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LATIN AMERICA AND THE INTERNATIONAL LENDING ORGANIZATIONS: THE TIES THAT BIND

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This thesis focuses on linkages between the international financial community and political systems in the region. A major theme of this interrelationship is that the nature of the growth models selected by most nations in Latin America has created the conditions for international lending organizations to act as important power contenders within the domestic political process. Without being a full participant in the process, these organizations are able to place demands upon the syst and have these demands satisified. → over

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They are able to require implementation of stabilization programs that often do not coincide with domestic goals and programs. The growth of regional external indebtedness has hardened the nature of unequal dependent linkages between lender and debtor, especially with respect to the most heavily indebted countries. Stabilization programs required by international lenders as a condition for continued access to foreign currency so urgently demanded by the indebted nations of the region are inherently disadvantageous to the majority of those nations' citizens and national entrepreneurs. Because of the problems associated with the application of these stabilization programs, this thesis concludes that there are significant linkages between external public indebtedness, requirements for domestic stabilization programs as problems in debt servicing arise, and the installation of authoritarian regimes to impose stabilization measures.

To Joe who taught me to ask the right questions; to Steve who helped me find the right answers; and to Nancy who made it all worthwhile.

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Council of the University of Florida in Partial
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LATIN AMERICA AND THE INTERNATIONAL LENDING ORGANIZATIONS:
THE TIES THAT BIND

By

Richard B. Brown

August 1980

Chairman: Dr. Steven E. Sanderson
Major Department: Latin American Studies

This thesis focuses on linkages between the international financial community and political systems in the region. A major theme of this interrelationship is that the nature of the growth models selected by most nations in Latin America has created the conditions for international lending organizations to act as important power contenders within the domestic political process. Without being a full participant in the process, these organizations are able to place demands upon the system and have these demands satisfied. They are able to require implementation of stabilization programs that often do not coincide with domestic goals and programs. Yet they are insulated from the feedback loop of discontent and dissatisfaction which places them in a dominant position with respect to the indebted nation.

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Steven E. Sanderson

Chairman

CHAPTER ONE
EXTERNAL DEBT IN LATIN AMERICA

The appearance of "new" authoritarian regimes (Collier, 1979) in the Southern Cone has served to refocus attention on the role of the state in Latin America and the nature of the political system in which it operates. Crucial, yet often overlooked variables in this analysis are the dependent linkages between external public debt, the international lending organizations, and the national decision making process. The central thesis of this work is that the restructuring of Latin America's insertion into the post-war international economic system, as seen in the growing importance of external debt, has allowed international lending organizations to function as power contenders in the national political process and is intimately linked to the reappearance of authoritarian regimes throughout the region.

External Debt Growth

External public debt[1] has been increasing rapidly within Latin America, as well as in the other underdeveloped areas of the world, over the past two decades. The quadrupling of oil prices in 1974 led to greatly increased reliance on external financing of massive balance of trade deficits and served to refocus attention on the "role" of external public debt. However, the role of external debt had been growing for some time as foreign capital supplied by direct private

investment or by official development assistance (ODA)[2] had been insufficient to fund developmental capital requirements. The nations of the region, unable and perhaps unwilling to bridge this gap with domestic savings and national revenues from taxation, turned increasingly to the international capital market.

Jane D'Arista (1979) has identified three major phases of LDC borrowing since 1960. In the 1960s, the perceived need by the developed countries for greater LDC development led to the formation of new programs and the creation of new lending institutions to channel more funds to "developing" countries. Implementation of the Alliance for Progress and establishment of the Inter-American Development Bank (IDB) represented the thrust of U.S. policies to Latin America during the early 1960s. ODA, as well as the supply of direct private investment, failed to reach anticipated targets. This ushered in the second major phase of borrowing made possible by large infusions of private funds from commercial banks that were awash in liquidity. As an example, borrowing from Eurocurrency banks increased from $300 million in 1970 to $4.5 billion in 1973; total external debt was estimated to be $78.5 billion by the end of 1973 (D'Arista, 1979, pp. 58-59). The third major phase followed the oil price hike of 1974 which created huge international payments imbalances. This intensified reliance on external financing which was now also used to resolve cumulative balance of payments deficits of some $78 billion between 1974 and 1976 for nonoil exporting developing nations. Total LDC debt

increased by more than $100 billion during this period as these countries financed about 60 percent of their current accounts deficits by bank loans (D'Arista, 1979, p. 59).

The increasing size of this debt has been exacerbated by its coincidental privatization (Stallings, 1979). Private commercial banks have assumed a primate position as a source of foreign capital to developing nations. This role was reinforced following the 1974 oil price hike as private banks recycled surplus OPEC petro-dollars to finance persistent balance of trade deficits incurred by many oil importing developing countries.

The effects of the increasing size of this debt have been compounded by higher ratios of annual payments to principal, stemming from two sources. First, inflation has caused nominal interest rates to soar, reducing the length of payback periods on the real principal. Second, the proportion of debt borrowed from private as opposed to public sources has risen. This has caused nominal interest rates to become even higher than they would have been had most of the funds continued to come from ODA. Moreover, nominal payback periods are shorter for private debts than for official debts, and have no grace period or grant element as do official loans. Privatization of the debt tends to put greater pressure on debt servicing and export earnings. The burden of debt service payments represents a relatively inflexible portion of export receipts and thus produces serious strains on the balance of payments during times of

shortfalls in foreign exchange earnings caused by balance of trade deficits (Islam, 1973, p. 228).

Shortfalls which produce serious strains on the country's ability to service its debt are usually caused by factors outside the control of the debtor country. This has given rise to increased interest over the dependent and interdependent economic linkages relating to this debt. The rapid expansion of external debt has heightened concern over the ability of indebted countries to repay this debt and the prospect of default (Aronson, 1979b, Part One and Part Two). The international economic and financial ramifications of default are indeed serious and warrant attention. However, preoccupation with this aspect of external debt overlooks the consequent debilitating effects on debtor countries and the often harsh economic, political, and social costs associated with debt repayment. Thus Ohlin argues that most studies concerning this debt reiterates a primitive concern about the sheer size of the debt and, above all, about the growth of debt service requirements (1976, p. 207). This emphasis on debt service and default that dominates the "international" perspective often overlooks the social and political linkages and consequences of this debt.

External Debt Linkages

The trend toward increasing reliance on international lenders to provide access to foreign capital has had several important impacts on the political economy of Latin America.

First, the increasing debt combined with an even more rapid rise in debt service payments is leading to an increased reliance or dependence of the domestic economy on the external sector to provide needed foreign exchange earnings. Second, governments that wish to maintain continued, uninterrupted access to foreign capital through loans or direct private investment have necessarily had to rationalize domestic policies to satisfy the requirements and gain the approval of the international financial community. Third, during times of financial crisis when funds are unavailable to finance balance of trade deficits or to meet debt service obligations, indebted nations must obtain new credits to meet these obligations or must renegotiate or refinance existing debts. While the first two factors may condition domestic political developments and policies, the last factor has a direct impact on the domestic political process.

Research Orientation

The purpose of this thesis is to look at the nature of external public debt in Latin America and some of its domestic economic and social, but especially, political consequences. Regarding the nature of external debt, factors that led to increasing demand for access to foreign capital will be presented. It will then be argued that growth of external public debt over the past two decades is a result of increased demand for foreign capital coinciding with a general stagnation in real terms in the size and amount of direct private

investment and official development assistance to the region. Regarding political consequences, case studies will be used to demonstrate the ability of international lending organizations, both official and private, to function as power contenders in the formulation and adoption of domestic policies and programs. An attempt will then be made to assess some of the political, as well as social and economic costs and consequences of the growing importance of the international financial community throughout Latin America.

Some of the reasons that are given for the growth of external debt revolve around the actual or perceived need for access to foreign capital and have little explanatory power in themselves for the growth of this debt. The "necessity" to raise foreign capital for development programs and the need to finance imported inputs (technology and capital goods) for development projects could be satisfied by direct private investment or through portfolio investment. The fact that foreign capital is not or cannot be obtained from these sources has been a major cause for the long term growth of external debt. It is suggested that there is an inverse relationship between changes in the rate of direct private investment and changes in the flow of loans from private and official lending organizations. That is, as direct private investment declines as a primary source of foreign capital, within the region, external public debt will increase. This relationship should exist because domestic savings and government revenues have historically

been insufficient to meet total capital, social, and infrastructure investment requirements. Thus, as direct private investment becomes less and less sufficient to meet total investment capital demanded, the role of external debt financing increases. Likewise, as the role of official lending declines, reliance on private commercial financing increases. Such a trend became almost naturally reinforced by the medium term private financing of massive trade imbalances which resulted from the 1974 oil price hike.

Following from this first inverse relationship between direct private investment and external public debt, there should be a positive, complementary relationship between countries that historically received the largest shares of direct private investment and countries that currently have the largest external public debt. This relationship should exist because the stagnation in direct private investment to the region is not a direct result of internal, intra-regional decisions, but external, extra-regional decisions. Therefore, countries that had the heaviest reliance on direct private investment as a source of foreign capital have become the most reliant on foreign loans to maintain access to this foreign capital.

The growth of external public debt has created increasing domestic economic reliance on the external sector and the international market. Historically, import and export levels were relatively flexible. Imports were dominated by consumer merchandise items that could be easily expanded

and contracted with corresponding "boom" and "bust" cycles in the export sector. Likewise, profit remittances from direct private investment--which was concentrated in the primary sector--also fluctuated with "boom" and "bust" cycles and so placed less pressure on the balance of payments (Avramovic, 1964, p. 85). It has been argued (Avramovic, 1964; Behrman and Hanson, 1979; Islam, 1973; and Villareal, 1977) that import substitution industrialization development has created a generally inelastic demand for imports. Most consumer items that had previously been imported are now manufactured domestically. Imports are now primarily intermediate and capital goods and certain raw materials vital to the industrialization process and foodstuffs the agricultural sector is unable to produce for domestic consumption. These imports, it is suggested, are not easily compressible as an option to offset current account deficits unless the country is willing to accept the consequent adverse effects it will have on the domestic economy. Growing external public indebtedness has placed greater pressure on export earnings because of the inflexible nature of debt service payments. As debt grows faster than export earnings--especially export earnings net import costs--larger and larger portions of export earnings will be needed to service the debt. The greater the reliance on the external sector to produce sufficient earnings to finance relatively inflexible imports and debt service requirements, the more sensitive domestic economic and political decision

making becomes to fluctuations in the external sector and the international market.

Thus the growing rigidity of imports and the inflexibility of debt service obligations constrain the options available to a government facing a debt crisis created by an absolute drop in export earnings or a relative drop created by the increasing value of imports to exports. Rapid import contraction and export expansion are difficult and require drastic measures because of inherent rigidities in both sectors over which policy makers have less and less control. Thus, during times of economic crisis when a nation is unable to finance balance of trade deficits or meet debt service payments new credits must be obtained or current obligations must be refinanced. It is during such periods that international lending organizations most visibly function as power contenders in the domestic political arena, placing demands directly on the policy making apparatus and having those demands satisfied as a precondition for approval of needed loans or credits.

This then is the major focus of this thesis. The growing reliance on external public debt as opposed to direct private investment as a source of foreign capital, in the wake of the then "new" international economic order created at Bretton Woods, restructured Latin America's insertion into the international capitalist system. Latin American nations have since become quite dependent on the international banking system and lending organizations not only as a source of

foreign loans and credits but also to handle their flow of trade. Access to foreign capital is "necessary" to fund domestic development projects and government deficits, and access to such services as deposits, transfers of funds, short term credits, and currency conversions are indispensable for the conduct of trade. The International Monetary Fund (IMF) is the keystone of this world financial system and is the preeminent international organization with which Latin American nations must deal. In order to maintain access to the international financial community it is crucial for a nation to be deemed credit-worthy by the IMF. The vast majority of credit sources in the developed capitalist system, whether private commercial lenders or bilateral or multilateral official organizations, will not extend credit to nor renegotiate loans with a country that refuses to harmonize or modify its national policies and programs in concert with IMF requirements. Such a nation will be labeled as financially irresponsible, will be denied access to the international financial system, and must then resolve the dilemma of withdrawing from the "system" or adopting policies and programs demanded by the international lending organizations.

The goal of this thesis will be to analyze the impact of these lending organizations on the political process within the region and consequent social and economic costs. The role of external public debt in restructuring Latin America's relationship to the world capitalist system and the

international financial community from a regional perspective will be presented. Then, by using case study analysis of Argentina, Brazil, and Peru, the impact of these linkages will be observed on domestic policy formulation. The role of the international lending organizations, as represented primarily by the IMF, wi_ be analyzed from the point of view of a potential power contender within the domestic political process. The outcomes politically, as well as socially and economically, and their costs, will be discussed in terms of their linkages to the imposition of authoritarian regimes within the region and the implications for increasing dependent or interdependent reliance on the international financial system.

Notes

[1] For the purposes of this paper, external public debt will be defined as "debt repayable in foreign currency, with an original or extended maturity of one year or more, contracted directly or with the guarantee of the central government, local government, or autonomous public entities of the debtor country" (IDB, 1978, p. 103).

[2] ODA is made up of resources mobilized by the official sector of developed countries for the principal purpose of promoting the development and social progress of lower-income countries. It includes grants, technical cooperation, and loans with a "grant element" of at least 25 percent of the nominal value of the loan (IDB, 1978, p. 87).

CHAPTER TWO
THE LATIN AMERICAN DEBT TRAP

Latin America's external public debt grew steadily during the 1960's and increased more rapidly during the 1970s. Debt growth occurred in response to increasing regional demand for foreign capital to finance economic growth plans to finance current account deficits, and most recently, in a few cases, to meet debt service obligations. Total debt which was about $6.6 billion for the region in 1960 grew to over $100 billion by the end of the 1970s.[1]

Historical View

To some the growing importance or role of external public debt in Latin America and the potential for default is not a new phenomenon but rather a slightly different permutation or combination of a problem that has plagued the region for a century and a half. Susan Strange (1967, 1979) articulates this point of view by arguing that

> in the nineteenth century and in the pre-1914 period the problem of default on international debt was a recurrent one, to which the creditor countries especially gave much time and thought seeking to devise theories, policies, legal concepts, and administrative remedies to deal with it. The sense of surprise with which the topic was rediscovered during the 1960's was possible only because for the two decades before World War II and the two decades after it the problem was suppressed rather than solved. It was not really a new problem; it only seemed so. (1979, pp. 7-8)

The Changing Nature of Debt

Such an argument is vulnerable on two basic counts: the nature of the debt itself and the institutionalization of debt management on an international scale. With regard to the nature of the debt, Avramovic (1964) contends that there is a major difference in international capital flows prior to World War II and in the post-World War II era. Prior to the 1940s, and especially in the nineteenth and early twentieth centuries, capital inflows were based on limited information, often did not have a sound basis, and were extremely sensitive to the ups and downs of the business cycle which created large ebbs and flows of capital; in a word, the loans were very speculative. As a result, borrowers charged very high rates of interest and default was "expected" during economic bad times (Avramovic, 1964, pp. 85-87).

In the post-World War II period, capital flows are based on much better information and investment decisions are much better prepared. Although swings in capital flows do exist, they are much less pronounced and, in general, capital inflows have maintained a fairly stable trend in most countries. In addition, debtor countries are believed to be in a better position; are not expected to default; and are thus charged "moderate" rates of interest.

Bretton Woods and International Debt Management

The changing nature of external public debt has been reinforced by the creation of international institutions to

manage or oversee debt repayment. Strange argued that pre-1914 creditor nations were concerned with theories, policies, legal concepts, and administrative remedies to deal with debt repayment and default. What she apparently overlooks, or fails to recognize, and this is the second major criticism of her argument, is that an international economic "order" and an institution to manage it were created at Bretton Woods in 1944.[2] The establishment of the IMF and the role it assumed in the maintenance of international economic order meant that external debt in the post-World War II era really was a new problem. It may not be a "new" problem in strictly economic considerations of a nation's payback ability and potential for default, but it certainly has become a "new" problem in terms of political economy and international relationships. A very brief review of some of the reasons behind the establishment of the IMF and the role it was to assume will be helpful for later analysis.

The IMF was established as a formal mechanism to ease problems of disequilibrium in the balance of payments, to facilitate payments adjustments and exchange-rate stability, and to insure international monetary cooperation and the expansion of trade (Blake and Walters, 1976, p. 46). Envisioned was a multilateral world economy where trade and capital flowed across national boundaries in response to the "law of supply and demand" without "political interference" favoring one nation or another (Block, 1977, p. 36). The goal of the U.S. was to maintain high levels of

employment and production in the post-war era without imposition of strong domestic deflationary measures or a greatly expanded governmental role in the management of the economy. This goal could be achieved only by maintaining huge export surpluses. Thus the idea of maintaining an export surplus was very closely tied to the idea of an open world economy and assuring the availability of foreign markets on a large scale.

> Abroad, the reality of U.S. foreign economic policy was effectively hidden by the skillful invocation of the rhetoric of the idealistic internationalists. The clearest example of this was the International Monetary Fund itself. It was originally conceived as an instrument to facilitate expansionary domestic economic policies, but it eventually became another means to impose the deflationary discipline of the gold standard. (Block, 1977, p. 37)

A basic role of the IMF is to harmonize the use and interchange of international currencies. It must insure that sufficient international reserves are available to finance the expansion of international transactions and it is impowered to assist nations with persistent balance of payments difficulties in order to maintain the acceptability of that country's currency and to extend credits which allow the country to continue to trade while it resolves its balance of payments difficulties. Issues surrounding international currency, transactions, and reserves appear to be technical questions beyond the scope of political actors or observers. This, in great part, accounts for the mystique that seems to surround IMF action and lends undue credibility to its policies and programs. Yet, the way in which

these technical problems are resolved vitally affects political, social, and economic relations within the nation as well as international relations:

> To help individual member states restore their balance-of-payments equilibrium and resist the attacks of speculators on their currencies, the IMF allows members to draw upon the resources of reserve currencies of the Fund (which come from mandatory quotas provided by member states) to meet their international debts. As countries have sought to increase their borrowing from the Fund, the IMF has had the opportunity to insist, where appropriate, that certain domestic economic measures be introduced to alleviate what the IMF views to be structural causes of a state's deficit condition. (Blake and Walters, 1976, p. 46, emphasis added)

Analysts, like Strange, who focus on the debt itself in terms of size, ability to pay, and potential for default see no difference in the nature of pre- and post-World War II debt structures. But, as Dewitt and Petras (1979) argue, default is not the real issue, rather it is the fact that international lending organizations have the ability, and legitimacy, to insist on the adoption of domestic measures to resolve balance of payments "difficulties" and restore international harmony no matter the domestic, national costs involved.

