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The great depression in Argentina, Brazil and Uruguay: revisiting vulnerabilities and policies

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III. The historical framework of the Great Depression

The outbreak of the Great Depression is undoubtedly linked to the US, due to a combination of internal structural problems and inappropriate policy responses from the government of the Republican Herbert Hoover. Its roots can be traced to the structural changes prompted by the First World War. This war favoured the US in such spectacular way that it turned into a major supplier of raw materials, foodstuffs and industrial products in the world. It was also the main creditor of the world and its industries were competitive. It was mostly free from pressure on its balance of international payments, the contribution of foreign trade to GDP was relatively small and its economic system was mostly liberal. It accounted for more than one-third of the global demand for primary products and more than 40% of the primary-product consumption of the fifteen leading industrial countries. The US imports and exports by 1929 represented nearly one-seventh of the total value of the imports and exports of all countries. However, there were serious structural problems, such as: unequal distribution of income, an unhealthy banking structure with small banks near collapse, bad corporate structure, capital concentration and lack of investment¹¹⁵. Thus, the US had achieved such a weight in the world's economy and capital flows, that whatever the consequences of those structural factors on the national economy, they would unavoidably have repercussions worldwide.

The US suffered three shocks to aggregate demand: the collapse of agricultural prices, the stock market crash of 1929 and the banking panics during 1930-1933¹¹⁶. Indeed, as Temin (1976, pp. 171-172) argues, it is equally incorrect to say that the crash of the New York Stock Exchange of 1929 caused the Depression by itself and that the Depression owed nothing to the crash. The crash was one of several deflationary factors, although hardly the largest. Before the crash, the rise of the stock-market was not based on sound profitability, but on a general and unloosed

¹¹⁵ Many authors have mentioned outstanding characteristics of the US economy. See for example Arndt, 1944; p. 89; Eichengreen, 1992b, p. 225; Eichengreen & Portes, 1987, p. 15; Erickson, 1972, p. 11; Fox, 1937, p. 20; Galbraith, 1955, p. 160; Rothermund, 1996, pp. 48-55; and Thorp, 2000, p. 5.

¹¹⁶ There are other events that can be highlighted. Eichengreen (2004) distinguishes estate boom in Florida in 1925, a Wall Street boom in 1928-9, and the consumer durables spending spree in the second half of the twenties. The classic work of Galbraith (1955) describes that during the twenties all the elements of the traditional speculative bubble in the real estate market were present, notoriously in the State of Florida. Kindleberger (1973), beyond the Florida estate boom put emphasis on the automobile and electric appliance industries.

speculation. And it was not only on the part of the biggest companies, but also of a great part of the population, which was driven more by prospects of increasing capital rather than earning dividends¹¹⁷. The sudden halt of the vicious circle in which rising prices prompted further speculation, came to a catastrophic end on October 29th, 1929. That day the US suffered the infamous ‘Great Crash’ of its stock exchange market, which signalled the seriousness of the most global and long lasting downturn in the last century. The stock market crash did have two observable effects. First, the fall in stock market prices reduced the wealth of consumers, who in turn reduced consumption expenditures. Second, both non-agricultural individuals and corporations, who during the twenties were borrowing in order to lend or to invest in financial assets like equities, began to reduce their leverage in 1930 fostering a process of disintermediation.

The deflation in stock markets added to the depression from agriculture. Natural conditions and market mechanics influenced this outcome. The 1929 harvest was poor in America and other exporting regions, but not in the importing areas of Europe, and as a consequence the production and revenue fell in the US. Madsen (2001, p. 357) argues that the decline in prices of agricultural products was a significant contributor to the decrease in output and the international transmission of the depression. That was because it resulted in a deflationary spiral with substantial redistribution of income and spill-over effects from the agricultural to the non-agricultural sector. Furthermore, commodity trade was highly exposed to price volatility. Most commodities were shipped to the various ports of the world on consignment, so that they were ordered, but not paid for in advance. When the Great Depression hit, confidence collapsed and commodity brokers became desperate to sell their wares and as a consequence their prices dropped dramatically¹¹⁸. Thus, prices fell through the economy, triggering the aforementioned mechanics of contraction in economic activity.

The third shock to the aggregate demand is linked to the financial crisis in the US that the Federal Reserve did not adequately prevent. The US experienced widespread banking panics in the fall of 1930, the spring of 1931, the fall of 1931, the fall of 1932 and the winter of 1933. And this last episode coincided with several transcendental economic and politic changes in the US. On March 4th, 1933 the Democratic Franklin D. Roosevelt received the presidency from the Republican Herbert Hoover, in the middle of one of the worst banking crises suffered by the US. Within two months he had to take radical measures. He declared a national ‘bank holiday’ on March 6th, 1933, imposed exchange control¹¹⁹ on March 9th and the suspension of the gold

¹¹⁷ The most illustrating example of this frantic speculation was the activities of Charles Ponzi in Florida, Clarence Hatry in London, and Ivar Kreuger in Stockholm (Eichengreen, 2004, p. 7), who established models of business that offered great returns as long as money kept flowing in, so that existing investors could be paid with the new money, or were plainly fraudulent.

¹¹⁸ See Clavin (2000, p. 100).

¹¹⁹ The Emergency Banking Relief Act passed on March 9th, 1933, gave the President the ability to declare a national emergency and assume absolute control over the US national finances and foreign exchange.

standard on April 19th. The banking panics were so severe that by 1933 one-fifth of the banks in existence at the start of 1930 had failed¹²⁰.

However, it is inaccurate to blame only the US. Europe also had a leading role in the Great Depression, along with the prevailing ideology of the time that prescribed the allegiance of governments to the gold standard orthodoxy. In this chapter we explore the national policies, the collapse of international trade, the failure of multilateral diplomacy, the general situation of Latin American countries in this context and finally we make a link to the present focusing on the Financial Crisis of 2008.

i. All mighty national interest

By that time, the worst hit section of the world economy was international trade. Between 1929 and 1933 the value of world trade shrank by more than 66% in gold dollar terms, with the contraction in trade of manufactures at -41% and raw materials -19%¹²¹. This downward trend was most eloquently illustrated in the widely reprinted diagram known as the ‘Contracting Spiral of World Trade’, reproduced in Figure 2, first published by the *Österreichischen Institutes für Konjunkturforschung* in 1933. This figure, used by the League of Nations in its Economic Survey for 1932-33, Eichengreen & Irwin (1995), Irwin (2012), Reinhart & Rogoff (2009) and Ferrantino (2009), among many others, shows the value of world trade spiralling downward: 5.3 billion gold dollars in 1929, 4.9 in 1930, 3.3 in 1931, and 2.1 in 1932, reaching its lower point of 1.8 billion in 1933. It is important to note, however, that the decline in the value of the world trade was not evenly distributed, since agricultural prices fell more than those of finished goods. In Table 2 we show the decline in average gold export prices of the main commodities associated with their main exporting countries during 1929-1934. For example, products like copper, wheat, coffee, maize, wool and cotton, all important staples in Latin American exports, lost by 1934 more than 50% of their 1929 value. Consequently, exporting countries of those products were negatively affected.

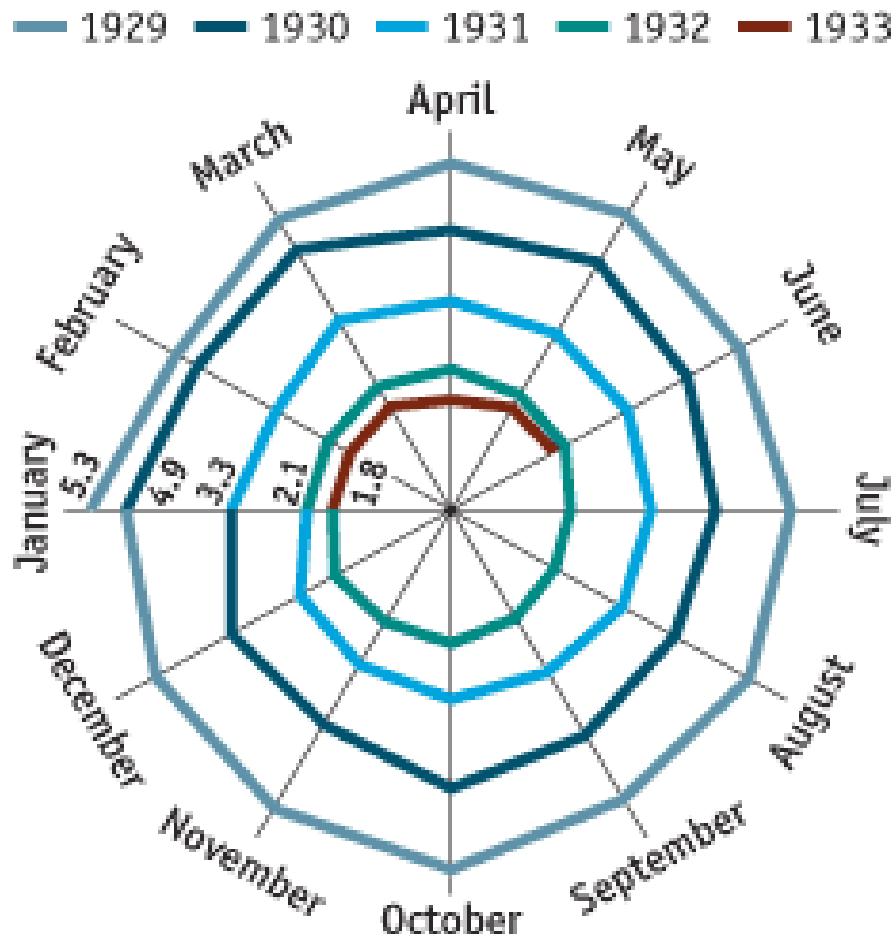
There is no doubt that the defensive measures adopted worldwide and the failure of international cooperation to overcome them contributed to the collapse of world trade. Indeed, after the crash of 1929, the natural reaction from several core countries was to close themselves except in their sphere of influence. As the League of Nations (1942b, p. 138) analyses, the closing of the established channels of trade and the breakdown of the worldwide multilateral system of settlements provoked attempts by many countries to develop their exchanges of goods and realize a system of settlement within restricted areas. Similarly, Eichengreen & Irwin (1995, p. 2) affirm that the traditional pattern of multilateral settlements was supplanted by a set of increasingly compartmentalized trade flows. Commercial policies channelled trade flows into self-contained regional, colonial and commercial blocs, which provided an opportunity to exploit scale economies by expanding output and increasing market shares through trade

¹²⁰ See Romer (2003, p. 3).

