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MAKING MONEY FLOW: LATIN AMERICAN BANKS AT THE ONSET OF THE GREAT DEPRESSION

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&

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MAKING MONEY FLOW
LATIN AMERICAN CENTRAL BANKS AT THE ONSET OF THE GREAT DEPRESSION[1]

Abstract

In Latin America most of the central banks that remain in operation today were founded during the interwar period. Largely established in the 1920s, these new institutions marked the determination reached by their respective governments to modernize the economy. Most central banks were developed on the advice of foreign monetary advisors with the aim of providing stability to new monetary regimes that were based on the gold standard. This paper analyzes how these newly created institutions responded to the onset of the Great Depression in 1929. It describes some of the initial responses, which strongly corresponded to the needs of the financial system, and compares them to the government policies that were implemented once the gold standard was abandoned. We show that central banks initially acted to prevent capital outflows and to protect their gold reserves. This led to a credit drop that had an impact on commercial banks, agriculturalists and industry. They would only receive support once governments decided to intervene actively in the economy. The central banks established after the crisis, during the course of the 1930s, would be designed to meet the new economic reality. Their targets would prioritize the capacity to implement counter-cyclical economic policies, including liquidity provision to the banking sector, together with the supply of domestic credit.

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Introduction

In 1934, five years after the onset of the Great Depression, Raúl Prebisch submitted a proposal for setting up a central bank in Argentina. [2] One of its main aims was to furnish the proposed central bank with a blueprint for a more proactive monetary policy. The proposal covered banking supervision, rediscount operations, and it provided a strategic plan for addressing the ongoing liquidity problems faced by Argentina's commercial banks. In it, Prebisch laid out some of his preliminary thinking on the role of counter-cyclical economic policies in peripheral economies, such as Argentina. Thus, the establishment of Argentina's new Central Bank in 1935 marked a new era in the development of monetary policy in Latin America.

Argentina was one of the few Latin American countries that had not established a central bank in the 1920s. Nevertheless, the country shared many of the economic problems faced by other countries in the region. Prebisch's proposal broke with the received orthodoxy which had guided the formation of other central banks in Latin America hitherto. In other parts of Latin America central banks had been set up in tandem with a range of fiscal and monetary reforms. In Bolivia, Chile, Colombia, Ecuador and Peru such reforms took place on the advice of Edwin Walter Kemmerer, Professor of Economics and International Finance at the University of Princeton, in his capacity as a foreign advisor.[3] It was hoped that his reforms would contribute to the formation of a stable of monetary system, based on the gold standard, which would boost economic recovery by expanding domestic credit, encouraging foreign investment, and granting access to international capital markets.

[2] Prebisch worked in the Banco de la Nación Argentina (BNA, in English Bank of the Argentine Nation) (1927-1935), had been Undersecretary of Finance (1930-1932) and counsellor to the Ministry of Finance and the Ministry of Agriculture (1933).

[3] Kemmerer had previously served as foreign advisor in Mexico (1917) and Guatemala (1919), though his recommendations were not immediately implemented due to political complications. In Mexico his role was secondary as compared to the one played in the Andean countries in the 1920s where he acted as chair of mission (Nodari 2019).

The first years of implementing Kemmerer's reforms were successful. Local currencies were stabilized and government loans were issued in New York and London. These external funds served to nourish the reserves of the new central banks and provided finance for infrastructure projects. Nevertheless, domestic credit remained low, and the new monetary system soon began to show its weaknesses. While the squeeze on credit was a direct consequence of the deflationary policies introduced to meet the requirements of pegging the currency to the gold standard, the economic crisis initiated by the stock market crash in 1929 aggravated the credit shortage in key sectors such as agriculture and industry; moreover, although most of the central banks recognised the need to act as a lender of last resort, being tied to the gold standard constrained their capacity to offer financial support to commercial banks.

This paper analyses the transition from the first to the second generation of Latin American central banks (those established in the 1930s) and it presents a comparative analysis of the changes that occurred across the region during this period. Previously, the literature has been focused on the reforms introduced by Kemmerer, or on individual national cases.[4] However, a regional comparison of the history of central banking in the inter-war period can yield interesting insights. Overall, we observe that the role of central banks in the economy became one in which credit provision was a central concern, along with the capacity to introduce counter-cyclical monetary policies. While the Great Depression triggered this shift, the economic fragilities that would motivate it – along with new ideas on the role of monetary policy in the economy – had been present earlier in the 1920s in almost every country analysed. Even so, some countries were more reluctant than others to abandon their newly introduced economic policies. As we shall see, developing a timeline to show the sequence in which Latin American countries left the gold standard (together with other fixed-exchange rate systems) shows that the first countries to do so were those that had not introduced economic policies on the advice of foreign consultants. In these countries the decision to abandon the gold standard took place even *before* the fall in international reserves.

A key reason for drawing up a comparative chronological sequence is to highlight the timing of this policy shift. The extensive literature on the gold standard has shown that poor economic performance, together with a change of thinking, and the weakening of the 'good housekeeping seal of approval' were the main factors that prompted governments to leave this monetary regime (Wolf and Yousef 2007). In many instances it was the urgent need to facilitate credit - both to the

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[4] Two important exceptions are Díaz-Alejandro (1982) and Jácome (2015). Díaz-Aleandro (1982) provides a general overview of monetary policy as one of other, macroeconomic aspects of Latin American policy reactions to the Great-Depression. Jácome (2015) describes the long-term evolution of central banking in the region since the 19th century.

government and to the private sector - that were contributing factors. It was also significant that many governments began to express misgivings about their capacity to secure foreign financial support. As we show below, the countries where Kemmerer's policies were implemented appear to have been most committed to the monetary and fiscal orthodoxy of the 1920s, despite the severity of the economic crisis and the upsurge in political volatility. In the most extreme case, Kemmerer arrived in Peru at the beginning of 1931, when the effects of the Great Depression were making themselves felt; despite the decline in economic activity, his advice remained unchanged however; the country entered the gold standard that year, and would go on to become one of the last Latin American countries to leave it. By contrast, countries without economic policies formulated by foreign financial advisors reacted more rapidly. Here, fiscal needs and pressure from the private sector motivated the introduction of policies that were best adapted to the new economic environment.

Finally, we analyse the consolidation of proactive monetary policies as governments responded to problems that had been present even *before* the crisis. We contrast the central bank project by Raul Prebisch for Argentina, with the proposal submitted by Otto Niemeyer, the British foreign advisor. Whilst Niemeyer's proposal followed orthodox monetary policies, Prebisch's proposal addressed the weaknesses that were present in most Latin America economies. His project was one of the first documents that served as a *post factum* intellectual basis for the more proactive role assumed by central banks and by the State in order to support economic activity in the decades thereafter.

This paper is organized as follows: in the first section we provide a brief overview of banking and credit in Latin America in the 1920s, and the role that the new central banks were expected to assume; section two presents the main features of Latin American central banks and emphasizes the differences between 'Kemmerer countries' and the rest in terms of monetary policy; in the third section we describe the reaction made by central banks to the ramifications of the Great Depression; the fourth section describes shifts in monetary policy and international cooperation; and, in the fifth section, we compare the different proposals to found a new central bank in Argentina and the need to conduct proactive monetary policy.

I. The advent of Latin America's central banks

In the aftermath of the Great War, the state of banking development in Latin America varied according to the economic requirements of different countries as well as their institutional and political stability[5]. In Argentina, Uruguay, Chile and Costa Rica, foreign and domestic banks had assumed a prominent role in the credit market, attracting high levels of deposits and channelling capital for domestic ventures, and for financing international trade.[6] Some banks held close relationships with their national governments: they acted as state banks, and enjoyed a monopoly for issuing banknotes. In Brazil, Bolivia, Ecuador and Mexico, government intervention (i.e. inflationary financing) and political instability had impeded the development of the banking sector. In Mexico, the Mexican Revolution had forestalled the development of banks, contributing to the low economic growth in its aftermath (Haber 2010). In Brazil, the level of domestic credit fluctuated before plummeting in the first decades of the 20th century. In 1929, it plunged to 6% of total GDP, estimated to be one of the lowest figures on record in the modern world (Musacchio, 2009; Calomiris and Haber, 2014).

