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From Financial to Climate Debt

Changing Patterns of Political Economy in Latin America

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A tutte le persone che ho avuto la fortuna di conoscere,

e a tutti gli sguardi che devo ancora incontrare.

Yo no hablo de venganzas ni perdones,

el olvido es la única venganza y el único perdón

Jorge Luis Borges

Abstract

La strada verso lo sviluppo economico in America Latina è stata spesso tortuosa, non lineare. Diverse teorie economiche si sono avvicendate fin dai tempi della Grande Depressione, quando un nuovo modello di sviluppo cominciò a diffondersi tra i vari paesi del continente sudamericano. Per introdurre il tema dello sviluppo, una revisione delle teorie di politica economica che emersero nella regione è inizialmente proposta. Gli studiosi riconducibili alla corrente strutturalista cercarono di dimostrare come la struttura dell'economia internazionale fosse intrinsecamente legata allo sfruttamento delle risorse dei paesi terzomondisti, proponendo soluzioni che avrebbero sovvertito le condizioni che impedivano la crescita economico. Questo lavoro propone una spiegazione delle teorie strutturaliste affermatesi in America Latina, le quali posero le basi per quella che sarà la politica economica dei regimi populisti, definita come una industrializzazione guidata dallo Stato. Mentre alcuni studi si concentrarono sulla struttura asimmetrica ed ineguale dell'ordine economico internazionale, la quale tutelava la divisione gerarchica prodotta dal sistema capitalistico impedendo il pieno sviluppo delle aree periferiche, altri insistettero sulla necessità di una vera e propria rivoluzione socialista. Nonostante gli incoraggianti successi ottenuti dalle politiche protezioniste, l'esaurirsi della spinta industrializzatrice venne criticata degli stessi studiosi strutturalisti, i quali perfezionarono le loro tesi elaborando la "teoria della dipendenza." Gli anni sessanta e settanta del novecento rappresentano un periodo significativo nella storia dell'economia internazionale. In questi anni i mercati di capitale finanziario si espansero considerevolmente, così come la presenza delle compagnie multinazionali nelle economie emergenti dell'America Latina. Il consolidamento del mercato degli Eurodollari portò all'affermarsi delle banche e dei fondi di investimento privati quali principali attori del mercato finanziario globale. In questo contesto, vennero ideati nuovi strumenti finanziari che permettevano ai governi dei paesi in via di sviluppo di accedere alla liquidità proveniente dai grandi fondi statunitensi, europei e giapponesi. In America Latina la quantità di prestiti fu decisamente significativa, anche in virtù del processo di riciclaggio dei petrodollari ricavati dall'aumento del prezzo del petrolio. Tuttavia, la crescita del debito estero e la diminuzione del consenso nei confronti dei partiti populisti anticiparono la fine del modello di sviluppo guidato dallo Stato. Un nuovo approccio doveva essere intrapreso. Le teorie neoliberali ideate a Chicago, e parzialmente applicate per la prima volta in Cile, vennero adottate ovunque nel continente, anche se in maniera diversa e con maggior enfasi specialmente nei paesi del Cono Sud. Tuttavia, la proliferazione di regimi militari e dittatoriali in questi paesi non rispecchiava fedelmente le idee di liberismo politico che avrebbero dovuto sottintendere il passaggio all'economia di mercato.

All'inizio degli anni ottanta, la stagnazione economica e l'inflazione resero necessaria l'adozione di alti tassi di interesse per compensare la contrazione della domanda globale. Fu in questo momento che numerosi paesi dell'America Latina subirono un forte shock finanziario, poiché non furono più in grado di ripagare i prestiti contratti per sopperire al crescente prezzo del petrolio, e per finanziare lo sviluppo nazionale. La situazione andò peggiorando, dal momento che i paesi latinoamericani erano ormai talmente indebitati da ritrovarsi sull'orlo del default finanziario. Per salvare i paesi indebitati da quella che era evidentemente diventata un crisi di carattere internazionale (poiché coinvolgeva sia i paesi del "Sud" del mondo, sia le banche del "Nord"), le più importanti istituzioni finanziarie decisero di intervenire con una strategia che avrebbe permesso ai primi di dilatare i tempi di pagamento e di mantenere l'accesso alle risorse dei fondi stranieri, assicurando ai secondi che il pagamento del debito sarebbero stati rispettato grazie all'applicazione di riforme strutturali. Questi pacchetti di riforma strutturale includevano misure di austerità come il taglio della spesa pubblica e una disciplina fiscale più restrittiva, ma prevedevano anche la privatizzazione delle attività economiche che prima erano in mano allo Stato, e la liberalizzazione dei mercati di beni e capitali. Il Fondo Monetario Internazionale e la Banca Mondiale si dimostrarono di fatto fondamentali nell'avviare un processo di riforma economica che implicava il passaggio alle politiche neoliberali. Nonostante i vari tentativi di stabilizzare la regione attraverso i programmi di riforma strutturale, i bilanci dei paesi latinoamericani continuavano ad essere negativi. Per risolvere il problema il modello di crescita sarebbe dovuto cambiare in favore di uno sviluppo basato sulle esportazioni. Insieme all'affermarsi della democrazia, crebbe anche l'integrazione commerciale tra i vari paesi e aree del continente americano. Tuttavia, in America Latina la crescita economica si rivelò più lenta del previsto, mentre le disuguaglianze sociali si fecero sempre più evidenti. Nel contempo, alcuni paesi dell'Asia orientale avevano intrapreso una politica industriale che li avrebbe presto portati a migliorare drasticamente i propri indicatori economici e sociali. Le riforme di libero mercato adottate in America Latina non produssero gli effetti sperati e, anzi, spinsero moltissime persone a cercare lavoro e fortuna nelle città, di fatto peggiorando le condizioni di vita già di per sé critiche, e inasprendo le tensioni sociali. Il caso della Bolivia viene presentato come un chiaro esempio di come le politiche monetarie nazionali vennero stravolte con l'avvento della crisi del debito e di una delle sue caratteristiche più disastrose: l'iperinflazione. Le riforme neoliberali non fecero altro che rafforzare un modello di sviluppo basato sull'estrazione e l'esportazione delle materie prime; tantomeno furono capaci di migliorare le condizioni di vita dei cittadini boliviani. Negli anni novanta, il realizzarsi delle condizioni democratiche favorì l'emergere di movimenti politici popolari, spesso caratterizzati da sentimenti anti-neoliberali. Pertanto, cercheremo di capire in che modo l’amministrazione di Evo Morales tentò di superare il paradigma neoliberale, e soprattutto se riuscì nell’intento di indirizzare il paese verso un nuovo modello di sviluppo.

Le più recenti mosse critiche contro il sistema di libero mercato e il processo di globalizzazione si sono spesso concentrate sull’aspetto climatico, ambientale, nonché sociale della questione. Perciò, oltre ad alcuni concetti basilari di economia ambientale, proveremo a capire ed interpretare gli effetti diretti e indiretti causati dalle riforme strutturali nei paesi dell’America Latina a partire da alcuni specifici casi studio. Ne conseguirà una valutazione generale sulla gestione delle risorse ambientali nel contesto delle politiche di libero mercato. In base ai dati presentati, ci si potrà rendere facilmente conto di come l’attuale modello di sviluppo sia sostanzialmente incompatibile con la salvaguardia dell’equilibrio climatico globale. La questione del debito climatico, re-definendo il termine “debito” come un problema sistemico piuttosto che finanziario, ha il potenziale per sovvertire l’attuale paradigma economico che inquadra i paesi in via di sviluppo nella categoria dei debitori e quelli ricchi come creditori. Infatti, la tesi del debito climatico sostiene che i paesi sviluppati siano i principali fautori dell’attuale crisi climatica, e propone delle forme di risarcimento nei confronti di quei paesi che ne hanno invece subito le conseguenze negative. Al fine di poter valutare la possibilità del riconoscimento del debito climatico, proveremo a fare chiarezza evidenziandone i punti di forza, ma anche le principali critiche mosse contro questa tesi. In conclusione, dopo aver esaminato le implicazioni del debito estero nell’ambito della conservazione ambientale, cercheremo di capire come il concetto di “sostenibilità” possa essere applicato al mondo della finanza. Ne deriveremo il fatto che, essendo la questione ambientale condizionata dagli aspetti sociali, i nuovi investimenti dovranno essere supportati da un radicale cambiamento nella definizione del concetto di responsabilità fiduciaria. Cercheremo di capire come la finanza sostenibile possa essere applicata al contesto latinoamericano, analizzando i vari meccanismi e strumenti che potrebbero essere utilizzati per migliorare le capacità di adattamento e mitigazione nei confronti degli effetti cambiamento climatico. Anche il sistema bancario sarà oggetto di una radicale trasformazione, grazie all’emergere di nuovi enti e istituzioni che si prefiggono di perseguire e patrocinare pratiche etiche e sostenibili.

Questa tesi ha come scopo principale quello di illustrare le fondamenta teoriche e le circostanze pratiche che hanno creato il presupposto per il cambiamento nelle politiche economiche dei paesi dell’America Latina. Pertanto, ci focalizzeremo sulla crisi del debito, dal momento che rappresenta un passaggio fondamentale di questa dinamica, così come sui cosiddetti programmi di riforma strutturale progettati dalle istituzioni finanziare internazionali. Distingueremo le diverse fasi che hanno caratterizzato la strategia di riduzione del debito messa in atto, al fine di valutare l’impatto di queste iniziative sulle condizioni economiche dei paesi latinoamericani. Evidenziando il fatto che le valutazioni riguardanti i programmi di riforma strutturale si siano troppo spesso concentrate su parametri economici, capiremo come anche i fattori politici e sociali influenzarono la mancata crescita della regione. La questione dello sviluppo, così come il superamento del retaggio del sistema coloniale, rientra tra le sfide poste dall'odierna globalizzazione. Poiché i paesi dell'America Latina sono tuttora ricchi di risorse naturali, e si sono specializzati nella produzione e nell'esportazione di queste, hanno mantenuto una posizione periferica all'interno del sistema economico internazionale. Con il paradigma neoliberale, inoltre, i ricavi delle esportazioni aumentarono solo i profitti degli investitori stranieri e delle élites locali, e non portarono alcun beneficio in termini di riduzione del debito estero. Oltre a creare forti disuguaglianze economiche e sociali, il modello di crescita basato sulle esportazioni non solo trascurò l'adeguamento delle attività economiche locali al nuovo contesto internazionale, ma espose i paesi latinoamericani alla volatilità dei mercati finanziari e della domanda globale. Nonostante l'attuazione delle politiche di aggiustamento e delle misure di austerità, le quali colpirono principalmente le classi sociali più condizionate dal taglio della spesa pubblica, la struttura economica dei paesi latinoamericana continuò a mostrare latenti problematiche legate all'alto debito pubblico e alle tendenze inflazionistiche. Per affrontare la sfida dello sviluppo, gli sforzi della popolazione e dei governi locali dovranno essere accompagnati da un dibattito internazionale aperto, chiaro, inclusivo, e che tenga in considerazione più aspetti possibili. La crescente attenzione riguardo alle tematiche ambientali impone una riconsiderazione dei rapporti economici tra i paesi sviluppati e quelli in via di sviluppo. In aggiunta, il ruolo della società civile e delle multinazionali nel panorama economico internazionale si fa sempre più decisivo. Le sfide poste dal cambiamento climatico contribuiscono alla necessità di proporre un nuovo paradigma basato su valori etici e democratici, e soprattutto sul rispetto del pianeta. Quando si potrà dire chiaramente di aver superato il modello di sviluppo basato sullo sfruttamento delle risorse naturali? Come potrà il sistema finanziario internazionale influenzare il cammino dei paesi in via di sviluppo verso un percorso più sostenibile? Trovare delle risposte a queste domande ed approfondire il dibattito sul collegamento tra politiche economiche ed ambientali è l'obiettivo finale di questo lavoro.

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Introduction

What does the financial crisis of the 1980s have to do with the global climate crisis we are currently experiencing? To understand, and then to answer, this question, a careful analysis of international political and economic relations must be carried out. Latin America is considered by many as the best example of how this connection has established over time, maybe because it is the region where the signs of the past are more evident than elsewhere. The main objective of this dissertation is, therefore, to provide a clear framing of the political and economic transformations that characterized Latin America since the last quarter of the past century. In particular, the most important theories of development are explored, and how they affected the political landscape of Latin American countries. By reviewing the thesis of the most influential scholars and thinkers, a detailed picture is built up on the economic and political paradigms which have been developed and implemented in the course of time. After examining the outcomes of the implementation of such theories onto the economic context, we will be able to discern the critical features of economic development in Latin American.

In order to follow a descriptive logic, the paper is structured according to a sequential order. In the first chapter, I will investigate the current known as "structuralism", as well as the claims made to address the most critical economic and structural problems of the region. We will see the political response to such assumptions, which emerged in those countries in the form of a broad agreement that economic growth was to be pursued by an industrialization strategy based on the substitution of imports. The benefits and the flaws of this development strategy are thus examined. This analysis allows us to conceptualize the political and economic paradigm typical of Latin American countries into a broader recognition of the pivotal role of the State as the main engine behind economic development. We will then be able to evaluate the results reached by the state-led model of development. In the second section of this first chapter, I will deliver a review of the international financial environment in which the shift toward the next model of development occurred. The period covered here, which stretches from the 1960s to the late 1970s, witnessed watershed events which set the basis for the subsequent economic crisis. Therefore, we will consider the role of the Eurodollar and petrodollar markets in affecting the financial posture of Latin American countries. The exhaustion of the state-led model was reflected in the political sphere by a radicalization of the region's political regimes from populism toward authoritarianism, but also by the emergence of – not so new – theories of political economy. We will understand how neoliberal ideas asserted themselves in the Latin American region by virtue of long-standing and oncoming trajectories. The third section of the first chapter will then be completed with a brief examination of the Chilean case, as the most emblematic example of neoliberal state.

The second chapter presents a crucial issue of this paper, that is why and how the Latin American debt crisis of the 1980s erupted, and which response were taken by the most influential international actors. Thus, the conduct of the international financial institutions in dealing with the crisis is critically examined. I will then frame the concept of structural adjustment, and explain how it was staged by the major financial institutions. The solution to financial problems in the region is presented as a renewed emphasis on a growth model based on the expansion of the export sector, as well as the transition towards democratic political regimes. In order to assess the development under the neoliberal paradigm, I will outline the major fields of reform, comparing the experiences of Latin American countries with the East-Asian ones. Eventually, I will discuss the success of such reforms by considering the outcomes of neoliberal policies in view of economic and social indicators. The second section of the second chapter focuses on the case of Bolivia, since her trajectory encompasses the adoption of neoliberal reform, first, and the attempt to abandon it, later. The particular features of this country will turn out useful in understanding the potential dangers of a growth model solely based on the extraction, and export, of natural resources.

The third chapter brings us to a new stage of the study of political economy in Latin America. This is characterized by a growing concern over environmental and social issues, and influenced by the enlarging role of civil society. First, I will try to evaluate the impacts of neoliberal reforms over the management of the region's environment. Second, I will describe an alternative framework that may help challenge the current trend of international capitalism by offering a new perspective over the historic relation between countries in the Global North and those in the Global South. Third, I will acknowledge that, in order to put forward the required environmental reforms, the role of international finance is to be questioned. Thus, I will provide a general approach to the rise of sustainable finance, and how it may be implemented in the emerging markets. In conclusion, a brief description of social banking is delivered, as it constitutes the cornerstone for the implementation of sustainable development practices.

1.1 Latin America’s transition toward a new paradigm of development

After the Great Depression, new theories of political economy were coming into view in Latin America. These theories constituted a distinctively Latin American contribution to development studies. The main purpose was to investigate the reasons for underdevelopment by focusing on the dynamics of international trade and on the international division of labor, which were viewed as obstacles for the growth of recently independent countries. As a matter of fact, the imperialist structure had still a great influence on trade relations among countries. The central topic of economic theory that was addressed in Latin America in the period after the Second World War was industrialization, as it was considered the only path toward economic development. Nevertheless, the question of whom should have driven the process of industrialization was matter of debate for various schools of thought worldwide.

1.1.1 The first structuralism and the theory of dependency

The current known as the first structuralism is usually associated with the Economic Commission for Latin America (ECLA), which was a United Nations’ regional commission established in 1948 to foster economic cooperation in Latin America. Its headquarters were in Santiago, Chile, and its members were twenty Latin American countries, the United States, England, France, and the Netherlands. The ECLA was guided by the ideas and personality of Raúl Prebisch (1901-1986). He believed that the fundamental reason for underdevelopment was to be found in the structure of the international economic system. He argued that the spread of capitalism had been dividing the world in two parts of the same structure: the “center,” i.e., the advanced countries which produced industrial goods, and the “periphery,” which included the underdeveloped and developing countries, sources of primary products such as food and raw materials. Prebisch first used the terminology center-periphery in 1946, when studying the economic cycles affecting the US and Latin America. He asserted that the business cycles depended on exogenous factors involving the balance-of-payments. In the upswing of the cycle, exports and foreign investment produced an inflow of credits in the “periphery,” which subsequently created new money and caused an increase of imports, thus, causing a trade deficit that should be repaid with more exports to the center.

The economic relations between the center and the periphery were regarded by Prebisch as being profoundly asymmetrical and unequal. First, gains from trade were not equally distributed between the two zones. As the Prebisch-Singer thesis explains, industrial countries benefitted from technological advances and, although technical progress permitted them a decrease in the price level, those countries kept high prices on their products. Second, the periphery was characterized by a slower productivity both in agriculture and in mining, which were the leading sectors in the context of international economy. Third, terms of trade were deteriorating, as primary goods producers had to increase their exports in order to obtain the same quantities of industrial product imports. Through the study of these dynamics, Prebisch questioned Ricardo's classical theory of comparative advantage and, conversely, he highlighted the fact that trade, far from equally distributing benefits, can be a sly vehicle for exploitation. He believed that trade cycle oscillations were set by the US economy for the whole international system, while monetary authorities in the US were able to manage internal policies like full employment without destabilizing their monetary system. Prebisch argued that those authorities did not estimate the impact of those policies on the dollar exchange rate relative to other currencies. Therefore, countries in the periphery could not be driven by the monetary projections of the center, and money supply could not be expanded in pursuit of full employment, because, with a high propensity to import, any expansion of income would quickly exhaust foreign exchange, leading to a devaluation of national currency. This implied that the peripherical nations were facing three undesirable options: first, they could have strong currencies and maintain high levels of imports at the cost of high unemployment; second, they could fight unemployment with an expansionary monetary policy, but would thereby create inflation and put pressure on the exchange rate, thus raising the cost of repaying foreign debts; or, third, if they used monetary policy to maintain high levels of employment, but failed to devalue, their reserves would disappear.[1] In addition, during the downside cycle, the prices of periphery's products began to fall, and peripheral countries were not able to defend the prices of their goods as the center did. Thus, equilibrium theories in international trade were not useful within those terms of trade.

The opinion of Prebisch on long-range terms of trade was permeated by the belief that the benefits of technological progress were absorbed by the center. A study conducted by Hans Singer of the U.N. Department of Economic Affairs about relative prices of exports and imports of underdeveloped countries provided an empirical foundation for Prebisch thesis. His work constituted an assessment of long-term trends in the relative prices of those goods which were traded between industrialized and raw materials-producing countries. He concluded that, for a long time, the terms of trade had been moving against the exporters of primary commodities and in favor of the exporters of industrial products. *"*On the average, a given quantity of primary exports would pay, at the end of this period,

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[1] Love, J. L., (1994); "Economic ideas and ideologies in Latin America since 1930"; in L. Bethell (ed.); *The Cambridge History of Latin America*, Volume VI, "Latin America since 1930: Economy, society and politics"*;* Cambridge, Cambridge University Press, p. 411.

for only 60% of the quantity of manufactured goods which it could buy at the beginning of the period" – Singer asserted.[2]

Again, the answer is to be found in trade cycles. During the upswing, the prices of primary goods rise more sharply than those of industrial goods and, during the downswing, the prices of the former fall more steeply than those of the latter. As a result, the real economic gains brought by the price increase are absorbed by the center. On the contrary, because the periphery absorbs more of the income contraction than does the center, wages do not increase proportionately during the upswing. As peripherical countries lacked a well-organized rural labor, and least of all, in agriculture, they were not able to resist the fall in wages during the downswing of the cycle. Another aspect that must be taken into consideration is the fact that peripheral countries did not have monopolies on the goods they offered in the world market. Rampant inflation constituted a problematic dynamic, too. The basic structuralist assumption was that the inflationary pressures were produced by the obstruction of the retarded sectors, in particular agriculture. The backwardness was chiefly caused by an inelastic response on the supply side with respect to the demand of the burgeoning urban masses, which was rapidly rising. Another structural cause for the lateness of economic development, was identified in the stagnation of the export sector, as repeated devaluations were carried out in order to raise export competitiveness. To a lesser degree, the ECLA economists recognized in the presence of national industrial monopolies and oligopolies, which were protected by high tariffs and which, therefore, could quickly raise prices, another source of inflation. These are the reasons why negative features such as structural unemployment, external disequilibrium, and deteriorating terms of trade, persisted in the economies of the periphery.

A gust of reformism in ECLA's view was brought by the raising concern over social issues, especially after the Cuban Revolution of 1959. In his 1963 essay *Toward a Dynamic Development Policy for Latin America*, Prebisch advocated for specific reforms in the agrarian structure, income distribution, and education system. He recognized that Latin American industrialization was based on labor-saving technology, but consumption patterns in the upper strata preferred more capital-intensive consumer goods. Therefore, the deterioration of domestic terms of trade was also exacerbated by the high propensity of the upper strata to consume imported goods. The insufficient dynamism inside national markets made difficult the absorption of the labor force, as such absorption was not required by the slow growth of demand for agricultural products and by the increased productivity in primary activities. This insufficient dynamism actually prevented a rise of wages in agriculture parallel to the

[2] Love, J. L., (1994); "Economic ideas and ideologies in Latin America since 1930", p. 414

increase in productivity, eventually losing, in part or in whole, the gains derived from technological progress. Other economists added further contributions to the structuralist tenet. For example, Paul A. Baran (1909-1964), thought that underdevelopment was fundamentally a by-product of the hierarchical international capitalist system, which was characterized by the transfer of surplus from underdeveloped countries to advanced countries. Multinational corporations were considered as key players in the international trade system, but also as agents that with their action were able to hinder the effective economic growth of developing countries. Furthermore, Baran stressed the fact that, as the owners of the resources in poor countries sought advantage in the international context, they tended to sought alliances in the international capitalist class and in multinational corporations, rather than other national actors. Another economist, Celso Monteiro Furtado (1920-2004), noted how Latin America's industrial employment had risen more slowly with respect to the overall industrial output. He found the solution to the problem in what was the labor-saving technology which the periphery imported from the center. Furtado argued that Latin American process of industrialization presented completely different characteristics with respect to European industrialization in the eighteenth and nineteenth centuries. While in Europe, during the classic phase of industrialization, technology continually cheapened the relative cost of capital goods, creating the possibility of solutions to many social problems, in twentieth-century Latin America technology was exogenous to the regional economy, and it was specifically projected for the requirements of industrialized countries. As a consequence, employment absorption did not depend on the relative availability of production factors, but rather on the type of technology used, and little choice could be exercised over this matter. Moreover, Latin American firms had to compete in their own national markets with those multinational corporations which disposed of high-technology and labor-saving capitals.

