

**The Political Evolution of the Industrial Bourgeoisie in Peru:
Industrialists, Bankers and the Garcia Government, 1985-1990**

Thesis submitted to the University of London in partial fulfilment
of the requirements for the degree of Ph.D.

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For Mom and Dad, Cathy, Teddy and Mery

ABSTRACT

This thesis examines the political evolution of the industrial bourgeoisie in Peru. It argues that the industrial bourgeoisie has been undergoing a rapid and dynamic process of economic development and political formation in the period since the reforms of 1968 which reduced the power of the landed oligarchy. The experience of the Garcia government (1985-1990) is used as a case study to illustrate the changing role of industrialists in the Peruvian development process. The Garcia government, a populist government with reformist tendencies and redistributive objectives, nonetheless attempted to forge an alliance with the industrial bourgeoisie as part of its heterodox economic strategy. This approach was later abandoned, as the government attempted to gain greater autonomy from the bourgeoisie through the expropriation of the financial system.

This thesis examines the way in which the industrial bourgeoisie organises itself to intervene in politics, and considers the political and economic factors which acted to stimulate this political development. In this period, industrialists demonstrated an increased ability to forge alliances with other fractions of the bourgeoisie to act collectively in the political sphere; first, through the formation of a confederation of industrial organisations known as CONFIEP, and second, through the successful opposition to the expropriation of the financial system in 1987. This thesis concludes, therefore, that the Garcia government acted as a catalyst for the political development of the industrial bourgeoisie which by 1990 had become a more prominent social and political actor.

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LIST OF ACRONYMS

ABP	Asociacion de Bancos Peruanos Association of Peruvian Banks
ADEX	Asociacion de Exportadores Association of Exporters
AP	Accion Popular Popular Action Party
APRA	Alianza Popular Revolucionaria Americana American Popular Revolutionary Alliance
BCR	Banco Central de Reservas Central Reserve Bank
CADE	Conferencia Anual de Ejecutivos Annual Conference of Executives
CAEM	Centro de Altos Estudios Militares Centre for Higher Military Studies
CERTEM	Certificado de Reintegro Tributario para Empleo Certificate of Tax Reimbursement for Employment
CERTEX	Certificado de Reintegro Tributario para la Exportacion Certificate of Tax Reimbursement for Exports
CGTP	Confederacion General de Trabajadores Peruanos General Confederation of Peruvian Workers
CONACO	Confederacion Nacional de Comerciantes National Confederation of Commerce
CONFIEP	Confederacion Nacional de Instituciones Empresariales Privadas National Confederation of Private Entrepreneurial Institutions
ESAN	Escuela de Administracion de Negocios para Graduados Graduate School of Business Administration
FIE	Fondo de Inversion y Empleo Investment and Employment Fund

FREDEMO	Frente Democrático Democratic Front
IDESI	Instituto de Desarrollo del Sector Informal Institute for the Development of the Informal Sector
IMF	International Monetary Fund
INP	Instituto Nacional de Planificación National Planning Institute
IPAE	Instituto Peruano de Administración de Empresas Peruvian Institute of Business Administration
IPC	International Petroleum Corporation
ISI	Import Substitution Industrialisation
IU	Izquierda Unida United Left
MEF	Ministerio de Economía y Finanzas Ministry of Economy and Finance
MRTA	Movimiento Revolucionario Tupac Amaru Revolutionary Movement Tupac Amaru
PAIT	Programa de Apoyo de Ingreso Temporal Programme of Support for Temporary Income
PPC	Partido Popular Cristiano Popular Christian Party
PROEM	Programa de Empleo Employment Programme
SBS	Superintendencia de Banca y Seguros Superintendent of Banks and Insurance Companies
SNI	Sociedad Nacional de Industria National Society of Industry
UEPP	Union de Empresarios Privados Peruanos Union of Private Peruvian Entrepreneurs

CHAPTER ONE

THE INDUSTRIAL BOURGEOISIE AND STATE IN PERU: A FRAMEWORK FOR ANALYSIS

Introduction

In 1985, the election of Alan Garcia Perez was heralded as a new opportunity for social change and economic growth for the crisis ridden country of Peru. This event raised popular expectations as it was the first time Peru's longest established party, the reformist APRA (American Popular Revolutionary Alliance) had assumed power. Rejecting monetarist stabilisation policies which had brought about deep recession twice in the past decade, the Garcia government developed and pursued 'heterodox' economic policies which emphasised reactivation over austerity, national economic growth over debt obligations, and an alliance with domestic industrialists in the face of what would rapidly become a hostile international community. The long-term objective of this heterodox strategy was to transform Peru's economic structure and its associated patterns of capital accumulation to one more compatible with domestic resources and more conducive to long-term, sustained economic growth.

The Garcia government proposed an alliance with the national industrial bourgeoisie in order to induce changes in patterns of investment and initiate these profound changes in the economy. The government proposed a policy known as '*concertación*' which would not only provide incentives for investment in priority areas of the economy, but would also promote dialogue and negotiation between policy makers and industrialists.

Despite *concertación*, the relationship between the government and industrialists deteriorated rapidly. On July 28, 1987, just two years after assuming office, Alan Garcia announced abruptly that he planned to expropriate the domestically owned financial system. In a televised address to Congress, President Garcia argued that the Peruvian bourgeoisie had acquired control over

the means of production as well as control over the financial system and that this concentrated economic power had become an obstacle to development. As a result, he contended, the excessive economic power of the Peruvian bourgeoisie needed to be curtailed.

A political battle ensued, as bankers and industrialists attempted to prevent the takeover by various means, including legal injunctions, strident lobbying of policy makers, and the rallying of public opinion. The recently created National Confederation of Private Entrepreneurial Institutions, known as CONFIEP, played a key role in leading the opposition to the expropriation policy. A newcomer on the Peruvian political landscape, CONFIEP surprised many analysts by mounting an effective opposition to the Garcia government's expropriation plans and mobilising public opinion. Presenting its campaign effectively in a broader framework of anti-statism and the demand for increased political and economic pluralism, CONFIEP helped to mobilise public opinion against the Garcia government. The strength of mounting opposition from all sectors of society, including some opposition from within Garcia's own APRA party, made the full implementation of the expropriation politically unviable, and the policy was eventually dropped.

These events must be placed in a historical context. The Garcia government's view of the concentration of economic and political power by the elite fraction of the bourgeoisie contrasts with many available studies, which characterise the domestic bourgeoisie as incipient, weak and subordinate to foreign capital (Wils 1979, Thorp and Bertram 1978). According to most accounts, neither the rupture of the alliance between the land based oligarchy and the Peruvian state through the Velasco government's reforms (1968-1975), nor the consolidation of a development orientation firmly committed to capitalist, industrial based growth, was sufficient to stimulate the development of a dynamic industrial bourgeoisie (Fitzgerald 1976, Gilbert 1980). Peruvian industrialists, moreover, had until the 1980s played a very low key political role, without becoming overtly involved in political struggles and ideological debates.

The experience of the Garcia government does not seem to bear out these conclusions, and suggests that important changes may have occurred in the decade since the majority of these studies were conducted. The failed expropriation of the financial system and the success of CONFIEP's resistance, in particular, suggests certain questions. Has the industrial bourgeoisie been able to extend its economic control in the wake of the 1968 reforms? Is it able to transform its increasing economic strength into political power and influence by organising collectively in the political sphere? Does this demonstrate a new willingness on behalf of Peru's industrialists to organise collectively and engage in political activity? These are some of the questions this thesis seeks to explore.

This thesis is concerned with the political evolution of the industrial bourgeoisie in Peru in the post oligarchic period, with a particular focus on the dynamics of its relationship with the Garcia administration of 1985-90. This thesis argues that throughout the 1980s, the industrial bourgeoisie has demonstrated an increased ability to engage in class action and to act directly in the political sphere. The creation of CONFIEP in 1984 which unified existing industrial organisations demonstrated an increased the ability of the industrial bourgeoisie to unify with other fractions of the bourgeoisie to act collectively and to make demands on the state and policy makers. The process of political organisation was further stimulated in the mid-1980s when the industrial bourgeoisie's inability to influence policy under the Garcia government and the subsequent attempt to nationalise privately owned banks, caused industrialists to reassess their relationship to the state. As a result, a significant number of leaders of industrial organisations began to participate in national politics as a means of redressing what they perceived as an imbalance of power between the industrial bourgeoisie and the state. This thesis concludes therefore, that the Garcia government acted as a catalyst for the social and political development of the industrial bourgeoisie in Peru.

The Garcia years therefore provide a rich case study, as it was a period of intense change in the way the industrial bourgeoisie sought to relate to the state,

and the state to the industrial bourgeoisie. It is an unusual case in that Garcia's was a populist government with reformist tendencies and redistributive objectives, but which nonetheless recognised the need to forge an alliance with industrialists in order to pursue economic growth. This approach was later abandoned, as the government attempted to free itself from the constraints imposed on policy making by *concertación* and implement policies, such as the expropriation of the financial system, which were contrary to the interests and demands of the industrial bourgeoisie. The political battle between industrialists and the government over the issue of the bank expropriation provides an interesting case study which illustrates the means by which the industrial bourgeoisie attempts to exercise political influence.

The overt struggle between state and capital in Peru in the late 1980s illustrates in a very clear form many of the subtle and often veiled manifestations of the relationship between capitalist states and bourgeoisies. Many of the strategic political and economic challenges which the Garcia government faced arose from the government's desire to enact reforms which would result in a more equitable distribution of ownership and income, while being conscious of the need to maintain business confidence and promote private sector investment. Garcia's apparent desire to implement deeper economic reforms was constrained by the need to maintain investor stability and engage the support of the industrial sector. The contradictions which emerged in economic policy were the result of the government's failed attempt to balance competing, and sometimes conflicting, class interests.

The sudden expropriation of the financial system represented an attempt by the Garcia government to free itself from the class contradictions which emerged from his economic strategy. The nationalisation can be understood as a deliberate attempt by the government to gain greater autonomy vis-à-vis the bourgeoisie and free itself from the policy making constraints placed on it by the *concertación* policy.

The central questions this thesis addresses relates to the political role of the industrial bourgeoisie and the ability of this group in society to influence the state. It is important to briefly examine the nature of the capitalist state, and to reflect on the nature of the relationship between capital and the state. Before turning to the case study itself, we must first critically examine the existing paradigms which attempt to conceptualise the political power of capitalists and to recognise some of the limitations of these approaches.

1.1 Classes, Economic Conflict and Political Interests

Some orthodox strands of Marxism suggest the simple and pure translation of economic power to political power. This instrumentalist interpretation of the nature of the capitalist state as 'executive committee of the bourgeoisie' fails to adequately account for the complexity of contemporary industrial societies. It is evident that, first, the state can and does implement policies to benefit the working classes which may be detrimental to the interests of capital; second, the notion of a cohesive dominant class with clearly identifiable class interests is problematic by failing to take into account the diversity of interests within the bourgeoisie, and the intra-class conflict which this diversity creates; and third, that the state has the potential for the autonomous formulation of policies and objectives (Skocpol 1985). This less than satisfactory conceptualisation of the state led contemporary Marxist theorists to reformulate the relationship between capitalist states and bourgeoisies. Poulantzas (1973) and others developed the concept of the relative autonomy of the state which sought to redefine the relationship between classes' economic interests and the political process, by assessing the degree of autonomy which the state can exercise from the bourgeoisie and wider class pressures, and seeking to understand the underlying structural mechanisms which may act to limit the ability of the state to act autonomously.

Rejecting the notion that the state is the direct political reflection of the economic structure, these authors argue that in order to perpetuate the capitalist system, the state must develop a degree of autonomy from the self interested and immediate demands of classes and class fractions within society. The heterogeneous nature of the bourgeoisie, moreover, prevents it from unifying or looking beyond parochial demands by class fractions for short term gains in their particular sector of the economy. The relative autonomy of the state therefore becomes essential for the perpetuation of the capitalist system, and frees the state from being subject to the immediate interests of either capital or labour.

These circumstances force the state to adopt a relatively autonomous

position from class pressures in order to implement policies to benefit the capitalist system as a whole. In doing so, the state performs a unifying role which the bourgeoisie itself cannot. However, the autonomy of the state, Poulantzas emphasises, is relative as it is limited by the need to maintain the capitalist system and ensure continued capital accumulation. It is not free from the need to respond to the overall interest of capital. Block (1993), for example, argues that a politically active and class conscious bourgeoisie is unnecessary as a result of the structural mechanisms, such as role of business confidence, which serve to direct the capitalist state.

What this means in practice is that governments and economic policy makers must seek gain the confidence of investors by maintaining economic stability and ensuring a margin of profitability. The real implications of this constraint are made clear by the experiences of the Garcia government whose ability to deepen the reformist programme was limited by the need to create the conditions for investment. The nature of the constraints and policy dilemmas which faced the Garcia government can only be understood by first examining the degree to which capital can act to constrain the decision making autonomy of the state.

Capitalists choose to invest or not to invest as a consequence of their perception of the potential for returns on their investment. This assessment of the prospects of future profitability encompasses a wide range of factors, both political and economic in nature. This is of particular importance in developing economies where the ease of capital mobility means that capital flight is the immediate response to political insecurity. Capital seeks safety, political scientists are fond of saying, but capital seeks profits too. In an era of global markets and integrated financial networks, the international rate of profit becomes the standard which domestic governments must strive to equal.

Investment strikes are the cumulative result of individual decisions to suspend investment plans, based on the impact of economic policy on capital

accumulation. There is no prerequisite of class consciousness or collective action in order for capitalists to engage in such behaviour, as is the case for labour. Investment strikes are in fact a structural mechanism, which are inevitable if the rate of return on investment declines. This factor must therefore be of particular concern to governments, not only because of the profound economic impact a drop in investment can have, but also because of its inevitability under certain economic conditions.

Thus, this concept of relative autonomy is crucial in understanding the constraints imposed on policy makers by capital. However, this level of abstractive argument stops short of explaining the complex and often turbulent political reality. While it is reasonable to suggest that the perpetuation of the capitalist system is a function the state will fulfil without the need for a class conscious and cohesive bourgeoisie, this places the widest of boundaries on what the state can and cannot do. Within those parameters there is still room for divergence of opinion over policy decisions, and the need for capitalists to influence those policy decisions therefore remains relevant. The concept of the state as guarantor of the system has enabled many studies to overlook the very real political debates, struggles and confrontation which occur, particularly in developing countries, between states and capitalists. Nationalisations are not uncommon, nor are rigid labour regimes. The state has proven itself both willing and capable on occasion of implementing policies which are against the interests of capitalists. The potential power of investment withholding does not obviate the need for political action.

This latter point is worth emphasising. The potential for investment strikes gives capitalists inherent, although often latent, power which does not necessarily translate into direct political influence. Investment strikes cannot be used for short-term political pressure nor can they be used consciously for political purposes. They can also be self defeating in times of economic growth and therefore in effect serve only as a last resort veto on overall policy direction. The limitations of investment power as a negative and reactive source of influence still leaves a need for interest articulation and proactive policy influence unmet. This

point is often overlooked by Marxist approaches which imply that as result of the state's role as protector of the system, political action by capitalists is largely unnecessary. For these reasons, Marxist approaches often fail to recognise or directly address the political behaviour of capitalists. Little attention is directed to the empirical study of the form and effectiveness of capitalists' political organisation or their ability to engage in collective action. The role of business associations, to give one notable example, has been largely ignored.¹

Similar gaps are found in the alternative conceptualisation of the link between the economic structure and politics offered by elite theory, which fails to provide a clear methodological approach to examine the way in which capitalists act politically. Instead, power is perceived largely in terms of control over resources. This approach was developed not only as a reaction against the deterministic aspects inherent in orthodox Marxist interpretations of state power, but also to offer an alternative to pluralism, which rejects the existence of concentrated power in favour of its dispersion. The research agenda was initially established by C. Wright Mills, in his controversial study of the American political system, entitled *The Power Elite*. Mills (1956) concluded that there were three major powerful sectors of society - military, political and economic - whose leading elements coalesce to form one cohesive power elite. Although Mills suggested that economic elites are not necessarily allied with political elites, elite studies conclude that it is true of most capitalist societies.

This approach, however, leaves many important questions unanswered. Through which means is the economic elite able to exercise its influence over the state? Does the corporate elite represent broader class interests, or is it using its influence simply to maximise its own profits? Or conversely, can the power of the state be conceptually reduced to the power of the political elite? This approach examines two powerful groups, the corporate elite and political elite, in isolation and away from their respective societal contexts. In actual fact, elite theorists

¹ This gap in the literature is becoming recognised. Recent studies by Becker (1990) and Gislason (1990) have examined business associations within a class framework.

conceptualise power as residing in large scale organisations which have control over resources; e.g., industrial, military and political bureaucracies. This approach tends to perceive the derivation of power in a static light and as institutionally based. Power is believed to be held by a small group which inevitably assumes control over these economic and political institutions. In Michel's *Iron Law of Oligarchy*, he states, 'organisation implies the tendency to oligarchy' (1993:113). The impossibility of direct democracy by the masses, both within organisations and at the national level, means that decisions are taken for and by the few.

A fundamental problem of the power elite concept, as suggested by Bottomore (1964), is the supposed cohesion between the three elite sectors, which is often assumed rather than demonstrated. Many elite theorists, such as Domhoff, argue that an important source of cohesion is a shared social class background. Many elite studies point to a shared social class background of political and economic elites as an important factor which leads to social interaction and leads them to preserve the interests of this social class (Bottomore 1989, Domhoff 1993, Kerbo 1993). It is assumed that political and economic elites, drawn from the same social class, with similar educational experiences, will share broadly similar perceptions regarding economic policy and share the same interest in preserving the overall structure of power in society. ²

The concern with institutional power may be due in part to the context in which most of these studies have been conducted.³ The vast majority of elite studies focus on the U.S. power structure, which is characterised by a stable government and policy regimes and a strong capitalist sector with a consistent

² For a study of the Peruvian power structure using an elite perspective, see Stephens (1971), who likens the oligarchy in Peru prior to 1968 to a ruling class, both economically and politically powerful.

³ Most empirical studies using an elite perspective focus on the U.S. power structure. Mills (1956) and Domhoff (1967) analyze the national power structure, while Hunter's classic text (1953) looks more narrowly at community power structures. One reason for this focus on the U.S. is that elite studies were developed in opposition to the prevailing notion of pluralism in the developed world and often challenge the notion of pure democracy which Western democratic systems are sometimes believed to enshrine.

policy preference for limited state intervention in the market. The application of elite theory which carefully examines the linkages between large scale organisations can be useful in explaining conditions under which the existing order can be perpetuated in a context of stability. It is less useful in explaining government attempts at reform, or the changing patterns of capital accumulation and endemic political instability which characterises most developing countries.

Elite theorists do of course recognise the potential for social change. Their emphasis is however on the circulation of elites and the conflict over power between elite groups, rather than conflict between the bourgeoisie and labour.

According to Prewitt and Stone:

History is the interminable struggle among elites to control the society. This struggle results in the circulation of elites, with established elites giving way to new ideas and new interests. Thus is social change wrought (1993: 126).

The concept of elite circulation is an important aspect of elite theory. In order to preempt mobilisation of excluded elements of society against the elites and well as to avoid explosive intra-elite conflict, there must be a circulation of individuals entering and exiting from their elite positions. Thus, elite theory does not necessarily imply a static and recalcitrant closed elite group. This perception of power and struggle does imply, however, that the large majority of the population, the masses, have very little role in politics and processes of social change. Interest group activity, voting, social movements or other forms of participation which pluralist theories emphasise as important mechanisms of political participation, are thought to have very little impact on the real power struggles in society.

Elite theorists also look at the role of elite alliances in the process of democratic consolidation and political stability. Higley and Burton (1989) suggest that political stability requires a degree of elite consensus and cooperation. In contexts where key elites are blocked from access to decision making arenas, democratic breakdown often results. These studies suggest, therefore, that elite alliances are essential determinants of democratic stability.

Most elite theorists however presuppose a well consolidated economic elite. However, there are salient characteristics of bourgeoisies in developing economies, which make them difficult to characterise and conceptualise. In developing economies, such as Peru's, a strong national capitalist sector able to compete with foreign capital hasn't yet emerged. Capitalists in developing countries lack resources, assets, and access to technology which places them in a comparatively weaker position than their international counterparts. In fact, a significant proportion of the corporate elite in a developing country such as Peru would be foreign. But power is not simply a matter of control over resources. In many Third World countries, economic nationalism has often encouraged states to intervene in the process of industrialisation on the side of domestic capital, and to implement controls on foreign capital.

In a context of unclear rules of the political game and abrupt changes in patterns of capital accumulation, the political role and influence of the bourgeoisie is far more fluid and historically specific than this theory accounts for. Political consensus between state elites and capitalists which elite theory helps to understand is lacking in Peru, where alliances between state and capitalists in recent history has been intermittent and short lived.

Neither of these two approaches on its own provides a clear and complete understanding the far more ambiguous political role of the bourgeoisie in Peru. This thesis demonstrates that the capitalists in Peru adopt a variety of political strategies and tactics, both formal and informal, as part of their efforts to influence economic and political policy. CONFIEP was established in order to increase the ability of capitalists to articulate their interests and make demands on policy makers. Although processes of collective action receive scant recognition in elite or Marxist theory, capitalists worldwide use interest group tactics as a means of influencing public policy and making demands on governments. Pluralist theory, with its focus on interest articulation and political bargaining can shed light on some of these processes.

Pluralists argue that power in society is dispersed among a wide variety of competing groups which seek to influence policy makers. This framework rejects the existence of the cumulative effect of power implied in elite theory, and argue that power in one area, such as in the economy, does not necessarily translate into power in the political arena. While the existence of elite groups in society are recognised, pluralists contend that in modern democratic societies of the developed countries, these elites are continuously vying for power, with no one group or group alliance able to monopolise power. In a classic empirical pluralist study of power, Dahl (1956) examined decision making in a local community in the United States and found that while there did exist certain elite groups, no one group has sufficient power to determine political outcomes.

In sharp contrast to elite theory, pluralists also examine the ways in which non-elites can enter the political process. Pluralists recognise a variety of mechanisms through which the population at large can influence policy and have an impact on decisions. In addition to the electoral process, the role of organised groups in society is thought to be a central means of political expression. The empirical focus is therefore often on 'intermediate' organisations which articulate the interests of specific groups and provide a mechanism through which these interests can be expressed to the state. These organisations are theoretically significant as they perform a mediating role, enabling the interests of groups in society to enter the political process.

Olsen (1993) argues that intermediate organisations and interest groups perform two distinct but essential functions. First, they serve to politicise the actions of individuals. They not only bring individuals into the public sphere but also have the effect of raising awareness and mobilising political activity amongst the population. Secondly, they perform a mediating role between individuals and groups in society to the government, providing a two way channel of information and communication.

An important question arising from this focus on organised groups is the

motivation of significant numbers of individuals which leads them to form groups. Analyses of the forms and structure of group organisation can therefore be enriched by the use of collective action theories which seek to examine the conditions under which groups emerge to act collectively. However, collective action is not reducible to interest group activity, as social movements and other less structured forms of organisation can also be an important ways in which social groups interact with the state.

Despite the advantages of collective action, political scientists have been sceptical about the tendency for groups, which may share concrete material interests, to organise. This point has been made by Olson (1971) from a rational choice perspective, who argues that individuals weigh the cost of organising to its potential benefits. In the case of very large groups, Olson argues, the individual is less likely to act, as his contribution is less liable to make a difference. In addition, the 'free rider' element stipulates that an individual will choose to not participate if others will do, hoping in this manner to reap benefits despite inactivity. Therefore, in the absence of incentives or coercion, it is expected that a rational individual will choose not to participate (Olson 1971). The implication of Olson's study is that one must not assume that mutual interest is a sufficient condition for organisation and collective action.

However, collective action of representative fractions of large groups does occur. This suggests that a pure cost-benefit analysis is not sufficient for understanding instances when collective action does occur. Other studies of collective action have attempted to incorporate 'extra-rational' factors which can act to motivate individuals in to organising and protesting. Other collective action theorists, such as Hardin (1982) suggest that other factors which explain an individual's participation in social movements include a sense of injustice, altruism and a desire to participate in politics (1982:101-24). Hirschman makes a similar point and suggests that non-quantitative elements such as disappointment as well as moral and political commitment need to be taken into account to understand instances of organisation and protest. He argues that groups that experience

repeated disappointment are more likely to protest (1985).

Analytical discussions of business associations and industrial organisations have traditionally been discussed within a pluralist, interest group framework. However, the pluralist paradigm views business associations as one competing interest group among many, albeit one with considerable financial resources at its disposal. The examination of business associations as interest groups leads to a conceptualisation of these associations as purely political organisations. This primary emphasis on organised political structures and bargaining through formal channels provides an incomplete picture of the diffuse sources and forms of the capitalists' actual and potential power. However, most analysts within a pluralist framework recognise that not all organised groups have equal power. More importantly, some argue, there are groups who may have power but which do not use interest group mechanisms to exercise this power. Wilson (1990) argues that in studying interest groups a key question to be considered is the importance of the interest group structure for a given group in society. He points out that in Britain in the first half of the nineteenth century, landed elites did not need interest group representation because of their immense power within government (1990:173). Thus, he argues that the careful study of interest groups, their importance and their functions, reveals much about the relationship between state and economic interests within a society. Wooton (1975) in examining the role and functions of interest groups concurs, pointing out that the business sector is perceived by governments to be the most indispensable of groups, whose support and confidence needs to be won.

Despite the qualifications offered by these authors, most analysts within a pluralist framework focus on the political to the exclusion of the economic. One notable exception is Linblom (1977) who takes this argument further by arguing that political organisation, conflict, and power cannot be divorced from an understanding of economic forces and the role of the market. In his analysis, he argues that there are two primary forms of social organisation. The first is through the 'authority of government'; the second through 'exchange and markets'

(1977:4). An understanding of power, politics and society must extend beyond an examination of organised groups and political structures and examine how the economy shapes society and politics. He emphasises that market forces constrain the power of the state and highlights the continual threat of investment strikes which means that the power of business extends beyond the power of its interest groups.

Therefore, while interest group processes and collective action are important mechanisms of political influence, they cannot be examined in isolation from the economic and political structures of society. It is also important to examine these political structures within a broader context of the historical processes of economic and social development which shape them. In its emphasis on political structures, pluralism often fails to come to terms with the underlying economic interests which business associations represent, or examine those factors which give rise to their formation.

This focus on interest groups therefore needs to be situated within a more comprehensive understanding of the economic structure and interests of this group in society. The political events that this thesis outlines are guided and influenced by economic processes. The analysis of the political role of industrialists cannot be divorced from an analysis of the economic roles and interests of this group. Furthermore, the study of the relationship between industrialists and government must be informed by an understanding of the impact of government policy on investment and patterns of capital accumulation. This study therefore examines the economic policies of the Garcia government in 1985-90 and examines the impact these policies had on both the economic and political behaviour of the industrial bourgeoisie. Only such an approach, which draws from both political science and political economy, allows a deeper understanding of the complex processes of the evolution of the political organisation, action, and ideology of industrialists and the nature of its interaction and influence with the state.

Out of interests, and conflicts of interests, at the economic level, political

organisations and parties emerge. Thus, political analyses must encompass changes in the economic structure and attempt to conceptualise its relationship with the political level. It is at this level where political science pluralist theory with its focus on interest groups can usefully supplement, without contradiction, essentially class focused analyses.

1.2 Economic and Political Interests of Third World Industrial Bourgeoisies

Considerable discussion has focused on the relationship between the economic condition of underdevelopment and the subsequent political behaviour of the industrial bourgeoisie. Much blame has been laid at the door of the domestic industrial bourgeoisie in Latin America. It is often held responsible for retarded economic development as a result of an alleged lack of Shumpeterian entrepreneurship, and is customarily described as weak, nascent and subordinate to foreign capital. Dependence theorists argue that Latin American industrial bourgeoisies are too weak to become hegemonic, and that this very weakness provokes an authoritarian response from governments to fill the power vacuum. On the other extreme, the bureaucratic-authoritarian literature characterises the Latin American industrialists as having reactionary right-wing views, a preference for authoritarianism and sufficient political power to evoke military coups. Reality, as ever, falls somewhere between these two extremes.

The political views of industrialists are necessarily determined by the potential for capital accumulation and the impact of government policy on those processes. Industrialists promote policies which they believe will increase the potential for returns on investment and will lend support to whichever political regime is most likely to generate conditions conducive to economic growth. Political stability is an obvious prerequisite for economic security, and for this reason, bourgeois support has often underpinned authoritarian regimes. Moreover, industrialists worldwide show a distinct preference for a limited state role in the economy. These political behaviours, provide evidence to support the characterisation that industrialists are prone to block reform and tend to lend support for neo-liberal governments. However, the political behaviour and beliefs of industrialists are not predetermined, but are directly shaped by economic processes. This thesis examines a more atypical case in which the industrial bourgeoisie actively supported a reformist government. This case demonstrates that industrialists are willing to accept a degree of reform and redistribution, if they believe that they too will benefit.

An examination of the evolving pattern of accumulation helps to explain the economic interests and conflict which give rise to particular forms of political organisation and policy preferences. The question which needs to be posed therefore, is not only, how are economic interests represented in the political sphere, but also, how are political beliefs and demands determined by economic interests. This perspective enables the industrial bourgeoisie's support for the reformist Garcia government to be more easily explained.

The political nature of Third World industrialists must be examined in the context of developing economies and their changing social structures. The industrial bourgeoisie will have different economic interests, and therefore policy preferences, at different stages in its development. In order to understand the complex and often contradictory political action of the industrial bourgeoisie in Peru, this behaviour must be viewed in the historic context of the recent decline of one class, the agrarian landowning class, and the ascendancy of another, an urban, capitalist bourgeoisie. The former, the landed oligarchy was comprised of both capitalist and pre-capitalist elements based in the primary sector of the economy which were largely export oriented. The boundaries between these two distinct classes remain blurred. Some fractions of the bourgeoisie retain links with traditional agricultural and export interests. As Zeitlin and Ratcliffe (1988) found in Chile, agrarian landlords and capitalists in other sectors of the economy are closely linked. However, these two often contending groups can be conceptualised as two distinct classes.

The urban capitalist bourgeoisie can also be differentiated, and is comprised of industrial, commercial and financial capital. An examination of political and economic evolution of the industrial bourgeoisie necessitates some understanding of intra-class structures and the relationship between the industrial bourgeoisie to other fractions of the bourgeoisie. The industrial bourgeoisie refers primarily to those groups engaged in capitalist production in the secondary, manufacturing sector of the economy. However, there is much overlap between fractions of the bourgeoisie and the conceptualisation of the industrial bourgeoisie

as a clearly defined class fraction is therefore difficult. This thesis illustrates, for example, that many leading industrial groups also control much of the financial and commercial sector, and that complex patterns of interlocking directorships link capitalists across sectors of the economy. The fusion between financial and industrial capital in Peru is particularly notable. However, the focus of this thesis on the industrial bourgeoisie reflects the predominance of industrial groups within the national bourgeoisie and the leading role of the industrial sector in the Peruvian economy.

The relationship of the industrial bourgeoisie to the wider bourgeoisie is problematic to define clearly. Attempts to identify similarity of economic and political interests within the bourgeoisie strictly along sectoral lines excludes other important variables, such as the size of holdings, the relationship with the international economy and with foreign capital, and can obscure the wide variety of potential fault lines within the bourgeoisie. This thesis illustrates, with reference to the Belaunde period of 1980-85, that sectoral interests are those around which capitalists do often coalesce to form intra-class alliances and coalitions. However, there are many variables which are important determinants of economic interests and policy preferences, even within the industrial fraction of the bourgeoisie.

The industrial groups geared toward the internal market have a clear interest in economic modernisation and a proactive state role in promoting industry. These interests in the expansion of the internal market and the development of national infrastructure are often shared by the commercial fraction of the bourgeoisie which is closely tied to urban economic growth. Finance capital, additionally shares an interest in the expansion of the urban economy, increased industrial investment and growing national surplus to fuel the development of the financial system.

There also exist modern and large scale industrial and commercial groups with links to foreign capital that are more closely tied to the external market. These capitalists who may operate companies with licenses from foreign

companies, or who may be geared toward exports, are better able to compete. With ready access to external finance and access to technology, these internationalised fractions of the bourgeoisie are less threatened by integration with the international economy and are more predisposed to advocate neo-liberal economic policies.

The different economic interests of different fractions of the bourgeoisie often manifest themselves in concrete and overt disagreements over policy and result in political conflict. Different groups within the bourgeoisie pursue monetary, tariff, and exchange rate policies to enhance the prospects of growth of their particular economic interests, and as a result, intra-class divisions and conflict continually surface. However, there are fundamental class interests which are clearly shared by all fractions of the bourgeoisie. These elemental underlying class interests, including control over labour, access to credit and capital, and the respect for private ownership, are related to the perpetuation of the capitalist system. When these are under threat, the bourgeoisie is often able to transcend sectoral conflicts.

This thesis sheds light on the ways in which the industrial bourgeoisie interacts with and allies itself with other fractions of the bourgeoisie. Concerted class action by the bourgeoisie as a whole is rare and more likely to occur in situations of crisis in which there is a general threat to private property or the capitalist system. As White (1992) argues, the political organisation of fractions of the bourgeoisie does not necessarily coincide with their economic definition, as intra-class alliances are fluid and shifting in response to changing economic and political circumstances. Thus, it is important to understand the factors which act to enable fractions of the bourgeoisie to form coalitions.

This thesis examines a period in which many factors combined to enable the bourgeoisie to overlook many of the immediate sectoral conflicts of interests which have often acted to inhibit collective action. Economic and political crises in Peru have encouraged unity within the bourgeoisie, and demonstrate the types of

conditions which evoke intra-class cooperation. In response to the severe economic recession of the early 1980s, the bourgeoisie responded initially by succumbing to overt conflict and open dissention, but followed with cooperation and collaboration in the founding of CONFIEP in 1984. In contrast, the primarily political nature of the threat posed by the attempted expropriation of the financial system in 1987 resulted more readily in immediate unification and consensus. While economic policies often benefit some sectors of the economy to the detriment of others, this widespread political attack on private property could in no way be perceived as a zero sum game. Preventing the takeover was unquestionably beneficial to private capital as a whole.

The expropriation of the financial system in 1987 provided motivation for different fractions of the bourgeoisie to draw together and to develop strategies not only to block the measure but also to attempt to advance the interests of the bourgeoisie as a whole. This thesis illustrates that while the industrial fraction of the bourgeoisie was at the core of the process of organisation and political participation, it was able to ally itself with fractions of the wider bourgeoisie.

1.2.a The Impact of Late Industrialisation in Latin America

The characteristics of late industrialisation, including the colonial legacy of a continued dependence on the export of raw materials, penetration of foreign capital in the early stages of industrialisation, has had considerable implications for the development of domestic industrial bourgeoisies in Latin America. Unlike the early industrial era in the West, the indigenous industrial bourgeoisies in these countries were neither the sole nor leading economic force of industrial growth. Both foreign capital and the state itself played significant roles in the process of capital accumulation.

It is generally concluded that the relative economic weakness of the domestic industrial bourgeoisie can act to limit its political leverage. This point has been emphasised by the dependency school. Some of these authors characterise the domestic industrial bourgeoisie as an active partner of foreign capital in

perpetuating dependence (Frank 1972), while others suggest that it is merely the unwitting servant of foreign capital (Cardoso and Faletto 1979). But all concur that the international economic structure constrains the emergence of a dynamic industrial bourgeoisie.

This ambiguous economic role of the domestic industrial bourgeoisie, however, has enabled it to periodically engage the state as an ally. Faced with stronger, more competitive foreign capital, there is a greater propensity on behalf of both the state and industrial bourgeoisie in developing economies to advocate state intervention as a response to the need for policies to build, nurture and protect the incipient industrial sector, and to place some limits on the power of foreign capital. The difficulties of promoting domestic industry in the context of a highly competitive international market has led to a history of state-led development strategies in Latin America. The import substitution industrialisation programmes implemented by most Latin American countries in the 1950s were designed to the development of local industry by restricting imports, imposing foreign exchange controls to encourage domestic production of previously imported goods, developing incentives for value added exports, and imposing controls on foreign capital.

A strong state with an active role in the economy can serve to benefit the industrial bourgeoisie. Despite this, it is often assumed that industrialists are predisposed to advocate neo-liberalism. Certainly, the economic autonomy from the state which can be gained through a pure neo-liberal regime is a feature which makes this approach attractive. But this also presupposes that industrialists are both willing and able to enter the international markets on a competitive basis. An opening of the borders to international trade accompanied by a reduction in subsidies, both fundamentals of neo-liberalism, can have disastrous consequences on a weak, uncompetitive industrial sector. This was clearly the case in Peru in 1980-1985 under the Belaunde government, during which the liberalisation of the economy had devastating consequences on the Peruvian industrial sector. The depth of the crisis had profound repercussions on the industrial bourgeoisie, both

politically and economically. The Belaunde government provides a clear demonstration of the threat neo-liberalism can pose to most fractions of the domestic bourgeoisie. After being confronted with the force of the market and faced with the inability to adapt and compete, the Peruvian industrial bourgeoisie found again that it had much it could gain from the state. The detrimental impact of the liberalisation of the economy in the early 1980s in Peru explains the renewed support by the industrial bourgeoisie for reformist and interventionist policies under the Garcia government. It also provided much of the motivation for the industrial bourgeoisie's efforts to organise and increase its capacity to apply collective pressure on policy makers.

Reformism is therefore a double edged sword for industrialists. There are concrete economic benefits to be gained by interventionist policies. The need for a larger internal market means that increased wages to stimulate domestic demand are needed for increased capital accumulation, but wage increases, conversely, can also act to reduce unitary profit margins. Controlled exchange rates, in addition, can be beneficial to many fractions of the bourgeoisie by cheapening imported inputs, but can have a detrimental impact on the export fraction of the bourgeoisie. Similarly, strict import licensing and protectionism bolsters the demand for locally produced products, while making access to imported inputs difficult. Thus, conflicts among capitalists with different sectoral interests inevitably emerge over the extent and nature of government intervention.

Reformism presents policy contradictions for governments as well. The Garcia government faced many difficult policy dilemmas as a result of its attempt to balance conflicting class pressures. The ability of the government to increase the income of workers by raising wages and controlling prices of consumer goods, for example, is constrained by the need to preserve a margin of profitability. Capitalist states face the perpetual pressure to entice continued investment and generate new positions of employment. Latin American governments, however, are also faced with pressure from subordinate classes for social and economic reform. At the time Garcia came to power, Peru was characterised by a highly

inequitable distribution of wealth, deepening poverty, and growing social conflict arising from these conditions. Policies which extend economic benefits and resources to marginalised sectors of society remain essential, but aren't compatible with preserving the interests of the economic elite.

The state's intervention in the economy means that economic policy making becomes politicised. State managers and government economic teams are continuously making decisions which have a direct impact on patterns of capital accumulation and surplus appropriation. Instead of allowing the allocation of resources to be determined by market forces, governments explicitly assume the role of deciding 'who gets what'.

The highly charged and volatile economic policy making arena therefore means that the autonomy of the state is continuously contested. Classes throughout society are engaged in an ongoing struggle to engage the state to act on their behalf, while the state, in turn is continuously testing the extent of its autonomy and reformulating its class alliances. The attempted expropriation shows the state testing the extent to which it can act autonomously from the bourgeoisie, and illustrates the way in which the bourgeoisie attempts to influence the state. This highlights the need to understand the way the bourgeoisie acts politically.

1.3 The Political Representation of Economic Interests

Although many theories presuppose that the bourgeoisie has limited need for political action, industrialists and capitalists throughout Latin America have increasingly become involved in politics. Industrialists in Peru have throughout the 1980s adopted a variety of strategies to engage politically, ranging from informal alliances with political parties, the development of interest group activities, to direct political participation by prominent industrial leaders. This thesis argues that throughout the 1980s, the industrial bourgeoisie has demonstrated an increased ability to form alliances with other fractions of the bourgeoisie and engage in class action. It will provide evidence to illustrate that the creation of a confederation of private industry in 1984 which unified the diverse industrial organisations demonstrated an increased ability of the bourgeoisie to act collectively and to make demands on the state and policy makers. This process was further stimulated in the mid-1980s when the industrial bourgeoisie's inability to influence policy under the Garcia government and the subsequent attempt to nationalise privately owned banks, caused industrialists to reassess their role within the power structure. As a result, leaders of industrial organisations began to participate in national politics.

The political manifestation of economic interests is difficult to conceptualise. Much of the debate over the nature of the relationship between social classes and political activity focuses on the issue of the viability of the representation of class interests. The conceptual link between economic classes and politics poses many problems for Marxist methods of analysis, as classes do not operate directly in politics. Economic interests are often presented or defended in the political arena through some form of representative institution, such as interest groups, trade unions or political parties. Representative organisations, such as business associations, therefore, can play an important role in translating what may be vague and poorly clarified class interests, into expressed political demands.

These intermediary structures such as political parties or interest groups, are important but partial forms by which economic interests impact on politics.

Although CONFIEP is an organisation of considerable political importance, it is important to recognise the wide variety of mechanisms by which industrialists can attempt to influence policy decisions. There are a variety of strategies, both formal and informal in nature, which industrialists have available to them without the need for collective action. Of course, in most cases, these methods exist simultaneously, although in variable degrees, and coexist alongside each other.

Industrialists have the opportunity for informal and personal contacts with government officials, and in many contexts (such as in 'pre-revolutionary' Peru), these personal forms of contact can act as the primary channel of communication. As elite theory argues, the shared social class backgrounds of capitalists and government officials facilitates communication and social interaction. Governments may often convene meetings with leading businessmen to discuss a particular aspect of economic policy, thereby, bypassing business associations. This type of regular format of debate and consultation on economic policy issues, was a feature of Garcia's *concertación* strategy. Additionally, in countries where the concentration of ownership and wealth is great, the elite sector of the bourgeoisie may often have sufficient political clout to be able to access senior policy makers and state officials at will.

Apart from informal contacts with politicians, business interests are sometimes broadly represented in an institutionalised party of the Right. This type of informal and stable alliance between business and a particular political party exists in many countries worldwide. On an individual level, moreover, industrialists can be politically active and may engage in partisan activities.

However, collective forms of pressure are important when these mechanisms are blocked, or for the small and medium industrial fractions of the bourgeoisie which are excluded from the types of informal strategies mentioned above. In some cases, including CONFIEP, elite industrialists refrained from participation in business associations, as a result of their individual influence which obviates the need for an alliance with other industrialists. However, in

circumstances of crisis, even these industrialists often turn to forms of collective action.⁴

Business associations can have impact which individual forms of political pressure cannot. In addition to the added weight collective pressure may have, associations have the financial and human resources to undertake research and engage in continuous lobbying at a variety of levels, from the executive, to Congress and state bureaucracies. Equally important are their public relations roles. Business associations such as CONFIEP often seek to influence and shape public opinion on political and economic issues through advertisements in the media. Spokespersons of these organisations generally have ready access to the media and are often asked to comment on government policy. This important function of shaping public debates is one which requires the existence of an outlet for collective expression. In the protest against the bank nationalisation, the ability of the bourgeoisie to shape and influence public debates became its single most potent weapon in its struggle with the Garcia government.

1.3.a Industrialists and Collective Action

Industrialists, not only in Latin America but also worldwide have increasingly adopted interest group tactics as a means of influencing public policy and making demands upon governments. Industrialists throughout Latin America have felt the need to organise in civil society for the purposes of influencing political leaders and policy makers. In a study of Mexican industrialists, Story argues that,

Industrialists have become aware of the need for political influence in order to secure economic advantages, and strategies to achieve political influence have become crucial to them... A particular concern of Latin American industrialists has been to achieve greater input into the economic planning process (1986:7).

⁴ Banker Guillermo Wiese, for example, admitted to never having felt the need to participate in CONFIEP until the expropriation of the financial system in 1987. See page 228.

Business associations have therefore assumed a greater importance in the 1980s as dynamic institutions stimulating entrepreneurial development in Peru and in other Latin American countries. These peak associations, or confederations comprised of sectoral industrial organisations, perform numerous functions such as providing technical and information support to members, acting as a representative organisation to lobby government for favourable policies, and providing arenas for analysis of current issues and debate between members of the bourgeoisie. It is through these institutions that the capitalists attempt to resolve basic internal conflicts and articulate their policy preferences to the state and to other sectors in society. These organisations, furthermore, provide a structured arena which is conducive to the identification of individuals as members of a larger group, which may develop an ideological framework to incorporate common interests. This process facilitates the ability of capitalists to engage collectively in a political manner to promote or defend these shared interests.

The issue of motivation is essential to explain cases where collective action is realised. The political strategies capitalists adopt, and the efficacy of these approaches, are influenced by many factors; including regime structures, international ideological trends, evolving domestic social forces, the degree of institutionalisation of the existing parties, and the degree of government receptiveness to lobbying and pressure. It is also important to consider the circumstances which led capitalists to organise at this particular historical conjuncture. In the early 1980s, in a context of poorly institutionalised parties and a renewed desire for protectionism, the formation of an interest group strategy to unify the various sector industrial organisations into one coherent interest group was the clearest option. It was during the period shortly after the transition to democracy which had created new spaces increased organisation in civil society. This interest group structure fills the need to negotiate with any government that came into power, rather than relying simply on one particular party.