Along with political instability, macro-economic volatility affected the region's economic performance. By the end of the 19th century most Latin American countries had adopted the gold standard, only to abandon it at the onset of World War I. Then, during the 1920s, Latin American governments started to succumb to the pressure to return to the gold standard in order to achieve monetary stabilisation. This followed discussions at the International Financial Conferences of Brussels and Genoa of 1920 and 1922, where it had been agreed that a new monetary system, the gold exchange standard, would be adopted (Fior, 2008). Because the pound sterling and the U.S. dollar were convertible to gold at a stable rate of exchange they could serve as the reserve currencies that could substitute pure gold reserves. In this system, the exchange rates, and therefore the value of national currencies, had to be stabilised by central banks. Central banks were established around the world with the aim of reorganizing financial and foreign exchange systems encouraging adherence to the gold standard.[7]

Most countries in Latin America followed suit. As opposed to the slow evolution of central banks in Europe, Latin America's central banks were established rapidly, and were shaped by the specific political and economic circumstances in play during a narrow period of time (Marichal and Díaz Fuentes 2016). In fact, it was the countries with more advanced financial systems, such as Argentina and Uruguay that were the last to found these institutions. But elsewhere, the changes did not take place without heated public debate. In Chile, for example, there had been a heated

[5] For a recent analysis on banking history in Latin America, see (Díaz Fuentes, Hoyo Aparicio, and Marichal 2017)
[6] Zegarra (2010) estimates that, in 1922, there were more than 14 banks for every million habitants in Uruguay. Costa Rica, Chile and Argentina followed with 10.3, 10.2 and 9.1 each. On the other extreme, Peru had the lowest number of banks (1.7), followed by Bolivia (2.8), and Guatemala (3.2).
[7] Among the Resolutions unanimously approved by the Brussels International Financial Conference, one reads: "In countries where there is no Central Bank of Issue, one should be established" (Resolution Proposed by the Commission on Currency and Exchange nº XIV). See League of Nations (1923), Annex I, page 225.

discussion, even prior to Kemmerer's arrival. The dispute concerned the diagnosis of Chile's monetary problems, and whether establishing a central bank was desirable at all (Carrasco, 2009). Those who wanted to establish a central bank with strict rules determined by the gold standard, were opposed by those who feared the rigidity of this type of monetary system.[8]

In Chile, the Government under Arturo Alessandri's presidency had invited Kemmerer to visit in 1922, before being ousted by a military coup two years later. The new *de facto* government intended to carry through the ongoing financial reforms without continuing parliamentary debate. It is interesting to note that this decision met with little public disapproval. Monetary instability and inflation had already sparked public protest, and Kemmerer's mission was apparently welcomed by many, including the working class (Carrasco, 2009; Gomez Betancourt 2008; Drake, 1989; Kemmerer 1927).[9] Indeed, labour unions considered that a central bank could halt inflation and improve earnings. According to Drake, 'Kemmerer did not clash with nationalists and leftists. Instead, he appeared as the champion of labor against nefarious aristocratic elites, who were allegedly debasing the currency and hoisting the cost of living to siphon income to themselves.' (Drake, 1989:76)

Similar attitudes prevailed elsewhere. In Bolivia, Kemmerer was introduced by the media as 'the magician of world finances' and several articles outlined the benefits that would stem from the proposed financial reforms (S*uperintendencia de Bancos y Entidades Financieras*, 2003). In Colombia, in spite of criticism from the nationalist parties, the most important parties in Parliament welcomed Kemmerer's project. Here, the general positive reaction derived from the widespread belief that new financial institutions and legislation might serve to bolster the purchasing power of the local currency.[10] Even in Ecuador, where the monetary supply had been in decline since 1920, pushing up inflation and eroding real wages, several favourable articles were published in the press during the course of 1927 (Almeida 1994; Marchan and Romeo 2005).

By contrast, there were those who rejected Kemmerer's proposals. Many exporters were opposed to the introduction of a gold standard, given that currency depreciation could be so advantageous for them. For example, Bolivian mine owners, who provided some of Bolivia's main exports, had benefited from the depreciation in the value of the boliviano prior to the 1920s because

[8]According to Carrasco, the President Arturo Alessandri was actively trying to create a Central Bank, and had invited a first time Kemmerer in 1922: "I was personally convinced that this Bank would normalize the financial development of the Republic and stabilize our currency, which would bring a higher trust in our trade and industries, boosting the activities of the country." (Carrasco, 2009, p.76)

[9] It is interesting to note that Kemmerer had led this mission without involving the US government, which could have damaged the "neutral" image of his financial advice.

[10] A summary of the press articles referring to the first mission of Kemmerer in Colombia can be found in (Edwin Walter Kemmerer 1994).

it had increased their competitiveness abroad whilst lowering the cost of wages and tax (Drake, 1989: 182).[11]

Commercial banks that had benefited from a close relation with the government, and had enjoyed the capacity to issue banknotes, were also opposed to the formation of central banks. In Argentina and Brazil, some commercial banks, who had benefited from a monopoly of issuing currency hitherto, managed to persuade their governments to impede the establishment of new central banks in the 1920s. (Marichal and Díaz Fuentes 2016). In Argentina, the *Banco de la Nación* allied itself with the political party that was opposed the creation of a central bank in 1917 (Rapoport 2006). In Brazil, *Banco do Brasil* was a state bank with privileges that boosted its profitability, such as its capacity of multi-branching; and, given that the Brazilian Federal State was its main owner, this was of benefit to the Government (Villela 2017).

In countries where commercial banknotes had been issued by several private banks, such as Bolivia and Colombia, the prospect of centralizing this highly profitable activity was met with general opposition. In Ecuador, the proposed reforms caused severe disagreements between regional groups of bankers who held different views and interests on the country's monetary policy. Nevertheless, after several years of high inflation, the first steps towards the centralisation of reserves and restricting the capacity to issue currency were undertaken prior the arrival of Kemmerer, through the foundation of an institution called '*Caja Central de Emision y Amortizacion*' (Naranjo Navas 2017).

In Mexico, the 1920s was a decade marked by the ongoing mistrust of paper money, given its overuse during the Mexican Revolution. Here, the notion of a central bank was unpopular, and the commercial banks were systematically opposed to the idea. The biggest commercial bank, *Banco Nacional de Mexico*, had traditionally acted as the government bank, and had sought to become the new central bank, was adversely affected by the Government's decision to establish a new institution in 1925 (Gomez-Galvarriato, n.d.). The new Central Bank was seen to enjoy too much political proximity to the Government. As we will show below, Mexican banking legislation did not require mandatory association to the Central Bank, and as a result, only two banks chose to become associate banks; this increased marginally in the first years of the Central Bank's existence, reaching five banks in 1929. So, in order to compensate for the lack of deposits from commercial banks, the Central Bank of Mexico was allowed to enter into transactions with the public, an activity that was perceived to be contrary to the interests of the commercial banks.

[11] Coffee exporters had also been against the establishment of a central bank, though their rejection was more related to the implicit currency appreciation from adhering to the gold standard. See (Fritsch 1988).

It was the agriculturalists and industrialists who initially supported Kemmerer reforms, even though they would begin to turn against them as their implementation progressed. But, in the early years, they had hoped to benefit from an increase in credit and a decline in interest rates. As Drake reports, in all the Andean countries visited by Kemmerer, the major problem was the scarcity and high cost of credit, which tended to favour merchants and governments (Drake 1989). The agriculturalists and industrialists believed that central banks might play a similar role to today's development banks, by granting long-term loans, something to which Kemmerer was systematically opposed. For him, mortgage and commercial banks should be responsible for the provision of long-term loans.[12] In what follows, we describe the features of the new central banks and the criticisms they provoked during the first years of their existence.

II. Central banking and monetary policy: a general overview

The constitution of the new central banks

Table 1. shows the structure and management of central banks established in Latin America during the 1920s. In most of these countries, Kemmerer was the main designer of these new institutions (hence, the term 'Kemmerer countries'), which were created along with new fiscal, banking and monetary legislation in each country. Table 1. includes the ambiguous cases of Mexico and Guatemala, as well as the first central bank of Peru. In Mexico, Kemmerer's mission ended with a plan to found a central bank in 1917, though the *Banco de México* was only established in 1925. Whereas the *Banco de México* remained close to Kemmerer's original proposal, certain differences could be observed. Kemmerer's proposal had envisaged a mixed private-public ownership, whereas the final version was exclusively publicly owned.[13] The Central Bank's role in managing the exchange rate differed too. The *Banco de México* operated very briefly in a gold-exchange regime in tandem with the Ministry of Finance, with whom it shared the responsibility for monetary policy, a feature unforeseen in the original proposal. Even then, the creation and evolution of the *Banco de México* during its first years of existence were depicted by contemporaries as following 'Kemmerer lines'.[14]

[12] See the discussion of the banking law in Ecuador, in « Economic Conferences » Sessions 8, February 26 1926 and March 7 1926 ». EKP, Box 154, Folder 1.
[13] See Nodari (2019) for a detailed comparison.
[14] Bank of England Archives, OV166/7.

In Guatemala, Kemmerer had been an advisor as early as 1919, even though the final legislation was implemented seven years later under Enrique Martínez Sobral (frequently called the Guatemalan 'Kemmerer'), who had participated in Kemmerer's missions to Chile and Mexico (Molina Calderón, 2007). This was similar to Peru. The Central Reserve Bank of Peru was founded in 1922 due to the influence of William Wilson Cumberland, a former student of Kemmerer, who acted as a senior customs collector in the country. During his time in Peru, he maintained regular correspondence with Kemmerer and became a member of the Board of Directors of the new Central Reserve Bank, remaining in office until 1924 (Rosenberg 1999:157).

