The ideas of young Prebisch

Adolfo Gurrieri

1. Introduction

Prebisch arrived at ECLA for the first time in 1949, to write a report in which he set out his views on the main problems then facing the economic development of Latin America (Prebisch, 1949). As he had been hired as an outside consultant, he did not receive the support of other members of the institution in its preparation, nor did he have much time at his disposal, so that the report was a reflection of the ideas he already held prior to joining ECLA. As the content of that work made a great impact on academic and political circles in the region and came to be considered one of the basic pillars of structuralist thinking, it has often been wondered when and why Prebisch incorporated those ideas into his thinking.1

In 1949 Prebisch already had a lengthy career as an academic and public official behind him and was, according to Furtado, “the only Latin American economist with an international reputation” (Furtado, 1985, p. 58). His first works date from the 1920s, and the general opinion is that in those years he was a firm supporter of neoclassical ideas, but there is very little in them that could have served as a basis for the 1949 report, and only as a result of the crisis that began in 1929 does he appear to have begun to abandon his neoclassical views and to look for new interpretations of the economic process and heterodox policies for reshaping it.2 The fact that Prebisch often confirmed this simple division of his thinking into two periods must have been one of the main reasons why this was accepted without question and a deeper study was not made of his thinking in the 1920s (Prebisch, 1983).

Attentive reading of the material he wrote during those years, however, shows that the continuity of his ideas was much greater than has been assumed, so that it would be very simplistic to divide the evolution of his thinking into two periods—orthodox and heterodox—separated by the 1929 crisis. Prebisch himself, when going into greater detail, recognized that the 1920s had not been a period of pure orthodoxy for him. For example, when referring in an interview to the first articles he had written, he said “In those articles I tried to interpret actual phenomena with my own eyes, and not with economic theories from outside. I attached

---

1 This question is different from another one which is also important but is not considered in this article: whether those were original ideas of Prebisch or not, and what sources they came from. See in this respect Love (1994 and 1999).

2 “When Prebisch began his career as an economist and professor, in the late 1920s, he was an ardent supporter of neoclassical theories. The Great Depression of the 1930s—the first great crisis of capitalism—was the prime cause of Prebisch’s conversion” (Sprout, 1992, p. 188). Similar opinions may be found in many other authors.
great importance to the balance of payments... I began to understand Argentina’s external vulnerability at that moment. This was between 1921 and 1923" (González and Pollock, 1991, p. 458). The fact that Prebisch often confirmed this simple division into two clearly opposed periods must have led those who have studied his thinking to take this for granted, with the already mentioned result that they did not study his thinking during the 1920s in greater depth.

The aim of this article, therefore, is to show that even from his first works, written in 1920, Prebisch began to shape the body of ideas that he formulated as a whole when he arrived at ECLA in 1949, and also that he did not need to go through the experience of the 1929 crisis in order to become aware of the defects of the primary export pattern, since these had already been clear to him even in the early 1920s, when the Argentine economic process was considered a shining example of successful growth. The brutal impact of the crisis merely served to confirm to him that he had not been mistaken about those defects and to lead him to definitively abandon his confidence in the Gold Standard as a basic criterion for economic policy management and seek new ways that would permit an improvement in the standard of living of the population.

2. The main ideas put forward in the 1949 report

The origin of the main ideas put forward in the 1949 report could hardly be traced back without first of all recalling them here, albeit in an extremely summary manner. In that report, Prebisch laid down the main lines of a strategy for promoting the economic development of Latin America, understood as a process designed to raise the standard of living of the population through a systematic increase in productivity. His main thesis with regard to the orientation of that strategy is that it could not be successful if economic activity were concentrated around the production of primary commodities and their export to the industrial centres, so that it was essential to promote industrialization. The primary export pattern had of course lost its dynamism as a result of the difficulties caused to international trade by the great crisis and the Second World War, and although the most negative effects of those events were coming to an end, Prebisch did not think it likely that that dynamism could be recovered, because of the protectionist policies applied by the United States since 1930, which had reduced external demand and the flow of capital. In view of that country’s importance as the main cyclical centre, he concluded that those policies imposed conditions which ruled out the restoration of a world economy compatible with the primary export pattern. In any case, even if the United States were to change its policies with regard to the rest of the world and international trade and capital movements expanded once again, it would not be a good idea for the Latin American countries to return to the primary export pattern, because this had three negative aspects. Firstly, as primary exporting countries, their economic processes were a reflection of those of the industrial countries, so that they were subject to the fluctuations of the latter and to considerable external vulnerability. Secondly, when the world economic system has been made up of industrial countries and primary exporting countries, the income generated by the system as a whole through increases in productivity has tended to be concentrated in the industrial countries because historically the terms of trade between industrial and primary goods have evolved in favour of the former, due primarily to the subordinate role played by primary commodities compared with industrial goods in the production process of the system as a whole. Thirdly, in most of the countries of the region, primary export activities have not been and will not be capable of absorbing the growing labour force and systematically raising its productivity.

