

# The rise and fall of economic development preoccupations in Argentina and the turn toward neoliberalism in the 1970s

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## 1. Introduction

It is broadly acknowledged in the literature that Argentina's first experiences in industrialisation started between the outbreak of the First World War and the Great Depression (Ferrer, 1956; Korol & Sabato, 1990; Rougier, 2017; Villanueva, 1972).<sup>1</sup> Until then, the economy was mainly based on the so-called *agro-export model*, which was established around the 1860s after Argentina's full integration into the global market. That model greatly benefited the export of staples and allowed the country to go through a relatively prosperous period, combining the natural conditions for crop production with the inflow of foreign investment devoted to building infrastructures. However, serious disruption of international conditions during the interwar period impinged on the export strategy. The challenge to the economy posed by both internal and external conditions led the country to start a complex process of industrialisation. Eventually, these early experiences would become broadly known as the first phase of import substitution industrialisation (ISI). While these experiences were not the result of any political strategy designed in advance (Ferrer, 1981), ISI arguably became the cornerstone of the development focus and debates in Latin America a few decades later.

The history of preoccupations with economic development can be viewed from two interrelated perspectives. First, development became an issue that went hand in hand with the actual historical experiences of industry following the First World War and, more intensively, after 1930. Second, development theories and discussions about them had their heyday in the 1950s and 1960s, a time when development theories from the structuralist school had already taken off in academia and policy circles. While these debates rooted their diagnoses and proposals in the real experience of past decades, it was only in the mid-twentieth century that the economic discussion centred on development issues, with economists and policy makers debating the strategies, institutions, policies and problems with a view to encouraging the process of industrialisation and making it sustainable in the long run (Altamirano, 1998). However, in the 1970s the 'old'

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<sup>1</sup> See also Di Tella & Zymelman (1967) and Díaz Alejandro (1970).

developmentalist analyses, policies and institutions targeted at industrialisation were drastically reoriented, marking the beginning of the neoliberal period.

The aim of this chapter is to offer a structured account of the transition in economic discussions in Argentina from debates on development and its relationship with industrialisation and the role of the state, to the rise of neoliberal thinking in the 1970s. In Section 2 we present the preoccupations of some antecedents of industry drawn from the first industrialisation experiences and their influence on some renowned Argentine structuralist authors. Section 3 traces the main lines of the development debates in Argentina among professional economists, policy makers and academics during the 1950s and throughout the 1960s. Then, Section 4 presents the historical circumstances that led to the end of development thought, stressing how the economic burdens that external constraints placed on the economy would later turn discussions toward prudent macroeconomic management. In Section 5 we identify the links between the rise of neoliberal ideas and some salient features of the economic policy implemented during the last Argentine dictatorship (1976-1983). We will argue that discussions on orthodox, macro-oriented policies aimed at ‘fighting inflation’ not only overshadowed discussions on development and development policies and strategies, but also became the ideological umbrella under which a drastic redistribution of income from labour to capital took place in the wake of a neoliberal policy. Section 6 provides some concluding remarks.

## **2. Industrialisation, development and structuralist ideas in Argentina**

After Argentina’s reunification in 1852, the predominant ideology was classical liberalism, based on the works of classical political economists (François Quesnay and Adam Smith, among others). It was also influenced by political events such as the French Revolution and the United States of America declaration of independence. One of the main intellectuals in this period was Juan Bautista Alberdi, whose ideas deeply influenced the content of the 1853 National Constitution. Alberdi argued for the importance of building the main institutions to develop a capitalist system of production. He viewed the constitution as “a complete system of economic policy, insofar as it guarantees by strict disposition the free action of labour, capital, and land as the main agents of production” (Alberdi, 1858, p. 363).<sup>2</sup> In other words, the constitution serves as an instrument dedicated to defending the private sector and protect it from the possible abuses of the public sector (Ferrucci, 1984). Ultimately, it attempted to promote and encourage the arrival of a foreign population and the inflow of foreign capital.

The 1853 Constitution is the basic institutional framework upon which the agro-export model was developed, an economic growth model based on the export of staples

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<sup>2</sup> Translated by the authors. If not otherwise mentioned, all translations into English have been made by the authors,

such as beef, maize, corn, and wool. Between 1870 and the late 1920s, the model worked smoothly by combining an exceptional increase in exports with a huge inflow of foreign investment in infrastructures such as harbours, railways, and several public utilities and facilities. Rising commodity prices and the exceptionally good lands of the Argentine *Pampas* ensured a prosperous period characterised by the production and exporting of primary goods to the European market (especially the UK). The current account surplus more than offset imports of both consumption and capital goods needed for the infrastructure and other domestic production (Díaz Alejandro, 1970).

The first industrialisation experiences began after signs of exhaustion of the agro-export model became apparent, particularly after the outbreak of the First World War (Rougier, 2017). These experiences essentially involved the development of ‘passive’ or ‘derivative’ branches of manufacturing, such as textiles, food, leather, construction and light metallurgy. Indeed, some of these branches, such as foods and beverages and textiles, dated back to the late nineteenth century (Rougier, 2017, pp. 25–26). It was therefore natural to assume that the evolution of the manufacturing sector would increase specialisation in these sectors (for example with the installation of big American meat-processing firms in the 1920s).

The Great Depression resulted in plunging export commodity prices and protectionist measures being implemented in the main export markets for Argentine goods (Ferrer, 1981). The development of the manufacturing sector before the recession did not eventually mean a total break with the agro-export model and now the external conditions for the continuation of solely the export strategy were so negative that it was evident that the country had to change its ‘dynamic centre’. As Ferrer (1981, p. 51) explains, by 1930, while the national elite of the *Pampas* and their main associated traders<sup>3</sup> searched for policies “to consolidate their interests, at the same time, [those policies] could open new frontiers toward national development.”

