

Chapter 3

Financing Argentine Industrial Corporate Development in the Aftermath of the First Perón Period

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I. Introduction

At the time that Juan Perón was ousted as dictator of Argentina in September of 1955, that country faced a compelling need and desire to develop and expand its industrial capacity. Argentina has possessed some industry for many years; Ford Motor Company, for example, had been assembling automobiles in Buenos Aires since 1913. But the great need and desire for a more advanced level of industrialization grew out of the experiences of the depression and World War II.

Before the depression, the Argentine economy was heavily oriented toward the export of primary products and import of manufactured items. Only relatively light industry existed. During the depression Argentine exports were heavily discriminated against in Argentina's various traditional European markets, and during World War II industrial imports had not been available. The deterioration in the stock of industrial goods which occurred can be seen from the estimate that the 1938 value of machinery and vehicle imports in the country was about half of the 1929 value, and the 1945 value was one tenth.¹

Increased industrialization was sought by Perón, who became president of Argentina in 1946. His ultranationalistic policies and his redistribution of national income and economic power to urban factory workers, however, discouraged investors, both foreign and Argentine, from committing the necessary resources.

The dozen years after the 1955 overthrow of Perón were characterized by repeated political upheaval and a succession of presidential administrations, each with a degree of

dedication toward encouraging economic growth and each with different ideas of the importance of the private sector in this process. The years were also characterized by a continuous high rate of inflation and sporadic crises in balance of payments. In this inauspicious environment, however, industrial manufacturing did expand significantly, albeit at a somewhat uneven pace because of the continually unsettled political and economic conditions.

The purpose of this study is to investigate the financial policies followed by Argentine-owned and -operated industrial manufacturing firms as they financed their capital needs from 1955 to 1966. The study encompasses five post-Perón administrations — three military and two elected — up to the administration of General Juan Carlos Onganía, who took over the presidency in July of 1966. It is hoped that a perspective on Argentine financial problems of this period will be valuable in understanding difficulties faced by private manufacturing firms participating in economic development under similar, unsettled, conditions.

Manufacturing in Argentina

In 1955, industrial manufacturing contributed 30.4 percent of the gross internal product of Argentina; by 1965 this figure had risen to 34.0 percent, although it did drop the following year as a result of a generally depressed economic situation. Gross internal product of Argentina in the years from 1955 through 1966, expressed in terms of 1966 pesos, is shown in Table 3-1.² The gross internal product, expressed in 1966 pesos, grew from AS2,638 billion in 1955 to AS4,043 billion in 1966, an average per annum compound growth rate

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¹Eprine Eshag and Rosemary Thorp, "Economic and Social Consequences of Orthodox Economic Policies in Argentina in the Post-War Years," *Bulletin of the Oxford University Institute of Economics and Statistics* (February 1965), p. 5.

²Unless otherwise indicated, all peso time series in this paper have been converted to 1966 pesos by inflating historical sums by the official wholesale price index for national, nonagricultural products (*precios al por mayor, nacional no agropecuarios*). Because the wholesale price index was created only in 1956, 1955 prices are linked to 1956 prices by the consumer price index (*índice del costo del nivel de vida en la Capital Federal*).

Table 3-1
ARGENTINE GROSS INTERNAL PRODUCT, 1955-66
(Billions of Argentine pesos)

Year	Gross internal product		Industrial manufacturing component of gross internal product		Manufacturing as percent of total gross internal product
	Current pesos	Constant 1966 pesos	Current pesos	Constant 1966 pesos	
1955	158	2,638	48	801	30.4
1956	199	2,961	59	878	29.7
1957	250	3,008	75	903	30.0
1958	368	3,401	117	1,081	31.8
1959	696	2,833	212	863	30.5
1960	882	3,073	284	990	32.2
1961	1,043	3,326	347	1,107	33.3
1962	1,302	3,249	417	1,041	32.0
1963	1,597	3,136	497	976	31.1
1964	2,207	3,441	696	1,085	31.5
1965	3,014	3,601	1,025	1,225	34.0
1966	4,043	4,043	1,242	1,242	30.7
Average percent compound growth rate per annum	34.5	2.7	35.3	3.3	

SOURCE: Current peso data from Dirección Nacional de Estadística y Censos, *Boletín de Estadística*, Julio/Sep-tiembre 1966, p. 260. Current peso values are converted to 1966 pesos by inflating the historical sums with the official wholesale price index for national, nonagricultural products

(precios al por mayor, nacional no agropecuarios). Because the wholesale price index was created only in 1956, 1955 prices are linked to 1956 prices by the consumer price index (*índice del costo del nivel de vida en la Capital Federal*).

of 2.7 percent. The industrial manufacturing component of gross internal product, reflecting the overall success of efforts to increase industrialization, increased somewhat faster: from AS801 billion in 1955 (at 1966 prices) to AS1,242 billion in 1966, an average annual compound rate of 3.3 percent.

