

# C4FE ECONOMIC INSIGHTS

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## Argentine Dollarization and its Potential Impact on the United States

On Sunday, November 19th, Javier Milei (LLA) emerged victorious in the runoff election for the next President of Argentina, defeating Sergio Massa (UxP). Milei's mandate is to address one of Argentina's most profound inflation crises, marked by over a decade of stagnation and a staggering 210% inflation rate, with hyperinflation looming on the horizon. Statistics reveal that 40% of the Argentinian population currently lives below the poverty line.

Milei's proposed solution to this economic turmoil is radical and intriguing: shut down the central bank, eliminate the Argentinian peso, and officially adopt the US dollar as the nation's currency. Throughout his campaign, Milei's passionate plea for dollarization garnered support from an electorate exhausted by monetary mismanagement. While some Argentine economists questioned the convenience of such a move, experience shows that dollarization is not as **crazy an idea** as it sounds. Among Latin American countries, three have successfully embraced dollarization, namely Panama (since 1903), Ecuador (since 2000), and El Salvador (since 2001).

Although Milei has no plans for immediate dollarization upon taking office, he is expected to pursue this strategy at a later stage. However, two significant challenges stand in the way: the economic problem of a central bank with no reserves and no access to international financial markets and the political challenge of securing Congressional votes for a dollarization law.

For the United States, Argentina's potential dollarization offers three indirect benefits. **Firstly**, it would lead to increased seigniorage revenue for the Federal Reserve. Since seigniorage is the income derived from issuing a currency in demand, it would rise as dollarization would boost Argentinians' demand for the US dollar. Additional seigniorage would be particularly welcomed as the Federal Reserve is experiencing **losses** for the first time in over a century.

**Secondly**, Argentina's dollarization would have geopolitical implications as China attempts to expand its influence in Latin America and is trying to challenge the US dollar as the world's reserve currency. For instance, in June 2023, Argentina repaid a 2.7-billion-dollar loan to the IMF **using Chinese Yuan**. Argentina's dollarization could help counterbalance China's involvement in the region, thereby reinforcing the significance of the US dollar.

The **third** potential benefit for the United States lies in improving diplomatic relations. Dollarization in Argentina might positively impact the country's strong anti-US sentiment, potentially paving the way for more cooperative political involvement between the two nations. Given Argentina's size and strategic importance, particularly in areas like the war on drugs, enhanced collaboration could be mutually beneficial and positively affect the region.

While the path to Argentine dollarization is fraught with challenges, the potential benefits for both Argentina and the United States are real. Argentina would be trading off some (modest) seigniorage to eliminate the Argentine government's proven capacity for monetary mischief. As Milei assumes the presidency, the world watches to see whether this bold economic experiment will bring stability to Argentina and reshape its relationship with the United States on both economic and diplomatic fronts.

## About the authors

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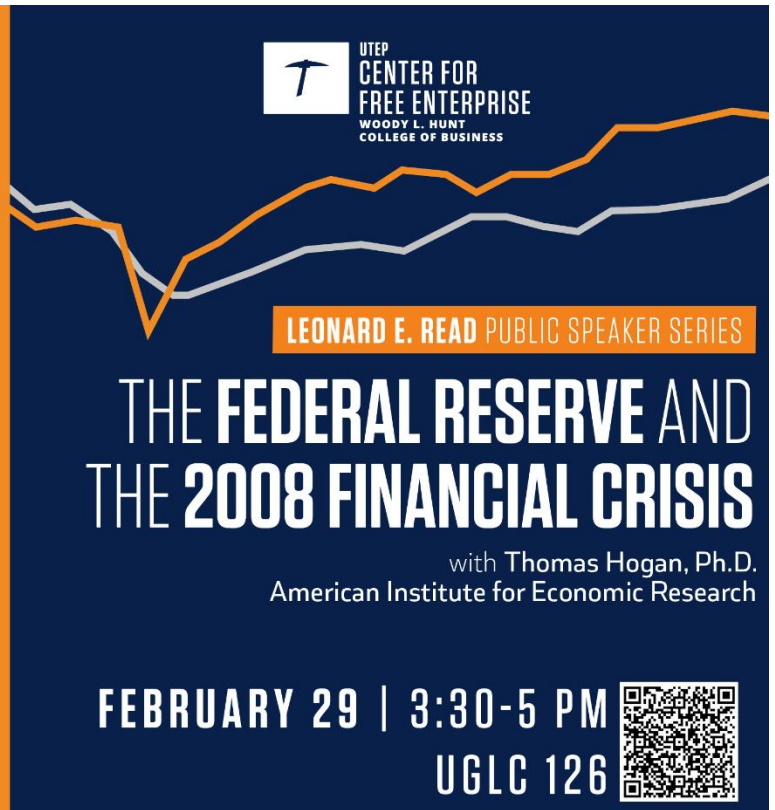



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**Dr. Thomas Hogan** is a Senior Fellow at the American Institute for Economic Research. He was formerly the Chief Economist for the U.S. Senate Committee on Banking, Housing, & Urban Affairs. His primary research interests include banking regulation and monetary policy.

Dr. Hogan has held a variety of positions in the academic and private sectors. He was previously a Fellow at Rice University's Baker Institute for Public Policy, Assistant Professor of Finance at Troy University, and Assistant Professor of Economics at West Texas A&M University. He has worked for Merrill Lynch's commodity trading group and investment firms in the U.S. and Europe. He was a consultant to the World Bank and a research fellow at the Cato Institute.

Dr. Hogan earned his Ph.D. in Economics from George Mason University and holds Bachelor's and Master's degrees in Business Administration from the University of Texas at Austin. His work has been published in academic journals such as *Economic Inquiry*, the *Journal of Regulatory Economics*, and the *Journal of Money, Credit & Banking*.

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