¹²¹ See Irwin (2012, p. 100).

diversion¹²². Trade blocs followed a similar setting as with exchange regimes. In the UK influential groups advocated protection and new and enhanced markets and the achievement of imperial preferences within the British Empire¹²³. The French pursued their policy of low tariff rates on trade with their colonies and enacted a particularly devastating quota system that had a bias against the US. And Germany focused on its commerce with the Balkans and Latin America¹²⁴. Accordingly, in the literature the main blocs were led by France, Germany, the UK and the US.

Figure 2 Breakdown of world trade 1929-1933 (billion US dollars)



Source: World Economic Survey 1932-1933, League of Nations (1934c).

¹²² There are other possible explanations. According to Chase (2004, p. 196), the formation of protectionist trade blocs in the thirties was a political response to the emergence of new technologies that demanded larger markets. Trade blocs were most attractive to firms that could not assimilate the mass production techniques developed in the pre-war era because of small national markets. Firms with sizable domestic markets for their goods already produced on a large scale, and were less interested in exclusive tariff privileges abroad. Small-scale producers with small domestic markets in Japan, the UK and Germany vigorously advocated the formation of protectionist trade blocs. However, large-scale firms in the US, with a vast continental market at their disposal, sought trade liberalization. Instead of seeking a trading bloc of their own, these firms also pushed to eliminate commercial discrimination in foreign empires.

¹²³ The British Empire comprised the dominions (Canada, Australia, New Zealand, Newfoundland, the Union of South Africa, and the Irish Free State, among others), colonies, protectorates, mandates and other territories ruled or administered by the UK.

¹²⁴ See Bancroft & Woolsey (1952, p. 800).

Table 2 Decline in average gold export prices, 1929-34 (per cent)

Raw silk (Japan)	84	Mechanical wood-pulp (Finland)	61
Copper (United States)	75	Wool (Argentina)	57
Butter (Denmark)	73	Sugar (Czechoslovakia)	57
Wheat (United States)	71	White cotton piece-goods (UK)	54
Grey cotton tissues (Japan)	68	Cement (Germany)	54
Petrol (United States)	68	Passenger motor-cars (US)	53
Coffee (Brazil)	68	Bacon (Denmark)	52
Rubber (British Malaya)	66	Tea (Ceylon)	48
Newsprint paper (Canada)	65	Pig-iron (UK)	47
Maize (Argentina)	65	Coal (UK)	39
Silk tissues (France)	64	Steel girders (Belgium)	36
Cotton (United States)	63	Tin (British Malaya)	32
Chilled beef (Argentina)	61	Mowing machines (Germany)	14

Source: Royal Institute of International Affairs (1937, p. 288) using data from the Review of World Trade, League of Nations (1934, pp. 14-15).

The American Smoot-Hawley tariff enacted in June 1930 is probably the most commented-on change of policy after the crash of 1929. Although dozens of countries had raised their tariffs after 1929 and the Smoot-Hawley Tariff was only the most prominent of them¹²⁵, its timing and contribution to the process of compartmentalization of trade place this bill as the equivalent in trade to the crash of 1929 in the financial system. At the same time, it was a defensive reaction by the US as the country most affected by the depression. According to data from O'Brien (2001), it raised the tariff by about 2 ½ percentage points to an average of 41.1% from the already high rates prevailing under the Fordney-McCumber tariff of 1922. However, this average hides the fact that some groupings of products were increased more than others, notably chemicals (29.7% to 36.1%), sugar (67.9% to 77.2%) and agricultural products (22.7% to 35.1%). As it passed the House of Representatives in May 1929, boycotts broke out and foreign governments moved to retaliate against US products¹²⁶. Extensive increases in duties were made almost immediately by Canada, Cuba, Mexico, France, Italy, Spain and Switzerland. For example, Italy objected to duties on hats and bonnets of straw, wool-felt hats, and olive oil; Spain reacted sharply to increases on cork and onions; Canada took umbrage at increases on maple sugar and syrup, potatoes, cream, butter, buttermilk and skimmed milk. Switzerland was moved to boycott American typewriters, fountain pens, motor cars and films because of

¹²⁵ See Eichengreen & Irwin (1995, p. 2).

¹²⁶ See Kindleberger (2002, p. 283).

increased duties on watches, clocks, embroidery, cheese and shoes¹²⁷. The tariff war initiated after the Smoot- Hawley Tariff continued to feed on itself, stimulated by the decline of world trade. Also, the effect of the depression on the balances of payments of individual countries resulted in the adoption of defensive measures that further aggravated the situation¹²⁸. As Milder (1999, p. 14) concludes, although the US tariff was not the cause of the Great Depression, its timing bears the responsibility for inaugurating a ‘parade of protection’ that ruined international trade during the thirties, of which the delayed retaliation of Great Britain, France and Germany was the most damaging.

Only after some initial hesitation, the Democrat administration of President Roosevelt decided on a reversion of the previous protectionist stance. Indeed, the Reciprocal Trade Agreements Act (RTAA) of June 1934, of which the Secretary of State Cordell Hull was an important advocate, authorized the President to reduce American tariffs. But, he could not reduce any duty by more than 50%. It also provided that any reductions of duties should be extended automatically to all other countries under the unconditional most-favoured-nation principle. With the proviso, however, that the President could withhold such benefits from countries which discriminated against American commerce¹²⁹. Furthermore, it prompted the negotiation of non-most-favoured-nation bilateral tariff agreements with selected countries¹³⁰. Although it is true that this Act started a policy of reducing US tariffs, such a policy made slow progress. That was due to the strong tariff wall built over the joint effect of the Smoot-Hawley Act itself and the deflation-induced increase in the incidence of specific duties¹³¹, as well as the compensating advantage of the abandonment of the gold standard and the devaluation of the dollar in April 1933. In Latin America, the US decisions translated into the ‘Good Neighbour’ policy, which, as the US Secretary of State Cordell Hull explained during the VII Inter-American Conference in Montevideo at the end of 1933, included the reduction of customs barriers. That measure was implemented by means of the negotiation of reciprocal bilateral treaties and the principle of equal treatment, among others.

Meanwhile, protective measures were imposed on Europe, as tariffs were supplemented by import quotas and licenses to favour particular countries or territories. In this regard, the League of Nations (1942b, pp. 67-68) explains that the adoption of quotas as an integral part of the French bargaining apparatus in the autumn of 1933; the adoption of agricultural quotas in England in 1933; and the New Plan introduced in Germany in the autumn of 1934 were

¹²⁷ See Kindleberger (1973, p. 132). For more examples of protectionist measures during this period, see also Kindleberger (2002, p. 282), Jones (1934), Chalmers (1953), and League of Nations (1942b).

¹²⁸ There is no consensus, however, on the real influence of this tariff in the global depression. The literature tends to agree that it was at least a contributing factor. Irwin (2012, pp. 15-16) doubts that it was a major cause of the Great Depression because of the modest increment on the tariff (38% to 45% on average) and the relatively low significance of the US for European exports (6%), although it did foster resentment in Europe and the spread of discriminatory policies. And Johnson (1997, p. 175) believes that the deflationary influence of Federal Reserve monetary policy almost certainly outweighed any countervailing influence from trade policy, among other reasons because historical data offer little support for the conclusion that the Smoot-Hawley tariff raised relative prices or increased relative demand in the US.

¹²⁹ See Schnietz (2000, p. 437).

¹³⁰ See Eichengreen & Irwin (1995, p. 2).

¹³¹ See Díaz Alejandro (2000, p. 19).

measures that contributed to consolidating the planning of foreign trade as a normal function of the government. Countries were very inventive and the proliferation of trade barriers was supplemented or even surpassed by exchange controls as the main instrument of trade restriction. Quantitative regulation tended to take the form of trade prohibition, mitigated in varying and uncertain degree by special permissions to import limited quantities of particular commodities from certain countries during a brief period. Quotas were preferred to tariffs because they brought more immediate and direct results in terms of effectively insulating domestic markets. Of course, they also proved to be highly destructive of trade ¹³².

In the British Commonwealth, the protectionist forces were on the move from the First World War onwards. Seeking a solution in Empire self-sufficiency, they fuelled a growing concern about foreign industrial rivals and increasing competition in trade. These forces achieved their goal during 1931-1932. The Abnormal Importations Act of November 1931, complemented a few weeks later by a similar Horticultural Products Act, allowed for duties of up to 100% on certain items, although only 50% were imposed. Later the Import Duties Act of February 1932 imposed a 10% tariff on all goods except those specifically exempted. The fact that neither economic activity nor trade balance fell so much during the Great Depression in the UK before 1931, suggests that those acts were not really the result of the downturn, but of pressures originating during the twenties from the dominions that sought preferences, under the argument that protectionism elsewhere would render the UK an easy destination for foreign industrial products. Not surprisingly, in 1932 the Ottawa Agreements strengthened tariff preferences within this bloc. In exchange for concessions in primary products in the British market, the UK expected to obtain reductions in dominions duties on its manufacturers, but instead the dominions instructed their respective tariff boards to adjust the British preference tariff to a level that would make British producers competitive with domestic industry¹³³. In this respect, as McDougall & Hutt (1954, pp. 233-257) estimate that the average rate of tariff preference on Commonwealth imports from the UK rose from 6% in 1929 to 10-11% in 1937, and on the British imports from the Commonwealth from 2-3% to 10-12%.

The change in trade policies by the UK had a great impact in many countries that depended greatly on the trade with that country. Using as leverage the Ottawa Agreements, the British established a very successful trade policy with countries that depended strongly on its market by granting simple promises of not increasing tariffs and not reducing quotas on a limited number of basic products. Although the UK government made several concessions to foreign producers, they were not comparable to the advantages obtained by the British producers¹³⁴. Import quotas on industrial products were avoided, but quotas on agricultural products were introduced since 1933 and became an important element in the trade agreements concluded from that year onwards. Agreements were made between 1933 and 1936 with Argentina, Poland, France, all the Scandinavian and Baltic countries and the Soviet Union. These agreements provided for the

¹³² See also Eichengreen & Irwin (1995, p. 2) and Condliffe (1932/1933, pp. 652-653).

¹³³ See Kindleberger (2002, pp. 286-287) and Capie (1983, pp. 6-44).

