

# Dollar Lifelines and Domestic Faultlines: Argentina's Crisis at a Crossroads - A Case Study on Inflation Dynamics, Exchange-Rate Pressures, and Strategic Stabilization Choices

Rajib Bhattacharya

Associate Professor, Bhawanipur Global Campus Kolkata, West Bengal, India

DOI: <https://doi.org/10.51244/IJRSI.2026.1303000164>

Received: 20 March 2026; Accepted: 25 March 2026; Published: 10 April 2026

## ABSTRACT

In October 2025, Argentina secured a USD 20 billion bilateral currency-swap arrangement with the United States at a moment of escalating macroeconomic stress. The country faced one of the highest inflation rates in the world, declining foreign exchange reserves, and deteriorating investor confidence. The swap facility was designed to provide temporary access to dollar liquidity, potentially stabilizing the Argentine peso and easing pressure on the country's balance of payments. This case examines the economic context that led to the agreement, the mechanics of the swap arrangement, and the policy dilemmas confronting Argentina's economic leadership. Although the swap line offered short-term financial relief, it did not address deeper structural weaknesses in fiscal policy, institutional credibility, and monetary governance. The case places readers in the position of Argentine policymakers who must determine whether to rely on external liquidity support, seek multilateral assistance, or pursue politically difficult domestic reforms. Through this decision framework, the case highlights broader issues in international macroeconomics, including financial crisis management in emerging markets, the role of central bank cooperation in the global financial system, and the political economy constraints shaping stabilization policy.

**Keywords:** Currency swap arrangements; Exchange rate crisis; Emerging market financial stability; Central bank cooperation; Macroeconomic stabilization policy

**JEL Codes:** F31, F33, E58, F34, E63

## Macroeconomic Context and the Origins of Argentina's Crisis

By the second half of 2025, Argentina once again found itself confronting a familiar but deeply unsettling economic reality. Inflation was rising rapidly, foreign exchange reserves were falling, and the Argentine peso was under sustained pressure in currency markets. For policymakers in Buenos Aires, the sense of déjà vu was difficult to ignore. Argentina had experienced repeated episodes of financial instability over the past several decades. Economic recoveries had often been followed by new crises characterized by inflation surges, currency depreciation, and sovereign debt restructuring. Scholars of financial crises frequently cite Argentina as one of the most prominent examples of recurrent macroeconomic instability in emerging markets (Reinhart & Rogoff, 2009).

The country's policymakers had attempted various stabilization strategies over the years. Exchange-rate pegs, capital controls, fiscal adjustments, and international financial assistance had all been deployed at different moments. Yet none of these measures had succeeded in producing lasting stability. By early 2025, the economic situation had once again become precarious. Argentina's inflation rate exceeded 120 percent on an annual basis, placing enormous strain on households and businesses (International Monetary Fund [IMF], 2024). At the same time, the country's foreign exchange reserves were steadily declining as the central bank attempted to defend the peso in currency markets (World Bank, 2024). Against this backdrop, Argentina negotiated a USD 20 billion currency-swap agreement with the United States. The arrangement allowed Argentina's central bank to access U.S. dollar liquidity, if necessary, potentially strengthening its reserve position and stabilizing exchange-rate expectations. The announcement of the swap line immediately attracted global attention. Financial markets interpreted the agreement as a signal that Argentina had secured external support at a critical moment. Yet

economists were quick to note an important limitation. Currency swaps can provide liquidity, but they do not eliminate underlying macroeconomic imbalances. As a result, the swap facility raised a critical policy question: would it become a turning point in Argentina's economic stabilization strategy, or simply another temporary response to a recurring crisis?

### **Argentina's Economic Legacy: A History of Instability**

Argentina's modern economic history has been shaped by repeated cycles of boom and crisis. While the country possesses vast natural resources and a relatively diversified economy, its macroeconomic policy framework has often struggled to maintain stability. Throughout much of the twentieth century, Argentina experienced alternating periods of economic expansion and severe financial disruption. Inflationary episodes were particularly common. In several periods, annual inflation exceeded triple-digit levels, eroding purchasing power and undermining confidence in the national currency (Eichengreen, 2011). One of the most significant crises occurred in 2001–2002, when Argentina abandoned its currency board system that had pegged the peso to the U.S. dollar. The collapse of the peg triggered a sharp economic contraction, a sovereign debt default, and widespread social unrest. At the time, Argentina's default represented the largest sovereign debt restructuring in history (Reinhart & Rogoff, 2009). The crisis also exposed deep institutional weaknesses in Argentina's economic governance. Fiscal deficits had accumulated for years, and the country's monetary policy framework lacked credibility among investors. When capital inflows slowed and reserves declined, the currency board became increasingly difficult to sustain. Argentina eventually recovered from the crisis during the mid-2000s, benefiting from strong global commodity prices and expanding exports. However, many structural vulnerabilities remained unresolved. Fiscal policy continued to rely heavily on government spending, often financed through monetary expansion. Economists describe this phenomenon as fiscal dominance, a situation in which fiscal pressures constrain the central bank's ability to maintain price stability (Sargent & Wallace, 1981). Under fiscal dominance, monetary policy becomes subordinate to government financing needs. The resulting expansion in the money supply can contribute to persistent inflation and currency depreciation. Over time, this dynamic weakened confidence in Argentina's monetary institutions. Investors and households alike became increasingly sensitive to signals of fiscal imbalance or policy inconsistency.

### **Inflation and Monetary Policy Challenges**

Inflation has long been one of Argentina's most persistent macroeconomic challenges. Unlike temporary price increases driven by external shocks, Argentina's inflation has often reflected structural issues in fiscal and monetary policy. Economic theory provides several explanations for sustained inflation in emerging markets. One widely discussed framework is the time-inconsistency problem in monetary policy, first articulated by Kydland and Prescott (1977). According to this theory, governments may face incentives to pursue expansionary policies that stimulate economic activity in the short term but ultimately lead to higher inflation. When economic actors anticipate such behaviour, inflation expectations become embedded in wage negotiations, price-setting decisions, and financial contracts. This dynamic can make inflation difficult to reduce without credible institutional reforms.

Argentina's experience illustrates this challenge. Even when policymakers attempted to tighten monetary policy, financial markets often remained sceptical about the durability of stabilization measures. The result was a persistent inflationary inertia, in which past inflation influenced expectations about future inflation. By the early 2020s, inflation in Argentina had reached levels rarely seen outside of extreme crisis situations. According to official data, annual consumer price inflation rose from approximately 50 percent in 2021 to more than 120 percent by 2024 (World Bank, 2024). Such high inflation had profound economic consequences. Households saw their real incomes eroded, savings lost value rapidly, and long-term financial planning became increasingly difficult. Businesses faced uncertainty regarding costs and pricing, complicating investment decisions. For policymakers, high inflation also complicated monetary management. Raising interest rates could slow inflation but risked triggering economic contraction. Allowing inflation to continue, however, risked further erosion of confidence in the peso.

