ARGENTINA'S UNSUSTAINABLE GROWTH TRAJECTORY:

CENTER AND PERIPHERY
IN IMPERIALISM AT THE AGE OF NEOLIBERALISM

Preliminary draft

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1 - Imperialism in the neoliberal era: Argentina's reprieve and crisis

This paper is about growth and crisis in Argentina. After a decade of stagnation, during the 1980s, the Argentinian economy grew at the average rate of 5.2% between 1991 and 1998. This performance was hailed as exemplar: the living demonstration of the efficiency of the new neoliberal "model of development". But neoliberalism is not a model of development. If it were so, it would be a complete failure in spite of the Argentinian reprieve of the 1990s. In general, and quite appropriately, the occurrence of a devastating crisis in the early 2000, after several years of recession, is invoked in retrospect to question the foundations of these years of "prosperity": This growth trajectory was actually *unsustainable*, biased from its first steps! In the left academy, there is a broad agreement on this assessment, even if diagnoses diverge to some extent. One aspect of the analysis in this paper is the formulation of an interpretation of these unsustainable trends.

But the framework of the paper is broader. We contend that the history of Argentina since the late 1970s, and the succession of growth and crisis, provide an interesting illustration of a political configuration emblematic of the new course of imperialism in the era of neoliberalism, what we denote as the *neoliberal-imperial mix*, characteristic of contemporary capitalism. Not only the countries of the Center, under the hegemony of the United States, are at issue; not only the ruling classes of these countries; but also the ruling classes of the Periphery (see box 1). Yes, in a sense, Argentinian ruling classes did participate in the establishment of this imperial configuration, but not passively, as consenting victims, rather as active agents in a complex set of relationships in which their own interests are at stake. Did they finally do badly, as the "unhappy ending" suggests? This paper contends rather the opposite, inasmuch as the interest of these classes is considered, rather than those of the "country".

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As a preliminary to this investigation, it is important to recall some salient features of contemporary capitalism. Since the early 1980s, a new phase of capitalism — denoted as *neoliberalism* — was asserted in the United States and other major capitalist countries as in Europe. The term *neoliberalism* itself is questionable. It refers to the rule of "markets" and the alleged diminished state intervention. The period could be more adequately labeled as a new "financial hegemony". By *finance*, we mean, in the phrase *financial hegemony*, the upper strata of the capitalist class and the financial institutions (banks, funds), in which their interests are embedded and that historically act in their favor.[1] This period followed the post-World War II (and post-Great Depression) decades of the *Keynesian compromise*. Although the transition from one phase to the other was somehow complex, in particular in the new situation created in the 1970s by the dollar crisis, we can date the emergence of neoliberalism to 1979, when the Federal Reserve decided to increase interest rates at any level supposedly required to curb inflation. This is what we denote as the *1979 coup*. As is well known, among many other effects, this decision ignited the so-called "third-world debt crisis". Neoliberalism was gradually exported to the rest of the planet.

1. G. Duménil, D. Lévy, *Capital Resurgent. Roots of the Neoliberal Revolution*, Harvard: Harvard University Press (2004).

1 - Ruling classes - Popular classes

Dealing with countries of the Center, like the United States or Europe, by "ruling classes", we mean the capitalist class and its allies in upper management, *management* being taken in a broad acceptation. (In the characterisation of this "upper management", one must include the upper fractions of public officials.) This definition relates to the work we have done on these countries, in particular with respect to neoliberalism, and our class interpretation of this new phase of capitalism. *(a)* By "popular classes", we mean production workers and clerical personnel.

Such class patterns prevail in any capitalist countries, but it is also obvious that this framework must be adapted to local circumstances, as in Argentina, and to particular historical periods. Specific features may play a prominent role. The existence of a large class of landowners (more or less related to the agribusiness) is a first example; the place occupied by the top of the military hierarchy may be central; a quite significant fraction of the economy may be performed within various forms of "underground economy". Thus, the concept of popular classes, as introduced above with respect to the structural pattern of social relationships in capitalism, must be given a considerably broader content.

It is also crucial to acknowledge that the leading families in a country are present in these various fields *(b)*, forming what is sometimes called oligarchies, in particular in countries of the Periphery. This is the expression of the "division of labor" in the "business of ruling".

(a) G. Duménil, D. Lévy, *Capital Resurgent. Roots of the Neoliberal Revolution*, Harvard: Harvard University Press (2004); Finance and Management in the Dynamics of Social Change. *Contrasting Two Trajectories: United States and France*, PSE, EconomiX, Paris (2005).

(b) M. Zeitlin, R.E. Ratcliff, *Landlords and Capitalists, the Dominant Class of Chile*, Princeton: Princeton University Press (1988).

In all countries, including countries of the Center, neoliberalism modified the functioning of capitalism to the advantage of ruling classes. The power and income of *finance*, as defined above, were considerably increased after a period of relative decline. After World War II, in countries like Japan or France, finance had been the object of a process of "repression". Real interest rates were low; corporations distributed little dividends; and the stock market was stagnating; financial institutions, with low, or even negative, profitability levels, acted in favor of the financing of the nonfinancial sector of the economy. The situation of ruling classes even worsened during the structural crisis of the 1970s (low profits, stock market to the floor, and very low real interest rates in the inflationary context of the period). In the United States, the same mechanisms were at work, though more mildly, and it would be more appropriate to refer to a process of "containment". Everywhere, policies were targeted to growth and full employment. In countries of the Periphery, as in Latin America, development models, with heavy state intervention and a large degree of protectionism, were implemented, with significant results in terms of growth. Local "national" bourgeoisies benefited from these models. This was also true in Europe, but the main features of the social framework of the Keynesian compromise were somehow distinct in various regions of the world.

Neoliberalism changed this social order to the benefit of the capitalist class and upper private management, that is the main components of ruling classes as defined in box 1. It was the result of a class struggle in which popular classes were defeated (also defined in the box). A new discipline was imposed to labor and management in general (as distinct of its upper fraction); new policies were established in which price stability is a central

2 - Imperialism

In his famous study devoted to imperialism *(a)*, Lenin defines imperialism as a stage of capitalism, the "highest stage". In the late 19th and early 20th centuries, the main powers were engaged in a devastating imperialist struggle to control the world, to establish colonies and empires (combining formal and informal dominations). And the United States were no exception, first in the accomplishment of their "manifest destiny *(b)*", the conquest of as much as possible of North America, and, second, in the rest of the world as in the Philipines. In Lenin's thinking, this configuration was tightly related to the new institutional framework of capitalism (large corporations, new financial institutions and mechanisms) and new challenges (the crisis of competition in the late 19th century). Capitalism survived to World War I and class struggle, contrary to Lenin's expectations. Among the features of capitalism that Lenin had identified, some were maintained as components of the institutional framework of modern capitalism, notably large corporations and financial institutions, others, such as the crisis of competition (and its specific institutions such as trusts and cartels), disappeared. A new configuration of international relations was established gradually. Imperialism remained a central aspect of capitalism, under new forms.

Wilson *(c)* was president of the United States between 1913 and 1921. He played a crucial role in the establishment of the new configuration of imperialism. The key element was the preference given to an informal imperial framework, liberal and democratic ("class" democracy obviously), under the hegemony of the United States, that was precisely asserted during those years. Colonies and empires survived for about half a century, but their importance was declining.

(a) V.I. Lenin, *Imperialism, The Highest Stage of Capitalism*, Peking: Foreign Language Press, 1973 (1916).

(b) A. Stephanson, *Manifest Destiny. American Expansion and the Empire of Right*, New York: Hill and Wang (1995).

(c) N. Gordon Levin, *Woodrow Wilson and World Politics*, Oxford: Oxford University Press (1968).

target; frontiers are opened allowing for the free circulation of goods and services, as well as capitals (but not human beings). Although the rise of transnational corporations is quite anterior to the assertion of neoliberalism, the new international configuration tends to the imposition of a new international division of production, under the aegis of transnational corporations, both financial and nonfinancial.

Although imperialism is a structural feature of capitalism (box 2) — in all of its phases of development, including the Keynesian compromise — , neoliberalism altered substantially the features of imperialism. A new step was accomplished in the establisment of the grand *informal* imperial domination on the rest of the world, à la Woodrow Wilson (box 2), on the part of the most advanced capitalist countries under U.S. hegemony. The gist of imperialist relations is the capability to draw maximum income and resources at low cost from the rest of the world. The first tool is straightforward "economic" violence, like the opening of frontiers among countries of unequal levels of development, always to the advantage of the most advanced; but it cannot be separated from plain violence, such as corruption, subversion, and war; local ruling classes or elites are invited to collaborate. The ultimate target is always the existence of an "imperial-friendly" government. "Class democracy" is favored; when it cannot be achieved, dictatorship is imposed, also with the collaboration of local interests; reactionnary regimes, as in Saoudi Arabia, are also welcome.

It is not the purpose of this paper to explain how this framework applies to countries of Latin America in general, a region of acute class struggle and direct involvement in imperialist domination, as is well known. In this region of the world, the timing of events was somehow distinct. The 1979 coup was felt in an acute manner. In addition, quite specific conditions resulted from dictatorships. The real turn to neoliberalism was more specifically characteristic of the 1990s, and the 1980s can be seen as a rather ambiguous period of transition.

Argentina perfectly fits into this historical broad picture. As suggested earlier, we believe that this country provides an emblematic example of the insertion of domestic ruling classes in the neoliberal-imperial mix. It strikingly illustrates the modalities of what we called above "collaboration", but it is also quite telling of the contradictions between ruling classes, at the Center and the Periphery. In the last instance, beyond the technicalities of macroeconomic analysis, this is the political lesson that we draw from the study of the last two or three decades of the Argentinian society.

The remainder of the paper is divided into eight sections. Section 2 discusses the break in growth rates in 1980, comparing Argentina, other Latin American countries, and countries of the Center. The main line of interpretation concerning the crisis is developed in sections 3 to 7: the foreign bias during the wave of accumulation of the 1990s, the growing public indebtedness, the inherent inability of the framework asserted during the 1990s to ensure macro stability, the impact of external shocks (in terms of trade, investment, and interest rates), and the succession of the recession and depression from 1998 onward. Sections 8 and 9 discuss the place of the Argentinian ruling classes in this imperialist world at the age of neoliberalism.

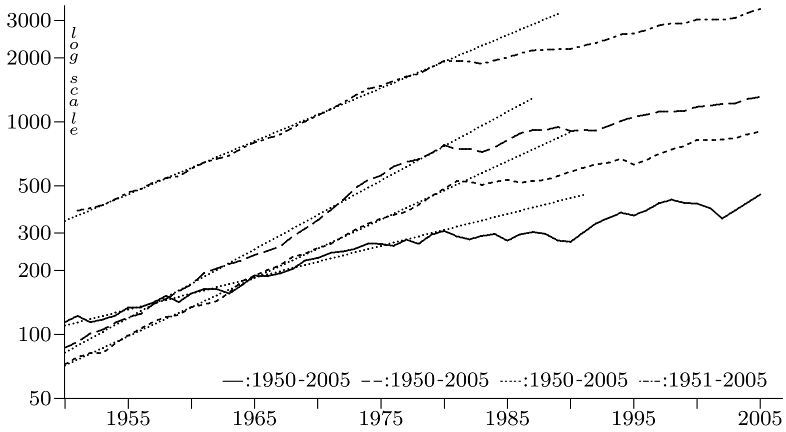
2 - The 1980 break

Section 2.1 documents what we call the *1980 break* in growth rates. Section 2.2 is devoted to the framework prevailing after World War II in the major capitalist countries and the Periphery, a model actually conducive to growth. Section 2.3 recalls the major aspects of the new course asserted after the crisis of the early 1980s (the so-called "third-world debt crisis"). Section 2.4 discusses the possible impact of a declining trend of profit rates and its combination with the new traits of the economy in the explanation of the break in growth rates.

2.1 Diminished growth rates

Considering the growth of the Latin American economy globally, the year 1980 marks a clear break. Most countries were growing comparatively rapidly during the first postwar decades, while the neoliberal decades can be characterized by diminished growth rates. This decline was practically general, and sudden. This is clearly apparent in figure 1, which shows the volume of output for the total of the seven major Latin American countries. The average growth rates in each period are presented in table 1. They declined from 5.7% to 2.2%. It is also striking, in figure 1, that the 1990s only performed slightly better than the

Figure 1 The growth of output (dollars of 1996, using PPP exchange rates): The total of the seven largest countries of Latin America, Brazil, Mexico, and Argentina



Argentine: (——)
Brasil: (— —)
Mexico: (-----)
Total (7 countries): (-·-·-)

The seven major countries of Latin America are: Argentina, Brazil, Chili, Colombia, Mexico, Peru, and Venezuela. Output is measured by the Gross Domestic Product (GDP) in constant dollars.
Purchasing-Power-Parity (PPP) exchange rate are used. PPP exchange rates are fictitious rates of exchange. If they prevailed, the levels of prices would appear, in the average, identical in the country and the United States. When there is some ambiguity, we call nominal GDP, in local currency, "GDP at going prices".
PPP exchange rates are questionable, since the proportions of output and total demand may differ considerably among countries. They must be considered as broad approximations. They are, however, the only meaningful way of aggregating or comparing the products of different countries. We also use such rates in the determination of ratios, whose numerator is typically expressed in dollars and the denominator is the GDP of the country, for example, the ratio of the imports or external debt of a country to its GDP. For example, using nominal exchange rates, the ratio of Argentina's external debt to GDP, at the end of 2001, prior to the devaluation, was 66%. After the devaluation, actually rapid but gradual depreciation of the currency at the beginning of 2002, it reached 160%. It is not the rise of the debt which accounts for the bulk of this increase, but the "devaluation" of GDP. If GDP is measured using PPP exchange rates, the percentages are 40% and 41%!

1980s. Rather than a "lost decade", the profile observed in figure 1 reveals a "lost quarter of a century". One can also notice that the course of the macroeconomy manifests more frequent and larger fluctuations since 1980: The macroeconomy turned more unstable with, in particular, more frequent recessions.

Figure 1 and table 1 also show the same variables for each of the three largest countries: Brazil, Mexico, and Argentina. One can notice the common growth pattern, with the diminished growth rates after 1980. The case of Argentina is, however, singular in two respects: (1) The growth rate is inferior in each subperiod to that of the two other countries; and (2) Business ups and downs are more frequent and pronounced.

This pattern is not specific to Latin America. Other countries of the Periphery suffered the same slowdown. It was so, for example, in Africa. As is well known, China and India are major exceptions.

Table 1 - Average annual growth rates (%)

	1950-1980	*1980-2004*
Seven major countries of L.A.	5.7	2.2
Brasil	7.6	2.1
Mexico	6.5	2.5
Argentina	3.3	1.3
France	4.4	2.0

In the interpretation of the 1980 break in Latin America, it is important to keep in mind that a somewhat similar evolution also occurred in the major countries of the Center. This is also illustrated in table 1, with the case of France, whose growth rate diminished from 4.4% to 2.0%. One difference is, however, that the decline was not as sudden; a more gradual slowdown is observed. The growth rates only diminished mildly in the United States. Due to its dominating position in the world economy, this country concentrates international savings, while engaged in a consumption spree.[2]

2.1 *One compelling observation emerges from this review of growth rates: Excepting the United States, to some extent, and countries like China and India, a sharp break was observed in 1980 in the major capitalist countries and Latin America (and other countries of the Periphery), with a significant reduction of growth rates. Such a broad phenomenon cannot be interpreted in relation to circumstances specific to a given country. It is the expression of a deep transformation of capitalism.*

2.2 A framework conducive to growth

This section is devoted to the "framework" which prevailed in the major capitalist countries of the Center during the first decades following World War II. It is difficult to qualify this framework as economic, political, social, national, or international, since all of these elements contributed to the specific features of the period, with impressive results in terms of growth and progress of purchasing power.

The emphasis is on countries of the Center and Latin America. Concerning this region of the world a particular attention is placed on Argentina, frequently taken as example.

2.2.1 The Keynesian compromise in countries of the Center

As a preliminary to the analysis of the new trends in Latin America, it is useful to recall the sequence of events in capitalist countries of the Center. The comparatively large growth rates of the postwar decades in the major capitalist countries were the combined effects of two types of determinants:

1. The United States emerged from World War II with large profit rates. The transformation of technology and organization from the beginning of the 20$^{\text{th}}$century, an effect of the corporate and managerial revolutions, had created the institutional conditions for a new

2. G. Duménil, D. Lévy, "The Economics of U.S. Imperialism at the Turn of the 21th Century", *Review of International Political Economy*, 11 (2004), p. 657-676.

productive efficiency. Originally this progress remained concentrated in the most advanced sector of the economy. Once the traditional sector had been eliminated as a result of the Great Depression and World War II, large average profitability levels were achieved, in spite of the parallel rise of the purchasing power of workers and the progress of social protection ("the welfare state"). These profit rates allowed for large accumulation rates and, consequently, large growth rates. Given the Keynesian institutional framework below, they also were an important factor in the consolidation of the "big" state of the war economy. Similar patterns of transformation were asserted in the major capitalist countries, as these countries were gradually catching up with the U.S. economy.

2. The entire institutional framework of the Keynesian compromise, led by the new classes of private managers and public officials, was targeted toward growth in a manner alien to the traditional functioning of capitalism. National industries were protected and states engaged in actions fostering the progress of industry; research and education were encouraged; profits were conserved within corporations and invested; macro policies were expansionary. It was globally so in the United States as well as in Europe and Japan, but with quite specific features in these latter countries (other than the United States). In France, for example, the financial sector was partly nationalized, with low profitability levels, acting in favor of the growth of the nonfinancial economy. The case of Japan is emblematic of this encouragement to industry. In this country, the public sector, the financial sector, and the nonfinancial sector were articulated in a very particular configuration. In many countries, inflation was tolerated. Internationally, the Bretton Woods system worked in favor of recurrent adjustments of exchange rates, in the context of the control of capital movements.

Many of the above traits — policies and managerial features — were, to some extent, less acute in the United States. But the success of Keynesian policies was hailed in the 1960s, in this country, exactly when the theories of managerial capitalism were blooming. This was not coincidental since the fresh autonomy of the managerial class was the linchpin of the postwar compromise.

2.2.2 The import-substitution model in Latin America

The mechanisms at work in Latin America were similar. In spite of the progress accomplished during World War II, these countries remained less developed than the major European countries. The involvement of the state in economic affairs was central; strong protections were implemented in the framework of what is known at the *import-substitution model*; international capital flows were controlled. As in Europe, this control did not hamper foreign direct investment, as transnational corporations were motivated to get assess to these markets in spite of trade barriers.[3] Also as in Europe, financing was easy and cheap. Yes, these economies were dependent from the countries of the Center but, in retrospect, this dependency appears mild in comparison to what happened following the assertion of neoliberalism.

A more detailed analysis would be required to establish the characteristic features of the social compromise that prevailed in these countries during those years. It is obvious that a national bourgeoisie benefited from the high level of trade protection proper to the import-substitution model. This trait was not alien to countries of the Center, but probably more

3. This is an aspect of these mechanisms that tends to be overlooked in contemporary discussions: the restriction of trade may encourage foreign direct investment.

intense in countries of Latin America. But other components of the Keynesian compromise, concerning the purchasing power of unionized workers and policies in particular, played a central role in these countries.

It is not the purpose of this paper to analyze in a detailed manner the growth trajectory in Latin America after World War II. But, in retrospect, the features of these decades appear quite striking. Consider the two following trends of the Argentinian economy:

1. *Purchasing power.* Figure 2 illustrates a first basic characteristic of this period: the progress of the purchasing power of wage earners. (We will return later to the dramatic decline since the 1970s.)

2. *Economic autonomy.* Figure 3 provides another spectacular indicator of this trajectory. It is the share of imported equipment in total investment in equipment in this country (shown since the beginning of the 20th century). This variable documents the changing levels of dependence of the country in its process of industrialization. One can observe that, at the beginning of the 20th century, more than half of total investment in equipment was imported. Then this percentage declines to about 10% during World War II, testifying of the rising industrial autonomy of the country. But it is interesting to note that this low percentage was maintained to the late 1970s. Import-substitution was not just a policy targeted to the limitation of the import of consumption goods. High levels of autonomy were reached, even if this domestic technology did not measure up to the most advanced international standards.

In Latin America, this framework proved rather efficient in terms of growth (section 2.1), even in comparison to countries of the Center. As shown in table 2, using Purchasing-Power-Parity (PPP) exchange rates (see the caption of figure 1), the total output of the Brazilian economy, for example, represented 5.4% of that of the United States in 1950; in 1980, the percentage reached 16.1%. For Mexico, the two percentages are 4.6% and 10.0%. (Conversely, Argentina grew slightly slower than the United States between 1950 and 1980.) For the total of the seven major countries of Latin America, the percentages are 22.4% and 40.1%. One can notice in the last column that all of these countries grew less rapidly than the United States between 1980 and 2004: the relative size of the seven countries fell from 40.1% to 31.9% of the U.S. economy.

Table 2 - Ratios of GDPs to U.S. GDP (%)

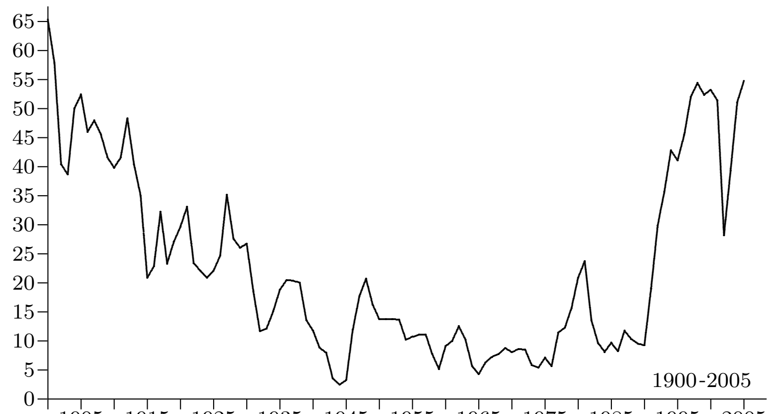
	1950	*1980*	*2004*
Seven major countries of L.A.	22.4	40.1	31.9
Brasil	5.4	16.1	12.5
Mexico	4.6	10.0	8.6
Argentina	7.3	6.5	4.1

2.2 *To sum up, it is not possible to reduce the interpretation of the 1980 break to a single mechanism. The the structural crisis in major capitalist countries created the conditions for a far-reaching transformation of capitalism. A new social order, neoliberalism, was imposed in most countries. The neoliberal framework was substituted for the earlier framework of the Keynesian compromise and import-substitution models of the first decades following World War II, which had proven very efficient in terms of growth.*

Figure 2 Real wages (index): Argentina

We use the series kindly communicated by Luis Beccaria, prolonged for recent years. (Up to 1984, a similar information can be found in G. Della Paolera, A.M. Taylor, *A new Economic History of Argentina*, Cambridge: Cambridge University Press (2003).) We use this figure repeatedly in the paper to document: (1) the upward trend up to 1974; (2) the following declining trend; (3) the plateau during the 1990s; and (4) the final return to the levels of the 1940s.

