

C E P A L

REVIEW

NUMBER 59
AUGUST 1996
SANTIAGO, CHILE

OSCAR ALTIMIR
Director of the Review

EUGENIO LAHERA
Technical Secretary



UNITED NATIONS

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The Argentine experience: *development or a* succession of bubbles?

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This article adopts the premise that development is endogenously driven by innovation mechanisms, of which the economic elite is an eminent vehicle in that it efficiently fulfils the function of generating innovation by seeking technological quasi-rents which creative competition permanently erodes. In order for this to happen, the necessary conditions must be present so that the search for technological quasi-rents predominates over other types of profit-seeking. The interaction between the Argentine economic elite and the institutional system has enabled it to acquire non-technological quasi-rents, being essentially quasi-rents from scarce natural resources, combined with political quasi-rents. This interaction—which has constituted a major restriction on development throughout Argentine economic history—became more accentuated from 1976 onwards, owing to the weakening of institutions and of a large number of organizations following the coup d'état in that year and to the neo-conservative policies adopted in subsequent years. In the 1990s, the institutional decline and economic policies based on neo-conservative recommendations of generalized non-intervention by the State (“hands-off” approach) increased the possibilities for acquiring non-technological quasi-rents and gave rise to a bubble generated predominantly by external indebtedness and by privatizations. Prior to the processes of privatization and deregulation, the existence of opportunities for obtaining quasi-rents that did not derive from advances in technology and production had crowded out innovation and investment. Subsequently, those processes—within a context of institutional fragility and extreme weakness of the system of checks and balances—encouraged this crowding out effect to continue in the 1990s.

What has not been properly appreciated ... is the distinction between different types of reaction to changes in conditions...

The interaction of institutional forms and entrepreneurial activity ... is ... a key topic for future research.

Joseph A. Schumpeter

I

Introduction and summary

This article postulates as its central thesis that the policies implemented in Argentina in the 1990s, based on neo-conservatism, have led to a bubble, generated predominantly by indebtedness and privatization, rather than to development. This thesis is based on a review of the period and on a set of hypotheses concerning the interaction between institutions and the economic elite, the latter being understood to mean the group of economic agents which in each period occupied a dominant position as regards the behaviour of the other economic agents and had a greater influence on institutions (see Nochteff, 1993 and 1994).

The concept of quasi-rent is used here as a tool for analysing the behaviour of the economy. It is considered that:

i) In statistical analysis, quasi-rent is analogous to the Ricardian differential rent; in dynamic terms, by introducing technological change, Ricardian rents ultimately become quasi-rents in cases where the rent derived from the scarcity of a natural factor diminishes because of technological innovation;¹

ii) Ricardian rents tend to be –at least in part– quasi-rents in that their acquisition is sustained by institutions which create supply rigidity (as occurred with the barriers to the possibility of trading in rubber plant seeds in Brazil, or with the land market institutions in Argentina, or with the Magna Carta clauses on obstacles in river beds in England);

iii) Quasi-rent which is obtained more through innovation than through other supply rigidities is a

typical development quasi-rent in the Schumpeterian sense, and it undergoes erosion from the outset through competition and imitation (its transitory nature is thus endogenous to the actual functioning of the economy);

iv) These features distinguish it from quasi-rents generated through institutional barriers to entry (reserved markets, finance privileges, subsidies), which we shall call political quasi-rents, including those arising from the scarcity of natural factors, accompanied by restrictive institutions;

v) Political quasi-rents are not development quasi-rents. Furthermore, they are not characterized by a transitory nature endogenous to the functioning of the economy but may be perpetuated for as long as the scarcity of natural factors and/or the existence of restrictive institutions endure (hence the use of the concept of “non-transitory monopolistic positions” in this article);

vi) Political quasi-rents encourage the formation of bubbles because they raise the value of assets above the long-term equilibrium level. Although they are not “transitory” in that they undergo erosion from the outset, in the long term they disappear because insufficiency of innovation and investment causes them to be crowded out, either because the restrictive institutions are not sufficient to make up for backwardness and low productivity or because the market segments that can be preserved with them diminish until they lose importance for their captors (which is what typically happens with those acquired through reserved markets in dynamic branches).²

□ This article is the outcome of a research project sponsored by the Volkswagen Foundation and undertaken, with the cooperation of Dr. Klaus Esser of the German Development Institute, by Daniel Azpiazu, Eduardo Basualdo, Adolfo Vispo and the author, who assumes responsibility for any errors.

¹ For a concurring approach, although it maintains the term rent, see Kaplinsky, 1995, p. 4.

² On this subject, see Napoleoni (1962, p. 1429 *et seq.*), Schumpeter (1968) and Kaplinsky (1995). Quasi-rent is analogous to abnormal profit (Ricardo, 1826). The term quasi-rent has been preferred in order to emphasize the link between present surplus and future cost, in the Marshallian sense, and institutional barriers to entry.

In short, what is being postulated is that the economy is undergoing a process of development only if technological quasi-rents predominate over the other types of quasi-rents. If this is not so, periods of expansion are regarded as “bubbles” in relation to innovation-based development.

In section II, very simplified hypotheses are set out concerning restrictions on innovation (and thus on development) in Argentina, and it is argued that such restrictions ought to be regarded not so much as an inadequate supply but rather as a scarce demand for innovation (and for public policies to promote such demand). This scarce demand has been caused by the ways in which institutions and organizations—particularly large enterprises—interact, making possible the acquisition of non-technological quasi-rents. It is contended that, at the different stages in Argentine economic history, neither the institutional system nor organizations induced the economic elites (which also differ in part) to seek technological quasi-rents; on the contrary, the influence of those elites on institutions and organizations³ facilitated their acquisition of political quasi-rents. This happened both in the agricultural/exporting stage and in the import substitution industrialization stage. In the former stage, political quasi-rents were acquired through extensive exploitation of natural resources, finances, speculation in fixed assets (in particular land) and financial assets, trade and the exercise of monopoly privileges granted by the State; these activities crowded out technological quasi-rent-seeking (Nun, 1995; Sábato, 1988). In the latter stage, political quasi-rents were obtained by virtue of the effective tariff structure, reserved markets, and direct or indirect subsidies (see Nochteff, 1994, p. 79, *et seq.*, and the bibliography quoted therein).