External Debt as a Means of Access to Foreign Capital

The growth model pursued by Latin American nations in the post-World War II period was based on two major strategies. The first was articulated by Raul Prebisch (1950) through the Economic Commission for Latin America (ECLA). His study sought to reject the Ricardian model of the international division of labor and comparative advantage by showing the secular

adverse nature in commodity terms of trade experienced by primary product producing countries. He championed national development using a strategy of "import substitution industrialization" (ISI) which was based on establishing and investing in industries which would satisfy local demands that had been previously met with imports. The assumption was that this development plan would lessen the demand for imports, eliminate chronic balance of payments deficits, and thus alter the nature of external linkages between the periphery and the great industrial centers.

The second major strategy drew on the "modernization" paradigm which during the 1950s, using anthropological and sociological research, projected a unilinear path of development from traditional to modern. This paradign was incorporated by Hirschman (1958) and Rostow (1960) into a model of economic development that stressed economic growth led by the modern, industrial sector that would occur in stages until the final stage of maturity would be reached and benefits would have trickled down to all members of society. Required were large infusions of modern technology and investment capital and the encouragement of national, modernizing elites who would use these inputs to create the conditions for economic take-off and nation building.

Although each strategy derives from contrasting philosophical bases, the former wishing to break dependent relationships; the latter promoting imitative, complementary relations, the common agreement on industrial-led economic

growth resulted in a general merging of the two strategies into a post-war "model" of development in the region. O'Brien's (1975) drawing on Dos Santos summarized the intentions of this model as follows:

> (1) a change from development hacia afuera to one hacia adentro would lessen dependence on foreign trade and lead to a more locally controlled economy;
>
> (2) industrialization would lessen the power of traditional oligarchies and lead to a process of political democratization which
>
> (3) would lead to more equal income distribution, and integrate the rural masses into a modern society;
>
> (4) the above three encouraging the emergence of a modern, developmentally-minded State which would in turn further their development;
>
> (5) and all would cause a change of consciousness, the emergence of a Latin American consciousness, which would help to unite society in the pursuit of national independence. (pp. 10-11)

Development projects formulated using this growth model were often very ambitious undertakings requiring large infusions of foreign capital and technology since domestic financing was generally insufficient due to inadequate domestic savings rates, small local capital markets, limited state taxing capacity and a "primitive" technological base. The United States during this period championed the cause of economic development in the region but stressed the role of direct private investment and insisted that only through private channels could an adequate volume of foreign capital be furnished to the region (Perloff, 1969, p. 12). Estimates of the amount of investment capital needed were indeed large.

The Alliance for Progress estimated the need for $100 billion of which $20 billion was to be provided from external sources and $80 billion to be raised locally to achieve a real annual growth rate of 2.5 percent per year for the decade of the 1960s. The Organization of American States (OAS) in the late 1960s developed some projections for the period 1969-1985. Projections were based on historical trends, especially with regard to the coefficient of savings and rate of export expansion. With the goal of achieving the same modest 2.5 percent growth rate, gross capital external financing requirements for this period were estimated to be $137 billion, roughly $8 billion each year (OAS, 1971, pp. 81-87).

Changing Role of Direct Private Investment

Despite the high expectations of the U.S. that direct private investment should play a key, dominant role in this development process and despite, also, the rhetoric which charges that it has played this crucial role, the inflow of direct foreign investment (Table 1, Appendix) has never even begun to approach required amounts projected, nor would it through the 1985 projections. Latin America's position as a prime recipient of direct private investment[3] has been declining over the past fifty years (Tables 1 and 3). Although total direct private investment in Latin America has grown in nominal value, in real terms its growth has stagnated. Direct investment in Latin America as a percent of total direct investment world wide has steadily declined over the

past three decades. In terms of "net" influxes of private investment the region has done even worse.

> In only a few years since
>
> 1950 has the inflow of private capital not been offset by the much larger outflows in profits, royalties, and interest remittances. United States investors received $5.7 billion <u>more</u> than they invested in Latin America (excluding Cuba) during the period 1950-1963. Total earnings by U.S. firms during that period were about $11.5 billion; total investment was about $5.8 billion, of which $3.2 billion was new investment and $2.6 billion came from reinvested earnings. (Perloff, 1969, p. 136)

Advent of Public Borrowing

As D'Arista (1979) pointed out, the decade of the 1960s was a period of rapid expansion of ODA through official bilateral and multilateral lending organizations. Some emphasized that external borrowing was essential to development and was possibly the only way in which poor countries could overcome stagnation and slow growth rates (Adler, 1973). For others, external borrowing represented a more viable and desirable means of utilizing foreign capital.

> External public borrowing widens the choices available to a country in determining the use of its resources over time. It thus creates additional opportunities for an intertemporal reallocation of resources. Such opportunities can result also from private capital movements and from receipt of grants and other unrequited transfers from abroad; all of these augment current resources in much the same way as loans to governments. But these other sources of external resources may not be under direct government control and do not present such well-defined policy alternatives as does public borrowing. (Areskoug, 1969, p. 3)

Official Development Assistance

Responding to this demand ODA became a major strategy for the infusion of foreign capital to the region during the 1960s. ODA was designed to play a special role in the flow of external capital into the region because of its concessional grant element and low nominal interest rates of the loans. Since the goal of ODA is to enhance development and social welfare programs, the funds are designed to be used for the difficult infrastructure investments so urgently required and that are so long in producing a return on investment. The use of ODA was an important factor in conditioning a trend toward the use of state, or state guaranteed borrowing as a means of access to foreign capital.

Deepening of ISI

Within this same general period of emphasis on economic development with industrial-led growth and use of external borrowing as a source of investment capital, the exhaustion of the "easy" phase of ISI had led to the onset of the more "difficult" stages of ISI--the "deepening" of the industrialization process (O'Donnell, 1973). The rapid expansion of consumer goods production, or "horizontal" integration, during the easy phase of ISI behind high tariff barriers reduced, to a certain extent, imports of luxury consumer items. However, the increased demand for intermediate goods to fuel this industrial process began to increase demand for and pressure on imports. As this phase of ISI waned, there was a stimulus for "vertical" integration, a deepening of the

industrialization process beyond that of consumer goods to include production of intermediate and capital goods which were used in the production process. The articulation of this stage of industrialization demanded increased imports of capital goods and their associated technology as well as that of intermediate goods and raw materials that were not available locally. These developments had the unintended result of creating generally inelastic demand for imports while concurrently increasing the value of imports.

These imports are necessary inputs for the modern, industrial sector and are essentially noncompetitive since local substitutes are generally not available. The inability to easily compress imports serves to constrain the options available to a government seeking to resolve balance of payments deficits caused by large shortfalls in the current account. Import cuts of any magnitude to release resources for liquidation of short term debts or trade deficits restores the international credit-worthiness of a country but at the expense of arresting or seriously retarding domestic economic growth.

Privatization of Public Borrowing

The conjunction of increased demand for foreign capital to finance expanding import requirements with stagnating levels of direct private investment and ODA coincided with excess funds available for lending from private commerical banks and from the Eurodollar market in the early 1970s. These countries were able to only partially finance the

importation of raw materials and intermediate and capital goods required for industrial growth with local resources and through imports of foreign capital from direct private investment or long term ODA loans. As an inferior but readily available alternative, they resorted to contracting medium-term loans at commercial interest rates from private banks. At the same time, this trend was reinforced by the generous extension of medium-term credits by the industrialized countries who in competition with each other were concerned with the promotion of their export trade (Avramovic, 1964). In addition, the shifting nature of direct private investment to the region from primary product investment to manufacturing accentuated the demand for foreign capital in the "semi-industrialized" countries that were now receiving the greatest amounts of direct investment. Thus, by the early 1970s a rapid expansion of external public debt can be seen in the region, as well as a developing trend toward the privatization of this debt (Tables 2 and 4 and Figure).

Structural factors had stimulated the rapid expansion of external public debt in the region prior to the huge oil price hike of 1974. Linkages between the "deepening" of the industrialization process, the need to finance the expansion of required imports, stagnation in direct private investment, and the unavailability of domestic investment capital in sufficient quantities led to significant increases in Latin America's net debt by 1973. The nature of some of these linkages was also changing.

Changing Role of Private Investment

Although direct private investment to the region has been stagnating, the shifting emphasis from the primary sector to the manufacturing sector has meant radically different impacts of the role of this investment on various countries. Those countries where direct investment was concentrated in the primary sector, e.g. Chile and Venezuela, have witnessed a steady disinvestment during the past two decades. Direct investment did not shift into the manufacturing sector of these countries, but rather shifted primarily into those countries where large, lucrative markets seemed to warrant large investments in the manufacturing sector, e.g. Brazil and Mexico. These two countries have received steady increases in direct private investment over the past two decades. This investment though geared toward the internal sector depended on imports of intermediate and capital goods, technology, and services. This increased pressure on the import sector which the export sector, though also growing, was unable to match.

The relative decline of direct private investment has been reinforced by the changing character of linkages between Transnational Corporations (TNCs) and underdeveloped countries. Equity participation in the form of investment capital is being replaced by the use of loans and supplier credits; direct managerial control by parent companies is being superseded by management participation, technical assistance agreements, production sharing, and supply

contracts. This forces even greater reliance on the availability of state guaranteed loans as a means of access to foreign capital.

Declining Importance of ODA

Stagnation in direct private investment has been paralleled by stagnation in the availability of ODA. Latin America's share of world-wide ODA has declined slightly from about 15 percent in the late 1960s to about 11 percent a decade later (IDB, 1978, Table III-11, p. 91). ODA from the United States to the region has declined since the late 1960s; however, ODA available from multilateral agencies has offset this decline in nominal terms. In general, however, ODA is stagnating:

> As the Director of the DAC [Development Assistance Committee] points out in his recent report: ". . . in the ten years before 1974, OECD [Organization for Economic Cooperation and Development] countries increased their national product by about two-thirds in real terms and exchanged among themselves some three-quarters of the average annual value of world trade. During this period the real value of official development assistance stagnated." (IDB, 1978, pp. 87-88)

This stagnation has occurred in approved ODA. When gross and net disbursements of ODA are considered, an even more disturbing development is found. Only 60 to 70 percent of total approved loans and grants has been disbursed over the past decade. The net flow of funds, obtained by subtracting loan paybacks from gross disbursements, has almost consistently been less than one-half approved disbursements over the past two decades. In the most recent period, net disbursements have been rapidly declining (Table 5).

For a variety of interconnected reasons, then, regional reliance on external public debt as a means of access to foreign capital was causing a rapid expansion of the debt. The need to finance massive balance of trade deficits in the wake of the 1974 oil price hike was created by rigid import requirements that could not be rapidly contracted to offset the high cost of oil without causing severe dislocations in the domestic economy. At the same time, private commercial banks needed to recycle surplus OPEC petro-dollars that they were rapidly accumulating. For the past six years, a persistent OPEC surplus has been used to finance an equally persistent LDC deficit in the balance of trade. As a result, total regional external indebtedness has been increasing rapidly (Table 2 and Figure).

The Debtor Nations

Having documented the growth of external public debt for the region, the discussion now turns to a consideration of which countries are the most heavily indebted. It has been argued in previous sections that to a significant degree the rise of external public debt in Latin America is inversely related to the declining role of direct private investment and is reinforced by the shifting nature of the investment patterns. In the face of general stagnation in the gross growth rate of direct investment and its relative decline as a source of foreign capital, those countries that historically have relied on direct private investment as a

source of investment capital would be expected to rely heavily on external borrowing to cover shortfalls between relative declines in direct foreign investment and expanding demand for foreign capital. Table 6 shows this relationship to be valid; countries that have been the most important recipients of direct private investment are now the most heavily indebted.[4] Since the early 1970s, the two countries with the largest shares of direct private investment are also the most indebted, a relationship that was not true in the 1950s and 1960s. This seems to be the case because of the concentration of direct private investment in the manufacturing sector which reinforces and stimulates increased demand for foreign capital to finance associated imports which must be satisfied by international borrowing.

The data in Table 7 generally support this contention. In those countries that have experienced a general stagnation in the growth of direct private investment or where disinvestment has occurred (Argentina, Chile, Colombia, and Venezuela) there has been an uneven, yet overall steady growth of external indebtedness. In those countries that have experienced a general increase in the growth of direct private investment (Brazil and Mexico) external debt has grown rapidly. Peru, where direct private investment has had a checkered history, attempted to "copy" the Brazilian and Mexican industrial experience, but without the heavy reliance on direct private investment. The commitment to state sponsored and directed investment in the industrial

sector produced the same rigid "requirements" for imports of capital goods and technology which export earnings proved insufficient to finance. The result was extremely rapid and large increases in external public indebtedness.

Somewhat the same process may now be occurring in Venezuela which since the early 1970s has been committed to a similar deepening of the industrial process. Oil revenues in the early 1970s appear to have been insufficient to offset the increased import requirements and thus the rapid growth in external indebtedness during this period. The huge oil price hike in 1974 temporarily halted this trend and even allowed some liquidation of the debt. However, by 1976 external indebtedness was skyrocketing again with a 123 percent increase in that year alone.

Imports as a Substitute for Foreign Capital

The strategy of an industrial-led economic growth model, complemented by a shift of direct private investment to the manufacturing sector and exacerbated by the exhaustion of the easy stage of ISI and the onset of more difficult stages has led to significant increases in imports of intermediate and capital goods. Villareal (1977) demonstrates this for the Mexican experience. In 1929, imports of intermediate and capital goods were 55 percent of Mexico's total imports; by 1970 this had grown to 90 percent of total imports. External dependence of Mexico has grown even though in national economic growth terms the import substitution

growth strategy has been most successful. Table 8 shows persistent deficits in the current accounts of the seven most heavily indebted nations with the greatest deficits occurring in the most heavily indebted countries. Foreign indebtedness has increased rapidly as a means of financing this deficit because of the growing inability of the economy to finance imports through the export of goods and services and the insufficiency of foreign investment to make up for such inability, even though Mexico and Brazil offered open doors to this investment (Villareal, 1977, p. 86). The industrialization process stimulated by this growth strategy has seen the substitution of an inflow of foreign investment with an inflow of imported capital and intermediate goods finance by external borrowing (Villareal, 1977, p. 81). Thus, the region has turned to the foreign capital market to finance its economic development programs which has been compounded by a need to finance large increases in balance of trade deficits since the mid-1970s.

Debt Servicing

The absolute size and rapid growth of external public indebtedness is not by itself a dangerous trend. A few of the heavily indebted countries, notably Colombia and Venezuela, appear to have been able to successfully manage this debt. The most commonly used rule of thumb to determine a country's ability to manage its debt is the debt service ratio, that is the ratio of total debt payment obligations

to total exports earnings. Although this is a somewhat imprecise measurement which overlooks, among other considerations, the strength of the domestic economy (see Avramovic, 1964, pp. 39-41), it is an easily calculated and readily available measure of a country's ability to service the debt and will be used as such a measure in this thesis.

The debt service ratio is an important measure of a country's ability to manage its debt because the debt must be repaid in a foreign currency which is obtained primarily through export earnings, but is also available from direct private investment and the international capital market. Unless a country is able or willing to obtain foreign currencies through direct private investment or external borrowing, it must rely on the export sector to generate sufficient funds to service this debt obligation. Thus the debt service ratio is a crucial measure not only of a country's ability or inability to manage its external indebtedness but it is also an important indicator of increasing dependence on the external sector as a means of servicing the debt.

Latin America's Debt Service Position

The significance of the debt service ratio for long-run analysis of a country's debt servicing capacity is minimal (Avramovic, 1964, p. 42). A country with a relatively high debt service ratio, e.g. Mexico over the past decade, was able to easily service its debt while a country with a much lower debt service ratio, e.g. Argentina from the late 1960s to the mid-1970s, experienced grave problems in debt service.

However, the significance of the debt service ratio lies in its indication of the short-term vulnerability of the country with respect to its export sector and the international financial community.

Countries with small debt service ratios can make relatively minor adjustments to the import/export sectors to release funds to service the debt. Countries with high debt service ratios and experiencing depressed export earnings must make much more drastic adjustments to their import/export sectors and/or cover the loss of export earnings by contracting foreign loans. The greater the debt service ratio, then, the more dependent a nation's economy is on the export sector and the more vulnerable is its international credit-worthiness.

On a region-wide basis, the debt service ratio has been relatively moderate during the last two decades averaging between 13 and 14 percent of total exports during the period 1961-1976. However, a much different picture emerges when five of the most heavily indebted countries (Argentina, Brazil, Chile, Mexico and Peru) are considered. These five countries --which in 1977 accounted for nearly three-quarters of total regional indebtedness--had an average debt service ratio of slightly more than 30 percent. As the decade ended, three countries--Brazil, Mexico and Peru--had debt service ratios of 50 percent or greater.

Debt service payments have been growing at a faster rate than external indebtedness itself. Between 1970 and

1977, regional debt service payments experienced a 383 percent increase while regional external indebtedness grew at a smaller, though still very rapid rate of 263 percent in nominal terms. The increasing privatization of this debt (Table 4) is in great part responsible for the rapidly increasing debt service payments since private loans mean higher nominal interest rates and shorter maturities with nonconcessional terms. Ohlin (1976) argues that debt service cannot indefinitely grow faster than the export sector of the economy. Rapid export growth, as well as high domestic growth rates, make possible continued borrowing on a large scale despite high debt service ratios and persistent balance of trade deficits. Sooner or later, however, a ceiling is necessarily reached and countries will have "used up" their "borrowing capacity" and will find their borrowing ability sharply curtailed as funds become scarce (Ohlin, 1976, p. 216).

Impact of Debt Service Requirements

External public debt, unlike direct private investment, represents a charge on the economy as a whole since it is guaranteed by the state. Even if the project for which the loan may have been contracted fails, the loan must still be repaid. Likewise, even if the loan's project is successful in domestic terms, a general stagnation in the export sector or deteriorating trade deficits can make loan repayment very difficult. Increasing debt service ratios represent greater and greater claims against export earnings for debt repayment

thus constraining alternative uses of foreign exchange earnings to finance imports required for development projects. As debt service ratios increase, a country becomes more dependent upon the external sector. Its ability to avoid debt servicing difficulties depends on maintaining access to and demand from the markets of the industrial centers for its exports and, more importantly, its ability to attract adequate levels of new financing (Crowe, 1979, p. 30).

