INTRODUCTION

This chapter examines why many Latin American countries whose economic development until the Second World War had been shaped overwhelmingly by agriculture and mining embarked on strategies that, instead, made industrialization a top priority. It looks at the main economic argument that justified this policy shift, called ‘structuralism’, and the profound implications this would have for the state and the character of politics in Latin America. The strategies proposed and adopted by economists to exploit a country’s resources are of great importance to the ways in which social and political systems evolve. They determine who will be the main winners in a process of economic development – and who will be the losers. In turn, they shape the nature of the state and the behaviour of the political actors who seek to influence its policymaking role. Until the 1930s the model of development in Latin America had been dominated by a small, landowning oligarchy controlling agricultural production on vast estates. This model of development found its main political reflection in systems that excluded all but the elite from policymaking and in extreme levels of inequality. However, ideas that came out of the Great Depression eventually led to a transformation in the structure of the region’s economies that placed a priority on industry. Industrialization nurtured a form of development that benefited urban social sectors and eroded the power of traditional landowners, but continued to exclude the peasants. It found new institutional expressions in
the emergence of unwieldy, centralizing states comprising large, bureaucratic ministries, and political expressions in the populism and corporatism that allowed elites dominating these states to maintain a core body of support to ensure stability (see Chapters 2, 6, 8, 13). However, like the models that had preceded it, rapid industrialization generated social and political strains and began to run out of steam. The exclusion of large numbers of people from the benefits it promised and from the coalitions by which it was maintained fuelled unrest. Millions of peasants abandoned the countryside and headed for the city, swelling urbanization. Radical economic perspectives based on the theme of ‘dependence’ gained force in the ideologically tense Cold War atmosphere. Political alternatives developed outside the formal institutions of politics and sought new sources of support in the countryside and among the urban poor. These stresses all contributed to authoritarian clampdowns by military regimes at a time when industrialization had begun to falter. Once again, this set back the achievement of democracy.

FROM EXPORT-LED GROWTH TO INDUSTRIALIZATION

Before the Great Depression many policymakers and economists in Latin America had believed that the region’s best prospects for growth could be found in exporting commodities that could be produced in abundance in their mainly agricultural and mining economies then sold to the growing industrial countries of Europe and to the US. This position was supported by the theory of comparative advantage in international trade, an influential doctrine that originated with the British economist David Ricardo (b.1772 – d.1823). The notion of comparative advantage suggests that a country will gain the greatest economic benefit in a trading relationship with other countries by concentrating its production on commodities that it can provide at a lower overall cost, either because these are found in relative abundance or they can be produced relatively easily within its territory. In turn, other countries in a trading relationship are themselves better off if they accept the cost advantage the first country may have in producing that commodity, and themselves concentrate on producing other commodities in which they have advantages. Comparative advantage is the main basis for most economists’ belief in free trade – international trade as free as possible from nationally imposed barriers such as tariffs and quotas on imports and exports. It is an important principle in economics because it implies an international division of labour in which some countries stick to producing agricultural or mineral commodities for sale to others that produce industrial goods. Comparative advantage and free trade are also important elements of the philosophy of economic liberalism, which places a premium on the benefits of free enterprise conducted within markets unimpeded by artificial barriers imposed by states.

In Argentina, Latin America’s most prosperous economy by the early twentieth century, such ideas appeared to make sense and the country’s role in the international
economy as a supplier of agricultural commodities and raw materials from mining (together known as ‘primary products’) seemed natural. These ideas suggested that Argentina was best served by concentrating on the production and sale of beef, which could be produced intensively and cheaply from huge herds of cattle grazing on the vast pampas plains, and exchanged in a free international market with the highest or most reliable bidder in return for imported manufactured products. After all, until the Depression such a model had delivered unprecedented rates of growth and even small socialist organizations did not question the bias in favour of export-led agricultural production. This economic model had nurtured the development of distinctive political systems based on the exclusion of the vast majority of people (see Box 15.1)

**BOX 15.1 SOCIETY**

Export-led growth and the politics of exclusion

The most important political and social characteristics of societies with export-led economies, such as those of Latin America, were inequality and exclusion. This is because the main beneficiary of export growth was a powerful oligarchy comprising large landowners and merchants who tried to maintain their control over politics in their own interests well into the 1920s. In Argentina, for example, ranchers and export merchants worked hard to exclude others from politics, and political institutions were designed and administered by these powerful groups to support the main objectives of an economic model that benefited them. The main losers from Latin America’s role in the international division of labour as a producer of agricultural goods and raw materials were poorly paid rural workers, many of whom began to head for the growing cities to find a better living, fuelling urbanization. At the same time, economic growth created new, mainly urban middle-class professionals, bureaucrats, shopkeepers and small businessmen (see Chapter 1). The spontaneous development of small industries and mines, and increases in immigration, led to the emergence of a small working class. Growing urban populations did not fit easily into the social hierarchy that had supported the development of large estates and ranches for export-led growth, and tended to be more politically volatile than rural populations. As a result, the model of export-led growth adopted across Latin America generated new class tensions and in some countries such as Mexico, the continuing exclusion of the middle classes and rural poor led to agitation and political conflict (see Box 1.5).