### **Exchange Rate Pressures and Capital Flows**

Argentina's inflation dynamics were closely intertwined with developments in the foreign exchange market. As inflation accelerated, the peso faced increasing downward pressure. Currency depreciation can amplify inflation

through exchange-rate pass-through, a mechanism in which weaker domestic currency raises the cost of imported goods (Obstfeld, Shambaugh, & Taylor, 2010). Argentina's heavy reliance on imported energy and industrial inputs made this effect particularly pronounced. At the same time, capital flows became increasingly volatile. Investors often responded to signs of macroeconomic instability by shifting assets into foreign currencies or transferring capital abroad. This behavior is consistent with the dynamics described in models of currency crises developed by Krugman (1979). According to these models, when investors believe that a government may be unable to defend its exchange rate, speculative pressures can intensify rapidly. Such expectations can become self-fulfilling. As investors move funds out of the domestic currency, pressure on the exchange rate increases, forcing policymakers to either intervene with foreign reserves or allow depreciation. By 2024, Argentina was facing precisely this challenge.

### **The Reserve Problem**

Foreign exchange reserves play a crucial role in stabilizing currency markets during periods of financial stress. When a central bank intervenes to support its currency, it typically sells foreign reserves while purchasing domestic currency. However, reserves are finite. If investors believe that reserves are insufficient to sustain intervention, speculative pressure on the currency may intensify. Economists often refer to this dynamic as the speculative attack problem in fixed or managed exchange-rate regimes (Krugman, 1979). Argentina's reserves had declined significantly during the early 2020s. Several factors contributed to the decline, including debt repayments, energy imports, and currency market interventions. According to IMF estimates, Argentina's gross international reserves fell from roughly USD 45 billion in 2022 to around USD 25 billion by early 2025 (IMF, 2024). These declining reserves increased the urgency of Argentina's search for external financial support.

### **The Global Context: International Liquidity and Swap Lines**

The growing importance of currency-swap arrangements in global finance provided one possible solution. Central bank swap lines are agreements that allow two central banks to exchange currencies temporarily. These arrangements enable countries experiencing liquidity shortages to access foreign currency without directly borrowing from international capital markets (Allen & Moessner, 2010). The significance of swap lines increased dramatically during the 2008 global financial crisis, when the U.S. Federal Reserve established swap facilities with several major central banks to stabilize global dollar funding markets (Bordo, Humpage, & Schwartz, 2015). In the years since the crisis, swap lines have become an important component of the global financial safety net. Alongside international reserves and multilateral lending institutions such as the IMF, they help provide liquidity during periods of financial stress. However, economists emphasize that swap lines are designed primarily to address liquidity shortages rather than fundamental solvency problems (Obstfeld et al., 2010). For Argentina, this distinction would become critically important.

### **The Road to the Swap Agreement**

As Argentina's economic pressures intensified during 2025, policymakers began exploring various options for securing additional dollar liquidity. Discussions with U.S. authorities initially focused on broader financial cooperation. Over time, however, the possibility of establishing a bilateral currency-swap arrangement began to take shape. For Argentina, such an arrangement offered several advantages. It could provide access to dollar liquidity, strengthen the central bank's reserve position, and signal international confidence in the country's financial system. For the United States, the arrangement represented a flexible form of financial cooperation that could support regional financial stability without requiring direct fiscal transfers. By mid-2025, negotiations were underway.

### **Escalating Financial Pressures and the Search for External Liquidity**

#### **The October Crisis Meeting**

On the evening of 10 October 2025, senior members of Argentina's economic leadership gathered in a conference room inside the Ministry of Economy in Buenos Aires. The meeting had been called on short notice. Market developments over the previous weeks had become increasingly alarming. Inflation had continued to

accelerate. The peso had weakened further in both official and parallel markets. International investors were demanding higher risk premiums on Argentine government bonds. Within the central bank, officials worried that the country's foreign exchange reserves were approaching levels that might prove insufficient to stabilize the currency. The room was quiet as the finance minister reviewed the latest economic briefing. Consumer prices had risen sharply again in the previous month. The central bank's intervention in currency markets had slowed the pace of depreciation, but doing so had required significant sales of foreign exchange reserves. Analysts warned that continued intervention at the same pace might not be sustainable. Argentina had faced similar moments before. Yet the combination of high inflation, declining reserves, and volatile capital flows created a particularly difficult policy environment. The newly announced USD 20 billion currency-swap agreement with the United States offered a potential lifeline. However, policymakers understood that the facility alone could not resolve Argentina's deeper macroeconomic challenges. The key question was how the government should respond.

### **Inflation Dynamics and Economic Pressures**

Inflation had long been a defining feature of Argentina's macroeconomic environment. By 2025, however, the scale of price increases had reached levels that many economists considered alarming. Official statistics indicated that annual inflation exceeded 120 percent, placing Argentina among the highest-inflation economies in the world (International Monetary Fund [IMF], 2024). For households, the consequences were visible in everyday life. Prices in supermarkets changed frequently. Wages struggled to keep pace with rising costs. Savings held in local currency lost value rapidly. For many Argentines, financial planning had become increasingly difficult. Economists often analyze sustained inflation through the framework of expectations-driven price dynamics. According to modern macroeconomic theory, inflation tends to persist when individuals expect prices to continue rising in the future. Firms adjust prices upward in anticipation of higher costs, while workers demand higher wages to maintain purchasing power (Mankiw, 2019).

Argentina's economic experience reflected precisely this dynamic. Businesses adjusted prices frequently, sometimes multiple times within a single month. Workers sought wage increases through collective bargaining agreements that attempted to keep pace with inflation. This phenomenon, often described as inflationary inertia, can make stabilization extremely difficult. Even when governments implement restrictive monetary policies, entrenched expectations may delay the decline in inflation (Blanchard & Johnson, 2013). Several structural factors contributed to Argentina's inflationary pressures. First, fiscal deficits had persisted for several years. Government spending frequently exceeded tax revenues, requiring the state to finance budget shortfalls through borrowing or monetary expansion. When central banks increase the money supply to finance government spending, the resulting increase in liquidity can place upward pressure on prices (Sargent & Wallace, 1981). Second, exchange-rate depreciation had contributed to rising import prices. Argentina relied heavily on imported energy, industrial inputs, and technology. As the peso weakened, the cost of these imports increased.

This process is known as exchange-rate pass-through, a mechanism in which currency depreciation leads to higher domestic prices (Obstfeld, Shambaugh, & Taylor, 2010). In economies with high import dependence, exchange-rate pass-through can significantly amplify inflation. Finally, Argentina's monetary policy credibility had been weakened by repeated policy reversals over previous decades. When investors and households doubt a government's commitment to price stability, inflation expectations become harder to anchor (Kydland & Prescott, 1977). Together, these factors created a complex policy challenge for Argentina's central bank.

