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## *Workshop 5: Economic Liberalism in the Americas*

Short Paper

*“State and Development: economic liberalism in theory and practice in Latin America c. 1900”*

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From the perspective of the twenty-first century, it is easy to depict the Argentine as a serial defaulter and classic example of crony capitalism. As is well appreciated, by contrast, around 1900, the country appeared to be model of ‘virtuous growth’, founded on sound money, an excellent international credit-rating and modern banking. In short, the country that was born to be liberal had become a poster child of contemporary economic liberalism in theory and practice, a depiction subsequently endorsed by new political economy and new institutional economics writing. At the beginning of the twentieth century, the Argentine was ‘liberal’ and ‘advanced’<sup>1</sup>.

Using the Argentine a case-study, this paper will consider a key element of macroeconomic policy - credit, money and banking - through the optic of new contributions to the literatures on monetary regimes and crony capitalism. Much recent work on the architecture of the international financial system and global monetary order c.1900 offers new perspectives on lender-creditor relations and the operation of world capital markets. Similarly, drawing on the public choice approach associated with the new political economy, some revisionist writing on cronyism provides a distinctly nuanced view of state-business engagement. If the late nineteenth century epitomised the high point of economic liberalism and economic internationalism, the Gold Standard was, arguably, the ‘rule’ that most encapsulated ideas about market self-regulation, in part setting the macroeconomic framework within which government and business interacted. The dominant monetary regime of the period, the Gold Standard governed the market through automatic adjustment and constraining the state. Given the centrality of the London, British banks (at home and overseas) are presented as one of the principal mechanisms of diffusing an orthodox market-based model of credit provision and monetary order. The global system was unstable, subject to frequent shocks, yet the Gold Standard and a competitive financial market ensure sound money and the survival of the fittest firms, thereby delivering long-run growth. To what extent do Argentinian monetary

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<sup>1</sup> Túlío Halperín Donghi ‘Argentina: liberalism in a country born liberal’ in Joseph L. Love and Nils Jacobson *Guiding the Invisible Hand: economic liberalism and the state in Latin American history* (New York: Praeger 1988) pp.99-117; Gerardo della Paolera and Alan M. Taylor ‘Introduction’ in Gerardo della Paolera and Alan M. Taylor (eds.) *A New Economic History of Argentine* (Cambridge: CUP 2003) pp.2-3.

and banking arrangements, and the role of London-registered firms operating in the country, conform with these stereotypes, and what insights are offered by new writing? Indeed, how close was the match between theory - old and new - and reality?

The paper begins by surveying select recent additions to the literatures on money, credit and the business of banking. It then presents a stylised monetary history of the Argentine, followed by an assessment of state-firm relations in the banking sector, largely viewed from the perspective of British banks. In the main, the paper takes as given key recent advances, using them to reappraise the history of money, credit and banking in terms of liberalism in theory and practice. The paper does not pretend to offer a technical analysis of credit and finance, or of the monetary system, nor does it seek to contribute to the on going 'what-went-wrong' approach to Argentinian history. Rather, it attempts to explain how and why, in some moments, things went right. Echoing revisionist approaches to policy and the politics of policy-making, the paper finds that initial efforts to deliver monetary stability were broadly well received by international agents, despite setback, until a profound loss of confidence provoked by the Baring Crisis, after which the recovery of 'virtue' depended on super-orthodoxy (and luck), and constraining cronyism - to a degree. In the case of the Argentinian banking sector, crony capitalism proved to be a worst-best, not a second-best alternative.

### Some General Propositions

International capital flows assume state capacity and credibility - as well as liquidity in the market. That is, in the case of sovereign borrowing, a credible commitment by governments to service and amortise debt. Private agents investing abroad require a minimum degree of security, a reasonably predictable economic and political order in which to make rational long-term decisions. For individuals and firms, that environment involves calculations about the exchange rate risk as well as about rates of return - an expectation that profits yield a return on capital and cover possible exchange depreciation when remitting from host to home economies, as well as expectations about protection against arbitrary government action. Reputation is and was critical. The ability of states to maintain their own credit shaped the general environment, as much as particular policy stances that had a direct impact on the macroeconomy. Was reputation, and predictability, delivered by adhesions to a rule - the Gold Standard? Could the markets discipline borrowers and ensure a reasonably stable business environment? Might prestigious merchant banks 'police' borrowers, and so ensure a market-friendly (orthodox?) policy mix?<sup>2</sup>

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<sup>2</sup> Marc Flandreau and Juan H. Flores 'Bondholders vs. bond-sellers?: investment banks and conditionality lending in the London market for foreign government debt, 1815-1913' European Historical Economics Society Working Paper 2011 - 0002, pp.

Two fairly recent discussions in the Gold Standard literature are relevant for this paper: that 'rules' operated differently in core and peripheral economies, and that there were several 'routes' to regime credibility. Thus, although a number of common assumptions prevailed, namely that the Gold Standard had become the recognised international monetary order by the end of the nineteenth century, and that currencies based on gold implied free convertibility, a fixed exchange rates and unregulated movements of metal and/or capital, quite distinct arrangements functioned for a large part of the nineteenth century. Some (mainly core) economies conformed closely with the formal rules of the 'full' Standard: the currency issue was virtually fully collateralised in gold (save for a small, discretionary fiduciary issue), notes and gold were freely convertible on demand and there was unrestricted movement of capital. Other economies operated a 'proportional' cover system, with the monetary authorities holding large reserves of gold, though a ratio of gold to paper that was substantially less than one hundred per cent of the stock of currency issued. In yet other cases, usually the periphery, it was recognised that economies remained in monetary 'transition' for a large part of the nineteenth century, moving towards gold from paper or bimetallic regimes, transitions that were frequently bumpy and reserves often composed of a mix of bullion, fully-back foreign currency notes and government debt - usually British Treasury bills. Even when formally 'on' the Gold Standard, in many late-nineteenth-century peripheral economies there was little domestic circulation of gold (paper or silver tended to predominate) and reserve ratios (usually a mix of bullion and paper) quite low. In effect, many peripheral countries operated what would later be know as the Gold Exchange Standard, rather than the pure Gold Standard. And even if the Gold Standard signalled good house-keeping - financial and fiscal probity, it was a contingent rule for a number of monetary authorities, and an aspiration for others<sup>3</sup>.

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<sup>3</sup> Barry Eichengreen and Marc Flandreau 'Introduction' in Barry Eichengreen and Marc Flandreau (eds.) *The Gold Standard in Theory and History* (London: Routledge, Second Edition 2005) pp.3-5; Michael D. Bordo and Finn E. Kydland 'The Gold Standard as a Rule' *Explorations in Economic History* XXXII (1995) pp. 423-64; Michael D. Bordo and Rockoff 'The Gold Standard as a "Good Housekeeping Seal of Approval"' *Journal of Economic History* LVI 2 (1996) pp. 389-428; Maurice Obstfeld and Alan M. Taylor 'Sovereign Risk, Credibility and the Gold Standard: 1870-1913 versus 1925-31' *The Economic Journal* CXIII 487 (2003) pp. 241-75; Matthias Morys 'The Emergence of the Classical Gold Standard' CHERRY Discussion Paper 12/01 (2012) pp.1-52, see esp. pp14-43.