Table 1. Central Banks established during the 1920s: Kemmerer and "Kemmererized" Central Banks

	Peru 9 March 1922	Colombia 11 July 1923	Chile 21 August 1925	Mexico 1 September 1925	Guatemala 11 December 1926	Ecuador 4 March 1927	Bolivia 20 July 1928	Peru 18 April 1931
Authorized capital (local currency)	2 million	10 million	150 million	100 million	10 million	10 million	30 million	30 million
Duration	25	20	50	30	30	50	50	30
Shareholding								
Total number of shares	200'000	100'000	150'000	1 million	1 million	100'000	300'000	300'000
State	0	5 million	20 million	At least 51%	No imposition	No imposition	No imposition	No imposition
Domestic Banks	10% of capital; 0.5 million Peruvian pounds	15% of capital and reserves	10% of capital and reserves	6% of capital and reserves	Not specified	15% of capital and reserves	"Associate banks" 15% of capital and reserves	10% of capital and reserves
Foreign Banks	10% of capital; 0.5 million Peruvian pounds	15% of capital and reserves	10% of capital and reserves	6% of capital and reserves	Not specified	15% of capital and reserves	15% of capital and reserves	10% of capital and reserves
Other	0.5 million Peruvian pounds offered to the public. No vote	Any individual or enterprise. They give a right to vote only if they reach 500.000 gold pesos.	Shares offered to individuals and firms if total amount of capital below 150 million	Shares "B" can be subscribed by the government or the public in general	The shares are offered to the public in general	Shares "B" offered to the public in general	Shares "C" offered to the public in general	Shares "B" offered to the public in general

Table 1. Continued

	Peru (1922)	Colombia	Chile	Mexico	Guatemala	Ecuador	Bolivia	Peru (1931)
Board of directors								
Presidency	President, Vice-president elected by board[2]	Manager and assistant manager elected by board	President, Vice-president and manager elected by board	Director elected by board	Manager and assistant manager elected by shareholders' General Assembly	President, Vice-president and manager elected by board	President, Vice-president and manager elected by board	President, Vice-president and manager elected by board
Total number of members[1]	10	9	10	9	9	9	9	10-11
Appointed by:								
State	3	3	3	5	2	2	2	3
Domestic banks	4[3]	2	2		1	2	2 by all associate banks	2
Foreign banks	2	1	1		0			1
Agriculture	0	3; appointed by domestic (1) and foreign banks (2)	1 appointed jointly by the National Society of Agriculture and by the Society for the Promotion of Textile Industry	0	0	1 appointed by the Chamber of Commerce and Agriculture of Guayaquil; 1 appointed by the Chamber of Commerce, Agriculture and Industry of Quito; 1 appointed by the National Society of Agriculture	1	3 appointed jointly by agricultural, commercial and industrial corporations
Industry	0			0	0		1; appointed by Mining industrialists	
Commerce	0		1 (by the Chilean corporation of Sales in Saltpetre and Iodine) and the Chilean Central Chamber of Commerce)	0	0		1; "National Chambers of Commerce"	
Trade unions	0	0	1		0	1		
Other	1 (Fiscal agency)	0	1	4 (Appointed by "Serie B" shareholders)	6 (foreign and national shareholders)	1	2; "the public"	1
Reserve requirements	50%	60%	50%	50%	40%	50%	50%	50%
Limit on gov lending	None	30%	30%	10%	10%	20%	25%	20%

Sources: Chile (1947); Banco Central de Reserva del Perú (1926); Colombia (1923); Banco Central de Bolivia (1930); Molina Calderón, José (2018); Banco de México,S.A. (1925). Notes: (1): This table does not report the number of substitute members. (2): However, these positions could only be held by members appointed by the State. (3): Domestic banks are divided in different categories according to their level of capital (the benchmark volume of capital being 250'000 Peruvian pounds).

Central banks owned and administered international reserves, and enjoyed the monopoly for issuing paper currency. In Chile, the Central Bank had to redeem all previously issued treasury notes, and replaced them with new convertible notes.[15] Countries with free-banking systems had to do the same for the banknotes previously issued by the commercial banks. The new central banks were intended to be independent, and free from political interference, a feature that explains the long duration of the concessions. Ownership was mixed, both public and private: in each country, the government, associated banks and other private stockholders had to contribute to its capital, though levels could vary, as shown in Table 1. The shares were divided in different groups, each of which entailed different voting rights. Certain kinds of shares could only be acquired either by banks, or the government, or the general public. In this regard, Mexico's Central Bank was the least independent as the Government was expected to hold, at any point in time, at least 51% of the total amount of shares.

In the countries visited by Kemmerer, the amount of capital needed was estimated on the basis of the scale of the total population, its reserves, and its money supply.[16] In all cases, there was a minimum reserve requirement for the central bank (in general, 50% of total deposits and bills issued by the central bank, though Colombia imposed a 60% level). An additional restriction concerned the total amount of loans that could be granted to the government, which could not exceed 30% of the bank's capital, although this amount was adjusted at the onset of the Great Depression. One of Kemmerer's main criticisms of the banks in charge issuing currency had been that they had extended too much credit the government. This was the case of the *Banco de la Nacion Boliviana*, which was considered to be a dependency of the National Treasure.[17] Banks were allowed to pursue operations for the general public, as this was an activity that could generate profits for these new institutions.[18] Nevertheless, this capacity was only rarely used in practice. As discussed during the first years of

[15] In compensation, the Bank would receive the financial assets that backed those treasury notes and most of the gold from the *Fondo de Conversión* (currency board). The government would continue to issue coins but under the supervision of the Central Bank, by fear that "*with excessive emissions the government could endanger the gold standard*" (Carrasco, 2009).
[16] This was the case for Bolivia and Ecuador. Once the mission estimated the amount of capital needed, the next estimation concerned the amount of capital that banks and the national government could provide. The mission's report also contained recommendations on the need for a foreign loan if financial resources were not sufficient. For Bolivia see Edwin W. Kemmerer Papers (Henceforth "EKP") – Box 76 Folder 2. For Ecuador, see EKP – Box 154 Folder 4.
[17] "Nota personal para el doctor Casto Rojas ", signed by R. Martínez Vargas, 23 de Mayo de 1927. EKP – Box 76 Folder 2.
[18] A summary of the characteristics of each bank can be found in Tamagna (1963) and Carrasco (2009).

operation, commercial banks' representatives on the boards of directors systematically opposed to operations with the general public, as they could generate undesirable competition.[19]

Kemmerer's central banks had boards of directors made up of representatives from the industrial sector, the agrarian sector, the government, and commercial banks. This marked them apart from their counterparts in Mexico, Guatemala, and the first Central Bank in Peru. A major achievement of the central banks Kemmerer designed was to have labour representatives on the board of directors for the first time. In Chile, it was the first time that a labour representative could 'interpret the Bank's activities and policies to labour and who can likewise interpret to the Bank labour's attitude on questions of currency and banking policy' and he concluded: 'The chief interests of Chile's economic life are represented on the Board of Directors, but no one interest has a majority'.[20] By contrast, in Colombia, both domestic and foreign banks were given the capacity to appoint representatives from agriculture and industry; a feature which would be forcefully criticised before it was changed in 1930.[21]

Kemmerer's central banks could conduct short-term rediscount operations for limited amounts; and they were expected to host the government accounts, and assume the role of clearing houses (Carrasco, 2009). Theoretically, central banks could act as lenders of last resort, granting emergency loans, stabilizing the international exchange rate of the peso, and managing the gold and convertible currency reserves. This was underpinned by banking legislation that laid out the regulatory framework together with the conditions where the central bank might offer support. In Ecuador, banking legislation explicitly included a clause for the provision of support to banks in an emergency.

