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**THE ECONOMIC SOLUTION FOR ARGENTINA
(TAKING INTO ACCOUNT INTERNAL-POLITICAL
AS WELL AS EXTERNAL CONSTRAINTS)**

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PREFATORY NOTE

Eduardo R. Conesa is a Senior Fellow at the Center for International Affairs, Harvard University. He received his M.A. and Ph.D. from the Wharton School of Economics, University of Pennsylvania, in 1971 and 1972, respectively. He also holds an M.A. in Development Economics from Williams College (1969), as well as Law and Public Administration degrees from the University of Buenos Aires (1962 and 1960). From 1972 to 1978 he was an economist with the World Bank, serving ultimately as its executive director. From 1979 to 1984, Dr. Conesa was with the Institute for Latin American Integration (Buenos Aires), working in conjunction with the Inter-American Development Bank. And during academic 1984-1985, he has been with the Center for International Affairs at Harvard.

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The present paper was completed in early June, 1985, at which time the Argentine economy appeared to be on the brink of hyperinflation. Soon thereafter, the government of President Raúl Alfonsín initiated a program which included measures very similar to many of those proposed here. Thus, this paper serves both as a backdrop against which to judge the Argentine Government's current efforts and as a comprehensive proposal in its own right.

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THE ECONOMIC SOLUTION FOR ARGENTINA
(Taking into Account Internal-Political as well as External Constraints)

by Eduardo R. Conesa, Ph.D.

INTRODUCTION¹

In the post-World War II period, two strikingly opposite patterns have emerged in the world economy. On the one hand, countries like Japan and Korea have experienced extraordinary economic growth; on the other hand, countries like Argentina--which are rich in natural resources and as rich as Japan and Korea in human resources--have been unable to achieve economic growth. In this paper, I will explain why Argentina has not shared the good fortune of Japan and Korea, and thereafter I will offer a means for solving Argentina's current economic problems. That solution takes into account both domestic political constraints and those imposed by the international economic environment. Before the post-World War II period can be considered, however, it will be necessary to trace the different stages through which the world economy has evolved, paying special attention to those aspects of special relevance to Argentina.

BACKGROUND

In the early nineteenth century, economic liberalism became very attractive to statesmen all over the world. In Argentina, after independence was achieved in 1810, the liberal theories of British and French political economists--particularly Adam Smith and Jean Baptiste Say, respectively--took a strong hold among many political, economic, and intellectual leaders. Perhaps the most significant liberal argument was that for "free trade." It was clear that the principal Argentine export under free trade would be hides--not a very important product--and thus that Argentina's role in the world economy would be limited if such a system were adopted during the early 1800's.

The world economic environment changed after 1840, however, for the United Kingdom repealed the "Corn Laws" and allowed for free trade in cereal grains. Only then were the liberal concepts of specialization, comparative advantage, and economic efficiency applied to international

¹This paper is a summary of a book-length study which is currently in progress. The author thanks Professor Jeffrey A. Cole of the University of Massachusetts at Amherst for editing and making useful suggestions to this paper, which is based on a lecture given at that university. The author also thanks Dr. Barbara B. Burn, Director of International Programs of the University of Massachusetts, for inviting him to give such a lecture, and Professor Robert A. Potash, for his sharp questions and comments. Harvard University, where the author is currently working as a Senior Fellow at Center for International Affairs, provided a stimulating environment for thinking on these matters. Discussions and talks with Professors Jeffrey Sachs, Richard Cooper, Dwight Perkins, Raymond Vernon, Sam Huntington, Stephen Haggard, and Robert Kohane helped to focus the paper. Nevertheless, the author alone is responsible for any errors that the paper might contain.

trade. As a result, the British market was opened to Argentine agricultural products, but the Anglo-Argentine trade was limited because the existing means of transportation did not permit long-distance shipments of agricultural products. In the second half of the nineteenth century, however, revolutionary advances in transportation technology--the development of the railways and trans-Atlantic steamships--made free trade viable for Argentina, which could now export wheat and meat in large quantities to an expanding British market. This was an opportunity that Argentina promptly grasped.

THE LIBERAL CONSTITUTION OF 1853

Liberalism is also intimately related to Argentine political development. In 1852, General Justo José de Urquiza, a prominent provincial caudillo, took it upon himself to organize Argentina constitutionally. After surrounding himself with a number of high-level intellectuals--Dr. Juan Bautista Alberdi among others--and winning the Battle of Caseros, Urquiza imposed upon the country a constitution patterned after the United States Constitution, incorporating as well the ideas of Montesquieu and the great liberal writers of the eighteenth century. The division of powers among the executive, legislative, and judicial branches of government is very similar to that provided for by the U.S. charter; indeed, the Argentine Constitution is at times a literal translation of the corresponding articles of the U.S. Constitution. Unlike the U.S. Constitution, however, the Argentine charter prescribes a national economic program.

Basic to this economic program are: (a) the right to free trade; (b) the right to practice industry; and (c) the obligation of the Argentine government to respect free trade and the freedom of industry. Moreover, the Constitution obligates the national government to promote the importation of capital, and not only of material capital, but people as well. The Argentine Constitution calls explicitly for European immigration.

The economic bases of the Constitution are discussed in detail by Juan Bautista Alberdi in his book, Sistema económico y rentístico de la Confederación Argentina según su Constitución de 1853.² In addition to the promotion of economic freedom, Alberdi argued that the key to the advancement of Argentine industry was public education.³ Primary

²Vol. 4 of the Obras completas de J. B. Alberdi; Buenos Aires: "La Tribuna Nacional," 1886).

³Alberdi, p. 177. Moreover, the father of the Argentine Constitution argued that the reference to the promotion of industry through the temporary concession of privileges in Article 67, number 16, of the Constitution refers only to the patent law for inventions indicated in Article 17 (ibid., p. 181). This restrictive interpretation is consistent with the principle of equality under the law included in Article 16.

education, according to the Constitution, is the obligation of the provinces; secondary and university education are the responsibility of the federal government.

Thus, Alberdi felt that the best way to advance the Argentine economy was through freedom of trade, freedom of industry, and the education of the people. Two other characteristics of the Constitution bear mentioning. First, Alberdi described his economic program as the antithesis of the economic policies followed by the sixteenth-century Spanish monarchs Charles V and Philip II.⁴ These kings established a monopolistic, protectionist economic system to ensure that the Spanish manufacturing sector would have unchallenged access to colonial American markets. Not only did the system require myriad regulations, it was a colossal failure. Spain in 1500 had been a rich country, with a well-developed manufacturing sector and a well-developed cultural sector. Fifty or sixty years later, however, the country started to experience the disastrous consequences of the monarchs' protectionist economic policies.

In condemning the policies of Charles V and Philip II, however, Alberdi ignored the profound reasons why the monarchs were forced to adopt economic protectionism. With the discovery of the Americas and the subsequent influx of gold and silver from Peru and Mexico, the supply of money in Spain expanded very quickly. As a consequence of this increase in the money supply, prices and wages in the metropolis suffered an inflation of 400 percent over the course of the sixteenth century. In England, France, Germany, and the Netherlands, meanwhile, the rate of wage inflation was only 30 percent.⁵

Because of this differential rate of inflation in Europe, particularly in wages, the cost of manufactured goods and agricultural products in Spain climbed so high that domestic industry and agriculture ceased to be profitable. Imports boomed, jobs were scarce, and many hard-working people--Arabs and Jews--were forced to emigrate. Thereafter, Spaniards turned to purely non-commercial careers, primarily service in the army or navy, or in the church.

