Argentina – Case study of past crises

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Case study of past crises:
Lessons learned from Argentina
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# TABLE OF CONTENTS

Main findings.......................................................................................................................................................... 1

Introduction ............................................................................................................................................................ 3

A. Argentina and the crisis today ............................................................................................................................ 3
   1. Stimulus package and policy responses to the crisis ......................................................................................... 5

B. Argentina and the 2001-02 crisis ..................................................................................................................... 12
   1. Drivers of the 2001-02 crisis .......................................................................................................................... 12
   2. Outcomes of the 2001-02 crisis ....................................................................................................................... 14
   3. Labour market policy responses to the crisis ................................................................................................. 18

C. Evaluation and lessons from labour market policy .......................................................................................... 21

Appendix A – Effects of government expenses in labour and social measures on employment growth – An empirical approach ......................................................................................................................... 24

References ............................................................................................................................................................. 27
List of figures and tables

Figure 1. Variation of real GDP and total employment since the onset of the crisis, selected countries (Peak to trough growth rates, %) ........................................................................................................... 5
Figure 2. Impact of the crisis on GDP and employment ................................................................................ 16
Figure 3. Evolution of Biannual Labour Market Indicators, 1990 to 2006* .............................................. 17

Table 1. Amount disbursed for anti-cyclical policies, 2008-2010 (Millions of pesos and % of GDP) ........................................................................................................................................................................... 6
Table 2. Social Policy Responses for the Crisis .............................................................................................. 10
Case study of past crises: lessons learned from Argentina

Main findings

- Untargeted and incomplete crisis related efforts can prove unsuccessful and may even be detrimental to economic recovery and social goals. This was the case in Argentina after the recessionary period of the 90s, where premature austerity and the absence of labour market measures proved unsuccessful in boosting output growth and reinforced the deteriorating employment and social conditions. Moreover, social and employment measures can boost aggregate demand and trigger, rather than detract from, an economic recovery. These lessons are of considerable importance for countries such as those in Europe and other high-income areas, where the economy has yet to embark on a sustainable recovery path – both in terms of jobs and growth.

- Argentina was not immune to the effects of the current crisis, but the impacts were relatively modest and short-lived:

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1 This paper has been prepared by Verónica Escudero from the International Institute for Labour Studies (IILS) within the framework of the joint project “Addressing European labour market and social challenges for a sustainable globalization”, which has been carried out by the European Commission (EC) and the International Labour Organization (ILO). This discussion paper provides background information and in-depth analysis for the concluding synthesis report “Building a Sustainable Job-rich Recovery” that summarizes the main findings of the project.
GDP started to decline at the end of 2008, with quarterly GDP dropping by 0.9 and again by 0.4 per cent in the first quarter of 2010. For the rest of 2009, output growth remained weak but proved by the fourth quarter grew at a pace of 1.9 percent.

The effects on the labour market were visible in the first half of 2009: 142,000 thousand jobs were lost in the first two quarters of 2009 and the employment-to-population ratio declined 3.3 percentage points in the four quarters to Q4 2009 (peak to trough). However, by the beginning of 2010, employment had started to grow again and has since re-attained pre-crisis levels.

The quick recovery was supported by labour market and social measures put in place during the previous crisis (as well as an improvement in the terms of trade):

On the fiscal side of the stimulus package, social policy responses were at the centre of the Argentinean effort. Since the beginning of the crisis, 35 per cent of the budget for counter-cyclical policies has been devoted to social policies, of which 63 per cent are labour and income policies.

Moreover, the ability to respond quickly to the onset of the crisis played a critical role in mitigating the effects. Importantly, the ability to adapt in an efficient and effective manner was due in part to the lessons learned and measures adopted during the crisis of 2000-2001: more than half (56 per cent) of the measures introduced during this crisis were a legacy of the past-crisis response.

Argentina’s response to the previous crisis could be characterized as two rather distinct – in both focus and direction – phases:

Phase 1: During the recession period – end of 1998 to end of 2001 – measures followed a trajectory similar to those implemented in the 1990s, i.e. along the lines of deregulation and precautionary policies. In addition, the crisis related effort was rather untargeted and minimized the role of labour and social policies. As a consequence of this and the underlying vulnerabilities of the system, the country was brought to the grips of an economic crisis in 2001 with severe employment and social consequences.

Phase 2: The first response thus proved ineffective and the extended recession period led to an economic crisis in 2001 with severe employment and social consequences. A radical shift in the policy approach was taken, one that was more comprehensive coupled with a targeted set of measures which succeeded in stabilizing the external market and in re-establishing the basic macroeconomic equilibrium. Importantly, it encompassed labour market measures that provided income to workers and in turn helped support aggregate demand. The measures were also effective in addressing the poverty effects of the crisis and fostering employability. Indeed, at the beginning of 2003 the economic and social conditions started to recover at an impressive rate.
Introduction

The global financial crisis hit Argentina in late 2008 after the country’s economy had been enjoying a prolonged recovery from its 2001-02 economic crisis. The impact on output was soon followed by a deterioration in labour market conditions at the beginning of 2009. However, in a relatively short period Argentina started to see signs of recovery, supported by an improvement of the terms of trade and positive conditions of its neighbouring countries.

In the context of the global financial crisis of 2008-09, Argentina’s has fared relatively well compared to other countries of similar characteristics. Moreover, compared to its own experience during the 2001-02 crisis, Argentina has managed to recover faster and avoid the devastating impacts brought by the past crisis. Efforts focusing on labour market and social policies – consistent with the principles of the Global Jobs Pact – were at the centre of the Argentinean stimulus package. And while the origins of past and current crises are different in nature and scope, the ability to respond in an efficient and effective manner in the current crisis is tied very much to the country’s previous experiences – in fact, the groundwork for many of the current programmes and measures was laid during the previous crisis and subsequent government reforms.

The effectiveness of past policy efforts have thus played a role in the positive performance of Argentina during the current crisis. Understanding these dynamics and shedding light on the effectiveness of the Argentina policy responses are the main objectives of this chapter. With that in mind, section A of this paper analyses the impacts of the crisis on output and employment and provides a comprehensive overview of stimulus measures, with emphasis on social and labour market measures undertaken. Section B examines in more detail the Argentinean crisis of 2001-02. This section starts by examining the origins and drivers of the 2001-02 crisis and analysing the economic and social effects of the downturn. Section B concludes by examining the different measures put in place at that time to address the crisis impacts. The third section (section C) will examine briefly – to the extent possible – the effectiveness of some key policies in restoring the labour market and mitigating the negative social effects of the crisis. The final section will conclude with potential lessons learned from the Argentina experience.

A. Argentina and the crisis today

The crisis that begun in 2008 was global in nature, affecting all regions of the world albeit at very different intensities and times. Indeed, while some countries were severely affected both in terms of GDP and employment (e.g. Turkey, Russia, Latvia and Lithuania – see Figure 1), others such as Argentina, Australia or Indonesia proved comparably resilient to the crisis.
In Argentina, the effects of the crisis were mixed but undoubtedly less severe compared to other countries’ experiences. Following a period of sustained economic expansion where annual GDP growth averaged 8.8 per cent between 2003 to 2007, the global crisis started to have an impact on the Argentine economy at the end of 2008 (Q4) and beginning of 2009 (Q1), as quarterly GDP fell by 0.9 and 0.4 per cent respectively. The goods production sector was the hardest hit, in particular subsectors related to construction and foreign trade. Exports declined by 19 per cent reduction during the first semester of 2009 mainly through declines in sales from the automotive sector.

