

# A Note on Argentina, Its Crisis, and the Theory of Exchange Rate Determination

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## Abstract

Argentina's crisis at the end of the twentieth century surprised economists. Argentina turned from a "Latin American miracle" to an unprecedented failure. This article looks into the crisis stressing the role of the exchange rate regime and emphasizes the overvaluation of the real exchange rate as a part of capital's strategy to decompose labor and restructure capital-labor relations. Argentina's crisis resulted from the combination of capital's strategic success and the recomposition of labor in the late nineties.

*JEL classification: E11, F32, F41*

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The rate of profit does not fall because labor becomes less productive, but because it becomes more productive.

—Marx (*Capital*, vol. III, section XIV)

## I. Introduction

Why did capital accumulation falter in Argentina during the nineties even though the country was the IMF's most brilliant student? Why did Argentina crash even though capital's ability to exploit labor improved on an unprecedented scale? Why did it stumble even though global capital had in Argentina more than fertile ground for its reproduction? These are questions that many scholars have tried to answer with little success. In general, the blame is placed on the state for failing to push reforms far enough, or on the contrary, for being too interventionist. However, it is clear that Argentina's capitalist state did more than its fair share to warrant the expanded reproduction of capital. It pushed through neoliberal reforms far deeper than in most countries. It intervened, there is no doubt about it, but to let capital take full control of society and not to displace it.

In this note, I will try to provide an alternative explanation of the crisis of capital in Argentina. I will explain how the crisis was not the result of Argentina's lack of success in applying the so-called "structural reforms." I will try to show that Argentina's crisis was the result of the contradictory character of capital's strategy to control Argentina's labor class. This strategy had as its main weapon the "convertibility plan" that included the convertibility of the currency, the opening of the current and capital accounts of the balance of payments, and the deregulation of the labor market, among others (see Carassai 1998). I will show that this strategy was successful in its objective of increasing the exploitation of labor by capital. However, capital's success would become the reason for its own failure, since it would create the preconditions for its crisis.

In the following section, I will discuss the reasons for the implementation of the convertibility regime and the presumed evolution of the key macroeconomic variables. I will show that most analysts used the same basic theoretical framework when discussing the convertibility's future evolution. In section 3, I will comment on the assumed overvaluation of Argentina's peso, which was seen as one of the main faults of the convertibility. I will also provide an alternative evaluation of the exchange rate policy. Instead of following a pragmatic approach (such as the determinants approach), I will work with a Marxian approach (following Anwar Shaikh's work). In section 4, I will discuss the implications of such a framework for the evaluation of capital's accumulation in Argentina during the nineties as well as for the understanding of the crisis of valorization of capital. I will show that the crisis of convertibility was the crisis of capital and was not a sign of its failure but of its success in restructuring Argentina's productive organization. In section 5, I present the main conclusions.

## 2. Convertibility, Overvaluation, and Capitalist Strategy

One of the key instruments for capital's success in controlling labor in the nineties was the overvaluation of the peso. The combined strategy of fixing the exchange rate of the peso to the United States dollar while establishing the dollar-convertibility of the domestic currency and completely eliminating restrictions on current and capital account transactions, what was commonly known as the "convertibility plan," induced an important appreciation of Argentina's peso.<sup>1</sup>

This policy not only increased the value of the domestic currency but also precluded the monetization of the labor conflict through inflation. Now, any wage concessions by firms would have to be absorbed by profits or by increased productivity. While overvaluation of the currency put at risk many individual capitals (especially small enterprises), it was in the interest of capital as a whole to restructure and gain greater control of the labor process and the reproduction of society. During the eighties, high inflation was an important expression of class struggle (Bonnet 2004). Capital, being unable to control labor's demands for wage indexation and facing serious difficulties in sustaining its hegemony

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1. To avoid the confusion that abounds in the discussions on exchange rate, a few brief definitions are required. The real exchange rate (RER) is an index that expresses (approximately) the inverse of the value of a currency. A currency is undervalued (overvalued) when the RER is high (low) in relation to some equilibrium level. For example, the peso would be undervalued when the dollar, and thus the RER, is too high.

over society, used its control over prices to translate this conflict to society as a whole. In the meantime, Argentina's economy suffered a violent and regressive productive restructuring (Aspiazu and Notcheff 1994). Within this process, which relied on capital's concentration and centralization (Basualdo 2000) and ever-higher inflation rates, capital looked forward to regaining control over labor.<sup>2</sup> The convertibility plan was thus a means for the consolidation of capital's rule and not just the beginning of some new process (Féliz 2004; Féliz and Pérez 2004). The plan allowed for the consolidation of capital's hegemony while satisfying, at least in the short run, the interests of productive capital and financial capital (Basualdo 2000). While the convertibility plan gave productive capital (in particular, concentrated capital) greater control over the direct exploitation of labor-power as it allowed capital to restructure labor processes, to find new places/spaces for valorization, and to reduce the value of labor-power, it also gave financial capital the stability it needed to be able to obtain important short-run profits implied by high real domestic interest rates and a massive external public debt.<sup>3</sup>

Although the convertibility plan was mainly an instrument of capital, most mainstream economists saw it mainly as a means to put an end to rampant inflation and economic inefficiency (Galiani, Heymann, and Tommasi 2003). As a means of economic policy, the convertibility was analyzed as basically a neutral, even benevolent institution. After years of high inflation and especially after the hyperinflationary shocks of 1989 and 1990, labor gave in and accepted the convertibility of the currency and the whole set of structural reforms (the convertibility plan) as a needed medicine for Argentina's "illness."<sup>4</sup> The subsequent decomposition of labor meant a reduction in its power to counter or oppose market reforms. For many years to come, neoliberal economic policies became something technical and not political; thus, policies could not be rejected on "political" grounds.<sup>5</sup> Capital had reestablished its hegemony over society by turning economic policy into a nonpolitical issue (Barbeito and Lo Vuolo 1998).

As stated above, one of the most common critiques of the convertibility plan was that although it had allowed for the reduction of inflation, the real exchange rate established at the beginning of the plan was too low for its intertemporal sustainability (among many others, see Canitrot 1995; Fanelli 1998; Feldstein 2002; Perry and Servén 2002; Calvo,

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2. The difficulties for capital's control over labor were reflected in growing labor conflicts. Strikes and public protests reached their peak in 1988. According to Pozzi and Schneider (1993), the number of conflicts between 1987 and 1989 represented more than 62 percent of all recorded labor conflicts since 1980.

3. The new hegemonic bloc constituted around the convertibility plan included mainly concentrated national capitals and transnational financial corporations (Basualdo 2000). They participated both in the process of restructuring of public debt and in the privatization of public enterprises and social security, two of the juiciest new spheres for capital's (re)production.

4. In a nutshell, labor accepted the implementation of structural reforms after having suffered the effects of hyperinflation (which created great fear among the population) and being betrayed by their most important organization (the CGT, General Conference of Labor). The fact that the government that implemented the reforms was led by a traditional prolabor movement (the Peronist Party) also helped to facilitate their passing through parliament. For more on the political economy of the reforms, see Battistini, Deledicque, and Féliz (2002).