All of this occurred not because the protectionist system was adopted in the sixteenth century; rather, the protectionist system was the product of the overvaluation of the Spanish currency. The monarchs were forced to take protectionist measures in a desperate effort to resolve deep economic

⁴Alberdi, p. 303.

⁵Eduardo R. Conesa, "Tipo de cambio y desarrollo: la decadencia económica de España hacia 1600," Revista de Integración Latinoamericana (Dec. 1980), p. 57. In recent years a vast literature has appeared on the so-called "Dutch Disease" produced by currency overvaluation [see Michael Roemer, "Dutch Disease in Developing Countries: Swallowing the Bitter Medicine" (unpublished paper, HIID, Harvard University) and W. M. Corden, "Booming Sector and Dutch Disease Economics," Oxford Economic Papers (Oxford, Eng.), 36 (1984)]. The name is wrong; it should have been called "the Spanish Disease."

problems. They should not be condemned as harshly as did Alberdi, for the science of political economy did not exist in their day. Those who overvalue their currencies today, however, may not be excused, for political economy does exist. To make the same mistakes in the twentieth century as were made by sixteenth-century Spanish monarchs is unforgivable.⁶

The second characteristic of the 1853 Constitution of which Alberdi made special mention is its implicit ban on state-owned enterprises. A passage from another of Alberdi's works bears quoting:

"A merchant who has a gun and the power of the state in one hand, and merchandise in the other, is a monster that eats all individual freedoms. It is impossible to compete with him because he pays no taxes and enjoys all the privileges of the government. Rightly the Argentine Constitution has forbidden this system, establishing the functions of the government as alien to industry, and leaving to industries alone the right to make industrial work and to produce, to all and each one of the inhabitants of the country. When the government is a merchant it does not govern, it does not earn money, and neither does it allow the private citizens to earn money."⁷

Accepting the opposition of the Argentine Constitution to protectionism and to state enterprises is fundamental to the restoration of a pattern of viable economic growth in Argentina.

THE ECONOMIC PROGRAM OF THE CONSTITUTION AT WORK

What was the impact of the constitutional program on the Argentine economy? It was a tremendous success. In 1860, Argentina was a very poor country; by 1940, Colin Clark, a British economist who published a book on The Conditions for Economic Progress,⁸ ranked Argentina among the leading countries of the world in income per capita. Although the exact figures are subject to dispute, Argentina in the 1920's and 1930's certainly had a higher income per capita than Italy, Japan, Spain, Yugoslavia, and a number of other countries that today top the list. By comparison, Argentina is currently ranked fortieth by the World Bank, well below Italy, Spain, and Japan.⁹

Argentine economic growth from 1860 to 1930 was based on the export of agricultural products. This was made possible, as noted above, by

⁶Conesa, "Tipo."

⁷Alberdi, p. 198.

⁸First ed. (London: MacMillan, 1940). Of course, later editions of this book dropped the reference to Argentina.

⁹World Bank, World Development Report (Washington, D.C., 1984).

technological advances in transport, railways and steamships. These transportation systems were developed with foreign capital. Also of vital importance was the invention of refrigerated shipping.

A few figures will serve to illustrate the extent to which transportation grew during the seventy years from 1860 to 1930.¹⁰ In 1870, Argentina had only 700 kilometers of railways; by 1913, there were 31,000 kilometers--with the same density as the United States (the U.S. had ten times as many kilometers of rail, but also ten times as much land and population). As a result of the progress made in transportation, agriculture became very profitable in Argentina. Exports of grain, for example, rose from nil in 1870 (indeed, Argentina imported grain during that decade) to 4.2 million tons in 1907--third in the world behind the United States (7.6 million tons) and Russia (7.2 million tons). In addition to grain, the export of meat became a key element in the Argentine economy, reaching 800,000 tons in 1927.

All of this was possible, we must remember, because of two important innovations in the world economic system: (a) technological advances in transportation; and (b) the application of free trade principles to the trade in agricultural products. Just as Argentina benefitted from a shift in international economic conditions after 1850, however, it would suffer as a result of changes in the international economic order following World War II.

THE DEPRESSION OF THE 1930'S

In 1930, the world fell into a depression. At the time, many intellectuals argued that the depression represented the end of the capitalistic age, and thus the end of economic liberalism. In fact, however, when viewed in terms of recent advances in economic theory, the depression of the 1930's was clearly the product of mistaken economic policies adopted by the leading nations of the world, beginning with the United Kingdom in 1925.¹¹ In that year, Winston Churchill, as Chancellor of the Exchequer, tried to restore the gold standard and overvalued the British pound by more than 10 percent. This provoked a very long recession in the United Kingdom, because the country found itself unable to export, while simultaneously importing a host of inexpensive goods from abroad. Under those conditions, British industry was unable to grow and the government resorted to permanently high interest rates in an effort to keep money in the country. This only served to depress domestic investment further, and the United Kingdom found itself in a permanent recession from 1925 to 1931, at which time the country abandoned the gold standard.

¹⁰Vicente Vázquez Presedo, El caso argentino. Migración de factores, comercio exterior y desarrollo, 1875-1914 (Buenos Aires: Eudeba, 1971).

¹¹John Maynard Keynes, "The Economic Consequences of Mr. Churchill," in his Essays in Persuasion (London: MacMillan, 1933), pp. 224-70.

Many authors, especially Charles Kindleberger,¹² feel that the United States committed a number of economic mistakes of its own because it was not yet ready to assume world economic leadership. The Smoot-Hartley Act, for example, raised tariffs considerably in an effort to protect domestic industry. Because other countries could no longer export to the United States, however, they were unable to repay loans contracted with the U.S. during and after World War I, because the loans had to be paid in dollars or gold [Argentina, we should note, did repay its loans nevertheless]. The result was a series of bankruptcies the world over, which compounded the effects of other fiscal and monetary policy errors, and led the world into depression. Just as the United Kingdom and the United States adopted protectionist economic policies, other countries, including Argentina, did as well. World trade fell to less than half the level it had been in 1914. Argentina sought to replace the goods it had imported earlier by undertaking the process of government-directed import substitution in the 1930's.

STATE ENTERPRISES IN ARGENTINA AFTER 1930

During the 1930's, Argentina benefitted from the knowledge and abilities of a large number of first-quality public servants, among them Dr. Raúl Prebisch, general manager of the Central Bank. Under their care, many successful state enterprises were established (some, like Yacimientos Petrolíferos Fiscales--the national petroleum company--date even to the 1920's) and their numbers have grown since. Today there are seventeen large federal enterprises, three binational entities, 30 military factories, more than 200 smaller federal enterprises (among them radio and television stations, hotels, etc.), and 89 municipal or provincial enterprises.¹³ This proliferation of government-owned businesses is attributable to the initial success of state enterprises during the 1930's.