These are the basic reasons why Prebisch maintained that the Latin American countries should not base their economic development on the primary export pattern but should adopt a strategy in which industrialization plays a decisive role. He made it clear, however, that while his criticisms were directed against a type of development centered on the production and export of primary commodities, they were not directed against those activities as such, since they must form an important part of the new strategy. He noted in that respect that industrialization would not do away with external constraints, so that in order to grow without upsetting the balance of payments it would be necessary to give a decided boost to primary commodity exports. In view of the diversity of national situations, he emphasized that each country must choose the sectoral mix most appropriate to the main objective, which was to raise the standard of living of the population. He was concerned that approaches based on the primary

---

3 The 1949 report can also be analysed as the basis for the structuralist theory of underdevelopment. Both these approaches are of course equally valid and mutually supportive. The work of Octavio Rodríguez represents the greatest contribution in this direction. See for example Rodríguez, 2001a and 2001b.
export sector should not be replaced outright with others based on industry, for selective sectoral development was a means rather than an end in itself. Yet although he expressed his ideas very clearly on repeated occasions, they have often been misrepresented either through ignorance or in order to serve particular interests, presenting them as though they advocated out and out industrialization and underrated or even despised primary activities.4

In his 1949 report, Prebisch also put forward several ideas on the means and conditions needed to promote this new development strategy. Two of these stood out above the rest. On the one hand, he stressed the need to combine the pursuit of development with the maintenance of monetary, fiscal and external sector balances. He rejected the idea that macroeconomic policy management should be guided by the automatic criteria of the Gold Standard, because these had shown themselves to be procyclical, when what was needed was to reduce fluctuations; deliberate intervention by the public authorities was essential in order to ensure that such management was both orderly and in keeping with the needs of development. On the other hand, he emphasized that development called for an enormous domestic saving effort and a considerable increase in the proportion of that saving used for productive investment. He explicitly rejected the idea of using inflation as a way of raising capital, because it put pressure on the balance of payments and was regressive in terms of income distribution: it was a kind of forced saving imposed on the mass of the population for the benefit of just a few, and there was no guarantee that the latter would use their growing income productively. At the same time, although he believed that it would be essential to use external saving in view of the shortage of domestic saving in many countries, he suggested that it should be employed with caution, because it too caused pressure on the balance of payments. It therefore seemed to him to be essential that most of the capital formation effort should be based on the domestic resources of each country, so that it was necessary to find “forms of (spontaneous or collectively determined) saving which... would make possible more appropriate use of resources for collective purposes”, including in particular the reduction of unproductive fiscal spending and of the conspicuous consumption of the highest income groups.5

Finally, this summary review cannot fail to mention that Prebisch fully acknowledged that his proposals were only tentative and that a great deal remained to be done in terms of research and practical action in order to improve our knowledge of Latin American development. In the pursuit of this greater knowledge, he recommended that we should avoid over-academic approaches, ensure that all ideas had a scientific basis, and not accept ideas formulated in the centres without first of all making sure that they take account of the special nature of our problems. He therefore advised us “not to confuse analytical knowledge of outside ideas with slavish mental subjection to them: something from which we are very slowly learning to free ourselves” (Prebisch, 1949, p. 107).

3. Inequality, vulnerability and the Gold Standard

Prebisch came up against the question of economic development right at the beginning of his intellectual career, but with reference to Europe. Thus, in 1921 he commented on the International Economic Conference which had been held at Brussels in 1920 in order to analyse and find solutions for the great economic and social problems caused by the 1914-1918 war, which affected millions of people all over that continent (Prebisch, 1921a). The central issue was the economic “reconstruction” of Europe, and Prebisch summarized the views of some of the economists invited to that Conference, who had made their diagnoses and prescribed the measures that should be taken. He did not share the views of Pantaleoni, who, as “champion of the old economic gospel”, proposed the restoration of laissez-faire as the sole solution. Instead, he identified himself more with Gide, Bruins and Pigou (and indeed most of the other participants), who considered that it was not sufficient merely to balance the public finances and control inflation: those efforts would be no use unless the forces of production were reconstructed and developed through better use of the factors of

4 See for example Viner, 1952. In contrast, Furtado understood very well the “limits” that Prebisch placed on industrial development, though he did not agree with them (Furtado, 1985, p. 62). Cattáneo (1991) gives an analysis of the relationship Prebisch envisaged between industry and agriculture.

5 Prebisch, 1949, p. 136 (the page numbers of the quotations from Prebisch correspond to the editions mentioned in the bibliography). Despite the emphasis placed by many governments and international agencies in recent years on the so-called first –and second– generation structural reforms as necessary conditions for economic development, a recent study concluded that the countries which grew most quickly from the mid-1970s to the end of the twentieth century were those which invested a high proportion of their GDP and maintained macroeconomic stability (Rodrik, 1998).
production, reduction of consumption in order to increase capital accumulation, removal of hindrances to trade, increased international cooperation, and the integration of efforts within each nation in order to tackle those great economic, social and political difficulties more effectively. These proposals are remarkably similar to those which Prebisch made when he arrived at ECLA thirty years later, so it may be held that they were turning over in his head right from the start of his intellectual evolution. It was also obvious that he was greatly attracted by the ambience of the Conference, where leading economists and politicians were discussing solutions that would affect the lives of millions of persons: it was a situation in which he would have loved to take part, as in fact he was to do so many times in later years. Prebisch did not take the ideas of the Conference as the starting point for his own thinking, because his main interest was in the Argentine economy, which did not need reconstruction or development at that time; on the contrary, its growth had been so successful that—for example—the value of its exports had increased fivefold in the first two decades of the century. That growth had its problems, however, and Prebisch drew attention to them, clearly showing that, as already noted, he was well aware of the shortcomings of the primary export-based growth pattern, even in an economy like that of Argentina which was growing at a rapid rate. He perceived two main problems: inequality and external vulnerability.

