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## Samuelson on populist democracy, fascist capitalism, and the vicissitudes of South American economic development (1948-1997)

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SAMUELSON ON POPULIST DEMOCRACY, FASCIST  
CAPITALISM, AND THE VICISSITUDES OF SOUTH AMERICAN  
ECONOMIC DEVELOPMENT (1948-1997)

BY MAURO BOIANOVSKY

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# ***Samuelson on populist democracy, fascist capitalism and the vicissitudes of South American economic development (1948-1997)***

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**Abstract.** Paul Samuelson was attracted to the economic dynamics of South American countries because of the links between economic performance and political factors. He discussed the influence of “populist democracy” on Argentina’s relative stagnation, which, he argued in the 1970s and early 1980s, served as a dangerous paradigm for the American economy under stagflation. Moreover, he applied his concept of “capitalist fascism” to deal with military dictatorships in Brazil and (especially) in Chile. The Brazilian translation of his *Economics* in 1973 brought about a correspondence with Brazilian economists about the “fascist” features of the regime. The main variable behind the South American economic and political processes discussed by Samuelson was inequality, which became also a feature of the American economy since the adoption of market-based policies in the 1980s and after.

**JEL classification.** B22, O11

**Key words.** Samuelson, populism, capitalist fascism, South America, economic development, inequality

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If we broaden our definition of failure to go beyond the behaviour of broad real aggregates of output and income, if we include failure of a market system to provide what electors deem a fair and equitable *degree of equality* of income and opportunity – if we do this, we can assert with propriety and confidence that *often failure of capitalism is what can be expected to result in its demise*. (Samuelson 1981a; italics in the original)

## 1. Stagflation and the end of the neoclassical synthesis

Since Adam Smith's *Wealth of Nations*, economists and social scientists have discussed Latin America from the perspective of what *distinguishes* it from Europe or the United States. This applies to Alexander von Humboldt's celebrated reports of his travels to the vice-kingdom of New Spain, which made available in early 19<sup>th</sup> century, for the first time, a description of the socio-economic structure of a Latin American region (Mexico). French economist Jean-Gustave Courcelle-Seneuil, often regarded as the first "money doctor", was instrumental in the establishment of free banking in Chile (instead of France) while living in that country between 1853 and 1863. Monetary conditions in South America drew the attention of Knut Wicksell, who in the early 20<sup>th</sup> century discussed the hyperinflation that took place during the Colombian Civil War in 1899-1902. By mid 20<sup>th</sup> century, with the emergence of development economics as a new field, Albert Hirschman, Hans Singer, Theodore Schultz, Dudley Seers and many other foreign economists investigated Latin American underdevelopment. After the 1960s, foreign experts in Latin American economy, history and society became conspicuous, including the so-called "Brazilianists" (e.g. Albert Fishlow, Werner Baer, Leslie Bethell, Roger Bastide, Warren Dean, Thomas Skidmore, Stanley Stein and Joseph Love).

By the late 1960s and early 1970s, Paul Samuelson and Milton Friedman, two prominent American economists who were not experts in South American economies, became interested in their economic and political features. They foresaw that chronic and accelerating inflation, as well as fragile economic growth, which beset a number of South American countries, would affect the U.S. economy as well. Hence, they

both became (for a time) interested in the economy of South American countries because they thought it could shed some light on future economic performance of their own country – it was not so much the distinctiveness as the prospective *similarity* between South American and United States’ macroeconomic problems that attracted their attention. Accelerating inflation episodes in Brazil, Argentina and Chile played a significant role in the formulation of Friedman’s (1968, 1977) concept of a long-run vertical Phillips curve and of mechanisms to cope with chronic and volatile inflation (see Boianovsky 2020).<sup>1</sup> Whereas Samuelson never set foot in any of those three countries, Friedman paid visits to Brazil in 1973 (Boianovsky 2020) and, famously, to Chile in 1975 and 1981 (Edwards and Montes 2020).

Samuelson’s main piece on South America as a “paradigm” for the United States and other industrialized economies was his 1980 plenary address to the International Economic Association (IEA) conference held in Mexico City, published in two versions with the same title (Samuelson 1983a; 1981b). Samuelson’s concern was that the 1970s stagflation of the American economy could be a sign that the United States was about to follow the same perverse path that had prevented Argentina from fulfilling its growth potential. Samuelson ascribed Argentina’s (as well as Chile’s and Uruguay’s) post-war growth failure not to purely economic causes but – reflecting his reading of Joseph Schumpeter’s *Capitalism, Socialism and Democracy* – to “political sickness” caused by the working out of “populist democracy” as individuals formed coalitions to use the state to change income distribution in non-optimal ways. That was also the main factor behind stagflation in industrialized economies, interpreted as the downside of the welfare state. Samuelson asked:

Oslo, Washington and New Delhi are a long way from Buenos Aires and Santiago. But is it far-fetched, as we try to peer into the decades just ahead and do so against the backdrop of the 1970’s era of worldwide stagflation, to fear that many of our mixed economies will begin to suffer from their own version of the Argentinian sickness? (Samuelson 1983a: 70)

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<sup>1</sup> Another illustration of the influence of Latin American economic events is provided by the development of the monetary approach to the balance of payments by Jacques Polak upon heading a mission of the International Monetary Fund to Mexico in 1955 (Boianovsky and Solís 2014).

Samuelson saw Chile's dictatorship after the 1973 *coup d'état* as an authoritarian "solution" to the problems posed by populist democracy. The Chilean regime imposed a political order that enabled the "free" working of the market, labeled "capitalist fascism" by Samuelson (1980a, 1981b, 1983a) under Vilfredo Pareto's influence. He claimed that monetarist policies implemented in Chile by the so-called "Chicago Boys" were made possible by prevailing political repression. Moreover, he believed that the same conditions were necessary for monetarism to succeed in fighting stagflation in the U.S. and in the U.K. (Samuelson [1980d] 1986). Brazilian high rates of economic growth between the late 1960s and mid 1970s, when a military regime ruled the country, were accompanied by noteworthy increase in income inequality, as Samuelson (1980a) observed. His description of the Brazilian regime as "fascist" in the 1973 edition of *Economics* raised critical reactions from the local publisher, backed by some influential Brazilian pro-government economists, which led to withholding the whole passage from the 1975 Brazilian edition.

Samuelson's 1980 Mexico lecture was the culmination of a couple of papers and of some passages in his hugely successful textbook. *Economics* went through 19 editions between 1948 and 2010; it was co-authored with William Nordhaus since the 12<sup>th</sup> (1985) edition. No other economics book went through so many editions for such a long time span, bearing witness to changes in economic ideas and to economic events through history. Unlike his analytically and mathematically framed 1947 *Foundations*, Samuelson's textbook paid attention to institutions and their role in shaping economic reality (Backhouse 2017: 593), although it did not shy away from (basic) economic modeling.

The first edition of *Economics*, written shortly after World War II, discussed fascism (together with socialism and communism) as an alternative system to "democratic capitalism". It mentioned the occurrence of "dictatorships" in "numerous countries of Latin America" and referred to "Perón's Argentina" as a fascist regime grouped together with contemporary Salazar's Portugal, Franco's Spain and previous Mussolini's Italy and Hitler's Germany (Samuelson 1948: 584, 586).<sup>2</sup> The section on fascism was kept, with revisions, until the 1980 edition. Samuelson ([1971] 1983; [1972] 1983) would discuss Argentina's disappointing economic performance as part of articles about the future of private corporations and of the welfare state. Years after

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<sup>2</sup> See Oren (2000: 152) on Samuelson's (1948) classification of Perón's administration as of the same kind as old and current European fascist regimes.

his 1980 Mexico address, Samuelson (1997a) still used Argentina as a case study of “Why economies grow and why they decay”.