Indeed, state enterprises work very well when they are administered by restrained and capable public servants. Dynamic leadership is difficult to maintain on a long-term basis, however, especially where bankruptcy laws do not apply and political patronage proliferates; and this has been the experience of Argentina. Unfortunately, the state-intervention apparatus created during the 1930's to permit the establishment of state enterprises has proven very difficult to dismantle, now that those enterprises are no longer viable. Current studies by the World Bank show that in good years the rate of return on capital invested in public enterprises in Argentina is about 4 percent, compared to 20-30 percent in private industry. Moreover, state enterprises do not pay taxes; and they often run large deficits, as was the case in 1984, when their combined

¹²Charles P. Kindleberger, The World in Depression, 1929-1939 (Berkeley: University of California Press, 1973).

¹³According to an unpublished work by Manuel Solanet and others, there are 353 public enterprises in Argentina [see Ambito Financiero (Buenos Aires), May 31, 1985, p. 1].

deficit reached 5 percent of Gross Domestic Product--total revenues were 10 percent and total expenditures were 15 percent of GDP. In fact, these state enterprises have become, in Alberdi's very words, "monsters that eat all individual freedoms." They are unconstitutional, but they exist; and they survive not because they are efficient, but because they are provided with privileges and subsidies.¹⁴

IMPORT SUBSTITUTION

Import substitution also worked rather well in the beginning. During the depression and World War II, it was not possible to import capital goods and raw materials, so Argentine industrialists had to be very efficient, and they were.¹⁵ The industrial sector in Argentina managed to grow, producing more and more with very little capital, using all available capital to maximum advantage. The situation after the war changed dramatically, however, primarily because the Argentine peso was vastly overvalued. This permitted industrialists to import inexpensive capital goods and raw materials, add very little in terms of value, and then sell the products in the domestic market at high prices, protected from outside competition by import controls on consumer goods. To make a profit in the post-war period, therefore, an industrialist either had to be efficient or he had to obtain privileges from the government for the free importation of raw materials and capital goods. Indeed, we may still classify Argentine industrialists into two types: the efficient and the inefficient/privileged.

A number of studies on effective economic protection in Argentina have been completed, the most renowned of which is a 1977 work prepared for the World Bank.¹⁶ This study showed that on average Argentine industry in the mid-1970's enjoyed an effective protection of 39 percent (i.e., the value added by Argentine industry was 39 percent more expensive than the same value added at world prices).

This is certainly a good yardstick with which to measure the efficiency of domestic industries, for those that need 40 percent protection or less can be deemed efficient; those that require more than 40 percent protection are inefficient. But this average conceals considerable internal variation. Some industries--like those producing tractors, agricultural machinery, refrigerators, and raw materials--have very high levels of efficiency, close to the world levels. If they cannot

¹⁴The World Bank has made a number of studies on the problem of administering public enterprises; see, for example, the "World Bank Staff Working paper No. 585" (Washington, D.C., 1983).

¹⁵Henry Bruton, "Productivity Growth in Latin America," American Economics Review, 57 (1967), pp. 1099-1116.

¹⁶Julio Berlinski, Protección arancelaria de actividades seleccionadas de la industria manufacturera Argentina (Buenos Aires: Ministerio de Economía, Sept. 1977).

compete internationally, it is because their raw materials must be bought at higher prices; but the specific industries themselves are efficient. At the same time, however, there are industries that need much higher levels of effective protection: motorcycles, 480 percent; radios and televisions sets, 114 percent; steel, 85 percent; synthetic fibers, 221 percent; etc. These industries appear, in the light of the World Bank study, to be inefficient.

IMPORT SUBSTITUTION AND THE POLITICAL PROCESS

There is another important ramification of the categorization of industrialists: those who are efficient pay little attention to politics. They do not need government privileges, tax exemptions, or import permits to survive; they make profits because their industries are technically and economically sound. Those industrialists who are inefficient--those whose fortunes depend upon their getting cheap import permits (at the official, overvalued rate) to import raw materials or capital goods and sell their products in the internal market--must be full-time political lobbyists. The latter are joined by those industrialists with a talent for obtaining industrial promotion decrees, who establish artificial industries on the basis of government subsidies.

Clearly, the industrialists who receive subsidies and privileges from the government must pay a price for those advantages; they contribute large sums of money to the campaign funds of the various political parties and maintain close connections with the political establishment. As a result, it is the inefficient industrialists who control the Argentine economy. This is a very important point to bear in mind, even though it is regularly ignored by analysts of the Argentine economy.

The importance of urban workers to Argentine politics is often emphasized by the analysts, however, and correctly so. One of the principal effects of the import substitution process, resulting from the subsequent growth of Argentine industry, was a significant increase in the number of urban industrial workers belonging to trade unions. These organizations became a very powerful force in Argentine politics as a result, primarily via the Justicialista [Social Justice] Party, or "Peronist" Party. The other important political party, which draws its support primarily from the Argentine middle classes, is the Unión Cívica Radical, or "Radical" Party. Despite their broad bases of support, both of these parties are fond of the system of exchange controls and permits, uneven effective protection, differential tariffs, and tax holidays for "industrial promotion."

If the economic system were efficient--if it were competitive--and had an effective bankruptcy law, the inefficient entrepreneurs would not be able to survive, for their enterprises would go bankrupt. In the United States economy, for example, there are integral mechanisms to ensure efficiency, competence, and a certain superiority within the entrepreneurial class. This is akin to a Darwinian "survival of the fittest" process; it is somewhat brutal, but it is very effective in ensuring that capable individuals will be in charge of enterprises, and thereby of the national economy.

Those who control the enterprises also have at their disposal extensive financial and economic resources, and thus wield considerable influence over the political process, through contributions to political campaigns, for example. Thus, with capable individuals in charge of the economy, it is quite likely that a country will also enjoy able political direction. The reverse is also true: when the economy is in the hands of inept individuals, the political system will also fall prey to inferior direction.

In the case of Argentina, the import-substitution system, as it is designed, is arbitrary, leading to economic stagnation and thereby to political conflicts and instability. One need only look at the figures included in the World Bank report to see the absurd variation of effective protection from industry to industry.¹⁷ A producer of shirts, for example, may enjoy a 130 percent rate of effective protection while a producer of socks--because of the high tariffs on synthetic fibers used in their production--suffers negative effective protection. In this way the Argentine price system has been ruined as an efficient means of allocating resources.

One of the basic principles of political economy defined by Adam Smith in The Wealth of Nations is that of the "invisible hand."¹⁸ When industrial and commercial competition is unrestricted, as each entrepreneur tries to maximize his own profit, he also maximizes the social gain, because the most profitable goods are those demanded by the market. The correlation between social gain and individual profit is missing in an economic system that is misshapen, one in which the system of incentives is distorted by privileges and other artificial factors.¹⁹ In the latter case, an individual makes a profit not by contributing to society, providing employment, or making useful products, but only because he receives privileges from the government. Typically, those privileges allow him to import cheap raw materials and capital goods, add some minimal value (perhaps 10 percent), and sell a product in the internal market for three times the world price. This is very common in developing countries, as in Argentina, and it occurs because import-substitution was implemented incorrectly.

¹⁷Berlinski, op cit..

¹⁸An Inquiry into the Nature and Causes of the Wealth of Nations (New York: Modern Library, 1937), p. 423.

¹⁹Alberdi, op cit. Referring to Adam Smith, he says literally, "A ésta escuela de libertad pertenece la doctrina económica de la Constitución Argentina" (ibid., p. 147). On this basis and more than 40 articles of the Constitution that refer to economic matters it is clear that high and uneven import tariffs, exchange controls, tax holidays, and all the interventionist apparatus existing now in Argentina are unconstitutional and serve no purpose--especially if the exchange rate policy recommended in this essay is adopted.

