Commitment Devices with Time Inconsistency Disease and Institutional Anomie

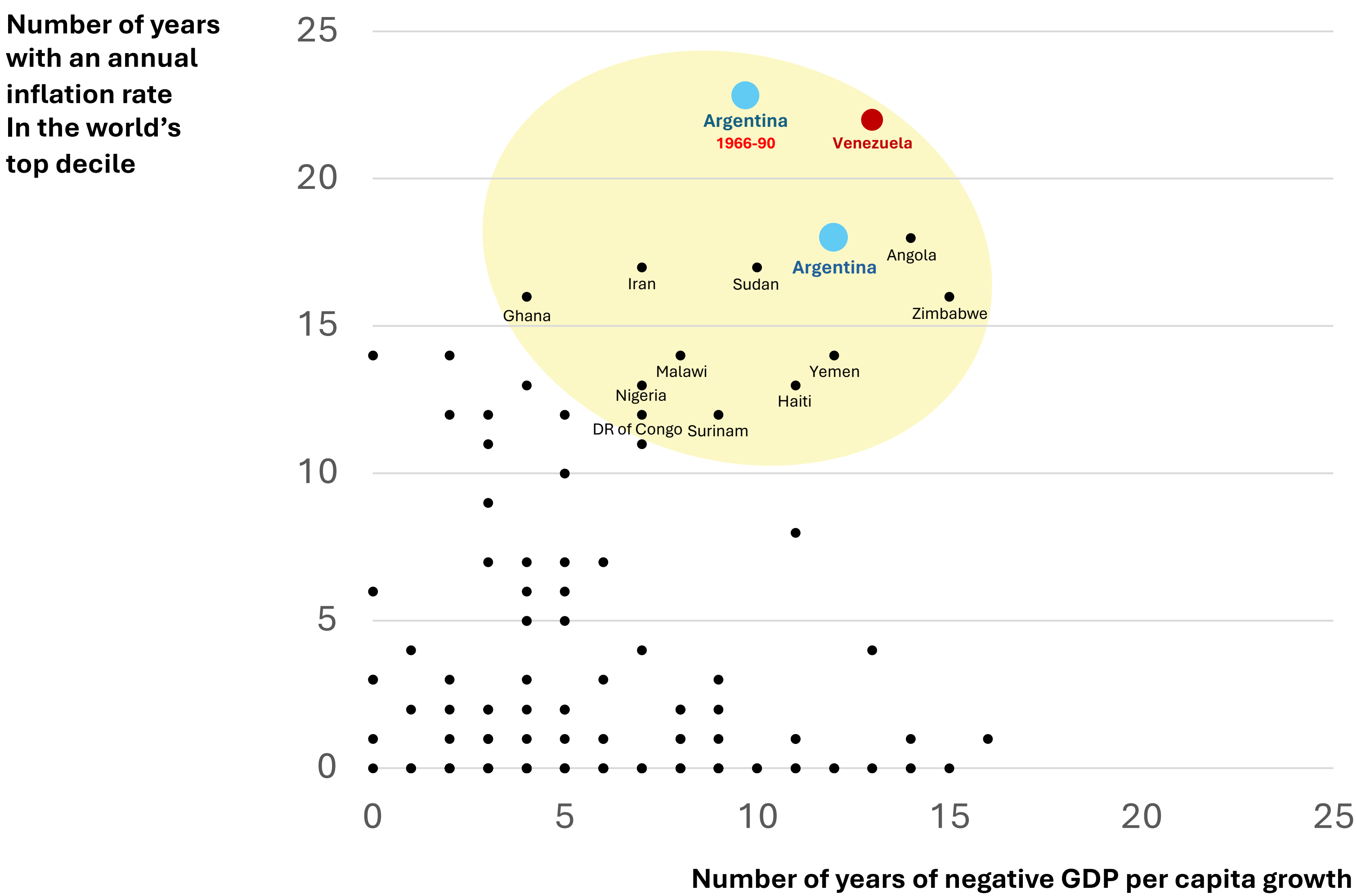
The Case of Argentina

Emilio Ocampo

May 2-3

Hoover Annual Monetary Conference

The World Champions of Stagflation 1999-2023



Source: Author based on latest IMF WEO and World Bank WDI data.

Time Inconsistency Disease

"**Argentina** is my prime example of a country that suffers from what I call the time inconsistency disease.

Policy seems to be very short run-oriented, which is bad for long run sustainable growth.

You see it in monetary policy but also in fiscal policy."

Finn Kydland (2004)

Is Time Inconsistency Disease Curable?

"An interesting question is: if a nation, such as Argentina, falls prey to the time inconsistency disease, how easy is it to rebuild its credibility?