The pressures generated by export-led growth helped to undermine the control of the oligarchs across much of Latin America, and political systems were in transition from the 1920s as elements of the oligarchy saw the need to incorporate the middle classes and workers into the policymaking process. Middle-class politicians often assumed nationalist positions that attacked foreign interests while advocating greater state intervention in the economy to ensure a fairer distribution of resources. Although oligarchical governments began to adapt by advocating more nationalist policies that proposed protectionism – the introduction of restrictions such as tariffs or quotas on some imports in order to favour local producers – it was the Great Depression that provided the stimulus for influential new ideas that would transform the economies and politics of Latin America (see Chapter 2).
The Great Depression that followed the Wall Street crash of 1929 hit Latin America hard as demand for its products withered and its ability to pay for imports declined, causing recessions and fuelling the growth of radical ideas and political unrest. The Depression forced Latin American countries to reconsider their relationship with the international economic system, with some thinkers arguing that the region had been forced into a disadvantaged position in the global division of labour. In particular, policymakers became aware of the need to reduce their reliance on the export of commodities and the import of manufactured goods, and in the 1930s most countries in the region took the first steps towards nurturing their own industries through import-substitution industrialization (ISI, see Chapter 2). They began to restructure their economies by adopting protectionist policies in order to protect local industries from foreign competition, and this was made easier by the nationalist climate of the period that justified hostility to foreign economic activities. Some countries, such as Brazil, adopted policies that had, by the Second World War, allowed them to achieve substantial industrial growth. This early industrialization coincided with a growing interest in Keynesianism – the body of economic thought developed by the British economist John Maynard Keynes (b.1883–d.1946) that advocated a greater role for the state in economic development – and with the apparent successes of central planning in the Soviet Union. These ideas all contributed in the 1940s to the emergence of the new ‘structuralist’ perspective in Latin America advocating the need for countries to create industry in order to rely less on the production of primary products. Structuralist ideas also represented a rejection of influential perspectives that were developing in the industrialized world about how agrarian societies developed into modern industrial economies (see Box 15.2).

**BOX 15.2 THEORIES AND DEBATES**

**Modernization**

The Marshall Plan pursued by the US following the Second World War pumped large amounts of aid into the devastated countries of Europe, enabling them to rebuild and modernize their economies in just a few years. This experience had an important influence on perspectives in the industrialized world about development in mainly agrarian societies. In this period, economists often began with an assumption that the industrialized countries had also once been underdeveloped agrarian societies, and so development could be understood as a series of successive stages through which all countries pass (Todaro, 1994). These evolutionary assumptions are the basis of modernization theory, sometimes called linear-stage or stages-of-growth theory, and reflected the optimism and anti-communism of the postwar era. Modernization perspectives became influential in US universities and are associated with the work of the sociologist Talcott Parsons (b.1902–d.1979) and the economic historian Walt W.
Given Argentina’s position in the vanguard of export-led growth, it is not surprising that the most influential Latin American structuralist to emerge from the period of reassessment following the Great Depression was an Argentine, Raúl Prebisch (b.1901–d.1986). Prebisch was the first director of the United Nations’ Comisión Económica para América Latina (CEPAL, Economic Commission for Latin America, whose acronym in English was originally ECLA, later ECLAC to incorporate the Caribbean) which, from 1948, became the source of many structuralist ideas (see Box 15.3). The ideas developed by Prebisch derived from his understanding of how the Depression had affected his native Argentina during the 1930s. They were refined in the years after the Second World War and were reinforced by the work of another UN economist, the German Hans Singer (b.1910–d.2006). The central argument that these economists developed is, as a result, sometimes referred to as the Prebisch-Singer thesis about unequal exchange in world trade. It had two underlying themes:

---

**Box 15.2 continued**

Rostow (b.1916–d.2003) (see Box 4.2). They presented development as a move away from a traditional society shaped by communities to one based on individual values by imitating the developed world under the leadership of local entrepreneurial elites, passing through different stages en route to modernity (see Parsons, 1954; Rostow, 1962). All that was necessary to enable backward countries in regions such as Latin America to follow the same path as the developed world was the right mixture of investment, aid and savings. Perspectives originating in modernization theory have been highly influential in shaping how development is understood in Latin America and the attitudes of the industrialized world towards the region. Such attitudes have a benign view of industrial capitalism and see the problems of developing countries as internal to them and not shaped by external factors. They emphasize the importance of culture and values, especially those of the middle class, by explaining development in terms of the characteristics of the US and Europe and how the absence of similar values is an obstacle for regions such as Latin America (ibid.). Lastly, modernization perspectives assumed that the conditions (such as markets, transport facilities, educated workers and efficient administration) that had enabled rapid reconstruction of postwar Europe also existed in underdeveloped nations. There have been many criticisms of the modernization perspective, and these criticisms formed the core of alternative models of political economy such as structuralism. Modernization theory has been described as ‘ethnocentric’ because it understood development and prescribed a formula for it from the perspective of the industrialized West. It has been criticized for ignoring history and turning a blind eye both to the impact of colonialism in the developing world and the complex realities of Latin America, where power has often been concentrated in the hands of a small elite. Stages theories have also been criticized for failing to take into account the crucial role played by international factors in developing economies.
BOX 15.3 INSTITUTIONS

The Economic Commission for Latin America and the Caribbean

The Economic Commission for Latin America (ECLA) was established by the United Nations in 1948 to contribute to the economic development of the region, to coordinate actions towards that end, and to reinforce economic relationships between Latin American countries and other nations. Its scope was later broadened to include the countries of the Caribbean and it changed its name to ECLAC in 1984. ECLAC's theories and approaches have been recognized in many parts of the world. In its early years it developed its own method of analysis – 'historical structuralism' – which it has largely maintained to the present day. This approach focuses on the analysis of the ways in which Latin America's inherited institutional and production structure influence its economic dynamics. ECLAC does not recognize the existence of the uniform 'stages of development' foreseen by modernization theory, arguing that circumstances are different for 'latecomers to development'. Five phases have been identified in ECLAC's theoretical work:

- 1950s: industrialization through import substitution (ISI);
- 1960s: reforms to facilitate industrialization;
- 1970s: reorientation of development 'styles' towards greater social homogeneity and diversification as a means of promoting exports;
- 1980s: overcoming the external debt crisis through 'adjustment with growth';
- 1990s: changing production patterns with social equity.

Since the end of the 1990s ECLAC has sought to demonstrate how the conditions of Latin America and the Caribbean's integration in the global economy have a negative effect on the region and cause macroeconomic instability, low growth and adverse social effects. It has also warned about the impact of neoliberal reforms on the region's economies and has argued that there is a need to seek a more balanced form of globalization, in order to 'reform the reforms' (see Chapters 16, 17).