Changes in the physical level of industrial production for certain selected items (Chart 3-1) show that very rapid increases of output took place for cement, electrical energy, and crude steel ingots during the period of this study. Automobile manufacturing rose from virtually nothing in 1955 (235 cars were manufactured in Argentina that year) to 133,816 cars in 1966. Commercial vehicle manufacturing rose from 6,156 units in 1955 to a high (in 1965) of 60,789. The automobile boom was spurred by President Frondizi's welcome to foreign automobile manufacturers; at one time during the Frondizi administration, 25 separate automotive companies had manufacturing plans submitted to the government.³ By 1966, 10 separate automobile companies were manufacturing vehicles in Argentina, and the majority of

cars were over 95 percent constructed in Argentina from local material.

The increase in capacity was even greater than the indicated growth of output, since after the expansion of 1960-61 many firms were forced to operate well below capacity. A survey by the Consejo Nacional de Desarrollo (CONADE) in late 1963 indicated that idle capacity ranged from about 40 percent in industries producing motor vehicles, tractors, and electrical machinery to 50 percent or more for manufacturers of agricultural and road machinery, machine tools, and ships.⁴

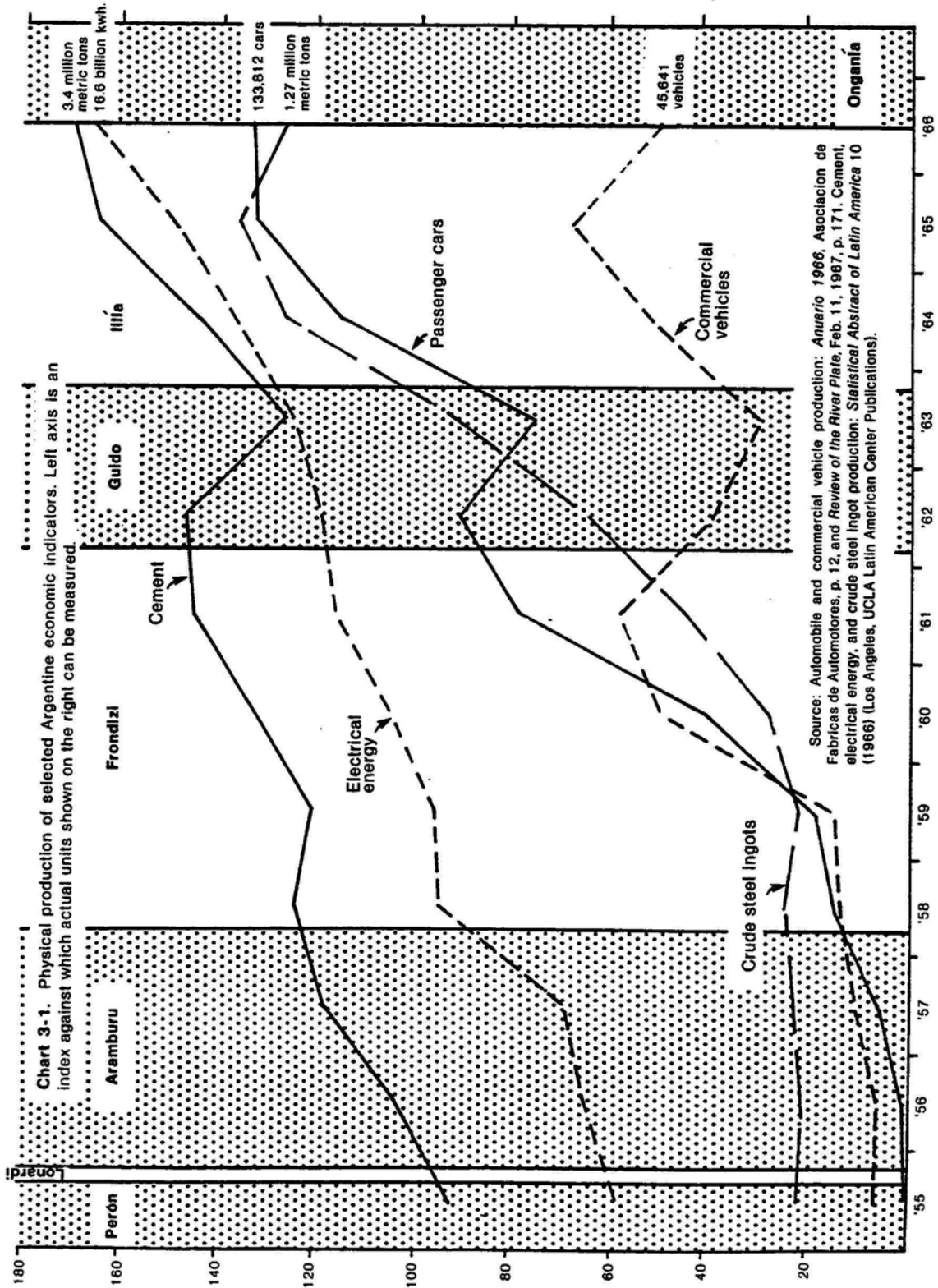
Financial Needs of Argentine Business

Financing a growing industrial sector involves, among other things, accumulating large sums of capital, needed initially to finance expenditures of fixed plant and equipment, and after the capital base is created, to finance working capital so that the capital base can be efficiently utilized. From output figures alone, a prima facie case exists that the industrial sector of the Argentine economy would need infu-

³Buenos Aires Herald, *Motor Car Supplement*, May 23, 1967, p. 4.

⁴Eshag and Thorp, "Economic and Social Consequences," p. 36.

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sions of capital in most of the years under study, and especially in the years after 1959.

In Argentina, capital needs were increased multifold by continued inflation. The official cost of living index (for an industrial worker living in the federal capital of Buenos Aires) and the peso cost of a U.S. dollar are shown in Chart 3-2. The cost of living increased from 19.7 in December, 1954 (1960 = 100) to 447.5 by the end of 1966, an average annual compound rate of increase of 29.7 percent. The increase in the price of the dollar was only slightly less.