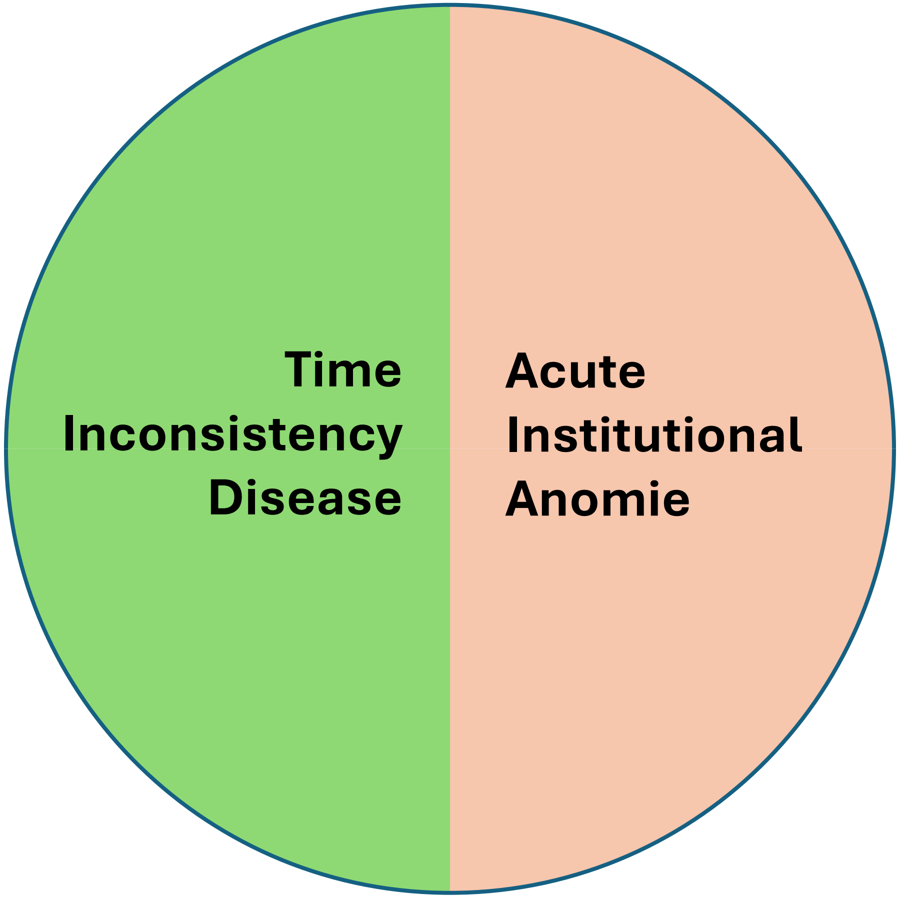
The answer has to be, **not easy at all**."

Finn Kydland (2004)