Although the decline lasted only two quarters output growth remained weak in 2009 at about 0.2 per cent on average in the first three quarters of the year. Growth at the end of 2009 proved stronger (1.9 percent, q-o-q), thanks to the revival of growth in some of Argentina’s export markets, notably to Brazil and China. In particular, the rebound was particular strong in manufacturing and agriculture (International Labour Office, 2010).

Similarly, the effects on the labour market were moderate compared to previous crises. By the fourth quarter of 2009, the unemployment rate was 1.1 percentage points higher compared to the year before, having reached 8.4 per cent. In addition, 142,000 thousand jobs were lost in the first two quarters of 2009 and the employment-to-population ratio declined 3.3 percentage points in the four quarters to Q4 2009 (peak to trough).

Despite these negative consequences brought about by the crisis, massive layoffs were avoided in Argentina. Indeed, data from the Ministry of Labour (MOL) shows that falls in formal employment during the first months of the crisis – at the end of 2008 – responded more to a deceleration of new hiring by private firms rather than to an increase in job cuts. As discussed below, the impact of the crisis was mitigated mainly through job retention measures and through policies aimed at increasing workers revenues, thus boosting demand and reviving economic growth. In this respect, Argentina is among the successful stories of the present crisis and an interesting case study.

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2 In the four quarters to quarter two 2009, the share of new employee hiring fell by 1.4 percentage points to attain 2 percent, the share of registered employee separations decreased 0.7 percentage points to reach 2.2 per cent.
Case study of past crises: lessons learned from Argentina

Figure 1. Variation of real GDP and total employment since the onset of the crisis, selected countries (Peak to trough growth rates, %)

Note: *The division between Advanced and Emerging G20 countries is based on a Median calculated on per capita GDP for the period. **Changes in GDP and employment are growth rates measured from peak to trough (where a trough has not yet been attained, the latest available information is used). The beginning of the crisis is country specific and is measured as the first term showing a negative change in either real GDP or employment. The comparison across countries in the same group is done relative to the group’s median.

Source: IILS estimates based on: OECD, Economic Outlook No. 86; Eurostat database; ILO, Laborsta database; and IMF, IFS database.

1. **Stimulus package and policy responses to the crisis**

The effects of the crisis were mitigated in great part due to government intervention, especially through a far reaching and comprehensive stimulus package comprised of monetary and financial policies, as well as fiscal measures and programmes tailored to support the labour market (see also Chapter 5 for an overview of countries’ responses).

By the beginning of 2010, the Government of Argentina had disbursed 91.7 billion pesos (8.8 per cent of GDP) in anti-cyclical policies put forth since 2008 to mitigate the effect of the crisis. Of this amount, the bulk (74 per cent) was spent in 2009 compared to 24 per cent in 2010. In 2009, the biggest share of the total budget for anti-cyclical policies was allocated to capital expenditure measures (e.g. infrastructure plans). Financing policies such as those financed with SIPA funds, came second with a 25 per cent share in the total. Discretionary measures such as social safety, family allowances, but also measures aiming
to stimulate labour demand (e.g. subsidies and tax reductions for SMEs, etc.) accounted for 21 percent; and structural measures for 15 per cent (see Table 1).

Table 1. Amount disbursed for anti-cyclical policies, 2008-2010 (Millions of pesos and % of GDP)

<table>
<thead>
<tr>
<th></th>
<th>2008</th>
<th>2009</th>
<th>2010</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Social safety (2)</td>
<td>1,200</td>
<td>2,670</td>
<td>3,870</td>
<td></td>
</tr>
<tr>
<td>Family allowances (2)</td>
<td>346</td>
<td>3,362</td>
<td>9,631</td>
<td>13,339</td>
</tr>
<tr>
<td>Tax deferral</td>
<td>1,500</td>
<td></td>
<td>1,500</td>
<td></td>
</tr>
<tr>
<td>Tax reduction</td>
<td>350</td>
<td>3,500</td>
<td>3,850</td>
<td></td>
</tr>
<tr>
<td>Reduction in export duties</td>
<td>730</td>
<td></td>
<td>730</td>
<td></td>
</tr>
<tr>
<td>Compensation for the agricultural sector</td>
<td>250</td>
<td>250</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Compensation for dairy production</td>
<td>968</td>
<td>968</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Compensation for livestock producers</td>
<td>500</td>
<td>500</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Subsidies to cover employee wage bills and other labour policies (2)</td>
<td>45</td>
<td>610</td>
<td>457</td>
<td>1,112</td>
</tr>
<tr>
<td>Cooperatives Plan (2)</td>
<td>180</td>
<td>1,800</td>
<td>1,980</td>
<td></td>
</tr>
<tr>
<td>Trade, consumption and production loans (1)</td>
<td>15,600</td>
<td>15,600</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Mortgage loans</td>
<td>1,140</td>
<td></td>
<td>1,140</td>
<td></td>
</tr>
<tr>
<td>Infrastructure plan (1)</td>
<td>24,000</td>
<td></td>
<td></td>
<td>24,000</td>
</tr>
<tr>
<td>Federal Solidarity Fund (export duties on soybeans)</td>
<td>2,941</td>
<td>2,941</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Law of Retirement Mobility (1)</td>
<td>7,750</td>
<td>6,900</td>
<td>14,650</td>
<td></td>
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<tr>
<td>Public Sector wage increases (1)</td>
<td>1,636</td>
<td>2,006</td>
<td>3,642</td>
<td></td>
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<tr>
<td>Increases in university employees wages and student grants (1)</td>
<td>734</td>
<td>899</td>
<td>1,633</td>
<td></td>
</tr>
<tr>
<td>Total budget per type of policy</td>
<td>0</td>
<td>Column</td>
<td>Column</td>
<td>Column</td>
</tr>
<tr>
<td>Social policies (I + II + III + IV, excluding infrastructure plan and consumption and production loans - 1)</td>
<td>1,941</td>
<td>18,351</td>
<td>11,888</td>
<td>32,180</td>
</tr>
<tr>
<td>% of GDP**</td>
<td>0.19</td>
<td>1.76</td>
<td>1.14</td>
<td>3.08</td>
</tr>
<tr>
<td>Income policies (2)</td>
<td>1,591</td>
<td>6,822</td>
<td>11,888</td>
<td>20,301</td>
</tr>
<tr>
<td>% of GDP**</td>
<td>0.15</td>
<td>0.65</td>
<td>1.14</td>
<td>1.95</td>
</tr>
</tbody>
</table>

Note: (1) measures excluded from the total cost of anti-cyclical policies; 2) measures considered as part of the aggregate income policy; **Reference GDP=1,043,632 million pesos.

Source: Ministry of Labour of Argentina, Undersecretary of Technical Programming and Labour Studies.

On the fiscal side of the stimulus package, social policy responses were at the centre of the Argentinean effort. Since the beginning of the crisis, 35 per cent of the budget for counter-cyclical policies has been devoted to social policies, of which 63 per cent are labour and income policies. Indeed, part of the success of the Argentinean policy package
can be attributed to this. However, another important point in this regard is related to the fact that most of the measures (56 per cent) were a legacy from past crises and as such could be adapted quickly to the new needs in an efficient way.

The social policy responses in Argentina can be divided into (i) programmes focused on stimulating labour demand; (ii) supporting job creation (or mitigating job losses); (iii) expanding social protection and food security, and; (iv) enhancing social dialogue and rights at work (see Table 2). The remaining of this section will pass revue to the details of the different programmes put in place.³

**Measures aimed to stimulate labour demand**

- As a means to stimulate labour demand, the government of Argentina announced an increase in spending on infrastructure projects through the Plan for public works (Plan de obras públicas). The budget for public works doubled in 2009 (compare to that of 2008). The plan focuses on building and repairing roads, bridges, railways lines but also on improving the water system and building hospitals and schools. In addition, the Scheme to promote investment in capital assets and infrastructure (Régimen de promoción de las inversiones en bienes de capital y obras de infraestructura – Law No. 26.360) put forth 1,200 million pesos per year for employment-intensive infrastructure projects.