The external situation was not the only factor promoting change, as domestic conditions in the Argentine economy had also drastically altered. While in 1880 the country was home to 2 million inhabitants, by 1930 that figure had reached 12 million, thereby creating a large domestic market (Ferrer, 1981, pp. 46–47). The changes in real conditions were concomitant with words of warning before 1930 from some influential scholars. The emphasis that, since the late 1910s Alejandro Bunge (1880-1943) and his group had placed on the signs of stagnation in the agro-export model, through the *Revista de Economía Argentina* in 1918, were perhaps the most influential (Bunge, 1940; Korol & Sabato, 1990, p. 8). Their main aim was to warn about the limits associated with primary products and overspecialisation in these, the concern being that they were highly dependent on international conditions. They called for the diversification of domestic production as well as protectionist measures (Bunge, 1940). This line of thinking had an

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<sup>3</sup> According to Bunge (1940, p. 245), in 1917 sixty-two per cent of traders in the country were foreign nationals.

enormous influence on Prebisch and structuralist thought, as we will see below.<sup>4</sup> Indeed, the Argentine economy only started to reach a turning point in its economic structure during the immediate years after the Great Depression, while the first basic elements of a set of diagnoses and proposals would later become part of the structuralist thought.

The new challenges posed by the international crisis led policymakers to adopt active state intervention. Yet by 1931, the early policies implemented had a real orthodox flavour: they were aimed at cutting public expenditure and wages to balance the budget and tackle inflation. A key protagonist and supporter of such policies was Raúl Prebisch (1901-1986), later the first president of the newly created Central Bank in 1935 and a notable economist. From 1949 he heavily influenced Latin American economic thought through his role in the United Nations' Economic Commission for Latin America (UN-ECLA), broadly known as CEPAL. Prebisch, in his capacity as advisor to the Ministry of Finance in 1931, believed that a return to recovery and to business-as-usual was “around the corner” (Prebisch, 1986, p. 135); but the scale and depth of the crisis made him realise that its effects were still the main factor in the contraction of the economy, rather than excessive public expenditure or the fiscal deficit (Prebisch, 1983, p. 175 and *passim*). The crux was that the balance of payments crisis prevented it from paying for the necessary imports, and without them, any economic recovery would be further postponed.

Perhaps eclectically, Prebisch considered it necessary to implement a series of non-orthodox measures such as an increase in customs tariffs, income taxes, minimum agricultural prices, and, especially, exchange rate controls. While these measures were fully in keeping with a program of industrialisation, it was not until 1940 that Prebisch *explicitly* recognised that such policies were aimed at industrialisation. This may be because measures such as minimum prices or exchange controls were originally meant to benefit the primary sector. Prebisch (1986, pp. 133–134, emphasis added) commented retrospectively that he did not declare his economic measures to be an open industrial policy in 1931 because of the still prevalent liberal ideas held by a wide range of political parties and intellectual groups:

I personally convinced those in government of the need to apply an orthodox policy, the only path I knew in those days. I do not think it was mistaken, given the need to stop inflation and check the fiscal deficit. (...) Not all was orthodoxy. Other, heterodox measures were also adopted, such as the rise in customs both for fiscal and protectionist reasons. But I must confess that in those days *we took great care not to speak about an industrialisation policy*, since the doctrine of the international division of labour was still prevalent not just among landowners but within the political parties themselves. Even the Socialist Party accepted the doctrine of the international division of labour.

One of the salient features of the core of structuralist thought is the active role of the government in managing the economy and in redirecting efforts towards industrialisation. The basic tenets of this approach (Diamand, 1973; Ferrer, 1956;

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<sup>4</sup> As Korol and Sabato (1990) stressed, Bunge's thought was very influential during the Peronist governments (1946-1955), whose two five-year plans were drafted by José Figueroa, a former disciple of Bunge.

Furtado, 1961; Prebisch, 1950) hold that economic development should be interpreted and analysed by taking a fresh look at the reality of Latin American economies (or peripheral economies in general). While orthodox thinking holds that specialisation in production and trade according to relative factor scarcities benefits both industrialised (capital-abundant economy) and non-industrialised (labour-abundant economy) countries, structuralist thought vehemently opposes this view because the latter's prescription of specialisation would only work for *structurally homogeneous* countries that only differ in their respective factor endowments. However, a striking feature of peripheral countries is their structural *heterogeneity*, manifested particularly in the diverging productivity levels of the different sectors within their economies (Pinto, 1970).

As Prebisch showed in the famous *CEPAL Manifesto* (Prebisch, 1950), trade integration between peripheral and central countries entailed a non-uniform distribution of the fruits of technical progress between the two groups. This was especially so because the prices of raw materials and primary products exported by the periphery tended to fall more rapidly than the prices of the manufactured goods that these countries imported. Since “the reduction of income, either profits or salaries, is less difficult” in the periphery than in the centre, and since “the agricultural workers employed in primary production in the peripheral countries [are disorganised]” (Prebisch, 1950, p. 20), the reduction in profits in the centre when demand falls is partially overcome by passing on those losses to peripheral countries through the prices of manufactured goods which they must import. In addition, the different income elasticity of demand levels for manufactured goods and primary products may explain the deterioration in the terms of trade for the periphery. The continuous downward trend for the purchasing power of exports from the periphery constituted enough evidence, in Prebisch's view, to promote industrialisation that could replace some of the imported goods. Since such a tendency was an undesired result of the free operation of markets, the drive for industrialisation required the active intervention of the state through planning.