1 Centre-periphery Prebisch believed the world comprised a ‘centre’ of developed industrialized countries and a ‘periphery’ of those that only produced agricultural goods and raw materials. He argued that the centre and periphery are closely interlinked through trade and that, because of the higher value of industrial products manufactured in the centre in relation to the raw materials and agricultural goods produced in the periphery, peripheral countries were at a natural disadvantage in any trading relationship. Prebisch believed the prices of products made in the more technically advanced economies rose more quickly than those produced by backward economies, and pointed to Latin America’s deteriorating terms of trade – the import prices of what countries in the region bought remained the same.
or rose, while the prices of what they sold on the world market declined. In the long term this meant that Latin American economies would have to export more to buy the same quantity of manufactured imports. In this way, peripheral economies that persisted in exporting primary products would not benefit from free trade.

2 *Surplus labour* Prebisch also argued that the pattern of economic development in peripheral countries under these arrangements was far more likely to generate a surplus of labour comprising workers squeezed out of primary products sectors such as agriculture by the constant need to control production costs because of the declining terms of trade. Unlike developed countries, however, it is more difficult in the periphery to redeploy these displaced workers to dynamic sectors such as manufacturing, because these sectors are so small and do not grow rapidly. If workers displaced from primary sectors are not absorbed, this pushes down the incomes of other workers. Low incomes are an important characteristic of underdevelopment and, in this way, it was believed that unequal exchange *caused* underdevelopment.

Prebisch concluded that the only way for Latin American countries to escape their disadvantaged position and hence underdevelopment was to reform the *structure* of their economies by creating industries and so relying less on the production of primary products. His ideas were influential in multilateral bodies and regional trade groupings, and shaped economic policies across Latin America. After 1949, ECLA advocated rapid industrialization and was highly critical of the ways in which world trade operated, calling for international agreements to protect the prices of primary products in order to counter the impact of volatile terms of trade on developing economies. In Latin America the 1950s was a period of unprecedented state intervention in the economy – statism – to direct the process of industrialization. These ideas challenged the vision of development held by the industrialized countries (see Box 15.4).

**BOX 15.4 THEORIES AND DEBATES**

**A challenge to economic liberalism**

Structuralism posed a fundamental challenge to the orthodox positions adopted by economic liberals about the role of the state and market in the economy and about free trade. It was one of the first coherent expressions of what became known as ‘development economics’ that advocated state activism to tackle the problems faced by Third World countries, and it adopted a pessimistic view about the ability of the free market to eradicate poverty. It coincided with nationalist perspectives in Latin America that proposed the achievement of greater economic independence and the sovereign control of resources. Nonetheless, it was not fundamentally anti-capitalist and accepted
that a form of national capitalism in which the state played a significant guiding role was the best hope for Latin American development.

**State versus market**

Economic liberalism suggests that rational, self-interested actors competing freely in the marketplace will produce the greatest good. The structuralists, by contrast, believed that the economy was shaped by power and politics and that Latin American markets were controlled by elites in ways that did little to generate growth. A dominant underlying theme of structuralism, therefore, was the notion that underdeveloped economies were characterized by failures of the free market, and this implied that state intervention to correct these failures was essential for development (see Box 16.2).

The ECLA theorists believed the state should reform an economy’s structure to create the right conditions for industrial development; that the domestic market should be enlarged through agrarian reform (see Chapter 8); and that income should be redistributed in order to raise the purchasing power of the majority. The state-versus-market debate continues to be reflected in longstanding disagreements between economists advocating planned industrialization and those recommending that industrial growth in developing countries is best allowed to evolve spontaneously from the stimulus provided by free markets and trade. Advocates of planned industrialization point to the example of rapidly growing Asian economies such as Korea to suggest that state direction within a capitalist economy may be essential for creating highly competitive, world-beating and technologically advanced industries. Each approach has different implications for the exercise of politics, as the former implies forms of corporatism and limitations upon the democratic pluralism frequently, if questionably, attributed to the latter (see Box 2.2, Chapters 4, 8, 9).

**Free trade**

Classical economic liberalism argued that international trade free from impediments such as tariffs and quotas benefits all nations. Structuralists, by contrast, argued that trade relations between centre and periphery reinforced higher levels of development in the centre and so free trade could actually be harmful to less-developed nations. In this way, the structuralists highlighted for the first time the dangers of economic strategies that involved indiscriminate integration into the international market for countries that were in the early stages of development, and sought reform of the structure of the world economy through international agreements. Structuralists also argued that developing countries had to reduce their reliance on trade with the industrialized centre by increasing trade among themselves through regional integration initiatives. ECLA backed integration efforts during the 1950s and 1960s to allow ISI to be carried out at a broader level, such as the Latin American Free Trade Area (LAFTA), the Central American Common Market (CACM), the Andean Pact and the Caribbean Common Market (see Chapters 2, 10). A common market in Latin America might have provided the demand and competition that industrialization required, but these early efforts at economic integration failed over disagreements between national states about removing protection for their individual industries or because of political instability.
ECLA ideas were criticized by many economists in the industrial countries, who rejected the centre–periphery division and argued that global trade would, in fact, equalize incomes among nations in the long term (Love, 1995). Many economists have since argued that the evidence confirms the long-run deterioration of the real prices of raw materials since the last decades of the nineteenth century, tending to confirm Prebisch’s broad hypothesis (see Ocampo, 1995). However, explanations for the decline in terms of trade may be far more complex than Prebisch suggested, because the prices of some primary products such as oil have performed much better than others; the deterioration in the terms of trade has not been the same for different Latin American countries; in some countries, such as Bolivia, Colombia, Costa Rica and Venezuela, terms of trade have improved; and it is unclear what effect changing technology has had on raw material prices (ibid.). Until the 1980s, for example, it was not economically viable to extract oil from sandy, surface deposits found in large expanses in the northern hemisphere – today technological advances mean that it is, and this could eventually depress prices. Large ‘oil sands’ or ‘tar sands’ deposits are found in Venezuela, for example.