Section III examines the period subsequent to 1976. This period resembles a new bubble of non-technological quasi-rent acquisition, generated basically by external indebtedness. It can be divided into three distinct phases. The first corresponds to the 1977-1981 borrowing phase, which gave rise to the external debt crisis. The second covers the recessionary decade of the 1980s, in which the economic elite acquired political quasi-rents through transfers of income in their favour (by means of subsidies, liquidation of their liabilities—particularly external ones—

³ As regards the interaction of institutions and organizations, the approach of Burns and Dietz, 1995, has been followed.

and State purchases), in which oligopolistic markets were created for internationally tradable and non-tradable commodities, and which ended with the recession and hyper-inflation of the two-year period 1989-1990. In the third and last phase—the 1991-1995 bubble—which was generated largely by a combination of foreign indebtedness, privatization and deregulation, political quasi-rents were further consolidated, and quasi-rents from cheap labour took on increasing importance.⁴ This section also examines the main long-term effects of what happened throughout the period as a whole—characterized by the predominance of neo-conservative recommendations and diagnoses—and puts forward more detailed arguments concerning the regressive effect which the 1991-1995 bubble had on development. It is considered that, following the liberalization of trade, the tradeable sector of the economy can in general be regarded as open and that, therefore, foreign trade properly reflects changes in the pattern of production. It is further contended that trends in foreign trade lend paramount importance to comparative advantages, which suggests a setback in terms of development and of competitiveness (or least of competitiveness compatible with rising levels of well-being and employment).⁵

It is also asserted that the neo-conservative policies applied since 1976, particularly in the periods 1976-1983 and 1991-1995, intensified the behaviour of the economic elite, because those policies weakened many of the institutions and

⁴ Llach (1987) notes that quasi-rents from cheap labour—which he terms “Lewisian” because of their link with excess supply of labour at constant wages—were not important in past Argentine economic history. Nonetheless, the drop in real wages, as from 1976, to half the level of previous years and the huge increase in unemployment and underemployment, as from 1992, radically changed the labour market (Cortés, 1985; Minujin, 1993; Barbeito and Lo Vuolo, 1993), giving rise to the acquisition of rents from cheap labour. The “Lewisian” quasi-rents increased during the downward phase of the 1991-1995 bubble. According to official surveys, 76% of unemployed persons seeking employment do so without expressing any conditions as regards length of working day or job status (Marcó del Pont, 1995) and hence also as regards the real hourly wage: a clearly Lewisian situation.

⁵ With reference to the relationship between development, industrialization and the foreign trade profile, we have largely followed the views of Klaus Esser on Latin America and those of Raphael Kaplinsky on the less developed countries, which are in substantial accord with the analysis of the Argentine economy in this article (Esser, 1991; Esser, Hillebrand, Messner and Meyer-Stamer, 1993; Kaplinsky, 1993 and 1995).

organizations which aimed to restrict the influence of this elite and its opportunities for acquiring political quasi-rents and created rules of the game that were beneficial to it.⁶ These quasi-rents raised the prices of assets (fixed and, in particular, monetary) and expenditure programmes far above the levels of long-term equilibrium and perfect information. These expenditure budgets could have been sustainable had there been a process of development, but that process did not occur because quasi-rents which were not associated with innovation or production crowded out investment; consequently, the increase and subsequent drop in wealth were merely phases of a bubble.

In this respect, it has been affirmed that neo-conservative policies have distorted prices (Fanelli, Kacef and Machinea, 1995) and relative returns in favour of the oligopolistic non-tradeable goods sectors, with adverse effects on the competitiveness of the economy. Thus, despite trade liberalization, the economy has tended to become closed and the economic elite, composed of local and transnational economic conglomerates, has increased its acquisition of political quasi-rents. Owing to the weakness of institutions and organizations, therefore, the free-market reforms based on neo-conservative thinking did not transfer the fixing of prices and profit margins from the State to the market, but rather to a small group of major economic agents (Azpiazu and Vispo, 1995; Azpiazu, Bang and Nochteff, 1995). The weakening of government institutions (institutional shock) was essentially connected with neo-conservative principles of non-intervention by the State (hands-off policy).⁷ No account was taken of the

⁶ See Azpiazu and Vispo, 1995; Azpiazu and Basualdo, 1995; Esser, 1991; Esser, Hillebrand, Messner and Meyer-Stamer, 1993; Basualdo, 1994.

⁷ It could be argued that the neo-conservative (also termed neo-liberal) recommendations linked by many writers to the so-called Washington Consensus were not restricted to the policies pursued in Argentina. Nonetheless, as was noted by Platteau (1994, p. 534), the way in which the recipe is normally presented implies or suggests that the market system can be supplanted with guaranteed success in any place and at any time. This disregard for the specific features of institutions, organizations and agencies has led—in many countries of the region—to a form of free-market economy that has given rise to an insouciant lack of regulation and direction in all sectors of the economy (Esser, Hillebrand, Messner and Meyer-Stamer, 1993). It can be accordingly affirmed that neo-conservatism was the framework on which the public policies of Argentina and much of the region have been based (Krugman, 1995; Nochteff, 1993).

fact that development which “springs” from the centre of society (endogenous development) “is the world which in reality is presupposed by neo-classical economic theory and allows its rules of behaviour and maximization to be valid; however, it is a complex historical product that cannot be achieved overnight” (Llach, 1987).