Table 2. shows the main features of the new Latin American central banks compared to other countries. The first column in Table 2. shows the date when monetary law referring to the adherence to the gold standard was introduced. In 'Kemmerer's countries', monetary laws were accompanied by new banking laws intended to regulate the banking sector and promote credit according to the commercial and industrial needs of the country.[22] Central banks had to meet two requirements: currency

[19] The press in Colombia reported on the first operations by the Central Bank with the general public in October 1930. The increase in credits to coffee growers was expected to have a direct and important impact on the economy ("El Banco de la República ha comenzado a otorgar prestamos a particulares", *El Tiempo*, 22 October 1930)
[20] Draft of an article written by Edwin Kemmerer published in the Annalist, 1 January 1926. EKP, - Box 85 Folder 3.
[21] This was explained in the Explanatory Memorandum for the modifications of the Banking Law in Colombia in 1930. EKP, Box 132 – Folder 5.
[22] For Ecuador, see (Almeida 1994)

stabilization through the adoption of a gold exchange standard; and banking development, though currency stabilisation was the primary target. The Kemmerer missions also founded institutions such as the banking superintendent's office, hosted by the ministry of finance, in charge of the supervision of commercial banks and of the central bank intended to serve the general public by guarding against bank failures.[23]

Table 2. Central Banks vs other cases: Latin America in the 1920s

Country	Adherence to Gold	Exchange rate management /Monopoly of issue	Regulation and monitoring of Banking Sector	Reserve requirements (% on notes and deposits)	Lending of Last Resort functions	Limit on gov't lending (% of bank's capital)
			A. Central Bank foundation with presence or influence of foreign advisors			
Peru	1922	Central Bank	NA	50	Yes	None
Colombia	23 July 1923	Central Bank	Banking Superintendency Office	60	Yes	30
Chile	21 August 1925	Central Bank	Banking Superintendency Office	50	Yes	20
Mexico	1925	Central Bank	National Banking Commission	50	Yes	10
Guatemala	30 June 1926	Central Bank	Ministry of Finance	40	Yes	40
Ecuador	4 March 1927	Central Bank	Banking Department at Ministry of Finance	50	Yes	20
Bolivia	11 July 1928	Central Bank	Banking Superintendency Office	50	Yes	25
			B. No Central Bank in the 1920s			
Argentina	1927	Exchange Stabilization Fund	Ministry of Finance	None	Banco de la Nación / Stablization Office	20
Brazil	1926	Stabilization Office	Ministry of Finance	None	Federal Government	25
Uruguay	Currency not convertible	Banco de la República	National Banking Inspectorate	40%	Banco de la República	None

Sources: Chile: (Carrasco 2009). Colombia is Ibañez Najar and Meisel Roca (1990). Mexico: Bett (1957), Almeida (1994). Guatemala: Molina Calderón (2007)Argentina: (Gómez 2017), Uruguay: .(Nahum, Moreira Goyetche, and Rodríguez Arrillaga 2014). Adherence to gold refers to the monetary law defining the convertibility of the currency.

[23] See for instance the case of Bolivia : "Project of a General Banking Law", June 26 1927. EKP – Box 79, Folder 2.

The banking and monetary system introduced in the Kemmerer countries meant that monetary policy would have to follow the regime's automatic mechanisms. New monetary laws stipulated the adoption of a gold-exchange standard with the establishment of gold parities. Kemmerer preferred the adoption of a gold-exchange standard: it had the same automatic mechanisms as the gold standard, but it discouraged the hoarding of metallic reserves. The gold exchange standard was thus seen to be particularly well suited to economies that 'did not have enough material resources to guarantee gold circulation and reserves or could not guarantee gold bullion convertibility' (Gomez Betancourt, 2008:231).

In Argentina, Brazil and Uruguay, countries without a proper central bank, the leading commercial banks were charged with the provision of rediscount operations to commercial banks, the management of public finances and servicing debt. In all cases, the common target was to maintain a fixed exchange standard, which largely imposed the same kind of restrictions on monetary policy. However, functions such as monetary issuing, banking regulation, and even monetary policy were shared with other entities such as the Ministry of Finance (Uruguay) or Exchange Stabilization Offices (Argentina and Brazil). In the case of Uruguay, the *Banco de la Republica* (BROU) held the monopoly of issuing currency, although the quantity of money in circulation and the supervision of commercial banks was pursued by the Government (Román 2010).

Credit provision

One of the main motivations for the introduction of banking reforms in the 1920s was the unsatisfied demand for long-term credit. However, given the generalized adoption of the gold standard, deflationary policies were followed during the first years of the new central banks. As a result, these new institutions were unable to solve the general need for capital sought by the private sector. [24]

The rise in credit was supposed to operate through increased availability of capital that could be lent at reduced interest rates. If the balance of payments was positive, credit could rise accordingly though correlation was far from complete. Furthermore, the presence of central bank branches aimed to foster internal credit. Turrent Díaz (1982:154) observes that this was the case in Mexico.

[24] Even in the case of Mexico, while being nominally on the gold standard, in practice silver coins constituted the bulk of the monetary base, while the price of gold pesos continued fluctuating until 1928, when the country returned de facto to the gold standard (Gomez-Galvarriato 2003: 391). The central bank was also obliged to reduce the monetary base to achieve currency stability.

However, the Banco de México was particular given its capacity to deal directly with the public as a commercial bank.

The disappointment that followed the establishment of central banks developed rapidly in most cases. Drake (1989:43) reports that in Colombia, agriculturalists felt excluded from the credit policy of the newly established Central Bank. This group had initially been in favour of a bank specialized in providing credit perceived as necessary to support the sector.[25] Overall, even before the impact of the Great Depression, criticisms had been raised in favour of a more proactive policy that could facilitate credit to the economy, something that central banks refused to do prior to the 1930s. In Chile, agriculturalists complained about credit shortages. In Ecuador, Almeida, (1994) reports that a fall in the prices primary exports triggered a deficit in the current account from 1927 onwards, prompting the Central Bank to reduce the monetary reserves. Nevertheless, the Bank maintained a level of reserve that largely exceeded the minimum required. Furthermore, even if discount rates decreased between 1927 and 1929, the Central Bank continued to reign in its credit policy. The Bank reacted to criticisms by referring to the fact that short-term credit had to be provided by commercial banks rather than by the Central Bank. However, continuing criticisms referred to the mismatch created by Kemmerer's banking laws and the real necessities of the economy (Almeida, 1994: 136).

In certain cases, governments mounted a response to the demand for credit increases through the establishment of public banks, or by promoting the establishment of specialized, commercial banks. In Guatemala, after the Central Bank was founded, a new bank was established whose main priority was to grant credit to the agricultural sector in 1929, called the *Crédito Hipotecario Nacional* (Molina Calderón, 2007). Furthermore, and contrary to 'Kemmerer banks', the Central Bank included an Agricultural Mortgage Department which was granted 25% of the paid-in capital of the bank.[26] In the Mexico, a similar bank called the *Banco Nacional de Crédito Agricola* was established in 1926, one year after the foundation of the Central Bank (Pani, 1951). In Chile, the same motivations prompted the government to create the *Caja de Crédito Hipotecario* and the *Caja de Crédito Agrario* (Drake, 1989: 113). As we shall see, complaints on the shortage of credit became even more acute once the effects of the crisis deepened throughout the region.

There were also increased demands for credit from the industrial sector. In Peru, the financial sector had concentrated on credit for consumption and imports since the late 19th century, and this remained a primary focus until the 1920s (Monsalve, 2011). Lobo Collantes (2013) argues that the

[25] Sánchez-Torres and Bedoya-Ospina (2017). By the time, the agriculture sector represented over 80% of Colombia's economy.
[26] Statutes of the Central Bank of Guatemala, published in (Molina Calderón, José 2018)

first initiatives to provide financial support Peru's industrial sector date from March 1929, following discussions in Parliament. According to this author, Kemmerer's banking laws affected long-term credit, as commercial banks prioritized short-term transactions. The lack of credit for the sector, along with agriculture, declined during the crisis years. As a result, the *Banco Agricola* was created in 1931, and the *Banco Industrial* one year later.

In countries that decided not to establish a central bank the picture was mixed. In Uruguay, there was a persistent criticism during the 1920s of the Government and the BROU for failing to provide sufficient credit to the rural and industrial sectors (Jacob 1981). The policy of restricting credit demonstrated that the Government's priority was to bring the country within the gold-exchange standard. In Argentina, Regalsky and Iglesias (2017) argue that the *Banco de la Nación* pursued a counter-cyclical credit policy, in contrast to commercial banks. This was related to the return to currency convertibility in 1927. Even if the level of deposits had been expanding in the late 1920s, the *Banco de la Nación*, along with other banks, initially decided to increase their levels of reserves, as the balance of payments was favourable. The increases of deposits and reserves ran parallel between 1928 and 1929 (Regalsky and Iglesias, 2017: 135). In Brazil, the expansion of credit was linked to the balance of payments – largely dependent upon the price of coffee - and the capacity of the Coffee Institute to stabilize it. As the balance of payments remained positive, the *Banco do Brasil* expanded its lending operations. Nevertheless, its sudden deterioration in 1928 triggered a shift in its lending policy. This sharp reversal severely affected the private sector, causing a liquidity crunch which required the *Banco* to intervene (Fritsch 1988).

III. The impact of the Great Depression

The extent of the decline in economic activity caused by the Great Depression was uneven in Latin America. Table 3. shows real GDP figures for a sample of countries between 1929 and 1934. The decline in economic activity seems to have been more acute in Chile and Peru, while Ecuador experienced a mild slowdown in the level of economic growth.[27] During that period, economic performance was strongly dependent upon the behaviour of the external sector. Table 2. shows that all countries shared a slump in the total value of exports, though here again, there were important differences among the countries analysed.

[27] Thorp argues that mining-exports were particularly hit by the crisis. Therefore, countries relying more on this sector were particularly affected (Bolivia, Chile, Mexico).