Other structuralist critics against Latin American's development firmly insisted on the balance-of-payments deficits and on high rates of inflation as the main sources of social tensions and political instability. For ECLA, these were chiefly structural problems, which traced back to the agrarian pattern of latifundium, to the industrial structure creating low labor absorption, and to the maldistribution of income due to the rigidly stratified social structure. On the political front, the intellectual climate was radicalized by the international resistance to the US military intervention in Vietnam. Anti-establishment protest, often led by students, sparked in a variety of countries, and reached a peak in the demonstrations and repressions of 1968, until, starting from the 1970s, liberal ideologies assumed the dominant position at the policy level in almost all Latin American countries. In Chile, the experience of the Frei administration (1964-1970) revealed the enormous political difficulties of implementing ECLA-inspired reforms as envisioned by Prebisch in his *Toward a Dynamic Development Policy*, and other structuralist writings of the 1960s. Ironically, in a retrospective analysis, the 1960s offered a rather favorable economic climate for Latin America. In the years when dependency analysis emerged, the rate of population growth in Latin America was at its highest point and the international economy was more dynamic in the period 1960-73 (ending with the OPEC oil price shock) than in any other period in the post-war era, permitting diversification of Latin American exports, including manufactures. Anyway, ECLA's theories and policy prescriptions were challenged both by the neo-classical right and by the heterodox left, some of whose members had been leading figures in the ECLA itself, notably Furtado and Sunkel. Through their "dependency theory," Furtado and Sunkel not only adopted an explicitly historical view of development, but they also depict the connection between development and underdevelopment in the form of a tendency for industrial economies to inhibit the growth of primary economies as a result of their own growth process.

Andre Gunder Frank (1929-2005), in his *Capitalism and Underdevelopment in Latin America* (1956), stressed the fact that a fundamental reassessment of Latin American Marxism was needed.[3] Yet the prevailing belief in most Latin American Communist Parties was that the local bourgeoisie was a progressive force, and socialist party spokesmen argued that proletarians and bourgeois had to struggle in concert to eliminate feudal residues and to contain imperialist penetration. However, the main issue that the Cuban revolution posed after October 1960 was the viability of the "uninterrupted path to socialism," a thesis proclaimed that year by Ernesto "Che" Guevara. After Fidel Castro's public adherence to the Marxist values, the idea that contemporary Latin America should have sustained bourgeois-democratic regimes began to be reappraised. Correspondingly, Frank argued that the historical process of the evolution of capitalism caused development in rich countries and underdevelopment in poor ones. For Frank, in order to exit from the system and to unhinge the local elite from its international alliances, a revolutionary struggle, following the Cuban example, was needed. He agreed with Cardoso and other dependency theorists on the existence of a single center-periphery system developing historically, and shared with them the belief that the gap between the center (the "metropolis") and the periphery (the "satellites") was widening in power, wealth, and income. More broadly, the Structuralist theorists highlighted the fact that oligopolies and multinational corporations shaped the rules of the international trade by increasing inequalities and imbalances, as well as by preventing underdeveloped countries from undertaking a true development path. The subsequent step within ECLA was, therefore, a plan for diminishing the dependence from

[3] Frank, A. G., (1967) *Capitalism and Underdevelopment in Latin America*. New York, Monthly Review Press.

advanced countries goods by producing them nationally through an import-substituting industrialization strategy (ISI). The model of industrialization advocated by ECLA was meant to replace the imported goods with domestic manufactures, following the existing demand patterns. However, during the 1960s, ISI began to be perceived of having failed in the attempt of bringing the desired economic prosperity, spreading pessimism among the structuralist circles. The publications of ECLA started to criticize its own former suggestions and efforts. It admitted its responsibilities in missing social and political targets and in framing a realistic development program. Sunkel identified two main chronic issues affecting the ISI strategy. These were the persistent dependency on the foreign sector, with its deteriorating terms of trade, and the falling share of employment in the industry sector vis-à-vis other non-agricultural sectors. For Sunkel, these conditions resembled the failure of the structuralist approach toward development.

Cardoso, during his association with ECLA, moved the dependency perspective toward an analysis of social relations, arriving at a pessimistic view of the "national bourgeoisie". In fact, through his empirical studies of industrialists in Brazil and Argentina, he argued that Latin America lacked a "conquering bourgeoisie". Unlike Sunkel, Cardoso and his Chilean collaborator, Enzo Faletto, preferred to speak of two sub-systems of global capitalism, one internal and one external. They linked the failure of import substitution with the demise of the populist political style and they believed that, in that specific phase of capital accumulation, authoritarian regimes were needed to assure a political demobilization of the masses. They also stated that poor countries could achieve development only through an active state policy aimed at pursuing national interest by contrasting local and international private interests. In essence, there were two phases in this story, corresponding to perceived failures in economic performance. The first was the failure of export-led growth, which gave rise to the Prebisch-Singer thesis and the "ECLA doctrine", and which has chiefly consisted in taking a critical and militant position toward the industrial center on behalf of the underdeveloped periphery. The second was the failure of import-substitution industrialization. The dependency theory as a body of doctrine grew out of the perceived inability of Latin American states to surmount the difficulties identified by ECLA, inflation above all, but also other problems rooted in institutional rigidities. Prebisch further denounced the pattern of industrialization in Latin America, pointing out that the exaggerated level of protection had allowed terribly inefficient industries to arise. As a result of these high tariffs, Latin America was deprived of the opportunity to set up economies of scale and to foster the specialization of exports.

1.1.2 Industrialization through Import-Substitution

As we have already seen in the previous section, the phase of development which is usually referred to as import-substitution industrialization represented the attempt made by less-developed countries to break with a world division of labor that saw them as a mere source of primary commodities for developed economies. Since Latin American countries exported mainly foodstuff and raw materials, and imported manufactured goods from the US and Europe, the main goal of ISI was to establish facilities for the domestic production of those manufactured goods that were imported from industrialized countries. In the aftermath of World War II, ISI policies were largely adopted in most of Latin American countries as a mean to attain economic development. These countries deliberately adhered to the view of the ECLA, which considered the transition toward a new world division of labor as the polar star of Latin American development. Because of the precariousness of world demand for traditional forms of exports, i.e., food and primary products, a more dynamic element was to be introduced in Latin American economy in order to meet the demands of an increasing urban population and, thus, reaching long-term development targets. Infant industries were to be protected by the government, and their growth encouraged. As explained by Baer in his 1972 article, ISI was pursued through a series of policy instruments: the most traditional were protective tariffs and exchange controls. Alternative tools consisted in special preferences for domestic and foreign firms importing capital goods for new industries, preferential import exchange rate for industrial raw materials, fuels and intermediate goods, cheap loans by government development banks for favored industries, the construction of infrastructure especially designed to complement industries, and the direct participation of the government in certain industrial sectors, especially the heavy industry.[4] ISI relied on a broad set of "developmental" tariffs, which consisted of protective rates for consumer goods (textiles, clothing, etc.) and low rates for necessary inputs and capital goods (oil, steel, machinery, etc.). Production inputs could be imported at relatively low tariffs rate, while consumer goods were permitted to be imported under extremely high tariffs rate. The common result with Latin America's ISI was an initial phase of rapid industrial expansion, as capacity grew in the "easier" sectors. Apart from tariff barriers, another key aspect of ISI was the direct support of the state in the manufacturing sector, i.e., the industrial policy. The industrial policy was elaborated in Latin America during the post-1960 phase of modified ISI. The major tools of the industrial policy included state owned enterprises (SOEs), subsidies to private firms, official agencies for improving quality standards, and government sponsorship for technical training and research. Foreign direct

[4] Baer, W. (1972); "Import Substitution and Industrialization in Latin America: Experiences and Interpretations"; *Latin American Research Review*, Spring 1972, Vol. 7, No.1, p. 98.

investments (FDIs) undertaken by developed-country firms were subject to tight control, requiring local inputs, as well as the sharing of technology with local partners through joint ventures. As newer, sophisticated industries seemed likely to grow rapidly and to stimulate innovation in related sectors, attention could be paid to the development of production methods which were appropriate for local circumstances.

However, two negative features of ISI policies in Latin America are readily recognizable. The first is that this strategy of industrialization operated in an indiscriminate way, as no attempt was made to provide subsidies only to those industrial sectors which had more potential in function of their comparative advantage. On the contrary, ISI was often conducted in favor of producers of consumer goods, which required low capital and simple technology for manufacturing. In some countries, i.e. Argentina, Chile and Venezuela, ISI policy was expanded also to those industries that produced durable consumer goods and which required more capital and more technologic inputs, e.g., the automobile industry. Moreover, in other countries governments subsided both consumer goods producers and the intermediate and capital goods sectors. The second peculiarity of Latin American ISI lays in the crucial role played by FDIs during the 1950s and the 1960s. Though their small relative size, they proved, indeed, fundamental for setting up key manufacturing industries by transferring know-how and organizational capabilities. In any case, also those sectors that were controlled by the government, i.e., infrastructure investments and heavy industries, benefitted from a spillover of international capitals. However, two major critics emerged against the capability of ISI policies of reaching economic development. First, the market critics deemed inefficiency and misallocation of resources as the main weak points of ISI. Since the world production is maximized only if each country specializes in the field with the greatest comparative advantage, Latin America should specialize in the production and transformation of primary commodities. The fact that no regard was paid to the specialization of specific sectors, as well as the indiscriminate way in which import-substitution was applied, led many critics to think that what many governments were pursuing was merely self-sufficiency and autarky. However, given the small markets, the limited capital, and a lack of skilled manpower, autarkic plans would only lead to the creation of inefficient and high-cost industries. Moreover, in those industries having high fixed costs, the situation became extremely complicated, as these industries required large-scale output in order to keep costs down to the levels of more advanced industrial countries. The steel and automobile industries, which have been established in most of the larger Latin American countries during the post-war years, represented the perfect examples. Specifically, in the case of automobiles the situation was worsened since many countries in the region permitted the establishment of a large number of firms, thus completely eliminating the possibilities of endowing their economies with a large-scale production in specialized sectors. Trade barriers, by confining the protected manufacturer to the domestic market, inhibited the formation of economies of scale, particularly in small countries. Furthermore, where government policies had suspended foreign competition, the scope for economies of scale was restricted even further, causing the emergence of too many firms, each with too small output capacity. The market critics also asserted that the stress on maximizing internal vertical industrial integration, so that to promote not only final goods production, but also intermediate and capital goods, impeded growth because resources were sidetracked where they won't have produced the highest possible output. If Latin American countries had specialized in only a few products with the greatest potential comparative advantage, and exported a large surplus while importing other goods, total output available would have been higher and these nations would have grown more rapidly than they actually did.[5] On the contrary, no attempt was made until the late 1960s to at least promote ISI on a regional basis and to build up a complementary industrial structure within Latin America. Furthermore, while the commodity composition of Latin America's exports remained almost unchanged, the commodity composition of imports was made up in increasingly proportion of raw materials, semi-finished products, and capital goods. As these were the inputs which were not available domestically, the result was that ISI placed Latin American countries in a new and more dangerous relationship of dependency with the more advanced industrial countries than ever before. In fact, in former times a decline in export receipts acted as a stimulus to ISI. But under the new circumstances, a decline in export receipts would not counterbalance capital inflows, resulting in forced import curtailments which, in turn, may cause an industrial recession. Such conditions have been experienced by Argentina and Colombia, as well as by other countries in the region.

The structural critics described why the ISI strategy failed to increase the low rates of labor absorption. This was not only because of social problems related to urban unemployment or underemployment, but also because of the implication for income distribution. In fact, with an uneven distribution of wealth, a malfunctioning fiscal system, and an industry sector characterized by incrementing capital/labor ratios, the trend was for income to become even more concentrated than before. The evidence available for Latin American countries tends to confirm this trend, as the share of the region's labor force employed in industry reached only about 25 per cent by the 1980s, compared to 35 per cent in the new-industrialized countries of the East Asia.[6] Because of the unequal concentration of income, the growth of demand for industrial products resulted in not being sufficient to maintain the initial ISI momentum. In addition, other imbalances characterized the ISI strategy. As it proceeded, protection gave a comfortable profit margin to all inside the market to neglect the search

[5] Baer, W. (1972); "Import Substitution and Industrialization in Latin America: Experiences and Interpretations", p. 104
[6] Ward, J., (2004); *Latin America: Development and Conflict since 194*5; Second edition, London, Routledge, p. 30

for greater efficiency. Had Latin American countries increased the resources earmarked for scientific and technological research, greater efforts in discovering more labor-intensive techniques would have been rewarded. On the contrary, protection encouraged the adoption of capital-intensive production methods. As a result, the learning and the assimilation of new techniques of production were not encouraged, and the efficiency of the industrial process was not improved. State bureaucrats with careless management and ill-judged plans ignored the basic condition regarding the infant-industry argument, which is that protection must be limited and must expire at some deadline, whether or not the infant industry has grown up. In fact, the success of a protectionist policy depends on the full credibility of its temporariness. If credibility is missing, protection degenerates into rent-seeking behavior. As SOEs proliferated, and elite interest groups secured wasteful allocations of state funds, the ISI strategy lost focus. The political weakness of Latin America's populist governments limited state revenues, and budget deficits were financed by enlarging the money supply. As a result, high inflation caused exports to became uncompetitive and made manufacturers' imported inputs more expensive. One possible response was a devaluation of the national currency. However, populist governments were reluctant to devalue, because doing so they would have benefited the traditional export interests of large landowners and foreign mining companies. On the other hand, overvaluation was a convenient way of taxing exporters. By and large, devaluation was postponed until balance-of-payments difficulties made it unavoidable, thus aggravating inflation by raising the cost of essential imports. These macroeconomic weaknesses, which were essentially domestic in their origin, provided the context for the rapid growth of Latin America's foreign debt in the late 1970s and early 1980s.

1.1.3 The State-led industrialization

This section examines the model of development which was adopted by the great bulk of Latin American countries from the 1930s until the 1970s. During those years, Latin American countries were dominated by populist governments, whose economic policies were chiefly dictated by and subordinated to the achievement of political goals. Although we often use the terms "import-substituting industrialization" when we refer to this particular period, Latin American development, in reality, involved an increasingly participation of the state, in particular within the economic and social spheres. So, speaking about a "state-led industrialization" may be more appropriate if we look at this period. In fact, the state took on a wider range of responsibilities, as well as a stronger, and sometimes, monopolistic, role in a series of strategic sectors. States often committed in improving directed credit, i.e., designing mechanisms for ensuring that private financial institutions would channel funds into priority sectors. They also committed in developing infrastructure and in providing support to private domestic firms through protection. From the financial point of view, development banks and commercial banks were often founded. As the state took on a more active role in the social sphere, the process of industrialization also entailed major political challenges. The population boom of the 1950s and 1960s was followed by a rapid urbanization, and so, power relations were redefined in the context of more urban societies. The relationship between the state and business elites changed as well, since the latter became increasingly powerful. Moreover, as inequality in the distribution of income was growing, new conflicts in urban zones emerged, as well as dateless tensions in rural areas.

As we have seen, ECLA considered industrialization the essential element for economic development, as it represented the main channel for the transfer of technological progress. On one hand, the production structure should be altered by increasing the share of modern industrial activities and by deflating the share of primary sectors, especially agriculture. On the other hand, ECLA found that industrialization should not be a mean to isolate Latin American from the international economy, but rather a way to reshape the old-time division of labor that did not allow the region to enjoy the benefits of technological change. However, as the dependency theory predicted, terms of trade for commodities were deteriorating over time. So, industrialization policies were changed as time passed, both to limit policy excesses and to seize the new opportunities the world economy was opening up starting from the 1960s. ECLA became increasingly critical of the excesses of import substitution and started to advocate what Bértola and Ocampo termed a "mixed" model, i.e., a model which combined import substitution with export diversification and regional integration.[7] The governments of the larger countries began to follow this model and to favor exports, in an attempt not to miss the opportunities that a more integrated market was offering. Almost every country of the region began to introduce a more pragmatic industrialization strategy, by employing differing mixes of both traditional and new policy tools. The traditional tools were tariff and non-tariff protection; multiple exchange rates and foreign-exchange rationing; development banks; and investments in infrastructure. The new policy tools were regulations governing sectoral allocations of credit for the private sector and interest rates; tax incentives; public-sector investments in strategic sectors, including energy, telecommunications, and some transport services, but also some steel, chemicals or petrochemicals industries. However, this model did not succeed in altering the structure of protection and in promoting new industries, but rather it added new layers of protection on existing ones. This practice gave rise to a stratified pattern of protectionist measures that would become the

[7] Bertola, L., and Ocampo, J. A. (2012); *The Economic Development of Latin America since Independence*; Oxford, Oxford University Press, p. 156.

critical feature of state-led industrialization in Latin American countries. The manufacturing sector was the engine of economic growth, but many other modern services were also appearing: financial services, transport infrastructure (with roads and air transport overshadowing railroads), telecommunications, and public utilities (electricity, water, and sewerage). These sectors were directly influenced by the state through the control of the industries that produced those kinds of goods and services. State-owned enterprises played a crucial role in the Southern Cone, but also in certain Andean countries. The state was the principal shareholder also in the petroleum industry and in large-scale mining activities, following a nationalization trend that was first opened up by Mexico in 1938. However, the main feature of this period was for the state to get involved in the production of modern utilities, chiefly by means of nationalizing those private companies which were earlier established by foreign companies.

The straightforward way to rationalize the protective structure consisted – according to ECLA's view – in more regional and subregional integration. Regional integration would reduce the downsides of import substitution by increasing the size of the market. It was also expected that integration would impose some market discipline on protected sectors. Integration would represent a platform for the development of new export activities, particularly in the manufacturing sector, but it was also necessary in attaining economies of scale in the larger countires, and in enabling the smaller economies to achieve some degree of industrialization. The coffee agreement was crucial in this direction, as it subsequently led to a series of other formal agreements that, with brief interruptions, regulated the world coffee market with quotas from 1962 to 1989.[8] Industrialization was also accompanied by local technological capacity-building and required an explicit learning process and an effort to adapt technologies, which gave rise to a considerable number of secondary innovations. The participants in this learning process ranged all the way from quite small companies to the largest corporations, including both the SOEs and the subsidiaries of multinational enterprises. Some of the larger corporations set up research and development departments and, sometimes, firms gained enough expertise to sell technology in the form of licenses and engineering services to other Latin American countries. This meant that a broader range of production units became a decisive factor in building the capacity required to take advantage of the opportunities opened up for the export of manufactures. Notwithstanding, national systems of innovation were not enough developed to establish solid technological networks like those that were built up at that time by Japan and some of the first Asian tigers (especially the Republic of Korea and Taiwan). Nor was set up any focused policy for promoting technological spillovers from foreign investment. Bértola and Ocampo

[8] Bertola, L., and Ocampo, J. A. (2012); *The Economic Development of Latin America since Independence*, p. 142.

suggested that policymakers mistakenly assumed that these kinds of spillovers would occur spontaneously. On the contrary, the education and research systems were not apprised of the needs of the production system, which, in addition, was not generating a demand for highly qualified technical teams.[9] As a result, Latin American countries failed to achieve a sustained reduction in the technological gap with respect to industrialized countries

The industrialization process reached its highest point in 1973-4, and despite it differed from place to place, it also made rapid headway in a number of small countries, particularly Ecuador and other Central American nations where industrial policies were mixed with traditional commodity exports. In the smaller economies, the more traditional industries accounted for between 60% and 80% of manufacturing value-added by the end of the most intensive phase of industrialization. The countries' production structures were heavily influenced by a few sectors in which they had or have acquired competitive advantages, such as textiles in some small economies (Uruguay and Bolivia, and, in Central America, Guatemala and El Salvador), processing industries (paper and chemicals) in Colombia, foodstuffs in Argentina, and transport equipment in Mexico. These patterns were mirrored in these countries' exports of manufactures, both during this period and the following phase of development. However, it must be noted that policies employed to stimulate industries have often been prejudicial to the functioning of the agricultural sector. The allocation of investment resources to new industries has often meant that fewer resources were available to increase efficiency in the agricultural sector. Overvalued exchange rates, which favored industries by providing cheap imported inputs, hurt agriculture by making its goods less competitive on the international market and by making it less profitable to export agricultural products.[10] Therefore, the process of rapid industrialization not only produced a substantial change in the sectoral composition of output, but also in the structure of employment; there was a substantial transfer of labor from agriculture to industry and then to services.

The analysis above explains why the particular ways in which industrialization took place enabled the region to achieve the highest rates of GDP growth of its history. Furthermore, during these years the rate of productivity grew faster, as total factor productivity climbed steeply between 1950 and 1975. These are the reasons that led Kuczynski and Williamson to name this period as the "golden age" of economic growth in Latin America. However, as we have noted, the growth process was also marked by critical setbacks in traditional export sectors and by the limited development of national

[9] Bertola, L., and Ocampo, J. A. (2012); *The Economic Development of Latin America since Independence,* p. 173.
[10] Baer, W. (1972); "Import Substitution and Industrialization in Latin America: Experiences and Interpretations", p. 105.

innovation systems, which prevented the region from engaging in a deeper structural change.[11] Indeed, a staunch opposition to industrialization was put up by traditional export sectors. In addition, governments dealt with harsh confrontations with the working class triggered by the industrialization process itself, especially in the Southern Cone. The picture was completed by the structural volatility of an export sector that still relied heavily on commodities, and by the financial volatility which exposed the system to frequent external shocks. Summing up, we can say that toward the end of the 1970s, Latin America countries had narrowed the gap as much as it could; however, what the region needed to do now was not only to open up to the world economy and reduce state intervention, it also needed to make a qualitative leap in terms of technological development by making significant advances in developing national innovation and education systems. In the end, the debt crisis of the 1980s limited the space to do so, and this is why, as we will see in the following sections, the shift to the neoliberal model did not help the region to overcome the constraints that the state-led model was facing.

1.2 Latin America in the Global Financial Environment

This section introduces the major financial dynamics of the period as they are crucial for analyzing the international financial environment and to understand the main drivers for new paradigms in Latin American political economy. The 1970s represented a real watershed for the region, as a series of events revolutionized the international financial setting. First of all, the post-WWII recovery of Western Europe and Japan was mainly completed, and industrialized countries began to experience a general slowdown of growth that correspondingly induced a deceleration in the growth rate of Third World countries. Because the latter were still highly dependent on primary commodities exports to the former, they had to face diminishing commercial inflows. In those years, even the US were facing economic difficulties and, exception for the huge profits coming from foreign investments, their monetary resources were contracting. In fact, the US balance-of-payments deficit was enlarged by growing expenditures due to the Vietnam War and other military interventions. However, though these events reduced the pace of US growth, as well as gold reserves, the dollar did not depreciate. In fact, the US dollar was the most used currency in all international transactions and it was supported

[11] Kuczynski, P.P. and Williamson, J. (2003). *After the Washington Consensus: restarting growth and reform in Latin America.* Washington, D.C.: Institute for International Economics, p. 29; 305.

by the central banks of both industrialized and industrializing countries, which were keeping US dollar reserves.