This development which springs from the centre of society, Schumpeterian endogenous development, did not occur in Argentina. On the contrary, the most powerful local conglomerates,⁸ which are gaining control of most of the privatized assets and are representative of the economic elite, are acquiring primarily political quasi-rents. Consequently, the institutional shock constituted by neo-conservatism affects an economy totally different from that presupposed by the neo-classical theory on which that movement is based, since change “is not achieved overnight”. As a result, the strategies of local conglomerates are totally different from those employed by leading enterprises both in developed economies and in the newly industrializing countries (NICs).⁹

The Argentine case may therefore be seen as an extreme example of what has happened in the major countries of the region. Prior to the processes of liberalization and deregulation, the possibility of acquiring quasi-rents not derived from advances in technology and production had crowded out investment in the first two periods of expansion referred to. Thereafter, these processes contributed to the continuation of that crowding-out effect in the recent past.

Section IV attempts to identify and describe briefly some—not all—of those features of the privatization and deregulation process initiated in 1991 (Azpiazu and Basualdo, 1995) which, as indicated in section III, helped to generate the 1991-1995 bubble. Finally, a summary of the conclusions is set out in section V.

⁸ The economic leadership which developed from 1976 onwards (Azpiazu, Basualdo and Khavisse, 1987) and became consolidated in the period 1991-1995 (Azpiazu and Basualdo, 1995).

⁹ Compare the strategies, particularly the diversification strategies, examined by Basualdo (1994) with those studied by Hikino and Amsden (1995).

II

Development and technology in Argentina: expansion of the agricultural export sector and import substitution industrialization

"... who made the discovery of the machine, or who first usefully applied it, would enjoy an additional advantage, by making great profits for a time but, in proportion as the machine [became] ... of general use, the price of the commodity produced would, from the effect of competition, sink to its costs of production, when the capitalist would get the same money profits as before..."

David Ricardo

1. Development or bubbles?

Development¹⁰ is driven by innovations¹¹ (and their associated investments) which are generated by enterprises and national innovation mechanisms, of which enterprises are part and in which the economic elite is a major and decisive actor (Dosi, Freeman, Nelson, Silverberg and Soete, 1988, parts II and V). Thus, development to a great extent depends on the economic elite's efficient fulfilment of its function in the developmental process.¹² That function is the acquisition of technological quasi-rents which, through

innovation, create monopolistic positions which creative imitation, competition and technology dissemination continuously erode and render necessarily transitory. In the words of Javier Villanueva, when Schumpeter's monopoly is established, Walras's dogs begin to chase after it.

For the economic elite, this is a "hard option"¹³ in terms of technology, risk, investment and social change. For society, it is what Napoleoni (1962), following Schumpeter, terms "development rent", which encourages a process of endogenously driven growth in which each cycle leaves capacities for generating a further endogenous development cycle (on the dynamic relationship between the cycles, see Kalecki, 1965, and the interpretation given in Nochteff, 1994).¹⁴

¹⁰ The term "development" is used here in the Schumpeterian sense, in contrast to a process tending towards a static equilibrium, with the exception of factors exogenous to the economy itself (Schumpeter, 1968).

¹¹ In the broad sense, which includes "Baumolian" creative imitation, accelerated learning, user innovation processes and product differentiations that are significant in terms of profits and market structure (Schumpeter, 1968; Freeman, 1982).

¹² In order to avoid the common confusion regarding the concept of "Schumpeterian entrepreneur", it should be noted that Schumpeter (1957, chap. II) explains that he "is not concerned with the specific factors of change but rather with the methods whereby those factors act, that is to say the mechanism of change". The "entrepreneur is merely the catalyst for this mechanism" and the profit arising from innovation (technological quasi-rent in the sense adopted here) is present in any development process, even in one where the entrepreneur has been replaced by any other agent fulfilling the same function (Schumpeter, 1968, chap. IV).

¹³ On the distinction between hard and soft options, see Esser, Hillebrand, Messner and Meyer-Stamer, 1993. In a concurring view, Kaplinsky (1995) distinguishes between what he calls the high road and the low road in economic performance, according to the type of rent being obtained ("natural resources", "skills", "human resources").

¹⁴ In the tradition of evolutionist economic dynamics, these concepts are associated more with the idea of sustained disequilibrium than with the idea of alternation between periods of disequilibrium/development and of stationary equilibrium. See, in this connection, the cyclical dynamic described by Kalecki (1965) and its comparison with Schumpeterian development in Nochteff (1994).

The Argentine economy (like most Latin American economies) does not seem to have followed this development path but rather an adaptive one of late imitation (a traditional path in the sense adopted by Freeman, 1982). Its performance is the meagre outcome of passive adjustment to exogenous stimuli or external opportunities created by other economies. The Argentine economic elite¹⁵ has adapted itself –and, to a great extent, forced institutions to adapt– to these opportunities, has kept itself shielded from competition by means of non-innovative and non-transitory monopolistic positions sustained by government policies and institutional barriers to entry, and has thus acquired political quasi-rents. For the economic elite, this is a “soft option” in the sense described. For the economy, it is not a process of development but rather a succession of booms or bubbles,¹⁶ which are more compatible with very long-term stagnation (in comparison with economies which are developing) than with a system of organizations, institutions and production forces that are capable of generating development.

