



What went wrong in Latin America? The Failures of Import-Substituting Industrialisation

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Let's put ourselves in the shoes of an immigrant from Italy before the First World War, pondering where to settle in search of a new life. Our choice would be to catch a steamship from Genoa or Palermo to New York or Buenos Aires. In 1910, it would be a marginal decision – after all, Argentina was one of the wealthiest countries in the world. The choice made then would have consequences for the migrants' descendants a century later.

Let's look at the differences between income levels in the two countries, and with other settler economies that exported primary products, such as Canada.

As we see from the graph, going to Argentina was not such a bad choice. In 1900, Argentina was among the top five countries in terms of income per head, ahead all of Europe except Britain and on a par with other settler economies. According to one estimate [della Paolera and Taylor p 3] Argentina's income per capita rose from 67 per cent of developed country level in 1870 to 90 per cent in 1900 and 100 per cent in 1913.

It was still a member of this small group of rich countries in 1929 – but from 1960 it would have been better for our migrant's grandchildren to have stayed in Italy. As a percentage of the income levels of OECD countries, Argentina fell from 84 per cent in 1950 to 65 per cent in 1973 and 43 per cent in 1987. By the early years of this century, income was only 40 per cent of the level of western Europe.

What went wrong? This is the 'Argentine paradox' – how to explain a 60 per cent relative drop in income levels? And it was not just Argentina - Latin America did not do well. Brazil also lagged; and Chile only pulled ahead since the 1970s.

To understand the trajectory of Argentina, we should start from its economy before the First World War – the pattern established then led to

- Social and political problems that disrupted the economy and its ability to sustain growth and high incomes.
- A strategy of economic nationalism based on import-substituting industrialisation – an attempt to develop local industries that would replace imports of manufactures from Europe and the United States.

ARGENTINA FROM INDEPENDENCE TO THE 1920s

Independence from Spain in 1810 was followed by a long period of turmoil and warfare:

- The Spanish viceroyalty broke into different states with competing claims over territory – war with neighbouring countries of Uruguay, Chile, Brazil.
- Linked with expansion of territory from area around Buenos Aires into the pampas and Patagonia – the war of the desert of 1833-4 and the conquest of the desert in 1870s-80s.
 - o Involved defeat – or genocide – of indigenous people.
 - o Suppression of gauchos: itinerant horsemen, usually Indian mothers and Spanish fathers – roamed the pampas, living off feral wild horses, cattle and game. Had fought in wars of independence and in

desert, but as cattle ranches expanded and were fenced off with barbed wire from the 1870s, they were forced to work on ranches as peons or move into towns.

A more settled political system with election of Julio Roca as president in 1880 – a leading general in the conquest of the desert. He and other men of 1880 continued to be powerful, and Argentinian politics were dominated by the Partido Autonomista Nacionalista up to 1916. Despite a wide franchise, the PAN retained power by ballot rigging, intimidation and, if all else failed, the president could impose his wishes.

This oligarchic autocracy was unlike other settler societies such as Canada and Australia which were not militarised, no civil war or conflicts with neighbours. To some two Australian historians [Duncan and Fogarty] ‘the contrast between the stable, flexible government of Australia and the bad government of Argentina is the key difference’. No dictatorship/military coups, repression and the ‘disappeared’.

The government encouraged European migrants to replace what were viewed as uncivilised gauchos: migration started on a large scale in the 1870s, attracted by high wages. By 1914, 40 per cent of the population was foreign born. Many were Italian – distinct from older Spanish migrants; urbanised with socialist and anarchist sympathies, unlike Canada and Australia where migrants were predominantly from UK. Suggested by Platt and Di Tella that a crucial difference was ‘the political tradition and the origins of the immigrant population’ from Britain compared with south Europeans in Argentina – though I will suggest more to do with systems of land tenure and resulting social structure; and level of migration and effect on wages.

Development was also heavily reliant on foreign capital, above all from Britain, to build railways to open the pampas, ports and meat packing facilities/cold stores, and to provide urban utilities such as gas and tramways in Buenos Aires which became a major world city – with a branch of Harrods, grand opera house and boulevards. Interest on the bonds and return on shares were often guaranteed by the state. The major banks were also British owned – above all the London, Buenos and River Plate Bank of 1862. The banks’ role was to service production of commodities for export. Argentina was part of the informal British empire.