ISI based on protectionist policies became a cornerstone of development strategies in Latin America until the 1980s, although each country had a different experience of it and in some, such as Peru, it began much later than in others (see Chapter 2). Strategies often began with the establishment of sectors seen as essential for industrialization, such as iron and steel, engineering, transportation and communications. An important structuralist assumption was that the state was the only economic actor with the resources able to run heavy industrial sectors such as oil, petrochemicals and telecommunications, and so state-owned enterprises were formed throughout Latin America. Governments complemented these policies by taking measures in their overall administration of the national economy – that is, in their ‘macro-economic’ policies – that were biased towards helping the new industries. In the first stages of ISI, for example, imports were usually allowed to rise so that emergent industries would have ready access to the inputs necessary for growth. To ease this development, states tended to maintain overvalued exchange rates in order to make some imports cheaper to purchase. The state also created national development banks to target investments in the economy; gave subsidies and tax credits to domestic companies; raised industrial wages to encourage internal demand and create a market for new products; and even encouraged foreign investment in areas where there was a shortage of local capital.

As a result of ISI, most countries in Latin America achieved the capacity to produce basic goods, and a few successfully created heavy industries. The larger economies, in particular, were able to diversify their exports beyond a single traditional primary product and provided an important source of employment (Alexander, 1995). Manufacturing sectors grew in importance as a proportion of GDP, and one measure of this was the declining share of the labour force employed in agriculture between 1930 and 1980. In Mexico, for example, the share of the labour force
employed in agriculture fell from 63 per cent in 1940 to 37 per cent in 1980, and in Chile it declined from 41 per cent to 16 per cent (Cardoso and Helwege, 1992). Some countries were also able to establish the foundations of sophisticated and globally competitive modern industries. In Brazil, national production of all manufactured goods increased by 266 per cent from 1949 to 1964 (Alexander, 1995). Industrial products now make up a majority of Brazil’s exports and the country has become a global force in sectors such as vehicle manufacturing, shipping and even aerospace (see Box 15.5). Protectionist policies also helped to stimulate growth. Throughout the 1950s Latin American economies were growing faster than Western economies – with annual growth rates thereafter averaging about 5.5 per cent during the years 1950–80 – and between 1950 and 1970 Latin American GDP trebled.

However, by the end of the 1950s the early phase of ISI was already becoming ‘exhausted’ as Brazil, Chile, Mexico, Argentina, Venezuela, Colombia and Peru began to run out of import-substitution possibilities (Cardoso and Helwege, 1992). ISI is exhausted when an economy has installed all those kinds of industries that can produce products formerly imported; if growth is to continue, the challenge then becomes one of amplifying existing markets (Alexander, 1995). A new ‘post-import substitution strategy’ becomes necessary involving more sophisticated forms of production to develop new products for local consumption and for export, and this requires greater efficiency, new skills and new consumption habits. By the 1960s Prebisch himself was recommending a post-ISI strategy to remove protection from some industries and develop non-traditional exports. Other supporters of ISI, such as Brazil’s president Juscelino Kubitschek (1956–61), proposed a post-ISI strategy of agricultural development and the stimulation of new industrial exports. In Chile, the Christian Democrat president Eduardo Frei (1964–70) also recognized the need to move on from ISI and promoted agrarian reform and the reorientation of industry towards exports. Frei’s agrarian reforms were also recognition of the strains that had been generated by the exclusion of the peasantry from development at a time of heightened political mobilization following the Cuban Revolution (see Box 2.3, Chapter 13).

Domestic industry was responsible for much of the industrial growth in Latin America until the 1950s, but as a shift towards more complex industrial products became necessary, its expansion was hampered by a lack of access to investment for large-scale projects and to the technology required for more sophisticated forms of manufacturing. ISI in Latin America had coincided in the postwar period with global expansion by many large US and later European corporations, and by the late 1950s many Latin American governments desperate for industrial investment began welcoming multinational corporations into their countries. They increasingly saw them as allies in the later phase of ISI and wanted them to produce goods for higher-income urban consumers as well as for export. Multinational companies brought capital, technology, skills and jobs, and helped to change consumption patterns, fitting the main objectives of the industrialization strategies adopted in the region. Governments could attract them with tariff protection warding off imports that provided them with a
captive market, subsidies on equipment, and overvalued exchange rates that made importing that equipment cheaper.

The coups of the 1960s and 1970s that inaugurated a period of military authoritarianism have been associated by some scholars with the exhaustion of the first phase of ISI (see Box 2.5). This position linked authoritarianism with the broad recognition

---

**BOX 15.5  CASE STUDY**

**Embraer – a Brazilian success story**

The remarkable growth of the Brazilian aeroplane manufacturer Empresa Brasileira de Aeronáutica (Embraer) is emblematic of the many successes within Latin America’s industrialization strategy. Founded in 1969 by the Brazilian government under a military officer as its chairman, Embraer delivered its first plane to the Brazilian Air Force in 1973. Embraer was present for the first time at the Paris International Airshow in 1977 and opened an office in the US in 1980. By the early 1980s it was producing several models, including the Tucano military training aircraft, AMX advanced pilot trainers, and small Brasilia passenger jets, and by 1986 it was investing hundreds of millions of dollars in developing new planes. The company began developing the ERJ 145, its first regional jet, in 1989 and by the late 1980s it was producing a range of sophisticated military planes that included remote-sensing aircraft and maritime patrol and anti-submarine warfare aircraft.