A country must relate the benefits of the addition of resources obtained through external borrowing to the cost of servicing this debt in terms of efficiency, transformation and liquidity (Adler, 1973). In order to easily service this debt, the country must first obtain a high enough rate of return on the foreign financed investment to offset amortization and interest costs. Second, at least part of this return must be transferred abroad. Thus, part of the increased output must generate additional exports, replace sufficient imports to service the debt, or somewhere else in the economy additional foreign exchange must be generated or set aside to service the debt. Finally, even if the borrowed foreign capital is invested to obtain high rates of return and foreign exchange earnings are increased, the country may still face a liquidity crisis caused by the bunching of private loans and supplier credits which have short maturities.

Another factor with regard to potential debt servicing problems concerns whether the use of borrowed funds is a

supplement to or a substitute for domestic investment and spending. Ohlin (1976) argues that projects which are attractive and have good potential for return and are financed by foreign loans may well have been undertaken without the loan because of their inherent attractiveness. Because the loan was obtained, it enables an entirely different expenditure at the margin for current consumption or for military spending. Peru's purchase of numerous weapons systems during the 1970s may well serve as an example of foreign loans substituting for, rather than supplementing domestic investment and expenditures.

Debt Service Implications

External public debt and debt servicing represent a charge to the society and the economy as a whole regardless of the purpose for which the funds are used. If inadequate rates of return are experienced or if export earnings fail to expand to meet debt service requirements there is no collateral to liquidate as in privately guaranteed loans. Debt servicing is a very rigid and inflexible portion of a country's balance of payments. Debt service problems generally manifest themselves as a liquidity crisis in the balance of payments caused by external factors, internal domestic economic crisis, or a combination. When a debt crisis occurs in conjunction with a crisis in the balance of payments, a country has several options: it may draw down its reserves, borrow from the IMF, seek new credits, compress imports, or ask for debt relief. In general,

foreign reserves are insufficient to provide more than immediate, short term relief. Likewise, a compression of imports, without access to additional credits, may require drastic cuts that would result in unacceptable domestic economic and social dislocations. As a result, the generally chosen option is to seek new credits or to borrow from the IMF.

The International Lenders and Debtor Countries

It is the desire to maintain access to international credits that shapes the relationship between debtor countries and the international lending organizations.

> The economic capacity to repay loans does not insure a willingness to do so, especially when debt service entails domestic political and economic repression. And repression is sometimes required if the debts are to be paid. Current consumption and investment may have to be depressed and foreign exchange diverted. Such conservative economic policies often have well-entrenched supporters, but enforcing them on the whole country is not a happy task. Compliance is not voluntary. Why, then, do so many states, with such diverse political structures, continue to service their debts in spite of the political and social costs? The answer lies in the political coherence of international finance, a system that revolves around the IMF. The network of multilateral banks, private lenders, and advanced capitalist states can consolidate and refinance debts in crises and can powerfully sanction borrowers in default. This coherent framework of economic sanctions has important consequences. The promise of sanctions, together with the borrowers' continuing need for international financial services, effectively translates the capacity to service debts into the willingness to bear the costs. (Lipson, 1979, pp. 322-323)

Lipson's analysis provides an excellent framework with which to analyze relations between the international lending

organizations and the heavily indebted countries of the region; generally as well as specifically.

The IMF's Crucial Role

The "political" coherence of the international financial community, to which Lipson refers, raises the specter of conspiracy among the developed centers and their financial arms. As was pointed out earlier, the coherence of this international financial system has its roots in the international economic order created at Bretton Woods in 1944 and the "logic" of the capitalist system which articulates it. The role of the IMF is to ensure the economic "freedom" of all participating nations, that is to insure the orderly management of "free" trade, the "free" market, and the "free" flow of international capital.

A crucial element in the maintenance of an open international trading system is the presence of a lending agency of last resort. The preeminence of the IMF as an international lending agency has not been achieved because of the large amount of funds it channels into underdeveloped countries; the volume of resources it provides has consistently been less than that provided by other bilateral and multilateral official lending agencies and private commerical institutions. Rather, the importance of the IMF derives from the conditionality it is able to attach to the provision of new credits. As the lender of last resort, its decisions and actions produce almost without exception similar reactions by the international financial community

(Thorp and Whitehead, 1979, Chapter 1). A nation which refuses to accept IMF conditionality will be denied further access to credits from the Fund's resources and will likewise find that access to credits from other international lenders are generally unavailable.

Convergence of Interests Among International Lenders

The extremely rapid growth of external public debt in the LDC's during the 1970s has produced grave concern among the international financial community about the ability of many of these nations to repay their debts in the 1980s. Some of the most heavily indebted nations that are least able to repay their loans, such as Peru and Zaire, face continued deterioration in their external sector and may simply become unable or unwilling to pay. A default on their part could conceivably trigger defaults by other heavily indebted underdeveloped countries. Such an occurrence would be an economic disaster for private commercial lenders and would cause a crisis in the already shaky international economic "order."

Facing this prospect, the attitudes and policies of private and official lending institutions tend to merge even more closely. Private bankers are advocating an increase in the supply of available public and international credits by raising resources available to the IMF and other international agencies, while imposing "vigorous" economic sanctions on nations borrowing these funds (Aronson and Stein, 1977). Perhaps in partial response to this demand, a new standby facility has been created in the IMF (to which

the United States contributed $10 billion) that is designed to make credits available to financially troubled nations. The IMF will require high risk nations to impose economic belt-tightening measures in return for new loans. These measures will in turn lower the risks of continued loans to such nations.

The IMF's Expanding Role

The IMF's role as the institution able to "impose vigorous economic sanctions" and to insure "economic belt-tightening measures" are adopted has gradually evolved since the 1950s. The IMF was established to substitute cooperation and consultation in monetary and financial affairs in place of the unilateral and independent decision making concerning these matters in which countries had previously engaged (Horsefield, 1969). As described by Blake and Walters (1976, Chapter 3), the cooperation and consultation on the part of the IMF allows the Fund an opportunity to insist that certain domestic fiscal and monetary policies be adopted "to alleviate what the IMF views to be structural causes of a state's persistent deficit condition" (Blake and Walters, 1976, p. 46). In an effort to alleviate balance of payments difficulties and to ameliorate inflationary pressures, the IMF has developed a comprehensive stabilization program centered around conservative neoclassic monetary and fiscal policies. The link between a country's adoption of a stabilization program and the IMF as a participant in this process is contained in the Fund's policies on the use

of its resources. Continued access to the Fund's resources are governed by the conditional acceptance of standby arrangements on the part of a nation seeking new extensions of credit. The importance of these arrangements has grown with time; since the 1960s a high proportion of all drawings is made under standby arrangements (Spitzer, 1969, p. 468), especially among the underdeveloped countries. These stand-by agreements represent the written, signed agreement of the indebted country to the conditions of the IMF loan.

Most governments depend quite totally on the international banking system to handle their flow of trade because of required access to such services as deposits, transfers of funds, short term credits, and currency conversions. Almost all countries have formally established currency convertibility in the IMF which "legally" binds them to convert their domestic currency into foreign currency, and vice-versa, for all current account transactions (Krause, 1971). For reasons outlined previously, the nations of the region have borrowed heavily from international lending organizations to fund development projects and programs and also to meet current consumption in the form of the excess value of imports to exports.

Given the huge levels of external indebtedness throughout the region and the growing burden and difficulties in servicing this debt, there has been an ever increasing tendency for the IMF, and other international lending agencies, to emerge as major participants in the decision making process of financially troubled governments in

reaching solutions to the complex and confused financial situation. During such a financial crisis, a nation desperately needs new loans or credits to avoid default and to cover trade deficits. This places the international bankers in a position to insist that the national government adopt certain domestic policies to "alleviate" the crisis.

Because the issues appear to be so complex and technical, it seems that only the technicians are fully aware of the causal factors and the solutions required to resolve the crisis. As a result of their common financial background and training, these experts tend to be financially conservative and thus recommend the adoption of classic, conservative austere fiscal and monetary measures. Thus when a financial crisis develops, governments may be required to take actions whose practicality and advisability depend upon the perceptions of the players involved (Krause, 1971, p. 535) and not upon the willingness and acceptance of the governed who must bear the costs of these programs.

> The criteria and quantitative goals that have to be met by the recipient country's economic policy . . . constitute a program based on the IMF's principles of how the problems of external disequilibrium and inflation should be approached. . . . These notions are expressed in the form of seemingly unquestionable "technical" criteria, expressions of an apparently axiomatic economic rationality. The IMF thus attributes universality and objectivity to a particular view of the functioning of the world economy and of what ought to be the "best" situation of the national economies. (Frenkel and O'Donnell, 1979, p. 175)

Operation of the IMF[5]

During the early 1950s the IMF established what came to be known as its "tranches policy" to meet the recurring need by some member countries to draw hard currency from the IMF to resolve balance of payments difficulties. Each tranche is equal to 25 percent of a country's total quota and represents how much hard currency can be drawn from that tranche to cover balance of payments deficits. The IMF has a generally liberal, open policy with regard to drawing from the first tranche and allows relatively unconditional access. However, when a member nation needs to draw from the second tranche, the Fund "determines the appropriate degree of conditionality to be applied to drawings under the arrangement in accordance with the particular circumstances, and within the framework of the Fund's tranche policy" (Spitzer, 1969, p. 475). The greater the amount to be drawn, the stronger must be the justification and programs adopted to resolve the "problem."

With regard to LDCs, the IMF has been concerned with the conjuncture of balance of payments difficulties and persistent domestic inflation. Excessive credit expansion, large fiscal deficits, price controls, wage hikes without corresponding productivity increases, deficiencies in the tax structure, and the process of economic development itself are usually seen as the main culprits. Adoption of stabilization programs containing fiscal and monetary policies to counteract the perceived problems is the condition under which the standby arrangement is reached. In order to reach

this arrangement a country must file a letter of intent with the IMF, outlining the stabilization measures it will take and targets (e.g. maximum size of deficit in budget, growth in money supply, etc.) it must reach to continue to receive assistance. The country must also agree to certain protective clauses in the standby arrangement which require consultation with and consent of the Fund prior to the nation taking any action in contravention to the agreement. Failure to comply with any portion of the agreement can, and usually does, result in suspension of IMF assistance.

By virtue of these standby agreements, the IMF, it will be later argued, is able to function as a significant power contender in the political and economic affairs of debtor nations. Its power derives from the fact that access to the Fund's resources can be unilaterally interrupted by the IMF based on *its* perception of a country's failure to comply with or attain the policies and goals of standby arrangements (Frenkel and O'Donnell, 1979, pp. 174-175). What gives the IMF such powerful leverage when dealing with nations in financial crisis is its role as the "technical secretariat" of the international financial community.

> The IMF's decision to enter into a standby agreement with a member country is considered by other financial sources a sign of approval for the stabilization program set forth in the letter of intention . . . . The unwritten rules of international finance have led both private and public financiers to wait for a decision by the IMF regarding a standby credit before negotiating their own agreements which often involve access to considerably higher amounts of hard currency than those provided by the standby credit itself. (Frenkel and O'Donnell, 1979, p. 175)

The Nature of IMF Stabilization Programs

Because of the conservative neoclassical approach advocated by the IMF to resolve inflation induced balance of payments crises, the stabilization programs recommended by the IMF have been quite uniform despite the country or time period involved. Its message is generally one of domestic economic stabilization through strict fiscal and monetary policies and controls and then exposing the economy to the full rigor of international competition through a freely convertible currency. Such recommendations usually translate into budget cuts, wage freezes, elimination of price controls and government subsidies, and limits on public and private credit on the one hand and devaluation, cuts in tariffs and import subsidies and restrictions, and unrestricted currency conversions on the other.

Impact of Stabilization Programs

IMF inspired orthodox stabilization policies tend to require a forceful imposition of the program--"the shock treatment"--on the entire economic, social, and political system because of its inherent external, anti-national bias and the deflationary restrictive nature of its policies. These programs as conceived in their totality are ones that are neither spontaneously chosen nor gradually evolved by the "people" of the affected country (Thorp and Whitehead, 1979, p. 18). Debt repayment, which is often at the heart of the economic crises to be "resolved" by the imposition of the stabilization program, is the responsibility of the

"state," or the population of the country at large.

> Whether the loans went into urban real-estate speculation, someone's Swiss bank account, or factory construction, the debt payments are assumed by the entire society. When creditors or the IMF demand "austerity" (cutbacks in public spending, wage freezes, credit squeezes) and freedom for private capital as a condition for loans to deal with past debts, the burden is borne by the classes that least benefit from the initial loans. (DeWitt and Petras, 1979, p. 204)

The Debt Trap

The rapid increase in regional external indebtedness with mounting problems in the servicing of this debt have resulted in the redefinition and rearticulation of several interdependent linkages between Latin America and the international financial community. Latin America's growing reliance on external borrowing as a means to obtain foreign capital for industrial development programs and, increasingly, to finance balance of trade deficits and debt servicing requirements is reinforcing unequal, dependent relations with the international lenders. By turning to the international lending institutions to finance balance of payments deficits, and especially debt servicing shortfalls, borrowing, in effect, is now being used to meet current consumption. Those nations which continue to experience large trade deficits, notably Brazil, Mexico, and Peru, have opted to become even more heavily indebted to meet these current consumption needs. These nations are becoming, in fact, so far in debt they cannot afford not to borrow.

For just the opposite reasons, the international bankers cannot afford not to lend the money. The influx of private loans to the region was stimulated by high rates of return and the availability of capital to lend. Following the 1974 oil price hike this trend was reinforced by the need to recycle surplus petro-dollars that these banks were accumulating. The economic shockwaves that would be triggered if a major debtor did default provide strong incentives to continue extensions of new credits and/or renegotiation of old debts to allow the debtor country to meet its debt service obligation.

Thus there is an almost symbiotic relationship developing. Indebted nations require continued access to foreign capital to meet current consumption needs and to maintain its national standard of living; the international lending institutions are required to extend more loans to avoid the specter of massive default. There is a tendency for the international bankers and the debtor nations to draw closer together because of their growing, mutual economic interdependence. The real danger is that in so doing the bankers will become deeply entangled in the internal affairs of these debtor nations. As the debt repayment burden mounts, bankers will become ever more hesitant to lend without greater assurances that the nation will be able to meet its debt servicing requirements. Greater pressure will be put on these indebted nations to adopt austere stabilization programs that will depress the domestic sector and expand the

external sector, thus generating foreign exchange earnings required to service the debt. During times of financial crisis the debtor nation, which has developed such vital linkages with the international financial community, desperately needs new loans or credits or it faces default and economic isolation. The regime in power is "willing" to adopt austere, domestically deflationary programs as a pre-condition for access to new loans and credits.

Thus, the debt trap.

Notes

[1]These figures, using constant 1967 dollars, are $7 billion and $53 billion respectively (see Table 2).

[2]For a brief overview of the Bretton Woods international monetary order and the creation of the IMF see Blake and Walters (1976, Chapter 3); a more thorough treatment is available in Block (1977). Horsefield's (1969) three volume analysis and history of the IMF provides a very detailed, though biased view of the first twenty years of that institution's history. A critical, contending view can be found in Payer (1974).

[3]U.S. direct private investment will be used as a proxy to make inferences and generalizations regarding total direct private investment in Latin America. While it would be much more satisfactory to use total data of all direct foreign private investment in Latin America, this information is very elusive, not readily available, and not easily comparable. In 1973 sources of worldwide investment in LDC's were distributed as follows: U.S., 52 percent; U.K., 15 percent; France, 5 percent; and West Germany, Japan, Canada, and Switzerland, 3-4 percent each. Although direct investment in Latin America by the "new" economic giants, like Japan, is rapidly increasing, it is still dwarfed by U.S. direct private investment. For example, in 1979 $5.0 billion was invested in the region by Japanese sources. This represented about 16 percent of Japan's worldwide investment that year, slightly higher than the 12 percent of U.S. investment that went to Latin America that year; however, the amount was nearly five times smaller than total U.S. investment to the region in 1979.

[4]Panama is the only exception to this observed relationship. Panama ranked sixth in 1950, eighth in 1960, fifth in 1970, and third in 1976 as a recipient of U.S. direct private investment. It ranked sixteenth in 1955, eleventh in 1960, twelfth in 1970 and ninth in 1976 in terms of total external public debt. An assessment of why Panama differs from the observed pattern is beyond the scope of this thesis. However, on the surface, several arguments can be made which would "explain" Panama as a "unique" case: U.S. construction of the Panama Canal and control of the Canal Zone; importance of Panama and the Canal Zone from a U.S. national security perspective; and Panama's position as an international transport link.

[5]A detailed history of the IMF and its operations can be found in Horsefield's (1969) three volumes on the IMF. Information in this section is drawn primarily from Chapters 18 and 20, Volume II. Short overviews that provide good insight into how the IMF works can be found in Frenkel and O'Donnell (1979) and Payer (1974).

CHAPTER THREE
LATIN AMERICA STRUGGLES WITH A NEW POWER CONTENDER

The growing mutual interdependence of the international lending organizations and the Latin American nations has a significant impact on the domestic political and economic decision-making process, with certain, almost inevitable social consequences. This chapter will attempt to expand this concept by demonstrating how the international financial community, and especially the IMF, is able to directly, and indirectly influence the political decision-making process of a nation. It will be argued that the IMF, as well as other official and private lenders, possesses significant power capabilities and is able, and willing, to use these capabilities as a power contender placing demands upon the political system and having them satisfied. Relations between the international lenders and Argentina, Brazil, and Peru during various time periods will be presented to discern how these institutions are able to participate in the political decision-making process.[1]

Power Capabilities and Power Contenders

Charles Anderson (1964, 1967) in his perceptive attempt to develop a "theory of Latin American politics" described the political scene in Latin America as one in which

> no particular techniques of mobilizing political power, no specific political resources are deemed more appropriate to political activities than others. No specific sources of political power are legitimate for all contenders for power. (1967, p. 90)

Anderson is arguing that the nature of the state has evolved and developed much differently in the region than it did historically in Great Britain and the United States where a homogeneous nation-state with a consensus of how power was to be shared emerged by the late eighteenth and early nineteenth centuries. Within Latin America, this homogeneous nation-state with its consensual political process has yet to arrive. Given this situation there is no universally agreed upon means of achieving political consensus or regime legitimacy, that is, there are no agreed upon "rules of the game."