5. In talking of composition and decomposition of labor, I follow Cleaver (1992). With the concept of class composition, I refer to a particular structure of power within the existing division of labor. On one hand, capital tries to structure a particular distribution of intraclass and interclass power that will maintain adequate control over labor to allow for a smooth process of valorization. Labor, on the other hand (with different levels of success), systematically confronts, rejects, and resists this control. They try to recompose the structures and distribution of power so as to change the correlation of power against capital (Cleaver 1992).

Izquierdo, and Talvi 2002; Alberola, López, and Servén 2004). The most widely cited sign of overvaluation of the peso was Argentina's growing current account deficit (Mayo 1998). In fact, during the nineties, the current account deficit was 2.6 percent of GDP on average, peaking at 4.3 percent in 1998.

According to the neoliberal economists (from the political Right), if market forces were allowed to work by themselves, domestic currency overvaluation would be corrected (Buscaglia 2001; Powell 2002; de la Torre, Levy Yeyati, and Schmukler 2002). The lack of competitiveness of national producers would force them to reduce their prices or go bankrupt. If they managed to reduce their prices, this would be the result of higher productivity and/or reduced costs. In this conception, the state should not intervene within the market but has much to do in helping firms reduce their costs, especially by reducing the direct as well as the indirect cost of labor (Gerchunoff and Machinea 1995). During the nineties, several steps were taken in this direction. Not only were most economic activities deregulated, but also the state took serious steps to reduce the cost of firms, in particular labor costs. Deregulation of the labor market was impressive, and reduction of taxes on the use of labor force was important (Battistini, Deledicque, and Félic 2002; Pérez 2001). Besides, the state took several steps to generate new markets for private-capitalist businesses—in particular, the privatization of state firms and the creation of mandatory pension funds. As an alternative/complementary proposal, neoliberal economists maintained that a reduction in public expenditure could be helpful in the process of price deflation (Gerchunoff and Machinea 1995).

While most critical (Left or progressive) economists in Argentina disagreed with the idea that market forces would revert by themselves the overvaluation of the currency, in any case, most of them thought that it could not be done without an important increase in labor productivity in export- and import-competing industries, which would require active state intervention (Lascano 2001; Gerchunoff and Machinea 1995; Diamand and Notcheff 1999). Besides, they believed that this could not be done without high cost in terms of output and unemployment of the labor force, since prices would not be flexible enough to regain competitiveness within the framework of currency convertibility (Gerchunoff and Machinea 1995). However, as we will see, although the prognosis was good (market forces would not work on their own), I believe that the economists' framework of analysis was somewhat flawed, for they sustained the belief that even within the convertibility, with higher productivity, the probability of the collapse of Argentina's economy could be greatly reduced if not eliminated (Diamand and Notcheff 1999).

To everyone's regret, as we shall see, although labor productivity grew at an outstanding rate and while GDP grew faster than in many decades, in the end the economy stumbled, falling into its deepest crisis since the thirties. In my opinion, it was not the lack of success in adjusting but the contrary that caused the crisis.

### **3. On the International Value of the Peso**

As I said, the main criticism of Argentina's economic policy for both the mainstream and its critics was that the peso was overvalued, as could be judged by the persistent current account deficit. But was the current account deficit the best sign of overvaluation of the currency? In any case, was the overvaluation of the peso a real problem for capital

accumulation, or would the restructuring of Argentina's capital and the weakening of labor as a class be enough to avoid the collapse of the scheme? To answer those questions, we need an appropriate theory of real exchange rate determination.

The real exchange rate (RER) can be defined as the ratio between the price level of foreign production and the price level of domestic production, both expressed in a common currency. In algebraic terms,

$$rer = \frac{p^*}{p} e \quad (1)$$

where  $p^*$  is the foreign price index,  $p$  is the domestic price index, and  $e$  is the nominal exchange rate (pesos per dollar). That is, when the RER is low, the value of the domestic currency (in this case, the peso) is high in comparison with the dollar.

A common way to calculate the RER is to take as a proxy of the relevant price index the producer price index or consumer price index of each country. In the case of Argentina, the real exchange rate has shown the following performance (Figure 1).

Many discussions on Argentina's RER have presented as complementary evidence of overvaluation of the domestic currency the fact that during the nineties the measured RER was very low compared to its level in the eighties. In the case of my estimation, for example, the average level for the RER from 1991 to 2001 was 20.7 percent lower than in the period from 1980 to 1989.<sup>6</sup>

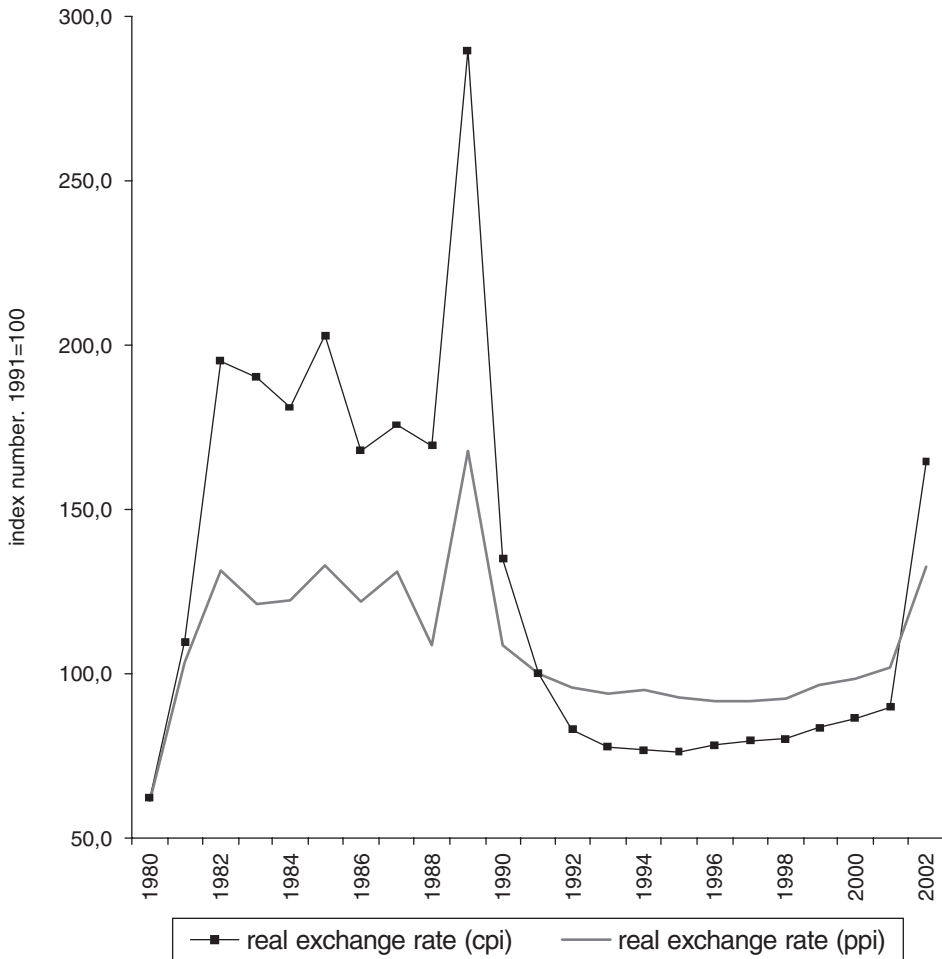
Another way of looking at the problem, that was usually taken as an example of currency overvaluation, was to present the level of nominal wages expressed in dollars. An excessively high dollar wage level would thus imply an overpriced domestic currency. Again, Argentina's experience showed that the dollar value of the nominal wages jumped by 117 percent between the eighties and the ten years of convertibility (Figure 2). This last fact, the excessive level of dollar-wages, was the most commonly used argument for the promotion of labor market deregulation. According to this point of view, labor costs were too high in dollar terms and had to be reduced by direct state intervention (through deregulation) or would be reduced by the "invisible hand" of the market (i.e., the pressure of growing unemployment).