¹³⁴ See González & Pollock (1991, p. 468).

purchase of definite quantities of certain British goods (e.g. coal) against quota privileges in the British market and, in some cases, the stabilisation or reduction of duties in either or both contracting countries¹³⁵.

Other countries resorted to the administration of the foreign exchange as a powerful trade distorting tool. With the collapse of the German banking system and the suspension of the gold standard in the UK in 1931, the tendency towards the forcible confinement of foreign exchange within borders was institutionalized in the widespread adoption of the system of 'blocked balances' unilaterally imposed by debtors in Central Europe (Germany, Austria and Hungary) and Latin America. Obstfeld & Taylor (2004, pp. 137-140) give a good description of the system. It allowed debtors to spare foreign exchange, by making debt payments with domestic currency placed in special, earmarked accounts. Then, the creditor might use those funds only in limited ways, e.g. for renewed direct investment in the debtor country or to buy more of the debtors' exports. An insolvent government might pay off debts into its 'blocked account' and then re-lend to itself out of the same funds. Inevitably, claims on such accounts soon began trading on the secondary market. Market rates diverged dramatically from the official par rates of the exchange-controlled domestic currency.

With this regard, the most notorious case is Germany, where a new conception of trade was closely associated with the development of exchange control. In September 1934, Dr Hjalmar Schacht, President of the *Reichsbank* and Minister of Finance under Adolf Hitler, announced his 'New Plan' which extended and centralized Germany's foreign-exchange controls. Sixteen different control boards allocated available foreign exchange for import transactions approved by the State. To facilitate trade under this regime of direct controls, bilateral clearing agreements were concluded with a number of countries. However, the resource to those agreements was not an innovation of the Nazi Germany. The first impulse towards the clearing agreements was given in 1931 when Germany's foreign creditors, and especially those in the US, began to call in their claims on Germany at an ever-increasing rate. The first came about on the initiative of Germany with the countries which themselves controlled their foreign exchange. By the end of the thirties some 25 countries had agreed to such arrangements and more than 80% of Germany's foreign trade was carried on with them. The development of a system of barter was particularly advantageous to Germany in its dealings with Latin American countries. Due to its ability and willingness to absorb or act as an intermediary for the sale of many of the raw products of which Latin America possessed an uncomfortable surplus, Germany was in a strong position to bargain on a barter basis with those countries. This system boosted Germany's trade with Latin America, especially with Argentina, Brazil, Chile and Uruguay¹³⁶.

¹³⁵ See League of Nations (1942b, pp. 74-75).

¹³⁶ See Irwin (2012, pp. 67-80), Rothermund (1996, pp. 68-69), Neal (1979, p. 39), Clark (1940, p. 169) and League of Nations (1942b, pp. 67-68).

ii. The failure of multilateral diplomacy

Although several attempts were made by the League of Nations to accomplish a multilateral system with fewer distortions, probably the period of history that we chose to analyse can be remembered as a paradigm of the failure of international cooperation in various fields. Probably, after the First World War, a first sign of the lack of cooperation was the failure to arrange a convention of central banks after the Genoa Conference of 1922. However, from 1925 to 1928, the momentum of commercial restrictions that had grown up in the immediate post-war years slackened. The World Economic Conference of 1927, whose core trade recommendations included the reduction of tariff levels, contributed to a slight reduction of trade barriers for a brief period and the most-favoured-nation principle had been re-established¹³⁷. The League of Nations (1942b, pp. 101-102) summarizes the objectives of the great international conferences of the first post-Armistice decade:

- (a) the extension of the code of international commercial law, commercial arbitration, trade facilitation and the removal of legal, fiscal and administrative obstructions to trade;
- (b) the abolition of war-time trade prohibitions and controls;
- (c) the restoration of pre-war tariff practices;
- (d) the elimination of 'excessive' or 'artificial' rates;
- (e) a general reduction of tariff levels; and,
- (f) special agreements between some of the small countries of Central and Eastern Europe for the purpose of achieving (b), (c) and (d).

Unfortunately, after 1930 all major efforts to achieve multilateral agreements failed. The Convention for the Abolition of Import and Export Prohibitions and Restrictions, worked out at the two Geneva conferences of 1927 and 1928, did not achieve success for the deadline established in 1930. The so-called 'Tariff Truce Conference', which was considered a previous preparatory step to a movement of concerted tariff reductions that was expected ultimately to result in a general agreement to keep tariffs unchanged for several years, could not agree in 1930 on more than tentative promises to stabilize duties contained in existing treaties for one year. In parallel to these multilateral treaties and conferences' failures, there was increasing criticism of the most-favoured-nation principle built into most existing treaties¹³⁸. Regarding this, many countries defended new exceptions on the grounds that if the most-favoured-nation clause was insisted upon with too great rigidity, it might obstruct its own purposes given the juncture of crisis and hardship¹³⁹.

These disappointing results can be linked to the political and economic strains in the core countries that started to play a significant role in the disintegration of the gold standard system

¹³⁷ For a detailed review on the efforts to improve international cooperation, see for example the League of Nations (1942b and 1933b), Falkus (1971, p. 623), Chalmers (1953, p. 39) and Kindleberger (1973, 2002).

¹³⁸ Kindleberger (2002), Chalmers (1953, pp. 59-61) and League of Nations (1942b), among others, give an account of the rise and the demise of the most-favoured-nation principle during the interwar period.

¹³⁹ See the report of the Sub-Commission of Commercial Policy of the Conference in the League of Nations (1933b, p. 23).

and the trading system. The priority of trade in international negotiations lost ground to the increasing concern about the failure of the gold standard system, so that negotiations turned to address this issue. But in the background the political juncture prevented the functioning of cooperation among monetary authorities¹⁴⁰. Eichengreen (2004, p. 12 and 1990, pp. 149-150), for example, explains that during the pre-1913 gold standard central banks cooperated when setting interest rates and supported one another with emergency assistance in times of crisis, preventing the collapse in this way. That element was missing in 1931, when the Bank of France hesitated to assist its Austrian and German counterparts and the Bank of International Settlements was prevented from doing so for a time because of the dispute over reparations, Germany's program of building pocket battle ships and the proposal for an Austro-German customs union in contravention of the Versailles Treaty¹⁴¹. Ultimately, in a definite sign of the rise of nationalism, governments turned to non-cooperative strategies within the framework of an increasing departure from the gold standard.

In this difficult context, a World Economic Conference was convened in London from June 12th to July 27th, 1933, with the main issues in the agenda being the exchange rate instability, deflation, tariffs and external debts. There were sixty seven countries invited for the Conference and sixty four sent representatives (League of Nations, 1933a and 1933b)¹⁴². But the main players were the UK, the US and France. A Preliminary Commission of economic experts was assembled, but it was a rather one-sided representation of the views on monetary stability prevailing in the few remaining gold standard countries¹⁴³. This Commission wrote a Draft Annotated Agenda of the Conference for a concerted action, whose core objective was summarized as follows: “in the absence of another international standard likely to be universally acceptable, (the Conference) will have to consider how the conditions for a successful restoration of a free gold standard could be fulfilled”. To achieve this goal, it supported an increase in international cooperation, the reduction of the minimum cover ratios of central

¹⁴⁰ The argument about more cooperation does not necessarily imply a good outcome. For example, Temin (1989, p. 87) affirms that every effort was made in 1931 to preserve the gold value of the mark, pound, and dollar, but the outcome would have been better if the leaders followed Britain's example in 1931 and joined in devaluing their currencies. But at the time the only kind of cooperation possible was under the gold standard orthodoxy. Cooperation, in other words, is not good in and of itself. Its usefulness depends on the purposes to which cooperation is bent.

¹⁴¹ For an account on the role of the Versailles Treaty in the failure of cooperation in the financial field and its influence on the financial panic in Austria, Germany and other countries, see for example Rothermun (1996) and Irwin (2012). John Maynard Keynes produced in 1919 a highly influential critique of the French reparations policy that he believed weakened Germany and posed a tremendous danger to Europe. Kindleberger (1973, p. 150) doubts that the French bank pulled their money from the Austrian Credit Anstalt bank on the instructions of their government. Clavin (2000, p. 26) insists that eventually, the Treaty of Versailles came to be vilified as the origin of both the Great Depression and the Second World War.

¹⁴² The invited countries were: Abyssinia, Albania, Argentina, Australia, Austria, Belgium, Bolivia, Bulgaria, Canada, Chile, China, Colombia, Cuba, Czechoslovakia, Denmark, Dominican Republic, Ecuador, Egypt, Estonia, Finland, France, Germany, Greece, Guatemala, Haiti, Honduras, Hungary, India, Iraq, Irish Free State, Iceland, Italy, Japan, Latvia, Liberia, Lithuania, Luxemburg, Mexico, Netherlands, New Zealand, Nicaragua, Norway, Panama, Paraguay, Persia, Peru, Poland, Portugal, Romania, Salvador, Saudi Arabia, Siam, South Africa, Spain, Sweden, Switzerland, Turkey, United Kingdom, Uruguay, Venezuela, Yugoslavia. Also Afghanistan, Brazil, Costa Rica, Danzig, the USSR and the United States participated as non-member states of the League of Nations.

¹⁴³ See Cassel (1936, pp. 106-107).

banks, and suggested that certain countries operating with currencies at par should alter their parities to a permanently lower level. That naturally required a termination of exchange restrictions and clearing agreements, which allegedly constituted an obstacle to the circulation of capital, and represented one of the main causes of the collapse of international trade. The Agenda also called for a revision of specific duties and supplementary duties and charges of an administrative, statistical or other nature that were levied on imported goods. It also called for a return to a reasonable degree of freedom in the movement of goods and services and the creation of a unified customs nomenclature. Another main suggestion was the use of the unconditional and unrestricted most-favoured-nation clause as the basis of commercial relations between nations¹⁴⁴.