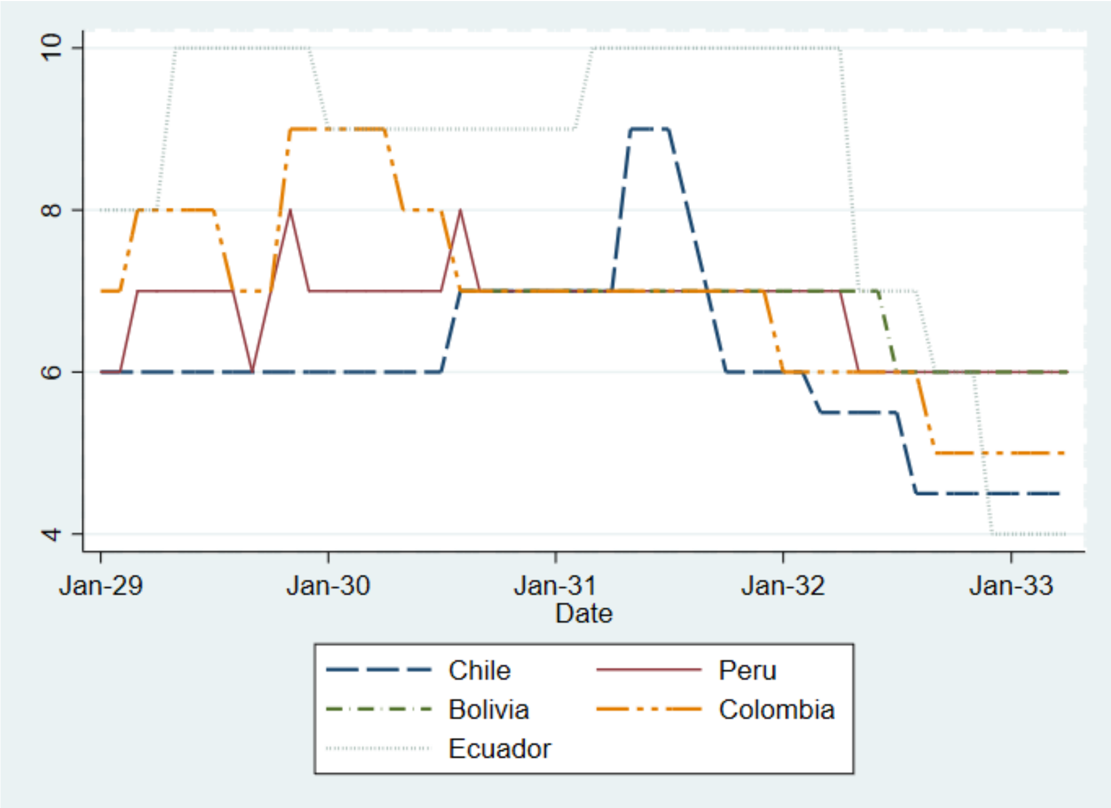
Table 3.

Years	ARG	BOL	BRA	CHI	COL	ECU	GUA	MEX	PER	URU
Real GDP (1929=100)										
1929	100.0	NA	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
1930	95.9	NA	94.0	84.0	99.1	103.8	104.3	93.7	88.5	113.7
1931	89.2	NA	91.9	66.2	97.6	104.5	97.4	96.9	81.4	94.0
1932	86.3	NA	95.1	55.9	104.0	105.1	85.1	82.3	78.3	87.3
1933	90.3	NA	102.6	68.9	109.9	107.4	86.0	91.7	87.1	76.3
1934	97.5	NA	111.1	83.2	116.8	109.8	97.4	97.9	98.8	90.9
Total exports (1929=100)										
1929	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
1930	98.7	70.3	158.3	58.1	89.0	94.1	96.0	129.0	65.7	94.6
1931	89.7	45.9	92.9	35.8	111.8	64.7	60.0	101.2	41.0	46.7
1932	62.7	37.8	67.1	12.2	77.2	47.1	44.0	57.6	28.4	29.3
1933	52.4	59.5	60.6	17.9	55.9	41.2	36.0	47.5	36.6	34.8
1934	52.4	97.3	62.6	34.4	61.4	82.4	60.0	58.4	52.2	34.8
Current account deficit as share of total exports (deficits shown as negative figures)										
1929	20.9	48.6	10.3	29.4	-7.9	0.0	-20.0	30.2	43.3	0.0
1930	-1.8	38.5	39.5	-4.9	39.8	18.8	29.2	52.9	42.0	10.3
1931	37.0	52.9	43.3	14.0	69.0	18.2	13.3	68.2	47.3	-14.0
1932	43.4	57.1	41.7	23.5	66.3	25.0	36.4	61.2	57.9	3.7
1933	30.7	50.0	15.6	46.0	36.6	28.6	11.1	42.1	59.2	3.1
1934	38.7	50.0	27.8	53.1	23.1	42.9	33.3	37.6	44.3	12.5
Losses in Gold reserve (1928=100)										
1929	85.71	225.10	100.20	83.09	58.51	92.37	75.00	161.61	90.01	88.93
1930	86.94	158.30	28.81	63.38	42.41	76.05	75.00	59.24	73.26	78.39
1931	53.27	62.35	13.83	36.25	21.21	41.05	56.25	40.28	62.64	67.06
1932	52.45	67.61	47.37	28.62	26.63	45.79	50.00	99.05	41.83	65.74
1933	50.41	41.30	63.36	31.04	26.01	48.16	58.33	86.73	47.03	69.43
1934	50.41	34.01	49.12	26.39	21.21	68.95	83.33	173.46	45.89	66.67

Sources: GDP and international trade figures are from Montevideo-Oxford Latin American Economic History Database. Data on reserves are from League of Nations. Economic Intelligence Service., various issues.

It is of interest that the decline in exports was not reflected in a deterioration in the current account balance of the countries included in the table. On the contrary, commercial deficits seem to have been the exception rather than the norm. This is related to the commercial policies to restrict imports, including contractionary monetary policies. As Table 3 shows, the fall in gold reserves was a prominent feature, suggesting that capital outflows were a major problem during these critical years. As central banks and monetary authorities followed the rules imposed by the monetary regime, the monetary base declined accordingly.

Figure 1. Discount rates in Latin America

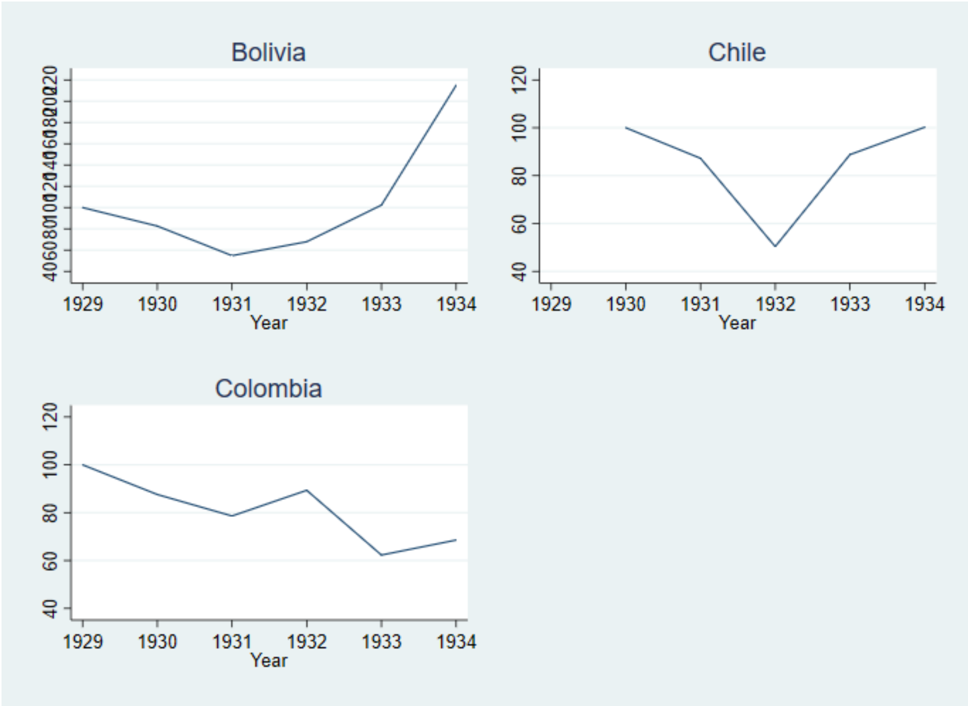


Source: Federal Reserve Bulletin, various issues. Chile's figures are those corresponding to "Rediscount Rates to Associated Banks" as published in the Central Bank's annual reports.