Collective action by capitalists, however, is particularly problematic as heterogeneity of the bourgeoisie means that its ability to engage in collective action

is generally limited to periods during which it perceives a fundamental threat to private capital accumulation. The different economic interests capitalists in different sectors of the economy will have can often translate into political differences. Different industrial organisations, such as the Sociedad Nacional de Industrias (SNI) and the Asociacion de Exportadores (ADEX), often have conflicting view on specific policy issues. Capitalists are in direct competition with each other economically, and their perception of each other as competitors means that joint action is rare and tends to occur only in times of crisis. The perception of threat needs to be one held by capitalists across different sectors of the economy and of sufficient menace to enable capitalists to overlook their individual interests and draw together to defend those interests. The neo-liberal economic crisis of 1982 and the expropriation of the banks in 1985 were two such cases. This latent source of political influence, however, is seldom realised. However, the expropriation illustrates that the existence of CONFIEP enables capitalists to mobilise private sector resources and to react rapidly to perceived threats.

CONFIEP is significant for a number of reasons. It is the first successful attempt to unify across sectoral borders and incorporate capitalists from all sectors of the economy. Its potential political influence is enhanced as a result of the massive constituent base which it represents. A distinction needs to be made between industrial level groups, such as the SNI (National Society of Industrialists) hereafter referred to as industrial organisations regardless of their actual sectoral interests, and business associations which act as federations of industrial organisations. The latter type of association tends to be more significant in political terms not only because it aggregates a wider range of capitalists than specific industrial organisations, but also because in its efforts to transcend these specific sectoral interests and concerns, they attempt to articulate views on wider economic and political policy issues. In a study of business associations in industrialised nations, the only such comprehensive comparative study to date, Windmuller found that while members do not entirely share political beliefs,

...there are certain broad areas of agreement that emerge, particularly from the positions expressed by the peak federations for the private sectors. For its is at their level that employer views on

broad policy issues are most often articulated. Industrial level associations through not oblivious to such matters, are for the most part interested in problems specific to their sector; regional and local groups tend to have an even narrower focus. To be sure, subordinate bodies may have to be, and can be mobilized behind a major issue the need arises... But the basic pronouncements are made at the top of the structure. (Windmuller 1984: 5-6).

Thus, CONFIEP is significant not only because of the scope of economic interests which it represents, but also because it seeks to play a broader political role. It marked a departure from the previously reactive and informal political behaviour of industrialists in Peru. The wider political role business associations generally attempt to perform is evidenced by the Venezuelan experience. In Venezuela, the peak association FEDECAMARAS (Federacion Venezolana de Camaras y Asociaciones de Comercio y Produccion) has been the subject of studies by Becker (1990) and Salgado (1987). While Salgado treats FEDECAMARAS simply as a self-interested pressure group, Becker argues that this association is representative of a bourgeois social movement which is, 'oriented to reforming the existing balance between state and civil society' (1990:115). It acts not only to defend its parochial economic interests, Becker asserts, but it also began openly to 'question the unrepresentativeness of the Venezuelan party system and the lack of real political pluralism' (1990:126). The primary source of ideological cohesion both within FEDECAMARAS and between it and other social groups in Venezuela was a growing conviction in anti-statism, not only in the economic sense, but also in a wider political framework. This has parallels, again, with the events that this thesis chronicles in the Peru in the late 1980s, as widespread disaffection with the statist Garcia government began to grow.

1.4 The Industrial Bourgeoisie as a Political Actor: The Study Objectives

This thesis examines the political evolution of the industrial bourgeoisie in Peru in the post-oligarchic period, with a particular focus on the dynamics of its relationship with the Garcia administration of 1985-90. In attempting to examine the industrial bourgeoisie's political behaviour, the formation and role of CONFIEP (The Confederation of Peruvian Private Enterprises) is emphasised. The broader theoretical question of the ability of the industrial bourgeoisie in Peru to engage in collective action for political purposes can therefore be presented as a more concrete research task which assesses and analyzes the functions and strengths of CONFIEP. It is not intended to assert that the political activities and beliefs of the industrial bourgeoisie can be reduced to the activities or ideological pronouncements of CONFIEP. Nor is CONFIEP a pure reflection of the class interests that it claims to represent. One of its primary functions is in fact to find areas of convergence between contending fractions of the bourgeoisie, which may have varying interests. Moreover, its leadership content may result in the over-representation of certain segments of the bourgeoisie, which may not necessarily represent the interests of the majority. Despite these admitted drawbacks, however, it is the most visible manifestation of the bourgeoisie as a social collectivity, involved in collective action in the political sphere. It is the political actor which explicitly aims to promote the interests of capitalists and is amenable to empirical political analysis.

This thesis adopts the position that the state is relatively autonomous, with the origin and impetus for policy decisions coming from within the government, although guided by concerns for business confidence and wider class pressures. The ability of the government to implement policies which have an adverse impact on profitability in various sectors of the economy, it is suggested, means that industrialists do need to develop strategies to engage in the political sphere to influence policy outcomes.

This is a study which examines the way in which the industrial bourgeoisie

organises itself to intervene in politics. In doing so, the method of analysis has much in common with pressure group theories, which examine the concrete and specific political organisations and the way in which they interact with the state. However, while focusing on processes of interest articulation and political leverage, this analysis will be tied to the nature of the economic system. Because of the intrinsic importance of the economic interests of capitalists, is inadequate to use a simple version of interest group analysis which focuses on political forms and structures to the exclusion of the economic forces it represents and the historical context of the development process in which it is situated. Although using class as the primary unit of analysis, this thesis does not adopt a Marxist framework. The intervention in politics by capitalists is a highly complex and often contradictory process which cannot be adequately understood by remaining within one of the broad theoretical paradigms outlined above.

This study will fill an important gap in the literature on politics in Peru, by examining the evolving political role of industrialists. Neither the ways in which the industrial bourgeoisie intervenes in politics, nor the political and economic processes which acted to stimulate this political development, have yet been studied. This is the first study to focus on the political organisation of the industrial bourgeoisie in the 1980s and to chronicle its development as a political force.

1.4.a Sources of Data

The views and political perception of industrialists presented here draws heavily from a publications published by industrial organisations. Particularly useful was the monthly publication *Industria Peruana*, published by the SNI (National Society of Industry), which often has a editorial and often overtly political tone to it. Also important in the 1987-1990 period was *Presencia*, established in 1987 by CONFIEP (National Confederation of Private Entrepreneurial Institutions). *Peru Exporta*, published by ADEX (The Association of Exporters), while less political in nature, offered an insights into the relationship between the exporters and Garcia government.

The annual reports and other publications from these industrial organisations were also used to gain an understanding of the structure, history and functioning of these organisations. Published proceedings of private sector yearly conferences conducted by CONFIEP, IPAE, as well as CADEs (Annual Conference of Executives) were also a useful indicator of private sector views. Published speeches and interviews with business leaders were also found in these and other publications throughout the period being studied. These published sources were useful in gauging the changing tone of the bourgeoisie and views towards the Garcia government.

In the period 1991-1992, a select number of unstructured interviews were conducted with representatives from the three leading industrial organisations: CONFIEP, SNI and ADEX. These personal interviews, conducted in the aftermath of the Garcia generated crisis, had the drawback of allowing only a static picture of the views of industrialists at a particular point in time. For this reason, more emphasis has been placed on published speeches and interviews with business leaders throughout the 1984-1990 period in an attempt to accurately portray the gradual evolution of their views.

Data on the structure of ownership in the industrial and financial sector were drawn from two primary sources, the Peru Report's annual listing of the top 1500 companies in Peru, and the similar listing published by the Andean Report. Information regarding directorships of the top economic groups was drawn from the yearly directory published by CONACO, the National Confederation of Commerce.

A chronology of the events which occurred during the 1984-1990 period were drawn from a variety of sources, most important among them being the Lima daily, *El Comercio* and *Resumen Semanal*, a weekly news summary published by DESCO in Lima. Also utilised were the *Latin American Weekly Report*, *Actualidad Economica*, *Caretas* and the *Andean Report*.

Peruvian government publications were used for economic data. Where possible, figures from the Annual Report (*Memoria*) of the Central Reserve Bank were utilised for consistency. Publications from the National Planning Institute were used for information on the heterodox strategy, as were published interviews with leading government officials. This was supplemented by select interviews with policy makers within the APRA government.

CHAPTER TWO

THE EMERGENCE OF THE INDUSTRIAL BOURGEOISIE

Introduction

The emergence of the domestic industrial bourgeoisie in Peru has been a late and slow phenomenon. The power of the landed oligarchy resided not only in its control over land, newspapers and the financial system, but also in its ability to secure economic policies which allowed the export sectors of the economy to flourish. The power of the landed oligarchy was broken only in 1968, when a radical military government enacted sweeping reforms, expropriating much of the oligarchy's material holdings.

The late development of the Peruvian industrial bourgeoisie was the result of a variety of factors, as this chapter will show. In the 1960s, at a critical period in the development of Peru's manufacturing sector, policies which encouraged direct foreign investment led to foreign capital domination of many key sectors of the economy. The incipient industrial bourgeoisie faced intense competition not only from foreign capital, but also faced additional obstacles including the landed oligarchy whose control over the financial system enabled it to direct surplus to the primary sector of the economy. In the absence of proactive industrial policies to develop and protect the indigenous industrial sector, Peruvian industrialists played a secondary role in the growth of most sectors of the economy.

The Peruvian 'revolution' of 1968 is generally agreed not to have been very revolutionary. This non-revolution did, however, effectively attack the material bases of power of the traditional oligarchy. This chapter will examine the factors which served to inhibit the growth of the industrial bourgeoisie, and will assess the impact of the Velasco reforms on those factors. This chapter will also examine the impact of the economic crisis of the early 1980s on the industrial sector before turning to the discussion of the socio-political development of the

industrial bourgeoisie in the chapters which follow.

2.1 Industrial Growth in Peru 1950-1968

Even within a Latin American context, Peru began to industrialise at a late stage. The pattern of delayed industrial development must be understood in the context of Peru's economic history and the crucial role of the export sector in leading the nation's economic growth. The guano boom in the late 1800s played a significant role in establishing the export of primary products as the foundation of economic growth in Peru (Palmer 1980:15). Both the state and local oligarchy benefited from the guano boom, and the export policies which were to become firmly entrenched as a development strategy were the result of the economic success experienced by Peru in entering the world market on this basis. This laissez faire economic strategy was sufficiently successful for it to be accepted as a proper development orientation until the mid-1950s. The export of mining and agricultural products, including sugar and cotton, were central to the Peruvian economy and these sectors formed the backbone of economic power of the landed oligarchy.

Peru's economy failed to diversify substantially beyond the export sectors for multiple reasons. The seminal work by Thorp and Bertram (1978) which closely chronicles the trends in the Peruvian economy in the 1900s reveals the lack of commitment by the state to industrial promotion prior to 1968 and demonstrates the adverse impact that the lack of a coherent policy has had on patterns of economic growth. Isolated period of government intervention in the economy to encourage local industry were largely ineffective. Relative prices and profitability, in a economy with a restricted internal market provided little financial incentives for Peruvian investors to shift their resources away from the export sectors to the manufacturing or urban commercial sectors. Low or non-existent tariffs and a small market enabled imports to largely satisfy existing demand.

However, the impetus for the small manufacturing sector which did exist was directly related to the expansion of Peru's export base which had spin-off

effects in other areas of the economy. In the 1940s the growth of the mining, fishing and agricultural sectors created a demand for capital goods and intermediate inputs, such as industrial chemicals and paper, and stimulated the weak manufacturing sector.

The open economic policy which predominated throughout the early to mid-1900s placed little controls on direct foreign investment, and as a result many of the key export sectors, such as mining, as well as the manufacturing sector became increasingly controlled by foreign capital. The incipient domestic entrepreneurial class found itself effectively crowded out from investment in certain key sectors of the economy, as it often faced competition from both foreign capital and the traditional landed oligarchy. There were occasions when the relative lack of interest of one or other of these competitors provided the space for the expansion of the local industrial sector. The fishing boom of the 1940s is one such example. In the absence of strong oligarchic interest in the fishing sector and minimal foreign investment, small local firms proliferated as a response to these opportunities (Thorp and Bertram 1978:181). Other areas with local entrepreneurial involvement were the small scale commercial and light consumer goods sectors.

Industrialisation began to gain impulse in the 1950s, with manufacturing growing from 19 percent of GDP in 1950 to 23.6 percent in 1960 finally outstripping the growth of agriculture and mining (see Tables 2.1 and 2.3). This coincided with a growing recognition of the need for industrialisation and diversification away from the export of primary products, as well as for the growth of urban employment, and the local production of consumer and durable goods. An industrial bourgeoisie, with interests in the urban manufacturing and commercial economy began to emerge during this time. In 1958, a economic recession, a declining export base, and an industrial group able to pressure the government for incentives and protection prompted a significant policy shift. Three factors simulated the industrial growth in this period: the devaluation of 1958, the industrial promotion law of 1959, and the growth of the domestic financial system

(Thorp and Bertram 1978). As a consequence, the volume of manufacturing output grew tremendously, both in real terms and relative to mining and agriculture, throughout the late 1950s and 1960s (see Table 2.1).

Table 2.1 Volume of Manufacturing, Agriculture and Mining Production: 1950-1974 (1963 = 100)

	50-52	53-54	55-56	57-59	60-65	66-68	69-70	71-74
manufacturing	40.62	49.75	56.07	61.44	96.93	135.01	148.99	190.21
agriculture	67.48	78.15	77.07	82.19	100.45	104.61	110.71	119.84
mining		44.39 ¹		75.59 ²	98.35	109.71	115.93	119.52

SOURCE: Fernando Gonzalez Vigil, *Capital Extranjero y Transnacionales en la Industria Peruana*. Editorial Horizonte, Lima. 1982. p.18.

1/ corresponds to the period 1950-55

2/ corresponds to the period 1955-60

The industrial policy developed in 1959 included an Industrial Promotion Law which provided incentives and a reduction in import duties for manufacturing inputs.¹ However, these incentives were applied to both domestic and foreign companies and as a result, the primary impetus for the rapid industrial growth between 1960 and 1966 was of foreign origin. Thorp and Bertram show that of the 242 foreign manufacturing corporations existing in Peru in 1969, at least 169 of them had entered Peru after 1960.² The percentage of U.S. direct investment in manufacturing continued to grow throughout this period (see Table 2.2).

The Industrial Promotion Law, paradoxically, failed to strengthen the budding domestic industrial bourgeoisie, and may have thwarted its development by encouraging foreign investment in the growing manufacturing sector. The law was, in fact, specifically designed to attract foreign investment. One important

¹ The Industrial Promotion Law was put forth in 1955, but not passed until 1959, as a result of strenuous opposition by exporters.

² Thorp and Bertram (1978:268) citing Anaya (1975).

implication of this is that the lack of domestic dynamism may not be primarily attributable to an inherent weakness in the Peruvian bourgeoisie. Thorp and Bertram conclude that in the 1960s, the weak behaviour of the 'obvious candidates for the part of the industrial bourgeoisie lay behind the continued incoherence of government policy' (1978:267). It can be suggested, therefore, that the lack of a dynamic and powerful industrial bourgeoisie at that stage was due, in part, to market forces and inappropriate government policies which emphasised exports over manufacturing, and encouraged foreign investment to the detriment of domestic investment.

Table 2.2 US Direct Investment in Manufacturing 1950-1968

	US\$ millions	% of total investment
1950	16	11.03%
1955	23	7.54%
1960	55	12.33%
1965	79	15.33%
1968	96	13.87%

SOURCE: Anthony Ferner. 1982. *La Burguesia Industrial en el Desarrollo Peruano*. Editorial ESAN, Lima. p.70

Processes of modernisation and industrialisation began to place strains on the economic and political position of the oligarchy. As the economic structure of Peru began to evolve, the social order built upon it grew more tenuous. Both inter-class and intra-class conflicts became more pronounced, as the hegemonic influence of the oligarchy began to wane. This landed agro-export elite, which has often been compared to a feudal ruling class, had under its control the key productive areas of the economy, including agriculture, mining and the financial system; newspapers; and the ability to direct economic policy to the benefit of its export interests. Until the military government's reforms, the oligarchy had shown great resilience, surviving not only successive economic crises, but also withstanding increased pressures from subordinate groups.

In must be noted that by this stage the oligarchy was not 'monolithic' but

was internally differentiated (Ferner 1979, Bourricaud 1970). At least two groups can be identified, the traditional Andean *gamonal*, and the more modern coastal elite, involved in intensive agricultural production. Some of the oligarchy, primarily those from the coastal elite involved in capitalist modes of agricultural production, began a process of economic diversification by extending their investments into the growing manufacturing and commercial sector of the economy. In addition to these fractions of the landed oligarchy, there existed a local entrepreneurial class whose interests lay in the urban economy. It is difficult to make a clear delineation as members of this growing urban-industrial bourgeoisie as they retained close ties to the oligarchy, both economically and socially. Many studies suggested that these first industrialists, usually of immigrant families, were later coopted by the oligarchy (Durand 1988a). Industrialists were often coopted into the social circles of the oligarchy, and were therefore often unwilling to engage in active opposition to the export elite (Astiz 1969). The permeability of the oligarchy enabled elites in banking, industry, commerce, and even government, to become a part of the socially defined upper class and obtain a highly respected position in the social order (Stephens 1971:107). According to Wils, therefore, the 'perception of an open and accessible upper class probably helped to sustain the existing social order' (1979:152). Through this type of cooptation, or the perception of upward mobility, much of the potential threat from industrialists was neutralised.

A key question arising from this sudden growth in manufacturing is whether this signalled the formation of a national industrial bourgeoisie. More specifically, to what extent can this be said to reflect an emerging industrial bourgeoisie whose income was derived primarily from urban oriented, manufacturing interests or did this simply reflect the diversification of the oligarchy and increased foreign capital investment in manufacturing?

Table 2.3 Composition of GDP: 1950-1985 (percentage of total GDP)

	1950	1955	1960	1965	1970	1975	1980	1985
manufacturing	19.0	21.7	23.6	24.6	24.9	25.1	23.8	22.1
agriculture	23.8	19.3	17.1	14.5	14.2	11.6	9.9	11.5
mining	7.6	7.9	10.3	9.0	9.1	7.2	12.9	12.6
other	49.6	51.1	49.0	51.9	51.8	56.1	53.4	53.8

SOURCE: Instituto Nacional de Estadística, *Compendio Estadístico 1988*. 1989, p. 213.

Many studies were inclined to consider the increasing growth of manufacturing to be an indication of the economic diversification of the oligarchy. Thus, according to authors such as Fitzgerald (1976, 1979) and Astiz (1969), much of this initial investment was carried out by members of the export oligarchy, rather than by entrepreneurs committed to industrialisation. This view is shared by Espinoza and Osorio (1972) in a major empirical study of the Peruvian industrial sector, which found the existence of six major industrial 'constellations' or conglomerates of industrial interests, which were closely linked with the traditional oligarchy as well as with foreign capital. According to Fitzgerald, at this time there was 'no real distinction between, say, the industrial entrepreneur on one hand and the feudal landowner on the other' (1976:18). This economic growth, these authors argued, could be explained by both increasing oligarchic investment in this area of the economy and to a greater degree, by the continued growth of foreign investment. The implication of the lack of a domestic and industrial bourgeoisie, according to Fitzgerald, was that there was no real commitment to industrialisation (1976:18).

A second school of thought shows the influence of the oligarchy in industry to have been minimal, and the role of national industrial capital during the period of industrial expansion to have been greatly underestimated. This argument has been advanced by Ferner, who asserts that this economic expansion was indicative of a growing national bourgeoisie, which dominated the food and wood industries and comprised a significant proportion of the metal and plastics industries (Ferner

1979:279).

This latter hypothesis is supported by an examination of ownership patterns in the industrial sector, which shows that the oligarchy's control over this sector was tenuous, at best. There is clear evidence to support the assertion that a domestic bourgeoisie based primarily on urban commercial and industrial interests began to emerge early in the century, with its growth and economic significance accelerating in the 1940s and 1950s. The industrial interests of the export oriented oligarchy comprised only a small proportion of existing industry. A Peruvian study found that in 1968, large scale landowners controlled a mere 13 of the 378 top industrial companies, while having minority shares in only 61 of them (Valderrama and Ludmann 1978:36). This study of industrial ownership also found that the oligarchy's participation in the industrial sector was characterised by minority shareholding, thus, dispelling the notion of the oligarchy as the entrepreneurial force leading the development of the urban economy. Wils, furthermore, found that after 1950, a declining proportion of investors in the consumer and intermediate goods sectors were from the oligarchy (Wils 1979:64). The innovative entrepreneurs in the industrial sector, according to Bourricaud, were either 'recent immigrants or Peruvians of fairly low social status', which led the oligarchs into lucrative areas which were previously untapped (Bourricaud 1970:47).

Thus, these studies provide convincing empirical evidence to show that the growth of manufacturing was in fact indicative of a growing industrial bourgeoisie. However, while the degree of oligarchic control over the manufacturing sector in the 1950s and 1960s may have been less than is sometimes assumed, there is also evidence to suggest that the both foreign capital and the oligarchy acted to block the development of the incipient industrial bourgeoisie. The growth of the domestic industrial bourgeoisie was not unfettered.

First, it has been argued that the oligarchs' control over the financial system enabled it to monopolise the use of credit, and in doing so, 'starved the

emerging Peruvian industrial capitalists of credit' (Weeks 1985:82). In the period between 1964 and 1967, Weeks found that the allocation of credit to the manufacturing sector declined despite both the growing importance of manufacturing as a percentage of GDP, and the declining role of agriculture. This argument takes on particular significance in light of the later development of the 'economic groups': a fraction of the bourgeoisie with interests in industry and the financial system, but which has clear oligarchic origins. These groups were able to use their access to credit to finance their expansion into the urban economy.³

Second, the government still wavered in its commitment to industrialisation, remaining hesitant to introduce the degree of control over foreign capital and protection of the internal market which would have been needed to stimulate domestic industry. Despite the industrial promotion law, the overall direction of Peru's economy remained export led. Foreign capital entered freely and the protection of most manufacturing sectors remained minimal.

Third, changing patterns of direct foreign investment away from large scale extractive projects to the manufacturing sector lead to foreign domination of many key manufacturing sectors. Encouraged in part by the generous incentives offered by the Industrial Promotion Law of 1959, direct foreign investment from the United States in manufacturing grew from US\$23 million in 1955 to US\$96 million in 1968 (see Table 2.2). The sectors in 1969 in which over 75 percent of production was produced by foreign capital included, tobacco, paper, rubber, petroleum derivatives, non-ferrous metals, cement, and transport equipment (Ferner 1982:68). Highly competitive foreign firms and a restricted internal market for manufactured goods left little space for Peruvian industrialists.

In conclusion, there is convincing evidence that the growth of the secondary sector in the 1950s and 1960s should not be seen purely as the result of oligarchic investment, but as an indication of a newly developing national

³ An in-depth discussion of the economic group structure is found in Chapter three.

industrial bourgeoisie committed to industrial and commercial interests. This fraction of the bourgeoisie, however, posed no real challenge to the hegemonic position of the agro-export elite and it remained unable to challenge the domination of foreign capital in the manufacturing sector.

The excessive degree of external dependence of the Peruvian economy became an important political issue and was addressed by the government of Fernando Belaunde of the Accion Popular (AP) party elected power in 1963. His mildly reformist campaign platform dealt with the growing political questions of agrarian reform, industrial promotion and the regulation of foreign capital. In regard to the latter point, one particular case, that of the International Petroleum Company (IPC), became a high profile issue. The favourable conditions granted to the company had become a rallying point for demands for harsher conditions for foreign capital as a more nationalist view toward economic development became widely accepted.⁴

Yet, the government appeared unable, or unwilling, to make a concerted break with the past and enact reforms to modernise the economic and social structure. While the Belaunde government was initially pro-industry, according to authors such as Caravedo, this alliance was quickly worn away by the persistent power of the oligarchy (1977:115-16). The tepid reformism of the Belaunde government failed to resolve the problems of foreign capital domination and the continued power of the landed elite. This impasse broken in 1968 by an unlikely source: the military.

⁴ See Kuczynski (1977) for an insiders account of the IPC case and a discussion of the first Belaunde administration.

2.2 The Velasco Government and the Industrial Bourgeoisie

The Revolutionary Government of the Armed Forces assumed power on October 3, 1968, and acted to speed the destruction of the oligarchic state, rather than preserve it.⁵ The government sought to make structural changes in the patterns of ownership and production in the Peruvian economy. The reformist military government declared as its central objectives a lessening of Peru's external dependence; a more equitable structure of ownership and income; and the development of a new model of economic growth that was neither capitalist nor communist.

Many of the reforms were designed to weaken the economic prominence of both the oligarchy and of foreign capital. The military moved quickly to translate this ambitious sounding rhetoric into action. The U.S. owned International Petroleum Company, whose generous conditions granted by the Belaunde government had become a political issue, was swiftly nationalised while a sweeping agrarian reform devastating to the power of the oligarchy was implemented. The agrarian reform and nationalisation of much of the national financial system, and well as some extractive industries such as fishing, effectively reduced the oligarchy's powerful role in the economy. In addition, the government decreed worker participation in the management and profits of private sector industry.⁶ The government also developed a corporatist organisation, SINAMOS (Sistema Nacional de Apoyo a la Movilizacion Social), to organise and mobilise the marginalised groups of society. The reforms of the first and more radical phase of the military government in 1968-1975, were designed to sweep away the rigid social order which characterised the oligarchic state, and

⁵ There is an extensive literature examining the reformist military government in Peru. For excellent collections of articles see Lowenthal (1976), McClintock and Lowenthal (1983), and Gorman (1983).

⁶ The Industrial Community legislation decreed that 15 percent of profits of industrial firms be transferred to its employees. Employees were also entitled to representation on the board of directors. For an in-depth discussion of the Industrial Community legislation and its impact on domestic industry, see Alberti, Santistevan, and Pasara (1977).

incorporate marginalised peasant and working classes into a more modern social, economic and political structure of Peru.

Why did the military suddenly turn against the social order that it had long protected? This process of industrialisation had generated both inter- and intra-class conflict throughout the 1950s and 1960s. The process of modernisation also prompted institutional changes within the military. Stepan and Trimberger emphasise the impact of two crucial issues on the military: first, the role of foreign capital and the IPC debate which generated a deeply nationalist ideology within the military; and second, the rural insurgency which led the military to recognise the potential conflict if the agrarian issue was not dealt with more directly. Furthermore, the military itself was becoming politicised and was developing a high degree of ideological unity. The new professionalism was linked to the development of the Centre for Higher Military Studies (CAEM), which enabled the military to develop its own political objectives and create a necessary leadership corp (Stepan 1978:136). The non-oligarchic origins of the military leaders enabled them to develop a high degree of autonomy from the oligarchy and accept the need for agrarian reform (Trimberger 1978).

Industrialisation was also a priority for the military government. Imports which directly competed with domestically produced goods were banned, while controls on foreign capital were tightened, preserving the market almost exclusively for domestic producers. Tax exonerations for investment were coupled by a reduction in tariffs on intermediate and capital goods in order to stimulate investment in the industrial sector. The military assumed that by reducing the role of the oligarchy and foreign capital in the economy, the industrial bourgeoisie, freed from subordination, would be in a position to lead the growth of the economy and modernise the productive structure.

The first two years of the Velasco government was characterised by a 'honeymoon period' between industrialists and the military government (Ferner 1982:147). The import substitution industrialisation (ISI) model implemented in

1968 had elements which coincided with the industrialists' own programme.⁷ The National Society of Industry (SNI), at the time the primary representative body of the industrial sector, welcomed the state's new role in directing economic development and promoting domestic industry. This support must be situated in the historical context in which it took place. The ISI proposals of the United Nations Economic Commission for Latin America (CEPAL) and the dependency school were influential throughout Latin America in this period. It was a school of thought which advocated a shift away from export led economic models, to one which prioritised the local production of goods through the development of domestic industry. For the emerging industrial bourgeoisie, subordinate to foreign capital as well as to the agro-export oligarchy, this proposal held strong appeal.

Until 1970, the industrial sector seemed united in its support for the Velasco government. However, as reformist measures deepened, unity within the industrial sector began to falter. The issue which provoked the deepest debate was the Industrial Community Law, which decreed worker participation in the management and profits of privately owned companies. The attitude of the SNI towards the military government which it had previously supported, shifted at this juncture to confrontation and opposition. For the small and medium industrialists which led the SNI at this time, the central issue was the role of the state in the economy.⁸ The labour legislation, in particular, directly threatened private property rights, and this led to fears of an increasingly statist model. However, not all industrialists agreed with this aggressive stance.⁹ The exporters, represented in the export committee of the SNI, believed that the benefits of reducing the level of industrial dependence upon imported technology and

⁷ The SNI had advocated ISI policies in the late 1960s. See, for example, Ferner (1982:83).

⁸ The SNI was led in 1968 by Raymond Duharte, head of the small industry committee within the SNI.

⁹ The aggressive stance of the SNI also drew retaliation from the government. The leader of the SNI, Raymond Duharte, was not allowed to reenter Peru upon returning from a trip from abroad, thereby being forcibly exiled. The Velasco government also accused the SNI of having too many foreigners as members, and forbade it to use the word 'national' in its name. The National Society of Industry temporarily became known as the Society of Industry.

consumer goods outweighed the less desirable aspects of the model (Ferner 1982:175). More significantly, some of the export sectors were benefitting economically from policies designed to promote non-traditional exports. In particular, the CERTEX (Certificate of Tax Reimbursement for Exports) policy implemented in 1969, which gave tax incentives for value added exports, contributed to the continued support of the exporters. The conflicting views within the industrial sector towards the government was great enough for the committee of exporters within the SNI to break away in 1973 and establish their own representative body: ADEX, the Association of Exporters. Yet as the reforms progressed and the economy began a recessive decline, even the exporters began to develop a more conservative stance and began to develop a deep seated distrust of the government as a result of the tremendous expansion of the state in the economy.

Threatening to the industrial bourgeoisie as a whole was the growth of the public sector, which was beginning to displace the private sector as leading economic actor. The industrial bourgeoisie saw the trend of increasing state expenditure and public sector expansion - which predates the Velasco government - expand rapidly in the 1970s. The increasing importance of the public sector in this period is revealed by the growing share of public sector fixed investment as a percentage of total investment. In 1955, the share of public sector investment was at 21 percent, growing slightly to 27 percent in 1967. By 1975, however, the share of public sector investment had soared to 51 percent, surpassing the private sector as primary investor (Fitzgerald 1979:184). Industrialists suddenly felt that the future of capitalism and private enterprise was being threatened (Gilbert 1980, Ferner 1979).

This was an important turning point in the ideological development of the industrial bourgeoisie, and one which again coincided with international trends in economic thought. Conaghan, Malloy and Abugattas (1990) in studying the trend of neo-liberalism in Peru, Bolivia and Ecuador found that,

The antistatist discourse that took hold in virtually all of the major

business interest groups in these countries during the 1970s was pivotal to the intellectual and political genesis of neo-liberal policy coalitions. Although business distrust of the state was nothing new, antistatism acquired a new depth and emotional sway over the domestic bourgeoisie during the 1970s due to the pace of state expansion in all three countries (1990:6).

United by the fear of state expansion, the industrial bourgeoisie began to pressure the government for more liberal economic measures. In 1975, the Peruvian 'revolution' entered its second phase under the leadership of General Francisco Morales Bermudez, and began to back away from the more radical policies begun under the first phase.

It is widely agreed that the Velasco government failed in its objective stimulating the emergence of a dynamic industrial bourgeoisie. The effect of the Velasco government on patterns of ownership has been vigorously debated. The dominant interpretation, put forth by Fitzgerald (1976, 1979) and Gilbert (1980) point to the expansion of the state during this period as a sign of the weakness of the Peruvian industrial bourgeoisie.

Fitzgerald argues that the government's belief that eliminating the role of the oligarchy and reforming the nature and amount of foreign capital investment would allow the domestic industrial sector to flourish was incorrect by failing to recognise that much of the modern industrial sector was owned by the oligarchy and foreign capital. Thus, the extensive expropriations enacted had the result of weakening the large scale investor groups (Fitzgerald 1983: 76).

According to Fitzgerald, prior to the reforms in 1968, foreign capital controlled well over half of the top two hundred firms in the manufacturing sector (1979:115). He argues that in the short term, while the degree of foreign influence in the mining, fishing and manufacturing sectors declined, the domestic industrial sector did not step in dynamically to fill the resulting gap. Fitzgerald points to the declining percentage of GDP produced by foreign enterprises from 22 in 1968 to 11 in 1975. However, the percent of GDP produced by domestic capital also

declined, from 34 percent to 27 percent during the same period. In order to compensate for this declining investment, the public sector role in the economy grew considerably, from 11 percent in 1968 to 21 percent in 1975 (Fitzgerald 1979:122). Fitzgerald concludes that the weakness of the domestic industrial response meant that the state attempted to 'take over the role and function of domestic capitalists' (1976:94).

Gilbert coincides with this view arguing that the failure of the government's economic objectives were in part due to the timid economic response of domestic industrialists, despite the considerable economic opportunities which were created and the continued corporate profitability during the Velasco years. He argues that,

The incipient national industrial bourgeoisie did not prove willing to assume the historic role which the regime had reserved for it. The transformation of the social and economic system, which was intended, in part, to encourage this class, only frightened it. Private investment declined rapidly (1980:33).

Thus, Gilbert concludes that the Velasco government failed in its objective of creating a dynamic industrial bourgeoisie.

It is important to attempt to understand the reasons why the Velasco reforms failed to have the expected catalytic impact on domestic private investment. The Velasco government's policies overall were largely favourable to the industrial bourgeoisie. The government was firmly committed to a capitalist economic growth model with domestic industry expected to play an essential role. The Peruvian industrial bourgeoisie at this point at time, it must be stressed, was not adverse to an active state role in the economy. The SNI had long been advocating increased protectionism, greater control on foreign capital, and incentives for domestic industry. While the wider objectives of the reformist programmes were in accordance with industrialists' own goals, many of the specific policies of the programme, however, were threatening. The industrial community legislation in particular, led to growing investor fears, as the legislation entailed the gradual transfer of ownership to workers. The uncertainty

created by this type of reform cast doubts over the role of private enterprise and of the government's willingness to defend private property rights. Industrialists' perceptions of economic and political instability are important as they directly impact on investment decisions. But the growing wariness of industrialists, while certainly a significant factor in explaining investor behaviour is only a partial explanation. An important question to consider is the impact of the Velasco reforms on the degree of foreign control over the manufacturing sector.

It is important to distinguish the government's policy towards foreign capital in the extractive sectors of the economy from those of the manufacturing sector. The vast majority of the nationalisations undertaken by the Velasco government were in the primary sectors of the economy, while less restrictive policies were developed in regard to the manufacturing sector. The policies developed for the manufacturing sector were aimed primarily at increasing the degree of Peruvian ownership and joint ventures were actively promoted and encouraged. Foreign owned corporations were a required to increase the amount of Peruvian control to 51 percent within fifteen years (Guasti 1983). The military government recognised the important role foreign capital played in economic growth, particularly in the sectors with high value added which required foreign technology.

The role of the state in the manufacturing sector must also be distinguished from that of the primary sectors. While the state played an increasingly powerful role in the extractive industries by 1975, its direct role in the manufacturing sector remained limited. There were, however, some notable exceptions in which the public sector did form joint ventures with large foreign corporations. Large scale joint ventures were negotiated with Bayer, Massey-Ferguson and Volvo (Stallings 1983:115). However, overall manufacturing remained under the control of private investors.

Weeks (1985) offers an alternative interpretation to that of Fitzgerald, questioning the real impact of the state's growing role in the economy. Weeks

argues that the state expanded into a small number of sectors which were characterised by declining profitability, such as sugar refining, petroleum refining, and copper processing. Weeks demonstrates that percentage of gross output in the manufacturing sector controlled by foreign capital between 1968 and 1975 remained largely unchanged. Although the role of the state in manufacturing grew slightly, on balance it remained limited in the manufacturing sector, accounting for only 10 percent of output in 1975 if excluding petroleum and copper refining. This growth, however, was at the expense of the role of domestic capital which declined from 72 percent to 66 percent in the same period (see Table 2.4). Thus the government's policies achieved only minor changes in the relationship between foreign and domestic capital in the manufacturing sector. Weeks concludes that,

As a result of what was not done, the development of the productive forces and the development of capitalism in Peru remained the domain of foreign capital and Peruvian national capital was assured its traditional, secondary place in the process of accumulation (Weeks 1985:222).

The implication of Weeks' study is that the Velasco government's failure to reduce external dependency by stimulating local industry was not so much the result of the timidness of the domestic industrial bourgeoisie, but rather the lack of forceful and effective policies to reduce the role of foreign capital in manufacturing.

Table 2.4 Origin of Ownership of Manufacturing: Percentage of Gross Output (selected years)

	1968	1969	1973	1975
Foreign	25	25	25	24
State	3	7	8	10
Domestic capital	72	68	67	66

SOURCE: John Weeks. 1985. *Limits to Capitalist Development: The Industrialisation of Peru*. Westview Press, Boulder. p.209

1/ petroleum and copper refining have been excluded.

Yet, this view must be tempered by the changing nature of foreign investment. The changing modality of foreign investment is not insignificant. An

increasing number of investments in the 1970s were conducted as joint ventures with local capitalists or the Peruvian state, thereby increasing local benefits. Many industrialists in the medium and large scale manufacturing sectors were able to capitalise on the predominance of joint ventures as the new pattern of foreign investment. Many elite investor groups forged alliances with foreign capital, thus receiving access to finance, new technology and 'knowledge capital'.¹⁰

There is also evidence to suggest that an elite fraction of the domestic industrial bourgeoisie, with close ties to the oligarchy was able to consolidate its control over certain sectors of the economy. The tables in Appendix 1 examine ownership data of the leading fifteen companies of the top four manufacturing sectors; agro-industry, petro-chemicals, textiles, and capital goods; and the mining sector. Although the limited data available makes a comprehensive conclusion difficult, these tables can give some indication of the degree of foreign and domestic control over these sectors. Although ownership data was only available for the top fifteen firms in each sector, the high degree of concentration which exists in Peruvian industry means that these findings do have some significance. In 1983, the top ten firms in the textile sector held 44 percent of the total market share, while in mining the figure was approximately 77 percent. In agro-industry, the top ten companies captured 40 percent of their market share (Alcorta 1987:27). The overall results from these tables are summarised in Table 2.5.

While the overall balance of control has shifted toward domestic capital, with seventy-three of the top one hundred companies in 1987 under domestic control, this dominant market position appears to be restricted to certain sectors of the economy (The Peru Report 1988:25).¹¹ In the textile sector, for example, domestic capital accounts for 83.3 percent of the total gross income of the top fifteen companies, in sharp contrast to 12.2 percent for foreign capital (see Table

¹⁰ This will be discussed in depth in Chapter three.

¹¹ According to the same source, only fifteen of the top fifty companies as ranked by income were foreign owned in 1987 (The Peru Report 1988:25).

2.5).¹² A similar degree of control is found in the leading manufacturing sector, agro-industry, where domestic capital accounts for 79.9 percent of market share.

However, the balance of ownership between foreign and domestic capital is reversed in other manufacturing sectors. In the capital goods and petro-chemical sectors, there is a considerable degree of both state and foreign involvement. In the petro-chemical sector, foreign capital controls 69.3 percent of total income, while domestic capital accounts for only 15.2 percent. There appears to be a clear division of labour within the manufacturing sector, with foreign capital concentration in the capital goods and heavy industry sectors. The mining sector, as well, is subject to foreign capital and state control, with domestic industrialists accounting for only 10.4 percent of income of the top fifteen companies.

Table 2.5 Ownership in the Manufacturing and Mining Sectors 1986 (percentage of total gross income of top fifteen companies)¹

	State	Foreign	Domestic
agro-industry	-	20.0	79.9
petro-chemicals	-	69.3	15.2
textiles	-	12.2	83.3
capital goods	5.0	65.9	10.6
mining	70.4	19.2	10.4

SOURCE: Calculated from Appendix 1.

1/ Totals do not reach 100 percent as ownership data was not available for all companies. See Tables 1, 2, 3, 4, 5 in Appendix 1.

Collaboration between the local elite fraction of the bourgeoisie and foreign capital also exists. The economic groups, in particular, demonstrate clear links with foreign capital. Sogewiese Limited, owned by the Wiese family, has 35 percent of its shares controlled by foreign financial companies: the Societe Financiera y Valores Industrielles et de Valores de Banque S.A. (France) and the International Finance Corp (US) (Anaya 1990:104). The Wiese family also has invested in the BASF subsidiary in Peru. These links are common, and according

¹² In 1988, the agro-industrial sector accounted for 277,764,000 intis, the petro-chemical sector for 114,474,000 intis, the textile sector for 128,950,000 intis and the capital goods sector for 86,832,000 intis. The mining sector accounted for 346,314,000 intis (INE 1989:195).

to Anaya, the Bentin family is one of the only economic group without such links to transnational capital (1990:95). The Banco de Credito, in which four groups participate, has a considerable degree of foreign shareholding.¹³ The Banco de Credito also has investments abroad, including subsidiaries in the Bahamas and New York (Malpica 1989:79).

The relationship between foreign and domestic capital today is complex and difficult to summarise succinctly. This examination of the new structures of ownership, albeit a brief one, suggests that the domestic industrial sector is not necessarily subordinate to foreign capital. It appears that the continued foreign capital presence is based in the sectors of heavy industry, which require large scale investment and imported technology. This structure of ownership can therefore be interpreted as a rational division of labour, with each sector playing an essential role. The Velasco reforms created new opportunities which large scale domestic investors were able to seize.

The impact of the reforms on medium and small scale industry are less clear. Ferner (1982) in assessing the pattern of manufacturing growth in the post-1968 period concluded that it remained largely similar to that prior to the reforms. Consumer goods for the upper and middle classes remained the primary mainstay of the manufacturing sector. The import substitution strategy resulted in increased demand for consumer goods, both durable and light manufacturing goods, such as textiles and shoes. These sectors, which were the domain of the Peruvian industrial bourgeoisie, grew throughout the 1970s.

The import substitution policies did have an impact on patterns of local demand and encouraged a minor shift towards the domestic production of intermediate and capital goods. Policies were implemented which required the public sector to purchase a percentage of locally produced intermediate and capital goods. Intermediate goods sector grew considerably in the 1970s, up nearly 53

¹³ The Ueberseebank A.G holds 13.61 percent, and Banque Sudameris holds 4.86 percent. The Peru Report (1987:126).

percent between 1973 and 1980. The production of capital goods grew by nearly 30 percent between 1973 and 1975, partly in response to demand generated by the public sector only to decline sharply after 1975 (BCR 1981:85).

As a result of the gradually increasing demand, the period between 1970 and 1975 was marked by steady increases in gross fixed private investment, from 19 million intis in 1970 to 29.9 million intis in 1975.¹⁴ The growth of private investment therefore, remained solid during the periods when economic conditions remained stable, in spite of the political insecurity generated by legislation such as the Industrial Community. Private investment however declined precipitously in the period between 1976 and 1980 as the economy stagnated.

In sum, the objective of the Velasco government to stimulate the growth of the domestic industrial bourgeoisie can be said to have been only a partial success. The Velasco government succeeded in eliminating the landed oligarchy as the leading domestic economic force. Its policies with regard to foreign capital, however, were less effective. The type of investment changed and foreign investors became more closely allied with emerging Peruvian elite investor groups. Recent data illustrates that domestic capital has consolidated its hold over certain traditional sectors of the economy, such as the textiles and agro-processing sector. Foreign capital remains important in the intermediate and capital goods sectors.

Small and medium size industrialists did not fare as well as a result of the reforms. The deepening of foreign capital throughout the 1960s was the key historical moment which left the domestic industrialists in a subordinate position in many key sectors of the economy. This was the result not only of an absence of policies designed to protect the incipient domestic industrial sector, but the continued appropriation of surplus to the extractive and agricultural sectors. Domestic industrialists, at a competitive disadvantage vis-à-vis foreign capital remained based in the light consumer goods sectors. The domestic industrial

¹⁴ These figures are millions of intis at the 1970 rate (Coronado *et.al.* 1986:38).

bourgeoisie has also faced adverse economic conditions. In addition to restricted access to capital, Peru's limited internal market remains a chief constraint on the growth of the manufacturing sector. As the data in Table 2.3 illustrates, between 1960 and 1985 the percentage of GDP produced by the manufacturing sector has remained stable. Thus, the overall macro economic context may not have favoured the growth of this sector.

This argument is particularly important when examining the period between 1975 and 1985, which experienced two severe industrial recessions as a result of the application of orthodox stabilisation policies. This will be the subject of the following section.