The eighth (1970) edition of *Economics* included two changes indirectly related to Samuelson’s concern over South American instability. He removed from the book references to the “neoclassical synthesis” between Keynesian macroeconomic management and (neo)classical microeconomics, a concept he had famously introduced in the 3rd edition.<sup>3</sup> The main reason why he dropped the neoclassical synthesis from 1970 on, as he later recalled (Samuelson 1997b: 155-56), was the onset of stagflation phenomena, which “lowered the self-esteem of the Keynesian and macroeconomists generally.” The observed incompatibility of full employment with price stability challenged the neoclassical synthesis and called for new tools of “description, understanding, and prediction” (Samuelson 1970: 808). Moreover, he added a new chapter on “Economic inequality” dealing with a related aspect of the working of the welfare state in mixed economies. It featured discussions of “equity versus efficiency” and of deadweight burdens of income redistribution so that “redistributing social pie may reduce its total” (Samuelson 1970: chapter 39: 766-68).

By 1973 Samuelson introduced into American economics the term “stagflation”, defined as “stagnation of growth and employment at the same time that prices are rising!” (Samuelson 1973a: 827). The expression had been originally used in British policy debates in the mid 1960s (Nelson and Nikolov 2004), but it only gained currency in the U.S. after Samuelson deployed it in 1973, in his textbook and in articles in *Newsweek* (Nelson 2019: 76-77). Around that time, Gunnar Myrdal (1973) introduced the term and concept to the European audience. The matter should be seen against the background of Friedman’s (1968) influential critique of the Phillips curve trade-off – a concept often ascribed to Samuelson and Solow (1960) – as workers adjust their inflation expectations. The braking down of estimated short-run Phillips curves as inflation accelerated in the United States in the early 1970s confirmed Friedman’s predictions of stagflation. Samuelson (1973a: 833) agreed: “As people fear and expect price inflation they shift upward their effective Phillips curves and bring on stagflation – unemployment and inflation.” He remained, however,

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<sup>3</sup> See Samuelson (1955: vi). Samuelson (1970: 309) still referred to the “so-called ‘post-Keynesian neoclassical synthesis’”, in the restricted sense of the IS-LM model as opposed to Friedman’s monetarism.

skeptical of a vertical long-run Phillips curve at the natural rate of unemployment (ibid, 835, n. 7).

The long-time rivalry between Samuelson and Friedman provides part of the background for the former's incursions into aspects of the economic development of South American countries. They both arrived at the University of Chicago in 1932, as freshman and graduate student, respectively (Warsh 2015). One of the issues they disagreed upon was the connection between market and personal freedoms. As Samuelson recalled,

I was taught at the University of Chicago that business freedoms and personal freedoms have to be strongly linked, both as a matter of brute empirical fact and a cogent deductive syllogism. For a long time I believed what I was taught. Gradually I had to acknowledge that the paradigm could not fit the facts. (Samuelson 1983b: 7)

Friedrich von Hayek, Samuelson noticed, shared the Chicago view on the matter. Chile, “with its military dictatorship cum-the-Chicago Boys” (ibid), provided a “dramatic” (but far from unique) example at the time of the working of efficient free markets under authoritarian political environments. Whereas Samuelson (1948) had initially opposed capitalism and fascism, by the early 1980s he coined the terms “capitalist fascism” and “market fascism” to describe the Chilean (and to some extent the Brazilian) economic system. By that, he distanced himself from what he had learned at Chicago about links between political and market freedom, and from what he perceived as an important aspect of Chicago economics in the 1970s/80s. The same is true of his criticism that Friedman and Hayek did not grasp the problems involved in the working of “populist democracies” in South America and elsewhere (Samuelson 1980b). From that perspective, the interpretation of the economic and political dynamics of South American countries provided, for a time, a battlefield for the dispute between Samuelson and Friedman over economic theory and policy.

## **2. Addressing the puzzle of Argentinian growth failure**



Samuelson's awareness of the economic features of some of the main South American countries reflected his overall interest in development and growth economics, as witnessed by the chapters on development and growth introduced in the 3<sup>rd</sup> (1955) and 6<sup>th</sup> (1964) editions of his *Economics* respectively (Boianovsky 2019; Boianovsky and Hoover 2014). Standard growth and development models could not account for the relatively poor economic performance of the Southern Cone countries over the 1950-1980 period and beyond. As put by Samuelson (1980a: 682) in his growth chapter, "there have been unpredictable failures of development. Few scholars expected Argentina, Chile and Uruguay ... to do so poorly in material terms since 1945" (see also Samuelson 1981b: 36; 1983a: 70).<sup>4</sup> Samuelson's main focus was Argentina, a country that in the late 19<sup>th</sup> and early 20<sup>th</sup> centuries was among the top 5 nations in income per capita in the world, on a par with the U.S., Canada and Australia. Since mid 20<sup>th</sup> century Argentina experienced a "growth disaster" marked by continuous divergence from developed economies (Jones 2002: 149-50; Taylor 2018).

Samuelson apparently had entertained high expectations about Argentina from early age. As he told his Mexico City audience in 1980,

Suppose someone in 1945 had asked: 'What part of the world do you expect to experience the most dramatic take-off in the next three decades?' Probably I would have given an answer something like the following: 'Argentina is the wave of the future. It has a temperate climate. Its density of population provides a favorable natural resource endowment per employee. By historical accident its present population is the fairly homogenous progeny of Western European nations. And Argentina is in 1945 at that intermediate stage of development from which rapid growth is most easily expected. (Samuelson 1983a: 69-70)

Samuelson ([1971] 1983: 277) had deployed that contra-factual "1945" scenario before. He would repeat it on a few occasions, as in his 2005 interview to *Der Spiegel*, in which he imagined what he would have replied if he had been asked in

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<sup>4</sup> Data on average rates of growth of GDP per capita in the period 1950-80 confirm the Southern Cone's relative stagnation: Argentina (1.6%), Chile (1.4%), Uruguay (1.3%), as compared to Brazil (4.1%), United States (2.2%) and the World as a whole (2.6%) (Ocampo and Ros 2011: 11).

1945 – when “I was a very able young economist at the peak of my powers” – which part of the world would develop fastest. I “would probably have said Latin America: Argentina or maybe Chile ... I was completely wrong.” (Samuelson 2005; see also Samuelson 1997: 2-3). His first reference to Argentina’s unfulfilled growth potential may be found in the 6<sup>th</sup> edition (1964) of *Economics*.<sup>5</sup>

The reasons behind the growth failure of Argentina, Chile and Uruguay (once called the “Switzerland of Latin America”, as Samuelson [1983a: 70] observed) were not essentially economic. Referring implicitly to his *Economics* chapter on economic development, Samuelson (1983a: 70; [1984] 1986: 504; [1981] 1986: 1000) argued that Southern Cone’s relative stagnation was not caused by economic factors such as Malthusian diminishing returns, technological backwardness or a downward shift in exports demand particularly unfavorable to that region. The explanation should be sought elsewhere. “Their sickness, Schumpeter would claim, is political and sociological rather than economic. It has to do with the breakdown of social consensus ... [and] with the workings out of the logic of populist democracy” (Samuelson 1983a: 70). He often discussed his hypothesis that Argentina’s “sickness” was essentially political.<sup>6</sup>

Samuelson ([1971] 1983, [1972] 1983) had advanced that point in the early 1970s<sup>7</sup>, while discussing Schumpeter’s (1942) well-known thesis that capitalism was economically stable but politically unstable, as its very success would bring about anti-market ideologies and anti-capitalist policies that would lead to its dismissal. Samuelson supported his old Harvard teacher intuition that optimal competitive market economies are prone to be interfered with by the political process, but disagreed that such interferences were intensified by economic progress as Schumpeter claimed. Instead, political interference was explained by the attempt to

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<sup>5</sup> “Economies like Argentina stagnated under Dictator Perón; despite natural resources and technology that many a poor country would envy, Argentina has continued to stagnate.” (Samuelson 1964: 799)

<sup>6</sup> For instance: “[Argentina’s] society, not its economy, seems to be sick. Its political system does not function in a way conducive to productivity. And these sicknesses in sociology and government do impair the economic health of the Argentine economy” (Samuelson [1984] 1986: 505).