### **Exchange Rate Instability**

While inflation dominated domestic economic discussions, developments in the foreign exchange market were equally concerning. Throughout 2024 and early 2025, the Argentine peso had experienced sustained depreciation against the U.S. dollar. Although the government maintained an official exchange rate through managed currency markets, parallel exchange markets increasingly reflected weaker valuations of the peso. The widening gap between official and unofficial exchange rates became a symbol of Argentina's economic tensions. Economists have long observed that dual exchange-rate systems often emerge in countries facing severe macroeconomic imbalances. When official exchange rates diverge significantly from market fundamentals, parallel markets develop as individuals and firms seek access to foreign currency at more realistic prices (Edwards, 1989). By

mid-2025, Argentina's parallel exchange rate had moved significantly above the official rate, reflecting persistent demand for U.S. dollars as a store of value. This demand was not surprising. In economies experiencing high inflation, individuals frequently shift savings into foreign currencies to preserve purchasing power. The U.S. dollar has long served as a global reserve currency and a safe haven during periods of financial uncertainty (Eichengreen, 2011). For Argentine households and firms, holding dollars offered protection against the erosion of the peso's value.

### **Capital Flows and Investor Sentiment**

International capital flows added another layer of complexity to Argentina's economic challenges. Foreign investors had historically played an important role in financing Argentina's government debt and private investment. However, confidence in Argentina's macroeconomic stability had fluctuated over time. By early 2025, many international investors had become increasingly cautious. Argentina's sovereign bond yields rose as investors demanded higher compensation for perceived risk. Rising borrowing costs created a feedback loop. Higher interest rates made government debt more expensive to service. Increased debt burdens raised concerns about fiscal sustainability, further reducing investor confidence. Economists describe this phenomenon as a sovereign risk spiral, in which declining confidence leads to higher borrowing costs, which in turn further undermine fiscal stability (Reinhart & Rogoff, 2009). Argentina had experienced similar dynamics in earlier crises. International investors were particularly sensitive to signals regarding foreign exchange reserves. Adequate reserves provide assurance that a country can meet external obligations and defend its currency if necessary. When reserves fall, investor concerns often intensify.

### **Declining Foreign Exchange Reserves**

Foreign exchange reserves represent a critical buffer in times of financial stress. Central banks use reserves to intervene in currency markets, stabilize exchange rates, and meet external payment obligations. Argentina's reserves had declined steadily during the early 2020s. Several factors contributed to this trend:

- repayment of external debt
- rising energy import costs
- capital outflows
- central bank intervention in currency markets

According to data compiled by the IMF (2024) and the Central Bank of Argentina, gross international reserves declined from approximately USD 44 billion in 2022 to around USD 25 billion by early 2025. This decline raised concerns among investors and policymakers alike. In currency crisis models developed by Krugman (1979), declining reserves can trigger speculative pressure on a country's currency. When investors believe that a central bank may eventually run out of reserves, they may rush to convert domestic currency into foreign currency. Such expectations can become self-fulfilling. As investors sell domestic currency, the central bank must either spend reserves to stabilize the exchange rate or allow the currency to depreciate further. Argentina faced exactly this dilemma.

### **The Policy Constraints**

Argentina's economic policymakers were therefore confronted with a complex set of constraints. Raising interest rates could help stabilize the currency by attracting capital inflows. However, higher interest rates risked slowing economic activity and increasing the cost of government borrowing. Allowing the peso to depreciate might help improve export competitiveness, but it could also accelerate inflation through exchange-rate pass-through. Increasing fiscal discipline could strengthen macroeconomic credibility, but spending cuts often face strong political resistance. Economists frequently analyze such policy trade-offs using the Mundell–Fleming model, which examines macroeconomic policy in open economies (Mundell, 1963). According to the model, governments face difficult choices when attempting to simultaneously maintain exchange-rate stability, independent monetary policy, and free capital flows. This constraint is sometimes described as the impossible

trinity or macroeconomic trilemma (Obstfeld et al., 2010). Argentina's policymakers were effectively navigating this trilemma.

### **The Search for External Liquidity**

Given these constraints, Argentina began exploring options for obtaining additional foreign currency liquidity. External financial support could strengthen the country's reserve position and reassure investors that Argentina would be able to meet its short-term financial obligations.

Traditionally, countries facing such challenges turn to multilateral institutions such as the International Monetary Fund. Argentina had a long history of IMF programs. However, these programs often involve strict policy conditions designed to restore fiscal and monetary discipline (Bird, 2007). Such conditions can be politically controversial. Domestic political leaders sometimes worry that IMF-supported reforms, particularly fiscal austerity measures, may trigger public protests or electoral backlash. As a result, Argentine policymakers explored alternative sources of liquidity support. One possibility was a bilateral currency-swap arrangement with a major central bank.

### **Early Discussions with the United States**

Initial conversations between Argentine and U.S. officials began during the first half of 2025. These discussions focused on broader financial cooperation and regional economic stability. Over time, the possibility of establishing a bilateral currency-swap facility began to gain momentum. Currency-swap agreements between central banks had become increasingly common in the global financial system. Following the 2008 global financial crisis, several major central banks, including the U.S. Federal Reserve, had established swap lines to provide dollar liquidity during periods of financial stress (Bordo, Humpage, & Schwartz, 2015). These arrangements allowed foreign central banks to obtain U.S. dollars temporarily in exchange for their own currencies. The transactions were structured so that the currencies would be exchanged back at a predetermined future date. Such agreements provided an important mechanism for stabilizing international financial markets. For Argentina, a swap line with the United States could provide several benefits:

- access to dollar liquidity
- strengthened reserve position
- improved market confidence

For the United States, the arrangement offered a flexible tool for supporting regional financial stability without committing direct fiscal resources.

### **Negotiating the Swap Facility**

Negotiations between the two governments progressed over several months. Key issues included:

- the total size of the swap line
- interest rates on swap drawings
- maturity structures
- operational procedures for accessing funds

Both sides recognized the importance of designing a facility that could provide meaningful liquidity support while maintaining appropriate safeguards. By October 2025, the negotiations reached a conclusion. Argentina and the United States announced the creation of a USD 20 billion currency-swap facility between their central banks. For Argentina, the agreement represented a potentially critical source of financial stability. But it also

raised an important question. Would the swap line merely delay a deeper crisis, or could it create an opportunity for meaningful economic reform?

## **The Currency-Swap Agreement and Market Reactions**

### **Announcement of the Agreement**

The announcement came early on the morning of 12 October 2025. Argentina's Ministry of Economy released a brief statement confirming that the Central Bank of Argentina (Banco Central de la República Argentina, BCRA) and the United States Federal Reserve System had agreed to establish a USD 20 billion bilateral currency-swap facility. The agreement would allow Argentina to obtain U.S. dollar liquidity if necessary to stabilize its financial system. Within minutes of the announcement, the news began circulating through global financial markets. Analysts in New York, London, and São Paulo quickly began evaluating the potential implications. The Argentine government framed the agreement as an important step toward restoring confidence in the country's financial system. Officials emphasized that the swap line would strengthen Argentina's international reserve position and provide a buffer against currency volatility. Yet the announcement also triggered a broader debate among economists and investors on whether the swap facility would be sufficient to stabilize Argentina's economy or would a deeper policy adjustment still be required.