> The problem of Latin American politics, then, is that of finding some formula for creating agreement between power contenders whose power capabilities are neither comparable nor compatible. The political system of Latin America may be described as the pattern by which Latin American statesmen conventionally attempt to cope with this variety of political resources used in their societies, and the way in which holders of these diverse power capabilities characteristically interact one with another. (Anderson, 1967, pp. 93-94)

Anderson completes his model by attempting to define the concepts of power capability and power contender. Given the imprecise nature of the political system within the region his definition is more descriptive than empirical, yet it has great analytical utility in assessing the nature of the political process and how demands are placed on the

system and how, and why, some are satisfied and others are not. Anderson equates power capabilities with political resources; that is, he defines power capabilities as "the property of a group or individual that enables it to be politically influential." Using this definition, he describes a power contender as "any individual or group which seeks to have its demands implemented through state machinery . . . through the exercise of a power capability" (Anderson, 1967, pp. 90-91).[2]

The IMF as a Power Contender

Anderson's use of power to define the political process within the region underscores the authoritarian nature of the state in Latin America where rule by consensus has been only episodic. However, the use of power in this model is somewhat more subtle than the concept of raw power that is central to Morgenthau's model. Within the Latin American context the most obvious use of power is seen in the direct application of a contender's power capabilities to have its demands implemented and satisfied, i.e., military force, labor strikes, and student riots. Equally important, however, is the ability of some power contenders to have their demands satisfied and implemented through the withdrawal of their power capability or resources, i.e. nonintervention by the military, economic nonparticipation by the middle sectors, and denial of credits by the international financial community. Withdrawal of power capabilities or resources can be as

effective in achieving a regime change or demand satisfaction and is often more effective than the overt imposition of a power capability or resource. In many respects the ability to obtain demand satisfaction by resource withdrawal is more desirable for a power contender since it is able to dissociate itself and maintain a certain distance from the actions taken and policies adopted by those political actors, or statesmen, that must seek to satisfy the demands.

It is from this vantage point that Anderson's model is a useful analytic tool to consider the relations between the IMF, and other lending institutions, and Latin American regimes. The power capability of the IMF derives from its ability to influence the access of Latin nations to international financial resources as the lender of last resort and the technical secretariat of the international financial community. The strength of this resource is enhanced and reinforced by the demand of the heavily indebted nations for continued, uninterrupted access to this source of foreign capital. The conditionality that the IMF is able to attach to access to new credits during times of economic crisis translates this financial resource into a political resource which allows the IMF to seek to have its demands implemented through state machinery by the exercise of its power capability.

The IMF, like many domestic power contenders, is not always an active participant in the political process, yet its ability to function effectively as a power contender

tends, to a certain extent, to condition the political and economic decision-making process. Regimes that are able to balance their payments and service their debt receive tacit IMF approval and thus are able to maintain access to international financial resources, "free" from the interference of the IMF. Under such conditions, the regime in power is able to develop and implement domestic fiscal and monetary policies without consideration or acceding to the demands of the IMF. During these periods, the IMF's ability to function as a power contender in the domestic political process is effectively neutralized. This follows from the IMF's charter to harmonize international transactions. As long as a country's external sector is in harmony with the international capitalist system there exists no legitimacy for IMF intervention, nor leverage for it to use.

However, during times of balance of payment and/or debt servicing crises, the role of the IMF is recast. These economic crises, as outlined in the previous chapter, are fundamentally problems in liquidity, in that a country faces serious foreign currency shortfalls and is unable to finance current account deficits and meet immediate debt service obligations. Because of the limits on their options, indebted nations have usually sought new lines of credit and renegotiation of old debts. Given the IMF's role within the international financial community, new credits will not be extended nor old debts renegotiated until a standby agreement is reached between the IMF and the nation in financial

crisis. It is during these periods that the IMF actively functions as a power contender within the domestic, political process of a nation. The nature of relations between the IMF, and the international lending institutions, and the indebted country in financial crisis will be the focus of the case studies which follow. These examples should provide evidence that the IMF is able to function as a very important power contender during times of financial crisis and is able to place demands upon the state and have these demands satisfied, i.e. the adoption of stabilization programs by diverse regime types with diverse ideological bases. It will be shown that most regimes are unable to carry out these programs and that only those regimes with the will and the ability to impose these programs do so successfully--and these are authoritarian regimes.

The Peruvian "Revolution" and the International Lenders

Peru has been chosen as the first case study because of its regional implications vis-à-vis the Argentine and Brazilian experiences. Its experience is also very current. Its major interactions with the IMF have occurred during the past four years; the situation remains very fluid; and the IMF remains an active power contender in the Peruvian political process. Finally, Peru also provides a special case where privatization of the debt led to private commercial banks' active participation in the domestic policy making process.

The Peruvian case illustrates the interactions between a nation and the international financial community; many characteristics of the Peruvian case also apply to our review of the Argentine and Brazilian experiences. The moment to moment accounting of "negotiations" between the IMF and domestic political actors is only of peripheral interest; demand placement, demand satisfaction or rejection, and political, social, and economic outcomes are of major interest and will be the primary thread that unites the three case studies. Viewing the IMF as a power contender placing demands upon the state machinery presents a more accurate picture of how the IMF is able to recommend stabilization programs and have them adopted. Viewed in this manner, stabilization programs can be seen as logical outputs adopted by the "free" choice of the domestic power contenders and not as programs these countries were somehow forced to adopt or were forcefully imposed by the IMF. This latter conclusion can be drawn, perhaps, when one concentrates too closely on the aspects of negotiations during financial crises when the strength of the IMF as a power contender appears to allow it to "intervene" and "impose" stabilization programs.

Background: The "Revolution" of 1968

The October 1968 military coup that brought Juan Velasco Alvarado to power ushered in a new era of political and economic development in Peru. Velasco's left of center program, developed in concert with his closest military associates, was eventually detailed in the Plan Inca. The new

Peruvian military regime hoped to steer a third course that was ni communista, ni capitalista in order to bring economic development and social justice to Peru. The military professed the ambitious goal of creating a modern state. Partly as a result of their studies at the Centro de Altos Estudios Militares (CAEM), military thinkers recognized that Peru would never achieve political stability without an infrastructure to support it; the generals also realized, as a result of their 1965 antiguerrilla campaign, that if those in power did not act, those without power would act (Freedman and Krauss, 1977, p. 468).

This "Peruvian model" was hailed by many observers in the early 1970s as a "new" means of achieving revolutionary goals without tremendous social upheaval. Within a decade, however, its economic underpinnings had collapsed. Peru's revolution was unique[3] and perhaps doomed, since it attempted to aggressively pursue simultaneously the goals of social justice and economic growth. Two major aspects of General Velasco's revolutionary program contained the seeds whose growth would eventually cause the program's failure. First --and of lesser importance since its contribution is indirect in nature--was a sweeping land reform initiated by the revolutionary government in which 70 percent of the land under cultivation changed hands and farmers' cooperatives replaced antiquated patterns of possession. The government, however, failed to implement agricultural reform in conjunction with the land reform by not providing access to credit,

technology, and other assistance so desperately needed by the new landowners. As a result, land management and production declined (Viorst, 1978, p. 18). The failure of the agricultural sector to meet the consumption needs of the nation forced an ever increasing reliance on imported foodstuffs during the 1970s, producing an increasing drain on export earnings. Costs and quantity of imported foodstuffs rose during this period requiring more foreign exchange earnings at precisely the same time the country needed greater proportions of foreign exchange earnings to service its foreign debt.

A second major aspect of the revolutionary program was its pursuit of economic reform and growth. Velasco's implementation of this program was even more massive and sweeping than the agrarian reform program.

> Velasco fashioned a remarkable record during his seven year tenure. His regime nationalized most of the country's larger enterprises and public utilities. It assumed control over 90 percent of the nation's exports and about half its imports. After acquiring the majority of Peru's financial institutions the state began to provide almost 50 percent of the republic's investment capital. A series of broad "general laws" regulated various sectors of the economy, imposed strict rules on foreign investors and reserved certain "basic industries" for development under government auspices. (Werlich, 1977, p. 61)

Velasco's program of "economic pluralism" was based on the coexistence of private, government controlled and worker-owned enterprises. Basic to the plan was heavy government involvement in the private sector which led to the creation of major government owned enterprises in mining, steel,

fishing, and oil. To support these and other enterprises, government investment in public works rose from $639.4 million a year in 1969 to $1.9 billion a year in 1974 (Freedman and Krauss, 1977, p. 466).

Debt-Financed Development

The military's goal was a self-sufficient economy free of foreign domination. Restrictions on direct foreign investment by TNCs were to be offset by heavy governmental investment in the private sector. Since government revenues were inadequate to meet these large investment requirements, the Peruvian government still required capital from the developed areas. Direct investments by the highly visible TNCs were politically unacceptable in important sectors of the economy, and so foreign capital was obtained by borrowing from the much less visible international lending organizations, and especially from private banks.

The Peruvian growth model was very successful in achieving relatively high, sustained rates of growth until the mid-1970s. Peru's apparent ability to attain this impressive economic growth while actively pursuing goals of social equality was in great part responsible for the increased attention being paid to the Peruvian model. Nevertheless, this "success" overshadowed the uncertain financial basis on which the model was based. Peru's gamble was that the long term success of its economic programs would eventually offset the heavy short term dependence on foreign capital and the export market.

Dramatic increases in Peru's external public debt occurred in the 1970s when heavy state involvement in the private sector became more fully operationalized. During the first six years of Velasco's regime Peru enjoyed a surplus of foreign exchange earnings which enhanced its creditworthiness, facilitated the influx of foreign loans, and eased the burden of debt servicing requirements. Peru's domestic economic program was structurally oriented and defied conservative, neoclassic policies. However, so long as its international position remained strong and solvent, Peru was free to pursue its somewhat unorthodox domestic economic program.

Four events dramatically altered this picture. First, oil prices quadrupled in 1974; Peru's oil expenditures rose from $56.5 million in 1973 to $224.5 million in 1974 with only a slight increase in the total amount of oil imported. In 1974, Peru experienced its first balance of trade deficit since 1967. The severity of this deficit was cushioned by continued high export earnings. In 1975, foreign exchange earnings dropped precipitously as a result of two simultaneous disasters: the price of copper plunged from $1.50 to $.50 a pound on the world market, and, due to a shift in the Humboldt Current, the anchovies quit running, paralyzing the country's fishmeal industry. Both were important foreign exchange earners for Peru. The balance of payments deficit in 1975 soared to $1.5 billion. Finally, underscoring the danger of Velasco's short term dependence on foreign loans,

wheat, Peru's principle imported foodstuff, experienced significant price increases during this period which exacerbated the trade deficit. Financial crisis threatened to bankrupt the nation.

A "Revolution" in Crisis

By mid-1975 confidence in General Velasco's ability to manage the revolutionary program deteriorated amidst growing economic pressures. Velasco's failing health reinforced this crisis of confidence and in June 1975 General Francisco Morales Bermudez led a peaceful palace coup replacing Velasco as the nation's President. Morales Bermudez labeled the coup a "revolution within a revolution," but quickly began to dismantle many of the revolutionary programs (Kinzer, 1979, p. 16). Bold experiments in worker management were terminated or significantly reduced in scope. Many industries were returned to private ownership, and in other areas worker control in the comunidades industriales was reduced from 50 percent to 33 percent to make investments more attractive. TNC's were invited back and more than 40 planned social property projects were shelved (Freedman and Krauss, 1977, p. 468; Kinzer, 1979, p. 16). Although the Morales Bermudez regime began to move the "revolution" to the right into a more centrist model, the military refused to retrench economically and continued to rely heavily on foreign loans to fuel the domestic economy. Between 1975 and 1977, foreign capital accounted for $3 billion of public investment, a little more

than one-half the total investment (Freedman and Krauss, 1977, p. 466).

Continued reliance on foreign loans allowed the military regime to keep the value of the sol artificially high which meant relatively cheap prices for basic foodstuffs, especially imported wheat. The international lenders were willing to go along with this program since the depression of copper prices and the absnece of anchovies were seen as temporary aberrations in Peru's economy. Nonetheless, this temporary phenomenon became increasingly persistent. Foreign exchange earnings in 1977, projected at $2.8 billion, totalled only $1.6 billion. By now the economic crisis had become an economic disaster. Peru tottered on the brink of bankruptcy, and the military government had to seek accommodation with the international banking community to avoid default.

Peru "Deals" with Commerical Bankers

Following the disastrous loss of foreign exchange earnings and the $1.5 billion deficit in 1975, Peru began to experience difficulties in meeting debt service payments. In early 1976, Peru borrowed $200 million from its first tranche in the IMF to meet debt service obligations. By late 1976, the military regime once again was facing debt servicing payments due at year's end with insufficient funds available, due to its billion dollar foreign trade deficit. Recognizing that if it turned once again to the IMF, there would be an obligation to submit to the Fund's formidable credit standards and comply with its stringent monetary and

fiscal targets, the military leaders turned to the private banks. This time, however, Peru was not requesting developmental funds that held the eventual promise of producing a return on investment, but was requesting a loan that would be used to meet payments due on previous loans. Peru needed breathing room in order to make it through the bottom of its economic cycle; the bankers were eager to make the loans to prevent default on the huge package of loans Peru had already accumulated. The military was requesting $390 million, of which $300 million would be used to meet interest and principal payments; for the banks this was "small change" compared to the $4 billion debt Peru had already accumulated. The arrangement worked out by November 1976 is most interesting in its details and the nature of the consortium involved, since it indicates a new "role" private commercial bankers had decided to adopt.

The international mix of the banking consortium that put together this package did not widen Peru's options, but narrowed them. The banking groups were as follows: two European syndicates, $115 million; a Canadian group, $30 million; a Japanese group, $35 million; and a syndicate of U.S. banks, $210 million. The international mix of this consortium involves all the major developed capitalist countries. Looking at the sources from strictly a geographical perspective one might feel that since Peru had spread its debt among several creditors, it would be able to play one against another to achieve better terms, thus

increasing its options. In fact, the opposite has occurred. As can be seen from the make-up of the consortium, Peru's liability has been spread among the banks of several nations. The international make-up of the consortium increases international effort to work in concert to insure that a debtor nation meets its obligations. This coalescence of private commercial lenders is similar to the "creditor-club mechanism" (Crowe, 1979) of debt renegotiations with official bilateral and multilateral lenders. This "mechanism" ensures that "creditors share the risks of lending identically" (Crowe, 1979, p. 40); it also ensures that there will be virtually no other avenues of credit open to the debtor nation facing economic crisis and default. Whereas international competition among TNCs to place direct private investment can when accompanied by enlightened domestic policies be turned to a nation's advantage, the coherence of the international financial community tends to be disadvantageous to a debtor country.

A second interesting aspect of this loan was the nature of the negotiations and the conditionality the private bankers attached to the loan. As a condition for granting this loan, the bankers demanded that Peru adopt economic measures designed to reduce its huge foreign exchange deficits and thus ease debt servicing problem. To insure that these actions were taken, the

> loan was accompanied by a side letter setting down the policy understanding on which the loan was granted, including periodic reporting on economic progress by the Central Bank, so that the private

> bankers could monitor Peru's compliance with the conditions of the loan. The arrangement broke new ground in the field of LDC lending. Not in recent memory had the banks been so fully drawn into the policy making process within an LDC. (Beim, 1977, p. 725)

In addition to the special conditions attached to the loan, the terms of the loan were very stiff. The interest rate charged was 2.25 percent above LIBOR (London Inter-Bank Offer Rate) with a five year maturity (Stallings, 1979, p. 240). In compliance with the terms of the loan, Peru devalued the sol by 30 percent, reduced the budget, cut back on imports, removed price controls, and instituted wage controls.

Curiously, while negotiations concerning the loan were still going on, the military purchased 36 SU-22 jet fighter aircraft from the Soviet Union for $250 million. The bankers expressed great reservations regarding the advisability of such a purchase in the midst of such severe economic problems; the generals quickly and firmly let it be known that while they would accept some interference with respect to economic matters, they would accept no such interference regarding military requirements to bolster the nation's "defensive" posture.[4]

Soon after the release of the second installment of $190 million, Peru's Central Bank was less forthcoming with required economic reporting and the military regime eased some of the measures previously enacted in response to mounting, though still relatively muted protest. Still, Peru faced even more severe debt servicing problems as balance of trade deficits remained. Private bank monitoring proved unworkable

by early 1977 and the bankers called upon the IMF to negotiate a new austerity package with Peru before extending further credit. The bankers complained that Peru had promised to do certain things and then did not comply: the government failed to cut the budget sharply enough; the military continued its arms purchases; and the Central Bank did not provide sufficient data.

The loan's conditionality and the private commerical bankers' monitoring of compliance became quite controversial within the international financial community. This, combined with Peru's eventual noncompliance with the conditions of the loan, led to the banks refusal to renegotiate the debt without IMF participation. Stallings (1979) identifies three sets of factors that led to the private banks' quick termination of active participation. First, there was immediate opposition to and criticism of the new monitoring role, not only from the left in Peru and internationally, but also from within the ranks of the private commerical lending institutions. They pointed out the risk of becoming scapegoats for the unpleasant results of the stabilization program which had been required and was being monitored. There was also doubt concerning their ability to enforce the conditions of the loan. The final two sets of factors concerned the advantages of working in concert with the IMF. First, the IMF provides a more neutral facade for imposing economic stabilization programs and is better organized to collect data and monitor compliance. Secondly, the IMF was

in a position to demand more stringent conditions and, as the lender of last resort, was in a better position to insure compliance.

Peru "Deals" with the IMF

By early July 1977, Peru and the IMF successfully negotiated a standby agreement and new credits of $130 million from Peru's second tranche were extended in exchange for new, tough restraints.

> In a typical set of demands, the IMF "suggested" that Peru (1) cut all subsidies to public enterprises, leaving them to acquire necessary financial resources through price increases; (2) raise gasoline and other fuel prices enough to both eliminate the Petroperu deficit (6 billion soles) and provide a surplus for the central government; (3) cut another 10-20 billion soles from the deficit by eliminating the purchase of capital goods for public sector investment and selling off firms to the private sector; (4) tighten up the tax system by eliminating all tax exemptions (including those on traditional exports), creating an emergency "wealth tax," and indexing tax payments; (5) eliminate noneconomic restrictions on imports (e.g. quotas); (6) devalue the sol by 30 percent (i.e. to 90 soles/dollar); (7) limit wage and salary increases to 10-15 percent. (Stallings, 1979, p. 245)

Not only was this agreement intolerable even to Peru's conservative financial officials, but as word of the "deal" with the IMF spread and its effects felt by greater and greater numbers of the country's impoverished classes, resentment and public opinion against the government's action grew. The protest was culminated by a massive general strike on July 19, 1977, with "enough of Peru's politically divided labor movement uniting to make it effective, especially in Lima, which had not seen so general a stoppage since 1919"

(Brockman, 1977, p. 150). The military government was caught between the IMF and private bankers' stabilization programs and popular disapproval of the measures. Requirements for greater austerity in the form of further devaluations of the sol and lessened government spending were met by massive strikes and protests demanding food at reasonable prices and increased government services. The military's response was twofold. It canceled its standby agreement with the IMF, plunging the country into greater economic turmoil on the international front. And, it adopted more repressive measures internally to stop the strikes and protests.