Since the evolution has been roughly the same in the long run for both estimations, from now on I will always refer to the real exchange rate adjusted by the producer price index (unless noted otherwise).

In any case, however persuasive the previous data might be, it is not possible to define the overvaluation of the currency unless we can show what the right level for the RER should have been. That is, we must compare the actual RER with the fundamental or equilibrium RER.

The neoclassical theory states that the equilibrium RER should reflect the evolution of some fundamental variables. These variables may include the relative money supply, the stock of debt, the level of public deficit, the level of productivity, and so on, depending on the theoretical model (Harvey 2001). However, neoclassical exchange rate theory is severely flawed, as its basic assumptions (such as the so-called purchasing power parity theorem or the full employment assumption) have been shown not to hold (Harvey 2001; Shaikh 1999).

6. This implied that the value of the peso was 26.1 percent higher between 1991 and 2001 than in the previous 10 years.



**Figure 1.**

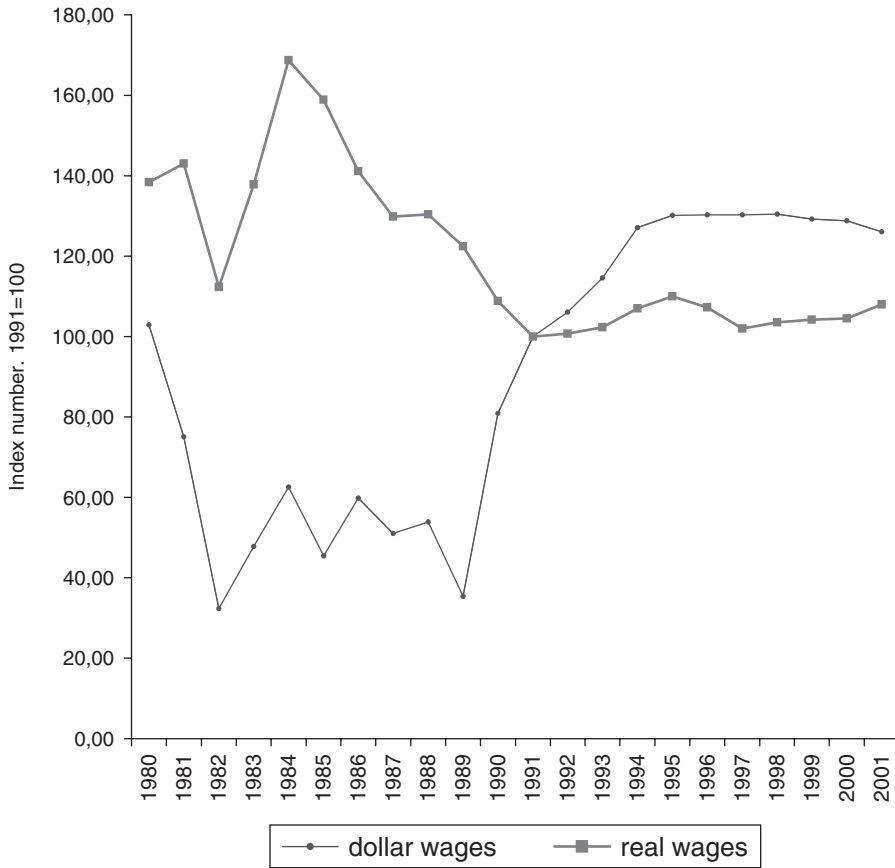
Real Exchange Rate, Argentina (Index numbers, 1991 = 100)

*Source:* Elaborated based on official data from the National Institute of Statistics and Census (INDEC) and Ministry of the Economy and Public Works of Argentina.

*Note:* The real exchange rate was calculated as the nominal exchange rate (pesos per dollar) times the United States relevant price index (ppi: producer prices, cpi: consumer prices) divided by Argentina's relevant price index (idem).

In contrast with neoclassical RER theory, recent developments from within the Marxist tradition provide a promising approach. In this line of work (developed mainly by Anwar Shaikh [2002, 1999]), the real exchange rate is expected to move (tendentally) to warrant that profit rates are equalized in regulating capitals across industries worldwide. That is, the common-currency relative price of two sets of tradable goods will tend to follow the best-practice vertically integrated unit labor costs of these same bundles of tradable goods, expressed in common-currency ( $v$  and  $v^*$ ; Shaikh 2002).

As noted above, the real exchange rate can be defined as  $\frac{e \cdot p^*}{p}$ , the common-currency relative price of the two sets of tradable goods. International competition will force the relative price of tradable goods, that is, the real exchange rate, to follow the ratio between



**Figure 2.**  
Real Hourly Wages and Dollar Hourly Wages, Argentina

Source: Ministry of Labor and Social Security of Argentina.

vertically integrated real unit labor costs. If we assume that there is some bundle of tradable consumer goods whose international prices ( $pc_t$  and  $pc_{t^*}$ ) are roughly equalized across countries and letting  $pc$  and  $pc^*$  be the general prices of consumer goods in both countries (comprising both tradable and nontradable goods), then we can define the real best-practice vertically integrated unit labor costs as  $vr = \frac{v}{pc}$ , and letting  $\tau = \frac{pc}{pc_t}$ , following Shaikh (2002), we can state that

$$rer \equiv \frac{e.p^*}{p} \approx \left( \frac{vr^*}{vr} \right) \cdot \left( \frac{\tau^*}{\tau} \right) \equiv rulc^*. \tag{2}$$

This implies, in conclusion, that the relative international price of tradable goods in the two countries—which is the tradable-goods real exchange rate between them—will be regulated by the real labor costs of the regulating capitals of those commodity bundles (RULC\*), adjusted for the tradable and nontradable content (openness) of the consumption bundle (Shaikh 2002).

According to this, if real hourly wages fall or hourly labor productivity increases, unit labor costs would fall, thus increasing (ceteris paribus) capital’s profitability. This increase

in profitability in regulating capital would tend to induce increase in the supply of commodities, which in turn would tend to reduce prices, so that the profit rates in regulating capitals across industries would tend to equalize. That is, the reduction in one country's real unit labor costs would tend to increase its RER (thus depreciating its currency) by reducing the relevant price level within that country, other things being equal (Shaikh 1999). In other terms, the reduction in the real unit labor costs implies an increase in the relationship between surplus and necessary labor, or a higher rate of exploitation.

