

AQ Podcast – An X-Ray of Javier Milei’s Argentina

Brian Winter, editor-in-chief of Americas Quarterly, with Eduardo Levy Yeyati

—Eduardo, it has been about nine months since Javier Milei took office, what is your overall assessment of Argentina’s economy today?

—This is a complex question because there is a difference between what you see and read and what is actually happening, as usual, but more so now because this government is very present in the news and social networks. Having said that, the key novelty for me is that the government has been faithful to its beliefs much more than people originally thought. Typically in the campaign you’d hear promises of changes that sound popular and then you’d see something different once the election is over. This was not the case, which is something new for Argentine politics. And this is good and bad. It is good because the government has focused almost exclusively on the economy and that was much needed. Milei seems to care much less about everything else. And, particularly, they have centered on the fiscal deficit with a strong conviction, meaning Milei actually thinks that this is the beginning and the end of the resolution of the Argentine crisis. Such a conviction becomes credible, where credibility was historically a problem. I would say that is the main novelty here, I want to emphasize this because I am not sure any other candidate would have done this like him.

—So let’s talk a little bit about the fiscal situation. I saw a headline in the Argentine press this week saying that the fiscal adjustment that Milei has pushed through is the biggest in more than 60 years in terms of percentage of GDP. The data also showed that they are managing a fiscal surplus, that is not a primary surplus, that is an actual nominal surplus, including interest’s payment on the debt, something that nobody thought was possible. You talked about what he said during the campaign, this was a guy who famously wheeled a chainsaw and who was reaping the names of ministries off of a wall, everybody remembers those images, so it is consistent with what he was saying during the campaign. I guess my question is why in the context of Argentina’s recent history was this a surprise?

—Well, everybody knew we had fiscal problems and there was usually the belief that, either because of a lack of social or political space, or simply because there is some inertia in the way public spending was distributed, that this was not feasible. And what this government has proven is that the social resistance was not there, maybe because people finally understood that we needed to adjust and that was a precondition for everything else. And the political opposition is completely dismantled, as many of the previous political referents, I would not say are obsolete, but lack political support, they lack the votes, so there is no organized political opposition. Also, the government found ways to reduce the public sector payroll beyond what experts thought was possible. So, there was a space and they went through. This is like a chicken game where one of the drivers has their hands tied to the wheel. Milei has, and shows that he has, his hands tied to the wheel, and all of a sudden the adjustment becomes credible and visible where people thought that there was no way to do it, at least not that fast.

—Because of Argentina's recent history many of us believe that if he came in with this kind of agenda that he might not last six months on the job before there was a popular revolt. But in practice, as you know, something very different has happened, his popularity in some poles is unchanged, around 50%. Do you think that is more a credit to him as a communicator or does it speak to just the way that the opposition was just so completely discredited that society has given him the latitude to do these things?

—I think both. First of all, a disclaimer: you know, economists have the tendency to answer any question, particularly the ones they don't know much about. Your question is not strictly economic in nature. Having said that, I believe that what we read about society was produced somewhere else, was produced by journalists or thinkers that have been somehow disconnected with the new generations, the majority of which actually supported Milei. Politicians, in particular, but also intellectuals, they talk to each other, they talk to people that are self-interested in the way they express their opinions, but they fail to find a way to communicate to the new generations that are increasingly the majority of votes. That seemed to be the case during the campaign.

At the beginning it was a surprise, but then you start analyzing the nature, the way in which Milei's voters think, and realize that in fact they have been there all the time, except nobody was actually listening to them. Milei, somehow, maybe intuitively, maybe because he was to some extent one of them, talked to them in a more direct way, communicated with them in a way that no traditional politician now could do. One problem that I see in the opposition, something we talked about in a recent piece in *Americas Quarterly*, is that there seems to be a lack of referents that find ways to communicate with this new majority of voters. Without that communication, liberal democracy simply doesn't work. And that seems to be what was exposed during the last campaign. People were expecting that voters would start to change their minds as the cost of the adjustment started to manifest itself, and that is not what happened. That said, half the population is anti-Milei, that everybody is in favor of him. But his 40 to 50% support is still very resilient, despite these relatively difficult nine months.