He referred to the economic inequality of Argentina above all in a lecture he delivered during a visit to Australia (Prebisch, 1924a). Very briefly, his view was that the benefits of the rapid growth attained in Argentina on the basis of the export of primary commodities were not equitably shared, mainly because land ownership was concentrated in a handful of big landowners. In order to change that situation, he maintained, it would be necessary to break up landholdings so that land ceased to be an instrument of privilege and became a means of efficient production in the hands of an extensive and more highly developed rural population. The great landowners have been able to use their political power to avoid any actions which could weaken their position, however.

This situation has impeded the settlement of a greater proportion of foreign immigrants in rural areas, has favoured extensive land use, and has given rise to an extraordinary degree of inequality between the living conditions of the rich and those of the middle and working classes. In other words, the concentration of land ownership, together with an oligarchic political power structure, has formed the basis, in conjunction with its external components, for a primary export pattern which has made possible a high rate of growth but has concentrated the benefits of that growth in only a few hands and given rise to great economic and social inequality. Prebisch did not return to the question of land distribution for many years, only doing so in the early 1960s (Prebisch, 1963), around the time when José Medina Echavarría was publishing in ECLA his analyses on the economic, social and political effects of the persistence of oligarchic power (Medina Echavarría, 1963).

With regard to the external vulnerability of the Argentine economy, he considered that this was due to the elementary fact that the dynamism of primary export activities depended on external demand and external capital, so that fluctuations in those two factors led to cycles of growth and crisis.

“Although Argentine monetary history appears to be confusing, it does in fact reflect a series of periods of boundless confidence and prosperity, of expansion of transactions, real estate speculation and financial bubbles, followed by more or less serious collapses causing outbreaks of panic which lead to the forced liquidation of operations, a slump in confidence, economic prostration and stagnation of business activities. Of course, these cycles are not exactly similar to each other in terms of their underlying conditions or their nature, but taken as a whole there are fundamental elements in them which are repeated and whose analysis can serve as the basis for theories on their evolution. In making this apparently a priori assertion, we have not

6 At the Conference, the participants talked about “reconstruction” rather than “development”, but there are many similarities between these two concepts, as noted by the Latin American delegates who promoted the establishment of ECLA at the United Nations Assembly after the Second World War. They emphasized the many common features between the reconstruction of Europe and the development of Latin America: if an Economic Commission for Europe had been set up to aid in the reconstruction of that continent, then a similar Commission should be set up in Latin America to aid in its development (see Santa Cruz, 1995).

7 In his comments on a government land settlement project he notes that “Every time an attempt to carry out agrarian reform is made in our country, the literature on these matters is copiously enriched by a flood of ideas and comments on foreign laws of this type. This great flood of words, however, contrasts vividly with the absence of effective action, which is smothered under lackadasical legislative actions and washed out by the influence of the interests of the great landowners” (Prebisch, 1924b, p. 393).
been influenced by the description of the classical process of crises formulated by some economists: on the contrary, we will seek to demonstrate that in our crises—apart from some other minor differences—there is a fundamental factor which is lacking from the European crises and is peculiar to the country’s degree of historical formation” (Prebisch, 1921d, p. 95).

Although his concern over inequality was only to re-surface a good many years later, his preoccupation with cyclical fluctuations was present in almost all his thinking throughout the next three decades, up to the time when he joined ECLA, when it was absorbed by the broader phenomenon of economic development. Prebisch embarked upon the historical study of the cyclical fluctuations of the Argentine economy because of his interest in finding the cause of the depreciation of the national currency, which had a highly negative impact on real wages: a very important matter in the Argentine socialist thinking of the period in which Prebisch was immersed.8 Encouraged by his professor, Augusto Bunge, he studied the various proposals for stabilizing the purchasing power of the currency (Prebisch, 1921e) and criticised the approach taken by Juan B. Justo, the main Argentine socialist leader of the time, who considered that the determining factor in depreciation was excessive currency issue, overlooking the decisive role played by the balance of payments fluctuations caused by the external factors already mentioned (Prebisch, 1921b).9

In his analysis of the various cycles which had taken place in the Argentine economy he highlighted the importance of external factors, which represented the main “objective” elements originally promoting periods of upward growth. In schematic terms, and taking into account the existence of strong external demand, he considered that it was the inflow of foreign loans and investments, especially from 1865 onwards, which made possible the convertibility of the peso and served as a basis for the increase in currency and credit which stimulated economic activity through the increase in opportunities for investment and gain and for the expansion of government expenditure, culminating in “excessive” expansion of the money supply—both with respect to the reserves and the volume of business—reflected in “artificial” growth marked especially by private speculation and fiscal irresponsibility. At that moment, he considered, the economic agents are full of “confidence” in the performance of the economy: a “subjective” factor of great importance in speeding up the cycles. The productive impulse is overtaken by an urge for speculation, however, which contains within it the seeds of its own failure: the balance of payments begins to register a deficit because of the disproportionate growth of imports and the increase in outlays on services, interest and other liabilities, so that reserves begin to flow out and the peso begins to depreciate, the bank reserves fall, credit becomes tighter, economic activity slows down, and the country finds itself in the midst of a downward phase, which normally makes it harder to obtain fresh external capital. At this point, the public and private actors who were originally responsible for the monetary and banking “excesses” that caused the “artificial” expansion of the economy try to check the downward trend through measures such as rediscounting and non-convertibility: these are the social forces which defend policies based on excessive currency issue or inflation. The crisis cannot be contained, however, and the fall in the reserves finally leads to a reduction in the money supply and credit, with consequent liquidation of assets and reduction of imports. The reduction of the latter makes it possible to obtain favourable trade balances which permit the payment of debts and reactivation of the economy, thus giving rise to a renewed climate of confidence which attracts foreign capital, setting off a new upward phase. In those days, Prebisch supported the idea that the liquidation of assets promoted by the application of the Gold Standard would make it possible to “cleanse” the economy of the excesses of “artificial” expansion and defeat the forces advocating currency issue and practising speculation, but the economic history of Argentina shows that this is only a transitory defeat, since these tendencies will reappear in the next upward phase. The inflow of external capital, of course, depends both on its availability and on the expectations of confidence and profitability that the investors perceive in the borrowing country. Prebisch notes that there have been occasions when the abundance of capital and the