- A series of measures aimed at firms, especially SMEs, were also introduced through increased access to credit, as well as subsidies and tax reductions. The programme Rate rebate scheme (Régimen de bonificación de tasa ), for example, grants preferential interest rates (decreased by up to 4 per cent) for loans of up to 300,000 pesos intended to finance working capital of small- and medium-sized enterprises. In April 2009, the government awarded 200 million pesos to 16 banks that offered up to a total of 498 million pesos to be granted in this type of loans. In addition, the programmes Tax credit for training (Crédito Fiscal para Capacitación) and Tax credit system 2009 (Régimen de Crédito Fiscal 2009), offers tax credits for the totality of costs incurred in training of their employees. Both programs favour SMEs in terms of the amount of funds allotted (up to 8 per cent of their total labour cost) and the latter benefits big enterprises as well but only up to an 8 per thousand of their total labour cost. Moreover, the scheme Buy Argentinean work (Régimen Compre Trabajo Argentino – Law No. 25.551) gives incentives to all public enterprises to prefer in their procurement goods of national origin and services provided locally. Finally, the

³ It is worth mentioning that the list of policies and programmes do not pretend to be an exhaustive one. The aim of this section is to discuss the most significant measures put in place nationwide by the Ministries of Labour, Employment and Social Security, Social Development, Production and Planning, Public Investment and Services. This means that those programmes carried out at a municipal and provincial level to meet the same objectives are not considered. This is the case of the plan called Guaranteed Right for Children (Derecho Garantizado para la Niñez) put forth by the Buenos Aires Province, which extends the payment of family allowances received by state workers to jobless households with children aged 0 to 6 years (International Labour Office, 2010).
Production Recovery Programme (Programa de Recuperación Productiva), also support firms through wage and labour cost reductions (see below for more detail on this programme).

**Measures aimed to support jobseekers, jobs and the unemployed**

- **Training measures** have been extensively used by the country to support the labour market. Besides the two tax credit programmes aimed at SMEs mentioned above, four additional programmes were put in place. The *Training for work programme* (Programa de formación para el trabajo), provides training and formal studies, along with employment search assistance. The programme is targeted towards adults and youth with incomplete levels of compulsory schooling. Note that the programme supports both the employed and the unemployed, preferably those already participating in other forms of welfare programs. Its goals are to provide better career opportunities for these individuals through professional training and employment search. Moreover, the *Youth with more and better work programme* (Programme Jóvenes con Más y Mejor Trabajo), provides education and help with job search for young people between 18 and 24 years old that have not completed primary and/or secondary education. As of May of 2009, the programme reported 34,308 beneficiaries. In addition, the programme called *Employment Services Network* (Red de Servicios de Empleo) provides free employment services such as assistance for individuals who are looking for a job but also for employers in need of hiring new workers. By April 2009, 278 offices were accommodated across the country for this purpose. The programme was supported by both the ILO and the International Italian Cooperation.

- Some of the measures put in place promoted employment retention through wage and labour cost reductions. *The Production Recovery Programme* (Programa de Recuperación Productiva), for example, subsidizes salaries up to 600 pesos for up to 12 months to companies that accept not to dismiss the employees benefitting from this programme. Though it was created in 2002, this programme was extended at the end of 2008 for one year. By November of 2009 coverage had extended to 2,658 businesses, 139,034 workers, compared to 448 and 22,846, enterprises and workers respectively, in 2008. Finally, the *Job Placement Programme for Workers with Disabilities* (Programa de Inserción Laboral par Trabajadores con Discapacidad), provides disabled workers with an allowance for up to 9 months, which the employer will deduct from the salaries payed. In this way, employers reduce their labour cost promoting employee retention. Employers also receive a deduction in taxes and social security contributions for up to 12 months.

- **Unemployment benefits were also extended** as a measure to support job losers during this crisis. The formal *Unemployment Insurance System* (Seguro por Desempleo), for example, extended the amount of its contributions by almost 50 per cent. Another example is the *Training and Employment Insurance Programme* (Seguro de Capacitación y Empleo), which was created in 2004 to help the unemployed who partake in the
Heads of Household Programme to help them find employment. This programme provides an allowance of 225 pesos per month (or 75 extra pesos to workers already receiving the 150 pesos of the Heads of Household Program), as well as job search assistance, training and career advice. Between May 2006 and April 2009, the programme reported a total of 117,460 beneficiaries, 56 per cent of which correspond to April 2009. Finally, the Programme for youth with more and better jobs, explained above, is another example in this direction.

- **In terms of sector specific packages or measures**, the Project Small Farmers Development (Proyecto de Desarrollo de Pequeños Productores Agropecuarios), created in May 1998, was reinforced to enlarge its coverage. It provides aid to workers in agriculture and fishing through technical and financial assistance with views to improve their level conditions and improve their income in a sustainable manner. It aims to increase production levels. The second phase of this project started in the second half of 2009 – with USD 54 million funding – and plans to involve 22,000 new producers for a period of 2.5 years. Notable also among the sectoral relief measures was a loan from the National Social Security Administration (ANSES) to General Motors to develop and commercialize a new car with locally produced inputs.

**Measures aimed to expand social protection and food security**

- **Social protection plays an important role in rebuilding society in times of crisis.** Argentina’s policy package had a number of initiatives along these lines, most notably, the renationalization of the pension system at the end of 2008, which was in large part privatized in 1994. The pension assets which had been administered by private firms, totalling about 10 per cent of GDP, were transferred to the National Social Security Administration (ANSES) and a sustainability reserve fund was created. In this effort to modify old-age pensions, minimum benefits were increased by 250 per cent. The plan also expanded coverage to include an additional 15 per cent of the population of age 60 and over (Prasad and Gerecke, 2009).

- **Moreover, a new programme was created to reinforce social security through tax reductions.** This is the Regularisation Scheme for Industrial Relations and Promotion for the Incorporation of New Jobs (Régimen para la Regularización de Relaciones Laborales y Promoción para la Incorporación de Nuevos Puestos de Trabajo – Law No. 26.476). This law, enacted in December 2008, provides discounts to employers’ social security contributions for all new hired workers and newly regularized working relations.

- **In terms of programmes intended to provide additional assistance for families with small children**, the Heads of Household Plan (Plan Jefes and Jefas de Hogar) was a very successful initiative. It is a large-scale cash transfer programme for unemployed heads of household created during the 2002 crisis. It provides a monthly allowance of USD 150 to unemployed heads of households, especially those with children under the age of 18, or disabled. In exchange, these workers must provide 20 hours of work in
sectors benefitting society, such as healthcare. Beneficiaries could also count training towards their required hours. Note that there is a high concentration of women in this programme (71 per cent) and of people under 35 (47 per cent). In addition, the Argentine government created a new programme during this crisis aimed at the 4 to 5 million children (in 2009) whose parents are unemployed or work in the informal sector have not been covered by family allowances. This is the Universal child allowance for social protection (Asignación Universal por Hijo para Protección Social), which consolidates the transfers currently provided through different social programmes into one major child benefit programme administered by ANSES.

- Finally, Argentina put forth a measure aimed to increase food subsidies with views to enhance food security. This is the National Food Security Plan (Plan Nacional de Seguridad Alimentaria), which unifies all plans and programmes aimed at the food problem. It provides food assistance to vulnerable families in effort to improve quality of life, health and nutrition in the medium and long terms. Another important goal of this programme is to reduce child mortality.