By the 1940s and 1950s, as the developmentalist school of the CEPAL strengthened its position in the region, it was customary to think of industrialisation, development and state intervention as a whole. The salient opposition to orthodox thinking in terms of state intervention naturally had Keynes' analysis of unemployment among its influences, thereby involving an examination of the lack of effective demand and the search for suitable policies. While the influence of Keynesian ideas on the structuralist school (Prebisch, 1947) is undeniable, it is important to note that CEPAL economists adopted some influential historical forerunners who had stressed the role of the state in the transformation of the economy. As noted above, this was the mark left by Alejandro Bunge on Prebisch and other structuralist authors. In relation to state intervention, in 1917 Bunge wrote:

This fact is undisputable: the country does not have the capacity to defend the national production through private initiative. If *action* is indispensable and we cannot wait for its emergence through private initiative, it is evident that it must emerge thanks to government action. It must intervene. Can it do so?

All governments in the world are actively intervening and without hesitation given the state of affairs.<sup>5</sup> (Bunge, 1940, p. 244)

Another Argentine economist of the structuralist tradition worth mentioning is Aldo Ferrer (1927-2016), a student of Prebisch at the University of Buenos Aires. His PhD dissertation (*El Estado y el Desarrollo Económico*), defended in March 1954 and published in 1956, is a clear-cut example of the structuralist vision of development, with the role of the state underlying this vision.

Ferrer saw development as an integral transformational process in which economic elements cannot be separated from the historical and political context in which the economic agents interact. In order to promote development, ISI should overcome the period of ‘derivative’ manufactured goods (1930-1953) and enhance the industrialisation of ‘dynamic’ branches such as capital equipment and machinery, infrastructure, chemicals and petrochemicals, and the iron and steel industry (Rougier & Odisio, 2012, p. 108). This is imperative for developing countries to bridge the productivity gap, because these sectors constitute the engine of technical progress and capitalisation. Industrialisation should be carried out neither too slowly (“prudent industrialisation”) nor too hurriedly (“hurried industrialisation”); indeed, development should be balanced (Ferrer, 1956, p. 202).<sup>6</sup> Industry and agriculture should develop uniformly. This is first because in overpopulated countries an ambitious industrialisation plan could accelerate the transfer of labour from the countryside to the urban centres, thus jeopardising agricultural production, which in turn “will not have the purchasing power to purchase the industrial production”. Second, in underpopulated countries producing for the world market (as in the Argentine case) the focus should be on the agriculture sector to accumulate reserves to finance the industrialisation process. The ultimate rationale behind Ferrer’s analysis is that “the promotion of *balanced development* requires the active participation of the state”, because it is “very doubtful that the private sector in underdeveloped countries would be able to carry out an endeavour of such magnitude on its own, which instead demands a coordinated collective effort” (*Ibid.*, p. 187). Ferrer’s arguments for the intrinsic necessity of state intervention derive from examining the role of public expenditure as a channel to boost production and balance divergences between “private and social interests”, which spring from the “superfluous consumption” of the highest strata of the population that jeopardises domestic capitalisation (*Ibid.*, p. 194). To counteract this structural feature, he argued that industrialisation should be based on the domestic markets.

While the country was going through a process of incipient industrialisation and recovering from the consequences of the recession (in 1935 and 1936 GDP and employment experienced positive trends, until 1937), the political scenario was characterised by conservative parties who alternated amongst themselves through fraudulent elections during the 1930s and until the mid-1940s. Thus, the economic cycle of alternating booms and recessions from 1930 had its mirror in the political cycle. ISI in

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<sup>5</sup> Official Report by the General Director of National Statistics, December 2017.

<sup>6</sup> In this sense, Ferrer’s analysis is closely related to that of Paul Rosenstein-Rodan and Ragnar Nurkse.

Argentina was rooted in the context of the interplay between the economic and political scenarios.

The influence of the Army's Nationalist Group within national politics and the rise to power of Juan Perón (1898-1974) in 1946 through free elections (re-elected in 1952), led core economic policies to be heavily focused on boosting industrialisation. Trade policies implemented by the *Instituto Argentino para la Promoción Industrial*, broadly known as IAPI, which monopolised the foreign trade of primary products, price and exchange controls, and the nationalisation of infrastructure and public utilities were amongst the most important policy measures of the concerted economic efforts to change the 'dynamic centre' of the economy. The rise of *Peronismo* at the same time meant a progressive redistribution of income, implementing direct allowances for the unemployed, institutionalising trade unions, holiday pay for workers, building civil constructions, and implementing a minimum wage policy—all measures intended to increase the domestic market to absorb the output of the new manufacturing branches. This scheme allowed the authorities to continue to rely on primary exports to finance the necessary imports of inputs and capital goods to keep the economy growing. As documented in Vernengo and Pérez Caldentey (2014), some elements of the Peronist economic policies had already been seen in the so-called *Plan Pinedo* (actually drafted by Prebisch in 1940), which in fact had never been approved.<sup>7</sup>

However, the economic cycle of the Peronist period was subject to the structural problems of peripheral countries, as Prebisch (1950) pointed out. Indeed, the deterioration in the terms of trade between the late 1940s and early 1950s entailed a drastic fall in the value of exports and therefore a reduction in the necessary imported goods. Argentine GDP grew at an annual rate of zero during 1948-1952, while real wages started to decline in the early 1950s due to inflationary pressures. As Rougier (2017) comments, after 1953 or 1958 a new phase in ISI in Argentina would begin.

Conflicts and disputes between the traditional elite and the Peronist government became more acute, and these were manifested in opposing economic policies aiming at the same objectives. While the traditional elite wanted to restore their power focussed on agricultural exports, the new industrialist bourgeoisie, together with a wide spectrum of the working class, supported Peronist policies. In the political sphere, while the Peronist government involved itself in modernising elements of the national economy (during this period there was a noticeable heavy boost for transport infrastructures, communications, education and science), it also had a particular *style* of doing politics and running the country that left little space for opposition parties to participate in the political debate, a practice seen by some opposition groups as 'authoritarian' and 'anti-liberal'. Such a state of affairs "weakened the main tenets of the Peronist project and contributed decisively to its fall. Thus, the Peronist project closed the very possibility of legitimising, on stable bases, the political power" (Ferrer, 1981, p. 54).