—We've spoken at some length about the fiscal situation, about how Milei has managed to maintain a certain consensus around those cuts. Let's talk about another really important barometer for Argentina, maybe the most important one, which is inflation. The month that Milei took office inflation was running at about a 25% monthly rate. Over the last couple of months that has been closer to 4. That suggests maybe some kind of stagnation in that fight, I mean, look I want to be fair here, going from 25 to 4 is pretty dramatic, but for it to come down further is going to be tough. So can you put your economist hat back on if you will and unpack for us a little bit what's happening with inflation right now and if there's any hope of it coming down further from this level that you know, again, it's about 50% on an annualized basis?

—First of all, we have to take the official rhetoric with caution. The 25% inflation was an epiphenomenon, something that only happened one month, following a dramatic exchange rate correction, and on top of that a liberalization of many prices that have been contained before. My impression is that they tried to frontload inflation so that they can attribute that to the previous government. The reference point probably is around 10%, which was the inflation inertia before that. So, what happened? Well, first of all, the government would say the elimination of the fiscal deficit eliminated the

source of monetary printing, the transfers from the central bank to the Treasury to finance that deficit, and that, by itself, plus some certain degree of credibility, brought down inflation from 10% to 4%. What happened is a mix of this explanation and something more real. The fiscal adjustment created a recession, the recession pushed down business mark ups and prices in general, and, on top of that, the government has been using and abusing the exchange rate anchor, which is typical of Argentine and, in general, in inflationary economies. In Argentina, because of the lack of monetary credibility, people look at the dollar as a reference to change prices. And politicians, because they lack monetary policy or a credible framework to address inflation, they use the exchange rate as an anchor: they depress artificially the exchange rate to lower inflation expectations. So, you put together the recession and the exchange rate misalignment, the overvaluation of the peso, and that probably explains a significant part of the decline in inflation. What would be the inflation rate if we were growing and we had the exchange rate moving with prices freely? Probably it would be a couple of points higher. So, there was some achievement, but part of it was artificially due to those two transitory factors that I just mentioned.

—Inflation is no doubt an important measure, it has a huge impact on people's day-to-day lives. Ultimately though, for this experiment to work, the real economy is going to have to start growing again. And the recession that the country has endured over these last nine plus months has been very severe. I mean, that's how you get to a decline in inflation like this. What are you seeing in terms of the real economy and how far away are we from that, you know, reactivation that so many people, including, obviously Javier Milei and his economic team, are hoping for?

—Well, remember that I started by saying that there were good and bad things related to Milei's obsession. The bad is that, because he believes that the fiscal deficit is almost the sole cause of everything wrong in the Argentine economy, he focused on adjusting the fiscal deficit and expects the private sector to make up for the decline in demand and everything to come into place just because the deficit is no longer there. Milei sincerely relies on the fiscal adjustment for growth. I don't think that's gonna happen. The private sector is still debating, in part because, you know, nobody wants

to invest in a country during a recession, in part because the exchange rate is perceived to be overvalued and investors may wait until it corrects itself. And we still have exchange rate controls, the so-called “cepo”, and we still have export taxes and import taxes because we now have a tax on foreign exchange purchases. In that environment, it's not clear where the driving force for the recovery of the real economy will come from. There are investments in extractive sectors, oil and gas, mining, that have a very partial trickle down to the real economy. Apart from that and some very generous investment promotion plans, it's not clear where the engine of the economy will come from. If we can sustain this exchange rate anchor and engineer a growth recovery next year, this might be a perfect victory. If not, we might face a crisis, pretty much like the one we faced in 2018 or 19.

—This is the thing, what some people don't realize from the outside is that Argentina is expensive again, not just if you go as a tourist, but if you're looking to make the kinds of investments that are necessary if they're going to come from abroad. Part of this is because of the gap again that we've seen, that was characteristic of the kircherista's years as well, the gap between the official exchange rate and I guess you could say the real exchange rate. This has led to speculation that this government might have to devalue again. Milei and his government team have said in public and private that they will not devalue, do you believe them?

—Yes, I believe he believes in what he said. Now, he may be wrong. I don't think he's tricking us into believing that the fiscal deficit will actually sort everything out, he's like an old-fashioned supply sider, putting it in American terms. I do believe that he will stick to the exchange rate anchor, in this case, a crawling peg, as the official exchange rate is going up by 2% per month, although inflation is around 3.5%-4%. I also believe that he will stick to that simply because inflation is the key victory that he can show next year, a mid-term election year, Milei will use the declining inflation as the best he can show, because growth will probably not be there. He will be betting increasingly on just one factor while exposing Argentina to external financial shocks, or real shocks like a drought.

