Wall Street loots Argentine workers' pensions

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One of the most important but least known aspects of the current Argentine crisis is the looting of workers' pension funds by the Buenos Aires government, local banks and Wall Street. Billions of dollars in savings by public employees and other workers are to be put up as collateral as part of the government's "patriotic call" to rescue Argentina from defaulting on its $130 billion foreign debt.

The prospect of default has thrown the government and the Argentine bourgeoisie into panic. In order to appease foreign investors, President Fernando De La Rua last month imposed an unpopular "zero deficit" plan that cuts salaries and pensions by 13 percent, while raising taxes.

Argentine workers have responded to these measures with several one-day general strikes that paralyzed Buenos Aires, a metropolitan center of 12 million people. Schoolteachers went on strike the same day children returned to classes. The strike wave includes hospital workers and doctors. The unemployed, who make up 16 percent of the working population, are staging a series of roadblocks, bringing traffic to a standstill. The jobless have also occupied government buildings and fierce confrontations with the police are taking place.

The chief of police expressed fear that the city's 18,000 policemen are unreliable because half of his men live below the poverty line and are suffering from the cuts. He warned that his forces could defy orders to repress the unemployed movement, saying it would be a confrontation of "the poor with the poor."

The crisis of confidence in the Argentine financial system has affected broad masses of people. The Argentine daily *El Clarín* estimated that close to "$7.4 billion in deposits, or about 9 percent" were lost in July "as Argentines withdrew their savings out of concern that the government may default on its debt or devalue the currency by breaking a decade-old fixed exchange rate with the US dollar." Due to withdrawals, the banks lost approximately "$354 million a day," according to *El Clarín*.

In the 1990s, the Peronist government of Carlos Menem carried out a program of privatizations, deregulation and the Convertibility Plan—tying the value of the Argentine peso directly to the US dollar—which it claimed would bring prosperity to Argentina. While these measures produced handsome profits for foreign banks and enriched a tiny elite of Argentine bankers and businessmen, it did so at the expense of the masses.

Because these measures are similar to those undertaken throughout the so-called "emerging markets" over the past decade, the way in which Argentina's private pension funds are being looted to save the country from default is a warning to workers internationally. Similar measures are being prepared in the major capitalist countries, such as the US, where George W. Bush has proposed changes in the structure of the Social Security system to allow workers to "bet" their savings in the volatile stock markets.

Under conditions of a sustained growth in the world's stock markets in the 1990s, Menem's policies of privatization and deregulation succeeded in attracting foreign investors to Argentina. The privatization of state-owned enterprises provided the government with billions in cash. While a sizable share of this income was siphoned off by corruption, it also created a temporary period of growth, with the Argentine GDP rising by 8.7 percent in 1992, 6 percent in 1993 and 7.4 percent in 1994. It fell by 4.6 percent in 1995, due partially to the Mexican crisis, but rose again in 1997. With the Asian crisis the following year, economic output declined sharply, and hasn't recovered since.

A central piece of Menem's economic program was the creation of private workers pension funds, called Insurers of Retirement and Pension Funds, and known by the Spanish acronym AFJP. The ostensible purpose of the AFJPs was to generate domestic savings to further economic growth and job creation.

But instead of long-term investment in industry, what dominated the Argentine economy for most of the 1990s was the churning of the stock market by what are known in Spanish as "fondos golondrinas," or "swallow funds"—because, like swallows, they freely fly in and out. The removal of all restrictions on foreign investment and capital repatriation created the opportunity for foreign capital to make a quick profit and leave the country as soon as the situation deteriorated, making Argentina ever more susceptible to international crises.

Under these ground rules, the AFJPs fell prey to the insatiable greed of foreign and domestic capital. For the past several years, the funds received about $300 million in monthly contributions from workers. This money, which today amounts to tens of billions of dollars, was invested primarily in the Argentine stock market and government bonds. Thanks to the AFJPs, Argentina boasts the largest domestic debt and securities markets of any of the so-called "emerging market" countries.

In the early 1990s, foreign banks quickly jumped in, offering sophisticated derivatives products that allowed the AFJPs to invest in virtually any market in the world. Wall Street took advantage of the inexperience of the funds' managers. The AFJPs regulatory body incorrectly estimated the dollar value of these products, allowing foreign banks to overcharge for them and reap enormous profits. (Had the US banks done such deals with inexperienced US clients, they could have been sued and found guilty, as Bankers Trust was sued by Procter & Gamble and other US customers.)