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<sup>7</sup> On this issue, see Llach (1984)

### **3. The consolidation of a developmentalist agenda and the rise of development preoccupations from the 1950s to the early 1970s**

After the experiences with the second Peronist government (1952-1955), and intensified by a context of political instability that led to the military coup that ousted Peron in 1955, progress in economic development came to a standstill. This background allowed the liberal strand of the debate to insist on the need to return to more orthodox policies, lifting price and trade controls and liberalising the exchange rate and prices. This was the political-economic approach seen across democratic and non-democratic administrations since the Great Depression, with the greatest crises and transitional periods being in 1930, 1943, and 1955. In fact, the divide between the two national projects meant not only a lack of cohesion between the national elite (split into those who supported the traditional agribusiness and those more favourable towards ISI and the domestic market) and the general population, but also limits on the ISI strategy carried out until then. Thus the economic cycle was not only conditioned by the world market, but also by the political cycle characterised by those antagonisms (O'Donnell, 1977). In a context of political and social conflict, there were attempts in the debate to associate ISI with the fiscal deficit and rising inflation. Remarkably enough, the stress on inflation, the liberalisation of the exchange rate and the losses suffered by the agro-export elite due to the Peronist price control policies were at the top of the agenda for debate in 1955 (Heredia, 2015).

However, the divide in the economic debate in Argentina did not exclusively refer to the rift between liberals and industrialists. While the actual content of economic policies and recommendations by CEPAL and Prebisch were quite similar to both that seen during the Peronist period (1945-1955) and to the policy seen during the democratically-elected Frondizi administration (1958-1962), the intellectuals advising and ideologically supporting the latter often criticised CEPAL's economists. This was the case for Rogelio Julio Frigerio (1914-2006), a key advisor of Frondizi and founder of the so-called *Pensamiento Desarrollista* in Argentina (Altamirano, 1998). For him, intellectuals linked to the ideological right, the economists from CEPAL, and the intellectuals of the Communist and Peronist Parties, all comprised the "ideological spectrum of anti-developmentalism" (Frigerio, [1967] 1983, p. 16). Hence, the ideological divide within developmentalists was *also* a salient feature of Argentine society in the 1950s.

Indeed, Prebisch, who was working in Santiago de Chile as CEPAL's executive secretary, reappeared on the national political scene in 1955, appointed to draft a report on the economic situation and provide key proposals for economic recovery. The *Informe Prebisch*, as the report was known, basically had two purposes. First, the plan envisaged an orthodox set of policies such as devaluation of the national currency, liberalisation of markets, and free entry and exit of foreign capital. However, secondly, the plan itself



recommended addressing long-term issues, such as the backwardness of agriculture and the still incipient diversification of the manufacturing sector. To cope with these challenges, the report recommended the introduction of technology into agriculture to boost production so that an increase in agricultural exports could help the industrialisation process through providing foreign currency (Altamirano, 1998, p. 76). For the manufacturing sector, the aim was to boost the steel, mechanical engineering, paper and pulp, petrochemical, and basic chemical industries, to extend railroads and to increase the state-run oil production and electric capacity. As Sikkink (1988, p. 97) points out, Prebisch “advocated adopting a development program, based on the in-depth CEPAL study [the 1950’s CEPAL Manifesto] to plan long-term capital investments.” Eventually, Prebisch’s recommendations were not put into practice, except the orthodox proposal of currency devaluation and the creation of the National Agricultural Technology Institute (INTA), whose aim was to develop technical and scientific methods to increase agricultural productivity. Measures aiming at boosting certain key manufacturing sectors were barely applied. Part of the failure to apply Prebisch’s plan was the result of many anti-Peronist policy makers during the *Revolución Libertadora* in 1955-1958 not being supporters of the various developmentalist elements present in the report. In addition, those who opposed the military government in 1955 strongly rejected the Prebisch Plan. For example, intellectuals connected to the Peronist movement, such as Arturo Jauretche ([1955] 1973), criticised the report by pointing exclusively to the orthodox and liberal elements while ignoring the developmentalist elements that it in fact endorsed (Vernengo & Pérez Caldentey, 2014). As Sikkink (1988, p. 96) puts it, the political context characterised by a national political and ideological divide left “little intermediate space for Prebisch’s developmentalism”.

In the late 1950s, the *Frigerista* group’s opposition to Prebisch and CEPAL was basically due to associating Prebisch with both the economic policies of the 1930s and the 1955 economic report for the military government. Rather than a theoretical disagreement, differences were largely motivated by the domestic political context. While the Peronist party was banned, the political campaign run by Frondizi and the Radical Party for the 1958 elections was characterised by their efforts to attract the Peronist vote. This could perhaps explain why Argentine *desarrollismo* was opposed to Prebisch’s *structuralism* (Altamirano, 1998).<sup>8</sup>

Despite the deeply rooted association made by certain intellectual groups between Prebisch (and CEPAL) and anti-Peronism in the 1950s and 1960s, the dominant structuralist ideas in CEPAL were widely disseminated in both academic and policy-oriented institutions. To begin with, in 1958 there was a change in the curriculum of the Economics course at the University of Buenos Aires, introducing economic development content based on the ideas of CEPAL and Prebisch. In addition, worthy of a mention is the setting-up of the national academic journal, *Desarrollo Económico*, in 1958,<sup>9</sup>

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<sup>8</sup> See also Portantiero (1977).