Figure 3 Imported equipment as a proportion of total investment in equipment (%): Argentina



Data elaborated by José Luis Maia and Pablo Nicholson, National Office for the Coordination of Macro Policies, Department of Economy. The two series are in constant pesos of 1993. This figure is, as the previous one, useful in various respects: (1) Here, to document a central aspect of the import-substitution model (its effectiveness); (2) Later, to discuss the features of technological change and relation to policies.

2.3 The debt crisis, the 1980s, and late "local" neoliberalism in Latin America, with special emphasis on Argentina

2.3.1 The 1970s and 1980s: A transition period?

In Latin America, the history of postwar decades was marked by the succession of *coups* and dictatorships, as in Chile in 1973 or Argentina in 1976, whenever the advance of class struggle threatened the property and income of ruling classes.[4] The policies implemented by these regimes are sometimes described as a laboratory for the forthcoming neoliberal revolution, but many aspects remained contradictory. In Argentina, for example, the first attempt at liberalization occurred in 1978, including partial convertibility. It was a complete failure, and tight controls were reestablished on imports and external financial transactions.[5]

Figure 2 illustrates, for Argentina, the sharp contrast between the first postwar decades and the 1980s concerning real wages. In several countries, wages were reduced from the late 1970s onward, in the context of hyperinflation and dictatorship. It is clear that the dictatorship and then neoliberalism — Argentinian style — in the 1990s, cumulated their effects, putting an end to a progressive era. (Note that actual movements are always difficult to assess during years of hyperinflation). Concerning wages, the 1980s appear as a transition period. (One can also notice the new adjustment downward after the crisis of 2001-2002.)

The dependency toward external financing (that is financing provided by foreigners, or equivalently here "nonresidents") began to increase in the 1970s, as these countries were borrowing from financial institutions of countries of the Center, in the context of low interest rates (given the rates of inflation prevaling during those years). The threat of a possible rise of interest rates was looming, as interest rates were flexible and, anyhow, the short-term component of this debt was growing. The symptoms of a major transformation were accumulating.

Large growth rates were maintained until 1980, when the major countries of Latin America entered successively into recession (figure 1). This crisis followed the sharp recession in the United States, where the growth rate began to slide during the first half of 1979, ushering in, during the early 1980s, the most severe recession of the postwar period in this country.

In the 1980s, the devaluation of currencies, the strengthening of the control of imports, exchange controls[6] and the diminished growth rates of consumption and investment allowed for a positive balance on trade. But these countries never recovered earlier growth trends.

This chain of events, at the Center and the Periphery, must be related to the decision by the Federal Reserve of the United States to increase interest rates. Besides the recession, it led to a major financial crisis in the United States[7] and, in the Periphery, to the "third-world debt" crisis in 1982, when Mexico declared its inability to service the debt. (The

4. This is what "fascism" is about, in the general (not limited to Mussolini's Italy) sense of the term. All social violence is not fascist.
5. J.M. Fanelli, J.L. Machinea, "Capital Movements in Argentina", *CEDES, Buenos Aires*, http://168.96.200.17/ar/libros/argentina/cedes/machinea.rtf.
6. H. Hopenhayn, P. NeumeyerA. , Economic Growth in Latin America and the Caribbean; Country Study for Argentina. The Role of Capital and Labor Reallocation in the Argentine Great Depression of the 1980s, Universidad Torcuato Di Tella (Argentina), Mimeo (2002).
7. See G. Duménil, D. Lévy, *Capital Resurgent, op. cit.* note 1, ch. 11.

debt crisis and the recession of the early 1980s are two distinct events, though obviously related.) The service of the debt placed a considerable burden on the economies of Latin American countries. This service, principal and interest, was, however, often paid by more debt, that is, in the last instance, unpaid.

Is the abandonment of the Latin American development model at issue? In Argentina, for example, it is said that the dictatorship led to a policy favoring the interests of specific sectors of the economy.[8] Capitals flew to foreign countries in spite of exchange controls. Such factors may explain part of the break in growth rates, in particular in Argentina where the 1980s display amazing negative trends. The transformation at issue here was, however, so far reaching and common to so many countries, that it is difficult to be content with such interpretations.

2.3.2 The 1990s: "Local" neoliberalism

A new metamorphosis occurred at the transition between the 1980s and 1990s. Capitals were allowed to move freely in and out of the countries with, possibly, limited restrictions as in Chile; hyperinflation was curbed in Argentina, although the exact timing differs among countries (figure 22). The entire pattern of functionning of the economy was modified, as in countries of the Center. The same new discipline was imposed on management and labor; the actual decline of real wages was confirmed at a new low plateau (figure 2); the financial system was reorganized and its property largely transferred to foreign interests ; new financial frameworks were implemented, as we will see for Argentina.

The 1990s were a period of considerable flows of capital. The channels of external financing can be broken down into: (1) foreign direct investment, and (2) other investment, that we denote as *nondirect investment*. (Direct investment refers to: (1) the acquisition of more than 10% of the ownership of a corporation, (2) the conservation of profits in such a corporation, or (3) investments in a corporation already owned by foreigners; the major fraction of nondirect investment is *portfolio investment*.)

Figure 4 shows direct investment and nondirect investment in the seven major countries of Latin America. Following the depressed levels of the 1980s, the first wave in the 1990s was overwhelmingly nondirect investment; then came the wave of direct investment; both proved ephemeral and sensitive to the macro conditions prevailing in the countries of destination and origin (in particular in the United States, section 6.2.1).

But even the large flows of direct investment did not substantially modify the patterns of growth and accumulation. Figure 4 also shows the growth rate of output in these seven countries. Although the series for investment only begin in 1979:

1. Although the data is not available for investment (not presented in the figure), growth rates were large in the 1970s, while foreign investment was limited. The recovery of growth rates after the debt crisis was not associated with large foreign investment. Only in the 1990s, one can observe the rise of foreign investment, associated with some recovery of growth rates.

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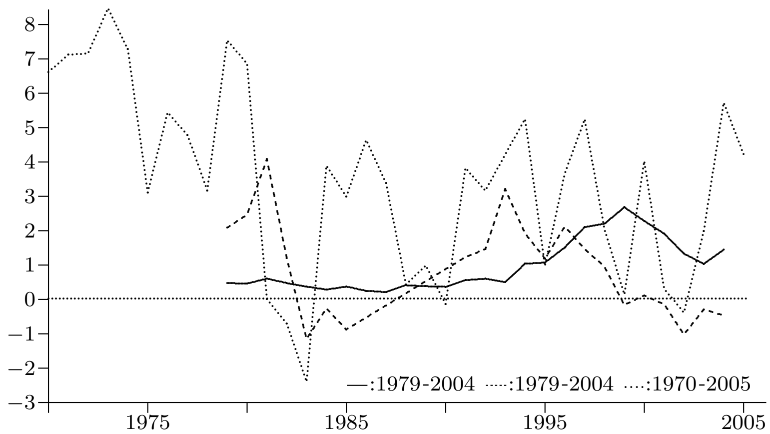
8. In addition to many other measures, such as the transfer to the public sector of 15 billion dollars of debt of the private sector (J. Fonseca, *Especialización productiva dentro de la Economía mundial. Industrialización y desindustrialización en la Argentina. Hasta 1984*, Madrid: Editorial de la Universidad Complutense (1992), IV.2.3; "Crisis Argentina: Causas y consecuencias", *in* Icex (ed.), *Claves de la economía mundial*, Madrid: Instituto Español de Comercio Exterior, 2002, p. 394-403).

Figure 4 Foreign direct and nondirect investment as a share of GDP(PPP) and the average growth rate (%): Seven major countries of Latin America



Foreign direct investment: (——)
Foreign nondirect investment: (-----)
Growth rate: (·········)

2. The increase of the growth rate always leads (in the sense of a leading variable, that is "moves before") that of foreign investment, direct and nondirect, not the reverse. This observation suggests that the direction of causation from foreign investment to growth is far from being obvious.

These observations contradict common assessments. Various interpretation can be given: (1) Direct investment, potentially the mere purchase of a corporation, does not materialize in physical investment; (2) The damages caused to the rest of the economy offset these potential benefits; and (3) Since the growth rate of output appears less stimulated than what could be expected given the amplitude of investment, one possible explanation could be that the main target of investment is the replacement of less efficient components of fixed capital. This is also where Argentina differs from Brazil and Mexico. As evident in figure 1, there was no growth in Argentina during the 1980s; conversely, a significant recovery is apparent in the 1990s, up to 1998. More than in other countries, this wave of investment coincided with the flows of foreign investment (section 3.1.2). This is what we denote as the *Argentinian reprieve*.

2.3 *The neoliberal course of capitalism, not conducive to growth, with specific features proper to Latin America, deeply affected the course of the economies in this region of the world: (1) the early transformation in the 1970s, with the rising debt, attempts at liberalization, and dictatorships; (2) the restrictive policies of the 1980s, with returns to controls and, then, gradual opening; and (3) the strengthening of neoliberal reforms, in the 1990s, under specific configurations. Neither in the 1980s nor in the 1990s, external financing worked in favor of growth, although, in the case of Argentina, it is not possible to completely exclude such an impact.*

2.4 The break in growth performances

In countries of the Center, as in the United States and France, the fall of growth rates was the combined effect of the structurally declining profit rate (technology, wages...) and finally the surge of interest rates (in the context of institutional transformations). It is difficult to assess whether Latin American countries were also affected by unfavorable trends of technical change and a structural profitability crisis (box 3). Two observations seem to indicate that it was not so:

- Contrary to the major countries of the Center, Latin American growth rates fell suddenly in 1980, suggesting the effect of an outright transformation rather than a structural bias. Capital accumulation remained strong up to the debt crisis.
- Latin American countries were catching up with those of the Center, and a new, more efficient, technology (the technology of countries of the Center) was still available and favorable to profitability trends. (Only a limited fraction of capital equipment was imported, but a wave of imports of capital goods occurred in the second half of the 1970s, as shown in figure 3.)

Under the assumption that the conditions for a profitability crisis had not been asserted in Latin America before the debt crisis, the explanatory scheme is that suggested earlier: The fall of the profit rate in major capitalist countries led to a structural crisis in these countries. This crisis provided the economic foundations for the transition to neoliberalism, a political move.[9] This new social order was gradually imposed to the entire planet (this movement is still on in the early 2000). Latin America played a specific political role, because of the social confrontation, popular struggles, and dictatorships. The debt crisis and the new unsustainable level of interest rates forced Latin American countries to adjust to the new circumstances with dramatic effects on accumulation and growth.

2.4 *The break in growth performances in Latin America after 1980 was the indirect effect of the new neoliberal framework in major capitalist countries, with large real interest rates. The break was sudden, as accumulation was maintained in the late 1970s due to the import of more efficient capital goods made possible by foreign financing. But the interruption was sharp when interest rate were increased and financing was stopped in the wake of the debt crisis.*

3 - The Argentinian reprieve: 1993-1998

Section 3.1 documents the revival of investment in Argentina during the 1990s after its sharp decline at the beginning of the 1980s. It analyzes the prevalence of a triangular relationship uniting investment in fixed capital, foreign financing, and imports, in which the import of capital goods is the key element. Section 3.2 contends that national savings were exported instead of contributing to national accumulation. Finally, section 3.3 explains how the expected benefits of accumulation were eventually deceived.

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9. G. Duménil, D. Lévy, "The Economics of U.S. Imperialism", *op. cit.* note 2.

3 - A falling profit rate after World War II in Argentina?

It is impossible to exclude the hypothesis of a downward trend of the profit rate in Argentina after World War II, as in countries of the Center. *(a)* The effects of such a decline could have been only delayed by the availability of new more efficient foreign capital goods during the wave of lending in the late 1970s, later interrupted.

The interpretation here would work as follows: (1) A country like Argentina experienced a declining trend of its profit rate, *à la Marx*, as in major capitalist countries: the combined expression of the features of locally produced capital equipment and of the trend of the labor cost; (2) The import of efficient foreign equipment in the late 1970s (figure 3), made possible by the availability of international financing, had a positive impact on profitability trends; (3) This short wave of import of capital goods was interrupted in the wake of the debt crisis (the sharp devaluation following the debt crisis increased the price of imports, external financing was cut, and restrictions were imposed on imports); (4) The potential positive effect of the implementation of such a more efficient imported technology on the trend of the profit rate came to an end; (5) The reversal to capital produced domestically (less efficient) interrupted the last bout of strong accumulation.

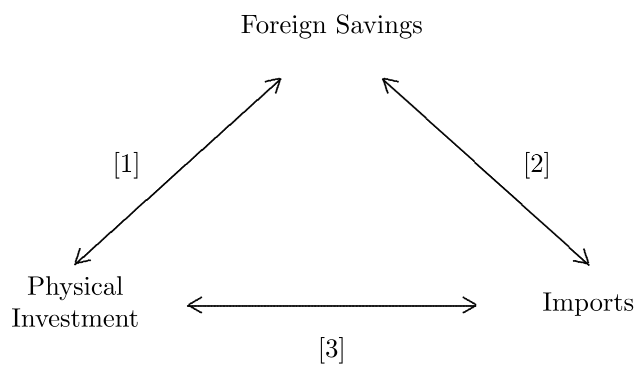
Note that this interpretation matches the hypothesis suggested earlier (section 2.3.2) that foreign investment (actually, both direct and nondirect investments) were used to replace earlier comparatively inefficient equipment. The restoration of the productivities of capital and labor was the target, more than the increase of output (section 3.3.2).

(a) Besides the lack of data, we are touching here complex theoretical issues. See G. Duménil, D. Lévy, "Technology and Distribution: Historical Trajectories à la Marx", *Journal of Economic Behavior and Organization*, 52 (2003), p. 201-233.

3.1 Investment, imports, and financing

Section 3.1.1, first, introduces the puzzling profile of physical investment in Argentina, its decline and revival. Section 3.1.2 shows how the revival of the 1990s was financed by foreign savings. Section 3.1.3 documents the link that unites imports and investment in capital goods.

A triangular pattern of relationship is revealed among major macrovariables:



Some among the variables considered in this discussion, imports and foreign financing, are linked by accounting relations; flows and stocks are at issue. Basic definitions and accounting relations are recalled in box 4.

3.1.1 The fall of investment and the revival of the 1990s

The 1980 break in the growth of output in Argentina, as documented in figure 1, is also apparent in investment. The fall of investment is documented in figures 5 and 7, and in table 3 where the investments of all agents (enterprises, public sector, and households) are considered. One can observe, in particular, in table 3, that the share of total investment in GDP fell from 26.8% in the 1970s to 18.4% in the 1990s. Simultaneously, the share of investment in equipment (one component of fixed capital) fell from 10.9% to 7.2%. The Argentinian reprieve (only up to 20%) took place between 1993 and 1998. The share of total investment recovered from the low rates of 1990, culminating at 21% in 1998, though well below earlier trends, and before entering a new phase of decline: short-lived and small!

To sum up: There was some recovery of investment in Argentina between 1993 and 1998. It remained, however, limited by historical standards, and led to a sudden collapse after 1998.

3.1.2 Foreign savings and investment

An important feature of the revival of investment during the 1990s is that it was financed by foreign countries. Figure 6 reproduces the share of total investment in GDP as in figure 5 for the years 1990-2003, but net of depreciation. The two additional lines break down the sources of financing of investment into two components, national savings (internal financing) and foreign savings (external financing).

The figure shows that foreign savings contributed largely (more than national savings) to the financing of the wave of accumulation between 1993 and 1998, as well as during the recession (1999-2000) before the depression. When investment declined in 1995, it also fell; in a similar manner, the decline of investment from 1999 onward coincided with the contraction of foreign savings. Thus, foreign savings appear: (1) as an important contributing factor of investment, and (2) tightly correlated to the *fluctuation* of investment (at least up to 2001).

Table 3 - Argentina: Ratios of investment to GDP (%)

	1950s	*1960s*	*1970s*	*1980s*	*1990s*	*(1993-1998)*
Total investment/GDP	20.3	23.0	26.8	20.9	18.4	(20.0)
Investment in equipment/GDP	7.6	10.3	10.9	6.9	7.2	(7.9)

The revival of investment during the 1990s was largely financed by foreign savings, whose role appears crucial.

3.1.3 Imports and investment in equipment

The present section focuses on one fraction of investment, equipment, one component of productive investment by enterprises, the other component being structures. (When imported, *equipment* corresponds to the import of *capital goods*.) This investigation shows that equipment is the key element in the triangular relationship introduced earlier.

This central role of equipment follows from the fact that, at least since 1980, about 80% of the imports of Argentina are capital goods. (The share of consumption goods rose between the 1980s and 1990s from 9.3% to 20.8%, but most of imports remained capital goods even after 1990.)

Figure 5 Total investment as a share of GDP (%): Argentina, 1950-2004

Total investment in this figure and table 3 means here gross investment by all agents, enterprises, public sector, and households, and in all categories of capital goods, structures (residential and nonresidential) and equipment.

Figure 6 Total net total investment and its financing as a share of GDP (%): Argentina, 1990-2003

Net domestic investment: (——)
Net national savings: (-----)
Foreign savings: (·········)

Investment is as in figure 5, but net of depreciation. The period is limited to the last segment of the line in figure 5: the restoration during the 1990s. The two other series break down its financing into net national savings and foreign (or external) financing.

4 - External accounts

The assets of a country in another country are denoted as its *foreign assets*, and, from the viewpoint of the recipient country, as the *foreign liabilities* of this latter country (liabilities to the investing country). The use of the term "foreign" can be misleading. For example, assume that these relationships are considered from the viewpoint of Argentina and that the foreign country is the United States. Foreign investment (or financing) means investment from the United States, while foreign assets refer to U.S. assets held by Argentines. Foreign liabilities means assets held by U.S. agents on the Agentinian economy (Argentinian securities or loans).
We use the following decomposition of the total foreign liabilities (to the rest of the world) contributing to the financing of a given country:

$$\begin{aligned} &\text{Foreign liabilities} = \text{Foreign direct investment in the country} \\ &+ \underbrace{\text{External borrowings} + \text{Others (basically stock shares in portfolio investment)}}_{\textit{Foreign nondirect investment}} \end{aligned}$$

Such investments are reciprocal. The net contribution of foreigners to the financing of a country, at a given point in time, is the balance of the stocks of foreign liabilities and assets of this country, which can be positive or negative. (If foreign liabilities are larger than foreign assets, the contribution of foreigners to the financing of the economy is positive.) This net foreign contribution varies over time. *Foreign savings*, also denoted earlier as *external financing*, is defined as the variation of the balance of the stocks of foreign liabilities and assets, or, equivalently, the difference between the variations of the two stocks:

$$\text{Foreign savings} = \text{Variation of foreign liabilities} - \text{Variation of foreign assets}$$

There is an accounting identity between foreign savings and the *balance on current accounts*, which is the sum of the balance on trade (exports minus imports) and of the balance on income flows between the country and the rest of the world:

$$\underbrace{\begin{bmatrix} +\text{Exports} \\ -\text{Imports} \\ +\text{Balance on income} \end{bmatrix}}_{\textit{Balance on current account}} = \underbrace{\begin{bmatrix} +\text{Variation of foreign assets} \\ -\text{Variation of foreign liabilities} \end{bmatrix}}_{-\begin{array}{c}\textit{Foreign savings} \\ \textit{(External financing)}\end{array}}$$

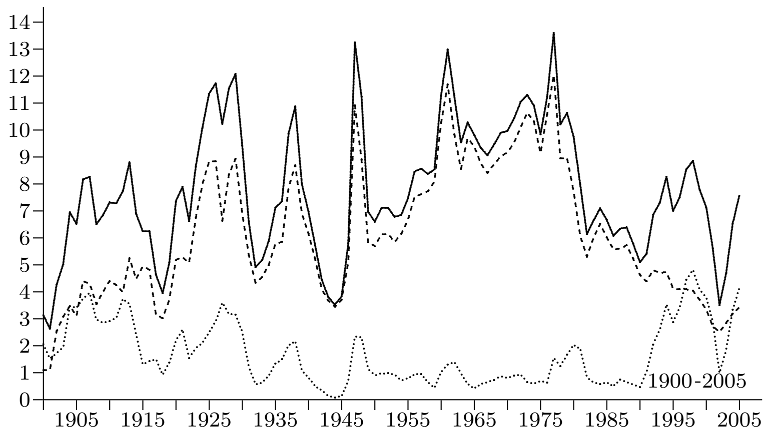
The following relationship can be deduced from the above. It lists the possible sources of financing of imports (Δ stands for "variation of"):

$$\begin{aligned} &\text{Imports} = \underbrace{\text{Exports} + \text{Balance on income}}_{\textit{Other components of the balance on current account}} + \\ &\underbrace{\Delta\text{ Foreign direct investment} + \Delta\text{ External borrowings} + \Delta\text{ Others} - \Delta\text{ Foreign assets}}_{\textit{Foreign savings}} \end{aligned}$$

Figure 7 shows the share (——) in GDP of investment in equipment since 1920 (see also the second line of table 3):

1. A preliminary remark is that the collapse of investment in equipment at the transition between the 1970s and 1980s matches that observed for total investment. The limited restoration during the 1990s is also clearly evident.
2. The two additional lines denote respectively equipment produced in Argentina and

Figure 7 Investment in equipment and its origin, as a share of GDP (%): Argentina



Total: (——)
Produced in Argentina: (-----)
Imported: (·········)

By "origin", we mean here equipment produced respectively in Argentina and abroad. This figure uses the same data source as figure 3.

Figure 8 Imported equipment and foreign direct and nondirect investment as shares of GDP (%): Argentina

Imported equipment: (——)
Foreign direct investment: (-----)
Foreign nondirect investment: (·········)

Investments are expressed dollars using PPP exchange rates and divided by GDP in the same unit. Equipment are measured in constant pesos of 1993 and divided by GDP in the same unit.

imported. The figure clearly documents the fact that the entire increase in investment in equipment during the 1990s came from abroad. In the early 2000s, about half of the investment in equipment is imported, and the final decline of investment is also mirrored in that of the imports of equipment. The high exchange rate during the 1990s rendered imports comparatively cheap and encouraged the import of capital goods from abroad.[10] Simultaneously, obstacles to free trade and to the free mobility of capital were removed.