Argentine local banks also found a way of profiting from workers' pension funds. The fluke in pricing by the AFJP

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regulators allowed local banks to borrow at sub-LIBOR rates (below the base interest paid on deposits in the Eurodollar market). Next, the banks invested the borrowed money in Argentine bonds that paid LIBOR plus a significant spread due to Argentine risk. (The spread above LIBOR measures the risk that a country may default. Thus, the higher the risk of default, the higher the spread a country has to pay for borrowing money.)

This operation was made possible through the creation of a floating rate certificate known in Spanish as DIVA—for Variable Interest Deposit—that the local banks sold to the pension funds.

A DIVA is essentially a bet in the stock market. If, at the end of a two-year period, stocks appreciate, the funds receive huge returns, but if instead stock prices remain the same or decline, the funds receive zero interest on their investments. The DIVA program was a partnership between local and foreign banks—the locals issued the debt certificates and Wall Street banks provided the return on the investment, if any. Since most DIVA returns were linked to the Buenos Aires stock market index, the MERVAL, which has been in decline since the Asian crisis in 1998, an amount in the order of $1 billion in DIVAs ended up paying zero interest.

Thus, the end result of the DIVA program was: (a) as long as the Convertibility Plan remained in place, guaranteeing parity between the Argentine peso and the US dollar, local banks were borrowing as if they were a risk as good as the US government, and lending to an emerging market—Argentina—without taking any emerging market risk, netting the whole spread as profits; and (b) the pension funds got zero return on their investments.

As if the DIVA fraud was not enough, the abuse of the pension funds continues today, with De La Rua’s plan calling upon the AFJPs to play a central role in saving the country from default. Of the $4.8 billion the government plans to raise to remain afloat, the lion’s share is to come out of the AFJPs. The pension funds will contribute $2.3 billion between August and December.

According to *El Clarín*, AFJP contributions “will begin in August with $650 million—$250 million on August 3, $150 million on August 9 and $250 million by the end of the month.”

“In exchange,” writes *El Clarín*, the pension funds “will receive trust certificates to a special fund with Argentine bonds as the main assets. The trust will mature on 2006. This financial engineering was used to allow AFJPs to invest in Argentine bonds at levels above the limits imposed by law.”

Just as foreign and local banks abused the AFJPs during the 1990s to reap super-profits, now the Argentine government in the name of “patriotism” will exploit the retirement accounts of the Argentine people in order to avoid, or postpone defaulting on its debt.

Not only will retired workers see their monthly checks cut by 13 percent as the “zero deficit” plan is implemented, but the pension funds themselves, upon which their retirements depend, are being mortgaged to the success of the De La Rua government.

If Argentina goes under, the billions in government bonds held by the AFJPs will dramatically lose value. Thus, if the “zero deficit” plan succeeds, workers will suffer disastrous wage cuts; and if it fails, it could take workers pension funds down with it.

One might think that with the threat of an Argentine default—and its dangerous implications for the world financial system—Wall Street banks would proceed with caution. On the contrary, US and European finance houses are searching for new ways of profiting off of the crisis by making deals that threaten to bring Argentina even closer to the brink.

Thus, the bond market stumbled recently when an unidentified US bank failed to deliver $30 million in floating rate Brady bonds (FRB) to a local Argentine bank. In a purely speculative trade, the US bank had agreed to sell bonds that it didn’t have, betting that their value would decline due to the Argentine crisis by the time it had buy and deliver them. The bank relied on being able to “lease” the bonds on the market, but found that there were no more bonds to be had because other foreign banks were speculating in the same fashion.

While Argentina’s finance minister Domingo Cavallo has threatened to impose restrictions on bond trades to put a halt to these speculative transactions, *El Clarín* warned that any regulatory measures could anger Wall Street, and that investors “may stop trading Argentine paper altogether,” intensifying the crisis.

The first government to develop a private pension fund system in Latin America was the ruthless regime of Augusto Pinochet in Chile, as part of an economic program designed by Milton Friedman and his “Chicago boys.” The Chilean model became successful mainly because it was imposed upon the working class at the point of a gun. Currently it is in use in Argentina and Peru and increasingly European governments invoke the policy as a means to dismantle the welfare state.

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