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TRADE POLICY OF ARGENTINA BETWEEN 2003 AND 2012 IN THE LIGHT OF INSTITUTIONAL ECONOMICS

A Ph.D. thesis in the field of economic sciences and in the discipline of economics, written under the supervision of Artur Nowak-Far

ABSTRACT:

Central thesis

Since 2003 Argentina has been one of the most protectionist economies in the world, as evidenced – among others – by WTO data, European Commission reports as well as the Global Trade Alert reports¹. Under the rule of Cristina Fernández de Kirchner (2007 - 2015) the country became notorious for its massive use of non-tariff import barriers. However, first signs of this phenomenon became apparent already during the presidency of her predecessor and husband, Nestor Kirchner (2003 - 2007). The starting point for this study is the question about sources of this surge in protectionism.

According to the central thesis of the study, an increase in Argentina’s protectionist tendencies between 2003 and 2012 was a side effect of the economic policies implemented opportunistically by the government within the context of weak state institutions. This thesis puts an equal emphasis on three issues: the existence of logical connections between trade policy and other elements of economic policy implemented by the government; the government’s opportunism reflected in its readiness to subordinate economic policy to private political agenda; and the weakness of state institutions considered as a precondition for such an opportunistic behaviour to become translated into a particular shape of public policies.

Three hypotheses were employed to verify the central thesis mentioned above and they correspond to three main chapters of the study. First, it was argued that trade barriers constituted a logical consequence and an integral part of the economic policy model implemented by Nestor Kirchner and Cristina Fernández de Kirchner. In order to explain that statement, a distinction was introduced between chronological and organic logic of protectionism. The "stop and go" model was also invoked in order to analyse the limits within which economic processes during the Kirchner's decade corresponded to this pattern, typically invoked to explain Argentina's economic and political dynamics\(^2\).

Secondly, it was argued that the economic policies of the Kirchners (including trade policy) were subordinated to their particularistic political interests which consisted, most of all, in staying in power for the longest possible period. This political mechanism was dismantled thanks to the use of the concepts of "opportunism" and "populism". Apart from that, an idea of "protectionist temptation" was introduced.

Thirdly, it was argued that the subordination of trade policy to particularistic interests of the government during the presidencies of Nestor Kirchner and Cristina Fernández de Kirchner was possible due to the weak state institutions. Argentina of the last decade was compared with other Latin American countries and other periods in the national history in terms of "institutional weakness". The concept of "privatisation of trade policy" was also introduced.

**Research question**

The introduction of trade barriers in Argentina, mainly during the government of Cristina Fernández de Kirchner, started already during the presidency of her predecessor. In 2004, Nestor Kirchner re-established the regime of non-automatic import licences, which had been eliminated in the 1990's by president Carlos Menem.

However, while before 2008 the use of these licences was restrained to just a couple of sectors, immediately after the outbreak of the global crisis Cristina Fernández de Kirchner's new government significantly intensified their use. In 2012 this led over 40 WTO members

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(including the US, the EU and Japan) to initiate a dispute settlement case against Argentina concerning its import restrictions and the way they were administered.

Given that non-automatic licenses brought about rising controversies, the government of Cristina Fernández de Kirchner decided to restrict their employment. Instead, pursuant to the Resolution 3252/2012 of the Argentinian tax agency (AFIP), it introduced a formal demand for importers to present a notarised declaration of any planned imports (the so-called affidavit for imports). This system was much easier to coordinate than the previous one, since it concerned all tariff lines and all of the country's trade partners. However, it also led to rising complaints on the part of Argentinian and foreign businesses who protested against the lack of transparency and a large dose of discretion in the use of this instrument by the tax agency and government officials. The system hampered industrial production which increasingly depended on foreign inputs. It was reported that some of the biggest producers were able to bypass this restriction thanks to their close relationship with Guillermo Moreno, State Secretary for Internal Trade. In turn, small and medium size companies did not have comparable influence. They were obliged to “stand in line” and wait for the opportunity to discuss their import needs with one of the administration officials. Companies usually submitted several import applications at once, in a belief that one of them would eventually be accepted. All of this translated into a peculiar red-tape bubble. Departments of foreign trade in companies operating in Argentina experienced a sudden growth, but mainly to deal with the rising paperwork.