2.3 Industrialists and Neo-Liberalism 1975-1985

The opposition to the Velasco government centred upon the growth of the state in the economy and threats to private property, and it was around this anti-statist stand that industrialists rallied. However, this new-found neo-liberal conviction was tested by both the Morales Bermudez government of 1975-1980, and the Belaunde government 1980-1985, as orthodox stabilisation policies implemented by both governments to attempt to control growing inflation and balance of payments difficulties had serious economic repercussions on the industrial sector. The latter attempt at orthodox stabilisation had a particularly severe impact on the industrial sector which was only beginning to recover from the earlier recession. This crisis, however, caused industrialists to reassess their strategies for political influence. Although initially intra-class conflict was accentuated, the adverse impact of this overt conflict on the status and effectiveness of existing industrial organisations provided the motivation for a renewed effort for the formal unification of these organisations.

Morales Bermudez assumed power in 1975 in a bloodless coup, and began to adopt more moderate policies than his predecessor. It rapidly became apparent, however, as balance of payments difficulties intensified and inflation began to gather force, that corrective economic measures were needed. After intense pressure was exerted initially by Peru's private creditor banks and later by the IMF, a strict monetarist stabilisation programme based on monetary and fiscal restraint was agreed. Measures to liberalise trade, and reduce the deficit were enacted, and in an attempt to improve the balance of payments, the exchange rate was floated, resulting in substantial devaluations of 56 percent in 1976 and 90 percent in 1977 (Daly 1983:63-63). This stabilisation programme did achieve some improvement in Peru's balance of payments by 1977, but the economy went into deep recession with internal demand and industrial output declining dramatically. These economic measures also failed to control inflation, which in this period continued to grow, from 38 percent in 1977 to 67.7 percent in 1979 (see Table 2.6).

The conciliatory attitude of the industrialists to the Morales Bermudez regime quickly dissolved. Industrialists began to oppose both the direction of economic policy and the continued dictatorial style of rule. As a means to mobilise and channel this mounting opposition, the private sector in 1977 established a peak association of existing industrial organisations, including the SNI and ADEX. Born of frustrated attempts to influence policy on an individual basis, The Union of Private Entrepreneurs of Peru (UEPP) presented a united front pressuring for democratic reforms and a softening of the liberalisation policies. Equally, the UEPP was a response to the growing labour unrest. In 1978, the CGTP labour confederation threatened a national strike and the UEPP assumed the primary responsibility for negotiating with both the state and labour, But the UEPP was racked by deep seated political conflicts, and was dissolved one year later. Nonetheless, it signalled an important shift in the political behaviour of industrialists. The economic crisis provided the motivation for the first serious attempt at collective action by capitalists from all sectors of the economy to influence policy.¹⁵ Lessons were drawn from the collapse of the UEPP which guided the development of the structure and formulation of policies of CONFIEP in 1984.¹⁶

The recession abated in 1979 owing to a sudden rise in market prices for many of Peru's commodity exports. The sharp upswing in the economy was accompanied by a transition to democratic rule in 1980 with the election of Fernando Belaunde of the Accion Popular party. Encouraged by the economic success of Pinochet's neo-conservative economic policy, and armed with a technocratic advisory team, the new government implemented a neo-liberal strategy based upon the reduction of state intervention in the economy. Belaunde's technocratic approach to economic management won it the support of most industrialists during the elections and in the early years of the new administration.

¹⁵ Two organisations which failed to join EUPP were CONACO, (Confederacion Nacional de Comerciantes) and the Association of Banks (Durand 1982: 161).

¹⁶ Interview, Julio Piccini (President of CONFIEP 1985), April 13, 1992, Lima. The reasons for the decline of the UEPP will be discussed later in this chapter.

The domestic bourgeoisie and international financial community supported these policies and the economy experienced a slow but steady growth rate between 1979 and 1982.

Table 2.6 Key Economic Indicators: 1977 - 1985
(percentage change)

	77	78	79	80	81	82	83	84
GDP	-0.3	-1.8	4.3	2.9	3.1	0.9	-12.0	4.7
inflation	38.0	57.8	67.7	59.2	75.4	64.5	111.1	110.2
investment	-22.4	-12.8	12.1	30.4	27.9	-4.5	-33.2	0.9
consumption	0.8	-6.7	-1.3	6.6	2.3	-0.3	-9.7	0.8

Source: Banco Central de Reservas. 1986. *Memorias*. p. 149.

Led by Finance Minister Manuel Ulloa, the process of economic liberalisation, begun under Morales Bermudez, was deepened. President Belaunde and his economic team developed an economic strategy based on the liberalisation of trade, privatisation of state owned enterprises, and monetary and fiscal restraint. Import controls, and incentives and subsidies for the private sector, were reduced in an attempt to make the domestic industrial sector more competitive. Direct foreign investment was actively sought, while tariffs were reduced in 1981 from 60 percent to 32 percent (Conaghan, Malloy and Abugattas 1990:16). Evidence of Belaunde's firm belief that state intervention was largely responsible for Peru's economic ills is found in his decision to sharply reduce in incentives for non-traditional exports, despite their contribution to the sectors' rapid growth from US\$353 million in 1978 to US\$810 million in 1979 (BCR 1986:167).

The upturn in the economy, however, was short-lived. This still fragile recovery was abruptly ended as commodity prices suddenly dropped in 1982. These economic difficulties were compounded by severe natural disasters, as the Pacific El Nino current brought floods in the north and droughts in the south. As GDP declined and inflation rose, Finance Minister Ulloa resigned in 1982. The Belaunde government then adopted an IMF-style austerity programme, which brought the industrial sector into an even deeper recession. Annual GDP

collapsed, from a solid 4.3 percent growth rate in 1979 to -12 percent in 1983, with inflation soaring from 67.7 percent to 111.1 percent in the same period (see Table 2.6). The real value of wages in the period 1973-83 declined by nearly 42 percent (Alarco and Falconi 1986:207). The elimination of subsidies on petrol and food sparked a dramatic rise in inflation, and triggered social unrest and national strikes, while tariff reductions led to a flood of imports devastating to local industry. The extent of the industrial crisis is evidenced most clearly by the decline in the volume of manufacturing, which in 1983 alone declined by 18 percent (see Table 2.7).¹⁷ Part of this precipitous decline, however, was due to a decline in fishmeal as a result of the El Nino Pacific current which had an adverse impact on fishing.

Table 2.7 Volume of Manufacturing Production 1979-1984
(1979=100)

	79	80	81	82	83	84
TOTAL	100	108.7	109.5	104.1	84.7	91.3
fishmeal	100	66.5	69.6	96.6	35.1	82.5
processed foods	100	107.0	106.8	105.1	94.2	98.7
textiles	100	103.5	102.6	106.8	90.5	96.1
wood, furniture	100	79.8	90.1	77.3	46.5	50.7
paper, printing	100	115.1	120.3	102.8	83.5	90.3
industrial chemicals	100	113.4	114.6	108.5	89.9	95.4
non-metallic minerals	100	121.2	115.6	109.2	90.0	78.1
basic metals	100	98.1	95.7	92.2	82.3	92.2
machinery, equipment	100	138.8	146.7	115.2	67.7	69.8

SOURCE: Instituto Nacional de Estadística, *Compendio Estadístico 1988*. 1989. p. 338.

As the data in Table 2.7 indicates, the recession was generalised, affecting all industrial sectors. This data provides evidence of the severity of the second stabilisation crisis, illustrating that manufacturing output in 1983 was 15.3 percent lower than in 1979. Recalling that in 1979 industry was only beginning to show signs of recovery from the 1977-78 recession, then this comparative decline is represents a significant reduction in productivity. This had obvious repercussions on the level of private investment in this period. In 1983 gross fixed private

¹⁷ A structuralist critique of orthodox stabilisation will be offered in Chapter four.

investment declined by a massive 31.5 percent, followed by a further fall of 7 percent in 1984 (Coronado et al 1986:38).

The combination of the international economic factors and climatic changes in a context of an on-going process of economic liberalisation was devastating. The industrial sector faced a multitude of threats. The textile sector, for example, affected not only by a shortage of cotton as a result of the climatic changes, and a sharp contraction of consumer demand, but also by increased competition from imports.¹⁸ The output of the textile sector in 1983 alone declined by over 15 percent. Other sectors experienced similar declines. The volume of basic metallic products and machinery dropped by over 50 percent in 1983, in part as a result of declining public sector demand, while the wood and furniture sector stagnated as a consequence of the low purchasing power of the population (see Table 2.7). Non-manufacturing sectors also fared poorly. The climatic changes took their toll on fishing whose contribution to GDP dropped by 40 percent, and agriculture which fell by 7.9 percent in 1983. The stagnation of internal demand and the cut back of public expenditure caused a 21.2 percent fall in the construction industry (Coronado et al 1986:35).

During this crisis, the bourgeoisie responded not by attempting to unite, but succumbed to internal strife and sectoral conflicts. The response of industrialists to the economic crisis reveals the real potential for intra-class conflict and rivalry both within the industrial bourgeoisie and between fractions of the bourgeoisie. The response of capitalists to the industrial crisis illustrates that there are many potential fault lines within the bourgeoisie which can emerge in times of economic hardship.

It is not possible to delineate clear class fractions, as intra-class divisions and coalitions are fluid, in response to the particular form of economic or political threat which emerges. There are, however, some basic distinctions that can be

¹⁸ See, *The Andean Report*, August 1985. p. 124.

made. Small and medium scale industry remains based largely in the light consumer goods sector of the economy. Small scale industrialists producing for the internal market are generally antagonistic towards foreign capital and are largely predisposed to support protectionist policies. Although these industrialists are generally more favourable to interventionist economic models, they also remain highly sensitive to specific policies such as labour legislation and artificially high wages. Small and medium industrialists are active in the SNI whose political pronouncements often reflect the interests and views of this group.¹⁹

A second group of medium and large industrialists geared primarily towards the export market are based in ADEX. These more modern capitalists are less inclined to support interventionist policies, although incentives for non-traditional exports have been important in the development of this sector. Conflicts and policy disagreements between the traditional industrialists in the SNI and the exporters in ADEX to continue to resurface periodically. The export sector of the economy was better able to withstand the economic crisis induced by the neo-liberal policies of Belaunde, and was at a definite disadvantage as a result of the controlled exchange rate policies of the Garcia government. The economic differences between the two groups often manifest themselves in political disagreements.

A third group, which will be examined in some depth in the following chapter, are the large scale investor groups, known as economic groups, which have interests in many sectors of the economy, including the financial system. The ready access to credit which these groups maintain, and their collaborative relationship with foreign capital have enabled them to accumulate, even in periods of economic recession. These modern outward looking groups, allied with other domestic large scale industrial groups, participate only indirectly in private sector organisations, relying instead upon personal contacts with government officials.

¹⁹ Interview, Francisco Martinotti (President of the Committee of Small Industry, SNI), April 14, 1992, Lima.

These economic groups, it will be argued, form the elite fraction of the bourgeoisie by virtue of the extensive holdings they have in all sectors of the economy, and the strong social links between these groups.

The nature and basis of intra-class conflict and the potential for intra-class alliances depended on a variety of factors, in particular the differential impact of economic policy and trends on industrial sectors and firms. Intra-class alliances are not static and unchanging. It is useful to briefly discuss how some of these conflicts of economic interests were manifested during the Belaunde government.

The impact of the recession was felt in varying degrees in different sectors of the economy, and many industrialists became frustrated by the sluggish behaviour of the SNI, which attempted to engage the government in dialogue with the government without much success. As a result, some sectoral committees within the SNI decided to bypass the SNI leadership and negotiate directly with the government. The committees representing the sectors which fared worst in the recession, such as the textile, clothing and metal-mechanic sectors began to approach the government on individual basis.²⁰ In addition, many of the economic groups, which were not active members in the SNI, used their prestigious positions to dialogue directly with Belaunde's economic team.

The actions of the sectoral committees within the SNI illustrate that sectoral interests are generally those around which industrialists coalesce more readily. In this case, the protection of sectoral interests within the manufacturing sector was of such immediate importance that unity which could have resulted in more effective political pressure to defend wider class interests was sacrificed. However, while these sectoral interests can lead to divisive behaviour, this level of dissent does not usually represent fundamental conflicts over macro-economic policy. Rather sectoral demands are generally concerned with gaining incentives for a particular sector, or to express disagreement over a particular tariff or tax which

²⁰ See, for example, Francisco Durand, 'Sociedad Nacional de Industrias en Quiebra?', *Actualidad Economica*, May 1983.

will benefit one sector over the other. In contrast, market orientation is one marker of differentiation of economic interests from which profound disagreements emerge on the broader issues of economic policy orientation.

This was the case under both the Morales Bermudez and Belaunde governments in which the devaluation of the sol became a particularly divisive issue. Devaluations, which are a central component of orthodox stabilisation, have been interpreted as 'a political instrument' because it transfers income and surplus away from the local industrialists to the exporters (Daly 1983:113).²¹ The differential impact of devaluations, therefore, suggests that the potential for conflict within the bourgeoisie on this issue is high, and can persist beyond the immediate and short-term differences in policy.

Not surprisingly, by 1982 the SNI and the exporters in ADEX were once again at odds with each other. Certainly, throughout this period, the issue of exchange rate devaluations heightened tensions within the bourgeoisie, and brought to the surface conflicting interests which are dormant during periods of economic growth and stability. It is evident that during the late 1970s, and early 1980s, this intra-class conflict served to limit the levels of cohesion necessary for effective political influence. The exporters adopted a more conciliatory stance vis-à-vis the government and the neo-liberal policies, in part because the devaluations which were a standard feature of the IMF-style stabilisation programme being implemented, gave them a sharp boost in profits. The exporters were less affected by the crisis and the value of exports in 1983 at the peak of the crisis, was still more than double than in 1976 when the gradual shift in economic policy toward neo-liberalism began. In 1976, exports totalled US\$1,341 million, increasing to US\$3,015 million by 1983 (BCR 1985:139). The impact of these policies, however, was quite different for industrialists producing for the internal market. As the market became flooded with imported consumer goods in the early 1980s, industrialists and businessmen began to realise that the very policies they had

²¹ In this passage, Daly is referring specifically to the devaluations in 1975-78 by the Morales Bermudez government.

advocated were detrimental to their economic survival.

Some firms in the textile sector were able to take advantage of CERTEX incentives and the increased competitiveness from the sol's devaluation, by expanding the volume of exports. Textile exports soared from US\$59 million in 1977 to US\$247 million in 1979 (BCR 1986:167). It is generally the large firms which are more able to take advantage of export opportunities. Brescia's La Union, for example, increased its share of exports from 12 percent to 42 percent in 1983 (Scott 1986:136).

Despite the severity of the recession, as the textile sector demonstrates, there are a variety of defence mechanisms that enabled most enterprises to survive. Webb (1987) examined the impact of the economic crisis of the financial situation of productive enterprises and found that net profits in the manufacturing sector remained positive. Although overall profitability fell by 75 percent between 1981 and 1983, by 1985 they had recovered nearly to their 1981 levels (1987:67). Webb further found that lower wages, a declining tax burden and negative interest rates enabled the manufacturing sector to partially offset rising production costs. In addition, the high profitability of dollar deposits in this period provided an alternative source of financial income. Foreign exchange holdings became the safest investment with high short term profitability, and were made at the expense of local reinvestment. Thus, Webb concludes, industrialists survived in part by transferring some of the financial adjustment to the state, through lower taxes, and to labour, through lower wages.

The large scale corporate conglomerates, often referred to as economic groups, had their own defence mechanisms in addition to the ones listed above. The groups which were characterised by a high degree of vertical integration of their enterprises were able to use this integration to capture the total value added, and in some cases, to allow one less profitable enterprise to subsidise others in the same group. One outcome of the repeated economic crisis in this period was a

greater degree of economic concentration.²² Smaller enterprises in some manufacturing sectors were only able to survive by returning to the informal sector (Scott 1986:136).

As the recession deepened, industrialists began to coincide in their opposition to the Belaunde government and to the neo-liberal policies being implemented. In 1984, for example, at the Annual Conference of Executives (CADE), a yearly forum for the exchange of views between government representatives and the private sector, the SNI in conjunction with the Peruvian Institute of Business Administration (IPAE), proposed a reassessment of the neo-liberal policies being implemented. They suggested 'corrective measures to make the opening of the economy more flexible' by implementing,

measures for the recuperation of the internal market, such as tariff readjustments and/or the imposition of selective and transitory licences for the import of certain products (IPAE 1984a:163).

Even the exporters coincided with the attempts to slow the liberalisation process, and demanded the reinstatement of CERTEX to its full level (IPAE 1984a). These protests met with some success. In 1984, after intense pressure from industry, the Belaunde government began to backtrack, reinstating CERTEX tax incentives to their 1979 levels and raising tariffs (Pastor and Wise 1992:89).

The political coalitions and economic outcomes of the Belaunde period can be said to have been both unexpected and contradictory. At the time of the elections in 1980, the future appeared promising for industry: the economy was showing strong signs of recovery, and the election of the centre-right Accion Popular party signalled a return to an economic model firmly based on the promotion of private enterprise. Although this apparently heralded a new era of collaborative state-private sector relations, with the exception of a brief honeymoon period in 1980-81, the state-private sector relationship was strained and often confrontational. Despite Belaunde's pro-business economic philosophy, industrialists found that the government failed to be responsive to their demands.

²² This assertion is born out by data on concentration found in Alcorta (1987). See page 99.

Industrialists found the Belaunde government dogmatic and impermeable to their efforts to initiate dialogue (Thorp 1991:197). The technocratic and closed policy making style meant that most business lobby efforts were ineffective (Conaghan, Malloy and Abugattas 1990). The government responded to industrialists' demands in 1984 only after the industrial sector had reached a profound state of crisis.

For industrialists then, the experience of economic crisis was compounded by a sense of political powerlessness. The existing strategy of individual lobbying by industrial organisations failed to achieve the desired results. The divisive impact of the crisis on the unity within these organisations provided the impetus for a critical assessment of the effectiveness of these organisations, and led to the formation of CONFIEP in 1984. This will be the subject of the following chapter.

This experience also shook the industrial bourgeoisie's confidence in the market, enough so for most industrialists to turn to the reformist Apra party as a potential ally. By 1985, the industrial bourgeoisie had come full circle, once again advocating inward-looking industrialisation strategies.

2.4 Conclusions

This late industrialisation of the Peruvian economy has made the emergence of the industrial bourgeoisie a late and slow phenomenon. This chapter has examined the factors which inhibited the development of strong local industrial bourgeoisie. As with many other Latin American countries, foreign capital played an important role early in the process of industrialisation. In Peru, at a critical moment at which the growth of the manufacturing began to gain impetus, the government developed policies specifically designed to encourage foreign capital investment. The incipient industrial bourgeoisie which was beginning to emerge at that time was faced with the influx of highly competitive foreign capital.

Unlike many other Latin American countries, import substitution industrialisation policies were not implemented until the late 1960s. The Peruvian state remained allied with the traditional agrarian oligarchy and firmly committed to export led growth. Despite this, this chapter has pointed to evidence to suggest that a local industrial group largely unrelated to the landed oligarchy did play an important role in the development of the manufacturing sector. Agrarian and export interests, with the exception of mining, lost ground after the Velasco government's reforms. However, it is important to note the while the growth of the secondary and tertiary sectors of the economy were stimulated by the Velasco reforms, the ascendancy of the role of manufacturing in the economy predates the Velasco government. The proportion of GDP produced by manufacturing had been gradually increasing, while agriculture had long been in decline when the military government took over.

This chapter has argued that despite the important role of foreign capital in the Peruvian industrial sector, domestic capital remains important in the process of accumulation. In 1975, domestic capital accounted for 66 percent of gross output in the manufacturing sector, compared to 10 percent from the state and 24 percent for foreign capital (see Table 2.4). As has been argued by Ferner (1982), the role of local, independent capital in the process of industrialisation has often been

underestimated. As this chapter has pointed out, in 1987, seventy three of the top one hundred companies were under domestic control (The Peru Report 1988:25).

Many of the local corporate groups which flourished in the post-Velasco conditions, did so by forming alliances with foreign capital. As the following chapter will demonstrate, large scale industrialists were able to form collaborative relationships with foreign capital. This consensus between local and foreign capital has enabled both these groups to continue accumulating. The economic crises of the late 1970s and early 1980s, as the following chapter will illustrate, served to reinforce the role of the leading investor groups. Certainly, the local fraction of the bourgeoisie allied to foreign capital has benefitted from this alliance. The same can not necessarily be said for the small and medium sectors.

Small scale local capital remains based in the traditional sectors of light industry. The industrial bourgeoisie has faced not only competition from more efficient foreign capital (Weeks 1985), but also extremely adverse conditions. Restricted access to capital has been a long-standing preoccupation of this group. More importantly, however, has been the lack of a stable and consistent period of economic growth and the creation of an internal market which remains a prerequisite for increased domestic industrial production.

The nature of the relationship between industrialists and state in the period covered by this chapter underwent significant changes. The long-standing alliance which existed between the state, landed oligarchy and foreign capital was definitively ruptured by the Velasco government. The landed oligarchy was displaced as the leading domestic economic actor and the Peruvian state became committed to the promotion of capitalist economic growth. The question which this turn of events poses is the degree to which the Velasco government can be said to reflect the class domination of the state by the industrial bourgeoisie as argued by Weeks (1985).

It is clear that the Velasco government was not acting exclusively on the

behalf of the industrial bourgeoisie. By 1968, as dissatisfaction with the indecisiveness of the Belaunde government grew, there were widespread pressures for modernisation, industrialisation and a reduction of the power and influence of both foreign capital and the oligarchy. Stepan (1978) and Trimberger (1978) furthermore, argued that the growing professionalism of the military increased its awareness of existing social and economic conditions and enabled the leadership of the Peruvian military to formulate its own objectives. The Velasco government can be said to have been responding to wider societal pressures while developing its capacity to formulate its own development agenda.

While the alliance between the state and oligarchy was broken, the new alliance between the state and industrial bourgeoisie was far more tenuous. The industrial bourgeoisie's ability to influence the state and exact policies which promoted their interests remained fragile. The Velasco government's policies were often at odds with the demands and interests of industrialists, and the relationship between industrialists and the state in the period between 1968-1985 remained strained and often confrontational.

The Peruvian state, as of 1968, did become and has remained firmly committed to capitalism. Despite the minor political differences which emerged, the Velasco government did act in the interests of the industrial bourgeoisie as a whole. However, the industrial bourgeoisie's control over the state was far from complete. Weeks' assertion that in 1968 the 'Peruvian bourgeoisie had fulfilled its historical role' was premature (1985:88). Throughout the 1980s and into the 1990s, the Peruvian industrial bourgeoisie developed a variety of strategies to consolidate its economic position and strengthen its relationship with the state. The remainder of this thesis will consider some elements of this process.

CHAPTER THREE

THE ECONOMIC AND POLITICAL ORGANISATION OF THE INDUSTRIAL BOURGEOISIE

Introduction

After the economic crisis induced by the orthodox economic policies of the Belaunde administration, the APRA party proposed a new strategy of economic development which combined state control over many economic policy instruments with an emphasis on the promotion of private investment. As later chapters illustrate, the *concertación* policy of dialogue with investors which the government pursued was two tiered. At one level, Garcia was concerned with discussing wide economic policy issues with a large number of industrialists. As the second level, the government was concerned with negotiating specific large scale investment projects with elite investor groups.

The primary objectives of the first level of *concertación* were to increase the transparency of the government's economic and political goals and objectives; and to establish a channel for two way dialogue and communication. The emergence of CONFIEP in 1984 unifying existing industrial organisations, made it the most suitable partner for such negotiations. CONFIEP incorporated a large number of capitalists in all sectors of the economy, and the Garcia government sought to forge a relationship with this representative body in order to establish and maintain business confidence.

At the second, more in-depth level of negotiation, the Garcia government developed on-going contact through a regular series of meetings with a select number of top corporate groups. These elite investors, known as 'economic groups' in Peru and elsewhere in Latin America, were actively courted by the government because of their immense economic holdings in various sectors of the economy and their ability to develop large scale investment projects almost immediately.

While the previous chapter examined in broad strokes the growing role of industry in the Peruvian economy, this chapter will focus in more detail on the two groups which Garcia chose to engage in dialogue with in 1985. These two structures, albeit one purely economically defined and one politically defined, both played important roles in shaping the political and economic events of the 1985-1990 period.

3.1 From Agrarian Oligarchs to Urban Industrialists

This section will examine the development of elite corporate groups, known as economic groups in Peru. These industrial groups with interests in the financial system, were granted a privileged position in the *concertación* dialogue with the government. An understanding of the ownership structure of these groups is particularly important in light of the Garcia government's efforts to court these groups in 1985, and to expropriate them in 1987. While it was the economic power of these groups which initially gave them a privileged role in negotiations with economic policy makers, this degree of economic strength also was a point of concern for the government, which later sought to weaken them by expropriating the financial system in 1987.

A further characteristic of the economic groups which merits further discussion is their oligarchic origins. A list of the fifty-three most prestigious oligarchic families, as developed by Gilbert (1982) and presented in Table 3.2, can be compared with a list of current industrial conglomerates in Table 3.1.¹ This comparison reveals that many of these top industrial families were once a part of the oligarchy. In fact, of the top ten industrial groups, only two, the Leigh and Arias families, were not once part of the traditional oligarchy.

The significance of this finding requires further elaboration. It appears contradictory in that on the eve of the Velasco government, the oligarchy's role in industry was shown to be minimal and characterised primarily by minority shareholding, while by the 1980s, oligarchic families head the list of the most prominent industrial empires. It is evident that not only did a sector of the oligarchy make a successful transition from agro-exporting interests to the urban

¹ Brief mention should be made regarding Gilbert's methodology. A panel of seven Peruvian 'judges' were asked to list families which they felt were formed part of the oligarchy. No definition of the term oligarchy was given. Gilbert eliminated three families from the list which were primarily industrial. The families which remain are agrarian families, as can be confirmed by lists of top landowners found in Stephens (1971), Malpica (1964) and Valderamma and Ludmann (1979).

commercial and manufacturing sectors, but that these groups are now the elite fraction of the bourgeoisie by virtue of the sheer magnitude of their holdings in all sectors of the economy.

The aim of this section is therefore to examine the evolution of these elite corporate groups and examine this transition from agrarian and export oriented interests to the urban economic sphere. It will, in particular, attempt to identify the traits and characteristics of these families which enabled them to withstand to the Velasco reforms and adapt to the changing political and economic conditions of post-oligarchic Peru. In order to understand the patterns and process of capital accumulation and industrial growth in this period, it is important to discern the factors, if any, which contributed to their apparent edge over existing independent industrial capital.

In comparing the list of oligarchic families in Table 3.2, with current industrial families in Table 3.1, a few clues can be found. First, the families which received between five to seven votes in Gilbert's study, indicating strong agreement on their oligarchic status prior to 1968, are conspicuously absent from the list of industrial conglomerates. None of these elite oligarchs, which include families such as Pardo, Prado, Gildemeister, Aspillaga and Miro Quesada, are among the list of top industrial groups of the 1980s. The elite stratum of the oligarchy, characterised by a central interest in the agricultural sector, a highly respected position in the social order and a considerable degree of political influence, appear not to have become as successful in the urban economic sphere as other less prominent members of the oligarchy.

Table 3.1 Top Industrial Conglomerates: 1988 ¹

GROUP ²	PRIMARY INTEREST	INCOME MNS US\$
1) Romero	textiles	167.3
2) Brescia	textiles	119.7
3) Nicolini	agro-industry	84.0
4) Bentin	beer	83.5
5) Benavides	mining	71.6
6) Arias	mining	68.4
7) Wiese	shipping	58.5
8) Lanatta-Piaggio	beer	58.3
9) Rizo-Patron	cement	55.8
10) Leigh	shipping	46.7
11) Ikeda	agro-industry	46.3
12) Rodriguez Banda	milk	46.2
13) Efco	pharmaceutical	44.9
14) Hochschild	mining	44.5
15) Monterrey	commerce	44.0
16) Montero	agro-industry	38.0
17) Zanatti	transport	37.2
18) Custer	commerce	36.4
19) Banchero-Agois	shipping	32.8
20) Galsky	fishing	31.2

SOURCE: *The Andean Report*, 'Groups 250', April 1990.

1/ Conglomerates ranked in order of total income of all related group companies, with the exception of financial sector holdings. State and foreign owned groups have been omitted.

2/ Names in bold are also found in Table 3.2

Table 3.2 Elite Oligarchic Families¹ (By Distribution of Votes)²

7 - Pardo, Piedra, Gildemeister
6 - Beltran, Prado
5 - Aspillaga, Ayulo, Miro Quesada
4 - Fernandini, Wiese , Picasso
3 - Banchero , Brescia , Carrillo, Olaechea, Mujica, Larco
2 - Barreda, Benavides , Bentin , Berckemeyer, Chopitea, D'onofrio, Ferrand, Grana, Lavallo, Malaga, Orbegoso, Ramos, Rizo-Patron
1 - Alba, Alvarez-Calderon, Bellido, Boza, Cilloniz, Durand, Ferreyros, Gallo, Ganoza, Isola, Izaga, Lanatta , Madueno, Martinto, Moreyra, Nicolini , Osma, Raffo, Reisner, Riva-Aguero, Romero , Thorndike, Ugarteche

SOURCE: Dennis L. Gilbert. 1982. *La Oligarquia Peruana: Historia de Tres Familias*. Lima: Editorial Horizonte. p. 223.

1/ Names in bold are also found in Table 3.1

2/ A panel of Peruvian judges was used to identify the top oligarchic families prior to the Velasco reforms. An increased number of votes (from one to seven) suggests more prestigious families.

There are various factors which may be used to explain this inability to adapt and grow in the post 'old regime' period. At a most basic level, it can be suggested that the prestigious social position of the elite stratum of the oligarchy made more impressive and easily defined targets for the Velasco government's expropriations. It is possible that in order to obtain the degree of autonomy necessary to make fundamental structural changes in the social order, the Velasco government acted with particular force against the elite, and most political fraction of the oligarchy.

Second, although some of these oligarchic families had diversified into the urban economy, they continued to place primary importance upon their agrarian base. It could be suggested that the social standing gained from landowning may be an important although unquantifiable reason for the oligarchy's inability to adequately develop their urban interests after the agrarian reform. For these elite families, the urban interests, while profitable, were considered secondary and less prestigious than landowning. It appears that the agricultural interests tended to dominate the families' financial strategy. They were unwilling to relinquish the defence of these dominant interests during the military regime, making it more difficult for them to develop their manufacturing interests later.²

This behaviour can be contrasted with the fraction of the oligarchy which not only survived the Velasco reforms, but thrived in the new economic conditions. In tracing the history of some of these families, such as the Romero, Brescia, Nicolini, Bentin and Wiese families, a number of striking characteristics in common becomes evident (see Table 3.3). First, these families were less dependent upon their land derived income for their well being. The Romero family, which by the 1980s owned the most powerful industrial conglomerate in Peru, diversified its interests early in the century from cotton growing to cotton

² See, for example, Stephens (1971), and Bourricaud (1970) on the extreme importance of land to the oligarchy. Land was the source not only of economic power but of social prestige.

processing, later expanding into the textile, oils and capital goods sectors.³ This transition was facilitated by the expansion into sectors which were closely integrated to the existing cotton interests. One important consequence of this early diversification is that an increasing proportion of the Romero family's income was derived from non-agricultural production. By the late 1960s, it has been estimated that only 50.25 percent of the Romero group's capital was tied to its original agrarian interests, with 33.94 percent in the industrial sector, primarily in beer and textile companies. A further 6.15 percent was based in the commercial sector, 1.72 percent in urban real estate and 7.94 percent in the financial system (Reano and Vasquez 1988:89).

Similar patterns of diversification are found in the Brescia, Nicolini and Bentin families which gradually depended less upon their landowning for their income. The Brescia family expanded rapidly into urban real estate, the Nicolini family into mills and food processing, and the Bentin family into mining and beer (Anaya 1990: *passim*). This confirms the suggestion by Ferner (1982) and Bourricaud (1970) that the oligarchy was undergoing a process of differentiation prior to the advent of the reformist government, with the existence of a fraction which was increasingly tied to the urban economy. Bourricaud suggested in the 1960s that,

The up-country gamonal is a very different person from the coastal estate owner, who puts his money to work in land or financial speculations. The traditional oligarchy, whose wealth comes from sugar, cotton, or the sale of metals in N.Y., London or Hamburg regards with suspicion the newly rich with their hazardous plans for rapid industrialization (Bourricaud 1970:344).

Secondly, this fraction of the oligarchy was not only able to withstand the reforms and emerge relatively unscathed economically, but they were well poised to take advantage of the new economic opportunities which arose. This sector of the oligarchy, with well developed urban and financial interests, were more

³ See Reano and Vasquez (1988) for a detailed economic history of the Romero family and its investment diversification from the beginning of the century to the 1980s.

flexible in their economic planning and investment strategies, unlike the more traditional oligarchy or its non-oligarchic counterparts in the industrial sector. In this period of investor uncertainty, with foreign capital in partial retreat and national industrial investment in decline due to a lack of confidence in the military government, these families demonstrated a willingness and ability to take advantage of investment opportunities. As many powerful foreign companies in the manufacturing, mining and financial sectors began to withdraw, these entrepreneurs moved in to fill the resulting economic vacuum. This rapid response to the reforms, cementing their control in the banking, financial and manufacturing sectors, contributed to their dominant economic position by the 1980s.

The Brescia and Romero families provide clear examples of this behaviour. The Romero family, unlike other large landowners in Piura, acquiesced in the face of the agrarian reform. While other families were fighting the expropriations in court, the Romero family gave up their lands and used government incentives which allowed them to convert agrarian bonds into industrial investment, and established two very profitable textile companies. The Romero group also purchased the American owned Anderson Clayton and Company in the oils sector, when it withdrew from Peru in the 1970s, thereby consolidating its position as leader in that sector (Reano and Vasquez 1988:107). Similarly, the Brescia family bought Duncan Fox's shares in Textile Union cementing its influence in the textile sector, in addition to buying up Grace and Company stocks in three mid-size mining companies (Malpica 1989:137). More significantly, these groups quickly mopped up foreign capital shares in the financial system when the restrictions placed a 20 percent ceiling on foreign capital shareholding in national banks. This measure allowed both the Romero and Brescia families, among others, to consolidate their hold over the Banco de Credito.⁴

The third, and possibly most important feature of these families which has

⁴ For a detailed economic history of these industrial families, see Anaya (1990) and Malpica (1989).

enabled them to develop powerful industrial empires, was an early participation in the financial system. Their involvement in the financial system enabled these financial-industrial conglomerates to use this ready access to credit to finance their industrial expansion. It is possible that this was done to the detriment of non-financial industrial capital. The families in the Banco de Credito, in particular, were able to use these resources to provide loans to their related companies, as evidenced by the large number of self-assigned loans. In 1979, for example, the Banco de Credito issued 4.75 percent of its total loans to the Romero group alone, and a significant proportion to other families represented on the board (Reano and Vasquez 1986:124). As Bourricaud remarked,

The banker is above all an arbiter: he chooses among the possible uses of a given supply of capital and plays the part of a sort of judge vis-à-vis potential investors . . . What characterizes business in Peru is that the saver, banker and investor are one and the same person (Bourricaud 1970:45).

Little has changed since the pre-reform era when Bourricaud made this observation. It is no coincidence that of the top ten industrial conglomerates listed in Table 3.1, only three are not also bankers. The Romero, Brescia, Nicolini, Bentin, Benavides, Wiese and Lanatta families all have some participation in the financial system.

In conclusion, it can be stated that there existed a fraction of the oligarchy which was already diversifying into the urban economy and which was not only able to withstand the Velasco reforms but also to continue this process of economic diversification and expansion. The deft and aggressive response of these families to the new economic conditions enabled them to increase their control over the financial system and increase their interests in the manufacturing sector. Other industrialists appear to have been more hesitant in their economic behaviour. They also had the definite disadvantage of not having control over credit to finance their economic expansion.

These economic groups have consolidated their economic position and now

control much of the private financial system and the leading industrial conglomerates. The following section will examine these groups in more detail and the new structure of capitalist ownership from which their power is derived.

Table 3.3 Top Economic Groups in Peru: 1988

Group	Original interests ¹	Primary interests ²	Banks ³	Dir ⁴
Bentin	mining	beer, glass, plastics	4	13
Berckemeyer	commerce	commerce, milk, mining	3	13
Brescia	agriculture	mining, real estate, textiles, beer	4	8
Ferreyros	industry commerce	commerce, agro-industry, capital goods	4	5
Lanatta	commerce petroleum	beer, plastics	2	11
Nicolini	mills	textiles, agro-industry	4	5
Olaechea	agriculture	construction, beer	2	10
Picasso	agriculture	mining, drinks, radio	2	7
Raffo	textiles	real estate, textiles	4	10
Romero	cotton	textiles, oils, commerce	7	8
Wiese	commerce mining	capital goods, mining, shipping	2	3

SOURCES:

- 1/ Dennis L. Gilbert. 1982. *La Oligarquía Peruana: Historia de Tres Familias*. Lima: Editorial Horizonte; and Eduardo Anaya. 1990. *Los Grupos de Poder Económico: Un Análisis de la Oligarquía Financiera*. Lima: Editorial Horizonte.
- 2/ primary economic interests drawn from the *Directorio Empresarial*, published by the National Confederation of Chambers of Commerce, CONACO, 1984; and The Peru Report, *The Top 1500 Companies*, 1988.
- 3/ number of banks, financial institutions and insurance companies in which at least one group member is on the board of directors, CONACO, *Directorio Empresarial* 1984.
- 4/ number of industrial companies in which at least one group member is a director, CONACO, *Directorio Empresarial*, 1984.

3.1.a The Economic Groups: The Elite Fraction of the Bourgeoisie

New patterns of ownership and economic control developed after the collapse of the traditional oligarchy. This economic group structure is a prevailing pattern of large scale ownership in Peru. These economic groups, whose principal characteristic is the fusion of industrial and financial capital are now the most economically powerful fraction of the bourgeoisie, due not only to the extent of their material holdings, but also for their control over two key sectors of the economy: the manufacturing sector and the financial system.

The fusion of industrial and financial capital, also referred to as finance capital, was first recognised in 1927 by Hilferding (1981). These economic groups, as they are known in Latin America, are a common pattern of capitalist ownership in the less developed countries, found in parts of Africa, Asia and Latin America. In the Latin American context, there has been an growing interest in this elite sector of the business community, with aspects of group dynamics studied in Nicaragua (Strachan 1979), Mexico (Aubey 1979), and Chile (Sanfuentes 1984) among others. However, the application of this concept to the Peruvian case has been more recent in origin. Although tentative efforts to examine 'industrial constellations' were made by Epinoza and Osorio (1972), it was not until the 1987 attempt to expropriate the financial system that more serious efforts were made to identify and analyze this new pattern of capitalist ownership (Anaya 1990, Malpica 1989).

Definition of what constitutes an economic group varies from author to author, but there is agreement on their general characteristics. A brief review of the literature can give a clearer picture of the structural composition and organisational functions of the group structure, which can be confirmed to exist in the Peruvian groups to be discussed below.

An economic group is essentially a conglomerate of enterprises in various sectors of the economy, which are owned and controlled by an extended family

unit through complex interlocking of stockholding and directorships. What distinguishes the group structure from other industrial conglomerates is that each group has a financial institution at its apex. The important feature of this multi-enterprise organisation is that it has one central decision making centre and an overall investment strategy emanating from that centre. The ability of the group to perform capital market functions and influence the allocation of credit has been a central focal point of analysis.⁵

The economic structure of a group is characterised both by a large degree of diversification in various sectors of the economy as well as vertical and horizontal integration between its companies. A single economic group often has enterprises in areas as varied as mining, real estate, textiles, glass and commerce. These same groups also tend to have a high degree of integration between their enterprises. The Bentin group provides an example of a highly integrated group. Its primary interests lie in the lucrative beer industry, and the Bentin group is comprised of companies which produce beer, beer bottles and plastic beer crates, as well as enterprises for transport and distribution (Anaya 1990:95).

The relationship between the enterprises within an economic group is forged through a web of interconnected directorships and shareholding. It is not uncommon for a prominent group member to be on the board of directors of various companies. Similarly, an economic group can have several family members on the board of directors of a single company, in an attempt to consolidate its control over that company. The Lanatta-Piaggio group, for example, has ten family members on the board of directors of the *Compania Nacional de Cerveza*, four on the board of *Molitalia*, and two on the board of the *Compania Minera Colquirrumi*, among others.⁶ The relationship between members of a group, it should be reiterated, transcends simple business

⁵ See, for example, Leff (1976, 1978) for a discussion of the ability of economic groups perform capital market functions.

⁶ Information on directorships for this chapter was taken from 'Directorio Empresarial', compiled and published by the National Confederation of Commerce. See CONACO (1984).

partnerships. They are bound by extended family ties which propagate an atmosphere of deep loyalty.

The nature of the relationship with the financial sector requires some clarification. Alcorta (1987) argues that a group need not own 51 percent of shares to have effective influence or control over a financial institution, and he therefore sets an operational definition of 20 percent shareholding as sufficient for control. A central weakness in this definition is the absence of directorships as an indicator in assessing 'control' over an institution.⁷ An economic group can more accurately be defined as controlling a bank when it holds a minority share if it also assumes directorship functions. Given this definition, therefore, a single bank can be 'controlled' by more than one group. In the Banco de Credito, for example, members of the Romero, Raffo, Brescia and Nicolini groups are on the board of directors; while on the Banco Wiese's board of directors are members of the Picasso, Wiese and Berckemeyer families.⁸

As suggested by the shared interests in the financial sector, there often exist alliances between economic groups and mutual interests in companies in the industrial sector. The board of Backus and Johnson beer company provides a clear example of group collaboration, by having representatives of the Olaechea, Brescia, Bentin, Berckemeyer and Raffo groups as board members. The Romero and Raffo groups in particular, have close ties, with mutual interests and control in various enterprises such as Universal Textile, Textile Piura, Inmobiliaria Portales and the Banco de Credito. Because of these combined interests, many have branded this collaboration as the Romero-Raffo group.⁹ While these families have a large number of enterprises in common, there is no evidence to show that each

⁷ In the modern corporate structure, it is argued that due to diversification of ownership through shareholding, control rests increasingly in the board of directors. See for example, Herman (1981), and Berle and Means (1932).

⁸ For information regarding shareholding and directorships in the financial system, see, The Peru Report (1987).

⁹ See, for example, Reid (1985) and Anaya (1990).

family subordinates its own profit maximisation strategy to one developed for the benefit of the union. The designation of the collaboration of these families to be one group therefore appears overstated.

Before attempting any estimation of the extent of economic group holdings in Peru, careful definition of terms is needed. Unfortunately, many studies of economic group power have greatly overestimated the extent of group ownership by considering even minuscule levels of stockholding as indicating 'control' over a particular company. Without attempting the type of complex definitions which would be necessary for an in-depth quantitative analysis, the following straightforward definitions can be used for the purposes of clarity.

Ownership can be said to exist if a group maintains 50 percent plus one of the shares in its possession, indicating outright ownership of the firm. Full ownership and control can be said to be synonymous. While minority levels of stockholding do not indicate ownership, it must be recognised that it can allow an economic group to influence company strategy and decision making. Again, if shareholding is reinforced by the presence of group members on the board of directors, high levels of influence over financial strategy and investment planning of a firm can be obtained. Although Bourricaud (1970) points out that directorships are not synonymous with control, in most cases, the major stockholders are either present or represented on the board of directors (Anderson 1974).

The top economic groups in Peru are identified in Table 3.3. The following four criteria were used in the identification of economic groups: 1) interests in more than one industrial sector, as defined by the Standard Industrial Classification Code, 2) a minimum of one top 100 company under its control, 3) interests in the financial system, and 4) a minimum of one directorship in the financial system to show operational control.

Each economic group, this data reveals, has varied economic interests.

The Picasso group is a typical example, with interests in sectors as diverse as mining, radio, and distilling. As is also illustrated in Appendix 1, the economic groups' companies are often the top income earners in their sector. The agro-industrial sector, the leading manufacturing sector in 1986, shows a great level of group control, with Nicolini Hermanos not only leading this sector but also ranked as number one grossing privately owned corporation in Peru. Prominent economic groups also control the third and fourth leading corporations, Backus and Johnson and Compania Nacional de Cerveza. The former has the Bentin family as principal stockholder, with additional participation from many other top groups, and the latter is controlled by the Lanatta-Piaggio group. Again, the groups own the textile leaders. The Brescia group's Tejidos Union is the largest textile company in Peru, grossing more than double its nearest competitor (see Appendix 1).