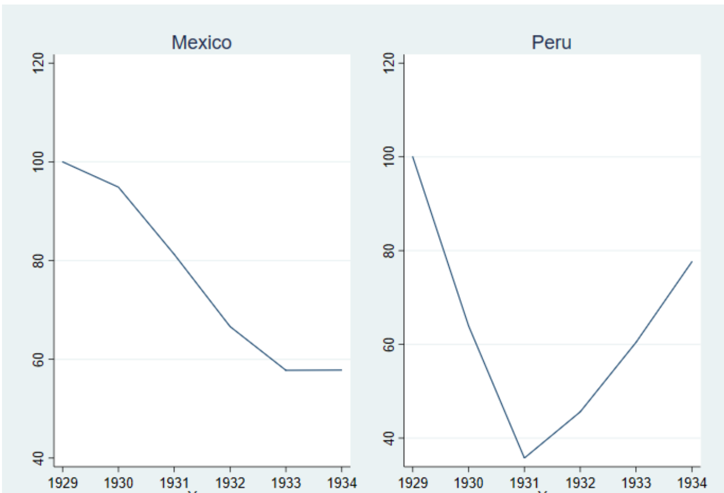
Defending the convertibility and value of Latin American currencies demanded that central banks reacted in terms of discount rates. These are shown in Figure 1. The initial reaction by central banks was to raise discount and rediscount rates, as dictated by the regime. However, this reaction was neither favourable to economic recovery nor to the needs of the central banks.

Figure 2. Fall in deposits: commercial banks

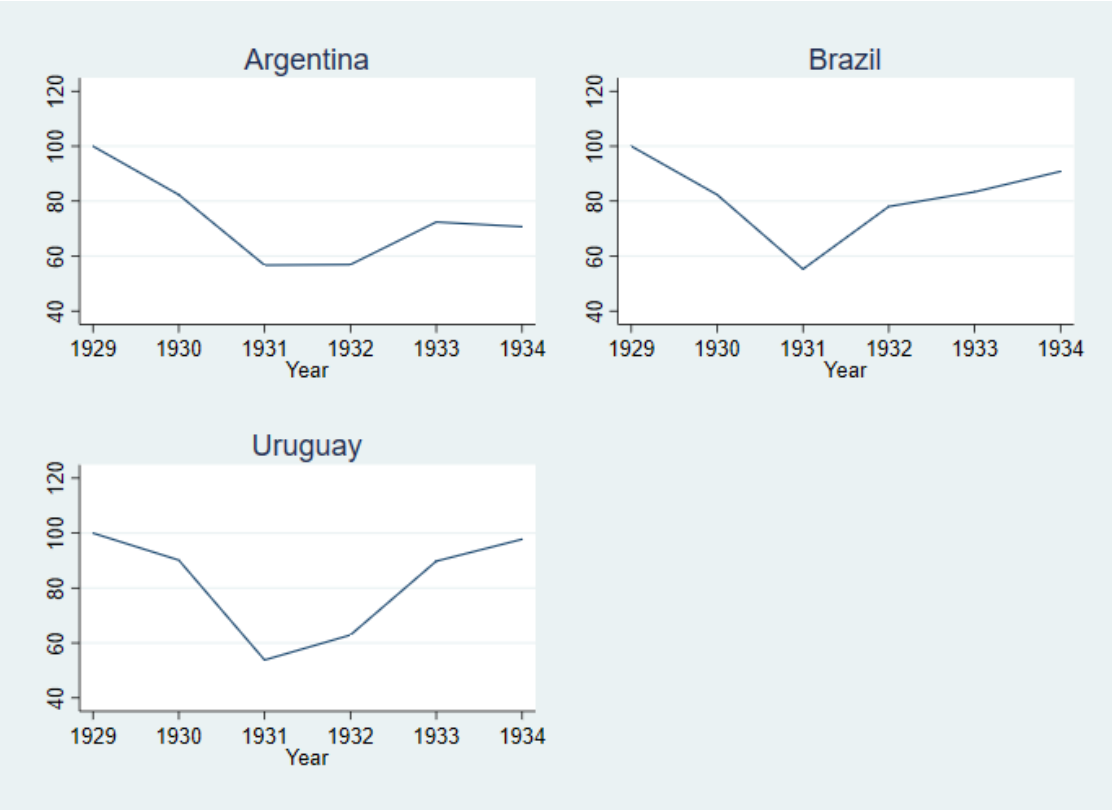
A. "Kemmerer" countries



B.Countries with central banks



C. Countries without central banks



Sources: League of Nations Yearbook (1929). Deposits are reported in local currency. They were converted to dollars using the exchange rates published in the same document. Indexes are estimated utilizing 1929 = 100 with exception of Chile (1930=100).

Previously the literature has drawn attention to the fact that no widespread banking failures were reported in Latin America during the 1930s. This conclusion stems from a comparative perspective that takes the US as the main benchmark.[28] Given differences in financial development, such a perspective is probably misleading. The banking sector in Latin America was persistently under financial distress, and banking failures and sporadic banking runs are reported in different countries after 1930. Figure 2. shows the generalized fall in deposits in all of the countries analyzed. For most of the new central banks, the crisis constituted a first, difficult test for which they were – at least in theory- well prepared. In most countries, banking failures had helped to motivate the establishment of central banks, as banking runs and banking failures had been a recurrent feature of the 1920s. In

[28] See for instance, (Alejandro 1983).

Argentina, the *Banco de la Nación* acted lender of last resort in 1923, when the *Banco Español* needed to be supported (Regalsky and Iglesias 2017). In Chile, banks had initially opposed the establishment of the new Central Bank, but the failure of the *Banco Español* in December 1925 gave a final blow to their resistance (Ossa 1991). In Colombia, the arrival of Kemmerer coincided with a major banking crisis in Bogotá, an event that accelerated the opening of the new Central Bank. In Guatemala, the Central Bank had already intervened with two banks in 1928 (*Banco Colombiano* and *Banco Americano de Guatemala*; see Molina Calderón, 2007). However, Aragón argues that the Central Bank only barely supported commercial banks, and even restricted its own credit to the general public as the Bank faced its own liquidity problems (Aragón 1996).

As the effects of the Great Depression hit, new pressures on the banks were reported. In Mexico, the constituency of the Central Bank provided several mechanisms through which the bank was allowed to support associated banks (Turrent Díaz 1982). This is a reason why rediscounting operations seem to have been limited until at least 1931 (Turrent Díaz, 1982: 221). A first banking run was experienced in Mexico City early in 1931, and a non-associated bank failed (Bett 1957). Even if the Central Bank was legally prevented from supporting non-associated banks, Bett argues that the bank helped several banks to weather the storm. Turrent Díaz (1982) further contends that the Central Bank utilized different means to support non-associated banks (other than rediscounting and current account credits), which were allowed, given its capacity to act as a commercial bank. The minutes of the boards of directors show that during 1931, the Bank conceded several loans and rediscount operations to associated and non-associated banks.[29] The only major bank which, after continuous support from the Central Bank, finally failed, was the *Banco de Sonora*.

In Peru, a first banking crisis hit after the military coup in August 1930. As public mistrust accelerated, the *Banco de Londres y del Peru* faced a massive run on its deposits in October. This bank was the most important bank of the country, though the whole banking system was particularly fragile as it operated without a proper regulation. The *Banco de Londres y del Peru* was in a delicate situation as it held a close relation with the deposed government and public suspicions concerning the misuse of funds triggered the panic (Quiroz 1989; Portocarrero 1981). The annual report of the Reserve Bank of Peru for that year does not provide further details about the support provided to the *Banco de Londres y del Peru*. The same report for 1929 shows that the bank absorbed around one fifth to one quarter of total loans and discount operations within the banking sector.

[29] These operations include loans to Banco Nacional de México in August 1931 and Banco Refaccionario de Occidente in September (both Associated Banks), and Banco de Nuevo León (Not Associated). See Actas de Consejo, 365, 368, 370, 378 – 1931.

IV. Policy shifts and external constraints

Even if the economic downturn had begun before 1929, in Brazil and Ecuador for ecxample, the initial reaction was to follow the rules of the gold standard, and to avoid the fiscal deficits that accompanied the economic slump. While the crisis was at first considered to be transitory, once exports continued falling and disequilibria in public finances became acute, other, alternative solutions were sought. One of these solutions involved a renewed round of visits from money doctors. Such initiatives occurred in Colombia and Peru, where governments invited Kemmerer since 1930 and whose visit occurred in 1930 (Colombia) and the first months of 1931 (Peru).

