

# CEPAL

## Review

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UNITED NATIONS  
ECONOMIC COMMISSION FOR LATIN AMERICA AND THE CARIBBEAN

SANTIAGO, CHILE, DECEMBER 1990

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Three dots (...) indicate that data are not available or are not separately reported.

A dash (—) indicates that the amount is nil or negligible.

A blank space in a table means that the item in question is not applicable.

A minus sign (-) indicates a deficit or decrease, unless otherwise specified.

A point (.) is used to indicate decimals.

A slash (/) indicates a crop year or fiscal year, e.g., 1970/1971.

Use of a hyphen (-) between years, e.g., 1971-1973, indicates reference to the complete number of calendar years involved, including the beginning and end years.

Reference to "tons" mean metric tons, and to "dollars", United States dollars, unless otherwise stated.

Unless otherwise stated, references to annual rates of growth or variation signify compound annual rates.

Individual figures and percentages in tables do not necessarily add up to corresponding totals, because of rounding.

LC/G. 1642 - P
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December 1990
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UNITED NATIONS PUBLICATION
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ISSN 0251-2920
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ISBN 92-1-121168-9
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Printed in Chile

# CEPAL

## Review

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Santiago, Chile

Number 42

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## The early teachings of Raúl Prebisch

*Aldo Ferrer*

This article recalls two periods in the author's relationship with Prebisch. The first relates to Prebisch's teaching at the University of Buenos Aires in 1948, and the second to his work as economic advisor to the Argentine Government that followed the overthrow of Perón in 1955.

As a result of his disagreement with traditional economic thought, Prebisch, in his capacity as a shaper of Argentine economic policy in the 1930s, searched for solutions to the problem of the massive imbalance in external payments. To do so, he had to break new ground in matters of fiscal, foreign-exchange and monetary policy. In this effort, Prebisch was one of the first economists to recognize the Keynesian revolution and make it known in Latin America. On the basis of these ideas, he developed a point of view concerning industrialization and State intervention in foreign-exchange operations and other markets.

In 1955 the set of proposals which he presented to the new Argentine Government was called the Prebisch Plan. In the new circumstances, Prebisch's first concern was to restore macroeconomic balances through an adjustment process. These short-term proposals encountered considerable resistance in Argentina, a country in which both images of Prebisch are still remembered today.

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Raúl Prebisch was my Professor of Political Economy at the University of Buenos Aires in 1948. From that time until the end of his life, I maintained a friendly and warm relationship with my former teacher, although it was not without disagreements concerning Argentine economic policy. In this article, I recall two periods in my relationship with Prebisch: his early teaching at the University of Buenos Aires and his work as economic advisor to the Argentine Government after the overthrow of Perón in 1955.

When classes began in the academic year of 1948, the story spread through the Economic Sciences Department of the University of Buenos Aires that Raúl Prebisch would be teaching Economic Dynamics again. He had withdrawn from teaching when he resigned as the General Manager of the Central Bank after the military coup of 1943. Prebisch's return generated an air of expectancy. Most of us students felt a visceral opposition to the conservative regimes which Prebisch had served in important posts. Nevertheless, his academic prestige placed him above the vicissitudes of political life.

On the first day of classes, in mid-March, Prebisch entered the small lecture room at the intersection of Avenida Córdoba and Junín, facing the present site of the Professors' Hall. That day I watched the arrival of a fine-looking man, head erect, of medium height, in his mid-forties. His dark suit, white shirt and pale tie gave him an elegance that matched his demeanour. He stepped up onto the podium, looked out over his audience and began in a firm and steady voice: "Gentlemen, today we shall start a course in which I propose to present to you my ideas about the behaviour of the economic system under present-day conditions."