Regarding the balance of national interests pursued in order to ensure the success of the agreement, according to Kindleberger (2002, pp. 295-296), the preparatory Commission fashioned a package in which the US would lower the Smoot-Hawley tariff, France would reduce quota restrictions, Germany would relax the foreign exchange control and the UK would stabilize the pound. War debts were excluded from the Agenda by the US, and consequently reparations by France and the UK. However, all these recommendations were made at a time of key changes in the US policy. Indeed, in his first inaugural address President Franklin Roosevelt on March 4th, 1933 had said: "I favour as a practical policy the putting of first things first (...) I shall spare no effort to restore world trade by international economic readjustment but the emergency at home cannot wait on that accomplishment". Then, on April 5th, 1933, the US went off the gold standard and the dollar was devalued. A few months later and just at the beginning of the London Conference of 1933, Roosevelt signalled his rejection of the rhetoric of the gold standard in his remembered 'bombshell' message of July 3rd 1933 that condemned the "old fetishes of so-called international bankers" for the gold standard and underlined his commitment to currency depreciation as a means of invigorating the international economy. The President added that "(...) the world will not long be lulled by the specious fallacy of achieving a temporary and probably an artificial stability in foreign exchange on the part of a few large countries only (...) the sound internal economic situation of a Nation is a greater factor in its wellbeing than the price of its currency". This statement, and others, did not contribute with the prospects of the Conference, and really boycotted its success¹⁴⁵. The message demonstrated Roosevelt's growing frustrations with European nationalism. France had persisted with its advocacy of gold standard orthodoxy, while Britain continued to call for the abolition of war debts. Britain also rejected the Secretary of State Cordell Hull's ground-breaking proposal for a RTAA between Britain and the US based on a flat rate reduction of 10% of existing barriers.

The most cited cause for the failure of the World Economic Conference is the impossibility of agreement among countries that continued under the gold standard with fixed exchange rates

¹⁴⁴ See Angell (1933, pp. 9-66).

¹⁴⁵ Many authors have commented on the negative impact of President's Roosevelt statements on the London Economic Conference. See for example Traynor (1949, pp. 104-105), Clavin (1992, pp. 306-308) and Eichengreen & Temin (2000, p. 205).

and those that were not under that system, such as the US and the countries under the sterling. The latter questioned the feasibility of returning to the gold standard, at least in the medium-term. For them, those countries with *laissez-faire* policies were at the mercy of the whimsical character of international capital flows and other countries' policies, so that they could not manage adequately their own economies and pursue their own objectives¹⁴⁶. The stabilization became the pivot of discussions and disagreements and prevented the discussion of most of the issues outlined in the agenda, including trade¹⁴⁷. From another perspective, Eichengreen & Uzan (2002, pp. 112-116) argue that the failure was the result of domestic politics and different conceptual frameworks. Policymakers were unable to agree on a concerted response to the economic crisis because they perceived it in very different ways. Lacking a shared diagnosis of the problem, they were unable to prescribe a cooperative response. For example, France attached priority to the restoration of international monetary stability, by which it meant the return to the gold standard by Britain and its trading partners and the removal of the exchange control by Germany and other Central European countries. The French also wished to preserve their freedom to use instruments such as tariffs and quotas which insulated them from financial and economic disturbances abroad. Britain's priority was reflation by means of a policy of cheap money, which implied freedom from external constraints. In contrast to France and Britain, there existed no dominant economic model in the US. Even with a purely monetary agreement ruled out, conceptual differences did not in principle preclude a cross-issue deal involving monetary concessions by Britain, tariff concessions by France, and war-debt concessions by the US. But such cross-issue agreement foundered on domestic politics, primarily the opposition of French agriculture to trade liberalization because of the structure of domestic political institutions and vested interest groups with considerable leverage. However, this is not a consensual explanation. For example, Kindleberger (2002, p. 296) blames the failure not on France, but on the refusal of the US to stabilize the exchange rate of the dollar.

In America, however, there were some modest advances regarding cooperation. In order to prevent further disintegration of world markets and to restore multilateral trade, the VII Inter-American Conference held in Montevideo, Uruguay, on December 1933, decided to reduce the high trade barriers through the negotiation of comprehensive bilateral reciprocity treaties based on mutual concessions, including the most-favoured-nation clause. However, the agreement provided for no tariff reduction, was signed by eight countries and only ratified by the US and Cuba¹⁴⁸. But, this resolution was a precursor of the program of reciprocal trade agreements on which the US government was authorized to embark by the RTAA¹⁴⁹. Also accordingly, the most significant long-term development of 1933 in South America was the quickened movement of reciprocal trade negotiations, which usually included exchanges of substantial import duty concessions. Examples of this were the considerable measure of free trade achieved in the agreements between Argentina and Brazil and between Brazil and Uruguay on groups of

¹⁴⁶ See González & Pollock (1991, p. 464).

¹⁴⁷ See Traynor (1949, p. 109).

¹⁴⁸ See Kindleberger (2002, p. 301).

¹⁴⁹ See League of Nations (1942b, p. 74).

each other's distinctive products. However, modest progress was reported on the tariff agreements worked in the Tripartite Economic Conference of 1931 among the three countries¹⁵⁰.

In order to summarize, it is possible to say that from 1930 to 1933, trade destructive instruments proliferated and the previously dominant perception of the gold standard as a warranty for stability faded. The Conference of 1933 was the last attempt to obtain a multilateral solution to the several world economic problems. Simply expressed by Eichengreen & Uzan (2002, p. 212), that Conference was a classic example of the failure to achieve international agreement. In spite of prior politically correct statements, the fact is that no useful decision was made. As a consequence, the failure of cooperation is probably the most outstanding characteristic of this period of history.

iii. Latin America: a lottery ticket

In line with our previous analysis of the worldwide experience, it is possible to agree with Eichengreen & Sachs (1985, p. 928) that the reasons for Latin American countries' difficulties were the decline in US foreign lending starting in 1928, the fall of primary commodity prices which accelerated dramatically in 1929 and the imposition of protective tariffs by industrial countries, notably on their imports of foodstuffs. But that outcome was possible because of the strong patterns of economic dependence from core countries and the weakness of internal markets¹⁵¹. Indeed, the standard paradigm at the time is that Latin America was a dependent area, tightly attached to the world economy and led by changes in spending and lending in Europe and the US. The gold standard also played a role. Latin American countries were affected by the outflow of gold reserves due to capital withdrawal in the framework of the previously mentioned asymmetry among countries experiencing balance of payments deficit and surplus. The combined effects of reducing trade receipts and gold outflows depleted Latin American gold reserves and forced a generalized suspension of the gold standard in 1931 and devaluation of currencies, as well as the imposition of exchange controls and debt defaults in many of those countries¹⁵².

The lack of trade autonomy of some countries is evidenced by, for example, the enormous vulnerability of Argentina's open economy to the evolution and needs of the capital and trade flows with the UK. Similarly, in Mexico the effect of the Great Depression was felt as much through low prices transmitted into the economy as through a lack of foreign exchange. The concentration of trade and ownership of productive assets by US nationals and the fact that goods could move freely between both countries, ensured that the falling prices were transmitted directly from the US to Mexico¹⁵³. The overall vulnerability is evidenced for example by Chile, El Salvador, Mexico or Peru whose export prices fell more than 50% and

¹⁵⁰ See Chalmers (1953, pp. 119-120).

¹⁵¹ See Kindleberger (2000, p. 275). Also Bethell (1994, p. 75) and Bulmer-Thomas (1994, p. 196).

¹⁵² See Temin (1993, pp. 93-94).

¹⁵³ See FitzGerald (2000, pp. 217-218).

export volumes more than 25% and the purchasing power of their exports was reduced by more than 50%¹⁵⁴. By contrast, there was no significant contraction in the Venezuelan indicators of foreign trade during the first years of the depression due to the performance of petroleum. Between 1928 and 1935 coffee underwent a fall of 50% in export prices, damaging countries such as Brazil, Colombia, Costa Rica and Guatemala¹⁵⁵. In any case, during the early stages of the crisis, the import quantum fell even more than the purchasing power of exports in most countries¹⁵⁶. The dependence on foreign capital and trade flows explain the fact that the downturn in many Latin American countries started in the second half of 1928 due to, as mentioned, the drought of foreign loans and weak commodity prices, and not after October 1929. The contraction of trade arrived just when they were struggling to meet debt obligations in spite of the cessation of capital inflows.

Regarding capital flows, during the twenties the US invested abroad a large surplus of its national product, with Latin American countries as an important destination for those investments. This country was making rapid headway in, for example, Peruvian and Chilean copper, Cuban sugar, Argentine chemical and pharmaceutical industries as well as in the Central American economies¹⁵⁷. It also consolidated its position as an increasingly important lender to municipal, state and national governments. However, as we have seen, by 1928 this trend reverted. The boom in the stock market before the Wall Street crash led to excess demand for credit and a rise in international interest rates, increasing the cost of holding inventories and reducing demand for many of the primary products exported by Latin America. The interest rates upswing boosted additional pressure on Latin America through the capital market when the more attractive rates of return offered in London, Paris and New York prompted a significant capital flight because of higher interest rates outside the region. The stock market crash in October 1929 provoked a chain of events in the main markets supplied by Latin America. The contraction in the value of financial assets reduced consumer demand through the so-called wealth effect; loan defaults led to a squeeze on new credit and monetary contraction and the whole of the financial system came under severe pressure. And although interest rates started to fall in the fourth quarter of 1929, importers were unable or unwilling to rebuild stocks of primary products in the face of credit restrictions and dropping demand¹⁵⁸. Countries such as Argentina, Brazil and Colombia were affected by the abrupt halt in foreign lending. According to Kindleberger (1973), in 1928 the American loans to Latin America declined 7.8% in relation to the previous year and in 1929 there was a further contraction of 46.8%. But the US was not the only contributor. The UK was also an important source of investment and capital, as the report of the Study Group of Members of the Royal Institute of International Affairs (1937, p. 142) illustrates. It found that among the British long-term investments overseas in 1930, South America was ranked second with 20.8% of the total, after the British Empire (59%). That is why

¹⁵⁴ See Viales (2000, p. 99).

¹⁵⁵ See Astorga (2003, pp. 642-643).

¹⁵⁶ See Díaz Alejandro (2000, p. 18).

¹⁵⁷ See Thorp (2000, pp. 3-4).

¹⁵⁸ See Bethell (1994, p. 75).

the reduction of loans from the UK to Latin America by 23.8% in 1928 in relation to the previous year and 18.8% in 1929 heavily impacted South America. The impact was especially strong in Argentina, Brazil, Chile and Uruguay because of the deep rooted British interests there.