The system of affidavits for imports has been complemented with further trade barriers, such as restrictions at the currency market (since 2012) and the introduction of an informal requirement to balance any import with an equivalent of exports, within the system called uno por uno (since 2013). Therefore, for particular sectors, it was no longer enough to acquire an import permit based on a notarised declaration. Entrepreneurs also needed to demonstrate that these imports were balanced with exports of the same value. This led to the creation of an informal market of import permits. Importing companies frequently chose to enter into deals with the country’s major exporters in order to exchange their export pools for importing rights. This generated further paperwork and higher operating costs, translating into a decline in international competitiveness of Argentinian products and higher costs for customers in the country. In turn, these processes contributed to a progressive decline in investments, production and exports, and the weakening of the country's trade balance.
Approach and methodology

The analysis of Argentinian protectionism presented in this study is based on tools and concepts typical for Institutional Economics\(^3\). Such an approach enabled the posing of questions about the deep roots of the analysed phenomenon. Mainstream economic theories usually consider the use of trade barriers as an inefficient policy solution\(^4\). Therefore, it is difficult to explain their practical use from the perspective of the classical or neoclassical approach. Meanwhile, a protectionist trade policy does not constitute an anomaly in the praxis of international trade – as evidenced inter alia by agricultural protectionism of the US, the EU or Japan, as well as the rising employment of trade barriers by non-Western powers. Nevertheless, even against this background, Argentina stands out as a particularly protectionist country, thus constituting a puzzle not only for economic theory, but also for the practice of international trade.

There is no one and only institutional explanation of Argentinian protectionism. Depending on the approach and perspective within the scope of Institutional Economics, different questions concerning this phenomenon may be asked and various answers to the same questions may be formulated. This is why it needs to be clarified what particular kind of an institutional approach has been employed in this study. First, it corresponds to the Original Institutional Economics – as opposed to the New Institutional Economics – which allows for multiple interrelated explanatory variables and considers the economic system as deeply embedded in the political system and vice versa. Secondly, it is a dynamic approach – as opposed to the static one – because the central research question ("Why did we see a surge in protectionist tendencies in Argentina after 2003?") refers to a sudden change in the character of the country’s trade policy. Thirdly, the study is based on the vested interests perspective – as opposed to the effectiveness-oriented one. This means that from the outset it was assumed that the key motivation behind the activity of "actors" responsible for the formulation and implementation of trade policy was to defend their particularistic interest and not necessarily to maximise the effectiveness of governance.

The study is relevant both for the question posed and for the economic theory as such. In other words, the effect of the research is not only a well-founded explanation of

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Argentina's protectionism, but also a case study in the use of tools of Institutional Economics for the analysis of protectionism in general. This is all the more important since explanations of this phenomenon have usually been confined to other, narrower approaches – such as the Economic Geography, the International Political Economy, the Economic Sociology or the Political Economy.

Apart from tools and concepts typical for the Institutional Economics, the study was based on the use of a very specific strategy of qualitative research – that is the Grounded Theory\(^5\). This means that the aim of the study was not to verify an *ex ante* deduced hypothesis which would reduce the dependent variable (in this case: Argentina's protectionism) to a possibly limited number of explanatory variables. Instead, the objective of the study was to build an exhaustive explanation of the problem in question, as a result of several iterations of data collection, hypotheses building and their verification. The aim was not to measure the exact magnitude of the phenomenon but to provide an empirically grounded proof of the existence of interrelations between key related concepts.

The choice of the Grounded Theory as the methodological base for the study translated also into the selection of methods which were applied over the course of the research. The study was prepared based on a series of in-depth interviews, the analysis of source documents and participating observation. The majority of elements of the research were carried out during a study visit in the capital of Argentina, Buenos Aires, in August and September of 2013. Draft hypotheses were formulated before that visit but later on they underwent several mutations in the course of data collection, participating observation and the testing of assumed interrelations between variables.

*The logic of protectionism*

In the first hypothesis of the study it was argued that trade barriers introduced by governments of Nestor Kirchner and Cristina Fernández de Kirchner constituted a logical consequence and an integral part of their economic policy model. However, it must be

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stressed that this was not an inevitable consequence but rather a conditional one. This is why the idea of a "side effect" was mentioned in the central thesis of the study.