It is interesting to return here to figure 3, which shows the proportion of imported equipment in total investment in equipment since the beginning of the 20th century (the ratio of the third (┈┈) to the first (——) series in figure 7). We already noted the reliance on domestically produced capital goods in the early 1970s and the wave of imports during the second half of the decade. Around 1975, the percentage had been diminished to about 7%; the subsequent wave of imports of foreign equipment reached 23% (during the first episode of foreign borrowing). These imports collapsed with the restrictions in the 1980s. The relevant aspect is now that, in less than a decade, between 1991 and 1999, the percentage returned to 50%.

We can now compare directly the investment in equipment and foreign financing. Figure 8 shows the shares of both direct and nondirect investment in GDP in Argentina and the share in GDP of imported equipment. As could be expected, the profile of imported equipment matches that of foreign direct and nondirect investments in figure 9. Investment in equipment was not only largely imported from abroad, but also financed by foreign investment, mostly nondirect investment. It is the key element in the above triangular set of relationships.

As shown in box 5, a similar pattern was manifest in Brazil, but it was not prolonged beyond 1995, when direct investment was substituted for lendings.

3.1 *This latter element brings the overall description of the investment wave in Argentina, and of its consequences, to its conclusion:*

1. The restoration of investment between 1991 and 1998 was real, though limited in size.

2. It was highly dependent on foreign countries, concerning its physical origin as well as its financing.

3. Most imports were made of equipment purchased abroad. It seems that the major fraction of external financing was the expression of loans linked to the purchase of capital goods, a crucial factor in the rise of the private external debt.

4. The importance of the import of capital goods in foreign trade is such that this component accounts for most of both total foreign financing and imports, whatever the directions of causation. Thus, investment in equipment and the corresponding foreign financing played a central role in the overall pattern of macroeconomic relationships: accumulation of capital, foreign trade, and external debt.

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10. When imports of equipment are paid in dollars, using credits in dollars, the exchange rate does not alter the cost of investment. However, if the output is sold in pesos and its price not adjusted in relation to the devaluation of the currency, the capacity of the cashflow to generate resources for the service of the debt is sensitive to the rate of exchange.

5 - Imports and foreign savings in Agentina and Brazil

It is interesting to compare the observation above to the pattern of events which prevailed in Brazil. The same basic mechanisms were at work, but differences are also telling.
Figure 9 shows the total imports (——) of Argentina (instead of only the imports of capital goods as in figure 8). The figure also shows external borrowings (– –) and foreign direct investment (-----). The relationship between investment and nondirect investment (borrowings) is again evident, except that imports are larger (since goods other than capital goods are imported). The fourth line (·········) is identical to imports (——) except that a given percentage of GDP has been subtracted. One can, thus, observe more easily the tight relationship between imports and external borrowings, which echoes the finding in figure 8. The interest of this exercice is to allow for a comparison with Brazil, for which similar data are available.
Figure 10 presents the same series for Brazil, exactly in the configuration of figure 9. A preliminary remark is that imports represent a percentage of GDP close to that observed for Argentina. From 1975 to 1995, the profile is similar to that of Argentina but, then, the divergence is dramatic, as borrowings fall to zero or below (as debt is repaid). Direct investment seems to compensate for part of the difference, thus earlier than in Argentina and in a much more stable manner. The wave of nondirect investment, that is basically borrowings, appears retrospectively shorter than in Argentina, as direct investment was substituted for nondirect investment. (The situation of Mexico is also thoroughly different from that of Argentina.)
To sum up: (1) The dependency of the wave of accumulation on imported capital goods and external financing, in Argentina, determined the general pattern of imports; (2) This mechanism was also observed in Brazil, but the singularity of Argentina is that it was maintained in this country throughout the reprieve of the 1990s, with a limited contribution of direct investment in spite of the late and ephemeral peak at the end of the 1990s. Nondirect investment, mostly borrowings, was the engine of this investment wave. Overall, the stubborn rise of indebtedness in relation to the import of capital goods, up to the late 1990s, appears as a striking singularity of the Argentinian economy.

3.2 Argentines' investment abroad

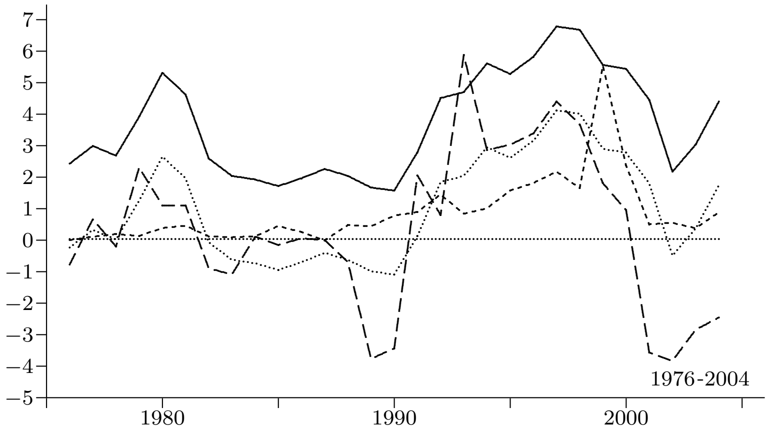
Time is now ripe to look at the other side of the coin. If the flows of foreign currency resulting from exports, the sale of enterprises, and the income on foreign assets was not used to pay imports (financed by specific loans), the question must be posed of their final destination (box 4).

The answer is straightforward. It is a well-known characteristic of the country that large flows of capital are invested abroad, both lawfully and unlawfully.[11] The establishment of the convertibility regime in 1991 made this practice legal and easy. The pegging to the dollar, at the high rate of one peso for one dollar, was very beneficial to Argentinian investors. Thus, the accumulation reprieve was paralleled by a large outflow of capitals.

Figure 11 shows the foreign assets and the external debt of the private nonfinancial sector (households and enterprises) in billion dollars. A preliminary remark is that assets are larger than the debt; the net external position of this sector is positive. One can observe that, in 1992, this sector already held assets in foreign countries amounting to about 16% of GDP(PPP), that is 49 billion dollars, while its external debt was very low: 6.8 billion dollars. In 2002, the amount of assets had about doubled, that is reached 29.5% of GDP(PPP). Simultaneously, the debt grew to 13.3% of GDP(PPP), that is 53 billion

11. Cámara de Diputados de la Argentina, *Fuga de Divisas en la Argentina*, Buenos Aires: Siglo XXI Editores Argentina S.A. (2005).

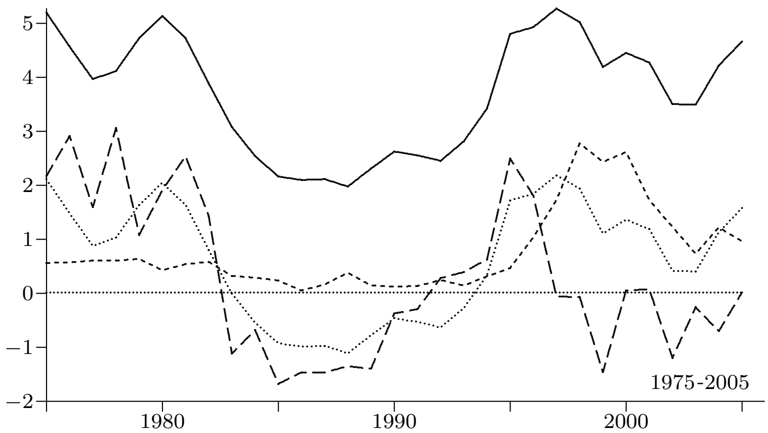
Figure 9 Imports and external borrowings as a share of GDP(PPP) (%): Argentina



Imports: (——)
External borrowings (debt): (— —)
Foreign direct investments: (-----)
Imports (shifted): (·······)

For legibility, the average difference between imports and borrowings for the years 1979 to 1995 has been subtracted from the series of imports, in the shifted import line (— —). This shift amounts to −2.6%. The relationship between the profiles of imports (— —) and external borrowings (——) is striking.

Figure 10 Imports and external borrowings as a share of GDP(PPP) (%): Brazil



Imports: (——)
External borrowings (debt): (— —)
Foreign direct investments: (-----)
Imports (shifted): (·······)

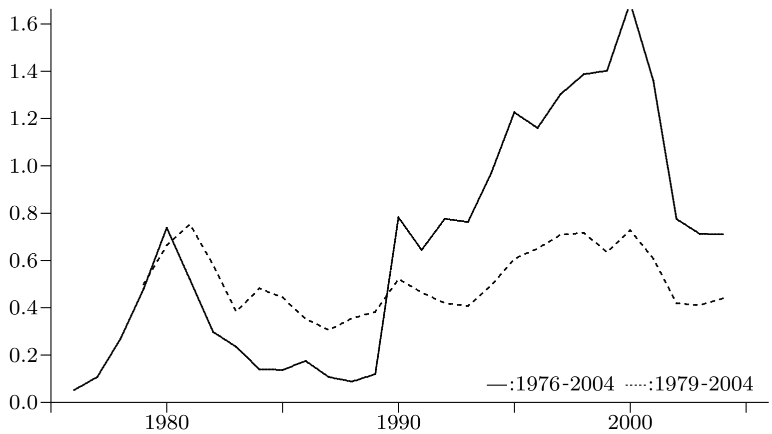
The variables are determined as in figure 9. The shift amounts to −3.1%.

Figure 11 Foreign assets and debt as a share of GDP(PPP) (%): Argentinian private nonfinancial sector

Foreign assets: (——)
Foreign liabilities: (-----)

The stocks of assets and debt (total liabilities) are measured as outstanding at the end of the year. One can surmise that assets are held by households and debt by enterprises. The breaks in the series in 2001 mirror the change of measurement, which particularly affected the intrafirm debt between parents and affiliates. This component of the debt was multiplied by two, from 2.1% of GDP(PPP) to 4.5%.

Figure 12 Inflows of financial income as a share of GDP(PPP) (%): Argentina and total of the seven major contries of Latin America



Argentina: (——)
7 major countries: (-----)

dollars. (Most of this debt corresponds to the financing of the investment in equipment described above.)

This feature of the Argentinian economy is also manifest in the inflows of financial income received from investment abroad. Figure 12 shows these flows as a percentage of GDP(PPP) in Argentina and in the seven major countries of Latin America. In particular in Argentina, the 1980s stand out as a decade of comparatively low income inflows; but the dramatic increase during the 1990s testifies of the mass of assets invested abroad. During this decade, income flows to Argentina stand dramatically above the average of the seven countries.

3.2 *Thus, the following striking features of the Argentinian economy and society in general, during the last decades, emerge unambiguously: The two tendencies, borrowings to finance accumulation and outflows of capital, progressed in tandem, signaling a process of substitution. Instead of financing investment in their own country, Argentines sent their capital abroad, and accumulation relied on borrowings in foreign currency. The same hemorrhage dimished the capacity of the country to finance its public expenses, as we will see.*

3.3 Deceived expectations: trade and profitability

In the best of the neoliberal worlds, the new wave of investment, benefiting from foreign technology at a relatively low price, was supposed to generate growth, an increased efficiency, and higher levels of profitability, allowing for the payment of comparatively high rates of interest, and augmenting the capability of the country to export.

As section 2.1 contends, expectations concerning growth performances were deceived. This apparent in figure 4, which allows for a closer look at growth rates (········). After the break at the beginning of the 1980s, earlier growth rates were never recovered.

Section 3.3.1 and 3.3.2 documents the two remaining aspects of these poor achivements, concerning trade and profitability.

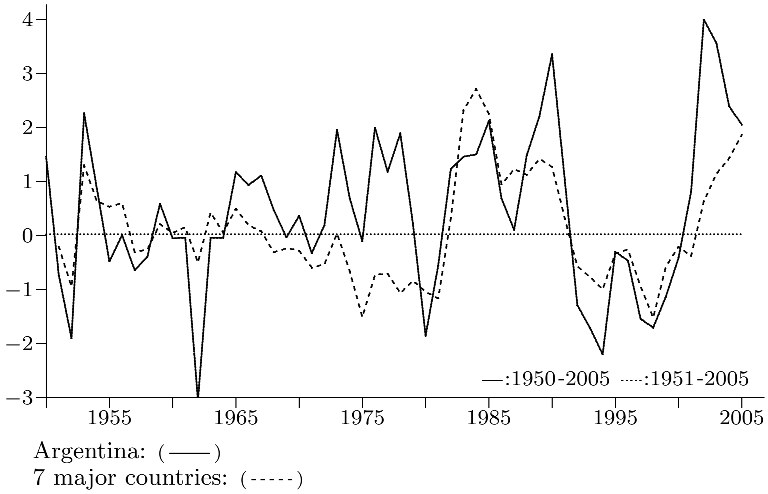
3.3.1 Trade

Obviously, the high exchange rate and the all-out opening of commercial frontiers required significant adjustment to the new conditions of international competition. The proportions of output were supposed to "adapt" the Argentinian economy to the new international division of labor. It could be feared that the "adjustment" would be mostly destructive, through the closing domestic enterprises. But the benefits, for, at least, the most dynamic sector of the economy, were expected to outweigh the costs.

The balance of trade is an interesting variable in the interpretation of these new trends. During the first half of the 1980s, the surplus of trade mirrored the comparative increase of manufacturing raw materials and combustibles, whose share in total exports reached 50%. This percentage fell dramatically from 1986 onward. Underlying these fluctuations, one can identify the tendencial comparative rise in the export of goods of industrial origin. In 1980, the exports of such goods represented about half of that of manufacturing goods originating in the agroindustry. In the early 2000s, these two components of exports were about equal. This tendencial rise of goods of manufacturing of industrial origin probably echoes the expansion of transnational corporations and the insertion of Argentina in the corresponding new international division of labor.

Concerning the balance of foreign trade, what actually happened was at odd with the optimistic expectations for the 1990s. A large deficit of trade was observed. This is shown in figure 13 which plots the balance on trade (goods and services) as a percentage of GDP(PPP), for Argentina and for the seven major countries of Latin America. In sharp contrast with the 1980s, the 1990s were a decade of deficits. (One can parenthetically notice the tight similarity of Argentina with the average of the seven major countries of Latin America, with the exception of the late 1970s.)

Figure 13 Balance on trade as a share of GDP(PPP) (%): Argentina and the total of the seven major countries of Latin America



3.3.2 Profitability

In what follows, we will rely on data concerning the 500 largest enterprises (excluding finance and the agroindustry) in the country. One particular interest of this data source is that enterprises are broken down by the nationality of the owners. Three groups are considered: (1) with foreign ownership lower than 10% of capital (denoted as *national enterprises*); (2) with foreign ownership above 50% (*foreign owned enterprises*); and (3) in between (a small category). For simplicity, we conserve the first and second groups.

A measure of profit rates for these enterprises is shown in figure 14. Profits are after paying indirect business taxes and interest; capital is enterprises' own funds (assets minus debt). One can observe that favorable profiles were maintained until 1996-1997. Then, a sharp decline occurred, a second manifestation of deceived expectations. One can also notice that national enterprises are less profitable than foreign enterprises, and that their profit rate diminished even more. The fall in profitability is quite spectacular, in particular within national industries, from a maximum of 12% in 1997, to a minimum of 2.2% in 2001. The year 1998 is already a low point, with profit rates even lower than 1996.

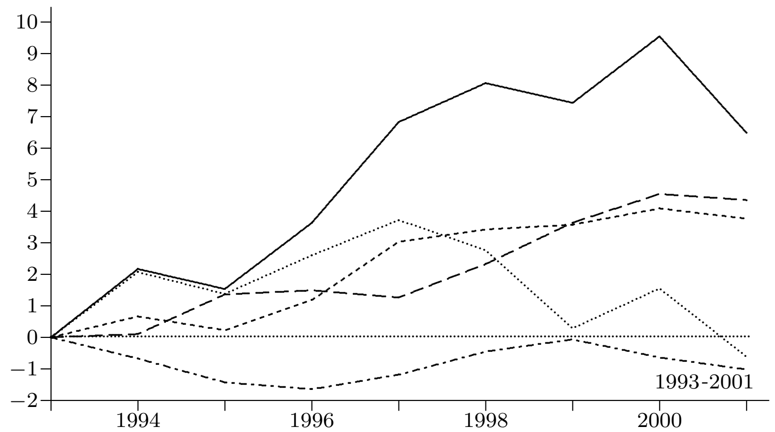
As evident in figures 14 and 15, the decline of the profit rate in these enterprises began when they were hurt by the recession, and it is hard to determine the direction of causation.

Figure 14 Profit rate (Billon pesos, 1993=0): Argentina, 500 largest enterprises

National enterprises (< 10 %): (——)
Foreign-owned enterprises (> 50 %): (-----)

The profit rate is defined as: $\frac{\text{Profits net of interest and business taxes}}{\text{Enterprises' own funds}}$

Figure 15 Value added, profits, and costs (billion of pesos of 2000, deviation from 1993, set to 0): Argentina, 500 largest enterprises



Net value added: (——)
Total compensation: (-−-−)
Indirect business taxes (minus subsidies): (-----)
Net interest paid: (— —)
Profits: (········)

All variables have been set to 0 in 1993. Consequently the values shown measure the deviation in each year from the value in 1993, in billion of pesos of 2000. One has:

Profits = Net value added − Costs = Net value added − (Compensation + Taxes + Interest)

The chain of event is further analyzed in figure 15. This figure plots value added, profits, and various components of costs in billion of pesos of 2000 for the total of the 500. All variables have been set equal to zero in 1993, therefore the lines account for the deviations from this year. The followings are noteworthy:

1. Profits culminated in 1997, and then began their dramatic decline (·········). This observation echoes that made above for the profit rate.

2. Indirect business taxes (-----) grew rapidly from 1995 to 1997, as output, and stagnated later.

3. The cost of labor (-–-–) remained constant, or even diminished. As shown in figure 2, real wages were stagnating, in spite of the rising labor productivity.

4. The major cause of the declining profitability between 1997 and 1999 was *indebtedness*, and the corresponding burden of interest (— —).

- The ratio of total debts to enterprises own funds rose from 79% in 1995, to 108% in 1998, and remained at about the same level in 1999.
- The share of interest the total nonwage income of enterprises (value added minus the compensation of labor) rose from 12% in 1997, to 17% in 1998, and 25 percent in 1999. Some complexity is created by the sharp, though ephemeral, rise of interest rate coinciding with the Tequila crisis in Mexico and the recession in Argentina in 1995. The percentage of interest in nonwage income peaked in 1995 at 17%. It diminished in 1997, though it never returned to its previous lower levels. This is when the new upward trend was asserted.
- To the growing indebtedness, one must add the rise of interest rates in the wake of the Asian crisis.
- The weight of interest later increased as the economy entered into recession after 1998.

In the analysis of the growing burden of interest and indebtedness, it is important to distinguish between foreign and national enterprises. Most of the growing debt was contracted by foreign enterprises to invest or to buy other enterprises, but the ratio of their debt to their own funds grew moderately (from 90% in 1995 to slightly more than 100% in 1998). These enterprises were also financed by retained profits and the issuance of new shares. They borrowed considerably but it appears that they were not going into debt when the entire pattern of their balance sheet is considered. National enterprises borrowed considerably less, but the ratio of their debt to their own funds passed from about 75% in 1995 to nearly 125% in 1998.

3.3 *Globally, it appears that the alleged virtuous circle, borrowings → investment in foreign advanced technology → high profitability levels and exports, as assumed in mainstream literature, thoroughly failed to materialize. The cost of the debt became unbearable, although wages were stagnating.*

The growing indebtedness of corporations is, however, only one of the mechanisms that led to the collapse of 2001. We now turn to second element, the rise of public deficits. High interest rates hurt directly enterprises, but they also caused public deficits which led the goverment to increase taxes, further encroaching on the profitability of enterprises.

4 - Public deficits and growing indebtedness

The Argentinian public sector includes the federal and provincial governments. To these units, we may aggregate or not the Central bank; if this bank is excluded, the unit is the nonfinancial public sector.

This section first considers the growing debt of the public sector (section 4.1) and, second, analyzes the main causes of the rise of the debt (section 4.2). Section 4.3 is devoted to the total external debt of the country, of which the public debt is a major component.

4.1 The public debt

Figure 16 shows the rise of the total debt of the nonfinancial public sector since the last quarter of 1992, in billion dollars. The most striking observation is the steady upward trend. The debt increased from 71 billion dollars at the end of 1992 to a peak of 191 at the end of in 2004. Figure 16 also breaks down the total public debt into securities and loans (plus arrears from 2003 onward):

1. *Public securities* (-----). (including guaranteed loans (-----)[12] from the end of 2001). The total of public securities (held by resi dents and nonresidents) accounts for a major share of the public debt: 76% at the end of 2000; the remaining 24% are loans. From 2002 onward, a new category of loans gained in importance in this total, *guaranteed loans*, as the public sector borrowed from commercial banks, under crisis conditions.

2. *Loans (national and international, including the IMF)* (·········). In this second component, loans from commercial banks remained practically null. Since 1993, the major fraction is made of international loans from international organizations, reaching a maximum 22% of the total debt at the end of 2001. Alone the loans from the IMF accounted for 19% of the public debt in this same year.

3. *Arrears* (— —). Beginning in 2003, one can observe the accumulation of unpaid debt, when Argentina began to default on its public debt, up to the drastic cancellation at the end of 2005. Between the first and second quarters of 2005, the debt was cut by 33%.

Overall, and abstracting from arrears, the public debt of Argentina is basically made of securities and loans from international organizations. The proportion is about 3 to 1.

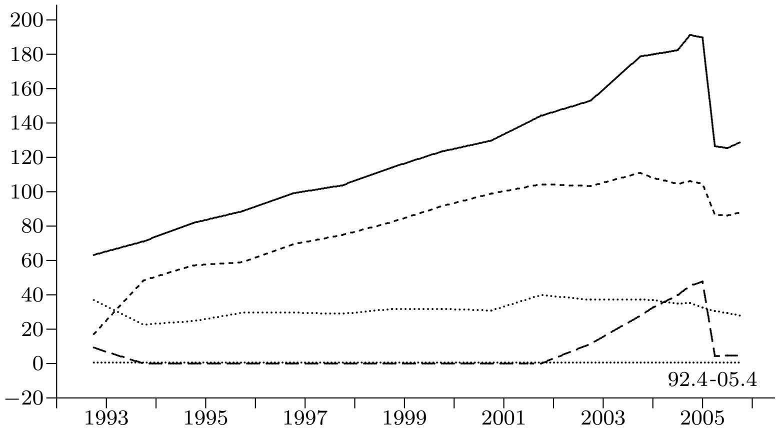
Figure 17 is devoted to public securities, combining two criteria: in national and foreign currency, on the one hand, and held by residents and nonresidents, on the other. Note that foreigners hold very little securities in national currency, as could be expected. The following observations can be made:

1. *Public securities in foreign currency held by nonresidents* (-----). This first important component amounted to more than 40% of the total debt up to 2000; since 2001, it was slightly inferior to the securities in foreign currency held by residents.