However, as the financial pressure augmented and the US gold reserves diminished, the equilibrium of the international monetary system was seriously undermined. In 1971, the Nixon administration unilaterally decided to exit the Bretton Woods agreement by abounding the fixed exchange rate which pegged dollars to gold through a standard rate of US$ 35 per one ounce of gold. Just after this convertibility was suspended, countries had to face floating exchange rates, and consequently, violent fluctuations that began to affect the stability not only of the financial system, but also of worldwide primary commodities markets. During the 1970s, most Latin American countries could readily access to cheap external capital. Since, at that time, foreign exchange requirements were particularly pressing because of the oil shocks of 1973 and 1979, borrowing did relax the foreign exchange constraint. However, it also tightened the connection between Latin American economies and both the international financial markets and the fiscal and monetary policies of the developed countries. The Vietnam War brough significant political and economic consequences, and contributed to the collapse of the Bretton Woods system, together with a decline in US political hegemony. As the US were facing growing constraint due to the increasing trade deficit, which in 1971 amounted to 2.3 billion of US$, the dollar was beginning to appreciate. This meant that the United States could no longer play the leading role in the management of global demand. In fact, the new system of floating exchange rates was not subject to any hegemonic control, nor was it guided by cooperative leadership which could replace the US. As financial imbalances exacerbated, due to closer links between balance-of-payments disequilibria, exchange rate fluctuations, and inflation, the new system was incapable of ensuring full-employment and an appropriate distribution of aggregate demand among countries.[12]

1.2.1 The Eurodollar Market

Since the times of the Bretton Woods agreement, regulation of financial market had always been considered an essential condition for the stability of the markets. However, as in the 1950s British banks began to offer higher interests for US$ denominated deposits, a growing number of US banks started opening new branches in the City of London, setting the bases for the emergence of the Eurodollar market, i.e., the market for dollar-denominated accounts held outside the US.

[12] French-Davis, R., Munoz, O., Gabriel Palma J. (1994); "The Latin American economies, 1950—1990"; in Bethell, L., (ed.); *The Cambridge History of Latin America*, Volume VI, *Latin America since 1930: Economy, society and politics;* Cambridge, Cambridge University Press, p. 164.

In a first stage, the Bank of England supervised the activity of American branches only in an informal way, coupled by the desire of maintaining London the major financial center at the global level. Not only was the Bank of England actively promoting the Eurodollar market, but the fear of pushing capital markets toward poorly regulated off-shore centers also refrained regulators from imposing stricter rules over the financial market. Moreover, the Bank of England took several important measures permitting the growth of a Eurobond market, such as the 1962 decision to allow to issue foreign securities denominated in foreign currencies in London.[13] The Eurodollar market enabled the UK to reduce its balance of payments deficit, as it represented a source of financial inflows, so, despite fears for market stability started emerging in the first half of the 1960s, new requirements were not imposed on foreign deposits of US banks. The support of the United States was equally important because of the dominant presence of American entities in the market and because of the growing amounts of dollars which began to be deposited outside the US, in particular in European banks in London, Paris and Berlin. So, even though they could, the United States did not prevent banks and corporations from operating in that market. The process of financial internationalization developed slowly, however, and the first signs of it were not seen in developing countries until world demand for their exports, which was by then including a broader set of manufactured products, began to strengthen in the 1960s. Thus, access to the Eurodollar market began to open up on a wider and deeper scale. Outflows of US$ accelerated toward the end of the decade as the US intervention in the Vietnam War exacerbated military expenditures, providing further stimulus to the development of the Eurodollar market.

In the early 1970s, with a growing financial liberalization and the consolidation of the Eurodollar market, banks emerged as the major suppliers of liquidity. In fact, a small group of very large banks with extensive overseas operations formed the backbone of the international system of borrowing and lending. The emerging of the Eurodollar market caused the formation of excessive liquidity, for which those banks had to find new borrowers. Newborn branches of US banks were willing to lend to multinational corporations (MNCs) in Latin America, while also bringing investment information and financial knowledge. Two major changes in landing practice started to spread: first, syndicated loans, which allowed to disperse the risk of default to foreign countries over a consortium of banks; and second, the shift to flexible rates of interest, which changed according to market conditions. These two innovations, coupled by the opportunity for large premium returns, made lending to sovereign

[13] Helleiner, E., (1994); *States and the Reemergence of Global Finance: From Bretton Woods to the 1990s*, Ithaca, Cornell University Press, p. 96.

countries highly profitable. Lending to a country seemed even less risky since it was believed that deficits encountered by states could be easily offset by means of a contraction in fiscal policies. As a result, bank lending accelerated in most Latin American counties, driven by foreign banks' loans. Informal interbank activity grew and spread, and underwent a process of formalization in the course of the 1970s. More and more commercial banks from Western Europe entered the market, licensed by changes in local legal codes. For the top ten US banks alone, the share of foreign earnings as a percentage of all gains rose from 1970 to 1982, on the eve of the debt crisis, from 17.5 percent to 54.7 percent.[14] Contrarily to the common opinion that credit markets are strongly influenced by the demand of money, banks, with their *modus operandi,* were active peddlers in the supply of liquidity, especially to Third World countries.

An extra degree of liberalization was achieved in the mid 1970s, when the United States and Britain began to abolish postwar capital controls. Moreover, the absence of interest rate regulation in the Eurodollar market, which meant that both official and private dollar holdings received higher interest rates than those in the United States or in continental Europe, made it an attractive place to hold investments. Summing up, the activity of US banks and multinational corporations, together with the active support of British financial authorities, transformed the Eurodollar market from a short-term money market into a full-fledged international capital market. This was not only a setting where banks and MNCs conducted their international activities free from unfriendly intrusions of national governments, but also the starting point for the inauguration of a more liberal financial order. Taking an approach that would prevail through the 1970s and 1980s, Washington policymakers fostered a more liberal international financial system as a way of preserving their policy autonomy in the face of growing external constraints. However, by escaping from its self-imposed monetary discipline, the massive outflow of dollars posed the conditions for the demise of the whole Keynesian post-war system.[15]

1.2.2 A Growing Indebtedness

During the 1970s, Latin American countries witnessed tremendous shocks. The first was caused by the US, as they were trying to deal with the outstanding trade deficit accumulated since the end of World War II. Apart from the US President Richard Nixon unilateral decision to abandon the Bretton Woods agreement, another considerable economic event was the four-fold increase in the price of oil, as well as the froze its sales, decided in fall 1973 by the OPEC. Since 1960, the oil-producer countries

[14] Suri, J., (2011); Henry *Kissinger and the Geopolitics of Globalization,* in Ferguson, N., Maier, C. S., Manela, E. (ed.); *The Shock of the Global: The 1970S in Perspective*; Cambridge, Belknap Press of the Harvard University, p. 118.
[15] Helleiner, E., (1994); *States and the Reemergence of Global Finance: From Bretton Woods to the 1990s*, p. 103.

had gathered in the OPEC, the Organization of Petroleum Exporting Countries. It represented a cartel among oil-producers, mostly Arab countries, for concerted actions on the oil sales, as oil had become a dominant source of energy both for the industrialized and the industrializing world. The increase in the cost of energy not only caused a recession in Latin American countries that relied on oil imports for their growth, but it also brought several macroeconomic problems: trade imbalances, fiscal deficits and high inflation rates.

The 1973 oil shock obviously had different effects on Latin American countries, as it affected terms of trade of oil exporters and oil importers in opposite ways. Among Latin America's oil exporters, Venezuela, Ecuador and, later, Mexico were the main beneficiaries of the oil shocks. Most other countries, including Brazil, were net importers. Venezuela, then the principal Latin American producer of oil, experienced a major increase in exports earnings and domestic disposable income. However, Venezuela followed OPEC's policy of reducing output in order to support prices; as a result, its exports fell by 20 per cent in 1975. Paradoxically, GDP including constant terms of trade did not increase after the oil shock. The non-oil sector grew but this was counter-balanced by the fall in oil output. In Mexico, the situation was different, as this country, which was not a member of OPEC, substantially increased output thanks to the discovery of new reserves. As a result, Mexico's share of Latin America's oil output rose from 9 per cent in 1973 to 44 per cent in 1982.[16] Due to their improved creditworthiness, Latin American oil exporters also substantially raised their levels of foreign borrowing. The sources of funds took the form of official borrowings, which could be bilateral, if the loan came from a single country, or multilateral if the loan were provided through a collective arrangement between more states. The latter way gained momentum through the activity of the international financial institutions, whose major exponents were the International Monetary Fund (IMF) and the World Bank (WB), but also the Inter-American development Bank (IDB). Bilateral loans were commonly tied to imports from creditor countries, while multilateral loans came with various forms of conditionality attached, usually related to economic policy. These conditionalities were often criticized by debtor countries. The expansion of non-conditional bank loans towards the end of the decade was therefore welcomed by debtor countries as an alternative to the restrictions attached to official loans.[17] On the other hand, Latin American oil importers responded to the first oil shock in various ways. Some, notably Brazil, behaved as if the change in the international price of oil was temporary and, by borrowing abroad, they sustained a high level of investment. The growth led by foreign debt not only helped countries like Brazil to continue their growth momentum, but also

[16] Thorp, R., (1998); Progress*, Poverty and Exclusion: History of Latin America in the 20th Century*; New York, John Hopkins University Press for Inter-American Development Bank, p. 217.
[17] French-Davis, R., Munoz, O., Gabriel Palma J. (1994); "The Latin American economies, 1950—1990", p. 230.

absorbed the massive transfer of resources provided by the petrodollar mechanism. As most countries were confronting an over-supply of cheap foreign funds, the common response was a growing appreciation of exchange-rates in relation to their purchasing power parities. Exchange-rate appreciations and easy access to financing were fostered by the implementation of import liberalization policies. This process was more intense in countries launching neo-conservative experiments such as Argentina and Chile, and in new oil-exporting countries like Mexico, whose foreign currency availability increased dramatically with both foreign loans and rapidly growing oil export proceeds.

The first oil crisis further stimulated profitable lending practices. The stock of eurocurrencies increased because of the recycling of those dollars which were first moved from oil-importing countries to oil-exporting countries, then deposited in US bank branches in Europe, and eventually lent to countries in Latin America. The second oil shock caused another increase in bank lending toward the region, fostered by the eagerness of international banks to supply those countries with ever new loans. And actually, Latin American countries were eager to receive them. The main causes for the high demand of bank loans to Latin American countries are straightforward. First of all, MNCs needed sources of capital in exchange for their technological expertise in certain fields, even though none of them contributed to the financing of balance-of-payments deficit. Second, commercial bank loans were more advantageous relative to other kinds of portfolio capital, as conditionality was lower. However, those banks were, deliberately or not, ignoring the real purposes for which most of their loans were used. The beneficiaries of bank loans were usually private corporations, state-owned enterprises, and governments, with the purpose of financing the fiscal budget and balance-of-payments deficits. While for oil-importing countries, e.g., Brazil, access to low-condition loans was a mean to offset the balance-of-payments deficit caused by the rise in oil prices, for oil-exporting countries, the high price of oil became a mean to expand the production, as happened in Ecuador and Mexico, or diversify the economy through massive investments in non-oil facilities, like in the case of Venezuela. Bank lending was not directed toward the public sector only, but all sorts of debt grew rapidly. Banks lent to private-sector corporations even without public guarantees, especially in the larger countries. In fact, Argentina, Brazil, Chile, Colombia, Mexico and Venezuela are the countries that received the great bulk of bank loans. Even though the smaller states (e.g., Costa Rica, Panama, Uruguay) continued to rely on official sources of capital, as they attracted little interest form international investors, their debt grew rapidly, too. The process of indebtedness received also a strong backing from the international financial institutions, as they did not sense any kind of danger. The lack of sensibility over the issue was exacerbated by a lack of information among national governments and the institutions of Bretton Woods. Indebtedness was subject to no sort of centralized control and, as a result, public enterprises and local administrations began to obtain easy financing without anyone recognizing that all those loans would have constituted a potential danger for the stability of the entire system.[18]

The recycling of petrodollars was also encouraged by negative real interest rates, which made borrowing seem even more consistent with the signals coming from the international financial market. Therefore, superficially at least, it seemed that the floating exchange-rate regime that followed the breakdown of Bretton Woods' fixed parities would, with the aid of the world financial system, be able to offset the financial disequilibria following the 1973 oil shock.[19] The second oil shock (1979) represented a real watershed for the global economic environment, as the recession spreading in developed countries brought down the prices of commodities. Simultaneously, contractionary monetary policies were implemented by increasing interest rates to record levels. When the growth of Latin American exports began to slow down, it was obvious that the debt-led model was no longer sustainable. In addition, under the new conditions, a strong and unstable financial link was added, characterized by floating interest rates and large amounts of loans with short term maturities. Thus, the unprecedented rise of interest rates at the end of the decade led to a sudden cessation of foreign lending. In conclusion, even though the global expansion of capital flows brought a substantial improvement in the efficiency and competitiveness of Latin American economies, it also brought an enormous increase in instability, as capital movements got more and more detached from real investments and became highly responsive to external fluctuations.[20]

1.3 The Birth of the Neoliberal State

The wave of authoritarian military regimes that submerged the Southern Cone implied the changeover to a market economy as defensive strategy in reaction to what was seen as an expansion of socialism. In light of this, the confrontation between social conflict and the transition to market economies in the midst of 1970s did not resembled the adaptation to a given economic structure, but rather a radical reconstruction of civil society. The lack of macroeconomic discipline was the primary problem in Brazil and the Southern Cone, but not in the rest of the region, at least until the mid-1970s. Things became more complex when the tendency to run an external deficit, which had been a long-standing

[18] Thorp, R., (1998); Progress*, Poverty and Exclusion: History of Latin America in the 20th Century,* p. 221.
[19] French-Davis, R., Munoz, O., Gabriel Palma J. (1994); "The Latin American economies, 1950—1990", p. 169.
[20] Thorp, R., (1998); Progress*, Poverty and Exclusion: History of Latin America in the 20th Century,* p. 217.

trend, grew stronger toward the end of the phase of state-led industrialization. In almost every country of the region, this was the result of an increasing demand for investments. The resulting trade imbalances were dealt with by resorting to bigger and bigger amounts of external borrowing. This turned out to be the final blow of the state-led the model. Even though the deficit registered between 1967 and 74 was not a problem, thanks to the striking growth experienced during those years, it became difficult to sustain it during the 1980s. The demise of state-led industrialization was also determined by a growing tendency to overburden the state with fiscal responsibilities without having enough resources to meet them. FitzGerald identified three main implications which were reflected in three main trends: first, an upward trend in public expenditure as a proportion of GDP, and a downward trend in the spending on social welfare programs in comparison with industrialized countries; second, a shift in the composition of the tax structure away from property and income taxes and toward indirect taxes; and third, rising borrowing requirements, due to the need to finance transfers to the private sector rather than redistributive social policies.[21] In the second half of the 1970s, whit the widespread access of Latin American countries to external lending, rising fiscal deficits made public-sector accounts highly vulnerable to any tightening of external credit, and may have potentially led to a disastrous financial crisis. Indeed, this is what eventually occurred.

1.3.1 A (quasi-) new Economic Paradigm

As we have seen in the previous section, the boom in external financing for Latin America was part of a broader move to rebuild the international capital market that had first taken shape in the Eurodollar market of the 1960s, and which was then emerging as a reactionary political framework with the name of neoliberalism. Some scholars believe that this process was underpinned by a single, fundamental principle, that is the supremacy of market competition. Conversely, others question the programmatic coherence of the existing neoliberalism, appraising it as a broad historical shift in ideology and practice rather than the influence of a single doctrine. Within the traditional narrative, it is commonly believed that the neoliberal doctrine arose from the ideas of a group of right-wing economists in the United States and Europe, principally Friedrich Hayek and Milton Friedman. They rejected the Keynesian economics of welfare state and argued for free markets to be the basis of decision-making in every sphere of economic life. Gradually spread via the Chicago school of economics, but also other corporate-funded foundations in the US, these ideas gained particularly relevance when picked up by Margaret Thatcher and Ronald Reagan as the new agenda for

[21] FitzGerald, E. V. K. (1978). *The Fiscal Crisis of the Latin American State,* in J. F. J. Toye (ed.), *Taxation and Economic Development.* Frank Cass, p. 125.

conservative politics, and by Paul Volker, the US Federal Reserve chairman, as a guide to economic policy. While Thatcher adopted these theories in order to led a direct attack against the welfare state, Reagan used them to carry on his battle against progressive taxation. The neoliberal ideology which was taught in Chicago was characterized by a global worldview, as well as by the belief that their principles should be adopted in every aspect of a country's life. As suggested by the term itself, the ground for these new theories was the liberal ideology of Adam Smith (1723-1790), whose principles are collected in its major work titled *The Wealth of Nations* (1776). These principles are: personal freedom, the legitimacy of private property, and the supremacy of markets. Smith argued that the search for personal benefit of an individual enable the development of collective social interests. Therefore, the free market would, as an "invisible hand", allocate resources in the best way possible.

The traditional approach treats neoliberalism mainly as a system of ideas amounting to a shift in the dominant ideology of capitalist society, which gained political influence in the North and which is then imposed on the global South. Nonetheless, neoliberalism was, in every respect, a new stage in the development of a more integrated capitalist system. However, a key question remains how neoliberalism came to be institutionalized as a framework for state policy in the global South, as here, a disturbing anomaly emerges. In fact, the first neoliberal regime was the military dictatorship of General Pinochet in Chile. In fact, by the time Reagan came to power in the United States, moves toward neoliberal policies were already proliferating around South America, where some of these currents had even emerged in the 1960s. There, neoliberal policymakers were leading an attack, often using a Cold War dialectic, against other development strategies, ISI in particular. Over time, neoliberal economists, journalists, and politicians generated, by sheer repetition, a widespread opinion that alternatives to the neoliberal paradigm have been exhausting or, more simply, have failed. However, the social settlements achieved by these alternative development strategies, such as labor rights and informal redistributive networks, were at great stake in this struggle, and were eventually disrupted by the triumph of neoliberalism. Furthermore, the rise of new transportation technologies redefined the economic and social significance of international trade. A key change was the invention of the freight container, which together with super-tankers, bulk ore carriers and jet air cargos, made possible a massive growth of transcontinental trade. The new transport technologies created conditions favorable for the restructuring of domestic economies, not by local social settlements, but via transnational markets. Thus, the growth of world trade, the collapse of the Soviet Union, and the turn to comparative advantage strategies across most of the periphery produced and expanded heterogeneous forms of global capitalism. However, as some parts of the periphery have de-industrialized in favor of primary export industries, the risk of deteriorating terms of trade on the long run, the problem Prebisch warned against in 1950s, became more and more tangible. Summing up, global neoliberalism cannot be understood as a simple by-product of the internal dynamics of the global North. Even though European and US ruling classes were surely important, the affirmation of neoliberalism in the global South should not be considered as a mere projection of Northern ideology or policy, but rather a renewed entwining of worldwide economic and social relationships.

The legitimacy of the neoliberal model in the global South could draw on a long historical trajectory of coercion. Colonial society was produced by the state through the installation of a colonizing structure, an apparatus of rules that undertook the integration of local economies into a capitalist world economy. Such structures were contested but not destroyed by decolonization, and their continuity had underpinned the power of post-colonial elites. In Achille Mbembe's view, as presented *On the Postcolony* (2001), those predatory post-colonial regimes were aided by international support for trade and minerals concessions, while violence, corruption, and deregulation led to "indirect private government", in which the state has lost its capacity for redistribution, but it continues to operate as an instrument of coercion.[22] Global neoliberalism has thus evolved into new organizational forms by offering opportunities for state elites in many parts of the South to re-affirm their interests. In the final analysis, the forms of political authoritarianism that emerged in the region did not rely on neoliberalism only as a self-optimizing mechanism to facilitate global trade, but rather as an economic strategy imposed by force. Although outside the Southern Cone social oppression had not a direct link with the transition to market economies, significative confrontations and unrest began to rise. Rural problems stemmed from the concentration of land ownership and, perhaps, from the commodity-export growth model. Moreover, in rural settings drug trafficking gained ground and provided funding for all sorts of violence. Illicit enterprises, police corruption, smuggling; the expansion of *narcotrafico* in Central America is a well-known story. The drug cartels of Colombia and Mexico were, indeed, lucrative export-oriented enterprises with great entrepreneurial flair, some kind of up-and-coming archetype which was often applaud by neoliberal advocates. If it weren't for the long trail of blood they left. In sum, even the informal economy and the growth of criminal business proved crucial for the successes of neoliberalism in Latin America.

[22] Connell, R., and Dados, N., (2014); *Where in the world does neoliberalism come from? The market agenda in southern perspective*; Springer Science+Business Media Dordrecht, p. 126 – 127.

1.3.2 The Chilean Workshop

Starting from the 1980s, nearly all of Latin America countries participated in a great political and economic experiment, that was the adoption of neoliberal and free market policies. The shift toward the neoliberal policy was built upon the conviction that neoliberalism would bring growth and economic development, and would improve the lives of most Latin Americans. Some nations, such as Chile under the dictatorship of Augusto Pinochet (1973–1990), adopted free market capitalist policies earlier and more fully. In 1976, after the military intervention against the government of Isabelita Perón, also Argentina endorsed these policies. Others came later and adopted less completely the neoliberal policy recommendations. The Pinochet regime in Chile had, in the 1970s, undertaken the first Latin American neoliberal revolution by means of a coup d'état that overthrew the democratically elected government of the socialist Salvador Allende. In order to counteract the mounting inflation, Allende had directed his economic policy toward an increase in the centrality of the state by transferring assets and resources from the private sector to the public domain. The main measures of his macroeconomic policy, i.e., the readjustment wages and price control, would have led to an increase in real wages, thus, a growing demand for basic goods. This would have resulted in a redistributive mechanism, inducing higher levels of production and employment.[23] However, when domestic business elites began to be threatened by Allende's reforms, a coupe d'état was orchestrated with the aid of US governmental agencies in order to establish a military regime. Since the import-substituting strategy had fallen into disrepute, a new approach was called for reviving the economy. However, the economic measures firstly adopted by the Pinochet regime were directed toward the dismantlement of Allende's reform, rather than the improvement of fiscal balance. During the Allende's socialist experiment public enterprises were formed in all branches of the economy. With Pinochet, mines, banks and factories which had been nationalize during the administration of Unidad Popular (1970 - 1973), were either restituted to previous owners or contracted to foreign companies. However, though the re-privatization program carried out under the dictatorship of Pinochet, a number of copper industries were kept into the hands of the state, and rationalized in a way that they would increase profitability by lowering investments.[24]

Only in a second moment did the regime assign a group of economists, later known as "the Chicago boys", the task to reconstruct the Chilean economy. These new figures had attended the lectures of

[23] Dornbush, R., Edwards, S., (1991); *The Macroeconomics of Populism in Latin America;* Chicago, The University of Chicago Press, p. 183.
[24] Castronovo, V. (2007); *Piazze e Caserme. I dilemmi dell'America Latina dal Novecento ad Oggi;* Bari, Edizioni Laterza, p. 203 – 204.

Milton Friedman at the University of Chicago, and they shared with him the same attachment to the neoliberal theories. The story of how they were chosen is an interesting one. Since the 1950s, as part of a Cold War program, the US had funded training of Chilean economists at the University of Chicago to counteract communist tendencies in Latin America. Chicago-trained economists later came to dominate at the private Catholic University in Santiago de Chile. Pinochet brought these economists into the government, where their first task was to negotiate loans with the International Monetary Fund. With the help of the financial institution, they rebuilt the economy according to their theories by making public assets private, by opening up natural resources (fisheries, timber, etc.) to private and unregulated exploitation (in many cases riding roughshod over the claims of indigenous inhabitants), by supporting foreign direct investment and free-trade policies. As a matter of fact, the IMF credits were directly supporting those Latin American dictatorships which were promoting neoliberal reform. Between 1974 and 1975 the IMF approved two *stand-by agreements* to the Pinochet's government, for which it disbursed more than 450 million dollars.[25] Other cases were Uruguay and Argentina, where loans were offered right after the coupe occurred.