British overseas capital calls for Argentina 1865-1914: 22.4 per cent to government; much of remainder for railways – 57.5 per cent, followed by 8.9 per cent to utilities. It was the third largest destination for British capital between 1865 and 1914: US was first with 20.5 per cent, Canada second with 10.1 and Argentina third with 8.6, just ahead of Australia with 8.3 per cent. Australia became less dependent on inflows – 1880s about half of its capital accumulation; 1900-10 turned negative. Foreigners only owned about 20 per cent of Australian capital stock in 1913 compared with 48 per cent in Argentina.

Note difference from the other settler economies:

- Argentina domestic savings rate was about 10 per cent lower than in Australia and Canada between 1900 and 1929 – largely explained by the higher dependency rate in Argentina. A higher proportion of capital came from outside in compensation.
- The costs of this capital were higher.
- Payment of interest and dividends was a large proportion of government revenue.
- Politics different: in Australia, 65.8 per cent of capital went to government so loans were in the hands of representative bodies; and most non-governmental loans were in hands of Australian owned and operated concerns. Although there was resentment at cost of loans in Australia in the great depression, it was on nothing like the scale of Argentina.

The result of this economic system was an alliance between British capital and owners of the large estancias that developed on the pampas which flourished in the later nineteenth and early twentieth centuries on the basis of an export economy based on wool, beef and wheat. If you are so minded – and rich enough - you can now visit them for luxurious outdoor holidays.

These estancias had started before independence but expanded in the early nineteenth century. At this point, cattle and sheep roamed large tracts of land, used slaves until around 1850 when replaced by free labour of peons. Large number of sheep from around 1850 providing wool to Britain. Before the development of refrigeration, cattle were used to supply hides, and carcasses of cattle and sheep were boiled down to produce tallow.

In 1854, Argentinian exports to Britain amounted to £1.3m of which 33.4 per cent was hides, 8.3 per cent wool, and 31.9 per cent tallow – together 73.6 per cent.

In 1870, export to Britain had risen to £2.4m of which 15.3 per cent was hides, 2.6 per cent wool and 27.7 per cent tallow – together 45.6 per cent. [data from Amaral, *The Rise of Capitalism on the Pampas*, pp230-1]. The nature of Argentina's export was starting to change with the export of better-quality meat and also wheat.

How did the cattle economy work?

- Cattle were bred on the pampas on improved pasture.
- Sent to fatten on better pastures on coast. Meat trade was initially in jerked beef – sun dried, salted – to Cuba and Brazil, for slave plantations and canned corned beef. In the last quarter of the nineteenth century, moved into better quality beef – selective breeding of cattle, fencing of land, grew alfalfa as a fodder crop and wheat for export – improved the land. Shifted to better quality for European markets - frozen and later chilled beef. Exports of jerked beef fell from 42,838 tons in 1894 to 2,383 in 1914; frozen beef rose from 267 tons to 328,278; and chilled from nil to 4,069 tons (see table).
- Some huge enterprises: San Jacinto hacienda had 100,000 cattle, 100,00 sheep and 10,000 horses on 244 square miles.
- Despite power of cattlemen, slaughter and meat packing was usually controlled by foreign interests and dominated by a few firms. Cattle were bought and processed by the frigorificos and not on behalf of the estancieros. The packers made agreements that controlled the market by 1911.
- Meat sent in refrigerated ships to cold stores in the docks in London and at Smithfield. One of the largest firms was started by William Vestey (1859-1940). His father, a provision merchant in Liverpool, sent him to the USA in 1876 to buy produce – started making corned beef, shifted to Argentina in 1890 and opened his first cold store in Liverpool the same year. Owned Union Cold Store, the Blue Star line and a chain of 2,635 butchers' shops, as well as cattle stations. He was skilled in tax avoidance as well as business, and the family remains one of the richest in Britain.

The system created an alliance of breeders, fatteners, railways, meat packers. A narrow oligarchy of large landowners dominated the government, represented by the Sociedad Rural Argentina, unlike small farmers in other settler societies. They worked with British capital in a common interest in expanding exports.

At the end of the nineteenth century, there was also a growth in wheat production for export – acreage rose ten-fold between 1890 and 1914. Wheat farming was on a different basis from Australia and Canada.