LIBERALIZATION ATTEMPTS AND THEIR FAILURE

Since 1955, there have been many proposals, most of them coming from liberal economists--of which there are still many in Argentina--to abandon the import-substitution process in favor of the free trade policies of the pre-1930 period. Most of these proposals have been implemented, interestingly enough, by military governments. In each case--1959, 1962, and 1976--one critical point was neglected, however: that although Argentina continues to enjoy a substantial comparative advantage in agricultural production, the world has become increasingly protectionist toward agricultural products.

If the Argentine economy were liberalized entirely and allowed to operate freely, the goods that would be produced at the least cost would be agricultural goods; this is as true now as it was in the late nineteenth century. Argentina could easily export three times as many agricultural products as it does at present, if it were somehow able to lower its export prices to compensate for agricultural tariffs abroad. But the world economic order has changed fundamentally since 1900. Tariffs on agricultural goods have risen continually, especially since World War II, affecting precisely on those products for which Argentina has a comparative advantage. At the same time, the world economic system has become progressively liberal toward industrial products, products for which production costs in Argentina are 40 percent higher than those for agriculture.

DEVALUATION, RECESSION, AND MORE INFLATION

What happened with the efforts to liberalize the Argentine economy? In each instance, the liberalization of the economy began with a devaluation of the peso--an attempt to lower agricultural production costs, in terms of dollars, and thus to promote exports. The result was higher prices for wheat and meat in the internal market, because once it was possible to export those products under the higher exchange rates, internal market prices had to rise to provide an incentive for producers to sell their products domestically. And as the price of food rose, the standard of living of the working classes and middle classes fell, leading to political unrest.

From the political viewpoint, therefore, it was extremely difficult--in fact, impossible--to maintain an effective devaluation. In 1959, for instance, a devaluation of more than 100 percent was quickly negated by 100 percent inflation. As a result, the impact of the devaluation on economic growth was minimal, but it sparked significant inflation.

These devaluations--traditional devaluations--also generated sharp recessions, because they lowered the standard of living for the working and middle classes. These had to buy the higher-priced food first, and their demand for industrial products was lowered as a result, producing a

recession.²⁰ The effects of a domestic recession were compounded by the fact that industrial production costs were higher and thus exports were impossible. Every traditional liberalization attempt to date has failed, therefore, because of its political ramifications; and all such efforts in the future will fail for the same reason.

Recently, a very active Argentine economist published a book proposing a flotation of the Argentine peso, suppression of export taxes, and the establishment of a land tax.²¹ This would mean repeating the traditional approach, albeit with a slightly more progressive slant, and it is politically impracticable in Argentina because it goes against the interests of the middle classes and the urban working classes. It seems to favor the agricultural classes. I say "seems" for two reasons: first, the agricultural sector will resist any proposal for a land tax; and second, the terms of trade will sooner or later overcome any initial gain caused by the program's adoption.

If the proposed program were to be implemented, the agricultural producers would initially receive much higher prices for their products, some 30-40 percent higher. That percentage would result from the floating of the exchange rate under the demand pressure created by the \$4-5 billion per year in external debt payments confronting the country at present. Clearly, the agricultural producers would benefit from the higher prices, and certainly the volume of agricultural exports would double within three or four years--from about 20 million tons of grain per year to 40 or more. But for this to happen, the government would have to restrain the wage demands of the industrial workers and middle class and thereby keep inflation from cancelling the effect of the devaluation; and this would be political suicide. Moreover, the demand for Argentine grain is not entirely elastic.²² In fact, the prices received would decline with increased exports. If Argentina doubled its agricultural exports, the price it received for those goods would fall by 25 percent--not only on the additional production, but on the former amount as well, resulting in an effective 50 percent monetary return on a 100 percent increase in production (see Figure 1: initially, price is OA and quantity exported is OC. After doubling volumes to OF, the price declines to OH. As a result, OHEF is greater than OABC by only 50 percent).

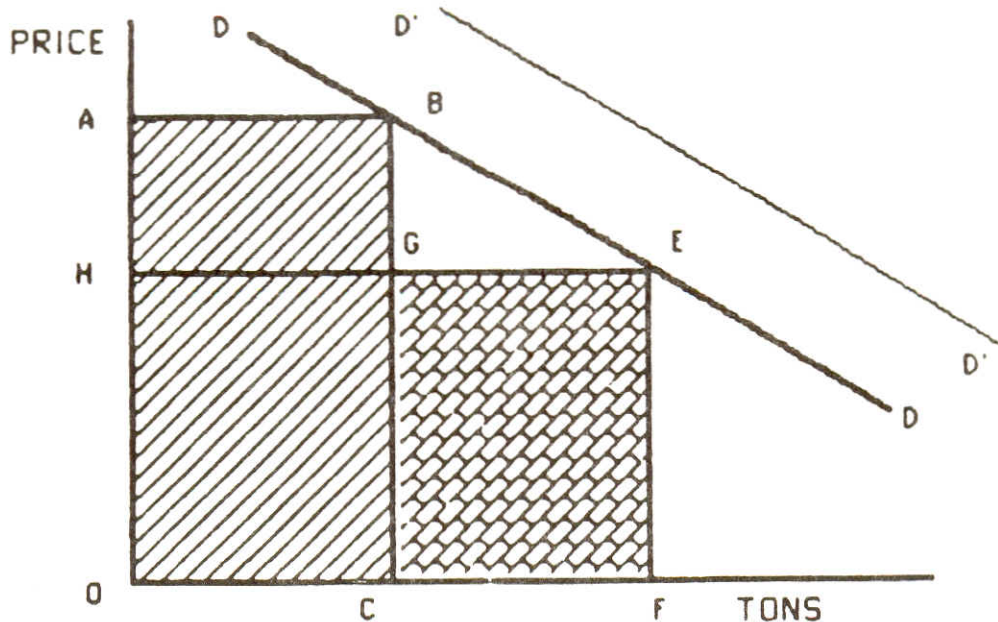
²⁰Carlos Díaz Alejandro, Exchange Rate Devaluation in a Semi-industrialized Country. The case of Argentina, 1955-1962 (Cambridge, MA: the MIT Press, 1965). See, also, Richard N. Cooper, "Currency Devaluation in Developing Countries," Essays in International Finance (Princeton Essays in International Finance, No. 86; Princeton: Princeton University Press, 1971).

²¹Domingo Cavallo, Volver a crecer (Buenos Aires: Sudamericana-Planeta, 1984).

²²Eduardo R. Conesa, Términos de intercambio y tarifa óptima en la Argentina (2 vols.; prologues by Raúl Prebisch and Adalberto Krieger Vasena; Buenos Aires: INTAL, 1983).

FIGURE 1

DEMAND ELASTICITY FOR TRADITIONAL EXPORTS



This would probably not be immediately apparent, and as the agricultural producers would make their own decisions--how to invest, when and whether to buy tractors, apply fertilizer, and open new agricultural lands, etc.--on the basis of the prices received during the initial post-devaluation period, many would soon face economic difficulties and go bankrupt within a few years.