Nonetheless, the Chicago Boys were not offering General Pinochet a textbook of economic theory, rather a solution to his main political problem: how to get legitimacy by satisfying his backers in the Chilean elite and by keeping the diplomatic support of the US. Neoliberalism as a development strategy met both these needs. Thus, the regime abandoned the previous strategy of industrialization and looked for growth in the expansion of export industries, which were individuated in mining and commercial agriculture. The economy was reoriented toward international trade and opened to international capitals. In the second half of the 1970s, the petrodollar era, investments did flow into Chile on a massive scale. As the right of foreign companies to repatriate profits from their Chilean operations was guaranteed, financial capital firms mushroomed around this flow. The Pinochet regime managed to control inflation through the devaluation of exchange rate, and eventually, achieved price stability. By the end of the 1970s, nearly 500 firms had been re-privatized by the regime. Another reform that was previously unthinkable was the privatization of the social security system, which allowed individuals to choose their own pension funds, overseen by government regulation. Similar market-friendly reforms were carried out in education and health. Yet, the liberalization imposed a heavy price on the Chilean working class: poverty increased from 17% to

[25] Nemiña, P., and Larralde, J., (2018) *Historical Stages of the Relationship between the International Monetary Fund and Latin America (1944-2015);* in *América Latina en la Historia Económica*; Ciudad de Mexico, Instituto de Investigaciones Dr. José María Luis Mora, p. 218.

45% between 1970 and 1985, and unemployment rose to 20–25% in the capital city, Santiago.[26] Despite the 1982 debt crisis, Chile's monetary stability acted as a demonstration of the ability of markets, rather than of states, to lead to economic development. Economists claimed that the deregulation of the labor market enabled Chile to attain a more flexible and adaptable economy. However, these legislative and regulatory changes were only made possible by a brutal repression of dissidents, which left thousand dead or in exile. As a result, it is not easy for neoliberal advocates to explain the contradiction between the necessity of economic liberalism and the lack of political freedom, which was inherent to the Chilean experience.

2.1 *La Década Perdida*: entering the Global Economy

The Latin American debt crisis of the 1980s marked the end of a century-long period during which Latin America had been gaining ground in the world economy. It also represented a radical deviation from the economic policies that had been in place since the Great Depression. The partial efforts to open up markets made in the mid-1970s, as the region's rapid industrialization process started to slow down, were followed in the mid-1980s by a widespread move toward neoliberalism. Neoliberal policies began to take firm control and remained in place until the first decade of the XXI century, when many countries took on different economic policy paths as a result of political movements that placed more emphasis on social issues and sought to re-strengthen the role of the state. The 1980s were, thus, a period of recession, and this explains why they were aptly labeled by ECLA as *La Década Perdida*, the lost decade. After discussing the origins and implications of the debt crisis, we will look at the economic programs that were launched as a response to it, and which were their main achievements and flaws.

2.1.1 The Debt Crisis

In 1982, the Latin American debt was in the hands of more than one thousand banks. About two thirds of those banks were from the US, but they were also European and Japanese. In fact, the participation of banks from countries other than the US surged in the years preceding the crisis. US banks privileged loans to Latin American and other developing countries, since, inside the US, more and more firms began to be attracted by the emerging stock market, instead of bank credits, in order to

[26] A. Barry, 1997; Graham, 1991 in Stokes, S. C., (2001). *Mandates and Democracy. Neoliberalism by Surprise in Latin America*; Cambridge, Cambridge University Press, p. 32.

obtain financing.[27] Moreover, as we have seen in the previous chapter, for years western banks have been encouraged by the major industrial countries and international financial institutions to assist oil-importing developing countries by on-lending the deposits of oil-exporting countries. Lending money to oil-importing developing countries represented an effective way to recycle the surplus of dollars generated by the peak of oil prices at the end of the 1970s. However, trade imbalances, which became more evident in those countries that were not able to generate enough export to restore their account equilibrium, became a severe constraint to the financial availability of many states in Latin America, as they were dealt with by resorting to greater and greater amounts of external borrowing. Mexico was the first borrowing country whose government announced that wouldn't be able to repay their debts, even though Mexican economy could rely on big exports of oil at that time. Total output was growing and foreign debt was slowing reducing; initially, there was no perception of a possible crisis threatening the stability of the entire financial system. Thus, the reasons for the break out of the crisis are to be found in the global economic environment of the 1980s. In 1981, the "Volcker Shock" brought a sharp increase in short-term interest rates, as the Federal Reserve was trying to put an end to the inflationary spiral that the US was experiencing at the time. The shock entailed significant repercussions on debt servicing, since much of Latin America's external debt had been contracted at floating interest rates. Increasing interest rates meant higher interest payments on foreign debts and, often, the higher payments could only be met by taking on more loans. Real interest rates in the US had been very low right up to the 1960s and were actually negative in the mid-1970s, but then skyrocketed in the late 1970s and remained high for the rest of the century, and this was especially true for rates relevant to Latin America. The situation was compounded by a sharp drop in the real price of raw materials, a softening demand for oil and a general slowdown of investments. At the time, Mexico was clearly overestimating the sustainability of high oil prices, which instead started retracting at the beginning of the 1980s. As reported by James Boughton in his IMF account of the 1980s, the IMF Managing Director Jacques de Laroisière maintained that Mexico's policy mistakes were the result of sharp increases in public sector spending over several years, largely financed by foreign commercial borrowing.[28] When Mexico turned to the IMF for help, it was made clear that the basis for any arrangement would rest on the ability of the Mexican government to find a way to avoid defaulting on its debts. This included to stay alert on interest payments and reach an agreement with creditors. Not surprisingly, Mexican finance minister, Jesús Silva Herzog, held very frequent

[27] Stallings, B., (2014); *La economía política de las negociaciones de la deuda: América Latina en la década de los ochenta;* in Ocampo, J. A., Stallings, B., Bustillo, I., Velloso, H., Frenkel, R., Helvia Velloso Roberto Frenkel (ed.); *La crisis latinoamericana de la deuda desde la perspectiva* histórica; Santiago de Chile, CEPAL, p. 61.
[28] Boughton, J. M., (2001); *Silent Revolution. The International Monetary Fund 1979–1989*; Washington DC, International Monetary Fund Publication Services, p. 282.

meetings with the Federal Reserve Chairman Paul Volker. From these meetings emerged the US commitment to make advanced payments for oil imports, which enabled the Mexican government to avoid default until IMF credits were made available. As it was recognized by de Laroisière, Mexico had borrowed small amounts from over than 500 commercial banks, so that total indebtedness turned out impressive. The IMF early identified the need of cooperating with those commercial banks in order to pursue its strategy. While commercial banks would have needed the Fund expertise in dealing with borrowing countries, the IMF would utilize banks' resources to help cover the borrowers' financial requirements. This "concerted lending" represented the first attempt of involving the private sector in the debt strategy. By making the success of the operation depending on small banks participation, the IMF was able to raise the stakes and diminish the free-rider problem. On the other hand, the IMF made assurances that borrowing countries would have to adjust their economic policies by lowering public sector financing requirements. In March 1983 the program was full on track and the initial phase of the debt crisis was passed.

Although the case of Mexico is emblematic, it could not be considered as explicative of the overall situation, since the crisis that erupted in 1982 severely affected oil-importing developing countries, too. Together with the two oil shocks and the Volcker shock, another exogenous obstacle put at risk the possibility for those countries to service their foreign debts completely. This was the recession that began to spread in industrialized countries over the years 1981 and 1982. The recession arose in the form of a general weakening of markets, which held back the ability of developing countries to generate enough foreign exchange from their market exports. As far as endogenous causes are concerned, long-standing policy errors had a cumulative effect on the governments' management of public spending, leading to a chronic inability to properly adjust their economic policies. As countries were more and more interconnected through broader trade relations and grater capital transactions, the debt crisis erupted in Latin America rapidly spread globally. So, the prospect of failures for overexposed banks worldwide and, in particular, in the US (Latin America's debt was equivalent to 180% of the capital of the nine largest US banks), made the US and other industrialized countries' governments put pressure on the IMF and other multilateral development banks to rescue the banks involved, and to deploy larger amounts of credit than they did in the past. The funds that they made available proved to be, in any case, rather modest relative to the impact of private resource transfers. In addition, this financing was also accompanied by unprecedented "structural" conditionalities, which took the shape of the reform process advocated by neoliberal think tanks, i.e., fiscal adjustments and market liberalization. The huge adjustments in fiscal and monetary policies, as well as in exchange rates, put additional stress on what were already precarious economic structures. The depreciation of real exchange rates, which was necessary in order to support the adjustment of export sector, was unavoidably accompanied by a surge in inflation. Although inflation had already sped up in the 1970s, as was happening elsewhere in the world, in the 1980s it reached proportions never seen before in Latin America. Inflationary spirals were, therefore, an effect, rather than a cause of the debt crisis.

In general, the crisis spurred from the loans made by commercial banks to central governments and SOEs. In Brazil and Mexico, where loans were contracted in order to purse the industrialization strategy, the great bulk of the debt led back to the public enterprises in sectors like petroleum, steel, energy and public services. In addition, governmental development banks got heavily indebted by transferring most of their inflows to those SOEs. However, Chile and Argentina, two examples of early economic liberalization, were characterized by a different pattern. The greater part of their debt, indeed, was attributable to the private sector, and in particular to domestic private banks without public guarantee. These banks had lent big sums to private firms and individuals, which employed bank financing for speculation and consume, respectively.[29] The crises that broke out in the financial sector after the hike in interest rates turned out disastrous, particularly in the Southern Cone. This is how the debt spiral came into being. In the view of Naomi Klein, this is also when Friedman's theories became self-reinforcing. The more the global economy followed his prescriptions, the more crisis-prone the system became, producing the precise type of meltdowns that Friedman considered as the only circumstances under which governments would take his radical advice. In this way – Klein continues - crisis was built into the Chicago School model.[30] As limitless sums of money were let to be free to circulate around the globe at a great speed, and speculators were permitted to bet on the value of everything from coffee beans to currencies, the outcome was a growing volatility. And since free-trade policies encouraged Latin American countries to continue to rely on the export of raw resources such as cocoa, copper, oil or wheat, they became particularly vulnerable to the incessant cyclical crises due to either debt shocks, price shocks and currency shocks. All this created an increasingly volatile and deregulated economic environment. The debt crisis, whose effects were to last nearly until the mid-2000s, coincided with a new era in North-South relations. It was the beginning of the lost decade, a period in which "structural adjustment" took over the former development strategies, making military dictatorships largely unneeded.

[29] Stallings, B., (2014); *La economía política de las negociaciones de la deuda: América Latina en la década de los ochenta,* p. 60.
[30] Klein, N., (2007); *The Shock Doctrine: The Rise of Disaster Capitalism*; Toronto, Knopf Canada, pp. 158 – 160.

2.1.2 Framing "Structural Adjustment"

The beginning of the 1980s brought significant changes in the world economy. The end of inflation in industrial countries, the collapse of primary commodity markets, the emergence of Pacific Asia as an economic power; all these circumstances were at the root of the financial imbalances and crises that started in 1982. Moreover, the shift in the Federal Reserve monetary policy led to a tighter quantitative control of money supplied to bank reserves. Throughout the 1980s, the international monetary system was still subject to a strong turbulence due to the instability of exchange rates, drawing the international financial institutions into a more active role in the formulation of macroeconomic adjustments. With the end of the gold exchange standard, countries around the world adopted a wide variety of exchange arrangements, with the exception of the largest industrial countries, which let their exchange rate float against each other. This posed a significant challenge to the IMF, which took on the task of overseeing the sustainability of exchange rate policies when a broadly agreed objective for international exchange rate policy was still lacking. As a result, the Fund was to surveille the overall stability of the international monetary system and to determine the consistency of members' macroeconomic policies. The World Economic Outlook, which was first formulated in 1969, became in the course of the 1980s, the main instrument to provide policy recommendations to member countries over financial issues. The new approach adopted by the IMF was based principally on a longer-term analysis and on economic theories forged by empirical models.

The Bretton Woods institutions acknowledged that the economic policies pursued in the preceding decades had overestimated the role of the State in controlling and managing national development strategies. The old growth model was attacked by the decline in capital flows to SOEs, on one hand, and by the growing consensus upon the need for the state to diminish its role and to be guided by neoliberal policies.[31] The two institutions maintained that governments had hindered national development, rather than promoting it, as they turned out highly inefficient and corrupted. However, they recognized too late that, in order to solve the financial emergency, radical reforms were to be imposed. Therefore, the IMF and the WB accordingly arranged a double-track strategy to relieve the increasingly deteriorating accounts of the most indebted countries. On one hand restrictive austerity measures were to be immediately enforced. On the other hand, a deeper process of structural transformation was required to adjust the economies to the market forces. Later, this planned

[31] Bulmer-Thomas, V., (1998); *The Economic History of Latin America Since Independence*; Ciudad de México, Fondo de Cultura Económica, p. 353.

transformation took the name of *structural adjustment*. The final point of the institutions' agenda was the defining of a new international economic order committed to the neoliberal values of free markets, private property, and a limited role for governments. To make sure that developing countries complied with their measures, the IMF and the WB attached their loans to a stricter conditionality and to the implementation of structural adjustment programs (SAPs). Because the Bretton Woods institutions detained the "seal of approval", they could force the developing countries to comply with their programs of adjustment. SAPs placed greater emphasis on structural measures to promote the mobilization of domestic resources, to eliminate price distortions, to secure increased access to imports, and to re-order investment priorities in countries craving financial assistance. A standard requirement was for the debtor state to pursue an export strategy at any cost, and without regard to domestic social stability. As the ultimate objective of the debt strategy was to restore the balance-of-payments equilibrium and to enable debtor countries to service its foreign debt, earning more cash through exports was an option all developing countries had to adopt. This was to be accomplished through a combination of wage and price stabilization policies combined with austerity programs. SAPs also included a mix of the following measures:

first, privatization of state and parastatal enterprises in order to reduce inefficiencies and government protection (monopolies); second, high interest rates and credit squeeze in order to reduce inflationary tendencies; third, trade liberalization in order to open up the internal market and expose local industry to world market competition and boost foreign trade exchange; fourth, domestic demand management leading to a lowering of state budgets and decreasing expenditures in the social sector; fifth, currency adjustments in order to improve the balance of payments by raising import prices and making exports more competitive; and sixth, free-market prices in order to remove distortions resulting from subsidized food and fertilizers and from import taxes on luxury items.[32]

As these adjustments necessitated a constitutional reform, juridical and institutional changes were introduced, along with new schemes to privatize social services. The two institutions also decided that the provision of further loans would be conceded only if countries were successfully implementing the neoliberal policy requirements.

In order to frame better what the structural adjustment consisted in, two chronological phases may be identified. The first phase required a "shock therapy" in order to restore the balance-of-payments

[32] Fernández Jilberto, A. E.; Mommen, A., (1996); *Setting the Neoliberal Development Agenda: Structural Adjustmnet and Export-led Industrialization*; in Fernández Jilberto, A. E.; Mommen, A., (ed.); *Liberalization in the Developing World. Institutional and economic changes in Latin America, Africa and Asia*; London, Routledge, p. 6.

stability. This consisted in a rapid liberalization of prices, the devaluation of national currencies, and the tightening of fiscal policies. These actions would have permitted governments to stabilize their economies by fighting inflation and reducing their fiscal debt. The following phase involved the liberalization of trade, the deregulation of markets, the privatization of state-owned industries, but also cuts in state spending on welfare and subsidies. Altogether, these measures would have allowed market forces to drive economic recovery. Indeed, most of the countries in the Global South which committed to SAPs were compelled to expose their economies to international trade and finance, and in order to be able to pay back their debt, they would have to expand their export shares and open their financial account to the private and mostly foreign capital flows. The Bretton Woods institutions jointly worked on loan provision by designing cross-conditionality programs to link international lending to the implementation of the SAPs, and this synchronic task eventually led to the crystallization of a shared economic and financial doctrine. The challenge posed by the crisis also imposed the modernization of their organizational and managerial structures, while the relations with other multilateral organizations became more complex. Recommendations directed to indebted countries became a matter of intense debate between the IMF and the World Bank. While the latter focused on growth by evaluating the optimal level of imports and external financing, the former treated output growth as endogenous, considering domestic savings stability and import restriction as the major factors for the recovery. Nonetheless, in the course of the 1980s the IMF and the World Bank learned to work more closely, as in the case of the Policy Framework Paper, a document that was negotiated by both institutions.[33] Over the years, and with the complete adherence of newly independent countries, the IMF and the WB formalized the practice of providing technical assistance over exchange rate management and over the conduct of monetary and fiscal policies.

The IMF and the WB actually sponsored the neoliberal recipe by celebrating its potential benefits. Countries which would pursue neoliberal policies would be able to augment their national saving thanks to international capital flows and to FDIs, which, by bringing state-of-the-art technology, would build the competitive advantage required to operate in the international markets. Conversely, had countries not conformed, they would have been excluded from the benefits offered by the neoliberal promise of a better resource allocation. In the radical view of Klein, the new guiding logic of the Bretton Woods institutions consisted in "crisis opportunism". The highly ideological administrations of R. Reagan and M. Thatcher were essentially able to use the power of the two institutions for their own ends, and to turn them into the primary vehicles for the advancement of the corporatist crusade. This was also the result of an unspoken process of colonization of the IMF and

[33] Boughton, J. M., (2001); *Silent Revolution. The International Monetary Fund 1979–1989*, p. 822.

the World Bank by Chicago School's economists, which became evident after J. Williamson unveiled what he called the *Washington Consensus*.[34] The concept of structural adjustment, as it packaged together micro and macroeconomic reforms, was sustained by a very simple assumption: countries in crisis would do anything in order to stabilize their currencies and to end inflation. So, when privatization and free-trade reforms were linked together with emergency financial aid, countries had little choice but to accept the whole package. What is more, the distinction between sound macroeconomic policies to maintain external balance and stable prices, on one hand, and policies that determine openness like market deregulation, on the other, was not particularly clear.

The debate about the crisis became particularly intense when, under the leadership of the Reagan administration, a creditors' cartel was put in place among the private and official lenders to Latin America. As a Bank Advisory Committee was set up for each country, creditor discipline was enforced by frequent formal and informal meetings between banks, governments and the financial institutions.[35] Further steps to liberalize the economy were undertaken: most foreign exchange controls were lifted and domestic financial markets deregulated. As far as financial sector is concerned, interest rates were liberalized, forms of directed credit that had been set up during the preceding period were eliminated, and bank reserve requirements were reduced and simplified. A wide range of SOEs were privatized, while public accounts were opened up to private investments. In this latter case, the process was more gradual because of the necessity to adopt regulatory schemes to enforce anti-trust legislation, and to strengthen financial oversight supervision in order to avoid the overexposure of financial institutions.[36] Indeed, without an appropriate oversight, the systemic stability would be put in jeopardy. Notwithstanding this, the new regulatory agenda was carried on at a slow and discontinuous rhythm, and only after a severe domestic financial crisis had broken out. As a consequence, the structural reforms of the 1980s turned out more of a side effect of short-term policies adopted to cope with the crisis, rather than a clearly defined multiyear strategy.

As the international debt problem was not only a problem for less-developed countries, but also a risk for the stability of the US financial system, the US response resulted in a growing concern over banks' capital positions. By the end of 1985, commercial banks worldwide had lent Latin America around $217 billion. US banks only held 41.7% of such exposure, while European banks 37%, and Canadian

[34] Klein, N., (2007); *The Shock Doctrine: The Rise of Disaster Capitalism*, p. 163.
[35] Bulmer-Thomas, V., (1998); *The Economic History of Latin America Since Independence*, p. 356
[36] Bertola, L., and Ocampo, J. A. (2012); *The Economic Development of Latin America since Independence*, pp. 218 – 219.

banks 7.6%.[37] In light of this we can assume that the IMF have never consider default a viable solution to the debt problem. The institution contested that defaulting would have caused indebted countries to lose access to international capital markets, and this would have resulted in higher costs than the sole economic and political costs of adjustment programs. On the other hand, Latin American countries began putting pressure on creditors through various attempts to establish debtor cartels. Example of this attempts are to be found in the Quito Declaration of 1984 and the so-called *Cartagena Consensus*, which, however, failed in reaching their goals. When Michel Camdessus took on the role of Managing Director in 1987, debtor countries even created a Debt Group within the IMF. To weaken these oppositions, since 1985 the IMF had been implementing a new debt strategy that would have kept countries into a one-to-one engagement. Through this "case-by-case" approach, as J. Boughton termed it, the IMF was pursuing a triple goal: to provide "small" financial needs, to adjust economic policies to reduce these financial needs, and to catalyze the provision of additional credit by third actors.[38] These objectives were functional to the implementation of market-based agreements that would have helped borrowers to reconstruct their debt. The new strategy, away from previous concerted lending, tended to focus on adjustment efforts aimed at intervening in borrowing countries' structural conditions under a longer-term perspective. Moreover, IMF programs of lending and adjustments enabled banks to take time to set aside liquidity reserves as a provision against potential losses. In the meantime, a secondary market in sovereign debt was created to give breath to the smaller banks. Summing up, negotiations between debtor countries and creditor institutions carried a significant implication: they lengthened the repayment periods by focusing the attention on adjustment programs that would have restored confidence in those countries. Nonetheless, what was really missing in the IMF strategy was a plan to re-orient policies toward a sustained economic growth. In fact, output and employment rates remained stagnant, and all the efforts made by indebted countries were based on the compression of imports rather than on the expansion of exports. The IMF always played the major role in coordinating the process of negotiations. But when the traditional stand-by agreements were substituted by the Baker Plan (named after the US Secretary of Treasury) in 1985, also the World Bank turned into an active participant of the debt strategy, as its potential for designing sectorial loans and adjustments was recognized.[39]

The Baker Plan resembled the willingness of the Washington institutions to restore a sustained growth through the implementation of structural reforms aimed at increasing the role of the export sector in

[37] Monteagudo, M., (1994); "The Debt Problem: The Baker Plan and the Brady Initiative: A Latin American Perspective"; *The International Lawyer*; Vol. 28, No. 1 (Spring 1994), p. 61.
[38] Boughton, J. M., (2001); *Silent Revolution. The International Monetary Fund 1979–1989*, p. 420.
[39] Stallings, B., (2014); *La economía política de las negociaciones de la deuda: América Latina en la década de los ochenta*, p. 64.

Latin American economies. It chiefly consisted in an increase of commercial bank financing which, concerted by the IMF and other development banks, would strengthen capital by absorbing eventual non-payments. However, little effort was made to reduce the burden of the debt on the assumption that banks would be unwilling to lend to countries that had failed to repay their previous debts. Thus, the success of the Baker plan was limited to the reduction of US banks' exposure relative to the primary capital market of borrowing countries. As already noted, after concerted lending the IMF engaged countries in a case-by-case approach aimed at delivering additional financing in the form of debt obligations, in order to cover the time required to implement adjustment programs and to restore normal financial relations. It is worthy to make clear this point, since it apparently seems a paradox to lend more money when the debtor is not yet able to fulfil previous commitments. A generally accepted view is that those countries faced a liquidity rather than a solvency crisis. This meant that, despite they actually had enough real resources to service their debts, they were dealing with a temporary inability to convert resources into foreign exchange. In light of this, the selected strategy was a debt-raising one because it would have allowed debtors to make their interest payments and, at the same time, defending their creditworthiness. However, many observers noted how the debt strategy had become too entangled with commercial banks' interests, and they asserted that the most indebted countries will never be able to restore their position without a substantial relief from their contractual obligations. Even though the attention of international public opinion contributed to open the way toward debt relief, one big obstacle remained. Despite all the measures undertaken by the IMF and the creditor banks to delay amortization further, the discounted present value on future payments remained undiminished. So, as high interest rates persisted, it soon became clear that a low return from investments made growth impossible.

