientos Carboniferos Fiscales
Gas del Estado	
AyE.E.	Agua y Energia Electrica
SEGBA	Servicios Electricos de Gran Buenos Aires
HIDRONOR	
F.A.	Ferrocarriles Argentinos
A.A.	Aerolineas Argentinas
ENTel	Empresa Nacional de Telecomunicaciones
ENCOTel	Empresa Nacional de Correos y Telegrafos
A.T.C.	Argentina Television Color
ELMA	Empresa de Lineas Maritimas Argentinas
A.G.P.	Administracion General de Puertos
YACYRETA	
Salto Grande	
COMIP	Comision Mixta Argentina Paraguaya
AFNE	Astilleros y Fabricas Navales del Estado
P.B.B.	Petroquimica Bahia Blanca
O.S.N.	Obras Sanitarias de la Nacion
YMAD	Yacimientos Mineros Aguas de Dionisio