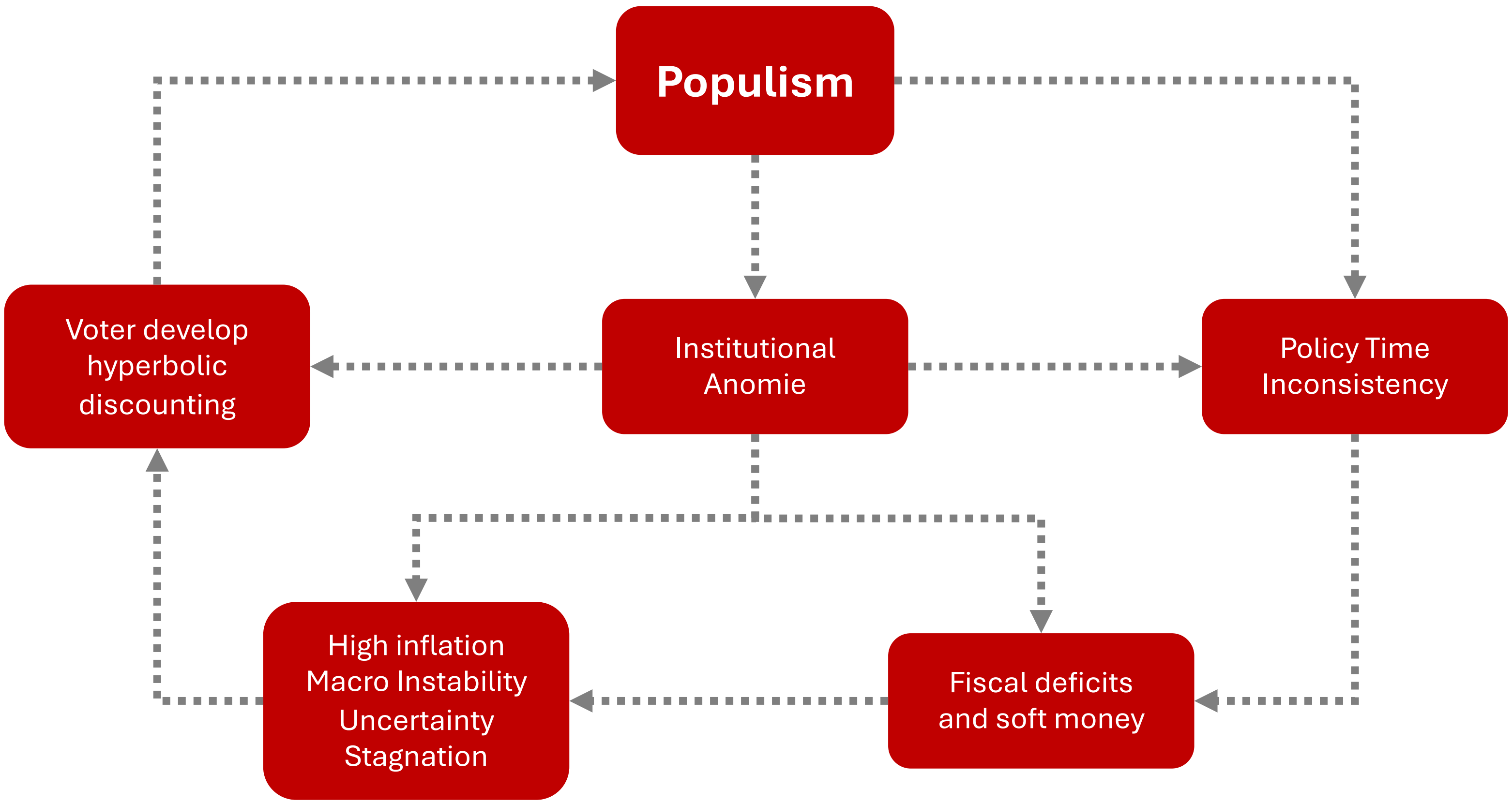
Difficult when Institutional Anomie Prevails

- The term originated in Nino (1992) and Waldmann (2004)
- Weak separation of powers → Executive Overreach
  - Laws are ignored, abrogated or modified *by the* Executive
  - **Executive does not enforce the laws, it is the main law-breaker**
- Congress and Judiciary passive enablers
- No formal ECD can exist under local jurisdiction
- **Acute institutional anomie tends to be associated with endemic populism**