Another attempt to overcome the crisis originated in Japan, where banks had actively participated in lending toward Latin America. Japan's government initially followed US steps, but soon recognized that a new focus was necessary. At the annual IMF meeting in 1988, Minister of Finance Keiichi Miyazawa, proposed to securitize the debt by converting the old loans in low-interest bonds. This would have occurred under the aegis of the IMF, in a way that would instill more confidence among international investors. The basic elements of the plan, which was firstly rejected by the US, were picked up six months later by the Secretary of Treasury Nicholas Brady, under the new administration of George H. W. Bush.[40] The 1989 Brady Plan was designed to rebuild the US banks capital position, but also to reduce borrowing countries' debt by reversing the region's engagement with international

[40] Stallings, B., (2014); *La economía política de las negociaciones de la deuda: América Latina en la década de los ochenta*, p. 71.

finance. It substantially offered indebted countries a partial debt forgiveness in return for commitments to policy reform along neoliberal tracks. The main vehicle for investment was no longer bank lending, which in the 1970s and early 1980s was dominated by few major institutions, but "portfolio" funds, raised through the sale of Latin American bonds and shares.[41] Under the Brady Plan, the practice of buyback gained momentum, as resources lent to member countries were earmarked for the repurchase of bank loans at prices approximating those prevailing in secondary market. As the plan evolved, banks took advantage of an increasingly sophisticated "menu" of options for participating. In this respect, the Brady plan laid the basis for the relief of large-scale capital flows to Latin America. Investors were thus encouraged by its first success, falling US interest rates, and the feeling that neoliberal reforms were beginning to solve Latin America's economic problems. Finally, the Brady Plan succeeded in providing a coordinated approach in which commercial banks, bilateral official creditors, and international financial institutions all played a role. The legacy of the Brady debt strategy was the realization that countries could not escape from stagnant economic conditions unless their debt-service obligations were reduced to a sustainable rate in relation to anticipated export levels.[42]

In the region, the increasing volume of international capital flows, the debt crisis and the costly period of adjustment which followed it, produced a gradual but radical paradigmatic shift which consolidated the position of Latin American economies inside the process of globalization. In the 1990s, investment began moderately to rise and national savings finally started to growth. Inflation reduced, but not enough. While employment in the formal sector grew modestly, in the informal sector the expansion was overwhelming. The move toward democracy contributed to the consolidation of the new model of development, too. Yet, the structural adjustment program suffered of two main problems: first, the increase in the volume of exports did not produce an increase in earnings as a result of the weakness of commodity prices. Thus, the debt-service ratio failed to improve. Second, the willingness of creditors to reschedule did not guarantee new lending. Official creditors at first increased their lending, but then private sources began to dry up. Small banks proved particularly reluctant, as new money packages for major debtors were often held up for months before being delivered.[43]

[41] Ward, J., (2004); *Latin America: Development and Conflict since 1945*; Second edition, London, Routledge, p. 71.
[42] Boughton, J. M., (2001); *Silent Revolution. The International Monetary Fund 1979–1989,* p. 551.
[43] Bulmer-Thomas, V., (1998); *The Economic History of Latin America Since Independence,* p. 358.

2.1.3 The export-led model

The importance of a growth model based on exports became widely accepted as an integral part of neoliberal ideas inspiring economic and political changes throughout the entire world. Export-led development required qualitative and quantitative transformations: an increase in savings rates, a fall in marginal capital/output ratios, a slowing down of inflation and cuts to unproductive imports. In this way, efficient industries would be permitted to assert themselves without being limited by the size of the domestic market. Moreover, a bias toward exports would generate a growing share of foreign exchange, thus lessening the economy's dependence on foreign capital inputs.[44] As we have seen in the first chapter, in Latin America export-led reforms were firstly carried out by military regimes. Later on, when post-dictatorial circumstances opened the way for democratic transitions, macroeconomic stability remained the major objective for many countries in the region. Export-led reforms also helped weaken the social and political power of the working classes, and achieve the "privatization" of the middle classes, as reduced state intervention caused social demands to be removed from the sphere of the state and transferred into the realm of the market forces. The transition to and the consolidation of democracy certainly affected the shift to the export-led strategy of industrial development. The political strength of the entrepreneurial class, which developed over the previous years, paved the way for well-organized popular sector groups to re-enter politics. So, elections were held to legitimize the post-dictatorial democratic regimes. In fact, far from provoking violent social disorders, Latin America witnessed in the 1980s a flowering of democratic transformations and a gradual revival of competitive capitalism.

Just as occurred with the collapse of the Soviet Union (1991), the refusal of populist-authoritarian politics went hand in hand with the downfall of the state-led economic model. Eventually, the global depression of the mid-1980s resulted in the "sword of Damocles" for all militarist, populist and communist regimes, but also for protectionist and statist economic ideologies across Latin America, Eastern Europe, Africa and Asia. With the collapse of the Soviet Union began the transition toward a new global order, the one of globalization and Pax Americana, as all political barriers to the free circulation of capital faded away. The new order was constructed upon various components: the military supremacy of the United States, the deploy of the technologic revolution (ICT, in particular), and the neoliberal political and ideological hegemony. All these factors underpinned the globalization of financial capitals and knowledge. The international financial institutions, by their side, tried to organize commercial relations by promoting the formation of multilateral organization that would

[44] Fernández Jilberto, A. E.; Mommen, A., (1996); *Setting the Neoliberal Development Agenda: Structural Adjustmnet and Export-led Industrialization*, p. 2.

manage the process of liberalization. Therefore, a new attempt was made in the 1990s to re-launch integration programs that would promote exports without encouraging protectionist reprisals. Regional economic integration, combined with trade liberalization, would take the path of an "open regionalism", a term coined by ECLA in 1994.[45] The first free-trade agreement between a Latin American country an industrialized country was the 1993 North American Free Trade Agreement (NAFTA), which involved Mexico, Canada, and the US. The Central American Common Market was relaunched in 1990, the Carribean Community (CARICOM) in 1992, and the Andean Community in 1995. However, the most significative integration plan was represented by the *Mercado Comun del Sur* (MERCOSUR), which was firstly adopted in 1991 by Argentina, Brazil, Paraguay, and Uruguay, and later, also by Chile and Bolivia. The MERCOSUR was inspired by the neoliberal idea that a liberalized regional market can boost the activities of regional firms. As long as overall imports and exports grew between 1989 and 1993 (see Table 1.3), also Latin America's image improved.[46] The *apertura* has made Latin America the world's fastest-growing market for goods manufactured in the US, and half of Latin America's trade is now with the US. With respect to these evidences, the consolidation of the export-model of growth signified an increased integration of Latin America into the global capitalist system.

Table 1.3 Trade push for ten South American countries, plus Mexico (but minus Guyana, Suriname and French Guyana)

	Exports *1989*	*1993*	*Imports* *1989*	*1993*
Total (in US$billion) of which	101.9	123.2	71.9	136.6
intra-regional, %	11.0	19.2	15.5	16.9
intra-Andean, %	4.1	9.7	5.3	9.2
intra-MERCOSUR, %	8.2	18.5	15.1	19.7

Source: The Economist *1994(47):52*

Under the aegis of the Brady Plan, Latin America also gained a better access to financial markets. As commercial banks restarted lending, Latin American countries contracted new loans and received foreign direct investment. Between 1990 and 1993 more than US$170 billion poured in, of which a third was constituted by private direct investment. Yet, manufactured exports did not compete in the global markets. Thus, the export substitution (ES) strategy was to be centered upon the necessity to

[45] Bertola, L., and Ocampo, J. A. (2012); *The Economic Development of Latin America since Independence*, p. 219.
[46] Bulmer-Thomas, V., (1998); *The Economic History of Latin America Since Independence*, p. 370.

replace high-cost local industrial products with less expensive imports. In this way domestic prices would have aligned to international prices, and the export sector would have become more competitive. As we have seen in the first chapter, the ES strategy, combined with continuous subsidies, was adopted in the three Southern Cone countries (Argentina, Chile and Uruguay) early in the 1970s. The remaining Southern and Central American nations did not pursue the ES model in that period. In fact, the commodity price boom in the 1970s made the traditional primary-export model seem more attractive. The rise in price created a revival of this strategy, which consists in gaining earnings from the export of primary products by taking advantage of favorable conditions in the international markets.[47] This was exactly the case of Venezuela (rich in oil reserves) and Bolivia (oil and tin). These countries both experienced an increase in earnings from commodity exports as a consequence of the increase in international prices. In 1972, Bolivia also began exporting natural gas with a pipeline to Argentina, and even though it is not often recorded, coca paste was another most-exported product, as it provided a great amount of *narcodollars*. Yet, in general, a strategy based on the export of primary commodities rarely leads to success. In fact, few were the republics which managed to expand export earnings at a rate consistent with the accumulation of foreign debt. Concluding, notwithstanding the neoliberal reforms, Latin America's economic performance did not improve in terms of productivity and quality, and the continent's reliance on foreign capital still worries. Savings and investment rates remained low, and inflation high. As the private industry did not created additional jobs, employment decreased and the income gap widened. By the way, the current global trade system reached a scale never seen before. Delocalization of production takes advantage of the growing disparity in the costs of labor force, while international finance has shaped a complex reality by creating big inequalities, but also new solidarities. As a result, the gap produced by the failure of dictatorial and populist regimes in Latin America was easily closed by the neoliberal model, which was radically changing the direction of the economic world system.

2.1.4 Assessment of Development under the neoliberal paradigm

Summing up what examined so far, we can distinguish seven major fields of reforms that characterized the Latin American neoliberal model. *(i)* Government austerity was the main policy implemented during the first stage of reforms, which were primarily concerned with economic stabilization in the wake of the debt crisis. During the second stage, most of the countries in the region carried out some mixture of *(ii)* privatization, (*iii)* trade liberalization, *(iv)* financial liberalization (both of "portfolio" assets and FDIs), *(v)* social reforms (in education, healthcare, poverty relief, and

[47] Bulmer-Thomas, V., (1998); *The Economic History of Latin America Since Independence*, p. 330.

pensions), *(vi)* regressive tax reform, and *(vii)* labor market deregulation aimed at the flexibilization of labor market. Although not all Latin American countries were able to carry out the entire list, most of these countries attempted to actuate most of these reforms. However, though many Latin American countries largely committed to the structural adjustment, their economies were not experiencing relevant improvements, but were rather facing stagnant economic output and worsening of living conditions. The liberalization of trade and finance opened national economies to foreign investments which, however, did not pursue national exigencies. Developing countries had also to cope with the increasing conditionality of loans and the rescheduling of debt payments. Where adjustment programs included cuts in basic public spending (e.g., education, health, and social services), political and social conflicts arose against the austerity reforms conducted by the IMF and WB. Moreover, to reconcile the interests of both the poor and the middle class was a considerable challenge for governments trying to generate the required domestic political support to implement the reform program. J. Boughton classifies protests over adjustment into three types: opposition to government policies, demonstrations in support of governmental opposition to Fund advice, and anger directed at the Fund as a scapegoat for actions the government did not take.[48] So, as the structural adjustment package elaborated by the Washington Consensus was not successfully accomplishing the craved economic upturn, during the 1990s it began to be questioned. It became clear that the economic and financial policies elaborated by the most important international institutions were not sufficient to reach the established goals. The emphasis on increased taxation and higher interest rates in many programs was reported to damage the country's growth potential. Adjustment programs raised strong criticism also over their distributional effects. Was the *trickle-down* approach still adequate, or a more people-sensitive orientation should have been taken? Since extreme income inequalities were often regarded as a source of political pressure, the IMF recognized the need for designing programs that minimize the long-run costs of adjustment. However, it was not always easy for the Fund to compel governments to take measures in favor of the most vulnerable part of the population.

Yet, other areas of the world were experiencing higher degrees of economic growth. The East-Asian "tigers", namely South Korea, Taiwan, Hong Kong, China, and Singapore, were working real economic miracles. South Korea and Taiwan became competitive in the world market thanks to the rise of high-value-added industries. As early as 1986, South Korea was the fifth biggest exporter of manufactures to the United States. South Korean high-tech industries, well before all European ones, succeeded in producing most of the semiconductor memory chips.[49] Following a different path, East-

[48] Boughton, J. M., (2001); *Silent Revolution. The International Monetary Fund 1979–1989*, p. 690.
[49] Fernández Jilberto, A. E.; Mommen, A., (1996); *Setting the Neoliberal Development Agenda: Structural Adjustmnet and Export-led Industrialization*, p. 14

Asian countries were embracing an export-oriented model which also involved state intervention in fostering certain selected industrial sectors. Researches suggested that the success of East-Asian economies did not depend on the self-adjustment of market forces, but rather on a pragmatic and well-directed governance of the market, underpinned by a clear-sighted industrial policy pursued by the state. The state took on an active role in the process of development, by largely investing in leading economic sectors. Even though private investment remained high, public investment was deployed on a counter-cyclical basis, i.e., it offset the reduction in private investment in periods of economic contraction. Finally, those countries strongly supported education. The Asian new-industrialized countries used very diverse combinations of economic policy, so we cannot talk about a single Asian model of development. However, in general, all countries shared two common elements, a sound macroeconomic climate and large investment in human capital. China undertook the export-led model in 1978, as Communist Party's leader Deng Xiaoping started a process of market liberalization. China's rapid growth relied on a state-led export push, but also on reforms giving farmers more possibilities to increase their productivity and to market their crops. China's policy also included tax reforms, currency devaluations and duty-free imports. Productivity gains were highest in the southern provinces, where tax-free areas could attract heavy investment flows from neighboring Hong Kong and Taiwan. In the agricultural sector, East Asian governments kept on supporting investment in high-yielding crops and in manufactured inputs (irrigation, electricity, fertilizers and equipment). Rising productivity in agriculture smoothed export-led industrial growth and prevented governments from excessively taxing agricultural outputs, or overvaluing currencies. This positive protection of agriculture suggests that the East Asian countries were able to avoid the transferring of resources from agriculture to industry. Transfers were rather the result of financial savings, and did not repress agricultural growth. As a group, the East Asian tigers increased their share in global exports from 8% in 1965 to 13% in 1980, and to 18% in 1990.[50] These growth rates were obtained chiefly by exporting manufactured goods. East Asian successful growth rates actually demonstrated to the other countries in the global South that an alternative development pattern could have revitalized their stagnant economies. A growing consensus over Asian and Latin American economists started to defy the prevailing theory of structural adjustment endorsed by the IMF and the WB. This sort of "Southern Consensus" primarily rejected the idea that economic development could be attained by conforming to a general and uniform paradigm. On the contrary, it assumed that policy measures should adapt to initial conditions of domestic and external structures, and should vary over time as conditions change.[51] In response to the mounting criticism, the WB argued that the flaws of

[50] Fernández Jilberto, A. E.; Mommen, A., (1996); *Setting the Neoliberal Development Agenda: Structural Adjustmnet and Export-led Industrialization*, p. 15.
[51] Harris, J., (2002); *Depoliticizing Development. The World Bank and Social Capital*, London, Anthem Press, p. 77.

the neoliberal were to be ascribed to the deficiencies of developing countries' governments, and that the benefits brought by the reforms got often lost because of corrupted political institutions and fragile legal systems.

The effects of the neoliberal policies seriously affected the poorer. People working in the SOEs were often laid off and unemployment widely spread. In addition, as efforts were not sufficient to restore stable economic conditions, the neoliberal policies were tightened in order to accomplish the structural changes expected by the international institutions. Towards the end of the 1980s, the failure of the measures elaborated by the IMF and by the WB to solve the problem of the debt crisis led to a shift in the framing of the issue. At first interpreted as a short-term liquidity problem, the debt crisis was then acknowledged to be a long-term issue concerning domestic dynamics of development. As long as interest rates remained high and prices of Latin American exports depressed, the economic activities would not recover. Although the changes in the economic orientation, Latin American continued to depend on foreign markets and capitals. As the export-led model was extremely dependent on foreign patterns of consumption, the region continued to be subordinated to the high volatility of primary goods' prices. Therefore, a change in the preferences of consumption in industrialized countries would have significative repercussions on Latin American fragile economies. Moreover, the infant Latin American industries were not protected enough vis-à-vis international competition. So, the mixed strategy undertook by the new leftist governments of the 1990s ran into the same defections of the previous models. The local elites, by following their own interests strictly linked with the ones of foreign investors, continued to represent an integral part of the capitalist gears of exploitation, which also presented old-time patterns of foreign domination. As underlined by E. Galeano in its masterpiece *Las venas abiertas de América Latina*, "the symbols of prosperity are also the symbols of dependence".[52] This is because the technology and knowledge received through foreign investments were not elaborated in order to start a domestic and independent pattern of modernization. During the 1980s the regional economy suffered a severe contraction in labor productivity. As we can see from Figure 3.1, during the first years of the 1980s output per head decreased drastically.[53] In addition, the imported technology, even though obsolete, caused the expulsion of a big share of workforce, swelling a huge mass of poor people which concentrated in the suburbs of the industrialized centers, forming the so-called slums. These places also received the unemployed agricultural workers migrating to the cities in order to find alternative ways of subsistence. Slums spread all over the biggest cities of the region: Rio de Janeiro, Santiago de Chile,

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[52] Galeano, E., (1997); *Las venas abiertas de América Latina*; Milano, Sperling & Kupfer Editori, p. 295.
[53] Ward, J., (2004); *Latin America: Development and Conflict since 194*5, p. 39.

Ciudad de Mexico, Caracas, Lima, Buenos Aires and Montevideo. The growing marginalization of the population in these cities also led to a further increase in the level of inequality.

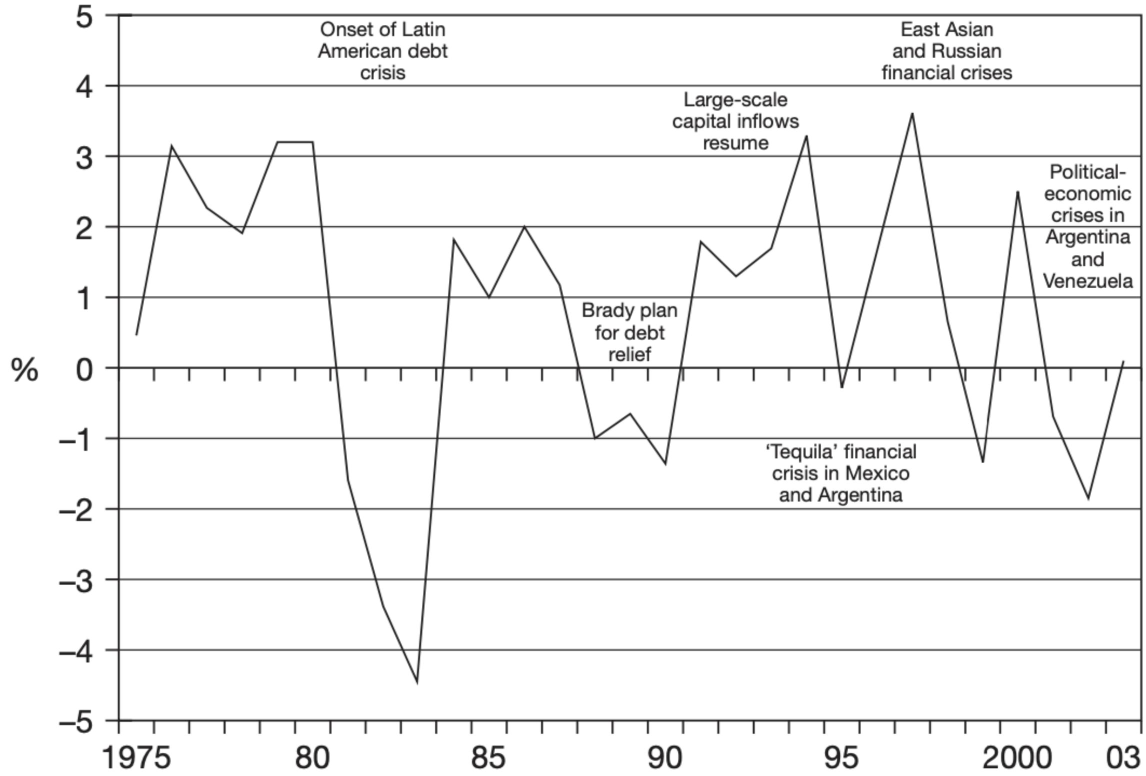


Figure 3.1 Output per head growth in Latin America, 1975–2003* (% change on a year earlier)

Sources: Maddison 2001; IMF 2002. Note: *Forecast estimate for 2003.

The 1990s financial downturns in Mexico (1994-1995) and Asia (1997-1998) reveal us the importance of rapid access to the liquidity required for the servicing of eventual deficits. This is why in both the Mexican and Asian crises, the GDP curve was V-shaped, as growth rapidly recovered after a sudden fall, while the 1980s crisis was L-shaped. The absence of well-organized export sectors in the 1980s meant that Latin American firms were not prepared to take advantage of the imminent devaluation of national currencies. The social costs of the lost decade proved massive. As far as ECLA's estimates are concerned, poverty index over the total population critically grew from 40,5% in 1980 to 48,3% in 1990.[54] The exacerbation of income inequality also contributed to the reversal of

[54] Ocampo, J. A., (2014); *La crisis latinoamericana de la deuda a la luz de la historia;* in Ocampo, J. A., Stallings, B., Bustillo, I., Velloso, H., Frenkel, R., Helvia Velloso Roberto Frenkel (ed.); *La crisis latinoamericana de la deuda desde la perspectiva* histórica; CEPAL, p. 44.

the advances made during the past decades. A critical factor was the fall in real wages in the formal sector, and a growth of the informal sector, since it lowered the pace of human and technological development. The informal sector, in which people do not enjoy of any protective regulation or benefits, today accounts for more than half of all workers in Latin America.[55] More recently, poverty rates started to decline. Yet, this is better associated with factors beyond economic policy. One was increasing remittances from Latin American workers laboring in the developed world, especially in the US. But the main contributor to the reduction of poverty was certainly the fall in the dependency ratio. This ratio measures the number of non-working age people who are supported by the working age population; so that the higher the dependency number, the greater the economic weight upon public accounts. Initially, lower infant mortality rates caused birth rates to stay high, while death rates were falling. However, after a generation, Latin America's birth rates began to decrease until matching the already low death rates. Therefore, the time passed between the fall in death rates and the eventual fall in birth rates witnessed an unprecedented population explosion. Lower poverty rates are not only explained by the increased number of working age people per household, but also by a greater female participation in the workforce. Despite there have been improvements, albeit modest, in lowering the Gini coefficient (the measure of economic inequality), significant areas of extreme poverty remain in Latin America, stressed by class, racial, gender, and regional divides.

2.2 The Bolivian case: overcoming the neoliberal model?

In Bolivia, the transition toward statism ended in April 1952, when a popular insurrection permitted the *Movimiento Nacionalista Revolucionario* to take power (1952-1964). The steps taken to transform the Bolivian society culminated with major political arrangements such as the universal suffrage (July 1952), the nationalization of mining facilities (October 1952), the Agrarian and Education reforms (August 1953 and January 1955; respectively).[56] The National Revolution of 1952 had imposed the advent of a period of economic development characterized by political populism and the emergence of the state as the main economic actor. Up until the National Revolution of 1952, Bolivian economy was dominated by private mining concentrated in the hands of three men better known as the tin barons. The Revolution substantially transferred nearly all of the productive power of the country in

[55] Pineo, R., (2014); "The Free Market Experiment in Latin America: Moving Beyond Past Policies to Search for a Pathway Forward"; *Journal of Developing Societies*; SAGE Publications, p. 178.