<sup>7</sup> Samuelson’s 1983 *Economics from the Heart* is a selection from his *Newsweek* articles, except for those two pieces. “What’s happening to the affluent state?”, written in 1971, was apparently never published before. “The businessman’s shrinking prerogatives” came out originally in *Business and Society Review*, spring 1972.

use the state to change income distribution, especially in economies with unequal distribution profile. Argentina and other Southern Cone nations provided some evidence that Schumpeter's prediction, as modified by Samuelson, was correct. South American instability record called attention to the risks of similar effects of stagflation on U.S. long-term economic performance. Why did Southern Cone countries manage to escape economic growth?

I suspect the answer has to be found in populist democracy. If in the time of England's Industrial Revolution men had had the political power to try to rectify within a generation the unconscionable inequities of life, in which a privileged few live well off the sweat of the multitude, it is doubtful that the industrial revolution could ever have continued ... The outcome would have been pretty much like that we have seen in those Latin American countries which have reached the brink of economic development while, so to speak, fully or overly developed in the political sphere. (Samuelson [1971] 1983: 278)

Samuelson borrowed the term "populist democracy" from Robert Dahl (1956: chapter 2), in the sense of unlimited power of majorities. Dahl had distinguished it from "Madisonian democracy" and its concern with reaching a compromise between the power of majorities and minorities. Like in the U.K., universal suffrage was absent from U.S. political history until mid 19<sup>th</sup> century. James Madison, John Adams, Thomas Macaulay – and Karl Marx after them – perceived populist democracy as a source of instability in market economies, incompatible with private property and capitalism (Samuelson 1973a: 803, 856; 1981a: 19; Przeworski and Limongi 1993: 52). Samuelson suggested that "class struggle" in populist democracies should be understood in terms of John von Neumann's game-theoretic concepts of collusions and coalitions (von Neumann and Morgenstern 1944). Under universal suffrage, the majority will legislate against the "minority of plutocrats", who in turn will use their "financial power" to try to limit this income redistribution, argued Samuelson (1973a: 505). He offered that "theorem" as an addendum to Schumpeter's explanation of the political instability of capitalism.

Social equilibrium à la Queen Victoria or Calvin Coolidge is unstable. If all groups but one adhere to its modes of behavior, then it definitely pays the remaining persons to form a collusion and use the state to depart from the

laissez faire beloved by Ludwig von Mises or Fredric Bastiat. (Samuelson 1983a: 71; see also 1981a: 19; 1981b: 43)

Stagflation was interpreted as a manifestation of the application of that theorem to the working of the welfare state in the mixed economy (Samuelson 1983a: 895-96; 1981b: 43). Samuelson did not provide a mathematical formulation of the proposition. He was not a game theorist – that was a rare occasion he built on aspects of von Neumann’s game theory. He did not take lightly von Neumann’s claim that economics needed new mathematics, distinct from the kind developed for physics as generally used by Samuelson (see Mirowski 2002: chapter 3).<sup>8</sup>

Political collusions interferences to redistribute income in populist “mixed economies” often entail deadweight loss and distortions, as Samuelson pointed out. Figure 1 below, introduced in the 8<sup>th</sup> edition of *Economics*, illustrates the trade off between equity and efficiency faced by the welfare state. The issue was how to get from present point *A* to equality point *E* without affecting efficiency through distortionary taxes or interference with market prices of goods and factors. The *ABZ* curve portrays the deadweight cost of strong state interference with the market allocation mechanism. “Conservatives” tended to exaggerate the distortions problem, but there was an element of truth in the proposition that “in seeking a *better* division of the pie, you will *reduce the size* of the pie by creating distorting inefficiencies” (Samuelson, 1970: 834, italics in the original).<sup>9</sup>

FIGURE 1 HERE (NOW AT THE END OF THE PAPER, BEFORE REFERENCES)

Argentina was Samuelson’s favorite example of the perverse effects of a “sick political and social system ... more concerned over the division of the social pie than its total size and growth” (Samuelson [1981] 1986: 1000). He was particularly

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<sup>8</sup> As Samuelson (1989: 112) put it: “Except for the philosophical complications introduced by games involving more than one person, I do not honestly perceive any basic newness in [von Neumann’s] so-called non-physics mathematics.” Collusions in populist democracies were among the “complications” Samuelson was referring to.

<sup>9</sup> Samuelson (1970) probably had some bearing on the adoption of the pie metaphor in the Brazilian 1971-74 intense debates about income distribution, as expressed in the widespread phrase “let the pie grow before sharing it” (“deixar o bolo crescer para depois distribuir”, in Portuguese) – a phrase usually (but imprecisely) attributed to the Brazilian government (see next section and Andrada & Boianovsky 2020).

concerned with attempts to change the distribution profile through increases in money wage rates by government decree within a brief period of time, as it happened in Argentina during Colonel Perón's terms as President in the 1940s and 1950s, and continued to happen "time and time again in the unhappy economic history of Latin America" (Samuelson [1972] 1983: 176). Instead of Lenin's famous remark, that the most effective way to ruin capitalism is by debauching its currency, Samuelson (1973a: 871) maintained that the way to kill off economic progress and exacerbate class struggle in mixed capitalist economy was "to contrive (as was done in Perón's Argentina) a 40 per cent overnight increase in wage rates", with ensuing economic instability and social unrest (Samuelson 1973a: 671).<sup>10</sup>

The slow growth of Argentina, Uruguay or pre-Allende Chile was related to the fact that these societies "are neither fish nor fowl nor good red herring", as they placed social demands on industry that could not be met (Samuelson [1972] 1983: 176). They lacked "social cohesiveness" or "consensus" (Samuelson 1983a: 70; [1984] 1986: 508). However, it was not just about Perón, since years after he had left Argentina, and before his return in 1973, chronic inflation and feeble growth characterized the Southern Cone, as Samuelson (1983a: 70) pointed out. It was "nonsense" to continue to blame Perón for a stagnation that prevailed in the decades after he lost office. But, it was "not nonsense to infer that the populist imperatives upon which Perón so skillfully played have a pivotal role in explaining the miracle of Argentinian stagnation" (Samuelson [1972] 1983: 176). Samuelson sometimes described Perón as "populist", on other occasions as "fascist". Such double description is not uncommon in the literature, as the Argentinean President merged both attributes (see Eatwell 2017).<sup>11</sup>

Samuelson's (1983a; 1981b) 1980 Mexico Address was an exercise in economic prediction. He started by referring to John M. Keynes's ([1930] 1931) famous essay, in which Keynes imagined that continuous technical progress and capital accumulation would produce an age of leisure and enjoyment of art and culture in a world with virtually no economic scarcity. Keynes's paradigm,

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<sup>10</sup> Samuelson did not cite any sources, but it is likely that he was influenced by Diaz-Alejandro's (1970) classic book, which had been recently published.

<sup>11</sup> As defined by Eatwell (2017: 365), political populism combine: (i) the unique defense of the *plain people*, (ii) hostility to *self-serving elites* and (ii) the goal of providing a political system which allows the *popular will* to prevail.

Samuelson (1983a: 60) suggested, ended in a kind of “Swedish utopia”, through the successful interaction of the multiplier and the accelerator brought about by monetary policy. The post-war success of the mixed economy, as epitomized by Sweden’s welfare state, accorded with Keynes’s prophecy. However, by the early 1970s the welfare state was showing signs of crisis, as stagflation problems erupted in industrialized economies. It was in that context that Samuelson turned to Schumpeter’s (instead of Keynes’) predictions, as adapted to Argentina – a country Schumpeter, of course, never referred to. In order to understand the future, Argentina (and some other South American countries) provided a more useful paradigm than Scandinavia, Samuelson (1983a: 69) claimed in a section titled “Latin America as paradigm”. As he put it in dramatic tone in the early 1970s,

If the balancing act by which Sweden is able to generate rapid technological advance within a framework of social redistribution gives out, what abyss lies below? ... Argentina, I dare to suggest, is the pattern which no modern man may face without crossing himself and saying, “There but for the Grace of God...” (Samuelson [1971] 1983: 277)

Samuelson’s “Latin American paradigm” included as well the authoritarian alternative to populist democracy, as discussed next.