<sup>9</sup> Volume 0 was published by the end of 1958 and throughout 1959, while Volume 1 was published in 1961.

publishing important works on economic development and industrialisation by national and international scholars. This had a lasting impact. These developments in the world of ideas naturally shared basic common ground rooted in policy-making, not only during the period of Frondizi (1958-1962), but also even later during both democratic and military governments until 1976. According to Altamirano (1998, p. 79), discussions about development issues thrived in Argentine intellectual and policy institutions for at least twenty odd years after 1955.

That common ground of ideas took root in the economic performance of the economy during those years. The positive trend in manufacturing output and employment made industry the dynamic core of the economy, especially after the mid-1960s (see Table 1). However, the industrialist project, while on the whole opposing the agro-business, required the foreign currency created by exports, which were mostly comprised of agricultural goods. Indeed, the political cycle was economically linked to the decline in the terms of trade for agricultural commodities in the 1960s and this deepened the political disputes within the elite, finally leading to a fresh military coup in 1962 against Frondizi. In 1963, new free elections (without the participation of the Peronist party though, as it was still officially illegal) saw the Radical party win the presidency, but in 1966 there was another military coup, led by General Onganía, which tried to restore the economy to more liberal paths.

Table 1.

|           | GDP <sup>a</sup> | Industry <sup>a</sup> | Productivity <sup>a</sup> | Real wage <sup>b</sup> | Income <sup>c</sup> |
|-----------|------------------|-----------------------|---------------------------|------------------------|---------------------|
| 1963-1974 | 5.08             | 7.13                  | 7.08                      | 100                    | 49                  |
| 1976-1983 | 1.02             | -0.52                 | -1.63                     | 78.7                   | 44                  |

<sup>a</sup> Average growth rate; productivity refers only to industry

<sup>b</sup> Average industry real wage

<sup>c</sup> Average income per capita as a share of US income per capita

Source: authors' own elaboration based on Ferreres (2009)

During the Onganía tenure (1966-1970) there was a remarkable shift in the direction of economic policy. As Wynia (1990, p. 261) documents, the fundamental problem according to Onganía's Finance minister, Adalbert Krieger Vassena, was the general inefficiency in the economy brought about by subsidised industry, undisciplined workers, and overextended welfare programmes. This description of the economy had a purely technocratic flavour, blaming the decline of the economy on the Peronist-style of state intervention by non-Peronist administrations since 1958. It is again noticeable in the public sphere how industrialisation, state intervention and welfare programmes were linked to problems of inflation and fiscal deficit. However, not even this government abandoned the industrialisation strategy, although now it had to be pursued with less state intervention and funded by foreign capital.<sup>10</sup> As in 1955-1958, during the second half of

<sup>10</sup> Indeed, this was not an unknown strategy in Argentina, as in 1958 Frondizi himself set-up a series of norms allowing foreign direct capital to be invested in the national manufacturing sectors (laws no. 14780 on foreign investments and no. 14781 on industrial promotion).

the 1960s real wages fell, the currency devalued, the rents from agribusiness increased for some years,<sup>11</sup> and inflation decreased to the lowest level since the Peronist governments (Wynia, *Ibid.*).

After internal military issues in 1970-71, the new military-appointed president, General Lanusse, not only continued with an industrialisation strategy, but expanded it by boosting heavy industry. Development institutions such as the National Council of Development (CONADE), founded in 1961, played a key role in economic planning and substitution industrialisation. In the political arena, Lanusse's administration allowed the Peronist party back into politics, which led to Peron and Peronist governments being in office from 1973 to 1976, the year of the last military coup.

In conclusion, although within a context of political instability, it can be argued that in the years before the military coup in March 1976 there was a 'developmentalist consensus' in Argentina. This consensus involved the main preoccupation being about the role of the state in managing the economy through protectionist measures, price controls, economic planning through CONADE, industrial policies, national integration, and the role of science through the INTA and the National Scientific and Technical Research Council (CONICET, founded in 1958). Indeed, a military faction was interested in national development as a way to increase the country's capacity to defend itself from outside threats (Ferrer, 1981). Differences arose, however, about the way to conduct macroeconomic policies that were compatible with such structural policies.

#### **4. The fall of development preoccupations and the rise of 'prudent' macroeconomic management**

As commented above, by the late 1960s, during the Onganía tenure, associating the industrialisation strategy with technical inefficiency, high inflation rates, public deficit, and over-staffed state-run companies turned out to be quite popular, both in public discourse and in the media. Indeed, the ISI strategy was pejoratively labelled as 'populist' economic policy or economic dirigisme.

Liberal-oriented economists argued that inflation was the outcome of uncontrolled spending by the Argentine government and general inefficiencies in industry. This was the credo of the traditional landowners of the *Sociedad Rural Argentina* that held that "the fundamental cause of [inflation] is excessive government spending" (public statement of 12/12/1978, in *Memorias SRA*, 1979, p. 60; quoted in Heredia, 2015, p. 91). Traditional monetarism served as a theoretical background to the liberal stance. Monetarism was not a new approach in 1970s Argentina. Pre-Keynesian thinking was dominant at the

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<sup>11</sup> The terms of trade experienced a rise from 1962 till 1964 and then gradually fell until the end of the 1970s (Ferrer, 2010).

beginning the twentieth century, if not in economics courses then certainly in the general approach taken by policy makers.<sup>12</sup>

However, as we discussed above, from the 1950s onwards, industrialisation and state-driven planning dominated the core of the economic debate and its teaching. Moreover, the structuralist approach offered an alternative view of inflation, according to which inflation is not the result of excessive money supply, in turn brought about by an excessive government deficit, but instead is due to structural bottlenecks of basic commodities whose price shock ripples out to the rest of the industries. How, then, did monetarist ideas revive in Argentina and gain a foothold in public policy?