[56] Pacheco Torrico, N., (2007); *Deuda externa Bolivia: los ciclos de auge en los precios de los productosde exportación y los ciclos de endeudamiento externo en el siglo xx e inicios del siglo xxi: 1900-2015*; in Velásquez-Castellanos, I., Pacheco Torrico, N., (ed.); *Un siglo de economía en Bolivia (1900-2015),* Tópicos de historia económica, Tomo I; Konrad Adenauer Stiftung, p. 375.

the hand of the State.[57] The financial policy of the new government was oriented towards the development of the industrial sector through the application of specific and differentiated rates of interest. However, despite all efforts to control credits and subsidies, it resulted easy to achieve financial resources at low interests and then diverging the sums towards other types of activity. As this became common practice, in May 1953 the government was obliged to devalue national currency and to peg it to the US dollar at a fixed rate. During the 1960s, the financial system considerably developed thanks to the participation of the Bolivian Central Bank and private entities. The number of national and foreign commercial banks began to increase as new branches were established in different parts of the country, but also thanks to growing amounts of financial transactions. Private banking, however, continued to be regulated by government disposal in favor of the stabilization of reserve requirements. During the 1970s, the state consolidated its position in the economy and reached high economic standards in the context of a positive conjuncture: first, a general increase in the price of minerals and agricultural products (chiefly cotton and sugar), second, a certain differentiation of exports, and third, the expansion of gas exports. However, during the decade external financing almost grew four-fold. The expansion of Bolivian economy lasted until the second half of the 1970s, when GDP growth began to weaken. In fact, the conduction of a flexible monetary policy allowed a greater flow of foreign resources which, by inflating Central Bank's reserves, gave the illusion that the national economy was improving in line with the global pace. Instead, this contributed to the creation of those conditions that were at the basis of the upcoming financial crisis. In addition, at the beginning of the 1970s, a strong demand for US dollars significantly reduced Central Bank's reserves, forcing it to devalue domestic currency. Foreign reserves fell steeply in 1978, as balance-of-payments deficit grew bigger and bigger, and eventually turned negative in 1980. At the beginning of the 1980s, the exportation of primary commodity fell into a profound crisis, as the international demand for minerals and ore was diminishing, prices were falling down, and the mining sector was rapidly decelerating. Decreasing revenues from commodity exports, combined with the boom of external deficits, prevented international financial resources to flow into the country. The contraction of aggregate supply provoked shortages of essential commodities, which had to be imported. Thus, while the demand for foreign currency was growing, the supply was withdrawing, and since the central bank was unable to meet this demand, a parallel, informal market for dollars

[57] Toranzo Roca, C. F., (1996); *Bolivia: Crisis, Structural Adjustment and Democracy*; in Fernández Jilberto, A. E.; Mommen, A., (ed.); *Liberalization in the Developing World. Institutional and economic changes in Latin America, Africa and Asia*; London, Routledge, p. 161.

emerged. This market rapidly became the benchmark for the determination of the exchange rate and of inflationary expectations, which became more and more intense.

The administration of general Garcia Meza (1980-82) marked the culmination of a period in which the military governments, often connected with the drug trafficking, disrupted public accounts. While the capacity of the Bolivian state to generate foreign exchange was degrading, it continued with its time-tested distributive role, also because of the pressure put by different actors inside the economy which, accustomed as they were in the past decades, requested subsidies, low-interest credit, and an increase in wages for public employees. Indeed, as SOEs were suffering deficit crises and lack of liquidity, the backbone of the Bolivian development was subject to tensions that it was no longer able to resist. During the first five years of the 1980s, Bolivia experienced a combination of negative economic circumstances: the contraction of economic activity, the close out of the major sources of external financing, high public expenses and the reduction of state revenues. All these factors caused high and persistent fiscal deficits, which were covered through further external borrowing. The resulting inflationary pressure, aggravated by speculation in the foreign exchange market, accrued inflationary expectations. Eventually, severe social and political conflicts, as well as the mismanagement of economic policies, gave ground to the 1980s hyperinflation. Between 1982 and 1985, various attempts were made in order to tackle the crisis. In these years the government approved six "packages" whose aim was to stabilize the macroeconomic environment and to reactivate production, but without success. The financial system entered a profound crisis, losing its role as intermediary. Nevertheless, the government continued to fix interest rates in behalf of the banking system, and passive interest rates turned negative in the high tide of inflation. Due to the mounting inflation, negative interest rates, and the overvalued exchange rate, financial operations diminished ostensibly.[58]

The hyperinflation, the loss of central control over the monetary policy, and the (quasi) collapse of the financial system seemed to anticipate the "exhaustion" of the state-led model. To confront the crisis, Víctor Paz Estenssoro, in his fourth mandate (1985-1989), promoted a series of neoliberal policies, and established them with the advisory of the economist Jeffrey Sachs in the form of the *Decreto Supremo* 21060. The decree, once approved at the end of August 1985, opened the way to the implementation of a macroeconomic program of stabilization, the first steps of a long-termed

[58] Pacheco Torrico, N., (2007); *Deuda externa Bolivia: los ciclos de auge en los precios de los productosde exportación y los ciclos de endeudamiento externo en el siglo xx e inicios del siglo xxi: 1900-2015*; in Velásquez-Castellanos, I., Pacheco Torrico, N., (ed.); *Un siglo de economía en Bolivia (1900-2015),* Tópicos de historia económica, Tomo I; Konrad Adenauer Stiftung, p. 382.

project of economic and political restoration based on the reorganization of national economy and public balances. It changed the nation's economic structure by imposing Friedman-inspired reforms. V. P. Estenssoro proposed to tighten aggregate demand, adjust relative prices and open up the economy. The major instrument to accomplish this was the decision to allow a single exchange with the US dollar for all currency operations. Moreover, financial markets were liberalized, as well as the market for goods, services and labor. The role of the State was accordingly restructured by rationalizing or decentralizing the activities of SOEs. Thanks to a contractionary fiscal policy of expenditure reductions and indirect tax increases, monetary balance was stabilized in few months. However, have we have seen, the volatility of primary commodities' prices (tin in particular) was a major source of problems. Already at the end of the 1970s the Bolivian mining industry entered a productional and technological crisis as state mining never developed processes of productive reinversion, nor processes of technological innovation. On one hand, the world entered into another technological era: innovation such as substituted minerals for clays and recycled minerals generally diminished the amount of minerals per manufactured unity. On the other hand, the Bolivian economy did not diversify and failed to create large industrial plants. Neither did it solve the problem of weak agricultural productivity. For these reasons, the mining crisis at the beginning of the 1980s had a considerable impact on the decrease of economic growth. The structural adjustment contained in the Decree 21060 was more than a policy of anti-inflationary "shock". Since 1985, Bolivia adopted a new model of economic development, which this time was based on economic liberalization. The adoption of market-oriented regulations marked the dismantlement of economic statism, the alienation of populism and revolutionary nationalism, as well as the weakening of the ideological impact of socialist and labor movements. The new economic model could count on both an active legitimation given by high-income middle classes, the military and small businessmen, and on a passive legitimation from popular sectors, which welcomed any new kind of economic politics that would be able to stop inflation. The new economic policy caused ideological transformation as well, because it had the capacity to change the old political concepts into liberal content. Concepts like socialism, revolutionary nationalism, economic statism, etc., were changed for categories that were charged with another world vision, like: elimination of fiscal deficit, budget equilibrium, free markets, deregulation, privatization, etc. All these economic categories turned into ideological concepts that defined a new political horizon.[59]

A critical part of structural adjustment programs was the creation of an environment favorable for free trade and foreign investment. This comprised a renewed emphasis on the primary-export model,

[59] Toranzo Roca, C. F., (1996); *Bolivia: Crisis, Structural Adjustment and Democracy*, p. 167.

but also the signing of regional and global trade agreements. In Bolivia, neoliberal reforms were firstly adopted in the early 1980s, when the country emerged from Meza's regime. Gonzalo Sánchez de Lozada deepened these measures during his two terms as the country's president (1992–1997, and 2002–2003), by instituting the set of orthodox reforms. The rationale for the radical transformation was based on the fact that the ISI encouraged "deviations" to the correct functioning of the market, and that only when every country would act on the basis of its competitive advantage, economic benefits will flow to all. The privatization of the railway system, which began in 1995, represented a good example of reform aimed at eliminating distortions. It was carried out not only as a mean to renovate the sector through the participation of private investors, but also with the objective of attracting capitals to invest in the improvement of State's infrastructure. However, the result of two decades of neoliberal practices has often been regarded as disastrous. A dramatic redistribution of wealth from the poorest people to the richest exacerbated, rather than reduced, the uneven geographies of development. The neoliberal policies of Sánchez de Lozada brought negative effects upon the Bolivian economy, but even more severe on the living standards of the population lower strata. Wages fell 40% within two years, unemployment grew from 20% to 30%, per capita GDP lowered from 845$ to 789$. Thousands of miners at the state mining corporation were retired, and mid-level bureaucrats were laid off. In the 1990s, the privatization of most publicly owned enterprises further cut public-sector employment. This restructuring of the labor market produced a huge pool of unemployed workers who turned to the informal market for fragile and uncertain subsistence. What is more, during the implementation of the reforms, hundreds of syndicalists and political opponents were kidnapped and illegally detained in prisons all over the country. The process of privatization resulted in a big loss of money for the Bolivian state. As the control over most of the country's economic surplus passed into the hands of foreign investors, the state did not receive the expected benefits. Bolivia's farm economy, which was the principal provider of domestic consumption products, was devastated by the commercial liberalization, due to the stronger competition of cheap supplies from abroad. This led to a massive increase in agricultural imports, which substituted national production, and caused internal migration from the countryside to the urban areas. To complete the picture, the US-driven policy of coca eradication at the end of the 1990s substantially destructed one of the major sources of income and also thousands of jobs directly or indirectly linked to this agricultural production. As the poor shouldered these burdens, incomes rose for the dominant classes, especially local economic and political elites, intensifying the sense among most Bolivians that these elites, together with the transnational capitalist class, had full control of the economy of the country. This was especially clear at the end of the Sánchez de Lozada government, when it was revealed that the president had secretly signed contracts with transnational gas companies in which the royalty percentages were far below those demanded by law. The growing concentration of income and wealth demonstrated that the neoliberal reforms did not enhance equity, and that the privately owned companies turned out uncapable of generating productive dynamics through increased productivity or competitiveness. The result was, indeed, paradoxical, as a model promising to boost exports and competitiveness eventually caused imports to increase and exports to decrease.

There is no doubt that for Bolivia a parallelism between the application of structural adjustment and the intensification of democracy existed, as the economic reforms were paired with the discourse over market democracy. The linkage between free trade and democracy resulted both in policies such as decentralization (the devolution of state power to cities and regions), and in the empowerment of civil society. Many of the duties of the state— health, education, policing—were now transferred to private entities. In addition, under the Bolivian Law of Popular Participation, adopted as part of the neoliberal reforms of the mid-1990s, indigenous and social movements were encouraged to participate in public decision-making at the municipal level. However, despite this plan did recognize indigenous people as legitimate actors, in most cases, it did not function in significantly redistributing resources. This was because pervasive racists stances, but also the continuing control of political parties by local elites, made it difficult for indigenous people to gain any meaningful access to the political process. In this way, civil society represented the site for both the construction of and the resistance to the neoliberal ideology. Finding little space for the exercise of their rights through traditional political institutions, indigenous and popular social movements fought back.[60] New political parties emerged from the demands of these popular sectors, like the MAS (*Movimiento al Socialismo*), which originated from the protests of the *cocaleros*, the coca growers in the rural province of The Chapare. The indigenous leader of this political organization, Evo Morales, actually centered his presidential campaign around anti-neoliberal arguments. With his election in Jenuary 2006, the role of the state began to change again.

The most interesting feature of Morales's anti-neoliberal program begun early in May 2006, when he declared the nationalization of the foreign-owned gas production facilities in the eastern part of the country. As seen above, mines and gas installations were nationalized by the state after the 1952 revolution and run by state-owned companies until the privatizations of the 1980s. Thus, we can say that a long collective memory existed, which associated the State with the legitimate exploitation of what was considered national patrimony, i.e., natural resources. In addition, mining activities

[60] Postero, N., (2013); *Bolivia's Challenge to "Colonial Neoliberalism"*; in Goodale, M., Postero, N., (ed.); *Neoliberalism, Interrupted, Social Change and Contested Governance in Contemporary Latin America; Stanford,* Stanford University Press, pp. 29 – 30.

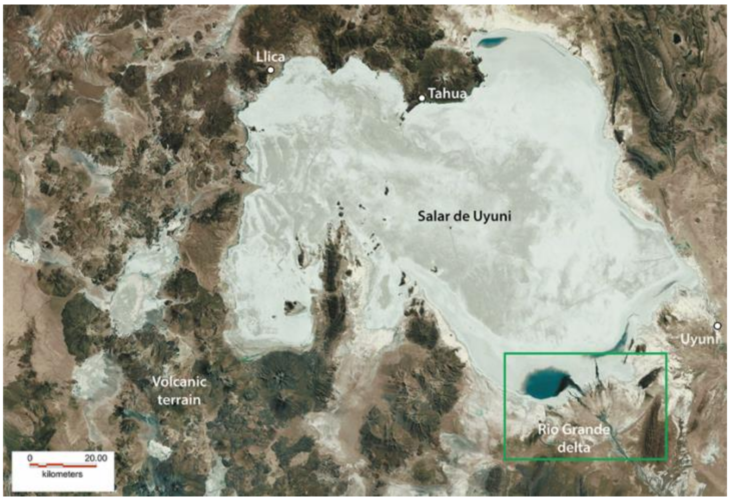
generated a considerable number of jobs with suitable wages and high reputation. So, the privatization of mines in the 1980s was seen by many Bolivians as a blow to the dignity of all the people. By touching these emotional chords, Morales was able to achieve a broad political consensus. The reassertion of the state's role in the economy clearly opposed the neoliberal model of development, but it was not a mere return to the past. Morales did not immediately seize the concessions of foreign companies operating in the gas sector. Rather, they were given six months to renegotiate their contracts with the state. In the meanwhile, he sharply raised taxes and royalties on gas production and created direct taxes from natural gas profits (*Impuestos Directos de los Hidrocarburos*). Previously, companies received on the order of 82% of the profits, which left the Bolivian state with only a small portion. The new taxes, royalties, and renegotiated contracts changed these proportions; now the central government received about 54% of the profits.[61] Thus, Morales's plan of nationalization consisted in a clear-sighted political move which disguised a pragmatic approach with populist rhetoric. Thanks to the fresh profits coming from the taxation of natural resources, Bolivia overturned its financial posture, as government income from oil and gas went from US$173 million in 2002 to an estimated US$1.57 billion in 2007.[62] Moreover, international climate was favorable due to high oil prices. For the first time since the crisis, Bolivia began to experience a trade surplus, as well as large foreign reserves. Eventually, this surplus in its fiscal policy proved to be helpful in coping with the subsequent financial downturn.

For Morales, no contradiction existed between his "mother Earth" discourse and what scholars call "extractivism", i.e., an idea of economic progress centered on the export of raw materials. However, Bolivia's commitment to natural-resource extraction may create quite a few negative consequences for the natural environment in the near future. Even after Morales' exile, the Bolivian economy continues to pursue "extractivist" policies. New megaprojects were ideated, notably the giant new lithium fields in the vast salt flat in the South-West, the *Salar de Uyuni*, whose potential impacts may be cataclysmic. This zone is estimated to contain around 21 million tons of lithium. To understand this number, we have to bear in mind that, as far as overall lithium reserves are concerned, Bolivia is followed by Argentina (19 million tons) and Chile (9 million tons). These three countries have even been named "the lithium triangle".[63] This newly discovered fields led the Bolivian government to plan the construction of lithium-processing plants to begin producing batteries for electric cars.

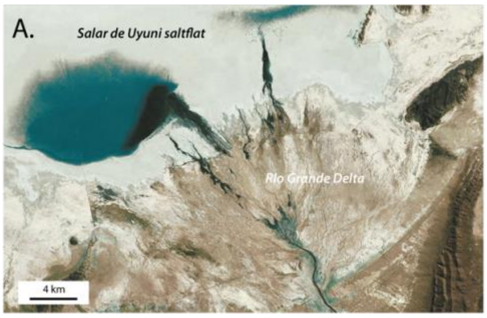
[61] Andean Information Network 2007a, 2007b in Postero, N., (2013); *Bolivia's Challenge to "Colonial Neoliberalism",* p. 38.
[62] Andean Information Network; 2008 in Postero, N., (2013); *Bolivia's Challenge to "Colonial Neoliberalism",* p. 38.
[63] Miranda, B., (2020); *Litio en Bolivia: por qué el país con las mayores reservas de este valioso recurso tiene tantos problemas para explotarlo*; BBC News Mundo; retrieved from https://www.bbc.com/mundo/noticias-america-latina-51666362

However, as with any other non-renewable resources, producing lithium will likely take high tolls on the fragile ecosystem of the *Salar* and the *Rio Grande* delta, where flamingos breed. While critics argue that the government has not yet carried out sufficient water or environmental studies, the Meridian Institute, an independent think tank, concluded that to extract enough lithium to meet even 10% of global automotive demand would cause irreversible and widespread damage to these environments.[64]

In this chapter, I have tried to trace the main political and economic transformations in Bolivia since the national revolution of 1952, describing how the general discourse over political economy has developed throughout the years. Even though Morales' project of development represented a direct opposition to the neoliberal model of the previous decades, doubts remain on the fact that a government that relies on the same capitalist-based resource-extraction pattern that of all previous governments could effectively be termed as post-neoliberal. What is certain is that, by responding to the demands of Bolivia's poor and indigenous citizens, the Morales government put forth an ambitious model of radical democracy, trying to re-embed economic policies within social and cultural structures.



(Aerial view of the Salar de Uyuni and the Rio Grande delta)



[64] Meridian International Research, 2008, in Postero, N., (2013); *Bolivia's Challenge to "Colonial Neoliberalism*, p. 48.

3.1 A new paradigm in the study of political economy

This last chapter consists of a critical overview of the way in which the study of environmental economics has contributed to the emergence of a new paradigm in the global debate over political economy. The first section contains a review of the effects of neoliberal policies over the management of the environment in the global South, and especially in Latin America. I will conclude that, even though the implementation of neoliberal reforms on local environments has varied greatly as a result of different institutional, economic, political, and social conditions, it carried some profound consequences on environmental management in Latin America. However, we should also remember that there are places and people that have adapted well to new conditions, and took advantage of neoliberal policies. In the second section I will shift the focus on the issue of climate debt, and I will explain why it may represent a subversive idea in addressing climate change. In the third section, I will explore the concept of sustainable finance and review its evolution. I will try to identify the main actors and practices that support the cause of sustainable finance in emerging economies. In conclusion, the notion of sustainability in the financial context is examined, together with the role of banks associated with social and environmental concerns.

3.1.1 Questioning environmental management under the neo-liberal paradigm

In Latin America, the neoliberal policies adopted since the mid-1970s have clearly altered the environmental management of industry, forests, water, agricultural land, and fisheries. Major reforms in the management of the environment under the neoliberal paradigm consisted of the privatization and the pricing of environmental services and common property resources. They also entailed the transfer of environmental management to local or non-governmental institutions. Apart from the commodification of unowned, state-owned, or common property resources such as forests and water, Liverman and Vilas noted other environmental effects of neoliberal policies. These include payments for environmental services, deregulation, cuts in public expenditure for environmental management, and the opening up of trade and investment.[65] The cases examined hitherto suggest that Latin America represents the best example of the experimentation and implementation of neoliberal processes and policies, and the subsequent spread of continent-wide privatization of natural ecosystems. Nowadays it is clear that the free trade, the privatization, and the diminishing role of the State have produced such a widespread danger to livelihoods and landscapes that even the promoters of neoliberalism, such as the IMF and the WB, are trying to mitigate the impacts of climate change. The empirical

[65] Liverman, D. M.; Vilas, S., (2006); “Neoliberalism and the Environment in Latin America”; *Annual Review Environmental Resources*, Oxford; Environmental Change Institute; p. 328

effects of these changes on environments, peoples, and economies are highly confrontational and, sometimes, they have provoked radical social reactions. Only in Latin America, millions of people took to the streets to contend neoliberal governments and policies.

On the other side, the mainstream argument in favor of neoliberalism is that, in contrast to the inefficient and high-cost government interventions, the free market is able to improve the efficiency of the global economic system, bringing "wealth for all." Advocates of neoliberal policies often argue that their reforms imply re-regulation, rather than deregulation. Re-regulation is meant as a combination of means to place controls on firms' behavior (such as pollution limits) and rules that guarantee the smooth functioning of the market (such as property rights and investment legislation). It is also frequently noted that neoliberalism in Latin American has coincided with a shift away from long-standing authoritarian or one-party governments and the consequential emergence of more democratic political systems. In light of the neoliberal agenda, nature and the environment provide new opportunities for capital accumulation, and even nature conservation may represent a profit-making activity if transferred to the private sector. In few words, the privatization and the monetization of natural resources promote a more efficient use and conservation of them.
Although critics argue that the free trade, by changing the composition and amount of trade, may result in increased resource demands and pollution, advocates suggest that environmental provisions inside trade agreements may actually improve environmental protection. It is often been argued that neoliberalism, far from being a single, monolithic principle, is best intended as a set of processes contingent on place and time, producing diverse and unpredictable outcomes. Thus, the impacts of neoliberal policies on the environment in Latin America not only depend on the peculiarity of political systems and on the past experience of environmental management, but also on the character of local landscapes and livelihoods.

The underlying economic theory behind the relation between neoliberalism and the environment identify environmental degradation as a negative externality, i.e., a negative outcome of the production (or consumption) processes, whose costs are extremely difficult to quantify. Although negative externalities can be addressed by government, free-market economists argue that this is inefficient because it limits flexibility and provides no incentive to improve environmental performance beyond the limits set by the political authority. On the other hand, free-market approaches are based on internalizing costs through the polluter-pays principle or by allocating quotas for pollution or credits that could be used, saved, or traded. This is the basis, for example, of the 1997 Kyoto protocol, under which a cap to greenhouse gas emissions was introduced in a way that any reduction with respect to the assigned threshold provides carbon credits that can be traded.[66] Neoliberal policies assigning private property rights over natural resources are partly based on the tragedy of commons theory. This theory explains that resources held in common are more likely to be overused by individuals, as they see immediate personal benefits rather than longer-term risks of the prolonged exploitation by the many people. On the contrary, private owners have a greater incentive to protect resources that they own. Thus, neoliberalist ideology assumes that land and other resources such as water and forests are better managed by private owners. As we have seen, also environmental protection is now becoming commodified, as property rights are established in order to value and trade environmental benefits. The basic assumption rests on the fact that the market would set a price which adequately reflects the value of protecting the environment or using it sustainably.

Another approach is based on the environmental Kuznets curve hypothesis. This assumes that wealthier societies tend to request the implementation of environmental protection not only because they are associated with a greater concern for environmental quality, but also because higher incomes allow them to pay for it. However, critics of neoliberal environmental management maintain that free trade, deregulation, and privatization are more likely to destroy the environment rather than protect it. They reject the environmental Kuznets curve since they assert that it only works for a limited number of countries, for per capita pollution data (and not in absolute terms), and for only a few pollutants. For example, most countries in Latin America are below the average income level at which pollution would theoretically begin to decrease. Critics also note that neoliberal trade and investment rules are likely to result in a "race to the bottom," as companies would flee the stricter environmental standards of the developed world in search for lower or unenforced environmental regulations in developing countries. Moreover, the highly unequal distribution of income in developing countries means that inequality will continue to drive environmental degradation. Some left-side theorists also underlined the imperial and colonial pattern of neoliberal processes, since natural resources continue to be expropriated and assigned to private property, commodified, and then, exported to support the capital accumulation of powerful interest groups.