2. *Public securities in foreign currency held by residents* (— —). Originally weak in the early 1990s, the amount of public securities in foreign currency held by residents kept rising

12. *Prestamos guarantizados* and *Deuda garantizada*.

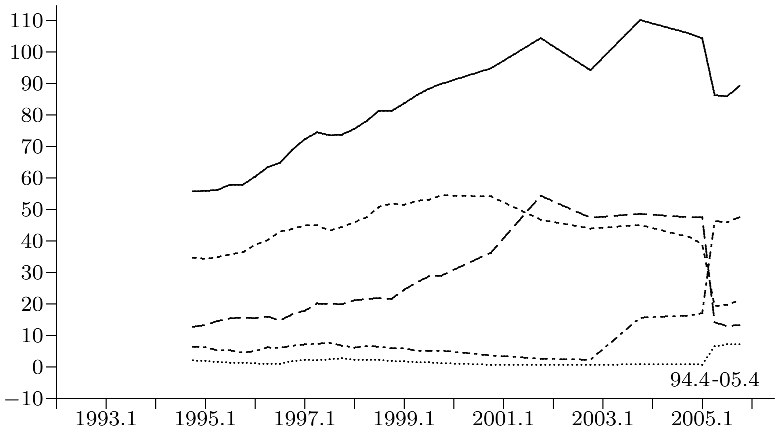
Figure 16 Total debt by instruments (billion dollars): Argentina, public sector (nonfinancial and financial)



Total public debt: (——)
Public securities: (-----)
Loans: (·········)
Arrears: (— —)

The series is, first, annual (stock outstanding in the fourth quarter of each year), and then quarterly from 2004 onward.

Figure 17 Public securities, including guaranteed loans, by holders and currency (billion dollars): Argentina, Public sector



Total (without arrears): (——)
Foreign currency, Residents: (— —)
Foreign currency, Nonresidents: (-----)
National currency, Residents: (-–-–)
National currency, Nonresidents: (·········)

The total (——), in this figure, is public securities (-----) in figure 16 .

up to 2001, when it slightly outweighed such securities held by nonresidents. From 2001 to 2004, the total amount remained about constant.

3. *Public securities in pesos held by residents* (-·-·-). The securities in pesos held by residents remained low up to 2003. They grew suddenly during the crisis, and, in the last observation, are a lot larger than the two previous components (each accounting of about one third of the public debt in securities).

Total public securities in foreign currency, held by residents and nonresidents, are not presented in figure 17, but the following commentaries can be made. Between 1995 and 2001, this component rose from 60% to 70% of the public debt. They always accounted for more than 80% of total public securities (up to 98% in 2002).

Figure 17 also documents the pattern of the cancellation in the last quarter of 2005. Comparing the years XXX and XXX, the total XXX% reduction can be decomposed between the debt in foreign currency of, respectively, residents and nonresidents by XXX% and XXX%, partially offset by the rise of the debt to residents in pesos, by XXX%.

4.1*Overall, the rise of the Argentinian public debt was dramatic, and maintained or accelerated up to the partial cancellation in early 2005:*

1. The debt to international organizations remained about constant. In the early 2000s, prior to the cancellation, it represented about XXX% of the public debt.

2. Before 2001, most of the rise of the public debt in securities can be imputed to securities in foreign currency held by residents.

3. The composition of the debt in securities was thoroughly modified by the crisis and its treatment:

- *In 2001, the public debt in securities was basically in foreign currency, and held half and half by nonresidents and residents.*

- In 2005, the public debt in securities was about 50% in pesos, held by residents. Another fraction amounting to 39% (in foreign currency) was partly held by residents (37%) and nonresidents (33%).

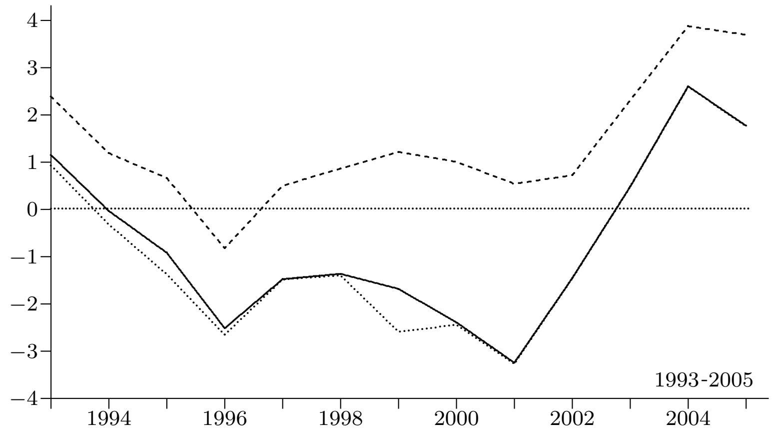
4.2 A surge of public expenses?

As shown in figure 16, the public debt was relatively weak in 1992, amounting to 63 billion of dollars, that is 28% of GDP at going prices. This percentage was, in no way, extraordinary, in spite of two episodes in which private debts were transferred to the government.[13] The growth of the public debt is, nonetheless, often described as the outcome of an explosion of public expenses and deficits. This is not what happened.

Actually, the burden of interest was the major cause of deficits during the 1990s. Overall, this burden was caused by the large interest rates characteristic of neoliberalism (figure 34) , in particular real interest rates, compared to those prevailing during the Keynesian compromise. There was generally no large spread charged on Argentinian borrowers (figure

13. By Domingo Carvallo during the dictatorship in 1982, and in 1985, under the administration of Alfonsín.

Figure 18 Balance on public accounts as a percentage of GDP (%): Argentina, nonfinancial public sector



Total balance: (——)
Primary balance: (-----)
Total balance without privatization: (·········)

Figure 19 Three components of public expenses as a percentage of GDP (%): Argentina, nonfinancial public sector

Interest: (——)
Transfers to the private sector: (-----)
Cost of the deficit of social security: (·········)

35, (——)). In particular the interest on the public debt prior to 1998 was not larger than in the United States.[14]

Figure 18 shows the balance on public accounts as a percentage of GDP. The figure distinguishes between the total balance and the primary balance, that is before the payment of the interest on the debt. The primary balance remained constantly positive, with only a small deficit in 1996. Conversely, the overall balance plunged during the early 1990s, manifesting deficits from 1995 onward. (The consideration of the revenue created by privatizations only slightly alters the profile, even in 1999, as shown in figure 18.) A surplus appears in 2003 and 2004.

Besides the burden of large interest rates, it is also well known that the levels of tax collection are low in Argentina. Larger flows of revenues could have help paying interest. The assessment of these mechanisms is, however, difficult. It would be necessary to estimate the impact on the economy of a more efficient tax collection and smaller deficits. The problem is that the consequences of the flows of interest paid (1) to nonresidents or (2) to rich social categories, with a strong propensity to export their savings abroad, are disastrous. Could have larger taxation rates compensated for this effect?

It is also sometimes contended that the Argentinian government was unable to control expenses, given the complex relationship between federal and provincial governments. This is certainly relevant to some extent, but one must keep in mind that the actual problem was not the explosion of basic expenses.

There is, however, a major exception to this assessment, which also relates to neoliberal options. It is the reform of social security (retirement), with the creation of pension funds in 1993. It is not coincidental that such a reform was undertaken during the euphoric episode of rise of the stock market woldwide. The fact that the new cohort of employees contributes to investment plans reduces the revenue of the traditional pay-as-you-go system, which still finances the retirement of ealier cohorts. The deficit must be paid by the government, and the cost was huge. Given the problems later faced by pension funds, notably in the United States[15], this option appears retrospectively as a blunder (or crime).

A third factor was the generous transfer of resources to the private sector. One should not forget here that neoliberalism relies less on the diminished intervention of the state, than on the promotion of private capitalist interests. The accumulation reprieve of section 3 benefited largely from the assistance of the government.

These three components of rising public expenses are illustrated in figure 19. The figure shows the percentages of GDP represented by: (1) interest; (2) transfers to the private sector; and (3) the cost of the deficit of social security. The shares in total GDP of the three latter components increased considerably between 1993 and 2001. Interest heads dramatically upward to reach 3.8% in 2001, as well as the cost of social security. It is easy to imagine the consequences of such trends and levels, in a country in which public revenue only represents 19% of GDP (average 1993-2004).

4.2 *There was no explosion of public expenses in Argentina. In spite of the low rate of collection of revenue, and given the complex system articulating the Federal and provincial governments, the entire deficits can be interpreted as a perverse effect of the new neoliberal trends (high interest rates and the move toward pension funds).*

---

14. We consider the apparent rate of interest on the total Argentinian debt, compared to the rates on U.S. government 10 years bonds. The rates are similar, except between 1998 and 2001.

15. Mirrored in the refusal of funds to commit themselves for the future (hence the move from defined benefits to defined contributions)!

4.3 The public debt in the total external debt

The public debt, as in section 4.2, differs from the external debt of Argentina, that is the debt toward nonresidents, on two obvious accounts. First, the private sector (the nonfinancial private sector, that is enterprises and households, and the financial private sector) is also in debt toward nonresidents (although the foreign assets of the private nonfinancial sector are larger than its debt, figure 11); second, only part of the public debt is toward nonresidents, that is external. One should also keep in mind that two concepts are at issue, *external debt*, and the debt in foreign currency in which residents also participate. Practically the total of the external debt was in foreign currency, and it is still the case in the mid-2000s.

Is the Argentinian debt exceptionnally large in comparison to Brazil or Mexico? The answer is positive.[16] This is shown in figure 20 which compares the external debts of Argentina, Brazil, and Mexico as percentages of GDP(PPP) from 1982 to 2002 . From the debt crisis to the mid-1990s, the percentages were similar in Argentina and Mexico, around 23%. Then, the weight of the debt of Mexico began to decline, as the country was paying its debt, while the Argentinian debt exploded. The ratio is lower for Brazil, and rather stable, fluctuating around 15%. The worst period for Argentina is, therefore, the second half of the 1990s and the early 2000s.

Figure 21 shows the external debt of Argentina and its components as shares of GDP(PPP), the debts of the: (1) public (nonfinancial and financial, that is the Central bank), (2) nonfinancial private sector, and (3) financial private sector. Additional information is provided in table 4. The period (1992-2004) covered in this figure is distinct from that in figure 20. The sources are different, and the two measures are not exactly the same. The following observations can be made:

Table 4 - Increase in Argentina's external debt as a share of GDP(PPP) (%)

	From 1992 to 1998	*From 1998 to 2001*	*From 2001 to 2004*
(1) Total	12.2	1.3	-2.5
(2) Public sector*	2.2	1.6	4.0
(3) Private sector	10.0	-0.3	-6.4
(3a) Nonfinancial private sector	*7.2*	*0.8*	*-4.2*
(3b) Financial private sector	*2.8*	*-1.1*	*-2.3*

* Nonfinancial and financial, that is including the Central bank.

1. The public debt (— —) is the major component of the external debt of Argentina, and it grew rather consistently throughout the period, although at varing paces.

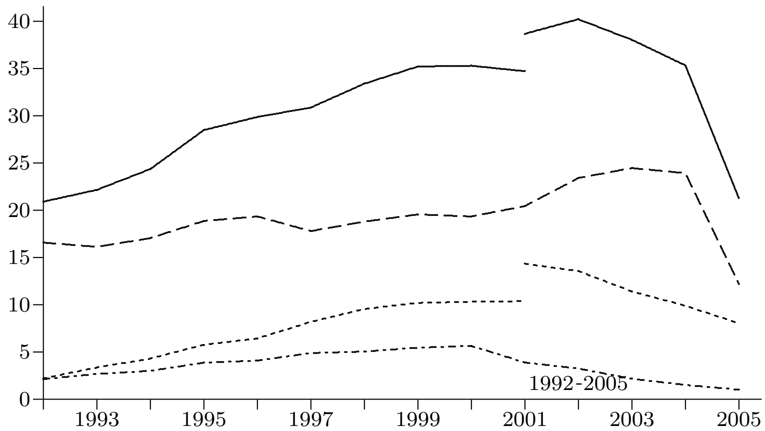
2. Up to the end of the 1990s, this rise remained, however, limited in comparison to the increase of the debt of the private sector, financial (-–-–) and, in particular, nonfinancial (-----). As shown in table 4, during the period 1992-1998, the public debt gained 2.2

16. Not in comparison to the United States, where the external debt in the strict sense, that is limited to credit market instrument, is larger than 50% of GDP.

Figure 20 The external debt as a share of GDP(PPP) (%): Argentina, Brazil, and Mexico

Argentina: (——)
Brazil: (-----)
Mexico: (·········)

Figure 21 The external debt and its components as shares of GDP(PPP) (%): Argentina, private sector and public sector (both nonfinancial and financial)



Total: (——)
Public sector (with the central bank): (— —)
Nonfinancial private sector: (-----)
Financial private sector: (-·-·-)

The break for the nonfinancial private sector (-----) is explained in the caption of fiugre 11, where the same series has already been presented.

percentage points of GDP(PPP), while the debt of the private sector gained 10 percentage points (7.2 points for the private nonfinancial sector).

3. Between 1998 and 2001, the private debt as a percentage of GDP(PPP) began to stagnate (diminished slightly). This observation is in line with the analysis, in section 3, of the termination of the accumulation wave, which reduced private borrowings.

4. It is during this latter phase that the public external debt (line 2 of table 4) began to increase sharply, gaining 4 percentage points.

4.3 *The public external debt went on rising during the ultimate, paroxystic stage, between 2001 and 2004, when the debt of the private sector was beginning to decline. The main factor responsible for the deteriorating situation of external accounts prior to 1998 was the nonfinancial private sector.*

5 - Macroeconomy out of control

This section discusses another aspect of the trajectory that led to the crisis: the difficulty to control the macroeconomy in the new institutional framework of the 1990s. These mechanisms do not question, but supplement, the earlier set of determinants. Argentina was not equipped, in terms of policy, to check the growing imbalance of the 1990s and the recession that began 1998. This unchecked recession evolved into a deep crisis.

Section 5.1 recalls the major aspects of the set of reforms implemented at the beginning of the 1990s. Section 5.2 is devoted to the end of hyperinflation. Section 5.3 discusses the macro policies of the 1990s, in particular the currency board. The functionning of the board is considered in relation to the behavior of financial "markets".

5.1 The framework established in the early 1990s

After ten years of stagnation and recurring recessions during the 1980s (in particular between 1988 and 1990), and with rates of inflation larger than 100% nearly every year and culminating at 3000% in 1989, Argentina underwent a thorough reform process, which conferred on the 1990s very specific characters. The major aspects were as follows[17]:

1. *Trade liberalization.* Most taxes and duties on exports and imports were eliminated, as well as quantitative restrictions.

2. *Privatization.* Most of the major public enterprises were privatized: Port services in 1992, Oil company in 1993, Ecoteza (Federal Post and Telegraph Company) in 1994, Postal system in 1997...

3. *Pensions.* The pay-as-you-go system was replaced by a combination of pension funds and public transfer.

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17. P. Pou, "Argentina's Structural Reforms of the 1990s", *Finance and Development, IMF*, 37 (2000), http://www.imf.org/external/pubs/ft/fandd/2000/03/. P. Pou was director of the Central bank. Writing in 2000, he hailed Argentina's "path to sustained growth", calling for more reforms.

4. *The Convertibility Law of 1991 and the Central Bank Charter of 1992.* Convertibility was established at the rate of 1 peso-1 dollar. The Central bank was compelled to maintain a given ratio between the monetary base and international reserves (a substitute for gold in the past). This mechanism is known as a *currency board.* It has three aspects: (1) convertibility; (2) fixed exchange rate; and (3) the ratio *monetary base / international reserves* equal to 2/3. In a narrower acception, the reference to the currency board is sometimes limited to the third element. One of its explicit purpose was to forbid the financing of public expenses (federal and provincial) by the Central bank. The Central bank was made independent from the government, and the role of the bank as lender of last resort was curtailed (as international capital markets were supposed to regulate the Argentinian macroeconomy), rendering monetary policy impossible.

5. *Bank regulation.* All restrictions to the establishment of foreign banks were lifted. Simultaneously, strong financing requirements were implemented. In 1991 and 1995, the capital requirement (the ratio of own funds to credits) was imposed at a comparatively high level. The reserve requirement (the ratio of the reserves of commercial banks in the central bank to deposits in their accounts) was fixed at 40% for checking and saving deposits (3% for time deposits). Balance sheets are permanently assessed through a set of standard indicators. Between 1991 and 1999, the number of banks declined from 167 to 119, among which the number of public banks was reduced from 35 to 16.

Although the currency board is not usually presented in this manner, it would have little meaning if such ratios were not established between the accounts of commercial banks and their reserves in the Central bank. The entire chain is:

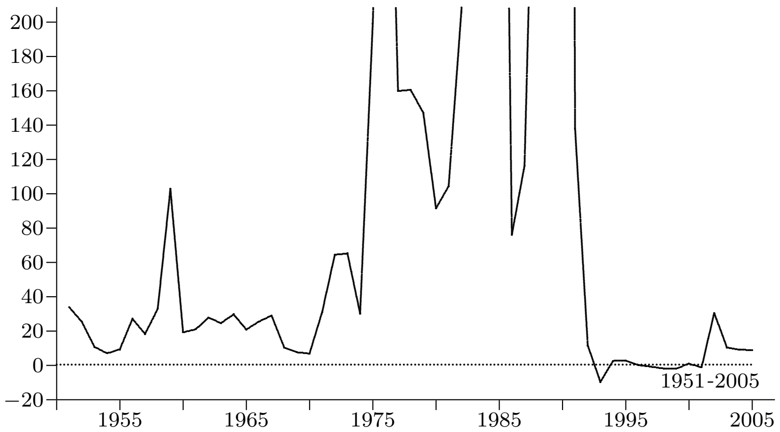
$$\text{Reserves of the Central bank in foreign currency} \xrightarrow{1} \text{Monetary base} \xrightarrow{2}$$
$$\text{Reserves of commercial banks in the Central bank} \xrightarrow{3}$$
$$\text{Credits and money in the economy}$$

The first link, 1 in the diagram above, is controlled by the ratio proper to the currency board, that of the monetary base to the reserves of the Central bank in foreign currency. The second link, 2, limits the capability of the Central bank to finance other banks by new loans in central money (the monetary base), inflating the accounts of these banks in the Central bank. The third link, 3, is controlled by the requirement on the ratios imposed on the balance sheets of banks. The deposits that they hold are pegged to their reserves at the Central bank, and this limits their capability to create money by granting new loans.

Indeed, these reforms, conferred on the 1990s specific institutional features. But another major transformation, which echoes what happened in countries of the Center, is the sharp control on wages from 1990 onward (figure 2). Not only inflation was curbed, also the demand from workers for better living conditions. The decline of wages was stopped for a few years at a low plateau, at levels actually similar to those of the 1950s — a puzzling profile, given the comparatively high rate of accumulation.

5.1 *The overall neoliberal inspiration of the reforms of the early 1990s is obvious: free trade, free capital movements, independent Central bank, privatization, crucial role conferred on international finance through the mechanical device of the currency board, etc. The interpretation of the pegging of the peso to the dollar, instead of a freely floating currency, is more ambiguous. This set of measures inserted Argentina into world imperialism in a quite specific position, that we discuss section 9. The neoliberal features of the period are also apparent in the new stagnation of real wages.*

Figure 22 Rate of inflation (%): Argentina



Rates have been cut to 200%. In 1989, the maximum rate was reached at 3060%.

5.2 Curbing inflation

The new framework proved very efficient to curb inflation. The episode of hyperinflation is shown in figure 22, from 1975 to 1991, culminating at 3060% in 1989. Hyperinflation was rapidly eliminated after nearly two decades, as inflation rates returned to levels similar to those prevailing in the United States. Figure 23 compares the index of prices in Argentina (——) and in the United States (– –) during the 1990s and early 2000s. It is striking to observe that, during those years, up to the crisis in 2002, prices rose actually less in Argentina than in the United States.

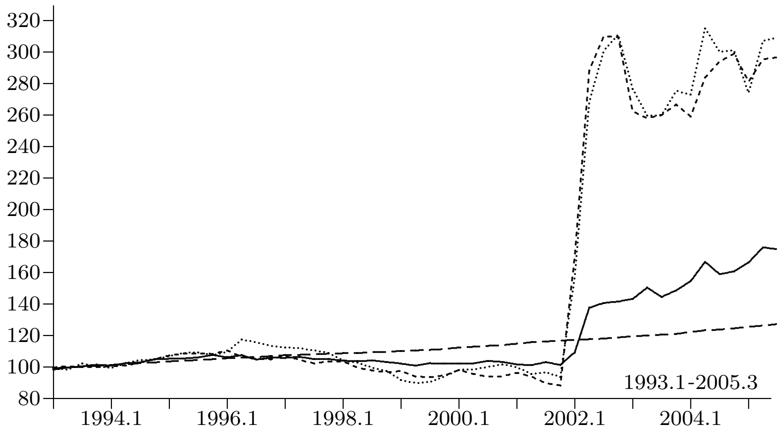
Various policy measures can account for the end of hyperinflation:

1. *High exchange rate.* Figure 24 shows the ratio of the actual exchange rate to the PPP exchange rates. This ratio is an indicator of the comparative evaluation of the national currency. "Levels" are difficult to assess because of the diverging patterns of production and demand in the countries considered, and the interpretation of variations is less ambiguous.

One can notice in the figure the sharp revaluation of the peso in the 1990s, and the maintenance of such levels up to the spectacular devaluation. The high level of the exchange rate after the reforms was a first obvious factor of disinflation, as the pressure of international competition appeared suddenly acute. (Domestic production was threatened by potential imports, and the import of consumption goods increased.) Symmetrically, the price of exports, which is established in dollars on international markets, was diminished when expressed in pesos, placing the profits of exporting enterprises under pressure.

2. *Tighter credit (denoted as "claims" in the data, both loans and securities).* Figure 25 testifies of another determinant: the drastic reduction of loans to the economy by domestic financial institutions (that is resident banks) in 1990. The diminished domestic credit to the private economy (·········) can be considered a factor in the taming of inflationnary trends. But the cut was even more severe concerning the public sector (-----). (This was one of the primary purposes of the implementation of the currency board.) These reductions opened simultaneously an avenue for foreign financing.

Figure 23 Price indexes: Argentina (GDP, imports, and exports) and United States (GDP)



Price indexes for Argentinian GDP: (——)
Price indexes for Argentinian imports: (-----)
Price indexes for Argentinian exports: (·········)
Price indexes for U.S. GDP: (— —)

Between 1993 and the devaluation, the inflation rate was lower in Argentina than in the United States. The effects of the devaluation are discussed in section 7.6.