### **Understanding Central Bank Currency Swaps**

Currency swaps between central banks are financial arrangements that allow participating institutions to exchange currencies temporarily with a commitment to reverse the transaction at a specified future date. These arrangements provide foreign currency liquidity during periods of market stress without requiring countries to borrow directly from international capital markets (Allen & Moessner, 2010). In a typical swap transaction, the central bank of one country exchanges its domestic currency for foreign currency supplied by another central bank. The two parties agree to reverse the transaction later at the same exchange rate, thereby eliminating exchange-rate risk. For example, under the Argentina–United States arrangement, the Argentine central bank could provide pesos to the U.S. Federal Reserve in exchange for dollars. At the maturity date of the swap, the currencies would be exchanged back at the same rate. Such agreements can play a crucial role in stabilizing global financial markets during periods of stress. During the 2008 global financial crisis, the U.S. Federal Reserve established swap lines with several major central banks to ensure that financial institutions outside the United States had access to dollar funding (Bordo, Humpage, & Schwartz, 2015). Dollar liquidity is particularly important because the U.S. dollar serves as the dominant currency in global trade and finance. Many international transactions, including commodity trading and cross-border investment, are denominated in dollars. As a result, disruptions in dollar funding markets can quickly affect financial systems around the world (Eichengreen, 2011). Swap lines therefore act as a form of international lender-of-last-resort mechanism, allowing central banks to supply liquidity when private funding markets become constrained (Bahaj & Reis, 2022).

### **The Global Financial Safety Net**

In recent years, economists have increasingly described the global system of financial crisis support as a global financial safety net.

This safety net consists of several layers:

- national foreign exchange reserves
- bilateral central bank swap lines
- regional financial arrangements
- multilateral institutions such as the IMF

Each layer serves a different function in stabilizing international financial markets (Obstfeld et al., 2010). Foreign exchange reserves represent the first line of defence. Countries accumulate reserves so that their central

banks can intervene in currency markets when necessary. However, reserve accumulation can be costly. Maintaining large reserve holdings often requires countries to invest in low-yielding foreign assets such as U.S. Treasury securities (Rodrik, 2006). Swap lines represent a complementary mechanism. Instead of always holding large reserves, countries can obtain temporary liquidity through agreements with other central banks.

Multilateral institutions such as the IMF represent the final layer of the safety net, providing financial assistance during more severe crises. Argentina's swap agreement with the United States thus represented one component of a broader international framework designed to manage financial instability.

### **Structure of the Argentina–United States Swap Facility**

Although the public announcement emphasized the headline figure of USD 20 billion, the structure of the swap arrangement was more complex. The agreement functioned primarily as a contingent liquidity facility, meaning that the funds would only be drawn if Argentina's central bank decided to activate the swap. The key features of the arrangement included:

- *Maximum Size:* The facility allowed Argentina to access up to USD 20 billion in dollar liquidity.
- *Reciprocal Currency Exchange:* The central banks would exchange Argentine pesos for U.S. dollars at the prevailing exchange rate at the time of the transaction.
- *Fixed Repurchase Agreement:* At the maturity date of the swap, the currencies would be exchanged back at the same rate used in the initial transaction.
- *Interest Charges:* Argentina would pay interest on any dollars drawn under the facility. The interest rate would typically be linked to benchmark U.S. policy rates.
- *Short-Term Maturity:* Most swap transactions between central banks have maturities ranging from several weeks to several months.

These design features ensured that the swap line would function as a short-term liquidity mechanism rather than a long-term financing tool. Economists emphasize that this distinction is important. Currency swaps are intended to address temporary funding shortages, not structural macroeconomic imbalances (Allen & Moessner, 2010).

### **Liquidity Versus Solvency**

The distinction between liquidity crises and solvency crises is central to understanding the potential effectiveness of the swap arrangement. A liquidity crisis occurs when a country temporarily lacks access to foreign currency needed to meet its financial obligations. In such cases, short-term financial support can stabilize markets and restore confidence. A solvency crisis, by contrast, arises when a country's underlying economic fundamentals make it unlikely that debts can be repaid without major policy adjustments. Economists have long emphasized the importance of distinguishing between these two situations when designing financial rescue mechanisms (Krugman, 1979). If a crisis is primarily driven by liquidity shortages, external support can often stabilize the situation quickly. However, if the crisis reflects deeper structural weaknesses e.g. unsustainable fiscal deficits or chronic inflation, liquidity support alone may not be sufficient. Many analysts viewed Argentina's situation as a combination of both problems. The country faced immediate liquidity pressures due to declining reserves and volatile capital flows. At the same time, persistent fiscal deficits and inflation suggested deeper structural vulnerabilities.

### **Immediate Market Reaction**

Financial markets reacted quickly to the announcement of the swap agreement. In the hours following the announcement, Argentina's sovereign bond prices rose modestly. The spread between Argentine government bonds and U.S. Treasury securities narrowed slightly, indicating that investors perceived a reduction in short-term financial risk. The Argentine peso also stabilized in currency markets. Although the currency remained volatile, the immediate pressure on the exchange rate appeared to ease. Market analysts interpreted the agreement as a signal that Argentina would have greater access to dollar liquidity if necessary. Financial markets often

respond strongly to such signals. Even when external financial support is not immediately used, the presence of a backstop can influence investor expectations (Corsetti, Guimarães, & Roubini, 2006). However, the positive reaction was cautious rather than enthusiastic. Many investors recognized that the swap facility addressed only part of Argentina's broader macroeconomic challenges. Inflation remained extremely high, fiscal imbalances persisted, and Argentina's long-term debt sustainability continued to be debated.

### **Investor Perspectives**

International investors viewed the swap arrangement through several different lenses. Some analysts argued that the facility represented a meaningful step toward stabilizing Argentina's financial system. Access to additional dollar liquidity could reduce the risk of sudden currency depreciation and improve Argentina's ability to meet external obligations. Others were more sceptical. Critics pointed out that Argentina had previously relied on external financial support during earlier crises without achieving lasting macroeconomic stabilization. In the absence of credible fiscal reforms, they argued, the swap facility might simply delay necessary policy adjustments. These debates reflected broader discussions in the economic literature about the effectiveness of international financial assistance. Some economists argue that external support can create moral hazard, reducing incentives for governments to implement difficult reforms (Corsetti et al., 2006). Others emphasize that financial crises can escalate rapidly without external intervention, making liquidity support essential for preventing systemic instability. Argentina's situation highlighted this tension.

### **Domestic Political Reactions**

The announcement of the swap facility also triggered debate within Argentina itself. Government officials presented the agreement as evidence that international partners supported Argentina's economic stabilization efforts. Opposition politicians, however, expressed concern that the government might rely too heavily on external financial support rather than implementing structural reforms. Public opinion was divided. Many Argentine citizens hoped that the swap arrangement would stabilize the currency and slow inflation. Yet others worried that temporary financial relief might postpone deeper economic reforms that were widely considered necessary. Economic policymaking in Argentina had long been shaped by these political tensions. Efforts to reduce fiscal deficits or tighten monetary policy often faced resistance from groups concerned about employment, wages, and social welfare. This dynamic reflects what economists describe as the political economy of stabilization policy, in which economic decisions are influenced by competing social and political interests (Drazen, 2000).

### **The Window of Opportunity**

For Argentina's economic leadership, the swap agreement created both an opportunity and a challenge. The facility offered temporary financial breathing space. If the central bank drew on the swap line, it could strengthen its foreign exchange reserves and reduce pressure on the peso.