It is important to highlight that within this framework, a current account deficit would be sustainable inasmuch as the valorization of capital is possible within an economy. Capital flows (be they as foreign direct investment [FDI], loans, etc.) will finance capitalist production within a country as long as it is possible to obtain the regulating profit rates in its production. Besides, changes in the RER would not tend to solve the current account imbalances as the neoclassical models assume. On the contrary, these imbalances will be persistent and will continue to be financed by short-run capital flows (and/or direct transfers).<sup>7</sup> The devaluation of the currency will not by itself correct the foreign payments' imbalance. It will only do so inasmuch as devaluation is able to change real unit labor costs by reducing real hourly wages and/or increasing labor productivity and/or changing the relative price of tradable versus nontradable commodities (Shaikh 2002).

Within this framework, increased labor productivity and/or reduced real wages will increase competitiveness, and by reducing nominal prices will increase the measured real exchange rate. However, there is something missing from Shaikh's framework. He assumes that every country has some industries with some sort of absolute cost advantage, and thus actually sets the international price of some commodities. However, peripheral countries such as Argentina might not have capitals able to set any of the international prices of the commodities they produce.<sup>8</sup> Thus, for these countries, one would have to expect that nominal price level be sticky downward. In that case, increased competitiveness (i.e., reduced real unit labor costs) by a country would tend to produce a general glut of commodities within the markets in which the country's producers participate, inducing a generalized inability to realize the increased profit rates. On the contrary, higher surplus labor would not be realized as surplus-value (and thus as higher profits) unless there is market space for the sale of commodities. If prices do not fall, and reduced relative real unit labor costs cannot be taken advantage of, relative excess production would result. In this situation, excess capital would tend to flow out of the country, turning into the most general expression of value (world money). The transformation of capital into world money would imply a tendency for the domestic currency to depreciate in nominal terms. Thus, in this case, the reduction in real unit labor costs (RULC\*) would also result in the real depreciation of the currency, although through a more indirect way. This last situation

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7. As Shaikh (2002) states, since the real exchange rate is pinned (through competition) by real unit costs, it is not free to adjust in such a way as to eliminate trade imbalances. Indeed, such imbalances will be persistent and will have to be covered by corresponding direct payments and/or capital flows. Of course, this must happen if the country sustaining a structural external deficit is to engage at all in international trade.

8. This process would imply, if the nominal exchange rate were fixed, sticky domestic prices when expressed in a common currency. This stickiness might include typical tradable commodities (such as food and energy commodities) but also some nontradables such as privatized public services. Of course, state regulations, lack of effective competition (oligopolies), and so on might also contribute to price stickiness.



does not seem problematic in cases of floating exchange rates. In contrast, in the case of a country with an extremely rigid exchange rate regime (such as Argentina's convertibility), the adjustment process could become problematic. We will keep this in mind in the analysis that follows.

#### 4. Argentina's Real Exchange Rate and the Crisis of Capital

Following Shaikh's theoretical proposition for defining the long-run, tendential, real exchange rate (RULC\*), I will estimate it for Argentina and use this estimation to analyze the development and crisis of capital accumulation in the country. I will work with data on industrial manufacturing productivity and wages since there is no adequate information for the economy as a whole.<sup>9</sup>

However, I will include one minor modification so as to take into account the effect of one important fact: the steep reduction of the indirect cost of labor (taxes on labor), in particular during the nineties in Argentina (Pérez 2001). In fact, what is important for capital is not just the direct real wage received by labor but the gross cost of hiring labor, which includes taxes on labor and other costs of using the labor force. While the restructuring and general deregulation of the labor market (higher unemployment and/or greater precariousness in labor contracts) should work its way into reduced real unit labor cost though increased labor productivity and/or the reductions in real wages, the reduction of taxes on the payroll should reduce these costs directly regardless of any other change. Since labor taxes are part of the price that capital has to pay for the use of the labor force, changes in the payroll taxes will imply changes in RULC\*, other things being equal.<sup>10</sup>

In the case of Argentina, as mentioned above, there was a strong state intervention with regard to the reduction of payroll taxes. As can be seen (Figure 3), payroll taxes paid by the employer fell from 38 percent of the nominal wage in 1990 to an average of 9.8 percent by 2001.<sup>11</sup>

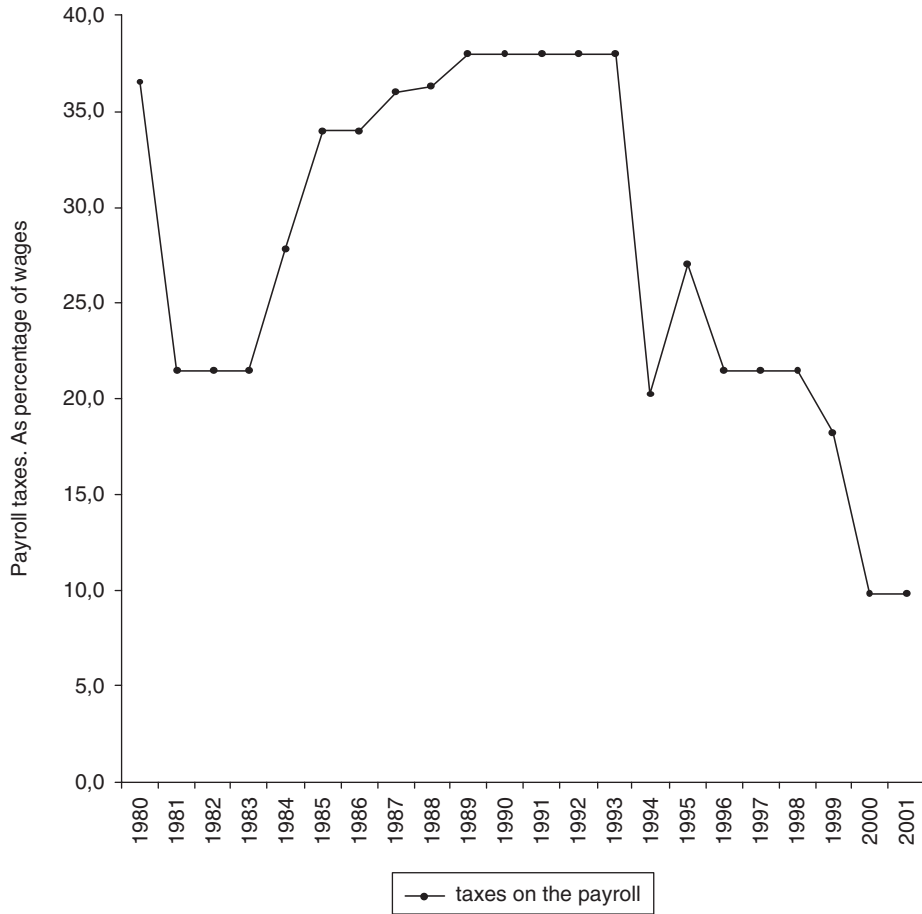
As a matter of fact, the reduction of labor taxes meant an important redistribution of resources. It is estimated that the state lost some 25,000 million pesos (25,000 million dollars, at the official exchange rate), or some 1.3 percent of GDP between 1993 and 1999, because of reduced income from taxes on the payroll (Pérez 2002). Accordingly, in Argentina, the real labor unit costs have fallen more than can be seen by the evolution of real wages and labor productivity alone.