Should the Soviet Union--the main buyer of Argentine grain--have two or three years of bad crops, however, the scenario sketched above might not be followed. In that case, Argentine production could be sold to the Soviet Union on better terms. But even if this were to happen, the economic relationship between Argentina and the Soviet Union would not be a beneficial one. Argentina could easily provide grain in increasing quantities to the Soviet Union, but there is very little that Argentina could import in return. The consumer-goods industry in the Soviet Union is poor in quality; the armaments industry, however, is excellent. Thus, the natural tendency would be to export grain and meat to the Soviet Union and import weapons; economic forces would lead to this pattern. And this too would go against the interests of the landed agricultural classes, because sooner or later the Soviet Union would seek to export not only weaponry but also its economic system to Argentina.

Clearly, we cannot return to 1900 and develop the country through agricultural exports. The first obstacle to the traditional approach is

the declining-terms-of-trade problem, which derives from the protectionism toward agricultural products currently in force in both industrial and developing countries. The European Common Market (EEC), for example, employs variable duties, which increase duties whenever an outside producer lowers its prices in an effort to penetrate the Market. Moreover, the EEC's high internal prices generate continual gluts of wheat, meat, butter, cheese, and other agricultural products; these surpluses are regularly dumped in the world market, further damaging the international position of Argentina, cancelling its comparative advantage in many world markets.

Japan has an even stiffer agricultural protectionist policy than the Europeans, and should Japan buy more wheat and agricultural products, it will buy them from the United States, in response to strong pressures to open Japanese markets to U.S. goods; the same is holds for of Korea. It is also true that the price of meat in the United States is twice or thrice the price of meat in Argentina, but the U.S. is very protectionist toward meat. It does not allow the importation of Argentine meat for sanitary reasons, haveing maintained since the 1920's that Argentine cattle have hoof-in-mouth disease. On this basis, which is clearly protectionist rather than medical, Argentine meat is kept out of the U.S. market. Developing countries' markets are also closed, either because of heavy import-substitution policies in agriculture or because they buy in the world market using long-term credit, which Argentina is not in a position to offer.

No country in the post-World War II period has been able to grow on the strength of its agricultural exports; this is an inescapable reality. If, in the future, the role of agricultural products in the world market changes, then it might be advantageous for Argentina to employ a traditional devaluation and make the concomitant sacrifices, but under present conditions--which are unlikely to be changed anytime soon--the best way is to proceed is in another direction, which I will describe presently.

THE CORRECT TECHNICAL SOLUTION

The result of alternating between these two contradictory economic policies in Argentina--the policy of import substitution, heavily supported by the populist political parties, and the policy of traditional devaluations and growth through agricultural exports, supported by some liberal economists, agricultural interests, and military governments--has been 40 years of stagnation. Neither of these approaches is correct from the technical viewpoint. The import substitution approach fails because it ruins the price system and favors inefficiency; the export of agricultural products approach fails because it faces an inelastic demand for agricultural products abroad and political resistance at home.

A viable economic solution must take into account first the internal constraints posed by the popular majority, the urban workers and urban middle classes; there is no escaping this. It is impossible for an elected government to implement successfully policies that go against the interests of the urban-working and middle classes. It is also impossible

for a military government to ignore the popular will, for the Argentine military is, in the final analysis, also responsible to the people (in fact, the social makeup of the Argentine military reflects the composition of the Argentine people; all classes, especially the middle classes, are represented). Any attempt to ignore the popular majority will result in inflation and eventually in failure. Second, a viable economic solution must take into account the prevailing restraints on international trade, and primarily the fact that the world is now heavily protectionist toward agricultural products.

If we take into account these two constraints, it is entirely possible to design an economic system for Argentina that can: (a) maintain a pattern of income distribution that favors the urban working and middle classes (or at least avoids a sharp increase in the price of food and a falling standard of living); and (b) promote economic development for all Argentines, urban and rural. Moreover, it is possible to reconcile the traditional Argentine economic dilemmas: social justice versus economic and political freedom; democracy versus inefficiency.

OVERCOMING THE UNWARRANTED OVERVALUATION OF THE PESO

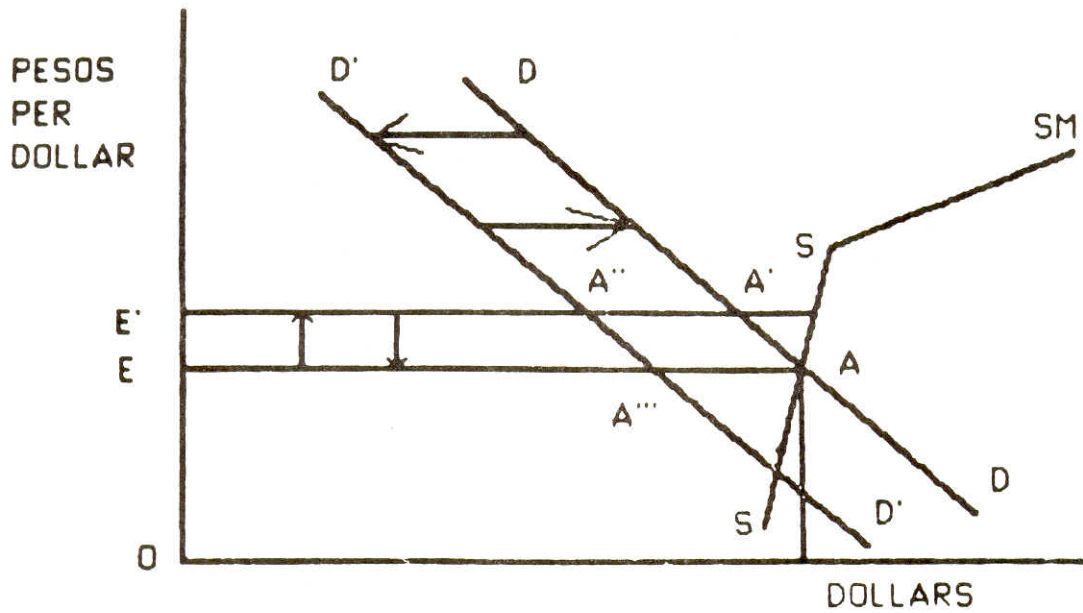
We begin with the unwarranted overvaluation of the Argentine peso. To lay the foundation for a solution to this problem, we must return to the problem of inelastic demand for Argentine agricultural exports, and bear in mind that when Argentina increases the volume of exports, the proceeds of foreign exchange do not increase in the same proportion, but rather less. Figure 2 represents foreign exchange supply and demand. On the ordinates scale is the ratio of pesos to dollar, that is, the exchange rate; on the abscissa axis is the number of dollars offered in the market. The supply curve for foreign exchange starts very much on the lower right of the figure because of Argentina's rich endowment of fertile agricultural land and thereafter is noticeably kinked, very inelastic, and very steep. Starting from the lower end of prices and moving up, the pitch of the curve remains very steep until it reaches a point at which there is a devaluation of 50 percent, where the Argentine industrial sector has reached a level competitive with world prices. At that point, the supply curve bends sharply to the right. Thus, the figure shows that the normal equilibrium exchange rate--the intersection of supply and demand--is well below that kink point; it is also clear that the exchange rate that is normally determined in the market overvalues the peso for the exportation of industrial products.²³

The normal rate that we observe in the market is the official parity, which is equivalent to the official parity in 1969, and similar to the 1978 figure. This is the traditional parity, at an overvalued exchange rate. In order to repay the external debt, Argentina needs to establish a much higher exchange rate which, if it were left free, would be some 30 percent over the official rate. If this were attempted in the traditional way, however, it would provoke a recession and political unrest (in Figure