Regarding trade, an era of export-led growth culminated early during the thirties. In some countries, such as Chile, Cuba and Brazil, the limitations of external demand for the traditional staple had become clear by the late twenties, although some years witnessed unprecedented export booms. Export flows were predominantly rural (such as coffee and livestock) and mining products¹⁵⁹. The concentration of Latin American exports was remarkable during the period 1913-1928 in ten main products: petroleum, coffee, maize, sugar, meat (bovine or ovine), wheat, flour, copper, cotton, wool and hides. Some countries had a clear tendency to monoculture, as the Central Americans, whereas others had a greater diversity of exports, as was the case of Argentina and Mexico. In most of the countries the four main export products represented more than 50% of total exports¹⁶⁰. Consequently, each country in the region was heavily affected by the price variability of its relevant commodities. In other words, they were highly vulnerable to what Díaz Alejandro (2000) called the 'commodity lottery', a term used to indicate that economic cycles depended on the nature of the commodity that a country produces for exportation: e.g. its ownership, production function, linkages, demand conditions and marketing¹⁶¹. Indeed, the behaviour of many commodities before the Great Depression was already showing a declining performance, so that when the depression really hit, the contraction was more damaging. The prices of agricultural products and minerals had been slipping since 1925 as European production after the war added to expanded wartime supplies outside Europe. Cobwebs in some products, especially sugar and coffee, led to excessive responses to post-war price increases. While the production of minerals -petroleum, copper, lead, zinc and Asian tin- also had expanded dangerously, some countries accumulated stocks to keep prices high in products such as coffee and linseed. Thus, Latin America contributed to this expansionary trend on the supply side, which eventually fuelled the collapse of prices and prevented the economies from recovering faster¹⁶². However, natural events in the North sometimes contributed to ameliorate this problem, as was the case of the droughts in North America that favoured exporters of temperate foodstuffs¹⁶³. In general, Brazilian cotton, Argentine maize, Peruvian and Colombian gold, Mexican silver and Venezuelan petroleum are examples of generally 'lucky' staples in the 'commodity lottery'¹⁶⁴.

¹⁵⁹ See Díaz Alejandro (2000, pp. 16-17).

¹⁶⁰ See Viales (2000, pp. 92-93).

¹⁶¹ See also Kindleberger (2000, p. 276).

¹⁶² See *Ibid.*, p. 274.

¹⁶³ See Kindleberger (1973, p. 93).

¹⁶⁴ See Díaz Alejandro (2000, pp. 17-19).

In Table 3 we show the Latin American countries' dependence on a few main export products and we also illustrate the strong contraction of commodity prices¹⁶⁵ between 1928 and 1932. It is possible to conclude that according to these sources and our research in terms of export prices' slump the most affected economies were: Argentina, Brazil, Cuba, Guatemala, Peru and especially Uruguay with contractions of more than 60%, above the average fall for the region (55%). Furthermore, as aforementioned, Argentina and Mexico present a productive structure more diversified than the remainder of the Latin American countries, followed by Peru and Uruguay. Although not included in this table, it is important to note the relatively quick resort to the suspension of the gold standard in most Latin American countries, and in the face of currency depreciation and capital outflows, the imposition of exchange controls to prevent dollar prices of traditional exports from worsening further. Most of these countries also defaulted on their foreign debts. According to Reinhart and Rogoff (2009) Bolivia, Brazil, Chile, Dominican Republic and Peru defaulted in 1931; and Colombia, Costa Rica, El Salvador, Nicaragua, Panama, Paraguay and Uruguay in 1932-1933. Those defaults had a profound negative impact on subsequent capital inflows to the region, as many of them were not settled until well after the Second World War.

Table 3 Effects of the Great Depression in Latin America, 1932 (1928 = 100)

Country	Export prices	Main product (% total)	Other products
Argentina	33	Maize (25)	Wheat, meat, linseed, wool, hides
Bolivia^{c)}	79	Tin (84)	Silver, rubber
Brazil	38	Coffee (68)	Cocoa, rubber, cotton
Chile	47	Nitrates (43)	Copper, wool
Colombia	48	Coffee (64)	Banana, petroleum, gold
Costa Rica	54	Coffee (67)	Banana, cocoa
Cuba	37	Sugar (68)	Tobacco, rum, cocoa
Ecuador	51	Cocoa (32)	Petroleum, panama hats,
Guatemala	37	Coffee (74)	Banana
Honduras	91	Banana (50)	Wood, silver
Mexico	49	Silver (15)	Petroleum, beef, lead, coffee, banana, cotton
Peru	39	Petroleum (33)	Copper, silver, sugar, cotton

¹⁶⁵ For more detailed information about export prices and export volumes contractions see Bulmer-Thomas (1994, pp. 196-199).

Venezuela	81	Petroleum (82)	Gold, coffee, cocoa
Uruguay	27	Meat (33)	Wool, hides, linseed, wheat
Latin America	45		

Sources: Astorga (2003, p. 642) and Viales (2000, p. 93).

Notes: a) for Argentina, Brazil and Uruguay, figures from the League of Nations (see relevant chapters in this thesis), b) share in total exports in parentheses and c) Bolivia (1929=100).

The ‘commodity lottery’ was frequently affected by policies in the core countries. For example, the US support programmes for silver and agricultural commodities improved a few Latin American export prices, although sometimes at the expense of market shares, as with Cuban sugar¹⁶⁶. However, most policies were protective and damaging. Taylor & Taylor (1943, pp. 107-126) provide some examples of trade policy measures enacted by core countries that especially affected Latin American agricultural exporting countries, and in particular ABU. With regard to wheat, in the three most important wheat-importing countries of continental Europe (Germany, Italy and France) tariffs were increased several times since 1929. Furthermore, they imposed quantitative regulation on the demand of millers, who were forced to grind a certain percentage of domestic wheat. Private and cooperative holding of stocks was encouraged by cheap loans and subsidies, and complemented by state purchases on the grain markets. Then, in 1933 important restrictions were introduced when crops reached record levels, due in part to favourable weather conditions. Also the main customer of Argentina, the UK, imposed a tariff of 6.1 cents per bushel (at the old mint par) on foreign wheat, while it continued allowing the free entry of wheat from the Empire. In the case of feedstuffs, in 1929-1930, Germany increased its tariffs on barley and in 1930 introduced tariffs on bran and monopolized the maize trade by means of a National Maize Office. Meanwhile, France imperialized its imports of feed grains to a large extent through protective tariffs. In the UK, effective January 1st, 1933, the Ottawa Agreements imposed a duty on foreign flaxseed, and the tariff protection for Empire linseed oils was increased to 15% ad valorem. The US also raised the duty on linseed oil from 40 cent dollars per bushel in 1922 to 65 cents per bushel in 1930. In the case of wool, prices were depressed due to the devaluation of currencies in Australia and New Zealand. The Union of South Africa also introduced subsidies to wool exports by 25%. Meat suffered less during the depression because the UK imposed no new import restrictions until 1932, but in 1933 beef was subjected to quantitative regulation, closely affecting imports from South America. In the US, the Smoot-Hawley tariff of 1930 doubled the duty on beef, apart from the embargo imposed on countries affected by the foot-and-mouth disease in 1926, which particularly hit the exportation of Argentine and Uruguayan meats. In 1930 Germany restored the pre-war sanitary restrictions on imports of frozen beef and raised the import tariffs on slaughter cattle and meat; beef was charged 5.9 cents per pound in 1931 and as much as 10.8 cents in 1933 (old mint par), compared with 4.1 cents before the crisis. France applied high import taxes and quotas, which after April 1934 came near to being an import prohibition on foreign beef.

¹⁶⁶ See Díaz Alejandro (2000, pp. 17-19).

With regard to Latin American trade policies, it is possible to say that the Great Depression consolidated and supported trends that already had begun before 1929. During the twenties, the prime object of the duty increases in most of the Latin American countries was usually larger governmental revenues. However, there was a growing trend for a more or less selective protection to aid existing lines of production and to encourage diversification into new ones, agricultural as well as industrial. In some countries tariffs increases were imposed on manufactured products regarded as luxurious, such as automobiles, tires and petroleum products. In parallel, those duty increases were accompanied by the reduction or removal of duties on imports of machinery, industrial materials and in some cases foodstuffs, with the purpose of encouraging local economic development or keeping reasonable costs of living. Duties were combined with other restrictions and commercial instruments in order to improve balances of payments, to promote domestic development or to foster exports¹⁶⁷. The turmoil of the Great Depression deepened this trend, as the currency instability, the US Smoot-Hawley Tariff of 1930, the trade war that followed and the British abandonment of the gold standard in September 1931 forced many countries to protect their agricultural and raw material producing industries against the fall in world prices. Such protection was afforded by increased import restrictions or by currency devaluation in countries that were on an import basis with respect to the commodities concerned. In the case of Latin American countries, where the terms of trade were increasingly unfavourable in relation to manufactured products, there was increasing interest in crop control and valorisation schemes¹⁶⁸. Export-led growth and fluctuations gave way to import substitution in the form of manufacturing industry because of adverse balances of payments, and to more active stabilisation policies¹⁶⁹. As early as 1931, the suspension of the gold standard and to various degrees the expansionary fiscal and monetary policies, combined with imposition of exchange controls and tariffs, reinforced the stimulus to industry¹⁷⁰. This occurred in an accidental form, but ultimately led to deliberate industrialization policies¹⁷¹.

Following Díaz Alejandro and Seibert (1979, pp. 154-155) and Díaz Alejandro (2000, p. 22), it is possible to distinguish active large countries, active small countries and passive small countries, according to their size and the level of intervention in the economy. During the thirties the large and active economies of the region showed an impressive capacity for transformation, since they generated new vital sectors within the industry¹⁷². Large countries such as Argentina, Brazil, Colombia and Mexico lead the policy experiments. Small or passive countries such as Cuba, Honduras, Guatemala, Haiti and Dominican Republic, among others, were impotent regarding protection and nominal exchange-rate management. Those countries

¹⁶⁷ See Chalmers (1953, pp. 64-65).

¹⁶⁸ See Díaz Alejandro (2000, pp. 22-31).

¹⁶⁹ See Kindleberger (2000, p. 275).

¹⁷⁰ See Thorp (2000, p. 3).

¹⁷¹ See González & Pollock (1991, p. 464).