It is obvious that such a curtailment of credit had a potentially recessionary impact. There was, however, no recession. The key to a nonrecessionary anti-inflationary recipe is the combination of: (1) the encouragement of productive investment, and (2) the taming of the other components of demand (demand, other than enterprises' investment, from households and the public sector) in adequate respective proportions.[18] This is what happened in Argentina, as a result of the lower prices of imported capital goods, allowed by the large borrowings abroad of the private sector that were described earlier.

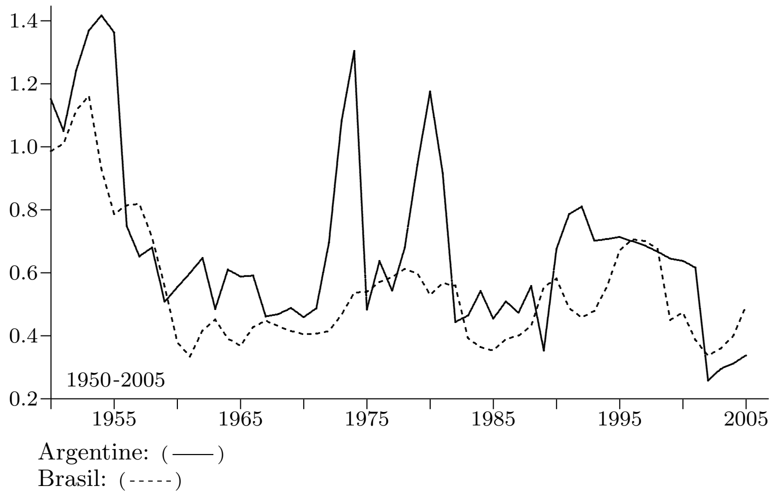
3. *A surplus of public accounts.* Public accounts were XXX balanced. This new situation did not last much as the interest paid on the public debt caused new deficits in the mid-1990s (section 4.2). Constrained by the currency board, forbidding any financing of public deficits by loans from the Central bank, the public sector had to resort to international borrowings to finance its deficits, that is to service its debt, a totally new configuration. This new course contributed to the rise of the external debt, though considerably less that the borrowings of the private sector (figure 21). .

5.2 *The new framework implemented at the beginning of the 1990s proved very efficient to curb hyperinflation. Monetary, budget, and exchange policies combined their effects.*

5.3 The currency board: A built-in destabilizer

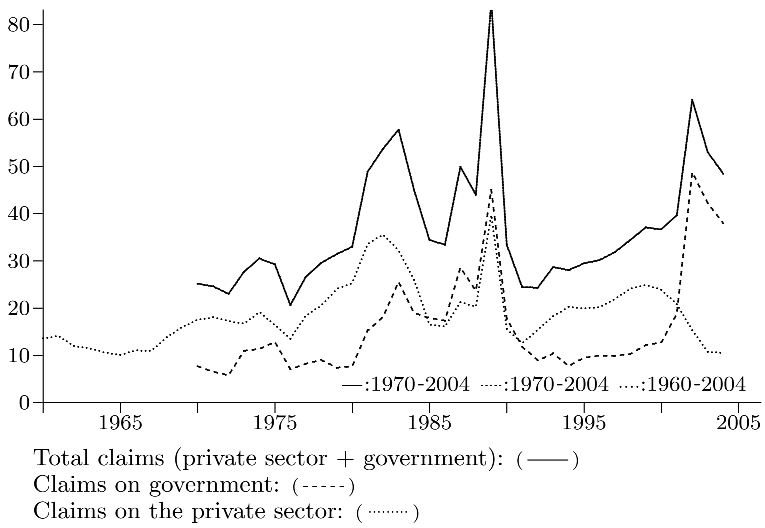
18. This is the true policy mix, of which the *monetary policy/deficit policy mix* is an inaccurate substitute in Keynesian accounts.

Figure 24 The ratio of exchange rates to purchasing power exchange rates: Argentina and Brazil



A ratio superior to 1 indicates that actual exchange rates are superior to purchasing power exchange rates. In general, in Latin America, the order of magnitude of these ratios, since World War II, was 0.4 or 0.5. Although absolute figures must be considered cautiously, the similar levels observed in the two countries are certainly not coincidental. Changes can be interpreted in a more straightforward manner.

Figure 25 Claims on government and the private sector by domestic financial institutions as a percentage of GDP (%): Argentina



"Claim" means "credit", both loans and securities. Public enterprises have been aggregated with the private sector.

The following sections consider, in turn, the three aspects of the currency board beginning with the control of credit (section 5.3.1) to which the board is often reduced, and then turning to the international free mobility of capital and the role of international financial institutions (section 5.3.2), and fixed exchange rates (section 5.3.3).

5.3.1 The control of credit

The framework of the currency board was meticulously established to control domestic credit, a function which is normally that of monetary policy. Credit and money were limited by the availability of reserves in foreign currency.

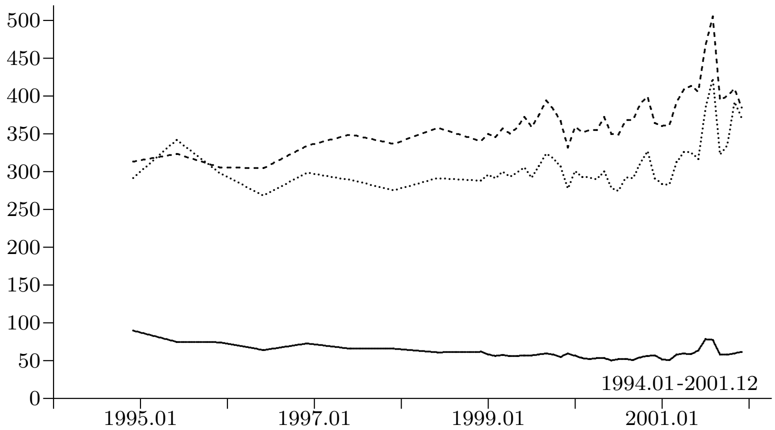
The basic ratios (section 2.3.2) of the currency board were actually maintained. Figure 26 shows the ratios of various stocks of domestic credits and monetary aggregates to the reserves of the Central bank up to the end of 2001. One can observe that, up to 2000, they all remained tendencially stable, with short-term fluctuations. This was the outcome of the three links, 1, 2, and 3, presented in the diagram in section 5.1.

The major contradictions lie downstream. The preservation of the basic ratios did not help monetary and financial aggregates from representing a growing percentage of output (instead of the reserves of the Central bank in foreign currency). Figure 27 illustrates this expansion. In 1994, total credit amounted to 18% of GDP; this percentage reached 28% at the end of 2001. The currency board controls credits in comparison to reserves in foreign currency but not to the total economy; it does not avoid the rise of credits and does not adjust to the needs of the macroeconomy in a situation of crisis; it is not a countercyclical monetary policy; it was not able to check the recession which began after 1998.

The concept of the currency board is based on an erroneous vision of monetary mechanisms, a survivance of the past:

1. A surplus of foreign trade provokes an inflow of foreign currency, and stimulates credit through the board. This credit, in turn stimulating demand is supposed boost importation and put an end to the surplus. The converse is true in the case of a trade deficit. Correct: this is an anticyclical mechanism. The board seems to have been conceived in this context.
2. But contemporary capitalism is also a world of free capital mobility:
   - Trade credit is not limited by the currency board.
   - Excepting trade credit, external financing (as in direct investment) generates an inflow of foreign currency. This flow may end up in the Central bank and stimulate domestic credit. Thus, external financing is transformed into internal financing. The effect is, therefore, cumulative instead of corrective, procyclical instead of anticyclical. (This is, to some extent, what happened during the episode of accumulation 1991-1998.) The converse is true in the case of a declining external financing: Through the mechanics of the board, the departure of foreign capital implies the restriction of domestic credit, when exactly the opposite would be required!
   - The Central bank itself or commercial banks may borrow, provoking an inflow of reserve currency, thus allowing for the expansion of domestic credit. But this is precisely what will not happen in the verge of a crisis. International private finance acts according to its own interests, not in conformity with the needs of the macroeconomy of the recipient country, and stops lending.

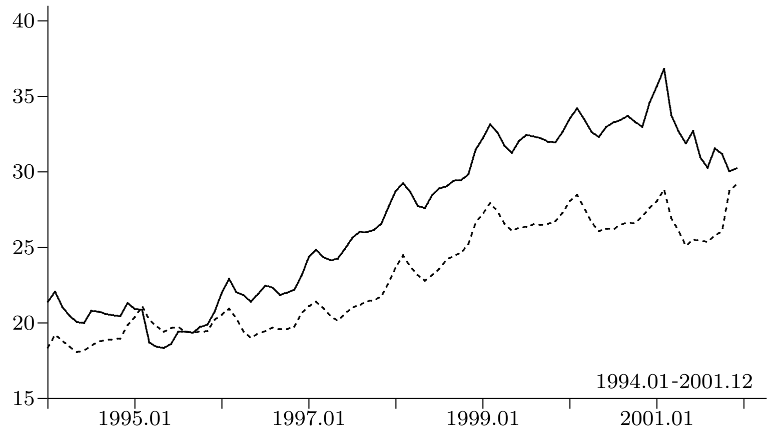
Figure 26 Credit and monetary aggregates as percentages of foreign currency reserves of the Central bank (%): Argentina



Monetary Basis: (——)
M3*: (-----)
Total loans: (·········)

M3* is M3 plus money and assets in dollars. The data is by semester untill 1999, and then by quarterly.

Figure 27 Credit by domestic financial institutions, and monetary aggregates, as percentages of GDP (%): Argentina



M3*: (——)
Total loans: (-----)

Monthly data.

Concerning Argentina, one should add the gradual dollarization of the economy to this inefficient control of credit, a fourth aspects of the overall framework, that of a *super-board*. In orthodox literature, the use of financing in dollars (external financing and the dollarization), instead of domestic financing *under control and in local currency*, is justified by two types of arguments. First, it is contended that Argentinian authorities were unable to stop lending when the funds were coming from local financial institutions in pesos, be they the Central bank or commercial banks. This only means that the blunder, that the establishment of the currency board represented, had social determinants, but does not alter its nature as such. Second, dollarization is often cited as a move tending to increase the cost of abandoning the board. The logic was to qualm the fears of international financial markets. This is a central theme in orthodox literature. But the pursuit of dollarization to the extreme had catastrophic consequences.

5.3.2 The free mobility of capitals: The role of international markets

One, often implicit, argument in favor of the currency board is that the smaller, more unstable, country, here Argentina, "relies" on the financial system of a "big brother", the United States, to "anchor" its own macroeconomy. This is pure propaganda. The behavior of U.S. financial institutions vis-à-vis Argentina is not clearly impacted by monetary policy in the United States, and certainly not determined by the requirements of the situation of the Argentinian macroeconomy. The monetary authorities in the United States do not determine their behavior in relation to the situation prevailing in another country. Argentina actually abandoned the control of its macroeconomy to international private financial institutions, in particular U.S. financial institutions (the so-called markets).

Yes, international finance had the last say on the Argentinian macroecomy, propelling it to extreme external indebtedness, before suddenly refusing to finance in accordance with its own perception of the local situation and its own interests:

1. "Markets" went on lending, up to the last stages of the growing deterioration of the situation. The threat of an impending dislocation of the board was negated. The cost of breaking the currency board was judged high and prohibitive!

2. The risk was perceived very lately, as apparent in the sharp rise of the *sovereign-debt spread over US Treasuries* spread in 2001, as it is emphatically labelled. This is documented in figure 35, (——). Note the sharp difference with the rate charged to the foreign affiliates of foreign financial institutions.

3. The IMF tends to play internationally the role conferred on national Central banks, or to supplement it. As the Argentinian crisis proved, the support of the IMF can be more resilient than that of private finance, but does not measure up to the task of stabilizing major crisis situations, and is subject to FMI's "stabilization plans" which add to the instability of the macroeconomy (as clearly exemplified during the Korean crisis).

International finance is not a substitute for a domestic central banks. It did not appreciate the Argentinian situation adequately. Its action worked in the exact opposite direction of an efficient — contracyclical — monetary policy: (1) too much during the boom, in particular to the private sector; (2) a sudden curtailment, in spite of the interventions of the IMF at the end of 2000 and beginning of 2001 ; and (3) no easing during the collapse.

In the currency board, international "markets" are supposed to take care of everything. This is precisely the point to which Keynes objected: Regulating the macroeconomy cannot be left within private hands. The device is a ghost of preKeynesian times, at least of the ideology of this remote epoch.[19] A country like the United States would never return to a situation in which the control of the macroeconomy is left to private financial institutions. Monetary policy is very strong in this country. (Imagine what would have happened in this country if credit and public expenses had been cut in 2001.) And international financial institutions would obviously not be trusted either by U.S. authorities.

5.3.3 The pegging of the peso to the dollar

As shown in figure 24, in terms of purchasing power parity, the peso was maintained at a comparatively high rate, an average of 0.6 between XXX and XXX. Abstracting from the two peaks which marked the period of hyperinflation (when assessing PPP exchange rates becomes practically impossible), the average PPP exchange rate was XXX.[20] Not only the level is at issue, but also the fact that the manipulation of the exchange rate could not be used as one of the tools of macro policy (as it was in Brazil). Abstracting from the curbing of inflation, the following observations can be made:

1. The high level of the exchange rate was one of the factors of the deficit of trade characteristic of the 1990s (figure 13).

2. The same situation acted in favor of the import of capital goods, which suddenly became cheaper for Argentinian importers. A benefit was expected in terms of efficiency (the expression of the larger productivity of foreign equipment), but this movement contributed to the rise of the foreign debt.

3. The comparison with Brazil shows that a downward adjustment of the exchange rate would have been required when the situation began to seriously deteriorate in the second half of the 1990s. The effect of the devaluation after the crisis confirms this diagnosis: Indeed, a lower rate of exchange improved the situation, but the measure came in the wake of the crisis!

5.3 *Controling the macroeconomy is a crucial, central, task in modern capitalism. It relies on anticyclical feedback mechanisms (reaction to disequilibrium). The currency board is not a substitute for such mechanisms. On the contrary, the behavior of "markets", which are assumed to perform the task, is procyclical.*

6 - External shocks

In the above account, the course of monetary and financial mechanisms was only assessed in relation to the situation prevailing in Argentina. In a world of free trade and free circulation of capitals, countries of Latin America are obviously also subject to the impact of the situation of other countries, in particular of the Center. In this section, we discuss commercial and financial relationships, with a special emphasis on the United States, in spite of the strong links between Latin America and Europe.

19. Even under the *National Banking System*, prior to the creation of the Federal Reserve, in 1913, the financial system did not work in this manner (G. Duménil, D. Lévy, *Capital Resurgent, op. cit.* note 1, Box 18.1).
20. .

Figure 28 Argentinian exports and output in the seven major countries of Latin America (%): growth rates

Argentina, rate of growth of exports (divided by 4): (——)
Brasil + Chile, rate of growth of GDP: (-----)

The two series have been deflated by the corresponding price indexes.

6.1 Foreign trade

As a preliminary to this analysis, it is useful to recall basic stylized facts concerning the external trade of Argentina. The share of the exports of Argentina to other countries of Latin America in its total exports grew dramatically during the 1990s, from slightly more than one fifth to nearly half. The share of exports to the United States remained stable since the beginning of the 1980s to only about 10% of total exports. Concerning imports, the share of Latin America in the imports of Argentina remained rather stable since the early 1980s, amounting to about one third of the total (and up to 40% after 2000). The share of the United States was about constant around 20%, that is the double of the share of exports.

An examination of the movement of the main variables suggests the following observations:

1. The variation of imports year after year clearly reflects the situation of the country and its capability to borrow with the sharp increase during the period of sustained accumulation and the decline into the crisis. Between 1998 and 2002, imports were divided by 3.

2. During the crisis of 1982 in the United States, the total exports of Argentina in the world were not diminished, which is not too surprising given the small share of exports going to this country. The relationship between the exports of Argentina and the situation prevailing in other countries must be sought within Latin America itself. Overall, Argentinian exports (in dollars) grew by XXX% between 1990 and 1997, and later stagnated (up to 2002) with some fluctuation, in particular a decline in 1999, when the average growth rate in the seven major countries of Latin America was about zero. Actually, there is a tight correlation between the average growth rate of these seven countries and the growth rate of Argentinian exports, as shown in figure 28.

3. It is often contended that the early devaluation of the Brazilian real in january 1999 (see figure 24) protected the Brazilian economy and damaged Argentina. One can observe in figure 28 that Argentinian exports diminished by about 3% in 1999. The earlier correlation was, however, restored from 2000 onward, though with growth rates diminished by approximately one percentage point.

6.1 *The impact of foreign trade on the macroeconomy of Argentina was felt in relation to other countries of Latin America (Brasil and Chili), to which most of Argentinian exports are destined.*

6.2 The impact of international financial flows

In our opinion, the major destabilizing effect of international relationships vis-à-vis countries of the Center is the impact of capital movements and their dramatic pattern of evolution. We already documented (figure 4) the large fluctuations of the flows of direct and nondirect investment in the seven major countries of Latin America, with: (1) the "pyramid" of direct investment during the second half of the 1990s, their surge and subsequent decline, with the summit reached in 1999; and (2) the wave of nondirect investment at the beginning of the 1990s and its gradual reduction. Figure 3 also shows (— —) the profile of Argentina's direct and nondirect investments: their sudden high levels (peaking in 1997), followed by their sharp fall from 1998 onward for Argentina, with negative values beginning in 2000.

6.2.1 Investment from the United States to Latin America

Further insight can be gained into these mechanisms by considering both investing countries of the Center and Latin America. Thus, we now focus on the overall relationship between the United States and Latin America globally.

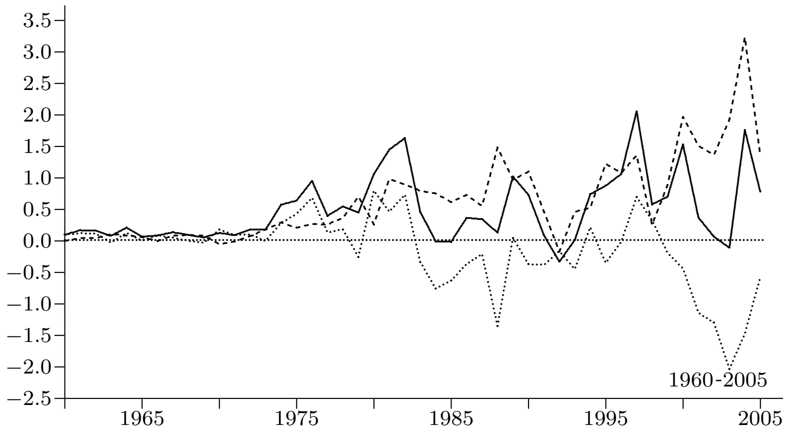
1. *The pattern of reciprocal investment.*

As a preliminary to the investigation of directions of causation, we recall the main features of investment between the United States and Latin America, successively nondirect and direct investment.

Figure 29 shows nondirect investment as a share of U.S. GDP, from the United States to Latin America and reciprocally:

- A preliminary observation is the strikingly high levels of nondirect investment from Latin America to the United States, often superior to the flow of nondirect investment from the United States.
- After 1982, that is in the wake of the debt crisis, the United States dramatically reduced its nondirect investment.
- The United States contributed lately to the explosion of nondirect investment in Latin America during the 1990s, actually mostly during the second half of the decade. This flow petered out beginning in 2001, when both the United States and Latin America were in recession.
- Up to 1997, practically all nondirect investment to the United States from this region of the world was *Government assets* (U.S. Public securities) . Conversely, the last fluctuation upward in the figure depicts investment toward the U.S. private sector.

Figure 29 Nondirect investment as a percentage of U.S. GDP (%): From the United States to Latin America and reciprocally



From the United States to Latin America: (——)
From Latin America to the United States: (-----)
From the United States to Latin America *minus* from Latin America to the United States: (·········)

Figure 30 Direct investment as a percentage of U.S. GDP (%): From the United States to Latin America, and reciprocally

From the United States to Latin America: (——)
From Latin America to the United States: (-----)
From the United States to Latin America *minus* from Latin America to the United States: (·········)

Symmetrically, U.S. nondirect investment in Latin America is practically exclusively directed toward the private sector.

Figure 30 shows the profile of direct investment:

- One should first notice that these flows are considerably smaller than those of nondirect investment. (For the entire period, they are about 4 times smaller.)
- There is a clear upward trend in the flows of U.S. direct investment abroad to Latin America.
- Two spectacular breaks are evident, first around 1982 and, then, beginning in 2002.

1. *Directions of causation.*

What causes U.S. investment abroad? Conditions prevailing in the United States or in Latin America? Both?

One important clue is that similar patterns of U.S. investment abroad are observed when the investment of the United States to all regions of the world is considered, besides Latin America. It is, thus, impossible to contend that the overall profile of U.S. investment abroad was the mere echo of chains of events proper to recipient countries. Consider nondirect investment and direct investment:

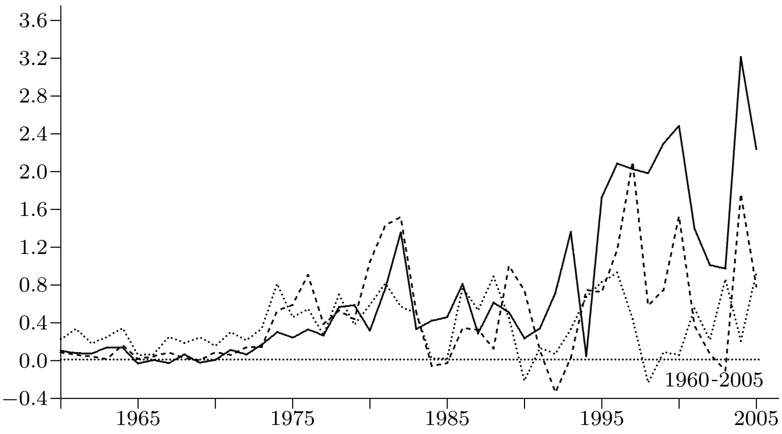
- The impact of the conditions prevailing in the United States is shown in figure 31 for nondirect investment toward three broad regions of the world: Europe, Latin America, and other countries. In the early 1980, one can notice the reduction (of the percentage of GDP) of the three flows, and the low levels maintained throughout the decade, a period of stagnating accumulation in the United States. The contrast is strong with the boom of the second half of the 1990s.

The above observation does not deny, however, feedback effects, as during the Argentinian crisis when nondirect foreign investment to Argentina was suddenly cut. (The trend of U.S. investment was downward when the crisis of 2001-2002 occurred, although flows of capital to Argentina were more resilient.) A few lessons can also be drawn, in this respect, from the crisis of the early 1980s, which also testifies of the feedback effect of conditions prevailing in the recipient country vis-à-vis the investing country.