The extent of the group's control over non-manufacturing sectors, however, is less strong. The mining sector, for example, has three powerful sources of non-group ownership: state, foreign capital and national mining conglomerates (see Appendix 1). Although some of the mid-size mining companies are owned by the economic groups, such as the Brescia and Picasso families, as a rule the groups are not heavily dependent upon mining and do not dominate that key sector of the economy. The mining sector is dominated by both foreign capital and public sector industry. In 1988, for example, the leading Peruvian mining group Benavides-Buenaventura had a gross income of US\$71.6 million, contrasting sharply with US\$650.9 million for the state mining companies, and US\$221.9 million for the top foreign company, Southern Peru.¹⁰

Alcorta has identified the existence of twenty-one domestic economic groups in Peru, along with four foreign owned groups. Alcorta further estimates that these twenty-five groups own 281 companies outright, and after accounting for their minority participation in other companies, he estimates that they account for

¹⁰ *The Andean Report*, 'Groups 250', April 1990.

12 to 15 percent of Peru's total GDP (1978:42-3).

What is the significance of the group structure? It is clear that this structure greatly facilitates the process of capital accumulation and expansion. The studies of economic groups in Latin America and elsewhere point to the ease of capital mobilisation by a group with control over a financial institution, giving it the powerful ability to finance their own investment projects.¹¹ Certainly the industrial conglomerates with strong financial sector participation are less likely to suffer from credit shortages than non-financial industrial conglomerates, and are likely to be subject to less stringent credit application requirements than non-group members. This constant access to credit when needed is an important feature of the group structure which has enabled these relatively few families to expand their industrial empires.

Beyond this function, there is little agreement about the supplementary functions which the group structure can perform. It has been noted that the objective of each group is profit maximisation at an overall level, and not necessarily of each a individual company (Sanfuentes 1984). This point has also been made by Anderson (1974) in regard to the American corporate structure. This hypothesis can take on particular importance in the Peruvian case, given the high level of integration common to most groups, which can allow one company to partially subsidise the others. In this fashion, an economic group can minimize the threat of costly or irregular suppliers, and simplify the production process. This facet of the structure can give a group of companies tremendous resilience and enable it to withstand and overcome periods of economic crisis. The total integration of the Romero textile industries, from the cotton plantation, to processing companies, textile production and trading companies for the exportation of the final product (similar in its degree of integration to the Bentin beer industries), can facilitate production, allow for the capture of total value added and minimize risk. The group structure, moreover, provides the flexibility to transfer

¹¹ See, for example, Leff (1976), Sanfuentes (1984), Strachan (1979) and Aubey (1979) on groups' ability to perform capital market functions.

capital and investment from one sector to another, according to relative rates of profit.

The potential for such a relationship between the financial institution and the related companies also exists. In 1982, the Romero group's Textile Piura was experiencing serious financial difficulties and was refinanced by the Banco de Credito.¹² In the absence of the fiduciary relationship which existed in this case, it is less likely that this generous refinancing would have occurred.¹³

It could further be suggested that this structure is designed as a rational economic response to continual economic crisis to protect the group from changing economic conditions. The neo-liberal policies which had an adverse impact on the industrial sector in 1978-80 and 1982-84 may have helped consolidate the groups' position, while eliminating much of the weaker competition. A glance at levels of concentration in 1973 and in 1983 suggest that this may be the case. According to a 1987 study, the level of concentration in the manufacturing sectors increased dramatically in this ten year period, from an average of 37.8 percent market share of the top four companies in 1973, to an average of 57.9 percent in 1983. The major beneficiaries of this have been the leaders in each sector which are principally controlled by the economic groups. The same study found that the top food processing company, presumably Nicolini Hermanos, increased its market share from 5.1 percent to 8.4 percent, while the top textile company, presumably Brescia's Tejidos Union, rose from 7.3 percent to 13.6 percent of all textile sales (Alcorta 1987:32). It can be concluded, therefore, that the group structure may be a part of a defensive investment strategy which serves to provide constant access to credit while offering some protection from the effects of continual recession.¹⁴

¹² See, for example, Julio Gamero, 'La Situacion Financiera de Textile Piura', *Actualidad Economica*, May 1983.

¹³ As will be discussed in chapter six, this facet of the economic groups was of central concern to the Garcia government, and contributed to the decision to expropriation the financial system.

¹⁴ Vertical integration is increasingly being recognised by economists as a response to uncertainty. See, for example, Blair and Kaserman (1983:102), who argue that it can serve in some cases as a 'market perfecting mechanism'.

This defensive structure has fortified the economic groups, and has enabled their continuous accumulation despite adverse economic conditions.

3.2 Organisation of the Bourgeoisie: The Formation of CONFIEP

While Garcia was able to dialogue directly with the leading investor groups, negotiation with the wider bourgeoisie needed to be conducted through some sort of representative organisation. In the past, as previous chapters have indicated, there were various industrial organisations representing different fractions of the bourgeoisie. While these organisations were able to represent the specific interests of the sectors which they represented, there was no umbrella group which would enable these organisations to speak as one on wider class issues. The sometimes conflicting lobbying of these organisations furthermore served to ensure that their political influence remained limited. In 1984, in responding to the weaknesses of earlier approaches, CONFIEP was established. CONFIEP eventually became an important actor in both the *concertación* stage of negotiation with the Garcia government, and more importantly, in the political conflict over the expropriation of the financial system.

This section will examine the establishment of CONFIEP in 1984 and will attempt to identify the factors which contributed to this sudden impetus to organise. The period of 1983-84 marked a turning point for the bourgeoisie, in which it attempted to enhance its political influence, by reorganising and revitalising its existing institutions, and by establishing a peak confederation of industrial organisations.

3.2.a Crisis of the SNI

The depth of the crisis in 1983 which affected the industrial sector led to a crisis in the private sector's institutions, and as a result, the SNI hit a low point in its history. Its cordial relationship with the government had faded and any semblance of unity within the industrial sector collapsed as internal committees began to bypass the SNI. The members' lack of interest in these institutions was obvious in this period; in one case a committee had three members of a total of

seventy turn out for the yearly election of new leaders.¹⁵

The lack of unity on a sectoral basis, furthermore, impeded a united front on broader issues on which there was some agreement, such as the reinstatement of tariffs. This limited cohesion severely reduced the possibility of effective and concerted class action, despite the existence of possible points of agreement around which the bourgeoisie could coalesce.

These representative institutions had reached a crisis point. However, this new low turned into a catalyst for the revitalisation of these organisations. As the 1985 elections loomed, business leaders¹⁶ began to participate in the political debate which would define Peru's immediate future. Business leaders made it clear that they would not be content to be a bystander during the political transition. The feeling of powerlessness instilled by the profound economic crisis under Belaunde had made them adamant about contributing to the political process, rather than simply reacting to it. In preparation for the 1984 CADE (Annual Conference of Executives), for example, the previously neutral and apolitical IPAE established an intensive review of the economy, in order to identify current conditions, interests and problems of the various industrial sectors. Four working groups were established to elaborate and define its own views, carefully drawing up sectoral development plans.¹⁷ The 1984 CADE was then utilised as a forum for the presentation of the resulting recommendations for economic policy.

The resulting final document entitled *Consenso Empresarial Para un Plan Nacional de Desarrollo* (Entrepreneurial Consensus for a National Development

¹⁵ Francisco Durand who has chronicled the behaviour and organisation of the industrial sector in various magazines, journals and books over many years, suggested in 1983 that the SNI was on the verge of collapse. See, 'Sociedad Nacional de Industrias En Quiebra?', *Actualidad Economica*, May 1983.

¹⁶ The term business leaders is used to refer to the elected leaders and managers of the various industrial organisations, such as CONFIEP, SNI, ADEX, CONACO etc.

¹⁷ See, for example, interview with the President of IPAE, Alberto Sacio Leon, in *Gerencia*, October 1984.

Plan) was a lengthy and in-depth examination of the prospects for economic growth accompanied by policy proposals for industrial development (IPAE 1984a). These conclusions were presented to the five presidential candidates and their party representatives. This was a substantial change in the business leaders' traditional behaviour, in that they did not only listen to the industrial strategies proposed by the candidates, but had designed their own guidelines and actively promoted them. The president of IPAE which organises the yearly event claimed that for first time, 'through this CADE, IPAE is participating in national politics.'¹⁸ As industrialists increasingly became embroiled in the political debate surrounding the forthcoming elections, business leaders emerged with renewed vigour and conviction and acted to establish a peak association to unify the diverse industrial organisations.

3.2.b The Creation of CONFIEP

An umbrella organisation unifying diverse industrial organisations, was developed in 1984. Its members, therefore, are industrial organisations, rather than individual entrepreneurs. The National Confederation of Private Entrepreneurial Institutions, known as CONFIEP, was comprised of six institutions when established; the SNI, ADEX, CAPECO (Organisation of Construction); CAMCO, (Chamber of Commerce); CONACO, (National Confederation of Commerce); SNP, (Society of Fishery); and SONAMINPET, (Society of Mining and Petroleum). Within the first two years, eight more organisations were added. Among the new member institutions were CONFECAMARAS, (National Confederation of Chambers of Commerce); ONA, (National Agrarian Organisation); and ABP, (Association of Peruvian Banks) (CONFIEP 1987). The scope and range of the enterprises represented in CONFIEP greatly transcended that of any other private sector institution.¹⁹

CONFIEP was designed to lobby the government on issues where there is

¹⁸ Interview, Alberto Sacio Leon, *Gerencia*, October 1984, p. 25.

¹⁹ According to CONFIEP, over 15,000 companies, which employ approximately 1.6 million people, are represented. CONFIEP leaflet, 1990.

agreement throughout the industrial sector, thereby presenting a united position to the government. Of the six stated objectives of CONFIEP at its inception, the first was to, 'promote, maintain and develop the union of private enterprises of Peru and of their representative entities.'²⁰ The objective of achieving unity and consensus within the bourgeoisie in order to increase its negotiating power with government has been a central difference between CONFIEP and other industrial organisations. In its effort to achieve unity, it has a specific policy of avoiding becoming embroiled in minor or policy level sectoral interests. CONFIEP's policy is to make statements only on issues where there is complete consensus.

This policy is partly a result of the failed experience of unification in 1978 with the UEPP. According to the first President of CONFIEP, Julio Piccini, previous efforts at unification had failed because they 'attempted to resolve sectoral problems.'²¹ CONFIEP in contrast, provides a structure for the defence of issues which affect all sectors, without sacrificing the independence of its member organisations. According to its first Vice-President Eduardo Iriarte:

The function of CONFIEP is to address macro-economic factors which affect entrepreneurs, while allowing each sector to deal with their own problems directly with the government.²²

CONFIEP, therefore, is inherently more stable by acting only on issues of total consensus, and avoiding potentially divisive issues. Although this serves to limit the issues upon which it takes action, the benefits of unity outweigh the price of having a restricted sphere of action. The unification of diverse sectors of the economy gave CONFIEP a massive constituent base, and the policy of speaking by consensus gave it increased legitimacy in its negotiations with government officials. In comparison with the SNI or ADEX, for example, CONFIEP was less

²⁰ See editorial in *Industria Peruana*, February 1985. p.1.

²¹ Interview, Julio Piccini (President of CONFIEP 1985), April 13, 1992, Lima.

²² Interview, Eduardo Iriarte Jimenez, (Vice President of CONFIEP 1984-87) April 11, 1992, Lima.

likely to be seen as an agent of basic sectoral interests.²³

The fact that the bourgeoisie turned to this interest group strategy so forcefully in the 1980s can be explained in part by the historical conjuncture in which it took place. There were diverse factors which gave birth to a renewed effort to organise and extend the role of capitalists beyond the productive sphere and into the political realm.

The transition to democracy was conducive to increased political participation of various social groups, whose activities had been partially suppressed throughout twelve years of dictatorial military rule. An easing of the constraints to organisation and political participation encouraged capitalists to reassess the effectiveness of their existing institutions and recognise the limits to effective collective action which had been evident during the past decade. The successive crises induced by the Velasco, Morales Bermudez and Belaunde governments, furthermore, had left capitalists deeply dissatisfied with these administrations and many felt at the mercy of policy swings. The need for more coordinated and concrete efforts to influence policy became increasingly obvious.

The industrial bourgeoisie in Peru, during this period, held relatively limited political influence. Although the industrial bourgeoisie's position as leading class fraction had been confirmed as the last vestiges of oligarchic domination had been overcome, and despite the fact that the oligarchy had been displaced as a political force, industrialists were not able to extend their influence over the state and policy making. The 1970s was dubbed the 'frustrated decade' by a president of the SNI, as an alliance between state and industrialists never materialised.²⁴ Although industrialists have had ample opportunity to express

²³ However, it should be recognised that many small businesses, and the informal sector, are not represented in CONFIEP.

²⁴ *The Frustrated Decade*, is the title of Durand's study of the relationship between state and industrialists during the 1970s named after a quote from a former president of the SNI, Alfredo Ferrand. Durand argues that part of this lack of political influence was due to the divided nature of the industrial class (1982).

their concerns, in varying degrees, to all governments from Velasco to Belaunde, they are frustrated not by lack of access to government, but by a lack of political leverage.

The appearance of CONFIEP can be linked, therefore, to a longer term frustration of the bourgeoisie's static role in the social and political structure. It could be argued that this is due in part to a lack of an organisation which would enable it to participate collectively in politics. In the absence of a such a structure, according to CONFIEP, the industrial sector had been,

notoriously distant from economic, social and political decision making. Its action was limited within the framework of industrial [sectoral] organisations and within its productive centres (CONFIEP 1987:31).

The creation of a peak business association was designed to redress this lack of political participation and provide a new means by which the bourgeoisie could participate more directly in the decision making process.

There is an absence of a well defined political party which clearly represents the interests of the capitalists. In the absence of such a party to develop a clearly identifiable ideological framework for policies which reinforce and sustain the accumulation pattern and incorporate class interests, business associations and industrial organisations assume a heightened importance. As Becker noted shortly before the creation of CONFIEP, 'trade and guild associations loom larger in Peruvian bourgeois class formation due to the lack of well-institutionalized class parties of the Right' (Becker 1983:254).

In this context, CONFIEP can be seen as a long-term product of the rupture of the oligarchy-state alliance in the late-1960s. The emerging industrial bourgeoisie had not been able to form a stable alliance with the state, nor find concrete representation through the political party structure, and its attempt to improve the balance of its relationship with the state then took the form of interest group representation. It is often suggested that this type of interest group action

demonstrates a political weakness of a given group which must resort to this structure to gain a voice.

Interest group organisation, given the historical conjuncture, was the clearest option and most viable strategy. In contrast to previous industrial organisations, it can be argued that CONFIEP reflects the broader objectives and more deep seated political aspirations of the bourgeoisie. The appearance of CONFIEP can therefore be interpreted as a response to this political weakness which may diminish in importance if the bourgeoisie were to gain a structurally powerful position within the political system.

It is also important to recognise the crucial role of an active and dynamic leadership perceptive to these changes in the social and political structure, which made the pivotal decision to organise. According to recent studies of collective action, emphasis is increasingly placed upon the existence of 'political entrepreneurs' able to mobilise resources and cultivate support.²⁵ In the case of CONFIEP there is evidence to suggest that an important impetus for organisation came from the leaders of various organisations, which shared social bonds as well as the common interest of increasing the political influence of the bourgeoisie. According to Eduardo Iriarte, the first vice-president of CONFIEP, one of the reasons why CONFIEP emerged in at this particular conjuncture was that those who rose simultaneously to the leadership of the Chamber of Commerce, the Association of Constructors, and the SNI had close personal ties.²⁶ The affinity between the three leaders, in agreement about the need for collective action, greatly facilitated the creation of CONFIEP. These leaders were willing to assume the burden and responsibility of organising the various industrial and commercial organisations, in exchange for the social prestige gained from

²⁵ See, Diani and Eyerman (1992) on the various approaches to the study of collective action. See also Hirschman (1985) who argues for the importance of political entrepreneurs as well as moral and political commitment of leaders to explain collective action and social movements.

²⁶ Interview, Eduardo Iriarte Jimenez (Vice President of CONFIEP 1984-87), April 7, 1992. Lima.

assuming such a position.

The interpretation of events presented here has emphasised that the stimulus for these efforts for increased organisation were primarily domestic in origin, and due primarily the social and political changes brought about by the transition to democracy in Peru. However, it should be noted that international trends reinforced this tendency to organise. A trend toward the increasing organisation of capitalists has been seen in Latin American and elsewhere. This trend, which has been called a 'global entrepreneurial movement', highlights the growing importance of means of transmission of management techniques, organisational practices, free market ideology and industrial organisation which link capitalists across national lines (Alvarez 1991). The establishment of IPAE and ESAN in Peru, both management training institutions, both serve as conduits for experiences to capitalists in developed countries, as do international conferences which provide forums for interaction between capitalists from around the world.²⁷ It is likely that the existence of peak associations in most developed countries as well as many other Latin American countries acted as models of industrial organisation. While these influences are primarily technocratic in nature, they tend to also have strong neo-liberal influences and political overtones.²⁸

²⁷ The Graduate School of Business Administration (ESAN) was developed in part by a grant by the United States Agency for International Development. IPAE, as well received international support in its early years (Redher 1968). CONFIEP, as well, received a grant from USAID in 1987. See chapter seven below.

²⁸ For a Venezuelan case study which treats business associations a component of social movement and bourgeois class action, see Becker (1990).

3.3 Conclusions

Within the decade, the bourgeoisie began a process of evolution from an apolitical, poorly organised and divided social group, to a well organised increasingly dynamic social and political actor. Through CONFIEP it made qualitative leap towards a 'class for itself'; that is, a social actor able to actively promote and defend its interests in the political arena.

CONFIEP incorporates not only the industrial fraction of the bourgeoisie, but other fractions of the bourgeoisie, including the financial and commercial fractions. It is important to note, however, that while CONFIEP represents capitalists more generally, the industrial groups within CONFIEP are often the most active in the formulation of policy. This interest group strategy proved effective as the reformist Garcia government introduced measures which threatened private property rights. As subsequent chapters will show, the ability of the bourgeoisie to engage in collective action manifested itself not only in the formation of CONFIEP, but also in the successful opposition to the expropriation of the financial system. The response of the bourgeoisie to the Garcia government must be understood in the context of capitalists' growing perception of the need to become more forcefully involved in politics and policy formulation. They were poised and ready, by 1987, to react against the reformist government through direct political participation.

As the previous chapters have established, the industrial bourgeoisie has undergone tremendous changes since the 1968 'revolution'. It was ready to demand a more active role in national politics in the mid-1980s, and the threatening nature of the reformist Garcia government sparked the emergence of the industrial bourgeoisie as a powerful actor in partisan politics by the 1990s.

CHAPTER FOUR

APRA, INDUSTRY AND THE HETERODOX MODEL

Introduction

In 1985, the APRA (American Popular Revolutionary Alliance) party candidate, Alan Garcia, was elected to the presidency. Young and charismatic, Garcia proposed a growth-first economic plan which aimed to reactivate the stagnant economy and boost incomes for both the urban and rural poor. The election of Garcia marked a return to an active state role to address the deteriorating economic and social conditions. Garcia's strategy held widespread appeal to most sectors of Peruvian society, as this interventionist approach to address the crisis was a welcome contrast to the weak and ineffectual nature of the exiting Belaunde government. This populist approach was responsible for Garcia's landslide election to office and for generating high expectations of economic growth and social reform.

Garcia's nationalist, centre-left approach drew heavily from APRA ideology. Garcia's ascension to power in 1985 represented a historical achievement for the APRA party. APRA, Peru's oldest political party, has had a chequered history. At various stages in its history, it had been poised for electoral success, only to have its path to power blocked by Peru's conservative political and military elites. This resistance originates from APRA's early days in which it held a radical reformist ideology, and an exceptionally disciplined mass following which presented a genuine reformist threat to the status quo. Its original revolutionary fervour and an Aprista uprising in Trujillo in 1932 in which some military officers were killed, earned APRA the long standing animosity of the military and the distrust of the oligarchy. Since this time, the APRA party has gradually moved toward the political centre and has modified its political and economic ideology. The heterodox economic policies of the Garcia government must be situated within the changing ideological currents of the APRA party. Since it was founded in the 1920, APRA has moderated its anti-oligarchic rhetoric and has been careful not to portray its economic policy as

outwardly confrontational with industrialists. This section will briefly review the history of the party and its evolving view of domestic industry in order to gain a broader historical understanding of how the alliance between industrialists and Garcia government developed.

4.1 The APRA Party and Industry

The American Popular Revolutionary Alliance, known as APRA, was founded by Victor Raul Haya de la Torre while in exile in Mexico in 1924. Its first statement of policy known as the "maximum programme", was inspired in part by the Mexican revolution and was comprised of five points which articulated the party's guiding principles. These five principles formed the ideological foundation for the party's anti-imperialist and anti-oligarchic stance. Prominent among these was point three: the nationalisation of land and industry.

These strident principles were gradually diluted as a direct result of Haya de la Torre's political pragmatism. Throughout the evolution of the APRA party, Haya de la Torre showed himself willing to compromise the party's ideological purity in order to enhance prospects for political power. Unable to gain power through the ballot box APRA formed tactical political alliances with the Bustamente y Rivero government in 1945 and again with the conservative Prado government in 1956. It was at this stage that much of the radical elements of the programme were modified or dropped (Palmer 1980).

APRA's stance on nationalisation of industry softened considerably. Haya de la Torre began to make a clearer conceptual distinction between foreign capital investment, which he felt was a necessary force for economic growth, and imperialism, which implies the added element of political influence and control. The APRA programme placed more emphasis on regulating foreign investment and referred to selective nationalisations in key areas of the economy. Heavy industry, in particular, fishing and mining which was a cornerstone of foreign capital in Peru, was targeted for state control. Haya de la Torre's pronouncements on nationalisations became less strident as he attempted to reassure both domestic and foreign investors. Haya de la Torre argued that, 'a wide field must be left for private initiative, national and foreign, in its constructive action in promoting the de-feudalization and the industrialization so indispensable to the progress of our peoples' (Alexander 1973:221).

As the party abandoned its most radical proposals, it was able to widen its social base of support. APRA increasingly gained middle class support which supplemented its traditional student and working class base. White collar unions were increasingly drawn to the moderated reformist message, with the teachers unions emerging as a new pillar of APRA support.

As early as 1956, prominent APRA leaders began to consider the potential for forming an alliance with domestic industrialists. The Aprista ideologues began to distinguish between the land-based oligarchy and the incipient local industrial sector. Haya pointed to two sources of economic power which perpetuated the semi-feudal social and economic structure of Peru: the landed oligarchy and international capital. The emphasis was on economic modernisation which Haya de la Torre believed would lead to a more modern and just social structure. Even foreign capital, if it contributed to such an end, was deemed permissible:

In conclusion, this principle of Aprismo should be mentioned: to the 'necessary and good' foreign capital-coming to our countries to contribute to the demise of the feudal regime and to stimulate the methods of capitalist industrialism, insofar as that signifies civilization-must be given ample governmental security (Haya de la Torre 1956 *in* Alexander 1973: 222).

APRA leaders perceived the growth of an indigenous industrial bourgeoisie, able to challenge the economic dominance of foreign capital, as an important element in the process of economic development. These overtures to local industrialists were moderately successful. This brand of economic nationalism was appealing to elements of the emerging urban industrial sector which had a vested interest in economic modernisation and which held more progressive views than did that landed oligarchy. There was a convergence of interests on the key issue of foreign capital and with the basic principle of breaking the power of foreign capital and local oligarchy. The protectionist elements of the programme were therefore appealing to the incipient industrial sector.

Alan Garcia rose rapidly through the party ranks in the early 1980s. With the death of Haya de la Torre in 1979, APRA was ill prepared to contest the democratic

elections of 1980. The APRA leadership was assumed by Armando Villanueva, a contemporary of Haya de la Torre who had long played an important role in the elite echelons of the party decision making hierarchy. Villanueva however was too closely linked by the public with APRA's violent militant factions and had little appeal beyond the party loyalists. Accordingly, APRA fared poorly in the 1980 elections. This defeat paved the way for a new generation of Aprista leadership, led by Alan Garcia.

With young and dynamic Alan Garcia at the helm, APRA was able to distance itself from its tarnished image of militancy and violence. The direction of APRA in the 1980s was heavily influenced by Garcia's own political ideology. He openly admired the democratic-socialist model of Spain's Felipe Gonzalez but tempered his reformist vision with economic pragmatism (Graham 1992:89). Garcia proposed a model of economic growth with redistribution, while arguing for a limited direct state role in production and the protection of the role of private investment in the economy.

Garcia set about trying to construct a multi-class coalition behind his candidacy. In 1983, APRA developed a commission to draw up its policy plans. CONAPLAN (Comision de Plan de Gobierno) provided a vehicle for engaging the support of industrialists. Many leading industrialists and leaders of industrial organisations were coopted into contributing to the government development plan (Vega Llona 1988). As APRA began to forge stronger ties with the industrial sector, Garcia began propounding his ideas regarding *concertación* and the need for a more formalised relationship with industry.

It is worth noting that the concept of a structured, corporatist relationship with representatives from industry and other economic actors did not originate from the Garcia government. Rather, it dates back to the early years of the APRA party, and has remained a part of its ideology since the 1930s.¹ APRA's minimum programme, or short-term government plan, presented in the 1931 presidential campaign proposed

¹ For a detailed history of the Economic Congress, see Pareja (1987).

the creation of an autonomous state entity incorporating representatives from the industry and labour, alongside academics and economists, to act as an investigative body and an advisor to the executive. The National Economic Congress, as it was called, was proposed as an institution to investigate socio-economic conditions and provide technical advice on various aspects of policy. According to Haya de la Torre, the National Economic Congress was designed to be a source of in-depth information for policy makers which would give the state 'new dimensions' by providing a forum for debate and discussion of economic policy with representatives of important economic and social actors.² The Congress would therefore play a unique and important role in the planning process by providing a non-partisan, and in fact 'apolitical', advisory service to the state.³

The concept of the National Economic Congress evolved over time, from that of an investigative body providing technical advice, to one of an institutionalised forum for the presentation of varying points of view from different economic actors. As defined in a bill presented by the APRA party, the Congress would be 'a representative state body of the factors of production', acting to 'coordinate and concert' between them (Pareja 1987:73). Although the Congress was never realised, the concept was incorporated into the constitution, albeit in a less comprehensive and institutionalised form. Article 111 of the 1979 constitution stated that political and economic policy which guides the private sector must be made in collaboration with it.

It is necessary to examine the *concertación* strategy in the context of the considerable emphasis which the principle of institutionalised *concertación* has historically received in Aprista economic and political doctrine. The Garcia government's conceptualisation of its relationship with industrialists is grounded in an ideology that considers the incorporation of various economic actors in the process of economic policy making essential for strong and effective state planning. By

² Speech given by Haya de la Torre, August 1932, reprinted in Pareja (1987:3)

³ The need for a skilled and 'apolitical' source of advice was expressed by Haya de la Torre in a speech in 1932, reprinted in Alexander (1973:209).

granting a structure and forum for the expression and defence of different interests, it was believed that the state would be better able to harmonize these interests and manage the economy. For this reason, the National Economic Congress has been considered to be 'the fundamental tool of the APRA state' (Barba [1986]:108).

It therefore not surprising that the first APRA government strongly emphasised the need to develop a solid relationship with industrialists. In the absence of an institution such as the National Economic Congress, the government was free to shape the relationship as it felt was needed.

4.1.a APRA in the 1980s: Garcia's rise to power

The election of Garcia and the return to a reform programme occurred at a crisis stage in the Peruvian economy and society and at a crossroads in development thinking in Latin America. Before considering the heterodox model itself and in particular, the role envisaged for industry, it is important to describe briefly the conjuncture of these occurrences.

The challenges that Garcia faced upon assuming power were as imposing as the wave of popularity and expectation which swept Garcia to office. The Garcia administration faced the serious and enduring problems of worsening poverty, an extremely skewed distribution of wealth and income, and social conflict arising from these inequalities. Deepening rural poverty spurred migration to urban areas, leading to the creation of vast squatter settlements in the desert plains surrounding Lima. It was estimated that by 1985, two of the five million residents of Lima lived in shantytowns (Ministerio de Vivienda y Construcción 1987:12). This rapid urbanisation introduced new problems of social and economic assimilation. The industrial sector was unable to absorb the growing economically active population, resulting in the creation of a large informal sector of the economy and a large marginalised urban population.

In the countryside, the effects of the neglect of the rural sector and the stagnation of agriculture had more ominous implications: the emergence of a rural

guerrilla movement, the Peruvian Communist Party (PCP), more commonly known as Sendero Luminoso (Shining Path). In the early eighties, this extremist, radical Maoist movement extended its activities from the highland areas to the capital, while a more recent revolutionary movement, MRTA (Revolutionary Movement Tupac Amaru) concentrated its activities in the jungle regions and in Lima. Growing violence was linked to another factor, the drugs trade, in the Upper Huallaga Valley. These debilitating factors combined to produce an intensification of violence, both in the Andean region and in Lima, as well as a process of social disintegration and profound political instability.

The APRA party proposed an direct state role in the allocation of resources to address these growing social and economic inequalities. Garcia developed an alternative 'heterodox' approach to economic management which received multi-class support. The heterodox approach, which called for a strong state role in the economy, differed from previous state directed models - such as the one pursued by the Velasco government - in its emphasis upon the role of the private sector in the economy. The Garcia programme explicitly rejected a significant expansion of the state's role in productive activities, aiming instead to create the conditions conducive to private domestic investment by stimulating consumer demand and increasing the purchasing power of the population. Garcia relied on the private sector to be the primary engine of economic growth, and advocated policies designed to protect and nurture domestic industry.

The adoption of such an approach was influenced by an intellectual resurgence of structuralist economic thought. When the reformist APRA party came to power in Peru, Latin America was at an important political and economic crossroads. A combination of factors which converged in the mid-1980s prompted a critical reconsideration of recent development strategies. First, the debt crisis crystallised and hardened Latin American views on its own external economic dependency and the fragility of its relationship with the world market. Second, democratisation in South America had advanced, with transitions from authoritarian to civilian governments in Peru in 1980, Argentina in 1983 and Brazil in 1985. The heightened

expectations of social reform in these societies in transition was reflected in the election of reformist governments, with a mandate for growth and redistribution. The development options for these governments at that juncture were starkly defined, by strict monetarist policies, such as those pursued by Pinochet in Chile, with its austere and authoritarian connotations, or populist economic strategies based on expansionist neo-structuralist economic policies. Third, and most importantly, the devastating economic impact of monetarist stabilisation programmes in various Latin American countries in the late 1970s and early 1980s, led to a search for an alternative to painful and recessive austerity measures.

Interest in the structuralist-monetarist debate was therefore revived in the early 1980s, and structuralism was once again considered as a viable development option. The governments of Alfonsín in Argentina, Sarney in Brazil, and García in Peru rejected the monetarist approach to stabilisation, opting instead to implement a 'heterodox' shock designed to control high inflation without sacrificing economic growth. It offered, in theory, painless stabilisation and zero inflation.

Democratic consolidation was an important task facing these governments, which attempted to engage the cooperation and participation of broad sectors of society. All three versions of heterodoxy, therefore, included a policy of *concertación*, or social pact, based on a neo-corporatist structure of state-society relations. Whereas in Argentina and Brazil provision was made to include state, industry and labour, in Peru, however, the García government focused almost exclusively on negotiation with industrialists.

This represents an important departure in the post-Velasco era in Peru. As argued in the previous chapter, the industrial bourgeoisie was unable to establish close links with government and policy makers, and had often assumed a reactive strategy toward policy initiatives. García's pledge to enhance channels of communication and negotiation between government officials and industrialists, provided an opportunity for better coordination and consensus between those who develop industrial policy and those who are affected by it.

The heterodox policy was, therefore, built upon an unusual policy coalition. This redistributive left-of-centre approach with rhetoric to appeal to the masses, existed alongside a policy to court investors and provide incentives to the industrial sector. The priority attached by the Garcia administration to forging a relationship with the industrial bourgeoisie, contrasted sharply with his predecessors.

4.1.b The Industrial Bourgeoisie and the Rejection of Neo-Liberalism: A New Opportunity for Change

Garcia ultimately failed to gain the long term support of industrialists.

The interventionist policy which was implemented, at one level provided incentives to induce investment in priority areas, and at another, more directly regulated the activities of the private sector. The failure to develop an accommodation between the state and industrial bourgeoisie is chiefly attributable to these increasing regulations which alienated industrialists.

This in itself is not surprising. The experience of many governments in Latin America, including the Velasco government, has shown increased capital accumulation to be insufficient to sustain the support of the industrial bourgeoisie (Gilbert 1980). Often, any sign of populist rhetoric or reformist policies will result in the sharp opposition by the industrialists who, rightly or wrongly, perceive these measures as a direct threat to private property rights (Conaghan, Malloy and Abugattas 1990, Conaghan 1988). What is perhaps more surprising about the experience of the Garcia government is that on closer examination, the early phases of the relationship show what may be considered to be an unusual degree of acceptance of reform on behalf of industrialists. Rather than being a conservative force in the 1985 elections, many industrialists acted in a progressive manner and actively supported the reformist APRA party.

The industrial bourgeoisie's acceptance of a limited amount of reform presented a new opportunity for change in Peru. This initial support for the economic strategy gave the Garcia government expanded room for manoeuvre, which it

ultimately failed to utilise to its advantage. In their support for the APRA party, industrialists indicated acceptance of a limited amount of interventionism, which they perceived as a necessary price of economic reactivation and the expansion of the internal market.

The Peruvian industrial bourgeoisie holds deep-seated reservations about an active state role in the economy, a view which has been shaped by historical experience rather than by pure ideological conviction. This heightened fear of state encroachment in the economy originated in the tremendous growth of the state in the second half of this century, and the adverse impact of state intervention on the industrial sector under the Velasco regime. The consistent and tremendous growth of the state since the 1950s has led the private sector to feel that its role as the primary engine of economic growth has been suppressed - if not usurped - by the state. Its initiative and dynamism have been affected not only in terms of the expansion of the public sector, but equally by the increased legislation regulating the economic activities of the private sector.⁴ Peruvian industrialists, furthermore, retain a profound fear of the gradual erosion or direct violation of private property rights, which is largely the result of the Velasco-era expropriations.

The industrial bourgeoisie's view of the role of the state, briefly summarized here, tends to validate the predominant characterisation of the industrial bourgeoisie as a very conservative and anti-reformist force in society. The question that needs consideration therefore, is why did the industrial bourgeoisie support the reformist APRA party in the 1985 campaign, rejecting the centre-right parties which advocated neo-liberal economic policies?

The formation of an alliance between a populist government and industrial bourgeoisie is unusual, but not unheard of. Conaghan (1988) provides a useful study of the response of Latin American industrialists to reformist governments, in which

⁴ Mario Rodriguez Rios (former vice-president of the SNI) argues that a central factor limiting industrialisation in Peru is not simply the growth of the public sector, but also the increasing legislation and regulation which hinders private sector economic activity. See *Industria Peruana*, October 1985, p. 10.

the concept of 'reactive participation' is used to explain those cases in which an alliance between industrialists and reformist governments have developed. She regards the formation of this alliance as a pragmatic response on behalf of the bourgeoisie when faced with a populist government, aims primarily to minimise possible threats. Conaghan argues that:

Their participation was reactive insofar as it was not the product of an autonomous initiative on their part, but rather a response to pressure from below. In all three cases, such an alliance came about only *after* a populist leadership came to power through elections. The electoral victories were by no means the fruits of dominant class manoeuvrings (Conaghan 1988:29).⁵

The relationship between the industrial bourgeoisie and the APRA candidate in Peru prior to the 1985 election contrasts sharply with this finding. Many industrialists firmly backed the candidacy of Alan Garcia, rather than the centre-right parties which they traditionally had supported, such as Accion Popular (AP) and Partido Popular Cristiano (PPC). This behaviour needs to be examined in the context of the historical juncture at which it took place. The intense economic and political frustration caused by the final years of the Belaunde administration (1980-85) prompted many industrialists to consider backing the Garcia candidacy. There were two main factors at play here; first, a reassessment of neo-liberalism as a result of both the 1978-79 and 1982-84 stabilisation crises; and second, the emergence of a new, reactivation strategy, which differed significantly from previous populist options.

The alliance which existed between industrialists and the Belaunde government (1980-85) had rapidly dissolved as the economy began to deteriorate, and the neo-liberal economic policies which contributed to the recession began to be questioned openly by industrialists. The sharp reduction in tariffs and subsidies for non-traditional exports (CERTEX) had revealed the harsh reality of liberalisation to the industrial sector, and many industrialists gradually realised that the very policies they advocated made them vulnerable. Economically devastated by these policies in a

⁵ In this passage, Conaghan is referring specifically to Argentina, Chile and Uruguay.

situation of growing crisis, industrialists began to resist the trend toward liberalisation. The poor economic results of the Belaunde government, as well as the stabilisation policies of the previous Morales Bermudez government (1975-80), led not only to the discrediting of the centre-right parties, but also to a broader rejection of orthodox stabilisation as an economic strategy. These experiences, and the approaching elections, led industrialists to reassess development options, as the scope of the Empresarial Consensus forums indicates.⁶ With its conviction in neo-liberalism shaken, industrialists began to consider backing APRA, which at the time provided the only serious alternative to the centre-right parties. In 1985, therefore, many industrialists opted to back the Garcia candidacy.⁷

It is clear, however, that while industrialists feared a recessionary stabilisation programme, they still retained their anti-statist views. Its support for the APRA party at this juncture was heavily influenced by the nature of the heterodox programme, which emphasised reactivation and industrial promotion over painful austerity measures. The appeal of this strategy in the wake of a harsh industrial recession is obvious. This nationalist, inward-looking model with its emphasis on the promotion of domestic industry, was particularly attractive to those industrialists sidelined by the Belaunde government's close ties with foreign capital and the export sector.

While this differs little conceptually from the 1968 reformist programme, there were other elements of the heterodox approach which distinguished it from the Velasco programme and made it less threatening to industrialists. First and most importantly, the strategy contained an explicit rejection of the nationalisation of private industries. The heterodox model, although reformist in nature, stressed the fundamental role of the private sector in the economy, and stipulated policies which were designed to stimulate and promote the growth of private industry. Although a

⁶ The Empresarial Consensus forums were established by the Peruvian Institute of Business Administration (IPAE) to examine economic policy and make recommendations to the presidential candidates during the 1984 Annual Conference of Executives (CADE). See chapter two.

⁷ It later emerged that prominent industrialists, including the director of the Banco de Credito, Dionisio Romero, and the head of the Association of Banks, Francisco Pardo Mesones, gave considerable financial support to the Garcia campaign. *Caretas*, August 17, 1987. p. 20.

substantial reduction in the public sector was not indicated, its growth was to be curtailed to allow the private sector to flourish. This was an important aspect of the model, and Garcia took great pains to emphasise this point to industrialists. At the 1984 Annual Conference of Executives (CADE), for example, Garcia attempted to clearly distinguish the heterodox strategy from a socialist programme in which the state would 'nationalise the means of production or socialise wealth' (IPAE 1984:265). Rather, he explained, APRA's projected role of the state is one whose main function would be planning, without monopolistic control over production. Garcia explained that APRA envisioned,

A state that plans, and which can be enterprising without being monopolistic, which is fundamental, because this kills and eliminates individual capacity (IPAE 1984:265).

In this manner, the heterodox model distinguished itself from many other state-directed, nationalist industrial models in which the state assumes a powerful role in the economy and increases its direct role in production. By promoting the private sector as the main engine of economic growth, Garcia explicitly allayed the bourgeoisie's fear of having its role usurped by the state. This economic strategy, which emphasised the importance of the private sector over the public sector and domestic industry over foreign capital, rather than threatening industrialists, clearly contained powerful psychological appeal for them.

A second element which enhanced the credibility of the APRA party was the policy of *concertación*. The proposed institutionalisation of industrialists' participation in policy making increased their confidence in their ability to exact beneficial economic policies and to restrain leftist forces within the government which might have posed a threat. The *concertación* policy helped the APRA party to project a moderate and centrist image and to present itself as a non-threatening alternative to Accion Popular and the Partido Popular Cristiano. In an era when the industrial bourgeoisie was actively attempting to increase its political influence, the proposal of increased and institutionalised access to government officials held powerful appeal.

The heterodox model therefore presented a new and attractive option to

industrialists. It was an economic strategy which proposed industrial promotion and reactivation over austerity - while posing no real threat to private property - and which posited an enhanced political role for industrialists.

It must be stated, however, that although industrialists were reassured by rejection of public sector expansion and the *concertación* policy, they were nonetheless aware of the reformist nature of the APRA party and the interventionist policies inherent in the heterodox strategy. Industrialists' rejection of the neo-liberal model and its support for the APRA party in 1985, therefore, indicated some acceptance of interventionism and reform, in itself giving the incoming government a considerable margin of support. In assessing possible development strategies prior to the elections, industrialists had grudgingly accepted the notion of direct state involvement in the economy for the purposes of stabilisation and reactivation, and all that it implied; including, price controls, high wages, and import restrictions. This enabled the Garcia government to implement its fundamentally populist policies with the consent and acquiescence of the industrial bourgeoisie. This factor - true multi-class support for the reformist regime - not only offered the Garcia government increased room for manoeuvre, but also presented a new opportunity for change. The industrial bourgeoisie showed itself willing to accept some elements of reform and redistributive policies, and for the first two years, the government and its economic strategy retained the support of the industrial bourgeoisie.

The remainder of this chapter will examine the structuralist economic philosophy as proposed by the Garcia government in order to understand the political coalitions which arose from it. It will focus on the proposed economic and political role of the industrial bourgeoisie, and will argue that the success of the Garcia government's industrial strategy depended upon a stable political alliance with the industrial bourgeoisie. The ideological basis for this alliance needs to be clearly understood, before turning to the analysis of the relationship between state and industrial bourgeoisie which is to follow in subsequent chapters.

The focus of this left-of-centre government on an alliance with industrialists,

rather than relying on a more popular and broad based coalition needs consideration and explanation. This chapter will examine the basis of the reformist programme in Peru, to explain how this uneasy alliance developed. Two important questions will be addressed. Why did the Garcia government place such a high emphasis upon a relationship with industrialists and what objectives was this alliance expected to achieve?

This chapter will argue that the government's focus upon an alliance with industrialists can be understood only by examining in some detail the deeper and long-term economic restructuring objectives of the Peruvian heterodox model. Because of this long-term focus, the heterodox strategy applied in Peru differs significantly from others in the region which were primarily concerned with the short-term control of inflation (Thorp 1987a).

4.2 The Neo-Structuralist Resurgence

The resurgence of structuralist policy prescriptions in the 1980s was stimulated by a lack of alternatives to structural adjustment programmes promoted by the IMF. Throughout the 1970s and 1980s, Latin American countries experiencing balance of payments difficulties and inflation were encouraged by the international financial community to adopt monetarist stabilisation programmes. These recommendations originate in neo-classical monetarist theory, which holds that the root of balance of payment difficulties lie largely in expansionist credit policies and deficit spending which generate excess aggregate demand. Accordingly, these crises, asserts the IMF, can be remedied by monetary and fiscal restraint, currency devaluations and trade liberalisation, which together should allow market forces to correct existing distortions in the economy.

The harsh experiences of orthodox stabilisation in Peru in the periods 1976-78 and 1983-85, contributed to the search for an alternative strategy. Although these programmes did manage to bring inflation under control and improve Peru's balance of payments, they did so at a high social and economic cost.⁸ The Morales Bermudez administration, after pressure from both private creditor banks and the IMF, implemented an orthodox stabilisation programme in 1976. Alongside measures to reduce the deficit and liberalise the economy, the Morales Bermudez administration floated the exchange rate in an attempt to improve the current account through export promotion and import reduction, resulting in a devaluation of 56 percent in 1976, and 90 percent in 1977 (Daly 1983:63-65). But as argued by both Daly and Thorp (1979), devaluation can be a costly tool, as the volume of Peru's commodity exports is determined primarily by installed capacity and supply, rather than by price or demand. Export volume is therefore not sensitive to currency fluctuations. Similarly, a significant percentage of imports is comprised by capital and intermediate goods, making efforts at import reduction difficult and costly. Rather than gaining

⁸ The impact of structural adjustment efforts in Peru have been carefully documented. See, for example, Daly (1983), Scheetz (1986), and Thorp (1979, 1987). These analyses highlight the structural features of the Peruvian economy which exacerbate the recessive impact of monetarist stabilisation policies.

a competitive edge from the devaluation of the sol, many industrial sectors found their production costs increasing as imported inputs became increasingly expensive. While the stabilisation programme contributed to a 15.9 percent increase in the value of exports in 1978, it also led to a 17 percent decline in real wages and growing labour unrest (BCR 1979:9-15).

Thorp notes that a similar stabilisation effort under the Belaunde government achieved a 27 percent reduction in imports only at the expense of a 21 percent fall in industrial output and a 34 percent fall in private investment (1987b:224). Cost push inflation also resulted, and exports stagnated. The lesson which many economists drew from this experience was that the economic cost of achieving minimal levels of balance of payments corrections is exceedingly high, and that the Peruvian experience demonstrates the inefficiency of austerity programmes in achieving stabilisation (1987b:225).