Macroeconomic management did not feature in the nineteenth-century lexicon of state craft, yet politicians, policy-makers and economic agents were aware of the implications of individual policies. Taxes affected prices and had distributional consequences; customs duties, even those intended primarily to raise revenue, changed relative prices and benefited some groups at the expense of others. Samuel Amaral argues persuasively that inflation, as a fiscal mechanism, was 'discovered during the early national period, and that its functions were understood and appreciated by those able to apply it to their advantage'<sup>4</sup>. Contemporaries may not have theorised about the 'trilemma', but they were aware that particular currency regimes had specific implications for credit systems, the exchange rate and monetary policy - and for the fiscal state<sup>5</sup>. The markets understood that the pure Gold Standard was rarely feasible in peripheral economies, particularly those lacking deep capital markets, well-developed, layered banking and financial institutions, and the means to accumulate substantial stocks of the metal, and that a transition from monetary disorder to order was difficult. Hence aspirations to virtue, coupled with a demonstrable and feasible commitment to deliver, facilitated a tolerance of delinquency - albeit limited. Temporary suspension of the rules of the game was accepted, provided that there was evidence of a credible commitment to re-apply them when conditions permitted. Market perceptions of a determination to be virtuous were enhanced by the presence of a prestigious 'patron' or 'parent bank', that is, the development of relationship banking between creditors and underwriter which gave the former a degree of policy ownership. Such patrons or parents were normally foreign merchant banks, usually London- or Paris-based. Closely involved in floating series of bond issues by particular creditors, the markets assumed that these banks could be relied on to encourage peripheral governments to practice good house-keeping in order to defend their own reputation as well that of capital-importing/creditor economies<sup>6</sup>.

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<sup>4</sup> Samuel Amaral 'El descubrimiento de la financiación inflacionaria: Buenos Aires, 1790-1830' *Investigaciones y Ensayos XXXVII* (1988) pp.379-418.

<sup>5</sup> Maurice Obstfeld, Jay C. Shambaugh and Alan M. Taylor (2005). 'The Trilemma in History: Tradeoffs Among Exchange Rates, Monetary Policies, and Capital Mobility' *American Economic Journal* 11 2 (2010) pp.57-94.

<sup>6</sup> Marc Flandreau 'Crises and Punishment. moral hazard and the pre-1914 International Financial Architecture' in Marc Flandreau (ed.) *Money Doctors. The Experience of International Financial Advice, 1850-2000*. (London: Routledge 2003) pp.13-48; Marc Flandreau and Juan H. Flores 'Bondholders vs. bond-sellers?: investment banks and conditionality lending in the London market for foreign government debt, 1815-1913' European Historical Economics Society Working Paper 2011 - 0002, pp.1-41.

Only recently has state capacity, especially the ability to raise taxes, hardly exercised economists. Unlike historians, who viewed the construction of the fiscal state as a fact to be explained, economists took institutional capacity as a given<sup>7</sup>. Consequently, cronyism - usually associated with constraints on the capacity to the state to tax elites and/or the conceding of privileges to such groups - was regarded negatively. It signalled weak institutional capacity and was/is bad for growth. Stressing the negative, Krueger provides a useful working definition of crony capitalism, a situation that involves those close to government receiving 'favours' that have significant economic value. While these favours can entail outright transfers of assets, they tend to involve the provision of economic entitlements with considerable capacity to generate rents<sup>8</sup>. Qualifying this definition, Haber observes that '... favours allow politically connected economics agents to earn returns above those that would prevail in an economy in which the factors of production were priced by the market.'<sup>9</sup>. However, along with colleagues, he takes a distinctly less negative stance than Krueger, and speculates about potentially positive aspect of cronyism, for example, the extent to which a second-best alternative to market competition might facilitate growth and be capable of evolving into more dynamic variants. Crony capitalism may yield a credible, protected environment in which private agents have the confidence to invest and do business. A promise of rents and security from asset expropriation by government thus delivers opportunities for growth. Individual can be the beneficiaries of such entitlements, but usually the recipients are groups or corporations, organisations that range from the highly structured to loose associations.

Company concessions - licences to form and run a business - were common in nineteenth-century Latin America, and bore many of the characteristics of cronyism. Franchisees were often granted an exclusive privilege, usually for a specified period, and exemption from particular taxes. In addition, some concessions involved asset transfers (for example, land and capital grants) and diverse from of subsidies (profit guarantees, cheap credit, below-cost access to crucial inputs, including labour). Concessions, then, were the norm, conforming with existing legal practice in those countries where modern commercial codes were in their infancy and various forms of corporate activity had historically required official entitlement to function, and where foreign investors sought the assumed additional protection of a government charter.

How useful are these ideas, drawn largely from the development, political economy and new institutional economics literatures, which tend to focus on the second globalisation of the late twentieth century, for framing an exploration of economic liberalism in late nineteenth-century Latin America? What insights are offered into a study of the credibility

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<sup>7</sup> Timothy Besley and Torsten Persson 'The Origins of State Capacity: property rights, taxation and politics' *American Economic Review* XCIX 4 (2009) p.1218.

<sup>8</sup> Anne O. Krueger 'Why Crony Capitalism is Bad for Growth' in Stephen Haber (ed.) *Crony Capitalism and Economic Growth in Latin America: theory and evidence* (Stanford: Stanford UP 2002) p.2

<sup>9</sup> Stephen Haber 'Introduction: the political econoym of crony capitalism' in Stephen Haber (ed.) *Crony Capitalism and Economic Growth in Latin America: theory and evidence* (Stanford: Stanford UP 2002) p.xii.

of macroeconomic 'management', the predictability of the environment within which business functioned and the proximity of the policy framework to theoretical depictions, and contemporary expectations, about liberal economics. In short, how did the market function: was it open, competitive and (relatively) stable, and free from arbitrary state action as assumed in some of the established literature; was there a disjuncture between economic liberalism in theory and practice; what did economic liberalism, as practised, deliver?

### A Stylised History of Credit, Money and Banking

This narrative seeks to provide a description of Argentinian currency regimes, state borrowing and banking in order to test some of the arguments about monetary order, state credibility, the business environment and cronyism outlined above. It begins with a short account of the monetary system and then explores the development of banking. Throughout there are references to borrowing and the macro economic environment.

The early monetary history of the republic was one of confusion and chaos. Different currencies circulated in various parts of the country. Complementary (or competitive) monetary regimes signalled the weakness of the central administration, and pretensions to statehood on the part of some provinces, as much as a general want of coinage and credit to serve the needs of production and trade<sup>10</sup>. Many provinces claimed monetary sovereignty. *After Independence several regional currency 'zones' emerged in the interior as silver coinage of various provenance and different degrees of fineness circulated. Foreign coins circulated widely. In Buenos Aires the paper peso was the principal medium of exchange.* The first 'national' money appeared in 1822 with the issue of simple bills printed for the 'Banco de Buenos-Ayres'. The following year, circulation was standardised with the arrival of silver peso coins struck for the province in Birmingham and a definitive series of notes (which were much more difficult to forge) printed in London. *Convertibility of the Buenos Aires paper peso was, however, 'suspended' in 1826, and would not be restored until 1866.* Although the paper peso served day-to-day needs in the city and province of Buenos Aires, silver was decidedly the metal of the interior, and external transactions were conducted in gold - bullion or specie. Almost everywhere, foreign coins had the status of legal tender though were normally only encountered in Buenos Aires. The growth in the volume and variety of paper was notorious. Paper money bore the stamp of several issuing authorities notwithstanding half-hearted attempts to retire old issues and unify new series. On the eve of the 1866 restoration of convertibility, several series of paper were still in circulation: namely, notes of the Banco de Buenos Aires (1822-26), the Banco de las Provincias Unidas de Río de la Plata (1826-36), the Casa de la Moneda (1836-1853) and the Banco y Casa de Moneda (1859-61). Collectively, these agencies had issued notes valued in excess of 400 million paper pesos<sup>11</sup>. In addition, it is possible that some forced loan

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<sup>10</sup> Angel M. Quintero Ramos *A History of Money and Banking in Argentina* (Río Piedras: University of Puerto Rico 1965) pp.24, 29.

<sup>11</sup> Alberto de Paula & Noemi M. Girbal-Blacha *et al History of the Banco de la*

certificates issued by revolutionary governments of the 1810s and 1820s (and accepted as currency) may have continued in circulation along with tokens (*vales*) passed out by merchants and *estancieros* at times of acute monetary scarcity<sup>12</sup>. Conditions were hardly different in the interior, save that the volume of emissions was more modest and the existence of institutions even more precarious. For example, between the mid 1860s and mid 1870s, seven banks had been floated and failed in the province of Santa Fé alone<sup>13</sup>.