### **3. Dealing with the Brazilian military regime**

South American economic history was not uniform. Unlike the Southern Cone countries, Brazil was a case of relatively successful economic growth over the period 1950-1980. As Samuelson ([1984] 1986: 499) described it, Brazil was a “tropical country with the racial heterogeneity often met in such regions.” He found Brazil’s ability to almost double between 1950 and 1980 its fraction of U.S. income per capita a “notable and all too rare phenomenon” among less developed countries (ibid; see note 4 above).<sup>12</sup> By the time he wrote the 9<sup>th</sup> (1973) edition of *Economics*, Samuelson paid attention to the ongoing so-called Brazil’s “economic miracle” of 1967-74, when

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<sup>12</sup> Samuelson’s mention of differences in race and climate between Argentina and Brazil does not easily square with his dismissal of theories about the influence of such variables on economic development as “superficial” (cf. Samuelson 1964: 758-59).

the Brazilian economy featured an annual rate of growth of per capita income around 7%. The Brazilian episode of intense economic growth under a military dictatorship led Samuelson (1973a: 870-71) to insert, as part of the section on “Fascism”, a subsection titled “Order and economic efficiency”. Moreover, he added the “Greek and Brazilian military juntas” to his original list of fascist regimes. That was the first time he changed that section since its inception in 1948. He kept from the 1<sup>st</sup> edition the description of fascism as characterized by “one-man dictatorship, one political party ... the disappearance of civil liberties”, and by strong nationalism together with the view that the “individual is to be secondary to the state” (Samuelson 1973: 870).

Samuelson saw the economic side of the Brazilian authoritarian regime, inaugurated with the 1964 coup d’état, as a reaction to the stagflation that affected the country in 1962-63 (see e.g. Skidmore 1988, chap. 1). When a “populist mixed economy” is running badly, beset by inflation and unemployment, there will often emerge a demand for a “fascist takeover – to restore ‘orderly conditions and promote economic growth’” (Samuelson 1973a: 871). Brazil was a case in point, to Samuelson’s dismay.

It is even sadder to have to witness an occasional success of such dictatorial regimes – in the short run. Thus, in the 1970s, the Brazilian military regime may be hard on professors, intellectuals, and a free press. But, as people used to say in Mussolini’s time, ‘At least the trains run on time...’ And ... Brazil has in recent years been the veritable Japan of Latin America... (Samuelson 1973a: 871)

Brazil’s relatively high average rate of economic growth since the late 1940s was mentioned elsewhere in *Economics*, in the context of the general strategy of economic planning that dominated development policy in the post-war period. Samuelson (1973a: 784-85) listed Brazil together with Taiwan, South Korea and Mexico as examples of “miracles of development” associated to economic planning in market economies. That fitted well with Samuelson’s overall support of the approach to development economics in terms of market failures, increasing returns, perfectly elastic labor supply and poverty traps that dominated the field (see Boianovsky

2019).<sup>13</sup> Indeed, Samuelson gave qualified support to Latin American Import Substitution Industrialization strategy (a concept he ascribed to Raul Prebisch) until the early 1980s, when he gradually joined its critics in view of the increasing evidence on lagging growth rates in Latin America as compared to the so-called Asian Tigers (Boianovsky 2019).<sup>14</sup>

The dynamics of real wage rates was another factor in Brazil's 1967-74 growth acceleration process. As part of a new appendix about Marxian economics, Samuelson (1973a: 863) asked whether real wages could be “determined by power”, instead of economic distribution theories of neoclassical, Marxian or Cambridge kinds. The matter was relevant to his treatment of the “economics of fascism”:

Strong-arm governments that are tough on unions and intellectuals can sometimes produce short-run, so-called ‘miracle’ sprints of real growth – even with near-term real-wage growth. (Brazil is the touted instance of the early 1970s.) (1973a: 863)

Apparently Samuelson's point was that the Brazilian authoritarian regime was able to interfere with the determination of real wages through minimum-wage legislation in an inflationary environment and repression of trade unions. Average real wages did go up after 1968, but by less than productivity growth. This may have contributed to increase the saving ratio, at the cost of higher inequality. By the 11<sup>th</sup> edition of *Economics*, Samuelson reduced the reference to Brazil in the section on fascism to a brief commentary on how the country's 1970s superlative economic growth was accompanied by income concentration – the lowest 20% of the population received only 2% of total household incomes, whereas the highest 20% got 67% of the total. He regarded that an “unusual disparity” when compared to other countries (Samuelson 1980a: 816).

*Economics*, in its several editions since 1948, was translated in Brazil, as it happened all over the world. Work on the Brazilian translation of Samuelson (1973a),

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<sup>13</sup> As argued by Diaz-Alejandro (1988, chap. 12), Brazil's higher rate of growth in 1950-80, as compared to Argentina, resulted in part from the fact that Brazil had a Lewis-type economy with surplus labor absorbed as it moved from low to high-productivity sectors.

<sup>14</sup> His early approval of Prebisch was probably influenced by the latter's position in the 1950s as “chief economic adviser to post-Perón Argentina” (Samuelson 1964: 693).



published in 1975 by Agir Editora, got started soon after the American edition came out. In November 8 1973 Ernst Fromm, director of Agir's office in Rio, wrote to William Orr – director of McGraw-Hill in New York City – asking to consult with Samuelson about changing the “biased portrait” of Brazil as a fascist country. Fromm (1973) found “inconceivable” to provide Brazilian students with a text that “presents their own country as a companion of Hitler's Germany or Mussolini's Italy and contains expressions of deep regret for the economic progress of Brazil.” Fromm urged Orr to ask Samuelson to change the wording, as to, without hiding his “liberal convictions”, avoid “offending Brazilians.” It was not a plain matter of censorship, as Fromm clarified that he was not concerned “so much about our authorities ... as about the normal reader.”<sup>15</sup>

The proprietor of Agir Editora, Cândido Guinle de Paula Machado, was close to General Golbery do Couto e Silva, whom, as head of the presidential staff of General Ernesto Geisel in 1974-79, would lead the political decompression plan (see Gaspari 2003; Skidmore 1989). Golbery showed interest in the controversy with Samuelson, and kept Geisel informed. Further to Fromm's letter to McGraw-Hill, Guinle asked Eugenio Gudin – the dean of Brazilian economics and well-connected internationally – and Roberto Campos (diplomat and former minister of planning in 1964-67) to write to Samuelson.

In correspondence of November 14 1973, Gudin wrote to Samuelson (with copy to Gudin's long-time friend Gottfried Haberler) that Brazil was a “para-military” regime, not a fascist one, and that restraints on freedom were a “matter of the past”. He also asserted that there were no full democracies in Latin American countries, which were not “politically ripe” for it. Campos sent Samuelson a long letter on December 27 1973. He argued that the most appropriate description of the Brazilian regime would be “consented authoritarianism”, as Brazilians had accepted a trade-off between a lesser degree of democratic freedom on one side and political stability, social discipline and economic growth on the other. After lengthy considerations

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<sup>15</sup> The 1973 correspondence involving the 1975 Brazilian translation is held in the Samuelson Papers (Box 81, Foreign Editions). It is also available online in Elio Gaspari's “Arquivos da Ditadura” (<http://arquivosdaditadura.com.br/>), as a supplement to Gaspari's (2003: 264-68) discussion of the whole episode. Gaspari made use of copies of the correspondence held in the Golbery do Couto e Silva Papers, in Gaspari's possession.

about the nature of authoritarianism in Brazil (with acknowledgement that there had been a few “isolated cases of police brutality”), Campos finished by stating that “I would hate to see the brilliance of your economic analysis marred by the flippancy of hasty political judgments.”<sup>16</sup>

Under pressure from McGraw-Hill, Agir and Brazilian pro-government economists, Samuelson caved in and proposed a new wording of the controversial passage in *Economics* (1973a: 871) quoted above. Samuelson (1973b), in his reply to Gudin, pointed out that he had never regarded himself as responsible for the many translations of several editions of *Economics*. Somewhat surprisingly, he wrote in correspondence with Campos: “Each translator on his own responsibility interprets the text in terms of his own country” (Samuelson 1974). Samuelson (1973b) recalled that, when asked about the omission of chapters and passages considered offensive in some leftist regimes, he replied that it was not a matter for him “to object to or to police.”<sup>17</sup> Concerning Brazil, he clarified to Gudin that his intention in the textbook was to point out the “objective fact” that often, to his regret, under “populist democracy” the environment for rapid and efficient economic progress “is not present.” Moreover, he recanted in the letter his speculation in *Economics* that Brazilian economic growth was likely to be short-lived. He offered the replacement of the offending passage for the following:

One must face up to the fact that, often in the short run, systems of government that many intellectuals oppose may register efficient growth. Thus, militant trade unions and revolutionary agitations may work out to be inimical to private investment and market efficiency. A preoccupation with an egalitarian distribution of income may turn out to be at the expense of growth in the total social pie and of a filtering down to the workers and the peasants of some of the increment in that pie. Thus, when one looks in the United

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<sup>16</sup> See Campos’ (1972) discussion of “consented authoritarianism”. Samuelson replied on January 9 1974 that he was not aware of that concept, but would “ponder over its distinction from our own and other forms of government.” Between the beginning of November, when the polemics with Samuelson started, and the end of December, when Campos wrote him, violence against regime opponents mounted (Gaspari 2003: 268). In that same month (December 1973), Milton Friedman visited Brazil. He described the political system as “dictatorship”, which he distinguished from a “totalitarian” regime (Boianovsky 2020).