Painful experiences with austerity programmes in Peru, not surprisingly, led to a search for an alternative economic stabilisation and growth model. Industrialists, which had experienced severe economic hardships as a result of these stabilisation policies, were also receptive to a new approach. The Garcia government, with the support of many industrialists, therefore, rejected the recessive policy prescriptions of standard stabilisation programmes, in favour of an expansionist heterodox strategy. This strategy, adopted in 1985, has its roots in structuralist analyses of inflation and stabilisation.

4.2.a. The Structuralist View of Inflation

The detrimental effects that neo-liberal policies had on the Peruvian economy, were explained by the failure of monetarist approaches to take into account other pressures creating balance of payments gaps. According to the heterodox economists, high debt payments, structural bottlenecks in export supply, and the inelasticity of many imports, which can be important contributing factors to balance of payments crises, are underemphasised in monetarist analysis and prescriptions.

This interpretation owes much to the original structuralist critique of monetarism. Motivated by the inefficacy of IMF-style stabilisation programmes in the Southern Cone countries that failed to solve the basic, yet critical, economic problems of chronic balance of payments disequilibria, Latin American economists turned to a structural analysis to understand the dynamics of development and underdevelopment. Monetarist theory, it was believed, had not only failed to provide a path to sustained and balanced growth, but had also failed to offer a satisfactory theoretical framework to understand the behaviour of underdeveloped economies.

The first wave of structuralist thought, much of which emanated from CEPAL (The United Nations Economic Commission on Latin America) in the 1950s and 1960s, held that monetarist analysis was one-dimensional in its focus on monetary factors to the exclusion of other relevant characteristics of the economy. Structuralism, in contrast, argues that,

[inflation] should be attributed to non-monetary imbalances, partly due to flaws in the economic and social organization of those countries; and that, therefore, the reliance on monetary restriction to check price rises in them is unjustified...It is essential therefore to search beneath the monetary surface, into the underlying region of physical flows, real prices, and sectoral disequilibria (Olivera 1964: 321).

An analysis transcending monetary factors was developed by Maynard (1961), Seers (1962) and others.⁹ While variations between authors exist, the core of the analysis lies in the identification of various inelasticities that contribute to the inflationary process. Particularly important are primary sector constraints in agriculture and commodities that adversely affect the economy as a whole. Excess aggregate demand, in this interpretation, need not be the driving inflationary force.¹⁰

This original structuralist theory was revised and expanded in the 1980s by a new generation of economists calling themselves 'neo-structuralist', 'inertialists', or

⁹ See, for example, Ardnt (1985) and Canavese (1982) for a history of structuralist economic thought.

¹⁰ de Oliveira Campos establishes that in fact, structuralism considers inflation to be a 'natural accompaniment of growth' (1961:70).

'heterodox' economists. Leading economists which heavily influenced the development of heterodox policies include Luis Bresser Pereira and Persio Arida in Brazil, Roberto Frenkel in Argentina, and Daniel Carbonetto and the CEDEP think tank in Peru.¹¹

As in earlier versions of structuralism, the heterodox economists place little emphasis on the monetary origins of inflation, and they question the role of excess demand in causing inflation.¹² The heterodox economists at the National Planning Institute (INP) in Peru pointed to the existence of 41 percent idle installed capacity present in industry as clear evidence in the Peruvian case to suggest that excess demand is not an adequate explanation of inflation, as the productive capacity of the industrial sector far exceeds consumer demand (Thorp 1987c:15). This difference between theories of inflation is crucial, in respect of the distinct policy recommendations which arise from them. The monetarist belief in excess demand leads to the conclusion that demand should be reduced and that a corrective recession is necessary. In contrast, from the structuralist assumption it follows that the economy must be reactivated, as domestic demand is too low.

The relaxed position of the Peruvian economists towards inflation is reflected in their view towards the potentially useful role of the deficit. According to the INP:

The argument that the fiscal deficit generates excess demand does not have any basis in the Peruvian economy. When accounting for external debt payments and imports, it is observed that the state generates in taxes more than it spends internally, thus having clearly recessive tendencies (INP 1988:9).

The deficit was seen instead as a useful tool for elevating the low level of aggregate demand in the economy. The economic analysis in the Peruvian case hinged on the belief that inflation was primarily cost push generated. The concern over costs led

¹¹ See, Arida (1986) for a collection of articles by leading heterodox economists.

¹² For examples of neo-structuralist interpretations of stabilisation and economic strategy, see Diamand (1978), Taylor (1983) and Bresser Pereira (1987). See also the debates in *CEPAL Review*, including Bitar (1988) and French-Davis (1988).

the Peruvian team to reject measures, such as increases in public services, which could help bridge the deficit.¹³

The analysis of the causes of inflation is representative of structuralist analysis of underdevelopment as a whole, in underlining structural obstacles to development. Economic distortions of central concern include concentration of land and capital, supply bottlenecks, inelastic import structures, and inefficient resource allocation, which combine to make market forces highly inefficient or ineffective. Structuralism, therefore, emphasises the need for economic alternatives that take into account the structural characteristics of these economies and actively attempt to transform them. The heterodox model developed by the Garcia administration in 1985 was strongly influenced by structuralist ideology and its broader emphasis of actively addressing the structural deficiencies of the economy.

Garcia's industrial policy, therefore, attempted to transform the productive and economic structure, making it more compatible with sustained growth and development. These far-reaching structuralist aims were to be initiated by a reorientation of investment toward industries which were labour intensive and integrated with locally produced intermediate and capital goods (INP 1987b). The following section will discuss the central objectives of Garcia's industrial policy, and the key role of private sector investment in the heterodox strategy.

¹³ In contrast, the Brazilian heterodox economists focused on the concept of inertial inflation, which suggests that it is not simply the expectation of future inflation, but the formal indexation of wages and contracts which assume future increases which makes inflation a self-perpetuating process (Bresser Pereira 1987:1038).

4.3 Industrial Restructuring

The heterodox industrial strategy had three phases: reactivation, reinvestment and restructuring.¹⁴ The first phase entailed economic reactivation through substantial increases in wages, accompanied by firm price controls, in order to stimulate consumer consumption. The second phase called for increases in private sector investment to expand productive capacity in order to transform the short-term consumer boom into medium to long-term growth, avoiding bottlenecks and inflationary pressures. The third phase sought to restructure the economy by using state developmental plans to guide investment towards priority areas of the economy.

Following from the assumption that the inflationary crisis is due to a recessive cycle of higher costs and declining demand, the heterodox model was based on a 'growth-first' ideology, which held that only by stimulating the stagnant economy could the crisis be overcome. The initial phase of the model, therefore, was designed to increase consumer consumption and encourage the absorption of idle installed capacity in industry.

The initial conjunction of policies was also intended to create conditions more conducive to investment. With no illusions of swaying investors simply by appealing to their goodwill, the theorists behind the economic strategy recognised the need to ensure profitability for the business sector. The first phase policies were expected to contribute to this enhanced profitability through both the creation of a vast internal market and a sharp reduction in costs of production. Influential government advisor and heterodox economist, Daniel Carbonetto, held that,

¹⁴ The heterodox strategy as presented here is drawn primarily from National Planning Institute documents and publications, including INP (1987a, 1988a, 1988b). Particularly useful is the *Plan Nacional de Desarrollo 1986-90* (INP 1987b). This chapter also draws from articles published in *Socialismo and Participacion*, a journal published by the CEDEP think-tank, which was very influential in shaping this economic philosophy, and with which Daniel Carbonetto was associated. See, for example, Carbonetto, Carazo and Ferrari (1987) and Ferrari (1986). For an earlier discussion, see *Socialismo and Participacion* editorial (1983). Also useful is an article by Central Bank Manager, Cesar Ferrari (1987), as well as Carbonetto, Carazo and Ferrari (1987b), and Shuldt (1986).

To achieve, therefore, a process of savings and productive investment there must be, in the first place, confidence in the economic process on the part of the private sector. Secondly, private sector behaviour is guided by the law of profits and for it to invest, profitability must be greater than deposits in national currency and other monetary mechanisms, and must be clearly superior to the dollar (Carbonetto, Carazo and Ferrari 1987a:47).

Garcia's economic team believed that the enhanced profitability resulting from the reactivation policies would discourage industrialists from engaging in defensive measures, such as price hikes in anticipation of inflation, exchange rate speculation and capital flight, and would instead encourage investment in productive activities. In addition, tax breaks, access to cheap credit and investment subsidies were to be granted for investment in priority areas. It was foreseen that this combination of policies would encourage risk taking and ensure moderate profitability for investors.

The Garcia government hoped that the investment boom expected to follow the reactivation policy would be guided into priority industrial sectors by the careful use of relative prices and incentives policies. According to the INP, shifts in investment patterns were to be encouraged to increase vertical integration, labour intensive methods and value-added exports. The capital goods sector, for example, was declared a high priority sector in order to begin a long-term process which would increase domestic forward and backward linkages, and reduce dependency upon imported capital goods. Incentives for value-added exports furthermore, were to be implemented to increase foreign exchange earnings and reduce precarious dependence on world market commodity prices. The long-term objective was to,

transform Peru from a primary exporter to a country vertically integrated with roots in a new massive internal market with consumption patterns more compatible with the resources of the country, and which exports manufactured products (Carbonetto, Carazo and Ferrari 1987a:51).

The INP pointed to the unequal distribution of income and use of resources as a key structural barrier to development. This economic heterogeneity manifests itself in the existence of four distinct sectors of the economy, with weak integration between them. Data compiled by the INP on the basis of a study by Daniel

Carbonetto illustrates the sectoral concentration of income, capital and employment in Peru (see Table 4.1).

Table 4.1 Sectors of the Economy and Selected Indicators 1981

Sector	%GDP produced	%Capital use	Monthly Income US\$
1 Urban modern	78.6	89.7	180
2 Rural modern	9.6	8.1	90
3 Informal urban	7.9	1.5	63
4 Rural Andean	4.8	0.7	48

SOURCE: Instituto Nacional de Planificacion. *Plan Nacional de Desarrollo: 1986-90*. 1987. p. 33.

On the basis of this data, the government proposed the reallocation of resources away from the urban industrial sector which requires more capital to produce a percentage of GDP than the other sectors. This sector utilizes 89.7 percent of all available capital, while producing only 78.6 percent of GDP. In contrast, the informal urban and rural andean sectors are starved of capital, utilizing 1.5 and 0.7 percent respectively of available capital, but jointly producing 12.7 percent of GDP.

This data also illustrates a highly unequal pattern of income distribution. The modern sectors, both urban and rural, show average monthly incomes of US\$180 and US\$90 respectively, in sharp contrast with the informal urban sector with an average of US\$63 and the rural andean sector with a mere US\$48. The Garcia government placed considerable emphasis upon the development of policies which would favour the rural and informal urban sectors, such as the use of relative pricing to benefit agricultural producers and the creation of massive public sector employment programmes.

Garcia's economic advisors, therefore, proposed to enact a policy which would ensure growth accompanied by income redistribution, while initiating an inter-sectoral transfer of capital. The model proposed a transfer of 30 percent of available capital from the modern urban sector to both the informal urban and rural andean sectors,

(i.e., the sectors which generate higher levels of production per investment dollar.)¹⁵ Programmes to extend access to credit to these sectors were emphasised. It was proposed that the Central Reserve Bank, for example, would establish lines of credit exclusively for the informal sector, with similar interest free lines to be established in development banks for agriculture. In sum, the heterodox model aspired to lessen the structural heterogeneity of the economy by easing the major gaps between sectors.

Although the Garcia government's industrial plan was ambitious and far reaching in its long-term objectives, it was also ambiguous about how this industrial restructuring was to be achieved. As mentioned above, one important means by which Garcia expected to initiate these changes was by securing the relative profitability of priority sectors of the economy. This was to be accomplished by the use of incentives, tax breaks, favourable exchange rates and selective import licences.

A second key part of the government's investment strategy, designed to reinforce these economic signals, was the *concertación* policy. A close relationship between the state and industrialists, it was envisioned, would give the state the ability to influence the economic plans of the private industrial sector. As stated in the National Development Plan, *concertación* was the 'indispensable instrument' for achieving its development goals (INP 1987b:186). Designed not only to increase investor confidence through increased government accessibility, the *concertación* policy also endeavoured to negotiate projects and generate letters of intent. The role and functions, as well as the feasibility, of the *concertación* strategy will be considered below.

¹⁵ For a discussion of these four sectors of the economy and proposals to increase the integration between them, see the editorial in *Socialismo y Participación*, no. 28, 1984. These conclusions were later incorporated into the National Development Plan.

4.4 Concertación: Some Conclusions

The economic objectives outlined above illustrate the central role of private sector investment in the heterodox strategy as well as the government's need to engage the cooperation and support of the industrial bourgeoisie. The essence of *concertación* was the coordination between state and private sector, in which the vanguard of the industrial bourgeoisie were to be consulted before policies affecting industry were made.

The Garcia government developed a two-tier *concertación* policy. At the first level, broad forums for discussion and exchange of ideas between business leaders and economic team were held on a regular basis. This strategy, not unique to the Garcia government, recognises that allowing industrialists to voice their opinions and concerns, as well as making government planning more transparent, contributes to an atmosphere of investor stability and confidence.

At the second level of *concertación*, there existed a far more ambitious and unusual proposal; namely, more intensive negotiation between individual investor groups and the government, for the purpose of discussing project-by-project investment plans. In exchange for letters of intent and a firm commitment to invest, the government would negotiate favourable economic terms for investors. Firm commitments on all aspects of the project were expected, leading to a final contract between the Ministry of Economy and the investor. Through this process, the government would attempt to encourage shifts toward import substitution, technological modernisation, the expansion of installed capacity, and value added exports. The government also sought concrete investment commitments on issues such as volume, labour utilization, and economic linkages through increased use of domestic inputs.

This type of negotiation has the advantage of producing concrete and definite results; large investment projects could be designed, a commitment to carry out a proposal extracted, and negotiation conducted on project details. Theoretically, this

combination would allow the government to influence the investment patterns at both macro-economic and micro-economic levels. The concrete structure of this negotiation known as 'selective *concertación*', could enable the government to extract specific investment commitments that a general and widespread appeal for investment through CONFIEP might not have allowed.

The emphasis on obtaining the cooperation of local, private capital is a feature of the Peruvian policy which distinguishes it from the Brazilian and Argentine versions of heterodoxy. In the latter cases, the 'social pact' was primarily concerned with establishing a mechanism for agreements on wages and prices between labour, private sector, and government. The Peruvian case, with its emphasis upon investors, reflects a deeper strategic political alliance, designed to facilitate its longer term economic objectives of industrial restructuring.

A second distinguishing characteristic of the Garcia approach, which at the same time helps to explain the emphasis he placed upon the private sector in Peru, was the development of a nationalistic and confrontational debt policy. The Garcia government recognised that its decision to place a ceiling on debt payments of 10 percent of export earnings was likely to have negative repercussions on the further inflows of funds from the international financial community. To compensate for the anticipated shortfall in external sources of finance, internal sources of investment needed to be mobilised. This antagonistic relationship with the international financial community meant that need for an alliance with domestic industrialists in the Peruvian case was therefore more acute. In contrast, both the Brazilian and Argentine governments assumed a more moderate stance toward the international financial community, to the extent that the Argentine experiment with heterodoxy actually received IMF approval.¹⁶

This chapter has therefore suggested that the role of private sector investment

¹⁶ For a discussion of Brazil's attempts at heterodox stabilisation, see Sola (1991), Bresser Periera (1987) and Arida and Lara-Resende (1986). For an analysis of the Argentine case, see Rozenwurcel (1986). See also Lagos and Galevotic (1989).

in the heterodox model cannot be overemphasised. It was regarded as the key to the fulfilment of Garcia's industrial policy and to its ultimate goal of restructuring the economy. The success or failure of the heterodox strategy depended to a large degree upon a successful investment strategy. In the absence of an increase in private sector investment, the reactivation policy would enable only a limited period of economic expansion.

However, this approach does have some serious shortcomings. The most obvious question must be the state's ability to fulfil this extensive role as coordinator, regulator, and integrator of the economy. The state's projected role in the heterodox strategy is to override market signals in the allocation of resources and investment. While the heterodox economists assumed that the market is inefficient and ineffective in correcting distortions in the productive structure, they did not take into consideration the questionable capacity of the state to direct scarce resources more efficiently. In order for this kind of delicate manipulation of market signals to have any chance of success, the state must have a well developed capacity in - at least - two crucial areas. First, it must establish real and adequate economic criteria for the designation of priority sectors and priority investment projects; and second, it must possess a flexible and streamlined administrative structure to oversee and facilitate the investment process, which may easily be hampered if assessed on a project-by-project basis. In the absence of these capabilities, this policy could result in an impediment to capital flow. Lacking, as the Peruvian government did, an administrative structure capable of fulfilling this function, project assessment would be conducted purely through informal meetings between government economic advisors and investors. The danger of this type of informal method of policy making is that it can be prone to subjective rather than solid economic decisions.

A second difficulty with the *concertación* planning method is the increased uncertainty created for investors. Differential economic terms, not only sector by sector, but also project by project, eliminates the possibility of stable 'rules of the game'. It creates serious difficulties for an investor to elaborate an investment proposal when the economic conditions are not known in advance. A policy such as

this which adds to investor instability in an already uncertain economic atmosphere is apt to reinforce defensive and cautious economic behaviour among entrepreneurs.

A third difficulty is the simple fact that the industrial bourgeoisie values strongly its autonomy and is not generally supportive of state planning. The experience of the Velasco government illustrated clearly that state intervention in the economy was sufficient to discourage investment. Moreover, the announcement made at CONFIEP's first press conference that 'the state should not plan for the private sector', gave adequate notice that the industrial bourgeoisie is likely to resist state attempts to influence its behaviour.¹⁷

A fourth potential difficulty with the heterodox approach is its over reliance on the cooperation of the private industrial sector. It is clear that the government only had the capacity to finance the short-term reactivation of the economy and the strategy therefore relied on the private sector to finance the investment phase of the model. The government had made an implicit agreement to industrialists: favourable economic conditions and an increased market would be provided in exchange for investment in priority areas. It was in essence a calculated risk, inflating the economy in hopes of private sector cooperation. This strategy, arguably, contains an essential weakness: it is dependent upon the cooperation of industrialists for its success. Yet the model makes no provision for the (likely?) event that the private sector will not transform rapidly or cooperate fully.

How viable was this goal? Can the government expect the private sector investment patterns to be subject to the governments political influence? An important factor, as suggested earlier, is the short time limit necessarily imposed by the unsustainable financial nature of the reactivation strategy, which could not possibly be prolonged long enough to await or initiate the transformations desired. The existing industrial structure, as demonstrated by the success of the economic groups, has been shaped by years of prolonged crises and has led to rational defensive

¹⁷ Julio Piccini (founder of CONFIEP), quoted in *El Comercio*, September 23, 1984.

economic behaviour among industrialists. A short-term economic boom is insufficient to reverse the deep set patterns of defensive behaviour, which require a prolonged period of economic stability and growth to overcome. The basis for a long-term and sustained increase in private sector investment can only be the result of a stable policy regime.

This factor is further compounded by the tremendous amount of idle capacity which existed in the economy. Although the existence of idle capacity allowed for immediate reactivation, it ultimately works against the model by enabling producers to withhold investment while increasing production and sales. Accompanied by strict price controls and wage increases, the industrial bourgeoisie's proclivity to invest immediately in this policy environment may be low. An added contradiction was the proposal to transfer of resources away from the urban industrial sector - the sector expected to be the primary engine of economic growth.

Although weaknesses in the model's design were clear even before they were applied, its application was even weaker, being both incoherent and marked by economic mismanagement. Although the heterodox economists were responding to a real need for reform, they were unable to translate this analysis into viable and effective policy prescriptions. The growth first strategy, more radical in its interpretation than either the Brazilian or Argentine models, allowed it to become lax in the face of the first signs of inflation. The emphasis on cost push inflation, however important in the Peruvian case, led the economic advisors behind the Garcia government to underplay or even ignore other possible sources of inflation. By the end of the Garcia years, hyperinflation was at levels previously unseen in Peru, and the economic crisis reached new depths.

Although this chapter has argued that the primary reason for this political alliance between state and industrial bourgeoisie was the long-term objective of economic restructuring, it can also be suggested that this policy was a calculated political measure, designed to get the support of industrialists, which traditionally had felt threatened by the radical nature of the APRA party. Thus, one of the underlying

political motivations of the *concertación* strategy was to gain broader, multi-class support, by making the party and its platform more palatable to industrialists. The rhetoric of *concertación* was designed to assuage fears of possible nationalisations and an increased state role in production. By developing the *concertación* policy, the government attempted to make explicit to industrialists the important role of private investment in its economic plans.

The adoption of such an approach, which relies heavily upon domestic, private investment has important implications for the political coalitions and class alliances which the government needed to establish. The need to sustain the support of the industrial bourgeoisie and maintain business confidence placed certain constraints upon the government's scope for manoeuvre. The following chapter will argue that these broad parameters were tested by the reformist essence of the model.

The rhetoric of *concertación* proved to be successful and industrialists supported the APRA campaign in the 1985 elections in large numbers. The *concertación* strategy also had an auspicious beginning, as the government and industrial sector in Peru initially established good and close relations. The reactivation strategy was also effective, and the economy grew strongly in 1985 and 1986. However, tensions in the relationship between the state and industrialists almost immediately began to emerge. The following chapter will examine the heterodox policy in implementation and its impact on the industrial sector.

CHAPTER FIVE

THE INDUSTRIAL BOURGEOISIE AND THE REFORMIST GOVERNMENT: 1985-87

Introduction

In contrast with previous administrations, the development of a close working relationship with the industrial bourgeoisie was a priority for the Garcia government. The *concertación* policy of dialogue and negotiation with industrialists became a cornerstone of economic policy in the 1985-87 period. Having established in the previous chapter the economic importance of private, domestic capital to the heterodox model, this study will now turn to the political relationship between the Garcia government and the industrialists.

This period marks an important change in the nature of the industrial bourgeoisie's relationship with the state in the post-Velasco era. By 1985, industrialists were well organised, were allied with capitalists in other sectors of the economy in CONFIEP, and were prepared to demand a greater role in policy making. The incoming government, as well, envisioned a more dynamic relationship with industrialists. In line with traditional Aprista ideology, the Garcia government proposed a institutionalised role for business leaders in order to transcend the usual approach of general appeals or informal, personal contacts which previous governments depended upon as channels of communication. Instead, the establishment of permanent forums for dialogue and structured arenas for negotiation with both business leaders and individual investors were meant to broaden the scope for private sector input into economic policy formulation. The institutionalisation of *concertación* was seen to provide a much needed forum for negotiation and collaboration between those who hold political power and those who hold economic power.

Yet, within two years, the state and industrial bourgeoisie in Peru were once again at odds. This chapter will examine the gradually emerging tensions, which culminated in the expropriation of the financial system in 1987. This move, it will be argued, signalled the rejection of the *concertación* strategy, as well as the abandonment of the heterodox model as originally conceived. It also had the effect of mobilising industrialists into direct political activity, thus, changing the face of contemporary Peruvian politics.

Any discussion of the relationship between state and industrialists can not be divorced from the economic impact of the policies being implemented. The impact of the heterodox policies on the industrial sector will therefore be considered. This chapter will illustrate some of the major contradictions of the government's investment and industrialisation policy, focusing on the failure of the strategy to move beyond a short-term consumer boom. It will show that as early as mid-1986, strong signs of weakness and inflationary pressures emerged, which were ignored by the economic team. The same expansive policies were continued throughout 1986 and 1987, resulting in a full blown economic crisis.

5.1 The Heterodox Shock

In 1985, Alan Garcia led the APRA party to its first presidential election victory.¹ Garcia easily won the election, with 45.7 percent of the vote in the first round. The centre-right parties AP and PPC did worse than expected, receiving 6.2 percent and 10.2 percent of the vote respectively. The second runner-up, Alfonso Barrantes of the Izquierda Unida (United Left) coalition, received a distant 21 percent of valid votes (Garcia Belaunde 1986:63).²

Although Garcia's margin of victory was encouraging, the economic conditions he inherited from his predecessor were daunting. By the end of the Belaunde years, inflation surpassed 100 percent and the economy was showing only minimal signs of recovery after the industrial collapse of 1983 (see Table 5.2). These economic circumstances, however, accompanied by high levels of idle capacity, low consumer demand and underemployment, provided the optimum conditions for attempts at reactivation.

The Garcia government assumed power on July 28, 1985 and immediately implemented an eighteen month 'economic emergency programme'. Led by Finance Minister Alva Castro and a team of economic advisors, including the prominent Argentine heterodox economist Daniel Carbonetto, the initial policies were designed to reactivate and stabilise the economy, through the stimulation of domestic demand and the stabilisation of basic costs to curtail inflation. The emergency programme attempted to reduce inflation, sharply and radically, by means of a 'heterodox shock'. Similar to anti-inflationary programmes in Brazil and Argentina, the Garcia government introduced a new currency (the inti), raised

¹ For an in-depth discussion of the 1985 election campaign and results, see Taylor (1986). For the statistical results of the election in each department, see Garcia Belaunde (1986).

² Alfonso Barrantes declined to contest the second round indicated by Peru's electoral procedures, recognising that Garcia would have extended his lead by capturing the centre-right votes.

wages, froze prices and reinstated tariffs.³ The anti-inflationary strategy relied upon the control of production costs and the implementation of price controls to eliminate rising consumer prices.

Policy makers attempted to stabilise production costs by controlling both exchange rates and interest rates. The government implemented a one-time devaluation followed by a strict freeze to fix the cost of imported intermediate and capital goods required by domestic producers. In addition, interest rates were greatly reduced in August, from 280 percent to 75 percent. Interest rates were again reduced in October to 45 percent, and finally to 40 percent in February 1986 (Alva Castro 1987a:343). The cost of credit, which had become a heavy burden for most producers, was thereby drastically reduced, compensating for the increased cost of wages and the initial increase in costs of imports.

The second component of the anti-inflationary programme was a widespread price freeze. Prices were declared frozen on all goods and services as of August 1, 1985, while many goods of primary necessity - such as kerosene - were brought under strict government control. This combination of measures was very effective, bringing the rate of inflation down from 10.3 percent in July to 3.0 percent in October (see Table 5.1). This trend had the positive effect of stabilising the economy and neutralising the inflationary expectations which often spur price increases. For industrialists, this gave a needed measure of stability, allowing for concrete micro-economic planning and forecasts of costs and income, in contrast to the volatile economic atmosphere previously existing. The anti-inflationary approach of freezing basic costs and controlling prices was effective throughout the eighteen months of the emergency programme, reducing inflation from 158.3 percent in 1985 to 62.9 percent in 1986 (see Table 5.2).

³ For a statement of economic measures in 1985-1987, see Alva Castro (1987a, 1987b), INP (1987a, 1987b, 1988a, 1988b). See also, 'Principales Normas Legales del Gobierno Aprista: Julio 1985-Enero 1987', *Actualidad Economica*, pp. 14-28. The discussion of economic policy in this chapter draws heavily from these sources.

Table 5.1 Monthly Inflation Rate: July - December 1985

July	August	September	October	November	December
10.3	10.8	3.5	3.0	2.7	2.8

SOURCE: Instituto Nacional de Estadística. *Compendio Estadístico 1988*. 1989 p. 165

Table 5.2 Selected Economic Indicators 1984-1986 (annual percentage growth)

	1984	1985	1986
GDP	5.8	2.2	9.2
inflation	111.5	158.3	62.9
consumption	.8	2.6	12.2
private	2.5	2.5	13.8
public	(13.5)	3.7	2.7

SOURCE: Banco Central de Reservas del Peru. *Memoria*. 1985-1992.

The immediate success of Garcia's economic programme met, and even exceeded, popular expectations. Inflation was down and the prospects for economic growth appeared promising. Garcia's domestic popularity was further boosted by his dynamic governing style, demonstrated in such policies as the nationalistic stance on Peru's foreign debt. Announcing a ceiling on foreign debt repayments to 10 percent of the value of export earnings, the government attempted to link the amount of payment to the ability to pay.⁴ Although immensely popular at home, this measure led Garcia to clash with the international financial community. This policy, more a political gesture than an economic measure, nonetheless freed the resources once destined for debt payments - amounting to nearly a quarter of export earnings in 1985 - for the reactivation of the economy (Alva Castro 1987a:122). This brash approach to the issue,

⁴ For a detailed discussion of the government's debt policy, see Finance Minister Luis Alva Castro's *Dueda o Desarrollo* (1987c).

however, resulted in the 1986 decision by the IMF to declare Peru ineligible for further loans.⁵

With the rate of inflation temporarily under control, the Garcia government then turned to the second objective of the emergency programme: the reactivation of the economy through an increase in domestic demand. The minimum wage was raised repeatedly, by 50 percent in August, 30 percent in February 1986 and a further 30 percent in October 1986, resulting in a modest 3 percent increase in real terms in 1986 (BCR 1986:30). Non-minimum wage earners fared significantly better: unionised private sector employees received an average real wage increase of 25 percent, while non-unionised and public sector employees received 17 and 28 percent, respectively (INP 1987a:136).

A second package of measures, announced in October 1985, included a further reduction in interest rates, and a decree establishing preferential state purchase of national products to boost domestic industry. Further measures to protect the internal market were introduced, expanding the list of prohibited imports. In addition, priority credit lines with preferential interest rates were developed to encourage reactivation and investment in priority areas of the economy. Agricultural producers in the Andean region, for example, were granted access to interest free loans. Other credit programmes with preferential interest rates were developed for non-traditional exports and the informal sector, while a programme of 'Financial Restructuring' was implemented to refinance companies on the brink of bankruptcy. Finally, a programme of Industrial Reactivation was developed offering preferential interest rates on loans from the Banco Industrial in order to encourage the expansion of productive facilities.⁶

⁵ It should be noted, however, that during the last years of the Belaunde government, the debt was not regularly being serviced. It was primarily Garcia's anti-imperialist rhetoric and his efforts to encourage other Latin American debtor nations to assume a similar position, which led to Peru being declared ineligible for further loans by the IMF. See, for example, Roett (1985).

⁶ *El Comercio*, September 13, 1985.

In conjunction with the general reactivation effort designed to stimulate surplus and savings, important changes were made in the existing tax structure and the financial system in 1985 and 1986 to encourage investment. In 1985, the government proposed the creation of financial districts to assure the availability of credit and capital in rural areas and to halt the flow of savings into the capital. This policy was designed to ensure that a certain percentage of savings generated within a regional district would be retained for productive purposes within that district.⁷

Another facet of the policy to develop a larger internal market was the development of a massive programme of temporary government employment. The Programme for the Support of Temporary Income (PAIT), generated approximately 70,000 positions of employment for the urban poor in 1986 alone (INP 1988b:22). In addition, the Programme of Employment (PROEM) made short-term labour contracts exempt from the labour stability legislation to encourage the expansion of productive capacity; while a further package of incentives was established, including tax reimbursements for each permanent position of employment created (CERTEM). These policies to increase employment, in conjunction with the general reactivation of production, were effective. The rate of unemployment declined from 11.8 percent in 1985, to 8.2 percent in 1986; while the rate of underemployment fell from 54.1 percent to 51.4 percent (INE 1989:393).

On balance, the reactivation programme was very effective in achieving its short-term goals. The effectiveness of the employment promotion policies, combined with the increased demand generated by increased real wages, sparked a consumer boom and a substantial reactivation of the economy. The economy grew at a very strong rate - 9.2 percent - in 1986, a substantial recovery from the previous year's rate of 2.2 percent (see Table 5.2). The restoration of the

⁷ A clear discussion of the government's policies with regard to the financial system can be found in a speech by the Finance Minister to the Congressional Budget Commission, reprinted in Alva Castro (1987a:303-15)

purchasing power of the population, supplemented by protectionist measures, greatly increased private consumption. Private consumption was the primarily motor for economic growth in 1986, increasing 13.8 percent in contrast to the public sector's rate of 2.7 percent (see Table 5.2). The increased demand generated by generalised higher incomes led to a surge in production. The manufacturing sector reflected a solid 4.1 percent growth rate in 1985. By 1986, the economic reactivation was in full swing, stimulating a massive 17.8 percent growth in manufacturing (BCR 1987:11).

The success of the economic reactivation programme meant that industrialists' support for the government remained strong. The following section will examine the relationship between state and industrialists in this initial period.

5.2 Concertación: The First Steps

During this honeymoon period, both business leaders and incoming government made important initiatives to forge a close working relationship. It was the SNI, led by Miguel Vega Alvear, which took the first step. In the months prior to Garcia's inauguration, the SNI developed a proposal for a social pact between industry and labour, designed to be broadened in scope at a later stage to include government participation. Discussions between labour and industry were initiated concerning two basic issues, the generation of employment and the restructuring of the social security system. It was hoped that this attempt at labour-industry *concertación*, though limited, would form the basis from which a more comprehensive and binding agreement could be reached on issues such as wages and prices.⁸ Meetings between business and labour leaders produced an initial declaration of a willingness to work together, signed by the SNI and CONFIEP, on behalf of industry, and three mid-size unions. However, the declaration was rejected outright by the most important union confederation, the Confederacion General de Trabajadores del Peru (CGTP), after a general vote.⁹

The government's relationship with industrialists began on a slightly better note. Under the leadership of its founder, Julio Piccini, CONFIEP submitted to the President-elect a more comprehensive and in-depth proposal for a formal political economic and social treaty between the state and private sector.¹⁰ The Garcia government responded to these initiatives by taking the first steps toward formalising and institutionalising the relationship with business leaders. Finance Minister Luis Alva Castro announced that the government's economic policy making would be guided by the 'advice of the business sector through permanent

⁸ See, for example, *Industria Peruana*, May 1985; *El Comercio*, June 4, 1985. The text of the agreement can also be found in IPAE (1985:257-63)

⁹ The three unions which signed the agreement were Central de Trabajadores de la Revolucion Peruana (CTRP), Confederacion de Trabajadores del Peru (CTP), and Central Nacional de Trabajadores (CNT). The CGTP cited disagreements with proposals put forward by CONFIEP regarding labour stability and social security. The text of the letter is reprinted in IPAE (1985:258).

¹⁰ See, for example, CONFIEP (1987), and *Industria Peruana*, May 1985.

dialogue'.¹¹ Accordingly, Alva Castro appointed both Miguel Vega Alvear and Julio Piccini to the Consultive Committee of the Ministry of Economy and Finance, thereby providing them with ready access to government officials. Forums for the exchange of views on economic policy were held throughout August and September, between industrialists and President Garcia, Alva Castro, and other members of the government's economic team.¹²

The emergency programme received the backing of most industrialists, who acutely felt the need to control soaring production costs. The SNI president, Miguel Vega Alvear, stated that he agreed with the heterodox view that inflation in Peru was caused primarily by rising costs and not by excess demand, identifying the high rates of interest and the continuous devaluation of the national currency as the two main culprits.¹³ The heterodox approach to stabilisation which entailed a reduction in interest rates and a fixed exchange rate, brought about a sharp decrease in inflation. This in turn, gave most industrialists an immediate economic advantage and an created an atmosphere of economic stability. In addition, policies introduced to supplement the reactivation plan, such as the selective restriction of imports, and the programme of Industrial Reactivation, gave added weight to the government's stated policy of industrial promotion. These beneficial economic measures, coupled by the initial gestures towards *concertación*, gave industrialists a measure of confidence in the government.

According to policy makers, these policies favourable to industry were being 'offered' in exchange for investment, as part of the *concertación* plan. The Minister of Industry, Manuel Romero Caro, explained to industrialists at the 1986 CADE, that the government expected investment to be oriented to designated

¹¹ *El Comercio*, August 8, 1985.

¹² See, for example, reports of meetings between government officials and private sector representatives in *El Comercio*, August 3, 8, 9, 16 and September 5, 29, 1985.

¹³ *El Comercio*, June 23, 1985.

priority areas, while the state would 'offer in return' measures such as tariff reductions and the expansion of the internal market to ensure profitability.

Minister Romero told industrialists:

The 'concertación' we are talking about has two levels. The first refers to the generation of business profitability, to increase savings and the accumulation of surplus which businessmen should reinvest for productive ends. This level of concertación includes, basically, agreements regarding the management of costs, margins, markets and prices, which will generate an acceptable level of productive profitability (Romero 1986:87).¹⁴

According to estimates by the Ministry of Economy and Finance (MEF), the initial package of measures would reduce production costs for producers by an average of 3.1 percent (see Table 5.3). It can be seen that while imports were expected to rise on average 12 percent, and the cost of labour by 18 percent, a substantial reduction in interest rates would be enacted to counter-balance these increased costs. This cost breakdown, however, merits two important qualifications. First, these economic forecasts were meant to apply to the case of an average producer. Smaller industries with a greater proportion of its costs incurred by labour rather than debt repayment could actually experience an increase in the overall cost of production. Second, it should be noted that this breakdown represents the projected immediate results of the first economic measures. Two of the variables used in the analysis - the cost of wages and imports - began to vary almost immediately; real wages were repeatedly increased throughout 1986, while the cost of imports inputs declined as a result of the increasingly overvalued inti and the reduction in tariffs for essential intermediate and capital good imports. Despite these caveats, however, the initial package had a positive impact on the economy and the Lima Chamber of Commerce publicly stated that the government's policies were successful in making production more profitable than speculation.¹⁵

¹⁴ The second level of *concertación* is the negotiation with individual investors.

¹⁵ The Chamber of Commerce also cautioned against long-term price freezes which would reverse this trend. *El Comercio*, December 23, 1985.

Table 5.3 Breakdown of Average Production Costs: July and August 1985

	before measures	percentage change	after measures
imports	47.4	12%	53.1
salaries	27.3	18%	32.2
credit	<u>25.3</u>	<u>-46%</u>	<u>-16.6</u>
TOTAL	100.0	-3.1	96.9

SOURCE: Luis Alva Castro. 1987. *Economía Peruana 1985-86: Retos y Respuestas*. Lima: *Cambio y Desarrollo* p.113.

The positive results of these initial measures enabled the government to institute other policies less welcome to industrialists with little opposition. These included the extension of price controls, and the mandatory purchase of Treasury Bonds amounting to 40 percent of 1984 net profits by mining companies, banks, finance and insurance companies. In November, the Consumer Protection Law, or the 'anti-monopoly' law as it was commonly known, was passed, establishing that prices were to be regulated for 'companies or groups of companies' which control 75 percent or more of their market share.¹⁶

Industrialists responded to this increasing interventionism, but with considerable restraint. Although the emergency programme implemented in August 1985 received public support by business leaders, some of the policies implemented did suggest a worrisome tendency toward excessive state interference in the economy, prompting CONFIEP to express these concerns to President Garcia. In a letter to the President, CONFIEP leader Julio Piccini acknowledged that the initial policies had been successful, but he also cited eight points of concern, among which featured the compulsory purchase of treasury bonds. Similarly, the enactment of policies which froze bank accounts and certificates of deposit in foreign currency, and the rescission of the contracts of two foreign

¹⁶ The text of the decree can be found in Ministerio de Justicia, *Normas Legales*, November 1985.

companies, Piccini warned, could affect the confidence of potential investors by failing to establish 'clear rules of the game'.¹⁷

Although these policies may have caused some concern, opposition to them by business leaders remained restrained. These policies were accepted in the context of the stabilisation programme in which they occurred, and the overall success in stabilising and reactivating the economy acted to legitimise the government's strategy. However, as the Garcia government intensified the process of reactivation, it introduced further measures which appeared unnecessarily restrictive towards private industry.

The first major move toward expansion of regulatory control over the private sector occurred with the labour stability and anti-monopoly bills proposed shortly after the Garcia government assumed power. The proposed labour stability legislation strengthened the existing laws by sharply reducing the time period required for stability from three years to three months, and by establishing firmer rights to payment and indemnity for dismissed employees.

For the first time, business leaders began testing the limits of - or perhaps the existence of - *concertación*, by making their first active attempts to influence policy. In response to these policy proposals, business leaders launched one of its more vigorous campaigns through CONFIEP and the SNI to influence policy and defend its interests. It is important to note in this case, that opposition to the bill was flexible, focusing on the scope of the bill, rather than campaigning outright against it. Industrialists pointed to two main areas of the bill which they felt were too rigid: the reduction of the time period needed to acquire stability and the terms of dismissal.¹⁸ CONFIEP and the SNI forcefully lobbied the government's

¹⁷ The letter from Julio Piccini to President Garcia is reprinted in *Industria Peruana*, October 1985, p. 60.

¹⁸ See, for example, the text of the speech by Miguel Vega Alvear (president of the SNI in 1986), in which he stated that industrialists are 'willing to negotiate on the time period'. *Industria Peruana*, March 1986, p. 25.

economic team and Congress for a more moderate one year period, arguing that a reduction to three months was too drastic and would only serve make producers hesitant about taking on extra employees. As argued by Alfredo Ferrand, a former president of the SNI, the strengthened labour stability legislation would prevent the fluctuation of levels of production as the market demands.¹⁹ Despite tax incentives for employment creation, the inability to reduce staff if the market contracts can have serious and costly consequences on an enterprise. According to Vega Alvear, to many employers this was a 'life or death issue'.²⁰

The resulting hesitation in creating new jobs in a period of rapid economic expansion emerged as a contradiction in Garcia's economic policy. Despite the primary goal of reactivation, this policy guaranteed stability almost certainly at the expense of the generation of employment. The likely result of such a policy is that the growth of employment would slow despite the rapid economic expansion and CERTEM tax benefits. The impact on the confidence of potential investors, however, could be more damaging. An SNI spokesperson and expert on labour issues, Mario Pasco Cosmopolis noted that,

Entrepreneurs feel, and with good reason, that labour stability reduces their power, limits their faculties, takes away their liberty, and limits their capacity to direct [their enterprises].²¹

The sharp reaction to the final promulgation of this legislation was not unexpected. From industrialists' point of view, the government had overstepped its boundaries and had established excessive interference, by severely restricting the ability of a producer to control the internal affairs of his enterprise. The government responded to this pressure with meetings and debates, but with no substantial concessions. Prominent industrialists publicly complained that while they were given ample opportunity to express their points of view, ultimately,

¹⁹ *Industria Peruana*, December 1985, p. 7.

²⁰ *Industria Peruana*, March 1986, p. 25.

²¹ *Industria Peruana*, September 1986, p.14.

their suggestions were not heeded.²² The labour stability legislation was promulgated in June 1986 and the recommendation that the period be a more moderate one year was discarded.

Similarly, the anti-monopoly legislation disconcerted industrialists more by the extreme rigour with which it was drafted, then by the conceptual nature of the measures. Although not affecting enterprises in such a direct manner, this policy was another example of increased regulation which intensified friction between the state and industrialists. As with the labour stability, it was the tone of the proposed legislation which reflected a regulatory bias that was opposed by the private sector rather than the actual content. The legislation, stipulating price controls for 'enterprises or groups of enterprises' which control 75 percent or more of their market, claimed to meet the 'need for protection of consumers in the face of abuses derived by dominant market positions.'²³ This principle was accepted by most business leaders, who publicly acknowledged the need to protect the consumer and to promote free competition. However, industrialists also held serious reservations about the scope and severity of the legislation, focusing on the fact that essential terms in the legislation, such as market or group of companies, were left vaguely defined, leaving the legislation open to possible misuse. The argument put forth was that were the market narrowly defined, many products could fall under this legislation. This is particularly true in Peru, it was argued, because the limited internal market means that a small number of companies often can satisfy demand.²⁴ Similarly, there is no definition for groups of companies, which industrialists again argued could be loosely, and therefore dangerously, defined.

²² See, for example, interview with Alfredo Aguirre Roca (former president of SNI), *Industria Peruana*, November 1985. p. 5, and the speech by Julio Piccini (president of CONFIEP in 1985), *Industria Peruana*, November 1985. p. 13.

²³ For the text of the law, DS 467-85-EF, see *Normas Legales*, Ministerio de Justicia, November 1985.

²⁴ See, for example, interview with Carlos Verme Katz (former President of the SNI), *Industria Peruana*, February/March 1986, p. 8.

The proposed legislation also established penalties, including prison sentences, for non-compliance, which industrialists felt to be excessively severe. The bill, while acceptable in its general principle, was formulated in such a way that, according to one private sector representative, it had 'an anti-business tone'.²⁵ Its vague wording made it a potential tool of an unfriendly government, and it was therefore perceived by industrialists as a potential threat. As the industrial organisations lobbied the congressional committees for more favourable terms, President Garcia passed the anti-monopoly bill by supreme decree, obviating the possibility of negotiation.²⁶

The reaction of business leaders to this increasing interventionism was muted and suppressed in order not to strain the relationship at this early stage. Reaction to the extension of price controls, for example, was expressed only through gentle criticism:

If on the one hand, price freezes are maintained, and on the other, public spending is maintained and more is asked of producers [in taxes] the prospects for the economy will not be, as all Peruvians would like, optimistic and promising.²⁷

More moderate policies of labour stability, and consumer protection would have facilitated the process of *concertación* at this critical stage. These measures, which were introduced early in the relationship, planted the first seeds of doubt in the minds of business leaders regarding the state's intentions to work in partnership with industry, and of policy makers' receptiveness to their concerns and demands. It is important to consider that neither of these measures were essential components of the heterodox strategy, and that most industrialists objected primarily to their extreme nature. The Garcia government, at this juncture had the definite advantage of industrial support for the model, even

²⁵ Interview with Alfredo Ferrand (Former President of the SNI), *Industria Peruana*, December 1985, pp. 8-9.