Simultaneously with the course, Prebisch conducted a seminar which gave students a greater opportunity for dialogue and closer acquaintance with the Professor. In the first meeting of the seminar, Prebisch put a question to the students. He began by saying that he was profoundly disillusioned with the neoclassical thought prevalent in academic circles at the time, with its interpretation of problems and with its principles of economic policy. Then he asked: "To what do you attribute this reaction of mine to traditional economic thought?" The students remained silent for a few moments. Watching the Professor's look of expectation, I found the courage to reply: "Doctor", I said, "the reason must be that kind of thought does not help solve the problems of

the real world". Prebisch looked at me and answered: "Exactly, that's right." He went on to discuss the problems he had faced in shaping Argentine economic policy during the 1930s, especially in the management of the Central Bank. He explained that the conventional approach was incapable of responding to the consequences of the world crisis and its impact on the Argentine economy. Then, tentatively and without a theoretical frame of reference, he proceeded to search for the fiscal, monetary and foreign-exchange policy answers that would help in resolving the severe imbalance in external payments caused by the collapse of the buying power of exports and the marked decrease in production and employment. In practice and throughout this search, Prebisch promoted and applied compensatory policies which would prove to be pioneering ideas at about the same time by a Professor at Cambridge whose theoretical foundations were being laid down. Prebisch was one of the first economists to take note of the Keynesian revolution and disseminate it in Latin America.

At the end of each meeting of the seminar, Prebisch left the Department and walked toward the corner of Callao and Charcas, the former site of our school. Don Raúl was always a great one for walking. Among the factors that explained his excellent health, he included walking, a form of exercise to which, years later, aerobic functions would be attributed. Prebisch knew this instinctively without the aid of the theories of Dr. Cooper and other specialists in the subject. I accompanied Prebisch many times on those walks.

One of the assignments in the seminar consisted in preparing brief monographs. My first academic work in economics was assigned by Prebisch and consisted of a commentary on Fritz Machlup's book on the multiplier effect in foreign trade. The Professor liked my work and remarked: "You have a considerably larger vocabulary than most economists, whose knowledge of language is rather mediocre." Prebisch always maintained a justified concern with questions of style. The clarity of his own language helps to explain the impact of his ideas. His works can be understood. This is more than can be said for the intellectual products of a good many of his colleagues, who surround the discipline with frequently sterile exercises reserved for the experts.

At mid-year, the course and the seminar ended. Shortly thereafter, the Government again barred Prebisch from teaching. Thus ended his teaching

career at the University of Buenos Aires. Prebisch then sought new horizons abroad which later established him as the most famous economist of Latin America and of the developing world.

The ideas which Prebisch disseminated in his writings through ECLAC were first put forward in organic fashion at the University of Buenos Aires in 1948. It is no accident that the renovation of economic theory in Latin America was begun by an Argentine economist. Towards the end of the 1940s our country was the most advanced in the region. With its natural and human resources, by 1930 Argentina's economy had achieved the highest levels of income and international participation. Seventy years of growth linked to the world market had made it possible to involve most of the active population. The style of outward-looking growth had reached its highest level of development in Argentina during the years before the crisis of the 1930s. Its financial system was the most sophisticated, and when the crisis came, its capital market was more developed than that of any other Latin American country.

Towards the end of the 1920s, exports accounted for about 25% of GDP, and imports for a similar share of the total demand. Such a high degree of international involvement made Argentina highly vulnerable to changes in world market activity levels and especially to changes in the hegemonic Power to which Argentina was closely tied. That instability, resulting from the economic cycle in the United Kingdom, inevitably attracted the attention of so acute an observer as Prebisch. Other features of the Argentine experience would also be decisive in shaping his main ideas.

When the crisis came, Argentina was a sub-industrialized country, to judge by the low ratio of manufacturing activity to per capita income and population. Even so, there was considerable diversity in the country's productive structure and a high level of ability in its human resources. The development achieved in the country's energy, transport and communications infrastructure, in the industries that processed commodities for export (refrigeration plants, mills, etc.), in the machine shops, support services and support manufacturing for the country's stock of capital goods, together with the rather sophisticated services available in a society with a high average income, constituted an abundance of human resources and a productive system which were capable of more complex undertakings. At the same time, there were imports which could easily be

replaced with national products in the textile industry, food processing, light machinery and chemical enterprises and other areas requiring relatively simple technology and low-intensity capital.

On the global scene, at that time, the most important economies were following strongly interventionist policies and assigning to the State responsibilities previously unknown in the prevalent liberal pattern. In the case of Argentina, the military coup of 1930 and the conservative regimes imposed through fraud and through the exclusion of majority political expression made it possible to suppress the struggles over distribution and to respond without much trouble to the conflicts arising from the initial process of import substitution.