- Figure 32 shows U.S. foreign direct investment as a share of U.S. GDP toward the same zones as in figure 31. One can observed that during the recession of the early 1980s in the United States, direct investment in both Europe and Latin America were diminished, in a manner quite similar to that apparent for nondirect investment, and this confirms the impact of conditions prevailing in the United States. Toward Latin America the flow even became negative, which is quite rare for direct investment. (It means selling affiliates or not renewing loans to these affiliates.) This suggests a cumulative effect of conditions prevailing in the United States and in Latin America (hurt by the debt crisis): again a reciprocal causation.

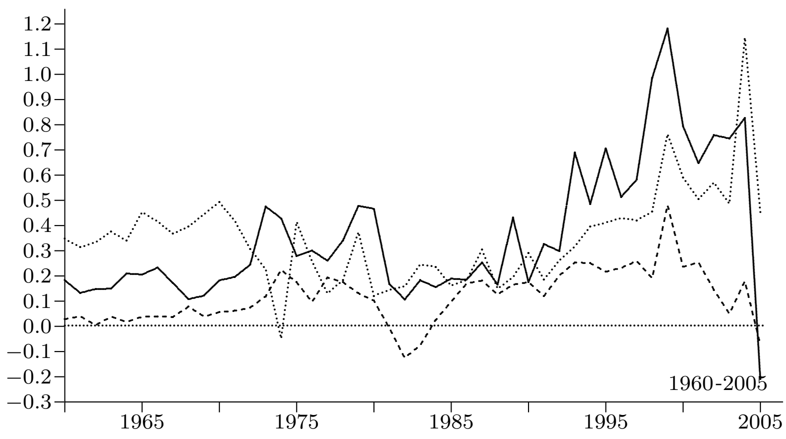
Overall, the foreign investment of United States rose during the U.S. long boom, as enterprises were investing (both domestically and abroad), as part of the same investing propensity proper to the United States. A causation running from the United States to foreign countries is, thus, apparent, but "local" conditions combined their effect when the situation began to deteriorate in Latin America.

Figure 31 U.S. nondirect investment in three region of the world, as a percentage of U.S. GDP (%): Europe, Latin America, and other countries



Europe: (——)
Latin America: (-----)
Other countries: (·········)

Figure 32 U.S. direct investment in three region of the world, as a percentage of GDP (%): Europe, Latin America, and other countries



Europe: (——)
Latin America: (-----)
Other countries: (·········)

6.2.2 Investment from Latin America to the United States and net investment

The mechanisms governing international capital movements must, however, be considered in both directions, inflows and outflows, rather than unilaterally. As shown in figure 29, very large flows of nondirect investment were sent from Latin American countries to the United States, in the 1980s, late 1990s, and early 2000s.

The net flow (········) of nondirect investment (from the United States toward Latin America *minus* from Latin America toward the United States, the distance between the two lines, (——) and (-----), in the figure) peaked in 1997 and began a dramatic slide to 2003. This net outflow of capitals from Latin America toward the United States began rather early, when the bubble was still on in this latter country; it was not interrupted by the crisis in the United States.

This hemorrhage of capital from Latin America occurred when the economic situation was deteriorating in this region of the world. Not only in Argentina: The macroeconomies of other countries were also affected in the late 1990s and early 2000s, though less drastically. Annual growth rates were null in 1998 in Mexico, in 1999 in Chili, and 2001 in Brazil, and equal to -4% in 1999 in Colombia.

Were such capital movements a cause or an effect of the situation in Latin America, or both?

1. Overall, it appears that in the general context of the recessionary trends at the end of the 1990s and in the early 2000s, international capital favored the Center, the United States, by nonexiting from this country or flowing to it from other countries where the situation was judged even more threatening.
2. It appears, finally, that, in 2004 and 2005, during the recovery in Latin America (with a grow rate larger than 4% in the seven major countries), capitals went on flowing from Latin America to the United States, and this observation suggests a more structural propensity to invest in the Center.
3. The main phenomenon was the sudden fall of U.S. nondirect investment to Latin America during the recession. The destabilizing character of free capital flows does not treat all countries evenly. In crisis situations, better being in the Center. *This stubbord "appeal" of the United States contributed to alleviate the crisis in this country, and to worsen it in Latin America.*

6.2.3 Capital flows: Argentina and the rest of the world

This section considers the flows of investment between Argentina and the rest of the world. The developments observed in Argentina are in line with those documented in figure 4 for the seven major countries of Latin America or the general trends described above for the United States and Latin America.

In the assessment of causation, the ambiguity is particularly strong concerning Argentina and the United States, because of the striking coincidence in time of macro events in the two countries (with the exception of the period 1998-2000 when the United States was booming and Argentina in recession). The wave of accumulation in Argentina coincided with the long boom of the second half of the 1990s in the United States, and the sudden contraction of output in the early 2000s occurred nearly simultaneously in both countries (though the recession was already under way in Argentina at a considerably slower pace, figure 38).

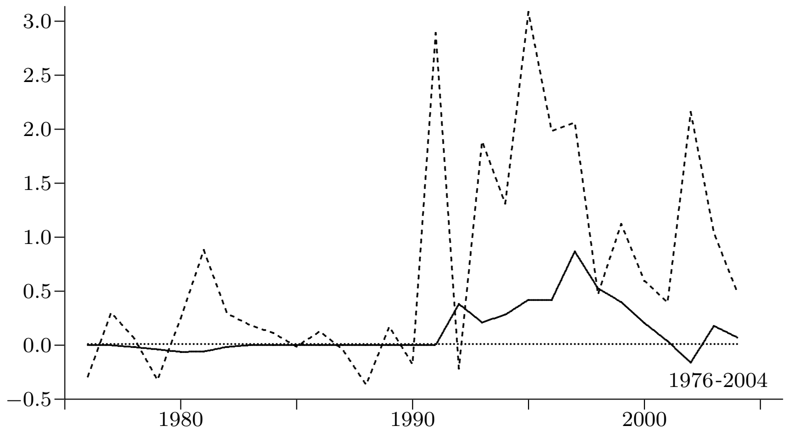
Figure 8 shows the inflows of foreign investment to Argentina:

1. The large "block" observed after 1990, concerning nondirect investment, is a common feature also observed in figure 4 for the seven major countries of Latin America, but, in Argentina, the levels achieved in the mid-1990s, are about the double of the average for the seven countries. This testifies of the strength of the wave of external financing and the corresponding stimulation of investment in Argentina (which does not appear clearly when the seven countries are considered globally).

2. The levels of direct investment are similar to those observed for the seven countries, though they are dwarfed in the figure by nondirect investment.

Whatever the origin of these movements, the Argentinian economy was successively pushed up and, later, precipitated downward with utmost violence when it was already in recession. Instead of compensating for the declining trend, these movements added fuel to the fire, as is typical of the mechanisms of the currency board. The chronology was as follows: (1) The recession began in the second half of 1998 (when the debt of investors was already large); (2) Nondirect investment fell from 1999 onward; (3) Direct investment fell from 2000; and (4) output collapsed in 2001. Within such a chain of event, it is vain to discuss whether the crisis was "caused" by financial markets: A reciprocal causation is at work.

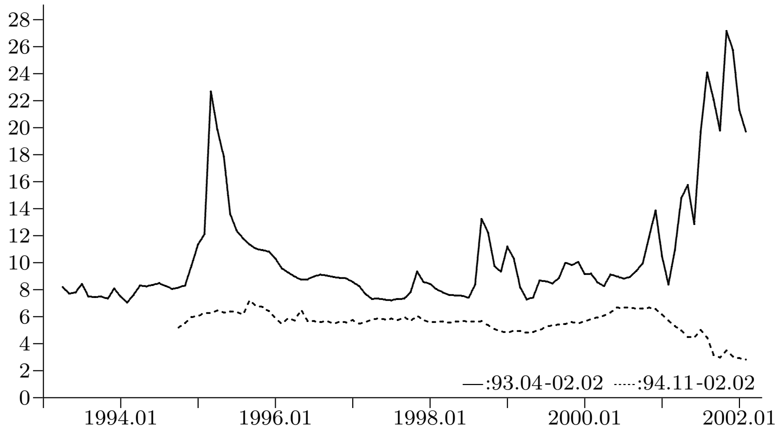
Figure 33 Foreign investment as a share of the Argentinian GDP(PPP): From Argentina to the rest of the world



Direct investment: (——)
Nondirect investment: (-----)

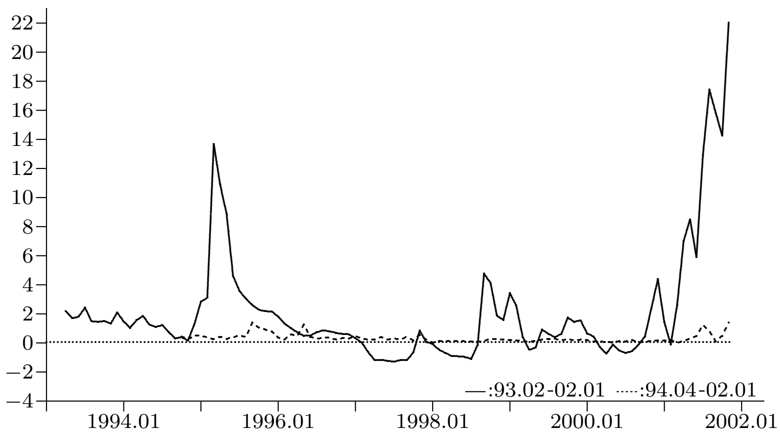
Figure 33 shows capital outflows from Argentina to the rest of the world. Foreign direct investment from Argentina to the rest of the world is typically low, contrary to nondirect investment that measures the exit of national capitals. The coincidence in time with the inflow of nondirect investment, in figure 8, is striking, though the outflows were smaller. During the 1990s, foreign nondirect investment stimulated accumulation in Argentina (as money was lent to finance investment in equipment), while the private sector of this country

Figure 34 Interest rates on loans in dollars (%): Argentina



Loans granted to prime companies: (——)
Loans granted to local financial institutions by related foreign institutions: (-----)

Figure 35 Spreads on loans in dollars (%): Argentina *minus* United States



Prime rate on short-term loans to business, Argentina *minus* U.S.: (——)
Loans by related foreign institutions *minus* U.S. Fed Fund: (-----)

The interest rate is the prime rate charged by banks on short-term loans to business and local financial institutions. The second rate (-----) is the rates charged to financial institutions, resident in Argentina, by the parent institutions.

was sending its capital abroad. This outflow did not stop during the first phase, that of recession before the crisis, although it was considerably reduced (while the corresponding inflows to Argentina fell and turned negative). It is obvious that these net outflows (inflows minus outflows) added to the financial difficulties of the national economy, private and public. The dramatic export of capitals in 2002 is clearly apparent, in the wake of the severe measures of the transition 2001-2002, and can be interpreted as a last move to leave the ship before the wreck.

6.2 *The behavior of countries of the Center in their decision to invest abroad is highly dependent on their own macroeconomic situation, with dramatic consequences for countries of the Periphery. It was so during the long boom in the United States, as well as the recession of the early 2000s in this country. The worst effect of these investments on the macroeconomy of Argentina, was its procyclical character (increased in a boom, cut in a recession), transmitted by the currency board. The emphasis is usually placed on short-term investment, but the same mechanisms are also at work concerning foreign direct investment. There is also an effect of local conditions prevailing in the country, acting in combination to the above; the combination of the two types of circumstances may have dramatic cumulative effects, as during the crisis in Argentina. Outflows from the countries of the Periphery, on the part of residents, are structurally large and may play a crucial role, as in the early 2000s, when the local conditions turned bad, with the same procyclical outcome.*

6.3 Interest rates in Argentina

Another conspicuous expression of the impact of external shocks is the movement of interest rates. We already commented on the impact of the sudden rise of interest rates in 1979. The two decades, that of the 1980s and 1990s, are years of large real interest rates, with dire consequences, both in the Center and Periphery. Rates are presented in figure 34. The first interest rate considered is the prime rate on short-term loans to nonfinancial business. The second is the rate charged by parent financial corporations to their affiliates. The present section focuses on the specific profile of rates in Argentina: the difference between rates in this country and those prevailing in the United States, known as "spread".

Figure 35 shows such spreads for the two rates considered in figure 34. The series (——) is the value of the rate charged to Argentinian business minus that charged to U.S. business. The second is that charged to institutions by parent financial corporations to their affiliates. The following commentaries can be made:

1. A first important observation is that, abstracting from recessions, no spread was charged during the second half of the 1990s.

2. On can observed in the figure the dramatic rise of interest rates in Argentina during the Mexican Tequila crisis of 1995, by which the Argentinian economy was only mildly affected. The gradual decline of rates after the crisis lasted to the XXX quarter of 1996. But, then, usual levels and fluctuations were again observed.

3. A second major shock was felt when the rouble collapsed in October 1998. About one year later, interest rates in Argentina were back to usual levels, or maybe slightly above.

4. We will discuss the latter movements of this variable in the analysis of the crisis in section 7.1. This is when the other series will be considered. The surge of the spread in the first series (——) must obviously be related to the sudden outflow of foreign capital.

6.3 *The recurrent sudden rise of interest rates testifies of the impact of foreign circumstances, as during the Tequila crisis in Mexico, in 1995, and in the wake of the collapse of the rouble in 1998. Finally, the dramatic rise of the spread in 2001 and 2002 testifies of the refusal of foreigners to lend to the Argentinan business, with the exception of financial affiliates.*

The combination of the weakness of monetary policy, as discussed in section 5.3, and the impact of international capital flows as in the above sections, shows that the ability of a country like Argentina to control its macroeconomy was radically deficient, both during the reprieve of the 1990s and when the situation later deteriorated.

7 - From recession to crisis, 1998-2001

Section 7.1 recalls the two-step process which led to the crisis. Section 7.2 shows how the growing debt of the public sector impacted the private sector. Section 7.3 considers the profile of interest rate under recession and crisis circumstances, as well as the contraction of credit up to the crisis. Section 7.4 is devoted to macro policies, and section 7.5 to the management of the crisis.

7.1 A two-step process

Figure 36 shows the profile of output during the Argentinian reprieve and crisis. Output grew in Argentina up to the second quarter of 1998. Then, the situation of the macroeconomy deteriorated in two steps prior to the final recovery:

1. The economy entered a period of recession after the peak in the second quarter of 1998, up to the second quarter of 2001. Output declined rather steadily at an annual rate of 2%, during 3 years, a quite unusual trajectory.

2. Beginning in the second half of 2001, the economy collapsed into a major crisis or depression up to the second quarter of 2002.

3. One can finally observe the rapid recovery. In the second quarter of 2005, a level superior to the 1998 peak was reached.

Table 5 shows the levels of output in each quarter, comparing to the peak in the second quarter of 1998 (taken as 100). Considering a seasonally adjusted series, one can assess the three-year decline from 100 to 93.8, the fall to 79.9, and the recovery to 105.2.

Figure 37 shows the capacity utilization rate in industry. It also provides a very clear image of the gradual slide of the economy from the first XXX quarter of 1998 to the third quarter of 2001, prior to the final collapse into the crisis. (The Four limited short-lived are the expression of seasonal fluctuation.) A capacity utilization rate of 56% is reached during this quarter. The figure also suggests a recovery, but only partial.

Figure 38 shows both GDP, as in figure 36, and investment in equipment (productive investment, a component of investment by enterprises). The two series have been normalized to 100 in the second quarter of 1998 for legibility. The movement of investment is

Figure 36 GDP (volume, quartely data, 1998.2=100)

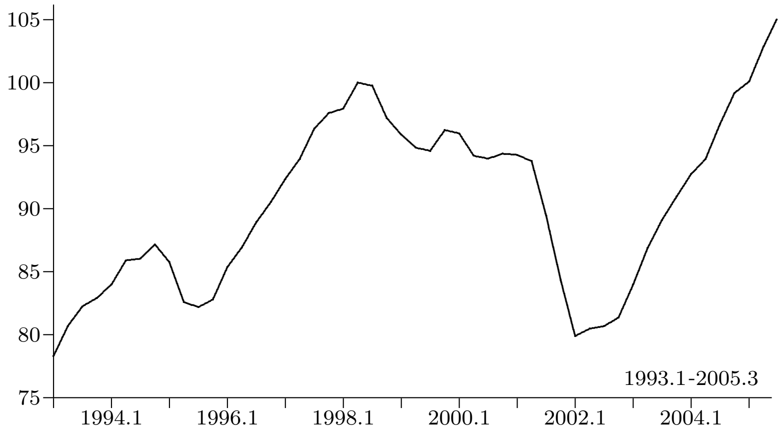


Table 5 - GDP and investment in equipment (1998.2=100)

	1998.2	*2001.2*	*2002.1*	*2005.2*
GDP	100.0	94.6	72.0	103.1
Seasonally adjusted GDP	100.0	93.8	79.9	105.2
Equipment	100.0			

Figure 37 Capacity utiliation rate (%): Argentinian industryXXX

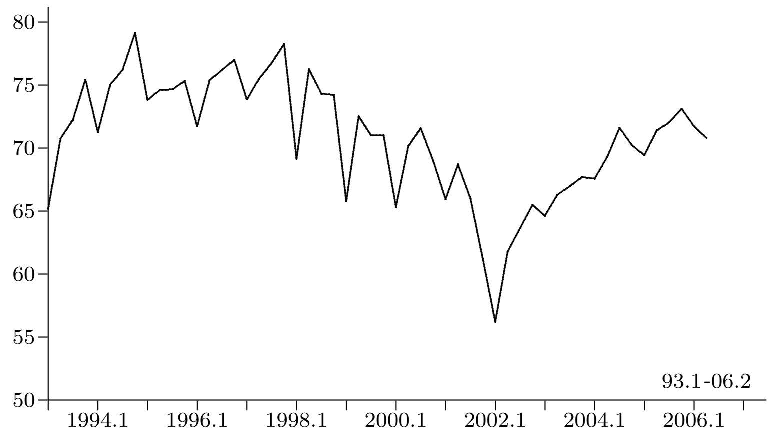


Figure 38 GDP and investment in equipment (Volume, quarterly data, 1998.2=100): Argentina

GDP: (——)
Investment in equipment: (-----)

The series for investment in equipment as already been shown in figure 7. The two series have been normalized to 100 in the second quarter of 1998 for legibility. .

similar to that of output, although the amplitude of its variation is considerably larger. Both output and investment grew in tandem from the low point of 1995 to 1998, more rapidly for investment; both series collapsed during the crisis although the fall of investment was dramatic and, finally, both recovered from 2002 onward. Table 5 shows the levels of investment in capital goods. Note the lowest point in the second quarter of 2002 , at XXX%.

Comparing figures 36 and 35, one can notice the coincidence between sharp contractions of output and the sudden increases of interest rates. The three episodes already identified are clearly apparent in figure 35: (1) the recession during the Tequila crisis in Mexico in 1995; (2) the Russian crisis in the late 1998, which coincided with the beginning of the recession XXX, but there was not restoration of output following the return to "normal" levels of interest rates; and (3) and the final surge of the spread beginning at the transition between 2000 and 2001.

The observations in this section are in line with those made in section 3.3 for the subset of the 500 largest enterprises. The overall contraction of output was, however, less severe for these large enterprises than for the total economy. Their output was maintained up to 2000, but in 1999 and 2000, their profits and profit rates had been considerably reduced, in particular for enterprises whose ownership was still national (figures 14). The rather comprehensive information available for this subset allows for the identification of directions of causation: Growing indebtedness encroached on the profitability of firms, which slowed their borrowings and investment.

7.1 *The contraction of output occurred in two steps, slowly during exactly 3 years, between 1998 and 2001, and then rapidly. The same profile was observed for investment, though more dramatically. These observations are in line for those made concerning the profitability of the 500 largest nonfinancial enterprises in section 3.3.2.*

7.2 The impact of the cost of the public debt on the private sector

Growing indebtedness was a crucial factor of the Argentinian crisis. Both enterprises and the public sector were affected. Sections 3 and 4 already accounted for these trends within public finance and the private sector, as independent mechanisms. Actually, they have much in common, such as the heavy reliance on external financing or financing in foreign currency. This section further contends that there was a significant impact of the public debt on the situation of the private sector.

The large and growing cost of the public debt, as discussed in section 4.2 (in combination with the growing transfers to the private sector and the deficit of social security, figure 19), resulted in a gradual deterioration of public accounts (figure 18):

1. Between 1995 and 1997, indirect business taxes were increased, at least for the 500 major enterprises considered earlier (*indirect taxes minus subsidies* rose), as an attempt to stem this deterioration.

2. An end was put to the downward trend of the primary surplus in public accounts, but this was not sufficient to stop the tendency toward increasing deficits. In spite of the limited relaxation due to the ephemeral income flow from the privatization of public enterprises in 1999, deficit of 2 or 3% of GDP were asserted. This process contributed to the rise of the public debt (figure 19).

3. The attempt to shift part of the cost of the public debt to enterprises by heavier taxation encroached gradually more on the profits of enterprises (what we observe in the accounts of the 500 largest enterprises in figure 15). The burden of taxation added to the profitability squeeze.

7.2 *The growing indebtedness of both the private and public sectors contributed to the final collapse of the economy. The burden of the cost of the public debt was partly transferred to the private sector (enterprises and, finally, households, via indirect taxes), adding to the profitability squeeze and encroaching on the purchasing power of households.*

7.3 The final blow: interest rates and the contraction of credit

7.3.1 International financial "markets"

The attitude of the so-called "markets", alias foreign and international finance, changed in a stepwise fashion:

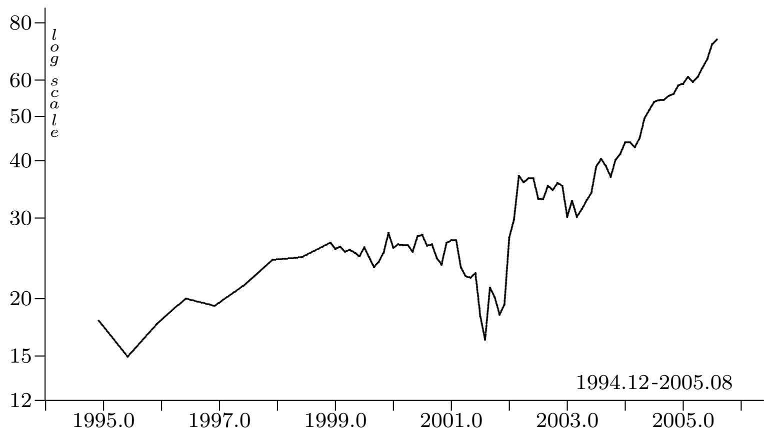
1. We return here to figure 35. As already noted, judging the assessment of the situation by the spread on interest rates, the first signs of concern were manifested in late 1998, when Russia defaulted and in the wake of the Asian crisis. The spread on interest paid by enterprises, which was actually negative, suddenly rose to more than 5%.