²⁶ In doing so, Garcia also upstaged both industrialists and Congress. See *The Andean Report*, November 1985, p. 226.

²⁷ Editorial, *Industria Peruana*, October 1985. p.1.

insofar as having support for price controls, and it is clear that some element of compromise would have contributed to retaining this support. Easing the severity of the legislation would have indicated to industrialists that their interests were being considered. The failure to make any conciliatory gesture was all the more damaging, given the high expectations which industrialists and business leaders had in the *concertación* process. Despite this opportunity to make a concession to industry without sacrificing any key elements of the heterodox strategy, the government pushed through the measures as originally drafted, disregarding the vigorous campaigns which were waged against them.

The proceedings of the November 1985 CADE, typifies the state of the relationship during this period, best characterised by general agreement although hinting at greater differences. Both state and private sector representatives used this opportunity to express their agreement on general objectives, such as the need to reactivate the economy. However, business leaders also took advantage of this opportunity to voice their concerns over the lack of clear and stable rules of the game. Industrialists, by this stage, had become anxious over the unpredictable nature of government's policy making objectives, and expressed deep concern over the expanding role of the state in the economy.²⁸

The honeymoon between Garcia and industrialists ended with the November CADE. The following month, the imposition of the tax reform legislation, which withdrew tax incentives for reinvestment in productive activities, initiated a new, and more overtly antagonistic phase in the relationship.

²⁸ See, for example, speeches by Piazza (1985) and Aguirre Roca (1985) in IPAE (1985).

5.3 Increasing Tensions: December 1985-June 1986

The second phase of the relationship began with the December tax reforms which caused a discernible shift in the tone and character of the relationship. Although tensions gradually began to build, the second phase was nonetheless marked by an increasing institutionalisation of the relationship. The new year was also a period of transition in which there were changes in some of the key players involved. Minister of Industry, Cesar Atala, was replaced by Manuel Romero Caro; while Miguel Vega Alvear, then president of the SNI, replaced Julio Piccini as president of CONFIEP.

Two fundamental issues dominated this period: the accelerating pressure of price freezes on profit margins and the repeal of tax exonerations for reinvestment in productive activities. Significant effort was made on behalf of SNI and CONFIEP to make their opposition to these measures known.

The first major blow to the relationship occurred not with increased regulation, but with the tax reform legislation of December 1985, which eliminated across the board tax exonerations for reinvestment in productive facilities. More than any other issue thus far, this legislation caused deep resentment and demonstrated, according to industrialists, a gap between the government's rhetoric of industrial promotion and its actual policies. The tax reform, D.L. (legislative decree) 362, was meant to revamp the existing incentive structure in accordance with the heterodox goal of restructuring the pattern of investment. Finance Minister Alva Castro argued that the indiscriminate granting of tax exonerations needed to be replaced with a more rational system of incentives in order to promote priority areas and discourage further investment in inappropriate areas. Alva Castro argued that the previous system, for example, 'encouraged the intensive use of capital goods to the detriment of labour.'²⁹ While this legislation did include total five-year exonerations for agriculture and

²⁹ *El Comercio*, December 30, 1985

fishing as part of APRA's agricultural promotion policy, as well as exonerations for industries outside of Lima, the promised new system of incentives for priority industrial areas did not appear until January 1987.

The tax reform legislation had a tremendous psychological impact upon the industrialists. Industrialists felt that this measure contradicted the government's objectives of promoting reactivation and investment. These tax breaks had been in effect for over fifteen years and according to Carlos Verme Katz, a former president of the SNI, this surprise move 'totally changes the rules of the game'.³⁰ In addition, the tax policy failed to expand the tax base, leading to the perception that a disproportionate share of the tax burden was being placed upon producers. An SNI editorial caustically noted that:

Only a mere 8 percent of the economically active population has the obligation to pay income tax. Does this mean that 92 percent of the economically active population has no income to declare? The tributary system appears to be geared to reduce the income of a select group of persons, and with particular zeal, of those who commit the indelicacy of dedicating themselves to productive activities.³¹

The strength of this view can also be seen in a CONFIEP public statement:

Article 139 of the Constitution states 'there is not to be confiscatory tax'. Unfortunately, this principle is dead. DL 362 is unjust and confiscatory and discourages the possibility of channelling investment to productive activities.³²

The suspension of incentives for reinvestment made government policy appear not only unpredictable but also contradictory. This decree was apparently counter to the stated objectives of encouraging domestic investment, and it served for the first time under the Garcia government to mobilise industrialists in active

³⁰ Interview with Carlos Verme Katz (former SNI president), *Industria Peruana*, February-March 1986. p.8.

³¹ Editorial, *Industria Peruana*, January 1986. p.1.

³² *Industria Peruana*, January 1986. p. 18.

opposition. An intense public campaign was waged to have this measure repealed. Full page ads were repeatedly published in the daily newspaper, *El Comercio*, by both the SNI and CONFIEP, claiming that the legislation would impede industrial development by halting any significant increase in investment.³³ Responding to this intense pressure, Finance Minister Alva Castro proposed the formation of a commission with business leaders to negotiate the implementation of the legislation.³⁴ An initial meeting was held, but the commission was never created and the legislation remained intact. This measure revealed the limits of *concertación*, as there had been neither consultation nor negotiation.

Although the industrial bourgeoisie opposed these measures, it continued to support the government and it benefited overall from Garcia's economic strategy. However, by mid-1986, the first signs of real concern with the overall strategy emerged. Arguing that the emergency programme had achieved its main objectives, CONFIEP launched a campaign calling for the end of the stabilisation measures, and a transition to more flexible economic policies.³⁵

Intensifying the friction brought about by the tax reform was the extension of the price controls. The imposition of price controls was an issue of contention which provoked the most significant and long-term debate. The first, yet mild, criticism on the editorial pages of *Industria Peruana* appeared in October of 1985, warning of increasing costs of production and the difficulties in adhering to artificially set prices. The editorial reminded the government that, 'it is a risk to assume that the factors which determine prices are all exclusively under the control of producers'.³⁶

³³ See, for example, CONFIEP statements in *El Comercio*, February 13, 1986, and April 4, 1986, criticising the government's tax and anti-monopoly policies. See, also, the SNI ad in *El Comercio*, January 21, 1986.

³⁴ *El Comercio*, March 20, 1986.

³⁵ *El Comercio*, February 10 and 16, 1986.

³⁶ Editorial, *Industria Peruana*, October 1985. p.1.

The continuation of the price controls into the new year caused resentment among industrialists, who argued that the reduction in interest rates no longer compensated for augmenting costs.³⁷ Public utilities, taxes and in particular, wages were raised on various occasions, while the price of manufactured goods remained under firm control, squeezing profit margins. A low-key but long-term campaign by the SNI and CONFIEP began in 1986, pushing for the 'gradual and flexible' lifting of price controls.³⁸

The weight of these issues overrode the efforts of the February package of measures designed to encourage investment and production. In line with past measures, wages were increased, interest rates lowered, sales tax dropped, and disguised devaluations given for exporters.³⁹ Although having benefited from a strong internal market, cheap credit, and inexpensive imports, industrialists became increasingly wary of the government's continued direct involvement in the economy.

As with the tax policy, it was in part the perception that industrialists were being asked to shoulder a disproportionate share of the burden which angered industrialists. The battle against inflation, they claimed, was being fought within their enterprises. Although at a macroeconomic level these policies were showing positive results, at a microeconomic level, they were beginning to squeeze profit margins.⁴⁰

The government countered by claiming that the MEF would evaluate applications for price increases, and would assure a degree of profitability for

³⁷ See, for example, SNI public notice in *El Comercio*, January 21, 1986; and statements from private sector representatives, *El Comercio*, February 10, 11, 16, 1986.

³⁸ See, SNI and CONFIEP advertisements in, *El Comercio*, January 21 1986, and February 16, 1986.

³⁹ Disguised devaluations were made by allowing exporters to change a higher percentage of earning at the parallel exchange rate.

⁴⁰ This argument was made by Juan Antonio Aguirre Roca, (former president of the SNI), in an interview with *Industria Peruana*, November 1985, p. 4.

producers.⁴¹ In response, the SNI drafted a proposal for a new system of price administration, submitting it to the MEF and the cabinet in August 1986, in the spirit of the continued government calls for *concertación*. The proposal emphasised the establishment of a system in which costs would be the determining factor for prices. The proposal said that,

the key point is for the government establish clear rules which guarantee industrialists that each time costs rise, final prices can be adjusted.⁴²

The effect of continued controls industrialists argued, would reverse the positive effects that the reactivation strategy had achieved thus far, and an SNI editorial clearly warned that, 'price freezes always brings investment freezes.'⁴³ Despite these warnings, the government developed a permanent system of price administration in 1987.

Although these issues combined to create an atmosphere of heightened tension, both parties remained eager to work together. Efforts to institutionalise the relationship showed some results. Under the auspices of the National Planning Institute, a Consultative Planning Committee was developed, consisting of representatives of CONFIEP, SNI and ADEX; academics, labour leaders, government officials and party representatives.⁴⁴ This advisory body was divided into committees to discuss economic policy and make short, medium and long-term policy recommendations, as well as to consider proposals for a permanent structure for *concertación*.⁴⁵

⁴¹ Interview with Manuel Romero Caro (Minister of Industry 1985-87), *Industria Peruana*, April 1986. p. 6.

⁴² The SNI proposal is reprinted in *Industria Peruana*, August 1986, p. 26.

⁴³ Editorial, *Industria Peruana*, August 1986. p. 1.

⁴⁴ Its structure and composition, therefore, is not too dissimilar from the Congreso Economico Nacional.

⁴⁵ Interview with Javier Tantalean (Chief of the National Planning Institute), *Industria Peruana*, December 1985. pp. 10-11.

The focus of dialogue in this period continued to be the industrial organisations and business associations. Although CONFIEP was the primary channel of communication, the Garcia government was careful not to completely sideline the other two important industrial organisations: ADEX and SNI. Their representatives were often included in forums for debate, as the above mentioned council illustrates.

As these attempts to institutionalise *concertación* continued, investment failed to increase to the levels desired by the government. A third phase of the relationship can be discerned beginning in mid-1986 which is characterised by increasing pressure for investment. During this phase, the government, substantially altered its tactics. It developed a new focus on the financial system, and shifted towards *concertación* with specific economic groups.

5.4 Investment Strategy: July 1986-July 1987

The government, still attempting to work within the framework of *concertación*, announced new restrictions for the national financial system on July 28, 1986, exactly one year after assuming power. These measures signalled a shift in policies towards the private sector. Until then, the relationship had been characterised by incentives policies in the hope that industrialists would voluntarily cooperate and respond. The second year, as typified by the decrees issued in July, entailed more forceful state intervention to stimulate investment. Proving to be overwhelmingly unpopular, these reforms appear in retrospect to be a last attempt by the government to collaborate with industrialists.

Forceful measures to contain capital flight and limit credit concentration were developed in July 1986. Limits were set on foreign exchange remittances abroad including private sector debt payments, interest, dividends, profits and royalties; while access to foreign exchange became even more tightly controlled. With the exception of small savings accounts under US\$1,000, all persons were legally obligated to maintain their resources in domestic currency. Further regulations were enacted to restrict the economic groups' access to credit, by setting limits on the amount of credit a borrower or groups of borrowers could receive. In a substantial move increasing state regulation, the Superintendencia de Banca y Seguros (SBS), furthermore, was given the discretionary power to establish financial management rules and force personnel dismissals.⁴⁶

These restrictions infuriated business leaders, who now felt the autonomy of private capital to be at risk. These measures exemplified the gradually hardening attitude of Garcia and his advisors, and they accordingly adopted a more forceful investment policy. According to the government, by the end of 1986, the optimum conditions for investment had been established. First, a mass market had been created with the ability for further expansion; second, the increase in

⁴⁶ See, for example, on the policies affecting the financial sector, *The Andean Report*, August 1986.

industrial production had absorbed much of the existing idle installed capacity; and third, surplus had been generated in the industrial sector which could finance the subsequent stages of investment and restructuring. The government, therefore, counted upon massive private sector investment in this period to begin a transition from a temporary consumer boom to medium-term industrial growth.

The government designated 1987 as 'the year of investment' and shifted to the more intense level of *concertación* with individual investor groups. This prompted the head of the National Planning Institute, Javier Tantalean to remark that, 'it is the first time the state is making certain demands for five year investment' (Tantalean 1986:293). In January of 1987, a National Investment Council was developed, with representatives from the private sector, labour and the state, to discuss and develop investment policies and priorities (Alva Castro 1987b:129).

In addition, major tax incentives were finally implemented which, unlike previous measures, were highly selective in nature. Priority industries in decentralised areas were entitled to up to 100 percent tax exonerations for seven years. Industries entitled to benefit from this legislation were those that were import substituting with emphasis on the production of capital goods, industries creating new technologies, labour intensive industries, value-added non-traditional exports, and agricultural and fish products for human consumption (Alva Castro 1987b:131).

The government then began its policy of selective *concertación* with the top economic groups. In July 1986, twelve top economic groups were chosen to have in-depth negotiations with the government. The 'twelve apostles', as they were quickly dubbed by the press, were composed of eleven top national economic groups; Romero, Raffo, Brescia, Nicolini, Olachea, Ferreyros, Lanatta-Piaggio, Bentin, Wiese, Cogorno, Picasso, and one foreign owned group, La Fabril.⁴⁷

⁴⁷ For a history of these economic groups, and detailed information regarding their economic interests, see chapter three.

These groups were chosen for their economic power and capacity to execute immediately any agreed investment projects. By the 1986 CADE, deals on specific projects had been made. Garcia announced that letters of intent amounting to over US\$100 million had already been received by key economic groups (IPAE 1986:340). Among the major projects agreed were large scale expansion of existing textile factories. La Fabril planned to double capacity with a US\$12 million investment, while the Romero group's Textile Piura planned to increase its capacity by 50 percent. The Brescia group proposed a new textile plant and cotton mills for processing.⁴⁸

The policy of selective *concertación*, however, angered many industrialists who felt excluded by the policy. More importantly, the selective *concertación* strategy had sidelined CONFIEP as the main channel of negotiation with the government. In disregarding existing industrial organisations and business associations in favour of a handful of businessmen, the government began to alienate the majority of industrialists. Many industrialists began to believe that this was a deliberate 'divide and conquer' tactic (Durand 1988:67).

In April 1987, the Garcia government adopted its most severe and aggressive stance on investment. Two investment funds were created, giving the entrepreneurs a tough option: companies could either invest in the Investment and Employment Fund (FIE) and receive government subsidies to do so, or they would be legally obligated to buy Treasury Bonds.

The FIE was created as a mechanism of project financing meant to develop the capital market by efficiently channelling funds to priority areas of the economy. Investors participating in this scheme would purchase deposit certificates from the government, would receive three bonds for every two purchased, thus receiving an immediate subsidy. These bonds were transferable in the stock exchange for selected priority investment projects. These funds would

⁴⁸ See, Doreen Gillespie, 'Survey of Peru: Big Investment Starts', *The Financial Times*, September 26, 1986.

then be channelled through the state entity, COFIDE (Financial Corporation for Development), to commercial banks to approved priority investment projects.⁴⁹ This subsidised investment programme was a breakthrough in the *concertación* process, until the initially popular programme was marred by a sudden decision to retain all funds in the Treasury instead of in commercial banks as originally planned. After protest by business leaders, the measure was quickly reversed. This erratic handling of the project caused a lack of confidence in the government, and investment began to taper off.

Shortly after the announcement of the FIE programme, Supreme Decree 085 was issued, requiring banks, insurance companies, financial corporations, drink, tobacco, textile, fish preserve and commerce companies to purchase Treasury bonds between 20 and 30 percent of 1986 gross profits. Two days later, Ministerial Resolution 115 reversed this, and allowed FIE certificates as alternatives to Treasury Bonds, for all companies except banks, financial and insurance companies.

This handling of the investment policy, both extremely aggressive and erratic, alienated potential investors. The government had, in effect, set down an ultimatum: either industrialists can invest voluntarily and receive subsidies through the FIE programme, or they must invest via treasury bonds. This stance, according to CONFIEP head Ricardo Vega Llona, was the 'death knell' of *concertación*.⁵⁰

The government made modest concessions, easing some exchange controls, for instance. But as Vega Llona aptly claimed, the death knell of *concertación* had rung. By this stage, the relationship was characterised more by conflict and confrontation than by cooperation. The primary concern of industrialists was now to retain their autonomy and protect their economic interests. For the government,

⁴⁹ See, for example, on the structure and functions of the FIE programme, Juan Alberto Campos Lama, 'El FIE: Factor de Desarrollo', *Actualidad Economica*, especial no 11, 1987.

⁵⁰ *Latin American Weekly Report*, April 23, 1987, p. 2.

however, the success of the economic model was at stake, as the failure of *concertación* dealt a devastating blow to the government's economic plans. Given these conditions, the appeal of extending state control over available credit grew. By expropriating the financial system, Garcia believed that the state could assume greater control of the investment process. On July 28, 1987, the government of Alan Garcia announced the expropriation of the Peruvian financial system. This move, the following chapter will argue, is a direct result of the failure of the investment/*concertación* policy. The expropriation marked the rejection of the heterodox model as originally conceived and the abandonment of the *concertación* policy. The government responded by expropriating the financial system to increase its ability to control and direct the investment policy and to attempt to salvage its economic strategy.

5.5 Limits to Private Sector Investment

According to President Garcia, much of the growth in private sector investment in this period was the result of small and medium producers reinvesting and expanding their enterprises, rather than the economic groups chosen to participate in the *concertación* process.⁵¹ The government argued that the economic groups, in particular, had taken advantage of both the consumer boom and the state subsidies on offer, but had invested relatively little and at the first signs of crisis, had begun to suspend investment plans and take their profits out of the country. State intervention was, therefore, needed to redirect profits towards the national economy.

Before considering in more detail the expropriation of the financial system, it is important to consider the reasons for this limited large scale investment. Is it evidence, as dependency theorists (and Garcia himself), might suggest, of a rentier bourgeoisie, out to reap profits at national expense and unwilling to invest domestically? Or was it simply the natural result of poor macroeconomic planning and management, which again failed to establish the degree of economic and policy stability necessary to induce long-term investment? This section will examine the factors which acted to slow investment. It will argue that the government failed to establish the conditions for investor stability; namely, confidence in the government and a stable policy regime. The logic of capital dictates that unless there is a reasonable expectation of future profitability, the withholding of investment will naturally result. In Peru, long-term investor stability has not existed, as a result of constant policy reversals and changing rules of the game, giving rise to capital flight and speculation.

5.5.a Economic Contradictions 1985-1987

The political relationship between industrialists and government, cannot be analyzed in isolation from the impact of economic policy. The response of

⁵¹ For the government's justification for the expropriation, see *Porque Se Nacionalisa el Sistema Financiera*, PAP (1987).

industrialists to government policy is directly shaped by the effect of policy on profit margins and the potential for accumulation. This section will show that while the heterodox strategy initially generated favourable conditions for the industrial sector, the failure to correct the distortions evident by the end of 1986 provoked foreign exchange shortages, credit scarcity and investor instability which definitively ended the possibility of sustaining this economic growth.

There is little doubt that the initial reactivation of the economy benefited producers. Manufacturers producing for the internal market, in particular, fared well, despite the government's firm control of prices. A study by the Ministry for Economy and Finances in 1988, supports this hypothesis, estimating that available surplus of the top one hundred companies in Peru, rose from 8.79 percent of gross income in 1985 to 11.92 percent in 1986 (MEF 1988).

Levels of investment in 1986 and 1987 show that a process of recovery was under way. In 1985, total investment was at 16.1 percent of GDP, and by 1987, this figure had risen to 22.7 percent (see Table 5.4). Despite this solid growth, total investment lagged behind the high levels which it reached during the upturn in the economy in the early 1980s. During the boom years of 1981 and 1982, the level of investment was at 32.6 percent and 30.2 percent of GDP respectively. However, when broken down to distinguish between public and private sector investment, the figures are more revealing. Private sector investment grew by 18.2 percent in 1986 and a further 26.9 percent in 1987 (see Table 5.5). While investment as a whole may have failed to reach the levels desired by the government, the evidence clearly illustrates that private sector investment was growing steadily.

Table 5.4 Investment as percentage of GDP 1980-1987

1980 - 28.3	1984 - 18.4
1981 - 32.6	1985 - 16.1
1982 - 30.2	1986 - 19.7
1983 - 21.4	1987 - 22.7

SOURCE: Instituto Nacional de Estadística. *Compendio Estadístico 1988*. 1989. p. 192.

Table 5.5 Gross Fixed Investment 1985-1987 (percentage growth)

	1985	1986	1987	1988
gross fixed investment	-15.7	2.6	14.6	14.2
public sector	-23.0	-10.7	-20.6	-18.0
private sector	-5.1	18.2	26.9	-13.4

SOURCE: Banco Central de Reservas del Perú. *Memoria*. 1986, 1988.

However, by 1987, a shortage of savings, credit and foreign exchange began to have an adverse impact on the private sector. The lack of government response to correct these distortions early on had two devastating results: it alienated industrialists, and provoked an economic crisis. Industrialists, sensitive to any signs of crisis, began to withdraw investment plans for investment and revert to speculative financial activities.

The economic contradictions of the strategy became apparent by mid-1986. First, although the drop in interest rates effectively contained production costs, it also made credit scarce. As interest rates were repeatedly lowered, they became negative in real terms and dropped to -22.5 percent in 1986.⁵² A significant decline in internal savings ensued. Although projected to increase to approximately 21.6 percent of GDP (INP 1987b:149), savings instead experienced

⁵² Calculated from monthly figures in INP (1987a:134).

a steady decline from 14.8 percent in 1985, to 10.8 percent in 1987 (BCR 1987:141).

This downward trend was exacerbated by reduced margins and declining availability of credit. The very narrow difference between active and passive rates, made bankers reluctant to assume the risk of loans.⁵³ In fact, the amount of credit the private sector received from the financial system declined by 5 percent in 1987 (BCR 1987:35).⁵⁴ The impact of the interest rate strategy which was designed to cheapen credit and increase investment, in the medium term acted to impede the continued growth of investment.

Second, the extension of price freezes began to squeeze profit margins in 1987. While the initial policies were successful in reining in soaring production costs, they were unable to keep costs under control in the long term. The final purchasing price of controlled goods, for example, were allowed to rise by an average of 74.2 percent in 1987, while the minimum wage during the same period was increased by 114.4 percent (BCR 1987:21). The costs of many imported goods also rose, as Garcia reduced the number of imports eligible to obtain the preferential MUC (Mercado Unico de Cambio) exchange rate.⁵⁵ The escalating costs of production, coupled with an insensitive price policy, began to exert some pressure upon profit margins. More seriously, it affected investor confidence.

⁵³ See, for example, *Latin American Weekly Report*, Special Report on Banking, December 1986.

⁵⁴ It is also important to note that the government required commercial banks to increase the amount of reserves held in the Central Reserve Bank. This had the effect of increasing the scarcity of credit.

⁵⁵ The MUC rate was applied for the import of priority products. This amounted to a real state subsidy for these imports.

Third, the export sector did not fare well with the heterodox policies.⁵⁶ This ambivalence about the promotion of exports was reflected in the continuous over-valuation of the inti to benefit importers. Although the strategy emphasised the expansion of the underdeveloped non-traditional export sector, through the establishment of a multi-tiered exchange rate system, increased tax reimbursements (CERTEX) and preferential credit lines for this sector, exports stagnated.

The differential exchange rate system which was developed attempted to reduce the cost of needed imports, while allowing for a slightly better rate for exporters, with an especially beneficial rate for priority non-traditional exports. The manipulation of the exchange rate favoured non-traditional exporters over traditional exporters. However, the rate system failed to compensate for the general overvaluation of the inti. Income from exports, both traditional and non-traditional, declined in 1985 by 5.8 percent and by 15.3 percent in 1986, although in 1987 there was a slight recovery (INP 1987a:116). This contraction was due to a combination of a decline in world prices for petroleum and other traditional exports in 1986, and a seriously overvalued inti. The recovery in 1987 was led by the non-traditional sector, which received a substantial devaluation of 33.3 percent over that of traditional exports (INE 1989:397-99).

The model was substantially biased against exports, allowing a cheap dollar in order to ensure a supply of imported inputs necessary for industrial reactivation. The worsening commercial balance in 1986, due to a 15.3 percent decline in export earnings and a 35 percent increase in the value of imports, showed clearly that the government's belief that its inward-looking strategy was compatible with its export promotion policy was mistaken (1987a:115). In attempting to reduce costs for production for the internal market, a marked anti-export bias emerged. The economic strategy drew heavily upon reserves and massively consumed

⁵⁶ Alva Castro claimed that the government planned to pursue an expansive adjustment of balance of payments based upon export growth combined with import substitution, rather than a recessive monetarist correction (Alva Castro 1987a).

imports without generating sufficient internal savings or foreign exchange to finance the investment phase. The strategy, by 1986, was not financially unsustainable. These distortions, which were evident by the end of 1986, were not corrected by the government's economic team, subsequently provoking a full blown economic crisis.⁵⁷

Fourth, as the government increased pressure for investment, it must be recalled that there existed a large degree of idle installed capacity in 1985 as a result of the industrial recession in 1983. Although the reactivation strategy did result in the absorption of a significant percentage of this capacity, at the end of 1986, there was still on average almost 30 percent idle capacity present (Thorp 1987c:15).

The continued existence of idle capacity meant that the private sector did not require immediate investment in order to continue to expand production. The criteria for a decision to invest in these circumstances, therefore, is the expectation of continued economic growth. The issue of confidence, in this context, becomes crucial. However, this conjunction of policies, (i.e., the overvaluation of the inti and the negative rates of interest), were conducive to increasing dollarisation of the economy and capital flight, as more attractive rates of return could be found abroad.⁵⁸ Industrialists were not convinced that this rate of economic growth could be sustained.

While the economic contradictions were important contributing factors to explain the slow growth in investment, there were other political factors which added to investor instability. Some, such as the growing international economic isolation, were the result of government policy. Other political factors, such as the upsurge in terrorist violence in the capital, were beyond the government's control. These factors will be briefly discussed below.

⁵⁷ For a critical discussion of the government's economic policy at this stage, see Thorp (1987c), published by the INP.

⁵⁸ The degree of capital flight in this period will be discussed in chapter six.

5.5.b Relationship with the International Economy

The inward-looking nature of the heterodox strategy, and Garcia's often antagonistic relationship with the international financial community and foreign capital, was a focus of concern by Peru's domestic industrialists. Industrialists questioned the feasibility of continued industrial growth in the context of declining foreign investment and limited external finance.

The foreign capital issue played an important role in industrialists' gradually disintegrating confidence in the Garcia government. President Garcia's first move against a foreign corporation came during his inaugural speech, in which he announced the rescission of the contracts of two foreign oil companies operating in Peru. Citing the failure of existing oil exploration contracts to establish proper tax obligations, the contracts of Belco and Occidental Petroleum were rescinded, pending renegotiation. Although Occidental eventually agreed to the new terms, Belco failed to renegotiate its contract, resulting in the takeover of its oilfield assets by the state enterprise, PetroPeru.

The following year, Garcia again acted against a foreign corporation. The President's Independence Day speech in 1986 announced the intervention of Leche Gloria in Arequipa, jointly owned by the Peruvian group, Berckemeyer and by the transnational corporation, Nestle.⁵⁹ Although the primary reason cited for the intervention was the monopoly Nestle held on canned milk, the government not only attempted to break Nestle's monopoly, but to promote a process of 'Peruvianisation' by mandating an increased percentage of national shareholders. Despite Nestle's actual monopoly, there existed a widespread perception that the anti-monopoly legislation was used as a justification for a populist attack on a foreign corporation.

Although the government's overall attitude towards foreign capital was less antagonistic or restrictive than many other nationalist-industrial models, its select

⁵⁹ On the Nestle takeover of Carnation shares in Leche Gloria, see Manuel Lajo, 'Monopolio Nestle-Berckemeyer va Ganando Este Round', in *Actualidad Economica*, July 1986.

attacks, such as these two expropriations within the first year, were sufficient to shake investor confidence. The policy of rescinding the existing oil contracts were particularly worrisome, and CONFIEP argued that any short-term benefits would be outweighed by the long-term investor instability that the move generated.⁶⁰ The suspension of the existing contracts by supreme decree was interpreted by industrialists as evidence of a disregard for private property rights, and pointed to the continuing fluctuation of terms for both foreign and domestic capital. More to the point, the state takeover of Belco signalled Garcia's willingness to resort to expropriation and to expand the public sector.

On a broader level, industrialists also displayed concern with Peru's increasingly isolated relationship with the international economy. While the declaration of Peru's ineligibility by the IMF was the most high-profile manifestation of this isolation, Garcia's policy of strictly controlling foreign exchange affected industrialists in a more direct fashion. Licenses were required for imports and access to foreign exchange, creating difficulties in importing intermediate and capital goods.⁶¹ In addition, the control on remittances abroad for private debt payments led to the suspension of credit links to privately owned Peruvian banks. The Banco de Credito, among other privately owned banks, became ineligible for export financing credit.⁶² These measures and circumstances contributed to industrialists' growing conviction that this isolationist stance would limit future growth in the medium term.

5.5.c Sendero Luminoso and the Industrial Sector

The growing lack of investor confidence was aggravated by another factor: the growing threat of terrorism. Both the government and industrialists were alarmed by the upsurge in terrorist activity in Lima in the mid-1980s. A common

⁶⁰ This point was expressed in a letter from CONFIEP president Julio Piccini to Alan Garcia in October 1985. See *Industria Peruana*, October 1985, p. 60.

⁶¹ See, for example, *Latin American Markets*, August 10, 1987, p. 12.

⁶² *Latin American Regional Report: Andean Group Report*, September 4, 1986. p. 7.

occurrence, directly affecting production, were repeated bombings of electrical pylons often requiring long periods of electricity rationing.⁶³ A growing number of bombing attacks, furthermore, were directed at private sector targets, including factories, mines, transport trucks and banks. The mining sector was particularly at risk, based in vulnerable rural areas.⁶⁴

A more widespread problem was the demand by terrorists for 'cupo' or protection money. Although most industrialists publicly denied acquiescing to such demands, a considerable number of businesses were forced to make regular and sizable payments to members of Sendero Luminoso. Gabriel Ferrer, former vice-president of the SNI, admitted that many businesses pay between £10,000 and £25,000 per month to Sendero for protection (Strong 1992:202). In addition, Sendero made its presence felt in the industrial sector by infiltrating existing labour unions, with varying degrees of success.⁶⁵

More alarming was the increase in personal attacks on prominent industrialists. The director of the Industrial Bank, Admiral Brescia Cafferata, was assassinated in 1986,⁶⁶ while a member of the Romero group, was kidnapped and held for months.⁶⁷ Security issues formed a considerable part of industrial concerns. The widespread atmosphere of growing political instability, further compounded by labour strikes, led many to withhold investment plans. A banker

⁶³ In 1985, 107 electrical pylons were bombed. In 1986 and 1987, this figure dropped to 31 and 67 respectively. However, the number of attacks increased to 137 in 1988 and 276 in 1989. It is estimated that in 1989, the opportunity costs caused by 62 days without electricity amounted to US\$520,232 (Webb and Fernandez Baca 1991:355-56).

⁶⁴ Strong claims that the state mining firm CENTROMIN lost £58.8 million due to sabotage alone (1992:200).

⁶⁵ For a case study of Sendero Luminoso's action in the Ate Vitarte section of Lima, see Smith (1992).

⁶⁶ Although the Industrial Bank is a public sector entity, Admiral Brescia was from the prominent Brescia economic group.

⁶⁷ It is unlikely that the kidnapping of Jose Antonio Onrubia Romero was conducted by Sendero, whose methods generally include assassination, not kidnapping. Nevertheless, this contributed to the increasing anxiety among industrialists.

told the *Latin America Regional Report* in June 1986 that the growth of terrorism was a more important factor than diminishing confidence in the government to explain the hesitancy in investment.⁶⁸

The unprecedented growth of violence in Lima, much of it directed against industry, created a further disincentive for reinvestment within productive facilities in Peru. Sendero was one of many destabilising factors in the economic and political system. Growing government regulation, on the one hand, and intensifying social conflict and labour unrest on the other, added to a profound sense of investor instability. Given these factors, the limited growth of investment and upsurge in capital flight is more easily understood.

⁶⁸ See *Latin American Regional Report: Andean Group Report*, June 26, 1986. p. 5.

5.6 Concertación?

The expropriation of the financial system marked the abandonment of the *concertación* policy. The relationship, by this stage, had deteriorated to the point where differences were barely disguised by the *concertación* rhetoric and framework. Garcia believed that the economic groups and other large scale industrial groups, although having benefited from the development model, had failed to reinvest their profits. Meanwhile, industrialists grew increasingly wary of the increasing government intervention in the economy.

The end of the *concertación* framework meant the end of the heterodox model as originally conceived. The promotion of private sector investment, and the incentives policy to influence investment and restructure the economy, had been the foundation of the heterodox strategy. The Garcia government's realisation that investment patterns could not be transformed in the short term, illustrates a basic weakness of its development model, and a basic misunderstanding of the economic and political factors which influence private sector investment.

This chapter has examined the conflicts which emerged between the state and industrialists prior to the expropriation. Despite these conflicts (which admittedly were of some intensity at times), and the growing evidence of the statist nature of the Garcia government, industrialists did not actively oppose the reformist model until mid-1987 when direct threats to private property emerged. Why was this redistributive model supported?

First, we have seen that the magnitude of the economic crisis under the Belaunde regime unquestionably shook the industrialists' conviction in the neo-liberal approach to economic management. Although the interventionist measures that were part of the heterodox option were obvious irritants to industrialists, they were perceived by most as necessary to reactivate the stagnant economy. This

view was most clearly expressed by Carlos Verme Katz, a former president of the SNI, in an interview in *Industria Peruana*:

I must admit that the political economy of the country was so out of balance, that I believe, despite not sympathising with controls, that they were necessary, but only when they are not permanent. ⁶⁹

These measures were received, as former president of the SNI, Antonio Aguirre Roca stated, with 'stoicism' by the industrial sector, in the hope that these policies would succeed in the crucial tasks of stabilising the economy, reducing speculation and inflation (Aguirre Roca 1985:246). As a result of the severe industrial recession provoked by the liberalisation of the economy in the early 1980's, therefore, the Peruvian industrialists were, in 1985, supportive of a policy based on strong state macroeconomic control.

Second, I would argue that Conaghan (1988) correctly links the acceptance of reform to the need for an expanded internal market. Most Peruvian industrialists, as a result of the industrial recession in 1983, had become acutely aware of the limitations imposed upon industrial growth by the restricted domestic market for manufactured goods. During the first two years of the Garcia administration, the rapid expansion of the domestic market resulted in an massive increase in sales for the industrial sector, thereby legitimising the heterodox approach. In this case, increased capital accumulation undoubtedly was the primary factor accounting for the continued support of industrialists.

However, this support gradually eroded as the Garcia government proceeded to implement long-term and vigorous economic. The extremely strict control of foreign exchange in particular, impeded production, while price controls were repeatedly extended. While industrialists may have accepted these controls as part of the temporary emergency programme, they were unwilling to accept them as part of a long-term economic strategy.

⁶⁹ *Industria Peruana*, February-March, 1986, p. 4.

This chapter has argued that support of industrialists gave the Garcia administration an increased margin for manoeuvre, enabling the government to implement its fundamentally populist policies with multi-class support. This chapter has also suggested that the industrial bourgeoisie's final rejection of heterodox model was more due to the inflexible implementation of many of these populist policies, than the statist essence of the model itself. As Garcia pursued policies such as the harsh labour stability or anti-monopoly legislation, measures which were blatantly anti-business and not essential to the economic strategy, the private sector's doubts grew about the value of *concertación*. As was shown in the first section, the *concertación* policy appealed to industrialists who felt that it would enable them to influence policy making to minimise or weaken potentially threatening policies. As the relationship progressed, however, industrialists became increasingly apprehensive as it became evident that the government was not willing to compromise on any issues.

The forcefulness with which the Garcia government pursued policies which were contrary to the interests of industrialists, raises a fundamental question. What was the true class orientation of the heterodox model? Although the stated objective of the Garcia government was to pursue an alliance with industrialists, in fact the government acted with considerable autonomy from it. The following section will consider the pressures on the Garcia government from the popular and working classes, and will examine the class orientation of the heterodox model.

5.6.a Class Alliances and the Heterodox Model

The implementation of the heterodox model required the formation of a complex web of class alliances, without which the economic success of the model would be seriously jeopardised. Projecting both strong alliances with industrialists and the urban working class, the contradictory policies which ensued served to alienate both industrialists and labour, hastening the downfall of the model itself. In the Garcia government's pursuit to retain the support of the working classes, it failed to understand the depth of its dependence upon continued private

investment. These proposed class alliances, which Garcia was unable to reconcile, illustrate an essential contradiction of the heterodox model.

The Garcia government's explicit objectives were to establish close alliances with the working class and with the industrial bourgeoisie. However, even a cursory look beyond the government's statements, reveals a clear bias in favour of the urban working classes, and to a lesser extent, the rural population, largely at the expense of the industrial bourgeoisie. A central objective of the heterodox model was to redistribute income from the top 10 percent of the population which controls 52 percent of wealth, to the deprived urban and rural sectors (INP 1987b:29). The model could therefore be defined as being essentially populist: a non-revolutionary approach appealing to, and designed to benefit the masses, with particular emphasis upon the urban working class. It is evident in this case that, while the subordinate classes were the intended beneficiaries, there was no intention of transforming the existing class structure.

The intended class orientation of the model, therefore, favoured the urban working class, not surprisingly APRA's main base of support. The issue that requires clarification, therefore, is the nature of the proposed alliance between the state and industrial bourgeoisie in the heterodox model.

The Garcia government had envisaged an important role for domestic private capital in its economic model. Through an alliance with industrialists, the government expected to exact investment commitments in priority areas, to restructure the economy. It was in essence, a modified trickle down theory: through strict government regulation of prices, wages and other variables to maximise benefits to workers and consumers, the reactivation of the economy and the increase in production would promote a generalised level of prosperity. The alliance with industrialists, therefore, was the means by which the government would implement policies which would ultimately favour the working and peasant classes, rather than an end in itself.

This is an important distinction. Whereas the industrial bourgeoisie saw the alliance as an opportunity to influence policy making for its own benefit, the government's ultimate purpose for developing the *concertación* policy was not to establish a mechanism to ensure that the interests of industrialists would be protected. The interests of capital in the model were considered only insofar as ensuring a degree of profitability to entice investment.

That the interests of the industrial bourgeoisie were deemed secondary, at best, illustrates a dilemma in the application of such a model. The model's dependence upon maintaining the support of the industrial bourgeoisie for its success, to some extent requires the government to protect the interests of capital. In developing this model, the Garcia government placed serious limitations upon its ability to act with autonomy from the industrial bourgeoisie. However, as the remainder of this section will show, in its defence of the working class, it in fact attempted to act with considerable autonomy from it.

5.6.b State, Labour and Private Sector in the Heterodox Model

It is difficult to characterise succinctly the nature of the labour's relationship with the government. Although the unions initially supported the Garcia government and were the beneficiaries of policies to increase income and strengthen labour rights, their relationship with the state, became increasingly strained, ultimately becoming antagonistic. A study by Balbi (1988) concludes that a major element in the conflict between state and labour pertained largely to the government's failure to grant labour leaders repeated requests for dialogue and increased participation in the *concertación* process. It is apparent that the government's mixed signals and confused class alliances played a significant role in the alienation of the working classes. Balbi argues that,

the lack of transparency of the government's objectives and goals have not enabled unions to evaluate the advantages and benefits which the reactivation brought (Balbi 1988:66).

Paradoxically, then, the labour stability legislation, which strengthened indemnity rights as well as guaranteeing stability, won Garcia little support from

organised labour, which argued that PROEM allowed employers to by-pass the stability legislation.⁷⁰ Organised labour also felt alienated by the government's focus on establishing programmes targeted at the urban poor and informal sector. The PAIT programme for temporary employment and the IDESI programme of credit for the informal sector, were the clearest indications of Garcia's central concern with the unemployed and underemployed. Garcia, furthermore, angered union leaders by claiming that organised labour was 'privileged' (Graham 1992:107).

One useful indicator to evaluate the class character of the heterodox model is the relative increases in income. The objective of raising income was initially effective, with real incomes rising on average 16 percent in 1986 (see Table 5.6). Independents, (i.e., agricultural producers and the informal sector), experienced the largest increase, showing an average increase in income of 33 percent. Agricultural producers benefited from a deliberate shift in relative prices to address the terms of trade between urban and rural areas. In the period from July 1985 to December 1986, the price of agricultural products grew 146.9 percent, in sharp contrast to the price of manufactured goods which grew a mere 23.8 percent (Leon and Paredes 1988:22). The urban informal sector also received support, through programmes of soft loans and technical assistance through IDESI. This sector also had the advantage of falling outside of the price control regulatory system, thereby allowing informal producers more flexibility in establishing final prices than most formal producers.

It is important to note the structure of income induced by the heterodox policies. Independents, agricultural producers and informal sector, benefited most. While the working class did not fare quite as well, it can be seen that average wages grew at a much higher rate than did profit margins for producers. Private sector employees received a 24 percent increase, while public sector employees received a 13 percent increase. In contrast, property owners experienced a more

⁷⁰ PROEM enabled enterprises to take on temporary staff without labour stability.

modest 8 percent increase in income. These results match the proposals of the heterodox model, by favouring the urban working classes and rural producers, while containing the profit margins of industrialists.

Table 5.6 Growth of Real Income 1986 (percentage change)

Average	16
waged	17
private sector	24
public sector	13
independents	33
agricultural	30
non-agricultural	35
property owners	8

SOURCE: Instituto Nacional de Planificacion, 1987a. *Evaluacion del Plan del Corto Plazo 1986*. p. 138.

Furthermore, as was suggested in the preceding section, the government remained responsive to the interests of the working class, if perhaps not so conspicuously to its articulated demands. The government tended to perceive many domestic policy issues in terms of two contrasting interests, that of consumer-producer and labour-employer, in most cases coming down on the side of consumers and workers. In doing so, as many industrialists noted, the economy strategy developed a marked 'anti-empresarial' or anti-business tone.

This can be illustrated clearly by recalling many of the issues which angered industrialists. The adverse reaction to the tax policies, for example, was not the result of the increased economic cost of the measure to producers, but was a response to their perception that increased taxes were levied upon producers, who already shouldered a disproportionate share of the tax burden, without a corresponding effort to expand the tax base. Similarly, the policy of long-term, strict price controls protected the purchasing power of the general population, at

the expense of profit margins. In addition, the rising costs of labour could not be reflected in higher consumer prices.

The balance between labour and employer was almost as clearly drawn. The main thrust of labour policy was to increase employment through a generalised increase in the utilisation of idle capacity, and by programmes such as CERTEM, PAIT, and PROEM. Despite this, minor concessions to the industrial sector such as PROEM, which allowed temporary personnel to be hired without stability rights, angered union leaders, despite the fact that the primary objective of the programme was to increase employment opportunities. Furthermore, with the exception of PROEM, labour rights were considerably strengthened through the comprehensive labour stability legislation. Certainly, too, the government's wage policy was designed to benefit workers, again at the expense of employers.

The Garcia government failed to establish a close relationship with unionised labour, which complained that the government was primarily interested in *concertación* with the industrial sector. Leading labour leaders had become resentful of the president's appearances at CADE, the selective *concertación* policy with the '12 apostles', and the rhetoric *concertación* which surrounded it. Balbi's study based on interviews with labour leaders, showed that there existed a high degree of resentment of the apparent closeness between the economic team and the industrial sector. This was a significant contributing factor to the antagonistic nature of the state-labour relations during this period (Balbi 1987:79).

It is paradoxical, therefore, that the working class became disillusioned with the Garcia government because of the lack of dialogue and access to policy makers, even though the government was responsive to its interests. Conversely, industrialists became alienated because, although they had access to government, their interests were not defended. It had become clear to the industrialists that *concertación* existed in name only, and despite the existence of forums for debates, its ability to influence policy was minimal. As influential business leader, Juan Antonio Aguirre Roca succinctly summed up about the relationship with the

state, 'there is an excess of conversation, but there is not *concertación*. Other interests are more important'.⁷¹

⁷¹ *Industria Peruana*, November 1985, p. 6.