- In Argentina there were some small-family-owned and farmed properties – but more were tenants with the land held by large owners who could turn it over to cattle, a flexible system which allowed an easy switch from cattle to wheat and back. The tenants – many of them Italian – held the property for three years, employed peons and Italian migrant workers, to produce as much wheat as they could before moving on. The Argentinian tenant farmers were nomadic – not settled, lived in temporary huts. Community life was weak – less democratic politics, large landowners had enormous political power.
- Reflected land policy: control of distribution of land was a matter for the provinces under 1853 constitution rather than the federal government. In Santa Fe, the provincial government gave some support to small farmers, but the largest province of Buenos Aires did not. Most land was held by large estates, an established landed elite.
- Tenancy often required crop of alfalfa to be planted in the first year – would last for about 15 years, so remained when tenants moved on. Estancieros saw agriculture as subsidiary to cattle ranching.
- The profit margin after paying rent was not sufficient to buy the land. They depended on credit, and they sold to a few large firms which controlled the market.
- Immigration was encouraged to Europeanize Argentina – meant lower wages, large share of profits to landowners.

Contrast with prairies of Canada:

- Family farms had ownership or secure tenancies. This reflected land policy – the federal government held most land, no established landed elite. In Canada, the homestead policy of 1872 followed example of USA in 1864 – distribution of land to owner-operating farmers.

- Settled population, built houses and communities with schools, cooperative ownership of grain elevators, active associational life.
- In Canada, as in Australia, more limited migration meant higher incomes and productivity.

The difference in social structure is clear in a comparison of the grain belt of the Canadian prairies and pampas.

	Percentage of farmers	
	Canadian prairies 1911	Argentinian pampas 1912-13
Owners	89.3	32.6
Renters	5.2	55.9
Other	5.3	12.3

Source: Solberg in Platt and Di Tella, p. 56.

The prosperity of Argentina before the First World War therefore rested on a particular set of circumstances that limited the prospect for longer term growth. Strains were apparent before 1914:

- Debt and finance: the private sector and government borrowed heavily, with servicing the debt a high proportion of revenue. Hit by recession in 1890, government responded by printing money, led to a loss of confidence. Exposed Baring Brothers – the dominant merchant bank in lending to Argentina - which had taken risky investments. It was unable to sell bonds, had to be bailed out by the Bank of England, serious financial crisis.
- The political order in Argentina was challenged – corruption of government, lack of political freedom and rights, sold out to foreign interests. In Argentina, Revolution of the Park in 1890: the Civic Union protested against corruption of the government which meant ‘political life has been turned into a for-profit industry’; it called for political rights and freedom. The president resigned but little else changed - the army stayed loyal and the alliance between British capital and Argentinian landowners was restored. PAN regained control through rigging votes, gerrymandering, presidential controls.
- Anarchism, syndicalism and socialism among immigrants in Buenos Aires. The anarchists wished to overturn the state; socialists and trade unions were more pragmatic.
- Grievances of tenant farmers who went on strike in 1912, created the Federacion Agraria Argentina with a socialist president. Hopes of a rural-urban alliance did not materialise – their interests were too different. The landowners did make concessions: five year contracts, compensation of improvements made to the land by tenants, more freedom to sell in the best market. But landowners remained in control – a conservative rural elite.

Roca returned as president in 1898 and faced strikes by workers and challenges from anarchists. In 1891, the Civic Union had split when its leader reached a deal with Roca - the Radical Civic Union led uprisings in 1893 and 1905 under its leader Hipolito Yrigoyen – opposed the oligarchy of Roca, drew together middle class, businessmen, rural workers and settlers, some cattlemen members of army but not the Socialist Party. The uprising failed and both RCU and socialists were repressed. In 1906, an amnesty which was followed in 1912 by secret ballot and universal franchise. The PAN hoped concessions would secure support and that it could work with the RCU – failed, and in 1916 Yrigoyen became president. The dominance of PAN ended but Yrigoyen did little to overturn the existing structure. He did not control parliament where conservatives blocked reform; in any case, he still hoped to continue the export model of growth. After the war, he combined repression of strikes in 1919 with concessions of minimum wage legislation in 1921.

The basis for Argentinian prosperity before 1914 was therefore fragile: it rested on a combination of exports dominated by great landowners, financed by British capital that led to a corrupt oligarchic government with support of army. It faced opposition from a variety of interests – urban workers, small farmers, urban middle class who thought that national interests had been abandoned. This system was to face serious challenges between the wars.

