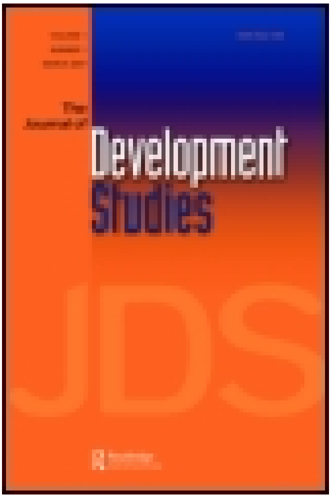

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Was Latin America too rich to prosper? Structural and political obstacles to export-led industrial growth

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Was Latin America Too Rich to Prosper? Structural and Political Obstacles to Export-Led Industrial Growth

JAMES E. MAHON, JR.

This essay explores the divergence in economic policy and performance between East Asia and Latin America. It offers a typology of explanations from the political economy literature. Evidence is presented for an explanation focused upon the relative size of the income sacrifice entailed in the competitive export of simple manufactures. In the 1960s, Latin American countries would have faced massive, politically unthinkable currency devaluations, had they sought to compete with East Asia. Thus Latin American dependency in the post-war period has been more complex than often supposed. The essay ends with thoughts on export-led industrialisation in indebted Latin America.

INTRODUCTION

Much of recent discussion about the political economy of development has turned upon a contrast between Latin America and East Asia. East Asian growth, seen largely as the result of dynamic export-oriented industrialisation (henceforth EOI), has been juxtaposed with a relatively more sluggish Latin American performance. This has raised the question: why did Latin America persist for so long with a more protectionist model emphasising import-substituting industrialisation (henceforth ISI), despite foreign exchange crises and IMF prodding? One common answer

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implicates political weaknesses that bloated the state, protected urban industrialists, and coddled labour unions. Alternatively, the divergence is explained with reference to the wishes of foreign actors, especially the US government. This essay emphasises another dimension of the contrast: the size of the structural and hence political obstacles faced by middle-income developing countries in the turn to exporting low-wage manufactured goods.

After recounting briefly the most important features of post-war industrialisation policies in each region, I review and classify some explanations for the inter-regional contrast. Looking closely at the late 1950s and the 1960s, I focus on the political and structural determinants of the foreign exchange and trade policies that formed the core of ISI and EOI. I present evidence for the hypothesis that Latin America's relatively productive primary exports posed an obstacle to a full reorientation of policy from ISI to EOI. In most of the major Latin American countries the embrace of EOI would have required a substantially greater income sacrifice to achieve world-competitive low wage levels via devaluation. This made the decision even riskier politically: it pushed the expected time at which pre-devaluation real wages might be reattained beyond the horizons of politicians. This helps explain how the very 'success' of Latin America's historical insertion into the world economy as a primary-product exporter served to discourage the policy reforms that would have been necessary to reinsert the region on more dynamic terms. The essay ends with reflections on the likelihood of successful reinsertion in the wake of the debt crisis.

As already noted, the contrast between East Asian EOI growth and Latin American ISI stagnation has been a prominent theme in the literature on development in the last five years.[1] My emphasis on the role of the primary export sector in discouraging EOI follows the analysis of Marcelo Diamand in his treatment of Argentina [*1973; 1986*]. It has been discussed in Keesing [*1981: 19–20*] and, within a comparative framework similar to mine, by Gereffi [*1987: 27–9*]. I am taking up Haggard's criticism of this line of argument, that it is 'too loose and too ahistorical to explain much' if it merely states that East Asia is resource poor and Latin America is resource rich [*1989: 148*]. I seek to show that during a crucial period when many Latin American countries were experiencing the kind of exchange crises that could provoke policy innovation, these countries also would have encountered large structural and political obstacles to low-wage, export-oriented industrial growth.

EXCHANGE POLICY AND LATIN AMERICAN DEVELOPMENT: THE RISE AND DECLINE OF ISI

The legacy of the Second World War to Latin American economies was a contradictory one. By 1945 the major countries of the region had accumulated large foreign exchange reserves, which though substantially inconvertible, were the largest they had ever held. There was postponed demand for investment goods, pent-up demand for foreign consumer goods (from newly-rich factory owners, among others), and a larger industrial work force. Wartime inflation had caused a decline in real wages in most places, but many governments repressed the demands of workers under laws ostensibly justified by the war emergency. Finally, in most major countries (except Argentina) price inflation had outrun similar trends in the United States during the 1940–46 period, while exchange rates stayed nearly fixed [*IMF, various issues*]. This made US goods seem relatively cheap in domestic currency terms. The stage was set for the appearance of several familiar problems of postwar Latin American economies: the rapid exhaustion of the foreign exchange reserves, inflation-driven wage disputes, and the entrenchment of an import-substitution model whose chief instruments were trade protection and state subsidy, rather than a reliance on relative price effects.