---

8 The first article on this matter seems to have been that which he published in the newspaper La Vanguardia (Prebisch, 1920). I should like to thank José Besa for providing me with a copy of that article, from the documentary records of Mrs. Adela Mol de Prebisch.

9 In criticising Justo he based his arguments on the study by Williams (1920) on monetary fluctuations in Argentina, which had a lasting influence on him, since it served as a guide both for his ideas and the method of investigation he used. At all events, he acknowledged a little later that his criticisms of Justo had been somewhat too harsh, because currency issues in the period studied had in fact been greater than Williams and he himself had stated (Prebisch, 1921d).
feeling of confidence prevailing in the lending countries have sometimes allowed Argentina to keep on receiving capital and putting off the start of the downward phase in spite of the existence of appreciable trade deficits, but such postponements have never succeeded in preventing the crisis from occurring eventually.

Although the foregoing outline of Prebisch’s view of the formation of cycles has been extremely brief, it nevertheless shows the significance of that view for the ideas which he put forward in 1949.

Above all, as he himself acknowledged, that view of cycles is the origin of his conviction that the primary export pattern is intrinsically vulnerable to variations in external demand and in the flow of capital, which thus become one of the main elements explaining economic fluctuations. In other words, he asserts that the Argentine economy has established a form of relationship with the industrial countries in which its functioning depends on the demand and capital of those countries, which has brought considerable growth, but growth subject to fluctuations which it has not been possible to control. Prebisch’s schematic view is a dichotomy: on one side are the industrial and creditor countries, and on the other is Argentina, as a primary exporting country and debtor. Between these two there is a difference in the degree of “historical formation” which is equivalent not so much to inequality of living conditions as to inequality of social and institutional solidity; at any rate, that is what emerges from the comparison he makes between the Argentine banks and the Bank of England. The concept which comes closest to this is the development-underdevelopment contrast, if understood in a manner which does not take account only of economic dimensions. In addition, however, there is not only a difference of degree between the members of that dichotomy, in the sense that they have unequal degrees of historical formation, but also a functional relation, in that they carry out functions and maintain relations of interdependence within the same structure, and furthermore that functional relation involves a relation of domination within the structure of the world market. 10

Decidedly, Prebisch does not like the fact that Argentina forms part of a structure in which it obtains benefits, but at the cost of loss of control. Obviously, there is only a single step separating this view from the centre-periphery scheme: all that is needed is to extend the approach to cover all primary exporting debtor countries. It will be recalled that external vulnerability is one of the defects attributed to the primary export pattern in the 1949 Report, although at that time Prebisch paid more attention to trade vulnerability than to financial vulnerability, because in those days the Latin American countries had very little access to international capital after the cessations of payment that followed the crisis. In recent decades, however, the financial vulnerability associated with the condition of debtor countries has recovered all its importance in Latin America.

Secondly, Prebisch placed great emphasis in his initial works on the importance of external factors in the cycle dynamics of Argentina, because he considered that they were not being given their due importance compared with internal factors. This did not mean, however, that he ignored the latter; on the contrary, his analytical approach is much more complex than one based on mere dependence on external stimuli, because it incorporates internal sociological and psychosocial stimuli. Both the feelings of the actors (especially their greater or lesser confidence in the economic outlook) and the “social forces” play a significant role in cycle dynamics. 11

In his view, the most suitable approach for the study of cycles was one similar to that which ECLA sociologists were to propose forty years later for studying the historical development process in Latin America: to pay considerable attention to external factors, but to remain constantly aware that their impact on peripheral society is not manifested directly, because it is affected by the attitudes and behaviour of the domestic social forces. Prebisch summed up his view by stating that the dynamics of an economy are the consequence of “a series of mutual actions and reactions between the two types of factors” (Prebisch, 1921d). Although he appreciated the importance of domestic factors, however, he regretted that he could not study them, perhaps because he felt that he lacked the sociological knowledge for doing so; apparently no such study was made by any sociologist of the time either, thus losing the opportunity to lay the bases for a sociological theory of the Argentine business cycles. 12

---

10 This latter aspect concerns what Max Weber calls “domination based on a constellation of interests”, which must be differentiated from domination based on authority (Weber, 1964, vol. II).

11 The incorporation of subjective factors into the analysis of cycles shows the influence of Pareto. For that author, social phenomena take the form of cyclic fluctuations, and in them the feelings of the actors—the basis for non-logical actions—play a decisive role (see Prebisch, 1923b).