THE GREAT DEPRESSION AND THE TURN TO IMPORT SUBSTITUTING INDUSTRIALISATION

Argentina prospered in an open world economy that existed before 1914 – free movement of capital and labour, open trade. Alan Taylor, a leading economic historian of Argentina, remarked that “A high-immigration and high-overseas borrowing strategy could work in a liberal world order characterized by free migration and internationally mobile capital.” It could not work after the war when these conditions changed.

The end of this era of globalisation after the war had a major impact on Argentina – as indeed on Canada and Australia, though as we will see policy choices made Argentina much worse.

The result was to undermine the model of growth that existed before 1914:

- Decline in migration, though did recover somewhat.
- More important – change in international capital markets. Flows of capital from overseas British – and other - capital stopped during the war and did not recover to the same extent. Investment boom before 1914 now ended. This general decline in capital flows hit all importing countries but particularly Argentina which was unusually reliant on inflows– foreign investment was 4.15 per cent of GDP in 1900, falling to 1.1 per cent in 1929 and 0.12 per cent in 1950 [Taylor 1998 p. 153]. Argentina had relied on inflows to compensate for low savings before 1914 – no longer feasible. Low domestic savings, fragile financial system, and capital was expensive. Foreign owners held 47.7 per cent of Argentinian capital stock in 1913; in Australia only 20 per cent, much less dependent on foreign inflows. In Argentina, fell to only 20.4 per cent in 1940 as a result of falls in inflows – had to rely on domestic accumulation which was much weaker. A big different in domestic savings rates:

	1900-13	1914-29
Argentina	4.5	5.0
Australia	15.6	13.4
Canada	15.9	16.6

Taylor, 1992 p. 922

Argentinian capital stock had grown by 4.8 per cent a year 1900-13; fell to 2.2 per cent 1913-29 - a remarkable drop. Shortage of investable funds contributed to the relative decline of Argentina. Led to lower capital intensity and productivity than Australia and Canada. Capital intensity fell in Argentina between the wars: had been converging with Australia before the war, now diverged.

- End of expansion of the frontier and comparative advantage of exports of primary commodities: extensive growth strategy reached its limits.
- Crash of 1929: trade volumes fell from about 80 per cent of GDP to 20 per cent – see graph. Argentina had extreme dependence on export markets which had serious economic impact.
- European countries restricted access to their markets to protect their own farmers. In 1932, Britain gave preference to food from its Dominions of Australia, New Zealand, Canada.
- Policy differences reflecting political calculations. In Canada in the 1920s, the leading Liberal politician needed electoral support of farmers. In Argentina, Yrigoyen did not rely on farmers on the pampas who were less likely to vote; instead, needed support of urban voters in Buenos Aires and the Radicals.
- Reflected in different experience with wheat: Canada pulled ahead in quantity and quality. Argentina was competitive before the First World War with cheaper labour, better environment, and access to coast; but after the war Canada benefited from agricultural research and education, grading and standardisation of wheat, better marketing through cooperative elevators. In 1910-14, Argentina produced 147.1m bushels a year compared with 167.5 m in Canada; by 1927-32, 249.2m compared to 416.6m.

- Also, Canada favoured export oriented industry, which was more possible given close links with US, unlike Argentina which turned to ISI.

Other primary producers in Latin America had similar difficulties – coffee in Brazil, copper and nitrates in Chile.

- Terms of trade moved against primary producers - that is, prices of agricultural goods fell relative to manufactured imports by between 21 and 45 per cent from 1929 to 1933. This decline in the purchasing power of exports was extremely serious.
- The economies of Latin America were highly dependent on trade. In 1928, exports from Argentina were 22.0 per cent of GDP, in Chile, 31.3 per cent and in Brazil 14.1 per cent.
- Government revenues were dependent on duties on trade. In Argentina in 1929, 47.1 per cent of tax revenue came from import duties and 2.5 per cent from export duties; in Chile 36.8 and 27.2 per cent, and in Brazil 23.0 and 10.7 per cent.
- The fall in commodity prices and reduction in the volume of world trade had serious consequences. If exports were 30 per cent of GNP, and the terms of trade deteriorated by a third, there was an immediate loss of 10 per cent of GNP, even without a drop in trade volume.
- Servicing of the large external debt rose to as much as 70 per cent of government revenue because of the collapse in income from exports and devaluation of local currencies. Foreign investment dropped, so that rolling over loans became more difficult, and many countries defaulted, depreciated currencies.