The foreign-exchange constraint soon became a major driving force of economic policy in nearly every country. For various reasons, the policy responses were similar across the region.[3] Foreign exchange shortfalls were to be ended by attending to the import side-industrial import substitution behind administrative barriers [*Baer, 1972*]. Hence many large Latin American countries erected multiple exchange rate systems designed to subsidise industrial-sector imports at the expense of the traditional export sector [*König, 1968*]. But by the late 1950s it was clear that this elaborate method of industrial subsidy did not solve the foreign sector problem. Export revenue stagnated or declined in the second half of the 1950s and early 1960s, while import needs as a proportion of GDP did not fall quickly enough.[4] Recurrent balance-of-payments crises became a regular feature in many countries, notably Argentina, Brazil, Chile, and Colombia, from the mid-1950s to the late 1960s. But now it was politically much more difficult to undertake sharp and effective currency depreciation than it had been in the early 1930s.[5]

Two perverse and unexpected results of Latin American ISI were particularly disturbing. The first was that it made the economy more, not less dependent on its capacity to import [*United Nations, ECLA, 1964; Diaz Alejandro, 1965b; Felix, 1968*]. By eliminating consumer goods imports in favour of imports of raw, intermediate, or capital goods, it placed jobs and economic growth at the mercy of the balance of payments. Instead of affecting only the consumption styles of the upper classes who bought imported wares, now foreign exchange crises would send shock waves through an entire industrial economy that depended on imported inputs [*Baer, 1972: 106*]. The second unfortunate result was the persistence or worsening of dependence on a few primary-commodity exports. Exchange rates artificially supported by trade and exchange controls (intended to benefit domestically-oriented industry) were unfavourable to exports, especially new or marginal ones. Special rates established for minor exports were fiscally costly in proportion to their aggressiveness, and often varied too much to be effective. Over the long term, exports tended to remain restricted to those best established. Combined, the greater import dependence and the persistent concentration in primary exports meant that when the terms of trade went against the country or a bad harvest curtailed its exports, the loss of import capacity brought industrial recession.

Politically, this situation was disastrous. The very groups who incarnated the old 'colonial' style of development were the ones to whom the country had to turn in the event of exchange shortfalls. The hopes that ISI could liberate the country from the clutches of foreign investors or domestic oligarchs were dashed repeatedly.

REFORMS OF THE ISI MODEL IN LATIN AMERICA

A full transition out of ISI and into EOI never really took place in Latin America, but in the face of recurrent exchange crises several countries did reform their foreign exchange regimes[6] and conduct partial or discontinuous liberalisations of trade. (The least partial and most continuous was, of course, Chile after mid-1975.) The typical exchange policy reform included a crawling-peg rate system, designed to keep real rates stable under inflation for the benefit of exports and the control of capital flows, and some continued reliance on exchange control to reduce procyclical pressures in the exchange market. Where the reforms were durable enough to survive until the borrowing spree of the late 1970s, countries suffered less from problems of speculation and capital flight [*Mahon, 1989*].

In most of the region, however, periodic exchange shortfalls, heavy reliance on foreign finance, and the periodic resuscitation of ISI programmes were the norm. None of the foreign-sector policy reforms constituted a thoroughgoing reorientation toward manufactured exports, or even toward exports in general. The more successful were what

Fishlow [*1987*] has called 'export-adequate' reforms: they retained the emphasis on a large internal market (as is implied by Brazil's debt-driven simultaneous pursuit of ISI and export objectives in the late 1970s), while diversifying and expanding exports in order to reduce commodity dependence and increase imports. They tended to benefit traditional rural elites who diversified agro-export production as much as they favoured export-minded industrial firms. Other countries, which had suffered few crises, left the fundamental structure of foreign-sector policy intact. In Mexico and Venezuela, for example, the regime of protected ISI was first supported but was then dramatically undermined by commodity prices and international capital flows.

FROM ISI TO EOI IN SOUTH KOREA AND TAIWAN

In many ways the experiences of South Korea and Taiwan with import substitution in the 1950s were similar to those of the larger Latin American countries. Analyses of economic development in these two countries place the stage of import substitution between 1953 and 1960 for South Korea and between 1953 and 1961 for Taiwan, with the latter boundary a gradual one, especially in Taiwan [*Mason, Kim, Perkins, et al., 1980: 126–7; Fei, Ranis and Kuo, 1979: 26–8;* also *Cole and Lyman, 1971; Jacoby, 1966; Gold, 1986*]. During these years policies were a familiar mix of subsidies, overvalued exchange rates, import protection, and credit rationing marked also by the discretionary use of political power to favour selected borrowers or importers. In South Korea especially, this system was associated with administrative complexity and corruption. One study of its foreign trade regime declared that 'the multiplicity of exchange rates and means of allocating foreign exchange from 1953 to 1960 are staggering to comprehend' [*Frank, Kim and Westphal, 1975: 36*]. Although both countries' trade policies also included substantial fiscal subsidies and other legal advantages for exporters, they ended the 1950s still immensely dependent on US aid to finance their imports.

Nevertheless, by 1965 both countries had embarked on concerted programmes to incorporate themselves into the international economy through the promotion of labour-intensive manufactured exports. Both had undertaken large devaluations (Korea twice in early 1961, then a 95 per cent devaluation in 1964; Taiwan in 1960) and had simplified their foreign exchange systems to allow the market more power in reducing imports and to increase incentives to export. Both had allowed domestic interest rates to rise, in part to help stabilise prices in the wake of the devaluations.

By the late 1960s foreign direct investment had risen greatly from its insubstantial previous level, especially in Taiwan, reinforcing these countries' positions as low-wage sites for export industry. The two countries were on a path of rapid employment growth and rising real wages; there were even labour shortages in Taiwan after the late 1960s and in Korea beginning somewhat later. In the 1970s and early 1980s backward linkages from export processing plants were strengthened and, along with new efforts at import substitution (especially in South Korea), each country began to export some higher value-added goods such as automobiles and personal computers. Although the problems of their EOI models became more evident in the late 1980s [*Bello and Rosenfeld, 1990*], the fact remains that these countries moved decisively from ISI to EOI and prospered as a result.

WHY DID LATIN AMERICA NOT FOLLOW THE EAST ASIAN PATH?

Despite the large foreign debt and recent labour protest in South Korea, by 1990 the contrast between advancing East Asia and debt-ridden Latin America was a stark one. As real wages rise in South Korea and Taiwan, Latin American per capita incomes have fallen to levels approximating those of the early 1970s. The inter-regional difference in real per capita GDP growth is especially strong for the 1986–89 period [*IBRD, 1989; OECD Development Centre, 1989; IMF, 1989*].