Trade barriers under the Kirchners, particularly those employed since 2011, have played an increasingly important role as an instrument subordinated to the management of the current account balance within the context of Argentina's falling trade surplus and its continuously restricted access to international capital markets after the country's 2001 bankruptcy. Still, trade barriers were in this context neither imperative nor inevitable. The government could just as well decide to opt for a currency devaluation or for the rise in energy prices combined with efforts to boost energy efficiency and to limit its consumption (rising energy imports were the most important reason behind falling trade surplus).

Nevertheless, out of potential solutions at its disposal, the government opted for the rationing of foreign trade. Therefore, the use of protectionism had many characteristics of an "unintended consequence" or of a "path-dependent" behaviour. Most of all, subsequent decisions of the government demonstrated that, from its point of view, the costs of changing the decision were considered higher than the costs of continuing the course. A series of controversial decisions – such as the taking of political control over the country's Central Bank, increased recourse to debt monetisation (that is the use of money emission to cover the budgetary debt), the use of currency reserves to pay for foreign debt, and last but not least the introduction of currency restrictions and non-tariff trade barriers – were all meant to make up for the government's previous economic wrongdoings. It became "locked in" in its initial economic choices. Only at the turn of 2013 and 2014 did it start to tentatively revise its economic policy, as it was already clear that Cristina Fernández de Kirchner would not be able to run for the third term in 2015, while at the same time the rise in public discontent due to growing inflation seemed to create a serious political risk of her being unable to finish even her second term.

Still, an explanation in terms of a logical sequence of economic events constitutes only one side of the equation. At the same time, ideological and political factors led the government to opt for protectionism out of the available set of policy instruments which could be employed to hamper the fall in foreign reserves. Ever since the Kirchners took over the power, protectionism was hanging in the air as a prospective element of their economic

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policy. This is because their governments were always close to the "interventionist" ideal type of Latin American economic policy, as opposed to the (neo)liberal ideal type, especially in the rhetoric. Therefore, protectionism fitted very well other elements of their model, such as the tendency to expand public spending, to nationalise the country's industry or to interfere with the Central Bank's formal independence.

Already in his 2003 electoral campaign, Nestor Kirchner promised such an exchange rate that would boost exports while at the same time enabling the needed substitution of imports. However, favourable market conditions between 2003 and 2007 as well as the natural protection provided by a devalued peso made the use of more explicit trade barriers unnecessary over the most part of the Nestor Kirchner's presidency. In turn, protectionist tendencies of the Kirchners became manifest once the natural protection provided by a devalued peso run out, while at the same time the international economic context deteriorated due to the 2008 global crisis and, last but not least, the government had to face negative consequences of its earlier political choices which translated into falling currency reserves and a growing risk of the country becoming unable to finance its balance of payments. In this context, trade barriers became a logical solution – not because the imbalances in question could not be eliminated with the help of other policy instruments, but because protectionism had already been implicitly present in the government's model of economic policy.

The temptation of protectionism

In the second hypothesis of the study it was argued that the economic policies of the Kirchners (including their trade policy) were subordinated to their particularistic political interests, consisting most of all in staying in power for the longest possible period. In this sense, protectionism was in many respects politically advantageous for the government, at least on the short term.

Thanks to the use of trade barriers, the government intensified its control over the economic and political sphere in the country. It strengthened its position vis a vis key players in the national economy. It generated economic rents that could subsequently be exploited by its supporters. At the same time, it took advantage of a widespread political support for an active role of the state in the national economy; a sentiment that was an aftermath of Argentina's 2001 bankruptcy and its earlier several-decades-long experiences with import
substitution industrialisation. On top of that, political benefits of protectionism coincided with the particularistic political agenda of the Kirchners. It is widely known and accepted that they planned to remain in power as long as possible, replacing one another at the position of the president of the country. This led to a very specific way of managing the national economy. Before every election, the government significantly increased public spending; it was also reluctant to unfreeze prices of electricity and transport. All of this, since 2007, translated into the rise of inflation over 10%. At the same time, in order to retain the political support among economic and social circles, the government had to create new rent-seeking opportunities.