At the same time, policymakers understood that the swap line was not a permanent solution. Any dollars drawn from the facility would eventually need to be repaid. If Argentina relied heavily on the swap without addressing underlying economic weaknesses, the country might face similar challenges again in the future. The question facing policymakers was therefore not simply whether the swap line would stabilize the economy. The more important question was how the temporary relief created by the swap should be used and should Argentina rely primarily on the swap facility to manage short-term financial pressures. Another question gained importance that should the government pursue a broader stabilization program involving fiscal reforms and monetary tightening, or should Argentina seek additional support from multilateral institutions such as the IMF. The decisions made in the coming months would shape the country's economic trajectory.

### **Policy Trade-offs and Argentina's Strategic Choices**

#### **Stakeholders in the Crisis**

The currency-swap agreement between Argentina and the United States had implications far beyond the technical operations of central banks. A wide range of stakeholders, both domestic and international, were directly affected by Argentina's evolving economic situation.

- **Argentine Government:** For Argentina's political leadership, the swap arrangement offered a valuable opportunity to stabilize financial markets at a moment of considerable economic uncertainty. Government officials hoped that improved liquidity conditions would reduce pressure on the peso and restore investor confidence. However, the political benefits of the swap were accompanied by potential risks. Critics argued that reliance on external liquidity could delay the structural reforms needed to restore macroeconomic stability. Argentina's economic history had repeatedly demonstrated the difficulty of sustaining stabilization efforts in the absence of credible fiscal and monetary reforms (Reinhart & Rogoff, 2009).
- **Central Bank of Argentina:** The Central Bank of Argentina (BCRA) stood at the center of the crisis. As the institution responsible for managing monetary policy and foreign exchange reserves, the central bank faced intense pressure to stabilize the currency while maintaining financial stability. Access to the swap facility offered a potentially important tool. By drawing dollars through the swap line, the BCRA could increase its reserve holdings and intervene more effectively in currency markets. Yet central bank officials also understood that excessive reliance on the facility could create new financial obligations in the future.
- **United States Authorities:** For the United States, the swap arrangement represented a mechanism for supporting financial stability in the Western Hemisphere without committing direct fiscal resources. Historically, the United States has occasionally used financial cooperation to support stability in neighbouring economies, particularly when instability could have spillover effects for global financial markets (Bordo et al., 2015). The reversible nature of swap transactions made them an attractive policy instrument. Because the currencies exchanged in the swap must eventually be returned, the arrangement involved limited long-term financial exposure for the United States.
- **International Investors:** Global investors closely monitored Argentina's economic developments. Many institutional investors held Argentine government bonds or maintained investments in Argentine financial markets. For these investors, the swap agreement provided reassurance that Argentina would have access to additional dollar liquidity. However, investment decisions ultimately depended on broader macroeconomic conditions. Persistent inflation, fiscal imbalances, and political uncertainty continued to influence investor sentiment toward Argentina.
- **Domestic Firms and Households:** The consequences of Argentina's economic instability were perhaps most visible for businesses and households. Argentine firms faced considerable uncertainty regarding exchange rates, import costs, and access to credit. Currency volatility complicated financial planning and discouraged long-term investment. Households experienced the impact of inflation through rising food prices, declining purchasing power, and uncertainty about savings held in domestic currency. As inflation accelerated, many Argentines sought to protect their wealth by purchasing foreign currency or real assets such as property.

## Policy Options for Argentina

Despite the swap agreement, Argentina's policymakers continued to face difficult strategic choices. The swap facility offered temporary liquidity support, but it did not resolve the deeper structural challenges affecting the Argentine economy. Three broad policy options emerged as possible paths forward.

**Option 1: Aggressive Use of the Swap Facility:** One possible strategy involved drawing heavily on the swap line to stabilize the peso and strengthen Argentina's reserve position. By accessing dollar liquidity through the swap arrangement, the central bank could intervene more aggressively in currency markets and meet short-term external payment obligations.

### Potential Advantages

- Immediate access to foreign currency liquidity
- Reduced volatility in the exchange rate

- Increased confidence among financial market participants
- Greater ability to defend the peso against speculative pressure

Such interventions could help slow the pace of currency depreciation and reduce inflationary pressures arising from exchange-rate pass-through (Obstfeld et al., 2010).

#### Potential Risks

- First, heavy reliance on the swap facility would increase Argentina's future repayment obligations. Any dollars drawn from the facility would eventually need to be returned to the United States.
- Second, reliance on external liquidity could reduce incentives for implementing difficult domestic reforms. Economists often describe this phenomenon as moral hazard, in which the availability of external financial support weakens incentives for governments to pursue prudent economic policies (Corsetti et al., 2006).

*Option 2: Seek Multilateral Financial Assistance:* A second option involved negotiating additional financial support from multilateral institutions such as the International Monetary Fund (IMF). Argentina had a long history of IMF programs. These programs typically provide financial resources in exchange for policy reforms aimed at restoring macroeconomic stability.

#### Potential Advantages

- Access to larger financial resources
- Increased policy credibility in international markets
- Structured framework for fiscal and monetary reform
- Potential support for rebuilding foreign exchange reserves

Multilateral programs can also signal international confidence in a country's reform efforts, potentially encouraging private investment (Bird, 2007).

#### Potential Risks

- IMF programs often involve strict policy conditions.
- Fiscal consolidation measures e.g. reducing government spending or increasing taxes—can be politically controversial. In Argentina, previous attempts to implement austerity policies had triggered protests and political instability.
- As a result, seeking multilateral assistance could involve significant domestic political costs.

*Option 3: Domestic Stabilization Reforms:* A third strategy involved pursuing aggressive domestic reforms aimed at restoring macroeconomic stability. These reforms could include:

- reducing fiscal deficits through spending cuts or tax reforms
- strengthening central bank independence
- tightening monetary policy to reduce inflation
- implementing structural reforms to improve economic productivity

#### Potential Advantages

---

- Domestic reforms could address the underlying causes of Argentina’s economic instability. By improving fiscal discipline and strengthening monetary credibility, policymakers could gradually restore confidence in the Argentine economy.
- Economic research suggests that credible policy reforms can significantly reduce inflation expectations and improve macroeconomic stability (Blanchard & Johnson, 2013).

### Potential Risks

- However, stabilization reforms often involve short-term economic costs. Fiscal austerity can slow economic growth, increase unemployment, and reduce household incomes.
- These economic consequences can generate political resistance and make reform efforts difficult to sustain.

### **The Decision Point**

As Argentina’s economic leadership evaluated these options, the stakes were high. The currency-swap facility had created a temporary window of opportunity. For the first time in months, the central bank possessed a mechanism for accessing additional dollar liquidity if necessary. Yet the facility also highlighted the limitations of external financial support. Currency swaps can provide short-term liquidity, but they cannot eliminate inflation, reduce fiscal deficits, or restore institutional credibility.

Argentina’s policymakers therefore faced a fundamental question:

Should the country rely primarily on external liquidity support to manage the crisis, or should it undertake politically difficult reforms aimed at restoring long-term economic stability?