Apparently, the East Asian countries followed a development strategy more appropriate to the international environment than that pursued by most of Latin America. Hence the puzzle which preoccupies many recent observers: why the contrast between the relatively smooth, unproblematic, and generally sustained transition from ISI to EOI in Taiwan and South Korea, and the more partial and difficult policy reorientation in much of Latin America before the debt crisis?

Answering this question involves accounting for the differing capabilities of governments to respond to foreign exchange crises by effectively turning policy from ISI to EOI. I would like to suggest that there are four dimensions to the explanation: first, the differing alignments of interests in civil society (the relative power of rural vs. urban groups, the role of multinational corporations, etc.); second, the power of the state over these societal interests (institutional insulation, repressive capability, foreign support); third, the severity and duration of the crises; and finally, the objective difficulty of an effective policy reorientation. That is, 'successful' countries may have had more societal allies and fewer enemies of policy change than did other countries; they also may have had stronger states, may have experienced more severe crises that provided stronger motivations for change, or may have faced a much more manageable task than did others.[7]

In this section I will review and assess the literature on this problem while showing how explanations can be analysed into the four dimensions noted above (and as in Figure 1, below). I will then present evidence supporting the fourth dimension and explore at greater length the implications of this evidence.[8]

Civil Society

Let us begin with arguments based upon the character and relative weight of interests in civil society. A recent study by Jeffrey Sachs [*1989*] makes such an argument. According to him, a crucial variable is the breadth of property distribution in the rural export sector. Where industrial activities are heavily protected they have a vested interest in a relatively appreciated exchange rate, above all on their imported inputs (capital and intermediate goods). What keeps them from getting their way for very long, in East Asia for example, is broad land distribution in tradeable-good agriculture that creates a large bloc in opposition to an appreciated currency. In Latin America, exchange rate depreciation is unpopular because it transfers income from workers and capitalists to a small, politically regressive class of landholders or export proprietors. Hence, by this argument, ISI and overvalued exchange rates were gone from South Korea and Taiwan by the mid-1960s, in favour of outward-oriented industrialisation, while overvalued rates hung on in Latin America.

Lin [*1988; 1989*] also located the main roots of policy divergence in civil society. His main argument rested upon differences in natural endowments and especially, population pressures. East Asian countries, smaller and more crowded, had less potential for primary exports and a greater need to develop labour-intensive industrial exports. As does Sachs, Lin noted that governments encountered little opposition from landed oligarchies (because of prior land reform) or from labour (Lin mentioned Confucianism as important here). This meant that export-oriented policies were easier to implement [*1988: S160; 1989: 146*]. Elsewhere, he added that hyperinflation in the later 1940s and early 1950s led to a broader acceptance of deflationary stabilisation programmes when they were undertaken later on [*1989: 144–5*].

While Lin's natural endowment thesis is hard to assess, the Sachs argument does catch an important aspect of the South Korean case. The 1960 student revolution fought expressly against the corrupt government–business ties that characterised ISI under Syngman Rhee. The new urban industrial economy became the focus of dissent not only for students but also for the peasantry. The participants in the 1961 coup and subsequent governments, who considered themselves heirs to the 1960 movement, were overwhelmingly of rural origin. They were 'populist' in one sense – they sought to redistribute wealth to farmers. In 1963, when Park Chung Hee sought an electoral mandate, one of his key slogans was 'Agriculture First' [*Cole and Lyman, 1971: 37–9, 95*].

Latin American policy experiences from the late 1950s to the debt crisis also provide some confirmation of the Sachs thesis. In Colombia, with a relatively broadly-held rural export sector, a powerful coffee interest organisation (FEDECAFE), and two major parties having strong rural organisations, policy has shown more attention to rural exporters. Lleras Restrepo's comprehensive 1967 foreign exchange reform did not have the same retrograde political significance as a similarly pro-export policy would have had elswhere. There were many rural producers that stood to benefit to be sure, in a sector characterised by grossly inequitable land distribution because they were export producers also [*Mahon, 1989: Ch. 3*]. In contrast, despite the spur of chronic exchange problems, in Brazil and Chile pro-export exchange reforms (1959 and 1961; 1965) failed to persist under elected governments. In neither case was the export sector as broadly owned as in Colombia. In Brazil, low commodity prices and protests at the inflationary results of devaluation led to back sliding under Goulart. In Chile, the Christian Democrats returned to fixed exchange rates under electoral pressure in 1970 [*Fishlow, 1976: 31–2*; *Skidmore, 1967: 195–7, 239–43*; *Behrman, 1976: 76*]. Seemingly, when the immediate beneficiaries were a small oligarchy or big foreign firms, pro-export exchange policies were hard to sustain under elected leaders.

State Autonomy

In his multifaceted comparison of economic development in East Asia and Latin America, Evans [*1987*] argues the importance of state power to successful policy reorientation. He notes that aid and trade links did not translate into greater foreign capitalist leverage over Taiwan and Korean economies, as they often did in Latin America. This was due to the fact that the state in East Asia was powerful and had consolidated its dominance over the (former) landed elites prior to the shift to EOI and the opening to direct foreign investment by multinational corporations (MNCs). State power was enhanced by the strong administration and industrial assets left behind by Japanese colonial rule; by close external threats to political survival; and in Taiwan, by the cohesive nature of the Kuomintang ruling elite that arrived fully formed from the mainland.

This power was most important in dealings with MNCs and especially with ex-landlords. It showed itself in land reform and rural development policies, which tended to give urban labour greater market power and led to a trend of rising real wages, which reduced overall inequality in Taiwan [*219–20*].