Amid a global downturn in the air transport industry in 1990, and facing bankruptcy, the privatization of Embraer began in 1991 and this was completed in 1994 with key shareholders including Brazilian investment and pension funds. Embraer began producing larger passenger aircraft and landed key contracts in the US, and in 1998 reported its first profit ($109 million) since becoming private. In 1999 Embraer signed a $4.9 billion contract for regional jetliners with the Swiss carrier Crossair, its largest to date. It began to develop a family of aircraft that included 98- and 108-passenger models through an Embraer-led multinational partnership among 16 aerospace companies. In 1999 a French aerospace consortium acquired 20 per cent of the Brazilian firm, and in 2000 Embraer was launched on the New York Stock Exchange. The company entered the market for business jets, targeted a rapidly growing China, and unveiled a new generation of larger planes for up to 110 passengers. Between 2001 and 2003, Embraer’s sales to military and corporate customers more than doubled, although sales to commercial customers declined, in part because of the impact of the 9/11 terrorist attacks in the US on the air transport industry. In June 2003, Embraer won a $3 billion order from the US budget carrier JetBlue to produce 100 E190 jets, and JetBlue also took out an option to buy a further 100 E190s, which could increase the eventual value of the deal to $6 billion. Embraer is now the world’s fourth largest aircraft manufacturer behind Airbus, Boeing, and Bombardier. It produces passenger jets and turboprops, and its military aircraft are used by more than 20 air forces across the world. It is Brazil’s second biggest exporter, with a total workforce of more than 12,000, and has announced plans to expand production within Europe.

Sources: www.embraer.com; Hoover’s (2003).
among economic policymakers in some countries that it had become necessary to
shift towards a more outward-looking economic policy combined with changes in
the nature of local consumption patterns. Subsequently, the authoritarian regimes
of Brazil, Chile, Uruguay and Argentina all made efforts to liberalize trade and
promote non-traditional exports, although there was considerable variation in the
policies they adopted and the extent to which they did, in fact, restructure their
economies (see Chapter 2). By the late 1970s ISI had come under sustained assault
by neoliberals restating the ideas of economic liberalism who argued that it had wasted
resources and created inefficient industries that had drained the economy (see
Chapter 16). In the 1980s and 1990s most Latin American leaders abandoned
ISI and undertook radical trade reforms.

The industrialization policies advocated by the structuralists had an important
impact on the development of political systems in Latin America. By the 1970s
ISI had benefited only limited sectors of the population, heightened inequalities,
generated inflation, weakened the priority placed upon economic efficiency, and
reinforced a tendency to adopt corporatist solutions to meeting political demands.

**Growth of the state**
Industrialization policies implied the need for greater government intervention in
the economy than in the past, and the state as a set of social institutions grew much
larger in Latin America after the 1950s (see Box 2.1). Ministries grew in size and new
government agencies were created to promote manufacturing as the public sector
expanded. In many countries the state nationalized key areas of production con-
sidered to be strategic, such as oil and minerals. Structuralists tended to hold to an
idealized and benevolent notion of the state and a belief that its efforts to correct
market failures would automatically result in better economic performance and
welfare. One result of this was that structuralist strategies invariably failed to take
into account the need for institutional and political ways of ensuring that state
interventions were, in fact, effective and to the benefit of the majority of the popu-
lation. Public services tended to be confined to urban industrial sectors, and the
imposition of tariffs, the need to obtain import licences, and the imposition of quotas
had all created new opportunities for corruption in government as bureaucrats
and politicians began to profit from protectionism. The growth of the central state
benefited presidential rule at the expense of party systems, and legislative politics
was often reduced to a struggle over the spoils offered by new opportunities for
corruption created by growing state expenditure (see Chapters 6, 7). The state’s
role in setting up new industries, providing credit to private firms, subsidies and
bureaucratic growth all fuelled public expenditure. This often led to inflation and
deficit spending, by which governments spent money that they did not have in the
expectation that they would be able to raise revenue in the future. Structuralists
were more accepting of inflation than their critics, and it became embedded in Latin
American economies (see Chapters 16, 17).
**Populism and corporatism**

Meeting inflationary expectations became an important aspect of economic management and political negotiation. Some countries such as Mexico sought to control inflation by using corporatist and authoritarian mechanisms that ensured prices and wages were only increased by levels acceptable to the state. This was only possible if the government had effective control over the labour movement and industrialists and was able to forge or impose a consensus between them. The industrializing state’s compulsion to maintain control over organized labour helps to explain why early ISI in Latin America was sometimes accompanied by populist alliances that galvanized political support for statist economic policies (see Chapters 2, 5). Populism is associated with such figures as Juan Domingo Perón (1946–55, 1973–74) in Argentina and Getúlio Vargas (1930–45, 1951–54) in Brazil, who opposed the status quo of primary product exports and favoured state ownership of key industries and intervention to protect workers. Populist movements helped to reduce class antagonisms by linking the working class and industrialists, often behind a shared nationalist ideology, and legitimized state corporatism (see Boxes 2.2, 8.1, 8.2). The growth of public spending that accompanied the expansion of the state offered new opportunities for politicians to dispense patronage in return for support. Corporatism combined with protectionism, subsidised credit and price controls tended to nurture the emergence of privileged interest groups, such as unions and business circles, that directed their energies towards lobbying for state benefits by taking advantage of their favoured position in the industrialization equation (see Chapters 2, 8). Any mobilization by these sectors increased the likelihood that the state would divert scarce funds to them and away from production and welfare in order to ensure their support. The close relationship the state maintained with some organized political interests could be counterproductive, substituting choices made on the basis of political calculations for those made on the basis of efficiency and national interest. Non-organized sectors of the population – in particular, the peasantry – were largely excluded from the benefits of industrial development, causing radicalization and instability. The Cuban Revolution (1959) and the strident rhetoric of its leaders inspired the development of political alternatives outside institutional structures, such as guerrilla movements (see Chapters 2, 13).