2. No jump in the spread occurred when the first IMF bail-out took place at the end of 2000.

3. It is in 2001 that the situation deteriorated, in spite of the second IMF bail-out mid-january 2001:

- As shown in figure 39, reserves remained stable until february 2001, above 26% of GDP. Then, they stabilized at a lower level of 22%, from april onward. This level was maintained up to june 2001, when the "mega-swap" occurred.[21]
- Between june and august 2001, reserves further fell.
- The spread jumped to 27% at the end of 2001.

Figure 39 International reserves of the Central Bank (billion dollars, quarterly and later monthly data)



International credit flows collapsed during this process, as evident in figure 9, where negative values are observed beginning in 2001, signaling the contraction of loans. This is when Argentina entered into depression and defaulted on its public debt.

7.3.2 Domestic credit

Figure 40 shows total loans by domestic financial institutions. The series (——) for total loans is identical to that in figure 27, but now expressed in billion pesos in figure 40 instead of a percentage of GDP in figure 27. Domestic credits were more resilient that international loans:

1. During the first phase, that of recession, there was no credit crunch of domestic financial institutions, in sharp contrast with nondirect foreign investment which fell to zero in 1999 and became negative in 2001 (figure 33).

2. During the second phase, beginning in 2001, there was a dramatic, rather steady, slide in total domestic loans.

3. It is the private nonfinancial sector (households and enterprises) that was hurt (·········), not the public sector, as already apparent in figure 25. From 1998 onward, during the recession, domestic loans to the private sector stopped rising; they began to decline slowly, and the fall accelerated in early 2001. A maximum of 61.1 billion pesos was reached at the

21. The mega-swap is XXX.

end of 1998, down to a minimum of 30.3 in 2003. In two or three years, the total stock of loans had been divided by more than two. Thus, demand levels emanating from the private sector were no longer preserved.

It is also important to keep in mind that the banking system was highly dollarized and, therefore, dependent on foreign banks. Figure 41 illustrates the continuous process of dollarization. At the end of 2001, 79% of total domestic loans by financial institutions were in dollars. This was one expression of the overall dependency on international finance perversely embedded, at this point, in the fabric of the domestic economy.

7.3 *Foreigners reacted strongly to the chaotic course of events. Credits from foreigners turned null in 1999 and negative in 2001, while domestic loans, whose major part was in dollars, were declining consistently. Interest-rate spreads rose in two steps: in the wake of the Russian default and then lately, when the symptoms of the incoming crisis were already obvious.*

7.4 Macro policies

The question must be posed of the macro policies during the process which led to the final collapse, both budget and monetary policy:

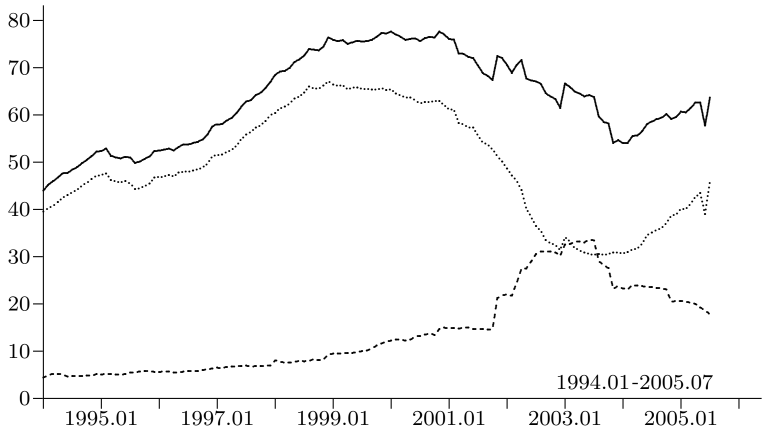
1. During the recession, domestic loans were maintained, while aggregate demand was stimulated by social expenses. Welfare expenses in education and health went on rising, or increased in comparison to other expenses up to 2001, and this stimulative impulse probably contributed to the postponent of the final contraction. (As we contended earlier, public expenses, in as much as they are due to the payment of interest to foreigners are not stimulative; the payment to rich national households may lead to further lending to the government or investment abroad, rather than additional expenses.)

2. In terms of monetary policy, there was, however, little leeway for an urgently required major feedback from monetary authorities due to the existence of the currency board:

- Actually, as recalled above, total domestic lending to the private sector culminated at the end of 1998, stagnated, and went on declining steadily.
- The same figure shows, however, that loans to the public sector were, to a considerable extent, compensating for this decline, but this stimulation did not stop the collapse of private investment. The cost of credit and the levels of indebtedness were too high, and not compatible with the profitability of enterprises in spite of the stagnation of the labor cost. (We recall that, prior to the final blow, this cost of credit was a general characteristic of neoliberalism, not specific to Argentina, since the spread, if any, was usually quite small.)

7.4 *The slide of the macroeconomy during three years (1998-2000) resulted from the negative impact of the burden of indebteness and large interest rates under neoliberalism placed on the investment of the private sector. The fall was probably delayed by the simultaneous stimulation of demand by budget and domestic monetary policy, though with deficient efficiency. In the context of a financial framework, that of the currency board, highly dependent on foreign financial mechanisms, the macroeconomy finally collapsed in 2001.*

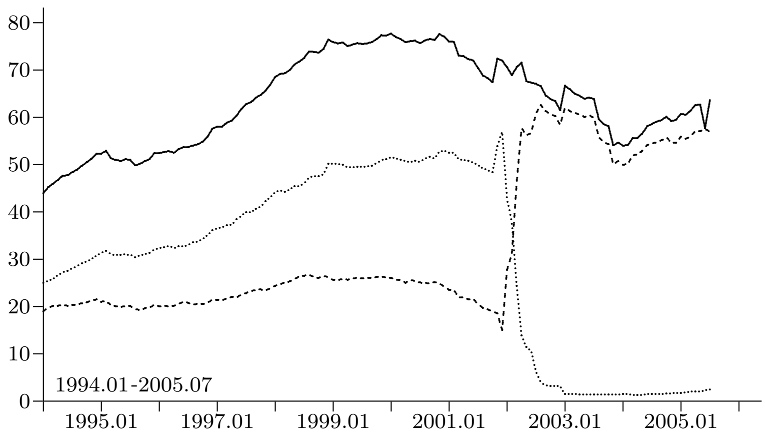
Figure 40 Total lending outstanding by domestic financial institutions (billion pesos): Argentina, Total loans, public and private nonfinancial sectors



Total loans: (——)
Loans to the public sector: (-----)
Loans to the nonfinancial private sector: (·········)

The series (——) for total loans is identical to to that in figure 27, but it is now expressed in billion pesos (instead of a percentage of GDP in figure 27). Only loans are considered; total claims are presented in figure 25 (using annual data).

Figure 41 Total lending outstanding by domestic financial institutions (billion pesos): Argentina, Total loans, in pesos and foreign currency



Total loans: (——)
Loans in pesos: (-----)
Loans in foreign currency: (·········)

The pesoisation, simultaneous to the devaluation, was sudden and performed at a rate of 1 to 1, so that no break is apparent in the total.

Table 6	
President	*in office*
Raúl Alfonsin	December 1983
Carlos Menem	May 1989
Fernando de la Rúa	December 1999
Ramón Puerta	December 2001
Rodriguez Saa	December 2001
Eduardo Duhalde	January 2002
Néstor Kirchner	May 2003

7.5 The management of the crisis

This section recalls the major aspects of the management of the crisis[22]. (Table 6 lists the successive presidents.) Three periods are distinguished.

7.5.1 Attempts at checking the public debt crisis: 1998-2001

1. *Cutting public expenses.* When the sovereign spread began to rise in 1998, in the context of the deterioration of the situation in Argentina and the occurrence of crises in other countries, not too surprisingly, the first move was fully orthodox: Public expenses had to be cut, it was contended, to initiate a virtuous circle (diminished deficit → diminished interest rates → larger growth rates).[23] These "trendy trends" culminated mid-2001, when a "zero-deficit" policy was established. Public wages and pensions were cut by 13%.

2. *Keeping the public debt rolling.* At the end of 2000, a substantial package of financial support was announced, with the contributions of the IMF, local banks, and pension funds (*blindaje*, that is "armor"); followed by the debt swap of mid-2001 (*megacanje*, mega-swap), increasing the debt and interest rates (in August extension of stand-by credits by the IMF); and, in november, a new swap, involving domestic banks and pension funds. This is when local agents' bond holdings were exchanged for *guaranteed loans* to the government.

7.5.2 Confronting the disaster: December 2001-February 2002

The depression occurred mid-2001. A massive flow of capitals out of the country was occurred, and reserves fell sharply from the beginning of the year (figure 39):

1. *Bank deposits and capital movements.* In December 2001, the government enacted sharp restrictions on bank deposits and capital movements to calm the situation. The limitation of bank withdrawals is known as the "baby pen" (*Corralito*).

2. *Defaulting on the debt.* In the context of growing social tensions, President de la Rúa resigned. President Saa, his ephemeral successor (one week), announced the default on the public debt (while keeping the currency board unaltered) in the last days of 2001 and resigned.

3. *The abandonment of the currency board.* To the end of 2001, the rate of exchange was still one-to-one. At the very beginning of 2002, President Duhalde, which succeeded Saa

22. A helpful study is M. Damill, R. Frenkel, M. Rapeti, The Argentinean Debt: History, Default and Restructuring, CEDES, Buenos Aires (2005).
23. The de la Rúa administration borrowed the argument from the Menem administration, with the support of the IMF.

on January 1st, decided the abandonment of the currency board, including the one-to-one exchange rate, initiating the depreciation of the peso. During the first quarter of 2002, the exchange rate was divided by a factor of 3.

The maximum devaluation was reached in june 2002 at a level of 3.8 pesos per dollar, before stabilizing slightly below 3 from march 2003. A more flexible monetary policy was introduced, which assisted the banks and, therefore, encouraged domestic credit, with more tolerance toward inflation. This is evident in figure 23. After a period (1998-2001) of relative deflation in comparison to the United States, the price level rose by 26% in the first quarter of 2002 (coinciding with the devaluation), prices rose at an average annual rate of 10% between 2003 and 2005. After the devaluation, the Central bank and the treasury intervened, buying dollars (selling pesos), to avoid the appreciation of the peso.

4. *Taxes on exports.* A tax on exports was established in the wake of the devaluation. Figure 23 shows that the prices of exports and imports are determined on international markets. When the devaluation occurred, they were maintained in dollars. Huge profits in pesos resulted for exporters (converting the dollars in which exports were paid, at a rate of exchange which meant three times more pesos, to be compared to costs of production mostly paid in pesos).

The IMF opposed to many of these measures: (1) exchange controls; (2) taxes on exports; (3) the new course of monetary policy; (4) the intervention of the Central bank and Treasury to control the rate of exchange. From the end of the convertibility regime, the IMF stopped supporting Argentina, defending the position of the fund as lender, and Argentina began to repay the IMF.

5. *Pesoization of bank accounts.* In February 2002, as a complement to the set of measures of the transition 2001-2002, the government of Duhalde initiated the process of pesoization. Banks were compelled to convert their assets and liabilities in dollars into pesos, at given rates (figure 41). (Simultaneously the rules controling withdrawals on demand and saving deposits were relaxed, and the term on time deposits was increased.)

6. *Pesoization of the public debt and the return of part of the debt of financial institutions to foreign currency.* Also in February 2002, the government converted into pesos part of its debt in foreign currency, a total of 57.5 billion dollars, mostly the guaranteed loans. Fixed interest rates were applied, between 2% and 5.5%, but the securities were indexed on prices. Pension funds and insurance were, however, allowed to reconvert part of their loans into foreign currency, and the pesoization only affected 22.1 billion dollars.

These measures were costly for the state, which was compelled to compensate for the damages caused to banks by the asymmetric pesoization (pesoization at different rates of exchange for assets and liabilities). To this end, the state issued public securities which were given to the banks, augmenting the public debt. In addition, the government compensated the loss on banks' assets due to the devaluation, as well as the losses of depositors and pension funds, at least part of it, again increasing the public debt. Inflation implied the revaluation of the pesoized public debt (pegged on prices). Part of the debt of provincial governments was transferred to the federal government. In two years, 2002 and 2003, the public debt, federal and provincial, had risen by 28.2 billion dollars.

7.5.3 The partial cancellation of the public debt: from the second quarter of 2002 onward

1. *Partial cancellation.* Originally with the agreement of the IMF, later under pressure, the process of restructuring of the defaulted debt (arrears) was initiated during the second half of 2003. The plan is known as the *Dubai proposal*, followed by the *Buenos Aires proposal.*[24] The stock of arrears was estimated at 87 billion dollars (debt issued prior to december 2001). A 75% haircut was imposed. Various categories of securities were defined. After a long and contradictory process, the new swap was launched in June 2004, it took place in January 2005, and was concluded within three weeks. 76% of creditors accepted. It meant a reduction in the public debt of 67 billion dollars, of which 44% were in pesos.

Table 7 - Public debt (end of the year)

	1992.4	*2001*	*2004*	*2005.2*
Debt (billion dollars)	71	144	191	126
Debt (\$) / GDP (\$) (%)	30	54	126	73
Debt (\$) / GDP (\$ PPP) (%)	21	33	39	23

Table 7 shows various measures of the public debt: (1) in billion dollars; (2) as a percentage of GDP at going prices; and (3) as a percentage of GDP(PPP). Four dates are considered: (1) the fourth quarter of 1992, the first quarter in the series in figure 16; (2) 2001, prior to the crisis; (3) 2004, after the devaluation but prior to the partial cancellation; and (4) the second quarter of 2005, after the cancellation. The followings are noteworthy:

- In billion dollars, the debt rose from 71 billion dollars in 1993 to 191 at the end of 2004, to reach 126, after the cancellation.
- As a share of GDP at going prices, the devaluation dramatically increased the percentage the debt represents in total output. From 2001 to 2004, before and after the devaluation, the percentage grew from 54% to 126%, while the debt was rising from 144 to 191 billion dollars.
- The most meaningfull measure of the weight of the debt is given in the third line of the table, using GDP(PPP). Between the same dates as above, 2001 and 2004, the public debt grew only from 33% to 39% when GDP(PPP) is considered. One can observe that, in 2005, the public debt in this measure was slightly above its relative level of 1993, at 23%. Back twelve years earlier!

7.5 *Overall, it is possible to define three subsequent phases, the first and the third comparatively lasting, and the second brief:*

- *A first phase, 1998-2001, can be defined, in which attempts were made at checking the impending public debt crisis. They failed (figure 16).*
- *Then, in a very short span of time, less than 3 months, between December 2001 and February 2002, four sets of drastic measures were taken: (1) limitation of withdrawals from bank accounts and implementation of capital controls; (2) default; (3) abandonment of the currency board (including the devaluation which followed the end of the 1 peso/1 dollar), and (4) pesoization (financial institutions and public debt).*

24. The decision in Argentina was highly consensual (G. Gigliani, "Argentina despues del canje: Se redujo la deuda pero crescieron los pagos", *Cuadernos del Sur*, X (2005)XX, p. XXX).

- *From the second quarter of 2002 to the second quarter of 2005, a process was conducted which led to the cancellation of part of the public debt. As a percentage of GDP(PPP), the debt recovered the levels reached 12 years earlier.*

7.6 Recovery

As shown in figure 38, the economy stabilized during 2002, and the upward trend was confirmed in the second quarter of 2003. The following features of the crisis and recovery are noteworthy:

1. *Public expenses.* The share of public expenses (excluding interest payment) in GDP increased during the first phase, that of recession (from 15.8% in 1993 to 17.9% in 1999), playing their typical role as stabilizers. This share later declined during the second phase, that of crisis, to 16%XXX. It finally rose from 2003 onward and possibly contributed to the recovery, though not as a crucial factor.

2. *Real wages.* The crisis created conditions for a new encroachment on salaried workers purchasing power (figure 2).

3. *The devaluation.* The devaluation was a primary factor in the recovery. It impacted on foreign trade, both imports and exports. Due to the devaluation, the price of exports rose dramatically. As shown in figure 23, the price of exports in pesos began to increase in the second quarter of 2002, just after the devaluation.

Imports fell, during the crisis, from 19 billion dollars in 2001 to 9 billion dollars in 2002. (They had reached 30 billion dollars in 1998.) The volume of exports stagnated during the crisis, but their total price went on rising. The increase in the price of exports was one factor in the restoration of profit rates and in the new upward trend of investment. With the devaluation in the second quarter of 2002, the composition of output (at going prices) was dramatically altered as the share of the production of goods (as opposed to services) gained more than 10 percentage points of GDP, from 33% to 47%. These gains were made in Agriculture and Mining but, above all, in Manufacturing (a progress of 7 percentage points of GDP).

As shown in figure 6, a wide shift occurred in the financing of investment as soon as it began to recover, that is from the second quarter of 2002: Investment was financed by domestic financing, while enterprises were paying their external debts . (External financing turned negative from the third quarter of 2001, and was still slightly negative in 2004XXX.)

Could the crisis had been worse? Yes, if public expenses had be been cut even more severely and if the trend of exports had not been maintained. The devaluation initiated a new favorable course of events, protecting national industries. Thanks to large profits and the curtailment of foreign credits, the Argentinian economy escaped, for the first time in many years, from the infernal pattern of financing which prevailed in the 1990s.

7.5 *The new course of the recovering economy is very different from that prevailing during the 1990s. Exports played a crucial role, and domestic financing was restored, probably in relation to the new profitability trends, which, besides the price of exports, benefited from the new encroachment on real wages.*

8 - Sharing the pie

In the analysis of the relationships between countries of the Center and national ruling classes of the Periphery, it is also important not to adopt a unilateral viewpoint. Indeed, the overall configuration is that of imperialism on a world scale. But imperialist relationships always rely on local ruling classes, possibly more on one fraction than another or, in some cases, on a clique. But the collaboration of local interests is always at issue. This is what we can observe in Argentina. In the analysis of the overall "sharing of the pie", we distinguish between income and capital ownership.

8.1 Income flows

It is a characteristic feature of the relationship between countries of the Center and Latin America, that: (1) capital incomes flow from this region of the world to the Center, since this is what imperialism is about; but, also that (2) capitalist classes of Latin America receive capital income flows from the Center. Again, we abstract from the strong link between Europe and Latin America, and limit the investigation to the United States.

Figure 42 shows the income receipts and payments between the aggregate of all countries of Latin America and the United States, in both directions, and the overall balance, expressed as percentages of U.S. GDP:

1. The figure documents the dramatic increase of inflows toward the United States, which rose from 0.2% of total income in this country to a plateau of about 0.7%, after a peak at 0.9%. (The percentage might be judged small, but it is important to know that the average total after-tax domestic profits of U.S. corporations, that is profits supposed to be made on U.S. territory, amounted to an average of 4.5% of GDP between 1980 and 1985.) The rise occurred between 1972 and 1982. This increase marks the massive entrance of U.S. capital into Latin America (notably the too famous loans of the late 1970s) and, after 1979, the increase of returns typical of neoliberalism.

2. But one can also notice the sharp rise of the outflows of capital income from the United States to Latin America, some six years later, between 1978 and 1988, reaching a plateau of about 0.5%.

3. The outcome of the combined two profiles is evident in the third series, the net inflows of capital income from Latin America to the United States. The sharp increased during the 1970s was suddenly reduced to little more than 0.1% of GDP during the 1990s. This observation must be related to the huge deficits, budget and external deficits, in the United States.[25]

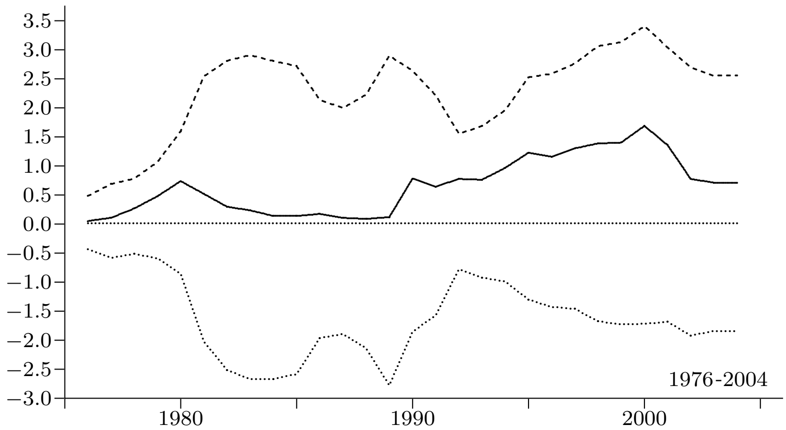
A more detailed analysis of the composition of foreign investments shows that the new configuration combines: (1) increased imperialist pressure; and (2) increased insertion of local capitalist classes in a "rentier" position (figures 29 and 32). By *rentier*, we mean the ovewhelming preeminence of nondirect investment in the investment abroad originating in Latin America, as opposed to the comparative importance of direct investment in the

25. G. Duménil, D. Lévy, "The Economics of U.S. Imperialism", *op. cit.* note 2.

Figure 42 Income receipt and payments as shares of U.S. GDP (%): From Latin America to the United States and reciprocally

Receipt of the United States from Latin America: (——)
Payments of the United States to Latin America: (-----)
Net receipt of the United States from Latin America: (·········)

Figure 43 Income receipt and payments as shares of the Argentinian GDP(PPP) (%): From Latin America to the rest of the world and reciprocally



Income receipt from the rest of the world: (——)
Income payments to the rest of the world: (-----)
Net income receipt from the rest of the world: (·········)

The line (——) for income receipts from the rest of the world is the same as in figure 12.

investment coming to Latin America from the rest of the world. Between the United States and Latin America, the flows income are close to compensating one another (section 6.2.1)!

As is well known, since the beginning of the 1990s, the investment abroad of rich Argentinian classes is huge by Latin American standards (as revealed by the comparative income flows in figure 12). Due to the exceptionnally large foreign indebtedness of the country, outflows of capital income to the United States are also large. This is shown in figure 43 for the relationship of Argentina to the entire world economy. One can observe the shares of inflows and outflows as percentages of Argentinian GDP(PPP). Outflows peaked in 2000 at 3.3% of GDP, while inflows culminated at 1.7% in the same year.

8.1 *If imperialism is about drawing capital income from the rest of the world, it is clear that imperialism in the era of neoliberalism is very efficient. But the ruling classes of the countries of the Periphery are also implied, in particular as a result of the external deficits of the United States. Argentina provides an emblematic example of this new configuration.*

8.2 The ownership of capital

There is, however, another side to the coin. Foreign capital is massively entering into Argentina. Or, to put the matter a bit more crudely, the Argentinian ruling classes are selling their productive system to foreigners (as a compensation, they buy U.S. securities as documented in section 3.2, figure 11).