Others have also pointed to an inter-regional contrast in the relative

FIGURE 1

WHAT EXPLAINS EAST ASIA'S SUCCESSFUL TRANSITION TO EXPORT-ORIENTED INDUSTRIALISATION, AND LATIN AMERICA'S FAILURE?

Explanatory Dimension	Authors and Hypotheses
1. Civil Society (national)	Sachs [*1989*]: unequal income distribution in Latin America, oligarchic rural sector, led to dominance of urban consumption interests over export interests, thus overvalued currency; East Asia differed because of past land reforms, big market-oriented peasantries. Lin [*1988; 1989*]: Asian populations pressure created greater need for labour-intensive industry; memory of hyperinflation of late 1940s and early 1950s created support for stabilisation policies in East Asia
(MNCs)	As noted by Evans [*1987*], multinational corporations (MNCs) were almost absent from East Asia until after EOI began, while they were dominant in Latin America; Could MNC strategy have led them to oppose EOI in Latin America?
2. State Autonomy *vis-à-vis* Societal Interests	Evans [*1987*], Haggard and Cheng [*1987*]: Helped by the USA, East Asian states defeated landlords, dominated domestic capital; external threat also fortified state. Hirschman [*1986*], Fishlow [*1987*]: Weakness of Latin American states led to overvaluation as a politically possible tax on export elites
3. Severity of Balance of Payments Crisis	Haggard and Cheng [*1987*]: East Asian transitions from import-substituting industrialisation to EOI were 'forced by development crises' which centered on the balance of payments, especially severe becasue the USA was seeking to reduce aid commitments, leaving Taiwan and South Korea 'the task of earning foreign exchange' Gereffi [*1987*]: Latin American crises came and went with oscillation of terms of trade, thus providing a lesser impetus to policy reform.
4. Income/Wage Cost of Shift To EOI	Diamand [*1973; 1986*], Keesing [*1981*], Gereffi [*1987*]: in Latin America, highly productive primary export sectors made manufactured exports uncompetitive internationally, even at 'equilibrium' exchange rates; this implied a larger sacrifice for the pursuit of low-wage EOI.

power of states over civil society. Like Evans, Haggard and Cheng [*1987*] point to states insulated from domestic societal interests (though not from the US), in which technocrats had a relatively broad power to impose the kind of policy reforms that were often desired but proved difficult in Latin America: land reform, restrictions on MNC investments, or large real depreciations that cut real wages in the short run. US security concerns greatly enhanced state autonomy from domestic political pressures. US pressure played a key role in pushing EOI policies over domestic business objections in Taiwan in April 1958, and in implementing stabilisation policies in Korea in 1963 [*1987: 113–14, 111*]. In a different and indirect way, Hirschman [*1968*] and Fishlow [*1987*] argue for the importance of state autonomy. In response to Sachs, Fishlow observes that it was not the weakness but the relative power of Latin American rural elites which forced states to turn to expedients like overvalued exchange rates to tax the export sector in favour of industry.

There can be little doubt that the state was stronger in Taiwan and South Korea, for several historical reasons. Two of these, Japanese occupation and post-Second World War pressure from the US, affected both countries. The Japanese occupation permanently weakened the former landed nobility in Korea, leaving a disorganised and discredited group of former clerks and lower aristocrats in possession of the land in 1945. This permitted the land reform of 1948–50 to proceed without strong opposition [*Cole and Lyman, 1971: 14–17*]. The large and war-disciplined South Korean army which took over the government in 1961 dedicated economic policy to defence against the North, and this entailed effective action to make up for the loss in US aid. In Taiwan, perhaps the most important feature was that the Kuomintang regime was virtually one of occupation, with few links to traditional elites on the island it ruled after 1949. Moreover, the leadership was convinced that its failure to achieve land reform was a key cause of its loss on the mainland, and was determined not to repeat the mistake on Taiwan [*Jacoby, 1966: 136*].

The Hirschman/Fishlow argument, which posits overvalued exchange rates as a kind of tax on a powerful export sector, seems to explain more about the early 1950s and about countries dominated by foreign export producers than it does about the policy battles later on. Even for countries like Chile before the nationalisation of copper, taxing the foreign companies was not the whole story behind overvaluation. There as elsewhere, it held other attractions for politicians apart from its convenience as a tax. What if a steep real depreciation had been tried in tandem with a land tax in Brazil or Argentina? One might suspect that the executive would have come under great pressure from landowners *and* labour unions.

The significance of foreign prodding may be overstated. It is well documented that US officials dictated the substance of policy reform to the Kuomintang in Taiwan and to the Korean military leaders [*Jacoby, 1966: 134–5; Gold, 1986: 77; Cumings, 1987, 70*]. Yet international advisers have made similar strong recommendations in Latin America and many of the reform efforts failed in the face of strong opposition. The relative ease with which foreign advice was translated into effective policy in Korea and Taiwan should not make us take state power and societal compliance for granted: Latin America reminds us why we cannot do so. Another difference in foreign influence lay in the magnitude, relative to total import capacity, of the sums at stake. In South Korea and Taiwan they were much larger than those involved in the typical Latin American negotiation with the IMF. This ties in with explanations based on the degree of foreign sector crisis.