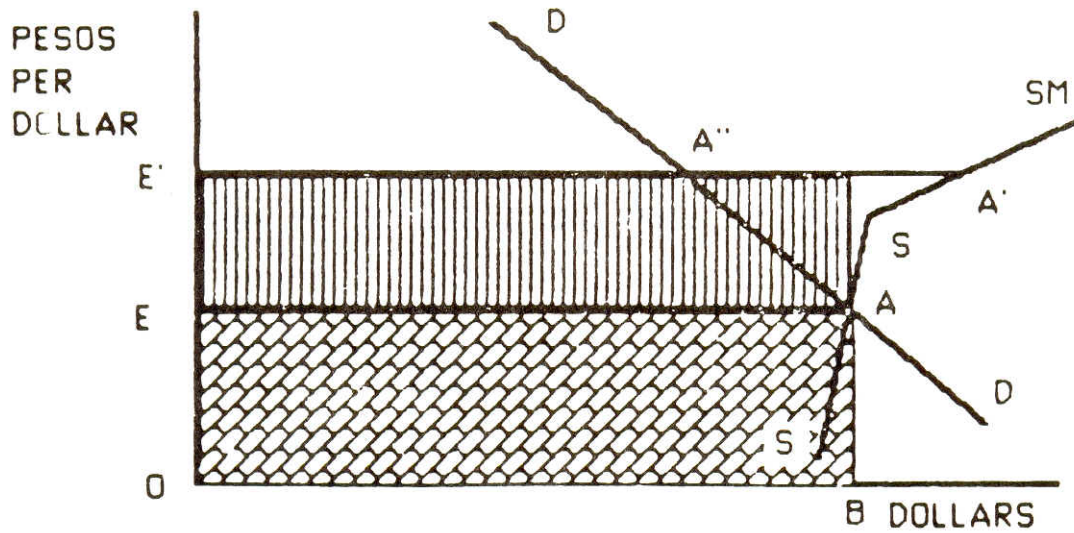
²³Conesa, *Términos*, p. 181, for example.

FIGURE 2

TRADITIONAL DEVALUATION AND RECESSION



INDUSTRIAL DEVALUATION WITHOUT RECESSION



EXPORT TAX COLLECTION

2, upper panel, the demand for imports will shift to the left from DD to D'D'). The solution lies in a devaluation that will not prompt a recession, and that will promote economic growth; and it is very simple.

The solution is a devaluation only for the exportation of industrial products. If the real measure of the devaluation is 60 percent, the industrial sector will be placed in a position to export. Maintaining the real level of the devaluation over time is key to its success.²⁴ To avoid the traditional inflationary wage demands of the urban workers and the urban middle classes, it will also be necessary to keep food prices low. This can be accomplished through the imposition of an agricultural export tax of some 50 percent, but varying from product to product in accordance with the inverse of the price elasticity of demand for each product (which is very low for soybeans, for example).²⁵ (In Figure 2, lower panel, the large devaluation from E to E' is compensated by a large export tax, the trade surplus is A'A', and there is no recession, as DD remains in place.)

The compensated devaluation cum agricultural export tax will permit the killing of six birds with one stone. First, it will make it possible for Argentine industry to export. Second, it will allow the government to collect some \$2 billion in new fiscal revenues, helping to offset the fiscal deficit. Third, the traditional post-devaluation recession will be avoided, for the price of food in the internal market will remain low because of the agricultural export tax. Because the price of food will not go up, the real wages of urban workers and the middle classes will not fall, and they will continue to demand industrial products, from automobiles to refrigerators.

Fourth, the program will lead to better use of industrial plant capacity. Not only will the industrial sector have new overseas markets for its products, but it will maintain markets at home, and therefore be able to use its full capacity. Currently, Argentine industry is working at 40 percent of capacity. With the new markets created by the devaluation, however, it would be possible to run three shifts, thereby reducing the cost of production per unit produced. Since the larger quantities of products will share the fixed cost of enterprises and as

²⁴Ann O. Krueger, Liberalization Attempts and Consequences (Cambridge, MA: Ballinger Publishing Co., 1978).

²⁵Conesa, Términos, p. 230. In the case of soybeans, the export tax should be very low because this product enjoys a relative free trade status in international markets. Consequently, the demand elasticity facing Argentina in world markets should be very high and the export tax low. In a few years, Argentina should be the first world producer of soybeans. A low export tax on soybeans will not affect the local standard of living because Argentines do not eat this grain. The low export tax will also be seen as a bonus for the agricultural sector, which will thereby benefit from the economic system that I propose. Interestingly enough, soybean cultivation in summer replenishes the nitrogen content of the soil and thereby increases the yields of winter crops.

salaries will drop sharply in terms of dollars, the total cost of production--fixed plus variable costs--will also go down. This will make it possible to hold the line on domestic prices, despite the devaluation and the increase in costs of imported raw materials.

A fifth advantage of this form of devaluation is that the terms of trade for agricultural exports will not be hurt. Part of the export tax will in fact be paid by the buyer in the world market.

The sixth advantage of the devaluation is that it will make it attractive for those Argentines with capital reserves abroad to bring some of their capital home to Argentina. In the beginning, admittedly, the repatriation of capital will be modest, but as the government generates confidence through the careful application of a new economic policy, well thought out and fairly implemented, more and more money will return to Argentina.

Not only Argentine capital will be invested in the revitalized economy. Given the heightened concern in European and North American societies about nuclear proliferation, once Argentina has established political and economic stability, its location in the southern hemisphere will place it in an optimal position to receive a substantial influx of European and U.S. capital, invested in Argentina for security reasons.²⁶ This will enhance both the scope and the pace of Argentine economic development.

ACHIEVING ZERO FISCAL DEFICIT

The devaluation cum agricultural export tax is vital to the establishment of economic stability with growth, but it will not be sufficient by itself. A second important measure, required to inspire confidence in the government's economic program, is a balanced federal budget. The government must not, under any circumstances, borrow from the Central Bank or from the internal capital market. It is very important that the public understand that the government will show self-restraint. When the devaluation cum agricultural export tax program is initiated, therefore, the government must explain in detail how it will balance its books.

How will this be achieved? First, the agricultural export tax will generate an additional 4 percent of GDP in fiscal revenues. Second, a

²⁶Albert Carnesale, Paul Doty, Stanley Hoffman, Samuel Huntington, Joseph Nye, and Scott Sagan, Living with Nuclear Weapons (New York: Bantam Books, 1983).

uniform import tax of 20 percent will be assessed,²⁷ allowing the government to collect an additional 1 percent of GDP in taxes. And as there will not be the usual post-devaluation recession, but rather an economic boom, government revenues will rise in concert with the expanded economic activity.

The government must also improve its tax administration apparatus. At present, for example, the Argentine value-added tax is collected from only a small fraction of the population--15,000 taxpayers pay 70 percent of the revenue generated by the tax, whereas 1 million are subject to it. By comparison, the turnover tax, collected by the provinces at rates of only 2.5 percent, 1.5 percent, and 1 percent--compared to 18 percent for the value-added tax--yields the provincial governments one-half the revenue produced by federal tax. Either the value-added tax should be collected effectively from everyone or it should be abolished and replaced by a workable tax; otherwise, the interests of free competition, efficiency, and fairness will not be served.