**Inequality**

Using Brazil as a concrete example, Evans (1979) argued that while industrialization proceeded at a rapid pace, it delivered few benefits to the vast majority of the population. The political model he developed envisaged statist industrialization based on a ‘triple alliance’ of the state, local capitalists and multinational corporations, each element of which had few incentives to share the product of growth with the majority. In theory, ISI had promised initially to create jobs for a burgeoning working class, but in fact industrial growth under ISI was capital intensive and the amount of labour new plants absorbed was limited in relation to the growth in the
labour force as workers moved from the countryside to the cities. This encouraged states to create jobs, further swelling the size of the state bureaucracy and agencies, and increasing the proportion of GDP committed to public expenditure. It also created a dual labour structure of relatively well-paid workers alongside many unemployed or underemployed workers in traditional sectors. An underemployed worker is one who works less than he or she would like to or needs to in order to survive. Although structuralists did not ignore the countryside, arguing that it was necessary to change patterns of land ownership through land reform, in practice ISI strengthened a tendency to disregard agricultural production as the state adopted measures that hurt traditional agricultural exporters in its effort to escape a reliance upon primary products. Credit was diverted to industry and public expenditures biased towards growing urban areas. Until the 1960s there were only limited efforts to change the social structure of the countryside and landholding patterns (see Chapter 8). Large landed estates remained in existence and low productivity persisted. Impoverished peasants abandoned the countryside to head for the city, fuelling urbanization. The neglect of agriculture further reinforced a need to import food-stuffs, as the countryside was unable to supply urban areas with the food necessary to maintain the industrial workforce. The neglect of agriculture also worsened the unequal distribution of income between urban and rural populations. Latin America was the only region of the world where the share of income going to the poorest 20 per cent of the population consistently declined between 1950 and the late 1970s (Sheahan, 1987). At the same time, the growth in importance of urban political forces such as the labour movement also began to change the traditional balance of power in the countryside and weaken traditional landholders (Cardoso and Helwege, 1992).

**Inefficiency**

Industrialization did not foster a new entrepreneurial class in Latin America, but generated a business class dependent on state protectionism for its existence. The behaviour of this group was sometimes referred to by economists as ‘rent-seeking’, meaning that they spent much time and energy seeking to capture the benefits that arose from the state’s many interventions in economic life. The absence of foreign competition meant that there was little incentive to improve the efficiency of production processes, and the quality of locally manufactured products was often inferior. Leaders of domestic industries were also able to profit from artificially high prices and had no incentive to bring these down. Tax evasion by industrialists limited the revenues the state could use for public spending. Latin American economies relied excessively on tariffs and quotas beyond the early stages of industrialization and, as a result, local industry failed to become competitive in world terms. Services such as electricity or telecommunications were frequently underpriced to stimulate growth, leading to heavy losses that were absorbed by the state and, in the longer term, resulting in underinvestment. By maintaining overvalued exchange rates to make some imports cheaper, the state hurt traditional exporters and so limited their
ability to earn foreign exchange to pay for these imports, and so the cost of imports soon began to outstrip foreign exchange earnings from exports. As a result, Latin American imports and exports in the 1950s and 1960s grew below the world average (Cardoso and Helwege, 1992). Many governments began to respond to declining levels of foreign exchange – and rising levels of state expenditure – by borrowing large amounts of capital from international creditors and banks, particularly during the 1970s, and debts soared. ISI was also marked by overcapacity, with industrial plants being either more numerous or larger than was required to meet domestic demand and operating at high costs. In the late 1960s, for example, there were 90 automobile companies in Latin America producing 600,000 cars annually – an average output of just 6,700 each (Baer, 1972).

**Authoritarianism**

The notion of ‘bureaucratic authoritarianism’ developed by O’Donnell (1973) was the most coherent effort to link the restructuring accompanying the exhaustion of the first phase of ISI with authoritarian rule (see Box 2.5). O’Donnell’s model suggested that, while initially during ISI locally manufactured goods had been aimed at a broad spectrum of the population, in the bureaucratic authoritarian phase from the mid-1960s onwards consumer durables such as cars and electrical appliances which only high-income sectors of the population could afford were seen as the main stimulus to growth. Therefore, continued growth required consumption to be concentrated in the high-income strata of the population, increasing inequality. Inevitably, governments would find it difficult to attract domestic support for such a policy shift among the popular sectors mobilized during the first phase of ISI that were now powerful and influential, particularly organized labour. Therefore, these sectors had to be brought under control to ensure that they did not obstruct economic change. Coalitions comprising the military, domestic and foreign capitalists, and technocrats took power in the most industrialized countries of the Southern Cone and exercised a characteristic form of rule that repressed labour and suppressed political opposition.

**DEPENDENCY APPROACHES**

In the 1960s and 1970s a more radical set of perspectives about development emerged from within the structuralist tradition emphasizing the severe limitations imposed by Latin America’s dependent status within the international economy – the dependency or dependencia school. The notion of dependency had been formulated by Prebisch and debated by ECLA since its foundation, but it did not form a central focus until the 1960s. Prebisch believed that the crucial decisions affecting international trade were inevitably taken in the centre, meaning peripheral countries were dependent on it for growth and so incapable of achieving development on their own.
The most substantial analysis of dependency by economists of the ECLA line was by the Chilean Oswaldo Sunkel (1969).

Dependency approaches grew in popularity in Latin America as criticisms that structuralist development policies had failed to tackle widespread poverty mounted and, as a result, these perspectives were more radical and political. Amid the broader ideological competition of the Cold War period, they coincided with ideas on the left about the objectives of development that were more hostile to capitalism, or advocated a form of capitalism in which social welfare was paramount (see Chapters 2, 13, 17). Dependency approaches began with the premise that the prospects of the developing world reproducing the type of capitalism found in the industrialized world were limited, and that the former could only escape its condition by restricting or even ending contact with the latter. They built upon the notion of a pre-established international capitalist economic system in which the possibilities open to peripheral countries had been rigidly determined by the expansion of the central economies. The policies adopted by the industrialized world perpetuated a condition of economic, political and cultural dependency in the Third World, whose role was to provide natural resources, cheap labour and markets that enabled industrialized countries to remain prosperous. These policies were enforced by the many ways in which industrialized countries set the rules of international trade, but also by the use of military force when necessary. This form of domination by the rich world ensured that the resources of poor countries were taken by industrialized countries, preventing reinvestment in developing nations and stunting their growth – and so the developed world was responsible for continuing underdevelopment in the Third World. Any attempt by dependent nations to resist this resulted in sanctions of some kind, and so economic development in the periphery was considered to be nearly impossible without drastic or, in some cases, revolutionary change.

