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## Open Economy, Closed Polity

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OPEN ECONOMY, CLOSED POLITY?

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## OPEN ECONOMY, CLOSED POLITY?

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### 1. INTRODUCTION

The suggestion, inspired by some recent Latin American experiences, that Third World economies open to international trade and capital flows are inexorably associated with authoritarian political regimes seems one that is very odd yet intriguing to one trained in mainstream economics. The standard training imparted in leading Ph.D.-granting centers provides only a little help in analyzing whatever links there may be between openness and authoritarianism, while the less formal tradition which the average graduate student will pick up at those centers, either by reading selected paragraphs from Smith, Ricardo, Mills, and even Marx, or by paradigmatic "common-sense," actually leads to an association of closed economies with assorted despotisms. This essay is an attempt by someone trained in mainstream economics to reflect on some of the various hypotheses, conjectures and insinuations which have been put forth regarding the link between openness and authoritarianism, particularly in the Latin American context. The broader topic of connections between economic systems and political freedom will not be explored; the nature and mainsprings of the authoritarian state must also be left aside.

Perhaps because of the limited aim of this essay, it is not easy to find clear statements of revisionist hypotheses and arguments linking open economies with authoritarian regimes. One line of reasoning argues that to compete in international markets and to attract investments, the domestic labour force must be kept cheap and docile. Investments with long gestation periods are also said to

require more predictable political environments; openness may be accompanied by more of those investments, calling forth authoritarian leaders eager to supply stability and order. Another line of reasoning emphasizes not the steady-state political requirements of openness, but the political preconditions for a transition from a closed to a more open economy. Such a change, the argument goes, will inevitably hurt vested interests which can only be disciplined by an authoritarian regime. Once the transition is accomplished, the need for authoritarianism would presumably disappear. While the first line of reasoning is usually found in the neo-Marxist literature, the latter is often suggested in the Capitalism-Now Freedom-Later literature.

Both lines of reasoning frequently make reference to what contemporary mainstream academic economics says and does not say regarding openness and several economic variables which may influence a country's political regime. The next section of this essay will sketch my(perhaps idiosyncratic) understanding of that matter. It should be useful in such an exercise to differentiate between what may be termed the academic and practical orthodoxies of mainstream economics.<sup>1/</sup> The former is the product of leading academic centers, is careful in stating its assumptions and conclusions, and tends toward flexibility and agnosticism. Its leading thinkers often are its own major critics, frequently curious about heterodox notions. For the topic at hand, glittering examples include James Meade, Bertil Ohlin, and Paul Samuelson. Practical orthodoxy is more assertive: it is found in editorials of the business press, among those who sought only "bottom-line" knowledge or just a smattering of paradigmatic "common-sense" from

their Master or even Ph.D. degrees, and among some of the more politically or financially ambitious (or simply lazy) academics away from the rigor of their Chairs. The main focus of the next section will be on academic orthodoxy; practical orthodoxy will not receive much attention, although its importance in the political world and in confusing the topic at hand is not denied.

The third section of this essay will be a rather quick overview of key events in Latin American economic history up to the mid-1960s which have helped to mold perceptions about openness. Since the discovery of the continent, Latin America has undergone a number of economic openings and closings, each leaving behind crucial memories which naturally influence one's gut reaction in discussing the topic of openness (say "sugar" to Cubans and many will reply "slavery"). The economic history of various Latin American countries should also provide, if not rigorous tests, at least some notion of the robustness of generalizations about links among openness, domestic economic variables and authoritarianism.

The fourth section will extend the historical narrative to the rest of the 1960s and to the 1970s, a period singularly traumatic for the region, when discussions about openness and authoritarianism became particularly urgent. A final section will present what I regard as the few valid generalizations arising from the rest of the essay and the many questions left open.

## 2. FROM THE MAINSTREAM: STURDY PROPOSITIONS OR CHIMERICAL FANTASIES?

Openness may refer to international trade in goods and services, or to international flows of capital and labor. Modern academic orthodoxy, contrary to popular impressions, has had surprisingly little to say about the welfare consequences of international factor flows. Until fairly recently, the bulk of serious research on international economics referred to commodity trade: the profession analysed nations exchanging wine for cloth, apples for blankets.

For many years I have been puzzled by the animosity shown by some heterodox economists toward the Heckscher-Ohlin-Samuelson models of international trade developed since the Second World War. Compared with earlier mainstream views of international trade, the modern formulations are much more modest about what can be claimed in favour of free trade and contain results which earlier orthodox economists regard as troublesome. For example, the Stolper-Samuelson theorem rigorously showed that freer trade policies could make some members of a nation absolutely worse off; in other words, not only were the gains from trade unequally distributed within a country, but for some groups there could also be losses under laissez-faire. Post-war welfare economics also emphasised that unless those benefitting from a certain policy actually compensated those made worse off by it, one could not say that the policy was desirable.

A recent interchange between Ronald Findlay and Gottfried Haberler illustrates this contrast between the new and the old. Haberler first stated that income distribution within LDCs had nothing to do with the international economic order. Findlay invoked the Stolper-Samuelson theorem. Haberler replied:

"As far as the Stopler-Samuelson theorem is concerned, I would say that it is ingenious from the purely theoretical standpoint but is of no help in the present context, because it is based on a two-factor model and breaks down, as Stopler and Samuelson recognize, when we introduce, as we surely must, more than two factors and two types of income, different types of labour, salaries, profits, interests, and so on. I therefore conclude that my statement that inequality of income has very little to do with the international order has emerged pretty much unscathed from the discussion. And the little systematic influence trade may have on income distribution may...go in either direction..."<sup>2/</sup>

Whether an assumption is judged to be a brilliant simplification or an unexcusable distortion of reality very much depends on whether one likes the conclusions drawn from it. The Findlay approach is an example of modern academic orthodoxy at its best: using its analytical tools it opens the way to systematic exploration of links between trade and income distribution, replacing the somewhat obscurantist older view, so timid in granting the possibility that anybody may be hurt by openings. The Findlay approach will not reach simple conclusions such as "trade benefits everybody" or "trade hurts everybody". It all depends (to the dismay of the lazy, the impatient or the seeker of mass-mobilising slogans) on the circumstances in which the trade takes place. But modern academic orthodoxy goes beyond boorish skeptical ignorance.

Take a country whose most abundant factor of production is land; a trade opening should witness land-intensive exports and benefits to landowners. This could improve income distribution if land is scattered evenly among sturdy Jeffersonian families and if the other major factor of production is a bundle of urban capital and labour, made up of a minority of families who had benefitted from trade prohibitions. Under these circumstances, a plausible conjecture is that freer trade will also strengthen democratic forces and contribute to a freer flow of ideas. Latin American history does not provide many examples of this possibility,

although Costa Rica and some Colombian coffee—growing areas approach it. But the point to be made here is that one cannot say much about the link between trade and income distribution without knowing something about the distribution of land. If only one family owns the land, it seems foolish to blame free trade for a bad income distribution. Decreasing trade without touching land tenure will be an expensive and probably short-lived way to improve income distribution.

The Heckscher-Ohlin-Samuelson positive theory of the structure of international trade assumes that a given production function for each industry is known to all economic agents all over the world. The model can accommodate differences and changes in technology, but not gracefully. Continuous innovations, both in production processes and in products, and their international diffusion seem best handled in other models, which may include economies of scale and product differentiation. Technological change not instantly diffused will naturally generate quasi-rents to those originating it; leaders may have to continually innovate not just to grow but even to maintain their real income in the presence of technological borrowing by follower countries. The market for technology will show obvious differences from markets for cloth and wine; it is not clear that free trade in technology will benefit both sides, and leaders will be tempted to restrict their sales. As noted by Paul R. Krugman:

"Success by less developed countries in accelerating their adoption of new techniques can leave workers in developed countries worse off; and it is easy to imagine that by encouraging protectionism such success could be self-defeating."