First, it is important to note that by the end of the 1960s there was a global revival of liberal ideas, strongly fostered by the *Société du Mont-Pèlerin* (Mirowski & Plehwe, 2009). Secondly, while the supply of economists in Argentina had been remarkably small until the mid-1950s and early 1960s, it appreciably increased during the 1960s onwards. In particular, as Biglaiser (2009, p. 63) has documented, this was thanks to the active role of US government agencies as well as private Argentine *think tanks* that financially supported future Argentine economists as they earned advanced degrees in the US.<sup>13</sup> Economists nurtured in the works of von Mises, Hayek, Friedman (all of them linked to neoliberal thinking) started to be available in the Argentine market for economic ideas (Heredia, 2015, p. 85). Third, the influence of these *think tanks* in the economic debate started to become noticeable by the 1970s, not only because they were able to place staff as top officials in the military government (more on this below), but also because economists working in those institutions were successful in imposing the discussion on inflation and macro prudential policies over academic preoccupations, to the expense of development thought.

Turning now to the objective reasons at play, it is important to note that while the terms of trade averaged around 96 points between 1955 and 1970, this gloomy picture changed in the early 1970s, with the terms of trade rising and reaching a peak of 143 in 1973 (see Figure 1). This rise stimulated an increase in agricultural supply and reactivated the demand of industries associated with the sector (tractors and machinery). The Peronist government (1973-76) sought to redistribute the higher income of the external sector by increasing the powers of the *Juntas Nacional de Carne y Granos*, which monopolised the foreign trade of such products. There was also a system of multiple exchange rates in force. This system had promoted an illegal or black exchange rate market. By the time the Peronist government took power in 1973, the black-market premium was around 100%. The premium started to increase, reaching a peak of more than 350% by the end of 1974.<sup>14</sup> In 1975, exports fell by 1 billion dollars, partially due to a decrease in export prices, but mainly because of increased smuggling of primary commodities, stimulated

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<sup>12</sup> See Dagnino Pastore (1989, p. 196) and Biglaiser (2009, p. 66).

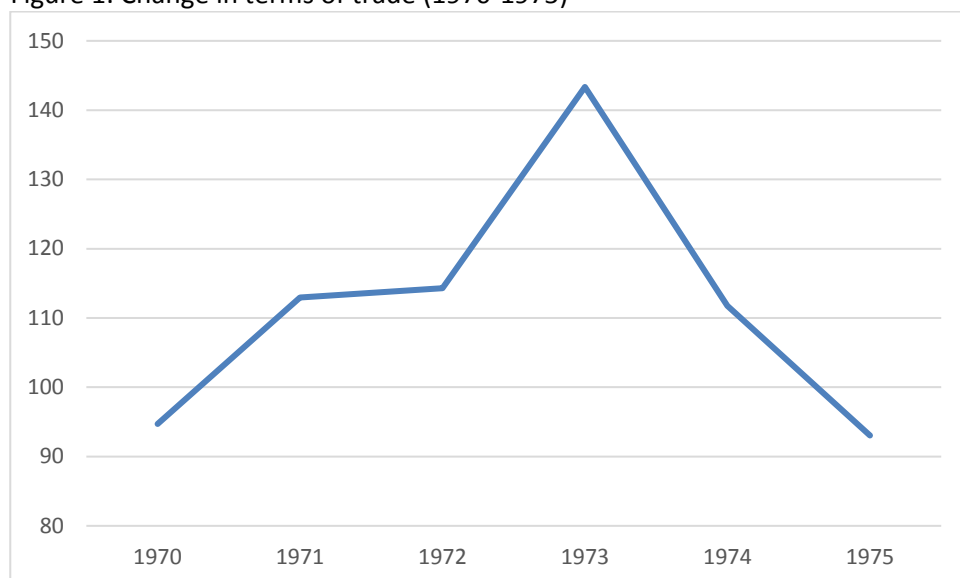
<sup>13</sup> These think tanks are *Fundación de Investigaciones Económicas Latinoamericanas-FIEL*, the *Instituto de Estudios Económicos sobre la Realidad Argentina y Latinoamericana*, the *Fundación Mediterránea* and the *Centro de Estudios Macroeconómicos-CEMA*, all founded between the mid-1960s and the early 1970s.

<sup>14</sup> Calculations based on Kaminsky et al. (2004).

by the black-market premium. Imports grew by 9% in current values with respect to the previous year. The current account deficit was almost 1.3 billion dollars and, in the absence of substantial capital imports, there was a loss of more than 1 billion in reserves.

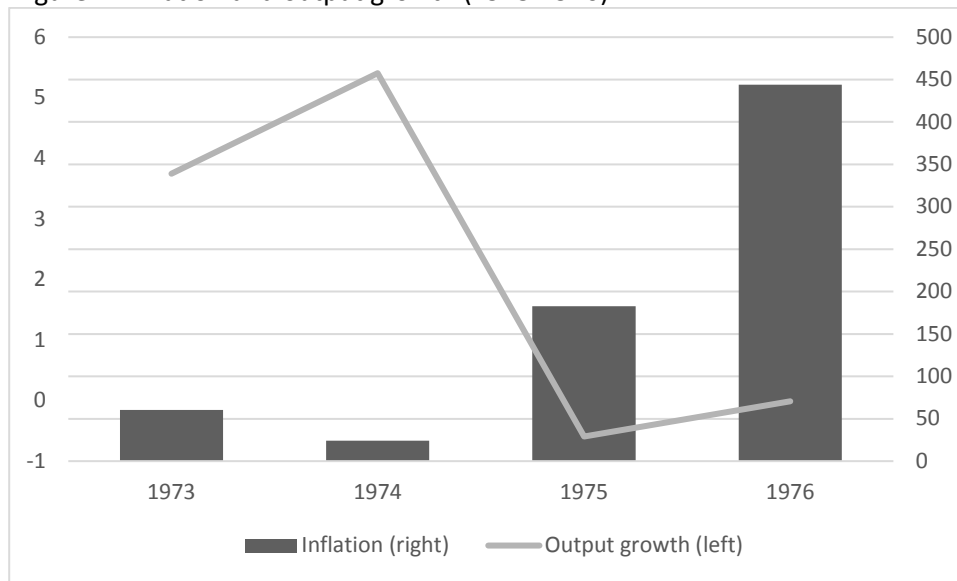
In an international context marked by stagflation in some industrialised countries due to the oil shock, the gloomy economic situation demanded immediate policies. Those adopted to avoid an external crisis were the classic ones: a strong devaluation combined with fiscal adjustment. However, the high levels of employment and the ability of unions to resist allowed them to renegotiate wages, and this led to a new round of price increases, devaluation, wage negotiations, and so on. The devaluation of the exchange rate for the year was 393%, inflation was 160%, and GDP growth fell sharply by 0.5%. Within a context of intensifying conflict, right-wing circles seized on the crisis to present it as crystal-clear evidence of the failure of the policies in previous years. The ISI growth model, according to them, was exhausted.