Severity of Balance-of-Payments Crises

One may argue that foreign exchange crises give policy reform a degree of urgency proportional to their magnitude, much as Diaz Alejandro observed about Latin American policy innovation in the 1930s [*1984: 22*]. This is the third dimension mentioned above. Haggard and Cheng note that the transition from ISI to EOI was 'forced by development crises' in South Korea and Taiwan [*1987: 86–7*]. Traditional export markets had been lost and foreign investment was scarce, which led to a dependence on US aid that was greater than any external dependence felt by Latin America. In the late 1950s the US sought to cut its long-term aid commitments to the region. Given this, 'both countries faced the task of earning foreign exchange' [*1987: 90*]. Gereffi [*1987*]. has noted that policy changes brought on by cyclical deterioration in the terms of trade are 'vulnerable to backsliding' when the situation improves [*1987: 29*]. According to this argument, recurrent but shorter Latin American exchange crises would have been less effective in provoking large and sustained reorientation of policy.

In South Korea and Taiwan extreme dependence on US aid for imports created a certain amount of resentment; but this was a weaker motivation to reform policy than the very likely prospect, by 1959 or 1960, that the US would soon phase out its aid altogether. This was a dire situation, given these countries' extent of aid dependence, compared to which Latin America's cyclical trends in the terms of trade were a weak and inconstant motivation for policy change. Gereffi's point may be further supported by this pattern in Latin America: after the overproduction and sustained price collapse in the coffee market in the early 1960s, the big coffee-exporting countries (Brazil and Colombia) distinguished themselves by their sustained adoption of policies aimed at export diversification.

Cost of the Shift to EOI

The fourth explanatory dimension relates to the objective size of the task implied by a reorientation of policy from ISI to EOI. Arguments of this type point to the factor cost differentials between regions, as noted by Keesing [*1981*] and treated at some length by Gereffi [*1987*].[9] An early formulation is due to Marcelo Diamand [*1973; 1986*]. According to him, most Latin American countries have an 'unbalanced productive structure,' one with a substantial productivity differential between the primary-product export sector and the manufacturing sector. Because of abundant primary exports, the equilibrium exchange rate is a relatively appreciated one. At this exchange rate the country's manufactures are relatively uncompetitive internationally and import-competing activities have to be protected in other ways. Pro-EOI reforms thus bear a large short- to medium-term cost in domestic income and wages, from the huge real devaluation that is required in order to make manufactured exports competitive and protection unnecessary. It also means that the political difficulty in reorienting policy toward low-wage manufactured exports will be greater as a country's primary exports are relatively more productive.

The fourth dimension is not wholly distinct from the third one, since levels are ultimately tied to trends. Still, the 'unbalanced productive structure' argument helps us understand a criticism that could be levelled at the Sachs hypothesis: whatever the relative power of rural and urban sectors, moving from ISI to EOI will be politically easier where its objective costs are lower. Where the productivity of the export sector is low, the country's manufactures might be competitive internationally even at an exchange rate typical of ISI. In this case, the extent of real currency depreciation and the sacrifices involved in embracing an entry-level EOI model (in terms of real wage losses and import cost increases) would be much smaller.

Of course, that East Asian economies are resource-poor has been widely noted. One expert concluded that 'as compared with the other LDCs, the common denominator of the East Asian NICs has been their relative shortage of natural resources' [*Ranis, 1988: 2*]. But few have argued that there is an advantage in resource poverty: despite the correlation he observed, the same expert added that resource-rich LDC's could 'take heart from the fact that their initial conditions are more favourable rather than less' [*1988: 23*].

The Diamand argument implies that resource poverty will be advantageous to manufactured exports. He apparently assumes nearly equivalent productivities of industrial processes across middle-income developing countries, regardless of how long or to what level of income ISI has proceeded. This may be defensible for the historical situation that interests us: first, for comparisons of low-technology manufacturing processes, given similar benefits from domestic learning; or especially, to capture the decision parameters of multinational corporations contemplating the use of standardised plant technology for export production.

Evidence on the Wage Cost of the Shift to EOI

For the sake of a more detailed comparison, let us follow Diamand in a Heckscher-Ohlin assumption of equal productivities across countries in Latin America and East Asia in the late 1950s and early 1960s.[10] Thus export competitiveness may be approximated by real wage levels.

This assumption permits the comparison which appears in the following table (Figure 2) of current-dollar wage rates for ten countries, including the USA and Japan. For those countries with multiple exchange rates or official rates that were significantly supported by controls, wages are converted to dollars at a midyear parallel market rate. A focus on the parallel market lets us look past artificially appreciated official rates and see what Diamand considered to be the effect of the productive structure on 'equilibrium' currency values.

Venezuela is clearly our most egregious example of what Diamand called an 'unbalanced productive structure'. Venezuela's postwar model for rapid growth depended on expanding oil revenues. The sacrifices involved in making Venezuelan manufactured exports competitive in world markets, through a unified exchange rate alone, would have been dramatic. In 1965 Venezuelan dollar wages would have had to fall to about one-eighth their existing level in order to compete with Taiwan's, or to about one-twelfth to match Korea's. In 1970, Venezuelan wages were still higher than Japan's in dollar terms (Figure 2).

The situation was less dramatic but similar elsewhere in Latin America. Even measured by parallel market rates – those which often served as the target when the IMF recommended 'realistic' currency values – Latin America appeared a high-wage part of the world compared to Taiwan and South Korea. Latin American wages were closely comparable with those of Japan for much of this period. Where Latin American parallel-dollar wages dipped most steeply, this often had much to do with a black market made jittery by political events or economic news (Colombia 1958–59, Chile 1964 or 1970).