It is interesting that these words appeared not in the Journal of the Union of Radical Political Economists, but in publication not famous for its heterodoxy.<sup>3/</sup>



Other post-war theoretical developments have added to the need for care in making the case for openness. Second-best theorising opened a Pandora's box of models that, by noting that some markets were either missing or incomplete, by assuming this market imperfection or that instrument limitation, could lead to a disconcerting variety of results regarding the effects of freer trade on welfare and desirable policies. Under certain assumptions, yet using modern orthodox methodology, it can be shown that free trade would lead to a worsening of a country's welfare; autarky would be preferable to free trade. Even technological change and growth can be shown to be immiserising for a country under some circumstances. True, the major message of these models is that while government actions are required to correct distortions, and thus laissez-faire is out, it is unlikely that first-best policies would involve trade restrictions, so free or freer trade was still desirable. But if first-best policies are not feasible, a great deal can be justified depending on one's judgment on particular constraints and willingness to accept noneconomic considerations.<sup>4/</sup> Judgments will differ on whether one can expect the required finesse from public officials in charge of these matters, but mainstream academic economics does provide the analytical tools to establish non-dogmatically a hierarchy of policies, ranging from first- to nth-best.

There is a serious gap in the array of analytical tools provided by mainstream trade theorists, who typically rely on the methodology of comparative statics. The path between two equilibrium situations is seldom discussed, because standard models are not suitable for those explorations. The policy maker who wonders what will happen on the way to freer trade may get some sensible advice but few firm predictions from the scrupulous trade theorist. Practical-orthodox quacks have

often rushed in to fill this gap in academic analysis.

Just as 1914-1950 bred pessimism regarding the net benefits of international trade, 1950-1973 was conducive to optimism. The sturdy academic proposition that some trade can potentially make everyone better off, as compared with no trade, was increasingly turned by some practical orthodox into the conviction that more trade at all times, places and conditions will not only improve efficiency and accelerate growth, but also increase employment, improve income distribution and reduce governmental corruption. The question that naturally followed was: If all of these good things, why not political democracy also?

It was perhaps the exaggerated claims made for the benefits of freer trade that led some observers to wonder how such a wonderful economic engine could often be associated with monstrous political machines. It was only a small further step in the dialectical crescendo to argue that authoritarian politics was a necessary condition (and to some perhaps not too high a price to pay) to obtain such wondrous economic results for at least part of the population.

The 1950-1973 period also witnessed the blooming of transnational enterprises (TNEs). "Wine Inc." and "Cloth Inc." spanned the world and every year came out with a "New Apple" and a "New Cloth." The question that must be asked is whether this is irrelevant institutional detail or something likely to modify even sturdy mainstream propositions. Does it matter for economics or politics whether exporters are Jeffersonian family farmers or Differentiated Apples, Inc., an integrated agrobusiness which handles apples from seed to mouth and hires the Mid-Ocean Auctioneer as PR man? This is a tougher

challenge to mainstream orthodoxy than complicated neo-Ricardian models of steady-state growth and heterogeneous capital goods, which can generate ahistorical chimerical fantasies of their own.<sup>5/</sup> Indeed, several kinds of traditional economic theories, from neoclassical to Marxist, are uneasy in the presence of imperfect competition and its modern corporation, and standard democratic theory has little room for "corporate citizens."

That so much of technical change is generated or diffused by oligopolies further complicates the analysis. Given the diversity of special assets and of the stimuli triggering foreign investment, one may doubt a priori claims regarding unambiguous welfare implications of TNE activities.<sup>6/</sup> This is reinforced by noting the heterogeneity of LDCs, not just in domestic market size and natural resource endowment, but also in the responsiveness of their government officials to different domestic social groups and in the bargaining ability of those officials. Such an agnostic approach is in the spirit of that line of economic thought which teaches that private profit-seeking behaviour may lead to socially desirable results but only if certain conditions are met, conditions which involve both economic and political variables, and whose presence cannot either be taken for granted nor regarded as impossible under LDC conditions.

The analysis of trade and investment in the context of specific historical circumstances should clear up at least some of the uncomfortable mists of agnosticism left by the "it all depends" of theorists. We have not discussed mainstream theoretical analysis of international flows of labour, a topic that only recently is being rediscovered in major academic centers. Many have noted the contrasting reactions to

a freer flow of capital vs a freer flow of labor among observers, including academic ones, in the industrialized world. Market imperfections, noneconomic reasons, or just "common sense" are more readily found to justify limiting the flow of the latter.<sup>7/</sup> This is how Gottfried Haberler reacted to Ronald Findlay's observation that a truly liberal international order should provide free movement not only of goods and capital but also of people:

"I, for one, simply took it for granted that there is no free migration from the LDCs to the DCs, and only in a few rare cases between the DCs, nor is there free migration between the LDCs for that matter. One may deplore this, but it would be unrealistic to expect a change. It is even doubtful whether a greater international mobility of labor can be regarded as desirable from the standpoint of international peace and harmony, despite the economic<sup>8/</sup> benefits for all participants that may be expected." —

### 3. SOME OPENINGS AND CLOSINGS IN LATIN AMERICAN HISTORY

Writers on the political economy of Latin America seem almost obsessed with the external sector as the source of all that is good or bad in the region.<sup>9/</sup> This is not surprising given the history of Latin America. The conquest of the continent was a sui generis forced opening of native economies making most local residents terribly worse off. (So far no bright cliometrician has challenged this conventional wisdom; Iberian conquistadores are perhaps less charismatic than Southern slaveowners). No fancy algebra nor definitional exercises are needed to call the system that emerged one of exploitation or unequal exchange. Encomiendas, slavery and debt-peonage characterised "the labour market;" royal favours, legal trickery and the force of arms cleared "the land market". Trade was limited as to countries, commodities and even harbours. Future generations were

to remember not only the trauma of forced opening but also the peculiar prosperity it yielded the conquering nations. Thoughtful Mexicans and Venezuelans, contemplating their present oil riches, wisely recall the melancholy rise and fall of Spain during the Sixteenth and Seventeenth centuries. An opening based on exhaustible natural resources, whether silver or oil, may make you very well off today but may induce habits and economic and social structures that, when the silver and oil run out, will make you sink back to a poverty perhaps worse than that of pre-bonanza days. Judicious intertemporal trade among generations of the same society, i.e., maintaining a prudent balance between consumption today and tomorrow, must accompany international trade based on exhaustible natural resources, otherwise openings may not lead to permanent gains. Even in the case of trade based on non-exhaustible natural resources yielding easy rents there are obvious dangers that a society may fail to expand into other sources of profitable trade.

The Bourbon liberalisation of decrepit Iberian mercantilism during the second half of the Eighteenth century led to export-led booms in many parts of Latin America. As the appetite grew with the eating, local elites became increasingly restless and resentful of the still extensive trade restrictions. Most of the leaders of the Latin American independence movements blamed Iberian crowns for artificially delinking the region from promising external markets. An 1800 tour of the "de-linker" Samir Amin<sup>10/</sup> through the flourishing "Economic Societies of Friends of the Country" might have required an escort of loyalist troops (or of poor but royalist pardos). To the patriotic intellectuals it was clear at that point that the less enlightened a despot and the greater the degree of political tyranny, the more trade restrictions

one would find. Arrogant and often ignorant Iberian bureaucrats had more to do with the popularity of such an idea than the writings of the peripheral Scot.

The excessive hopes of the liberal patriots were dashed during the chaotic 1820s. The destruction and disorganisation caused by the wars of independence, veritable civil wars, and unfavorable international market conditions combined to make post-liberation openings weak or ambiguous in their impact on growth. Even if the supply was willing, the demand was weak; as noted by Arthur Lewis, before the second half of the nineteenth century the British and European industrial revolutions needed few inputs from today's Third World.<sup>11/</sup> The United States South dominated the cotton trade, and only a few luxury products, such as sugar, could overcome high transport costs, thanks largely to slavery and the "mining" of new soils. The post-independence decades are one of the most obscure periods in Latin American economic history, but one may conjecture that in most of the region per capita incomes in 1850 were below those of 1800. After a burst of libertarian measures, immediately following independence, a conservative and traditionalist reaction spread throughout most of the new nations, generating titanic despots, who to this day exert enormous fascination.