In this setting, one can readily understand the viability of a process of industrialization based on the domestic market and reductions in the import coefficient and, at the same time, the feasibility of keeping conflicts concerning distribution under control, while maintaining macroeconomic balances. Optimism about the prospect of transforming reality through public policy and of bringing about change in the behaviour of participants in social action was possible in that context.

This message of confidence in our own capacity to understand the world and change it helps to explain the widespread acceptance of Prebisch's early ideas and, later, of the ECLAC model.

That was the scene. And what kind of man was the man acting in it? First of all, he was a clear-headed man, with a profound vocation for analysis, willing to understand the reality around him in terms beyond conventional theoretical clichés. Moreover, Prebisch had a rich store of operational experience. This produced a distinctive stamp of his career: understand in order to act. Constantly and uninterruptedly, he moved forward from theoretical ideas to the conclusions needed to make proposals for economic policy. From the 1920s on, he distinguished himself as an astute analyst. In the 1930s, he held important economic policy posts, culminating in 1935 with his assignment as General Manager of the recently formed Central Bank. These personal traits and this experience constituted the personality of the professor who, on that mid-March morning in 1948, began his discourses in the Economic Sciences Department of the University of Buenos Aires.

What were Prebisch's reservations about the neoclassical model and its interpretation of tendencies in the real world of the early post-war period? What

conclusions were to be drawn from the depression of the 1930s which brought about the collapse of the international economic order and ultimately led to the Second World War? What were the implications of the theoretical revision he set in motion?

Until the crisis of 1930, the neoclassical approach had prevailed in Latin America. It guaranteed the balance of international payments with optimum use of available resources so long as free-trade policies were maintained. Freedom in trade and international payments made possible the exploitation of the comparative advantages arising from the availability of resources and ensured a balance in prices, interest rates and exchange rates. Any deviation due to imprudent policies that increased domestic credit and public spending brought about a drop in international reserves, a shrinking of the monetary base, a rise in the interest rate, a drop in demand and, eventually, the restoration of balance. If the initial deviations were caused by a change in international conditions for example, a drop in export prices the economy would follow the same course of adjustment. The system made it possible to absorb changes in the real income of productive factors and to maintain the stability of overall price levels.

The initial effort to respond to the extraordinary events brought on by the global crisis of the 1930s with that theoretical scaffolding produced a disaster. The collapse of world trade and the crisis of the financial markets generated an imbalance in international payments which proved to be unmanageable with conventional policies. Attempts to recover the lost balance through reductions in spending accelerated the collapse of production and employment. The resulting reduction of imports was insufficient to offset the violent drop in exports. With the notable exception of Argentina, the crisis in international payments made unilateral decisions to declare foreign-debt moratoria the rule in Latin America.

The 1930s burned into the collective memory of the region the conviction that the crisis of that decade was not merely another phase of the economic cycle. In Argentina, since the mid-1930s, attempts were made through foreign-exchange, fiscal and monetary policies to compensate for the impact of the contraction in exports and capital inputs on domestic demand, production and employment. Moreover, Keynes's theoretical revision, the policies of the New Deal and the expansion of State intervention aimed at

remedying the consequences of the crisis were gaining influence in the region. Protectionism and foreign-exchange controls became the general practice in industrialized countries. In Germany and Italy the crisis swept away theoretical models and conventional policies and also wiped out democratic systems.

The Second World War provoked further disruptions in Latin America. The interruption of imports from traditional sources brought about the forced isolation of the region's economies. Import substitution was dictated by events. Each national economy responded on the basis of its previously accumulated industrial and technological capacity, the size of its domestic market, the response capacity of the public sector and the maturity of its private sector.

When the war ended, 15 years of considerable transformations in the economic structure and international participation of Latin America had elapsed. In the rest of the world, the post-war reconstruction of Europe and Japan was based on protectionist policies and on regulations controlling foreign trade and international payments. The sphere of State action was broadened through the nationalization of enterprises within the financial sector and through income policies based on price and wage controls.

By the end of the 1940s, the neoclassical theoretical structure that had been predominant in Latin America from the mid-nineteenth century until 1930 was in ruins. With the collapse of theoretical models, traditional policies became discredited. At that time the region lacked a theory of long-term development and short-term balance. The gold standard, free trade, limits on State intervention and respect for the virtues of market laws could not withstand the onslaught of the 15 years that began in 1930 and ended with the end of the war.