The general response in Latin America was to turn away from export-led growth to import-substituting industrialization, developing local industries to replace imported manufactures, often complemented by labour codes that gave a right to unionise within a corporatist system of conciliation boards representing workers, employers, and the state, as a way of containing radical working-class movements.

One of the best examples was the policy of Getulio Vargas who became president of Brazil from 1930. He introduced tariffs on goods that could be produced at home with exceptions for those needed for industrialisation. He realised he needed foreign exchange to develop industry and that farmers needed income to buy domestically produced goods – hence a need to support coffee growers. In Brazil, as elsewhere in Latin America, traditional exports could not be neglected - they were a large part of the economy. Currency depreciation in response to balance of payments deficits raised the cost of servicing the external debt – it also made their goods cheaper in export markets and increased the price of imported goods, so encouraging import substituting industrialisation. Vargas combined the ideas of Italian fascism and Salazar's Estado Novo in Portugal – nationalist policies of autarchy, a claim to unite workers and employers in a nationalistic, corporatist economy, based on state planning and the creation of major new industries.

What about Argentina? The political situation in the 1920s was unstable. Yrigoyen was forced out of the presidency, the RCU split and the old ruling elite returned. There were continued threats from anarchists and the emergence of Liga Republicana based on Italian fascism. Yrigoyen returned as president in 1928 and offered to improve rights to workers – but continued political unrest and the impact of the depression led to an army coup in 1930 that removed the RCU from power and repressed the opposition.

The leader of the coup, General Jose Felix Uriburu, was part of the Nacionalista movement that had emerged before the First World War – a far right group that opposed socialism and liberalism, supported the Catholic church and large landed estates, expressed hostility to foreigners, wished to regain land ceded to neighbouring states, and aimed to create an organic, corporatist society that restored harmony between classes on the lines of the papal encyclical Rerum Novarum of 1891.

Uriburu went too far for other generals and was replaced in 1932 by a more moderate general. The government was then in the hands of military-oriented conservatives with continued conflict with radicals and fascists. This was the so-called 'infamous decade'.

- Treaty with Britain in 1933: gave Argentina access to British market for meat – but at a modest level with condition that 85 per cent from British packers, access to Argentinian markets for British goods and

concessions to British firms in Argentina. Led to outcry about surrender to Britain.

- New central bank established to stabilise currencies – advice from Bank of England, tied to private banks and Britain.
- Juntas Reguladores Nacionales to support prices, limit overproduction.
- Currency depreciation, high tariffs, controls, shift to import-substituting industrialisation led to distortions, high price for capital.
- In some provinces, more progressive policies: Luciano Molinas of Santa Fe adopted policies of minimum wages, workers' rights, public works, land reform. Opposed by central government which took control there and in other provinces.
- Protests against corruption in meat industry, selling out to foreign interests.

These tensions led to a military coup in 1943.

PERONISM

After the coup, Juan Peron became Minister of Labour. He was popular with trade unions with whom he worked on improved conditions – led to his dismissal and imprisonment from which he was released after demonstrations. He was elected president in 1946. His wife Eva was popular and politically active.

Peron advocated a policy of social justice, economic independence, and political sovereignty designed to restore the moral and material greatness of Argentina. It was a form of anti-capitalist populist nationalism, a third way between Communism and free markets.

The ideology is difficult to pin down – to some, it was a form of fascism, to others left-wing populism, or even a form of New Deal.

Peron was part of the coup of 1930 with Uriburu and some similarities with his corporatism and social Catholicism, and with Vargas. But after he lost power in 1955 and before his return in 1973, he turned to the left – supported Castro and was welcomed by Che Guevara and by Catholic liberation theology. Peronism has continued to have different ideological strands, ranging from socialist to paternalistic conservative.