Indeed, in the feverish intellectual climate of the 1960s, those great tyrants, who had allied themselves with a very pre-Maryknoll Church and had opposed public education, were rediscovered and glorified by some segments of the Left. The obscurity of the period encouraged their being perceived as great industrialisers and opponents of "the imperialism of free trade." The liberals were cast as the destroyers of local crafts and manufactures, in an unholy alliance with British

imperialism. By some of these revisionist accounts, a good share of the time of British leadership during the first half of the Nineteenth century was devoted to snuffing out Paraguayan industrialisation. This type of revisionism has not spread to Mexico, whose Nineteenth century conservatives ended not with the courageous stand of a Lopez but behind the weak shield of a Maximilian.

By the last third of the Nineteenth century growing demand in Europe and North America for primary products and a drastic lowering of ocean freight-costs presented tempting trade options to most Latin American countries. Local resource endowments and probably domestic politics influenced the rapidity and degree of the openings that took place and which continued at least until the First World War. Thus, the Argentine and Uruguayan openings came earlier and went further than that of Colombia, whose civil wars continued until the beginning of this century.

By the late 1920s Latin America actively participated in international trade, was an important recipient of international capital flows, and some countries had witnessed large inflows of labour. Monetary arrangements by the late 1920s tended to conform with the restored international gold standard. Relative to its past and future history, the region probably reached its maximum degree of opening toward trade, capital and labour during the 1920s. The crude indicators of opening and development shown in Table 1 emphasise the heterogeneity found in the region regarding both opening and development; compare the figures for Argentina, Chile, Cuba, and Uruguay, at one extreme, with those for most of the Caribbean and Central America, Bolivia, and Ecuador at the other.

We do not have indices of political democracy for those years; nor do we have estimates of per capita income for more than a handful of countries. The per capita imports shown in Table 1 are likely to be highly correlated with two variables: positively with per capita income and negatively with size of country, measured by population. Bearing these two offsetting influences in mind and leaving aside colonial or quasi-colonial territories, Table 1 suggests that the degree of political democracy in Latin America in the 1920s was correlated with per capita income. But the correlation is unlikely to be very high, and as later years were to show, far from robust. Table 1 offers the stronger hint that in the 1920s relatively high per capita incomes went together with a high degree of opening to both trade and investment, even if openings were to be measured not as per capita trade and investment but as trade as a share of gross national product, and as foreign investment as a percentage of all capital. Again, however, such gross correlations are unlikely to take us very far, at least using ranges observed in Latin America. Specific features of national histories are likely to dominate the explanatory power of macroeconomic variables.

Take, for example, the cases of Chile, Cuba, and Uruguay as they stood in the late 1920s. Their per capita incomes were probably roughly similar, as were their populations and opening to trade. Yet both the extravagant Cuban opening to foreign capital and its miserable politics must be explained by its quasi-colonial status and by geography. Domestic income distribution and politics in these three countries also had something to do with the characteristics of major export products: mineral, tropical and temperate staples surely had different Hirschmanesque



TABLE 1

Indicators of Openness and Development; Latin America circa 1928

	Openness		Development			
	Current US\$ per capita		Percentages of Population		Per 1,000 Inhabitants	
	Imports	Stock of British and U.S. Investments	In cities of 25,000 or over	Able to read and write	Railway miles	Telephones
Argentina	\$80	\$258	35	60	22	19
Bolivia	9	56	9	30	4	1
Brazil	10	47	13	26	5	3
British West Indies	41	na	na	na	2	6
Chile	33	195	27	44	13	8
Colombia	16	41	17	25	2	3
Costa Rica	35	134	11	30	9	5
Cuba	72	494	24	48	8	18
Dominican Republic	27	24	3	41	1	2
Ecuador	5	24	11	20	3	2
French West Indies	22	na	na	na	na	3
Guatemala	10	39	15	25	2	1
Haiti	7	12	5	10	1	1
Honduras	15	52	4	28	14	2
Mexico	11	172	15	38	9	4
Nicaragua	16	43	17	20	3	2
Panama	29	88	19	26	6	16
Paraguay	14	34	20	40	5	1
Peru	13	53	10	24	4	2
Puerto Rico	76	na	na	na	2	9
Salvador	9	15	18	35	2	2
Uruguay	50	164	30	62	11	16
Venezuela	23	82	9	29	2	4

Source: Max Winkler, Investments of United States Capital in Latin America.  
 Port Washington, New York: Kennikat Press, 1971 (First published in 1928))  
 pp. 276, 278, 283 and 286-7.

The letters na indicate data are not available.

linkages. Post 1929 history for these three countries also shows the bewildering variety of political paths which may be taken even by economies similar in per capita income and their degree of opening to trade. But a detailed comparison of these three fascinating economies and polities cannot be undertaken here.

There are additional measures of openings besides the ones suggested in earlier paragraphs. An important one would be a country's policies toward trade and international flows of capital and labour. One could, for example, compare levels and structures of tariffs and subsidies on traded goods and quantitative restrictions on investment and migration. Domestic policies, factor endowments and other domestic variables interacting with external conditions will in fact yield such observed measures of opening as imports as a percentage of gross product. Regarding tariffs, the then predominant instrument to restrict trade, it would be difficult to argue that in the 1920s protectionism was a general banner of progressive political movements in Latin America. The Argentine Socialist Party was firmly for free trade in goods (and for the gold standard as well). One of the most interesting protectionist experiments during that decade in Latin America occurred, of all places, in Cuba, and was sponsored by General Gerardo Machado, known otherwise as "The Butcher." The Leguia dictatorship in Peru was frankly protectionist, at least since 1922. Contrary to widespread misconceptions, Latin American countries did not embrace free trade absolutely even during export booms. In most countries tariffs were fairly high both for revenue and for mildly protectionist purposes. A modest but significant import-substituting industrialisation process had started in many countries before 1929. Argentina and Brazil witnessed in the 1920s

tariff-jumping direct foreign investment in manufacturing. In many countries there were severe criticisms of monoculture and the concentration of exports on a few markets. But these legitimate pre-occupations typically led to prescriptions for diversifying export products and markets rather than delinking from the international economy.

A clearer picture existed regarding foreign capital, where the need to bargain and regulate more effectively was felt from the Rio Grande to Patagonia. Modern mainstream theorists, aware of the oligopolistic nature of many industries where foreign capital concentrated, and of the Ricardian and Hotelling rents yielded by natural resources exploited by foreign enterprise, may find little to quarrel about with the modest Latin American aspirations of those years. Some types of international labour flows were also viewed with disfavour among progressives and others; most democratic Cuban opinion disliked the inflows of labour from elsewhere in the Caribbean during the sugar harvest. Such species of labour protectionism was not without racist overtones, like that practiced in Australia for many years, and that which marked the end of laissez-passer in the United States during the 1920s.

A comparison between Latin America and Africa and Asia circa 1928 was bound to suggest net positive dividends in terms of economic and political welfare due to sovereignty and a sustained non-preferential opening to global international trade, in spite of the obvious flaws in Latin American societies: skewed income and wealth distribution, vulnerability to shocks from the world economy, an irritating reliance on foreign capital and limited political participation by broad segments

of the population. A comparison between the Latin America of 1928 with that of 1878 would have yielded a similar feeling of relative satisfaction, in contrast with an 1828-1878 comparison and, alas, also in contrast with a 1928-1978 Southern Cone comparison.

Depression and war generated external demand and supply shocks to Latin American economies during the 1930s and 1940s. Trade declined absolutely and relative to gross national product; capital flows practically disappeared as early as 1929; and domestic rural-urban migrations dwarfed any international ones. The relatively healthy reaction of many countries in the region to those cataclysmic events has often been narrated: domestic manufactures and even primary products replaced many imports, and domestic savings financed nearly all capital formation.<sup>12/</sup> During the early years of the crisis most incumbent administrations were swept out of power; few other political generalisations seem possible. Import substituting industrialisation proceeded under Conservative regimes as in Argentina, as well as under Reformist ones, as in Mexico. Changes in relative prices, generated in world markets or as a consequence of attempts to equilibrate the balance of payments, plus stop-gap measures to deal with depressed demand were observed in most countries with some degree of autonomy in economic policy, regardless of the precise colouration of governments.