¹⁷² Díaz Alejandro and Seibert (1979, pp. 147-156) distinguish *active large countries*: Argentina, Brazil, Colombia and Mexico, leading the policy experiments; *active small countries*: Chile, Costa Rica, Peru and Uruguay who in spite of their size departed early from the orthodoxy of the free exchange and the gold standard; and *passive small countries*: Cuba, Dominican Republic, Guatemala, Honduras and Haiti essentially waited for a recovery based on their exports.

waited for a recovery based on their exports and resorted to import and exchange controls only sparingly. Cuba reduced tariffs in 1934, undoing much of the protectionist effect of its anomalous Tariff Act of 1927. In Mexico and Peru tariff rates underwent few changes in levels or structure, and behaved in a manner more like the smaller countries. By contrast, Brazil and the Southern Cone countries (Argentina, Chile and Uruguay) employed import and exchange controls in a more extensive way. Argentina, Brazil, Chile, Costa Rica, Colombia and Uruguay controlled trade along bilateral lines by means of exchange controls or clearing agreements. Such arrangements forced the canalization of trade bilaterally not by choice, but by the actions of European trading partners, and to the detriment of rival markets. Especially in Latin America, the composition of trade of many countries was altered by, for example, trading with Nazi Germany under ASKI ('compensation') marks¹⁷³. Colombia had an intermediate set of policies, as most of the changes in the prices of its imported non-traditional manufactures between 1927 and 1936 have been attributed to devaluation rather than tariff increases, although increments in effective protection stimulated some industries, including cement, soap and rayon textiles. Colombia also exercised import and exchange controls with greater vigour than Mexico and Peru.

Planned or not, juncture and policies led countries such as Argentina, Brazil, Chile, Colombia, Mexico, Peru and Uruguay to start a new stage of industrialization, which caused a change in the structure of imports, with a reduction of the consumption goods and an increase of intermediate and capital goods. New sectors started to grow such as chemical products, pharmaceuticals, metals and paper¹⁷⁴. As we have already discussed, this trend was later intellectually legitimized as the so-called model of 'import substitution industrialization' or 'ISI' promoted by the Economic Commission for Latin America (ECLA) created in 1948, under the influence of intellectuals such as Raúl Prebisch and Celso Furtado. As expressed by Bulmer-Thomas (1994, p. 232), the changes during the thirties can be seen as laying the foundations for a transition towards the genuine import substitution model, which reached its most extreme form in the fifties and sixties.

iv. The Financial Crisis of 2008: Déjà vu?

Until now we addressed the scenario during the thirties. However, before starting to address the cases of ABU, it seems appropriate to make a link to the present, so that we can shed more light on some of the elements that we have identified for the thirties in this chapter from our own contemporary experience.

The international financial crisis that started in 2008 has been signalled by the failure of the investment bank Lehman Brothers and the consequent crash of the US Stock Exchange. However, its roots are to be found much earlier. After the tech bubble burst of 2000-2001, the US Federal Reserve lowered the benchmark interest rate to a record level (from a yearly average

¹⁷³ See Obstfeld & Taylor (2004, pp. 137-140).

¹⁷⁴ See Viales (2000, p. 104).

of 6.24% in 2000 to 1.67% in 2002)¹⁷⁵, a decision that fuelled another bubble in the American real estate sector, evidenced by the fact that between 1997 and 2006 the housing prices in the US increased 124%¹⁷⁶. This occurred because credit was cheap and there were no barriers to prevent the money from being invested to excess into the housing market, which on top of that was perceived as a balanced option for savings that ensured profitability and security. The demand for loans increased and the banks multiplied their offer of mortgage loans, so that household debt increased 130% between 1997 and 2007¹⁷⁷. The problem was that a significant share of mortgages was granted to people with low incomes, which entailed a high risk of default. The financial system disregarded those risks, and by contrast securitized¹⁷⁸ those so-called ‘subprime mortgages’ with sophisticated financial instruments that mixed good and bad debt and hid the real risks they carried.

In 2007, the Federal Reserve decided to raise interest rates, so that those who purchased mortgage loans at variable interest rates were hit and a growing number of families failed to keep paying their mortgages. Consequently, home prices began to decline to a point at which the mortgage debt of a large number of families ended up bigger than the current value of their properties. As the housing bubble burst, the number of foreclosures rose nationwide. The property portfolios of the banks began to lose value as well as all derivatives that included mortgage loans as underlying assets. The banks stopped their lending operations because they lost confidence in the soundness of their counterparts, and as a consequence interbank rates such as the Libor and Euribor rose. On the other hand, financial speculators began to divert their investments to other markets such as raw materials and oil where profits were still available, pushing their prices up. In this way, the financial crisis in the US started to spread to the world economy¹⁷⁹.

In 2008 the situation worsened and many banks and financial institutions became insolvent. The bankruptcy of the giant investment bank Lehman Brothers in September 2008 became the most visible landmark of the financial crisis, but also many important firms such as Fannie Mae and Freddie Mac (mortgages), AIG (insurances) and Bear Stearns (investment bank) were in trouble as early as the end of 2007. By the end of 2008, all these firms were either nationalized or acquired by other companies (e.g. Bear Stearns was acquired by JP Morgan Chase). Many hedge funds sank and financial pyramids resembling ‘Ponzi’ schemes¹⁸⁰ came to light with the

¹⁷⁵ See the federal funds effective rate, in <http://www.federalreserve.gov/releases/h15/data.htm>, page visited in September 2012.

¹⁷⁶ This figure was taken from Skidelsky (2010, p. 5).

¹⁷⁷ This figure was taken from Torres López & Garzón Espinosa (2008, p. 2).

¹⁷⁸ Securitization is the process of bundling up individual mortgages into tranches of different risks which can be sold on by the originating bank (Skidelsky, 2010, p. 7).

¹⁷⁹ There were various analysts that predicted this outcome, among them, Nouriel Roubini, Joseph Stiglitz, Paul Krugman, George Soros, Stephen Roach, Robert Shiller and Robert Wescott; all of them Keynesian economists (Stiglitz, 2010, pp. 18-19).

¹⁸⁰ A Ponzi scheme is a fraudulent investment operation that pays returns to its investors from their own money or the money paid by subsequent investors, rather than from profit earned by the individual or organization running the operation. The Ponzi scheme usually entices new investors by offering higher returns than other investments, in the form of short-term returns that are either abnormally high or unusually consistent. Perpetuation of the high returns requires an ever-increasing flow of money from new investors to

prosecution of the well-known businessman Mr. Bernard Madoff. After the Lehman Brothers collapse, the stocks in the New York Stock Exchange experienced an abrupt decline during the period September-November 2008. The financial market was out of control as volatility and uncertainty reigned. 'Market manias' or 'irrationalities' are terms coined by Kindleberger & Aliber (2005) that describe quite accurately those events. The entire US economy began to collapse. Domestic demand fell as consumers found it increasingly difficult to gain access to credit and spent less. Global corporations underwent heavy financial losses, businesses and factories closed and the unemployment rate jumped to an unprecedented 10% in 2009 as workers lost their jobs in alarming numbers.

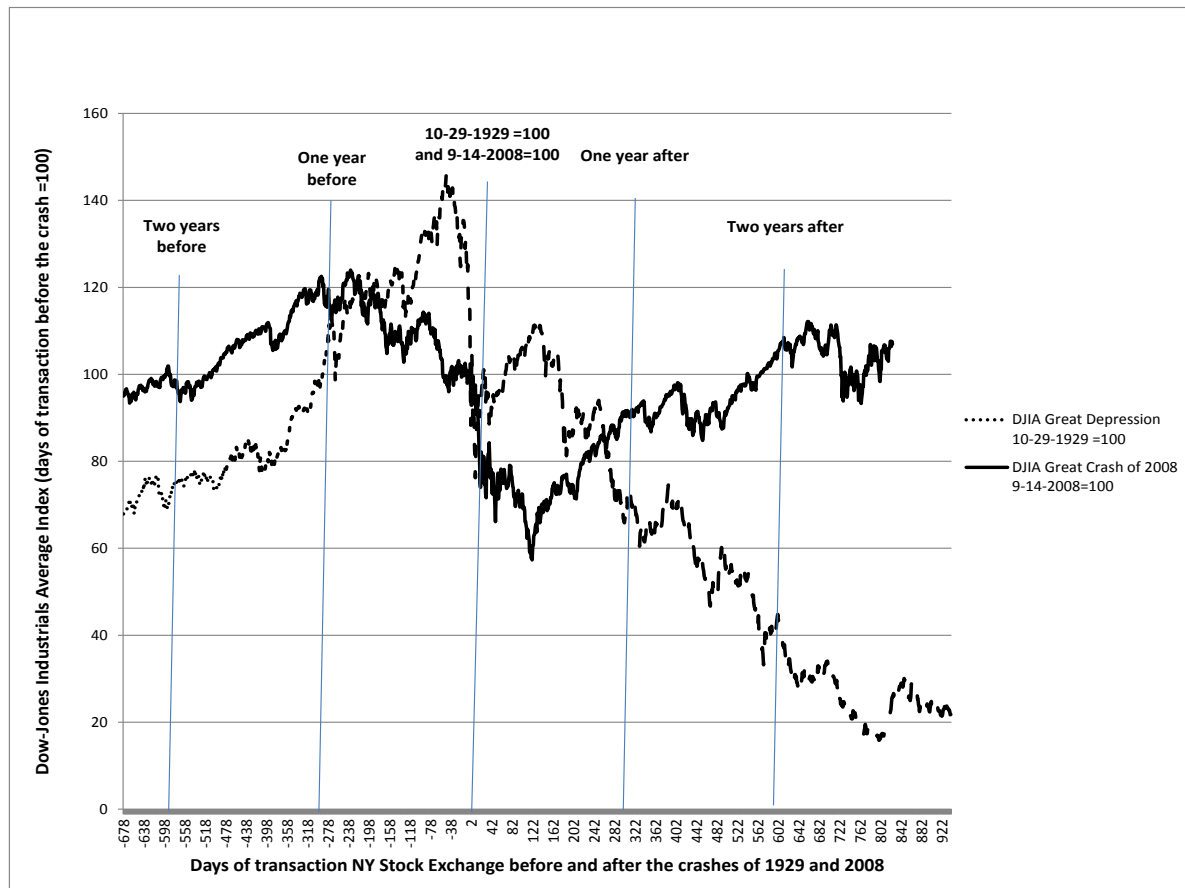
No-one has doubts about the similarities of recent history to our description of the Great Depression. As a matter of fact many analysts thought that the world was at the start of another economic depression, but the prediction did not materialize, at least not in the same way. As Sosa Clavijo (2010, pp. 60-61) argues, this time the stock market fell more sharply but also recovered faster. This assessment is consistent with the evolution of the Dow Jones Industrial Average of the New York Stock Exchange (DJIA) presented in Figure 3. The X axis includes the number of working sessions before and after the date considered as the landmark for each event (October 29th, 1929 and September 14th, 2008). The figure illustrates that the stock markets boomed in both events during the previous years, but the speculative bubbles eventually burst. However, the financial recovery was faster in the current crisis. Indeed, one year after the Great Depression's crash the DJIA had fallen 25.2%, while after the collapse of Lehman Brothers the market contraction reached 12.2%. However, two years later the DJIA had fallen 61.4%, while in the latest event it actually grew 3.5%. Otherwise, comparing the peak with the lowest point of the curves, the market fell 89.2% over 845 working sessions then and only 51.1% but over 357 sessions now.