While direct labor costs fell only slightly up until the mid-eighties because of labor's resistance to reductions in the real wage (but mainly because of the rejection of capital's imposition of higher productivity, and thus, higher exploitation) and very fast between 1985

9. This being a first attempt at this analysis, I will use for both Argentina and the United States data from each country's manufacturing producers. The data are provided by the National Institute of Statistics and Census (INDEC) and Ministry of the Economy and Public Works in the case of Argentina and the Bureau of Labor Statistics in the case of the United States.

10. In my estimations, I do not consider United States's labor taxes, since they have practically stayed unchanged during the period under analysis (Bureau of Labor Statistics 2003).

11. The reduction in payroll taxes was not homogeneous across industries, activities, and regions. By the year 2000, for example, industries located further away from Argentina's capital city received greater reductions on their payroll taxes (Pérez 2001).

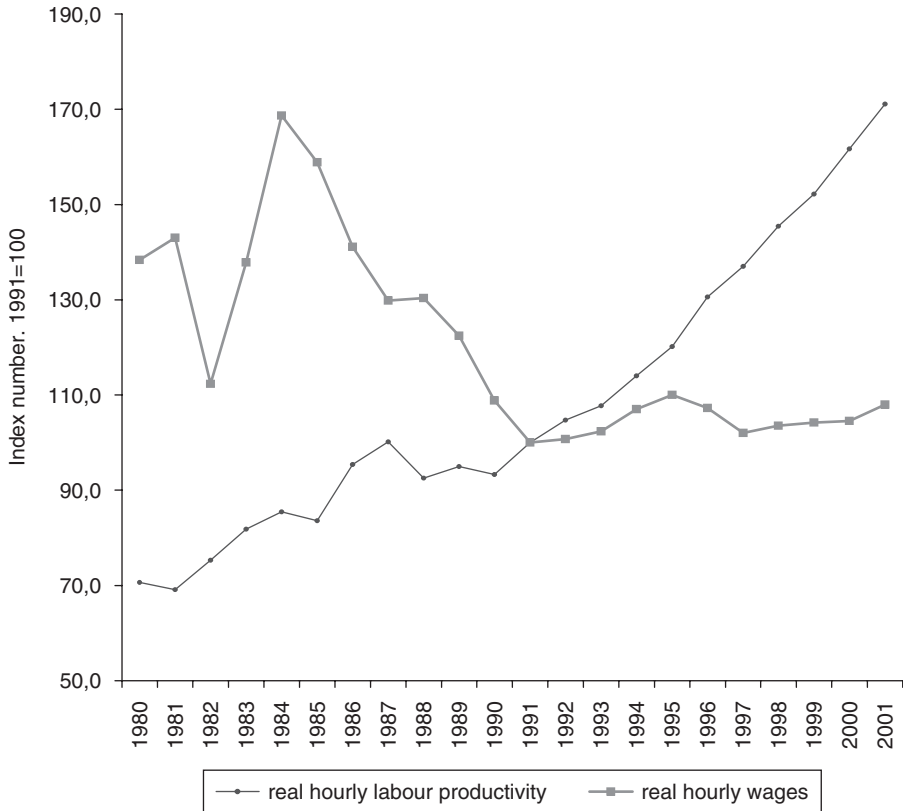
**Figure 3.**

Tax Rate on the Payroll, Argentina

Source: Ministry of Labor and Social Security of Argentina.

and 1991 (as labor's temporary defeat set in), in the nineties, structural reforms produced an important increase in labor productivity while holding down real wages (Figure 4). Labor productivity was increased in several ways. First, productivity was augmented through the introduction of newer technology in the form of imports of new machinery; while imports grew by almost 300 percent to more than 30,000 million dollars (Mayo 1998), the value of imported capital goods and spare parts for machinery rose from 25 percent of total imports in 1991 to 45 percent in 1998 (Halevi 2002). Second, the changes in the labor processes implied the increasing intensity of labor though the reduction in lunch breaks, the introduction of multitasking by workers, and so on (Martínez 1998; Battistini, Deledicque, and Félic 2002). Many of these changes were introduced in new collective bargaining agreements, but many were forced in directly by capitalists (Battistini, Deledicque, and Félic 2002).

As a consequence, while the real exchange rate may have been low during the first years of the convertibility, according to the rough estimate already mentioned (Figure 1), this surely changed rapidly. From the year 1991, the real unit labor costs in Argentina descended much faster than in the United States (Figure 5).

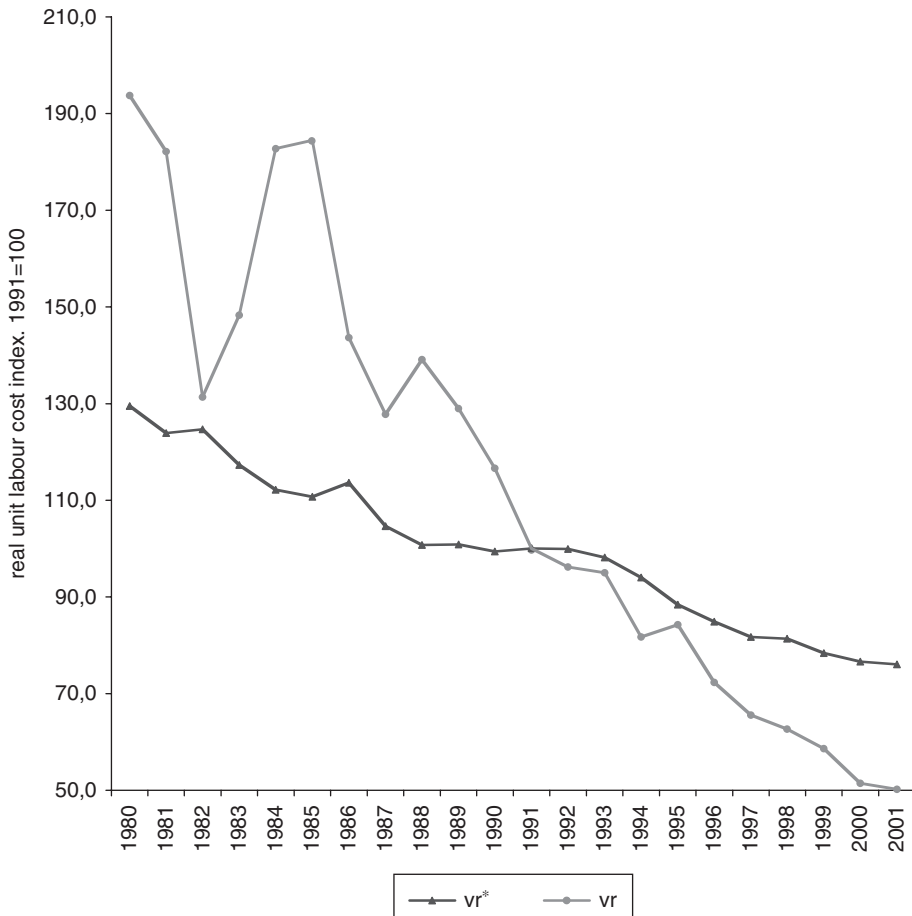


**Figure 4.**  
 Labor Productivity and Real Wages, Argentina (Index number, 1991 = 100)

*Source:* Elaborated based on official data from the National Institute of Statistics and Census (INDEC), the Ministry of the Economy and Public Works of Argentina, and FIEL (private foundation).