These closings of the 1930s and early 1940s did stimulate inventiveness among public and private actors. New public agencies to promote development were created and new national entrepreneurs appear to have come to the fore. The economic and political power of export-oriented traditional landowners waned. By the end of the Second World War the relative position of Latin America in the world economy looked strong, and these nations had a modest but significant voice in the emerging Bretton Woods institutions and the United Nations.

But Latin America during the 1930s and 1940s appears healthy relative to the depths of depression and the destruction and political horrors elsewhere. It is doubtful that per capita incomes grew during 1929-45 faster than during earlier decades; available evidence shows that they grew less than in later years. Except for Brazil, manufacturing growth was lower during 1929-45 than in earlier or later years. The relatively good performance of countries with significant autonomy in economic policy, including not only large countries like Argentina and Brazil but also Chile and Uruguay, was to an important extent based on the economic and institutional infrastructure developed during the era of export-led growth. Large pre-1929 exports in those countries led to the high per capita imports reported in Table 1; those high per capita imports provided rich and obvious targets for entrepreneurs during 1929-45.

The immediate post-war years, say 1946-48, may have witnessed the peak of Latin America euphoria. In most countries, external demand for traditional exports boomed again, and the supply of capital goods and intermediate products still difficult to produce in the region was becoming more plentiful than in earlier years. Contrary to the gloomy views of some conservative observers, industrialisation not only maintained gains registered during the war but advanced further in the post-war world. It was during 1946-48 when value added in Latin American manufacturing surpassed that in rural activities. As late as 1953, when he should have known better, General Peron was telling General Ibanez, then President of Chile, that there is nothing more elastic than the economy. As noted by Albert Hirschman the industrialisation of the 1930s and 1940s (coupled with favourable terms of trade during

the immediate post-war period) led to delusions of economic invulnerability among some policy makers.<sup>13/</sup>

If import substitution, protection and rigorous exchange controls had done so well during the 1930s and 1940s, why not continue and strengthen those policies? The fierce protectionism and arrogant economic nationalism embraced by major industrialised countries since the late 1920s had scarred peripheral nations who prior to 1929 had allocated their meagre resources largely on the assumption that hegemonic powers were serious about free trade and convertibility. The Bretton Woods agreement and the International Trade Organisation (ITO) promised a partial return to freer trade and some convertibility, but the abortive British return to convertibility in 1947 and the 1950 death of ITO in the United States Congress were ominous signs. A sharp recession in the United States during 1948-49 and the difficulties experienced by European post-war reconstruction (before the Marshall Plan) revived fears of a new Great Depression. The coup d'etat in Prague and the Berlin blockade in 1948, the victory of the Chinese communists in 1949, and the outbreak of the Korean war in 1950 made those forecasting an imminent world war worthy of at least a hearing. Even if a hot world war was avoided, a prolonged cold war between the two superpowers looked very likely, as evidenced by the signing of the North Atlantic Treaty Organization (NATO) and the detonation of the first Soviet atomic bomb in 1949.

An economic opening under those circumstances seemed to imply for Latin American countries the abandonment of any pretensions to an independent foreign policy. Many pre-war European markets appeared lost or reduced; the old continent could not be counted on, as in the past, to act as an offsetting influence to that of the United States.

Around 1950 "The Third Position" was the monopoly of Argentina, Spain, Sweden, and Switzerland, neither a politically homogeneous group nor a formidable economic block. Naturally, those who had prospered in Latin America under the protective circumstances of the 1930s and 1940s made the most of the gloomy outlook for the international economy. Shortages of external supplies of steel, shipping, and weapons during the early 1940s placed many a member of the Latin American Armed Forces in the post-war protectionist camp.

The 1950s mood of export pessimism, which nevertheless rejected autarky, predominating in Brazil and the Southern Cone countries well into the 1960s, was expressed in a 1953 report of the United Nations Economic Commission for Latin America. Discussing possible export incentives, the report noted the instability of foreign markets, adding:

"A sharp fall in prices, such as that which occurred a short time ago, while retaining some of the benefits from the increase preceding the Korean War, revives a series of previous vicissitudes which hardly encourage production for export. Although coffee prices are today relatively high, it should not be forgotten that Brazil was once obliged to destroy large unsaleable stocks of this commodity. For similar reasons, during the war, Argentina accumulated several grain harvests which had later to be wasted as emergency fuel. In contrast, the prospects on the domestic market are generally more stable, above all, in manufacturing activities. Industry, however, requires certain exports which provide it with essential goods."<sup>14/</sup>

Some medium and large Latin American countries, such as Mexico and Peru, early in the post-war phased out a good part of their depression and war time policies, moving towards more evenhanded incentives between exports and import substitution, while retaining non-trivial levels of protection. The Peruvian transition was managed by the dictatorship of General Odria; the Mexican one occurred under the administrations heir to the Mexican Revolution. Central American countries, which had exercised little policy choice during 1929-45, on the whole continued to

ride along with the impulses emanating from abroad, come what may. These small, open and mostly passive economies registered as a group impressive growth rates in exports and gross national product during the 1950s and 1960s. Those two decades also witnessed economic expansion in both Mexico and Peru. Curiously, the relatively open and fast-growing Central American and Peruvian economies moved toward greater protectionism during the early 1960s, perhaps under Southern Cone influences, but without reaching the extreme protectionism of that region.

Brazil and the Southern Cone, which so many social scientists seem to regard as the whole of Latin America, struggled along with stagnant exports and increasingly expensive import substitution until around the mid-1960s, when an opening trend, timid in some countries, became noticeable. The persistence of 1930s trade policies into the 1950s hurt Brazil less than Argentina, and hurt Uruguay more than Argentina, the reason being that in small markets and in the context of an expanding economy the costs of protection, in terms of efficiency and growth, escalated sharply.

Table 2 compares the dollar value of Latin American exports during the five years 1961 through 1965 with those registered during 1946 through 1950, with all data at current prices. During an interval of fifteen years a variety of export records were achieved. Luck in the commodity lottery and other particular events and circumstances influenced the outcome, but a role for trade policies would be difficult to deny. (Those trade policies may have led to some Latin American countries gaining at the expense of others' market shares.) Compare the performance of Chile with that of Peru, those of Uruguay and Costa Rica, and those of



TABLE 2

Dollar Values of Latin American Merchandise Exports At Current Prices, 1961-65

(Values for 1946-50 equal 100)

Nicaragua	535
Peru	359
El Salvador	334
Panama	314
Ecuador	303
Venezuela	278
Costa Rica	258
Mexico	244
Guatemala	228
Chile	206
Dominican Republic	204
Honduras	184
Colombia	168
Paraguay	149
Haiti	121
Brazil	120
Argentina	99
Bolivia	96
Cuba	94
Uruguay	92

Source: Basic data obtained from Naciones Unidas, America Latina:

Relacion de Precios del Intercambio. (Santiago de Chile, 1976.)

According to this source, for Latin America as a whole import unit values in 1961-65 stood at 128, with 1946-50 equal 100

Argentina and Mexico. The conjecture that feeble external demand during the 1950s induced the persistence of favourable incentives for import substitution is weakened by the substantial export expansions of many countries, large and small. Somoza's Nicaragua heads the list, and the then democratic Uruguay is at the bottom, but no robust political generalisations emerge from Table 2. Costa Rica does somewhat better than Guatemala, while Paraguay and Haiti have export performances about as dismal as that of the then democratic Brazil.

When a longer retrospective look is taken at the evolution of Latin American foreign trade, the astonishing fact emerges that in most countries (or at least in countries where the largest share of Latin Americans live) per capita imports, measured at constant prices, were during the early 1960s below, in some cases substantially below, levels reached during the late 1920s. Table 3 lists countries for which such data are available. The growth in per capita Gross National Product which occurred during that interval clearly involved profound shifts in both production and consumption structures. The fine performance of El Salvador is a reminder, if one is needed, that a prosperous external sector need not eliminate all development problems. The similar performance of Mexico and Venezuela is also interesting; the latter underwent an oil boom during the period covered in Table 3, while the former saw its oil exports dwindle and vanish after the 1938 nationalisations.