In this context, some key lessons from the Great Depression guided policymakers. On the one hand, recalling Friedman & Schwartz (2008) the depression was the result of the Federal Reserve's policy failure in the aftermath of 1929 due to a massive monetary contraction that was responsible for the severity of the downturn and therefore they recommended that central banks should provide extra liquidity in such cases. On the other hand, John Maynard Keynes blamed the collapse in private demand as the main cause of the downturn and as a result he argued the urgent need for enhanced public sector demand and for fiscal activism. The US government followed these recommendations and applied more Keynesian policies and nationalized private debt and banks. Indeed, Figure 4 illustrates the evolution of the relevant US discount rate. The X axis includes the number of months before and after the month considered as the landmark for each event (October 1929 and September 2008). After December 2008 the Federal Reserve cut its benchmark interest rate to a record low target range of 0%-0.25%, much faster, sharper, deeper and sooner than in the twenties and thirties. It also applied a strong expansionary monetary policy, hoping that the greater liquidity would counteract the economic downturn, in a

keep the scheme going. "Ponzi Schemes – Frequently Asked Questions". See US Securities and Exchange Commission, US Securities and Exchange Commission. Retrieved June 23rd, 2012.

policy that is mostly in force nowadays. In addition, the government resorted to rescue packages or financial bail-outs to prevent key companies from going into bankruptcy. They were mainly financial and automotive companies labelled by the press as ‘too big to fail’¹⁸¹.

Figure 3 Great Depression and the Global Crash of 2008 in the NY Stock Exchange



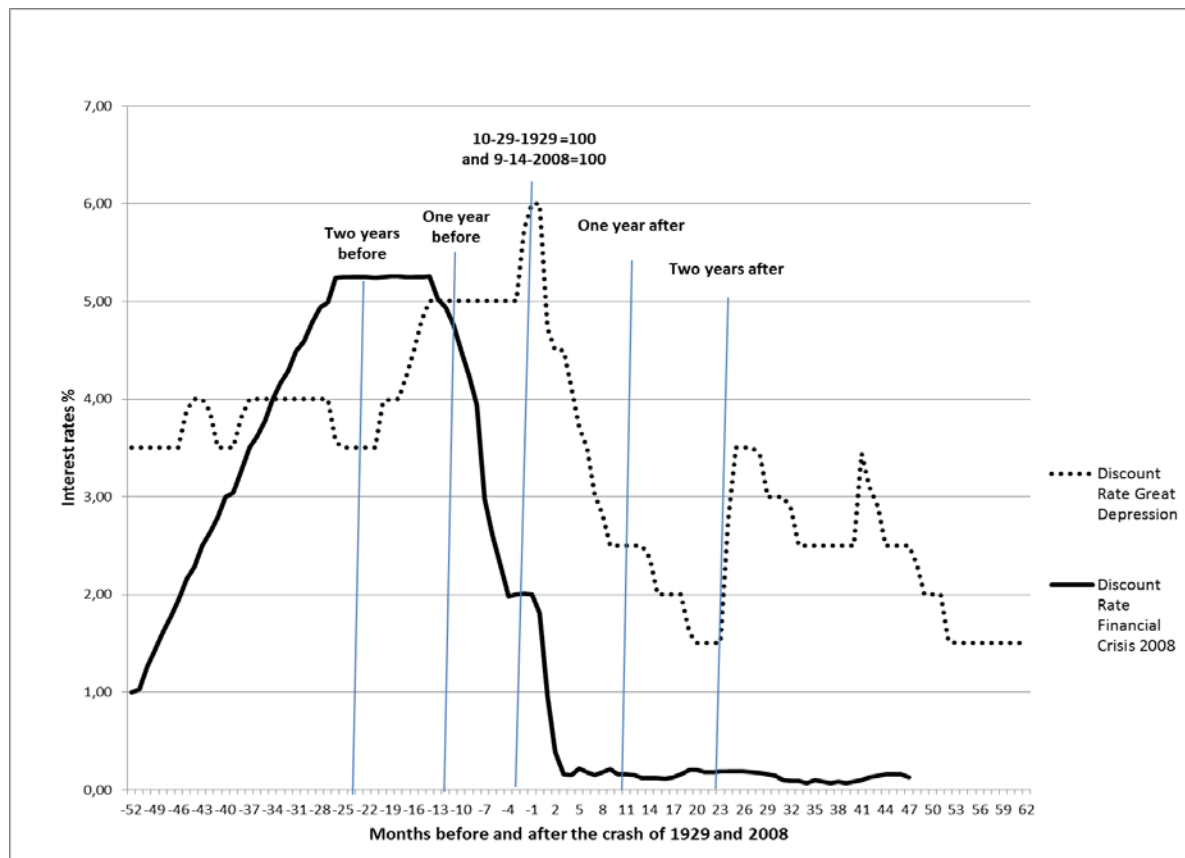
Source: calculated from Williamson (2011), “Daily Closing Values of the DJIA in the United States, 1885 to Present”, MeasuringWorth. URL: <http://www.measuringworth.com/DJA/>

By the end of 2008, stock markets fell worldwide, including the major Latin American economies of Argentina, Brazil and Mexico. The contraction of global demand negatively affected many economies, where trade contracted, levels of industrial production plunged, retail sales fell and unemployment rose. The transmission was truly global and in this aspect it is perfectly comparable with the thirties. However, this time the difference is that many countries followed the example of the US and applied active policies to avert the phantom of the Great Depression, although the actions were far from coordinated. While the European Union adopted limited remedies due to its confidence on automatic fiscal stabilizing mechanisms, China’s stimulus package was one of the largest in the world. The latter proved to be effective as the Chinese economy managed to grow and keep its dynamism. And this is a key element of

¹⁸¹ For more detailed information about the origins of the current crisis see for example Torres López & Garzón Espinosa (2008), Fresno (2009), Krugman (2009, pp. 165-180), Roubini & Mihm (2010, pp. 13-37), Stiglitz (2010, pp. 1-57) and Skidelsky (2010, pp. 3-51).

contrast with the Great Depression. Indeed, China has achieved in the last three decades an important role in the fields of production, international trade, foreign direct investment and gradual internationalization of its companies. It is also the world's major holder of foreign exchange reserves and public US debt held in US dollars. During the Financial Crisis of 2008, it is possible to say that the Chinese economy managed to take the role of locomotive from the US, so that the crisis in global terms was more a recession than a depression, a feature especially true for the period 2009-2010, and for our case studies. By contrast, the European countries paved the way for what is nowadays known as the crisis of the sovereign debt.

Figure 4 Discount rates of the United States



Source: Federal funds effective rate from the Federal Reserve System 2004 to date, and US Discount Rates, Federal Reserve Bank of New York from NBER.

Regarding the recovery, not surprisingly, those economies that have been increasingly dependent on trade and investment flows with China (e.g. Latin American economies and particularly South American ones) managed to recover faster. Even in Europe there were signs of early recovery that can be linked to Chinese resilience. For example, Germany, which suffered a strong real GDP contraction of 5.3% in 2009¹⁸², a figure even worse than the US, the UK and France, showed signs of recovery in 2010, and until today has prevented the European Union from falling even harder. However, in 2011 there was a growing concern about the possible default on the foreign debt of Ireland, Greece and Portugal, as well as the potential

¹⁸² This figure was taken from Sosa Clavijo (2010, p. 77).

failure of bigger countries such as Italy and Spain. Those fears provoked chaos in the global financial markets, the European stock exchanges became volatile and many questioned the long-term viability of the euro as the single European currency, and even the stability of the British pound. Thus, the answer to the question about the duration of both crises depends on how this episode of the sovereign debt is considered. If we limit our analysis to 2007-2010, the Financial Crisis of 2008 has been shorter and less strong. But, if it is considered as an on-going process of multiple stages, the outcome is already uncertain and the comparison relative and changing.

Another important difference is the institutional framework in which the international community has tried to coordinate the national responses and prevent the kind of trade war that erupted during the thirties. Although it is clear that states still operate under the rule of the national interest, certainly there is more international cooperation nowadays, evidenced by the high degree of institutionalization of international relations, a feature that can be analysed multilaterally and regionally. Regarding the multilateral level, the World Trade Organization (WTO), successor of the old GATT, has been in pursuit of open borders, the guarantee of most-favoured-nation principle and non-discriminatory treatment among members, and the openness of national markets to international trade, with justifiable exceptions or with adequate flexibilities. However, progression of multilateralism is slow, as it is evidenced by the Doha Development Round, and the alternative multiplication of bilateral, regional and interregional trade agreements relegated that in a way undermine the broader multilateral approach¹⁸³.

Another symptom of this trend was the quasi-recreation of the London Conference of 1933, although this time in the form of the group of the twenty largest economies of the world, also known as G20¹⁸⁴. This group met with the aim of coordinating a response to the Financial Crisis of 2008 and to avert the potential effects of a new Great Depression. In fact, by November 2008 the magnitude of the crisis was such that decision makers came to the conclusion that a high level of coordinated response was required. Thus, the US convened the G20, knowing that it represented developed and emerging economies, and that its relatively small membership allows agreements to be reached more efficiently. The leaders of those economies agreed to implement an action plan around three main objectives: restoring global growth, strengthening the international financial system and reforming the international financial institutions. Negotiations were difficult, and national interest prevailed. The summit of 2009 concluded that greater

¹⁸³ As the Director-General of the WTO, Pascal Lamy, said in a speech in October 2006, since the creation of the GATT and its successor the WTO, 362 regional trade agreements have been notified to the WTO, of which 211 were in force. But if we take into account agreements that are in force but have not been notified, those signed but not yet in force, those currently being negotiated, and those in the proposal stage, we arrive at a figure of close to 400 agreements that could be implemented by 2010. He added that there is a growing trend away from the traditional concept of integration among natural trading partners in geographically contiguous countries, towards cross-regional trade agreements among countries across regions and hemispheres. Examples abound, among them EFTA-Chile, US-Australia or EC-South Africa to name but a few. See http://www.wto.org/english/news_e/sppl_e/sppl46_e.htm, page visited in October 2012.