5.7 Conclusions

Is there a contradiction in a fundamentally populist model depending upon the rapid growth of private sector investment for its success? It is undeniable that the balancing of interests in such a strategy model would prove to be an inordinately difficult task. In this case, however, as the first section established, the Garcia government had a definite advantage in having the support of industrialists for this reformist and redistributive type of model. The industrial bourgeoisie at this time was one which was unusually tolerant of regulation, giving the Garcia government a greater margin for error. Despite this, the government failed to achieve the delicate balance of interests which may have prevented outright confrontation with industrialists. The actions of the government revealed that the interests of industrialists were subordinate to other class interests, as its policies often trod on the rights of private property.

The effect of this realisation on business confidence was further exacerbated by the raised expectations generated by the rhetoric of *concertación* and power sharing. *Concertación* quickly proved to be more rhetoric than reality and industrialists grew fearful of their inability to have any impact on policy. The instability generated, therefore, by the Garcia government's increasing interventionism and constantly evolving rules of the game, resulted in investment withholding, and the failure of the emergency programme to generate long-term growth. This suggests that *concertación*, in fact, had different meanings for industrialists as it did to the government. While industrialists has aspired for its to become a means by which their input into the economic policy making process could be increased, for the government, this was essentially a tactical political alliance designed to contribute to business confidence.

One possible interpretation of these events is simply that the government's policies were too ambitious, attempting to please both labour and industrialists, as well as agricultural producers and independents. The confused class alliances resulted in contradictory policies which prevented the Garcia government from

establishing close ties with either sector. A second possible interpretation is that the *concertación* policy was purely an attempt to make APRA's reformist policies more palatable to industrialists, many of which have traditionally opposed APRA. A political alliance with the industrial bourgeoisie was proposed to achieve the economic objectives of the model, although the characteristics of the model were at odds with industrialists (i.e., the statist essence of the model, and its class orientation) and precluded an alliance.

In either case, Garcia found the *concertación* policy difficult to reconcile with the reformist and redistributive objectives of the model. While the heterodox approach in theory emphasised the need to maintain business confidence and ensure adequate rates of return for domestic capital, the Garcia government was unwilling or unable to do so in practice. The government's concern for maximising benefits for workers meant that redistributive policies received priority over policies which would have maintained business confidence. The government ultimately sacrificed long-term investor stability for short-term political gains, by pushing ahead with non-essential populist policies. The continued support by industrialists for the reformist programme until 1987, and the gradually growing rates of private sector investment, suggest that the objective of a generalised rise in incomes was not necessarily incompatible with continued investment.

The Garcia government's alienation from all sectors of the society increased as the economic boom reached its limits and inflation began to gather force. The following chapter will illustrate that as a response to this declining popularity and confused class alliances, the government attempted rejected the *concertación* strategy and announced the expropriation of the financial system. This measure was, in part, an attempt to gain a greater degree of autonomy from the bourgeoisie, therefore enabling it to deepen its reforms. While in the first two years of the Garcia administration, the government attempted to co-opt and court the industrial sector in order to achieve a degree of influence over investment decisions, through the expropriation, Garcia attempted to use force and coercion to achieve the same objectives. The following chapter will examine the political and

economic concerns which contributed to Garcia's decision to expropriate the financial system.

CHAPTER SIX

THE EXPROPRIATION OF THE PERUVIAN FINANCIAL SYSTEM: POPULISM REVIVED

Introduction

At the 1984 Annual Conference of Executives (CADE), the President of the Banco Mercantil, Francisco Pardo Mesones, asked a question of Presidential candidate Alan Garcia: 'Are you going to nationalise insurance companies and banks? Yes or no?' To which Garcia replied, 'No...we will not nationalise' (IPAE 1984b:273-74). Less than three years later, Francisco Pardo Mesones, leader of the Association of Peruvian Banks (ABP), was leading an active opposition to President Garcia's attempted expropriation of the Peruvian financial system.¹

Alan Garcia's sudden announcement that the state would assume control over Peru's private banks, financial corporations, and insurance companies, shattered the relative calm of his first two years in office. Proving to be highly unpopular, it marked the beginning of a profound crisis from which the Garcia government never recovered. Although it was not the sole cause, it accelerated the social conflict, economic crisis and mounting opposition which characterised Garcia's last three years in office. The expropriation policy, designed in part to allow Garcia to regain the political initiative and recover declining popularity, backfired. The decree was finally repealed after widespread opposition meant that it was not politically viable.

The sudden decision to expropriate was sudden and unexpected. Until mid-1987, the relationship between the government and industrialists remained cordial, with in-depth government negotiations underway with investors. Letters of intent

¹ The Association of Peruvian Banks (ABP) is a member organisation of CONFIEP.

had been negotiated between many top economic groups, including the Romero, Raffo and Ferreyro groups, for the development of large scale industrial investment projects. Thus, the expropriation was even more startling in that it targeted the very economic groups which with the government had sought to co-opt. What, then, contributed to this abrupt reversal of tactic, from wooing potential investors to expropriating nationally owned private property?

There were pressing concerns on both the political and economic fronts which led policy makers to consider such a dramatic change in policy. First, as suggested above, the measure was an attempt by Garcia to revive his declining popularity by generating renewed support with impassioned populist and anti-oligarchic rhetoric. Secondly, mounting inflation, declining reserves and a growing gap in the commercial balance, all signalled the exhaustion of the heterodox policies and provided evidence of an overheated economy and impending economic difficulties. According to the government, however, much of the growing crisis was the result of low levels of industrial investment and a sudden upsurge in capital flight, primarily by the economic groups which also owned much of the financial (PAP 1987). By extending state control over the financial system, policy makers believed that the government could induce further investment and sustain the growth of the economy. In this context, the expropriation measure can also be seen as the government's final attempt to salvage its heterodox economic strategy, which by this point was showing signs of weakness, as well as renewing the underlying political support necessary to sustain the model.

The obvious and short-term political gains which Garcia attempted to achieve with this policy, however, have led most analysts to underplay the long-term objectives of the expropriation.² *The Financial Times*, for example, stated that the move was 'best interpreted as another of President Garcia's colourful

² One exception is Crabtree (1992), who acknowledges the long-term economic objectives the government held with regard to the financial system.

gestures designed to bolster his domestic political situation.’³ Similarly, Rudolph (1992) argues that the expropriation was Garcia’s response to growing opposition within his own party, in particular, from his ex-Finance Minister, Luis Alva Castro. Although immediate political and economic concerns were important to Garcia, this chapter will offer evidence to show that the expropriation was a genuine attempt to enact deeper, structural reforms in the allocation of resources. The measure aimed to redress certain structural disequilibria in the Peruvian financial system through a fundamental reform of its ownership structure. The control over credit by a small, elite group, the economic groups, which has the ability to channel it to related companies at the expense of smaller and growing industries, was perceived as an obstacle to industrial restructuring along the lines proposed by the heterodox economists.⁴ The government attempted to create the conditions for industrial restructuring and growth by breaking the power of the economic groups and increasing the flow of credit to subordinate fractions of the bourgeoisie.

This preoccupation over the excessive concentration of credit was evident throughout the first two years of the APRA government, as various policies were implemented in 1985 and 1986 to initiate a process of the deconcentration and regional decentralisation of access to credit. In fact, this theme had been developed as early as 1982 in Garcia’s book, *A Different Future*, written when Garcia led the APRA party’s National Commission of Ideology and Doctrine. In this book, and in speeches throughout 1987, Garcia discussed the need to reduce the power of the bourgeoisie to address the unequal distribution of wealth in Peru. The expropriation of the financial system in this context, it will be argued, was perceived by the government as a necessary step to free itself from the constraints imposed by the *concertación* policy and to enhance its ability to enact deeper reforms.

³ ‘Peru Retreats into Populism’, *The Financial Times*, July 30, 1987.

⁴ For a discussion of the structure of the economic groups, and their ability to perform capital market functions, see chapter three.

The political and economic objectives of the expropriation are deeply entwined. This chapter will attempt to shed light on the reasons behind the government's decision to expropriate the financial system. The first section will examine the political events which triggered the policy, while the second will examine the move in the context of the government's industrial restructuring plans.

6.1 Populism Revived

In mid-1987 the effects of the expansionist, demand boosting policies applied since 1985 were still being felt: the economy was growing and consumer consumption remained high. However, inflation was beginning to gather force and evidence was emerging that the expansion of the economy may be reaching its limit. It was, of course, the 'year of investment', which foresaw a surge of private investment in manufacturing and industry to offset inflationary bottlenecks. The disappointing result of the investment policy threatened the future of the government's economic plans and forced a reevaluation of existing policy.

A sense of growing political crisis also existed. Garcia's overall popularity, although still high, had been slowly declining as a result of the first signs of inflation. His popularity was further damaged as the first signs of internal conflict and dissent within the inner policy making circle of the government became public. His approval rating of 78 percent at the end of 1986, showed a gradual decrease, reaching a new low of 59.4 percent in May 1987.⁵ Finance Minister Luis Alva Castro, who had played a leading role in economic policy making since 1985, was at odds with the more radical ministers and advisors within the economic team and resigned in June 1987. This was, in part, a well-timed move by Alva Castro designed to ensure that he left office with an unblemished record of economic management to aid his quest for the 1990 APRA candidacy. President Garcia was politically damaged by these intra-party divisions, as his ex-Finance Minister turned rival was elected president of the chamber of deputies in July 1987, and subsequently Secretary General of the APRA party, against Garcia's wishes.⁶

The subsequent resignation of the cabinet, which is standard protocol after the Prime Minister resigns, prompted personnel changes which allowed Garcia to

⁵ DATUM poll results, *The Peru Report*, vol. 2, no.1. January 1988, 7-3.

⁶ Alva Castro was elected Secretary General of the APRA party in 1988, with the vote of Apristas which had become disillusioned with Garcia's autocratic ruling style.

close ranks with like-minded policy makers. Alva Castro was replaced by his vice-minister Gustavo Saberbein, and Leonel Figueroa, who had some substantive disagreements with President Garcia over economic policy was removed from his position as Central Bank president. Figueroa was replaced by Pedro Coronado in August, with Cesar Ferrari, a prominent, radical heterodox economist, assuming the position of general manager. The more radical policy makers, including Daniel Carbonetto, influential presidential advisor; Cesar Ferrari, Manager of the Central Bank; Javier Tantalean, head of the National Planning Institute; and Gustavo Saberbein, Minister of the Economy; known publicly as Los Audaces (The Bold Ones), now dominated economic policy.⁷

This period of transition, just one month before the bank decision, allowed Garcia to recruit like-minded advisors and cabinet members, and strengthen his position vis-à-vis the growing internal opposition led by Alva Castro. These personnel changes in June 1987 foreshadow the events to follow by indicating a fundamental political realignment. The shift in the make-up of the policy making team reflected a decision to deepen, rather than soften, the heterodox approach to economic policy. That same month, interest rates were once again lowered, devaluations made to promote exports, wages increased, and price freezes extended. It is evident that at this stage, rather than reverse to tactics and retreat to orthodoxy, the Bold Ones planned to pursue their vision of heterodoxy and extend the regulation of the economy.

The development of the expropriation policy began in virtual secrecy at this stage. It was a decision made by Garcia and planned with his closest advisors and selected ministers.⁸ According to the then-Minister of Industry, Manuel Romero Caro, the expropriation plan was never discussed at full cabinet meetings, but

⁷ *Latin American Weekly Report*, July 2, 1987, p. 1.

⁸ According to *Caretas*, the advisors involved in the expropriation plan were Carlos Franco, Javier Tantalean, Cesar Ferrari and Daniel Carbonetto. August 3, 1987. p.13-4. With the exception of Tantalean, these advisors were all affiliated with the Velasquista CEDEP think tank.

worked on privately between Garcia and his most trusted advisors.⁹ Most of the APRA party members, senators and deputies, became aware of the policy only as it was announced to the Congress on July 28, 1987, during the president's annual televised Independence Day speech. Citing a lack of investment and the concentration of wealth and power, Garcia announced the immediate state takeover of all domestically owned banks, insurance companies and financial corporations.

With impassioned rhetoric, Garcia attempted to engage the population by casting the nationalisation debate in terms of a struggle of rich versus poor.¹⁰ The concentration of wealth and power in the financial system, he argued, are mechanisms of 'power which are incompatible with social justice'.¹¹ With the nationalisation of the banks, Garcia repeatedly said, a democratic 'revolution' would begin'.¹²

The rhetoric was meant to appeal to the popular sectors as the government attempted to reestablish and reaffirm its reformist position. Concerned about popular perception of the *concertación* strategy, which alienated much of the working class, the government chose to abandon its wavering centrist position in favour of a more marked leftist approach. As advisor Daniel Carbonetto explained, 'we had to establish APRA's clear centre-left option.'¹³ In order to do so, the government ended the high profile policy of *concertación* and with it, the public perception of an alliance with Peru's leading businessmen.

Mario Varga Llosa, prominent writer and Peruvian intellectual who emerged to lead the opposition to the expropriation explained the logic behind the

⁹ Interview, Manuel Romero Caro, (Minister of Industry 1985-87), March 25, 1992, Lima.

¹⁰ Furthermore, claimed a presidential advisor, 'It's good for the poor to see that the rich also have something to cry over'. *Latin American Weekly Report*, August 13, 1987, p. 8.

¹¹ The text of Garcia's speech can be found in Calle (1987).

¹² See, for example, Robert Seavey, 'Background Report on Peruvian President Garcia's Intention to Nationalize the Banks', *Associated Press*, September 1, 1987.

¹³ *Latin American Weekly Report*, August 13, 1987, p. 8.

measure and its potential appeal:

No one likes bankers. They symbolise affluence, selfish capitalism, imperialism, all causes of Third World wretchedness and backwardness. Alan Garcia has found, in financiers, the ideal scapegoat for the failure of his programmes: the financial oligarchies had removed their dollars from Peru and made secret loans out of the savings accounts of others to their own companies. With the financial system in the hands of the people, everything would change (Vargas Llosa 1991:22).

The symbolism of the *concertación* policy had been heightened by the exclusive focus on Peru's top industrial and financial families, dubbed by the press as 'the twelve apostles', rather than more broadly negotiating with industrialists through CONFIEP or the SNI. This created an image of a government overly concerned with business profits - an image which was disturbing to Garcia and many of his advisors. This concern was evident in Garcia's announcement of the expropriation in which he claimed that, 'dissatisfaction grows among the people who see how the economic model can be perverted to benefit a small group of privileged people.'¹⁴ Garcia evidently hoped that the nationalisation would enable him to demonstrate the reformist nature of this government, thereby counteracting the perception that economic policy was designed solely to benefit industrialists.

The high profile policy of *concertación* was also disturbing to the government's ideologues, who found it difficult to justify the fact that Peru's wealthiest families were receiving preferential treatment while reaping huge profits. It appeared not as an economic necessity - the economy was booming - but as an inequitable policy serving to increase the already soaring profits of the private sector. One of Garcia's influential advisors, Carlos Franco of the CEDEP Velasquista think tank, who is widely believed to have been a foremost proponent of the expropriation plan, argued that the heterodox approach was contradictory, in that it depended economically upon an alliance with industrialists; an alliance which was incompatible with the government's political orientation. He wrote in

¹⁴ BBC Monitoring Service, *Summary of World Broadcasts*, July 30 1987.

1987:

concertación with all the economic agents, economic, social and political, which characterises the original plan, gave way to exclusive *concertación* with large private capital. This meant the conceptualisation of the heterodox approach as an 'economic model', distinct from, although complementary to, the 'political model'. ... this economic model supposed, expressed, or implied an 'inherent political model', based in the maintenance of the unequal structure of national power and precluded any alternative of structural change. What happened next is well known history (Franco 1987:19).

The expropriation policy, as this view suggests, indicates an attempt by the government not only to distance itself publicly from industrialists to regain popular support, but also to give the government a greater degree of autonomy not just from the industrial bourgeoisie, but also the bourgeoisie as a whole, in order to enable it to deepen its structural reforms.

The expropriation must therefore be seen in light of the reformist orientation of the heterodox model and its broader social objectives. The ideological emphasis underlying these economic policies was on breaking down the structural barriers to equity and on promoting a less hierarchical and concentrated power structure by incorporating previously marginalised sectors of the population into the economy and society through the intersectoral transfer of resources.¹⁵ These goals presupposes a class character which contradict the orientation of the investment policy which in practice favoured industrialists. As Franco's statement above suggests, the heterodox theorists were coming to the conclusion that this policy of investment would reinforce, rather than transform, the structure of the production and ownership. Garcia also believed that *concertación* was incompatible the government's vision of reform. During an interview with *The Peru Report*, Garcia said that the expropriation was due to the realisation that, 'Peru was growing, but with the same structures, the same injustices. The country has to change' (The Peru Report 1987:6).

¹⁵ The objectives of the heterodox strategy, and its long-term goals of redistributing income are discussed more fully in chapter four.

This measure can also be interpreted as an attempt by the government reaffirm the class character of the government. As argued in the previous chapter, during the first two years, the Garcia government had attempted to develop policies which would gain the support of both the working class and industrial bourgeoisie. However, the contradictory policies which ensued had failed to gain the confidence of either group. The expropriation, in contrast, marked a rejection of the original proposal of a multi-class coalition and reflected a clear decision by the government to gain greater autonomy for itself vis-à-vis the bourgeoisie, in view of the looming economic problems and declining popular support for the government. As the economy slowed and stagnation threatened, Garcia attempted to regain the wavering support of the population by demonstrating that his government would no longer favour big business. The government also was facing strong criticism from parties on both the left and right as a result of this centrist position. This move, government advisors believed, would enable Garcia to regain the support of the disillusioned left, which felt that the reforms were not deep enough.¹⁶

The expropriation of the financial sector was a bold political manoeuvre designed to allow Garcia to regain the political initiative by showing a renewed energy and focus to policy. This move was consistent with Garcia's governing style, characterised by brash populist gestures, such as the defiant debt stand, which contributed to an image of Garcia as a charismatic, strong leader. This time, however, Garcia's aggressive gamble failed to pay off.

With hindsight, it is easy to suggest that this measure was a result of political misjudgment and government isolation, which should have been avoided. Yet, this bold populist approach had won Garcia much popularity in the past. For example, the government's debt policy had earned widespread public support, even

¹⁶ See, for example, the *Latin American Weekly Report* which argued that the main purpose of the expropriation was to 'take the government and ruling APRA party out of the isolation into which they had fallen following criticism by Left and Right.' August 13, 1987, p. 8. Graham further argues that the Garcia government felt that the expropriation could enable APRA to renew its links with the United Left coalition (1992:115).

when Peru was declared ineligible by the IMF in August 1986. In that case, the popular sectors of society responded to Garcia's carefully crafted nationalistic rhetoric. It is evident that Garcia believed that this approach would enable him to marshal popular support once again, this time by replacing the anti-imperialist message with imagery of class struggle and promises of the redistribution of wealth and power.¹⁷

The precedent set in Mexico might also have influenced Garcia.¹⁸ The government of Lopez Portillo nationalised the Mexican banking system in September 1982. While this had provoked widespread debate and considerable opposition from the Mexican bourgeoisie, the policy had nonetheless won the support of many sectors of the population.¹⁹ According to Basanez (1990), the nationalisation of the banks in Mexico served to legitimise the state to the popular sectors which were becoming discontented with the government. According to a poll conducted in Mexico in 1982, 71 percent of the respondents were in favour of the measure.²⁰

In Peru, as well, in the immediate aftermath of the surprise announcement, a preliminary poll showed that 51 percent of the population supported the measure.²¹ Initially, many important sectors of society as well came out in support of the proposal, including the trade union confederation, the CGTP, and the Confederation of Bank Employees.²² In addition, the influential head of the

¹⁷ Even Mario Vargas Llosa, who led the opposition to the expropriation later claimed that when he first heard of the measure, he assumed that the Peruvian population would respond positively to this anti-oligarchic rhetoric (Vargas Llosa 1991).

¹⁸ The influence of the Mexican experience on Garcia was suggested by Sergio Armiento, 'Mexico's Phantom Bankers come Out of the Shadows', *Wall Street Journal*, August 7, 1987.

¹⁹ For a class analysis of the Mexican Bank nationalisation, see White (1992). For a more economic approach, see Stewart (1985).

²⁰ Basanez (1990:233-35) conducted 4,928 interviews in November 1982.

²¹ *Caretas*, August 3, 1987. p. 13.

²² Associated Press, August 5, 1987.

Peruvian church, Cardinal Landazuri, said that the expropriation was 'important and positive'.²³

Subsequently, however, opposition to the expropriation began to mount. Garcia's approval rating of 68.5 percent in June dropped to 47.2 percent in September of 1987, largely as a reaction against the bank measure.²⁴ The degree of opposition which later emerged was sufficient to force Garcia to backtrack and return the banks to their original owners.²⁵ This growing opposition needs explanation and consideration, as it was neither an expected or inevitable conclusion.²⁶

The following chapter will discuss the public reaction and industrial response to the bank move, and will consider the reasons for this widespread opposition. The following section, however, will first examine more closely the government's claims that control over the financial system would enable it to enact important reforms in the allocation of credit.

²³ Latin American Weekly Report, August 6, 1987, pg. 1.

²⁴ DATUM poll results, published in the Peru Report, Vol.2, No.1. January 1988, 7-3.

²⁵ Garcia never fully implemented the nationalisation law, tacitly abandoning it in October 1988 when banker Guillermo Wiese was reinstated as to his post as President of the Banco Wiese. However, the decree was not officially repealed until December 1990, by Garcia's successor, President Alberto Fujimori. See, for example, Sally Bowen, 'Peru Bank Law Repealed', *The Financial Times*, December 27, 1990.

²⁶ These issues will be examined in chapter seven (below).

6.2 The 'Financial Circuit' as a New Model of Dependent Development

The government believed that the financial system and the control over credit was a tool of a powerful fraction of the bourgeoisie used to consolidate its economic and social position. 'Peru's financial system nowadays is the most powerful was to attain economic power, and therefore, political influence,' Garcia claimed.²⁷

This view was long held by President Garcia. Acting in 1982 as president of the National Commission of Ideology and Doctrine of the APRA Party, Garcia had written at length about the development of economic groups in Peru. According to Garcia, the economic groups' structure, which he referred to as financial circuits, impede industrial development by concentrating credit and assigning loans to enterprises within the group. The Peruvian financial system, Garcia concludes, has been transformed from a structure which mobilises resources for national development, to one which acts primarily as a instrument of accumulation for a few elite groups. He argues that,

The diversification of production emerges from a financial nucleus, becoming linked to 'corporations' or 'circuits', resulting in a central, hegemonic group which does not fulfil a passive role in the provision and restriction of monetary flows, rather they selectively channel the savings of the community to investments to which have some link to the same circuit. In this way, its privileged position due to its control over credit allows it to replace the industrial fraction, and share with the transnational enterprises the preeminent position within the dominant class (Garcia 1987:233).

Garcia's analysis, heavily influenced by dependency theory, emphasises the impact of the international economy on domestic patterns of accumulation and social class formation. Economic groups, in this analysis, are simply the most visible manifestation of a new pattern of dependent development. He labels this new pattern of accumulation as the model of 'Financial Circuits'. In the 1987

²⁷ Independence Day speech, July 28, 1987, reprinted in Calle (1987).

forward to the second edition his book *A Different Future*, he summarises his argument:

A new phase of imperialist capitalism which emerged since 1970 gave rise in our society to the financial circuits. That is to say, having exhausted its capacity to create material value, international capital has organised our society around banks as a means to manage capital directly and make profits without generating value. I warned how this process now existed in our country, centralising the largest enterprises around the banks, in the midst of an economic crisis (1987:27-8).

The central focal point of the analysis is the impact of the international economy on the evolution of the Peruvian economy. Low market prices for commodity exports, restricted access to export markets, and the global acceptance (and imposition through the IMF) of neo-liberal recessionary policies, Garcia argues at length, gave rise to a new structure of accumulation which favours those who control the national surplus (1987:39). The enterprises linked to the financial system capture and circulate scarce resources between them. These conglomerates not only thrive in an atmosphere of declining overall investment and production, but act to reinforce it. The rapid velocity of circulation of money within these constellations of enterprises, result in the overvaluation of credit, and an institutionalised source of inflation (1987:231). The economic groups, furthermore, faced with a stagnating domestic market, naturally revert to capital flight. The concentration of credit in the hands of the economic groups, he concludes, 'results in the permanent decapitalisation of the country' (1987:238-9).

It is clear that the government viewed the financial sector as an important source of power for the elite fraction of the bourgeoisie. This mechanism of power, which allows it to mobilise and utilise existing savings, was perceived as an obstacle to expanding the role of small and medium industry in the Peruvian economy. Through the expropriation, the government believed that it could eliminate one of its primary 'mechanisms of domination' held by the bourgeoisie (1987:26). For Garcia, the concentration of ownership in the financial system, was the most visible, domestic manifestation of Peru's dependent economic growth

patterns. For Garcia then, the expropriation of the financial system went beyond symbolic attack on the bourgeoisie for ideological reasons, but demonstrated an attempt to break the patterns of economic dependency. The economic groups, closely allied with transnational capital, symbolised the unequal international economic order, and its detrimental impact on third world countries. The rupture of this structure of accumulation was a necessary prerequisite for the essential structural reforms spelled out in the national development plan.²⁸

The evidence suggests, therefore, that interpretations of the expropriation which point solely to political concerns ignore the underlying and long standing preoccupation of the heterodox policy makers with economic reforms. The suggestion by Rudolph (1992), for example, that the bank policy was purely a response to Alva Castro's growing power within the APRA party, fails to look beyond the political factors which may have precipitated the decision at that particular juncture. The discussion of the financial circuits was developed by Garcia as part of the APRA ideological development committee in the early 1980s, confirming that the move was not developed purely as a response to immediate circumstances. It remains unclear, however, if Garcia would have implemented the expropriation if the investment policy had been more successful. The increasing regulation of the financial system in the period between 1985 and 1987, suggests that Garcia may have been willing to attempt to make these reforms without resorting to a state takeover of the banks. On the other hand, the strength of Garcia's anti-oligarchic views means that it is possible that he had always planned to expropriate the financial system, and was simply awaiting an opportune moment.

The following section will examine the policies towards the financial system in the period between 1985 and 1987. It will also briefly consider the

²⁸ The expropriation policy formed a part of an ideological vision of dependency, which was inextricably linked to Garcia's debt policy. Garcia's concern was that the imposition of neo-liberal policies reinforce this new distorted structure of development. In order to make structural changes in patterns of development, both domestic and international relations which perpetuate this, need to be ruptured (1987:239).

basic characteristics of the financial system prior to the expropriation in order to assess the validity of the government's concerns regarding the concentration of credit.

Table 6.1 Deposits in the Peruvian Financial System July 1987 (percentage of market share of domestic currency)

Bank	% of Deposits
Private	
Banco de Credito	26.92
Banco Wiese	7.06
Banco de Lima	4.88
Banco Latino	4.16
Banco del Sur del Peru	2.46
Banco Mercantil	1.95
Banco de Comercio	1.68
Banco Regional del Norte	1.46
Banco Financiero	1.05
Banco de Desarrollo	.97
TOTAL DOMESTIC PRIVATE BANKS	52.59
State Associated¹	
Banco Continental	15.99
Interbanc	9.78
Banco Popular	6.86
Banco Nor Peru	2.60
Surmeban	2.46
Banco Amazonico	2.01
Banco de los Andes	1.54
Caja de Ahorros de Lima	2.38
TOTAL STATE ASSOCIATED BANKS	43.62

SOURCE: The Peru Report, *The Peruvian Financial System at the Time of the Expropriation*. 1987. pp. 38-41.

¹ This includes banks which are totally or partially owned by the state.

6.3 The Peruvian Financial System

A review of government policies suggests that the government was concerned about levels of concentration of ownership and of the use of credit through self-assigned loans prior to the expropriation. Policies were introduced in 1985 and 1986 to attempt to regulate this aspect of the financial system. One of Garcia's first measures in 1985, for example, initiated a process of decentralisation of the financial system through the creation of eight regional financial districts (Alva Castro 1987a:309). This legislation mandated that banks which operate in more than three districts must establish subsidiaries in each district, and ensure that a certain percentage of savings generated within a given regional district would be retained for productive purposes within it.²⁹ This policy, as part of the government's industrial restructuring plan, was designed to ensure the availability of credit and capital in rural areas and to halt the flow of savings into the capital.

In addition to policies to encourage private sector banks to decentralise operations and establish branch offices outside Lima, steps were taken to decentralise public sector banks. COFIDE, a state development agency, opened offices in the Andean towns of Puno and Ayacucho, while the Agrarian Bank opened 129 new offices in the Andean region. Commercial banks under government control underwent a similar process, as Interbanc and Banco Continental opened seventeen and eight branches respectively (Alva Castro 1987a:310).

Policies were also implemented that would specifically regulate the level of concentration of access to credit. As part of a package of measures increasing the regulation of the financial system in July 1986, the government set maximum limits on the amount which a borrower or group of borrowers could receive.³⁰ The ability of economic groups to channel the nation's surplus into those industries

²⁹ *Peru: Economic Report 1987*. London: Lloyds Bank. p. 19.

³⁰ See, *The Andean Report*, 'Peru Banking Portfolio', August 1986, on the increasing regulation of the financial system.

in which they have a direct financial interest was very disturbing to President Garcia and his economic team, and the policies implemented were designed to ensure some degree of government control over the number of self-assigned loans. The Superintendent of Banks (SBS), the state advisory body, was given sweeping powers to regulate the financial system, and in a move which generated widespread opposition, was given the power to force dismissals from the board of the directors. Although the legislation was drafted to give the Superintendency power to ensure proper management, Finance Minister Alva Castro revealed the true intentions behind the measure in a speech to Congress:

The Superintendency of Banks and Insurance Companies is given the power through Supreme Decree no. 244-86-EF to recommend the dismissal of a director of a bank when it considers that his background or *personal credit position or that of enterprises linked to him*, make it improper for him to be elected or maintained in his post (Alva Castro 1987a:304).³¹

The concerns over the characteristics of the Peruvian financial system, particularly the concentration of ownership, therefore, were reflected in the increasing regulation of the financial system from the beginning of the Garcia government. In order to assess the validity of the economic rationale presented by the Garcia government, it is necessary to examine the major characteristics of the financial system prior to the expropriation.

It was demonstrated earlier that the financial system came increasingly under the control of industrial and manufacturing based groups, after the Velasco reforms reduced foreign stakes in the financial system.³² The fusion of domestic industrial, commercial, and financial capital, often referred to as finance capital, began to play an increasingly important role in the process of financial intermediation in the Peruvian economy.

³¹ The emphasis is my own.

³² Chapter three argues that the economic groups' control over credit enabled them to adapt to the post-Velasco era, and use this ready access to credit to build powerful industrial empires.

In the early 1980s, the financial system underwent a period of crisis, culminating in the bankruptcies of various private commercial banks. The first to collapse was the Banco Comercial, owned by the Bertello family group, followed within two years by smaller banks, including the Banco Amazonico, Banco de los Andes, Banco Popular, and Banco-Nor Peru. Between 1982-1985, seven commercial banks failed in Peru.³³ The government responded in most cases by having public sector banks absorb the failing banks, thus extending state participation in the financial system throughout the 1980s. It is important to note that, due in part to this policy of absorption, the percentage of savings captured by state banks increased from 33.5 percent in 1980 to 42.9 percent in 1985.³⁴

In 1987, the remaining private sector financial institutions subject to expropriation included ten nationally owned private banks, six financial corporations, and seventeen insurance companies.³⁵ The public sector was at the time comprised of three state-owned commercial banks, five regional banks, and the Banco de la Nacion, which handles Treasury accounts and tax collection.

Data which illustrates the relative importance of the public and private financial system is provided in Table 6.1. By 1987, the state controlled 43.62 percent of savings, with another 26.92 percent controlled by the largest private bank, the Banco de Credito. Thus, only 29.42 percent was controlled by Peru's other nine private commercial banks. The degree of concentration of savings

³³ *Peru: Lloyds Bank Economic Report 1986*. London: Lloyds Bank. p. 19.

³⁴ Calculated from Superintendencia de Banca y Seguros (SBS) figures, as found in Coronado et. al. (1986:107).

³⁵ The financial entities which were targeted for expropriation are as follows: Commercial Banks: Banco de Credito del Peru, Banco de Comercio, Banco de Desarrollo, Banco de Lima, Banco Latino, Banco Mercantil de Peru S.A., Banco Financiero del Peru, Banco Regional del Norte, Banco del Sur del Peru, Banco Wiese Limitado; Finance Corporations: Financiera de Credito del Peru S.A., Financiera del Sur S.A., Financiera Nacional S.A., Financiera Progreso S.A., Financiera Sudamericana S.A., Promotora Peruana S.A.; Insurance Companies: America Terrestre y Maritima S. A., Atlas, Condor, El Pacifico, Sol de Seguros Generales Internacional, Italo Peruana de Seguros Generales, Internacional, La Colmena, La Fenix Peruana, La Nacional, La Real, La Positiva, La Universal, La Vitalicia, Panamericana, Peruano Suiza, Rimac. See Calle (1987).

within the top bank substantiates the widespread perception that the measure was directed at curtailing the economic power of the groups which control the Banco de Credito, in particular the Romero and Raffo groups. The Romero and Raffo groups alone have controlling interest in two insurance companies (El Pacifico Compania de Seguros y Reaseguros, and Compania de Seguros y Reaseguros Peruano-Suiza), and various large scale textile and oil processing plants, among other interests. The Banco de Credito is also the umbrella for Peru's third and fourth largest business groups, Nicolini and Brescia. The number of related companies, therefore, with overlapping shareholders and/or directors is considerable.³⁶ The second largest bank, the Banco Wiese, is substantially less extensive, although it too holds controlling shares in twelve enterprises (Alcorta 1987:43). These families, particularly those within the Banco de Credit, exemplify the nature of the interrelationship between the top industrial groups and the financial system.³⁷ Although it is extremely difficult to quantify, the SBS has estimated that the Banco de Credito has holdings in over 128 companies. The five largest economic groups are estimated to have control over or influence in 335 companies, with a total value of approximately 1.4 billion dollars (PAP 1987:6).

This high degree of concentration of ownership may hinder industrial development if credit is granted to bank related corporations at the expense of non-related companies. Under these circumstances, banks are less likely to utilise objective and market driven criteria for credit allocation. A large percentage of self-assigned loans can make access to credit more difficult for other sectors, such as small and medium industrialists, which are vital for economic development. The detrimental effects of such a high degree of concentration were confirmed by a World Bank study, which concluded that important bank failures in Peru in the 1980s were due in part to excessive lending to businesses related to the principal shareholders (Morris et. al. 1990).

³⁶ See Table 3.3 (above) for additional information regarding ownership of the top economic groups.

³⁷ The extent of this fusion is demonstrated by the fact that all but two of the twelve apostles were also bankers.

This brief look at the financial system suggests the existence of solid basis for concern regarding the concentration of the financial system, and its potentially adverse effects. The question remains, however, whether or not state control would enable changes to be enacted.

Apart from the long term structural reforms which the government hoped to enact, it also had immediate economic goals, designed primarily to stave off the impending economic crisis. The government argued that control over the financial system would enable it to entice investors to invest, slow capital flight and democratise access to credit. Having effected these changes, the government believed that it could continue its demand induced growth strategy, and sustain the growth of the economy.

The expropriation, on the contrary, eliminated any possibility of promoting investment or salvaging the economic strategy. It completely ruptured the relationship which had been carefully cultivated between the state and industrialists. In addition, it transformed the image of the government to that of an unpredictable actor, possibly embarking on a course towards increasing levels of state ownership in the economy. Investment plans immediately began to reflect this lack of confidence. A poll conducted at a CONFIEP conference showed that only 14 percent of businessmen polled would invest as previously planned, with 54 percent claiming that they would postpone investments until the political and economic situation stabilised.³⁸ This atmosphere was pervasive, with many companies withdrawing investment plans. A representative in Peru for the Caterpillar Corporation, for example, announced that it would abandon twelve investment projects out of the fifteen planned.³⁹

The goal of democratising credit, furthermore, could have more readily been achieved by other means. It can also be suggested that if the concentration

³⁸ *Latin American Weekly Report*, October 1, 1987. p. 5.

³⁹ *Latin American Weekly Review*, October 8, 1987, p. 11.

of credit allocation was the government's primary concern, it could have made efforts to democratise access to the 43.6 percent of savings which the state already controlled. In fact, the economic groups, which were the intended targets of the expropriation, receive a considerable amount of finance from public sector banks. According to the government's own figures, 3.6 percent of the Banco Industrial's credit was given to the Nicolini group, with a further 1.8 percent to the Romero and Raffo groups (PAP 1987:7).⁴⁰

This raises serious questions about the government's intended plans of democratising credit for investment in priority areas. It is unlikely that investor groups with the capacity to carry out these large-scale projects would have emerged in the short term. Because of this, credit was likely to go to the same leading investors as before.⁴¹ Parallels again can be drawn with the Mexican bank nationalisation in 1982, where concerns over the oligopolistic nature of the financial system and inefficient patterns of credit allocation contributed to a state takeover of banks. However, some analysts conclude that the nationalisation had little or no impact on the patterns of credit allocation (Stewart 1988).

The economic and structural reforms that the nationalisation of the bank was expected to initiate were questionable. The political and economic chaos which ensued eliminated any hope of increasing investment. Moreover, the seeds of hyperinflation had already been sown, so that the economic crisis at this stage probably could not have been averted in any case.

Most of the investment projects agreed with the government were withdrawn after the expropriation, and as the economy experienced a severe

⁴⁰ In an interview after the expropriation, Juan Francisco Raffo said that he was not worried about access to credit, as much of his group's commercial activity depended on state finance, particularly the Industrial Bank, and COFIDE. *The Peru Report*, January 1988, p. 3-3.

⁴¹ Interestingly, this point was made also by prominent labour leaders. Pablo Checa, Subsecretary of the CGTP, stated that 'the first thing that APRA must do is publish investment plans so that we can see where credit is going to, because if credit continues to go to the hands of the twelve apostles then nothing is changing in this country.' Balbi (1988:56-7) cites interview with Pablo Checa in *Cuadernos Laborales*, no. 42, August-September 1987.

contraction, with annual inflation reaching 7,650 percent by the end of the Garcia years (see Table 7.1). This 'investment on demand' approach fails to recognise that a substantial turn around in investment can only be induced through a relatively long-term period of economic growth and investor stability. It also reveals that the government had unrealistic expectations of what investment could achieve in the short term. The Minister of Industry Manuel Romero, who resigned in protest over the nationalisation, later claimed that the economic groups were in the process of developing large scale investment projects and had demonstrated the intention of expanding productive capacity along the lines suggested by the government. These projects, requiring substantial capital investment, had lengthy incubation periods, and were preempted by the nationalisation attempt. The twelve apostles, he stated, were negotiating in good faith.⁴² The suggestion that control over the financial system would enable the government to entice investors to invest, reveals a lack of understanding of the need for long-term stability in order to revive domestic investment. The negative impact on business confidence should have been foreseen.

The issue of capital flight was central to the concerns of Garcia, who felt that the industrialists who had made profits through the protection of the internal market and increased domestic demand, had an obligation to reinvest nationally. Garcia stated that he condemned the fact that scarce foreign exchange was leaving the country in profit remittances and debt repayments, as well as capital flight, and implemented strict legal limits in 1986 on the amount of foreign exchange which could leave the country.⁴³ The government was therefore sensitive to the Banco de Credito's expansion overseas in the early 1980s. Establishing subsidiaries in New York and Nassau, and a holding company in the Cayman Islands, the Banco de Credito had given the Romero group, and the other influential groups within the bank, an easy channel for capital movements. There is some evidence to

⁴² He further claimed that some of these investment projects were initiated and later abandoned as a result of the expropriation and subsequent economic crisis. Interview, Manuel Romero Caro, (Minister of Industry 1985-87), March 25, 1992, Lima.

⁴³ *Latin American Weekly Report*, August 14, 1986. p. 2.

suggest that the Garcia government had considered expropriating the Banco de Credito as early as 1986.⁴⁴

Despite Garcia's concerns, capital flight, in fact, had been in decline. Estimates of capital flight, using the World Bank method of calculation, for 1985 was US\$407 million, dropping to US\$68.9 million in 1986. In 1987, capital flight increased to US\$378.9 million, although much of this may have been a consequence of the nationalisation itself.⁴⁵ Moreover, the government failed to realise its own contributions to the problem, namely, the combination of negative interest rates, foreign exchange restrictions, and overvalued exchange rate which was conducive to speculative activities and capital flight.

These policies are particularly contradictory given the model's explicit dependence upon private sector investment. The Velasco government (1968-75) reforms resulted in a lack of business confidence and subsequent 'investment strike', which in that case paved the way for an increased state role in production to fill the resulting economic vacuum. Given that the fundamental premise of the heterodox approach was the stimulation of private investment, albeit carefully guided by the state, the nationalisation appears to be at odds with the heterodox approach. However, the logic behind the measure appeared to be that eliminating the elite fraction of the bourgeoisie would enable subordinate fractions of the bourgeoisie to emerge and lead the growth of the economy in a more equitable and productive fashion. The economic groups allied with transnational capital, Garcia claimed, subordinated the other - truly national - fractions of the bourgeoisie.⁴⁶

There is some evidence to suggest that the measure was specifically

⁴⁴ *The Andean Report*, Peru Banking Portfolio 1986. August 1986. p. 9.

⁴⁵ Paus (1991: 432) citing *Punto de Equilibrio*, 1990, Table 1.

⁴⁶ Garcia (1987:233). See page 187 above.

directed at the owners of the Banco de Credito.⁴⁷ The government felt that the control of credit by these groups limited the potential for wider economic growth by the industrial sector as a whole. The *Latin American Weekly Report* reported in October 1987, that Garcia had originally intended to expropriate only the Banco de Credito, but widened the scope of the measure when informed that it would be unconstitutional to takeover one bank.⁴⁸

While Garcia never admitted to be targeting the Romero group in particular, he did state that the move was 'aimed at disrupting the power of four large companies that own the leading banks'.⁴⁹ It can be inferred from this statement that the four largest economic 'companies' or economic groups being targeted were the Brescia, Romero, Nicolini and Raffo groups which control the Banco de Credito. Garcia further claimed that 'the other business groups have not understood that this expropriation was designed to aid them.'⁵⁰ In the aftermath of the expropriation announcement, the government attempted to reassure industrialists. The Interior Minister, in a televised speech explained that the government,

supports and will support capital investments in the productive and industrial sectors. The nationalisation law does not affect private property or industrial investments. Quite the contrary, this is a measure that supports those who invest in the industrial sector, and guarantees that they will remain independent from a monopolistic and speculative domination.'⁵¹

⁴⁷ Juan Francisco Raffo, of the Raffo group stated: 'The whole expropriation reeks of aggressiveness towards the Banco de Credito. President Garcia does not care a jot about the other banks, although Francisco Pardo's political clout may strike him as a nuisance.' *The Peru Report*, vol. 2, no. 1, January 1988 3-2.

⁴⁸ *Latin American Weekly Report*, October 15, 1987. pp. 6-7.

⁴⁹ Speech in the Plaza de Armas, August 11 1987, BBC Monitoring Service, *Summary of World Broadcasts*.

⁵⁰ Michael L. Smith. 'Peru Pauses on Way to Bank Seizure; President Suspends Decree, Will Seek Nationalisation Law'. *The Washington Post*. August 8, 1987.

⁵¹ BBC Monitoring Service, *Summary of World Broadcasts*, October 16, 1987.

This suggests that Garcia did not intend to alter substantially the balance between the state and private sector in the economy, nor dramatically increase the state's role in production. Instead, he expected small and medium industrialists to step in and fill the economic gap.

6.4 Conclusions

This chapter has examined the underlying factors leading the Garcia government to abandon attempts at *concertación*. The expropriation was precipitated by a growing sense of crisis within the government, which prompted a serious reconsideration of existing policy. On the economic front, the exhaustion of the reactivation policies and mounting inflation threatened the future of the heterodox strategy. The first signs of declining political support also began to emerge and the widespread consensus of the first two years of the Garcia government by this stage had begun to wane. The Left in Congress was disillusioned that the reforms did not go far enough, organised labour felt sidelined by the *concertación* strategy, and industrialists became wary of the degree of state intervention which marked Garcia's economic policy making. Garcia even faced dissent from within his own party, which had been alienated by his closed and autocratic policy making style.

The previous chapter argued that the Garcia government found it difficult in practice to reconcile its reformist objectives with the aim of attracting business investment. The contradictory policies which ensued resulted in the growing alienation of the government from various social classes. An increasingly discordant relationship between the state and the working class, as well as between the state and the industrial bourgeoisie, disquieted the government, which was very sensitive to public opinion polls.

Yet, as the first fractures in the multi-class coalition began to widen, Garcia did not attempt to fortify and/or reconstruct this complex coalition of actors. Instead, it appears that Garcia chose to sacrifice the alliance with the leading financial fraction of the bourgeoisie, believing that this would enable it to generate support from other classes, in addition to much of the industrial bourgeoisie.