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*Provincia de Buenos Aires, 1822-1997* (Buenos Aires: Banco de la Provincia de Buenos Aires 1998) vol. I, pp.38-41, 45-7; María Alejandra Irigoin 'Finance, Politics and Economics in Buenos Aires, 1820-1860: the political economy of currency stabilisation', unpublished University of London doctoral dissertation, 2000, pp.28&ff. De Paula and Girbal-Blacha provide a descriptive account of currency and banking legislation and detail the formation/liquidation of individual 'banks'; Irigoin offers an analysis of monetary history and policy.

<sup>12</sup> Angel M. Quintero Ramos *A History of Money and Banking in Argentina* (Río Piedras: University of Puerto Rico 1965) pp.28-41.

<sup>13</sup> Charles A. Jones, 'Personalism, Indebtedness and Venality: the political environment of British firms in Santa Fe province, 1865 - 1900' *Ibero-Amerikanisches Archiv* IX 2/3 (1983) pp.385-6.

Attempts in 1860s to stabilise the monetary regime, and effect a return to convertibility, were founded on a bimetallic standard that assumed the Spanish-American gold ounce (*onza de oro*) to be equal 16 silver ounces (*pesos fuertes*), and one silver (hard) peso equal to 25 paper pesos. This gave the gold *onza* an official value of \$400 paper (approximately the price of gold then prevailing in the market)<sup>14</sup>. Efforts to establish a new national currency were aided by export growth (particularly sharply rising wool shipments), an influx of foreign investment linked to a new wave of railway construction which in turn fostered a further growth of production and overseas trade, and the good offices of Barings<sup>15</sup>. Enhanced political stability resulting from repurification also contributed to greater confidence. These conditions were not to last. Monetary order was tested by the outbreak of the war against Paraguay in 1865 - the War of the Triple Alliance - and the world crisis of 1866. Initially, an inflow of Brazilian subsidies and war-related boom sustained optimism. In the long-run, over-issue of notes embarrassed the Banco de la Provincia de Buenos Aires and killed convertibility. The onset of another global commercial and financial crisis in 1873 strained the resources of the bank, which was further compromised by domestic political instability. With the prospect of renewed conflict between the province of Buenos Aires and the federal government, gold was transferred from the Emission Office of the bank to the provincial government and the convertibility of Banco de la Provincia de Buenos Aires notes suspended - the only notes to have national legal tender status<sup>16</sup>. Set up in 1867 as a separate department for the bank, the Emission Office had been charged with accumulating sufficient metallic reserves to manage the return to convertibility. New emissions to finance the Paraguay war, coupled with contracting world trade and declining export prices, ended any possibility of sustaining convertibility. Yet, by 1875, there were further efforts to establish a stable national currency. Again the preference was for convertibility based upon a bimetallic, or limping gold, standard. The bullion market was to be unregulated, and while no limit was placed on the minting of gold, silver coinage was not to exceed a value of two pesos per inhabitant. The legal tender status of silver was similarly restricted<sup>17</sup>. These measures were never put into effect and the new *peso fuerte* remained exclusively a unit of account, yet they evidenced an aspiration to be virtuous, certainly on the part of some policy-makers.

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<sup>14</sup> Jorge A. Difrieri *Moneda y bancos en la República Argentina* (Buenos Aires: Abeledo-Perrot 1967) p.102.

<sup>15</sup> Ricardo M. Ortíz *Historia económica de la Argentina* (Buenos Aires: Ediciones Pampa y Cielo 1964), I, pp.144-5; Jorge A. Difrieri *Moneda y bancos en la República Argentina* (Buenos Aires: Abeledo-Perrot 1967) pp.100-1.

<sup>16</sup> Angel M. Quintero Ramos *A History of Money and Banking in Argentina* (Río Piedras: University of Puerto Rico 1965) pp.51-5; Alberto de Paula & Noemi M. Girbal-Blacha *et al History of the Banco de la Provincia de Buenos Aires, 1822-1997* (Buenos Aires: Banco de la Provincia de Buenos Aires 1998) vol. I, pp.157-63. Though issued by the provincial bank, some series of notes were over-stamped with a federal government guarantee.

<sup>17</sup> Jorge A. Difrieri *Moneda y bancos en la República Argentina* (Buenos Aires: Abeledo-Perrot 1967) p.117; Angel M. Quintero Ramos *A History of Money and Banking in Argentina* (Río Piedras: University of Puerto Rico 1965) p.61.

Generalist 'aspiration' and 'parent banking' approaches explain 'tolerance' of periodic delinquency in the 1860s and 1870s. Irigoín provides an intriguing specific dimension. Bad money may have driven out good, but second-best money was better than none. Debased silver and paper served as growth-inducing mechanisms, monetising and marketising the economy, even if implying substantial transactions costs, as contemporary economic agents were aware and used to their advantage<sup>18</sup>. This construct presents traditional accounts of 'monetary chaos' in a new light. Was the situation one of monetary chaos or monetary complementarity or monetary competition. The complementarity hypothesis suggests that different kinds of money were employed for distinct purposes; the competition hypothesis suggests an arrangement favoured by some liberal monetary theorists - currency choice enabled some users to select which type of money to use for particular transactions.

For much of this period, the history of currency reform was one of a struggle between countervailing demands for easy access to money and for fixed external parities, and between contending models of monetary order - bimetallicism versus gold monometalism. Opinions differed as to the developmental function of money and banks. Currency supply and credit requirements were inexorably linked. While external sources of credit were limited, government and exporters shared a common interest in loose monetary policies. Money equalled credit: inflation generalised the cost of interest charges and debt repayment. The benefits derived by debtors and producers from easy money and exchange depreciation were manifold. Profit margins widened as producers were paid in gold for exports but defrayed domestic costs in paper. And, at times of increased competition in world markets, a soft peso conferred a competitive edge on Argentinian exports. Various attempts during the 1860s, 1870s and 1880s to establish the peso successively on a silver standard, a bimetallic standard or the gold standard were defeated by a combination of circumstances such as sharp deteriorations in the external accounts, pressures upon the budget and seasonal and cyclical demand for credit during phases of rapid economic expansion. Nevertheless, for Panettieri the principal stumbling block was the incorrigible preference of the dominant rural oligarchy for soft money and easy credit. This was the key sector in the policy game, and the state obliged. Cronyism flourished. With investment in land virtually inflation proof, landowners had everything to gain from easy credit, facilitated by a system of currency inconvertibility, coupled with an unregulated bullion market<sup>19</sup>. Yet, as foreign borrowing

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<sup>18</sup> María Alejandra Irigoín 'La fabricación de moneda en Buenos Aires y Potosí y la transformación de la economía colonial en el Río de la Plata, 1820-180' in María Alejandra Irigoín and Roberto Schmit (eds.) *La desintegración de la economía colonial: comercio y moneda en el interior del espacio colonial, 1800-1860* (Buenos Aires: Editorial Biblos 2003) pp. 57-91. For an application of the Irigoín thesis to another currency zone, see the discussion of an 'irrational' preference for silver in the Ottoman Empire in Coskun Tuncer 'Fiscal Autonomy, Monetary regime and Sovereign Risk: foreign borrowing and international financial control in the Ottoman Empire, Greece and Egypt during the classic Gold Standard era', unpublished London School of Economics & Political Science doctoral dissertation, 2011.

<sup>19</sup> José Panettieri 'La ley de conversión monetaria de 1864 y la oficina de cambio de 1867: causas y consecuencias economicos-sociales' *Desarrollo Económico* XX:79 (1980) pp.383-412.

increased during the last decades of the nineteenth century, some politicians and officials argued the case for convertibility. This led to yet another new currency project in 1881.