Between 1991 and 1997, Argentina’s real labor unit costs fell at an average 6.1 percent a year (7.7 percent including reductions in payroll taxes). Afterward, the increasing difficulties by capital to continue to augment labor productivity and growing conflicts over the organization of social production (both within the factories and outside them) were only partially neutralized by the reduction in payroll taxes.<sup>12</sup> As an average, after 1997, the real unit labor costs went down in Argentina at a 4 percent (6.4 percent with taxes) yearly rate (during the eighties, the average yearly reduction was 4 percent and 3.8 percent without including labor taxes and including them, respectively).

12. Social conflict never disappeared from the scene, even though its intensity was greatly reduced during 1991–1993. However, from December 1993 (with the popular uprising “Santiagazo” in a poor province of the country) to the generalized uprising of December 2001, there was increasing popular discontent. The reorganization of the labor movement, the stabilization of the rate of unemployment, and the reduced momentum in the drive for reforms (political opposition to neoliberal reforms was building up, both within and outside the country) all were events that help explain the growing difficulties for capital in controlling labor and increasing social productivity (Bonnet 2002).



**Figure 5.**

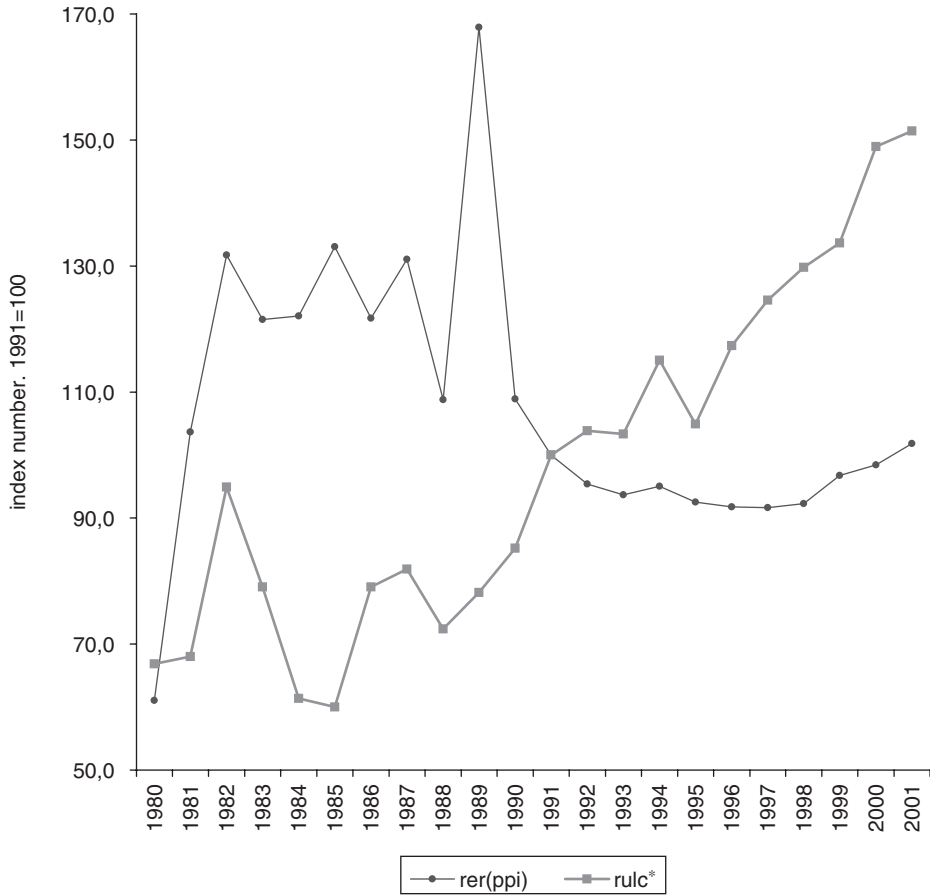
Real Unit Labor Cost Index, Argentina ( $vr$ ) and United States ( $vr^*$ ) (Index number, 1991 = 100)

*Source:* Elaborated based on official data from the National Institute of Statistics and Census (INDEC), the Ministry of the Economy and Public Works of Argentina, and the Bureau of Labor Statistics of the United States.

*Note:* In the case of Argentina, the labor cost is corrected for changes in payroll taxes;  $vr$  and  $vr^*$  are calculated as the real hourly wages divided by real hourly labor productivity for each country's manufacturing industry.

Since in the United States, the reduction on the real unit labor costs (in the manufacturing industry) was far smaller (at an average of just 2.4 percent a year since 1991), between 1991 and 2001, Argentina's long-run real exchange rate (RULC\*) increased by 51.4 percent (from now on, indications on RULC\* will refer to the estimation including labor taxes, unless stated otherwise; Figure 6).<sup>13</sup>

13. The relative real unit labor costs (RULC\*) for Argentina were calculated as real unit labor costs in United States manufacturing / real unit labor costs in Argentina manufacturing. Thus, a higher RULC\* means a more devalued long-run peso against the dollar. Since I did not count with adequate data, I decided to leave out the correction for the tradable/nontradable content of the consumption bundle ( $\tau$  and  $\tau^*$ ) suggested by equation (2). However, if we followed Shaikh's suggestion of using the ratio of producer prices to consumer prices as a proxy of  $\tau$  and  $\tau^*$  for each country, the main conclusions would not be altered (see Figure 7).

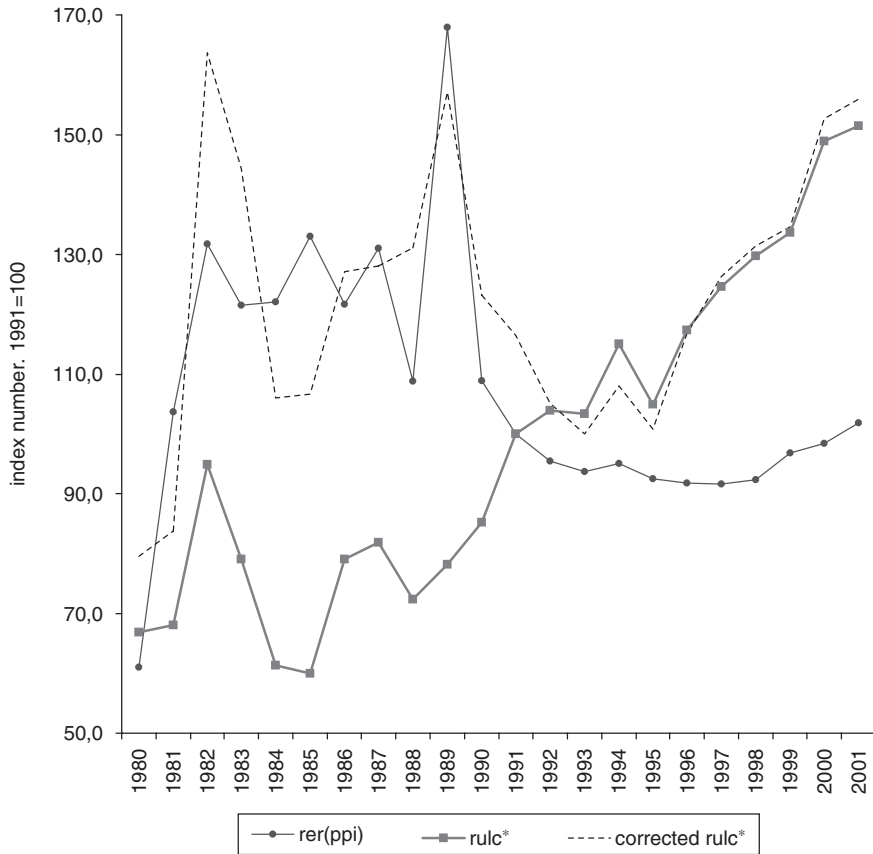


**Figure 6.**  
 Real Exchange Rate (peso-dollar) and Relative Real Unit Labor Cost (RULC\*),  
 Argentina (Index number, 1991 = 100)