The decision would shape Argentina’s economic trajectory for years to come.

### **DISCUSSION QUESTIONS**

1. Was the USD 20 billion currency-swap agreement an appropriate response to Argentina’s economic crisis?
2. What are the advantages and limitations of currency swaps as crisis-management tools?
3. How should policymakers balance short-term financial stabilization with long-term structural reforms?
4. What risks arise when countries rely heavily on external liquidity support?
5. How do political constraints influence macroeconomic policy decisions in emerging market economies?

### **Exhibits**

#### **Exhibit 1: Selected Macroeconomic Indicators: Argentina**

<i>Year</i>	<i>Inflation (%)</i>	<i>FX Reserves (USD Bn)</i>	<i>Exchange Rate ARS/USD (Avg)</i>	<i>Public Debt (% GDP)</i>
2022	72.4	44	130	80
2023	94.8	38	210	84
2024	133.5	30	340	89
2025*	~120	25	420	91

\*2025 estimates

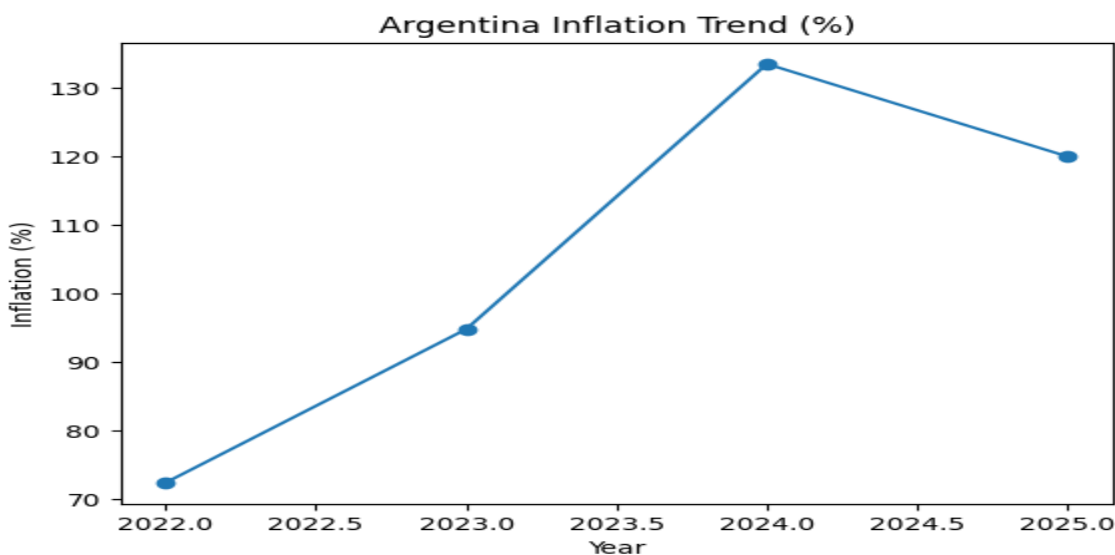
Sources: International Monetary Fund (2024); World Bank (2024); Trading Economics (2025); Central Bank of Argentina statistics.

**Exhibit 2: Timeline of Key Economic Developments**

Year	Key Development
2022	Inflation rises sharply following post-pandemic recovery
2023	Currency volatility increases and reserves begin declining
2024	Inflation exceeds 130%; widening parallel exchange rate
Early 2025	Foreign exchange reserves fall below USD 30 billion
October 2025	USD 20 billion currency-swap agreement announced

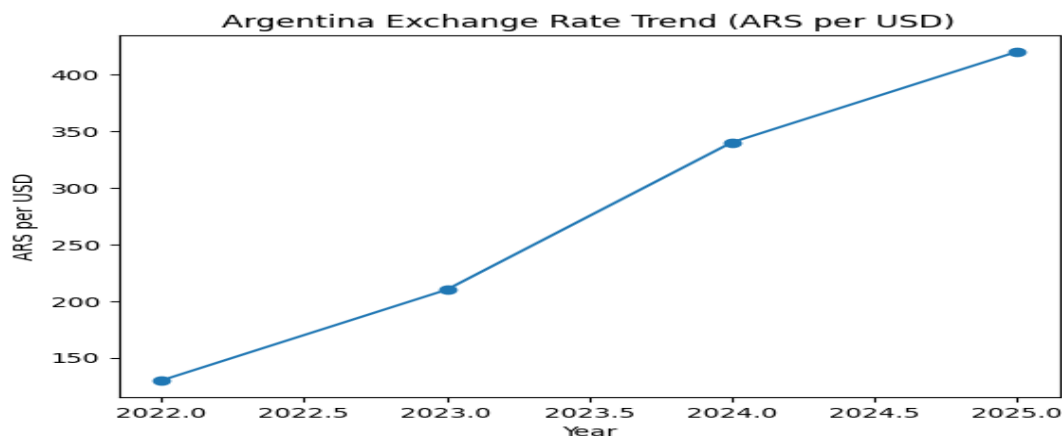
Sources: IMF reports; BCRA statistics; World Bank economic updates.

**Exhibit 3: Inflation trend in Argentina (%)**



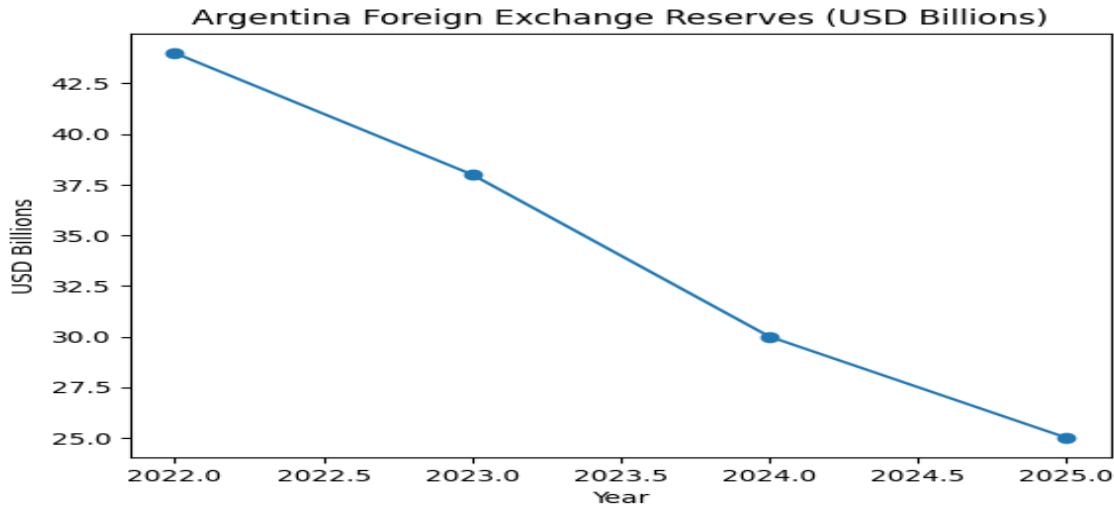
Source: International Monetary Fund (2024); World Bank (2024); Central Bank of Argentina statistics.