The relatively rapid response of the Peruvian poor to austerity measures taken by the central government is a result of the country's need to import a large quantity of basic foodstuffs. A devaluation almost instantly raises the cost of living. For example, following the devaluation in 1976, basic foodstuffs rose 11-57 percent depending on the item and since wage limits had been enforced and subsidies reduced, the devaluation meant higher prices for essential goods with only token wage increases. Thus, a significant decline in real wages and real purchasing power resulted.

In the face of a pressing need to meet debt servicing obligations at year's end, Peru and the IMF reached a second standby agreement for new credits in late 1977. In return for $106 million in standby credits, the military government agreed to yet another strict austerity plan: the federal budget deficit would be reduced from the 1977 rate of 6.7

percent of GNP to 2.6 percent in 1978 and 1.8 percent in 1979; anti-inflationary measures would be adopted to reduce inflation from 40 percent to 20 percent; average wage increases would be limited to 10 percent and the sol would be cut loose from artificial control. The new austerity measures brought a swift response of renewed strikes and protests and the now familiar military response of an abandonment of many of the promised measures and increased repression to restore order. As a result of the internal social and economic disorders, the economic crisis mounted.

The economic nightmare reached yet another critical point in May 1978. Inflation had soared to 120 percent and GDP declined by 1.8 percent. By now, nearly 50 percent of Peru's export earnings were required to finance debt payments, and in July $185 million was due with no cash on hand. Because of Peru's failure to follow through on the agreed upon austerity measures, the IMF had refused to release the stand-by credit installment in February. Negotiations with private banks for a new loan package predicated on the IMF's standby credit collapsed as a result. Peru's credit rating was at rock bottom; the country could no longer service its debt, and faced a real danger of not being able to import enough foodstuffs and other essential commodities to meet her needs.

In mid-May, a new civilian ministerial team led by Finance Minister Silva Ruete was given the unwelcome task of launching new anti-inflationary measures. This marked the seventh shake-up of economic ministerial leadership in the

less than three years since the June 1975 coup brought General Morales Bermudez to power. As the new team began to implement measures to control inflation the Peruvian poor, anticipating further unacceptable monetary and fiscal measures to meet IMF demands, again took to the streets with riots, strikes and protests reminiscent of those of July 1977. Due to the severity of the protests, anti-inflationary measures were eased and negotiations with the IMF were once again interrupted. Still, Peru faced July debt servicing payments with no cash on hand. On the brink of bankruptcy and default once again, the Peruvian government turned to her Latin American neighbors and Spain for assistance and was able to obtain approximately $86 million in order to meet the impending financial crisis.[5] With this cash on hand, Peru was able to persuade the private banks to delay the July debt payment until January 1979 and was able to reopen negotiations with the IMF.

The End of the "Revolutionary" Experience

The pattern of these two years was to become a fixture: a deterioration of the economic situation, debt service payments due with insufficient cash on hand, negotiations with the IMF and private bankers for credit extensions, agreement to enact conservative fiscal and monetary policies, receipt of the credits or loans, strikes and riots protesting the actions taken, abandonment of stabilization programs accompanied by increasing repression, and then coming full cycle by again facing debt servicing requirements with insufficient

cash on hand. This cycle was repeated several times during the remainder of 1978 and 1979.

If anything, the pattern worsened. Most of the loans from the banking consortium were short term, maturing in five to seven years. These types of loans had been increasingly contracted since the 1974-1975 period. As 1980 approached, loan repayments began to be bunched together creating even greater debt servicing problems. Kinzer reports that without IMF sponsored renegotiations, Peru would have been required to pay more than two-thirds of 1979's export earnings for debt repayment, a situation that almost certainly would have led to default (Kinzer, 1979, p. 17). One of the strategies that has been adopted is to either renegotiate old loans or negotiate new loans over longer periods of time, most generally 12-15 years. This "strategy" will prevent bunching loan repayments in the short term; but seems to insure long term economic problems for Peru barring an economic miracle that might rescue it from this ill-fated posture.

Kinzer has aptly labeled Peru a "ward of the international banking system" (Kinzer, 1979, p. 17). Peru's foreign debt currently stands between $8-9 billion, nearly half of which is owed to private banks. The debt servicing requirement is hovering near 50 percent of export earnings. The country's military leadership is disillusioned; its "revolution" is in disarray. In an effort to preserve what remains of their institutional "dignity," the generals have

turned power back to civilian leadership which now faces a nightmare of economic problems requiring extremely difficult and complex solutions. It is most uncertain whether they will be equal to the task. Perhaps an insight into their potential for success can be gained by consideration of how Citibank, heavily involved in international lending to LDC's, determines a nation's credit-worthiness. It looks for governments that are able to demonstrate political stability and the will and administrative ability to divert resources from current consumption and investment in order to meet its foreign obligations on schedule (Clevland and Brittain, 1977, p. 733). In other words, how capable is the government of enacting austerity measures and controlling popular unrest in the wake of these measures? It is doubtful that any civilian administration will be able to demonstrate the will or stability required to resolve the present financial situation.

"Modernization" and the IMF: The Argentine Experience

Argentina has nearly a twenty-five year history of repeated economic crises in the export sector, negotiations with the IMF, and imposition of a variety of stabilization programs. The similarity of the stabilization measures adopted despite the type of regime in power or the problems to be solved and goals to be attained will be helpful in analyzing the role of the IMF as a power contender in the domestic political process.

Historical Background

Argentina, from the point of view of many proponents of modernization theory, appears to possess all the necessary prerequisites for rapid, industrial economic growth and the concomitant establishment of "modern" social and political institutions. It emerged in the late 1940s from two decades of relative isolation--dictated by a worldwide depression followed by a world war--in a seemingly strong economic position. Internationally, Argentina had built huge foreign exchange reserves and its exports were in high demand; domestically, there existed a nascent industrial base, a growing entrepreneurial middle sector, a dynamic metropolis, and a mobilized working class providing a mass consumer market. Rostow judged Argentina to be in its "take-off" stage.[6] Argentina's "drive to maturity" seemed to be merely a question of time and the proper application of capital and technology by the country's modernizing elites who were charged with the responsibility of overseeing this process of economic growth and nation building.

Through the conjunction of fate, Eva Perón, and the mass popular support of a recently mobilized labor movement, Juan Domingo Perón became the appointed overseer of this modernization process. His model for development sought to meld the best of two worlds: ECLA's ISI growth model which was to be driven by capital appropriated from the dynamic agricultural export sector. Although achieving apparent initial success, Perón's program was foundering by the early 1950s.

> At the end of Perón's rule, Argentina was passing through one of the worst economic crises of its history. The failure of the Peronist program of autarkic industrialization, coupled with the policies of mass mobilization and welfarism that had characterized the regime, had left a sequel of inflation and misdevelopment, changing the nature of, but not abolishing, dependency, and reinforcing the pattern of "superstructural" modernization typical of Argentine social change. (Corradi, 1974, pp. 375-376)

The decade of Perón's rule set in motion two major interconnected and interrelated conflicts that were to plague Argentina for the next 25 years: stabilization vs. national economic development politically represented by the Armed Forces vs. the Peronist labor movement.

Argentina has been subjected to seven major stabilization programs during the past three decades.[7] All but one of these programs were triggered by balance of payments crises (Table 9). What is of particular interest is the similarity that exists among the seven programs (Table 10). The orthodox, conservative, neoclassic approach dominated the philosophical basis for these programs. The goal was to attain "fiscal responsibility" by a three pronged attack on the problem: (1) a domestic anti-inflationary or deflation program (freezing wages, or sharply curtailing wage increases, eliminating price controls, tightening monetary policies and credit controls, and reducing public expenditures); (2) expansion of exports and reduction of imports (mainly via devaluation); and (3) actively seeking foreign investment and capital (Blake and Walters, 1976, p. 71). As Table 9 shows, these stabilization programs have

been notably unsuccessful in achieving the first two goals, except on a very short term basis. Inflation has continued to plague consumers and balance of trade deficits recur despite the continued imposition of measures designed to reverse this trend. Only the inflow of foreign capital has responded as anticipated; foreign direct private investment has grown, in nominal terms, from $356 million in 1950 to $1.1 billion in 1975, while external public debt has grown from $600 million in 1955 to nearly $9 billion in 1978.

Economic Stagnation, Stabilization, and the IMF

O'Donnell (1973) argues that Argentina's failure to sustain the rapid economic growth predicted by Rostow was a function of the exhaustion of the easy phase of ISI by the late 1940s. This was a primary cause of Argentina's economic stagnation in the post-World War II era leading to a balance of payments crises and intense domestic conflict. The easy stage of ISI, stimulated by the dynamic export sector, had allowed the state to relatively easily satisfy demands placed by the export oriented agricultural sector, domestic entrepreneurs and the recently mobilized popular sector. With the onset of the more difficult stages of ISI in the late 1940s and early 1950s, declining productivity in the export sector combined with rigid, high cost imports of raw materials and intermediate and capital goods led to frequent foreign exchange shortfalls, stabilization-induced recessions, declining domestic resources available for distribution, and thus difficulties in satisfying all demands being placed.

Competition for these increasingly scarce resources polarized the country into two antagonistic coalitions, one composed of the propertied classes and most of the urban middle class and the other drawn from the labor union-led popular classes (Wynia, 1978, p. 10). The armed forces served as an arbiter of this process, not always allied with the propertied and middle class, but always opposed to the Peronist labor movement. Prior to 1976, no "solution" to this conflict was apparent. A variety of regime types, attempting to respond to the demands of the various power contenders was adopted. The diversity of regime types and domestic programs planned or adopted stands in stark contrast to the continuity of stabilization programs these administrations adopted in response to balance of payments crises. Frenkel and O'Donnell (1979) argue that these administrations, facing the convergence of high rates of inflation and acute balance of payments crises, felt it was imperative to regain the confidence of the international financial community by instituting a program that would make available the foreign capital resources required to alleviate the crises. In addition, these administrations were convinced that these objectives and policy measures were economically rational, and without their implementation it would be impossible to rescue the country from its crises:

> What we are really facing is a convergence of determinations, or better still, a case of overdetermination. Even without the need for the IMF's blessings, the stabilization program of these cabinet ministers would have been similar to the one they agreed on with the IMF. On the other hand, even if the

> respective economic teams did not believe that these policies would succeed, the need to formulate a program to satisfy the IMF and the international financial community would also have determined a policy package similar to the one actually approved. This convergence is one of the issues we are interested in exploring here. (Frenkel and O'Donnell, 1979, p. 199)

This relationship, or "convergence of interests," is most graphically demonstrated in the stabilization programs enacted by three diverse regime types, the Frondizi administration in 1959, the Onganía administration in 1967, and the Videla administration in 1976.

Stabilization Under Frondizi[8]

Frondizi's election to the presidency in 1958 represented the first attempt by the military after the overthrow of Peron in 1955 to reopen the political process to consensus based, democratic rule. The "openness" of the process was tainted by the exclusion of the Peronist party from the electoral process and the vulnerability of Frondizi to the military which placed the constitutional system "on trial" throughout his administration (Wynia, 1978, p. 93).

Shortly after his inauguration in May 1958, Frondizi and his economic advisers developed a "comprehensive program aimed at promoting sustainable economic growth" (Wynia, 1978, p. 86). He believed that Peron's development program had failed because it had relied on Argentine resources alone. Stressing the need to use foreign capital to help finance the industrialization of a country that suffered from acute capital shortages, Frondizi defended the use of foreign

investment as a temporary expedient leading to eventual national economic independence (Wynia, 1978, p. 87). However, the conjuncture of desired access to foreign capital and a deteriorating balance of payments situation forced radical alterations in Frondizi's program in order to solve the immediate crisis.

Frondizi asked the IMF for emergency standby credits to deal with the situation. The IMF now had the opportunity to recommend certain domestic measures be adopted. The Frondizi administration was advised that its current policy of import restrictions alone was insufficient to solve the balance of payments problem and that domestic demand needed to be sharply reduced by cutting public expenditures, curtailing credit, keeping salaries in line with productivity, and reducing public investments below the levels projected in the current development program. Frondizi, at the outset, was reluctant to implement these IMF "proposals," but

> it required little tutoring in economics to understand that inaction in the face of the payments crisis would be disastrous for the entire economy, negating whatever development programs he might choose to sponsor. Moreover, few foreign investors would be attracted to a country that had been condemned as financially irresponsible by the International Monetary Fund. (Wynia, 1978, pp. 88-89)

In formulating his economic programs, Frondizi faced the delicate political task of retaining the tenuous support of the Peronist labor movement while acceding to the demands of the anti-Peronist military. Despite awarding labor a 60 percent wage increase shortly after his inauguration,

increasing strains between labor and the president developed in conjunction with the increasing rate of inflation, deterioration in the balance of payments situation, and the IMF proposals.

> His final break with labor came when most Peronist unions, ignoring the president's plea for restraint, supported a strike against the state petroleum company. After some hesitation, and several failures at compromise, he declared a state of siege to suppress the strike and in so doing hastened the end of his coalition with organized labor. With his path cleared, Frondizi addressed the nation on December 29, 1958, to announce the most drastic economic stabilization program in Argentine history. (Wynia, 1978, p. 89)

As a result of the "shock treatment" of this program, income was quickly redistributed away from the labor sector which saw its real income fall by about 25 percent in 1959. Frondizi, the "democrat," had no illusions that labor would support his stabilization program, but had hoped to resolve labor conflicts through peaceful government regulated collective bargaining. However, his tenuous hold on the presidency in the face of military demands for stability and order compelled him to use physical repression to keep recalcitrant unions in line. Small, national firms were also disadvantaged by the stabilization program which led to the bankruptcy of many "uncompetitive" firms and their absorption by foreign capital.

The stabilization program appeared to be "successful;" inflation was down, GNP growth was up, and foreign capital was flowing in freely.

> If one looked beyond these indices there was another less reassuring side. The government's heavy borrowing abroad trebled the country's foreign debt. The balance of payments, which had taken a positive turn in 1959, experienced a deficit of $572 million in 1961 . . . the deficit which had been only 9.9 percent of total expenditures in 1956 . . . averaged 23.1 percent during Frondizi's four years. (Wynia, 1978, p. 104)

By 1962, the resurgent Peronist movement supported by Frondizi in the face of growing domestic opposition combined with a balance of payments and liquidity crisis led to his removal by the military.

Stabilization Under Onganía

The "stabilization" program adopted by the Onganía administration in 1967 was the only such program that was freely adopted by national political actors and that was not adopted in partial or complete response to a balance of payments crisis and the demands of the international financial community. The military regime that he headed was also unlike those that preceded and followed. Stepan (1978) has characterized the Onganía regime as "corporatist exclusionary." What Onganía attempted to install was a centrally directed program designed to complete Argentina's industrialization program with the assistance of large transnational corporations that could supply the capital and technology the country was lacking. This required a strong government that could guarantee political order and a "friendly" investment climate (Wynia, 1978, p. 167).

The economic development program chosen by Onganía and his chief economic advisor, Krieger Vasena, sought to

stimulate a stagnating domestic economy, reduce inflation, and build up the country's low international reserves by improving Argentina's balance of trade. The program, because it required ready access to foreign capital, contained many policies that closely paralleled the country's four previously imposed stabilization programs.

> But rather than slavishly adhering to past policies or the dictates of the International Monetary Fund, they sought to fashion an innovative global program that coordinated measures dealing with price exchange, wage, agricultural, and industrial objectives. . . . There is no doubt that the measures announced in March 1967 represented Argentina's most sophisticated and comprehensive attempt to combat inflation. (Wynia, 1978, pp. 169-171)

Among the classic stabilization measures adopted were a 40 percent devaluation, wage freezes and controls, voluntary price controls, reduction of government deficit by increasing the price of services and increasing taxation, and promoting a shift to foreign investment and use of foreign capital. Several of the measures were contrary to other stabilization programs, notably the expansion of credit and the money supply and increasing government investment in the private sector. Argentina's positive balance of trade position since 1963 permitted Onganía a relatively free hand in domestic economic policy formulation, much like that enjoyed by Velasco in Peru.

Although income was less severely redistributed under this program than during those stabilization programs previously adopted, Onganía's anti-labor policy combined with stagnation in real wages and double digit inflation alienated

the labor movement. Likewise small, national firms were disadvantaged by this program as before and Ongania was criticized for the "denationalization" of domestic industry and finance through foreign takeovers. Dissatisfaction with Onganía's program culminated in the Cordobazo of May 1969 when several days of labor riots required harsh repression to resolve and led to a retreat by Onganía from many of his hardline policies, not unlike the experience of Frondizi. This led to his eventual overthrow by an internal military coup which was significant in that it underscored the continued lack of institutional unity within the military regarding a uniform, unwavering policy to be adopted toward the Peronist labor movement. Onganía's plight, and the military's as an institution, was the "failure" to replicate all of the stern repressive measures employed by the Brazilians when challenged by labor during the Cordobazo (Wynia, 1978, p. 187).[9]

Prelude to Videla

The presence of a large, well organized, highly mobilized labor movement in Argentina has posed significant problems in the implementation of stabilization programs. The Peronist labor movement was able to influence the political process with its sizable voting bloc and its ability to effectively demonstrate and protest government policies. It was also able to disrupt the economic process with its ability to strike. The cyclical nature of the political process and the on-again/off-again nature of stabilization programs were

reflections of the strengths of Argentina's two major power contenders: the Peronist labor movement and the military. The inability of the Peronists to accomplish their objectives and the unwillingness of the military to impose theirs led to two decades of chaotic stalemate.

In the last analysis it was access to foreign capital as a solution to the economic crises and/or as a funding source for industrial development programs that dictated the adoption of stabilization programs and rationalization of domestic programs and policies to satisfy the demands/requirements of the international financial community despite their adverse domestic political and economic implications. And yet, ironically, these programs were consistently justified as being domestically and internally necessary to combat demand-pull inflation created by wage rates that exceeded productivity and price supports and controls that caused huge budget deficits. But domestic improvements were of short duration and thus stabilization programs had minimal impact on pressing internal economic and political problems. Politically, this resulted in a cyclical alternation of democratic and authoritarian regimes, the former unable to compellingly convince and the latter unwilling to sufficiently coerce those who were required to pay the costs associated with the stabilization measures. This cyclical process had the unfortunate result of fragmenting and weakening the democratic process while unifying and strengthening the authoritarian process. Prior to the

advent of the 1970s, the election of Illia in 1963 with 26 percent of the vote was indicative of the former process, while the Cordobazo in 1969 is indicative that the latter process was yet to be fully institutionalized.