TABLE 3

Per Capita Import Quantum of Some Latin American CountriesIn 1963-65 Relative to 1928-30

(1928-30 = 100)

Argentina	38
Brazil	60
Colombia	71
Chile	59
Ecuador	171
El Salvador	259
Mexico	90
Peru	201
Venezuela	92

Sources: Merchandise imports at constant 1963 dollar prices obtained from Naciones Unidas, America Latina: Relacion de Precios del Intercambio (Santiago de Chile, 1976). Population data obtained from United Nations, Statistical Bulletin for Latin America (New York, March 1964). Peruvian data refer to 1929-30 and 1964-65.

#### 4. OPENINGS SINCE THE MID-1960s

This section will review some salient features of the trade and financial openings which have occurred in Latin America since approximately the mid-1960s. The variety of experiments has been large; that variety has existed regarding timing, persistence, instrumentation, political circumstances, and even direction of policy trends. For example, Colombia has on the whole followed a clear trend toward opening in trade since 1966, in the sense of moving toward more balanced incentives between export and import-substituting activities, while Brazil moved in that direction during 1964-73, showing some hesitations since then. However, both countries have maintained throughout significant restrictions on capital flows. Argentine political instability led to bewildering changes in trading and payments policies during 1963-81. The Peruvian Armed Forces marched against the general trend in the late 1960s and 1970s, but the new constitutional administration is returning to traditional Peruvian policies. In spite of their variety, some generalisations regarding the economic results of the openings may be presented. The heterogeneous political circumstances surrounding the openings will also be noted.

Moves toward export promotion worked in the sense that the target of expanding exports was achieved. Export pessimists were simply wrong; when incentives were provided both domestic supply and external demand proved to be sufficiently elastic. While Brazilian and Colombian merchandise exports, measured at current dollar prices, expanded between 1970-71 and 1978-79 at an annual rate of 22 percent, those for Peru grew at only 12 percent. Fast export growth was accompanied by substantial commodity diversification; by 1981 coffee amounted to less

than 15 percent of Brazilian merchandise exports, a fact few would have forecasted in 1963. Fast export growth, it should be emphasised, need not be accompanied by laissez-faire policies, nor indeed by the elimination of all protection. Brazilian and Colombian export achievements have been registered while substantial (excessive for many sectors) protection was maintained, and with the public sector actively intervening in the export drive. Such "Japanese approach" toward export promotion seems to have been followed by some Asian super-exporters, e.g., South Korea and Taiwan, countries which have maintained non-trivial import restrictions and rigorous exchange controls, while relying on subsidised credit, public enterprises and managed exchange rates as parts of their policy package. These experiences suggest that in a dynamic context the best index of trade openness for industrialising countries may not be relative levels of effective rates of protection and subsidisation as between import substitution and exports, but actual export growth rates, particularly those for non-traditional exports. Imports, after all, are the tangible fruits of the gains from trade, and if exports grow at a high and sustained fashion, imports will follow suit sooner or later.

Export promotion does not, as is often portrayed, inevitably lead to greater dependence on "the capitalist-imperialist center." This can be seen in Table 4 which shows the geographical destination of increases in merchandise exports for several Latin American countries between the averages for 1970-71 and 1978-79. The degree of diversification and the relatively modest share going to the United States, the traditionally hegemonic power of the region, are remarkable. It is noteworthy that the country whose exports grew least, Peru, shows the greatest concentration

on two markets. Compare also Peruvian and Uruguayan trade with Other Western Hemisphere countries in Table 4; note that the former was a rhetorical champion of Latin American integration during the 1970s. Adding the figures for oil exporting countries (which include Venezuela) plus Other Western Hemisphere countries yields the highest numbers for Argentina, Chile and Uruguay, three countries that by the late 1970s were hardly champions of third world solidarity.

Behind the aggregate figures there is further evidence that the realities of a multipolar trading world seem to have been missed by the metaphysical categories of some "delinkers", whose writings would not prepare their readers to expect massive trade between an Argentina ruled by conservative military and the U.S.S.R., nor significant Brazilian exports of weapons to the Middle East, nor active commercial links between post-1973 Chile and China.

The traditional primary products/manufactures dichotomy can also be misleading. Both economically and politically, in the world of 1981 exporters of wheat, soybeans and corn look better than exporters of steel and petrochemicals. As an example contrast the economic benefits and international autonomy the latter industries have brought Argentina, with those generated from Argentine sales of corn, sorghum and beef to the Soviets.

There is considerable evidence for the post-war years showing that in the medium- and the long-term faster export growth has been associated with faster growth in Gross Domestic Product, even leaving aside from the latter the value added by the export sector.<sup>15/</sup> Faster growth also appears to have been associated with larger expansions of employment opportunities in modern sectors. Beyond that the claims for export-led

TABLE 4

Geographical Destination of Increases in Merchandise Exports  
Between 1970-71 and 1978-79  
 (Percentage of total increase)

	<u>Argentina</u>	<u>Brazil</u>	<u>Chile</u>	<u>Colombia</u>	<u>Peru</u>	<u>Uruguay</u>
United States	7	20	12	30	43	17
Japan	6	6	9	4	15	2
European Economic Community	31	29	28	30	6	28
Oil exporting countries	5	7	5	13	2	2
Other Western Hemisphere Countries	22	14	29	5	14	42
USSR, Eastern Europe and China	12	7	3	3	7	3
Other countries	17	17	13	15	13	6
 <u>Memo:</u> Average annual percentage growth rate of exports, at current dollar prices	 19	 22	 14	 22	 12	 16

Sources: International Monetary Fund, Direction of Trade  
Yearbook. Washington D.C., several issues. "Oil exporting countries"  
 includes Venezuela. "Other Western Hemisphere" covers basically  
 Latin America and the Caribbean, excluding Canada and Venezuela

growth achieved in Latin America become weaker. The effects on income distribution are complex but of unclear direction and strength, partly because the variety of non-traditional exports cannot be simply labelled "labor-intensive" nor "land-intensive".

Neither the effect of trade openings on political change, nor the effect of political regimes on trade policies are unambiguous. Since the mid-1960s, regimes moving in the direction of export promotion, albeit at different speeds and using different instruments, have included the Frei administration and Pinochet government in Chile, several constitutional Colombian governments, the second Belaunde administration in Peru, and the Cuban government led by Fidel Castro. Other countries have witnessed a steady concern for a healthy export sector, including Barbados, Costa Rica, Ecuador, Mexico, Paraguay, Trinidad-Tobago, and Venezuela. Ecuador and Venezuela have mixed oil exports with democratic politics, with Venezuela since 1958 having an admirable record of constitutional government. Some might argue that oil makes Venezuela a special case, but they should then explain why Saudi Arabia has not surpassed Sweden in social democracy and constitutional liberty.

The open economies of Central America, while maintaining prosperous export sectors, experimented with moderate collective protection during the 1960s; in most countries the domestic beneficiaries of that common market appear to have been privileged social groups not too different from those benefitting from exports. Direct foreign investors, as elsewhere in Latin America, also benefitted from such "infant industry" protection: a combination of partial closing in trade and opening toward direct foreign investment seems both economically and politically



dangerous, particularly for small economies, as foreign investment can magnify the distortive effects of excessive protection, while creating powerful vested interests for the maintenance of trade restrictions. Caribbean open economies flirted with the Central American approach during the 1970s, but on the whole have maintained great concern for dynamic exports of goods and services. In spite of adverse economic shocks and difficult social circumstances during the 1970s many of these island economies have maintained fairly open political regimes; examples include Barbados, the Dominican Republic and Jamaica.