We can create a simple illustrative model of the choice that might have faced Latin American policy-makers. If they sought to export manufactures in competition with Taiwan and South Korea – and not with Japan – they would have had to devalue the currency mercilessly, far in excess of what the IMF typically recommended. They might have asked: how quickly can I expect real wages (in current parallel dollars) to recover fully from this devaluation? Taking 1962 wage figures from

FIGURE 2

HOURLY WAGE RATES IN MANUFACTURING, ALL INDUSTRIES, 1955–70 (current US dollars)

Country	1955	1958	1959	1960	1961	1962	1963	1964	1965	1970
Argentina	.20	.32	.25	.36	.32	.27	.30	.33	.25	.41
Brazil	.19	.20	.20			.19	.21	.24	.26	.36
Chile				.26	.30	.21	.16	.16	.20	.23
Colombia	.17	.14	.12	.23	.22	.23	.29	.33	.19	.27
Mexico	.22	.28	.30	.34	.36	.38	.45	.50	.54	.70
Venezuela								.82	.87	1.07
S.Korea	.08	.09	.10	.08	.09	.10	.07	.06	.07	.19
Taiwan	.06	.07	.06	.08	.10	.10	.11	.11	.11	.19
Japan	.21	.24	.25	.28	.31	.34	.38	.44	.49	1.06
U.S.A.	1.86			2.26					2.61	3.36
	1955	1958	1959	1960	1961	1962	1963	1964	1965	1970

Sources: International Monetary Fund, *International Financial Statistics*, various issues; International Labour Office, *Yearbook of Labour Statistics* (Geneva), various issues; *Pick's Currency Yearbook*, various issues.

Notes: *Exchange rates* used to compute dollar wages as follows: rates for Argentina, Brazil, Chile, and Colombia are from *Pick's* for all years. End of June figure used unless it was out of trend, then nearest in-trend month used. Japan, South Korea, and Taiwan are from *Pick's* for 1955 through 1965. All other years and countries are period average official rates from IMF. *Nominal wages*: hourly wages used, except Chile, Mexico, Venezuela, Japan, South Korea, and pre-1961 Argentina and Brazil, were computed from ILO monthly wage; ILO monthly hours of work used as divisor unless lacking (Argentina, Brazil, Chile, Venezuela all years, South Korea before 1963), where it is assumed 48 hrs/wk for 1955, 47 hrs/wk from 1958 to 1965, and 46 hrs/wk for 1970. Taiwan computed from ILO weekly earnings and weekly hours of work. *Important series changes*: 1960 to 1961 Argentina changes from all manufacturing wages to minimum wages for unskilled workers; 1962 to 1963 South Korea changes from (assumed) 47 hrs/wk to 54.4 hrs/wk (reported to the ILO).

Figure 2 – the competitive wage would be $0.10/hour – and generously assuming an annual dollar wage regain of 15 per cent,[11] the results would be as follows (1962 wages in parentheses):

Argentina (0.271), 63 per cent devaluation, recovered in 7 years;
Brazil (0.186), 46 per cent devaluation, recovered in 4.5 years;
Chile (0.211), 53 per cent devaluation, recovered in 5.3 years;
Colombia (0.234), 57 per cent devaluation, recovered in 6 years;
Mexico (0.384), 74 per cent devaluation, recovered in 9.5 years.

Notice that for Argentina and Brazil, 1962 shows parallel-dollar wages well below their average trend, and that the competitive wage is based partly upon Korea before its 95 per cent devaluation of 1964.

To complete the scenario, one would have to add the doubt in the decision-maker's mind about the near-term viability of exporting manufactures (probably to the USA and Europe), relative to the prospects for an upturn in primary exports. One would also have to note that a return to previous dollar wage rates would come much sooner than would a recovery of the total dollar buying power lost in the interval, sooner still than the recovery of buying power measured at official dollar rates in countries where these were supported by controls. Then, we would have to assess the likelihood that the politician or someone with whom he identified would still be around to reap the eventual political benefits of success, however defined. Considering all these factors, it would seem that this distant, uncertain future attainment of economic 'success' would be very heavily discounted indeed. Moreover, we have not even considered whether the IMF would have allowed this kind of competitive devaluation.

This discussion may also shed light on the behaviour of multinational corporations. Did the vastly different profile of MNC investment in the two regions, much more prominent in Latin America than in Taiwan and South Korea, affect the likelihood of successful policy reform? As Evans [*1987*] notes, MNC investment in East Asia was practically non-existent until after economic policy had been reoriented toward exports; but it was present from an early date in Latin America [*1987: 206–9*]. Would an established MNC have sought to block host country initiatives to raise manufactured exports because these conflicted with global corporate strategy?

From the data in Figure 2 one could argue that this strategy would have been shaped by relative costs and by timing. Once MNCs had made a commitment to exporting worldwide from one low-wage area, their enthusiasm for exporting from other, higher-wage countries would have lessened. Better, in this case, to continue selling in the protected market of countries whose domestic buying power would surely suffer from drastic policy reform. This analysis offers one reason why MNCs in manufacturing industry might have been, at best, indifferent to radical pro-export policy reforms in higher-wage developing countries.

DEPENDENCY AND THE 'UNBALANCED PRODUCTIVE STRUCTURE'

Central to most accounts of twentieth-century Latin American political and economic development is an appreciation of the difficulty involved in breaking with an economic model of primary-product export that favoured a traditional, chiefly land-based oligarchy and its foreign allies. Industrialisation was delayed and difficult to achieve politically because the groups that commanded the majority of the productive base, the consumption share, and the political apparatus were positively against it. The Depression served as a catalyst for change because to varying degrees it weakened these established forces, often forcing them to rely on the state to support their income, while creating the conditions for industrial growth. But even after some amount of import substitution had been spurred on by the currency depreciations of the 1930s or by the trade disruption of the Second World War, the traditional oligarchy was still strong, especially if allied with the military in an anti-democratic conspiracy.

In short, it appeared that the crucial barrier to continued industrial development presented by the primary export sector (whether foreign or domestically controlled) was its political resistance. From this perspective, many of the roots of dependency could be traced to the persistence of an export sector which reflected the nineteenth-century conditions of its origin and often fought to re-establish them.