In development processes, owing to the predominance of technological quasi-rent seeking, policies and institutions that promote science, innovation, industrialization and investment are of enormous importance on the agendas of Governments, economic elites and society as a whole; and endeavours in science and technology are directly linked to patterns of production, investment and foreign trade. In an economy such as that of Argentina, which is of the adaptive, lagging imitative or “traditional” type, all these questions are secondary on those agendas, and scientific and technological endeavours are only weakly linked to such patterns. It is the acquisition of political quasi-rents (and of Ricardian rents) which makes this weakness due less to an inadequate supply of science and technology than to an insufficient

effective demand for them (Cereijido, 1990).¹⁷ In short, this demand insufficiency is directly linked to the economic elite’s behaviour (choice and acquisition of soft options), which is related to the ineffectiveness of institutions in generating long-term growth, and to the weakness of social and political checks and balances that could influence, limit or change such behaviour.¹⁸

2. Soft options: a retrospective view

a) *Expansion: 1880-1914*

As already indicated, the first soft option for the Argentine economic elite was the expansionary cycle –or rather the bubble– generated largely by primary exporting and the expansion of the agricultural frontier. The combination of “natural” comparative advantages with technological and economic changes in the European economies; market imperfections (such as the non-existence of a world land market); institutional barriers to entry (local land and tenancy laws, and the systems of financing land acquisition, farming and livestock production) and privileges granted by the State enabled the economic elite in that period to acquire Ricardian rents combined with and enhanced by political quasi-rents. They led to the consolidation of an institutional system and of a pattern of economic elite behaviour that seem to have endured, despite the changes in the Argentine economy and even in the composition of a good part of the economic elite. This behaviour may be characterized by a great capacity for adaptation –of a speculative nature– in order to take advantage of opportunities to acquire political quasi-rents, for the exertion of a very strong influence on public policies and institutions, –which makes the acquisition of such quasi-rents possible–, and for rapid diversification and changes of activity. In contrast, the elite kept a low profile in terms of investment, technological innovation, production efficiency and specialization (Sábato, 1988).

¹⁵ The topics examined in this section are dealt with in detail in Nochteff, 1993 and 1994.

¹⁶ In this article, some long periods are also regarded as bubbles i) when the increase in wealth and the value of assets in one such period exceeds that sustainable by increased investment, productivity and the pattern of production and foreign trade, and ii) when they leave institutional and economic systems that are highly ineffective for a process of development. This does not mean ignoring the fact that bubbles in the more usual meaning of the term can occur within each period.

¹⁷ With the predominance of political quasi-rents, the neo-conservative recommendation regarding science and technology has a particularly perverse effect. When it is advocated that endeavours in this area should be guided exclusively by enterprise demand, it is a mistake to assume that firms have perfect technological information (Bessant, 1991); and if, in addition, the economic elite seeks non-technological quasi-rents, the error is compounded still further.

¹⁸ For a case study on the failure of public policies in such a context, see Nochteff, 1995.

b) *Industrialization*

The Argentine style of industrialization, particularly since the crisis in the 1930s that ended the first big bubble, has, to a large extent, resulted from the behaviour and attitudes of the traditional economic elite (Nochteff, 1994, pp. 52-74), which expanded, particularly after the 1940s, to include transnational industrial enterprises, giving rise to import substitution industrialization led by those enterprises. This industrialization was the second major soft option for the economic elite and gave rise to a second "big bubble" in the Argentine economy, which accentuated its characteristics of adaptation and lagged imitation, and created new restrictions on development.

Import substitution industrialization led to a heterogeneous productivity pattern or developmental Dutch disease,¹⁹ owing to the path that was chosen—the "protectionist option"—largely through the influence of some leading local entrepreneurs and the transnational enterprises.²⁰

In very simplified terms, the main features of developmental Dutch disease are as follows:

i) There is a major difference between the marginal costs of the primary sector and of the industrial sector²¹ (in reality, between those of the sectors with

"natural" comparative advantages and those with man-made comparative advantages). Marginal costs do not increase, in a continuous manner from some primary sectors to others, and then from some industrial sectors to others, but rather in a discrete manner (there are one or more "steps" in comparative marginal costs).

ii) The exchange rate tends to be situated (partly because of the economic policies adopted) around what could be called primary-sector cost parity.

Because of these two factors, monetary prices and costs in the industrial sector have been higher than they were internationally, and industrial activities expanded because they were working with an import-only exchange rate close to the industry cost parity, shaped by tariff and non-tariff subsidies.

Since the export exchange rate was not situated around the industrial-sector cost parity (effective export prices were not equivalent to effective import prices),²² the industrial sectors simply did not export (to put it very simply). The economy was basically made up of two sectors: the tradable goods production and export sector (primary sector) and the sector producing non-tradable goods requiring foreign exchange (industrial sector plus tertiary sector).

These patterns of behaviour have far-reaching effects. Firstly, they encourage a closed economy, that is to say an economy in which the tradable goods producing sector is small. This means that the greater part of the economy avoids international competition, thus facilitating the acquisition of political quasi-rents by the major economic agents, shielded in non-transitory monopolistic positions.

Secondly, the supply of foreign exchange from primary-sector exports allows equilibrium only in conditions of stagnation and high unemployment. In simplified terms, if it is desired that the non-tradables sector (industrial sector plus tertiary sector) than should grow more than the primary export sector, an external restriction is encountered. If the restriction is temporarily overcome by borrowing, future foreign exchange demand (debt servicing) increases even more, for the same level of exports (other conditions being equal), and this aggravates the problem still further. This gave rise to a "stop-and-go" economy (Diamand, 1988; Heymann, 1984).

¹⁹ The name "developmental Dutch disease" was used by Schydrowsky (1993), although the phenomenon had already been examined in the 1960s by Oscar Braun and by Marcelo Diamand (who referred to it as an unbalanced pattern of production). It was subsequently studied by a number of economists, such as Mallon and Sourrouille (1976), Diamand (1988) and Heymann (1984), who also presents a model that can explain with considerable precision the macroeconomic aspects of the 1991-1995 bubble.

²⁰ Nochteff (1994) examines the range of institutions, actors, limitations and opportunities that prompted the economic elite to favour the path of substitution industrialization, led by transnational enterprises, which is known as the "protectionist option", as distinct from the "orthodox", "devaluation", "export industry" or "extended neutrality" options. In his view, this last option was the one pursued by the successful economies of South-East Asia.

²¹ It is very important to bear in mind that, to put it very simply, the primary sector includes primary and industrial activities having a very direct connection with comparative advantages provided by natural resources, while the industrial sector produces more widely differentiated goods, where highly skilled labour has a major impact on cost and where competitiveness is closely associated with inherent capacity for innovation (including rapid creative imitation). Hence, on the basis of this classification, the primary sector would include oil refineries, vegetable oil production for bulk sale, basic milk production and even basic petrochemical and iron and steel plants, while the industrial sector would include the production of capital goods, fine chemicals, the production of high-priced edible oils, milk and cheeses for export, the production of special steels, and iron and steel services.