Two Sides of the Same Coin



Populism and Institutional Anomie: A Vicious Cycle

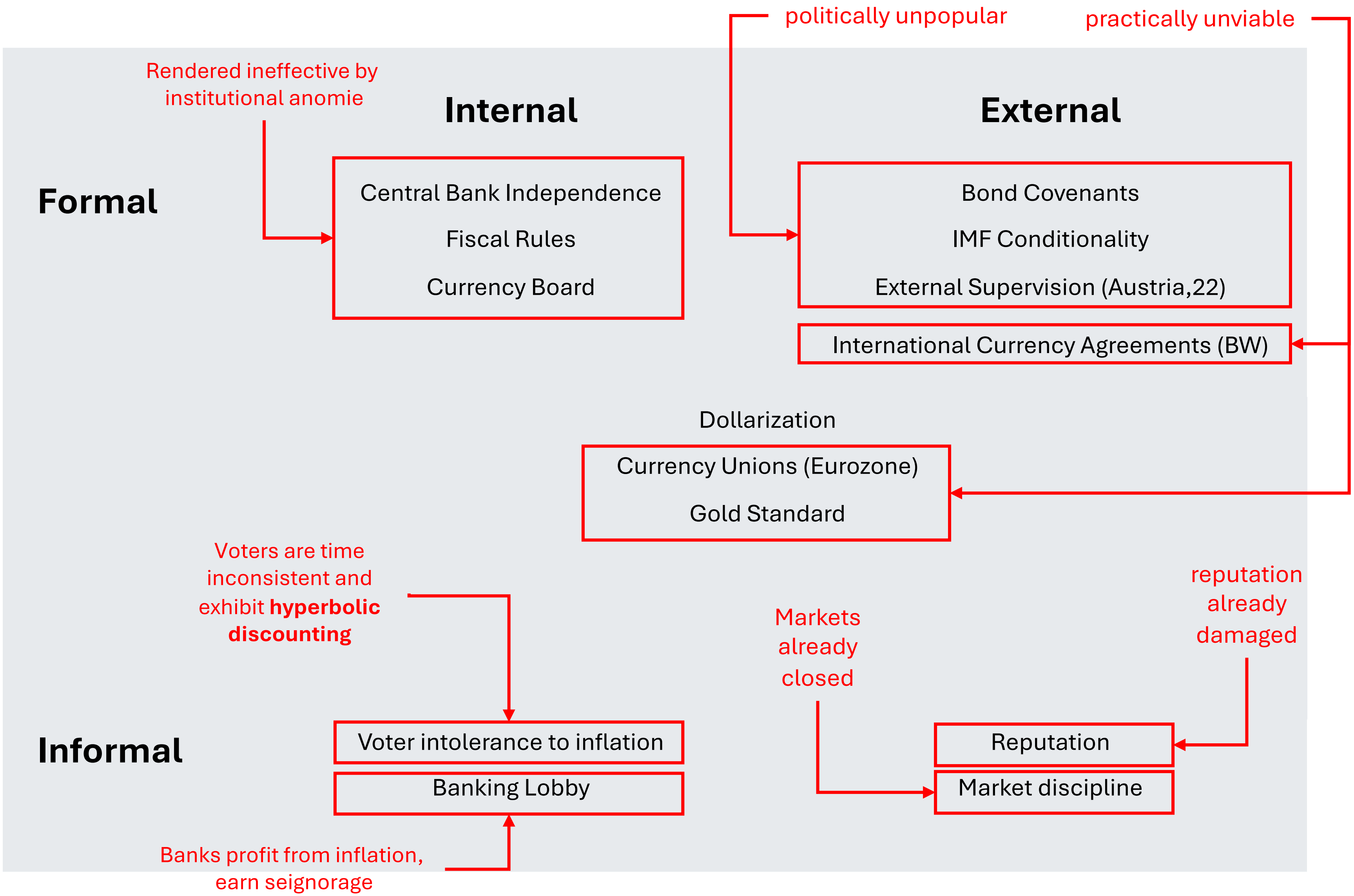


CDs as a cure for Time Inconsistency

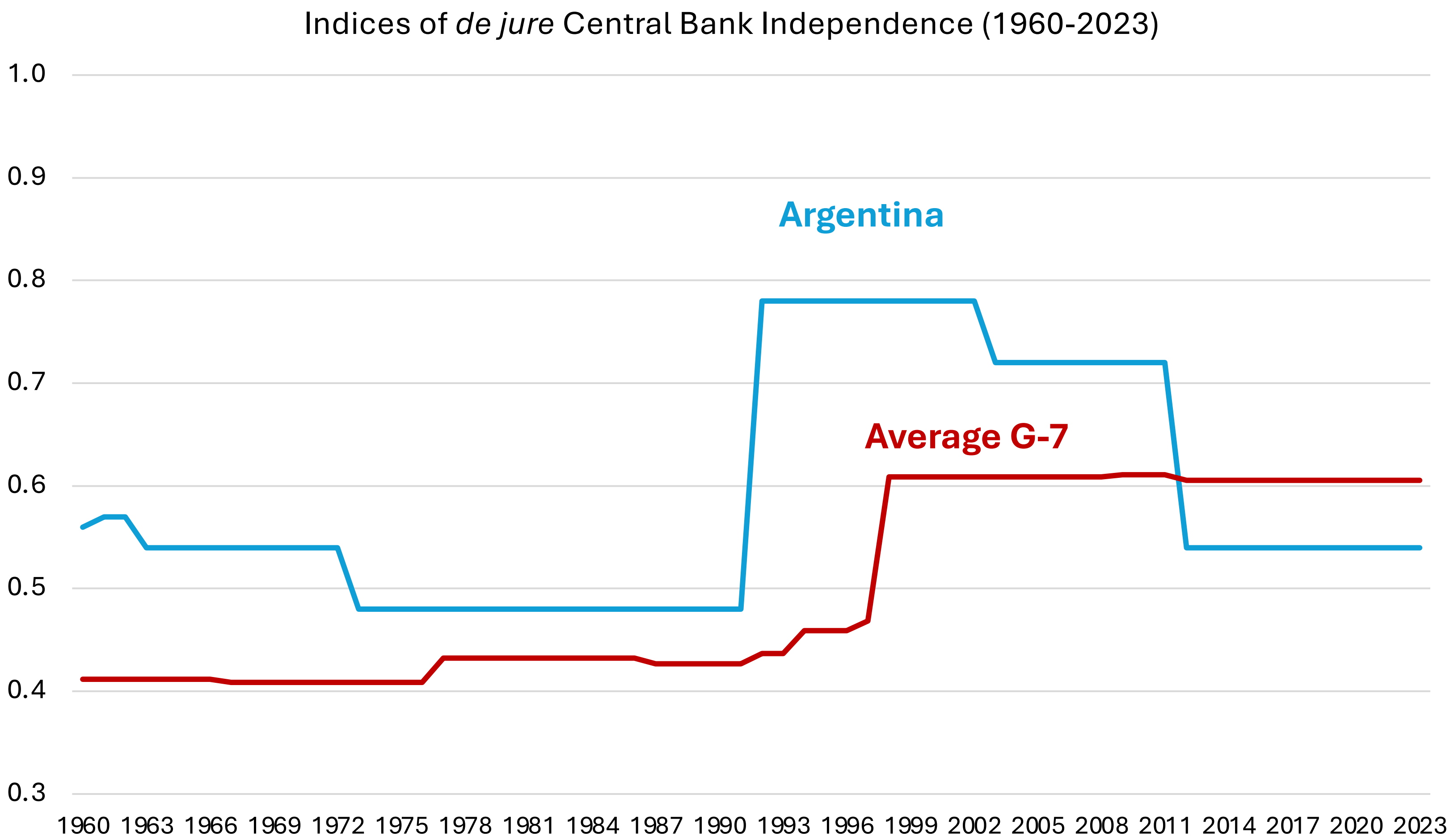
A Menu of Commitment Devices (CDs)