The antecedents to the military coup of March 1976 can be traced to the first Perón regime; but it was Perón's return to power in 1973 that created the immediate and most compelling conditions for the installation of an authoritarian regime. Perón's unwillingness to institutionalize a line of succession within the Peronist movement and his alignment with the "rightist" elements of his movement after his return to power were the two major factors that would lead to the violent disintegration of the Peronist movement and the consequent rupture of the Argentine social fabric. Juan Perón was able to maintain a thin veneer of solidarity within the movement, but with his death in July 1974 and the assumption of the presidency by Isabel Perón, Argentina disintegrated into social and economic chaos. Corruption fostered by wage-price controls and a black market underscored the social decay that saw its most violent and bloody expression as left fought right in a struggle that was tantamount to a civil war. The military stood by and allowed the struggle to deteriorate until the Peronist movement had spent itself and was thoroughly discredited. Regarding the military's decision to stand by and delay one of the most anticipated coups in Argentine history, one military officer observed "better a minute too late than a minute too soon" (Jordan, 1977, p. 59).

<u>Stabilization Under Videla</u>

Following the March 24, 1976 coup, General Videla announced that "he was prepared to do everything necessary to eradicate domestic insurgency and political corruption and to put an end to the country's economic decline and demoralization" (Wynia, 1978, p. 228). The economic conditions present in 1976 and the stabilization measures adopted to counteract these conditions were familiar ones. While recognizing these measures had been tried numerous times with only minimal success, the military government reasoned that the measures "deserved" another chance since they had yet to receive a fair "testing" in past administrations. This time the military possessed not only the power but, more importantly, the will and promised to see stabilization measures through to their conclusion. As a result of this commitment, the stabilization program has been eminently successful. Argentina's international position is the best it has been in three decades: balance of trade is positive and foreign exchange reserves are high; foreign direct private investment is slowly returning; Argentina's credit rating is excellent; and the deflationary stabilization measures have won the praise of foreign bankers and the international financial community.

Domestically, the stabilization program has been even more "successful" than its predecessors in reinforcing inequalities. The inflation rate, which had previously "normalized" around 20-30 percent after the adoption of

stabilization measures, has "normalized" at about 175 percent for the past three years. Working class living standards have drastically declined as real wages fell 44 percent in 1976 and 42 percent in 1977 nearly halving labor's buying power. For having achieved these "successes," Argentina's Finance Minister Martinez de Hoz had been called "miracle man" and the "Wizzard de Hoz."

The military's stabilization program has not merely been confined to the imposition of severe economic costs; Argentina's citizens have had to pay harsh social costs as well. In addition to reversing the economic decline, the military suppressed the trade union movement and unleashed an all out attack to eliminate subversion. To accomplish this objective, the military "resorted to every known strategem of repression" in its anti-guerrilla campaign as "outrage bred outrage, and fear corroded self-restraint" (Stern, 1978, p. 802). In the words of another observer "Argentina today is governed by terrorists in military uniforms who have unleashed a reign of savagery unmatched in the modern history of the Western hemisphere" (Kinzer, 1978, p. 17). The campaign has brought into the vocabulary a new, but foreboding term, desaparecidos, to describe the thousands who have "disappeared" to a world beyond all legal, and human, rights.

The stabilization program implemented by the Videla regime has been most common regarding the nature of the measures taken; it has, however, imposed these measures with

uncommon ferocity and vigor. To support these measures, the international financial community extended loans of $1.3 billion in 1976 to resolve huge balance of trade deficits and impending debt servicing problems.

> Argentina has now been firmly welcomed into the international capital markets. In 1976, with reserves at the Central Bank almost at zero, the maximum maturity on loans was four years, and spreads were above 2 percent over LIBOR in some cases. But times have changed. The Central Bank now holds gross reserves of more than $6 billion. ("How Argentina is Consolidating Success," 1978, p. 25)

Indeed, how the times have changed. The domestic social, economic, and political costs that were required to be paid to achieve this success have been very high. The necessary concurrence of these relationships will be discussed in the concluding chapter.

The Brazilian "Miracle"

While Argentina has won the praise of foreign bankers who readily attribute its rapid economic recovery to the vigorous and sustained application of an orthodox stabilization program, Brazil remains as their greatest achievement. The post-1964 "economic miracle" in Brazil was made possible, in their view, by a sustained commitment to orthodoxy and stabilization, the rationalization of the domestic economy with the international capitalist system, and state sponsored and protected reliance on private and foreign capital. The Brazilian experience provides a third view of the impact of stabilization programs that is a reflection

and at the same time an antithesis of the Peruvian and Argentine experiences.

The Antecedents to the "Revolution" of 1964

The decade that precedes the military coup of April 1964 was characterized by numerous, incomplete attempts to impose stabilization programs, not unlike the experience of Argentina. A major theme of Brazil's economic policy making during this period was one of controlling inflation (Skidmore, 1973) and easing balance of payments crises associated with the onset of the difficult stages of ISI. "There were incomplete attempts at stabilization in 1953-54, 1955-56, 1958-59, 1961, and 1963-64" (Skidmore, 1973, p. 20). During this "democratic" interval between the populist authoritarian Estado Novo and the post-1964 military authoritarian regime, anti-inflationary stabilization programs failed to receive the sustained, firm, and continued backing of the executive. The inherently denationalizing, anti-labor bias of these policies resulted in only short-term commitment to such programs in order to gain immediate access to new credits and foreign capital, and then the jettisoning of these programs in the face of mounting popular unrest.

The on-again, off-again nature of the stabilization programs meant that high rates of inflation continued unabated exacerbating periodic balance of payments crises. The commitment to vertically integrated industrialization placed increasing strains on the export sector and access to foreign capital to finance imports required for this

growth strategy. Payer (1974) asserts that Brazil provides one of the clearest examples of how a democratic political system is unequal to the difficult challenge posed by a growth model that contains this foreign exchange "constraint." The external bias of policies necessary for uninterrupted access to foreign capital conflicts with the internal policies necessary to maintain popular support. None of the presidents during this period were able to reconcile these seemingly mutually exclusive imperatives.

Kubitschek Snubs the IMF

The Juscelino Kubitschek administration, 1956-1961, promised the country "fifty years progress in five." Although his program embraced a concept of "developmentalist nationalism," the major emphasis lay in securing large quantities of foreign investment to stimulate industrialization in basic industries. Foreign investment was given special incentives regarding taxes and profit remittances and import restrictions were liberalized for intermediate and capital goods. At the same time, national businessmen were provided easy credit and continued protection from imports of competing consumer items.

This growth, as in similar models in the region, stressed the combination of foreign capital and imported technology and capital goods which produced almost immediate strains on Brazil's balance of trade position. Balanced current accounts in 1955 and 1956 turned into a deficit position by 1957 and the inflation rate began to accelerate. Recognizing the need for an anti-inflationary stabilization program,

Kubitschek attempted to implement a gradualized program and avoid the necessity of an IMF "shock treatment."

By 1959 the situation was becoming critical and Brazil urgently needed a $300 million U.S. loan that had been negotiated but whose release hinged on IMF approval of Brazil's current stabilization program. Kubitschek was "faced with a choice between continuing the drive to fulfill his targets and the need to constrict the domestic economy to satisfy foreign creditors and Brazilian anti-inflationists" and he opted for the latter (Skidmore, 1967, p. 181).

His rejection of IMF demands won Kubitschek great admiration and praise both domestically and internationally. But the problem of obtaining needed foreign currency remained and was "solved" by short term borrowing at high interest rates from private commercial sources. His success was stopgap at best and since commitment to the growth model remained, Kubitschek's defiance of the IMF merely postponed Brazil's day of reckoning with the international financial community. This proved to be a task to which Quadros, Goulart, and the democratic process would be unequal.

The Economic "Miracle"

The increased class polarization and impending social crisis that occurred in conjunction with a deteriorating economic situation during the early 1960s was the product of sectoral tensions and internal conflicts inherent in the deepening of the industrialization process and the stabilization programs that had been repeatedly applied to pursue

this growth model. Socially, Brazil's political elite, influenced by the hemispheric, cold-war atmosphere in the post-Cuban revolution era, greatly exaggerated the threat of subversion from the left and feared destruction of the "system." Economically, the "system" was indeed in crisis both internally and externally.

> The economic crisis had grown acute since the end of the Kubitschek presidency. By early 1964 Brazil was experiencing a negative per capita growth (-1.5 percent in 1963) and was on the verge of hyperinflation (the annual rate had exceeded 100 percent in the quarter) and default on international debts ($2 billion due before the end of 1965). The policy-making chaos was so great and confidence so low that the crisis could only be met by a government armed with extraordinary powers. (Skidmore, 1973, pp. 4-5)

By 1964, the successful imposition of a stabilization program was required if economic growth were to continue within the framework of the international capitalist system. The ability of a democratically elected regime to carry out the stabilization program demanded by the IMF to resolve Brazil's economic crisis was problematic. The choice, it seemed, was between an authoritarian government capable and willing to impose stabilization policies or rejection of the "system" through a social revolution from the left. Fearing the latter, the middle sectors and national elites allied with the military to "save the system."

In retrospect, it is clear that the social crisis was not nearly as severe as the economic crisis. Although repression was indeed applied, it was neither as brutal nor as extensive as that of the Chilean and Argentine experiences

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a decade later. Consistent with its mandate for economic stabilization, the military pursued a classic, orthodox program which decreased the money supply, cut public spending, froze wages, and devalued the cruzeiro. Following some hesitancy in 1965, the adoption of the Second Institutional Act reinforced the extraordinary powers of the president.

By the end of 1967, inflation was reduced to an "acceptable" level of 31 percent a year; the orthodox fiscal, monetary, and wage policies had served their purpose for the domestic sector. Increased capital inflows, renegotiations of short term debts and the promotion of exports helped strengthen the balance of payments position, thus relieving external pressure on policy makers (Skidmore, 1973, p. 12). The success of this stabilization program, and the failure of previous stabilization efforts is directly linked not only to the regime type that imposed it, but also its institutional unity and commitment to the program.

> In sum, the military governments have enjoyed more "freedom" in policy making because they have repressed certain social sectors, such as labor and the rural masses, whose economic shares have correspondingly fallen. Other sectors, such as the officer corps and foreign investors, who were well placed to pressure the government, have gained. Unlike the anti-Peronist Argentine military of the 1960s, Brazil's military government had the will and the ability to impose a socially regressive policy over an extended period. (Skidmore, 1973, p. 28)

Economic Growth Under Stabilization

Donnelly (1972) contends that the "foreign exchange gap" replaced the "savings-investment gap" as Brazil's

dominant resource gap in the postwar growth model it pursued. This became the principal determinant of external financing requirements and almost all regimes pursued a policy of "determined external indebtedness" as a means of filling the gap. This to a great extent explains the necessity for repeated applications of stabilization programs. It also helps to explain the success of the post-1964 regime in obtaining access to generally unlimited new credits and attracting steady influxes of direct private investment. The persistent, unwavering application of the stabilization program rationalized Brazil's internal and external sectors with the international capitalist system. This gave Brazil excellent credit ratings and, with its large internal market, provided the stability and incentive for direct private investment.

The nature of this "associated dependent development" (Cardoso, 1973; Evans, 1979) most clearly creates the conditions, and problems, associated with the deepening of the industrialization process. This difficult stage of ISI can be seen as the substitution of one kind of import dependence for another--an import dependence that is extremely inflexible because imports are now crucial inputs that fuel the engines of growth, both for internal and external markets. The ISI development process, as experienced by Brazil, must now be geared to satisfy not only the internal market, but also an external market which is a crucial provider of foreign exchange earnings necessary to finance the development process. The development process has produced two serious

problems which Brazil's power contenders must face: (1) the capital-intensive industrialization process is producing consumer goods for a relatively small, exclusive national market; and (2) the country must increase and divesify exports to meet the growing foreign exchange gap. This articulation of ISI, with no compensating structural changes in the economy, results in increased inequalities in income distribution which will tend to inhibit expansion of the size of the market. The inadequacy of the internal market to absorb expanding production and the necessity for greater export earnings gives Brazil no alternative but to expand outward to obtain an external market for their production. This requires a commitment to continued adherence to orthodoxy and stabilization.

Brazil's strategy for financing the economic miracle --external public indebtedness--has not narrowed its structural foreign exchange gap but has expanded it. The adequacy of Brazil's long-run capacity to service its external debt is a function of its long-run ability to generate sufficient convertible foreign exchange to meet its foreign exchange transfer obligations without having to compress imports and lower domestic economic growth rates. This requires a fundamental improvement in Brazil's export-import ratio over a period of time (Donnelly, 1972, p. 116). Persistent deficits in Brazil's current account have been exacerbated by the higher cost of imported oil since 1974.

Financing the "Miracle"

The role of the TNCs in the transformation of Brazil's industrial sector into a relatively modern, industrialized nation has been crucial. Evans (1979) argues that the triple alliance of multinational, state, and local capital has been crucial for the rapid economic growth in Brazil. Industrialization in Brazil was designed not only to satisfy local demand, as in the classic ISI model, but also to stimulate growth by producing for the export sector as an alternative to reliance solely on primary products as major foreign exchange earners.

State capital dominated this triple alliance; state investment grew from 25 percent in 1953-1956, to 37 percent in 1957, and represented 48 percent of total investment by the 1960s (Evans, 1979, p. 93) and continued to grow thereafter. Domestic revenues were inadequate to meet the increased demand for state capital and so Brazil turned increasingly to external borrowing as a means of providing investment capital. The "successful" stabilization program of the mid-1960s paved the way for Brazil's high credit rating within the international financial community and huge increases in foreign indebtedness. There were growing strains on Brazil's balance of payments during the "miracle." Exports were diversified, but export growth was unable to offset the rapidly increasing costs of imports, especially those induced by oil after 1973. External borrowing was used to cover some of these costs, as well as to fund state

investment needs; external indebtedness grew rapidly especially during the 1970s (Table 7).

Although Brazil's external indebtedness was rapidly increasing, the strategy seemed successful. The debt service ratio between 1966 and 1976 remained fairly stable, fluctuating between 13 and 17 percent. During this same period, Brazil's domestic economic growth rate was the highest in the hemisphere. But, in 1977 the debt service ratio jumped to 25.8 percent and by 1979 it was between 50 and 60 percent. Total external indebtedness was between $55 and $56 billion.

The ability of Brazil to continue its present growth strategy fueled by external borrowing and maintain high rates of growth without major changes politically is becoming increasingly problematic. Capital inflows from direct investment and external borrowing can substitute for foreign exchange earnings shortfalls in the near term, but the ability to continue to service the debt and cover private remittances depends on increasing export earnings. As Table 8 shows, Brazil was unable to do so during the 1970s and the beginning of the 1980s shows no change. The trade gap for 1980 is expected to again be between $3-4 billion.

Brazil's "miracle man," Delfim Neto, won a minor power struggle at the beginning of the year regarding how to solve Brazil's mounting inflation, trade deficit, and debt servicing requirements. Delfim Neto's plan, like that which brought him to fame nearly a decade before, was for Brazil to borrow and spend its way out of the situation. But his plan fell

on hard times; external loans were not forthcoming in the amounts Brazil needed and inflation continued to soar near the 100 percent mark.

> The publication of the April trade figures amount to an admission by the Brazilian government that the ambitious economic goals established for this year by planning minister Delfim Neto are no longer feasible. The tacit admission has jeopardised the country's long term strategy and aroused fears among international bankers that Brazil may be forced to default on its foreign debt repayments in 1981. ("Brazil Admits Targets Out of Reach," 1980, p. 1)

The article also indicates that Brazil may use its foreign exchange reserves to provide short-term relief to the situation. However this move would reduce Brazil's creditworthiness at a time when its worsening debt profile is already causing serious concern among international bankers who had until recently staunchly defended Brazil's creditworthiness.

Authoritarianism: The Brazilian Experience

Although the first cracks in what seems to be a very secure and stable regime type may be appearing, a brief look at authoritarianism in Brazil should prove instructive regarding linkages between IMF stabilization programs and the imposition of military-led authoritarian regimes. As pointed out earlier, one of the principle constraints that inhibits successful implementation of stabilization programs is that of popular discontent and demonstrations against these policies. Regimes adopting these policies are generally unable to persuade those most seriously disadvantaged to

bear the costs of stabilization. In Brazil, as in Argentina and Peru, the power contenders had either to respond to popular pressure and cease implementation of stabilization policies or use force to insure compliance. Because the growth model being followed was so dependent on continued access to the international financial system and international trade, the regime had to respond to the IMF's demand for stabilization and remove popular pressures by coercing compliance with these policies.

> Popular mobilization, whether through elections, strikes, or street demonstrations, was sharply curtailed, sometimes by heavy-handed repression. Policy makers were able, for example, to assume that a deliberate policy of depressing real wages would not produce mass strikes, nor would concessions to foreign investment risk giving nationalist politicians bargaining power in a divided legislature, nor would full-cost pricing of government-produced gasoline provoke paralyzing bus boycotts in major cities. Policy makers have not had to worry about the income share going to the lowest sectors of Brazilian society. The suppression of most rural organizations after 1964 removed any effective popular pressure from the countryside. The manipulation of urban labor unions has eliminated any independent source of organized pressure from the urban poor. Given this relative freedom from pressures that might be brought by (or on behalf of) the marginalized masses, policy makers have been free to pursue an economic policy based on the market-oriented high-consumption society of the industrializing Center-South region. (Skidmore, 1973, pp. 26-27)

Skidmore also notes that while the regime has been authoritarian it has always kept the pretense of eventual return to consensual civilian rule. This "pretense" began to be a reality during the past two years. However, Brazil's ability to successfully return to democratic rule will be linked quite crucially to its ability to service the debt

and finance persistent current account deficits. Brazil's continued commitment to orthodox, neoclassic economic policies during the 1970s resulted in high credit ratings despite the continued high rate of inflation and balance of payments disequilibria. Also, an important component of this credit-worthiness was Brazil's relatively low debt service ratio and impressive economic growth rates. Now with the debt service ratio over 50 percent, domestic growth slowing, and inflation near 100 percent, questions are being posed regarding the viability of Brazil's growth plan as currently articulated. Brazil as a "success story" to justify IMF stabilization programs may well prove to be fiction, not fact.