²² Unlike what happened in the NICs, where the so-called extended neutrality system has tended to bring the profitability of sales to the domestic market close to those of export sales.

Thirdly, microeconomic performance in the industrial sector is highly dependent on exchange-rate and trade policies. In general, changes in parity and in trade policy are far more significant for enterprises than almost any technological change. Technological efforts are not aimed at reaching leading-edge best practices, but rather at making relatively minor adjustments to existing (and generally backward) technologies introduced to a great extent through the importation of inputs and capital goods (largely second-hand or more or less obsolete). Learning paths tend to take the form of technological efforts to adapt to the limitations (of scale, or of availability of inputs, suppliers or infrastructure) found in a closed industrial economy and generated by the same developmental Dutch disease, but they do not eliminate the marginal cost "steps", and thus reproduce the disease.

Fourthly, policies relating to trade, foreign exchange, subsidies, and reserved and quasi reserved market concessions, and generally all policies that make possible the acquisition, preservation or distribution of political quasi-rents and Ricardian rents,

are key items on the agendas of the economic elite, Governments and society. Policies directed towards promoting innovation, the learning of best practices, investment and increased productivity are accordingly relegated to very secondary positions.

Finally, there is no synergy between the primary sector and the industrial sector, dynamic and static comparative advantages are not exploited, and the primary sector lags behind and does not move towards more differentiated products, in comparison with other economies (Esser, Hillebrand, Messner and Meyer-Stamer, 1993).

In short, import substitution industrialization was for the economic elite a sort of "big bubble"²³ driven by the acquisition of non-technological quasi-rents and resulting from the interaction between the institutional system and the economic elite (and other organizations and actors), rather than a process of development in the Schumpeterian sense. On the contrary, developmental Dutch disease created new economic, technological, institutional and organizational restrictions on development.²⁴

III

The neo-conservative movement and the debt-promoted bubble

Even with the limitations of substitution industrialization, during its last period (and particularly between 1964 and 1974) a process of dynamic industrialization took place: in that decade, per capita GDP growth was the highest of the century and lagged least behind other countries (Sourrouille and Lucángeli, 1980; Llach, 1987).²⁵ This dynamism was largely due to the learning processes, to the partial correction of the protectionist path, to the socio-political deadlock that placed limits on the economic elite, and to the growth of global industry and trade (Nochteff, 1994). The political and economic crisis of 1975 and the

military coup of 1976 broke this deadlock, and the economic elite recovered the power that had been partly impaired during the period of substitution industrialization.

1. Neo-conservatism and the big bubble in three periods

a) 1977-1981

From that time, the economic elite forced another period of easy options and of political quasi-

²³ Because –particularly during the initial phases– it maintained the values of profit margins and assets in the non-tradables sector (industry plus services) above the long-term values. As already stated, this leads to a kind of simplification in which a series of bubbles are assimilated into a single bubble according to the factors which drive them.

²⁴ This phenomenon was particularly evident in the import substitution industrialization period prior to the "partial corrections" of the 1960s (Nochteff, 1994). The 1950s were thus relatively the most backward decade, in terms of per capita gross product, of the whole period 1929-1983 (Llach, 1987).

²⁵ On substitution industrialization as a whole and in this period in particular, see Mallon and Sourrouille, 1976.

rent acquisition. From the standpoint of its main causal factor, external indebtedness, this period can be regarded as a single "big bubble". However, three stages should be distinguished. During the first stage, essentially between 1977 and 1981, the economic elite took advantage of the opportunity provided by the increase in liquidity and the drop in interest rates around the world. During this period, political quasi-rents focused on financial activity (Basualdo, 1987) and on non-tradeable goods sectors that were protected in the midst of intense trade liberalization. Furthermore, the extent of quasi-rents from cheap labour began to increase.

b) 1982-1990

In a second phase, after the external debt crisis that ended the first bubble (1977-1981), the conglomerates succeeded in maintaining political quasi-rents by securing large-scale transfers of income through different types of subsidies (Azpiazu and Basualdo, 1987; IMF, 1986). They accordingly continued to grow during the recessionary decade of the 1980s and built up the capital and economic power that subsequently enabled them to take advantage of the bubble generated predominantly by external indebtedness and privatizations in the 1990s. This process also made a crucial contribution to the fiscal crisis that set off the recessions and hyperinflation of the period 1989-1990.

c) From 1991 onwards

From 1991, with the virtual repetition of the phenomenon of high liquidity and low interest rates worldwide, the bubble that had begun around 1976-1977 swelled up once again. This time the neo-conservative policies had far more impact, since the combination of external indebtedness with privatizations, deregulation and trade liberalization helped to make possible the acquisition of non-technological quasi-rents.

2. A review of economic performance in the period subsequent to 1976

The performance of the economy after the breakdown of substitution industrialization can be summed up as follows.²⁶

²⁶ The figures used in this section and in the following one were prepared on the basis of Azpiazu and Nochteff (1994a), FIDE (1996), FIEL (1996), Argentina, Ministry of Economic Affairs and Public Works and Services (1995) and ECLAC (1995).

In 1995 the per capita product was 12.7% less than in 1974. Gross fixed investment in 1995 was 18.6% of GDP: 3.6% lower than in 1974.

The real average wage in 1993 was 51.2% less than in 1974 and, although no data are available on subsequent movements, it is estimated that in 1995 it was even lower.

As regards employment, between 1974 and 1995 the open unemployment rate increased by 411.8% (from 3.4% to 17.4%), while visible underemployment rose from 5.4% to 12.0%.