Source: Elaborated based on official data from the National Institute of Statistics and Census (INDEC), the Ministry of the Economy and Public Works of Argentina, and the Bureau of Labor Statistics of the United States.

Note: The RULC\* is calculated as  $vr^* / vr$ . The real exchange rate, RER(ppi), is calculated as explained for Figure 1.

Therefore, contrary to what is usually believed, the long-run real exchange rate (as estimated from the evolution of RULC\*) increased some 63.4 percent on average between the eighties and the nineties. In the nineties, a (precarious) triumph of capital allowed it to engage in a full-blown attack on labor. After years of struggle, capital's reorganization and labor class decomposition gave way to a phase of deep social restructuring that allowed for the huge increase in the long-run real exchange rate. Following Shaikh's model, the steep increase in productivity and the direct reduction in labor costs in Argentina relative to the United States gave way to an important increase in capital's potential profitability. However, as I have proposed, the absence of regulating capitals in Argentina precluded the reduction of prices, and thus the increase in actual profitability (competitiveness).



**Figure 7.**

Real Exchange Rate (peso-dollar), Relative Real Unit Labor Cost (RULC\*), and RULC\* Corrected by Tradable/Nontradable Content of Consumption Basket, Argentina (Index number, 1991 = 100)

*Source:* Elaborated based on official data from the National Institute of Statistics and Census (INDEC), the Ministry of the Economy and Public Works of Argentina, and the Bureau of Labor Statistics of the United States.

*Note:* The RULC\* is calculated as  $vr^* / vr$ . The RULC\* corrected by the tradable/nontradable content of the consumption basket (corrected RULC\*) was calculated as RULC\* times  $\tau^* / \tau$ , where  $\tau^*$  and  $\tau$  are the ratios between the producer price index and the consumer price index for the United States and Argentina, respectively. The real exchange rate, RER(ppi), is calculated as explained for Figure 1.

While during the eighties, the RULC\* remained fairly stable, the actual RER was very high (the value of the peso was extremely low). This was mainly because of the difficulty found by capital to control labor and reorganize production. As a matter of fact, during the eighties, Argentina witnessed one great battle between capital and labor for the control of social production. The difficulties found by capital to control labor were apparent in its impossibility to stop labor's wage demands (directly within the factories or indirectly by means of state intervention). This difficulty reflected most openly in the process of capital flight that grew from 15,000 million dollars to more than 43,000 million dollars in the decade (Basualdo and Kulfas 2000). Since capital could not get a grip on labor, it preferred to fly to (apparently) more quiet grounds. Besides, at a social level, during the eighties, the debt crisis put an enormous strain on Argentina's capital accumulation (gross fixed investment fell at a 1.7 percent yearly rate between 1984 and 1990; see Félic and Pérez 2004). Capital flight

in a moment of relative dollar scarcity put great pressure on the foreign exchange markets.<sup>14</sup> This process helps explain the extremely high exchange rate that predominated through the eighties.

In the nineties, on the contrary, capital's offensive was fed by millions of dollars in money-capital. The possibility of higher rates of exploitation, and thus (potentially) higher profit rates, lured financial capital into Argentina. Money-capital continued to enter Argentina in the light of lower(ing) relative real unit labor costs, and thus growing expected profit rates.<sup>15</sup> However, the regulation of money through convertibility entered into conflict with the need to actually realize surplus value.

While the relative real unit labor costs were being reduced in Argentina in relation to the United States, the long-run real exchange rate (RULC\*) was increasing to allow for the equalization of profit rates. However, the actual RER (as measured by  $\frac{e \cdot p^*}{p}$ ) would not

increase fast enough. With the nominal exchange fixed by law, the pressure to adjust was put on nominal prices. With real unit labor costs falling, expected profit rates were increasing. Thus, productive capacity and actual production also increased (between 1991 and 1997, real manufacturing production increased by 22.5 percent). Higher production would not be sold unless there was increased domestic and/or foreign effective demand. However, growing unemployment of the labor force<sup>16</sup> and falling household incomes limited domestic consumption demand, while the fixed exchange rate and slow world-demand growth<sup>17</sup> put a lid on foreign demand. In conclusion, deflationary pressures began to build up: by the year 1997, the annual variation of producer prices had reduced to just 0.1 percent (while, for example, it was 1.9 percent in the United States). From 1998 onward, producer prices showed an outright reduction (-5.4 percent from 1998 to 2001).

Falling domestic prices would allow for domestic capitals to increase their market share in world markets, and thus, realize their higher surplus value in higher profits. But the deflation, which some mainstream economists expected to solve the problem, was extremely dangerous for the circuit of capital as a whole. While the nominal devaluation of the domestic currency would have allowed for the actual RER to keep up with the evolution of the RULC\*, domestic price deflation could achieve the same objective but at the risk of stalling the process of expanded reproduction of capital. A growing pressure to reduce prices was a negative sign for investment (since it would be a signal of falling profitability), and thus for capital accumulation. Reduced prices meant an immediately reduced cash flow, and thus greater difficulties to make room for debt payments.<sup>18</sup> Cash flow problems would then

14. The dollar's relative scarcity was caused by the United States Federal Reserve's policy of high interest rates, which were extremely high by historical standards.

15. Between 1992 and 1998, Argentina received almost 30,000 million dollars in foreign direct investment (Iñigo Carrera 1999). Besides, local capitals (nonfinancial) received around 14,000 millions dollars through the issuing of negotiable obligations (Basualdo 2000).

16. Argentina's general unemployment rate grew from an average of 8.4 percent between 1990 and 1994 to 15.3 percent, on average, from 1995 to 1999 (Pérez 2002).

17. This expressed for Argentina in terms of reduced export prices that, according to the Ministry of the Economy of Argentina, fell by 12.3 percent between 1991-1997 and between 1998-2002.