If the Diamand hypothesis of the 'unbalanced productive structure' has merit, it shows another side of Latin American dependency under ISI. A thoroughgoing insertion of a country into the world market on the basis of its primary exports (Argentina is the archetype) would have discouraged industrial exports for other reasons. The most fundamental would have been the effect of high primary-export productivity on the exchange rate.[12]

This conclusion puts the postwar history of Latin American development in an interesting light. The catastrophe of the 1930s pushed the major countries of Latin America to undertake an import substitution process that was driven mainly by real depreciations that made all imports expensive. Postwar ISI differed. It would hew more closely to an easier but less sustainable path of making selected imports cheap to selected buyers, while exploiting the favourable trends in Latin American terms of trade in the decade after 1945.

The new postwar policies responded more to an economically stronger and ideologically more assertive industrial bourgeoisie, and less to the interests of the traditional export sector. While the social base of the top industrialists was often not very distinct from that of the traditional rural elites (especially in the smaller countries), the economic base had changed, with commerce and primary commodities weakened and industry strengthened by a decade and a half of reduced or interrupted trade. Still, factory owners were not the only supporters of the new set of policies. The pro-ISI enthusiasm was shared by most sectors of the military, labour, and many technocrats.

Reasons for avoiding devaluation could be traced to both new and old elements of this political economy. The most important foes of devaluation were urban industrial capitalists, who tended to be favoured by the exchange control systems erected in lieu of devaluation, and urban workers, who would lose from any acceleration of inflation not compensated immediately by equivalent nominal wage gains. Organised labour was especially prominent in postponing devaluation. Policy-makers also found good 'technical' reasons for resisting devaluation – the crucial one being an 'elasticity pessimism' about the probable response in supply and (if the country was a dominant world producer) international price of the country's key commodity to the move [*Diaz Alejandro, 1965a: Ch. 1*].[13] Meanwhile, clamouring for devaluation and trade liberalisation were the traditional export sectors and international financial interests. All in all, many found it easy to see which side of the issue was the popular, 'national', and reasonable one.

These trends led to the familiar policy deadlock. A period of recurrent exchange crises accompanied industrial growth. By the time the crises put policy reform on the agenda, the interests holding fast to ISI were even stronger than they had been in 1945.

Many policy-makers understood that the problem lay in the export sector. Accepting that the country could not expect permanently rising export revenue from primary products, it was clear that other (perhaps more income-elastic) exports had to be substituted. But the high productivity of the primary sector made this difficult. Beginning in the 1960s, one had to compete in the new sectors with exporters of similar productivity, whose exchange rates were not buoyed up by the material legacy of a 'successful' primary-export stage.

More: in Taiwan and Korea the material legacy of primary-export development was practically insignificant. Even within East Asia, Taiwan and South Korea are distinguished by the disastrous declines of their primary export sectors after 1945. The difference between Latin America and these two countries was especially striking in the first postwar decade. In 1954 Latin America was just coming off a fairly sustained rise in its terms of trade. The coffee boom was still on; the metals bonanzas had ended with the Korean War a year earlier. Still, relative prices were ahead of 1945 (and 1939). In contrast, South Korea's export sector was in shambles. Exports in 1956 had fallen to less than half of their real value of 1950 [*Westphal and Kim, 1982: 212*]. In Taiwan, the loss of the Japanese market for tropical foodstuff exports compounded the countrywide problems of hyperinflation and rapid real depreciation, attendant upon civil war in 1945–49. One result of these disasters was the abject dependence of both East Asian countries on US aid to finance imports. Another was a depreciated level of parallel exchange rates, despite the aid inflow.

The poverty of primary exports in the two Asian countries had other social consequences, too. Because this resource poverty permitted an ISI process only at a low level of income, the pie was too small for it to be used, Argentina-style, as a basis for a strong political alliance of newly-mobilised labour and domestically-oriented business. It was less tempting to continue with it, and its limitations meant that the interests defending it would be relatively weak.

For Latin American politicians to have duplicated the disaster that befell the primary export sectors of Taiwan and South Korea, they would have had to re-create the Depression experience through state policy. This, of course, was inconceivable to them. Yet the problem illustrates a bit of the complexity in the dependent relations of a primary-export country. It shows another side to a phenomenon which theorists pose in abstract terms, when they speak of the 'substantial contradictions to be overcome if a country enmeshed in the capitalist world system was to change its position in the international division of labour' [*Evans, 1987: 204*].

Ironically, under the typical structure of Latin American ISI a 'contradiction' was felt most directly by the politicians who were most sensitive to the interests of urban wage-earners. 'Populists' were the ones most loath to contemplate any drastic export reorientations – including programmes which would have started by redistributing rural property – because of the benefits to urban consumers that could be derived from a more aggressive exploitation of the existing rural export structure (or its accumulated surpluses). The experience of post-1959 Cuba may indicate that it is hard for leaders of any persuasion to refuse to support consumption through primary-product exports, when they have inherited the opportunity to do so.

Let me repeat that I am not trying to argue that only one feature distinguishes Taiwan and South Korea from Latin America. I have simply tried to provide one more reason why urban consumption interests were more powerful in Latin America. It was not just a matter of relative state power, societal interests, exchange crises, or international forces. Relative to Latin America, in East Asia the transition to EOI bore a much smaller income cost. This is a contrast that is often hidden when the successes of Taiwan and South Korea are compared to the less adept or permanent policy changes in Latin America.