With reference to income distribution, in 1995 the share of the first four deciles was 28% less than it had been 20 years earlier, that of the next four deciles was 11.6% less, but that of the two highest income deciles was 24.4% higher than in 1974. The decile that lost most during the period was the lowest income decile (-41.9%), and the decile that gained most was the highest income decile (+43.5%). If one considers per capita GDP, the absolute loss suffered by the poorest decile was 52% and the absolute gain achieved by the richest decile was 29%.

Poverty increased from 4% to 20% (i.e., 600%) between 1974 and 1992-1993.

The degree of openness of the economy ($X=M/GDP$) in 1995 was approximately 15%, around 7% lower than the 1973 figure of 16.2%. The X/GDP ratio dropped by 16.7% (from 9.6% in 1973 to approximately 8% in 1995).

External vulnerability (the ratio between external debt and exports) is estimated to have increased by 164.3%. In 1974 the public external debt was equivalent to 1.4 years' exports, whereas in 1995 the public external financial debt was equivalent to 3.7 years' exports (a ratio 200% greater than that of the developing countries).²⁷

In short, Argentina's economic and social turnaround in the period subsequent to 1976 was, to say the least, very serious.²⁸

²⁷ Estimates concerning the public external financial debt in 1995 vary greatly. It has been decided to use the calculations of Machinea, 1996.

²⁸ Comparison "between peaks" may give rise to some doubt, but it should be pointed out that, in all cases, the adjustment of the yearly data for the period to straight-line paths by the least squares method confirms that these are long-term trends (Azpiazu and Nochteff, 1994a, figures 1 to 6).

3. Factors for analysing the 1991-1995 bubble

Helped by the world financial situation, the application of neo-conservative policies involving a reduced role for the State, the economic crisis, and extreme institutional weakness aggravated by hyperinflation and the decline of organizations,²⁹ the consolidated economic elite took advantage of a new bubble, this time generated largely by external indebtedness, privatizations and deregulation, in which it vigorously pursued and intensified the acquisition of political and Lewisian quasi-rents.

The combination of high peso interest rates,³⁰ the fixed exchange rate and financial decontrol prompted –as in the 1977-1981 bubble– a large-scale influx of capital. The bulk of this capital was used: i) to finance the acquisition of public enterprises by conglomerates, of which those involved in the privatization process accounted for 77% of the private external debt in 1990-1994 (Basualdo, 1994); ii) to finance a consumption boom, particularly in non-essential goods, as can be surmised from the distribution of income and the low propensity to save, lower even than the propensity to invest, given the major inflow of capital; in 1991-1994 the consumption/GDP ratio was 82.1%, while the ratio between gross investment and GDP was only 17.4% (the maximum value, in 1994, was 20%, and the figure fell abruptly in 1995).

The influx of capital and the inflation registered in non-tradable goods –boosted by consumption and high charges for privatized public services– caused the currency to appreciate. Combined with a marked liberalization of trade, they severely eroded competitiveness and shifted improvements in prices and relative profit margins, together with the small amount of investment, to the non-tradable goods sector (Fanelli, Kacef and Machinea, 1995; Kacef, 1994; Coloma, 1993).

Both domestic investment and foreign direct investment (FDI) focused on enterprise acquisition and restructuring and, to a lesser extent, on the construction of new plants. The main destinations of the investment were privatized public services and

production for the domestic market or, possibly, complementarity within MERCOSUR. Investment in new plants for tradable goods occupied a secondary place and was centred on the extraction and production of non-differentiated exportable goods, basically mining products, gas and petroleum, agricultural products and simple agriculture-based manufactures (on FDI, see Chudnovsky and López, 1994). In the industrial sectors that most improved prices and productivity, exports continued to be basically anti-cyclical, the market became oligopolistic, and investments –both actual and projected– do not appear sufficient to sustain competitiveness (see, for example, Azpiazu and Nochteff, 1994b).

Deregulation –in a very weak institutional and organizational context, with no effective anti-monopoly agencies or legislation, and during a process of privatization in which some of the largest enterprises were sold– did not transfer the fixing of prices and profit margins and the allocation of resources from the State to the market, but mainly to a group of interrelated conglomerates (Azpiazu and Basualdo, 1995). Not only did the institutional and organizational framework of the privatizations not lead to greater competition, but it actually obstructed the market mechanisms (see Azpiazu and Nochteff, 1994a, pp. 157 to 221; Azpiazu and Basualdo, 1995).

Consequently, in spite of the almost complete liberalization of foreign exchange (UNCTAD, 1995), the economy tended to become closed: the X + M/GDP ratio in 1991-1995 was in the region of 13 to 14%, one of the lowest in Argentine history; in the preceding five-year period it had been 15.8% (FIDE, 1996) and in 1969-1973, at the height of import substitution, 16.8%.

In this closed and oligopolized economy, the conglomerates forming the centre of the economic elite moved even further towards monopolistic or oligopolistic markets for non-tradable goods that were shielded from external and internal competition, enhancing and strengthening their ability to acquire political quasi-rents and diverging increasingly from the structure and behaviour of conglomerates in dynamic economies. In 1994, the last year of expansion of the bubble, almost 40% of the total profits of the 20 highest-earning firms was achieved in monopolistic or duopolistic non-tradable privatized public services sectors, a further 45% in oligopolistic activities concerned with the exploitation of non-re-

²⁹ State, trade-union, political and business organizations.

³⁰ Monetary behaviour was not totally endogenous: financial and fiscal policies tended to raise interest rates.

newable natural resources (gas and oil), and only around 13% in industry (Gaggero, 1995).

In 1994 the bubble “imploded”. The trigger was the “tequila effect”, but the main cause was the extreme external fragility of the economy.³¹ This can be seen from the growing disparity in the foreign trade balance (which went from a surplus of 8,274 million dollars to a deficit of 5,752 million between 1990 and 1994), the fall in the X/GDP ratio (from 11.9% in 1990 to 5.7% in 1994), the rise in the current account deficit (a 40-fold increase between 1991 and 1994), the very high ratio between external debt and exports, and the increase in the net public external debt by an amount equivalent to 109.5% of exports for 1994 (Poli and Peirano, 1996), despite the Brady Plan and the receipt of 27 billion dollars during the period from privatizations. (According to Machinea, 1996, it was as though an enterprise had increased its debt while at the same time selling its assets.)