The personal income tax in Argentina is a colossal failure at present, costing the government more to collect than it yields. Given the importance of repatriating Argentine capital to the proposed economic solution, the provision for taxing patrimonial increments contained in the personal income tax law should be eliminated. The United States, the country with the most effective income tax law, does not have such a provision.

Tax collection must also be streamlined to lessen the effects of the current 40-day lag between the imposition of taxes and their collection. Under the present system, the government loses 30 percent its tax revenues to inflation. Of course, once inflation is under control this will be less of a problem, but in the short run it is vital that the government receive its revenues promptly.

Another important measure required to revitalize the Argentine economy is the abolition of all "industrial promotion laws," which do not promote industry but rather the so-called "rent seeking" society--those entrepreneurs who are not efficient. The government will save 0.5 percent of GDP with this measure; in addition, the elimination of industrial export incentives will save another 0.5 percent of GDP.

Moreover, the expensive bureaucracy required to administer the current system of exchange permits and industrial promotion laws will no longer be necessary and should be scrapped. It will also be easier to collect import duties, because in place of the current myriad classifications of

²⁷The case for uniform tariffs emerges from Article 67, number 1, and Article 16 of the Argentine Constitution, interpreted in conjunction with the principle of the "invisible hand." A scientific economic case for uniform tariffs can be seen in William Cline, "Negotiating Strategy for Latin American Integration," in Terms of Trade and the Optimum Tariff in Latin America (ed. by the staffs of INTAL and IDB; Washington, D.C., 1984).

goods used by the customs office a simple uniform duty will be imposed; and fewer customs officials will be needed. Thus a number of government agencies will either be eliminated or streamlined, and this will contribute to the reduction of government expenditures. The concurrent growth in demand for labor in the industrial sector will allow for a gradual reallocation of workers from the affected government agencies to the private sector.

THE RETURN OF PUBLIC ENTERPRISES TO THE PEOPLE

Another means of augmenting government revenue is to sell some 200 small industrial enterprises and services currently owned by the government. There is no reason why the government should administer these enterprises; indeed, as Alberdi maintained, state-owned enterprises are unconstitutional "monsters." Large industrial enterprises and utilities are important to the national interest, but the principal custodians of the national interest are the Argentine people themselves. The large government-owned enterprises should be transformed into private corporations [many of them are already structured as corporations], the shares of which will be donated to the Argentine people. Thereafter, the shareholders will vote to decide how these enterprises should be administered. The shares will be distributed in proportion to use made of each service or product. For example, those who own a single telephone will receive one share of the telephone company; those who own three telephones will receive three shares. Similar formulae will be used in assigning shares of the electric company and other utilities. Tariffs will have to be raised to cover operating costs and interest on capital invested in the companies, but the users/shareholders will be those most interested in holding costs down and thereby paying lower tariffs.

Divestment of the national petroleum, steel, and railway companies will be more complex, but there are objective yardsticks that can be used in distributing the shares of these enterprises. In the case of the petroleum company, and other enterprises exploiting natural resources, the people who live in the provinces from which the resources come should receive a larger percentage of the companies than those who merely consume the products. To determine the precise means of achieving these ends, preliminary studies will be necessary, but it should not be difficult to design a fair system that will be highly popular, benefit the Argentine people, and fortify Argentine democracy.

Democracy becomes difficult in a patrimonial state. The patrimonial state assigns too much power to the political clientele administering state enterprises. Economic freedoms and efficiency suffer, democracy tends to decline into hyperinflation and economic chaos. Political freedom, meanwhile, is suffocated by the government-owned broadcast media. When the government owns the television and radio stations, it monopolizes the propaganda apparatus and prevents the opposition from voicing effective control and criticism. The Argentine Constitution states that the Congress shall not restrict freedom of the press, nor establish federal jurisdiction over the press. Though it is true that there were no broadcast media when the Constitution was written, the article pertaining to freedom of the press clearly applied to all media.

The relationship between the government and the media is unmistakable: federally owned broadcast and print media are unconstitutional.

No Argentine government may claim adherence to the Constitution of 1853 unless it makes a determined effort to divest itself of all state-owned enterprises and return them to the private sector. And it is economically unsound to maintain government ownership of all these enterprises for another reason: the taxes that otherwise could be collected from them. With divestment there will be no federal deficit; the government will be rich because society will be rich. This is the meaning and the intent of the Argentine Constitution.

STOPPING INFLATION ALTOGETHER, AND AT ONCE

Key to each of the preceding elements of the economic solution for Argentina is the harnessing of inflation--putting a halt to the vicious circle in which the country finds itself and establishing a virtuous circle for the future. It is true that balancing the federal budget is crucial to achieving monetary stability, but it will take time for the Argentine people--who have been living with hyperinflation for many years--to develop faith in the government's program. The people will look not at the quantity theory of money and or to complex technical measures for evidence that the government is committed to solving the national economic crisis, but to its policies vis-à-vis wages and prices. It will be necessary in the near short term, therefore, to freeze prices and wages, while in the medium and long term, market forces must be left free to operate.

If there is no such direct assault on price increases, the people will not have faith in the government's actions and a recession will be necessary to halt the resultant inflation. If, however, the government uses all its propaganda apparati to enlist the cooperation of all Argentine citizens, as public servants, in reporting illegal price increases, then the vicious circle can be broken. Inflationary forces survive largely because of inertia;²⁸ today's salaries are indexed to yesterday's inflation and today's prices are determined by the interest rates that are expected to prevail tomorrow. To break this inertia, a direct, dramatic, and well publicized frontal attack will be necessary.

It is true that a freezing of wages and prices will violate constitutional guarantees of freedom of trade, property rights, and the right to work. However, the Argentine Constitution also provides, in Article 23, for a temporary suspension of constitutional liberties and rights under a "state of siege." Prices and wages could therefore be frozen for three months, under this provision of the Constitution, as an

²⁸John Williamson, ed., Inflation and Indexation: Argentina, Brazil, and Israel (Cambridge, MA: the MIT Press, 1985) [see especially the papers by Persio Arida and André Lara Resende, "Inertial Inflation and Monetary Reform: Brazil," and Adalberto Krieger Vasena and Enrique Szewach, "Inflation and Indexation: Argentina"].

emergency measure, as in a wartime economy. For the freeze to work, however, real wages must be protected, and even increased slightly.

INTEREST RATE POLICY

Interest rates will not only have to be frozen, but substantially decreased, because current interest rates reflect prevailing rates of inflation. Minimal interest rates equal expected inflation rates--this is a universal law first described by Irving Fisher in his magnum opus, The Purchasing Power of Money.²⁹ With increasing inflation, moreover, interest rates tend to creep well above the inflation rate. In concert with the freezing of prices and wages, therefore, it is necessary to reduce interest rates radically.

At present, interest rates are on the order of 45 percent per month; they must be set at an annual rate of 2 percentage points above the world interest rates--the LIBOR or PRIME rate in the United States--and no higher. This also must be accomplished, provisionally, by decree-law under Article 23 of the Constitution. Not only will the measure attack spiraling inflation, it will also reduce considerably the financial costs of industrial production, for interest payments now represent some 40 percent of total costs. Thus, entrepreneurs will not suffer as a result of having their prices frozen during the three-month period, but will in fact see their costs reduced and their profits increased.