18. Debt accumulation by the private sector was also an important problem. While capital was sure that structural reforms would increase its ability to exploit labor, it happily financed the process. The stock of private debt grew from 8,600 million dollars in 1991 to 49,500 million dollars in 1997 (Basualdo 2000). However, the accumulation of debt turned into a big problem when it seemed clear that the expanded reproduction of capital would not be so easy, and the recomposition of the labor class was putting at risk the whole process of reforms.

translate into trouble for the financial system. Besides, increased exploitation at a country-wide scale meant a lower participation of labor on value added and a probable reduction on popular consumption that would act in feedback fashion to increase relative excess supply. In fact, the participation of wages in total value added dropped from 35.5 percent in 1991 to just more than 27 percent in 1997.<sup>19</sup> To this, I might add the increasing pressure of competition by capital in Brazil (which had devalued its currency by late 1998), and later, the crisis in the so-called Asian Tigers and Russia. In this situation, capital pressured for greater reductions in real unit labor costs and asked for even lower taxes. While from the individual capital's point of view, it would make sense to keep reducing unit costs, from the perspective of productive capital as a whole, it would only add to the already excessive productive capacity.

In a nutshell, the growing difficulties for the expanded reproduction of capital expressed the contradiction between capital's drive for accumulation together with its inner tendency to reduce the variable (value producing) part of capital; the mounting crisis was the actualization (the turning into an actual event) of the tendency for the profit rate to fall.

Besides, by 1998, the labor class had consolidated a new political composition that would allow it to confront capital with greater success. After more than a decade of defeats, labor had begun to confront in an organized manner capital's advances.<sup>20</sup>

In the factories, labor productivity began to stagnate after several years of pronounced increases. Labor productivity growth in manufacturing fell from an annual average of 5.7 percent between 1991 and 1997 to just 4 percent a year afterward. This was showing the growing loss of momentum of the process of reforms in the midst of increasing social and political turmoil.

Outside capitalists' enterprises, the labor class had begun to successfully resist neoliberal reforms. Unemployed workers, state employees, students, petty producers, small farmers, and peasants, among others, were confronting the state in its attempts to help capital counter the growing crisis. While capital found greater difficulties in converting surplus value into actual profits, it demanded from the state a deepening in structural reforms. The struggle for the reduction in taxes and in public spending (particularly of wages and salaries of public-sector employees) as well as for further reforms became the new battlefield. If profits could not be realized in the market, capital's intent was to obtain them through direct transfers of value by the state, especially through income tax cuts and further reductions in payroll taxes. However, a growing public-sector deficit (which reached 2.5 percent of GDP in 2000) and increasing difficulties in servicing public debt (which, by the year 2000, had reached 51 percent of GDP) were making it increasingly difficult for the state to give capital a hand.

19. This is my own estimation, based on data from Iñigo Carrera (2001) and Beccaria (1991).

20. The consolidation of new labor organizations that opposed the neoliberal reforms and concentrated their force in such strategic sectors as the state (mainly, the new Central de los Trabajadores Argentinos, CTA) and the transport sector (the Movimiento de los Trabajadores Argentinos, MTA) was an important qualitative transformation that consolidated at this time (Battistini, Deledicque, and Féliz 2002). Besides, I should stress the growing importance of movements of unemployed workers (among them the autonomous Movimiento de Trabajadores Desocupados Anibal Verón, with several thousand members), of small farmers' organizations (such as the MOCASE and APENOC, which grouped more than 10,000 peasant families), and of small business organizations (such as APYME), which turned into the most important social forces opposing reforms (Féliz 2004).



In the midst of growing difficulties to realize profits and with deflation knocking at the door, with increasing social and political conflict, capital turned into its most liquid form, money-capital, and tried to fly out before it was too late. This changed the direction in the flows of capital as it accelerated the process of adjustment that was threatening to blow capital away.<sup>21</sup> The story after this is well known: banking crisis, loss of reserves, financial troubles, and so on (see, for example, Mussa 2002). Eventually, capital's dominant agents accepted that there was no alternative but to opt out of the convertibility of the currency. Thus, devaluation of the peso followed. In January 2002, the peso was allowed to float; from December 2001 to December 2003, the nominal peso value of the United States dollar increased by 198 percent.

It is my understanding that capital took devaluation as the last available choice. Devaluation was a troublesome option since restructuring had been financed mainly by a growing external (foreign currency denominated) debt. Accordingly, devaluation meant a huge redistribution of surplus value. Concentrated capital took a risky bet when it accepted getting rid of the convertible currency. Growing popular discontent meant that the effects (social, political, and economic) of devaluation were uncertain; no one knew what the reaction of the workers would be to higher food and fuel prices, what the state's margin was to absorb and socialize private sector external debt, and so on. However, standing by the convertibility was, at that moment, a ticking bomb.

Devaluation has caused a further reduction in real wages (–15.95 percent from December 2001 to December 2003), increasing the RULC\*.<sup>22</sup> Most importantly, devaluation has generated a change in the measured RER, thus taking it closer to its tendential level (RULC\*). The measured real exchange rate has jumped by 122 percent between December 2001 and December 2003, more than offsetting the increase in the RULC\* between 1991 and 2001 (51.4 percent).<sup>23</sup>

I have stated that the crisis was to be expected, since the convertibility regime created the preconditions for its own demise. However, does this mean that without the convertibility, capital would have been able to avoid the crisis? I believe not, since the convertibility plan was precisely an integral, if contested, strategy of capital to counter the power of labor. This program of reforms was in fact successful from capital's point of view, since it allowed capital to gain greater control over labor (by restructuring most production processes). Besides, it gave capital the chance to appropriate new spaces for the valorization of value (privatization of social security, privatization of natural resources, greater participation in the provision of health and educational services, privatized state enterprises, etc.). As a result of this process, capital as a whole has not only increased the real subjection of labor, and thus of society, under its rule, but it has also been able to increase the

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21. Between December 2000 and December 2001, total deposits in the financial system fell by 25 percent (20,000 million dollars), while capital flight (registered in the balance of payments as “net nonfinancial private sector”) amounted to 12,247 million dollars (Brenta 2002).

22. However, I do not have enough data for years 2002 and 2003 to calculate the actual evolution of RULC\*.

23. The actual real exchange rate is now probably higher than its tendential value. Real devaluation has turned the current account deficit into an important surplus. However, this has been done on the basis of reduced imports and a partial default on the external debt, something that will not stand as capital accumulation regains momentum.

ratio of surplus to necessary labor. This is expressed in increasing productivity of labor, and correspondingly, as I showed, a rising tendential real exchange rate.

## 5. Conclusion

Argentina proved to be, during the nineties, the IMF's most brilliant student. However, neoliberal reforms did not bring a prolonged period of stability and prosperity but resulted in the deepest crisis in the country's history.

However, the crisis did not happen because of capital's failure to restructure and regain control over labor through Washington's consensus-type reforms. It was precisely its success that created the preconditions for its own demise.

Capital's restructuring increased productivity, created new spaces for the valorization of value (i.e., the expansion of surplus value), and disorganized traditional working class resistance. This process (re)created, nonetheless, the chronic limitations of dependent capitalism. While restructuring allowed for an important increase in labor productivity, and thus in potential surplus-value, the impossibility of translating such increases into lower prices, and thus greater profits, created the preconditions for Argentina's crisis.

The crisis was, then, not caused by labor's resistance (although it did play an important role in the events that led to the end of convertibility) or by Argentina's capital's lack of success in increasing its productivity (Bonnet 2002); on the contrary, it was precisely the result of capital's tremendous success. In fact, after devaluation, real wages fell significantly, showing labor's difficulties in confronting capital in the new correlation of power.

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