12 This gap was filled for a time during the 1960s in ECLA studies by a number of sociologists, notably José Medina Echavarria and...
Thirdly, and paradoxically, in those years Prebisch combined his critical view of the primary export pattern with a conviction that the rules of the Gold Standard would make it possible to "cleanse" the economy of monetary and fiscal excesses and external sector imbalances, thus recovering macroeconomic balance, disciplining the social forces and resuming growth. This was the orthodox dimension which remained in his thinking and only disappeared with the 1929 crisis, although there are some indications that he had already begun to have his doubts about it before that date. His confidence in the Gold Standard led him to reject the initiatives for the creation of some kind of institution designed to regulate the economic cycle. He called Norberto Piñero's idea of setting up a bank to regulate cycles "banking orthopaedics" (Prebisch, 1921c) and likewise criticised Emilio Frers' proposal to set up an International Convertibility Board. "All the countries with depreciated currencies long to get back to the Gold Standard. So why interfere with it? And some of them, through drastic disinflation of the money supply, through savings on public expenditure and through a determined effort to improve their international balance of payments position, are on the point of doing so. Such is the case of Great Britain. Noted economists are already pointing to it as an example to follow" (Prebisch, 1923a, p. 359).

The paradoxical aspect of this is that at the same time that he was drawing attention to the importance of external factors in the dynamics of cycles, he accepted that economic policy should be based on a mechanism which asserted that domestic factors were responsible for external imbalances. At all events, Prebisch believed that the policy of "liquidation" needed to restore order after the "excesses" should be used to ensure that they were not repeated, by reorienting the economy towards a more genuine form of growth. This meant that production and financial activities should be based preferentially on domestic saving (since external saving was a source of vulnerability and instability, because it always ended up by disappearing) and the money supply and credit should be adapted to the existing reserves and the real needs of the economy. In other words, he wanted a more productive and less speculative economy, with a solidity coming from within, based on domestic saving and investment, whose growth is less spasmodic, and with a sound currency and solid banks. He did not say anything about changes in the development pattern and made no mention of industrialization, but it may be presumed that he must have had them in mind, for otherwise how could Argentina raise its degree of "historical formation" and reduce its external vulnerability?

Finally, it is very likely that the scant attention paid by the Argentine economists of that time to the role of external factors in the evolution of Argentine cycles (in keeping with the ideas then prevailing in the centres) brought home very clearly to Prebisch for the first time the danger of accepting out of hand theories developed in other contexts and leaving out of the reckoning the special features of the Argentine situation: a danger he reiterated in 1949. As already noted, this does not mean that he proposed ignoring those theoretical efforts: on the contrary, he considered that their elements of value must be extracted from them to the full, as he himself did in the case of the studies by Harvard economist John Williams, which showed him the importance that should be attached to external factors in Argentina's cycles. He noted in this respect that the under-estimation of those factors has led to serious policy errors even in the centres, as for example in the case of the international recommendations made to the German Government at that time for tackling its grave monetary problems. Those recommendations, which were based on the classical approach, maintained that those problems were caused by the increase in the money supply, which must be reduced at all costs, and they failed to notice that that increase was due to the demands for the payment of war reparations. Prebisch concluded that it was useless to insist that the German Government must control monetary expansion without first reaching an international agreement to relieve the burden of the reparations (Prebisch, 1922a).

4. The crisis, and the consolidation of his heterodox approach

Prebisch formulated the foregoing ideas between 1921 and 1924. In the following years, he continued to be very interested in studying the cyclic problems of the Argentine economy, but was faced with the problem of the lack of empirical information, so he made a great effort to prepare and compile statistics that would enable him to make a deeper analysis. He first of all occupied the post of Deputy Director of the National Statistical Institute, then of the Statistical Office of the Sociedad...
Rural Argentina, and subsequently, from 1927, of the Bureau of Research and Information of the Banco de la Nación Argentina. The information collected served as the basis—especially in the last-named post—for the preparation of detailed descriptions of the economic situation; his approach continued to be that which he had developed in previous years, but—as was to be expected from an author working in a government office—he reduced his criticisms and increased the amount of empirical description.

These studies reflect his effort to unravel the significance of the recessive tendencies which he perceived from 1928 on. The first symptoms of what was subsequently to become the great crisis of 1929 allowed him to assert that once again Argentina—as a country which depended on outside demand and capital—was being affected by turbulences originating in the main industrial economies. In mid-1928 the inflow of external capital began to go down because of the increase in interest rates imposed by the Federal Reserve, which was very worried about the expansion in the amount of credit used for stock market speculation, and moreover the prices of Argentina’s exports fell because of the lower demand by the industrial countries. This obliged the Argentine Government to cover its growing balance of payments deficit through an outflow of hard money, with its natural consequences for the monetary process (Prebisch, 1929 and 1930a). In those studies he also noted for the first time, however, that the fall in the prices of agricultural commodities was aggravated by the fact that those prices fell more than those of industrial goods. That process of relative deterioration of commodity prices compared with those of industrial goods could be due to various causes, but on that occasion he only argued that it was due to the fact that the inelasticity of agricultural supply had not allowed it to evolve in line with the drop in external demand.

Up to mid-1930, Prebisch (1930a and 1930b) held that those phenomena were merely specific manifestations of yet another cyclic decline, of the many that Argentina had experienced. “It may be considered as a short-term economic phenomenon, a downward period in the up and down movements that normally mark the evolution of any country; as a purely superficial event... which does not in itself affect the structure of the national economy or involve any significant departure from the ongoing upward trend in the country’s economic activities” (Prebisch, 1930a, pp. 613-619).