The 1881 act broke new ground on several fronts. It set a more realistic mint ratio between gold and silver. Foreign coins were gradually to lose their legal tender status thereby obviating the need for a complicated schedule of official values. The proposal attempted to link the peso to the system arrangement by the Latin Monetary Union (originally formed by France, Italy, Belgium and Switzerland, later joined by Spain, Greece, Romania, Bulgaria and Serbia - and Venezuela) then attracting attention in Latin America, and now presented by monetary historians as a step towards gold monometalism<sup>20</sup>. Notes of the Banco de la Provincia de Buenos Aires were to be accepted at the rate of \$25 per gold peso. For a few years the system worked. Export growth and overseas borrowing increased reserves. Gold coins began to enter into circulation. Old notes were gradually retired and the size of the fiduciary issue (mainly fractionary notes) tightly regulated. However, by the end of 1884 the system was beginning to unravel. The balance of trade deteriorated and the external accounts were further pressured by rising interest charges. Convertibility was suspended in 1885 and the country embarked upon a debt-led boom that ended in the Baring Crisis. Monetary emissions mushroomed, overseas borrowing rocketed and direct foreign investment soared. The general course of events during the 1880s has been well documented and lie largely outside the scope of this paper<sup>21</sup>. The misconduct of official banks, and their role in the speculative bubble that preceded the crash and post-Crisis reforms in banking and currency legislation are, however, of direct relevance, providing a neat Kruegeresque example of cronyism.

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<sup>20</sup> Angel M. Quintero Ramos *A History of Money and Banking in Argentina* (Río Piedras: University of Puerto Rico 1965) pp.70-5; Barry Eichengreen and Marc Flandreau 'Introduction' in Barry Eichengreen and Marc Flandreau (eds.) *The Gold Standard in Theory and History* (London: Routledge, Second Edition 2005) p.5 ; Matthias Morys 'The Emergence of the Classical Gold Standard' *CHERRY Discussion Paper 12/01* (2012) pp.25, 26-8.

<sup>21</sup> The classic accounts of the causes and course of the Baring Crisis remain Alex G. Ford 'Argentina and the Baring Crisis of 1890' *Oxford Economic Papers* 8 (1956), 127-50 and Harry S. Ferns *Britain and Argentina* (Oxford: Clarendon 1960) chapters 8 and 14. See also Carlos Marichal *A Century of Debt Crises in Latin America: from Independence to the Great Depression, 1820-1930* (Princeton: Princeton University Press 1989) chapters 5 and 6. See also, Juan H. Flores 'A microeconomic analysis of the Baring Crisis, 1880-1890' Universidad de Carlos III Working Paper (2008) and 'Information Asymmetries, Borrowing Costs and the Baring Crisis, 1880-1890' Universidad de Carlos III Working Paper (2009) pp.1-28.

When the dust settled, the worst expectations of contemporary observers were confirmed. Government debt had mushroomed, with service and amortisation payments consuming a rising proportion of contracting revenues. Official banks had lent well beyond authorised limits: large, unsecured credits had been channelled to friends of the regime in a splurge of crony-lending. In 1890, debt service consumed around 40 percent of federal government tax revenue and represented a similar proportion of export earnings. The total consolidated debt, excluding liabilities such as railway guarantees, was about three and a half times export earnings. In 1890 alone the consolidated debt grew by around 11 percent<sup>22</sup>. Between 1887, when new banking legislation had come into force, and 1889, the money supply increased by an average of 40 percent a year, with the monetary base increasing by a further 40 percent in 1890, largely due to emissions by the guaranteed banks<sup>23</sup>. The medium-to-long-term consequences of the speculative bubble were a massive outward movement of the production frontier, but at considerable institution and personal cost in the short-run.

On the eve of the inauguration of his second term, and the return to convertibility, president Julio A Roca promised a policy of rigorous economy, involving retrenchment, strict finance and a balanced budget. He would have no truck with protectionism, profligacy and a 'low exchange'<sup>24</sup>. These fine words were backed by hard commitments. Debt service resumed and the gold premium tumbled. Confidence strengthened further as wool and cereal prices rose and export volumes increased. By the late 1890s, prefiguring Roca's stance, and following agreement with foreign creditors, government expenditure was subject to tighter control as more orthodox attitudes to banking, finance and currency prevailed. Although some foreign creditors had mooted the idea of establishing an International Financial Commission or Customs Receivership to supervise Argentinian finances and debt repayment,

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<sup>22</sup> Parliamentary Papers (hereafter PP) 'Report for the years 1990-10 on the finances of the Argentine Republic', (1911) XC, p.32, Cd 30465, No. 466; Vicente Vázquez-Prasedo *Estadísticas históricas argentinas (comparadas): primera parte, 1875-1914* (Buenos Aires: Ediciones Macchi 1971) pp.65, 93-5; Gerardo della Paolera and Alan M. Taylor *Straining at the Anchor: the Argentine Currency Board and the search for macroeconomic stability, 1880-1935* (Chicago: University of Chicago Press 2001) pp.68. Including railways guarantees payment would have raised debt service by approximately 50 percent, bringing total debt service to around 60 percent of government revenue and export earnings.

<sup>23</sup> Gerardo della Paolera and Alan M. Taylor *Straining at the Anchor: the Argentine Currency Board and the search for macroeconomic stability, 1880-1935* (Chicago: University of Chicago Press 2001) pp.53-61, 68; Nicolás Cachanosky 'The Law of National Guaranteed Banks in Argentina, 1887-1890: free-banking failure or regulatory failure?' mimeo 2012. In 1890 the guaranteed banks began to call in credit, but the velocity of monetary circulation more than compensated.

<sup>24</sup> *The Manchester Guardian* 11<sup>th</sup> November, 1898 8a&b.

a mechanism that would have resulted in the surrender of fiscal and monetary sovereignty, in the event 'discipline' was restored largely at the instigation of domestic actors exemplified by Roca. By that time the Argentine was thoroughly integrated into the world trading and financial system. Having rejected a course of debt repudiation and economic isolation in 1889 - an option momentarily contemplated by a section of the elite - a final effort was made to join the gold club. At this point, recent experience had demonstrated to the pampean rural oligarchy that large supplies of overseas credit and cheap labour were available and that sustainable development based upon export-led growth was apparently within reach. The opportunity costs were hardly considered but benefits for the agropecuarian sector were tangible. In narrower terms, the dramatic growth in the volume of exports coupled with price improvements both eased the cost of currency reform and threatened to drive up the value of the peso.

In 1899 when the Argentine returned to gold, in effect by operating a gold exchange standard, the choice was no longer between currency stability and exchange depreciation but between stability and currency appreciation. Agricultural interests knew what course they preferred and, in the face of vociferous opposition from groups such as importers who advocated continued appreciation, pushed the new conversion law through Congress<sup>25</sup>. Policy-ownership remained decidedly local, though restoring market confidence entailed substantial long-term domestic political and economic costs<sup>26</sup>. New writing suggests that had an International Financial Commission been set up around 1890, it is likely that credit would have been forthcoming earlier and at relatively low rates of interest, a sweetener that would have eased the way to fiscal and financial 'orthodoxy'<sup>27</sup>. If debt repudiation and acceptance of foreign financial control lay at the opposite ends of the creditor/borrower crisis spectrum, the Argentinian response the Baring Crisis lay somewhere in the middle, entailing the application of a programme largely in line with external expectations, but to a timetable (and with modifications) principally determined by domestic interests<sup>28</sup>.

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<sup>25</sup> J. Panettieri, 'La ley de conversión de 1899 en el marco de formación de la Argentina modern', *Desarrollo Económico* 21:82 (1981) 231-256; Angel M. Quintero Ramos *A History of Money and Banking in Argentina* (Río Piedras: University of Puerto Rico 1965) pp.117-24. Panettieri goes further, arguing that moves to establish the currency on a metallic basis were always designed to prevent currency appreciation - in 1899, as in 1881 and the 1860s. For the agrarian sector, a fixed parity was preferable to currency appreciation, though the best-option was a soft peso.

<sup>26</sup> Harry S. Ferns *Britain and Argentina* (Oxford: Clarendon 1960) pp.471-4; Gerardo della Paolera and Alan M. Taylor (eds.) *A New Economic History of Argentina* (Cambridge: CUP 2003) pp.108-14.