**Measures aimed to enhance social dialogue and rights at work**

- Consultation between social parties is a powerful measure to enhance social dialogue and rights at work in times of crisis. One programme was reinforced in Argentina with this aim. The Crisis prevention procedure (Procedimiento Preventivo de Crisis) is an instance of negotiation and agreement between the parties, with state mediation or intervention, in cases where companies decide to take actions that affect employment (in particular dismissals) motivated by issues of “force majeure”, such as economic crises. This policy was first implemented in 1991 and gained a momentum in 2008, seeking to reduce dismissals and suspensions resulting from the crisis. Between October 2008 and May 2009, approximately 12,000 workers in affected firms requested PPC intervention. In about 70 per cent of the cases firms decided to suspend or shorten working hours instead of laying-off workers. The programme also connects companies to the Production Recovery Programme mentioned above.

- Another measure that aimed to reinforce rights at work during the crisis was the National Programme of Labour Regularization (Programa Nacional de Regularización del Trabajo). The main objective of this programme is to reinforce labour inspection capacity, verifying that enterprises comply with adequate working conditions and social protection. This measure exists since 2003.
### Table 2. Social Policy Responses for the Crisis

<table>
<thead>
<tr>
<th>Policy categories</th>
<th>Programmes and schemes</th>
<th>Legacy from past crises?</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Stimulating Labour Demand</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Additional spending on infrastructure</td>
<td>- Plan for public works</td>
<td>No</td>
</tr>
<tr>
<td></td>
<td>- Scheme to promote investment in capital assets and infrastructure – Law No. 26.360</td>
<td>Yes</td>
</tr>
<tr>
<td>Increase in public employment</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Incentives/subsidies to hire</td>
<td>- Employment Services Network (*)</td>
<td>No</td>
</tr>
<tr>
<td></td>
<td>- Job Placement Programme for Workers with Disabilities (*)</td>
<td>No</td>
</tr>
<tr>
<td>Access to credit for SMEs</td>
<td>- Rate rebate scheme</td>
<td>No</td>
</tr>
<tr>
<td>Subsidies and tax reductions for SMEs</td>
<td>- Tax credit for training</td>
<td>Yes</td>
</tr>
<tr>
<td></td>
<td>- Tax credit system 2009</td>
<td>No</td>
</tr>
<tr>
<td></td>
<td>- Buy Argentinian work – Law No. 25.551</td>
<td>Yes</td>
</tr>
<tr>
<td><strong>Supporting Jobseekers, jobs, and unemployed</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Additional training measures</td>
<td>- Training for work programme</td>
<td>Yes</td>
</tr>
<tr>
<td></td>
<td>- Programme for youth with more and better jobs</td>
<td>No</td>
</tr>
<tr>
<td></td>
<td>- Employment Services Network</td>
<td>No</td>
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<tr>
<td>New emp. measures for migrant workers</td>
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<td></td>
</tr>
<tr>
<td>Partial unemployment with training and part-time work</td>
<td>- Production Recovery Programme (REPRO) (*)</td>
<td>No</td>
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<tr>
<td></td>
<td>- Training for work programme (*)</td>
<td>Yes</td>
</tr>
<tr>
<td></td>
<td>- Regularisation for Industrial Relations and Promotion for the Incorporation of New Jobs – Law No. 26.476 (*)</td>
<td>No</td>
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<tr>
<td>Wage and Labour cost reductions</td>
<td>- Production Recovery Programme (REPRO)</td>
<td>Yes</td>
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<td></td>
<td>- Job Placement Programme for Workers with Disabilities</td>
<td>No</td>
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<tr>
<td>Extension of unemployment benefits</td>
<td>- Unemployment Insurance System</td>
<td>Yes</td>
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<tr>
<td></td>
<td>- Training and Employment Insurance Programme</td>
<td>Yes</td>
</tr>
<tr>
<td></td>
<td>- Programme for youth with more and better jobs</td>
<td>Yes</td>
</tr>
<tr>
<td>Sector Specific packages or measures</td>
<td>- Project Small Farmers Development</td>
<td>No</td>
</tr>
<tr>
<td></td>
<td>- Measures aimed at General Motors to develop and commercialize a new car with locally produced inputs</td>
<td>No</td>
</tr>
<tr>
<td><strong>Expanding Social Protection and Food Security</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Social security tax reductions</td>
<td>- Regularisation for Industrial Relations and Promotion for the Incorporation of New Jobs – Law No. 26.476 (*)</td>
<td>No</td>
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<tr>
<td>Income tax reductions</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Increased access to health benefits</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Changes in old-age pensions</td>
<td>- Renationalization of the pension system</td>
<td>No</td>
</tr>
<tr>
<td>Increase in the minimum wages</td>
<td></td>
<td></td>
</tr>
<tr>
<td>New protection measures for migrant workers</td>
<td></td>
<td></td>
</tr>
<tr>
<td>State aid to buy and rent housing</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Additional assistance for families with small children</td>
<td>- Heads of Household Plan</td>
<td>No</td>
</tr>
<tr>
<td></td>
<td>- Universal child allowance for social protection</td>
<td>Yes</td>
</tr>
<tr>
<td>Introduction of increased food subsidies</td>
<td>- National Food Security Plan</td>
<td>Yes</td>
</tr>
<tr>
<td><strong>Social Dialogue and Rights at Work</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Consultation on crisis response</td>
<td>- Crisis prevention procedure (PCC)</td>
<td>Yes</td>
</tr>
<tr>
<td></td>
<td>- Production Recovery Programme (REPRO) (*)</td>
<td>Yes</td>
</tr>
<tr>
<td>Agreements at national level</td>
<td>- Crisis prevention procedure (PCC) (*)</td>
<td>Yes</td>
</tr>
<tr>
<td>Agreements at sectoral level</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Changes in labour law</td>
<td>- Regularisation for Industrial Relations and Promotion for the Incorporation of New Jobs – Law No. 26.476 (*)</td>
<td>No</td>
</tr>
<tr>
<td></td>
<td>- Buy Argentinian work – Law No. 25.551 (*)</td>
<td>Yes</td>
</tr>
<tr>
<td></td>
<td>- Scheme to promote investment in capital assets and infrastructure – Law No. 26.360 (*)</td>
<td>Yes</td>
</tr>
<tr>
<td>Increased capacity of labour inspection</td>
<td>- Programme of Labour Regularization</td>
<td>Yes</td>
</tr>
</tbody>
</table>
B. Argentina and the 2001-02 crisis

In 2001-02 Argentina experienced one of the worst economic crises in its history. The crisis broke after a decade of relatively strong economic performance where Argentina was praised as a model of successful macroeconomic policy and structural reforms in the context of financial globalization (Damill, et al., 2007). Indeed, following a long period where the whole region suffered from economic instability, including the Latin America debt crisis and hyperinflation of the 1980s, Argentina was able to: (i) reduce inflation to low single digits; (ii) attain consistently strong output growth; and (iii) successfully withstand the Tequila crisis of the mid-1990s.

Despite its strong economic performance and the economic reforms and precautionary measures put forth – most of them following a succession of IMF-sponsored programmes – Argentina fell into a depression in the late 1990s. In 2001, the underlying vulnerabilities of the system in place became unsustainable and combined with slippages in policy formulation brought the country to the grips of an economic crisis with severe employment and social consequences.5

However, since the beginning of 2003 the economic conditions started to recover at an impressive rate – GDP grew at an average year-on-year rate of almost 9 per cent. Positive effects of devaluation – especially the shift in relative prices – had a key role in boosting the recovery. However, the set of measures put in place succeeded in stabilizing the external market and in re-establishing the basic macroeconomic equilibrium. Importantly, the labour market measures undertaken as part of the response provided income and improvements in nominal wages, bolstering demand and decreased unemployment.