<sup>17</sup> See Gerschenkron (1978) on the many differences between the original American text of *Economics* and the Russian translation published in the USSR. It is unlikely that Samuelson was aware of or informed about all changes.

Nations Statistical Yearbook, one finds in the 1970's Brazil has been the veritable Japan of Latin America, averaging annual real GDP rates of growth of 10 per cent per year. Supporters of that system might claim that this would not have been possible in the disorderly environment of earlier decades. (Samuelson 1973b)

The pie metaphor, discussed in section 2 above, is used in the proposed new paragraph as a warning against premature emphasis on income distribution, which probably pleased both Gudin and Campos. Moreover, in the revised passage Samuelson touches upon the matter of the relation between authoritarianism and economic growth in societies in early stages of development, a subject that received much attention from social scientists at the time. Harvard political scientist Samuel Huntington – who would visit Brazil under Golbery's invitation in 1972 and 1974 in connection with the political decompression process (Skidmore 1989) – wrote an influential book in 1968 arguing, against classic modernization theory à la Rostow-Lipset, that growth acceleration in developing countries tended to be accompanied by political instability instead of democracy.

Samuelson's "capitulation" – in the double sense that he left his Brazilian "censors" free to take whatever course of action they deemed best, and in view of his suggested rewording – was celebrated by Guinle and Golbery (Gaspari 2003: 266-67). Nevertheless, the Brazilian publisher decided to reject Samuelson's offer and to eliminate any references to the Brazilian political system from the translated book. Hence, the original passage from Samuelson (1973a: 871) was deleted in the translation (Samuelson [1973] 1975: 924), with no replacement by Samuelson's revised text. Moreover, Brazil was excluded from the list of fascist regimes (923) at the start of the section.<sup>18</sup> Interestingly enough, the paragraph in Samuelson (1973a: 863) quoted above, with a reference to the Brazilian "fascist" economy, apparently went unnoticed by Brazilian "censors" and was kept in the translation. It is worth noting that the Spanish translation of the first edition of *Economics* eliminated references to Perón's Argentina and Franco's Spain from that list (Samuelson [1948]

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<sup>18</sup> Another Portuguese translation of the 9<sup>th</sup> edition was published in Portugal, in 1977. It included the passage eliminated from the Brazilian edition (Samuelson [1973] 1977: 1337). That translation, however, could not be sold in Brazil for market reasons.

1951: 624), which continued to be the case in other Spanish editions until 1983, when the Mexican office of McGraw-Hill took over the translation. That also explains why Samuelson's (1980a) discussion of Chile's "capitalist fascism" was not deleted in the 1983 Spanish translation.

Despite Samuelson's correspondence with Gudin and Campos, the next (10<sup>th</sup>) edition of *Economics* kept the section on fascism nearly the same as in the 9<sup>th</sup> edition, including the polemical (from the perspective of the Brazilian establishment) passage on Brazil. The only differences were the addition of the "Chilean junta" to the list of fascist countries, the suppression of the words "it is even sadder to have to witness" and the addition of the phrase "social disorder kills off economic progress" at the end of the section (Samuelson 1976: 870-71). That edition was not translated in Brazil by Agir or by any other publisher. (It was only in the 1990s, after Nordhaus joined as co-author, that the translation of *Economics* was resumed in Brazil, this time by McGraw-Hill's office in Rio.) South American economies continued to attract Samuelson's attention throughout the 1970s and early 1980s.<sup>19</sup> By the 11<sup>th</sup> (1980) edition, Samuelson would shift the focus of his discussion of South American authoritarian regimes from Brazil to Chile, following upon the worldwide interest in the Chilean mix of free markets and oppressive dictatorship.

#### **4. Targeting Chile's Chicago Boys**

Samuelson (1980a: 814) added Argentina's military junta (1976-1983) to the list of fascist regimes, but the main change in the section about fascism was his discussion of "capitalist fascism" in Chile (815-16). From Samuelson's perspective, what made the Chilean experience unique in South America was that, unlike other contemporary military regimes in Brazil, Argentina or Uruguay, it was firmly based on Chicago economics, with its combination of microeconomic unregulated markets (as the key to resources allocation) and macroeconomic monetarism (as the foundation of economic stabilization). Samuelson (1980a: 815-16; 1983a: 75-76; 1981b: 44) further

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<sup>19</sup> As told by Persio Arida – PhD student at the MIT economics department in the late 1970s – in conversation of August 16 2019, Samuelson showed evident interest in South American economies in contacts with MIT graduate students from the region at the time.

elaborated on his point – advanced in his 1973 treatment of Brazil’s “economic miracle” discussed above – about the “fascist solution” to stagflation. In a section titled “The devil’s fix that does not fix”, Samuelson (1983a: 75) tackled the “fascist solution” as a way out of the dilemmas of the democratic populist mixed economy, a notion he attributed to Georges Sorel and, especially, Vilfredo Pareto. It was only implicit in Schumpeter, who in conversation with Samuelson disclosed the “obvious moral” from his insight about the political instability of capitalism.

What I am alluding to is of course the fascist solution. If the efficient market is politically unstable, then fascist sympathizers conclude: ‘*Get rid of democracy and impose upon society the market regime.* Never mind that trade unions must be emasculated and pesky intellectuals put into jail or exile.’ (Samuelson 1983a: 75)

The notion of “imposed capitalism” was the main element of Samuelson’s (ibid) theory of the “distasteful subject of capitalist fascism” (or “market fascism”). He was inspired by Pareto’s theory of circulation of elites and discussion of the economic and political situation in Italy during 1914-22 (see e.g. Pareto [1920] 1984), as well as by the experience of contemporary Pinochet’s Chile. As a graduate student in the 1930s, Samuelson had attended seminars of the famous Harvard Pareto Circle. Although his recollection in the 1990s was that he avoided the Circle seminars about Pareto’s sociology (see Backhouse 2017: 197), Samuelson’s (1983a; 1981b) references to Pareto indicate that he was familiar with the Italian’s sociological contributions, apart from the economic ones. From the 1<sup>st</sup> edition of *Economics*, Samuelson (1948: 66), while discussing Pareto’s Law of income distribution, mentioned that Pareto was “often called, with somewhat questionable accuracy, the ideological precursor of fascism.” He probably read a draft of Schumpeter’s (1949: 153) article with its claim that Pareto could not unambiguously be labeled fascist and its explanation of the circumstances surrounding Pareto’s support of Mussolini. As Samuelson ([1973c] 1983: 220) put it, Pareto was a “disillusioned liberal who flirted with Mussolini’s fascism until that too disillusioned him.”

Samuelson’s (1973a: 870) assertion – that “Fascism is the great spoiler. It thrives on the breakdown of markets and of democratic processes” – is consistent with Pareto’s criticism of Italian social disorganization, which Pareto associated to “demagogic plutocracy” and decadent parliamentary democracy (see Mosca and

Somaini 2018). Samuelson's concept of "capitalist fascism" was a contradiction in terms if compared to his original discussion, from the 1<sup>st</sup> edition of *Economics* on, of fascism as an *alternative* to capitalism. This is explained by Samuelson's early notion – inherited from Chicago – that market freedoms and personal freedoms were necessarily intertwined, which he later rejected (see Samuelson 1983b). Furthermore, he changed his approach to the economics of fascism in the 11<sup>th</sup> (1980) edition of *Economics*.