<table>
<tr><th></th><th>Internal</th><th>External</th></tr>
<tr><td rowspan="2">Formal</td><td>Central Bank Independence (CBI)
Fiscal Rules
Currency Boards</td><td>Bond Covenants
IMF Conditionality
External Supervision (Austria,22)
International Currency Agreements (BW)</td></tr>
<tr><td colspan="2">Dollarization
Currency Unions (Eurozone)
Gold Standard</td></tr>
<tr><td>Informal</td><td>Voter intolerance to inflation
Banking Lobby</td><td>Reputation
Market discipline</td></tr>
</table>

Menu of Commitment Devices



Evidence of Institutional Anomie:
de facto CBI < *de jure* CBI

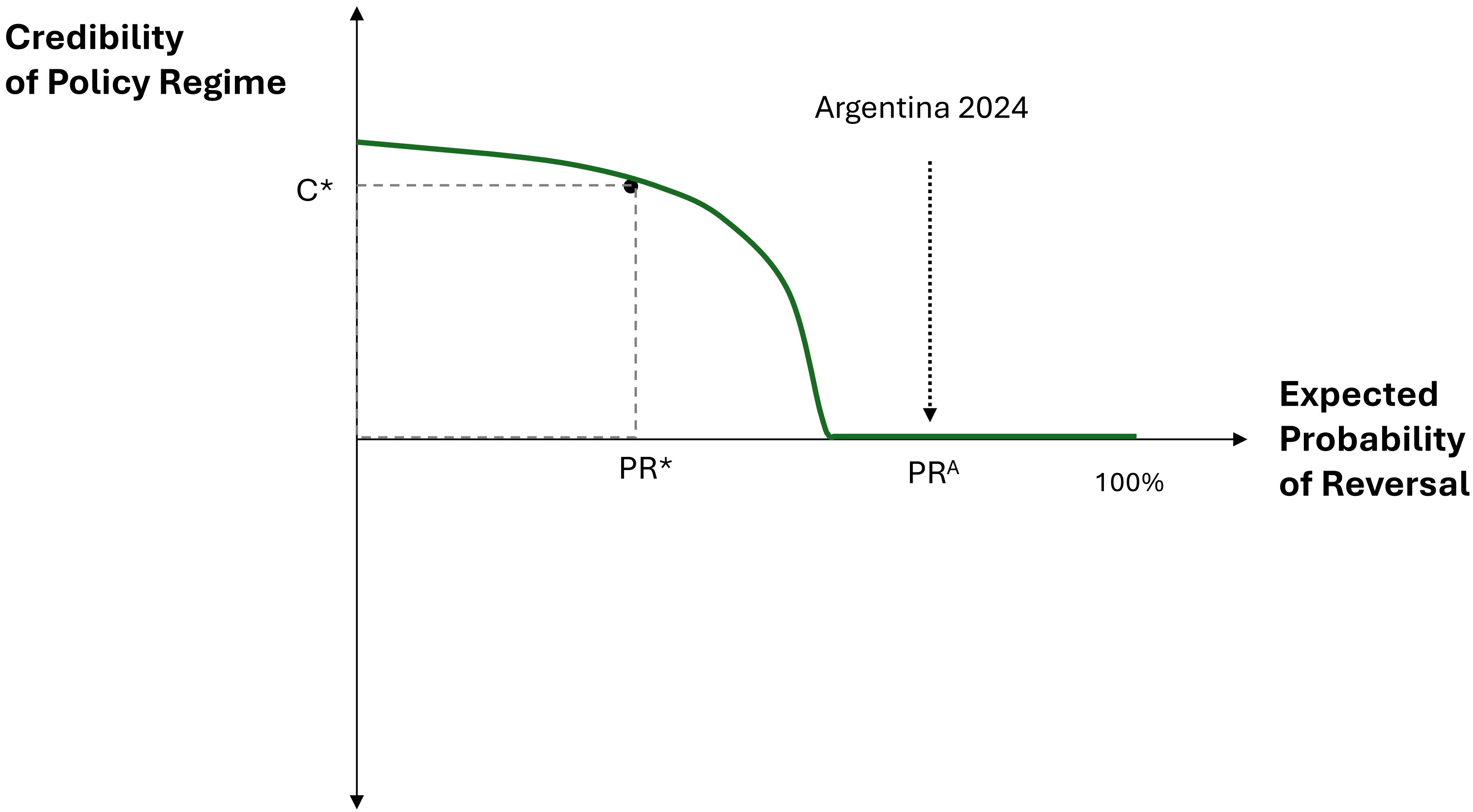


Source: Romelli (2022, 2024)

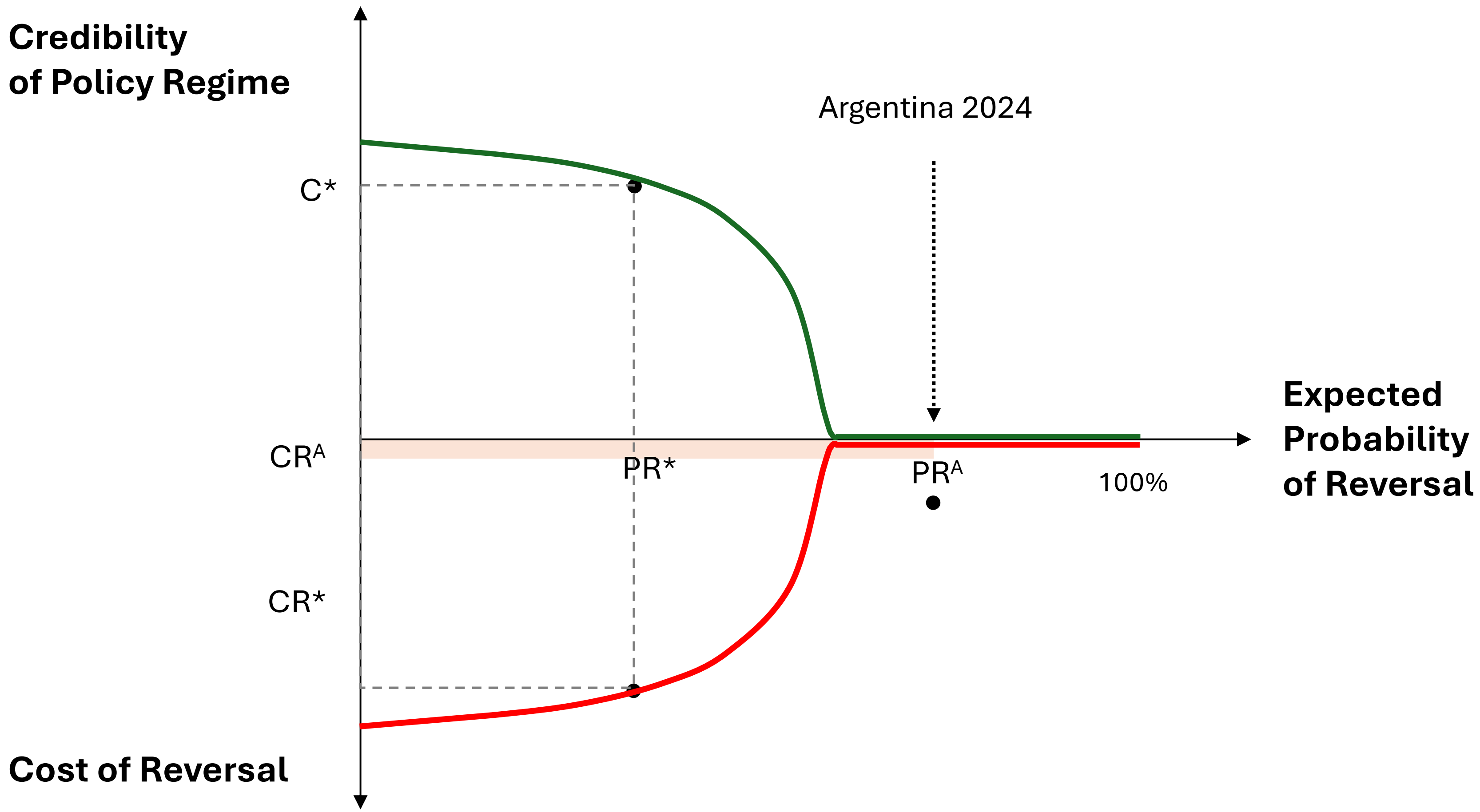
Credible vs. Non-Credible Commitments: The Case of Argentina