This section provides: (i) a brief overview of some of the vulnerabilities associated with the downturn; (ii) a synthesis of the economic and the labour market consequences of the collapse; and (iii) a detail of the different policy responses put in place to mitigate these shocks.

1. Drivers of the 2001-02 crisis

There is some debate as to the role played by the different factors associated to the 2000-01 economic downturn in Argentina. A vast literature exists supporting the idea that the

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4 The Argentinean plan for stabilization and structural reforms better known as the “Convertibility Plan” was launched in April 1991 as a measure to boost the economy after one and a half decades of economic stagnation and high inflation – GDP shrank 6.9% in 1989 and the inflation rate exceeded 3,000% (WDI, 2007). The core reform of the Plan was the adoption of a currency board; which was accompanied by structural reforms to strengthen the domestic financial sector and open the economy to international capital markets, and to boost microeconomic efficiency through trade liberalization and privatization of state enterprises.

5 In the midst of the recession the Argentinean government put forth contractionary policies aimed at rebalancing fiscal deficits and restoring confidence in the system (Stiglitz, 2002)
Case study of past crises: lessons learned from Argentina

crisis was rooted in insufficient fiscal tightening during the booming growth years of the mid 90s. Other authors place greater emphasis on the choice of a fixed exchange rate regime – combined with large fiscal deficits or coupled with devaluation by Argentina’s major trading partners – in explaining the crisis. Yet, some blame the collapse to the sudden stop in capital flows due to the high unofficial dollarization and the relatively closed economy; or to the choice of contractionary policies put forth to address the recession.

What is clear, however, is that weaknesses existed in each of these areas, which were built during the stabilization process a decade before the crisis erupted. Yet, it is the interaction of the different factors that led to a larger vulnerability to external shocks.

Systemic vulnerabilities to external shocks were built during the economic boom...

There is a wide recognition that a central vulnerability in Argentina was the sustained increase in public sector indebtedness. Subsequent headline deficits although low (around 1.5 per cent of GDP over 1992 to 1998) were combined with increasing off-budget spending that raised borrowing requirements above 3 per cent of GDP per year, increasing on-balance interest payments. As a consequence, the structural fiscal position worsened from close to equilibrium at the beginning of the decade to -2.75 per cent in 1998. Consequently, public debt increased from 18 to 35 per cent of exports from 1992 to 1998. Hence, increased dependence on private capital flows was built during the decade trying to meet the public sector’s rising borrowing needs.

Argentina’s low share of exports in the economy (around 9 per cent of GDP during the 90s) limited the ability of the external sector to act as a buffer against sudden changes in domestic demand. Moreover, exports’ high concentration on primary products and lack of market diversification – 45 per cent of products were exported to Mercosur, Chile and Bolivia in 1998, with Brazil making up two-thirds of this – intensified the external sector weakness. As a result, the economy was increasingly reliant on capital flows – to generate...

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6 See for example Mussa (2002); IMF (2003)
7 See for example De la Torre, et al. (2002); Feldstein (2002); Perry, et al. (2003); Roubini (2001)
8 See for example Calvo, et al. (2003)
9 See for example Stiglitz (2002b)
10 Due mainly to compensation payments after the social security reform on the early 1990s (International Monetary Fund, 2003).
11 Assuming a potential growth of close to 3.5 per cent during the period (International Monetary Fund, 2003)
12 Public and publicly guaranteed debt service as a percentage of exports (excluding workers’ remittances) (WDI, 2009)
13 This vulnerability was evidenced in 1998, when impacts of the Asian financial crisis pushed Brazil to devaluate its currency, which caused profound pervasive effects in Argentina. In fact Argentina entered its prolonged recession following Brazilian’s devaluation.
revenues to cover excess imports and the increasing costs of debt service. This meant the country was vulnerable to shifts of investors’ confidence in international capital markets. This was of particular concern for Argentina, which under the currency board regime, needed international reserves to back its currency.

However, the financial system in Argentina remained relatively underdeveloped – ranking low in market capitalization, total domestic credit, private sector credit, M2, etc. – and lacked the capacity to bear the risks of this increasing need for capital flows. The small size of the domestic financial sector encouraged heavy reliance on foreign financing and extensive informal dollarization. In addition, the extensive privatization process followed in Argentina from 1990 onwards, financial liberalization and the application of the stabilization programme – thanks to which a big stock of reserves was accumulated – increased entry of foreign financial institutions and encouraged substantial consolidation among existing ones. While these transformations improved the banking sector’s strength and efficiency, it also made it more vulnerable to credit risk in the event of a devaluation – given the high unofficial dollarization – and to increased financial volatility (foreign-owned banks are less tight to the domestic economy and therefore more susceptible of reducing exposure in times of risk). In addition, the reformed banking sector failed to lend to small- and medium-sized enterprises, hampering furthering growth prospects.

These vulnerabilities were all the more important in the context of Argentina’s structural adjustment programme. The programme included privatization, tax reform, deregulation, trade liberalization and the adoption of a currency board. The latter reform brought significant benefits, yet at the cost of restraining the use of monetary policy and the exchange rate as an instrument for adjustment. Domestic liquidity and credit, under these conditions, became fully dependant on the changes of foreign reserves, which is on the balance of payment results. Macroeconomic stabilization had therefore to be done through fiscal policy, which required a greater fiscal space and nominal flexibility of the economy.

2. Outcomes of the 2001-02 crisis

The crisis broke with a run on banks that reduced private sector deposits by more than 6 per cent of the deposit base and cut bank reserves by 2 billion pesos during November 28-30, 2001. Aggressive protests and riots followed the government efforts to control banking and foreign exchange transactions. The political situation deteriorated, a partial default of the public debt was announced and finally the currency board was dropped in January 2002.

14 One of the main reasons behind the continuous current account deficits during the 90s was the sharp appreciation of the real exchange rate. In fact, the real exchange rate was already appreciated when the nominal exchange rate was pegged to the dollar in March 1991 (Damill, et al., 2007)
The end of the macroeconomic regime of the nineties translated into severe economic, employment and social consequences. Real GDP fell by 20 per cent during the 15 quarters leading to Q1 2002 (peak to trough, see Figure 2), with 80 per cent of the fall occurring during the last 4 quarters. The two biggest sectors in the economy were hit even harder during this period (Q1 2001 – Q1 2000): whole- and retail sales fell by 26 per cent followed by industrial manufacturing (-22 per cent). As a result, tax revenues dropped by 17 per cent from Q4 2001 to Q4 2000, and although spending cuts were carried out across the board, the government’s overall fiscal position worsened to 10.5 per cent of GDP in 2002. The public debt ratio also worsened (doubling from 63 per cent of GDP at the end of 2001 to around 135 per cent at the end of 2002), which reflected the effects of the exchange rate depreciation on foreign-currency denominated debt, the issuance of debt to compensate banks for the depreciation and the accumulation or arrears (IMF, 2003).