The way was open to search for new solutions to the problems of development and balance. Prebisch's greatest contribution lay in his decision to understand these problems from our point of view that is, on the basis of the reality of what he defined soon thereafter as the peripheral countries. Traditionally, the economic universe had been studied according to theories generated in the centres of the international system. This hindered our understanding of our own reality and, consequently, the discovery of valid solutions to the problems of growth and stability. The cost of operating with borrowed ideas during the

crisis years had been overwhelming. That error was not to be repeated. When, beginning in the 1970s, orthodox monetarist thought again became predominant in Latin America, the accuracy of Prebisch's ideas became evident once more.

In 1948 Prebisch was engaged in explaining the behaviour of the terms of trade between the export of basic commodities from the periphery and the export of manufactured goods from the centres. In his judgement, this was the principal factor that shed light on the distribution of the fruits of technological progress throughout the world economy. The cause that explained the phenomena lay in the fact that manpower was more plentiful in the periphery than in the centres. For that reason, in industrial countries the increases in productivity generated by technological progress were held back by productive factors through real wages and earnings. In the periphery, on the other hand, those increases were transferred to buyers through the relatively lower prices of exports. The inability to increase employment to the same real-wage levels kept labour from sharing in the fruits of technological progress. This unequal relationship between centre and periphery cast doubt on the validity of the neoclassical model. At the same time, it revealed inequities in the distribution of the benefits generated by the international division of labour and by the comparative advantages resulting from the relative abundance of productive factors.

Moreover, the gold standard and the free circulation of capital subjected periphery countries to the effects of ups and downs of the economic cycle in the industrial centres. The gold standard made the periphery impotent in the face of variations occurring in the central economies of the system. In those circumstances, the process of adjustment was painful and imposed high economic and social costs on the periphery countries.

If this was the behaviour of the global economy, free-market policies caused long-term economic stagnation and short-term production and employment instability in the periphery. The frontal challenge to these consequences of market dynamics led inevitably to a rejection of the free-trade model and to the creation of an alternative economic policy. Since specialization in the production and export of basic commodities was incompatible with domestic retention of the fruits of technological progress, it was necessary to create other productive activities and sources of employment. In other words, industrialization was necessary. At the same time,

given that the free movement of capital and freedom in exchange rates brought about an adjustment process with high economic and social costs, it was also necessary to regulate both the exchange market and the movement of funds between Latin America and other regions.

All this had, in fact, been happening since the 1930s. These were the ad hoc policy responses of a number of Latin American countries to the problems arising from the global crisis. But according to Prebisch's revision of theory, these policies were no longer of a transitory nature, to be maintained until "normality", that is, the neoclassical universe, could be restored. Instead, since that time, industrialization and State intervention in international foreign-exchange and in other markets became central economic policy objectives and instruments. From being temporary emergency measures, they had become policies aimed at transforming the country's production system and its participation in the international economy by means of direct political intervention in the allocation of resources.

These early measures provoked a chain reaction. If industrialization was to assume the leadership position in development, it was necessary to study what had been done in other countries whose industrial development had come much later than that of the United Kingdom, the leader of the first industrial revolution. The experience of the United States, Germany, Japan and other countries was revealing. In every case, industrialization had been supported by protection of the domestic market and its reservation for the country's own industrial production. Moreover, State intervention had not been limited to the imposition of restrictions on imports that would compete with domestic production. It had also included other support instruments, in particular the financing of capital formation.

Consequently, it was necessary to base industrialization on the domestic market and to extend public measures to a number of areas whose activities were aimed at the same target of industrialization. In that way, beginning in the late 1940s, inward-looking growth was supported by convincing theoretical arguments and, in some countries, by policies which were increasingly divergent from the free-trade model.

The evolution of economic policy in the main economies of the region reinforced tendencies that had been observed since the 1930s. The State

emerged as a leading participant in the development process, intervening in three main areas: first, by raising tariffs and implementing trade controls and other import restrictions in order to reserve the domestic market for domestic products and to make import substitution viable; second, by improving transport, communications and energy infrastructures through increased public investment and the creation of State companies in those areas and, increasingly, in certain other basic industries requiring large capital investment; third, by applying subsidies and, especially, by manipulating relative prices in favour of growth industries. By the end of the 1940s, the principal economies of the region were armed not only with a theory to justify public intervention in the promotion of industrialization and the transformation of productive structures but also with an interventionist arsenal that exerted a powerful influence on the functioning of markets, the determination of production and income, foreign trade, capital formation, relative prices and income distribution.