Openings toward international financial flows have been more dramatic than those toward trade. Since the late 1960s a number of Latin American countries have borrowed extensively from private international banks; these flows have surpassed those for direct foreign investment and concessional finance. This vast topic can be discussed in great detail,<sup>16/</sup> but here only a few features will be highlighted, again pointing to the non-uniqueness of the openings-politics link. The list of borrowing countries includes Cuba, Chile, post-revolutionary Nicaragua, and Guatemala. The management and instrumentation of borrowings have been highly diverse. For example, Brazil and Colombia have maintained exchange controls and have closely supervised regulated external borrowing. On the other hand, Argentina during 1978-81 moved close to a laissez-faire attitude toward connections between domestic and international financial markets. Controls over the direct presence of international banks in domestic economies have also varied. A look elsewhere confirms this heterogeneous picture: major borrowers also include Hungary and Poland, South Korea, and the Philippines.

The incentives and opportunities available in international

financial markets interacting with domestic financial and exchange rate policies naturally affect domestic economic actors in different ways, and political implications may follow from changed international circumstances. It can be argued, for example, that the liquidity of the Eurocurrency market during the 1970s allowed many Latin American public enterprises a degree of initiative and autonomy not available previously. That market also strengthened the potential bargaining power of governments in negotiating with Trans-National Enterprises as well as with the International Monetary Fund, the World Bank and countries dispensing either concessional finance or selling weapons. Financial pressures by the Carter administration against the Chilean government in an effort to gain human rights concessions were dulled by the Chilean ability to borrow in the Eurocurrency market, an expedient also used by the Cuban government during the 1970s. Of course, borrowing gives flexibility today but if the funds are not managed wisely, or if one is just unlucky in the commodity lottery, it will decrease flexibility tomorrow, as both Peru and Poland found out.

Some types of 1970s openings toward capital flows have yielded new experiences and dilemmas. The great mobility of financial flows has raised the possibility that openings to capital may conflict with sustained trade openings. Consider the bizarre Argentine experience of 1978-81 where massive borrowing sustained an appreciation of the real exchange rate which clashed with export promotion efforts. That Argentine experience shows that, at least for some years, one can wreck both the import-competing and the export sectors with the gainers from such policies including some bankers and a few other groups. Chilean and Uruguayan exporting efforts appear threatened by similar considerations.

Direct foreign investment has shown itself shier than financial capital in accepting the lure of more open doors. Regulations on TNEs have been relaxed in many Latin American countries, although the picture remains quite heterogeneous in this field also. Post-1973 Chile has been the clearest example of a drastic opening toward direct foreign investment. In spite of almost pathetic invitations from Chilean authorities, and in spite of the rhetoric of some business publications praising investment climates created by authoritarian regimes, the inflows of TNE investments into post-1973 Chile have been modest, and not obviously higher than those going into other economically comparable Latin American countries having stiffer regulations on direct foreign investment. It is one thing to lend other people's money and another to commit one's equity, when the stability of the rules of the game in the host country may depend on one person's caprice or heartbeat.

## 5. CONCLUSIONS AND DOUBTS

Even a hasty review of Latin American economic history provides damaging counterexamples against simple generalisations about the openness-politics link, whether of the optimistic, classical economists' variety, or of the more recent delinkers' species. The degree of openness of an economy and its political system may be regarded as just two endogenous variables in a socioeconomic general equilibrium system; partial correlations between those two variables in isolation are unlikely to yield robust or meaningful results. In an interesting pioneering study John F.O. Bilson has attempted to econometrically explain the degree of civil liberties in 55 developed and developing countries as a function of several economic variables, including

openness to international trade, measured as the ratio of exports to Gross National Product. Population, per capita income, share of wages in aggregate income and other variables are included. The coefficient for openness indicates a positive link with civil liberties, but it is not statistically significant. The only economic indicator found to be a significant predictor of differences in the extent of civil liberties was the level of per capita income.<sup>17/</sup> These econometric results are compatible with our historical review for Latin America.

The non-uniqueness and looseness of the openness-politics link is confirmed by other regions and other times. Within the group of socialist countries, Albania, 1960s China, Pol Pot's Kampuchea, and Romania on the whole minimized and scorned outside links. Cuba, Hungary, Poland, and Yugoslavia have maintained extensive international commerce with anyone willing to trade with them. At first sight such a contrast within the socialist camp gives some (modest) support to the hypothesis of classical economists.

Over the last 60 years the Mediterranean world, always of interest to Latin America, has witnessed authoritarian regimes which sometimes favored delinking (Mussolini during the 1930s and Franco during the 1940s and 1950s), while at other times followed orthodox outward-oriented trade policies (Mussolini during the 1920s, Franco during the 1960s, and the Greek colonels during the late 1960s and early 1970s).

As in the Mediterranean world, authoritarianism in Latin America has much to do with the Armed Forces. The nature and laws of motion of the collection of men in uniform are the darkest black boxes in Latin American social science, but one may conclude that the attitude of the Armed Forces toward economic openness has been neither

unambiguous nor steady. The case of the Peruvian Armed Forces is particularly interesting: led by General Odeia, they favored across-the-board openness in trade and investment but under General Velasco Alvarado they increased import barriers and neglected non-traditional exports, while trying to maintain traditional exports under state direction. Regarding capital flows the Velasco Alvarado administration borrowed substantially abroad but increased controls over direct foreign investment. The heterogeneity of economic views within the Argentine and Brazilian Armed Forces is well known (and arguments about economic policies between various factions have more alarming side effects than those between Samir Amin and Arnold Habegger). Armed Forces, at least in South America, are unlikely to be great enthusiasts of free trade in goods and services, will be skeptical about direct foreign investment and financial flows, and will certainly be hostile to free migration with neighbouring countries. Argentine and Brazilian generals in charge of public enterprises are unlikely to permit tariff reductions increasing foreign competition to "their" firms.

Other points noted in this essay may be worth stressing. It does appear possible to argue that the role of the foreign sector in Latin American development has been exaggerated and indeed mythologised. Of course policies towards international trade and capital play an important role in terms of efficiency and growth, and are more important the smaller a country is. Interaction with the rest of the world offers some potential gains; that is why most clever politicians firmly in control will try to take advantage of them. Those interactions will cause problems and set constraints, so clever politicians, uniformed or not, will keep an eye on those links and will select those with the highest

benefit-cost ratios, at least to themselves. But even in a small country the foreign sector will influence only indirectly many key developmental variables, such as productivity in non-export agriculture, willingness to save and decisions to invest in human capital. Income distribution and political participation will be more influenced by these and other domestic variables than by whether effective rates of protection are 10 or 150 percent.

The need for care in the definition of economic openness is another important point emerging from this essay, even if no definitive formula has emerged. (Others will have to dwell on definitions of authoritarianism and liberty.) The literature is full of judgmental labels, such as "outward-oriented" and "inward-oriented" economies. The matter is not an easy one, even if one focuses just on international trade in goods and services. The problem lies in separating the effect on observed trade of policy measures from those generated by the natural endowment, population and per capita income of a country. Examining the balance between policy incentives for exporting versus import substitution is one approach, but it should be noted that such a balance may exist both at zero (or negative) incentives for both, or at high levels of incentives for both. Other policy variables which could be mentioned only briefly in this essay, such as the exchange rate and credit, are of critical importance in determining the size of the sector producing internationally traded goods and services. Clearly trade may occur under a variety of institutional arrangements: Chile, Hungary, Japan, South Korea, and Yugoslavia may be said to be economies fairly opened to trade, yet their policy instruments are

far from identical. The nature of those instruments and institutions are important for determining the effect of openness to trade on other domestic variables, whether economic or political. Openness was once closely linked with policies of laissez faire, laissez passer, but such an association is no longer valid.

The workings of an economy, whether open or closed, imposes constraints on what political actors do. Is the open economy more of a "delicate watch" than a closed economy? The point is debatable. Insofar as certain types of openness increase the international mobility of some economic actors, such as financial capital and skilled labour, it augments their bargaining power vis-a-vis the less mobile factors (those whose wealth is tied up in land and unskilled labour with nowhere to go). Yet openness may also increase the flexibility of a political leader bent on neglecting one productive sector to benefit others; if you can import grains, you can neglect food production as long as you have something to export in exchange or somebody lends you money. However, on balance, it seems plausible that specialisation tends to increase vulnerability, and that the lower the international mobility of an economic agent, the greater its vulnerability will be. Trade unions of unskilled workers in activities producing exportable goods, whether in Sweden, Japan or Colombia, will have limits set on their wage aspirations by international conditions, yet their real incomes and welfare may be higher than under a closed economy perhaps giving them job security but neither gains from trade nor greater personal liberty. Note also that any economy, whether open or closed, aiming at high rates of capital formation or defense expenditures, will have to limit consumption and real wages. Closedness did not generate

much growth in real wages in the Soviet Union of the 1930s nor the Spain of the 1940s, while South Korean real wages appear to have risen faster than those of Burma during the last twenty years.