Nor is this a policy brief in favour of low wages. The idea that all middle-income developing countries ought to be subjected to competition on the basis of wage rates would be immoral and absurd; it is nearly as contradictory as supposing that they could all become major exporters of simple manufactures at the same time. My purpose has been to counteract the somewhat voluntaristic tone that sometimes inhabits these inter-regional comparisons. The East Asian achievement, that rare example of a region rising quickly in the hierarchy of the capitalist world, was facilitated by other rare events, usually beyond the ability of politicians to duplicate.

CAN LATIN AMERICA NOW IMITATE EAST ASIAN SUCCESS?

The previous discussion treats explanations for Latin America's relative failure to adopt a development strategy oriented to the export of manufactures in the postwar period. It has given particular emphasis to the differences in primary export productivity which affected real wage levels under the ISI regime, and thus to the degree of sacrifice necessary to achieve export competitiveness. Latin America was 'disadvantaged' in this regard, for having been an important world producer of primary goods for centuries, and for not having suffered the kind of catastrophe which afflicted Taiwan or especially Korea in the first postwar decade.

But with the debt crisis, this catastrophe has come. Real wages have fallen steeply all across the region. Large real devaluations and, in Argentina, Brazil, and Peru, hyperinflation have been part of a trend pushing real wages down again. Now Latin American countries are among the world's low-wage industrial economies, as they struggle to boost exports and pay their debts. Does this mean that they will follow the East Asian example?

This is where the other elements of the Sachs argument may be instructive. According to him, Latin America also differs from East Asia in the *pressure* for 'populist' solutions, and this pressure is the result of unequal income distribution. The extreme poverty in Taiwan and Korea in the 1950s was broadly shared: more extreme in Korea, it was also shared more widely. Given the previous land reforms and the small (initial) economic size of rural export producers, policies set to benefit exports did not have the pro-oligarchic significance they had in Latin America.

The same events responsible for making Latin America suddenly competitive in manufactured exports may have weakened the political basis of the low-wage model. Where capital flight played a prominent role in bringing on the debt crisis (Argentina, Mexico, Venezuela), the political problem is obvious: poor citizens forced to sacrifice so that the country can pay a debt that financed the purchase of foreign assets by the rich. But even if the foreign debts were forgiven tomorrow, there would be a problem. Among the prime beneficiaries from steep currency depreciation have been the holders of undepreciated foreign assets. Capital flight has favoured them over those without this kind of wealth. Moreover, in all debt-strapped countries the shortage of capital has driven up real interest rates on domestic securities, enriching holders of government paper. In short, it is likely that the debt crisis has accentuated the regressive pattern of income distribution in Latin America in the same measure as it has made the debtors into internationally competitive manufacturers. If so, this is not a very favourable climate for a sustained low-wage export drive.

NOTES

1. A short bibliography would include Evans [*1987*]; Fishlow [*1987*]; Gereffi [*1987*]; Gereffi and Wyman [*1989*]; Gereffi and Wyman [*1989*]; Gereffi and Wyman [forthcoming]; Lin [*1989*]; special issues of *Economic Development and Cultural Change*, Vol.36, April 1988, *World Development*, Vol.17, No.9, 1989, and *The Annals of the American Academy of Political and Social Science*, Vol.505, Sept. 1989.
2. Raymond Mikesell, in the US delegation at Bretton Woods, wrote in 1949 that the IMF allowed overvalued rates in many Latin American countries to persist because it 'evidently believed that stability of exchange rates was more significant than an appropriate rate pattern' [*1949: 397*].
3. Apart from imputing an influence to nationalist business, many analyses emphasise the roles of the Depression and the writings of ECLA economists on Latin American policy-makers. An exception to this line of argument is Maxfield and Nolt [*1990*], which traces the role of US government and business interests in promoting ISI.
4. In current dollar terms, Argentina did not surpass its export revenues of 1951 until 1963; Chile, favoured by the rise in copper prices in the 1960s, reached its 1955 level by 1963; Colombia's export earnings did not exceed their 1954 value until 1969; while worst of all, Brazil took until 1969 to better its export performance (even in current dollars) of 1951 [*IMF, International Financial Statistics, various issues*]. On the problematic trend of import elasticities, see the discussion and works cited below.

5. Although the argument has many elements familiar in this literature, several of these draw on observations made in Cooper [*1971*] and Hirschman [*1968*]. It is illustrated for Brazil in Arnold [*1972*].
6. Exchange policy reforms in the late 1950s and 1960s were more serious in proportion to the degree of crisis in the export sector, as Diaz-Alejandro [*1984*] observed about the 1930s. They were also more durable where the old export interests, despite the distress in the market for the traditional main commodity, were still powerful enough to provide significant political support for a sustained reorientation. For more detail on the determinants of exchange policy leading up to the capital flight of the early 1980s, see Mahon [*1989*].
7. In this scheme, international forces show up through their effects on the domestic political economy.
8. In this sense my purpose differs from that of Gereffi [*1987*] or Gereffi and Wyman [*1989*]. As reviews of the various approaches to the inter-regional comparison these articles are to be recommended.
9. See also Leff on the contrast between Japanese and Brazilian textile manufacturing in the early twentieth century [*1982, Vol. 1: 1984–6*].
10. I am aware of some of the problems of this assumption. I have not located good data on unit labour costs (wages deflated by productivity) for the period and countries in question. However, I have noticed that doubts about the assumption for this comparison tend to relate to the possibility of *higher* productivity in East Asia, leaving the argument of Figure 2 intact.
11. Dollar wages after n years given by $(0.10)\ (1.15)^n$.
12. Another might have been the contribution of still-powerful traditional elites to the failure to make ISI-bred firms internationally competitive at this relatively appreciated exchange rate.
13. Diaz-Alejandro noted that policymakers tended in their 'elasticity pessimism' to discount the creation of *new* export activities. This tendency may be attributable to pro-ISI ideology.

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