Figure 1. Change in terms of trade (1970-1975)



Source: authors' own elaboration based on Ferreres (2009).

Figure 2. Inflation and output growth (1973-1976)



Source: authors' own elaboration based on INDEC and Ferreres (2010).

## 5. The turn to neoliberal ideas and economic policy in 1976-1983

### 5.1. The military macroeconomic program

A group was formed around the figure of Jaime Perriau, a lawyer with close links to the military, who brought together a group of liberal-conservative intellectuals.<sup>15</sup> The main aspiration of these intellectuals was to 'refinance' Argentine democracy based on the political-ideological guidelines of the '1880s generation', the ruling elite of Argentina during the agro-export model (Vicente, 2012). The military appointed economic minister was José Alfredo Martínez de Hoz, a lawyer and member of the traditional agricultural elite.

There is evidence showing that the group acted as one of the main civil articulators of the dictatorship. It was one of the main promoters of the business lockout against the government of María Estela Martínez de Perón in February 1976, an event that the military interpreted as a sign of civil support for a coup, which took place the following month. There is also evidence that the economic plan of the military was first drafted and discussed within the group (Muleiro, 2001). The liberal faction of the military had to negotiate some controversial parts of the plan with the nationalist faction. Suggestions by

<sup>15</sup> Besides Martínez de Hoz, other members included Cardenas Madariaga and Jorge Zorriegueta, both high ranking officials in the former's ministry; Ricardo Zinn, a close advisor to Martínez de Hoz and member of the SOCMA (Sociedad Macri) group; and Lorenzo Sigaut, successor to Martínez de Hoz in the ministry.

the newly appointed economic team to reduce the fiscal deficit (one of the instruments for this being privatisation) to moderate inflation was met with opposition by different branches within the military that were unwilling to cut back on the public areas for which they had direct responsibility (Ferrer, 1981).<sup>16</sup> Notwithstanding these details, the spirit of the plan was entirely consistent with the political objectives of the military.

In the short run, the main concern of the economic team was to reduce inflation. The military economic team designed the working of the Argentine economy on the basis of Chicago's monetarism extension to international trade, proposed during the 1970s in the wake of the so-called "monetarist counter-revolution" (Johnson, 1971). This 'novel' approach provided an alternative explanation to balance of payments disequilibria based on the mismatch between aggregate money supply and the demand of a nation. The theory has two versions, one with fixed exchange rates and the other with free-floating rates. The first version is best suited for small and open economies that, in principle, do not affect international prices. In such a case, for a fixed exchange rate level, inflation in the small economy should converge to the international rate of inflation. In addition, with free international capital mobility, the domestic real interest rate is equal to the international real interest rate. Hence, within this framework, a small economy cannot determine either its money supply or its nominal interest rate. An expansion of the money supply by increasing domestic credit<sup>17</sup> (say, financing the public deficit) leads to an excessive money supply; that is, people find that they have more money than they desire. This leads to an increase in private spending which, in the context of full employment, brings about a trade deficit that drains international reserves up to the point that is equal to the total amount of domestic credit originally generated. So, financing fiscal deficits by issuing money was the main cause of the balance of payments disequilibria in Argentina, which led to a drain on the reserves that first forced a devaluation and then increased domestic prices.<sup>18</sup> The causal sequence was strictly the opposite of that advanced by structuralist theory.

It is important to note that this economic approach went beyond short-run policy recommendations. The search for 'prudent' macroeconomic management also required structural reforms in the economy that implied the dismantling (or the reorientation) of several developmentalist institutions created in the previous years. In this scenario, two crucial policies were implemented. The first was a financial reform. In the previous years, commercial banks acted as agents of the Central Bank, taking deposits on its behalf and giving loans according to certain criteria and in quantities defined by the former. In 1977, a new banking law was passed. The law was aimed at liberalising the interest rate and decentralising deposits. Banks now had to compete for deposits and were free to decide to whom they wished to lend. The Central Bank, on the other hand, guaranteed the

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<sup>16</sup> As Heredia (2015, p. 89) argues, economic decision making within the military administration turned out to be too sluggish.

<sup>17</sup> The money supply consists of, broadly speaking, the sum of domestic credit and international reserves.

<sup>18</sup> Alternatively, if the exchange rate is not fixed and floats freely, the excess money supply translates first into price increases and second into exchange rate increases.

deposits. In the next few years, the number of private financial institutions mushroomed markedly. The second was trade liberalisation. The government aspired to open up the economy and expose it to greater international competition to increase the levels of efficiency and productivity. In fact, the measures were aimed at restructuring the income of the exporting sectors. By 1978, all export taxes (*retenciones*) had been eliminated. On the import side, a progressive and programmed reduction of tariff levels was carried out. Finally, the capital account was deregulated and the exchange rate unified.