—You mentioned this view that Milei is depending too much essentially on fiscal policy to do the work of turning around Argentina's economy. That is a view I've heard elsewhere. In your mind, what is the most urgent reform that is still necessary to turn the economy around, whether it's on his wish list or not? What do you see as kind of the most important politically viable steps that could be taken to ensure that this turnaround really does take hold?

—There are two things related to that question. The first one is we still have to sort out our macroeconomic crisis. We still haven't stabilized, people are still expecting the exchange rate to go up. And, if that happens, you will have another pick on inflation. And we still have to work your way around that inflation inertia and bring it down back to states 2%, and eventually to single digits annually. So, we haven't done the job, the first job, which is stabilizing. Without stabilization any other reform will fail. Now, once you do that, there are a number of reforms that have been in the reform list for ages. The tax reform, for sure; we have a tax system that is populated by a number of useless taxes. And we need to have, as soon as possible, a Social Security reform, because we had universal pensions in Argentina, by law since 2016, and we have an increasing degree of informality. Very few are contributing to the system, while everybody is getting something out of it. So sooner or later that, coupled with the demographics of aging, will open up a fiscal deficit. I would add a labor reform, we don't want to have 70% of our private workforce working precariously, either informally or independently, we want to create good jobs. Current labor regulation is actually outdated and probably one of the many barriers creating these good jobs that we so badly need. Those are the three reforms that I would put at the top of the list. It's not simple and stabilization is the priority, but we need to start thinking about those reforms for the day after.

—It's quite the list and testimony that many accumulated years of economic disfunction in Argentina. What do you hear from members of Argentina's private sector? You have some business leaders like Marcos Galperin, the Mercado Libre founder, who have been very positive in public. Behind closed doors, what are business leaders generally saying?

—There are always winners and losers. Marcos Galperin is one clear winner. But the industrial sector in particular, and some micro, small and medium enterprises, are suffering from inflation, from the lack of deregulation, although the government has tried to deregulate some markets, and, particularly, from lack of competition: in Argentina, only the agricultural sector is actually competitive. So you have a lot of monopolies and oligopolies that are benefiting from their market and political power, at the expense of a small enterprises that are ultimately the ones in charge of creating new jobs. So the winners are very vocal in favor of the government and the losers are cautiously critical. And then there are a number of smaller voices that are not even represented in the debate, which are to a large extent probably suffering the transition.

—We've been kind of dancing around this a little bit but let me try to inspire a little bit of a moment of truth here, where do you think Argentina's economy will be one year from now?

—If I wanted to be popular and grab a headline, I would say this time we're going to grow by 7%. Or, alternatively, that we will have a crisis next year like in 2019. Both propositions would be attractive from a media perspective. But I believe next year we will be pretty much what where we are right now, meaning the government will not budge, will not change directions. We will have a problem with the exchange rate, we will have a problem to get net resources from the IMF, although probably we will roll over the program with another program sometime next year. We will have problems to rebound, as we should because we have been going down for a long time and this year is going to be particularly bad, so we need to grow by 5-6-7% a couple of years only to recover the losses and I don't see that happening. Politically, I think Milei will defeat the opposition because the opposition is not there, he is the only player in the field and, even if he loses some support, he will still be the winner of whatever contest next year's election represents.

—Eduardo, that answer may reinforce a little bit of what you wrote in this recent piece for America's Quarterly about the need for a new centrist agenda in Latin America. What inspired you to write this piece which you co-authored for us with Mauricio Cárdenas, the former Colombian finance minister, who is now a professor here at Columbia university in New York. What inspired you guys to write this?