**Exhibit 4: Exchange rate trend of Argentina (ARS/USD)**



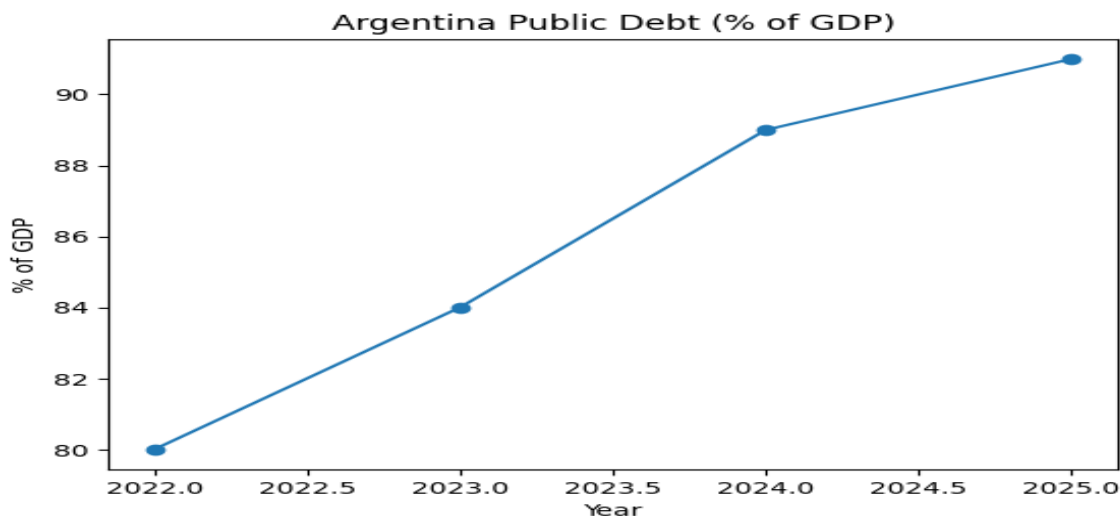
Source: Trading Economics (2025); Central Bank of Argentina.

**Exhibit 5: Foreign exchange reserve of Argentina (USD Billions)**



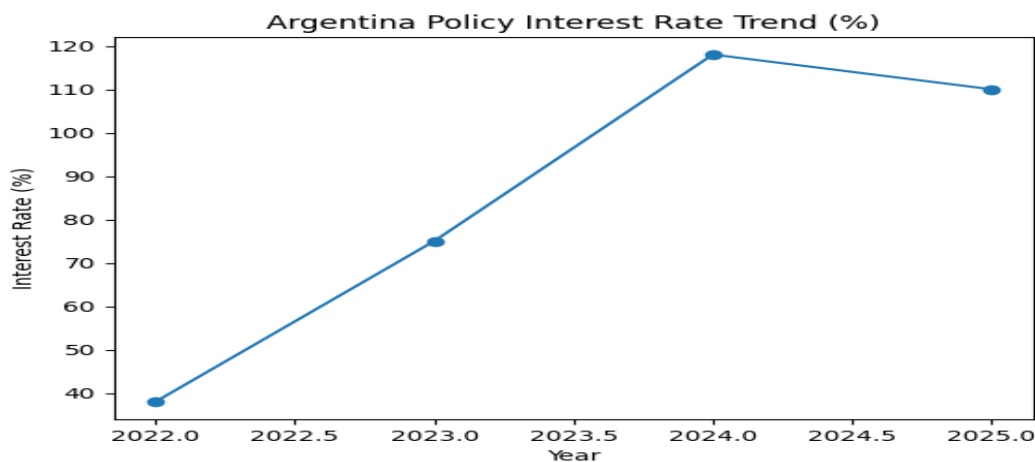
Source: International Monetary Fund (2024); BCRA statistical database.

**Exhibit 6: Public debt of Argentina (% of GDP)**



Source: IMF World Economic Outlook database; World Bank World Development Indicators.

**Exhibit 7: Policy interest rate of Argentina (%)**



Source: Central Bank of Argentina monetary policy reports.

## Teaching Note

### Currency Crisis and Geopolitics: The Case of the USD 20 Billion U.S. Backstop for Argentina's Peso

#### Instructor Abstract

This teaching note accompanies the case examining Argentina's macroeconomic crisis and the policy choices confronting its economic leadership following the announcement of a USD 20 billion currency-swap arrangement with the United States. The case places students in the role of policymakers who must decide how to respond to severe inflationary pressures, declining foreign exchange reserves and weakening investor confidence. The swap facility offers temporary access to dollar liquidity, yet it does not address deeper structural weaknesses within the Argentine economy. The case encourages students to evaluate alternative stabilization strategies, including reliance on the swap arrangement, seeking multilateral assistance or implementing domestic economic reforms. The discussion highlights broader themes in international macroeconomics, including currency crises in emerging markets, the role of central bank cooperation in the global financial system and the political economy constraints that shape stabilization policy.

#### Case Overview

The case examines Argentina's economic policy dilemma during a period of significant macroeconomic stress. By 2025 the country was experiencing extremely high inflation, declining foreign exchange reserves and growing volatility in currency markets. In response to these pressures, Argentina negotiated a bilateral currency-swap agreement with the United States that would allow its central bank to access up to USD 20 billion in dollar liquidity if required.

From a policy perspective, the swap facility represented both an opportunity and a challenge. On the one hand, the arrangement strengthened Argentina's reserve position and signalled international financial support. On the other hand, many analysts questioned whether such external liquidity could address the deeper structural problems affecting the Argentine economy.

The case places students in the position of Argentina's economic leadership at a moment when critical policy decisions must be made. Policymakers must determine whether to rely on external liquidity support, seek assistance from multilateral institutions or undertake politically difficult domestic reforms aimed at restoring macroeconomic stability. The decision requires balancing short-term financial stabilization with long-term economic sustainability.

#### Learning Objectives

The case is designed to help students develop a deeper understanding of several key concepts in international finance and macroeconomic policy.

First, the case encourages students to examine the economic conditions that often precede currency crises in emerging markets, including persistent inflation, declining foreign exchange reserves and volatile capital flows.

Second, it introduces students to the role of central bank currency-swap arrangements as instruments for providing liquidity during periods of financial stress.

Third, the case allows students to explore the distinction between liquidity crises and solvency crises, a central issue in the design of international financial rescue mechanisms.

Finally, the case highlights the political economy dimensions of macroeconomic stabilization, illustrating how political constraints and social considerations influence economic policy choices.

#### Intended Courses and Target Audience

The case is suitable for graduate-level teaching in business schools and economics programmes.

It can be used effectively in courses such as:

- International Financial Management
- Global Macroeconomics
- Emerging Market Finance
- Central Banking and Monetary Policy
- International Political Economy

The case is particularly useful in modules focusing on currency crises, financial stabilization policies and the evolving structure of the global financial safety net.

### **Research Method**

The case was developed using publicly available secondary data sources relating to Argentina's macroeconomic conditions and international financial cooperation mechanisms.