Both inflation and deterioration in the value of the peso increased financial needs. With inflation, the normal turnover of inventory into receivables into cash fails to provide sufficient pesos to acquire the next unit of inventory. Continued infusions of peso capital were needed in Argentina to maintain a constant physical volume of operations. To finance expansion an even larger infusion of peso capital is needed.

In noninflationary environments, manufacturing firms borrow funds needed to finance expanded current assets. Potential lenders in an economy of continued inflation, however, soon realize the risks of being a creditor; loans become difficult if not impossible to arrange. The credit shortage in Argentina compounded after 1962, when an even greater than normal demand for funds to finance the working capital needed to bring the fixed plant and equipment just installed into full operation coincided with a rapidly deteriorating peso.

The need for increased peso working capital caused by high inflation is purely a domestic phenomenon. Many of the capital expenditures during the 1959-61 period were financed from abroad, in part because much of the capital equipment had to be purchased in Europe or the United States. This equipment was financed by foreign currency loans during the period from mid-1959 to early 1962 when the peso held a constant value vis-à-vis the dollar. When this exchange rate collapsed after the ouster of Arturo Frondizi, the peso cost of servicing foreign currency loans jumped proportionally. This then added a second thorn to the crown of financial problems being experienced by Argentine industrial manufacturing corporations. The need for infusion of peso capital during the period under study was enormous.

The Recessions of 1959 and 1962-63

Argentina suffered a sharp recession in 1958, and a less sharp but somewhat longer recession in 1962 and 1963. The 1959 recession immediately preceded the period of rapid capital expansion, and the 1962-63 recession came at the close of the same period. Since these two recessions had an effect upon working-capital needs, as well as upon the decisions that led to the beginning and end of the 1960-62 expansion phases, it is important to look at their causes.⁵

The 1959 recession resulted from a severe foreign exchange crisis in 1958, which in turn resulted from an

excess of imports over exports during the immediately preceding years. The continued loss of foreign exchange reserves in the years after the fall of Perón eventually led to a need for help from the International Monetary Fund. The IMF granted funds to Argentina, but extracted in return promises for a number of restrictive budgetary, monetary, and wage policies.⁶ One of the required measures was a large devaluation of the exchange rate, which served (as was intended) to improve the Argentine balance of payments position, but which also led to a drop in industrial production.