—We are old fashioned. We were used to political parties and political debates around the center. The center doesn't exist per se, it is a zero-measure point in the distribution. The center is where people on the right and left gather to discuss policies that have some resilience to a change in government, which is something that, particularly in Argentina, but in Latin America in general, creates one of the greatest disincentives for growth. Because if you know that things will change, that the rules of the game will be changing every four years, then it's very hard for investors, for the private sector to make long-run plans and investments, except the most extractive ones. We were used to that center and now we are missing that space. What we see is a lot of negative identification. People voting against the Other: It's not that I really like Milei, but I will never vote for Masa, and vice versa. That means that you're not contributing to a debate in favor of some measures, you're essentially trying to destroy something you think is wrong for the country. And that destructive dialectics are in part what explains why our countries have been so disappointing. In particular, Argentina, but I'm thinking also of Colombia or Chile. Milei face may be eventually replaced by a Milei of a different sign, but it will still be the same message. So, we're trying to make people come back to the center, back to negotiating something that has more than 4 years of life. That was the inspiration. Without that center space, our democracies will be weak and may eventually become authoritarian or illiberal.

—I think that there is clear evidence that governments who, you know, they might not call themselves centrist, you might call them center left or center right, but there are lots of examples of governments that have gotten in the kinds of enduring results that you're talking about. You mentioned in your article, Uruguay is still a place where you see a good bit of centerish leadership. I think of leaders like Michelle Bachelet in Chile. I would actually make an argument that Lula's governments have had centerish

elements to them from time to time. But I can also, you know, as I say this, I can sense part of our audience rolling their eyes a little bit because centrism as you know in your article has become unfashionable or old fashioned, I believe you described yourself even just now. Why is that?

—First of all, it is true that, as I said before, the center doesn't exist. The examples that you mentioned, Uruguay, Chile's Bachelet, but also the center right of Chile 10 years ago, or Lula, are the exceptions to the rule. You don't see that generally; you see that as an exception. To the audience I don't really know what to say. It's true, it's unfashionable. But, you know, this is politics, not fashion. So we have to think more rationally and see where we are failing. Why, decade after decade, we're discussing about the lost decades of Latin America. We're still writing about the middle-income trap we cannot get out of. Latin America is the only region where we have poor countries that are also democratic. So we have to find a way to keep being democratic and get out of the income trap, and that way is through the center, somewhere around that symbolic center.

—Well, but look, you mentioned Latin America's challenges and fair enough that's what we do here on this podcast. But let's also be honest. This migration of people to the ideological polls is something that we've seen all over the democratic world in the last 10/15 years. This has been analyzed at length by others. Social media is a big part of it. It's not the only reason, though. So that said, my final question for you and I would encourage our audience to go read the piece on the America's Quarterly website, but in just, you know, in a nutshell, how can centrists in your mind compete with the adrenaline boost and that shot of righteous anger that often accompanies being on either side of the of those ideological poles and as part of what makes them so attractive?

—Well, the first thing to note is that, and this is a personal statement, I wouldn't vote for many of my centrist referents myself. I think they're obsolete, they're old. At some point, I have the feeling that they don't care about the voter anymore. They remind me

of a Warren Beatty movie, *Bulworth*, about a formerly radical Democratic senator that is completely burnt out, sold out to lobbyists, a has been, a politician that go through the motions without any conviction. Those guys are not going to revive the center unless they change, which is unlikely. You have to find new, younger referents with new ways of thinking. You have not to think out-of-the-box but to create a new box, that's difficult to propose to politicians because they actually like being there and they do believe that they have the votes for a support that they in fact lost long ago.

—Maybe part of the problem is that centrism so often feels like a defense of the status quo and you know, there is no attempt to appeal to people's. Emotions and recognize what's wrong with their day-to-day lives. Do you believe that's at least partly true?

—Absolutely. I think centrism, which doesn't exist per se, was the space of reformism where people actually wanted to change the system within the system, instead of just revolutionizing everything, bringing down governments. That was the origin of the center. The center was reformist. Today, after so many years and a good deal of failures, these same guys gave up on reform and novelty and change, but they are still there crowding out the new people. And that's part of what happened in the center. They don't want to share their power, their shrinking square meter of power. And it has a lot to do with the politicians, the fact that the center has lost appeal, because it's an objective truth that they simply don't seem to care, they don't care about the voter, but they expect the voter to keep voting for them because they are the old guys that have been there since forever. The fact that you have such a rapid generational change was one of the reasons why these guys seems to have been retired. That is not bad or good, it is just the way in which politics evolve. Once you have new faces, faces that can recognize the demands from these new voters, then the connection may be more natural. It's not the format, it's not that you don't have to go to the TV, that you need to use streamers or social networks, that's easily done. It's the fact that you have to have someone that at least has a minimal connection with the demands of the new folks. That is still not there.