After 1946, Peron set out the ideas of justicialismo or Christian national socialism. The main principles were:

- "A true democracy is that one in which the government does what the people want and defends only one interest: the people's."
- "Peronism is essentially of the common people. Any political elite is anti-people, and thus, not Peronist."
- "For Peronism, there is only one class of person: those who work."
- "Working is a right that creates the dignity of men; and it's a duty, because it's fair that everyone should produce as much as they consume at the very least."
- "The two arms of Peronism are social justice and social help. With them, we can give a hug of justice and love to the people."
- "Justicialism is a new philosophy of life: simple, practical, of the common people, and profoundly Christian and humanist."
- "As political doctrine, Justicialism balances the right of the individual and society."
- "As an economic doctrine, Justicialism proposes a social market, putting capital to the service of the economy and the well-being of the people."
- "As a social doctrine, Justicialism carries out social justice, which gives each person their rights in accordance to their social function."
- "Peronism wants an Argentina socially 'fair', economically 'free' and politically 'sovereign'."

The five-year plan for 1947-51 was devised to increase pay, achieve full employment, develop industry and improve social welfare, in close association with the trade union movement who were major figures in his government. He made an alliance with labour, with a bias against exporters. A central feature was redistribution in favour of workers through subsidies, taxation, fiscal deficits.

Used seigniorage – issuing money – to finance welfare; led to inflation. Average inflation rate from 1944 to 2024 has been about 190 per cent. Companies were not allowed to adjust their financial statements to allow for higher costs – that is taxed on increase in value created by government's inflation. This reliance on inflation and inflation tax was one of the key differences from Canada and Australia – hit capital investment, violation of property rights.

He also involved industrialists such as Miguel Miranda who had formed a close relationship with Peron from 1944 through the state industrial bank and the National Post-War Council. He supported Peron's policies of closing the gap between rich and poor, and of freeing Argentina from dependence on exports. The export sector was used to finance forced industrialisation by substitution for imports.

Making Argentina great posed a serious financial problem, not least because Peron was committed to nationalising railways and other utilities owned by British and American investors.

The answer was the Institute for the Promotion of Trade (IAPI), under the control of Miranda as president of the newly nationalised central bank. The IAPI bought the harvest from the agrarian elite; it would then be sold overseas at a large profit:

- to reinvest in state-sponsored industry and economic development.
- To finance welfare schemes and higher wages, so boosting the domestic market. In Peron's words, income should be redistributed from rich landowners who had 'raised fat cows and thin peons'.

Naturally, these policies were opposed by landowners whose interests were threatened, and there were justified suspicions that Miranda was taking personal advantage for his food-processing business and from corruption and kickbacks.

The economy was soon close to collapse. Foreign reserves built up during the war were used to pay compensation for nationalisation, to finance investment in the infrastructure, and to modernise the armed forces. The balance of payments deteriorated as a result of imports of capital goods and falling grain prices. The peso was devalued, and workers were hit by falling wages and austerity. In January 1949, Miranda was dismissed and Peron's anti-American economic nationalism was toned down.

The second five-year plan showed greater concern for agriculture. But inflation led to tighter monetary policy, cuts in spending and increased taxes, unrest – Peron was overthrown in 1955 and went into exile.

A period of coups, social unrest, violence followed with disorder from right and left. Peron briefly returned as president in 1973. He died in 1974 when he was succeeded by his wife.

RAUL PREBISCH AND STRUCTURALISTS

ISI was the preferred strategy for Latin America after the Second World War. It arose from economic circumstances of primary producers in the Great Depression but after the Second World War also had a theoretical justification from the work of Raul Prebisch – an Argentinian economist who had been head of the central bank until he lost his position under Peron.

Prebisch joined the new United Nations organisation – the Economic Commission for Latin America and the Caribbean in 1949. In 1950, his report on The Economic Development of Latin America and its Principal Problems stressed a long term trend in the deterioration of the terms of trade against primary producers caused by structural features of the world economy. Trade benefited exporters of manufactured goods at the expense of primary producers, and per capita income between the two groups of countries widened as trade grew.

He concluded that 'industrialization is the only means by which the Latin-American countries may fully obtain the advantages of technical progress'. It was a justification for ISI – but unlike Peron's domestic populism he saw a need for structural change in the world economy.

Divide between core and periphery.

- Costs were sticky in core industrialised countries because of the power of unions: labour was better able to retain gains from technical improvements.
- Trade cycle had a differential impact on core and periphery. The price of primary products rose faster than industrial prices in booms but in a slump they fell more because of workers' resistance to cutting wages in the core countries. By contrast, workers in primary producing countries could not increase wages so much in the boom or maintain them in the slump.