It was in these circumstances that a new stage in Prebisch’s life began when, in 1931, he took office as Undersecretary of Finance and was called upon to make a decisive contribution to the task of formulating and applying policies to deal with the crisis. During that year and the next, government policy combined orthodox measures, such as the reduction of public expenditure, higher taxes and tighter credit, with other measures of a heterodox nature such as authorizing rediscounting operations in order to improve the situation of the banks and their creditors (Prebisch, 1931a), raising tariffs in order to check the balance of payments deficit and reduce the fiscal deficit, controlling the exchange rate in order to defend the value of the peso with respect to gold (Prebisch, 1931b), and introducing income tax in order to improve fiscal revenue (Prebisch, 1932a). These heterodox measures which Prebisch helped to formulate and implement as from 1931 were always presented as transitory and extraordinary, so that they were accepted by the rest of the members of the government and by the economic elite, among whom orthodox economic policy tendencies prevailed. They were always presented as being essential for dealing with an abnormal real situation; when things returned to normal they would be abandoned, and good normal doctrines would prevail once more. In addition, there was a project for the establishment of a Central Bank, which Prebisch drafted in 1931 but which the Executive did not dare to present to Congress because it was afraid it would be considered too interventionist and permanent, which proposed to regulate not only the inflationary tendencies in the upward phases of cycles but also (which was considered an unacceptably heterodox idea) the recessive tendencies in the downward phases (Prebisch, 1972).

Thus, he very quickly abandoned the Gold Standard and turned to heterodoxy, when he still believed that the crisis was merely a cyclic downturn; he no longer accepted that the liquidation of assets was an acceptable way out of the crisis, or that the automatic market mechanisms should be given full freedom to act. The rapidity of this change in his ideas raises the suspicion that he had already begun to doubt the validity of such convictions even before the crisis: indeed, he had already explicitly expressed his doubts about the efficacy of the market mechanisms when, years before the crisis, he supported State intervention in the meat market (Prebisch, 1927). Likewise, in the bill for the authorization of rediscounting operations in 1931, and very emphatically in 1932, he rejected the “liquidation” of assets as a way of putting the economy on a sounder footing and restoring growth; the State, of course, could not be liquidated, and he saw no advantage in
liquidating rural producers who could not pay off their loans because of the fall in the international prices for their products.

In his writings of those years, he returned to his old idea that the dynamics of cycles are affected by both external and internal factors; thus, he asserted that the problems Argentina was suffering were due both to monetary and fiscal excesses and to the external difficulties caused by the drop in export prices and the fall in capital inflows, as well as the country’s weak monetary institutions. The proposal he put forward in mid-1932 was therefore to attack all those factors simultaneously through restrictive monetary and fiscal measures, exchange controls and foreign trade control measures, and a Central Bank which would put monetary institutions and policies in order and regulate cyclic fluctuations. At that time he still maintained that the crisis was merely a cyclic downturn, but he was beginning to suspect something worse: for many decades the evolution of the Argentine economy had been one of “growth only interrupted by depressions that were of short duration and low amplitude, in contrast with the severe features of the present recession” (Prebisch, 1932b, p. 86).

In 1933, however, he no longer had any doubt that the crisis was not just a cyclic downturn; between 1929 and 1933 agricultural commodity prices had gone down by almost half in pesos and by over two-thirds in gold; indeed, the prices in gold in 1933 were well below those prevailing in 1900. This reduction was much greater and longer-lasting than those which had occurred in cyclic downturns, and its impact was therefore broader and deeper, to the point of “….. violently upsetting the economic structure of the country” (Prebisch, 1933c, p. 135). Because of this, in order to pay the same amount of interest on its debt Argentina needed 78% more of the former to buy a given amount of the latter in 1933 than in 1929.

This serious diagnosis was accompanied by a pessimistic forecast regarding the possibility of returning to the pre-crisis situation in the short term. This appraisal must have been considerably influenced by two events. First, when he took part in the organization of the 1932/1933 World Economic Conference he became aware of the enormous political, trade and financial difficulties hindering the evolution of the international economy, including the persistence of the problems connected with war debts, the obstacles standing in the way of tariff reduction, the dislocation of exchange rates, and the protectionist and reserve-building policy followed by the United States. This latter issue, which was to be given considerable prominence in Prebisch (1949), was a source of special concern to him in view of the central position of that country in the international economy. Some of those problems (such as the war debts and protectionist tendencies) already existed before 1929, but the crisis made them worse and also created other new problems (Prebisch, 1933a). His pessimism must have been further heightened by the conditions that Argentina had to accept in its negotiations with Great Britain, which culminated in the 1933 Roca-Runciman agreement. Prebisch formed part of the Argentine negotiating team and knew at first hand the force with which Great Britain (the main buyer of Argentine products) took advantage of its economic power in order to regulate trade with Argentina in line with its own interests (Prebisch, 1933b).

In such circumstances, three ideas must have come together in Prebisch’s mind: i) full confirmation of his long-standing criticisms of the Argentine economy’s external vulnerability as an agricultural commodity exporting and debtor country, along with the more recent idea of the deterioration of the terms of trade; ii) the conviction that the crisis was much broader and deeper than a mere cyclic downturn, and that it shook the very foundations of the economy; and iii) the improbability that Argentina would be able to return to the situation existing before the crisis, because of the problems affecting the international economy at both the multilateral and bilateral levels. Those ideas must have convinced him that it was necessary to make an even deeper search for new ways of bringing his country out of its present situation.