A bubble in a fixed exchange rate system with convertibility similar to the gold standard does not explode, but rather “implodes”. To date, the most reliable indicator of “implosion” is the unemployment rate. As the bubble grew, the shedding of manpower from the tradable goods sectors and from the privatized public enterprises was disguised by the emergence of self-employed workers, who used their severance payments to finance non-viable activities, and was only very partially offset by the boom in the non-tradable goods sector, so that open unemployment rose from 6.9% in 1991 to 10.7% in 1994. When the “implosion” occurred, the workers shed by the non-tradables sector joined those from the tradables sector and the assets from the redundancy payments ran out, with the result that the figure reached 18.6% in 1995, i.e., an increase of 73.8% in one year (Kacef, 1994), in a situation of full employment flexibility and labour supply with diminishing wages and conditions (Marcó del Pont, 1995).

All the foregoing confirms three points: i) the economic policies based on neo-conservatism, combined with institutional fragility, the weakness of political and social checks and balances and the

behaviour of the economic elite, led to a bubble and not to a process of development; ii) the economic elite squeezed the bubble still further in order to acquire political quasi-rents, Lewisian quasi-rents (particularly from 1994 onwards) and, to some extent, rents from non-renewable natural resources (which, in the sense adopted in this article, and given the extent of government concessions in those activities, are to some extent political quasi-rents); iii) as a result, policies and efforts aimed at the acquisition of development quasi-rents have been thrust even further into the background than before. One indicator of the scant importance attached to them is the expenditure on science and technology. Its share of public spending fell from an infinitesimal 0.27% (1980-1987) to 0.24% in the 1990s, and its share of GDP has steadily decreased since 1992. In 1994, total expenditure on scientific and technological research was 0.29% of the product: ten times less than the percentage in the developed countries and between four and seven times less than in the Asian NICs (Chudnovsky and López, 1995).

4. Bubbles, political quasi-rents and patterns of production

In a closed economy with low competitiveness,³² exports tend to follow an anti-cyclical trend: thus, when the implosion occurred exports rose by 46% in the first quarter of 1995. As might be expected, this increase was not linked to greater penetration in open and developed economies,³³ but was brought about rather by the fall in internal demand, which boosted exported units, by the increase in the prices of basic commodities and by the recovery of the Brazilian economy, coupled with the rise in the value of the Brazilian real. Almost 52% of the increase in total exports and 75% of the increase in industrial exports were to MERCOSUR, essentially to Brazil (Porta, 1995).

With no figures available on GDP per branch, and following trade liberalization, the pattern of trade is a good reflection of techno-productive performance: i) the trade balance showed a surplus only when the

³¹ For a macroeconomic analysis of the bubble, see Fanelli, Kacef and Machinea (1995).

³² For a concurring analysis of competitiveness, see Messner and Meyer-Stamer (1994).

³³ In this connection, it is worth noting that in 1993-1994 Argentina had only 30 enterprises with ISO 9000 certificates of quality, whereas Brazil had 500.

“implosion” occurred and there were favourable (and fragile) exogenous conditions and ii) high priority was allocated to exploiting comparative advantages.

While other countries of the region were entering the “second export phase” of an open economy (Díaz, 1995), Argentina tended to regress to a more closed economy and a “first export phase”. In the view of Beckerman and Sirlin (1996), Argentine foreign trade’s revealed comparative advantages (RCAs) indicate that during the period these advantages diminished in manufacturing activities compared with primary activities (in particular those connected with non-renewable natural resources), in industrial manufacturing compared with agriculture-based manufacturing activities,³⁴ and in medium- and, in particular, high-technology activities in comparison with traditional industrial activities involving low-technology inputs in widespread use (non-differentiated). Comparative advantages in manufacturing activities also decreased in direct (although not proportional) relation to their use of skilled labour (Bisang, 1995).

Taken overall, analyses of foreign trade show a major technological and industrial decline,³⁵ which is consistent with the contentions in this article and, in particular, with the view of an increasing movement on the part of the economic elite towards the non-tradable goods sector and towards the acquisition of political quasi-rents: an attitude which imposes further restrictions on development.

5. Observations on the privatization and deregulation process

The privatization and deregulation process,³⁶ as implemented in Argentina, was one of the key elements

in the application of policies based on neo-conservative thinking, in the 1991-1995 bubble, and in the acquisition of political quasi-rents.³⁷

This process was the main plank of the reform of the State. In contrast, in the countries of the Organization for Economic Cooperation and Development (OECD), the reforms focused on a set of measures that included the introduction of market mechanisms, changes in the functions of the central administration and management bodies, and decentralization, far more than on privatization (OECD, 1993).

The speed and scale of the process were far greater than those generally seen in the Western world: within four years, virtually all State service and industrial enterprises were privatized.

Government action and approaches displayed very marked changes and breaks in continuity that affected the State’s negotiating capacity.

In general, the establishment of regulatory frameworks and bodies took place almost simultaneously with or, in some cases, subsequent to the privatizations.

The privatizations were used mainly as part of short-term macroeconomic policy, particularly in order to offset the fiscal and current account imbalances and to create conditions that would make it possible to maintain a fixed exchange rate, sacrificing long-term objectives.

There was ongoing and recurrent renegotiation of the rules governing privatization, in most instances in order to gain the confidence of the big firms. This increased the social costs, because of the benefits which the State granted after acknowledging that the enterprises possessed acquired rights and that the changes could affect their future profits.