Interestingly, the national and the global context provided the government with an opportunity to opt for protectionism without the need to incur political costs of such a decision. These elements of the context included not only a widespread disillusion with neoliberalism across the Argentinian society, but also rising prices of commodities at the global markets. Meanwhile, among Argentinians there has been a widespread – even if nowadays much less justified than a few decades ago – belief that high prices of commodities favour the local land-owning elite, thus demanding a compensatory action on the part of the government. This normally opens a room for protectionism and for some sorts of political populism.

**Protectionism and institutional weakness**

In the third hypothesis of the study it was argued that the subordination of trade policy to particularistic interests of the government was possible during the presidencies of Nestor Kirchner and Cristina Fernández de Kirchner due to the existence of weak state institutions. The research demonstrated that this was a key factor enabling an opportunistic behaviour on the part of the government which took the form, among others, of increased protectionism. This does not mean that there should exist a causal link between the weakness of state institutions and protectionism. Still, institutional weakness creates room for the subordination of trade policy to narrow political considerations of the executive power. Interestingly,

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depending on the national and international context, the government may seek the accomplishment of its particularistic interests either through a protectionist trade policy, or by way of trade liberalisation (as happened during the presidency of Carlos Menem in Argentina of the 1990’s).

Although the period of democratic transition in Argentina started already over three decades ago, the institutional system of the country continues to exhibit a number of severe inefficiencies. This is manifested *inter alia* by frequent takeovers of the Parliament’s competences in the area of trade policy by the executive branch⁹; or (in a wider sense) by presidents repeatedly stepping down before the end of their terms¹⁰.

According to Pablo Spiller and Mariano Tomassi, “public policy in Argentina has a dual characteristic: over some issues it exhibits excess volatility, while over other issues it is too rigid. In general it lacks credibility and coherence. (...) [There exist] some key features of the institutional environment that do not promote inter-temporal political agreements: a legislature uninterested in legislative activities, a bureaucracy with no long-term objectives, a judiciary that has often been aligned with the executive, a federal system that grants provinces little incentives for fiscal responsibility, and an executive with excessive leeway for unilateral moves. These features, which can be traced back to basic constitutional and electoral rules, as well as to the history of democratic instability, have increased the number of key players, limited their political horizons, and moved politics away from institutionalized arenas, increasing the difficulty to reach cooperative outcomes among policy decision-makers”¹¹. What is worse, any constitutional reform which would seek to amend those institutional failures, would hardly find sufficient political support. This means that the current situation constitutes a *de facto* equilibrium point.

These characteristics of Argentina’s institutional system translate into the country’s consistently low position in the most prominent international comparisons – such as the World Economic Forum’s “Global Competitiveness Report”, World Bank’s “Doing Business” or Heritage Foundation’s “Index of Economic Freedom” – which measure and compare institutional quality of countries around the world. In turn, Argentina’s institutional

weakness is reflected in the country’s trade policy. This is manifested, among other things, in a frequent divergence of the political practice from the formal rules in this area, as well as by a preponderant position of individuals (above all, the president and his or her closest circle) in shaping the trade policy and carrying it out.

Conclusions

A reflection about the sources of Argentina’s institutional weakness extends far beyond the scope of the central thesis of this study. Nonetheless, in the concluding chapter, potential explanations for this phenomenon were analysed and discussed. In this sense, the country’s recent wave of protectionism was explained not only in terms of its most immediate sources, but also in terms of its deeper cultural and historical roots.

In particular, it was suggested that Argentina’s institutional weakness may be considered as a result of a widespread belief among the society that the country used to be a major power at some point in the past and therefore it should seek to restore its lost glory\(^\text{12}\). Argentinians frequently consider themselves as a unique case of a country, given that they belonged to the ten wealthiest nations in the world at the turn of the 19\(^{\text{th}}\) and 20\(^{\text{th}}\) century, while experiencing a progressive decline ever since\(^\text{13}\). Therefore a hypothesis may be formulated that, in search to restore the country’s lost glory, Argentinians may be excessively tolerant towards authoritarian or populist regimes, as long as political leaders manage to credibly promise them the restoration of national power. It is also in this sense that over twelve years of popular support for the Kirchners and for their interventionist policy (e.g. in the trade area) should be analysed.

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