As the crisis developed, the need for external support mounted. The Meeting of South American Central Banks in Lima in December 1931 served to raise the tone in this direction. Initially convened by Bolivia's Central Bank, the participants of the conference included representatives from Colombia, Chile, Peru, and the US. Five main issues were discussed: the diminution of gold reserves, the consequent reduction of the circulating medium, the forced restriction of credits, debt defaults leading to capital outflows, and the effective remedies to mitigate the effects of the crisis.[30]

The Memorandum sent by Bolivia's Central Bank insisted upon the problem of restriction of credit. This was seen to aggravate the crisis, as a policy to decrease the monetary supply, was seen as 'withdrawing the means from various fiscal, commercial and industrial activities of the nation".[31] Among the solutions proposed in the Memorandum, one related to the assistance from the Federal Reserve Board to provide credit 'that it would grant us and on conditions adjustable to the existing circumstances'. Other solutions directly involved the monetary regime, such as those having the 'object of giving greater elasticity to paper money.'[32] The final communiqué from the conference showed the willingness of Kemmerer central banks to cooperate and remain on the gold standard. However, as the British observer reported to the Foreign Office, what the [South] American 'Bankers really wanted was further loans from New York or, as I was told in another quarter, to persuade the Federal Reserve Bank to extend credit over longer periods.'[33]

While the first countries to seek external support had been the 'Kemmerer countries', they were not alone. In Mexico the promoters of the gold standard within the government had been in

[30] A translated version of the "Memorandum on the subjects to be submitted to the Conference of the Central Banks" (November 18, 1931) can be found in Bank of England Archives, OV 188/1.
[31] Ibid,
[32] Ibid.
[33] Letter from C.H.Bentinck to Sir John Simon, 17 December 1931. BoE Archives, OV 188/1.

contact with the foreign monetary advisor though no formal invitation was sent.[34] In Uruguay, policy recommendations were provided by H.A. Lawrence, from the bank "Glynn, Mills and Co." to face the economic crisis,albeit exhorting the government to adhere to the gold standard (Jacob, 1981; Thorp 1984). In Brazil, British foreign monetary advisors had been present in the 1920s, though their visits had sought different targets. In 1924, Edwin Montagu, former Secretary of State for India, visited the country to provide policy recommendations to foster the Federal Government's fiscal capacity. This visit was planned after the bank Rothschild refused to underwrite any new government loan. In 1929, the visit of D'Abernon intended to foster the commercial links between Britain and Brazil. In 1931, after a severe fall in the Banco do Brazil's gold reserves, and aiming to receive additional external funding, the Government appealed to Otto Niemeyer, who was expected to provide policy recommendations mainly regarding monetary stability and the establishment of a central bank (Abreu 1974).

Scholars have argued that maintenance of economic orthodoxy was difficult to sustain given the economic needs of the countries assisted by foreign financial advisors. For Triffin (1944: 97), Kemmerer banks constituted only a minor advance beyond the exchange-office system. This author argued that the central banks created by Kemmerer were not sufficiently flexible to adapt to events such as the Great Depression, and their gold and currency reserves decreased. In his view:

'As lenders of last resort, the central banks created by Kemmerer proved helpful in the avoidance of the bankruptcies that used to accompany a financial panic. Their role, however, and certainly their effectiveness, did not extend much further. Monetary management, in particular, remained outside their sphere of action. The money was tied to a rigid gold or gold exchange standard, the only way in which the bank could influence it being the manipulation of the discount rate'. (Triffin, 1944, p.97)

Certain scholars have advanced that, for foreign advisors, the main priority was the defence of private interests from creditor countries, in particular to protect investments and promote trade (Seidel 1972:521). For instance, there had been an increase in foreign investments and loans (in particular from the United States), and this was a common phenomenon for the Latin American countries where Kemmerer had been present. Indeed, 'having the approval of British or American experts facilitated borrowing from these countries. In some cases, important conflicts of interest appeared; for instance, Edwin Kemmerer worked as an investor advisor for the bank Dillon & Read, a relationship that was kept a secret […]. In general, *money doctors* were complementary to capital flows' (Sember, 2018: 71). According to Gomez Betancourt, the Kemmerer missions in Latin America benefitted the interests

[34] This was the case of Montes de Oca, Minister of Finance (Merchant 2013). This author disputes the argument by which the Minister favored a strong contractionary economic policy stemming from a pure "blind obstinacy" on the benefits of the gold standard.

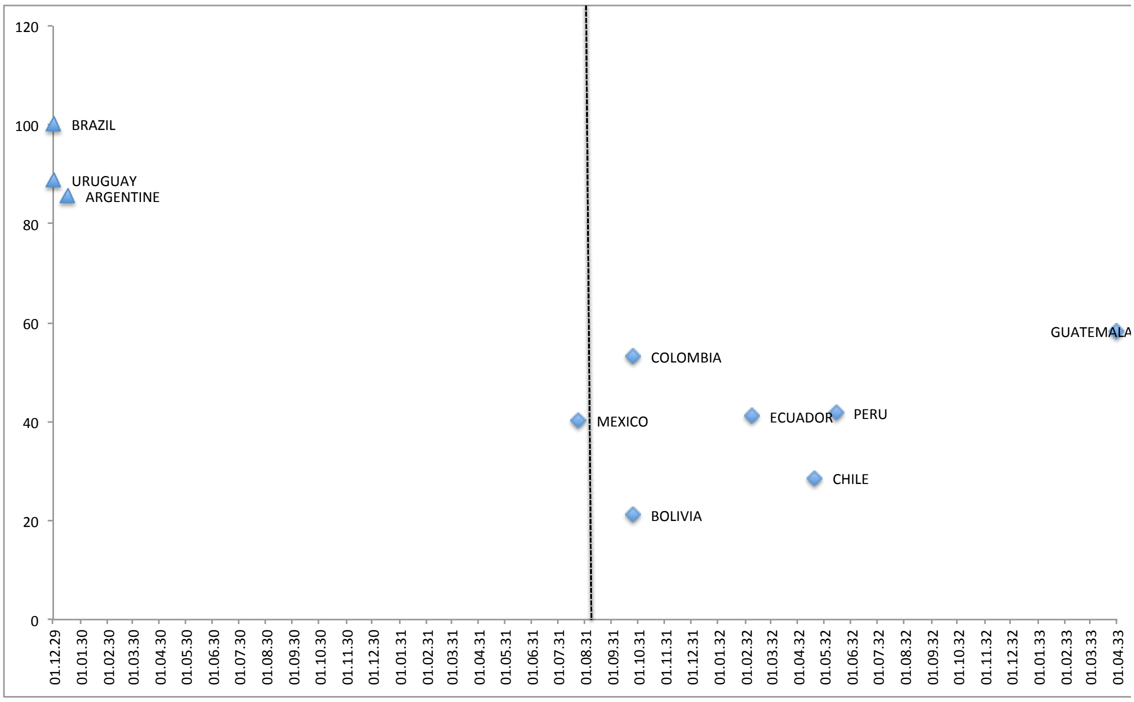
of US bankers, and lobbies would use the money doctors as intermediaries: ‘these missions had driven the Latin American countries to borrow on the one hand to finance their imports, and on the other hand to service their debts, which led them to perpetual indebtedness’. (Gomez Betancourt, 2008:100)

The orthodox reactions of Latin American governments did not mean that they were unaware of the problems that persisted in their economies. In Colombia, the demands from different sectors of the economy favored an expansionary monetary policy ((Ibañez Najar and Meisel Roca 1990). In the case of Mexico, Alberto Pani, who had already acted as Secretary of Finance since 1923 promoted a pension and a banking reform that intended to increase domestic savings and credit (Gomez-Galvarriato, 2003). In fact, as stressed by Thorp (1984), the need for state intervention, particularly regarding banking development, had been present for long time before the Great Depression, though the event permitted rather than created the new economic paradigm that would emerge since the 1930s.

Nevertheless, in several cases, the anticipated policy shift was delayed for several years. Figure 5 shows the dates at which a sample of Latin American countries left the gold standard and the ratio of gold reserves to the issues of banknotes as the decision was implemented. Figure 3 confirms that the low level of reserves was not necessarily the main variable explaining the decision to abandon the monetary regime. As Kemmerer himself argued: ‘A number of these countries which went off the gold standard had large amounts of gold.’[35] It is worth noting that the countries without a central bank were those that left first, even though the level of reserves was still relatively important. By contrast, countries that had submitted to ‘money doctoring’ were those that left last. Della Paolera (1998) distinguishes countries, such as Argentina, choosing to depreciate as part of a regime change as compared to those being forced to do so. The author estimates that, even two years after leaving the gold standard, Argentina had still a monetary base that was backed with gold.

[35] Statement of Edwin Walter Kemmerer at the "Banking Act of 1935. Hearings before a subcommittee of the committee on Banking and Currency, United States Senate, April 19 to May 13, 14 to May 22, 1935" (United States, 1935). Exchange controls began to be introduced in different countries in 1931.

Figure 3. Gold reserves to note issue ratio and abandonment of the gold standard.



Sources: Gold reserves and note issues: League of Nations Statistical Yearbooks: 1934, 1937. Dates for countries leaving gold standard, Federal Reserve Monthly Bulletin, various issues.

Argentina rejected the advice provided by Otto Niemeyer, the foreign financial consultant who visited the country in 1933, but it was not alone to do so. Brazil's government, led by Getulio Vargas, refused to follow Niemeyer's proposal to found a central bank. Here again, the provision of credit – for the government and for the local industry – prevented the country from establishing a central bank and joining the gold standard. These countries were among the first to facilitate discount facilities to their banking sectors in unorthodox ways. The reaction in Brazil to the Great Depression included the provision of rediscounting facilities through the Rediscount Portfolio in 1930. This policy was complimented by making available the reserves of the *Caixa de Mobilização Bancária* in 1932, while Argentina's government, facilitated discount operation by the *Caja de Conversión* and also established an *Instituto Movilizador de Inversiones Bancarias* (as did Brazil).