Linking neoliberal reforms to specific environmental impacts is not an effortless task. However, we can generally argue that most reforms caused indirect environmental impacts through changes in trade, investment, and environmental regulation. The NAFTA agreement had significative consequences for Mexico. As Mexican economy was opened up to foreign investment, new

[66] Liverman, D. M.; Vilas, S., (2006); "Neoliberalism and the Environment in Latin America"; p. 331.

manufacturing enterprises, known as *maquiladoras*, or *maquilas*, rapidly emerged. These companies took advantage of cheap labor to assemble products, and then reimported them back into the US without paying high tariffs. *Maquila*-type operations have now spread to many other countries, such as Guatemala and Costa Rica, were low-tariff export manufacturing zones have also been established. Advocates of free trade argued that the NAFTA agreement would support environmental quality. However, a lack of legislation and enforcement, together with a weak institutional framework, have allowed foreign-owned manufacturing companies to violate environment (and labor) laws continuously, causing environmental degradation and health risks in the US-Mexico border region. Evidences of the serious environmental damage caused by *maquilas* in the border cities is to be found in increased air and water pollution, as well as inadequate waste management. The increase in the number of border *maquiladora* plants, from 2000 to 3500 between the years 1995 and 2000, was mostly concentrated in five cities (Tijuana, Mexicali, Ciudad Juarez, Matamoros, and Reynosa), where environmental degradation became increasingly evident. Apart from the environmental impact of individual manufacturing plants, the growth of industrial activity has brought serious environmental effects in terms of environmental footprint and unplanned urban growth. Controversy over potential environmental impacts during the NAFTA negotiations resulted in the establishment of the trilateral Commission on Environmental Cooperation (CEC), an institution designed to address regional environmental concerns, and to promote the effective enforcement of environmental law (http://www.cec.org). In Costa Rica, maquila facilities increased from 10 in 1986 companies to 186 in 1995.[67] However, it is reported that this industrial growth was undertaken without an adequate environmental control from the regulators, and within the context of a lack of information on the environmental aftereffects. The legal framework and the government's *laissez-faire* attitude did little to increase enforcement and compliance, as it was feared that a stricter control would have led to the flight of companies to other under-regulated countries. Few companies at the time reckoned the benefits of a cleaner production, and consequently, they did not consider it as the crucial ingredient to improve competitiveness.

As we have seen in the second chapter, the mining sector has been the most important source of exports for Latin American countries. As the economies opened the doors to foreign direct investments in what had been, until that time, a heavily protected sector, the mining and extractive industry experienced a great boom. By the end of the 1990s, mining represented over 40% of total export earnings in countries such as Chile, Bolivia, and Peru. The restructuring of the mining industry in Latin America represents the litmus test for the evaluation of the implications of globalization upon

[67] Liverman, D. M.; Vilas, S., (2006); "Neoliberalism and the Environment in Latin America"; p. 337

environmental management. The mining sector has been widely blamed for its environmental damages, such as land and soil degradation, depletion of rivers, air pollution, high-energy use, inadequate cleanup of liquid and solid residue, impacts on flora, fauna, and workers health. Substantial improvements in mining practices in Chile were encouraged by the transition from Pinochet's dictatorship, which had often repressed public (also environmental) protests, to the democratic regime. However, the International Institute for Environment and Development (IIED) found that water extraction in northern arid areas (where mining activities are concentrated) is of significative concern, due to conflicts created with other traditional users such as farmers and indigenous groups. In these regions, the use of underground water has reduced the availability of surface water for irrigation and for human-use.[68]

The privatization of water resources is another controversial aspect of neoliberal reforms in Latin America. Water privatization includes the commodification of the entire resource (supply, distribution, waste), or just of the services that provide it to consumers. While the advocates of market-based solutions argue that water should be a private and tradable resource, so that everyone would pay for it and its treatment, critics believe that water, being a basic need, should be provided by the community or through public sector at no-profit and little cost, particularly to the poor.
Once again, truth lies somewhere in between. A minimum level of compensation is required to deliver the poor a basic level of provision, but charges should progressively rise in accordance with the wealth of water users. The most noteworthy case is represented by the Cochabamba's "water war" in Bolivia, where, in 1999, a 40-year concession was granted to a foreign-owned consortium (led by the Bechtel corporation) to manage the city water system. At the moment of privatization, only half of the rapidly growing city of Cochabamba had access to clean piped water, and an increasing water competition between commercial farms around the city was further aggravating the situation. When a steep hike in water charges was decided, a series of protests was staged by an alliance of workers, farmers, and environmentalists, which eventually compelled the government to revoke the concession.[69] In the course of the years, water privatization projects have been opposed by many poor citizens and environmentalists across Latin America, mainly on the grounds that the practice of pricing threatens basic rights, equity, and environmental quality. The water issue also became the symbol of larger anti-globalization movements. However, with many governments unable to pay for entirely public water provision systems, a re-regulation should be designed and enforced in order to require water companies to secure that the poor receive adequate water, and that ecosystems are preserved. The

[68] Liverman, D. M.; Vilas, S., (2006); "Neoliberalism and the Environment in Latin America"; p. 339.
[69] Liverman, D. M.; Vilas, S., (2006); "Neoliberalism and the Environment in Latin America"; p. 345.

State may provide the necessary financial support, and also monitor private performance by ensuring that the terms of contracts would not be breached.

Many studies suggest that the main drivers of economic growth are to be found in human capital and technology. But we should not forget the connection between those aspects and the preservation of natural capital (both the environment and natural resources). If human and natural capital are supported at adequate levels, this will prevent long-run growth from becoming unsustainable. As a result, countries that fail to promote sufficient human capital, and which rely too heavily on physical capital accumulation, would be affected by growing income distribution, poverty, and environmental degradation.[70] This clearly constrain any chance of sustaining economic growth. On the contrary, adequate investments in human knowledge eventually allow for high rates of return to investments in physical assets to persist, and thus, to preserve the incentives to continue investing over time. However, this is feasible only if expanding human assets would be complementary to and regardful of physical assets. As long as human capital is accumulated, it will spill over the population and compensate for the decreasing marginal returns to private investments, eventually leading to a better distribution of income. As the income of poor people is highly dependent on natural capital, the costs of the degradation of natural capital are primarily paid by them. While the wealthy can substitute environmental losses with more private goods, the poor can do this only to a limited extent. This is why the protection of natural capital is most beneficial to the poor and tends to promote more social equity. Furthermore, investments in human capital are generally less environmentally demanding than those based on physical capital accumulation. By properly balancing human and physical assets it is possible to achieve not only a higher degree of social equity, but also of environmental protection, with additional spillovers in favor of the poor. Along the path towards economic growth, human and natural capitals are therefore likely to play both a direct and indirect role in the provision of public welfare.

However, capital accumulation is also affected by significative market failures, especially in developing countries, which are translated into difficulties in collateralizing human capital. This means that, in the absence of government intervention, much of the population needs to rely only on their own savings to finance investments in human capital. However, most of the population in poor countries still not have this capacity to realize such investments without public support, even where high rates of return are possible. This is exactly why the patterns of accumulation of human capital

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[70] Lopez, R. (2006); "Structural Adjustment and Sustainable Development"; in Lopez, R.; Toman, M. A. (ed.); *Economic Development and Environmental Sustainability. New Policy Options;* Oxford, Oxford University Press; p. 154.

(including R&D) and environmental assets are largely dependent on the role of the state. The presumption that developing countries demonstrate a tendency to under invest in human and natural capital is based on the following consideration. In less-advanced countries, the State tends to be controlled by economically powerful groups that are likely to lobby governments for subsidies that benefit them directly, rather than for the provision of public goods and services, whose benefits are only partially obtained. Governments in developing countries face strenuous financial constraints due, for example, to the fact that the countries have little access to international lending sources, and they often spend public resources in dubious investments and unproductive ways, usually at the advantage of the rich. A study for Brazil, for example, shows that in 1998 the federal government alone spent more than 6% of GDP and almost 30 percent of the total federal government revenues in subsidies in favor of the rich. These included direct credits to corporations, financial subventions, and forgone government revenues related to natural resources given free of charge to powerful economic groups with government connections. It is enough clear that a great bulk of these subsidies were not connected to positive spillovers due to firms' investments; instead, much of the tax incentives provided to corporations in Brazil generated rent-seeking behavior.[71]

A recent study of Lopez including 10 Latin American countries shows that over the period 1985–2000, on average the countries spent about 55 percent of their total government budget for the rural sector in private goods or subsidies mainly to the wealthy. Only about 40 percent of the rural government budget was spent on public goods including education, health, R&D, roads and the environment. He found that increasing the share of non-social subsidies in rural expenditures greatly reduces agricultural per capita GDP by promoting a pattern of agricultural growth that is based more on land expansion than on intensification.[72] In countries where there are forests, this extensive pattern of growth resulted in the expansion deforestation. Thus, subsidies in rural areas are detrimental for agricultural growth, social equity and the environment. As long as governments spend a large portion of their revenues in low yielding or even counter-productive subsidies, it is natural to search for governance failures as the explanation for this phenomenon. The form of government also represents a crucial factor affecting the supply of public goods and services. The more democratic the regime, the greater the involvement of the civil society in monitoring government's actions and less the risk for it to be manipulated by small power groups in their favor. Venezuela, Ecuador, and Bolivia are the countries where the degree of accountability and transparency of the government has been most inadequate.

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[71] Lopez, R. (2006); "Structural Adjustment and Sustainable Development", p. 163.
[72] Lopez, R. (2006); "Structural Adjustment and Sustainable Development", p. 164.

Structural adjustment programs turned out not sufficient to promote a sustainable economic growth over time. One of the main elements of inefficiency was the low priority that governments gave to investing in public goods. From this point of view, reforms which focused on cuts in fiscal deficits without paying much attention to the implementation of such cuts, have ostensibly contributed to exacerbate the deep inequalities in the allocation of resources, as well as to consolidate rather than eradicate the "triple curse" effect (economic stagnation, social inequity and environmental degradation). The tools employed to achieve the goal of reducing unsustainable deficits, which was seen as an unavoidable component for macroeconomic stability, carried significative consequences. A general approach was to curtail those public expenditures which were the easiest to do, that is public programs supported by the weakest voting public. On the other hand, to cut subsidies to the rich was politically problematic, as this group was actually able to lobby and bribe influential politicians. For governments, it resulted easier and politically convenient to reduce social expenditures favoring the poorest and least influential sectors. Fiscal adjustments also reduced the already limited funds available for those programs which could help manage and supervise the environmental impact of large engineering projects (such as mining, dam-building, and infrastructures). The reliance on cutting public goods as well as social and environmental public expenditures to reach fiscal equilibrium implied not only a social cost, but also the worsening of that distortion which is the cause for economic stagnation and environmental degradation in most developing countries. The SAPs lost the opportunity of integrating the short-term goals typical of fiscal adjustment with desirable long-run objectives of reallocating public sector priorities for the provision of more public goods. Thus, in a context of under-investment in public goods, it is more likely that further environmental degradation would surface, as well as slower improvements in human capital. In Latin America, the decline of per capita human and environmental wealth, and the slow rates of economic growth, may in part correspond to the growing reliance on foreign financial capitals and to the misled political response to macroeconomic imbalances. Summing up, behind the 'triple curse' effect there is an evident policy failure for governments in investing enough in public goods such as R&D, human capital and in the management of the environment, even though such investments yielded very high rates of return. Instead, they kept on spending great amounts of economic resources in subsidies of dubious economic value. Thus, we can conclude that adjustment has failed to lay the foundations for a sustained, and sustainable, development. Ultimately, even though more recent reforms have promoted investments in poverty alleviation and human capital, they have not simultaneously cut enough government subsidies to support the financial costs that such programs involve. Therefore, the effectiveness of the neoliberal approach has been widely circumscribed, and in some cases, it has contributed to the creation of an unsustainable public debt which makes even more difficult to change the traditional government approach.

3.1.2 The Climate Debt: a subversive idea?

In recent years, many progressive movements have adopted "climate debt" as a slogan to be employed in the context of climate negotiations, and it is easy to understand why. "Debt" describes in just one word a simple notion, that is, losses must be paid. The concept of climate debt addresses the historical responsibility for climate change owed by rich countries towards the poor ones. As now it is the global South which is demanding payment to the rich (which are usually seen as the creditor), the idea of "debt" is redefined in the form of a systemic problem, rather than a mere financial issue. Even though there is no commonly agreed definition of what is meant with the term "climate debt," it is useful to provide a conceptualization in order to understand the principal tenets of this framework. We can define the climate debt as part of a more general ecological debt accumulated by the industrial countries of the global North with respect to the global South, in view of resource despoilment, environmental damages, and the free occupation of environmental space to dump wastes like greenhouse gases. Since the early 1990s, thinkers in Latin America have developed variations on the concept of ecological debt that address various unsustainable patterns of resource use. These patterns encompass not only carbon emissions, but also the overuse of natural endowments such as forests and fisheries. The theory of climate debt, which has also been developed upon earlier structuralist theorists, is characterized by two main features: it is both *international* and *intergenerational*, i.e., accumulated by current and past people and owed to future generations.[73]

The discourse around climate debt can be divided into three main components: the first relates to the costs of adapting to the impacts of the excessive emission of greenhouse gases that cause global warming, and whose side-effects are extreme and frequent climate events like floods, droughts, storms, disease, and much more. The second component is the cost of mitigating the effects of climatic changes by means of reorganizing societies and economies in a way that greenhouse gas emissions are drastically reduced. The third element of the climate debt - also called the emissions debt - refers to the fact that the atmosphere's capacity to absorb greenhouse gases has been historically used by the North. Given that there is a very high correlation between economic growth and greenhouse gas emissions in the current technological context, the Global South is left with no space to growth without exacerbating the greenhouse effect. As a result, the only way to compensate this

[73] Pickering, J., Barry, C., (2012); "On the concept of Climate Debt: its moral and political value"; C*ritical Review of International Social and Political Philosophy*; 15:5; p. 669.

debt is for the rich countries to drastically reduce their own emissions (Bullard; 2010). However, the solutions to climate change proposed so far have been centered on a top-down approach, which preserves the status quo and which de-contextualizes it from the historical process that have contributed to its emergence. On the other hand, the notion of climate debt may offer a counter-hegemonic discourse that directly tackles the imbalances that have accrued with the exploitation of local environmental resources. Unlike many other conceptual climate frameworks, the climate debt one can count on a bottom-up support among Southern and Northern NGOs.

Latin America is, once again, the best context for the implementation of a climate debt scheme, due to its history of foreign debt, but also to its considerable contribution to the global export of natural resources to the detriment of Indigenous peoples' livelihood, landscapes, and biodiversity. We are living in an era in which the world is rapidly and radically changing, and it is in this context that new solutions to the global climate crisis must be pursued. Following the Copenhagen UN climate change conference in 2009, many nations in Latin America proposed a reparation policy based on climate debt, as states in the Global South, which were the least contributors to the carbon-dioxide emissions, will ironically be the most vulnerable to the consequences of extreme weather events. In fact, for developing countries, potential negative impacts are disproportionately related to the benefit they receive from "extractivist" practices of natural resources and intensive food production. The experience of many Indigenous groups in Latin America clearly reveals this reality. Even with a marginal increase in global temperature of 0.5 degrees, we will likely see agricultural devastation, the depletion of natural resources integral to Indigenous practices, and the breakdown of traditional knowledge systems. National and international governance institutions, which are perhaps more interested in continuing their policies of "extractivism" in the name of development and private corporate interests, have long been opposing the attempts of Indigenous people to strengthen the relationship between the management of the environment and their traditional practices and ancestral wisdom. Through a delegitimizing process, Indigenous peoples' ways of perceiving space and time have been relegated to a mythology that belongs to the past, rather than a body of living knowledges that must hold weight in contemporary policy creation.[74]

Common arguments in favor of climate debt focuses on moral responsibility. Countries that have emitted the greatest share of emissions have the moral responsibility towards low-emitting countries for the impacts of climate change. Moreover, these moral responsibilities are such that they constitute a debt that is rightfully claimable. There are at least three ways in which climate debt could be repaid.

[74] Santos, D., (2021); "Climate Debt: a model for Indigenous Latin American self-determination?"; E-International Relations; p. 2.

The first is by distributing emissions rights in such a way that they effectively compensate developing countries for the historical despoilment and, at the same time, allow developing countries to rise their emission shares in order to accommodate their development needs. This proposal place emphasis on the idea that emissions debt should offset past overuse by discharging the allocation of future emissions rights to developing countries. Developed countries should rapidly curb their emissions and provide finance to help developing countries to adopt low-emissions technologies and to adjust to the adverse impacts of climate change. The second possibility rests on the need to directly compensate less-developed nations for the adverse effects of climate change. The primary factor in evaluating the amount of each country’s debt may be the magnitude of its cumulative share of global emissions since the times of the Industrial Revolution. Another alternative could be to allocate emissions entitlements on an per capita basis, and to compensate for previous overuse by compelling developed countries to finance any reductions needed in developing countries to meet their per capita quota.[75]

Nonetheless, several objections have been raised over the legitimacy of climate debt claims. A critical one lies on the belief that excessive emissions do not result in any moral obligation, nor in any other kind of debt. For example, this argument was brought at the Copenhagen conference by the United States’ chief negotiator Todd Stern, who asserted the categorically rejection of any “sense of guilt or culpability”.[76] On the other hand, supporters of climate debt, such as Climate Justice Now movement, argue that climate debt, as any other form of debt, does not assign guilt or direct culpability, but rather the responsibility for bearing costs of damage made. Another objection relates to the intergenerational character of climate debt, as it claims that it is unconvincing to hold countries responsible for the conduct undertaken by who came before the current generations. In response to this assumption, it is argued that the passing of the debt from a generation to the next is also a feature of sovereign debt. This is because the current treatment of sovereign debt is basically underpinned by the universally accepted principle that agreements must be kept (*pacta sunt servanda*). Under international law, when a sovereign borrower defaults it is treated as it has breached a contract. Unless the creditor decides to cancel the debt, the borrower is obliged to repay the loan, while the creditor retains the legal right to claim it. Even though, generally speaking, debts should not be transferred from one generation to another, in the case of climate change both the benefits and the costs have been passed across generations through the individual participation in the economic system. However, in order to be more feasible, climate debt logic needs to move away from the rigid demarcation between developed

[75] Pickering, J., Barry, C., (2012); “On the concept of Climate Debt: its moral and political value”; p. 677.
[76] Pickering, J., Barry, C., (2012); “On the concept of Climate Debt: its moral and political value”; p. 672.

and developing countries as the only categories to identify creditors and debtors. On the contrary, fair shares of responsibility should be addressed to those groups and individuals who can be effectively felt guilty for the damages produced to the environment.

While the principles sustaining the ecological debt theory are certainly compelling, the implementation of debt schemes raises several problems, as a policy proposal to establish a mechanism through which calculate and collect the debt is still lacking. Calculations are usually focused on carbon emissions and are determined by the abatement costs which have not been paid. However, advocates of climate debt tend to resist the attempts to put a price on it, since it would not be appropriate to value environmental goods and services according to capitalist, and neoliberal, benchmarks, which are in the first place seen as the main responsible for the ecological crisis.[77] In addition, the question over how to collect the ecological debt is rather controversial. Available literature offers three main approaches to address the issue. The first retains that debt repayments should serve to fund protection programs and renewable energy projects to shift the global economic development away from the reliance on non-renewable resources. The second approach focuses on climate debt as simply a payment to creditors, which should be allowed to employ it as they wish.[78] The third, and most preferred, model seeks to use climate debt as a leverage to cancel external foreign debt accumulated by countries in the Global South, which fuels a cycle that can only be satisfied by performing eco-unfriendly practices. In the context of Latin America, the latter option could be the most suitable, given the long legacy of unsustainable debt ratios. Moreover, Latin American countries have represented the earliest test for the IMF's and World Bank's neoliberal development policies, which have eventually reinforced their dependence on "extractivist" practices and on the export of commodities to the industrialized core.[79] However, the lack of practical application has quite limited the space for climate debt to be adopted as a framework in global environmental negotiations. In any case, the concept of climate debt has been often employed by civil society and non-governmental organizations as a campaigning tool. Invoking climate debts should not be intended as a mere remuneration, but rather as a way of providing a framework for understanding how responsibilities should be distributed. In light of this, we can argue that it is the vision of climate debt which held the political weight, not its implementation. Although some aspects of the debt can be certainly counted and calculated (for example, the costs of clean technology, restoring devastated forests, shifting to sustainable agriculture, or building climate-ready infrastructure), the real amount of the climate debt

[77] Martinez-Alier, J. (2002); "The Environmentalism of the Poor: A Study of Ecological Conflicts and Valuation"; Cheltenham; Edward Elgar Publishing; p.249.
[78] Warlenius, R., Pierce, G., Ramasar, V.; (2015); "Reversing the arrow of arrears: The concept of ''ecological debt'' and its value for environmental justice"; Global Environmental Change 30: 21; p. 26.
[79] Wallerstein, I. (2004); "World Systems Analysis"; Durham; Duke University Press; p. 24

remains unmeasurable. In fact, it is much more than a matter money; climate debt is the symbol of over 500 years of unequal relations between, and within, rich and poor countries. Still nowadays, the neoliberal economic and ideologic super-structure, which is also endorsed by many leftist parties worldwide, supports a model principally based on transnational “extractivism.” We begin to see the situation we find ourselves in. The global web of capitalism connects the dependency upon fossil-fuels of the North to the alteration of landscapes in the South, and the dynamic interaction between these two elements is at the core of the analysis over the degradation of the environmental and human capital. Furthermore, moving beyond “extractivism” does not seem a real possibility for countries like Bolivia, which remain so deeply dependent upon their natural resources.

In this section I have tried to clarify the concept of climate debt and to assess its value for conceptualizing responsibilities associated with climate change. However, climate debt may not offer a helpful frame for promoting global justice in the context of international climate negotiations, as it is only one of the existing means of resolving political conflict over the problems posed by human-induced environmental transformations. As far as these political considerations are concerned, even if we accept that the idea of climate debt is coherent and morally plausible, this does not mean that it must necessarily be adopted in the context of climate negotiations. While this frame may have played a valuable role in giving voice to the claims of some developing countries, alternative frames are more likely to be embraced in the institution of binding agreements. For example, the concept of a ‘carbon budget’ is now emerging as the scientific and policy benchmark for quantifying the maximum level of carbon dioxide that is allowed to be emitted in order to stay within the danger threshold. Although some aspects associated with the term “budget” may appear similar to those of “debt”, this idea does not stress the divisive relationship between debtors and creditors. On the contrary, it proposes that all countries should take part in a common “budget balancing”.[80] Climate debt represents one of several possible frames to address responsibilities for climate change. On one hand, the problem rests on the fact that if accurate estimates cannot be produced, assertions of climate debt are likely to be interpreted more as political rhetoric rather than concrete policy proposals. Climate debt is characterized by a form of bonding rhetoric, which means that it is aimed at motivating people who are already similarly disposed. On the other hand, by virtue of its peculiar rhetorical emphasis, this framework may contribute to the struggle for a broader range of political objectives. Indeed, the use of climate debt helped to direct the attention to the concerns of countries and civil society groups that had had little influence in climate negotiations.

[80] Pickering, J., Barry, C., (2012); “On the concept of Climate Debt: its moral and political value”; p. 680.