A Brief Look to the Future

Brazil's situation, though containing many dissimilarities, has much in common with the prospects facing Peru. Peru's problems are certainly more serious because at present it does not have the economic and industrial capacity, nor a large internal market that could be "primed" or "stabilized" easily to turn the situation around in the short-term. Its decision to allow the democratic process a chance to deal with the domestic situation and the international financial community may well have disastrous results.

Brazil faces a somewhat similar situation. Since the late 1970s, Brazil's ruling military have experimented with a gradual decompression of the political decision making

process in an attempt to find an acceptable alternative to continued authoritarian military rule. This attempt has been fraught with many problems, from the military's perspective. To the extent that Brazil's external economic position deteriorates and its credit-worthiness becomes more and more suspect to the international financial community, there will be greater pressure for the forceful reimposition of stabilization measures to resolve Brazil's deteriorating international position. The choice between decompression and stabilization may produce a crisis of confidence within the country and an institutional crisis within the military regarding which policy to pursue.

During such a crisis, the Argentine "model" will take on added significance regarding the direction Brazil, and Peru, may be headed. Successful stabilization requires a regime with the ability, and the will, to see the program through. During such a period there seems to be little room for moderation which merely postpones the inevitable; extremism becomes the order of the day. Given the inequality of strength from which the power contenders operate, moderation and consensus seem likely to lose to extremism and authoritarianism.

Notes

[1]The selection of these three countries is not random nor were they chosen as convenient straw men to support the main argument of the thesis. All three have received significant amounts of direct private investment and are among the most heavily indebted countries in the region

(Table 6). All three have had major economic crises during the past several decades which have required the "assistance" of the IMF. The regime types that have interacted with the IMF have varied from consensus based to authoritarian and from "revolutionary" to "reactionary." While arguments can be made for the exclusion of some or all of these countries and the inclusion of other countries, it is felt that case studies of these three countries will provide an adequate basis for the analysis of relations between the region and the international lending organizations and for drawing implications and prospects for the region.

[2]The full definition is ". . . a contender for power will be defined as any individual or group which seeks to have its demands implemented through state machinery, to control the allocation of values for the society through state machinery, or to make a specific source of power legitimate for the society through the exercise of a power capability" (Anderson, 1967, p. 90, emphasis added). Since a power contender can have any one of the three attributes described, and since the first most clearly relates to the IMF and the international lending organizations, it will be the attribute used to define and describe the IMF as a power contender.

[3]Peru's "uniqueness" stems in part from the observation that revolutionary models like Mexico, and military models like Brazil (post-1964), Chile (post-1973), and Argentina (post-1976) have emphasized economic growth at the expense of social justice; and revolutionary models like Cuba have emphasized social justice at the expense of economic growth. Its "uniqueness" is also a function of the fact that a military regime adopted such apparently "revolutionary" programs.

[4]Purchases of weapons systems during the decade have been estimated as high as $1.5 billion. These purchases combined with the military's refusal to hold its own pay in line exacerbated the economic situation and further incensed labor whose wages were periodically frozen and declined in real value. This tends to support Ohlin's (1976) contention that the influx of foreign capital from international loans allows a different expenditure at the margin for current consumption or military spending.

[5]According to Szulc (1978), Finance Minister Silva Ruete grabbed the telephone and called personal friends in a dozen foreign governments. Within hours he had obtained $86 million from Brazil, Spain, Mexico, Venezuela, and the Dominican Republic with no "conditions" and no "feasibility" studies (Szulc, 1978, p. 176).

[6] Rostow dates Argentina's "take-off" as beginning in 1935. He notes, however, that "in one sense the Argentine economy began its take-off during the First World War. But by and large, down to the pit of the post-1929 depression, the growth of its modern sector, stimulated during the war, tended to slacken; and like a good part of the Western world, the Argentine sought during the 1920s to return to a pre-1914 normalcy. It was not until the mid-1930s that a sustained take-off was inaugurated, which by and large can now be judged to have been successful despite the structural vicissitudes of that economy" (Rostow, 1960, p. 38).

[7] The seven administrations and the dates the programs were adopted are: Perón (1952), Aramburu (1957), Frondizi (1959), Guido (1962), Onganía (1967), Perón (1975), and Videla (1976).

[8] The discussion that follows relies heavily on Wynia (1978, Chapter 4).

[9] Wynia, however, disagrees with this assessment and presents his reasons in the paragraphs that immediately follow this quote. However, I think his disagreement is untenable especially following the Videla experience since 1976.

CHAPTER FOUR
DEBT, STABILIZATION, AND AUTHORITARIANISM: THE TIES THAT BIND

The political decision to adopt stabilization measures because of disequilibria in the export sector has almost immediate social and economic consequences, and has eventual political consequences. Even a cursory review of stabilization programs in Argentina, Brazil, and Peru provides three immediate impressions: the similarity of measures adopted, the consistently high domestic sacrifices that are incurred, and the difficulty in forcing those most severely disadvantaged to pay the costs involved.

Who Pays the Costs

The consequences of anti-inflationary programs are felt most immediately by those who are least able to bear the burden of economic sacrifice in the name of stabilization (Epstein, 1978). Wage freezes, corrective inflation, reduction in or higher prices for government services, rising cost of imported foodstuffs purchased with a devalued currency, and high rates of unemployment work to the immediate disadvantage of the working class, peasants, and the marginally employed poor. Income, whose distribution is already skewed to the detriment of the lower classes because of the nature of the growth models being followed, is further redistributed away from these sectors to the upper classes.

Since the lowest classes pay the highest costs initially, protest against the continued imposition of such programs is most immediately felt from these sectors. If these were the only groups that were adversely affected by stabilization measures, the other power contenders might easily unite to force these sectors to bear the burden since the poor possess less persuasive power capabilities. However, the middle sectors and domestic entrepreneurial elites are also greatly disadvantaged by the continued imposition of stabilization programs. The depressed national economy shrinks the already small national consumer market; tight monetary and credit policies strain capital short, "noncompetitive" domestic firms. Foreign capital, TNCs, and national elites with trans-national linkages are relatively advantaged by the policies and absorb bankrupt firms and/or enter the markets these firms have been forced to vacate. The middle class and domestic-oriented elites are opposed to this denationalization process and either withdraw support from the ruling coalition (O'Donnell, 1979) or actively join the lowest sectors in protesting these deflationary, anti-national policies.

Problems in Pursuing Stabilization Programs

The frequency with which stabilization programs have been adopted in the countries studied and the frequency and rapidity with which they have been abandoned give testimony to the difficulty surrounding the enforcement of these policies. Epstein (1978) argues that those without adequate

representation in the government of the day will be the groups "chosen" to pay the price of stabilization. This, however, seems to miss the crux of the problem, namely, no matter what regime type or power contenders impose stabilization programs, the same sectors will be required to pay the costs.

Consensus based, democratic regimes are generally the least able to pursue a program of domestic stabilization because those most adversely affected are members of the most populous sectors upon whose support the consensual coalition was built. Thus, the "democratic" regimes in Argentina and especially in Brazil were forced to quickly abandon these programs or rely on the coercive power of the military to enforce the measures. The consequences of either action, continued economic crisis or breakdown of consensus, led to the supplantation of the "democratic" regime with one more authoritarian.

Even authoritarian regime types built around a coalition of power contenders with the military as the dominant member were often unable to successfully administer and adhere to stabilization measures. The administrations of Aramburu, Guido, and Onganía in Argentina and Morales Bermudez in Peru faced well entrenched and united domestic opposition to stabilization measures. They eventually relented and acceded to the demands of those most seriously disadvantaged rather than resort to the repression required to overcome and eliminate the outward vestiges of opposition.

It was only when the conjuncture of deep social and economic crises produced an authoritarian regime with the will, as well as the ability, on the part of those factions of the major power contenders dominating the coalition, that stabilization programs were "successfully" carried out. This point will be further developed and explored shortly.

The "Logic" of Stabilization

Stabilization programs have been shown to be inherently disadvantageous to the domestic economic sector causing severe domestic economic dislocations with high social costs. The problems to be resolved are rarely corrected, though temporary relief may be obtained. Inflation may be reduced but it remains at persistently high rates; balance of trade deficits may become positive in the short run, but generally quickly return to a deficit position. Yet the orthodox monetarist policies so rigidly adhered to by the international financial community continue to be recommended as necessary to resolve these economic problems. The question is almost begged: why, given their poor track record does the international financial community continue to insist on these fiscal and monetary policies? And why given their inherent anti-domestic nature with high social costs, as well as their poor performance, do diverse regime types in Latin America continue to impose stabilization programs?

The previous two chapters have attempted to provide some insight that may allow some partial, tentative conclusions to these questions; answers that might be subsumed

under the general rubric, its the "logic" of the system. The Bretton Woods international economic order was an agreement struck among the developed, industrial nations of the world with almost no consideration given to nor inputs asked from the underdeveloped regions. The economic principles that underpin this system whether derived from Keynes, Samuelson, or Friedman and the Chicago School are considered rational economic laws. To the international financial community, these "laws" are embodied in orthodox, neoclassic policies and have universal application. "The IMF attributes universality and objectivity to a particular view of the functioning of the world economy and of what ought to be the 'best' situation of the national economies" (Frenkel and O'Donnell, 1979, p. 175).

For their part, the nations of the region, especially those studied in Chapters Two and Three, have adopted growth models that depend quite crucially on continued participation in the international capitalist system as a source of imports of capital goods and technology; as a market for their exports; as a source of foreign capital and credits to finance economic growth and balance of trade shortfalls; and most recently, to service previous debts. These nations have become heavily dependent on these linkages to the international financial system. Thus when economic crises arise from domestic economic inflation, balance of payments deficits, and problems in servicing the debt, power contenders with widely diverse power capabilities interact to develop and adopt a program to resolve the economic situation.

It is from this vantage point that the IMF's ability to function as a power contender comes most clearly into focus. Those who support the IMF and its role within the international financial system argue that the IMF does not impose stabilization measures, rather they are "freely" adopted by the country in economic crisis. And while they are absolutely correct, left unsaid is how these countries "freely" choose these programs. Because the role of the IMF has evolved such that it can legitimately attach conditionality to further extensions of credit, it becomes an active power contender in the domestic political process by seeking to have its demands (stabilization programs) implemented through state machinery through the exercise of a power capability (extension or denial of credits).

The IMF as a power contender is seen most clearly when there is opposition among the major, national competing power contenders, e.g. during the administrations of Frondizi in Argentina, Morales Bermudez in Peru, and Kubitschek in Brazil. Because of the strength of its power capability--technical secretariat of the international financial community and lender of last resort--the IMF becomes the dominant power contender during times of economic crises in the external sector: balance of payments deficits and debt servicing problems. As such, its demands are almost always acceded to which tends to explain why stabilization programs are "freely" adopted by diverse regime types. A few regimes, notably Kubitschek's in Brazil, have rejected IMF demands.

The strength of the IMF's power capability can be seen, however, in the fact that this defiance is short-lived and the national power contenders must eventually reach accommodation with the IMF to continue its participation in the international capitalist system.

A final factor that enhances the strength of the IMF as a power contender is that, unlike domestic power contenders, the IMF only participates in the demand placement portion of the domestic political process. Once an output has been produced which meets its demands, the IMF is able to withdraw from the political process leaving the regime "free" to administer the stabilization program and to respond to feedback from the domestic power contenders disadvantaged by the program. This insulation from the requirement to respond to the adverse national impacts of its programs tends to reinforce the universality of the IMF's world view. It is able to point to the successes achieved in lowering domestic inflation, balance of trade surpluses, and ability to service the debt by those regimes able to carry out the programs. Regimes that abandon stabilization programs because of the intensity of the feedback from domestic power contenders experience continued external economic disequilibrium and are unsuccessful because they did not adhere to the program.

Authoritarianism and Stabilization

Dependent linkages to the international capitalist system reinforced by the nature of the growth models pursued

throughout the region have strengthened the IMF's position as a dominant power contender in the domestic political process. The result has been recurring adoption of stabilization programs despite their adverse consequences domestically and difficulties in imposing them. Epstein (1978) echoes this by arguing that the "idea of a neutral government rationally seeking that policy best suited to fulfill a supposed national interest must certainly be considered one of the principal myths of liberal social theory" (p. 225). These regimes, nevertheless, do "freely" adopt these stabilization programs.

The problem then arises regarding how to carry these programs out. As has been seen, consensual "democratic" regimes are as incapable of pursuing continued, unrelenting application of the shock treatment as are authoritarian regimes whose ideology is intensely nationalistic. These failures have the unfortunate results of not merely perpetuating, but deepening the economic crisis. In a similar manner, the limited application of stabilization measures alienates those sectors that had previously supported the regime. These cleavages become more distinct and opposed as the economic situation deteriorates and the social costs of stabilization rise. The conjunction of deep economic and social crises, as in Brazil in 1964 and Argentina in 1976, results in the imposition of highly authoritarian regimes as a "frightened reaction to what is perceived as a grave threat to the survival of the basic capitalist parameters of society" (O'Donnell, 1979, p. 295).

The "New" Authoritarianism

The imposition of harsh, repressive authoritarian regimes in the Southern Cone of Latin America during the 1970s in the wake of the developmentalist authoritarian regimes of the 1960s led some observers to explain this phenomenon in terms of the corporatist nature of the state in Latin America (Malloy, 1977; Stepan, 1978) or in terms of the "new" authoritarian nature of the state (Collier, 1979). It is the argument of this thesis that the state is not "corporatist" in the region, though some regime types did display corporatist features. Nor is there anything "new" about the authoritarian nature of the state other than the refinement of its bureaucratic, institutional nature as opposed to the "strongman," caudillo nature of authoritarianism in the previous century in the countries under study.

The authoritarian nature of the state derives from the conditions of its insertion into the international capitalist system (Cardoso and Faletto, 1979) and the requirement of the state to oversee the distribution of scarce resources among competing power contenders of diverse power capabilities with no consensual agreement upon the "rules of the game." The transitory experimentation with populism and representative political participation occurred while the interest of the developed countries, being riveted elsewhere, coincided with the easy stages of ISI. This allowed relatively easy demand satisfaction of competing power contenders by the state. The reinsertion of the region into the international economic

order created at Bretton Woods coincided, at varying time periods, with the onset of the difficult stages of industrialization, which was a function of the growth models chosen. The state once again experienced grave difficulties in satisfying the demands of competing power contenders; neither populist "democratic" nor "nationalistic" authoritarian regimes were able to satisfy the competing demands.

The crisis produced by the inability of the state, and the economic growth model, to satisfy competing demands resulted in satisfaction of those demands placed by the most powerful of the contenders on the state machinery, namely stabilization programs. Because of the social and economic costs involved, the only regime type that could satisfy these demands and "successfully" impose stabilization programs was the authoritarian regime.

What sets this "new" authoritarian regime apart from the "old" authoritarian regime is its institutionalization, O'Donnell's (1973, 1979) Bureaucratic-Authoritarian regime. This institutionalization is a product of the same process, "modernization," that was to bring consensual democracy with economic growth. However, the articulation of each country's insertion into the international capitalist system--Payer's (1974) "skeleton"--has generally similar results. Those countries experiencing rapid growth in external public indebtedness, mounting balance of trade deficits, and debt servicing crises combined with domestic social crises experienced the imposition of rational, technocratic

authoritarian regimes committed to the economic laws of orthodox neoclassic policies. The economic, social and political costs involved were not a result of the greed of a "strong-man" of "old" authoritarianism but rather were merely a necessary result of compliance with rational economic laws.

Prospects for the 1980s

Having presented a model that is designed to provide some tentative explanations for the current articulation of the political process in Latin America and its development, one generally desires to use this design to provide some judgments regarding impacts these observations may have regarding future developments in the region. The current articulation of the economic process in the countries studied, the mounting debt servicing problems in Brazil and Peru, and the commitment to development within the current formulation of the international financial system seems to portend the increasing authoritarian nature of regimes in the countries studied.

Peru's hopeful attempt at consensual democratic rule in the face of serious economic problems, continued trade deficits, and huge external indebtedness seems almost quixotic. Barring a fortuitous economic turn around, spurred perhaps by the discovery of oil in large exportable quantities, Peru's democratic regime will likely prove incapable of successfully imposing stabilization measures that will be

required as conditions for further access to desperately needed credits. Economic and social crises are likely to follow and, so too, the imposition of an authoritarian military regime committed to guarantee the imposition of stabilization programs. Like Brazil (1964) and Argentina (1976), the repressive nature of the regime will be a function in large part of the depth of the social and economic crisis preceding its implantation.

Brazil for the first time in a decade and a half is facing serious external disequilibria and a deteriorating credit position. Although Brazil has been consistently experiencing huge trade, and budget, deficits, its excellent credit standing has allowed immediate access to generally unlimited credit. However, Brazil's current, tenuous position is likely to require the reimposition of classic, orthodox monetary and fiscal policies which will probably short-circuit the attempts at decompression and opening up of the political system to representative participation. It may well also produce a crisis within the military institution between the nationalists committed to internal development and the opening up of the system and the internationalists committed to the current growth model and export expansion to finance it.

Argentina's prospects are less than clear. Stabilization has been successful but at very high social costs. Given its narrow base of support (O'Donnell, 1979) and the high social costs paid, opposition which remains sporadic

at present is likely to mount. There may in the near term be a swing further to the right with an even more authoritarian and repressive leadership clique taking control. That this could conceivably happen can be gleaned from the division of the current military regime between the *duros* and the *blandos*. General Videla is the leader of the "soft" faction.

In summary, the elites, military and civilian, who impose stabilization measures called for by the international financial community are like "high priests" at Berger's (1976) *Pyramids of Sacrifice*, and the nation's citizens are their potential victims or beneficiaries.

> Policy makers and theorists together constitute an elite vis-a-vis the great mass of people in society. . . . This elite almost invariably legitimates its privileged position in terms of alleged benefits it is bestowing or getting ready to bestow upon "the people." The elite is the guardian or the vanguard of the general welfare. Insofar as an elite has been affected by some version of democratic ideology, its members also like to see themselves as "spokesmen" for "the masses." The latter are presumed to be afflicted with great difficulty in speaking for themselves or in understanding their own situation, so the elite very kindly performs these functions vicariously. (Berger, 1976, p. 11)

The elites' perception of their role is reinforced by the modernization paradigm and the economic development model to which, in varying degrees, they subscribe. It prescribes that underdeveloped countries must (or will) "replicate the basic steps through which Western societies passed in their ascent from rags to riches" (Berger, 1976, p. 12). Unfortunately this approach to development has been fraught with

repeated economic dislocations, severe internal and external economic crises, and the continued imposition of stabilization programs.