As Samuelson acknowledged from the 1<sup>st</sup> edition of his textbook, fascism was easier to describe politically than economically. From the economic perspective, he referred to Mussolini's "syndicalist" or "corporate" state, but did not dwell on corporatism – particularly important in Italy and Portugal – as a form of organization of economic activity (see Almodovar and Cardoso 2005). "Almost all" fascist regimes gave central government "great regulatory power over every sphere of economic life", Samuelson (1976: 870) remarked in all editions up to 1976. In the 11<sup>th</sup> edition he replaced "almost all" for "some", as befitted his new theory of "capitalist fascism" (Samuelson 1980a: 815). That concept, with its combination of market freedom and political restraint, displayed a clear Paretian pedigree. Pareto supported free market instead of corporatism, unlike the dominant approach to fascism. He was an ultraliberal laissez-faire economist, but of a different kind from J.S. Mill and other classical economists, as he distrusted parliamentary democracy and dissociated market and political freedoms (Schumpeter 1949: 152). Samuelson (1980b: 40) shared Schumpeter's assessment.

In August 1980, immediately after the IEA Mexico conference, Samuelson traveled to Peru to lecture on the same topic of his Mexico talk. While in Peru he gave an interview to *Caretas*, a leading Peruvian newsmagazine.<sup>20</sup> Samuelson (1980b: 40) charged Friedman and the Chicago School for missing the point – understood by "sophisticated conservatives" like Pareto and Schumpeter – that, under democracies, market laissez faire would always suffer interferences from agents' pursue of their

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<sup>20</sup> In November that year, Milton Friedman also came to Peru and was interviewed by the same magazine (Edwards and Montes 2020). Samuelson ([1980c] 1983) wrote a report for *Newsweek* about his travel to Peru, which was then experiencing a democratic recovery. That was apparently his only time in South America. As Samuelson ([1981c] 1986: 1000) described it, "Last summer when I visited Peru ... the press at my lectures tried to build me as an anti-Friedman. That is not my preferred role."

own interests in the political arena. Neither did Chicago economists realize its corollary that an imposed political system may assure market freedom and stability. He referred the readers to the new section on “capitalist fascism” in the 1980 edition of *Economics*, with its discussion of the Chilean example as a “Harvard case study.”

In the same interview, however, he ascribed to market conservative economists in general the view that personal freedoms (together with economic equality) should be sacrificed in the short run at the altar of market freedom and economic efficiency. Chicago economists expected that economic growth would in the long run bring about democracy and larger slices of the social “pie” to everyone, even if inequality increased in the meantime (Samuelson 1980b: 39-40). Samuelson doubted that final natural outcome of “capitalist fascism” in Chile and elsewhere. While individuals wait for the pie to increase, “those who are hungry die of starvation.” Concerning democratization, Samuelson repeated his claim, advanced in *Economics*, that capitalist fascism “cannot evolve into normal democracy”, as its “business freedoms are maintainable only by being *imposed* on the populist voters. The dictators dare not ease up on repression” (Samuelson 1980a: 816). He was not just an impartial spectator: “I abhor Chile with its fascist capitalism – Chicago economics imposed by political force” (Samuelson [1981c] 1986: 999).

That notion – that a “free society”, regulated by the market, had to be forcefully “imposed” – prevailed in Chile after the 1973 military coup d’état, as a reaction to the hitherto pattern of an interventionist state and an egalitarian inclination towards “social justice”, as pointed out by Valdes (1996: 5) in his narrative of how the Chicago School came to dominate economic thought and policy in that country. The argument that the establishment in Chile of a free market economy required an authoritarian regime gained support in the mid 1970s (ibid). Valdes’ account is compatible with Samuelson’s interpretation, although he did not refer to the MIT economist.<sup>21</sup> Samuelson used the Chilean case to illustrate what he saw as a new paradigm. If Chile and the Chicago Boys had not existed, he suggested, “we should have to invent then as a paradigm” (Samuelson 1983a: 75). He provided a brief but sharp account of the working of capitalist fascism in Chile in the 1970s and early 1980s.

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<sup>21</sup> Samuelson’s concept of capitalist (or market) fascism was mentioned in the 1980s and early 1990s literature on Latin American economic development (e.g. Tavares 1990; Sigmund 1984).

Generals and admirals take power ... But, in this variant of market fascism, the military leaders stay out of the economy. *They* don't plan and don't take bribes. They turn over all economics to religious zealots – zealots whose religion is the laissez faire market, zealots who also take no bribes. (Opponents of the Chilean regime somewhat unfairly called this group 'the Chicago Boys', in recognition that many of them had been trained or influenced by University of Chicago economists who favored free markets.) (Samuelson 1980a: 816; 1983a: 75)

Chicago libertarian economics represented a return to aspects of 19<sup>th</sup> century laissez faire:

Then the clock of history is turned back. The market is set free, and the money supply is strictly controlled. Without welfare transfer payments, workers must work or starve. Those unemployed now hold down the growth of the competitive wage rate. Inflation may well be reduced if not wiped out. (Samuelson 1980a: 816; 1983a: 75)

Indeed, the Chilean inflation rate dropped from 508% in 1973 to 9.5% in 1981, whereas unemployment in Greater Santiago increased from 4.7% in 1973 to 11% in 1981, accompanied by changes in the rate of GDP growth from minus 3.6% in 1973 to positive 5.7% in 1981 (Sigmund 1984: 5). At the same time, real wages came down significantly, together with a huge gap driven between rich and poor classes. Increased economic inequality remained a feature of Chile's society even after the resumption of democracy in 1990 (Valdes 1996: 4). The economic outcome of the Chicago experiment in Chile was unequal economic growth, under the stimulus of foreign capital inflow in a repressive regime:

If the production-index rises and foreign investments pour in, what is there to complaint about? Political freedom aside, *there does tend to be a significant increase in the degree of inequality of incomes, consumption and wealth* under the archetypical pattern here envisaged. (Samuelson 1980a: 816; 1983a: 75-76; italics in the original)<sup>22</sup>

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<sup>22</sup> Instead of reporting Chilean data, Samuelson (1980a: 816) referred to numbers of increasing inequality in Brazil, a favorite international example at the time (see section 3 above).



Chile provided the most dramatic illustration of an economic-political phenomenon that was not restricted to Latin America, but reached as well the so-called Asian Tigers. Together with Chile, countries like Brazil, Mexico, South Korea, Singapore and Taiwan were all examples of “*successfully developing countries*” that were also “*one-party political systems, some of them outright dictatorships*” (Samuelson 1983a: 76; italics in the original). Contrary to the logic of Hayek’s (1944) *Road to Serfdom* and to the teachings of Chicago economists since the 1930s, fast growing countries with efficient free markets lived under quasi-fascist or outright fascist regimes in the 1970s and early 1980s (Samuelson 1983b: 60; 1983b: 7; for a broad criticism of Hayek’s thesis about the connection between personal and market freedoms see Samuelson 1970: 834-35, repeated in other editions of *Economics*). Based on historical episodes – such as Mussolini’s Italy – Samuelson (1980a: 816) did not expect economic growth under fascist (or quasi-fascist) regimes to be sustainable in the long run.