In conclusion, we should recognize that employing this concept in support of a meaningful and fair agreement on climate-related responsibilities may sound quite demanding. In addition, developing countries' emissions are growing rapidly (as in the case of China and India) and, in cumulative terms, they have already exceeded those of developed countries. Thus, some countries that were previous creditors may eventually become debtors, and vice versa. In light of this, addressing the problem of climate change need not only to take into account past patterns of emissions, but also to put together a comprehensive plan for the fair distribution of future rights and responsibilities. As the scope of climate debt is clearly circumscribed, alternative frameworks may emerge which seek to build bridges, rather than divides. However, a minimum compensation for the climate debt may consist in developed nations recognizing the damage done, and adopting a universal declaration on the rights of the environment to ensure that past abuses will never be repeated in future. This requires a systemic change, both in the North and in the South, which would need to break the historic relations of inequality, one and for all, by cancelling present debts and preventing new ones from emerging. We find ourselves at a political moment of great importance. Climate debt certainly represents a powerful rhetoric that challenges the international neoliberal discourse, but it may also provide the base for building a global movement which aims at both resisting the present brand of ecological reform and offering new strategies and tactics that directly threaten the major centers of political and economic power. These are the reasons why climate debt is such a subversive idea.

3.2 The rise of Sustainable Finance

In the aftermath of the second oil price shock of 1979, developing countries began to face a growing amount of international payment obligations. While industrial countries reacted to the deterioration in their terms of trade with higher interest rates and higher prices for their exports, developing countries, especially oil-importing ones, resorted to financing from multinational banks and multilateral institutions. Overall, debt burden was exacerbated by three main factors: first, a dramatic increase in real interest rates; second, poor returns on money borrowed; and third, deterioration in the terms of trade. As, over time, the inability to repay international debts spread to many developing countries worldwide, it became evident that repayment of this debt through increasing the share of exports was causing serious environmental degradation in these countries. The hallmark of the production of these exports was that they were resource-intensive, little value-added and, as noted by the structuralist critic, marked by deteriorating terms of trade. Thus, the expansion of exports, combined with the impoverishment in the countryside resulting from the debt-induced economic crisis, clearly contributed to the human-driven processes of deforestation and loss of biodiversity. In addition, as the value of forests, water, and biodiversity was not expressed in market terms, these resources were undoubtedly being undervalued and overexploited.[81] Public awareness of environmental problems has gradually led to the development of environmental regulation and liability legislation. Although environmental liability carries a real risk for companies and investors, it has also created significant business opportunities for companies which sought to innovate. Now, corporate environmentalism, i.e., the adoption of environmental-friendly practices and corporate social responsibility, constitutes the main driver for brand differentiation, product development, and thus, competitive advantage. The next step is to further expand the point for corporate environmentalism to the wide-embracing notion of sustainable finance. Sustainable finance does not only mean that investors would disinvest from environmental-damaging stocks, but also that they would look for firms which gain competitive advantages through good environmental and social habits, and public reputation. While in the US and Europe we are beginning to witness the first signs of a virtuous circle connecting public and private concerns with the needs of financial markets, the very concept of fiduciary responsibility is being under attack, as critics argue that it should be expanded to include the broader interests of capital shareholders, moving beyond profit maximization logics.

The financial sector has not always kept up with changes in corporate environmentalism. Most banks, insurance companies, pension funds and other financial institutions have proved relatively slow to

[81] Jah, R., Schatan, C.; (2001); "Debt for Nature: A Swap whose Time has Gone?"; Mexico; ECLA; p. 7.

recognize that environmental risks are also potential financial risks. In the past a real problem was represented by a lack of track records, measurement tools, and commonly accepted benchmarks; nowadays, however, these are no longer obstacles, as a number of environmental and social rating agencies began to provide rating systems based on eco-efficiency and other indicators. Legislation has been one of the initial drivers for such a change, posing the conditions for market demand to expand, and serving as a catalyst for the transformation of financial markets. But, beyond the importance of legislation in managing pollution thanks to the "command and control" approach, another less acknowledged force influence the behavior of financial investors. This is the power of financial liability, i.e., when legislation identifies the borrower of an asset as the responsible for a certain environmental delict, while the lender and the owner may be found co-responsible. This occurs when legislation proves the connection between an environmental harm, an economic activity, and the financiers to that activity, generating the motivation for the financial entity to act more conscientiously. Once conditions are set in legislation, financial risks are more likely to be accounted for by both lenders and investors. As the risk is actualized, money-lenders would avoid it by increasing the cost of capitals associated with hazardous assets. As demonstrated in the case of global warming, overfishing, or deforestation, markets alone do not reflect (or internalize) environmental costs and risks into the economy, and thus, governmental regulation is required. Today, environmentally risky engagements in the form of loans, assets trade, insurance coverage, or stock exchange needs to be carefully evaluated in order to avoid financial losses. In addition, as both consumers and businesses started to care about the eco-efficiency of products when they make purchase decisions, also investors have to track how this aspect influences the competitive strength of companies which they invest in. If on one side of the coin is risk, on the other is opportunity. As investors seek to improve the financial performance of their portfolios, an innovative element comes into play. By eliminating risky enterprises and including eco-efficient ones, investors demand a growing commitment to environmental protection which may, indeed, create new space for financial opportunities.

These opportunities have given rise to a new class of mutual, eco-efficiency funds which seek to invest in companies that meet certain well-defined sustainable development criteria. The first two funds of this kind in Europe were *Bank Saracin*'s Environment Fund, created in 1995, and *Storebrand*'s Environmental Value Fund. In 1998, *SBC* and *Credit Suisse* began to implement sustainable development criteria into some client portfolios. Around the same time, two Swedish banks also launched environment funds (*SEB* and *Foreningsbanken*).[82] However, the investment

[82] Joly, C., (1999); "The Greening of Financial Markets"; in Hoist, J., Lee, D., Olson, E., (ed.); *Finance for Sustainable Development: Testing New Policy Approaches*; New York; United Nations publications; p. 286.

community has generally resisted environmental and social screening or commitment into socially responsible investments (SRIs) on the grounds of certain ideological and operational bias. First, as believed by Milton Friedman and the Chicago school economists, capital should have only one goal, yield maximization. Second, also fiduciary responsibility means profit maximization, and SRIs are seen as restricting the investment choice, leading to less diversification and lowers returns. As SRIs involve a subjective judgment, it is impossible to apply an index which statistically measure investment data, making it rather expensive relative to traditional investment practices. However, whatever merits might free market capitalism have as dogma, it did not prove feasible in reality, as short-run profits today may mean long-term losses tomorrow, particularly if environmental liabilities are ignored. In the present world, the only way a major corporation can make long-term profits is by acknowledging social responsibilities, and by acquiring good reputation trough a conscientious behavior. In the case of savings and pension funds, the interests of owners should include, in addition to their mere financial interests, also their social and environmental interests. Moreover, the concept of fiduciary responsibility needs to be revisited within a framework of prudent financial management, by expanding fiduciary legislation to include criteria of sustainable development. Because the current fiduciary statute defines the interests of owners too narrowly, capital flows have not really moved in the direction of sustainable development. Thus, there is an urgent need to speed up the process by creating the adequate market demand through socially responsible investments legislation.

While it is essential that all nations embark in the path toward zero emissions, it is also obviously that rich countries have vaster resources for financing it than poor ones. This is even more true if we remember that richer countries are, in the first place, the major responsible for the environmental crisis. Time is ripe to start talking about "sustainable finance", *in primis* by addressing industrial and financial policies as an integrated framework for building a greener global economy. Industrial policies will be required to promote technical innovations and, more broadly, to adapt existing clean energy technologies, as each country should specialize within its specific conditions. Governments should become the larger investors in renewable energy and in energy efficiency. In this respect, *green bonds* may represent a cheap and accessible way to provide financing to eco-efficient projects. The response to the 2008 global financial crisis highlighted the fact that the Federal Reserve is actually able to supply unlimited bailout funds to private financial corporations that were just "too big to fail." Similarly, green bonds at long-term zero-interest-rate may be issued through various public entities, such as the World Bank, and injected into the global economy. The Fed would then purchase these bonds, enabling the various public entities to inject those funds into the global economy and to pursue all the projects falling under the global agenda of sustainable development.

Despite such a framework has not yet been introduced into policy discussions at the Federal Reserve, green bonds are becoming more and more crucial at the European Central Bank. The Financial Times reported in December 2019 that the ECB president Christine Lagarde was "pushing to include climate change considerations in a review the central bank is due to hold into the way it conducts monetary policy. Because the [European] central bank is by far the biggest influence on financial conditions in the market, it can make a significant difference to investment decisions that determine how Europe's climate transition goes".[83] The green bond financing proposal may involve the world's two largest central banks in printing the required money as they did during the 2008 financial crisis, not to keep alive the Wall Street's financial elite, but to bail out the planet in this ultimate, desperate appeal.

3.2.1 Sustainable Finance in Developing Countries

In developed countries we are just beginning to see the outlines of a virtuous circle, connecting public concerns, environmental legislation, corporate environmentalism and financial markets. Here, it has taken about thirty years to get from grass roots public awareness on environmental legislation to the beginnings of sustainable investing. But can the developing world afford to pursue the same transformation, and at the same pace? Or is the pace of environmental devastation pushing towards an acceleration of this process? How can environmental concerns combine with the priority of alleviating poverty and creating jobs with better wages? The challenge of sustainable finance in the developing world may spur truly innovative responses to such questions. Nonetheless, the attention of financial institutions in emerging markets has long been centered upon the discourse around economic growth, without accounting for environmental problems. Today, the process of globalization of capital markets should be oriented towards the cause of sustainable development, and not only to GNP growth. Social criteria, as well as clear standards of eco-efficiency and eco-effectivity, should accompany the flow of private and public financial capital and knowledge from North to South. The world-wide deregulation of national financial markets has been playing a pivotal role since the sharp increase of capital flows of the 1970s. Moreover, the strong growth in foreign portfolio investment seems destined to continue in future. While most of the required foreign capitals would come from the private sector, the public sector will have to offer new subsidies and guarantees to encourage the monitoring of environmental standards of investment portfolios in the developing world. Investments of multilateral developmental agencies and northern governments may prove important for the reason that they may "trade" economic resources for environmental policy reforms, much as the IMF and the WB did in the case of structural adjustment programs of the 1980s. The

[83] Sandbu, M., (December 2, 2019); "Lagarde's Green Push in Monetary Policy Would Be a Huge Step"; *Financial Times.*

globalization of financial markets and the fast integration of emerging markets into the global financial system makes environment-minded capitals readily available. Therefore, practices of environment investment screening should be aimed at ensuring that capitals in emerging markets are employed in the most eco-effective way. Even though their base is in developed countries, multinational corporations will need to focus more and more on how to apply the new criteria in their operations in emerging markets.

However, there is still little awareness about environmental protection being good for profits (by cost reduction, anticipatory compliance, green image and better employee relations). In the view of many, the environment is still considered to be a financial burden, rather than a potential opportunity. In order to change this perspective, two things should happen at once: first, institutional investors should be motivated to search for, and invest in environmental leaders in emerging markets. This can be achieved with the help of legislation activity. Second, both local companies and MNCs should make themselves more attractive to foreign capital by putting in place environmental reporting and action plans that shows their commitment to environment protection. In addition, multilateral development agencies and governments may contribute by making available local environmental plans, as well as consultancy and reporting services, which would help companies to practice corporate environmentalism in a way that financial market can recognize and reward their commitment.[84] Eventually, the greening of consumer markets in the Global North could be tied to the greening of companies in emerging markets, which seek to gain wider shares of developed countries' market by promoting their eco-friendly practices and products. Given the challenge posed by this transformation, developing countries will be the recipients of growing amounts of capital flows. Nonetheless it is important to acknowledge that the resources needed for the sole adaptation to climate change are much more than what is now available. A report published jointly by the Inter-American Development Bank (IDB), the ECLA and the World Wildlife Fund (WWF) estimates that, in Latin America, it will "only" require between 17-27 billion US$ to adapt to the physical impacts of climate change. The same report predicts that the overall costs of dealing with climate change in the region will amount at around 100 billion dollars by 2050.[85]

[84] Joly, C., (1999); "The Greening of Financial Markets"; p. 299.
[85] Vergara, W., Rios, A., Galindo, L., Gutman, P., Isbell, P., Suding, P., Samaniego, J., (2013); "The climate and development challenge for Latin America and the Caribbean: Options for climate-resilient, low-carbon development"; New York; Inter-American Development Bank World Wide Fund for Nature; ECLA; pp. 13-14

Meirovich *et al.* offer an outline of the financial mechanisms and instruments that may be employed to transfer financial resources into climate change programs of developing countries, Latin American countries in particular.[86] He identifies two main mechanisms:

1. *National Climate Funds*: a national climate fund allows countries to collect, and manage both international and national capital inflows related to climate change by grouping them into one, centralized fund. This fund, in turn, would allocate resources through a variety of instruments in order to finance "green" projects in the country.

2. *National Carbon Markets*: they represent the first attempt to use a market mechanism to reduce greenhouse gas (GHG) emissions by pricing them. Because of the smaller involvement of the state in this mechanism, revenues from carbon markets cannot be directed towards national priorities. However, in this way economic efficiency is maximized and corruption minimized.

In the case of the National Climate Funds, the following financial instruments are to be adopted. Far from suggesting a one-fits-all approach, the instruments discussed below are appropriate only if matched with specific economic contexts.

a. *Non-concessional and Concessional Loans*: Whether these loans are characterized by longer repayment terms and low interest rates, attention must be devoted to ensure that funds are actually allocated to climate change objectives. Ministries of finance play a key role as they may create climate change plans (with a clear portfolio of projects and transparent budget mechanisms) that would facilitate the recipient countries in allocating the international aid to "green" projects.
b. *Multilateral and Bilateral Grants*: they can be used to help capitalize the financial mechanisms related to adaptation, forestry, and environmental preservation.
c. *Guarantees*: guarantees help to mitigate and manage the risks associated with the feasibility of the project by compelling the guarantor to fulfill the obligations of a borrower to a lender in the event of non-performance or default of its obligations, in exchange for a fee. Guarantees can cover the entire investment, or just a portion.
d. *Insurance Instruments*: these consist in risk transfer and risk prevention mechanisms. Instead of relying on international loans to finance post-disaster expenditures, governments should use insurances, particularly for low-to-medium loss events that happen relatively frequently. These mechanisms are, economically, more efficient to create risk transfer mechanisms by shifting loss responsibilities from the state to the capital market investors.

[86] Meirovich, H., Peters, S., Rios, A., (2013); "Financial instruments and mechanisms for climate change programs in Latin America and the Caribbean. A guide for Ministries of Finance"; Policy Brief N. IDB-PB-212; New York; Inter-American Development Bank; p. 1

e. *Debt and Debt-for-Climate Swaps*: Debt swaps involve the sale of foreign currency-denominated debt by the creditor nation to an international investor (either a non-profit organization or a central bank). The investor can then exchange this debt with local currency, shares in a national company or development projects. The strong point of debt swaps is that they are financed at no extra fiscal cost to the recipient government, as payments are immediately redirected to the coffers of the debtor country.[87] Only very recently have debt swaps been expanded to include climate change programs. As the positive relationship between the debt crisis and deforestation became more and more evident, environmental organizations started to argue that debtor countries may repay creditor countries by linking debt reduction to the conservation of forest and other "green" projects. Debt-for-climate swaps represent a mean of facilitating this type of issue linkage. The idea of debt-for-climate swaps was initiated by Thomas Lovejoy, who articulated the rationale for his theory while working at the World Wildlife Fund (WWF). Basically, he argued that the financial crisis in developing countries resulted in a substantial reduction in their already scarce environmental budgets. Moreover, the increased emphasis put on export promotion led to a growing exploitation of natural resources. Therefore, the protection of the natural environment in developing countries may be matched by the demand for debt relief. The ECLA identifies two kinds of debt-for-climate: "private swaps" and "public swaps". Generally, a "private swap" engages three participants: first, an international organization or development bank, which usually initiates the process by agreeing to purchase part of the debtor country's international debt at a discounted price in the secondary market. Second, a national NGOs, which is primarily responsible for implementing environmental action. Third, one or more governmental agencies in the developing country, such as the central bank, which agrees to convert a portion of the country's external debt into domestic currency obligations. On the other hand, in a "public" swap, a developed country government takes the place of the international conservation organization, while the other two parties to the agreement remain the same.[88] Despite debt-for-climate swaps have been very scarcely used so far, partly because of the complexity of the negotiations involved, in the latest versions they have become simpler, gaining importance in terms of the amount of debt involved and financial support to environmental projects. Yet, debt-for-nature swaps are likely to have a say in the global environmental and financial scenario.

3.2.2 Defining Sustainability in the Banking System

To begin with, we must acknowledge that the term "environmental sustainability" is somehow controversial, as the environment cannot be sustained in a vacuum. Therefore, if we want to cope with the issues of sustainable development, we must first tackle problems of poverty, equity, and justice, and do it forthwith, as the well-being of the social context is the essential condition for the

[87] Meirovich, H., Peters, S., Rios, A., (2013); "Financial instruments and mechanisms for climate change programs in Latin America and the Caribbean. A guide for Ministries of Finance"; p. 2 – 5.
[88] Jah, R., Schatan, C.; (2001); "Debt for Nature: A Swap whose Time has Gone?"; p. 9.

implementation of environmental-friendly practices. So, if we agree that sustainability is a broader concept than the mere protection of the environment, then we have to consider the contribution of banks and other financial entities in dealing with sustainable development. It is now clear that financial corporations and institutions which operate with the only goal of capitalizing all the gains in the interests of nominal stakeholders are socially, and ethically, unsustainable. When looking at the broader concept of sustainability, the consequences of financial behavior should be considered, assessing profitability and responsibility with respect to the social costs borne by the society as a whole. In this respect, *public development banks* will play a major role, in particular in developing countries, in channeling resources from international lenders to specific projects in the field of renewable energies and technological innovation. A public development bank is a national financial institution whose mandate is to promote socioeconomic development by investing in specific projects or economic segments. This definition entails the public participation in the financial system with the goal of correcting the factors that create market failures. Market failures often cause credit constraints, as they prevent intermediaries from evaluating the true credit risk of certain projects or economic sectors. This is partly due to information asymmetries, which occur when a financial intermediary cannot obtain accurate and verifiable information about a client's ability to repay the loan. Given the high costs of obtaining such information, private financial entities may decide not to participate in the market and not to grant the loan. The inability, or unwillingness, of private financial intermediaries to assume certain risks may also be due to the high opportunity costs of allocating capital to businesses which are less attractive in terms of risks and returns. In most Latin American countries, systems for overseeing financial transactions are usually inefficient, slow, and costly. So, in general, risks tend to be over-estimated, causing loans via private channels to be either denied or provided at very high cost.

The most efficient measures for solving the problems connected with market failures such as information asymmetries are to be found in the nature of the banking system itself. Advances can be achieved by means of banking regulation reforms that improve the information infrastructure and that promote innovation by strengthening financial transaction security. Reforms may create the space in which innovative financial products and new technologies can be invented and developed. Even though new financial practices such as mobile banking may help to overcome logistical difficulties, broader measures must be taken to promote competition and decentralization in the banking sector.[89] Public development banks are part of a broader system of *social banking*, which is characterized by

[89] De Olloqui, F., (2013); "Public Development Banks. Toward a new paradigm?"; Washington D.C.; Inter-American Development Bank; p. XVIIII

ethical and sustainable practices. Despite there is no precise and commonly accepted definition of social banking, we must acknowledge its existence. I would define social banking as a type of banking which, by using classic and innovative financial tools, aims at positively impact people, environment and culture. The most important financial instrument in the case of social banking may be: affordable savings accounts, micro-loans, "green" investments and also "gift money". Weber and Remer identify two main groups of social banks. These are *poverty alleviation banks* in the Global South and *ethical banks* in the Global North.[90] Concluding, social banking may directly address the major financial deficiencies in the emerging countries by enhancing lending to and investing in organizations that benefit people, the environment and culture. Practices of social banking may also influence people indirectly, by showing that a different approach to banking is both possible and necessary, and by actively participating in the wider discussion about the future of the financial system.

[90] Weber, O., Remer, S., (2011); "Social Banking", in Weber, O., Remer, S., (ed.); Social Banks and the Future of Sustainable Finance; New York; Routledge; p. 2.

Conclusions

This dissertation has tried to establish a connection between the economic development models historically adopted in Latin America and the wider discourse about climate change and environmental sustainability. In order to do so, the main theorical approaches to the issue of development were examined, and how the shift from one model to another has affected political and economic regional context. The studies analyzed in this paper have showed that the financial environment of the 1970s and 1980s was critical to the crystallization of the economic relationship between Latin American countries and developed countries in the North. Economic instability was directly intertwined with the region's specialization patterns and development models. Even nowadays, instability gravitates around natural resources, commodities export, and access to financial markets. The volatility associated with these exogenous factors has often led to episodes of "truncated convergence" – as termed by Bértola and Ocampo – in which period of economic expansion were followed by periods of rapid contraction.[91] Economic instability was also accompanied by institutional instability, as political and economic institutions developed at a very slow pace. It resulted that the shift in development policies and paradigms toward economic liberalism was not immediately matched by the emergence of political liberalism, at least until the 1980s. This is why the debt crisis turned out a real shock, overturning both the economic and political system of the whole continent. In this context, the international financial institutions took on a new and crucial role, becoming landers of last resort for countries threatening the default. Eventually, the transition from the state-led to the export-led model was necessary for the integration of Latin American countries into the international financial markets and the global economic system.

This study is consistent with previous researches on the matter in asserting that, under the neoliberal paradigm, the region lost ground to developed countries both in terms of economic and social development, as it was unable to take advantage of the opportunities brought by the wave of globalization. Inequality increased not only in relations with developed countries, but also between and within the individual countries of Latin America. Attempts to overcome the dominant free-market pattern did not succeed in adequately adapting national economies to the increasing demand for those social and financial needs that would have helped a better allocation of resources between all stakeholders. In terms of environmental protection, mega-projects, deforestation, soil and water depletion, driven by the intensification of the "extractivist" model, are threatening the existence of the region's biodiversity and traditional livelihoods. This is why social policies are not enough to

[91] Bértola, L., Ocampo, J. A., (2012); *The Economic Development of Latin America since Independence*, p. 261.

make significative advances in terms of increased social equity and environmental protection. As long as the global economic system continues to reproduce the current patterns, any advance in technology, education and production will never be able to significatively reduce still high levels of social inequality.

Even though it may never be adopted as a strategy in international environmental negotiations, the case of climate debt remains a strong rhetorical framework which may inspire further considerations about the nature of North-South relations. As it is now broadly recognized that the protection of the environment is closely connected with social issues, financial activity should attain new, stringent requirements. A brief review has also been provided about the mechanisms and instruments which may be adopted in order to raise the required financing to implement sustainable projects and practices in emerging economies. An interesting instrument to overcome both the financial and the climate debt may consist in "debt-for-climate swaps", which would exchange debt reduction with programs aimed at tackling climate change. In line with more recent trends, future researches may focus on the environmental aspects of the international financial market, and how governments and institutions may incentive the improvement of the efficiency of sustainable financial circuits in emerging economies. Both private and public financial institutions are likely to play a major role in investing in projects that enhance resilience capabilities, and which may contrast the impacts of climate change. New banking practices may emerge, which, by influencing people's everyday life, may indirectly bring a change in the way we perceive the relation between climate change and economic development. In view of the evidence brought in this dissertation, studies in the field of political economy may consider the correlation between economic and environmental factors as the critical point in the development of new economic theories. By exploring the evolution of industrialization strategies in Latin America, we have been able to discern the major causes behind the region's backwardness, and this has allowed us to assess the main implications of a more sustainable path toward development. In conclusion, even though it is never easy to look at the past through the lenses of today, this is necessary in order to understand the errors made and to find new solutions to the problems we are currently facing.

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