Unlike Peron's nationalistic approach, Prebisch and ECLAC wanted international action to shift the terms of trade by increasing the relative price of primary products and to open markets in developed economies by giving preference to less developed economies.,.

By the late 1950s, Prebisch modified his views. He accepted that there had been no alternative to ISI between 1929 and 1952 when Latin America was hit by weak markets for primary products. But he now argued that continued reliance on ISI could harm welfare.

- The small size of national markets 'often made the cost of industries excessive and necessitated recourse to very high protective tariffs' which 'generally insulated national markets from external competition, weakening and even destroying the incentive necessary for improving the quality of output and lowering costs under the private-enterprise system.'
- The 'water-tight compartments' of import-substituting national economies were too small to achieve the economies of scale for advanced industrial goods. A Latin American common market was needed to create greater regional specialisation and diversification of exports. Treaty of Montevideo, 1960 created a free trade area that eventually became Mercosur.
- Protectionism weakened productivity and the private sector by encouraging a large, inefficient state. What was needed was limited, focussed intervention to support the private sector. Private enterprise had 'tremendous possibilities', but if was to survive, it needed higher standards of living and social mobility through 'a large-scale international transfer of capital and technique', with the state providing financial assistance. industrialisation needed to be carefully planned to prevent the emergence of uneconomical industries.
- He called for a third way between foreign domination and nationalism, based on cooperation through state development programmes, reform of land tenure, encouragement of more dynamic groups in society, and the pursuit of distributive justice.

He was shifting to 'a rational policy judiciously combining import substitution with industrial exports'.

This 'outward-looking industrialisation' required developed countries to open their markets on preferential terms and to reshape the world trading system in the interests of less developed primary producers. As secretary general of the United Nations Conference on Trade and Development from 1964 he pursued this policy.

- He rejected free-trade orthodoxy on the grounds that systemic bias in the world economy reduced the benefits of trade to under-developed countries.
- He urged action to increase world prices for primary products and compensation for their trade deficits.
- Non-reciprocal, preferential treatment for manufactures from less developed countries – the Generalized System of Preferences.

His policies had little success – advanced countries had no interest in changing the shape of the world economy.

But it was becoming clear that ISI had failed and that it was hurting growth as was apparent in divergence with East Asian tigers.

- Difference in openness to world economy: Asian industry had to compete in world markets for exports, kept incentives. In Latin America, industry, workers, and consumers expected to be shielded from world markets.
- Differences in investment: in East Asian high levels of saving and investment, deepening of capital coordinated by the state; in Latin America, had followed a path of low investment.

THE END OF ISI

To understand the end of ISI, let's cross the Andes to Chile.

The major change from ISI was to occur in Chile after the overthrow of the government of Salvador Allende and the dictatorship of Augusto Pinochet in 1973.

Before the coup, the external sector in Chile was a mess:

- all imports needed a license;
- duties ranged from zero to 250 per cent;
- 10 official exchange rates;
- importers had to make a deposit of 10,000 per cent of value of imports while in transit;
- hit agriculture: high cost of fertiliser, equipment; low exchange rate hit exports;
- manufactured goods had high level of protection.

In 1955, the US State Department's 'Chile project' trained Chilean economists at the University of Chicago. From late 1950s, war of ideas:

Chicago Boys based at the Catholic University favoured free trade and argued against economists based at the University of Chile who favoured Prebisch's structuralism and ISI.

To the Chicago boys, these policies led to inefficiencies:

- Trade liberalisation would benefit poorer countries.
- Over-valued exchange rate led to speculation, increased external debt, discouraged exports – should devalue, reduce tariffs and controls to improve efficiency and resource allocation.
- Price controls not effective way of redistributing income
- Freeing interest rates allow them to find equilibrium and improve economic efficiency.

At first, not make much headway – proposed in 1970 presidential campaign for the conservative candidate Jorge Alessandri. His reaction was 'Get these crazy men out of here; and make sure they never come back'. Why such hostility?

- Government argued such an approach would hurt industrialisation and import substitution.
- Devaluation ineffective because of low price elasticity of imports and exports – argued that not work in poor countries.
- Business supported ISI, with government assistance, subsidised credit, import protection, regulation to limit foreign competition.
- Difficulty of securing free trade: Chile a member of the Andean Pact, a customs union of western South America; assign manufactures to each country by regional planning authority, secure economies of scale, protected by import duties.
- Army officers not happy- most were statisticians who argued for security.

