

Living and Dying with Hard Pegs: The Rise and Fall of Argentina's Currency Board

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The rise and fall of Argentina's currency board illustrates the extent to which the advantages of hard pegs have been overstated. The currency board provided nominal stability and boosted financial intermediation, at the cost of endogenous financial dollarization, but it did not foster fiscal or monetary discipline.

Argentina fell into a currency-growth-debt trap at the end of the 1990s; the failure to adequately address this problem precipitated a run on the currency and the banks, followed by the abandonment of the currency board and a sovereign debt default. The crisis can best be interpreted as a bad outcome of a high-stakes strategy to overcome a weak currency problem. To increase the credibility of the hard peg, the government raised its exit costs, which deepened the crisis once exit could no longer be avoided. Some alternative exit strategies would have been less destructive than the one adopted.