<sup>27</sup> Niall Ferguson and Moritz Schularick 'The Empire Effect: country risk in the first age of globalisation, 1880-1913' *Journal of Economic History* LXVI 2 (2006) pp.283-312; Coskun Tuncer 'Fiscal Autonomy, Monetary regime and Sovereign Risk: foreign borrowing and international financial control in the Ottoman Empire, Greece and Egypt during the classic Gold Standard era', unpublished PhD dissertation, LSE, 2011, pp.256-76.

<sup>28</sup> Gerardo della Paolera and Alan M. Taylor *Straining at the Anchor: the Argentine Currency Board and the search for macroeconomic stability*,



When convertibility was suspended in January, 1885, the gold premium stood at 21. This meant that \$121 paper (or formerly convertible 'gold' notes) were required to purchase \$100 gold pesos. Towards the end of the year the premium almost touched 50 before falling back as the 1885/6 harvest came in. Thereafter, there was a modest annual rise in the premium, if somewhat obscured by seasonal variations, until the beginning of 1889. At that point substantial monthly hikes were registered. At the height of the Crisis in October, 1891, the monthly average for the gold premium was 336. As the premium rose, the value of Argentinian securities fell. In the eighteen months to June, 1891, the market value of federal bonds in London halved; provincial securities declined to a third of their nominal value by January, 1890.<sup>29</sup> Austerity measures and a strengthening of the trade balance for much of 1892 effected a temporary decline in the premium but further increases were registered in the second half of 1893 and early 1894. Subsequently, the trend was downward. At the beginning of 1898 the premium touched a low of 107 while the average for the year was 127.<sup>30</sup> This was virtually the rate at which convertibility was restored according to a novel formula: the par value of \$1.00 gold was set at \$2.25 paper, giving the \$1.00 paper a value of 44 gold cents. In effect this gold/paper parity represented a 56 per cent devaluation of the 1881 paper peso which had enjoyed one-to-one parity with the *peso oro*. This was the tolerance ceiling of monetary virtue, or of the retrenchment and rigorous economy promised by president Roca. It also marked the limit to the 'reform' of cronyism - so far, but no further. Deflation, and tight credit, was acceptable, but only up to a point<sup>31</sup>.

For the next half century, the Argentine experienced a period of remarkable monetary stability. Notwithstanding the effect of inflation during the First World War, the general suspension of the gold standard by most major trading nations in 1914, and a piecemeal return to gold during the 1920s followed by the final breakdown of the system in the early 1930s, the Argentinian peso remained relatively firm. This stability was reflected in foreign exchange markets. As Table I shows, from the 1900s until the 1940s currency supply was tightly controlled - possibly excessively so - and the external value of the peso carefully managed. Super-orthodoxy was the cost of repeated losses of monetary and fiscal virtue in the late nineteenth century, coupled with continuing domestic policy ownership thereafter. A high level of demonstrable commitment was necessary to sustain the confidence of the markets - and some local agents.

Table I: Money Supply and Purchasing Power

	<u>Money Supply</u> (millions of pesos)	<u>Gold Cover</u> (%)	<u>Purchasing Power</u> (1900 = 100)
1900/04	335	* 14.7	100.03

<sup>29</sup> *The Economist*, 6th June 1891 p.725.

<sup>30</sup> J. Alvaréz, *Temas de historia económica argentina* (Buenos Aires, 1929) pp.122-3.

<sup>31</sup> *Gerardo della Paolera and Alan M. Taylor Straining at the Anchor: the Argentine Currency Board and the search for macroeconomic stability, 1880-1935* (Chicago: University of Chicago Press 2001) pp.114-17.

1905/09	565	48.1	89.03
1910/14	773	62.6	82.81
1915/19	1,069	57.4	59.89
1920/24	1,354	77.8	52.49
1925/29	1,334	78.1	60.46
1930/34	1,246	51.6	71.20
1935/39	1,314	-	67.97
1940/44	1,981	-	60.63
1945/49	6,141	-	36.89
1950/54	22,086	-	12.82
1955/59	60,360	-	5.79

\* 1901/4

*Source:* Elaborated from FIAT Concord, Dirección de Planificación y Estudios *Argentina económica y financiera* (Buenos Aires 1966) pp.316-22, tables 258, 260, 263, 266.

As already argued, the growth in the volume of notes and coins in circulation during the early decades of the twentieth century barely kept pace with the huge expansion in economic activity. Massive growth in exports, coupled with positive trade balances and a foreign investment boom before 1914 enabled the Exchange Office to accumulate a substantial stock of gold. In compliance with the 1899 conversion law, the fiduciary issue was reduced as gold cover rose progressively from the 1900s to the 1920s<sup>32</sup>. For much of the First World War, the peso appreciated against sterling and rose strongly against other European and Latin American currencies. At various points during the 1920s the peso stood above par against the currencies of most of the country's major trading partners even, briefly, against the US dollar. Reserve cover continued to grow steadily during the latter part of the war and early 1920s (years of inconvertibility) and touched a high of 80 per cent in 1923. When convertibility was restored in 1927 the rate of gold cover was 78 per cent and remained at around this figure until the peso came off gold. Bullion reserves only fell sharply in 1931 before gold exports were banned and sales of foreign exchange regulated<sup>33</sup>.

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<sup>32</sup> Gerardo della Paolera and Alan M. Taylor *Straining at the Anchor: the Argentine Currency Board and the search for macroeconomic stability, 1880-1935* (Chicago: University of Chicago Press 2001) pp.120-2.

<sup>33</sup> *Revista de economía argentina*, (June 1927) p.488; Angel M. Quintero Ramos *A History of Money and Banking in Argentina* (Río Piedras: University of Puerto Rico 1965) pp.125, 153, 175, 207; .

Both on and off the gold standard, there was relatively little change in currency supply between 1916 and 1941, years when many countries were rapidly inflating the volume of notes in circulation. Argentinian money supply moved largely in line with economic activity. From a 1914 par value against sterling of \$11.4545, the paper peso slipped to \$17.21 in September, 1931, only to recover thereafter as the pound itself came under pressure. In December, 1939, the free market rate on London was \$17.27 against an official selling rate of \$17.00. The exchange on New York was softer. In December, 1939, the dollar bought \$4.39 on the free market against an official selling rate of \$4.23 and an official 1914 parity of \$2.35 paper pesos. The story after the late 1940s was very different, with multiple rates of exchange, repeated abrupt devaluations and a widening gap between the free market and official rates. The Central Bank maintained an official selling rate of \$4.23 on the dollar until 1948. In 1949 the average was \$4.85. From 1951 to 1954 the official selling price was held at \$7.50. In 1955 the average rate was \$10.12 to the dollar. An official rate of \$18.00 was defended from 1956 until 1958. By 1959 the dollar bought \$80.63. Thereafter the rate slipped continuously until 1968-69 when a rate of \$350.00 was <sup>34</sup>defended. However, even this degree of instability appears almost negligible when set against the collapse of the exchange rate in the late 1980s. These details hardly convey the scale of confusion in foreign exchange markets. For much of the period from the 1940s to the 1970s a multiplicity of official and buying rates applied. There were frequent adjustments to individual rates while the list of transactions that could be conducted at the official rates was itself subject to change.

What construction can be placed on this narrative of Argentinian monetary history? As Flores shows, while the phrase had not been coined when he was writing, Ferns would have denied that Barings and Buenos Aires engaged in relationship banking. Flandreau, too, denies a 'parental' relationship<sup>35</sup>. On the other hand, Ziegler argues that Barings played a large role in reassuring the markets<sup>36</sup>. During the 1860s and 1870s, the House was engaged in floating a number of funding and 'developmental' loans, and its participation interpreted by the markets as conferring a seal of approval. Barings' internal correspondence also displays an acute concern about political and policy issues, and a willingness to proffer advice. How could it not, given the default on the 1824 loan underwritten by Barings, decades of non-payment and protracted negotiations, and the long memory of the market<sup>37</sup>? This engagement was well

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<sup>34</sup> Vicente Vásquez-Prasedo, *Estadísticas*, II p.280-83; R.D. Mallon and J.V. Sourrouille, *Economic Policymaking in a conflict society: the Argentine Case* (Cambridge, Mass. 1975), p.23.