As mentioned above, the project presented by Otto Niemeyer to establish a central bank in Argentina differed sharply from the central bank that was finally adopted in the country. A main motivation was Raul Prebisch views, that were shared by many other contemporary observers. The new central bank should be able to support domestic credit, to provide liquidity to its banking sector and to support commercial activities. However, Kemmerer's banks and Niemeyer's propositions lacked the instruments to endorse that role.

V. A new model of central bank

Sember (2010, 2018) provides an interesting comparison between Niemeyer's central bank project for Argentina, and the project that was finally adopted in 1935, strongly influenced by Prebisch.[36] One difference concerned the autonomy of the bank. In Niemeyer's project, the bank was a joint stock company owned by national and foreign banks whose capital exceeded one million pesos. The national Government was not allowed to own any bank shares. In the final project, the Central Bank was a mixed entity, the Government owning initially 50% of its capital.

A second important contrast was the presence of different sectors on the bank board. In Niemeyer's project, the bank had to be managed by a president, a vice-president and seven directors nominated by the General Meeting of Shareholders,[37] five of them working in banks (two of which were foreign), one representing the livestock sector, and one the agriculture. In the final project, there were twelve directors, one nominated by the Government, 2 from public banks, 3 from national private banks and 2 from foreign banks; the production sector was represented by 4 directors: one from the livestock sector, one from agriculture, one from commerce and one from industry (Banco Central de la República Argentina, 1970). In other words, the productive sectors enjoyed an increased presence under the final project.

The purpose of the bank, in Niemeyer's view, was to 'regulate the volume of credit and demand for money in order to maintain the external value of the peso stated by the law' (Art. 3). Instead, the mission of the central bank in the Government's project was to 'concentrate enough reserves to mitigate the consequences of fluctuations in exports and foreign capital investment on the money, credit and commercial activities, aiming to maintain money's value', and to 'adapt the quantity of credit and means of payment, to make them fit to the real volume of business'[38]. In other words, in the final project the Argentine Central Bank had to lead a counter-cyclical action by restricting credit and accumulating reserves during the ascending phase of the cycle, so that these

[36] For this work, we selected the elements that seemed most important. For a more thorough analysis and for more information on the creation of the Argentine Central Bank and Prebisch's influence in it, see Sember (2010, 2012, 2018).
[37] The national government had to approve the nomination of the Bank's president and vice-president.
[38] Both projects are published in Banco Central de la República Argentina (1970).

gold and currency reserves could be used during the downward phase of the cycle.[39] This would allow the country to adapt to the external fluctuations and to soften the impact of the cycles on the economy. These considerations were absent from Niemeyer's project, even though this problem of external vulnerability was of great importance in the Argentine economy.

Another important element was that banking supervision concerned the prerogative of the central bank and not that of a distinct institution like in Kemmerer's central banks. Sember (2010) points out that Niemeyer's project did not give this function to the central bank either. As we mentioned previously, by assuming a supervisory role, the central bank was enabled to gather sufficient information for a rapid reaction in case of liquidity shortages or any early sign of a banking crisis.[40] This conception of an active central bank with counter-cyclical objectives meant that the return to the gold standard was no longer a primary objective. In the project for a central bank of 1934, Prebisch argued that the Argentine structure was not compatible with a strict tie with the gold standard and its automatic mechanisms. External fluctuations or bad harvests could trigger massive gold outflow or inflow, destabilising the whole economy (Prebisch, 1934).

At first sight, it might seem that both Niemeyer's proposal and the Government's aimed to re-establish a version of the gold standard at some point in the future. Indeed, both the Niemeyer and Government projects stated that the central bank would be obliged to change its notes for gold or foreign currencies; although both texts also included a transitory provision that delayed the application of that article until the end of exchange controls (Niemeyer's project) or the adoption of a 'special law' (Government's project) (*Banco Central de la República Argentina*, 1970). However, in Niemeyer's project, conversion would be made at the fixed gold parity established by the monetary law, whereas in the final project the conversion would follow the market's rates. Hence, in the final project, gold reserves had a central importance, but the principle of the gold standard was not respected. Based on archival evidence from the Bank of England, Sember argues that Niemeyer's project aimed at the adoption of the gold exchange standard based on the pound, although no specific currency was explicitly named in his project. This contrasts with Prebisch's project, in which foreign currencies included in the Bank's reserves could not exceed 10% of gold reserves, in order to reduce the cost of a possible devaluation of foreign currencies (Sember, 2018:87 -88).

[39] In general, Prebisch considered that investment should be made by savings, so "artificial credit" should be avoided, and the credit and quantity of money in circulation should be adapted to the needs of commerce and economic activity (Sember 2018, p.83).

[40] Furthermore, the Instituto Movilizador de Inversiones Bancarias was created along with the Bank and "*its role was to buy frozen assets of banks and trying to pay them off gradually* […]" (Sember, 2018, p.84).

Regarding the monetary tools at the disposal of the central bank, Prebisch and Niemeyer differed. As previously mentioned, the Central Bank had an active role, and some of the most important tools at its disposal were open-market operations, rediscount and exchange control. Open-market operations were a vital counter-cyclical tool that allowed to '*mitigate external fluctuations and regulate the liquidity of the market*' (Sember, 2018:85). Rediscount was not a new policy, as it had been used by the BNA in October 1931[41] in order to avoid bankruptcies and maintain economic activity in the midst of the Great Depression. Exchange controls had also proved to be an essential tool during the Great Depression because they enabled mitigation against the deterioration of the balance of payments of the country. However, Niemeyer was against open-market operations and exchange control (ibid).

Niemeyer's and Prebisch's concept of the role of the central bank was profoundly divergent. Niemeyer's project was essentially one of a passive central bank that was intended to prioritise monetary stability and maintain it through adherence to the gold standard. Prebisch's conception of the institution gave more importance to flexibility and discretionary action. After working in the Research Bureau of the BNA, in the Finance Ministry and in the Agriculture Ministry, he had a first-hand experience of the economic architecture of Argentina, and was increasingly aware of the problems caused by its external vulnerability and dependency. Since the Bank was an essential asset to maintain the internal stability and the economic activity, its role extended beyond the monetary sphere.

VI. Conclusion

The argument raised by Eichengreen and Temin (2000) regarding the 'change of mentality' towards the gold standard was a global phenomenon that led to reforms and the emergence of new actors and ideas. As these authors note, in the US a major policy reform was the 1935 Banking Act that sought to promote the 'stability of employment and business.' New actors were appointed to conduct the monetary policy of the country. In 1936, as discussions were taking place regarding the candidates to become the new members of the Board of Governors of the Federal Reserve, Kemmerer was rapidly dismissed. The prime reason for this was his allegiance 'to the old-fashioned gold-standard' by his record as 'money doctor' for nation. During the course of the Depression he has only warned against inflation, never against deflation".[42]

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[41] Rediscounts were allowed since 1913, but were never used before.

[42] Unsigned memo addressed to US president Franklin D. Roosevelt, 16 January 1936. Franklin D. Roosevelt, Papers as President: The President's Secretary's File (PSF), Box 134.

To a large extent, despite having brought a halt to extended periods of high inflation, Kemmerer's central banks were unable to adapt to the changing needs of Latin American economies. Kemmerer’s commitment to monetary stability and the gold exchange standard failed to adjust to extraordinary events such as the Great Depression. Niemeyer's project for Argentina was not radically different: it aimed for a return to the gold exchange standard, without assigning the function of banking supervision to the central bank, which was envisaged as having a mostly passive role. Niemeyer’s proposal intended to establish an orthodox central bank that for many reflected the vision and interests of Great Britain. The main difference between Kemmerer’s and the new Argentine Central Bank was that in the last case, the Government acknowledged that this kind of central bank was inappropriate for the interests of the country.

Although the global economic and financial crisis had forced developed and developing countries alike to abandon the gold standard, this had not been enough for changing the views of many monetary authorities and experts. Indeed, even though Niemeyer’s visit to Argentina occurred well after the Great Depression, the bank he proposed was not sufficiently equipped to face cycles and crises. The crisis by itself did not radically change his conception of central banking, and Kemmerer, as we have seen, would also continue to defend the gold standard both during and after the crisis (Gomez Betancourt, 2008). By contrast, Prebisch was concerned by the concrete problems faced by Argentina and took into consideration the peculiar situation of the country. Hence, from 1935 to 1938, the Bank focused on counter-cyclical policies, creating reserves during the boom years to use them during the periods of need.

It is interesting to note that similar economic policies were being implemented in other countries. In Mexico, Manuel Gómez Morín participated in the elaboration of a set of laws that intended to facilitate the relations between the central bank and commercial banks and to foster credit in the economy (Gomez-Galvarriato, n.d.). Gómez Morín would later serve as foreign advisor to Ecuador in 1938 (Marchán Romero 2005). Hermann Max, a Chilean economist at the central bank, and who was critical the gold standard, also advised countries such as Costa Rica in 1936 and Venezuela in 1939 (Monge 2008). A new paradigm was on the rise.

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