In terms of stabilisation policies, several programs were tested over a span of four years and all failed (Gerchunoff & Llach, 2010). However, by the end of 1978, there was a big shift in monetary policy. Beginning in 1979, there would be a schedule specifying the exchange rate level, thus pre-announcing the rate of devaluation over time, which eventually would reach zero. This schedule, famously known as the *tablita*, attempted to lower the inflation rate by making it converge to the international inflation rate and the expected devaluation rate.

Given that in certain periods the exchange rate was fixed, the local nominal interest rate should equal the sum of the international real interest rate plus the international inflation rate (in the absence of uncertainty). However, given that domestic inflation did not immediately converge, nominal local interest rates were higher than international ones, and given the relative stability of the exchange rate, this permitted higher yields for financial investments in the domestic currency. Since domestic inflation was higher than international inflation plus the expected rate of devaluation, then, according to the monetary approach to the balance of payments, there should be a trade deficit, even if no expansion of domestic credit occurred. Thus, reserves should go down to adjust the balance of payments. However, the differential attracted foreign capital for domestic financial investments. Another source of reserves was issuing public debt.<sup>19</sup> Thus, reserves did not fall and in fact increased. In fact, the possibility of sustaining the *tablita* depended, in the end, on the capacity to obtain finance from abroad, that is, on the capacity to import capital.

However, the economic team believed that the balance of payments disequilibrium would self-correct. This depended on the speed of reduction of inflation in non-tradable commodities. The government thought that eventually the inflation of such products would converge to the international inflation rate since the increase in the relative prices of those products should lead consumers to substitute them for tradable products, thus reducing the demand for the former. Domestic inflation and interest rates would converge to their respective international benchmarks. However, this was not the case and interest rates differentials persisted. When international credit experienced a crunch and Martínez de Hoz left the government, this generated doubts about the

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<sup>19</sup> The difficulties in reducing the fiscal deficit and the unwillingness to finance it with Central Banks loans led Martínez de Hoz to follow the alternative strategy of issuing debt denominated in domestic and foreign currency.



sustainability of the *tablita*. In the face of an imminent devaluation, there was a capital flight effectively forcing several devaluations in 1981.

## 5.2. *The impact of the macroeconomic program*

There is widespread agreement in the literature about the idea that the real appreciation of the Argentine peso was one of the causes, if not the most significant cause, of de-industrialisation (Gerchunoff & Llach, 2010; Müller, 2002; Schvarzer, 1996). According to the literature, given the low level of the real exchange rate, exporting industries lost competitiveness in international markets and domestic industries could not compete against increasing imports.

It should also be added that the new financial strategy and monetary policy, especially the *tablita*, had a strong influence on the confidence of industry by altering the incentives of business leaders. Most firms that had a positive cash flow or were able to take credit from abroad transformed themselves into financial agents. The mechanism was as follows: they obtained credit at low international interest rates in a foreign currency; exchanged this for pesos and lent it short-term at high local rates; later, they collected the interest and repayment of the loan and converted it into foreign currency or restarted the cycle. The operation was almost risk-free and extremely profitable since the *tablita* made clear when there would be an exchange rate increase; hence, the difference between the local interest rate and the expected rate of devaluation was higher than the international interest rate. The productive plant and other productive assets served as debt guarantees. Companies were bought and sold according to this capacity.

This speculative behaviour led to a substantial increase in the foreign indebtedness of private firms. The major capital flight occurred after Martínez de Hoz left office and tougher international credit conditions gave rise to successive devaluations in 1981, leading to the generalised bankruptcy of private firms. To avoid the collapse of the financial system, the government absorbed most of the private debt. By 1975, Argentina's foreign debt amounted to 8 billion dollars, while by 1983, the last year of the dictatorship, it was about 45 billion (Wynia, 1990, p. 267). This was, in the end, one of the worst legacies of the military government.

The other heavy burden left after 1983 was the shift in income distribution. As shown in Table 1 (see above, Section 3), by 1974, Argentine income per capita was about half of US income per capita, while by 1983 it represented only about 40 percent. In 1974, the share of manufacturing activities in GDP had reached almost the 24 percent, but by 1982 it was only about 18.5 percent. The real industrial wage also decreased. In the context of low output growth, this decrease meant a redistribution in favour of the owning class.

## 6. Concluding remarks

Preoccupations about economic development, the need for innovative economic policies, and an increasing awareness of more active state intervention gained strength in economic debate once the agro-export model started to show signs of exhaustion after the outbreak of the First World War. The first ISI experiences took place between the two World Wars, but they were not the result of a strategic plan. Only after 1945, with the rise of Perón to power, did industrialisation take off, guided and directed by the state through planning and sector-based policies. By that time, ISI also had the intellectual support of the CEPAL and the academic community.

The “developmentalist consensus” established itself in Argentina between the 1950s and 1970s. Despite the political instability in the country, all the political groups (civil and military) that came to power pursued, with different nuances, the objective of industrialisation. During this period, most of the developmentalist institutions prospered and the topic of development thrived both in Argentine academia and in policy circles.

However, by the end of the 1970s, the need to pursue ‘prudent’ macroeconomic management and tackle inflation started to gain a foothold in economic and public debates. This was successfully introduced into the ‘collective unconsciousness’ as the worst of all evils. ‘Prudent’ macroeconomic management entailed not only changes in the manner of conducting short-run policies but also long-term reforms in the economy, most of which implied the dismantling of several developmentalist institutions created in the previous period.

The last military dictatorship in 1976 was the propitious laboratory for the ‘prudent’ macroeconomic management experiment. The experience was a total failure, both in terms of its inability to lower inflation and to enhance output growth, but also in terms of long-run development. Looking at its results, rather than making the economy grow along a more sustainable path, one could conclude that the main objective was to redistribute income in favour of the owning class and discipline an involved workforce, whose strength had grown during the ISI.

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