<sup>35</sup> Harry S. Ferns *Britain and Argentina* (Oxford: Clarendon 1960) pp.260-1, 307 315-6, 320.-4; ; Juan H. Flores 'Information Asymmetries, Borrowing Costs and the Baring Crisis, 1880-1890' Universidad de Carlos III Working Paper (2009) p.8; Marc Flandreau and Juan H. Flores 'Bondholders vs. bond-sellers?: investment banks and conditionality lending in the London market for foreign government debt, 1815-1913' European Historical Economics Society Working Paper 2011 - 0002, p.17, FN49.

<sup>36</sup> Phillip Ziegler (1988). *The Sixth Great Power: Barings, 1762-1929* (London: Collins 1988) p.233&ff.

<sup>37</sup> Baring Archive HC 4.1.65.

known in London, and efforts to re-establish 'sound money' were widely reported. Repeated attempts to restore the currency on a metallic basis between 1866 and 1881 may be seen as much as a commitment to sound money as failure, possibly explaining why overseas borrowing grew as the government floated railway, public works and funding loans in London between the late 1860s and mid/late 1880s. Perhaps the tolerance threshold of delinquency increased. Did good parenting have influence in the 1881 project, especially the commitment to gold? If parent banking had been a feature of previous decades, the situation changed in the 1880s. International liquidity and the entry on new players considerably reduced the influence of the House. Its 'good offices' were no longer necessary to foster market appreciation of opportunities in the River Plate and cautionary advice less likely to be heeded - if it ever had been.

It may be argued that from the 1860s to the mid 1880s, monetary policy was more orthodox than has sometimes been allowed. There was sufficient evidence of a credible commitment to liberal monetary orthodoxy to reassure the markets. Despite repeated failures to sustain convertibility, suspension was accompanied by reasonably convincing evidence of an aspiration to conform. Until the 1880s, that is. After the 1889-91 crisis, markets were considerably more sceptical. Serial delinquency, coupled with the unfortunate loss of a parent/patron, meant that domestic policy ownership could only be sustained by super-orthodoxy.

#### Banks, Orthodoxy and Cronyism

If the condition of the local currency established one set of parameters within which banks, including foreign financial houses operated, official participation in the sector and government regulation provided another. For much of the nineteenth century the most important institution in the country was the Banco de la Provincia de Buenos Aires which, as the name implies, was the Buenos Aires state bank. Founded in 1863, it replaced the Banco y Casa de Moneda del Estado de Buenos Aires created in 1856. The Banco y Casa had served as the main financial instrument of the province when Buenos Aires sought to establish its independence from the Confederation and was by far the most important financial institution in the region. Yet its activities were those of a money-creating agency rather than a bank, a function which had also been the principal purpose of its predecessor, the Casa de Moneda, liquidated in 1854.

Banks could be brought down by a political crisis - a change of regime, when the 'ins' became the 'outs'. But what happened in the case of an economic crisis? Before central banks and the development of central banking practices, there was no lender of last resort. States were the protector of last resort. But which banks to bail out? Was the decision taken rationally and impartially, or discretionally? Did governments distinguish between those institutions suffering a liquidity crisis, temporarily embarrassed by an economic downturn, and those that were insolvent, possibly as the result of reckless behaviour that had precipitated the crisis? As Charles Jones has argued, in the Argentine in the nineteenth-century, the key question was not 'What bank?' but 'Whose Bank?' By mid-century there was a well-established precedent of cronyism and its consequences, namely the liquidation and reconstruction of official institutions when they suffered financial embarrassment. The sequence of bankruptcy, liquidation and refinancing hardly served to construct credible commitment - or stability - in the 'banking sector', but became the standard response to political and economic crisis. Banks were 'allowed to fail' to escape some obligations, but not at the expense of favoured friends of

a regime. The interests of some were protected, those of others were not. Politics, not the market, determined which institutions would be protected.

On the other hand, the sequence of foundation, liquidation and re-foundation mirrored that of efforts to establish the currency on a metallic basis. During the 1860s the Banco de la Provincia painfully established a reputation as a reasonably solid, dynamic institution. In 1882 the bank boasted 24 branches (including head office) in the city and province of Buenos Aires, accounted for the lion's share of capital invested banking and held the greater part of total deposits. At that point, the premier British bank, the London and River Plate Bank Limited, had four branches, though one was located in Montevideo and another, Córdoba, was about to be wound up<sup>38</sup>. By 1884, the provincial bank accounted for 44.0 per cent of the capital of banks operating in Buenos Aires and 68.1 per cent of deposits. At that point, the national bank was held 27.8 per cent of total bank capital and 14.3 per cent of deposits, with the now two-branch London bank accounting for 16.7 per cent of capital and 7.5 per cent of deposits<sup>39</sup>.

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<sup>38</sup> Province de Buénos-Ayres, Ministère de Gouvernement, Bureau de Statistique Générale *Annuaire Statistique de la Province de Buénos-Ayres, deuxième année, 1882* (Buenos Aires, 1883), p.316.

<sup>39</sup> Mulhalls, *Handbook, 1892*, p.37.

Repeated attempts at currency reform (and the exercise of political patronage) resulted in a tendency to restrict the right of issue, a privilege that was increasingly reserved for official banks. As Jones notes, before the large-scale overhaul of state banking in the 1890s, the conferment or cancellation of the right of issue was less determined by banking theory than the political connexions of a particular institution<sup>40</sup>. The provincial authorities in Buenos Aires were notoriously restrictive and jealously attempted to maintain the monopoly rights of the Banco de la Provincia, before and after the separation of the province from the Confederation in the 1850s. Nevertheless, across the country, issue rights were almost entirely confined to official banks by 1886, when the authorised issue of the national bank accounted for 48 per cent of money supply, the Banco de la Provincia 40 per cent, with other provincial banks accounting for most of the balance<sup>41</sup>. All official banks failed during the Baring Crisis, when British institutions found their presence in the sector - share of capital and deposits - soar. The provincial bank was reconstructed after the Crisis and, having got into further difficulties, was reorganised again in 1906 as a mixed entity. It never attained the predominance of its predecessors. The dominant position in the sector came to be held by the successor of the federal entity set up in 1872 explicitly to challenge the primacy of the Buenos Aires provincial bank. Like the early incarnations of the Buenos Aires provincial bank, the National Bank served as an instrument of government policy.

Set up as a mixed entity (the government was to hold 10 per cent of the equity), the Banco Nacional initially led a chequered existence and, until the 1890s, was but a pale shadow of its provincial counterpart. Although the original capital was rapidly subscribed, its operations were limited by the established position of the Banco de la Provincia in Buenos Aires and by the status enjoyed by provincial banknotes from 1874 until 1881. When convertibility was suspended in 1874, only the notes of the provincial bank were granted the status of legal tender in the province<sup>42</sup>. The National Bank suffered a further setback in 1876 when all notes other than those of the Banco de la Provincia were excluded from Buenos Aires. These circumstances only changed in 1881 with the federalisation of the city of Buenos Aires and the introduction of the gold standard. Following the suspension of convertibility in 1884, like most of the other official and semi-official banks, the Banco Nacional was encouraged to over issue. This tendency was compounded by new banking regulations introduced in 1887.

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<sup>40</sup> Charles Jones 'Personalism, Indebtedness and Venality: *the political environment of British firms in Santa Fé province, 1865-1900*' *Ibero-Amerikanisches Archiv* IX 3/4 (1983) pp.381, 389.

<sup>41</sup> Angel M. Quintero Ramos *A History of Money and Banking in Argentina* (Río Piedras: University of Puerto Rico 1965) p.83.

<sup>42</sup> Angel M. Quintero Ramos *A History of Money and Banking in Argentina* (Río Piedras: University of Puerto Rico 1965) pp.54, 55-9.