But it is not the paradigm itself that is at fault nor is there an implicit demand for the application of a new paradigm. Berger (1976, Chapters II and III) adequately points out the strengths and shortcomings of both capitalism and socialism and the contending modernization and dependency paradigms. What is important is the rejection of a total, unquestioning, uncritical commitment to either paradigm

> because the theoretical and practical issues are shot through with mythic themes, and without understanding the latter, it is not possible to understand the former. Because there are differences to be made among myths, some of which give life, others of which kill. Because myth fosters total commitment, and people who are so committed tend to be blind to mythologically inconvenient facts and indifferent to the human costs of their mythologically legitimated programs. For all these reasons, "demythologization" is both theoretically and politically important in the area of development. A "demythologizing" approach to the problem of development will, therefore, insist that facts be faced and costs counted. (Berger, 1976, p. 30)

Given the disappointing results of stabilization programs and the pressing problems in the internal and external sectors the "time seems ripe to reexamine the applicability of modern stabilization analysis to the special situation of the developing countries" (Behrman and Hanson, 1979, p. 4). The time, also, is ripe for domestic power contenders to reassess and reconstitute the nature of economic, as well as social and political, linkages with the developed world and the international financial community. Unfortunately

such a view may well be hopelessly idealistic given the strength of the "logic" of international capitalism and the domestic elites who have adopted its principles, as well as its zealous rejection by revolutionary elites who seek to construct a new order.

APPENDIX

TABLES AND FIGURE

TABLE 1

Book value (in constant 1967 dollars) of United States direct private investment, 1946-1978. ($U.S. Million)

Year	Total LatAm	Annual Change	Total World	Annual Change	LatAm/ World
1946	4,494	-	12,649	-	35.5%
1947	5,007	11.4%	13,466	6.5%	37.2%
1948	5,298	5.8%	14,025	4.2%	37.8%
1949	5,915	11.6%	13,789	-1.7%	42.9%
1950	5,994	1.3%	14,921	8.2%	40.2%
1951	5,984	-0.1%	15,132	1.4%	39.5%
1952	6,695	11.8%	17,231	13.9%	38.9%
1953	7,090	5.9%	19,188	11.4%	37.0%
1954	7,320	3.2%	20,663	7.7%	35.4%
1955	7,728	5.6%	22,588	9.3%	34.2%
1956	8,486	9.8%	25,230	11.7%	33.6%
1957	8,160	-3.8%	27,730	9.9%	29.4%
1958	8,316	1.9%	29,244	5.5%	28.4%
1959	8,707	4.7%	32,048	10.0%	27.1%
1960	8,790	0.9%	34,863	8.8%	25.2%
1961	8,781	-0.1%	37,016	6.2%	23.5%
1962	8,962	2.1%	39,602	7.0%	22.6%
1963	9,244	3.2%	43,422	9.6%	21.3%
1964	9,452	2.2%	47,169	8.6%	20.0%
1965	9,813	3.8%	51,544	9.3%	19.0%
1966	9,945	1.3%	55,375	7.4%	18.0%
1967	10,265	3.2%	59,486	7.4%	17.3%
1968	10,722	4.5%	63,152	6.2%	17.0%
1969	10,945	2.1%	66,382	5.1%	16.5%
1970	11,108	1.5%	70,878	6.8%	15.7%
1971	11,418	2.8%	75,812	6.9%	15.1%
1972	11,661	2.1%	80,492	6.2%	14.5%
1973	10,576	-9.3%	81,059	0.7%	13.1%
1974	9,969	-5.7%	80,416	-0.8%	12.4%
1975	10,033	0.6%	76,017	-5.5%	13.2%
1976	10,050	0.2%	80,589	6.0%	12.5%
1977	10,370	3.2%	82,382	2.2%	12.6%
1978	10,964	5.7%	86,373	4.8%	12.7%

SOURCE: Compiled from Department of Commerce (Monthly editions, 1951-1979). Data were generally published yearly in the August or October issues. Nominal figures have been adjusted to constant 1967 dollars using Table B-54 (Economic Report of the President, 1980, p. 265).

NOTE: The Producer Price Index (Economic Report of the President, 1980, pp. 265-269) has been used as a crude proxy for a regional index to adjust nominal regional data to constant dollars. 1967 has been used as the base year for all data in all tables.

TABLE 2

Latin America: Total external public debt, 1955-1978

Year	Total Debt (\$U.S. Million)[a]	Annual Change (Percent)
1955	4,673	-
1956	4,865	4.1
1957	5,402	11.0
1958	6,154	13.9
1959	6,253	1.6
1960	7,007	12.1
1961	8,623	23.1[c]
1962	10,119	17.3
1963	10,991	8.6
1964	11,748	6.9
1965	12,544	6.8
1966	13,096	4.4
1967	14,689	12.2
1968	16,176	10.1
1969	16,750	3.6
1970	17,444	4.1
1971	21,383	22.5[c]
1972	24,904	16.4
1973	27,982	12.4
1974	31,090	11.1
1975	32,885	5.7
1976	40,445	22.9
1977	44,887	11.0
1978	52,929[b]	17.9[c]

SOURCE: 1955-1960 (Avramovic, 1964, Table 5, p. 104); 1961-1970 (IDB, 1973, Table 36, p. 372); 1971-1977 (IDB, 1978, Table 56, p. 457); and 1978 (IDB, 1978, p. 93). All figures adjusted to constant 1967 dollars using Table 54 (Economic Report of the President, 1980, p. 265).

[a]constant 1967 dollars.

[b]estimate.

[c]Percent change may have been distorted by data source change.

TABLE 3

Distribution of U.S. direct private investment by region, selected years. (Percentages)

Year	Latin America	Canada	Europe	Other
1929	46.0	26.7	16.8	10.5
1936	41.9	29.2	17.4	11.2
1943	34.6	30.2	22.7	12.4
1950	37.7	30.4	14.7	17.2
1960	25.6	34.2	20.4	19.8
1970	15.7	29.2	31.4	23.7

SOURCE: Hunter and Foley, 1975, Table 7-1, p. 204.

TABLE 4

Latin America: Composition of the external public debt by type of creditor, 1961-1977. (Percentages)

	1961 -65	1966 -70	1971	1972	1973	1974	1975	1976	1977
Private	46.8	41.2	46.3	47.3	50.4	53.7	55.3	58.2	61.2
Official	53.2	58.8	53.7	52.7	49.6	46.3	44.7	41.8	38.8

SOURCE: IDB, 1978, Table III-23, p. 105.

TABLE 5

Latin America: Loans and grants (in constant 1967 dollars) approved by the United States and Multilateral Institutions, gross disbursements and net disbursements, 1961-1978. ($U.S. Billions)

	1961-65	1966-70	1971-75	1974	1975	1976	1977	1978
Approved	2.0	2.1	2.5	2.4	2.8	3.2	2.7	3.1
Gross	1.5	1.6	1.8	2.0	1.9	2.2	1.5	1.6
Net	.9	1.0	1.1	1.4	1.3	1.5	.8	.5

SOURCE: Adapted from IDB, 1978, Tables III-16, III-19, and III-20, pp. 99-103. All nominal figures have been adjusted to constant 1967 dollars using Table B-54 (Economic Report of the President, 1980, p. 265).

TABLE 6

Latin American countries receiving largest amounts of United States direct private investment and those countries with the greatest external public indebtedness, 1950-1977. (Rank ordered)[a]

	Argentina		Brazil		Chile		Colombia		Mexico		Peru		Venezuela	
	Priv Inv	Debt	Priv Inv	Debt	Priv Inv	Debt	Priv Inv	Debt	Priv Inv	Debt	Priv Inv	Debt	Priv Inv	Debt
1950	5	b	2	b	3	b	7	b	4	b	8	b	1	b
1955	5	2	2	1	3	4	8	5	4	3	7	7	1	6
1960	5	2	2	1	4	4	7	5	3	3	6	7	1	6
1965	4	3	3	1	5	4	7	5	2	2	8	6	1	7
1970	4	4	2	1	6	3	7	5	3	2	8	6	1	7
1971	5	3	2	1	7	4	6	5	3	2	8	7	1	6
1972	5	3	2	1	8	4	6	5	3	2	7	7	1	6
1973	5	3	1	1	7	4	8	5	2	2	6	6	3	7
1974	5	3	1	1	8	4	7	6	2	2	6	5	3	7
1975	6	3	1	1	8	4	7	6	2	2	5	5	4	7
1976	5	3	1	1	8	5	7	6	2	2	6	4	4	7
1977	5	3	1	1	8	6	7	7	2	2	6	4	4	5

SOURCE: Data for U.S. direct private investment in Latin America from Department of Commerce (1951-1979); data for external public indebtedness from IDB (1978, Table 56, p. 457), except for 1955 data which is from Avramovic (1964, Table 5, p. 104) and 1965 data which is from IDB (1973, Table 36, p. 372).

[a]The number for each country represents its position that year within the region with respect to total U.S. direct investment and to total indebtedness.

[b]Data not available.

TABLE 7

Relative annual change in United States direct private investment and external public indebtedness in seven countries, 1961-1977. (Percentages)

	Argentina		Brazil		Chile		Colombia		Mexico		Peru		Venezuela	
	Priv Inv	Debt	Priv Inv	Debt	Priv Inv	Debt	Priv Inv	Debt	Priv Inv	Debt	Priv Inv	Debt	Priv Inv	Debt
1961	40.3	47.2	6.1	-8.1	0.8	37.0	0.7	26.5	4.9	4.0	-1.7	8.8	17.5	7.1
1962	21.0	11.7	7.7	20.2	2.6	13.6	7.0	41.2	4.4	21.7	3.8	44.8	-6.5	-5.0
1963	4.0	0.7	4.6	2.8	1.9	13.0	2.4	14.7	4.8	16.3	-0.9	6.2	-0.1	12.2
1964	5.9	-13.7	-12.4	1.6	2.2	8.4	8.7	15.3	13.5	21.6	3.1	33.3	-1.3	13.3
1965	9.2	4.6	4.4	4.4	1.8	3.8	0.2	8.6	11.0	0.7	7.7	13.3	-6.2	11.6
1966	2.1	-4.4	13.9	5.1	-0.4	13.6	6.4	0.5	3.4	5.4	4.2	30.4	-5.5	-5.0
1967	2.9	5.5	4.8	6.7	2.5	38.5	3.0	12.5	6.0	15.2	18.8	8.2	-3.9	6.0
1968	3.7	3.5	8.7	3.5	6.3	4.6	2.8	10.5	6.1	13.2	1.7	3.7	-0.3	-1.0
1969	2.8	2.3	5.2	14.8	-16.9	2.7	3.4	12.5	6.5	5.0	-3.1	-0.4	-3.2	20.0
1970	1.3	1.5	10.7	-5.1	-13.8	16.8	-1.2	14.1	6.6	8.1	-4.0	4.1	-1.2	12.4
1971	1.6	16.9	7.8	20.8	-6.8	4.3	4.6	8.4	0.5	8.2	-3.6	9.2	-3.1	44.2
1972	-0.8	12.6	18.0	23.9	-17.7	14.6	-4.6	8.9	4.5	10.0	0.0	22.5	-4.4	28.0
1973	-29.6	-10.1	4.1	7.6	-8.3	-8.2	-29.5	4.1	7.6	39.2	8.5	53.5	-35.4	-1.2
1974	-18.8	17.9	12.0	7.5	-73.7	12.7	-16.8	-17.3	1.7	23.2	-13.5	21.2	-30.3	-23.1
1975	-5.2	-2.4	15.2	11.0	-46.0	-6.9	-1.6	1.8	5.5	25.4	29.1	6.4	-2.8	-32.9
1976	15.1	21.7	15.0	24.8	-0.4	-5.5	-2.4	8.5	-10.9	28.7	8.4	35.1	-22.9	122.7
1977	2.5	5.6	2.9	16.3	1.2	2.2	-0.2	3.6	1.9	4.8	-4.2	7.6	19.3	41.4

SOURCES: Data for book value United States direct private investment from Department of Commerce (1962-1979); data on external public debt for 1961 to 1970 taken from IDB (1973, Table 36, p. 372) and data for 1971 to 1977 taken from IDB (1978, Table 56, p. 457). Data adjusted to constant 1967 dollars using Table B-57 (Economic Report of the President, 1980, p. 269).

TABLE 8

Latin America: Selected countries, current account balance (in constant 1967 dollars), 1971-1977. ($U.S. Millions)

	1971	1972	1973	1974	1975	1976	1977
Argentina	- 342	- 194	+ 555	+ 80	- 788	+ 382	+ 716
Brazil	-1436	-1442	-1687	-5127	-4289	-3845	-2680
Chile	- 173	- 402	- 218	- 121	- 345	+ 110	- 248
Columbia	- 389	- 162	- 43	- 237	- 67	+ 121	+ 238
Mexico	- 733	- 782	-1106	-1949	-2481	-2003	- 981
Peru	- 30	- 27	- 204	- 492	- 943	- 700	- 509
Venezuela	+ 76	- 33	+ 708	+3974	+1465	+ 568	-1136

SOURCE: IDB, 1978, Table 42, p. 445. Nominal figures have been adjusted to constant 1967 dollars using Table B-54 (Economic Report of the President, 1980, p. 265).

TABLE 9

Argentina: Inflation rates and balance of trade positions, 1951-1978.

Year	Change in Cost of Living (Percentage)	Balance of Trade Position -- Current Account ($US Million)[a]	Regime with Stabilization Program
1951	27.1	-[b]	
1952	38.1	-[b]	Peron
1953	4.3	+[b]	
1954	3.5	+[b]	
1955	12.5	-[b]	
1956	13.1	-146.7	
1957	25.0	-329.3	Aramburu
1958	31.4	-274.4	
1959	113.9	14.0	Frondizi
1960	27.1	-211.3	
1961	13.7	-573.1	
1962	26.2	-286.2	Guido
1963	25.9	247.6	
1964	22.1	38.3	
1965	28.6	234.0	
1966	31.9	263.0	
1967	29.2	184.0	Ongania
1968	16.2	-47.6	
1969	7.6	-212.0	
1970	13.6	-144.2	
1971	34.7	-343.0	
1972	58.5	-190.3	
1973	62.3	559.8	
1974	92.4	84.7	
1975	89.2	-784.5	Peron
1976	401.8	383.4	Videla
1977	173.8	729.8	
1978	175.5	1233.3 (est)	

SOURCES: Change in Cost of Living data, 1952-1972 from Epstein (1978); 1951 and 1973-1978 data calculated from IDB (1978) and IMF (1957). Balance of Trade data 1956-1978 from IMF (1957-1979); relative data for 1951-1955 from Wynia (1978). Nominal balance of trade figures adjusted to constant 1967 dollars using Table B-54 (<u>Economic Report of the President</u>, 1980, p. 265).

[a] In constant 1967 dollars.

[b] Data not available from sources consulted. Positive or negative sign indicates relative balance of trade position for that year.

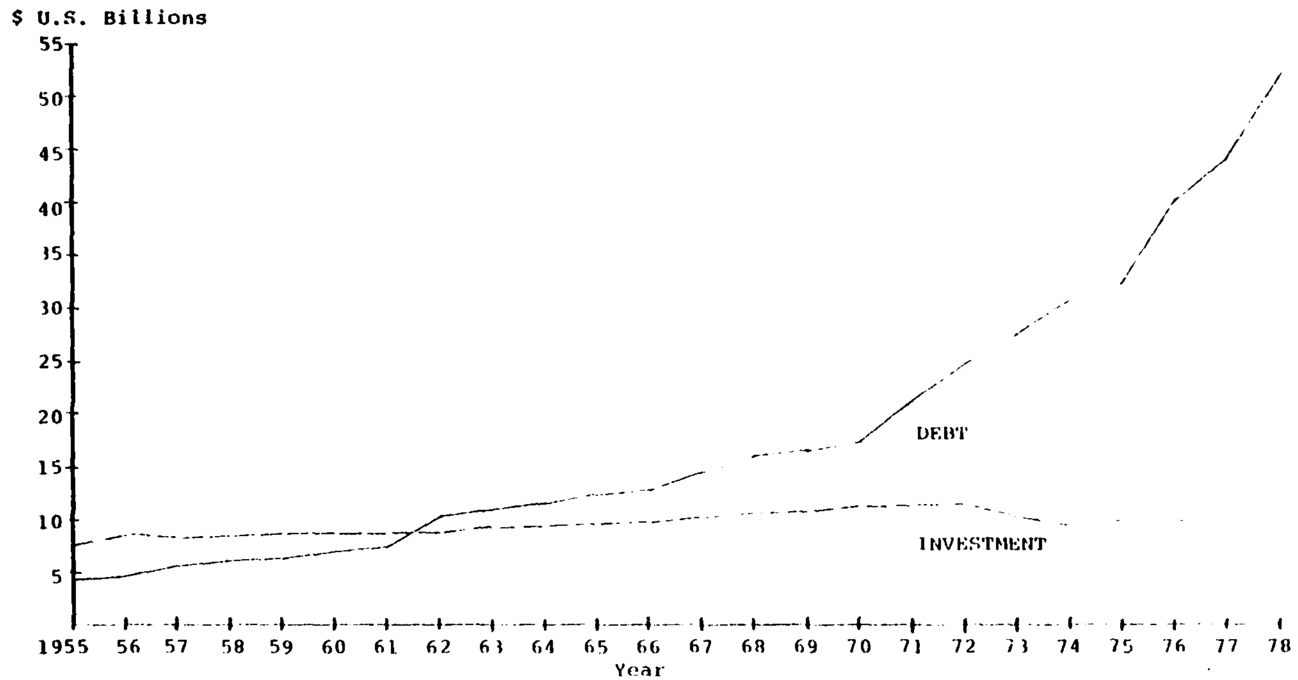
TABLE 10

Argentina: Major policy options adopted by administrations implementing stabilization programs, 1950-1980.

	Administrations						
Policy Options	Peron	Aramburu	Frondizi	Guido	Ongania	Peron	Videla
Freeze Wages	X	X	X	X	X	X	X
Eliminate Price Controls		X	X			X	X
Stringent Monetary and Credit Policies	X	X	X	X			X
Reduce Public Expenditures	X	X	X				X
Devaluation		X	X	X	X	X	X
Access to Foreign Capital	X	X	X	X	X		X

SOURCE: Compiled from Wynia (1978).

X: Indicates policy adopted.



Latin America: Relationship between total regional external public debt and total U.S. direct private investment in Latin America in constant 1967 dollars, 1955-1978 ($U.S. Billions).

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I certify that I have read this study and that in my opinion it conforms to acceptable standards of scholarly presentation and is fully adequate, in scope and quality, as a thesis for the degree of Master of Arts.

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