Examples of trade-offs between gains from trade and security are easily multiplied: oil importers prefer to trade with suppliers who cannot always guarantee deliveries to being self-sufficient in energy when only charcoal is available at home. Additional constraints imposed by openness can also be illustrated by international financial flows: clearly a country borrowing today commits itself to earn or save enough foreign exchange tomorrow to service the debt. This commonsensical reality may lead a country to conclude, like Polonius, that it is best to "neither lender nor borrower be," but other nations with attractive investment projects will think otherwise.

Openness will set limits particularly on political actors seeking drastic and rapid transformations in their societies. Freedom to migrate presents obvious headaches; capital mobility may or may not work in their favour; trade in goods and services provides dangerous conduits to the enemy during revolutionary times. Revolutionaries, whether fascists, religious fundamentalists or leftists, will usually favor sharp degrees of delinking to establish their power and achieve a radical transformation in the economy and the polity. Once firmly in control, openings may follow.

The untangling of the economic and political consequences of a certain degree of openness maintained over many years from the effects of a transition toward (or away) from that degree of openness is one of the most difficult questions raised by this essay. Recorded Latin American economic history may be viewed as the result of long term



forces disturbed by frequent external shocks and often erratic changes in domestic policies; allocating observed events to each of these causes is not a simple task. As noted in the review of what mainstream economics does and does not say regarding openness, there is a notorious lack of integration between the pure theory of international trade, which addresses long-run questions using the method of comparative statics (or comparative dynamics), and the theory of Balance-of-Payments adjustment mechanisms, which addresses short-run macro-economic questions, sharing with modern macroeconomics a good deal of controversy and confusion. The study of Latin American openings and closings requires that attention be paid both to short- and long-run considerations, and seldom will both bring unambiguous gains or losses.

In an important paper John Sheahan has argued that at the start of the 1960s economic distortions of all sorts had accumulated to such a point in many Latin American countries that repression appeared to be, falsely but understandably, the necessary condition of economic policy.<sup>18/</sup> The poor economic performance generated by the distortions, including those in the area of foreign trade, undermined support for open governments; those governments, Sheahan argues, which gave great emphasis to efficiency criteria were placed by the distorted structure of the economy in automatic alliance with the wealthy minority against organised urban labour.

Sheahan's article emphasises how transition problems may create a demand for authoritarian regimes; his article also covers broader economic policies, going beyond those related to the external sector, underlining the complexity of the transition process. Nevertheless, my conjecture is that the demand for authoritarian regimes in the

Southern Cone of Latin America mainly came not from poor long-run economic performance, but more immediately from unhinged macro-economic conditions, including three-digit inflation and unsustainable balance-of-payments deficits. The chaotic climate created by those short-term circumstances opened the way for the men in uniform.

Did the poor long-term economic performance induced by sluggish exports lead to short-term macroeconomic disorder in the Southern Cone? Perhaps. Mediocre growth, under the 1960s political circumstances of Latin America (including the then-shining example of the Cuban Revolution) increased the appeal of clashing authoritarian formulas, first from the left and then from the right, promising to break out of perceived economic and social miasmas, at the expense of previous democratic achievements. Populist regimes first rode the crest of demands for reform, but lost control of macroeconomic conditions unleashing hyperinflations and balance-of-payments crises.

But poor long-term performance need not have led inevitably to chaotic populism nor to murderous authoritarianism. Consider a mental experiment: suppose a country had very stiff import restrictions, sluggish export growth and tight controls over capital flows, but inflation remained in single digits, the balance-of-payments was problematical but under control, and there was low but reasonably steady growth. Under these circumstances it is difficult to imagine an abrupt authoritarian offensive to eliminate market distortions. And if it came about, the recessions, unemployment and real wage cuts associated with Southern Cone stabilisation plans would be much less likely to happen. The mental experiment has a fairly close real-world

counterpart: to the exasperation of nearly all types of economists, for more than thirty years India has combined a mediocre economic performance with reasonably democratic political institutions.

Why Southern Cone authoritarian regimes chose certain economic policies, and why peculiar alliances were forged between rational economic technocrats and leading generals is a fascinating topic (not unlike the Speer-Hitler connection), but one from which few generalisations may be drawn, at least for the openness-authoritarianism link. The need to check hyperinflation and quickly correct balance-of-payments deficits is one which naturally brings together those used to discipline, command, and punish with those emphasising order and soundness in budgetary and monetary policies, at least regarding civilian expenditures and credit. Anti-inflationary measures do require a degree of persistence that make authoritarian politics appealing to some economists (and businessmen). The need to check hyperinflation may then provide a convenient cover to liquidate trade unions and political enemies. But note that even within the Southern Cone the degree to which authoritarian regimes have moved toward free trade and free capital movements is far from uniform. As during the 1950s, some observers tend to generalize from the Chilean case to all of Latin America. Chilean tariff books in 1981 paradoxically looked more like those of Switzerland than those of Argentina, Brazil or Uruguay.

It is time to close this essay by looking at the future. What was done in the Southern Cone during the 1970s was badly and brutally done. But it does not follow that those who will come after the authoritarians should undo everything which was done. The advantages of dynamic export growth was a lesson learned before Mr. Pinochet

became notorious, and should survive him. It would be foolish to rule out the use of exchange controls because they were used by Hitler; it would be silly to oppose lower tariffs because Pinochet liked them.

But what if the 1980s turn out to be more like the 1930s than like the 1960s as far as external demand for exports? That possibility, although unlikely, cannot be ruled out. Private entrepreneurs deciding whether to produce for the foreign or the domestic markets are aware of these uncertainties, and it is debatable whether public policy should push them very far one way or another. The public sector in most countries still faces many spending and investment decisions for which expectations regarding the buoyancy and openness of external markets are important. It would be premature to adopt an expectation of external catastrophe in these decisions. While selling abroad during the 1980s may not be as easy as implied by the comfortable small country assumption, the likely effort appears to be worth a try in many activities. A country like Japan plans its exports come what may; circumstances may force changes in products and markets, but the decision to maintain a brisk export expansion is unquestioned. Whether because the need for irreplaceable imports, such as oil, or because of commitments to service their debt (so long as there are no major changes in the working of international capital markets), or because of plausible opportunity cost calculations, Latin American countries may be wise to follow the Japanese example. If such an openness strategy is followed for trade, a more active participation in international rules would be desirable. But that is another matter.<sup>19/</sup>

Similar considerations apply to interactions with international capital markets.

The favourable conditions which existed for some borrowers during the 1970s, such as plentiful credit at negative real interest rates, are unlikely to exist in the 1980s. Just as Brazil exhausted opportunities for easy import substitution in the 1930s and 1940s, it exhausted its easy borrowing phase in the 1970s. Yet the option to borrow abroad, for Brazil and the rest of Latin America, is likely to remain during the 1980s a profitable one for the careful investor and a dangerous one for the spendthrift.

One may note that Southern delinkers have become "objective allies" of Northern protectionists who cloud the LDC outlook for the 1980s. Many a Northern observer expresses concern about Southern despotism only after his or her profits or wages have been harmed by Brazilian or South Korean exports (if the exports were Indian, old concerns about the morality of neutralism may be voiced instead). The old "pauper labour" argument for protection has become the "repressed labour" argument for higher tariffs. The development strategies of Albania, Burma, and Kampuchea have a powerful appeal to Northern capitalists and workers battling competition from Colombia and Taiwan. It is not so surprising then, that Business Week should refer to Samir Amin as one of the Third World's best economists and expound his views.<sup>20/</sup> South-South trade and a basic-needs development strategy are also viewed with favor by many Northern protectionists. One cannot easily reconcile criticisms of Northern protectionism as unfair to the LDCs with proposals for Southern delinking. Some Northern academics, especially in Europe, who regard themselves as progressives and friends of the LDCs appear to take the paternalistic view that if LDCs do not delink on their own, Northern progressives (those academics and their trade union allies) will do it for

them, by erecting import controls.