Allende won the election. What did he do?

- Socialism had to be created quickly, based on workers power.
- Wanted a planned, controlled economy.
- End power of foreign capital and latifundia; 1971 took over US copper mines without compensation; expropriated farmland for cooperatives or state farms.; nationalised banks.
- Boost demand to take up under-utilised capacity by central bank – assumed not lead to inflation.

Money supply grew 150 per cent in 1971

The 'crazy men' came back. Brought Sergio de Castro, the most senior Chicago boys into government. A major change in policies set out in *A Programme for Economic Development* – a thick document called The Brick, written by Catholic University economists before the coup, at request of senior officers. Had

considerable influence not only in Chile – basis for neoliberal revolution, not on the more fundamentalist lines of Milton Friedman but pragmatic strand of Al Harberger.

- Combined markets with decentralised planning; state had an active role in allocation – rejected classic liberalism of 19th century but also Allende’ rigid controls.
- The Brick suggested tariffs at uniform 30 per cent – not the ISI pushed by structuralists, but neither was it free trade. But then went beyond this. 1976 highest tariff was 65 per cent, most around 50 per cent. By 1978 removed all licences, quotas for 2872 goods. Within five years, well beyond The Brick. Uniform tariff of 10 per cent which ended incentives to lobby for reclassification of imports.
- Devalue the currency.
- Reduce extreme poverty through targeted rather than universal social programmes.
- Stop land reform: issue was lack of effective markets and protectionism of ISI – allow farmers to find best markets - move from traditional crops to more valuable crops to sell in north in off-season - peaches, pears, cherries, avocados.

At first, Pinochet was undecided – nationalist officers and business whose wealth rested on protectionism were uneasy. This tension continued– but he was convinced by Friedman in 1975. Castro became minister of economics and pushed ahead with pragmatic neoliberalism through market, privatisation, competitiveness in exports, attract foreign investment.

With the return to democracy in 1990, many of the ideas were continued by both Christian Democrats and Socialist governments– alongside improved welfare policies, what can be defined as inclusive neoliberalism.

ECLAC had also shifted its approach from the mid-1980s. It moved from import-substituting industrialization and a concern for the terms of trade to emphasize international competitiveness and reform of domestic production, in part as a response to the greater success of economies in East Asia.

There were some similarities with Pinochet’s advocacy of market liberalism, but ECLAC also realized that controlling inflation and increasing exports came at a cost of falling real wages, rising unemployment and growing inequality. ECLAC combined competitiveness and a more open market with an attack on poverty and social inequality, stressing that ‘the prime common task’ was ‘the transformation of the productive structures of the region in a context of growing social equity’. Changes in production should be linked with redistribution by supporting microentrepreneurs and peasants, developing social services for the poorest members of society, and using fiscal policy and public expenditure. These ‘economic strategies and policies must be applied within a democratic, pluralistic and participatory context’ that reflected majority opinion and ‘concerted strategies’ of agreements between the state and the main political and social actors. The role of the state was to create agreement on long-term aims, and to ensure that the public sector had a ‘positive impact on the efficiency and effectiveness of the economic system as a whole’. This ‘integrated approach’ gave a larger role to the state in industrial, technological and educational policy than did the ‘Chicago boys’. But there was a new approach to economic policy. ISI was now a thing of the past.

CONCLUSION

Let’s reflect on this story to pull out main reasons for the 60 per cent drop in Argentina’s relative income.

- Agrarian structure: large estates versus smaller family farms in other settler societies.
- Owners of large estates an alliance with British capital: needed to cover low savings rate but led to resentment, more than in other settler societies.
 - o Low savings rate at home, used foreign capital which more expensive;
 - o And provoked hostility – owned and controlled assets unlike in Canada and Australia.
- Political system lacked stability – autocratic power of PAN, opposition from socialists/anarchists, populist hostility to foreign control; and then turned to ISI.
- State adopted policies that limited growth – ISI distorted the economy with subsidies, controls, tariffs.
- Reliance on inflation as a strategy for finance.

We could think back to my previous lecture on South Korea and Japan: there, government ensured that not controlled by foreign capital; there was a high level of domestic savings. State had a clear industrial strategy based on exports in key sectors.

Could Argentina break from its current problems and regain its position? The prospects are not bright. ISI might be dead – but many of the other problems remain.

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