Prebisch's teachings at the University of Buenos Aires were optimistic in content. The efforts at development and the international context posed serious challenges, but those could be faced successfully on the basis of a clear diagnosis rooted in our own interpretations of reality.

After Prebisch left the University, I did not see him until we met in early 1950 in New York, where I was working at the United Nations Secretariat. At that time Prebisch was negotiating his transfer from the Studies Directorate of ECLAC to the leadership of its Executive Secretariat. The United Nations Secretariat was at that time one of the powerhouses of new development theories and had on its staff such eminent economists as Michael Kalecki and Hans Singer. The latter, together with Prebisch, later sponsored the theory of the secular tendency towards deterioration of the terms of trade of basic commodities. In New York I followed ECLAC's pioneering research closely and published my first studies. One of these, relating to real wages and income distribution, was produced in collaboration with the Mexican economist Horacio Flores de la Peña, member of Kalecki's team. The most important ECLAC economists often visited the Secretariat, and on those occasions I established my first friendships and intellectual ties with Celso Furtado and other eminent Latin American economists.



In early 1953 I resigned my post at the United Nations and returned to Buenos Aires. I became involved in politics as a member of the Unión Cívica Radical, whose National Committee had as its Chairman a rising and talented young politician named Arturo Frondizi. Those were the last days of the first Peronist Government. The regime was collapsing, exhausted by the conflicts generated by its own policies and by the divisions existing in Argentine society.

Within the party, I served as economic advisor to the National Committee and the group of national representatives led by Oscar Alende. Some other members of our advisory team were Norberto González, Federico Herschell and Samuel Itzcovich. We prepared various papers in support of the critical positions taken by the Radicals. From the standpoint of the theoretical model emerging in Latin America at that time, we criticized the irrationality of the Peronist income policy, the lags in investment, the inadequate development of infrastructure and basic industries, the actions taken against export activities and the Government's promotion of foreign-capital participation in the petroleum industry and other sectors. In other words, we were criticizing Peronism for being inconsistent with a number of its initial proposals for change. That criticism was made within the context of a rejection of Peronism's violations of democratic legality. Our approach represented the "national and popular" positions embodied by Radicalism in the Avellaneda Declaration of 1947. One of the main exponents of that line of thought was Frondizi himself, whose book *Petróleo y Política* was part of the anti-imperialist and progressive current.

These references are relevant to my second recollection of my relationship with Prebisch. In September 1955 Perón was overthrown, and shortly thereafter the new Government, known as the Government of the Liberating Revolution, summoned Raúl Prebisch, who was Executive Secretary of ECLAC at that time. Prebisch agreed to serve as economic advisor without assuming any executive responsibilities. During the final months of 1955 he prepared a number of reports which he submitted to the authorities and which became the subject of vigorous public debate. The first was *Informe preliminar acerca de la situación económica* ["Preliminary report on the economic situation"]. Later, he submitted two other papers: *Moneda sana o inflación incontrolable* ["Sound money or uncontrolled inflation"] and *Plan de restablecimiento*

*económico* ["Plan of economic restoration"]. That set of ideas and proposals was referred to at the time as the Prebisch Plan.

Prebisch's return to the field of Argentine economic policy occurred in circumstances very different from those he had faced previously as the principal participant in the country's economic management during the 1930s and up to the military coup of 1943. The situation was very different for various reasons. In the first place, the problem of development was more complex than at the time of the collapse of the primary export model. The balance-of-payments crisis was primarily due not to a reduced capacity to cover foreign debts as a result of a shrinking world market but to the structural deficit arising from industry's orientation towards the domestic market and its dependence on traditional farm-export earnings. By 1955 industrialization, growth and foreign balances were considered in terms very different from those that Prebisch had known up to 1943 as administrator of economic policy. In the second place, the country's social and political realities had changed radically. The social forces unleashed by Peronism since the mid-1940s defined the struggle over distribution and short-term policy management in terms that were more complex and more difficult to deal with administratively than in the past. Political instability had brought a radicalization of positions. The traditional Right tied to farm production intended for export, exerted powerful pressures for the modification of relative prices in its favour, mainly through devaluations of the currency. At the same time, workers and other urban sectors sought to increase their share of overall income through an increase in wages and in the margins of industry and services profit. By 1955, the price-wage-devaluation spiral had generated conditions that later came to be known as inertial inflation. Lastly, the State which Prebisch found in 1955 was not the one he had left in 1943. It was much larger, intervened powerfully in income distribution and resource allocation and suffered from a chronic tendency towards imbalance.