In spite of the troubled and uncertain outlook, the 1980s could witness Latin American economies which are open to trade and finance, in a selective fashion not unlike that of smaller European countries (such as Denmark, Finland or Hungary), while Latin American polities either emerge from the nightmares of the 1970s or deepen their earlier democratic achievements. Surely the message of this essay is that there is nothing unscientific in such a vision.

Footnotes

\*The title of this paper was snatched from Ronald Findlay, to whom I am also grateful for stimulating discussions. Gabriel Palma, Diana Tussie and other participants at the Millenium conference of the London School of Economics in April-May 1981 were also generous with comments and advice. An earlier draft benefitted from criticisms from Marcelo Cavarozzi, Jonathan Eaton, Albert Fishlow, Albert Hirschman, Louka Katseli, and John Sheahan. The usual caveats apply.

1/ This distinction was presented in Edmar Bacha and Carlos F. Diaz-Alejandro, "Financial markets: A view from the semi-periphery", a paper part of a project on External Financial Relations and their Impact on the Latinamerican Economies, carried on under the coordination of CIEPLAN and the support of the Ford Foundation.

2/ Gottfried Haberler, "Postscript", in R.C. Amacher, G. Haberler, and T.D. Willett (eds.), Challenges To a Liberal International Economic Order (Washington, D.C. : American Enterprise Institute for Public Policy Research, 1979) p.87. The remarks by Ronald Findlay are in this volume, pp. 73-80.

3/ See Paul R. Krugman, "A model of innovation, technology transfer and the world distribution of income" Journal of Political Economy (Volume 87, Number 2, April 1979) pp. 253-266. See also "U.S. Blunts Japan's Technology Quest" in The Wall Street Journal, September 8, 1981, p.39 reporting that there is widespread fear among U.S. manufacturers that selling technology to the Japanese will boomerang.

4/ I am drawing here on my "Delinking North and South: Unshackled or Unhinged?", in Albert Fishlow, et al, Rich and Poor Nations in the World Economy (New York: McGraw Hill Book Company, 1978) pp. 87-162, and on the works cited there, especially that of W.N. Corden. For a review of the post-war literature the interested reader may consult my "Trade policies and economic development", in Peter B. Kenen (ed.), International Trade and Finance (Cambridge: Cambridge University Press, 1975) pp. 93-150.

5/ See Avinash Dixit, "The export of capital theory", Journal of International Economics (Volume 11, No.2, May 1981) pp. 279-294.

"The general result on gains from trade shows that, given the necessary redistributive tools, an autarkic economy should move to free trade, and a free-trading economy should not move to autarky. This is so irrespective of the comparison of the two steady-state consumption levels. Economies in the real world are clearly constrained by their historically determined initial conditions. The kind of ahistoric comparison made in the Golden Rule result, or the result of Steedman et al, is clearly of no practical relevance for accumulation or trade policy" p.288.

6/ See Carlos F. Diaz-Alejandro, "The Less-Developed Countries and Transnational Enterprises", in Sven Grassman and Erik Lundberg, The World Economic Order: Past and Prospects (London: The Macmillan Press, Ltd., 1981) pp. 233-256. For a discussion regarding corporations and democratic theory see Charles E. Lindblom, Politics and Markets: The World's Political-Economic Systems (New York: Basic Books, 1977) pp.5 and 356.

7/ For more discussion on the modest question: Why not seek world efficiency via labour movements instead of capital movements?, see my "North-South relations: the economic component", International Organization (Volume 29, Number 1, Winter 1975) pp. 218-221.



8/ Gottfried Haberler, "Postscript", op cit, p.86. Professor Haberler has been consistent on this point. In 1943 he argued:

"In fact, the obstacles to free or freer migration are so formidable, so much greater than those to free or freer trade, that it may well be argued that the question should be dropped altogether or at least not linked with the question of freeing the movement of goods in order not to jeopardise the chances of achieving something in the trade field"

In a footnote to this sentence he added:

"Just think of the chances of persuading the people of the United States, Australia, or any other country with a high standard of living to permit the free immigration of Chinese (not to speak of Japanese) labour after the war! Also, from a selfish point of view of the country or of large groups (e.g., labour) in the country into which immigration is to take place, much more serious objections can be raised against free immigration than against the free importation of goods".

See Gottfried Haberler, "The Political Economy of Regional or Continental Blocs", in Seymour E. Harris (ed), Postwar Economic Problems (New York: McGraw-Hill Book Company, Inc. 1943). pp.326-327.

9/ This observation is based on the reactions of students to a course taught jointly by Hugh Patrick and myself at Yale University on the Economic History of Follower Countries. The students have often remarked on the manner in which the Latin American section of the course spends much more time dealing with the external sector than does the Japanese half of the course; though, of course, this may be due to the idiosyncracies of the teachers involved.

10/ For an overview of Samir Amin's and other similar arguments extolling the virtues of withdrawal or "delinking" from the international economy, see Carlos F. Diaz-Alejandro, "Delinking North and South: Unshackled or Unhinged?" op cit.

11/ W. Arthur Lewis, The Evolution of the International Economic Order (Princeton: Princeton University Press, 1978) pp. 5-6.

12/ For my interpretation of these events see "Latin America in Depression, 1929-1939", and "Stories of the 1930s for the 1980s", Yale Economic Growth Center Discussion Papers No. 344 and 376, March 1980 and April 1981, respectively.

13/ See his brilliant "The turn to authoritarianism in Latin America and the search for its economic determinants", in David Collier (ed.), The New Authoritarianism in Latin America (Princeton: Princeton University Press, 1979) pp. 61-98. The letter from Peron to Ibanez appears in p.65.

14/ See United Nations Economic Commission for Latin America, Economic Survey of Latin America 1951-1952 (United Nations document E/CN.12/291/Rev.1, 28 March 1953) p.xxii.

15/ See Michael Michaely, "Exports and growth: An empirical investigation", Journal of Development Economics (Volume 4, No. 1, March 1977) pp. 49-54; and Michael Michaely, "Export and growth: A reply", Journal of Development Economics (Volume 6, No.1, March 1979) pp.141-143.

16/ See the essay by S. Griffith-Jones in this volume, and also E. Bacha and C.F. Diaz-Alejandro, op cit, for a more detailed discussion of the interactions of Latin American countries with international capital markets.

17/ See John F.O. Bilson, "Civil Liberty—An Econometric Investigation", Kyklos (forthcoming, January 1982). Bilson also concludes:

"...there is no clear evidence that a gradual move towards greater government intervention in a democratic state will be associated with a decline in civil liberty. There is, however, a clear and predictable correlation between the concentration in the political system and the extent of personal freedom. In other words, if an individual is told that a country is capitalist this information is not very informative with regard to the extent of civil liberty in that country. On the other hand, if the individual is told that the country has a multi-party political system, this information is valuable".

18/ See John Sheahan, "Market-oriented Economic Policies and Political Repression in Latin America", Economic Development and Cultural Change (Volume 28, No. 2, January 1980) pp. 267-291.

19/ That matter is discussed in my "Latin America and the World Economy in the 1980s", Economic Forum, Vol.XI, No. 2, Winter 1980-81, pp.38-53. For interesting proposals for reforming major international organisations see Miriam Camps and Catherine Gwin, Collective Management; The Reform of Global Economic Organisations (New York: McGraw-Hill Book Company, 1981). Hungary and Poland applied during 1981 for admission to the International Monetary Fund and the World Bank; China joined those organisations earlier. It remains to be seen whether a similar trend toward globalisation will also occur in GATT.

20/ See Business Week, November 9, 1981, p.29. Not all Northern capitalists, of course, will fear Southern export expansion. In terms of international trade models, attitudes will depend on the degree of mobility, domestic and international, of the different factors of production.