In spite of this drop in production, the net result of the International Monetary Fund assistance was that foreign investors regained confidence in Argentina in 1958 and 1959. President Frondizi's policies to encourage capital investing took advantage of the improved climate, and a large inflow of foreign capital took place, both in the form of loans and investments in private industry and of loans to the government. Of particular interest for this study, significant sums of money were loaned to Argentine businesses wanting to modernize or expand their capital equipment. Local credit also became more available as the inflow of foreign credit led to relaxed local credit conditions and to a general aura of economic optimism.⁷

The net result was that Argentina's balance of payments on capital account improved sharply in 1960 and early 1961. However, exports did not increase, in part because the industrial sector continued to operate at very high cost by world standards, and the country continued to run a deficit on current account.

By the end of 1962, short-term foreign debts incurred a few years earlier were coming due. The pressure of the maturities, coupled with a bad agricultural year (owing to weather) and the political crisis over Frondizi's allowing the Peronistas to vote, reversed the flow of capital sharply at the end of 1962. Confidence in the peso dropped, foreign credits disappeared, local capital began to leave the country, and foreign exchange reserves deteriorated. The government was forced to adopt restrictive monetary, credit, and import policies, and the recession of 1962-63 began.

Fiscal and Monetary Policy, 1955-66

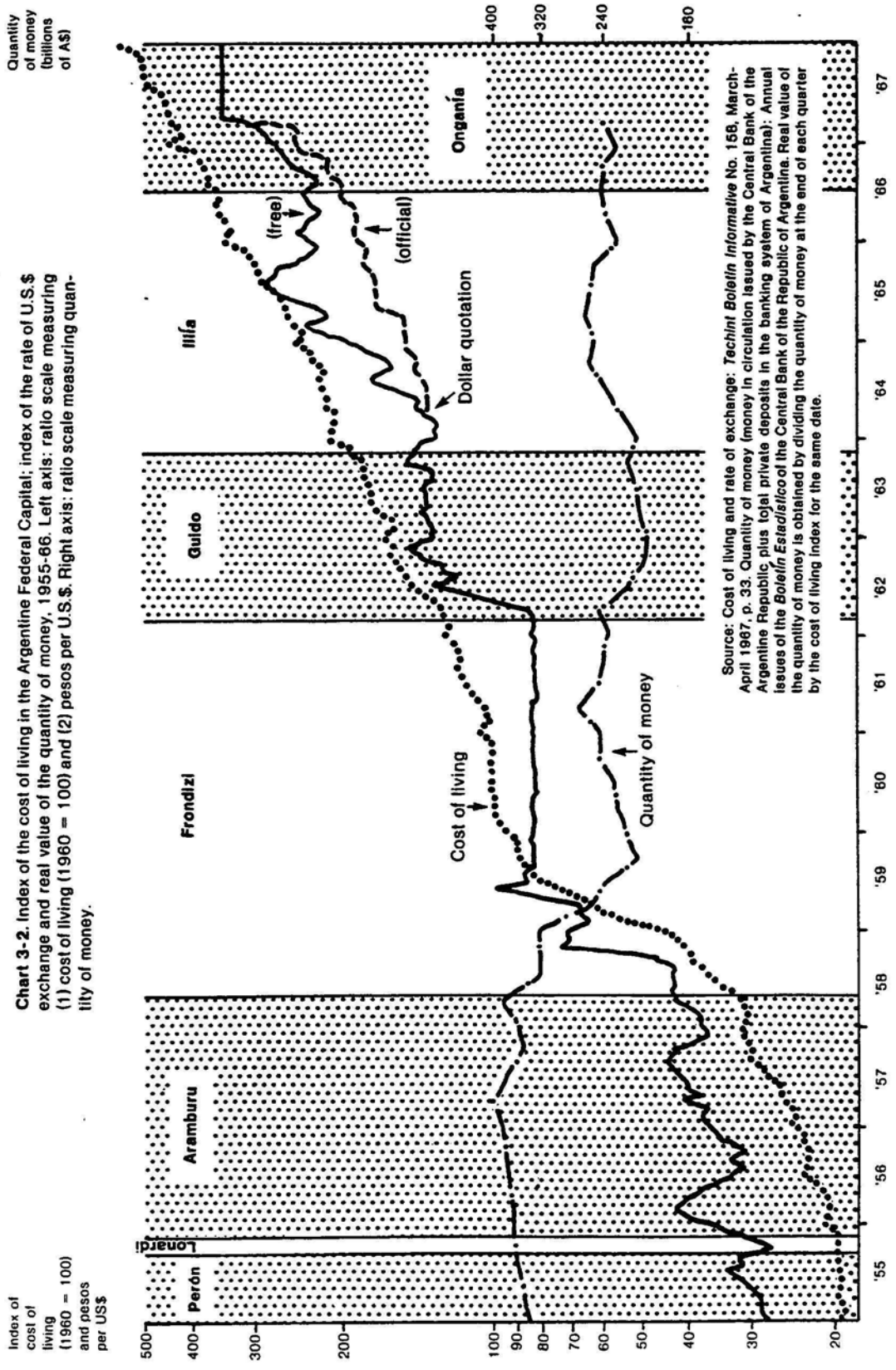
Corporate financing during the era from 1955 to 1966 cannot be separated from governmental policies to restrict