In those circumstances, Prebisch's first concern was to re-establish macroeconomic balance or, in a well-known phrase, to put the house in order. That was indeed a necessary condition for the realistic renewal of development strategy after the overthrow of Perón in 1955. It is understandable that his proposals encountered resistance from popular

sectors, which felt aggrieved by the adjustment strategy, and from the Right, which rejected the ideas for transformation and industrialization that Prebisch had popularized in his leadership position at ECLAC.

The Unión Cívica Radical adopted a critical position with respect to Prebisch's programme. We, the young economic advisors to the National Committee and to the party's representatives in the Junta Consultiva, whose chief delegate was Oscar Alende, prepared various studies which provided data and arguments for the party's spokesmen. Prebisch's approach seemed to us to be very conservative, with excessive emphasis on foreign adjustments, price stability, the virtues of foreign capital and the freer play of market forces. We also criticized the gaps we detected in structural and social questions and in others that would strengthen Argentina's position in the face of foreign interests.

Don Raúl was perplexed by the criticism coming from those who had been his disciples and the followers of his main ideas in theoretical matters. We dared to suppose that, when he returned to Argentina to concern himself with the concrete and urgent problems of the nation's economy, he became once again the old conservative-regime functionary of the 1930s, with his old friends and his predominant interests in monetary and balance-of-payments questions. At the same time, it was true that traditional conservatives also rejected the ideas he had developed and promoted in Argentina and throughout Latin America. Prebisch's positions on the short-term management of the Argentine economy, a question to which he returned several times during the years following 1955, reawakened the doubts of both his disciples and other economists who recognized in him a pioneer of new ideas about development. While in the rest of Latin America and in the third world Prebisch is viewed as the main exponent of reform thought, in Argentina his image retains more complex and contradictory nuances.

Shortly thereafter, I was assigned to the Argentine Embassy in London as an economic advisor, and in mid-1956, I was a member of the

Argentine delegation to the United Nations Economic and Social Council in Geneva. Prebisch was there, having returned to ECLAC after leaving his post as economic advisor to the revolutionary Government. We spoke at length about the events of the past year and the critical position taken by the Radicals. Prebisch was particularly concerned about the criticism from the "progressive" camp. I tried to explain that Radicalism was seeking a new synthesis for integration with the popular forces of a defeated Peronism and an economic policy model far removed from orthodox recipes and based on "national and popular" proposals. This naturally implied short-term unorthodox management which, even if one recognized the need for fiscal balance and monetary prudence, was far removed from the emphasis Prebisch had placed on the adjustment process and the reincorporation of Argentina into international financial circles. Of course, I did not convince him. When his mission in Geneva ended, I went to the airport to see him off. I found him eating an excellent luncheon. When he had finished with good wine and a variety of cheeses, he asked for coffee and -of all things- saccharine! When he saw my smile, he said, "Don't laugh. Saccharine, like confession for Catholics, wipes away sin".

In 1959, while I was serving as Minister of Economy and Finance in the Alende government of the Province of Buenos Aires, I met Prebisch again. Towards the end of the preceding year the Frondizi Government had signed an agreement with the International Monetary Fund and was pursuing an orthodox fiscal and monetary policy. There was great displeasure in the ranks of intransigent Radicalism. When we met in Buenos Aires, Don Raúl chided me: "Tell me, my friend, can you explain to me now why you criticized my proposals?" At that time, I found it difficult to answer. From a historical perspective it could be said that those decisions taken by Frondizi and Rogelio Frigerio were part of what would be described today as a "capitalist shock" for accumulation and growth, but that is a different question altogether.