The Law of National Guaranteed Banks, or the free banking law, of 1887 is conventionally presented as an example of laissez faire ideology<sup>43</sup>. Founded on the liberal principle of 'bounded competition' - essentially market-regulated competitive banking underpinned by government inspection and guarantee - the act was loosely modelled on US free banking legislation. The 'reform' was designed to serve a number of functions, but rapidly degenerated into a classic example of crony banking, triggering the question whether the collapse of the experiment signalled market or state failure<sup>44</sup>. Among the principal objectives of the act, intended to ensure stability and flexibility, were the repatriation of the overseas debt, controlled extension of money supply and the promotion of public confidence by laying down stringent reserve requirements and the creation of a banking inspectorate. Capitalised at no less than \$250,000, guaranteed banks were required to deposit gold with the Banco Nacional: for each \$85 gold deposited, the bank would receive a \$100 gold bond, up to the limited of subscribed capital. The gold bonds were to be left on deposited at the National Bank, earning interest at 4.5 per cent. The note issue of guaranteed banks was limited to 90 per cent of gold bonds, and they were required to maintain reserves of at least 10 per cent. Only banks accepting the provisions of the legislation would be permitted to issue notes. Emission limits and reserve requirements were to be policed by the bank inspectorate. Should a bank fail, creditors would be reimbursed from assets held at the Banco Nacional<sup>45</sup>.

Most of the acceding banks were national and official, floating loans overseas to accumulate gold to deposit at the National Bank, an operation that implied considerable leverage in order to increase the monetary base. Firmly in the pockets of provincial rural oligarchies and a federal government anxious to consolidate support, under the guise of fostering agricultural development and infrastructure modernisation, the guaranteed banks served as a source of easy credit for administrations, public corporations and favoured individuals alike. Seven of the 12 banks operating in the country in 1887 acceded. In addition, 13 new guaranteed banks were floated under the provisions of the act during the next year or so, over half of which were official provincial banks<sup>46</sup>. During the currency of the act, money supply more than doubled from \$85 million paper pesos at the end of 1886 to almost \$197 million in 1890.

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<sup>43</sup> Gerardo della Paolera and Alan M. Taylor (eds.) *A New Economic History of Argentina* (Cambridge: CUP 2003) p.240.

<sup>44</sup> Nicolás Cachanosky 'The Law of National Guaranteed Banks in Argentina, 1887-1890: free-banking failure or regulatory failure?' mimeo 2012.

<sup>45</sup> Ricardo M. Ortíz *Historia*, pp.297-8; Jorge A. Difrieri *Moneda y bancos en la República Argentina* (Buenos Aires: Abeledo-Perrot 1967) pp.127-30; Gerardo della Paolera and Alan M. Taylor (eds.) *A New Economic History of Argentina* (Cambridge: CUP 2003) pp.24-5, 58..

<sup>46</sup> Angel M. Quintero Ramos *A History of Money and Banking in Argentina* (Río Piedras: University of Puerto Rico 1965) pp. 87-8.

Sceptical about the objectives and operation of the 1887 law, British banks declined to seek accreditation, accepting the loss of issue as a consequence. Like some other private banks, British-registered houses doubted both the competence and the confidentiality of the regulatory agency, and questioned its impartiality. Loss of the right of issue was of little significance to the London bank by this stage. In Buenos Aires, the London bank had learnt to live with the note monopoly previously enjoyed by the Banco de la Provincia, a situation that was hardly dented when similar privileges were granted to the national bank and other provincial agencies registering as guaranteed banks. In 1882, notes issued by the Córdoba branch of the London bank had been called in when the branch was liquidated. Issue rights of the Rosario branch had been cancelled unilaterally by the Santa Fé provincial government in 1875, then in dispute with the London bank. The British bank had protested but yielded to *force majeure*<sup>47</sup>.

The nature of their business determined that regulation, rather than competition with state institutions, was most likely to exercise British and other overseas banks, hence the heightened concern about the impartiality of regulatory agencies. Local banks - semi-official and official - tended to offer accommodation to government (national and provincial) and a narrow circle of politicians and powerful landowners. Perforce, foreign banks often had to offer accommodation to political figures but preferred not to. Instead, British banks wished to concentrate on short-term commercial business and managing the accounts of British residents and companies. However, potential for conflict with local firms should not be underestimated during early years of operations in the River Plate. Again, as Jones has shown, local bankers were infuriated by the unwillingness of the principal British banks to come to their assistance at moments of difficulty and were thoroughly displeased by the ability of some London registered institutions to survive when domestic firms were forced to close their doors. Even more disappointing were the conservative practices of British institutions, considered ill-tuned to the requirements of an expanding capital- and credit-hungry economy. Tensions were often greatest when closer supervision was imposed from London on Latin American branches, curbing looser lending practices applied by managers who had grown accustomed to the local way of doing business<sup>48</sup>.

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<sup>47</sup> Charles Jones 'Personalism, Indebtedness and Venality: *the political environment of British firms in Santa Fé province, 1865-1900*' *Ibero-Amerikanisches Archiv* IX 3/4 (1983) pp.389-90; Ezequiel Gallo 'El Gobierno de Santa Fé versus el Banco de Londres y Río de la Plata: 1876' mimeo 1972.

<sup>48</sup> Charles Jones 'Personalism, Indebtedness and Venality: *the political environment of British firms in Santa Fé province, 1865-1900*' *Ibero-Amerikanisches Archiv* IX 3/4 (1983) pp.381-99 and 'British Capital in Argentine History: structures, rhetoric and change' in Alistair Hennessy and John King (eds.) *The Land that England Lost: Argentina and Britain, a special relationship* (London: British Academic Press/Tauris 1992) p.72. Commercial Banks', 'The State and Business Practice'

Foreign banks were also exercised by the threat of discriminatory taxation, action they depicted as illiberal and decidedly likely to damage business. As part of a package of measures devised to restore public finances at the onset of the Baring Crisis, bank profits were subject to a tax of 7 per cent but an additional levy of 2 per cent was to be charged on deposits placed in foreign banks. Although presented as an emergency fiscal measure, discriminatory legislation was intended to strengthen the position of official banks at the expense of foreign. The refusal of the (mainly) foreign banks to accept the provisions of the guaranteed banks act had been widely resented in government circles and by 1890 was held to have damaged confidence in the new system. Only with the imminent collapse of the National and Provincial banks was the threat countered in 1890/91. Pressed by the government to participate in a loan to save the two premier official banks, the price extracted by the London bank was that discriminatory taxation on deposits should be abandoned<sup>49</sup>.

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Charles Jones 'British Capital in Argentine History: structures, rhetoric and change' in Alistair Hennessy and John King (eds.) *The Land that England Lost: Argentina and Britain, a special relationship* (London: British Academic Press/Tauris 1992) p.72.

Unsurprisingly, until 1899, another problem confronting banks - particularly foreign houses - arose from the currency situation. Foreign banks were always anxious about the position of gold accounts. Conducting business in both gold and paper, they paid special attention to movements of gold into and out of the country. Despite aspirations to virtue, the problems encountered in attempting to establish the currency on a metallic basis advised considerable caution both during periods of convertibility and inconvertibility. While gold always circulated freely in the city of Buenos Aires, not least when the paper peso was inconvertible, during periods of convertibility private banks were vigilant lest they be embarrassed by the declaration of a *curso forzoso*, a sudden suspension of convertibility of the notes of official and semi-official banks, or a decree authorising the settlement of gold obligations in paper. Consequently, foreign banks were frequently subject to the charge of conspiring against the currency. Managers of foreign banks might argue that an unwillingness to hold very large amounts of 'gold notes' was simple prudence, an action justified by the monetary history of the Republic. Local banks of issue and their supporters, on the other hand, almost invariably viewed the regular presentation of notes for conversion into gold by a foreign competitor as a crude strategy to undermine their position. Local politicians also interpreted such action as at best unfriendly or a conscious ploy to frustrate imaginative monetary reform. Antagonism was inevitable when actions regarded by foreign banks as an issue of business management were viewed by officials and politicians as an attack on policy<sup>50</sup>.