⁶Eshag and Thorpe are critical of these policies.

⁷Eshag and Thorpe state: "The recovery in production in 1960 and 1961 owed much to the influx of foreign capital. The renewal of the IMF standby agreement at the end of 1959, which signified a continued approval of the country's sound fiscal and monetary policy, and the more favourable attitude adopted towards foreign capital by the authorities, resulted in a strengthening of the confidence of the international business and banking communities in the Argentine Government. There was considerable rise in the volume of direct foreign investment and in official foreign loans during 1960. Direct foreign capital receipts rose by US\$180 million to US\$427 million, much of which went to the petroleum industry. Large sums were also invested in the chemical, motor car and certain other branches of industry. In addition, a substantial volume of trade credit was extended to importers by foreign suppliers" (p. 26).

⁵A detailed background to these recessions is provided by Eshag and Thorpe (*ibid.*), from which much of this background summary is drawn.

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inflation and protect foreign exchange reserves.⁸ In formulating these policies, the various governments faced a real dilemma, for they had been unable to reduce the size of the deficit which was caused in large part by the operating and capital deficits of the large national enterprises. (The railroad deficit alone was greater than half the national deficit.) The size of the deficit relative to the ability of the capital markets to supply loan funds to the government was also very large. Consequently, the deficit was "covered" by the simple process of expanding the money supply, while conventional restraints on credit — applied to the private sector — were used in an attempt to restrain inflation. Although these policies were applied in an on-again, off-again manner over the period, the general effect was to force the private sector to bear the brunt of the restrictive policies intended to restrain the inflation caused by the deficits of the public sector. Thus, inflation and tight money continued side by side. Chart 3-2 also shows the real value (deflated by wholesale price index) of the money supply of Argentina from 1957 to 1966, which dropped precipitously from early 1957 to late 1959, rebounded in early 1961, and dropped sharply for the following two years.

Maynard and Van Rijckeghem list several causes of the inability upon the part of the government to reduce its budgetary deficits.⁹ One reason is a tax system in which tax revenues were inelastic with respect to the money supply. Thus, tax revenue failed to rise as fast as GNP in both the short and long run. This owed in part to inefficient tax administration and in part to the structural nature of the tax system. A significant time lag existed between earning a taxable income and the receipt by the government of the corresponding tax revenue on that income. Income taxes on current income and current sales were estimated according to the preceding year's tax base, and were not normally collected in their entirety until the following year. With inflation, the real value of the monetary sums due the government continued to fall behind; but government expenditures did not lag in a similar manner. Thus, the current cash deficit was increased.

The fact that a drop in the real value of tax payments was achieved when taxes were paid 1 or 2 years in arrears in deflated pesos was not lost on taxpayers, who very frequently delayed payment of taxes as long as possible. At times the penalty levied on delinquent taxes, expressed as a percent per annum cost, was less than the cost to businesses of borrowing from commercial sources to finance additional working capital needs.¹⁰ The government deficit was further exacerbated by the fact that a significant portion of revenue

was raised by specific excise taxes, which were not adjusted upward fast enough to keep pace with inflation. Lastly, the government was often reluctant to raise rates charged by governmental enterprises, especially utilities and transportation services, for political reasons as well as to avoid pushing up the cost of living index. Hence deficits of the governmental enterprises were met by the Treasury.