Samuelson’s notion of “capitalist fascism” fits aspects of “bureaucratic authoritarianism”, an influential concept introduced by Argentinean political scientist Guillermo O’Donnell (1973, 1978) to characterize the civil-military dictatorships of the Southern Cone countries and Brazil between the 1960s and 1980s. That new political system featured strong bureaucratic organization, technocratic decision-making, the exclusion of popular sectors and the repression of political dissidence (see also Heiss 2017). Bureaucratic authoritarianism resulted from the process of late modernization and deepening of import substituting industrialization in South America, which tended to destabilize the democratic institutional order (see also Huntington 1968). O’Donnell (1978: 30) distinguished bureaucratic authoritarianism from classic fascism, in which the dynamic role was held by the state and national bourgeoisie, and the political expression of the working class took place through quite different channels. Gudin’s and (especially) Campos’ criticism, in correspondence with Samuelson discussed above, of the description of Brazil’s military regime as “fascist” should be seen against that background. Interestingly enough, Prebisch (1983) presented at the Mexico IEA 1980 conference a paper about the combination of political authoritarianism and economic liberalism as the “natural” (if regrettable) consequence of the dynamics of peripheral capitalism. Prebisch raised issues similar

to Samuelson (1983a), but he did not dwell on the implications of the analysis for developed nations such as the U.S.

Monetarist policies à la Chicago could only succeed in fighting stagflation in the U.S. and other developed economies if the same harsh political conditions that prevailed in Chile were reproduced in those countries, Samuelson ([1980d] 1986: 972) claimed. This would entail “abolishing the humane society, reverting to the 19<sup>th</sup> century jungle of ruthless capitalism and to the dogmas of frozen money supplies and ever-balanced budgets”, with ensuing inequality and suffering incompatible with democracy. A “fascist political state”, like in Chile, would be needed to “impose such a regime and preserve it.” The Chilean monetarist experiment was the “conservatives’ ‘final solution’ to stagflation and to the need for an ‘incomes policy’” (Samuelson 1980a: 815). Short of a “military junta”, Samuelson ([1980d] 1986) deemed that solution to the stagflation problem in the U.S. as “unrealistic” and “undesirable” to most.

Daunted by the Chilean stabilization episode, Samuelson was one of the very few academic economists in Anglo-Saxon countries who put monetarism and fascism together. Nicholas Kaldor (1978), a well-known opponent of Friedman’s monetary theory, made a similar claim, but in a somewhat different guise. Kaldor argued that the inflation rate came down in Chile in 1976-77 not because of the contraction in the rate of growth of money supply, but due to the “prohibition of wage increases with concentration camps for those who disobey” – a sort of incomes policy only possible under “fascist dictatorships”, unthinkable in the U.K. Friedman’s (1982) *Newsweek* article – a likely reaction to Samuelson – criticized the generalization of the context of Chile’s macroeconomic stabilization and economic reforms as a basis for the “myth that only an authoritarian regime can successfully implement a free market policy.” As the 1980s unfolded, with the increasing dominance of conservative policies in the U.S and the U.K., the issue would acquire a new meaning.

## **5. Inequality and instability**

By the end of the 20<sup>th</sup> century, it became clear that Samuelson’s (1983a; 1981b) fear that the United States’ economy would approach Argentina’s growth failure had not

been confirmed, as stagflation gave way to the “Great Moderation” period. That was influenced by profound changes in the working of the mixed economy and of the welfare state – although changes were not of the “utopian” kind Samuelson (1983a: 76; 1983b: 7) hoped for, based on an “optimizing compromise” between equality and efficiency. In 1997 Samuelson wrote a paper outline for a conference in Buenos Aires, which he did not attend. Although he no longer regarded Argentina as a “paradigm”, the country still provided a forceful illustration of the impact of political factors on economic growth. Samuelson (1997a) resumed his 1981 hypothesis – quoted at the outset of this paper – that the political instability of capitalism comes from its inability to produce a degree of equality deemed fair by electors (Samuelson 1981a: 19). After repeating his argument about how Argentina after World War II was poised to embark on a “great spurt of productivity innovation”, Samuelson asked: “what went wrong?” Income and wealth inequality provided an answer.

[In Argentina] There was a history of considerable inequality of wealth between rich landowners and uneducated urban populations. Democracy, as elsewhere in Latin America, evolved in a *populist* direction ... by promising the lower-income majority programs that would interfere with the verdicts of competitive markets. (Samuelson 1997: 3-4)

Such redistributive programs were usually accompanied by loose macroeconomic policies conducive to high inflation rates and balance of payments disequilibria, called “populist hyperinflation” by Samuelson (1997a: 6).

As many others in the 1990s, Samuelson was interested in the factors that could account for the contrast between the long-run growth paths of Argentina and other South American countries on one side and East Asian countries such as South Korea and Japan on the other. Due to their relatively low degree of income inequality, both Korea and Japan featured a degree of social cohesion that was lacking in Argentina.

Market capitalism always produces a degree of interpersonal inequality. But, where like people start not too far apart in endowments, the degree of the resulting inequality is moderate. It then follows that a more serene political system can flourish, within which the efficiencies of a market system of profit-and-loss can best be realized. (Samuelson 1997a: 4-5)

By the time Samuelson drafted his 1997 Buenos Aires paper, the view had become widespread of macroeconomic populism as a prevailing characteristic throughout Latin American 20<sup>th</sup> century economic history. The repetitive failure of Latin American economic populism – understood as an approach to economics that stresses growth and redistribution, with little attention to the risks of inflation and external constraints – was the theme of an influential book edited in 1991 by Rudiger Dornbusch (Samuelson's colleague at MIT) and Chilean economist Sebastian Edwards. The topic was also investigated at the time by Jeffrey Sachs (1989), who argued that high income inequality in Latin America led to political pressures for macroeconomic policies to raise the income of the poor, which in turn led to bad policy choices and fragile economic performance in the region.<sup>23</sup>

The broad theoretical and empirical investigations of the effects of income distribution on economic policy, and by that on economic growth, entered the research agenda of growth economists in the 1990s, from the perspective of new political economy. Alesina and Rodrick (1994), for instance, argued in a theoretical-empirical model that inequality in land (a proxy for wealth) and income distribution is negatively correlated with subsequent economic growth. The model is based on the median-voter theorem, according to which the tax rate decided by the government reflects the preferences of the median voter. If the mean income exceeds median income, majority voting favors redistribution from rich to poor, which may affect growth negatively because of distortionary taxes or any other kind of redistributive policy that reduces the incentive to capital accumulation. Such generalization of the median-voter theorem, established by Meltzer and Richard (1981) among others, is compatible with Samuelson's approach to inequality and populist democracy in terms of von Neumann's game theory, discussed above. By the time Samuelson delivered his 1980 Mexico address, such implications of the median voter theorem were not well known as yet. Shortly after that lecture, Mancur Olson's (1982) book came out, with Samuelson's endorsement in its back cover. Olson's thesis – that game-theoretic struggles between different interest groups in a democracy are likely to produce deadweight losses, Pareto inefficiency and economic decline, as witnessed by

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<sup>23</sup> Samuelson's discussion of populism and of Argentina's stagnation was not mentioned in that literature, but it was noticed elsewhere (see e.g. Di Tella and Platt 1986: 201, 2014, 210; Glaeser, Di Tella and Llach 2018:6).

stagflation phenomena – was close to Samuelson’s own approach to the political instability of capitalism (Samuelson [1984] 1986: 504).

Samuelson’s discussion of the perverse effects on economic efficiency of attempted changes in distribution through the political process was reminiscent of aspects of Pareto’s Law of income distribution. According to Pareto’s (1897: book 3: chapter 1) famous empirical proposition, there is a tendency for income to be distributed in the same (skewed) way, regardless of social and political institutions and of taxation. Pareto’s Law of stability of income distribution provided the basis for his theory of circulation of elites. Samuelson (1948: 66) discussed critically that proposition since the first edition of *Economics*, as part of his overall interest in income distribution.<sup>24</sup>

In his new chapter on distribution, Samuelson (1970: 764) noted that Pareto followed the tradition of (most) classical economists who approached economics as the dismal science of unalterable distribution of income. If trade unions or political parties tried to use the state to modify distribution, all that they would accomplish would be to “*contrive a smaller social pie*, which would probably get distributed in about the same way.” However, in contradiction with Pareto’s Law, the inception of modern welfare state in developed countries reduced the degree of income inequality in the first half of the 20<sup>th</sup> century, which remained stabilized for around three decades. The problem, from that perspective, was how to assure that democratic interferences with the market economy were “nicely optimal”, without deadweight losses and distortions (Samuelson 1983a: 72).<sup>25</sup> It is assumed in Samuelson’s argument about Argentina as a paradigm that South American economies were prone to non-optimal interferences – as it became the case in the U.S and other developed countries as well in the 1970s.