Social conditions worsened dramatically in 2001-2002. Unemployment soared to 22 per cent in the first semester 2002 – an increase of 9 percentage points from the trough (second semester 1998) to peak. Employment fell by 9.5 per cent in the 4 quarters leading to Q3 2002. The proportion of people living below the poverty line more than doubled – rising to 57 per cent in May 2002 compared to 24 per cent four years earlier.

\[15\] There was a change in methodology at the beginning of 2003 and therefore a break in series. If new methodology is taken into account, unemployment rate at the peak would have been at 25 per cent.

\[16\] Monthly information on employment is not available before August 2001 and therefore the analysis based on this information points to Q3 2001 as the peak of employment before the jobs crisis. However, available biannual employment information shows that job losses started before, since the second semester 2000 (Oct-2000). Thus, the Argentinean labour market suffered from an additional fall in employment of 4.1 per cent (y-o-y) in the year to Oct-2001 (Ministerio de Trabajo Empleo y Seguridad Social, 2004).
**Figure 2. Impact of the crisis on GDP and employment**

<table>
<thead>
<tr>
<th>Year</th>
<th>Real GDP</th>
<th>Employment</th>
</tr>
</thead>
<tbody>
<tr>
<td>1998</td>
<td>Q2: -2.2</td>
<td>Q2: -1.4</td>
</tr>
<tr>
<td>1999</td>
<td>Q3: -0.11</td>
<td>Q3: -4.1*</td>
</tr>
<tr>
<td>2000</td>
<td>Q4: -1.4</td>
<td>Q4: -9.5</td>
</tr>
<tr>
<td>2001</td>
<td>Q1: -0.5</td>
<td></td>
</tr>
<tr>
<td>2002</td>
<td>Q2: -9.5</td>
<td></td>
</tr>
</tbody>
</table>

Note: Figures in parenthesis correspond to Q1 year-on-year changes for Real GDP and Q3 year-on-year changes for Employment. *Year-on-year change from Oct 2000 to Oct 2001, given unavailability of monthly information on employment for all urban conglomerates (see footnote 12 for additional information on this).

Source: IILS estimates based on INDEC and Ministerio de Trabajo Empleo y Seguridad Social (2008)

**But the employment cycle was clearly observable during the Convertibility regime, long before the crisis...**

In the first instance, the achievements attained during the first years of the stabilization programme in terms of higher economic growth and lower inflation rates had positive effects on the labour market. Indeed, greater economic activity was translated into greater demand for labour and the reduced inflation real wages and purchasing power with particular positive effects for the lowest wage-earners. As a result, the aggregate employment rate tended to rise between the launching of the reforms and 1993 (Figure 3, panel A); the same occurred with the participation rate that shows a clear acceleration in its 1991-1993 positive trend.

On the other hand, stabilization programmes like the one put forth in Argentina are characterized by having negative effects for the labour market given that, for example, privatization processes often involve staff cuts and national expenditure adjustments including public employment reductions. However, the negative consequences on employment and wages should be a one-time-phenomena (Damill, et al., 2007) – i.e. until employment adjusts to the new economic order. Yet, this was not the case in Argentina. As shown in panel A of Figure 3 the employment rate deteriorated steadily from 1993 to attain in 1996 levels well below the 1990 (pre-Convertibility) ones. And when the employment rate started to recover, it did not have time to attain 1993 levels that the new economic cycle affected employment again bringing the rate down to levels never seen since the 70s.
It is important to note that, the employment retrenchment mainly affected full-time employment, which means that the rate of underemployment (involuntary underemployment) tended to increase in the same period (Figure 3, panel B). Another important characteristic of employment during this period is that job losses were concentrated in manufacturing. This means that while privatization and fiscal adjustment processes had negative effects on employment, the heaviest employment shock came from the restructuring and concentration of activities in the production of tradable goods – especially in the manufacturing sector – pushed by trade openness and exchange-rate appreciation.

On the other hand, the labour force participation rate shows a relatively steady growing trend, which does not seem to be correlated to the economic cycle (Figure 3, panel A). Some argue this is due to a sustained increase in female participation in the labour force (Damill, et al., 2007). On the contrary, the unemployment rate increased sharply during almost the whole period analyzed due to the increasing participation rate and the relative stagnation of the employment rate (Figure 3, panel B). The only decrease in unemployment is noticeable from 1995 to 1998. The first half of this period seems to be related to a slight decrease in participation rates – probably through a discouraged worker effects – and the second half to a slight increase in the employment rate.

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**Figure 3. Evolution of biannual labour market indicators, 1990 to 2006**

![Chart showing participation and employment rates]

17 Full-employment rate fell 6 percentage points from the peak to trough (first half 1991 to second half of 2001) compared to a contraction of 4.6 percentage points in the aggregate employment rate (second half 1992 to first half of 2002).
Despite a strong economic contraction and long labour market recession, which started before the actual crisis, the recovery was fast and rather V shaped. By the end of 2003, both the employment and unemployment rates attained pre-crisis levels. In fact, during this recovery period the full-time employment rate recuperated all the fall experienced during the Convertibility regime period reaching similar levels to the early eighties. Similarly, the total employment rate (without social plans) reached the highest levels in the available series. Wages also recovered significantly during this period. Importantly, there was also a reduction in the wage gap between the tails of the distribution which in turn contributed to the reduction in inequality among workers (Damill, et al., 2007).

A number of factors, both external and internal, were at the origin of this fast crisis recovery (see section C); however, effective social and labour policies launched in the second half of 2002 are often underlined as having an important role in stimulating aggregate demand by supporting household income.

3. **Labour market policy responses to the crisis**

An important amount of policies were put forth by the government to mitigate the economic and social effects of the 2001-02 crisis. These measures were put forth as early as 1998. Yet, two clearly different phases can be distinguished in terms of the focus and directionality of these crisis related measures:
During the recession period, the crisis related effort was untargeted and incomplete …

The first phase of the policy response corresponds to the recession period going from end of 1998 to end of 2001. Measures during this phase follow the same path of deregulation and flexibility policies implemented during the 90s, which were unsuccessful in stabilizing macroeconomic conditions and fostering output growth. In addition, only fiscal and monetary measures were part of this first effort; it was an incomplete package that minimized the role of labour and social policies.

**Fiscal measures**: Fiscal austerity was at the centre of the fiscal objective of this first policy phase. The Congress passed two laws in this direction: i) the Fiscal Responsibility Law in September 1999 committing to large reductions in both federal and provincial government spending; and ii) the Zero Deficit Law in July 2001, requiring a balanced budget by the end of 2001. As a result, large reductions in Government spending were carried out in 2000 and 2001 in hopes that fiscal responsibility will bring renewed confidence to economy.\(^\text{18}\) The economy did not rebound due in part to these measures and as federal revenue transfers continued to decline, the government decided to use provincial bonds as titles to pay public salaries – which deteriorated even further the position of aggregate demand as a trigger for economic growth.

**Monetary measures**: The first voluntary restructuring of debt was carried out during this phase (June 2001). It aimed at raising liquidity through an exchange of short-term debt for new debt with longer maturities although at higher interest rates. In addition, the peso was allowed to devaluate – for the first time since the peg was established – 7 per cent (peso exchange rate was priced 50/50 dollar-euro peg) for activities related to foreign trade in hopes of improving Argentina’s international competitiveness.

… but a radical shift in the approach drove the recovery – both in terms of growth and employment.

The second phase of crisis related efforts had a totally different approach. Since this phase started with the crush of macroeconomic indicators and the peak of social unrest at the end of 2001, policies during this phase were more targeted, coordinated and decisive. The package assured success because it was comprehensive. It comprised monetary and financial policies, an important and varied set of fiscal measures, and labour market and social protection measures.

**Monetary measures**: The first monetary policy put in place during this new phase was the reversal of the Convertibility regime and devaluation of the Argentinean peso – effective in January 2002. This produced a shift in relative prices, which bolstered the first stages of recovery through an increase in exports but also through the increase in local production and imports substitution. Later in Q1 2002, the peso was led to float which provoked a

\(^{18}\) Another objective of this measure was, however, to meet the conditions for a three-year stand-by arrangement with the IMF for 7.2 billion dollars.
real exchange rate overshooting during the first semester 2002 (RER rose 180 per cent). Although this erratic exchange rate policy was harmful for the financial sector, the exchange rate started to stabilize by July 2002 thanks to foreign exchange market stabilization.