Governmental response to its financial problems was to delay debt payment to its own suppliers of goods and services and to restrict credit to the private sector. For example, between October 1961 and March 1962, central government indebtedness on account of nonpayment of its bills rose from AS17 billion to AS29 billion. This "represented a delay of about two months in the payments of public sector wages and pensions plus outstanding debts to suppliers which in some cases were more than one year overdue."¹¹

As businesses responded by delaying payment of their tax debts to the government, a vicious circle ensued in which the government and the private sector sought financial advantage over each other by deferring debt payments to each other. In the meantime, the real value of the unpaid sums diminished as inflation continued.

General governmental policy of tightening credit to the private sector, in order to control the inflation rate and resolve balance of payments pressures, coupled with the carousel effect of both government and private sector nonpayment of debts to each other, appears to have restricted industrial growth. Traditional economic theory holds that tight credit to the private sector will reduce demand for goods and services, thus restraining the inflationary pressure caused by the phenomenon, as it is sometimes expressed, of "too much money chasing too few goods." In the case of Argentina, it is argued by Maynard and Van Rijckeghem, monetary restrictions had a double effect: in addition to reducing demand, they also produced a severe liquidity crisis in the private sector of the economy as producers found themselves short of the working capital needed to finance output at continuously rising costs. Unable to finance the needed capital infusions, businessmen were forced to reduce output.¹²

Because a large industrial base was constructed between 1959 and 1962, inability to achieve full output in turn often meant only partial utilization of fixed capacity. This in turn meant that fixed costs (including debt service) were large relative to the volume of sales actually achieved, and operations were not in general conducted at the volume needed to lower costs or operate at a satisfactory profit level.

II. Methodology for Analyzing Argentine Corporate Financing

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VIII. Conclusions

In the foregoing pages were reviewed the various aspects of corporate financial policy for Argentine-owned industrial enterprises during the 12 years that followed the

⁸A good description of the government's policies appears in Geoffrey Maynard and Willy Van Rijckeghem, *Stabilization Policy in an Inflationary Economy: Argentina*, Cambridge, Mass.: Center for International Affairs, Harvard University, Report Number 34, June 1966.

⁹*Ibid.*, pp. 36-37.

¹⁰Argentine corporate taxes are explained in greater detail in section VI below.

1955 ouster of dictator Juan Perón. Those 12 years comprised a period of significant growth in the Argentine industrial sector, but they were also a period of rapid inflation and chaotic political conditions. It is hoped that the facts and trends brought to light in this study will cast perspective on similar problems of financing locally owned corporate industrial growth in other countries of the world which are experiencing similar environmental conditions.

Methodology. — Basic data for this study were derived from annual financial statements of a sample of 50 Argentine-owned industrial corporations. The common stock of these corporations is traded on the Buenos Aires Stock Exchange, so for all companies a significant degree of public ownership exists. Financial statements of these companies were filed with the Buenos Aires Stock Exchange within one quarter after the end of each fiscal year in a uniform and detailed format prescribed by Argentine statute. Although inflation of the Argentine type distorts certain financial statistics, there is reason to believe that Argentine financial reporting is consistent for each company on a year-to-year basis. The types of financial statement items considered here are those that are comparatively immune from major distortion owing to inflation.

Uses of funds. — The major use of funds during the 1955-66 period was to increase assets. Debt reduction was only a minor use. From 1955 to 1960, the major use of funds was to increase such working capital items as inventory and receivables. Very little addition was made to cash balances, and only modest additions were made to net fixed assets.

From 1960 to 1962, major additions were made to net plant and equipment, although the amount of increase in real terms is distorted by the accounting revaluation which took place after 1959. Additional funds were used to increase receivable balances, but inventory growth as a use of funds was relatively modest.

From 1962 to 1966 the major use of funds was to increase receivables. Only modest fund flows went to inventory (except in 1964-65) or to increasing net plant and equipment.