¹⁸⁴ The G20 was created during the nineties with the objective of achieving global economic stability and sustainable growth; to promote financial regulations that reduce risks and prevent future financial crises; and to create a new international financial architecture. It is integrated by: Argentina, Australia, Brazil, Canada, China, France, Germany, India, Indonesia, Italy, Japan, Mexico, Republic of Korea, Russia, Saudi Arabia, South Africa, Turkey, the UK, the US and the European Union. For more detailed information see www.g20.org, page visited in September 2012.

savings in European countries and the US were required, while in rapidly growing economies such as India and China, the request was more spending to boost the world economy. However, there were disagreements on the most adequate way of dealing with the crisis. Unlike France and Germany, the UK was reluctant to impose greater regulation on the financial system fearing that such proposals could damage the City of London as an international financial centre. Nevertheless, it is possible to state that the worst fears of a trade or currency war did not progress beyond a point of no return, and the role of the G20 in that outcome has been important.

Another aspect to highlight is the composition of the G20. Although it only includes nineteen country members and the European Union, they altogether represent around 90% of global GDP, 80% of global trade and two thirds of the world's population¹⁸⁵. However, from another point of view, it only comprises twenty economies of a total of the United Nations' 193 member states. For example, Uruguay took part in the London 1933 Conference, but it was not invited to the G20. Moreover, among the 34 Latin American and the Caribbean countries, only Argentina, Brazil and Mexico are members of this select group. Another big difference is the role of Brazil, which is a major player nowadays. During the presidency of the charismatic Luiz Inácio Lula da Silva, Brazil consistently advocated for non-protectionist policies by developed countries and a greater role for developing countries in the world economy. Moreover, this country is referred along with China, India, Russia and South Africa as one of the 'BRICS' countries, a term coined by the American firm Goldman Sachs in 2001 after concluding that those economies would constitute a significant share of the world's flow of trade and investment by mid-century.

But how can we summarize the analogies and differences between the global crisis of 2008 and the Great Depression? Table 4 presents those key elements for a comparative analysis. Both crises broke out in the US in a context of excessive liberalization and deregulation, which became global. In addition, in both events there was capital flight, credit crunch, contraction of GDP, increase of the unemployment rate and so on. However, the international financial scenario is much more complex because financial institutions tend to create more intricate and/or sophisticated instruments that hide real high risks and evade regulations. And whenever risky transactions derail, negative waves spread all over the world in seconds via the Internet. Another big difference is that while most of the economies had adopted the gold-exchange standard during the twenties, now those countries have more room to manoeuvre against foreign exchange instability because they enjoy a system of floating exchange rates. Although during 2008-2010 there was concern about a potential currency war -e.g. US dollar vs. Chinese yuan-, international cooperation in the framework of the G20 contributed to reducing the magnitude of competitive devaluations. By contrast, for that period, many countries suffered currency appreciations that contributed to curbing the ghost of high inflation. Meanwhile, trade wars and competitive devaluation –beggar thy neighbour– prevailed during the thirties.

Protectionist trends also emerged after 2008, although in a different modality. Baldwin & Evenett (2009, p. 4) coined the term 'murky protectionism', referring to measures that are not

¹⁸⁵ See <http://www.g20.org/index.php/en/the-origins-and-evolution-of-the-g20>, retrieved on September 2012.

direct violations of WTO obligations, but that constitute abuse of legitimate discretion and really discriminate against foreign goods, companies, workers and investors. For example, some of them are: the abuse of the health and safety regulations and some components of the stimulus packages that provide for the allocation of spending to domestic producers. In relation to protectionist measures, the ABU's dairy sector trade was negatively affected by the decision of the European Union to reintroduce the refunds (*reintegros*) to the exports and the incentives applied by the US to the exports of this type of products. Moreover, Brazil and Argentina, exporters of petroleum and petroleum products were affected by the decision of Russia and Bielorrusia to increase tariffs on these products. But also intra-regional trade was affected by this kind of protectionism. Brazil and specially Uruguay with its narrow market were affected by the imposition of non-automatic import licenses by Argentina in several sectors¹⁸⁶. Finally, the international political context is also different. While during the thirties the world was under the shadow of war and in particular Latin American countries went through a period of revolutions and regime changes, during 2007-2010 there were no major conflicts worldwide or in Latin America.

Regarding the experience of the Latin American countries in general, according to Ocampo (2009, p. 10) during 2003-2007 the region benefited from a combination of financial boom, rising commodity prices and high level of remittances from migrant workers. However, after 2008 the region was hard hit by the reduction in external demand, falling export prices, limited access to the financial system, capital flight and a high degree of uncertainty. The contraction of international trade was perhaps the most important transmission channel from the US and other core countries. Nevertheless, the magnitude of the impact of the crisis on each country depended on the importance of North America and Europe on their trade and capital flows. During 2008-2009 several economies with strong ties to the US or which were very close geographically, such as Colombia, Mexico, Venezuela and the smaller economies of Central America experienced a major slowdown.

In the meantime, and as already mentioned, in the early months of 2009 the expansionary policy implemented in the US and to a lesser extent in Europe contributed to boosting confidence in the determination of the authorities to do everything possible to prevent the failure of institutions with systemic scope. The monetary policy in several developed countries was aimed at restoring liquidity, and for that purpose they kept interest rates close to zero and offered certain guarantees for interbank lending to restore credit availability. Thus, in the first quarter of 2009 the perception of risk fell in emerging countries, and there was a renewed access to the international capital markets, which started to accept again sovereign and corporate bonds. However, and as Sosa Clavijo (2010, pp. 87-88) points out, the trade flows remained a concern. In comparison with the Great Depression, in both episodes the international trade contraction affected the Latin American countries more in value than in volume, due to the continuous dependence on a limited basket of products, or as the author recalls, the 'commodity lottery' that affected those countries. But there are some differences, because international commodity prices

¹⁸⁶ See for example Estrades (2009).

fell sharply during the twenties, whereas before 2009 the world economy enjoyed a boom that provided some cushion. Moreover, the Latin American economies are less vulnerable nowadays because their economies are more diversified in terms of their export baskets and the market destinations of their produce.

The Great Depression also meant for the peripheral countries of Latin America a major debt crisis. The year 1931 was dominated by Latin American defaults. By contrast, in 2008 the economies of the region entered into the financial crisis with a less vulnerable macroeconomic position, because of their lower external public debt in relation to GDP and the high level of international reserves. Latin American countries had reduced their debt levels strongly in previous years, and in some cases restructured their obligations in terms of maturities and rates. In addition, another favourable element is the composition of external debt. According to the International Monetary Fund (2009, p. 56) while in Europe and Asia most of the debt belongs to the banking sector, in Latin America it belongs to the governmental and non-banking sectors.

v. Conclusion

The Great Depression was the most difficult economic time for humanity, for at least a century. And if compared with our recent history, it includes a number of characteristics not present nowadays that justify the strength and persistence of its effects. Most Latin American countries first received the impact of the sudden halt in foreign capital on which they were dependent. The contraction of trade flows and the collapse of commodity prices added to and deepened the crisis to levels of unexpected proportions.

These elements were present both in the Great Depression and in the Financial Crisis of 2008, but in the past the international institutions that could give an adequate framework to settle disputes and conflicts of national interests were weaker. Every country reacted without any commitment to worldwide stability. Nowadays, trade retaliations and competitive devaluations are less evident, and the efforts of groups like the G20 during 2008-2010 were more efficient than the more comprehensive ambitious efforts of the League of Nations conferences.

The gold standard system, a feature unique to the thirties, together with the depression scenario, prevented governments from adopting more expansive policies at the right time. By contrast, for many countries it meant a monetary contraction at the worst time possible. Furthermore, standard policy instruments used currently to deal with the economic contraction were lacking in the past. The nowadays orthodox mainstream of Keynesianism, for example, was just developing. It was a heterodox trend difficult to accept at the time.

Table 4 Analogies and differences between both crises

Analogies (1928-1934 and 2007-2010)	
Crises broke out in the US in a scenario of frantic speculation and deregulation. Burst of a price bubble in the housing market and then in the stock exchange, resulting in a financial crisis.	
Economic activity contracted and unemployment rose.	
The crisis was transmitted abroad and became 'global'.	
The 'commodity lottery' was relevant.	
There was credit crunch and capital flight.	
Trade protectionism.	
The financial channel hit first Latin America, but the transmission was stronger via the trade channel.	
Foreign trade in Latin America contracted more in values than in volumes.	
Differences	
Crisis 1928-1934	Crisis 2007-2010
The international financial system was less integrated and interconnected than nowadays.	The global financial system is more integrated, sophisticated and globalized, but its opacity has reached unprecedented levels. Thus, the financial transmission was reinforced.
The shadow of war was present. The issue of war debts and reparations added complexity to international economic negotiations.	Regional conflicts did exist, but there was no prospect of a major conflict.
Most of the economies had adopted the gold standard.	Most of the economies had flexible or floating exchange rates.
With the drought of the US loans, international reserves fell abruptly and countries eventually defaulted on their foreign debt.	High level of international reserves allowed the partial offsetting of the shrinkage of the gross capital inflows, to keep paying foreign debt and to implement countercyclical policies.
During the twenties, there were periods of plunging prices of main export commodities.	Unprecedented growth in commodity prices during 2003-2007.
Contraction of key export commodity prices was prolonged and deep.	Export prices contracted mainly in 2009.
Public finances heavily depended on tariffs.	Government revenues are more diversified and less vulnerable to foreign trade shocks.
On average, public consumption contracted.	Public consumption increased due to the implementation of active fiscal policies.
Deflation.	Inflation.
Interest rates remained high.	Interest rates lowered faster and earlier.
The gold standard orthodoxy conditioned government responses.	Active fiscal and monetary policies.
Deep contraction of economic activity and employment worldwide.	Real GDP fell less than during the thirties.
Trade and capital flows were strongly dependent on the US, the UK, France and Germany.	Increasing dependence on the largest Asian economies, particularly China. Integration schemes have increased intra-regional trade.
Trade and currency war, 'beggar thy neighbour'.	Murky protectionism.
Major international conferences failed.	Several mechanisms of regional (e.g. Mercosur) and multilateral (e.g. WTO, G20) coordination.