Key sources include:

- reports from the International Monetary Fund and the World Bank
- statistical publications of the Central Bank of Argentina
- academic literature on currency crises and financial stabilization
- research on central bank cooperation and international liquidity provision

The objective was to combine empirical information about Argentina's macroeconomic situation with insights from the scholarly literature on international finance.

### **Teaching Strategy**

The case works well in a class session of approximately 75–90 minutes.

A useful teaching approach is to organize the discussion around the central decision problem presented in the case.

The instructor may begin by asking students whether the currency-swap agreement represents a meaningful solution to Argentina's economic difficulties. This opening question encourages students to reflect on the distinction between temporary liquidity support and structural macroeconomic reform.

Once the discussion begins, the instructor can guide students through three stages of analysis.

The first stage involves diagnosing the macroeconomic conditions that led to the crisis. Students should identify the role of inflation, declining foreign exchange reserves and weakening investor confidence in creating pressure on the national currency.

The second stage focuses on understanding how currency-swap arrangements operate. Instructors may explain that such agreements allow central banks to exchange currencies temporarily, thereby providing liquidity during periods of financial stress.

The final stage of the discussion involves evaluating the policy options available to Argentina's economic leadership.

## Discussion Questions

1. What macroeconomic conditions led Argentina to seek a currency-swap arrangement with the United States?
2. How do central bank currency swaps function in the international financial system?
3. To what extent does Argentina's crisis reflect short-term liquidity pressures versus deeper structural economic weaknesses?
4. Should Argentina rely primarily on the swap facility to stabilize its economy?
5. What broader lessons can be drawn about financial crisis management in emerging markets?

## Analysis of the Case

Argentina's economic situation illustrates several important dynamics commonly associated with emerging-market financial crises.

One of the most significant challenges facing the country is persistent inflation. High inflation erodes purchasing power, weakens confidence in the national currency and complicates long-term economic planning. When inflation becomes entrenched, it also influences expectations, making stabilization efforts more difficult.

At the same time, declining foreign exchange reserves reduce the central bank's ability to intervene in currency markets. When investors believe that reserves are insufficient to defend the exchange rate, speculative pressures on the currency can intensify rapidly.

The currency-swap agreement with the United States was designed to address these immediate liquidity pressures. By providing access to dollar funding, the swap facility could strengthen Argentina's reserve position and reduce short-term volatility in financial markets.

However, the effectiveness of such arrangements depends heavily on the underlying economic context. If the crisis is primarily driven by temporary liquidity shortages, external financial support may help restore stability. If deeper structural problems exist, liquidity support alone may not be sufficient.

Argentina's economic history suggests that structural factors e.g. fiscal imbalances and weak monetary credibility, played a significant role in the country's recurring financial instability.

## Discussion of Policy Options

The case presents three broad strategic options for Argentina's policymakers.

One possibility is to rely heavily on the swap facility to defend the currency and stabilize financial markets. While this approach could provide immediate relief, it also carries risks. Swap transactions must eventually be reversed, meaning that heavy reliance on the facility would create future repayment obligations.

A second option is to seek financial assistance from multilateral institutions such as the International Monetary Fund. IMF programmes can provide substantial financial resources and policy guidance aimed at restoring macroeconomic stability. However, such programmes are often accompanied by policy conditions that may be politically controversial.

A third option involves pursuing domestic economic reforms designed to address the underlying causes of instability. These reforms could include fiscal consolidation, stronger monetary policy frameworks and institutional measures to improve policy credibility. Although such reforms may offer the most durable solution, they often involve significant short-term economic and political costs.

## Teaching Outcomes

By the end of the discussion, students should recognize several important insights.

First, financial crises in emerging markets are rarely the result of a single factor. Instead, they typically arise from the interaction between domestic economic policies and international financial conditions.

Second, international financial cooperation mechanisms e.g. central bank swap lines, play an increasingly important role in the global financial system by providing liquidity during periods of market stress.

Finally, sustainable macroeconomic stability ultimately depends on credible domestic economic institutions and policies. External financial support can provide temporary relief, but it cannot substitute for effective economic governance.

## Epilogue

Instructors may conclude the discussion by encouraging students to reflect on the broader implications of Argentina's experience. The case highlights the challenges that many emerging-market economies face in balancing short-term stabilization with long-term structural reform.

While international financial support can help prevent crises from escalating, the long-term stability of an economy ultimately depends on domestic policy credibility, institutional strength and the ability of governments to implement difficult reforms.

## REFERENCES

1. Allen, W. A., & Moessner, R. (2010). Central bank cooperation and international liquidity provision. *International Finance*, 13(2), 215–235.
2. Bahaj, S., & Reis, R. (2022). Central bank swap lines. *Review of Economic Studies*, 89(4), 1654–1692.
3. Bird, G. (2007). The IMF: A bird's eye view of its role and operations. *Journal of Economic Surveys*, 21(4), 683–745.
4. Blanchard, O., & Johnson, D. (2013). *Macroeconomics* (6th ed.). Pearson.
5. Bordo, M., Humpage, O., & Schwartz, A. (2015). *Strained relations: U.S. foreign exchange operations and monetary policy in the twentieth century*. University of Chicago Press.
6. Calvo, G. (1998). Capital flows and capital-market crises. *Journal of Applied Economics*, 1(1), 35–54.
7. Corsetti, G., Guimarães, B., & Roubini, N. (2006). International lending of last resort and moral hazard. *Journal of Monetary Economics*, 53(3), 441–471.
8. Drazen, A. (2000). *Political economy in macroeconomics*. Princeton University Press.
9. Edwards, S. (1989). *Real exchange rates, devaluation, and adjustment*. MIT Press.
10. Eichengreen, B. (2011). *Exorbitant privilege*. Oxford University Press.
11. Frenkel, R., & Rapetti, M. (2010). Economic development and the international monetary system. *Journal of Post Keynesian Economics*.
12. International Monetary Fund. (2024). *Argentina Article IV consultation report*.
13. Krugman, P. (1979). A model of balance-of-payments crises. *Journal of Money, Credit and Banking*.
14. Kydland, F., & Prescott, E. (1977). Rules rather than discretion. *Journal of Political Economy*.
15. Mankiw, N. G. (2019). *Macroeconomics* (10th ed.). Worth Publishers.
16. Mundell, R. (1963). Capital mobility and stabilization policy. *Canadian Journal of Economics and Political Science*.
17. Obstfeld, M., Shambaugh, J., & Taylor, A. (2010). Financial stability and reserves. *American Economic Journal: Macroeconomics*.
18. Reinhart, C., & Rogoff, K. (2009). *This time is different*. Princeton University Press.
19. Rodrik, D. (2006). The social cost of foreign exchange reserves. *International Economic Journal*.
20. Sargent, T., & Wallace, N. (1981). Some unpleasant monetarist arithmetic. *Federal Reserve Bank of Minneapolis Quarterly Review*.
21. Stiglitz, J. (2002). *Globalization and its discontents*. W. W. Norton.

22. World Bank. (2024). World development indicators.
23. Trading Economics. (2025). Argentina inflation and macroeconomic statistics.
24. Central Bank of Argentina (BCRA). Statistical database.
25. OECD. (2025). OECD economic outlook: Argentina.