The share of top decile in national income increased significantly in the U.S. since the 1980s (see Piketty [2013] 2014: 22-25). Samuelson’s (1980a) anticipation of higher inequality due to the adoption of free-market policies in Chile after 1973

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<sup>24</sup> Samuelson (1965) argued formally that the relative invariance of the Pareto coefficients was consistent with long-term observed reduction in inequality in developed countries.

<sup>25</sup> Samuelson’s (1947: chapter 8) social welfare function distinguished between Pareto optimality (allocative efficiency) and distributive equity. A distinct optimum is associated with every possible income distribution. But, if one follows Pareto in assuming that the distribution looked quite similar and stable across most societies, it is unnecessary to discuss alternative efficiency points (see Persky 1992).

had been borne out in that country. Market-based economic policies followed in the 1980s and 1990s in the U.S and in the U.K. – although in a democratic environment – which also played a role in increasing inequality in those countries (Samuelson and Nordhaus 2001: chapter 19). Unregulated capitalism, Samuelson (2008) claimed, had caused “intolerable inequality” in America. Such inequality, instead of being the price to encourage innovation and progress, brought about shortfalls in total factor productivity. Samuelson found evidence for that in the increase of CEO pay relatively to median employee pay (400 to 1) in 2001-2008 while industrial progress declined in the U.S. in the period.

Samuelson (1981b: 42) referred in his 1980 Mexico address to the “new trend towards libertarianism” in the U.S. and the U.K. But he could not anticipate the full extent of the changes that were about to come in the “Reagan era revolution”, when for the first time since the 1930s, the electorate shifted away from redistributive welfare state and economic regulation (Samuelson and Nordhaus 2001: 25; Samuelson 1999b). The usual ebb and flow of political elections in the U.S., up to the 1980s, had involved only marginal changes in the “American *Zeitgeist*”, with no trend back to the “Victorian conditions” (Samuelson 1973a: 734). After returning to democracy in 1990, Chilean economic policy continued to be essentially market-based, featuring steady economic growth, as Samuelson and Nordhaus (25) noted. In his Buenos Aires paper, Samuelson (1997a: 9) hailed Chile’s “excellent recovery from its socialistic venture and ensuing military fascism”, and hoped that Argentina, Brazil and other South American economies would follow that path – disregarding its effects on inequality.<sup>26</sup>

Although inspired by South American events, Samuelson (1981b: 44; see also 1983a: 75) saw his notion of “capitalist fascism” as relevant above the equator as well, as he applied it to Propositions 2 ½ and 13 (Samuelson imprecisely wrote 19). Those were constitutional amendments that placed limits on the powers of legislative majorities to impose taxes in Massachusetts and California respectively. As he

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<sup>26</sup> As Samuelson (1973a) had anticipated, the Brazilian “economic miracle” was short-lived, as the economy went through a deep stagflation in the 1980s. The reasons, however, were not purely endogenous, but associated to the external debt crises that hit Latin American (and other) countries in the 1980s and 1990s (see Samuelson and Nordhaus 1989, which includes many references to the effects of the debt crises on the Brazilian economy). In an interview to the Brazilian business weekly *Exame*, Samuelson (1999a: 40) wondered whether the “specter of a military solution” of a fascist kind still existed in Brazil, which the reporter denied.

interpreted it, “if democracy cannot be trusted, write once and forever in the constitution that capitalism must be the law of the land.” That was a controversial assessment, which raised critical reactions from James Buchanan in an unpublished paper prepared for the 1981 meetings of the Mont Pelerin Society in Chile (see Farrant and Tarko 2019). Buchanan accepted Samuelson’s description of Pinochet’s regime as “capitalist fascism”, but rejected the transfer of the concept to democratic United States.

The wave of democratization in East Asian and South American countries in the 1980s and 1990s brought new light to the relation between authoritarianism and economic growth discussed by Samuelson and others in the late 1960s and the 1970s. Samuelson and Nordhaus (2001: 750-51) produced a diagram plotting data for income per capita and political freedom for a set of countries in the years 1972 and 1998. Data indicated a general positive association (see also Acemoglu and Robinson 2012 for a detailed treatment). However, that did not mean a return to the Chicago view Samuelson (1983b) had criticized. There were “important exceptions” to that rule, “for a market economy is neither necessary nor sufficient for democracy.” Countries in the “transition to advanced capitalism pass through a period of authoritarian rule”, as illustrated by East Asia and many Latin American countries throughout the 20<sup>th</sup> century. Moreover, during periods of economic difficulties, countries sometimes experience democracy “fatigue” and allow its overthrow by authoritarian rulers (Samuelson and Nordhaus 2001: 750). By then, Samuelson (2004) had turned its attention to economic development in the Pacific Rim and its implications for trade and income distribution in the U.S. Like in his previous investigation of South American economies, Samuelson (2004) discussed China and South Korea from his perspective as an American economist interested in drawing conclusions for the economic development of his own country.

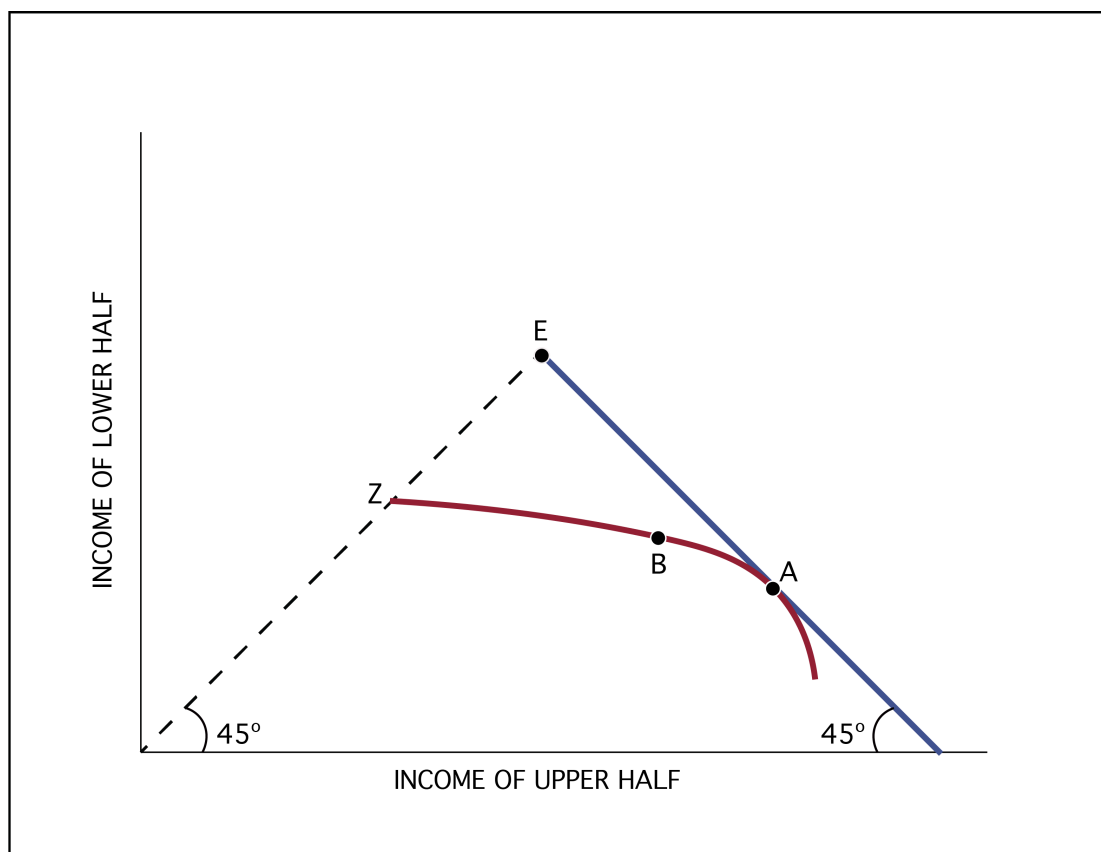


Figure 1. Redistributing social pie may reduce its total.  
Source: Samuelson 1970, p. 767.

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