How Argentina's provincial governments operated, after the country's debt default in 1998, has many possible lessons for Greece now

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The prospect of a Greek exit from the Euro, or of Greece defaulting on its government debts, has created huge anxiety because both appear to be steps into the complete unknown. However, **Mark Hallerberg** *argues that looking at the potentially similar case of Argentina's debt default can suggest interesting temporary solutions. From 1998 to 2001 Argentina's provinces coped with many after-shock problems by issuing their own regional currencies. A similar approach might work to mitigate the worst effects in Greece.*

The recent debate about the Greek predicament after the May 6 elections has again turned to whether Greece should stay in the Eurozone. When the question first came up two years ago, there were suggestions for some sort of interim solution. Martin Feldstein (2010) argued that Greece should only temporarily leave the Eurozone. Julian Le Grand has suggested on this blog that the country could leave, but then instantly rejoin the Eurozone at a devalued level. Reflecting on the Argentine example, de la Torre et al suggested that direct bailouts would be preferable to the route that Argentine provinces took when they issued their own currencies pegged to the peso in the run-up to the collapse.

While EU authorities and the IMF have taken that advice not once but twice, and while the second bailout included significant debt restructuring, the country remains in trouble. There are three immediate problems facing Greek authorities. The first is that, despite the debt 'haircut' a few months ago, the Greek debt level remains very high at about 160 per cent of GDP. This makes it difficult to get to the primary surplus the troika (the EU, IMF, and the European Central Bank) would like to see in place. The second issue is an uncompetitive economy. Real wages will have to continue to fall. Note that both problems require time to address, probably 3-5 years at a minimum. The third problem is political – the population has severe reform fatigue.

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The Argentine example from 1998 to 2001 may yet be instructive for the Greeks and address all three problems. The provinces issued their own currencies at the time and paid their workers as well as their bills in these currencies. Crucially, they also pegged their new currencies to the national currency, the peso. Nominal wages remained the same.

These policies of course did not end the crisis. A big problem in Argentina's case was that too many provinces took this step; as de la Torre et al note, the quasi-monies in the Argentine case did not lead to a devaluation, and a run on the peso in any case led to a monetary contraction, which had the opposite effect intended. In Europe's case, however, there would be plenty of remaining euro liquidity and the ECB would have every incentive to maintain that liquidity for the rest of the Eurozone, something the Argentine central bank in the end could not do and the international community was not interested in doing to help Buenos

Aires. Would it make sense for one country in Europe to follow the same route as the sub-national governments of this southern country did? [Thomas Mayer](#) from Deutsche Bank has also raised this issue recently in his call for a 'geuro', and the Argentine example suggests that such a move could make sense.

Imagine the following scenario. The government issues quasi-notes, which are known as 'Ploutos' (named after the god of wealth). The government pays its employees and those who have debt against the government in Ploutos instead of Euros. Moreover, the government issues a promise on the bills that Ploutos will be fully convertible into euros in 5 years. These Ploutos are also fully transferable. As in the Argentine provincial case, the government will also accept them for the payment of taxes and services.

What are the economic effects? Because there is uncertainty about the ability of the government to fulfill its obligations and because of opportunity costs, these bills trade at a discount. This means in practice a real salary cut in the wages of public workers. Because some of these notes will disappear over time, they provide the government with some amount of seignorage. (Technically seignorage is the revenue obtained directly by the government from minting coin or printing notes, which is the difference between the cost of metal or notes and their face value. Here seignorage arises because the government realizes more value from the notes it has issued than it actually has to make good on). In the Argentine case, nominal salaries remained the same, and governments could pay on time. The payment in these quasi-moneys generated less discomfort in the population than the reduction in nominal salaries that the Argentine federal government instituted, and which the government had to reverse later on in the crisis.

What about the political effects? One would think there would be more riots in the streets as angry civil servants take to the barricades. This may happen, but matters were not so dire in Argentina. Initially, the anger was turned on the private sector for not accepting the various scripts, not at the provincial government for issuing them. Eventually most businesses took them, and, because the government would accept them at face value for taxes, they knew they could move the script.

One should be realistic about what this course of action does and does not do. Foreign debts in Greece that are denominated in euros would remain as onerous as before. So the move does not on its own solve the country's competitiveness problem. In fact, because the currency should return to par in five years, it is not a longer-term devaluation. This is not a bazooka or magic bullet.

A key aspect of this proposal is that it buys the government time to continue reforms. It provides a limited internal devaluation that does not imply a full rewriting of contracts in the private sector and the economic damage that implies with a full euro exit. Moreover, because these bills become fully convertible into euros at a fixed time in the future so long as the government keeps its promises, it provides identifiable winners in Greek society from reforms. Greece sorely needs a political constituency to support the reform effort, and this proposal would make many more people clear winners.

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