He had already become convinced that the automatic mechanisms of the Gold Standard were not appropriate to the Argentine situation, since they were procyclical and attacked the external imbalance only indirectly, through restrictive fiscal and monetary measures, which led to an economic and social cost which was unacceptable to him; instead, that imbalance should be tackled through direct measures designed to regulate the exchange market and foreign trade. This was an advance in his heterodox thinking, but it only

---

13 The article by González and Pollock (1991) gives a very good analysis of the influence of these events on Prebisch’s thinking—and state of mind.
referred to the manner –interventionist rather than automatic– of achieving balanced external accounts. A further decisive step was needed in terms of the application of active policies to bring the Argentine economy out of recession, and it was necessary to decide to what extent that called for the establishment of a new development pattern, now that it was clear to him that the primary export model would not be capable –at least for a long time to come– of playing the dynamic role that it had had before the crisis. In this aspect, Prebisch was influenced both by the ideas being formulated in those years in the industrial countries (especially the contribution of Keynes) and the policies being applied in them, especially in Great Britain and the United States. An analysis of this aspect is outside the scope of this article, however.14

He began to take this step with the National Economic Plan of Action which he prepared together with a number of colleagues in late 1933, with the explicit aim of “lightening the burden of the economic depression on the country” (Prebisch, 1934a, p. 146). After having put the monetary and fiscal situation in order, the Plan provided for a first set of measures to tackle the balance of payments deficit problem that Argentina suffered as an agricultural-exporting and debtor country, through devaluation and exchange and import controls. In defending these measures he explicitly and definitively broke with the Gold Standard system, since that only served to correct price and balance of payments upsets caused by an excessive increase in the money supply, but in 1933 no-one doubted that such upsets had not been caused by “excesses” or faults in the calculations of the economic agents, but rather by an unusually great and unforeseeable drop in international prices. Applying the Gold Standard mechanism, while ignoring the fundamental importance of external factors, would merely make the crisis still worse by causing an extraordinarily severe liquidation of assets.15 He had already set forth these ideas earlier, but in this Plan it was noteworthy that, as well as seeking to balance the external sector, these measures were also designed to reactivate the economy; exchange and import controls would protect industrial activities from outside competition, and the devaluation would have a beneficial effect on rural producers. Without devaluation, the domestic prices of agricultural products would drop in line with international prices, and producers would not be able to pay their debts contracted at higher price levels, thus causing enormous successive liquidations of assets; in contrast, devaluation would reduce the impact of the drop in international prices on those producers.

A second set of measures was designed to promote reactivation of industrial production directly through a recovery in domestic demand. He argued that the reduction in the purchasing power of the population had reduced economic activity and increased unemployment, giving rise to a situation which needed to be corrected by the government through a large-scale public works plan designed to reduce unemployment and increase the purchasing power and consumption of the population, thus stimulating the reactivation of domestic industrial production, which would be further protected by the inability to import goods from abroad. He noted that in recent years tariff protection and the higher cost of foreign exchange had favoured domestic consumption and production, giving rise to an extremely important process: “local industries … have managed to expand their production, while foreign trade has declined” (Prebisch, 1934b, p. 201). In short, “... it is very unlikely that the stimulus so desperately needed by the Argentine economy can come from outside; solutions must be sought within the country itself” (Ibid., p. 144).

The Plan also has many other aspects worthy of interest, such as for example its attention to the redistributive effects of the economic policy measures on the different social groups, as already hinted in his early studies. This in turn leads the way to another issue of great importance: the social consequences of economic policies, for when redistributive effects are caused by the hidden hand of the market, as under the Gold Standard system, economists are not obliged to take complex ethical decisions, but when such effects are caused by their own interventions they have no alternative but to take them into account and analyse them carefully. Thus, for example, devaluation favours rural producers by improving the domestic prices of their products, which seemed fair to Prebisch because they had been one of the groups most seriously affected by the crisis. But this can encourage some of them to sell their products abroad at knockdown prices, thus adversely affecting the rest, so the government prevented this by setting up an institution to control this process (the National Cereals Board). Or other producers may try to derive excessive benefits by selling

14 See, in this respect, the articles by Love (1994 and 1999), González and Pollock (1991), and Rodríguez (2001a and 2001b).
15 His criticism of the Gold Standard appears in various studies of the time. See in particular Prebisch, 1934c.
the foreign exchange they obtain on the black market, so the government took steps to oblige them to change it on the official market. This shows that the Plan is important not only for its heterodoxy and its expansionary nature but also for its concern for the distributive effects of the measures taken.

How far did this Plan seek to reorient economic activity towards a development pattern in which industrial development played a decisive role, or was it only concerned with stimulating economic activity? Bearing in mind what we said earlier about the previous evolution of his ideas, there can be no doubt that the Plan was Prebisch’s first answer to the question of how Argentina could cease to be an agricultural exporting debtor country: a question that Prebisch must have posed himself right from the start of his intellectual life, when he saw the problems that those problems brought with them. At that time he would have said that Argentina’s situation as a debtor country could be overcome through a big domestic saving effort, but up to 1933 he had not written anything about how that country could overcome its dependence on agricultural exports. The idea of industrialization must have passed through his mind, however, for how otherwise could Argentina overcome that situation and raise its “degree of historical formation” to a level comparable with that of the important countries of the world? It would have been difficult to defend such ideas, as long as Argentina was registering high growth rates as an agricultural exporting country and the economic power was in the hands of an elite whose core consisted of great landowners. The situation changed in 1933, however, when it was clear that agricultural export activities had sunk into a deep crisis because of the serious drop in export prices, the deterioration of the terms of trade and the dislocation of international trade due to the crisis and United States protectionism, whereas industrialization had shown its capacity for increasing the supply of goods and improving employment and incomes.