³⁴ Beckerman and Sirlin (1996) show that, between 1990 and 1994, primary goods exports increased their positive contribution to RCAs by 60% and agriculture-based manufactures by 10 per cent, while energy exports’ share of trade rose from an insignificant level to a relative contribution close on 12% of positive RCAs. At the same time, the negative contribution of industrial manufactures to RCAs rose 1.5 times. These results are made worse by the fact that agriculture-based manufactures tend not to form techno-productive clusters. For example, while by-products of vegetable oil extraction have been used in Brazil to develop an intensive poultry breeding industry, Argentina exports them as “food industry waste” (one of the country’s main export items).

³⁵ For concurring results obtained using different methodologies, see Cepeda (1995a and b).

³⁶ This section identifies some of the traits of the privatization and deregulation process that contributed to the 1991-1995 bubble and to the acquisition of political quasi-rents. Consequently, it is not and must not be taken as an overall assessment of that process. No analysis is thus being made here of the substantial improvement in the provision of services or other aspects of the deregulation (for example, the increased competition in markets, such as those for professional services, or the reduced cost of services, such as port services). Nor is any analysis made here of the sharp increase in the prices of most privatized public services (Azpiazu, Bang and Nochteff, 1995).

³⁷ This section is based on Azpiazu and Vispo (1995); Azpiazu and Basualdo (1995), and Azpiazu, Bang and Nochteff (1995).

The complete disregard for expanding ownership—contrary to international recommendations and experiences—gave rise to marked economic concentration, both within the privatized companies, where the purchasers have guaranteed control, and in the economy as a whole. One small group of conglomerates diversified into completely heterogeneous activities and achieved a major presence in virtually the entire range of privatized activities. This “heterogeneous diversification” hampers microeconomic efficiency and techno-productive specialization.³⁸

The regulatory weakness and the features mentioned above were decisive factors in strengthening the positions from which political quasi-rents can be acquired. Thus, the big conglomerates have achieved: i) a very significant increase in assets, which strengthened their capacity for self-financing abroad at rates far below domestic rates; ii) conditions in which the risk is very slight or nil; iii) ample scope for price fixing; iv) considerable leeway to increase their costs by transferring profits to associated enterprises (for instance, in the purchasing of equipment or the hiring of services), and v) a significant influence on relative prices and profit margins in the economy. One indicator of this is the very large share of the privatized oil complex and public services in the profits of the 20 highest-earning enterprises.

This concentration of economic power and the consolidation of reserved markets with political quasi-rents are obstructing the emergence of a new and more competitive entrepreneurial class. Moreover, the concentration of the ownership of privatized enterprises, intensified by cross shareholdings and inter-firm agreements, combines with the weakness of the regulatory bodies and frameworks to produce constraints and restrictions. Of these, mention should be made of: i) planned investment that is even below

the very low level of the 1980s; ii) the increased risk of co-optior of the regulatory agencies, aggravated by the establishment of specific agencies for each service, with little or no coordination between them; iii) the intensification of barriers to entry other than techno-productive barriers; iv) the increasing imbalance in negotiating capacity between the State and the conglomerates, since the latter control the public services but the State still has ultimate responsibility for the service; v) the loss of negotiating capacity of the other private agents *vis-à-vis* the conglomerates; vi) a growing opaqueness of the markets and the consequent risk of transfer price practices. One example of these latter problems is the impossibility of the public authorities gaining access to supply contracts among transporters, distributors and major users of gas, or between generators and major users of electricity (in many cases belonging to the same conglomerate).

In short, many of the traits assumed by the Argentine privatization and deregulation process³⁹ ultimately led to greater imperfections in the market, to greater divergences between private and social benefits, and to similar or greater internal distortions, while at the same time reinforcing the trend towards a semi-closed and oligopolistic economy centred on political quasi-rents.

In fact, this process was a major contributory factor in the change in relative profit margins to the detriment of tradable goods. In addition, while the prices of other non-tradeable goods that have an impact on the costs of tradable goods may be reduced by devaluation or deflation, neither of those measures can bring about a significant reduction in the prices of privatized public services, owing to the fact that they are implicitly or explicitly indexed through the rate of exchange, or owing to their low elasticity, and/or the oligopolistic nature of the respective markets.

³⁸ This diversification does not take place around a techno-productive nucleus in medium- and high-technology activities usually in the tradables sector (in contrast to what occurs in developed economies), or in a small number of nuclei of this type (as tends to happen in the NICs). For example, one of the main local conglomerates has diversified and expanded from iron and steel into electricity distribution, gas transportation, gas distribution, petroleum production, telecommunications services, rail transport, port services and highway concessions (Basualdo, 1994).

³⁹ These traits distinguish the Argentine privatization and deregulation process from successful privatization experiences and at the same time make it in many respects similar to the more negative experiences of Eastern Europe (on these, see OECD, 1994).

IV

Some conclusions

"Economic history is overwhelmingly a story of economies that failed to produce a set of economic rules of the game that induce sustained economic growth."

Douglas North

The structural reforms and economic policies implemented in Argentina since 1991 have given rise to a bubble generated largely by borrowing, privatizations, deregulation and trade liberalization; this bubble intensified the economic elites' seeking of political quasi-rents that were unconnected with technology, investment and competition in external markets, leading to a further decline in the economic structure⁴⁰ and in foreign trade, and to an economy as closed as that of the period of import substitution industrialization.

The recommendations of what Ralf Dahrendorf called the conservatism of unconcern, adopted in large measure in the neo-conservative propositions, concur with the socio-economic behaviour of the

traditional economic elite of Argentina (and of many other countries of the region), creating further restrictions on the transition to a more open, dynamic, innovative and competitive economy. In view of this and following the observations of Schumpeter (1968), it is reasonable to think that academic and public policy debate and research should be dealing increasingly with the problems arising in the interaction between institutions and entrepreneurs or, in general, between the institutions, agencies and organizations specific to each economy, since the building of efficient institutions and the establishment of a system of checks and balances between social actors are prerequisites for development (Nochteff, 1994).

(Original: Spanish)

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⁴⁰ According to Nochteff (1994), this decline was a continuation of that which began in the mid-1970s.

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