INCREASING THE DEMAND FOR MONEY AND REPLENISHING CENTRAL BANK RESERVES

The combination of frozen prices and controlled interest rates will increase the demand for money-- M_1 , that is, currency in circulation plus demand deposits.³⁰ Without massive inflation, people will want to have more money at their disposal. At present, inflation represents a heavy tax on those with money in their pockets or in their demand deposits. As a result, M_1 in Argentina equals 3 percent of GDP, whereas a 20 percent figure is normal. If inflation is halted and as a result people keep more money at hand and in their demand deposits, then within three or four months, M_1 should equal 5-7 percent of GDP, and begin growing toward a normal ratio.

This process will also facilitate the Central Bank's efforts to buy foreign exchange. In order to maintain the new, devalued-peso exchange rate, given the influx of capital and increased export of industrial goods, the Central Bank will have to buy considerable amounts of foreign currency. To do so, it will have to issue Argentine currency, but in this instance the result will not be inflation, for the demand for money in the

³⁰Eduardo R. Conesa, "Keynes vuelve por sus fueros," Revista IDEA (Buenos Aires), May 1982. The demand for money in Argentina, as in any other country, varies inversely with the interest rate and the expected rate of inflation, and directly as a function of income. Econometric estimations are provided in this article.

private sector will grow fast enough to keep pace with or surpass the money supply. This is normal, and it is economically sound.

THE DISSOLUTION OF THE EXTERNAL DEBT PROBLEM

The Argentine external debt must also be considered. With all of the above measures in place and working, not only will the nation's external debt not be a problem, it will begin to be repaid. This will be possible even though the external debt currently amounts to \$47 billion, because Argentine citizens have some \$20 billion in assets overseas.³¹ What is needed, therefore, is a means to repatriate those assets. This can only be accomplished if confidence in the domestic economy is restored and domestic deposits are secure; once these conditions are met, there will be no reason for Argentines to keep so much of their capital abroad. Indeed, one generally receives a much larger return on his investment locally, and this will be especially true with the new opportunities created by augmented industrial exports fostered by the maximum devaluation. Once confidence in the economy is restored, therefore, we can expect much of the overseas capital to return home, and thereby subtract some \$10 billion or more from the \$47 billion external debt, making it less imposing.

This will take some time--we cannot expect the Argentine capital to return home immediately--but even if only the interest earned by those overseas reserves enters into the balance-of-payments equation, it will amount to \$2 billion a year and improve significantly Argentina's credit worthiness. And with foreign exchange reserves augmented through this process, it will be much easier to obtain fresh funds and to refinance the external debt with extended periods of repayment and lower interest rates. Thus, for the most part, the problem of the external debt will solve itself, especially if this economic program is revised for the IMF and receives that agency's support (under the proposed program, meeting the targets set for Argentina by the IMF would be quite easy).³²

PLANNING AND ECONOMIC INTEGRATION

There are a number of other measures that must be taken if Argentina is to have not only short-term stabilization, but also long-term economic growth. First of all, it will be necessary to establish an economic planning agency, in which the long range problems of the country will be studied and debated at the highest level; this will be especially important in associated sectors like education, technology, and health

³¹Morgan Guaranty Trust Co. of New York, World Financial Markets, Feb. 1985, p. 9. Some \$3-5 billion circulate inside of Argentina in the form of "greenbacks."

³²William Cline, "Economic Stabilization in Developing Countries. Theory and Stylized Facts," in IMF Conditionality (ed. John Williamson; Institute for International Economics, Washington, D.C.; Cambridge, MA: the MIT Press, 1983), chap. 9.

infrastructure, where the "invisible hand" does not work well. The planning agency will also need to monitor short-term changes on the macroeconomic level, usign modern macro-econometric and computable general-equilibrium models that allow policy-makers to posit questions and project answers with a reasonable degree of accuracy.³³ Indeed, it is possible to project the impact of any combination of factors--for example, an increase in money supply, lower interest rates, augmented taxation, higher import duties, and a lower exchange rate--on the domestic economy. It is also possible to simulate the effects on the Argentine economy of policy changes elsewhere, for instance a decision by the United States to lower its interest rates or reduce its fiscal deficit. Thus, by analyzing economic command variables with the applicable economic models, Argentina will be able to make much improved analyses of future economic trends, and to develop viable economic strategies that take them into account.

Finally, a word about one important factor that I have as yet not mentioned, but one that Argentina must consider seriously: economic integration with other Latin American nations. Such integration cannot be achieved all at once, and it may not involve every country in Latin America during the initial stages. Nonetheless, there would be considerable advantages gained by a partial integration, especially with those countries closest to Argentina--Chile, Paraguay, Uruguay, Bolivia, Brazil, and Perú. Individual agreements, involving partial economic ties, could be signed within the context of the Latin American Integration Association (LAIA), as the first step in a solid process of economic integration. The agreements must be fair, just, and based on equality;³⁴ the partners to each agreement must benefit equally from the integration process. It will be necessary to proceed step-by-step, beginning with one or two partners, and when other countries see that this sort of economic integration is mutually beneficial, they will most likely request inclusion in the process.

CONCLUSION

This essay has provided an alternative to the two contradictory economic policies that have been followed, intermittently, by Argentina during the last 40 years: the policy of import substitution, supported by the large political parties, and the policy of traditional devaluations, supported by the conservative sectors of Argentine society. The result of adherence to these policies has been 40 years of stagnation. The import substitution approach has failed because it ruins the price system and

³³Dervis, De Melo, and Robinson, General Equilibrium Models for Development Policies (The World Bank, Washington, D.C.; Cambridge, Eng.: Cambridge University Press, 1982). See, also, Alan Gelb, "Adjustment to Windfall Gains: A Comparative Analysis of Oil Exporting Countries" (unpublished paper, World Bank, 1982).

³⁴Eduardo R. Conesa, "Un mecanismo de mercado equilibrador en comercio entre países que desean integrarse económicamente," [Revista de INTAL] Integración Latinoamericana, 82 (Aug. 1983).

favors inefficiency; the export of agricultural products approach has failed because it faces an inelastic demand for those products abroad and political resistance at home.

"My economic solution is viable because it takes into account, first, the internal constraints posed by the popular majority--the urban workers and the urban middle classes. It is impossible for an elected or a military government to implement policies that run counter to the interests of the urban working and middle classes. All such efforts have failed in the past and are doomed to fail in the future. Second, my economic solution is viable because it takes into consideration the prevailing protectionism toward agricultural products in the world market.

With both of these constraints in mind, I have presented an economic program for Argentina that will: (a) maintain and improve a pattern of income distribution that favors the urban working and middle classes; and (b) promotes economic development for all Argentines rich or poor, urban or rural. Indeed, the proposed program will provide the means to reconcile the traditional Argentine economic dilemmas: social justice versus economic freedom; liberalism versus the popular will; and democracy versus efficiency. Moreover, it will comply with the economic principles set forth by the Argentine Constitution.

The implementation of the economic program presented in this paper will require national authorities with vision, courage, and the willingness to undertake a radical attack against the unconstitutional economic system of privileges and sincecures that today inhibits the initiative, imagination, and incentives to work hard of able Argentines. The time has come for just such an initiative.

Harvard University and the University of Massachusetts at Amherst
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