Financial measures: The first stages of recovery occurred in a context of financial instability. Financial variables were following a conflicting path fuelled by past devaluation expectations and fear of default that let the public to withdraw deposits massively. Facing this reality, the first governmental measure was liquidity support for the banking sector. Yet, negative expectations on the sector did not improve. Thus, to avoid further run on banks, a bank holiday was decreed for three weeks and further measures to limit withdrawals were implemented upon their reopening.

Fiscal measures: One of the main pillars of the fiscal policy package during the recovery phase was a strong commitment to adjustment in the fiscal accounts and the balance of payments. Yet, this was not done through a decrease in government spending, like during the recession period. On the contrary, an important step in this direction was the temporary default of the public debt (announced at the end of 2001). It reduced substantially the nominal amount of public financial liabilities and also the interest rate, increasing at the same time maturity. Another contribution to fiscal consolidation was the income effect of the peso devaluation that the government was able to capture through export taxes.

The other key pillar of the fiscal front was linked to the design and management of labour and employment policies aimed at stimulating private consumption. Three were the main goals the government had in mind when including labour policies at the centre of the fiscal efforts:

- Strengthening employment: The most significant measure in this direction was the Unemployed Heads of Household Plan (Plan Jefes y Jefas de Hogar Desocupados) launched in May 2002. It constituted a transfer of income in return for work, which provided income to about 2 million beneficiaries at a cost of 1 per cent of GDP by October 2002. It is estimated that 25 per cent of those beneficiaries were incorporated in the formal labour market and that indigence was reduced by 29 per cent (Ministerio de Trabajo, Empleo y Seguridad Social, 2002). Another significant plan was the Integrated Employment Promotion Plan “More and Better Jobs”, which promoted entry into quality jobs and training of unemployment workers.

19 The partial default on debt was the second effort of improving the public fiscal position through debt renegotiation. The first effort in this direction was a voluntary debt swap announced in November 2001 that exchanged bonds with average interest rates of 11-12 per cent for extended maturity notes at only 7 per cent.

20 A similar plan called Work Plan (Plan Trabajar) existed already during the nineties. It was a plan aimed at workers in temporary employment which gave recipients 200 pesos per month, access to health care and coverage of risks. Overall, this and other social and employment plans benefited about 140,000 workers in the peak year (1997).
• Reducing income inequalities: A set of income policies was also developed in order to equilibrate income distribution. As part of this effort: i) the minimum living and adjustable wage (salario mínimo, vital y móvil – SMVM) was recovered after it was abandoned during the 90s. Thanks to this approach, the minimum wage increased by 300 per cent during the period 2003-06. ii) the increase in the minimum pension (haber mínimo jubilatorio – HJM) also became a strategic resource in crisis policy formulation. The HJM rose by 114 per cent from December 2003 to June 2006.

• Strengthening of labour institutions: Two major efforts were put in place to restore the institutional foundations lost during the 90s: (i) Law No. 25,877 that set out for the first time the promotion of decent work as a priority objective, passed in 2004 (Damill, et al., 2007). The law had clauses promoting collective agreements and also provided with differential treatment for social security contributions for small- and medium-sized companies. And, (ii) a National Plan for the Regularization of Work (Plan Nacional de Regularización del Trabajo – PNRT) was launched to increase registration of jobs. Between 2004 and 2006, around 400 thousand firms and one million workers were inspected.

C. Evaluation and lessons from labour market policy

Although the crisis that hit Argentina in the 2001 was unprecedented, so too was the recovery. Indeed, output and labour market contraction came to an end and the recovery was under way one quarter after the devaluation and the default. Various factors have influenced the fast recovery of the crisis. Macroeconomic policies had a key role in alleviating the negative impacts of the crisis, especially the shift in relative prices caused by the devaluation and policies targeted towards stabilizing the trade market and recuperating the basic macroeconomic equilibrium. 21 The favourable economic environment also played an important role – although only as a catalyst – as an increase in export prices and decline in foreign interest rates contributed to consolidate a new economic expansion.

However, a sustained recovery could not have been achieved by the mere application of macroeconomic policies on the hope that external conditions would remain stable. A correct and timely mix of policies was key for an efficient policy response. In this regard, there are two main lessons to be learned from the 2002 crisis in Argentina:

• Untargeted and incomplete crisis related efforts are unsuccessful and may even be detrimental to economic recovery and social goals. This was the case in Argentina, where fiscal austerity measures combined with monetary measures put forth to tackle the recessionary period of the 90s proved unsuccessful in stabilizing macroeconomic

21 For more information on this, please see: Damill, et al., 2007 and International Monetary Fund, 2003.
conditions and fostering output growth. Indeed, premature austerity and the absence of labour market measures reinforced the downward spiral of deteriorating social conditions. Indeed, levels of poverty, unemployment, income distribution, informal work, and other social variables drastically worsened.

- A fundamental consideration with regards sustainability of economic growth is the role of social and employment measures put in place during the crisis to absorb and accommodate the shock and trigger economic and labour market recovery. In this regard, the second phase of the crisis related efforts proved successful because measures were more targeted, coordinated and decisive. The package assured success because it was comprehensive. It comprised monetary and financial policies, an important and varied set of fiscal measures, as well as labour market and social protection measures. Indeed, labour programmes were effective in addressing the poverty effects of the crisis and fostering employability. This is the case of the Plan Jefes y Jefas, which is estimated to have reduced aggregate unemployment by about 2.5 percentage points between 2001 and 2002 (Galasso et al, 2003).

What is more, empirical evidence of the effectiveness of labour and social policies in boosting employment during past crises supports these conclusions. These results have been estimated by way of an econometric analysis of the impact of government expenses in social assistance, the provisional system and family allowances on employment creation (See Appendix A for methodological considerations). The study depicts two types of government-spending multipliers: one that measures the effect of fiscal expenses during the average moment of the economic cycle, and another that assesses the same effect but during times of crisis. The analysis finds that:

- Of the three types of government spending, the one in social assistance has the highest estimated impact on employment creation both during past economic shocks but even during the average moment of the economic cycle.

- Moreover, government spending in the provisional system seemed to have had a positive effect in boosting employment only when implemented during economic shocks, which means only when implemented counter-cyclically.

- These findings are especially important for the case of Argentina given that social assistance and social prevision corresponded to over 40 per cent of the total social spending of the Government during the crisis years (1994 to 2004).

Noteworthy, the social policy responses and programmes laid during the 2001-02 crisis, which were reinforced after the economic turmoil and produced subsequent government reforms, were key in today’s crisis (see also Chapter 5). Indeed, the ability to respond quickly during this crisis in Argentina was unprecedented and had a
definite role in supporting broader recovery. This could not have been possible without the automatic stabilizers already in place.\textsuperscript{22}

The lessons learned from the Argentinean case are all the more relevant for EU countries now that the financial crisis has entered a new phase characterized by concern over fiscal consolidation. As such, pressures to cut spending, in particular on pro-employment programmes, are growing, which is only likely to delay the employment recovery further exacerbating the challenge for policy makers to build and ensure a sustainable and inclusive overall recovery.