Much as bankers would have wished it otherwise, the currency situation was a hazard endowed with political as well as business implications. And - as all parties were aware - good profits could be made from exchange speculation. Experience dictated that a balance had to be kept between gold and paper obligations and exposure reduced when difficulties were anticipated. For example, during 1875 the Bank of London reduced by 60 per cent the value of its notes in circulation.<sup>51</sup> In part this was due to the dispute in Santa Fé which resulted in the cancellation of issue rights of the Rosario branch, but was also due to concern that the anticipated suspension of convertibility of notes of the Banco de la Provincia might produce a run on all banks. (The decree suspending the convertibility of provincial notes came early in 1876).

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<sup>50</sup> For distinct positions on the 'ideology' of monetary policy, and implications for banking practice, see Charles Jones 'The Transfer of Banking Techniques from Britain to Argentina, 1862-1914' *Révue Internationale d'Histoire de la Banque* XXVI 7 (1983) pp.255-61.

<sup>51</sup> David Joslin research notes, London and River Plate Bank Limited, Capital and Liabilities, 1863-1877.

Again, the Baring Crisis was pivotal, influencing banking practice as monetary policy. If policy-makers ultimately viewed super-orthodoxy as the price of monometalism in 1899, banking practice was reshaped in the fallout from the crisis. Contemporaries viewed guaranteed banks, responsible for incontinent note issue, as the principal cause of the crisis. Illegal emissions and the failure of supervision were a function of crony banking. The National and Provincial banks were prime examples of cronyism, and the first to experience a run. Of twenty banks organised to conform with the provisions of the 1887 free-banking legislation, all but two failed in the Crisis. The outcome was a return to forms of conservative banking long advocated by British houses<sup>52</sup>. After the crash, the Banco Nacional was reorganised in 1891 as the Banco de la Nación Argentina. As earlier, the stated intention was to float the bank as a mixed corporation in order to prevent political control, but the public was wary - as well as weary - of an official entity, suspecting a resurgence of cronyism<sup>53</sup>. The bank conducted a modest business until 1904 when its charter was modified, becoming an exclusively state institution. As the principal official bank, demonstrably adhering to the rules of the game, it gradually grew in prestige from the turn of the century. Before 1914 it was already the dominant institution in the local market and gained in importance thereafter. On the eve of the First World War the Banco de la Nación held almost half the reserves of the whole banking system.<sup>54</sup> From this position it began to perform quasi-central banking functions during the 1920s.

Most bankers thoroughly approved the managed appreciation of the peso until 1899 when the Gold Exchange Office (Caja de Conversión) reopened its doors. The Caja held the greater part of the country's gold reserves, shown in Table I, and retained responsibility for the issue of currency until the 1930s. If there were complaints, they were over details of practice not policy. By 1914 and during the 1920s bankers bemoaned the excessive caution of the Banco de la Nación, its failure to offer re-discounting facilities in the face of rigid monetary control (aggravated by the retention of Argentinian paper pesos in neighbouring republics, especially Paraguay, where Argentinian notes were held as a reserve currency)<sup>55</sup>. There were grumbles

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<sup>52</sup> F Pakenham, British Minister in Buenos Aires, to Marquis of Salisbury, Secretary of State, 9th December 1889, Public Record Office (hereafter PRO), Foreign Office correspondence (hereafter FO) 6/404:159-61, Pakenham to Salisbury, 8th June 1890, FO 6/409: 69-73. Pakenham reported on illegal currency emissions by provincial banks and the national bank in 1889 and 1890 which were widely rumoured in the press and subsequently the subject of a congressional enquiry. See also, Gerardo della Paolera and Alan M. Taylor (eds.) *A New Economic History of Argentina* (Cambridge: CUP 2003) pp.51-61, 70-4; Nicolás Cachanosky 'The Law of National Guaranteed Banks in Argentina, 1887-1890: free-banking failure or regulatory failure?' mimeo 2012.

<sup>53</sup> Gerardo della Paolera and Alan M. Taylor (eds.) *A New Economic History of Argentina* (Cambridge: CUP 2003) pp.107.

<sup>54</sup> Angel M. Quintero Ramos *A History of Money and Banking in Argentina* (Río Piedras: University of Puerto Rico 1965) p.138.

<sup>55</sup> Gerardo della Paolera and Alan M. Taylor (eds.) *A New Economic History of*

too at the tardy establishment of a Clearing House and the refusal of the Banco de la Nación to participate. From 1892 until 1912, when the agency was finally transferred to the national bank, the Clearing House operated from the premises of the London bank. Nevertheless, bankers in general, and foreign bankers in particular, welcomed continuing commitment to the monetary rule of the day, and probably recognised that super-orthodoxy was the price of guarantee bank delinquency.

## Preliminary Findings

This paper has revisited money and banking in the Argentine around 1900 to test whether or not policy was liberal in intent and/or outcome, arguing that the monetary regime of the day, the Gold Standard, was one of the key components of the prevailing order. The Gold Standard rule was predicated on assumptions of a market-based self-regulating mechanism. In much of the traditional literature on the history of money and banking in the Argentine, British banks are depicted as the principal exponents of orthodox (non-developmental) banking practices that conformed closely with the maintenance of the monometallic currency regime.

Conventionally, the (unsuccessful) struggle 'permanently' to establish the currency on a metallic basis for much of the second half of the nineteenth was presented as a failure (or unwillingness) to abide by the rules of the game. Viewed through the optic of new lines of thinking, this paper questions that assessment. The sequence of moments when the currency was convertible - backed by silver or gold or both - and reasonably convincing efforts to return to metal when the moment was opportune, may be depicted in a different light. With the support of a 'parent' lending some credence to these efforts, and aware of the exogenous nature of most crises, as well as a sense of movements in the external accounts, domestic and international markets tolerated temporary 'delinquency', recognising periodic declarations of a *curso forzoso* as an inevitable (and appropriate) policy response at moments of stress. Or, rather, that internal and domestic markets did so until the Baring Crisis. The debacle of 1890 produced an attitudinal change in the markets. Thereafter, and in part a function of a strong emphasis on domestic policy ownership, confidence and credibility was only established (and sustained) by an exceptionally conservative approach to currency and credit management, an approach that also necessitated demonstrable efforts to curb cronyism in the banking sector. In other circumstances, cronyism might have been a useful developmental tool, but the experience of free-banking in the run-up to the crisis generated public and market intolerance of practices that diverged too far from the exceedingly cautious or conservative.

The revisionist literature shows that cronyism may function as a second best alternative to market capitalism, as conventionally presented, when privileged access to politics secures the property rights of insiders, favours generate rents and rents are productively applied. Crony banks neatly typifies these characteristics. They enjoy special favours, which may include monopoly rights such as that to print currency, and official support in moments of distress. They serve as money/credit machines for those with potentially profitable ventures in which to invest. In short, the arrangement generates funds, opportunities and reduces risk, and is conducive to growth. Crony banking in the Argentine before and during the 1880s manifest a

number of these features. For example, monopoly rights of issue secured by various incarnations of the Buenos Aires provincial bank, protection from the costs of failure enjoyed by successive officials banks (or favoured insiders), differential (or discretionary) application of the rules of the game, and freedom to manufacture money. Did the system facilitate growth (ultimately productive capacity expansion and resources generation), or an ephemeral bubble? As stated above, there was an outward movement of the frontier of production, which included some over-build or generation of ( temporary) excess capacity, features of investment booms and the business cycle in general. The bubble of the late 1880s displayed some of traits; it also manifest distinctly negative features. Acute macroeconomic volatility, represented by rapid monetary expansion, fiscal incapacity, accelerating inflation and exchange depreciation detailed above, weakened property rights and incentives. Temporary asset valorisation and credit diversion, as occurred in the latter part of the 1880s, did not signal productive capacity expansion. In addition, the opportunity cost was high, as illustrated by the task of restoring credibility to the banking sector - the locomotive of growth (?) - following the collapse of crony guaranteed banks. Free-banking in the Argentine barely conformed with the theory of economic liberalism, the practice was even more distant. Rapacious insider banking, yes; efficient, self-regulating, disciplined by the market and conforming to liberal/orthodox precepts, or delivering second-best growth, hardly - or not until long after the Crisis.