It is possible to assess the amplitude of this mechanism for the pool of the 500 largest enterprises (nonfinancial and excluding the agribusiness). Figure 44 shows the share of total value added of the 500, for the two categories of ownership already used in figure 14. One can see that, in 1993, enterprises with foreign ownership superior to 50% realized 34% of total value added; in 2002, the percentage reaches 80%.[26] It is not, therefore, that there are no more large national enterprises, but that they are steadily loosing ground in front of foreign ownership. Figure 45 shows the share of both categories in total profits. One can observe the gradual shift of profits toward foreign enterprises. In the early 2000, they garnered 80% of total profits.

One can surmise that transnational corporations do not buy small enterprises. Those are eliminated differently, as everywhere, when they go bankrupt under the competition of large enterprises. This is true of retail trade ruined by shopping mals, crafts ruined by imports, restaurants ruined by well-known chains, etc.

8.2 *Considering the 500 largest enterprises resident in Argentina, foreign-owned enterprises now make 80% of both value added and profits, signaling a dramatic transfer of ownership to foreigners.*

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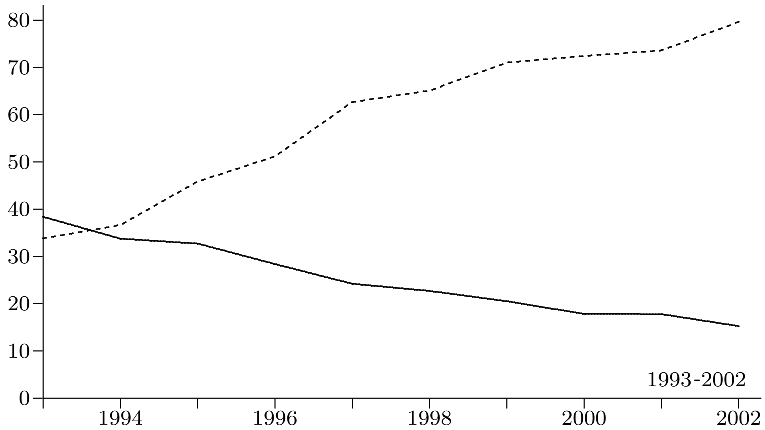
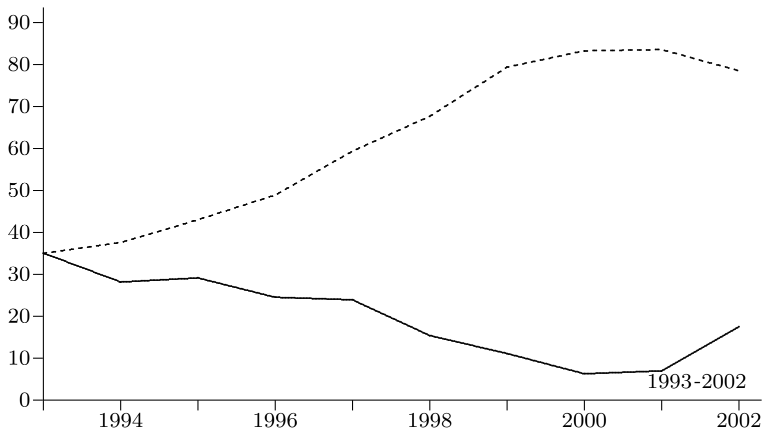
26. The foreign ownership of the banking system rose dramatically during the second half of the 1990s. In december 1994, the assets of banks whose foreign ownership was above 50% held 17.9% of total bank assets. In december 1999, this percentage reached 48.6% (D. Mathieson, M. Shinasi, Developments, Prospects, and Key Policy Issues, IMF, World Economic and Financial Surveys, Washington (2000)).

Figure 44 Share in total value added, by nationality of ownership (%): Argentina, 500 largest enterprises



National enterprises (< 10 %): (——)
Foreign-owned enterprises (> 50 %): (-----)

Figure 45 Share in total profits, by nationality of ownership (%): Argentina, 500 largest enterprises



National enterprises (< 10 %): (——)
Foreign-owned enterprises (> 50 %): (-----)

9 - The neoliberal-imperial mix in Argentina: Social roots and perspectives

A first obvious difficulty in the interpretation of the Argentinian crisis is to articulate the various mechanisms at work, indeed a broad set of economic, social, and political determinants. But it is also clear that the crisis can only be understood when considered within the overall historical framework in which it took place: neoliberalism, imperialism, and the relationship between ruling classes of the Center and of the country itself.

A first very broad line of interpretation, in the left academy, refers the crisis to neoliberalism. This relation is strong, as is evident when the crisis is viewed as an episode in the sequence of similar crises of the 1990s and early 2000s in Latin America, Russia, Turkey, and Asia. In spite of obvious idiosyncracies, they all occurred in the context of the neoliberal opening of commercial and financial frontiers; all of them were marked by the sudden exiting flows of foreign capitals. These outflows destabilized not only a comparatively lowly performing economy like that of Argentina, but countries growing rapidly and inserted in the world economy with high technological records, such as Korea.

Such analyses, however, when reduced to the "technicalities" of the free mobility of capital (for example, when the emphasis is placed on the implementation of a Tobin tax), miss the central political point. Contemporary Capitalism cannot understood abstracting from imperialist patterns and underlying class relations. Much of the complexity of the crisis derives from the quite specific role played by local ruling classes. These classes cannot be presented as mere passive victims in a world of domination. A new configuration of imperialism is at issue. What role should we confer on this new setting in the explanation of the crisis?

The first section recapitulates the major aspects of the overall interpretation of the economics and politics of the crisis in this study, with special emphasis on the role of capitalist classes of countries of the Center and Argentina (section 9.1). Section 9.2 discusses perspectives.

9.1 Capitalist classes of the Center and Argentina in the neoliberal-imperial mix

In the analysis of class interests and strategies, it is obviously always difficult to separate between deliberate moves and adjustement to new contexts. One should not underestimate, however, the capability of such social entities to appreciate their interests and act correspondingly through existing governments and institutions (financial institutions, Universities, etc.). Often, clear strategies are expressed in political and academic writings. (For example, the basic tenets of neoliberalism, still a project, were stated unambiguously during the first half of the 20th century[27].)

A preliminary observation is that, at least since World War II, the Argentinian capitalist class has never been very performing in terms of savings and accumulation, judging

27. The most famous example is that of von Hayek (F.A. Hayek, *The Road to Serfdom*, Chicago (1980): The University of Chicago Press (1944))

by the comparatively low growth rates achieved in this country. The situation even deteriorated after 1980. The wave of accumulation between 1991 and 1997 did not signal a true revival and was not financed by local capitalists.

We begin with imperialism. The major traits of the new international configuration can be summarized as follows:

1. Purchase of the productive and financial economy by imperialist capitalist classes of the Center.

2. Transformation of the local capitalist class in a class of rentiers, directly contributing to its own demise as active national capitalists.

3. Correlatively, the U.S. capitalist class borrows cheap to finance the public expenses of the country and garners large returns on its investment[28].

Europe or Japan are also involved in this pattern, but the United States are the primary beneficiaries of the exports of capital from Latin America.

Macro policies define a first issue. It was certainly necessary to curb hyperinflation, and the high and rigid rate of exchange was an important component of the device. But beyond this urgent necessity, the question must be raised: To whom high exchange rates and convertibility benefited?

1. High exchange rates allowed Argentinian "industrial capitalists" to adapt their equipment to the new more efficient technology, by importing capital goods at a rather favorable price. Conversely, the export of manufactured goods became more difficult and imports of consumption goods posed a threat on local producers. The rigidity and high value of the exchange rate damaged the Argentinian economy, placing a strong pressure on domestic production, which, in combination with the increasing burden of interest resulting from the growing indebtedness, led to the decline of the profit rate. So, not only the liberalization of trade and capital flows were at issue in the circumstances which led to the collapse, but also the specific internal conditions in which they occurred.

2. The massive exports of capital directly followed the establishment of the high rate of exchange and free convertibility. Convertibility at a high exchange rate allowed for the purchase of foreign securities by Argentines under favorable conditions. To put the matter differently: as a high dollar is a crucial element in the strategy of U.S. finance buying the world, the options taken by Argentinian ruling classes guaranteed them an advantageous insertion in the new imperialist configuration, though in a subaltern position. They learned the lesson. The slogan was *in, but well enough*!

Can a single policy be interpreted in terms of contradictions between industrial interests and rentier interests? The contradiction could be more apparent than real. First, the new overwhelming "rentier" stand does not excludes other subsidiairy forms of integration in the new international division of capital (paralleling that of labor). National capitalists can find ways of integrating themselves in this new international division of capitalist ownership within specific industries, for example in international trade; they may also conserve important portfolios of shares in corporations which are controlled by foreigners. We can surmise that the policies of the 1990s became consensual in Argentina, since they globally favored such apparently diverging interests. In any instance, it is important to keep in mind that the interests of the same rich individuals and families typically combine various

28. G. Duménil, D. Lévy, "The Economics of U.S. Imperialism", *op. cit.* note 2.

stands (for example, one fraction of the fortune is invested in a local industry while another is invested in the United States).[29]

The new pattern of the Argentinian economy suggests a combination of these various elements. The main point is the prevalence of a new configuration where local capitalist classes are placed in a subordinate position.[30] If the new strategy of Argentinian ruling classes was deliberate, one can judge that it has been rather successful; and the new position is safer and more confortable.

The issue of neoliberalism must also be approached in its various facets. As already stated, the major aspects of the new social order were there in Argentina, but the reforms of the 1990s also manifested more ambiguous features. In particular, the question of the establishment of the currency board must be posed:

1. A first aspect of the board is quite in line with the neoliberal agenda: the Central bank is not supposed to finance excess spendings. Think "cutting social expenses". Good for national and international capitalists! Convertibility is also perfectly welcome. But the capability to control the macroeconomy is lost.

2. A contradiction is that at least the ideology of neoliberalism celebrates "free markets". Why, thus, a fixed exchange rate? A first obvious answer is that the one-to-one full convertibility had a reassuring effect on foreign creditors. But, as is well known, the United States are not in favor of the pegging of currencies to the dollar. One reason is that such mechanisms diminish their capability to use exchange rates as a tool in the control of the macroeconomy.[31] Analyses by economists of the IMF question the existence of fixed exchange rates and favor floating rates (for the same reason). In a more subtle manner, such studies contend that fixed rates transfer the burden of adjustment to local "markets", primarily the labor market; the lost competitivity of a country can only be recovered by comparative deflation; if this does not occur, wages are obviously responsible.[32] Flexibility! A rapid examination of the profile of real wages after 1998 unambiguously reveals the hypocritical and cynical character of such assertions. Pure ruling class ideology!

3. The result of the establishment of the board was unambiguous. The control of the macroeconomy was transferred to international finance — in which Argentinian ruling classes were inserting themselves in a subordinate position. The alleged automatic stabilizing effect of the ratios of the currency boad proved completely inefficient — as international finance cares little for the macroeconomy and much for its own safety (what it ensured with success), in the purest 19$^{\text{th}}$ century vein. Rather consistently, Argentinian ruling classes cared as little for the stabilizing of their macroeconomy as for the financing of their own national accumulation.

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29. This is the central point emphasized in M. Zeitlin, R.E. Ratcliff, *Landlords and Capitalists, the Dominant Class of Chile*, Princeton: Princeton University Press (1988).

30. This is another expression of what we denoted in other studies as "two-tier capitalism", a crucial feature of the neoliberal-neoimperial mix. We touch here the international facet of such hierarchies, supplementing the class hierarchy within ruling classes, between capitalist classes and the upper fraction of wage-earners, in particular in the United States (G. Duménil, D. Lévy, "Neoliberal Income Trends. Wealth, Class and Ownership in the USA", *New Left Review*, 30 (2004), p. 105-133).

31. The hypocritical character of such assertions is obvious. While "markets" are invoked, the actual motivation is the capability to manipulate exchange markets, selling or buying dollars when necessary.

32. T. Geithner, Lessons from the Crisis in Argentina, IMF, Policy Development and Review Department (2003).

4. Neoliberalism is obviously at issue concerning the public debt. Three traditional features are evident: (1) the financing by "markets", that is rich households and financial institutions; (2) high interest rates; and (3) the transition to pension funds. To this, we can add a fourth one: (4) credits in dollars. This latter feature is also typical of the options taken by local ruling classes, placing themselves in the position of foreigners within their own country (in a period in which international "markets" were not even manifesting signs of concerns). No serious move was made to stop these trends, in particular to improve the pattern of relationships between the federal and provincial governments, and to raise the taxation on high incomes.

Thus, besides "standard" neoliberal options, the reforms of the 1990s testify of the choices of Argentinian capitalist classes, sometimes contradicting neoliberal rules. Concerning the relationship with capitalist classes of the Center, one can observe converging trends but also conflicting aspects along the route to the new imperialist configuration.

9.2 A new social compromise, a new insertion in the world economy?

The crisis and the popular struggle that it aroused resulted in a situation of exception. Measures were taken, in particular the depreciation of the currency, the abandonment of the ratios of the currency board, the pesoization, and the cancellation of a signficiant fraction of the public debt. Do these measures signal a new strategy of Argentinian ruling classes, a new insertion in imperialism, a new autonomy of managerial and official classes (as in the wake of the Great Depression and World War II), and a new compromise with popular classes? Can we identify the first features of an Argentinian "New Deal"? Analysts, critical of capitalism, often contend that the management of the crisis testifies more of a desire to place both the nonfinancial economy and financial institutions back on the track, than to deeply alter the nature of social relationships.[33]

Obviously, none of the capitalist features of the country have been unsettled, but new patterns are apparent concerning the insertion of Argentina in the world economy (imperialism) and neoliberalism:

1. In several fields, the country gained some autonomy with respect to international finance. A measure like pesoization implied a strong interference of public authorities into financial institutions, whose ownership was largely foreign. The decision not to pay a significant fraction of the public debt is another daring move. It is important, however, to keep in mind that U.S. investors held a very small fraction of the public debt as it was affected. In addition, loans from the IMF remained unscathed. But Argentina also demonstrated that the debt is not sacred. Unfortunately, no other countries of Latin America followed suit, in particular Brazil did not.

2. Concerning imperialism, the new stance is similar to that adopted by other countries, of which China is the emblematic example: to sell its goods and enterprises (and labor) as cheap as possible, by way of a low exchange rate and a cheap labor. This is manifest in figures 2 and 24, and the comparaison with Brazil shows that this latter country is moving along a similar line. The strategy of Argentinian ruling classes appears now less arrogant vis-à-vis other countries of Latin America, and the idea of a (south)continental solidarity is,

33. Or simply to serve the interests of ruling classes (C. Katz, Quien gana con el canje?, Universidad de Buenos Aires, Conicet (2005)).

somehow, on the agenda. Argentina apparently abandoned its ambition of standing within the new imperial configuration in a priviledged position, "closer" to the imperial center than other Latin American countries — as is still the case of Mexico in spite of its poor performances. (But what are the ambitions of Lula's Brazil?) This new stand is evident in Mercosur countries' attitude toward the Free Trade Area of the Americas (FTAA, known in the region as ALCA), the declarations of President Kirchner in Mar del Plata toward U.S. imperialism, and the entry of Chavez's Venezuela into Mercosur.

3. Significant distance was taken from many of the basic rules of neoliberalism. A degree of inflation was accepted; interest rates were diminished, in particular those charged to enterprises; taxes were increased, and the proportions between its various components were altered, with the comparative decline of indirect business taxes, and a rise of income taxes; taxes were levied on exports. Real wages and social taxes were, however, cut.

4. The sharp intervention of the state in the management of the crisis is obviously at odd with the neoliberal ideology concerning the ability of "market" mechanisms to ensure balanced growth. One can surmise a determination to recover part of the control of the macroeconomy. Once the currency board eliminated, there is some leeway for such an endeavor, although it is still early to identify new policy trends.

5. These movements must be interpreted as one aspect of broader, global, new trajectories. Considering countries of the Center, we contend in other studies[34] that a transition beyond neoliberalism, or at least a distinct phase, is now under way. The record interest rates and capital gains on the stock market of the 1990s probably belong to the past. New class configurations and alliances are gradually asserted, paralleling new modes of appropriation of surplus-value. In addition, the pressure to confront imperialism is, somehow, mounting in Latin America. In this context of global restructuring and struggles, and given the political shock of the crisis and the threat it posed, Argentinian ruling classes are constrained to stabilize their position in a very uncertain and changing environment, and no definite strategy can easily be indentifed.

A few things can, however, be asserted concerning perspectives: (1) It is impossible for Argentinian ruling classes to repeat a strategy such as that of the 1990s; and (2) The new framework must reestablish a degree of national control of macro stability. This is in line with what was already undertakened: away from dollarization and high exchange rates, out of the currency board, managing the public/external debt. How the situation will exactly be consolidated remains uncertain. A further element would be some degree of commercial and financial protection, although the strategy remains shy (defensive, as in the resistance to FTAA). If a crisis occurred in the United States, the problem would be posed in a similar manner, although the overwhelming advantage of being the dominant economy would broaden the options. The macroeconomics of neoliberalism are at issue, not its social components, in particular the new discipline imposed on labor and the management of enterprises. The treatment of the debt will require simultaneously a determination to confront foreign investors and popular classes in the country. In both instances, "cuts" are on the agenda (haircuts for lenders and social cuts for the people), and have already been realized. It would be unduly optimistic to expect a complete "break" from neoliberalism. *To reverse such trends, a powerful social movement would be necessary.*

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34. G. Duménil, D. Lévy, "The Economics of U.S. Imperialism", *op. cit.* note 2; Finance and Management in the Dynamics of Social Change. *Contrasting Two Trajectories: United States and France*, PSE, EconomiX, Paris (2005).

Concerning the insertion within imperialist relations, we expect a "banalization" of the stand of Argentinian ruling classes after their high performances of the 1990s, unless they prove really imaginative and combative. A configuration has now been established, with large portfolios abroad, and a financial and nonfinancial economy largely sold to foreign capital. *To reverse such trends, and reestablish the lineaments of a "nonrentier" insertion, a strong (south)continental common anti-imperialist front would be required.* From a Left point of view, a combination of the two reversals (popular pressure and antiimperialist front) would define the optimal blend.

10 - Additional figures

Figure 46 Foreign liabilities and assets of the nonfinancial sector: Argentina

Figure 47 Foreign liabilities and assets of the private financial sector: Argentina

Figure 48 The external debt as a share of GDP(PPP) (%), Argentina: Total and Private sector

Total: (——)
Public sector (with the central bank): (— —)
Private sector: (-----)

Figure 49 Exports and Imports as a share of GDP(PPP): Argentina

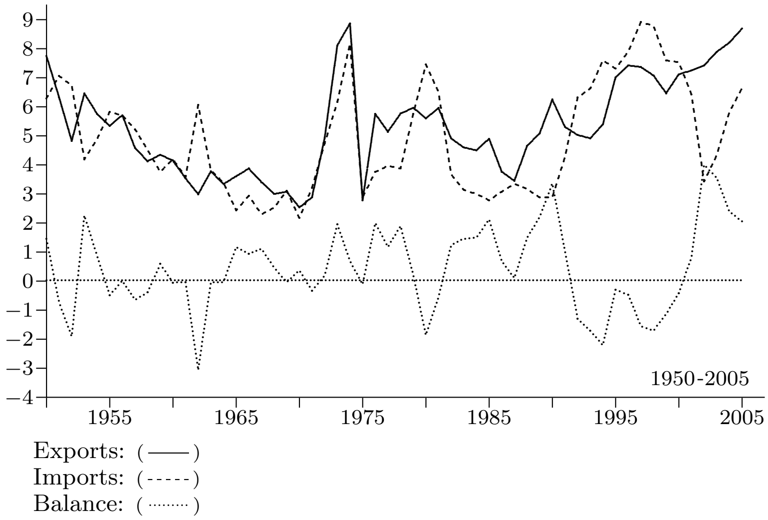


Figure 50 Exports and Imports as a share of GDP(PPP): 7 major Latin American countries

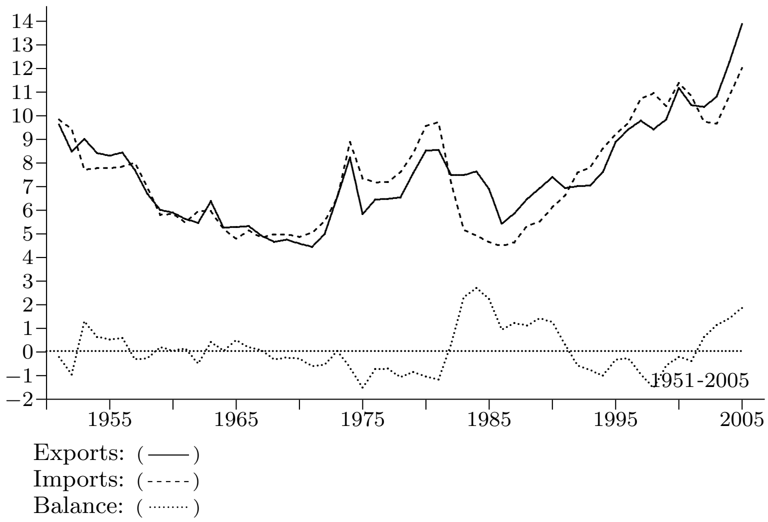
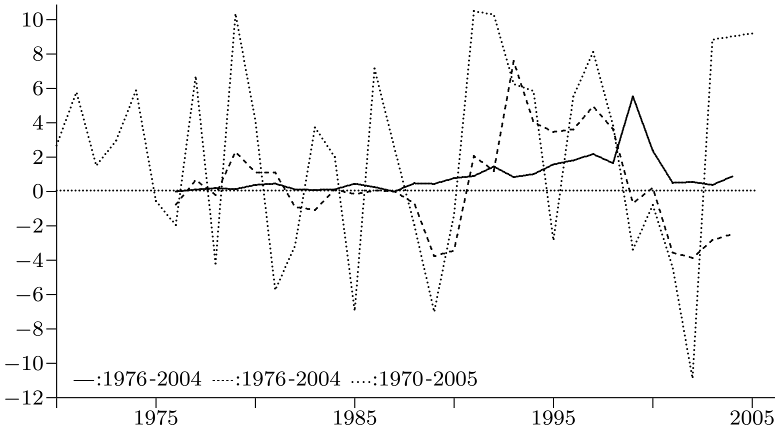


Figure 51 Foreign investment as a share of GDP(PPP) and growth rates (%): Argentina



Foreign direct investment: (——)
Foreign nondirect investment: (-----)
Growth rate: (·········)

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