Finally, some comments are called for on Prebisch’s views in his early years about State intervention in the economy: a matter he never dealt with explicitly. Above all, Prebisch was always a fervent defender of disciplined and austere economic processes and he rejected all “excesses”, be they monetary, fiscal, or in the fields of external trade, consumption or other areas. This attitude was always present in his thinking, right from the start of his personal and intellectual life, and is the reason why he always believed that countries must maintain well-ordered accounts, avoid conspicuous consumption, and base their growth on domestic saving, without resorting to the easy but spurious “solutions” of external indebtedness and inflation. At first, he believed that the free play of the market forces would be sufficient to achieve this, but between the late 1920s and the early 1930s he gradually realized that this was not the way to go, and he began to advocate State intervention. He had no doubt that it was necessary to guide and discipline the private economic actors: for example, scornfully referred to landowners who were not capable of seeing where their real interests lay, and in the decree serving as the basis for exchange controls he argues flatly that “the harmful anarchy prevailing in the market must be replaced with a centralized approach run by the most capable elements” (Prebisch, 1931b, p. 4). It was increasingly clear to him that the economic process must be regulated by an enlightened State elite capable of avoiding the pressures of powerful economic agents and also of governments themselves, which, as he showed in his first analyses on cycles, usually handle their economic affairs in an improvident, electoralist and often corrupt manner.

5. Conclusions

Prebisch’s work on development began in 1921, when he became aware that the Argentine economy was highly vulnerable to the fluctuations caused by the industrial countries because of the position they occupied in the world economic system. This was the foundation-stone of the body of theories he built up over the years, which took its final shape in the centre-periphery scheme. As the most important exponent of Latin American structuralist thinking, he did not need to wait for the impact of the 1929 crisis in order to be aware of the intrinsically vulnerable and unequal nature of a development pattern whose functioning depended on foreign demand and capital and which was based on the concentration of land ownership; the crisis confirmed his diagnosis and made it urgently necessary

---

16 With regard to ECLAC’s thinking on the role of the State, see Gurrieri, 1987.

17 “…the stock-raising crisis has shaken the great Argentine landowners out of their lethargy and may be a powerful element in turning their class instincts—mostly incoherent, disoriented and negative—into a clear awareness of their economic interests” (Prebisch, 1922b, p. 349).
to seek solutions, but it was not itself the prime cause of the problems. There is therefore a marked continuity in the evolution of Prebisch’s ideas from his first youthful studies to the 1949 Report in which he presented his developmentalist “manifesto”: those early studies already contain, to a greater or lesser extent, almost all the ideas he put forward when he joined ECLA, so it would be a mistake to overlook them as if they were merely another expression of neoclassical thinking.

Ever since 1921 Prebisch was concerned with the question of finding a less vulnerable and unequal way of organizing economic activity in Argentina. With regard to the dependence on external capital, his answer was immediate: much greater emphasis should be placed on domestic saving. The answers to the problem of dependence on external demand and the reduction of inequality were much more complicated, however, because they involved profound restructuring of the economy and came into conflict with the dominant interests. As already noted, he only returned to the question of inequality due to the concentration of ownership in the early 1960s, but he already gave a first response to the problem of external demand in the 1933 Plan, although he had probably been turning it over in his mind much earlier. What we can say for sure on the basis of his works is that in seeking new ways of reducing external vulnerability he had to abandon above all his support for the Gold Standard. This occurred when he became convinced that that standard was unsuitable because it subjected monetary and exchange policies to a criterion which took no account of the interests of the Argentine economy, since it expanded the cyclic fluctuations instead of reducing them and involved the application of restrictive monetary and fiscal measures which gave rise to high social costs. It was at this point that he proposed direct intervention on the exchange rate and foreign trade, and he began to apply measures in that direction when he took up a government post in 1931. Those measures not only helped to balance the balance of payments, however, but also helped to reactivate the economy, because they fostered domestic production, with beneficial effects on employment and income. In other words they showed –if such a demonstration were needed– that industrialization should be an essential component of policies designed to reduce the dependence on external demand, so that in late 1933 he helped draft a Plan which combined control measures for the external sector with others expressly aimed at stimulating domestic supply and demand. This was his first consistent response on how to change the Argentine economy’s situation of external vulnerability. The industrial development which took place in those years, however, revealed to him that industrialization also brings its own external vulnerability with it, so he insisted on the need to make such development compatible with the expansion of exports: a matter to which he devoted much attention in the 1949 Report.

Many other ideas put forward in that Report had already been present in his early works: the aggravation of external vulnerability through the deterioration in the terms of trade; the difficulties caused by the protectionist policies of the United States, and the error of accepting out of hand diagnoses and proposals prepared in the industrial countries, because they could well refer to different situations, so that economists must exercise a considerable degree of independent creation and critical judgement if they want to understand and successfully cope with the problems of their own national situations. He was also already convinced even as a young man that a combination of the market and State intervention was required in order to reorient the economy in the desired direction and promote its growth. As he was mistrustful of the political elites, he considered that such intervention should be carried out by an institution with a high degree of autonomy, staffed by technicians capable of disciplining and guiding the private and public agents in line with a technical and substantive rationale aimed at the benefit of the community as a whole. This perfectly expresses the way he then conceived the role of technicians in the decision-making process, and this is the line he took in ECLA and in the Central Bank of Argentina, which he helped to set up and of which he became General Manager in 1935.

(Original: Spanish)
Bibliography


(1963): Hacia una dinámica del desarrollo latinoamericano, Mexico City, Fondo de Cultura Económica (FCE).


(heren): Prebisch: the continuing validity of his basic ideas, CEPAL Review, No. 75, Santiago, Chile, ECLAC.