\textsuperscript{22} Indeed, various empirical studies have suggested that the most successful labour market policies are those that were already in existence before the crisis (see for example, Eichhorst, 2010).
Appendix A – Effects of government expenses in labour and social measures on employment growth: An empirical approach

Section C analyzed the government-spending multipliers of the different labour and social policies put in place during the 1997 crisis in Korea. These government-spending multipliers illustrate the influence of government expenses in labour and social measures on employment growth during past crises. They were estimated following equation (1), based on Barro and Redlick’s model to assess the effects of military spending and taxes on real per capita GDP growth rate.23

\[
\Delta E_t = \beta_0 + \sum_{i=1}^{n} \beta_{g_i,t} \Delta g_{i,t} + \sum_{i=1}^{n} \beta_{I_i,t}(\Delta g_{i,t} \cdot x_{t-1}) + \omega_{t-1} + \epsilon_t
\]

Where \( \Delta E_t \) represents the growth rate of employment in time \( t \); \( \Delta g_{i,t} \) is the growth rate of government spending24 in each labour and social measure in time \( t \); \( n \) corresponds to the number of measures included in the analysis, in this case \( n=3 \) since three types of measures were included in the empirical model: social assistance, the provisional system and family allowances. Moreover, \( \beta_{g_i,t} \) is the government-spending multiplier, which shows the percentage increase in employment produced by a 1 per cent increase in spending on each labour and social measure. The goal of the analysis is to assess if/which coefficients are greater than 0, which will imply that an increase in labour and social spending is associated with employment creation at all moments of the economic cycle. However, often these coefficients are not significant given their very low relative size. In fact, previous evaluations of policies in OECD countries indicate that labour programs usually have at best a modest impact on participants’ labour market prospects (Heckman et al, 1999).

To gauge the slack of the economy, the equation considers the lagged output gap, \( x_{t-1} \). The output gap is measured as actual output minus potential output and is expressed as a percentage of potential output. As expected, the output gap is highly significant and has a positive relationship with employment growth in our analysis. In addition, interaction terms between the output gap and the different variables for government spending were added to the equation in order to measure how the multipliers perform differently depending on the functioning of the economy. Since the output gap is negative when actual performance is less than potential, a negative coefficient on the interaction term shows that labour policies are counter-cyclical, when the coefficient for government spending corresponding to that interaction term is greater than 0.

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24 Note that the real government spending in social measures is considered here; yet, we deflate \( g_t \) using the GDP deflator so as the units of \( y \) and \( g \) are comparable and \( \beta_1 \) reveal the effect of an extra unit of government spending on employment.
Finally, $\omega_{t-1}$ represents a set of time-lagged variables of the demand for labour (2). The inclusion of this set of variables keeps the dynamics of the labour market from influencing the estimated coefficients of the fiscal variables.

Labour demand is represented by the following equation:

$$(2) \quad n = \lambda_0 + \lambda_1 w + \lambda_2 q + \lambda_3 t$$

Where $n$ and $q$ are the natural logarithms of labour input ($N$) and output ($Q$), respectively, and $w$ is the natural logarithm of the real product wage. These are incorporated into the first equation in a lagged form, as follows:

$$(3) \quad \omega_{t-1} = \beta_3 \Delta E_{t-1} + \beta_4 \Delta y_{t-1} + \beta_5 \Delta w_{t-1}$$

Where, $\Delta E_{t-1}$ is the annual lag of the dependant variable; $\Delta y_{t-1}$ is the previous year’s Real GDP growth; and $\Delta w_{t-1}$ is the growth rate of the compensation of employees.

In this way, an average of 14 observations were included in the analysis with information on employment growth and government spending in social assistance, the provisional system and family allowances since 1994 until today. The analysis finds that:

- The estimated impact on employment creation of an increase in government spending on social assistance is relatively important and highly significant. This is the case during normal times, but also during economic shocks, i.e. when interacting with the output gap.
- Government spending in the provisional system seemed to have had a positive effect in boosting employment only when implemented during economic shocks, which means only when implemented counter-cyclically.
- Government spending on family allowances, on the contrary, seems to have had a negative impact in employment creation both when implemented during the economic shock and during normal times.

Table A1 gives a synthetic review of the econometric estimates reporting these government-spending multipliers.

To take into account the peculiarities of the data set, regressions have been rerun to account for robustness. As can be seen in the different panels of Table A1, government-spending multipliers in times of crisis ($\beta_{g_{ann}}$) remain highly significant and the absolute size of the estimated effects changes relatively little between different estimation methods.

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25 This variable although included in the analysis, turned out not to be statistically significant once the output gap variable is included.

26 This conclusion does not come as a total surprise since several authors (see for example, Layard et al., 1992; OECD, 1991; and OECD, 1994) have found already that PLMPs might have a positive effect on unemployment when policies are not well instrumented or when programmes (such as too generous unemployment benefit systems) extended for excessively long periods.
giving some confidence in the estimated effects. To ensure that one or some of control variables did not influence the results, reduced regressions were also estimated by excluding the variables one at a time.

Moreover, despite the short time series available for analysis, there is not an important difference between the R-squared and Adjusted R-squared diagnostic statistics. This gives some confidence to the analysis made and shows that even after having made adjustments on the degrees-of-freedom, the model was not penalized with an important loss of parsimony.

### Table A1. Regression results and alternative estimators

<table>
<thead>
<tr>
<th></th>
<th>OLS (Baseline)</th>
<th>OLS (Robust)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Lag 1 of Government spending in Social Assistance (Annual growth rate)</td>
<td>0.303</td>
<td>0.303</td>
</tr>
<tr>
<td></td>
<td>(8.92)**</td>
<td>(10.83)**</td>
</tr>
<tr>
<td>Interaction term for Social Assistance</td>
<td>0.012</td>
<td>0.012</td>
</tr>
<tr>
<td></td>
<td>(4.15)*</td>
<td>(3.25)*</td>
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<tr>
<td>Lag 1 of Government spending in Provisional System (Annual growth rate)</td>
<td>0.086</td>
<td></td>
</tr>
<tr>
<td></td>
<td>(1.74)</td>
<td></td>
</tr>
<tr>
<td>Interaction term for Provisional System</td>
<td>-0.029</td>
<td>-0.029</td>
</tr>
<tr>
<td></td>
<td>(-6.36)**</td>
<td>(-4.52)*</td>
</tr>
<tr>
<td>Lag 1 of Government spending in Family Allowances (Annual growth rate)</td>
<td>-0.336</td>
<td>-0.336</td>
</tr>
<tr>
<td></td>
<td>(-7.39)**</td>
<td>(-6.63)**</td>
</tr>
<tr>
<td>Interaction term for Family Allowances</td>
<td>-0.075</td>
<td>-0.075</td>
</tr>
<tr>
<td></td>
<td>(-9.90)**</td>
<td>(-11.69)**</td>
</tr>
<tr>
<td>Lag 1 of Output gap</td>
<td>0.91</td>
<td>0.91</td>
</tr>
<tr>
<td></td>
<td>(6.94)**</td>
<td>(8.56)**</td>
</tr>
<tr>
<td>Real GDP (Annual growth rate)</td>
<td>0.27</td>
<td>0.27</td>
</tr>
<tr>
<td></td>
<td>(5.49)**</td>
<td>(6.1)**</td>
</tr>
<tr>
<td>Compensation of Employees (Annual growth rate)</td>
<td>0.177</td>
<td>0.177</td>
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<tr>
<td></td>
<td>(6.23)**</td>
<td>(8.46)**</td>
</tr>
<tr>
<td>Constant</td>
<td>-3.26</td>
<td>-3.26</td>
</tr>
<tr>
<td></td>
<td>(-4.3)*</td>
<td>(-4.94)*</td>
</tr>
<tr>
<td>Observations</td>
<td>14</td>
<td>14</td>
</tr>
<tr>
<td>R-squared</td>
<td>0.987</td>
<td>0.987</td>
</tr>
<tr>
<td>Adjusted R-squared</td>
<td>0.942</td>
<td></td>
</tr>
</tbody>
</table>

Estimated based on ordinary least squares. Absolute value of t-statistics in parentheses. Significance levels: *significant at 5 per cent; **significant at 1 per cent. (1)
References


Roxana, M.; Perrot, B.; and Villafañe, S. 2008. *How important were social and labour market policies in reducing poverty across different families in Argentina? A dynamic approach.* Ministry of Labour and Social Security or Argentina.