Uses of funds by individual industries during these same three periods generally conformed to the overall pattern described above. One exception was that in 1960-62 (and to a lesser degree in 1962-66), a number of companies in assorted industries made portfolio investments large enough to influence the overall industry fund flow statistics. Apparently the 1960-62 period of plant and equipment expansion was accompanied by an acquisition and/or merger movement which, to the author's knowledge, has not been generally recognized by economic observers.

A second exception noted from the individual industry statistics is that in 1962-66, a number of companies used funds to reduce debt owed to financieras.

Sources of funds. — In all periods, the largest source of funds was the increase in owner's equity resulting from retention of large inflation-induced peso profits. The second most important source of funds was increases in debt to sup-

pliers, while increases in bank debt were of lesser importance. Financiera money was an important source between 1960 and 1964.

Changes in the proportion of funds derived from the banking system as compared to other debt sources indicates that banks provided a relatively inelastic supply of emergency funds. Cyclical expansion in the total need for funds tended to be met by delayed payment of suppliers or, as a last resort, by borrowing from financieras, rather than by increasing bank debt. One suspects that the inability of the banking system to satisfy incremental corporate needs for funds is caused by the types of restrictive monetary policy followed by Argentine governments during those years. This leads one to the conclusion that restrictive monetary policies of the traditional type applied in inflation-prone economies tend to force business away from the banking system and toward new types of nonbank financial intermediaries.

At all times, increase in other debts and accruals — which together primarily reflect sums due governmental units for taxes and social charges — was a major source of funds. In 1962-63 and 1965-66 it was the single most important source of debt funds to Argentine business.

If debt sources of funds, which exclude increased equity, are viewed in relation to the three distinct time periods identified in studying uses of funds data, it is observed that during the 1955-60 interval, increased debt to suppliers was of greatest significance, followed in importance by bank debt earlier in this period and governmental debt in the later years.

During the fixed plant expansion period from 1960 to 1962, debt funds were again derived primarily from suppliers and banks, although financieras rose in relative importance.

During the period from 1962 to 1966, generally characterized by economic stagnation and investment in receivables, the major debt source of funds was nonpayment of supplier debts. Very pronounced and irregular changes took place from year to year in the relative importance of other sources of debt funds.

Working capital turnover. — As would be expected from the sources and uses of funds information, working capital turnover periods are long — much longer than is common for businesses operating in the United States. In addition, a steady lengthening of working capital turnover periods occurred between 1955 and 1963. Between these two years, for example, receivable turnover more than doubled, rising from 96 days (1955) to 208 days (1963), and inventory turnover also increased, although to a lesser degree, rising from 124 days to 152 days. Liability turnover doubled, rising from 152 days to 330 days.

The very long receivables turnover periods and the increase in the length of these periods during most of the period of study give an extraordinary picture of how operations in an inflationary environment demand constant additions of capital. Competition to sell under these inflationary conditions is all too often reduced to the simple matter of exceeding competitor's credit terms.

Balance sheet proportions. — Trade accounts payable was the single most important source of debt funds during the period of study, constituting about 34 percent of all debt. Of almost equal importance was the sum of other debt and accruals, which together reflected primarily sums due governmental units.

Third in importance as a source of debt money was bank debt. Data presented showed an almost perfect negative correlation between the amount of trade payables and of bank debt. In general, a decline in one was matched by an offsetting increase in the other, and vice versa, such that the sum of the two constituted approximately 57 percent of total debt. This relationship indicates that when tight money policies in Argentina restrict credit availability to the larger corporations of the type studied, the problem is passed on by these corporations to their (presumed) smaller suppliers.

Financiera money, being relatively high cost, is important primarily as a marginal source of money. This source was most popular during the 1959-62 expansion phase, when it rose to almost 12 percent of total debt.

Debt by Monetary Unit and Maturity

Total debt may also be analyzed in terms of the proportion of short-versus-long-term maturity and the proportion that is peso denominated versus foreign currency denominated. Such information was available for most of the companies in the sample starting in 1960.

Before 1961, foreign currency denominated debt was of comparatively little importance, and peso debt was mostly of a short-term nature. The industrial expansion that began during the administration of Arturo Frondizi was characterized by a sharp rise in the proportion of foreign currency denominated debt. This development saddled many Argentine corporations with extremely large hard-currency debt, payable only with ever increasing peso amounts as the Argentine peso dropped in value after 1962. Living with this hard currency debt after 1962 was a major task of financial management.