Diverse dependency schools emerged and many economic thinkers adapted them to Marxist positions, giving them significant force following the Cuban Revolution. Several of these ‘neo-Marxist’ advocates of dependency theory were non-Latin Americans such as the Ukrainian-born American Paul A. Baran (b.1910–d.1964) and the German André Gunder Frank (b.1929–d.2005). However, dependency approaches also influenced many non-Marxists such as Pope John Paul II (1978–2005), and some dependency theorists took a reformist line that had more in common with structuralist positions. As a young economist Fernando Henrique Cardoso (who went on to become Brazil’s president during 1995–2003) together with a colleague, Enzo Faletto, argued that, despite dependency, there were opportunities to adopt strategies that allowed for national control of production and economic growth – ‘associated dependent capitalism’ – through, for example, limiting or taxing foreign capital, controlling capital flows and land reform (see Cardoso and Faletto, 1969). Nonetheless, serious disagreements between social scientists and economists meant that there was no single unified ‘dependency theory’, and dependency approaches were roundly rejected by many economists in the industrial world (see Box 15.6).
Dependency approaches to international economics were also primarily theoretical and spawned few successful practical solutions to the problems of underdevelopment. The Cuban Revolution (1959) and the revolutionary regime’s attempt to industrialize after it had severed ties of economic dependency with the US were of particular interest to theorists. However, in reality, Cuba substituted its economic dependence on the US for an equivalent dependence upon the Soviet Union (see Boxes 2.3, 11.5, and Chapter 17).

Dependency approaches built upon the core–periphery dichotomy in the international economic system envisaged by Prebisch, but diverged from structuralism in important respects:

- **Internal versus external causes of underdevelopment** Structuralism attributed underdevelopment mainly to internal constraints on economic development, and advocated changes in an economy’s internal structure so that it was not as disadvantaged within the international economy. Dependency approaches, by contrast, argued that underdevelopment was externally induced by the existence and policies of the industrial capitalist countries constituting the centre. Some dependencistas reformulated theories of imperialism, arguing that the coexistence in the world economy of development and underdevelopment reflected a neocolonial economic relationship (see Chapters 1, 11). By keeping the Third World underdeveloped, the bourgeoisie of the First World ensured a cheap supply of raw

---

**BOX 15.6 THEORIES AND DEBATES**

**Criticisms of dependency approaches**

Dependency perspectives were heavily criticized, particularly from within the countries they blamed for Latin America’s economic ills, but remain influential today and often coincide with arguments deployed in opposition to free trade and economic globalization (see Chapter 16). However, evidence does not always support the notion that the stronger the ties between rich and poor countries, the greater the latter’s underdevelopment. Supporters of the idea of economic integration, for example, often argue that the weaker partner in an interdependent relationship gains more than the stronger, challenging the idea that centre develops at expense of periphery. The jury is still out, for example, about the extent to which Mexico has gained long-term advantages from formal economic integration with the US and Canada within NAFTA (see Box 16.4). Liberal political economists insist that developing economies have reaped net benefits from their relationship with the industrialized world which, far from generating poverty, has been an agent of progress. They insist that without the access to markets and foreign capital that a close, co-operative relationship with the developed world can offer, developing countries will not be able to secure the investment and foreign exchange that are essential for growth (see Box 16.1).
materials and a market for their manufactured goods, while stifling local capitalism by draining off the resources that could have been used for investment.

- **Capitalism and class** Dependency approaches were mostly hostile to capitalism and appealed, in particular, to Marxists because they drew naturally upon theories of class. Baran (1973) argued that the neocolonial relationship between centre and periphery was sustained by a system of class relations in both. Certain groups within developing countries such as entrepreneurs, landlords and military rulers constituted an elite ruling class whose principal interest was in the perpetuation of the international capitalist system. Capitalists from the central countries dominated Latin America through these local elites. Industrialization would, in fact, threaten this dependent bourgeoisie because it would challenge their privileged position. It was, therefore, against the interests of the advanced capitalist countries for underdeveloped regions to develop. Gunder Frank (1971) developed the notion of ‘internal colonialism’, which asserts that centre–periphery relations were reproduced within countries. Just as the developed centre grew at the expense of the periphery, thereby perpetuating underdevelopment, within countries urban areas absorbed resources from rural areas creating ‘dual economies’ and ‘dual societies’ that were simultaneously traditional and modern.

- **Pessimism** Dependency approaches were more pessimistic about the prospects of escaping underdevelopment than structuralist positions, which suggested that, with the correct mixture of industrialization policies and state investment, a country could overcome its disadvantageous position in the international system. Dependency approaches suggested that the relations between dominant and dependent states were dynamic, and so dependency was an ongoing and constantly changing process. These shifting interactions between centre and periphery tended to intensify unequal patterns of development. Later dependency analysis maintained that it would be hard for Third World countries to escape dependence through industrial development because ISI had, in practice, created new forms of dependency on foreign countries for machinery and capital, leading to indebtedness. First World countries had a vested interest in establishing capital-intensive forms of assembly in the Third World in order to take advantage of their cheap labour without losing technological advantages (see Sheahan, 1987).

- **National revolution** Advocates of dependency approaches placed great emphasis on international power imbalances and the need either for revolution or fundamental economic and political reforms, both within countries and the international system. As they were, in essence, pessimistic about the prospects of a developing country escaping dependence, and believed that the forms of domination by the centre were constantly changing, this left states with few options but to undergo revolutionary change. Marxists who employed dependency theory often advocated a socialist revolution as the only way to achieve the shift in power that was necessary for a country to escape its peripheral condition and achieve national economic autonomy. Gunder Frank, for example, argued that, given the complicity of the
Latin American elites in imperialism, it was only by mobilizing the working class and the peasants to seize power through revolution that the ties of dependency could be broken.