1967	Public announcement by Economy Minister (3 years)
1978	Public announcement by Economy Minister (3 years)
1985	Austral Plan by Presidential decree (10 months)
1991	Convertibility Plan by Law approved by Congress (10 years)
2015	Presidential “promise” of Central Bank Independence (2 years)
2023	Presidential “promise” of 2% crawling peg (4 months so far)

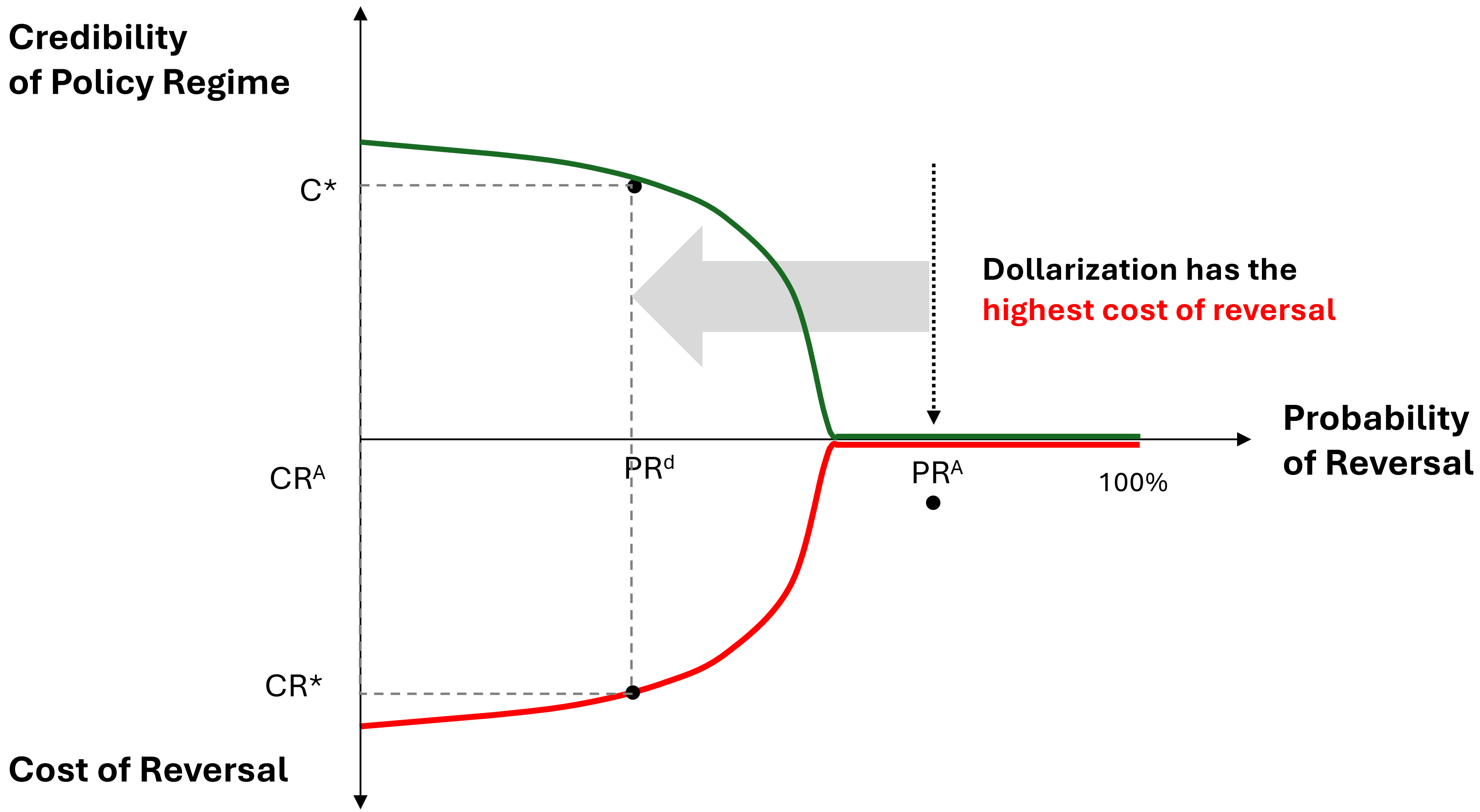
No Credibility with Institutional Anomie



Credibility with Institutional Anomie



Credibility with Institutional Anomie



Effective Commitment Devices (ECDs)

"The commitment level to a policy regime is determined by the political cost of breaking it."

Alan Cukierman (1993)

Dollarization as an ECD

"There are few politicians in Ecuador who currently talk about a possible return to the sucre.

The debate on de-dollarization is almost non-existent.

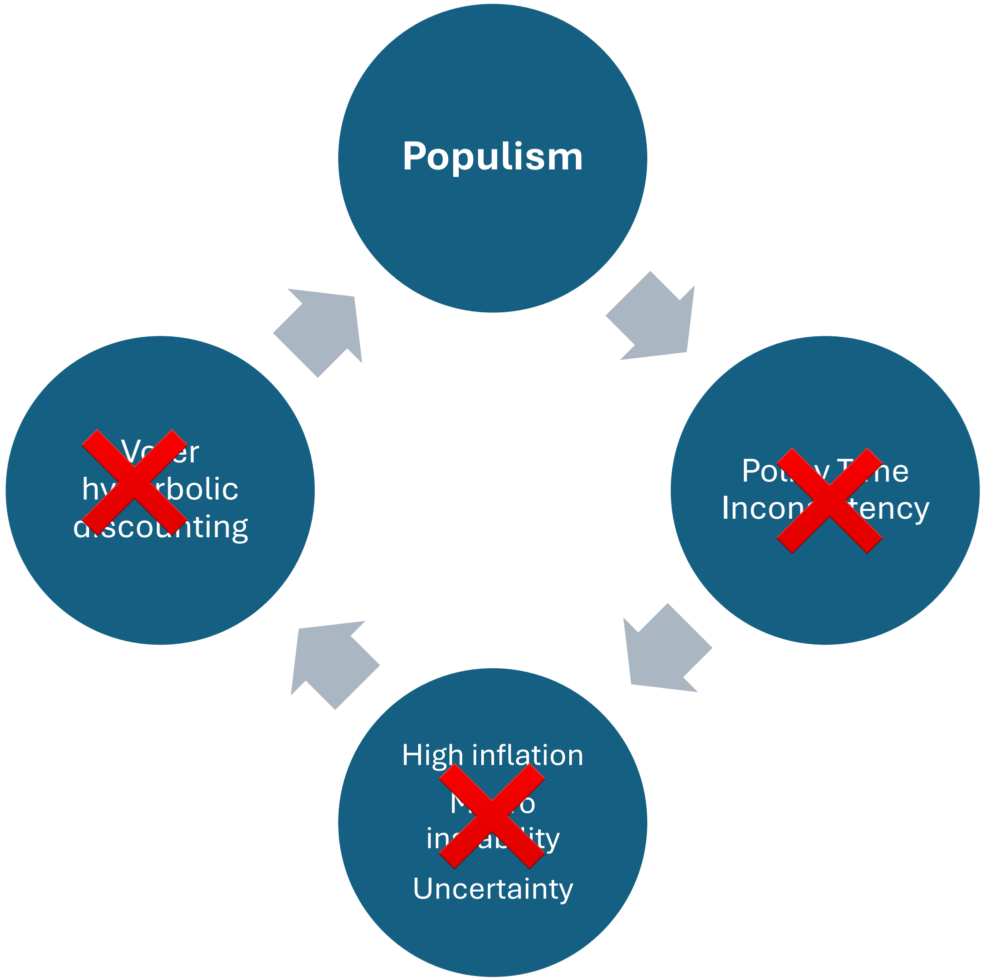
And the sucre represents the past for many. It is the memory of the economic crisis and the constant devaluation that ruined the economy for millions of people.

The dollar, on the other hand, represents stability. It is viewed as a strong currency managed from abroad. **And in this, some economists say, lies the key to its success among Ecuadorians.**

According to the last survey carried out in the country on the subject, which dates back to 2015, **85% of Ecuadorians responded that they support dollarization**."

BBC News, January 2020

Dollarization can break the Vicious Cycle of Populism



Milton Friedman was Right

"The whole reason why it is an advantage for a developing country to tie [its currency] to a major country is that, historically speaking, the internal policies of developing countries have been very bad. U.S. policy has been bad, but their policies have been far worse.

There are no gyrations in American monetary policy which can hold a candle to the gyrations which have occurred in Argentinian domestic monetary policy.

So, the whole reason why tying to a major currency would be an advantage to Argentina is that precisely that it would prevent them from following bad domestic monetary policies. They would have less of an adjustment problem simply because our policy will prove to be more stable than theirs."

Milton Friedman, Testimony to Congress, June 1973

Thank you