- **Foreign investment and sovereignty** Marxist dependencistas advocated egalitarian policies to reduce poverty and provide more diversified employment opportunities. Some called for the outright expropriation of privately owned companies in the belief that public ownership was essential to eradicating poverty and inequality. They argued that a much greater degree of national control over the economy and foreign investment was essential. Therefore, developing economies needed to limit their contacts with the industrialized countries, take control of national production, and become more self-sufficient. Dependency theorists were particularly critical of foreign investment and their positions appealed to nationalist sentiments that blamed foreign capital for underdevelopment at a time when multinational corporations were investing heavily in Latin America. Latin Americans have long had a love-hate relationship with foreign companies, objecting to the extraction by foreign firms of profits yet also welcoming them as sources of technology and capital essential to achieving development (see Box 16.1). Dependencistas argued that the historical concentration of foreign investment in Latin America in agriculture and the production of raw materials had benefited international capitalists and led to a net capital outflow from developing nations (see Cardoso and Helwege, 1992). They also argued that foreign investment affected political relations by creating a local bourgeoisie whose interests were tied to the success of foreign firms, which in turn gained disproportionate influence over economic policymaking. One of the ironies of the industrialization process in Latin America was that it had been seen by many as a means of achieving greater national control over the economy by freeing a country from the constraints imposed by its reliance on agricultural commodities. However, in order to attract foreign investment, governments were often inclined to adopt policies that favoured foreign firms to the detriment of local producers or that kept organized labour or even the political opposition under control. By the 1960s dependencistas were associating multinational corporations with a lack of full national control over the economy because, in order to attract them, governments had been forced to adopt policies and permit conditions that they argued were not in the national interest and had limited the ability to take sovereign decisions.

**SUMMARY**

The model of economic development adopted in a country has an important bearing on the character of the political system. Growth models based on the export of agricultural and mining products had, by the early twentieth century, nurtured political systems characterized by the domination of an oligarchic elite to the
exclusion of almost everyone else. An established body of liberal theory justified the development of export-led growth as natural and inevitable, given Latin America’s inheritance and position as a supplier of raw materials in the international economy. The Great Depression changed this, forcing Latin American countries to take the first steps towards creating industries that would lessen their reliance on the temperamental international commodities market and that promised the kind of prosperity enjoyed in the developed world. Countries in the region began to subscribe to the economic theory of structuralism, which argued that only if they transformed the structure of their economies by prioritizing industry could they escape underdevelopment. Structuralism challenged some of the central ideas about trade and the role of the state held by economic liberalism. It also rejected the assumptions of the modernization theory developing simultaneously in the industrialized world that assumed countries in regions like Latin America should develop along similar evolutionary lines to them. The creation of industries to manufacture products formerly imported was called import-substitution industrialization, and this required the imposition of barriers to imports through protectionist measures such as tariffs. ISI led to substantial industrialization in Latin America, and in some cases laid the basis for the creation of large, globally competitive industries. Industrialization also had profound social and political implications, fuelling both urbanization and poverty in the countryside, and leading to the creation of large central states that maintained stability through corporatism. The limitations of the rapid industrial growth of the 1950s had become apparent by the 1960s, when countries began to recognize the need to manufacture more sophisticated and valuable products that required greater levels of investment and technological know-how. Now policymakers began to stress the merits of industrial exports and the need for a change in the nature of local consumption patterns to allow more sophisticated forms of manufacturing to develop. One way of securing the high levels of investment and technical knowledge needed to produce more complex goods was by allowing multinational corporations to set up. At the same time, the limited levels of political inclusion implied by industrialization policies and the growth of inequality generated new social and political strains in Latin American countries. A radical theoretical response to the exhaustion of the first phase of ISI and to the social and political strains of the era developed in the form of dependency approaches, which often chimed with Marxist ideas. These advocated breaking Latin America’s economic dependency on the industrialized economies completely. The change in the nature of industrialization combined with growing social and political unrest in the 1960s has been associated by some scholars with the military clampdowns in this period, especially in the more industrially developed Southern Cone countries.
## DISCUSSION POINTS

- By what criteria can the notions of ‘centre’ and ‘periphery’ be distinguished?
- What is protectionism and how can it be justified?
- Was state-led industrialization in Latin America a success?
- How are dependency perspectives related to structuralism?
- Are internal or external economic factors more important for successful development?
- Is it possible to end dependence in Latin America?

## Useful websites

- **www.eclac.cl**  Comisión Económica para América Latina (CEPAL, Economic Commission for Latin America and the Caribbean). See, in particular, ‘Background information – Evolution of ECLAC ideas’
- **www.oecd.org/home**  Organization for Economic Co-operation and Development, a useful source of up-to-date information and assessment
- **www.oswego.edu/~economic/econweb.htm**  Useful site of Internet resources for economists
- **www.embraer.com/english/content/home**  Empresa Brasileira de Aeronáutica (Embraer)
- **www.pdvsa.com**  Petróleos de Venezuela SA (PDVSA), Venezuela’s state oil corporation

## Recommended reading


> Essential, comprehensive yet accessible overview of Latin American economic development since the Independence era and a valuable work of reference.


> Useful examination of specific challenges facing Latin American economic development such as debt and trade with helpful sections on theory and economic populism.

Valuable collection containing essays by various authors that provides helpful theoretical discussions of some important schools of thought.


Essential introduction to the specific developmental problems faced by Latin America for students with varying levels of economic knowledge that includes valuable chapters on the role of the state and contemporary challenges.


Valuable exploration of key problems in Latin American development from poverty to land ownership, and why there have been different national responses to these.