The expropriation signalled the abandonment of the heterodox approach as

originally conceived, and the multi-class coalition upon which it was built. Through the expropriation, the government intentionally restructured its political base of support and attempted to gain greater autonomy from the bourgeoisie as a whole.

The expropriation became an important turning point, both for the political fortunes of the Garcia government and for the degree of organisation and unity within the bourgeoisie. The bourgeoisie, already mobilised by the *concertación* policy, acted collectively to protest the measure, and emerged from the battle victorious and strengthened. The expropriation also became a watershed event in contemporary Peruvian politics. It had a powerful impact upon Peruvian society as a whole, revealing a widespread wariness of state expansion. It revived the dormant Right and created the conditions for the reaffirmation of economic liberalism in Peru. Rather than fulfilling the objectives of redistributing wealth and power, the expropriation inadvertently served to reinforced the power of the bourgeoisie in Peru.

CHAPTER SEVEN

FROM PROTEST TO POLITICS: 1987-90

Introduction

The expropriation announcement in July 1987 brought an end to the *concertación* policy and the relationship, however tenuous, which had developed between the government and industrial bourgeoisie. This sudden turn in economic policy awakened doubts in industrialists regarding the long-term ability of the Peruvian state to protect their interests, and it revived an underlying fear of the expansion of the state and the violation of private property rights. From the view of most industrialists, the government did not merely alter the rules of the game yet again, but with this measure changed the game itself. Industrialists felt that the capitalist system had been attacked and they prepared themselves to resist a further decline into statism.

The government's failed attempt to assume control of the financial system provides an illuminating case study inasmuch as it reveals important characteristics of the industrial bourgeoisie and illustrates the dynamics of its interaction with the Peruvian state. This chapter will argue that the successful opposition to the expropriation indicates the increased ability of the bourgeoisie to organise and act collectively. This threat enabled the industrial bourgeoisie to ally itself with other fractions of the bourgeoisie and illustrates the conditions under which this class unity can arise.

This expropriation also led to the politicisation of a significant number of industrialists and business leaders. Industrialists had grown increasingly dissatisfied with their limited participation in the socio-political sphere and became frustrated at their inability to influence policy making despite the growing strength of their industrial organisations. This feeling of impotence was especially pronounced in light of the high expectations which the Garcia government's *concertación* rhetoric had created. Rather than reinforcing industrialist's traditionally apolitical

tendencies, this feeling of powerlessness resulted instead in the decision of many business leaders to participate actively and directly in national politics.

The Garcia government, therefore, contrary to its goals and objectives, acted as a powerful catalyst to the political development of the industrial bourgeoisie. This rejection of the previous apolitical role marked a second major shift in strategy since the formation of unified and dynamic lobby groups in the early 1980s. In less than ten years, the industrial bourgeoisie has consolidated its forces and appears to have become a permanent actor in the national political process.

7.1 The Private Sector Response

Although tensions between the government and private sector had grown steadily throughout 1987, the rhetoric of *concertación* had not been abandoned. As late as June 1987, CONFIEP held hopes for improving its relationship with the Garcia government. In an editorial entitled 'Finding *Concertación*', CONFIEP expressed confidence that, 'we are on the path to total *concertación*.'¹

The expropriation preempted this possibility by fatally undermining the bourgeoisie's confidence in the government. Not surprisingly, SNI and CONFIEP publicly proclaimed the measure to be illegal and confiscatory, and immediately began to coordinate an opposition campaign. What was perhaps more surprising was that the bankers' stance was not only to protest the measure, but to defy and ultimately prevent the takeover. This section will examine the strategies developed by the bourgeoisie in response to the expropriation threat, in order to assess its ability to affect policy and influence the state. A few questions are implicit here. Does the frustrated expropriation attempt indicate an increasingly powerful bourgeoisie, able to influence the state by virtue of its economic strength? Or does it illustrate an autonomous and increasingly authoritarian state, acting as an independent actor which is not necessarily responding to class pressures at all? While these issues will be considered in the following chapter, it is nonetheless useful to keep them in mind as the bourgeoisie's changing behaviour and its evolving position vis-à-vis the state is briefly examined.

It can further be suggested that the fight against the expropriation of the financial system was a crucial test case for CONFIEP. CONFIEP's experience thus far had been in representing the interests of industrialists and of capitalists in general, in the context of a government which had granted it an unusually high degree of accessibility to policy makers, and which had avoided (at least initially), overtly confrontational policies. It was exceedingly more difficult to attempt to

¹ *Presencia*, June-July 1987, p. 2.

defend private property rights effectively under what appeared to be an increasingly statist government. It would require that the bourgeoisie mobilise its political resources and attempt to use it to influence the course of events. In short, it was an important test of its political influence and power.

There were three basic lines of action available to capitalists to respond to this threat and defend their interests. The first was government lobbying, through the industrial organisations and personal contacts, in order to encourage the repeal of the legislation. The second available tactic was a legal battle, questioning the constitutionality of the measure in the courts, and the third, was an intensive public opinion campaign designed to generate widespread opposition to the measure.

All of these strategies were pursued vigorously, each by a different sector of the bourgeoisie. The third strategy, which rather surprisingly proved to be the private sector's strongest weapon, was the mobilisation of public opinion, led by the industrial organisations and business associations, primarily CONFIEP and its affiliated member organisation, the Association of Peruvian Banks (APB).

7.1.a The Judicial Battle

A judicial battle was initiated by the bankers themselves in the direct defence of their threatened property. The legal strategy proved very effective in the short term. Bankers sought injunctions against the government claiming that Garcia's attempt to intervene immediately in the banks without waiting for the bill to pass through Congress violated the law. Within a week, various court orders were issued which required the temporary suspension of the intervention.² After intense pressure from the courts and public opinion, Garcia announced on August

² The first court order was issued on July 31, 1987, in favour of Guillermo Wiese of the Banco Wiese. In the days that followed, similar orders were issued on behalf of the other banks and insurance companies. See, for example, Calle (1987:7) and *Caretas*, August 3, 1987, pp. 16-7.

8 that the intervention would be lifted until the bill was passed by Congress.³

This forced reversal of policy dealt a severe blow to Garcia's prestige and left the fate of the nationalisation project in doubt. The policy was widely viewed as hastily prepared and a finance ministry advisor's admission that, 'we overlooked the legal aspect', seemed to substantiate this perception.⁴ Despite strong public resistance Garcia pressed ahead with the expropriation and sent the bill to Congress.

The constitution is the bankers' most powerful weapon, argued CONFIEP leader Ricardo Vega Llona and others.⁵ The bankers argued that they were protected by the constitution which guarantees of private property (article 125), and economic pluralism (article 112).⁶ The 1979 constitution in fact permitted expropriations and state monopolies, but only in cases of emergency or in instances where the economic activity is deemed to be of 'public necessity' or in the 'social interest'. The question of whether or not the expropriation of the financial system could be justified by public necessity and social interest, generated much debate in the ensuing weeks. Later, the government undermined its credibility by attempting to declare the financial system to be in a state of emergency, and then by abandoning this attempt.⁷

The draft of the law generated further confusion by failing to distinguish

³ Alan Garcia made this announcement in a speech to supporters in the Plaza de Armas, August 8, 1987.

⁴ *Latin American Weekly Report*, August 29, 1987, p.11.

⁵ See, for example, interview with Ricardo Vega Llona in *El Expreso*, September 20, 1987, reprinted in Vega Llona [1988].

⁶ *Constitucion Politica del Peru*, Edicion Oficial, Camara de Diputados (1988).

⁷ See, for example, *Caretas*, October 5, 1987, p. 8.

between private, state and mixed ownership banks.⁸ The head of the prestigious School of Lawyers of Lima argued that the legal justification for the expropriation was confused: a declaration that the financial system is in the national interest, obviates the grounds for expropriating only nationally owned banks, rather than the financial system in its entirety.⁹

While the injunctions effectively stalled the measure for a few weeks, the longer term prospects for defeating the measure appeared less promising. The bankers' arguments failed in court, and two of the injunctions against the government were overturned.¹⁰ Meanwhile, the bill was pushed through the lower house, the Chamber of Deputies, and was approved after only two days of debate. Despite pressure from other parties and some dissent within the APRA party itself, the bill had not been substantially modified. By September 29, the bill had completed its passage through Congress and was awaiting only Garcia's signature for its final promulgation into law.

Once the bill had been signed into law, the bankers had few options left. Representatives of the Banco Mercantil, Banco Latino, and Banco Financiero assumed a belligerent stance, physically occupying their banks, and challenging the government to remove them by force. Led by Francisco Pardo Mesones, the leader of the Association of Peruvian Banks within CONFIEP, these bankers were prepared to defy the law. The directors of the Banco de Credito and Banco Wiese on the other hand, stated that they had no choice but to await the final court

⁸ See the chronology of events of the nationalisation; the text of the bill and its subsequent drafts; the debate in the Chamber of Deputies and Senate; and the final text of the Nationalisation Law #24723, reprinted in Calle (1987).

⁹ This argument was expressed by Raul Ferrero Costas, a leading opponent of the measure and head of the prestigious Colegio de Abogados (School of Lawyers) in Lima, in an article in *Caretas*, October 5, 1987 p. 26. Raul Ferrero later became an activist for the Libertad party, and was elected to the Senate in 1990.

¹⁰ See, *Caretas*, October 5, 1987.

decision and respect the law.¹¹

Nevertheless, the Banco de Credito attempted to find a legal means of resistance, and engineered the sale of 50.57 percent of its shares to its employees in an attempt to thwart the government's plans. In a very deft move, the Banco de Credito's related financial company (Financiera de Credito), which was also targeted for expropriation, financed the US\$32 million employee buy-out, using the stocks as collateral.¹² The Banco de Credito stock sales placed the government in a delicate position by challenging it to expropriate the bank from its employees. It also left the impression that the bankers had in fact outsmarted the government. This option of selling shares to workers was unavailable to the smaller banks, whose small number of employees were unable to bear the cost of buying out the banks. Some of these banks adopted the alternative tactic of declaring a staff holiday and temporarily closing down.

Alan Garcia declared the Bank of Credito's stock sales null and void and on October 9, promulgated the expropriation legislation.¹³ On October 15, using tanks and tear gas, government troops took over the Banco de Credito and Banco Wiese, forcefully installing a state management team. This brutal and violent take over of the bank, in which a tank was driven through the front doors of the bank, had a tremendous impact on public opinion. The opposition to Garcia and the expropriation policy began to grow rapidly.

The bankers acted in concert in all stages of the fight, mounting a joint offensive in the courts,¹⁴ and quietly pressuring for government concessions

¹¹ See, for example, *Caretas*, October 5, 1987, and interview with Augusto Wiese in *Caretas*, February 1, 1988.

¹² See, for example, *Latin American Markets*, October 19, 1987.

¹³ Garcia carefully timed the promulgation of the law. October 9 was the date of the historic International Petroleum Corporation expropriation by General Velasco in 1968.

¹⁴ The bankers acquired a lawyer, Armando Lengua Balbi, to defend them and develop a long term legal strategy. According to Lengua, the bankers planned to prolong the legal battle until which time the government would no longer have the strength to continue the takeover. See,

behind the scenes.¹⁵ The coordinated reaction to this threat demonstrated a high level of unity and cohesion among the bankers, which facilitated collective action in the defence of their interests.¹⁶ Francisco Pardo Mesones, when asked to characterise the degree of coordination among the bankers, described it as, 'Total. And at the highest levels.'¹⁷

The bankers' response, however, was primarily confined to what was directly at stake: the legal defence of their banks. They concentrated their efforts on the most direct and concrete lines of action to defend their institutions, through legal action, the transfer of shares or simply by locking the government management teams out of the banks. Although they revealed a capacity for effective collective action, it seemed unwilling to get directly embroiled in the national political debate which was gathering force in Peru. At one level, a partisan battle was developing. At a broader level, there was a deeper questioning about the role the state should play not only in the economy, but also in society. The potential of this fraction of the bourgeoisie to become an important actor shaping the growing national debate was derived from the fact that they were the direct adversaries of the government. Furthermore, they had the advantages of having considerable financial resources for publicity purposes and an elite status which would facilitate access to the media. Despite the obvious opportunity for them to become 'political actors', they chose to maintain a low public profile and operate in a very limited sphere. These bankers, most of whom were leaders of the most important economic groups, failed to develop a level of political discourse which would influence others to join in their defence, and made only limited effort to use the media to sway public opinion. With the exception of

Caretas, October 19, 1987, p. 32.

¹⁵ Low profile meetings between the bankers and representatives of the government occurred into early 1988. See, for example, *Caretas*, October 12, 1987 p. 15; October 17, 1987 p. 14; December 14, 1987, p. 30; March 28, 1988 p. 13.

¹⁶ Meetings between the bankers were held throughout September and October. See, for example, reports in *Caretas*, August 24, October 12, October 19, 1987.

¹⁷ Interview with Francisco Pardo Mesones, (President of the Banco Mercantil and President of the Association of Peruvian Bankers 1987) April 13, 1992. Lima.

Francisco Pardo Mesones, who staged a high publicity sit-in at the Banco Mercantil for twenty-five days, the bankers hesitated to become publicly or politically involved. They were either unable or unwilling to attempt to engage in more comprehensive means of class action.

In contrast, the leadership of the SNI and CONFIEP were active, organised and effective in the social and political arena. The bankers ceded to CONFIEP the leading role in presenting the bankers' case to the public, by developing ideological justification for these class interests and mobilising public support. Banker Guillermo Wiese later claimed that prior to the expropriation, he had participated only minimally in CONFIEP, yet found that during the expropriation debate, he was dependent upon it to defend his interests.¹⁸ CONFIEP's mobilisation of public opposition to the populist measure became the entrepreneurs' most potent weapon.

7.1.b The Public Opinion Campaign

The private sector organisations, CONFIEP in particular, mounted an intensive and coordinated public opinion campaign designed to mobilise opposition to the Garcia government. Using the media to its fullest advantage, CONFIEP and its member organisations worked to shape public opinion and defend the financial fraction of the bourgeoisie against the government accusations of monopolising credit and 'perpetuating inequality'.¹⁹ Numerous full page ads were placed in the major dailies in Peru, decrying the illegality of the measure. The leaders of the main industrial organisations, the SNI, ABP (Association of Peruvian Bankers), and of course, CONFIEP, actively defended the bankers in numerous interviews and in declarations to the press.

The expropriation became a turning point in the popularity of the Garcia government. Designed in part to bolster the government's standing in the eyes of

¹⁸ Interview with Guillermo Wiese in *Presencia*, March 1990, p. 8.

¹⁹ Alan Garcia in a televised speech to Congress July 28, 1987.

the urban poor and working classes, the measure instead backfired and generated widespread opposition to the government. Much of the lower classes, and in particular organised labour sided with the bankers in large numbers. Neither the government nor the bankers expected this upsurge of support for the anti-expropriation movement. To a degree, this support can be attributed to the development of an effective political discourse which held widespread appeal and projected the defence of principles of democracy and freedom, rather than a self-serving campaign specifically geared to repeal the expropriation legislation and protect the bankers. The campaign was careful to present a non-partisan opposition to what was perceived as a trend toward greater levels of state control in the economy. Business leaders and the anti-expropriation camp appeared as defenders of democracy against a government with authoritarian tendencies. This non-partisan opposition developed a persuasive but vague ideological discourse based upon the containment of state expansion; a stance which struck a responsive chord with the urban population and tapped into existing dissatisfaction with the bloated state apparatus and inefficient bureaucracy.

CONFIEP also effectively countered the government's economic justifications for the expansion of state control over credit. The government's democratisation argument was effectively refuted by arguing that much of the financial system was already partially or totally owned by the state, and the government could apply measures to enhance access to state controlled credit, if that was in fact the true objective.²⁰ The possible political motivation of the takeover attempt was repeatedly stressed, and the bankers began to be seen as government scapegoats.

In addition to the clear protest from all fractions of the bourgeoisie, a resounding response came from other social sectors. Academics, journalists, prominent intellectuals, most notably novelist Mario Vargas Llosa, most of the

²⁰ See, for example, full page advertisement in *El Comercio*, August 3, 1987 published by the SNI, with the title 'Nationalisation is not Democratisation' or CONFIEP advertisement, *El Comercio*, August 30, 1987.

middle class, and even some of the labour unions, combined efforts and joined the opposition movement. An intellectual social movement, with widespread and multi-class appeal, which at least in its initial stages, was not explicitly political or partisan in nature, led a powerful opposition to the Garcia government.

It is evident that the campaign gained credibility through the leadership of Mario Vargas Llosa and other intellectuals who had no personal monetary interests at stake. To a lesser degree, the same could be said about the leadership operating within CONFIEP, such as Ricardo Vega Llona, which played a leading public role, rather than the bankers themselves. This ad hoc opposition evolved over time, and eventually took the form of a political party, Libertad (Liberty), which was closely allied with the traditional centre-right parties: Accion Popular and Partido Popular Cristiano. These politically dormant parties were energised by the sudden surge of anti-statist discourse and a growing neo-liberal intellectual trend sparked by the expropriation.

The expropriation attempt caused much of the industrial bourgeoisie, which played a leading role in CONFIEP and in leading the campaign, to reassess its political strategy and the nature of its relationship with the state. The state, both prior to and during the Garcia government, had seemed virtually impervious to its efforts to influence policy, and had been subject to swings between pro- and anti-business policies. The fact that the expropriation policy was drawn up and initially implemented demonstrated in itself how vulnerable it was to these swings.

The Garcia government at this stage appeared determined to proceed with its expropriation plans, and it was not yet clear whether further nationalisations would follow. The growing recognition by industrialists of their inability to influence the government coincided with another spate of statist policies. Industrialists began to feel that the interests of domestic capital were not adequately represented within the existing system. Business leaders, reflecting this growing unease then turned to the one strategy available to it: direct political participation. In 1988, the ad hoc protest movement, begun initially by

industrialists and capitalists, rapidly evolved into a powerful political movement, and the revitalisation of the Right in Peru.

7.2 The Industrial Bourgeoisie and The Rise of the New Right in Peru

The industrial bourgeoisie in the post-Velasco era had never played an active role in the political process, and in general had shown a certain disdain for anything political. CONFIEP, for example, has always been careful to portray its activities as non-political, and preferred not to acknowledge that the creation of a lobby group to influence government is in fact a political activity.²¹ On an individual basis, with a few notable exceptions, industrialists have generally avoided partisan struggles or the pursuit of public office, and have resisted becoming directly involved in the political process.²²

The expropriation debate sparked a period of intense reassessment by leading industrialists concerning their existing role in the political system. Their inability to influence policy in the face of a direct threat to its economic interests, made business leaders question the interest group strategy and its fundamentally apolitical role as sufficient to guarantee that the interests of capital were protected within the existing political structure. This led many to conclude, as did Ricardo Vega Llona, prominent CONFIEP president that, 'businessmen now have no other option than to participate in politics.'²³ Participation was not simply a new option or strategy, according to other business leaders, it was now an 'obligation'.²⁴

²¹ Founder Julio Piccini resisted the designation of CONFIEP as an interest group or lobby group, preferring instead to emphasise its non-political functions. Interview, Julio Piccini, (President of CONFIEP 1984-5), April 13, 1992, Lima.

²² A few industrialists held important roles during the Belaunde administration. For example, Roberto Persivale, president of ADEX in 1988 and PPC activist, was Minister of Industry, as was Walter Piazza, prominent industrialist. Ernesto Lanatta Piaggio, brother of one-time SNI president Gabriel Lanatta Piaggio, and member of the Lanatta-Piaggio economic group was elected to Congress in 1985 on the PPC list.

²³ Interview with Ricardo Vega Llona (CONFIEP President 1987), in *Peru Exporta*, July 1989, p. 13.

²⁴ Speech by Rafael Villegas (CONFIEP President 1988), reprinted in *Peru Exporta*, December 1987, p. 22.

Business leaders, with virtual unanimity, began publicly exhorting their members to political activism. A CONFIEP editorial, for example, declared as early as September 1987 that,

We must acknowledge that the majority of businessmen have traditionally manifested a certain resistance to bothering about politics or even further, acting or becoming involved in it... It is necessary, an imperative, that businessmen now participate in politics.²⁵

There was widespread agreement on the need for more direct and coordinated action. What was less clear to the leadership was the means by which this new political activism would be channelled. The calls for participation were left in vague and ambiguous terms, but various options appeared to be under consideration. First, was the possibility of greater participation in the existing traditional centre-right parties which to a certain degree in the past had maintained an informal alliance with the industrialists, such as Accion Popular and Partido Popular Cristiano, in order to play an enhanced role in the decision making process of these parties. A second option was the creation of a new political party, or 'movement' of independents founded by, but not confined to, entrepreneurs. A third proposal was the continued rejection of partisan politics, but concentrated focus upon a powerful and dynamic social movement, whose primary role would be the shaping of public opinion, and defence of the principles of liberty, justice, private property rights, and democracy.²⁶ In addition, CONFIEP members demonstrated increasing support for the association's adoption of more political tactics. At a CONFIEP conference in 1989, a poll of those in attendance showed that 72 percent felt that CONFIEP should develop its non-partisan political activities. An additional 3 percent accepted the validity of its participation in partisan politics, while only 19 percent felt that CONFIEP should

²⁵ *Presencia*, editorial, September 1987, p. 2.

²⁶ On options for political participation in this period, see, for example, Juan Antonio Aguirre Roca's views (former president of the SNI), summarised in *Industria Peruana*, August 1989, p. 6; interview with Ricardo Vega Llona (CONFIEP President 1987) in *Peru Exporta*, July 20, 1989 pp. 13-16; and interview with Rafael Villegas (CONFIEP President 1988) in *Gente*, December 3, 1987, p. 7, among others.

not participate in politics (CONFIEP 1989:134).

As these options were debated, the public opinion campaign gained momentum. The anti-statist discourse which formed the core of the protest was quickly embraced by the traditional centre-right political parties, Partido Popular Cristiano and Accion Popular, which attempted to capitalise on growing anti-government sentiment to fuel their own parties. This attempt did rekindle some support for these parties, but in general the public appeared to have grown tired of the long-serving party leadership. The leader of Accion Popular in this period was still Fernando Belaunde, who had been president in the mid-1960s, overthrown by the military in 1968, and reelected to power in 1980s. Leading the Partido Popular Cristiano was Luis Bedoya Reyes, who had unsuccessfully run for president in 1980 and 1985. These traditional long-standing politicians failed to provide dynamic leadership for this growing social movement.

The movement only gained force once Mario Vargas Llosa, prominent novelist and intellectual, wrote a short essay protesting the expropriation campaign, and warning of the dangers of totalitarian government.²⁷ With a well respected, non-politician at the helm, the ad hoc protest movement, begun by business leaders, rapidly evolved into a powerful independent political movement, transcending the level of a private sector protest. While its tone was deliberately apolitical at its inception - one of the first major rallies, for example, was known as the Civic Encounter for Liberty - this force was later harnessed by Vargas Llosa who formed a political party known as Libertad (Liberty).²⁸

The consolidation of Vargas Llosa's civic movement into a political party

²⁷ The letter published as a full page ad in the major dailies was entitled, 'Against the Totalitarian Threat', and was written by Vargas Llosa but signed by various other intellectuals and public figures. *El Comercio*, August 5, 1987.

²⁸ Vargas Llosa held a mass anti-government rally in Arequipa on August 25. Due to a power failure, it was not televised as planned. Vargas Llosa later suggested that the broadcast was sabotaged as part of the government's campaign to counter the opposition. *Associated Press*, August 27, 1987.

with momentum and widespread support effectively eased the industrialists' dilemma concerning which of method of political participation to employ and offered an appealing alternative to the traditional parties. It presented activists with an opportunity to influence policy within the framework of a new political party which shared the same broad principles with many capitalists, and showed great promise for electoral success.

The basic tenet of Libertad's platform was a return to orthodox economic policies. Libertad laid the blame for much of Peru's problems on the inefficient and intrusive role of the state and Vargas Llosa proclaimed the necessity to transform it from a 'large and weak state to a small and strong state'.²⁹ The transition from a state which intervened directly in the economy to an economy guided by market forces, Vargas Llosa claimed, was needed in light of the international trend toward freer trade and the disastrous experience of state intervention under Garcia. Vargas Llosa heralded the need to implement an IMF influenced 'shock' strategy to combat the soaring inflation rate, which reached 2,775 percent in 1989 (see Table 7.1).

Both the industrial fraction of the bourgeoisie and the wider bourgeoisie, which had indicated in 1985 that they would tolerate a degree of state intervention, had once again swung the other way, advocating free market policies with virtual unanimity. Industrialists and capitalists in all sectors of the economy widely supported Libertad, believing that its economic policies would provide the international financial support necessary to withstand the recession and economic stability needed to spur a process of economic growth. The immediate interests of capitalists coincided with the ideological principles espoused by Libertad, and as a result, its direct involvement with the party was considerable. Miguel Vega Alvear, president of both CONFIEP and the SNI in 1986, became the 'Development Secretary' of Libertad and one of its representatives in the Democratic Front (FREDEMO) alliance (CONFIEP 1989:80).

²⁹ Vargas Llosa quoted in, *Caretas*, March 21, 1988, p. 21.

Many business leaders became party activists, and large numbers of industrialists became active supporters. Public demonstrations of private sector participation were made, such as in May 1988, when 200 capitalists joined *Libertad en masse*.³⁰ In the 1990 elections, three of the five ex-presidents of CONFIEP ran for Congress for the Libertad party: Rafael Villegas, Miguel Vega Alvear and Ricardo Vega Llona.

Direct involvement by leading capitalists in Libertad led to the widespread perception that it was a party which solely represented the interests of capitalists. A well known Accion Popular congressman, for example, publicly criticised Vargas Llosa's inexperience and attacked his party for being comprised solely of bankers and industrialists.³¹ While it is true that the party originally arose out of a movement which may appear to have been specifically geared to defend of rights of the bankers, its general ideological anti-statist orientation was a conviction being increasingly attractive to all strata of Peruvian society. It would not be correct to assume that these principles were adopted by the Libertad party structure to appease industrialists and bankers, nor would it be correct to assume that they controlled Libertad, but rather that their interests and beliefs coincided with this growing ideological trend. It was a current of thought increasingly adhered to by most of the middle and upper classes, and one greatly influenced by international trends and a continental shift towards orthodoxy. These variables are much more persuasive in explaining the ideological orientation of the Libertad party and the revival of the dormant Right in Peru, than a simple attribution to the influence of capitalists.

This point merits further consideration. The ease with which the population was mobilised against the expropriation and the growing support for Libertad's anti-statist discourse cannot be ascribed solely to the effectiveness of the CONFIEP's public opinion campaign. The rapid rise of the Right and rejection of

³⁰ *Resumen Semanal* quoting the major dailies May 7, 1989.

³¹ This claim was made by Victor Andres Garcia Belaunde, senator from Accion Popular. *Resumen Semanal*, 31 March - 6 April, 1989.

the expropriation can be attributed to a large extent to a crisis of the Peruvian state, evidently perceived more clearly by the masses than by the government.

7.3 The Crisis of the Peruvian State in the 1980s

The proposal to extend state control over the financial system was not popular in Peru, in contrast with the Mexican experience, in which the government received support from both the middle and lower classes. Garcia, and his policy making team, moreover, believed that this attack on the Peruvian elite would rally the support of the masses, by tapping into deep seated resentment over extremes of income inequality which are found in Peru. The expropriation debate instead tapped into a deeper disenchantment, that with the state.

The disillusionment with the state can be discerned within many social groups throughout Peruvian society. At one level, the crisis of the state is demonstrated by the existence of a large marginalised population, manifested in part by the growth of informal sector in the economy. At another level, the mid-1980s witnessed an ideological shift within certain influential segments of the Peruvian intelligentsia, which began to articulate their concerns with the deficiencies of the state. These changes in Peru were compatible with trends towards neo-liberalism and free market economics elsewhere on the continent and beyond.

The crisis of the state is most clearly reflected in the growing marginalised population, and the growth of the informal sector. Because of a lack of formal positions of employment, a significant proportion of the population in Peru depends upon informal economic activities. The Ministry of Labour estimated in 1986 that the informal sector in Lima provided employment for approximately 830,000 people, almost 45 percent of the economically active population (Pait 1989:25). These informal sector workers exist beyond the reach of the state; their enterprises are not legally registered, they do not pay taxes, and they have no access to social security or other benefits. In addition, due to rapid urbanisation, the state has been unable to meet the demand for housing, infrastructure and services for the urban poor. In the long term, the state has been deficient in the provision of services, and during the Garcia years, the expansion of public

services was virtually paralysed. In the period between 1985 and 1987, for example, the percentage of houses in the shantytowns in Lima with plumbing dropped from 35 percent to 27 percent.³² In the face of inadequate state provision of housing and urban planning, self help strategies dominate.

The problems of the inability of the state to meet the needs of the population are compounded by institutionalised corruption and graft within the bureaucracy. It is part due to this engrained corruption that the proposal of extending state control over the financial system did not appeal to the majority of Peruvians. State control, it was widely believed, would not necessarily have democratised access to credit and increased equal opportunities for loans, but would have increased bureaucratic obstacles and delays. Furthermore, it was feared that it would create the potential for new forms of corruption, and great concern existed over the degree of clientelism which characterises the Peruvian state. This fear was greatly exacerbated by the nature of the ruling APRA party, which was known to reward to partisan loyalists with state positions of employment.³³ Deriving from these concerns was the widespread claim that the nationalisation of the banks would lead not to the democratisation of credit, but to the 'Aprista-isation' of the banks. In these circumstances, it was feared that Apristas would have priority in the allocation of credit. Unlike the Mexican case where the popular view of the state is of a benevolent - or at least, not harmful - actor, in the Peruvian case the perception was one of engrained corruption and bureaucratic barriers. The degree of informality which exists suggests that people adapt by seeking to shield themselves from the reach of the state, rather than by expecting the state to provide protection and benefits.

By the late 1980s, the state in Peru had become closely identified with the

³² Estimated from data from in Ministerio de Vivienda y Construcción. 1989. *Estadística Sobre Asentamientos Humanos Marginales (PP.JJ.) al Año 1987*, and Ministerio de Vivienda y Construcción. 1986. *Estadística Sobre Asentamientos Humanos Marginales (PP.JJ.) al Año 1985*.

³³ See, for example, Graham (1991) who argues that the PAIT employment programme was marred by partisan clientelism.

ills of society: oppressive bureaucracy, corruption, and inefficiency. The state, rather than being seen as promoting growth, was perceived as an obstacle to development. This growing disenchantment within Peruvian society found expression in the revival of the Right, and the Libertad movement led by Vargas Llosa.

The hypothesis of the state as a barrier to economic development was developed by Hernando de Soto (1989) in *The Other Path*, a book which stimulated the ideological and intellectual revival of the Right. A simulated exercise conducted by de Soto and his research institute, Institute for Liberty and Democracy, found that it took approximately 289 days, at a cost of \$1,231 in fees and lost wages to register a small enterprise in Lima (de Soto 1989:134). In de Soto's simulation, the registration also required various bribes at different stages of the registration procedure. Accordingly, *The Other Path* argued that the state acts as an obstacle to economic growth. Equating Peru with the mercantilist societies of Europe of the 15th century where producers were a privileged class protected by the state, de Soto argued that formal entry into most sectors of the economy are extremely time consuming, costly or in some cases (such as the transport sector) blocked.

More important than the assertion that the state impedes development were the alternative strategies which de Soto advocated and their political implications. By reforming and reducing the role of the state and its regulation of the economy, he asserted, the dynamism of the Peruvian people and the economy would be unleashed. This emphasis upon the informal sector was significant, as for the first time, a conservative strategy was presented as one which would benefit the urban poor, rather than simply elites. It was a neo-liberal strategy, which was also compatible with reform, inasmuch as it allowed informal sector workers rights and opportunities to which they had previously been denied. It was a new brand of conservatism, which for the first time, had appeal beyond the upper classes and

was attractive to the marginalised population.³⁴ The anti-statist theme of the book had tremendous impact in Peru and abroad. Domestically, it provided an intellectual justification for the Libertad party and its proposals to pare the size and function of the state. The book, whose forward had been written by Vargas Llosa in 1985, helped to define this new view of the state.

This intellectual support for the Right and for notions of personal liberty in a classical liberal tradition, constituted a departure from the intellectual tradition in the Peruvian case, which has long been dominated by leftist thinkers and ideas of social reform and state-led development.³⁵ This left wing intellectual orientation, widespread throughout Latin America and reflected in institutions such as CEPAL, had for decades been convinced that the state was required to intervene directly in the economic process and break patterns of dependency and inequitable growth. Among many Peruvian intellectuals, this long held conviction was finally rejected in the late eighties.

Durand (1992) emphasises the role of Peruvian intellectuals in the rise of the New Right, and argues that this transition can be traced back to the latter half of the 1970s as a reaction against the Velasco reforms. Durand points to three key intellectuals who, he claims, form the intellectual vanguard of the New Right: Mario Vargas Llosa, Hernando de Soto and Felipe Ortis de Zevallos (1992:247). This new intellectual vanguard had begun to disseminate neo-liberal ideals well before the nationalisation of the financial system, and was instrumental in offering an alternative to the dominant paradigm of state-led growth, with its Marxist and dependency theory roots.

The rise of the New Right in Peru occurred in the context of a regional and international revival in neo-liberal thinking and policy. These changes in thinking were influenced by a continental shift toward orthodoxy and free market policies.

³⁴ The importance of this aspect of the ideological aspect of the Right in Peru was emphasised by Durand (1992:248).

³⁵ On the intellectual tradition of anti-oligarchic thought in Peru, see Gorman (1982).

Previously active and interventionist states in countries such as Mexico and Chile, had made an important shift in their development orientation towards the liberalisation of their economies. The comparative achievements of the conservative economic advisors in Chile, known as the Chicago Boys (named after the University of Chicago department of economics), offered a success story close to home. This continental shift paralleled a global shift towards neo-liberalism, as the rise of the Reagan-Thatcher ideology extolling the virtues of a limited state role in the economy influenced governments and capitalists world-wide. This international ideological trend found fertile ground in Peru, coinciding with both the long-term crisis of the Peruvian state, and the more immediate problem of the growing economic crisis of the Garcia interventionist model.

The mobilisation of the popular sector was also heavily influenced by the sudden and dramatic downturn in the economy. As the government continued to pursue its expansionist heterodox policies, exhausting available resources, the economy rapidly went from boom to bust, precipitating the greatest economic crisis of this century in Peru.

7.3.a Crisis of the Heterodox Model and the Decline of Alan Garcia 1988-90

The interventionist model of the Garcia government by 1988 faced extreme difficulties. It is clear that the government's structuralist, cost-push view of inflation led it to reject the initial warning signs of crisis, allowing the economic team to proceed with expansive policies. One source of inflation, for example, was public sector deficit, which the heterodox economists viewed as a 'complement to demand stimulus' (INP 1988:8). Moreover, monetary emissions used to finance the public sector were at unsustainable levels and were highly inflationary. Inflation steadily mounted, surpassing 100 percent in 1987, while foreign currency reserves held in the Central Bank had experienced a precipitous decline, from US\$968 million in 1986, to US\$43 million in 1987 (BCR 1988:37).

The limits of the economic boom had been reached.³⁶

Garcia and his key economic advisors were slow to respond to these signals. In 1988, Garcia announced that his government would be pursuing selective rather than generalised growth. But this minor shift in policy was not sufficient to counter the growing economic crisis. By September the government was forced to abandon its heterodox growth strategy and revert to orthodox methods of stabilising the economy.

The stabilisation measures introduced in September raised controlled prices by as much as 300 percent, accompanied by an increase in public sector prices to bridge the deficit gap, and a devaluation to ease the widening commercial balance. The government also triggered a massive increase in the prices of industrial products by allowing the private sector to correct its prices before a further 120 day freeze. The huge adjustment upwards resulted in the first signs of hyperinflation, a 114 percent inflation rate for September alone (Caceres and Paredes 1991:92).

The government also introduced a final effort at *concertación* at this stage. The administration widened the scope of the negotiation to include labour as well as the private sector, and established the National Solidarity Economic Pact. The government hoped to be able to contain the increasing expectations of inflation with this renewed effort at *concertación*, and retain control over the economy. Although industrialists initially refused to participate, they acquiesced, acknowledging that it was in their interests to support this effort to obtain a national consensus. Yet, both labour and industrialists lost confidence in the government as economic conditions continued to deteriorate. The first general strike occurred in 1988 as workers protested the declining value of real wages.³⁷

³⁶ For a critique of the heterodox policy and of stabilisation efforts during the Garcia administration, see Paredes and Sachs (1991), Paus (1991), Thorp (1991), and Pastor and Wise (1992).

³⁷ Barbara Durr, 'Peru Hit By General Strike', *The Financial Times*, July 21, 1988.

Further packages of measures were introduced in November and throughout 1989 to stabilise the economy, but the hyperinflationary process, with roots in the earlier policies of printing money and raising wages was set. The 'gradualist' process of economic stabilisation failed to control inflation or halt the declining production. The economic team continued to implement gradual adjustments in prices and the value of the inti, rejecting an IMF-style one-time 'shock'.

Some key indicators of the economy can be found in Table 7.1. Production began a steep and steady decline, with GDP declining 8.3 percent in 1988, 11.9 percent in 1989, with a further fall of 4.6 percent in 1990 (BCR 1990:45). Inflation in this period soared, from 1,722.3 percent in 1988, to 2,775.3 in 1989, peaking at 7,649.6 percent in 1990 (BCR 1992:21).

Table 7.1 Selected Economic Indicators 1985-1990 (annual percentage growth)

	1985	1986	1987	1988	1989	1990
inflation	158.3	62.9	114.5	1,722.3	2,775.3	7,649.6
GDP	2.2	9.2	8.3	-8.3	-11.9	-4.6
invest/GDP ¹	18.6	22.9	22.0	23.9	17.2	14.6

SOURCE: Banco Central de Reservas del Peru, *Memoria*, 1990, 1992.

1/ Investment as a percentage of GDP

The economic crisis had a devastating impact of the standard of living of most sectors of the population as real wages plummeted. The economic indicators for 1988 and 1989 illustrate the unprecedented depth and scope of the economic collapse. The impact was particularly harsh on the working classes. Real wages declined by 27.7 percent in 1988, with a further decline of 33.7 percent in 1989 (BCR 1990:23). By 1990, only 18.9 percent of the economically active population

was adequately employed, with the vast majority (72.8 percent) underemployed and 8.3 percent unemployed (BCR 1990:26).

How had such a high degree of economic mismanagement come about? In addition to the weaknesses in the heterodox theory itself, in particular its view of inflation, there was a clear inability of the state to implement and coordinate economic policy effectively. One factor which contributed to this was Garcia's autocratic policy making style, which relied on an ever decreasing circle of advisors. As became evident with the expropriation decision, government advisors, such as Daniel Carbonetto, played more important roles than many cabinet ministers. The autocratic and isolated nature of policy making by an impermeable circle of heterodox minded economic advisors insulated Garcia from criticism and suggestions from economic think tanks and economists with divergent points of view. In the single minded pursuit of economic growth and expansion, the economic team turned a blind eye to potential sources of inflation.

Inter-agency conflicts and poor coordination between departments were also limited the effectiveness of policy implementation.³⁸ Disagreements over economic policy existed between essential bureaucratic institutions, such as the National Planning Institute, the Central Bank and Ministry of Economy, each of which passed through various leadership changes throughout the Garcia years. Tensions also surfaced between state managers and the political appointees at the head of these institutions. Wise and Pastor argue that state managers, which generally tend to moderate policy and prevent radical policy swings were bypassed by the Garcia government (1992:105). Key decisions were made by a closed circle within the executive branch, or by Garcia himself.

The degree to which Garcia subordinated the bureaucratic institutions which theoretically are supposed to have a degree of independence from the executive is illustrated by his conflicts with the Central Bank. In 1989, Garcia again attempted

³⁸ The point was made by Franco (1987) a political insider and informal Garcia advisor.

to introduce measures which would gradually reactivate the economy. The Central Bank opposed this policy, and the president of the Board of Governors resigned. The post was not filled for the remainder of the Garcia presidency (Caceres and Paredes 1991:94-95).

The extent of the crisis which the interventionist model induced provoked a real questioning about the suitability of the state intervention in the economy. Widespread disillusionment with the Garcia administration, for a population which just a few years earlier had held high hopes for social change and economic growth, further fuelled the growth of the Right, allowing it to capture the support of sectors which had traditionally supported the left.

7.4 The 1990 Elections

In 1988, Vargas Llosa's Libertad party joined in an alliance with the two established centre-right parties, the Partido Popular Cristiano led by Luis Bedoya Reyes, and Accion Popular, still led by ex-President Belaunde.³⁹ The first challenge facing the alliance, known as the Democratic Front or FREDEMO, was the 1989 municipal elections. Serious internal disagreements erupted regarding Vargas Llosa's insistence that FREDEMO present joint candidates rather than each party putting forth its own, Vargas Llosa resigned from Libertad, only to rejoin when the other leaders capitulated.⁴⁰

The municipal elections presented the first indication of declining popular support for the FREDEMO campaign and image. The FREDEMO candidate, Juan Inchaustegui, was defeated by a television presenter and political unknown, Ricardo Belmont. The declining support for the immensely popular Vargas Llosa was, to a large degree, a reaction against the alliance with the established centre-right parties of the alliance, which were perceived as institutions representative of the upper classes. The initial widespread appeal of Vargas Llosa and the Libertad movement had originated in the popular perception that the movement was independent and provided an alternative for those who had grown disenchanted with the politicians who had long dominated the established political parties and the national political agenda. The political parties, in particular the Accion Popular and Partido Popular Cristiano were dominated by a closed circle of long standing political elites, offering little opportunity for new faces or new ideas. The tight control by an elite clique over the traditional political parties resulted in a surge of support for non-politicians. Ironically, television personality Ricardo Belmont, candidate to the position of Mayor of Lima who defeated FREDEMO's

³⁹ Two small right parties also joined the Fredemo alliance, SODE (Solidarity and Democracy), and UCI (Civic Independent Union). See, Resumen Semanal April 7 and May 7, 1989.

⁴⁰ For a first hand account of the establishment of Libertad and FREDEMO, see Vargas Llosa (1991).

choice, successfully campaigned by presenting himself as leader of an independent political movement. Thus, Libertad's independence was compromised by its alignment with existing parties, while the very tactics which had previously been responsible for its popularity were exploited successfully by the opposition.

This growing perception of Libertad as too closely allied with the established parties was also expressed by some industrialists who felt that the independent nature of the new party was being sacrificed. In 1990, banker Francisco Pardo Mesones of the Banco Mercantil who had gained public support during his 'sit in' in 1987 broke away from Libertad, and created a new party 'Somos Libres'.⁴¹ With him large numbers of industrialists, who lacked confidence in the traditional political parties within the FREDEMO alliance, ran for Congress on the Somos Libres ticket, including first CONFIEP president, Julio Piccini. Somos Libres, which was truly a party of industrialists, claimed to be an independent movement which would in turn provide qualified support to a Libertad/Fredemo presidency.⁴² This ambiguous message failed to gain any measure of popular support, and only served to fragment the unity behind the Vargas Llosa candidacy.

The polls placed Vargas Llosa with a firm lead. Three months before the elections, Vargas Llosa maintained 46 percent of the polls, contrasting with a mere 11 percent of the socialist candidate who was in second place.⁴³ Until the eve of the election, pollsters claimed that Vargas Llosa would have to face a run-off election with either Luis Alva Castro, the APRA candidate, or Alfonso Barrantes from the Izquierda Unida, his two nearest rivals.⁴⁴ It was thus very surprising

⁴¹ Somos Libres literally means, we are free. It is the first line of the Peruvian national anthem.

⁴² Interviews, Francisco Pardo Mesones (President of the Association of Banks 1987, and President of the Banco Mercantil), April 13, 1992, Lima; and Elena Maria Delgado (Senate candidate for Somos Libres); March 4, 1992, Lima.

⁴³ *Latin American Weekly Report*, February 8, 1990. p. 7.

⁴⁴ *Latin American Weekly Report*. April 12 1990, p. 1.

when an unknown candidate from Cambio 90, Alberto Fujimori, came in second place in the first round of elections, and won the run-off presidential elections in June 1990.

How can such a tremendous political upset be explained? The public opposition to the traditional political parties was a factor apparently underestimated by the Vargas Llosa team, and its alliance with the Accion Popular and Partido Popular Cristiano certainly hindered its campaign. It gave the impression of an alliance with the old political guard, which had their turn at government, and had failed to offer Peru a path to sustained or equitable growth.

The rejection of these traditional Right parties also needs to be linked with potent issues of race and class in Peru. Vargas Llosa and his political allies were generally middle and upper class and of Spanish descent. The overt alliance between the traditional right wing political powers, and the new economic powers, the industrialists, gave a strong impression of a new type of oligarchic domination. Fujimori, an outsider who was not a product of the social upper class, appeared to the substantial peasant majority outside of Lima and to the urban squatter residents to be a candidate more likely to take their interests into account.

Moreover, Fujimori had the political acumen and foresight to court the informal sector by choosing as his vice-president, Maximo San Roman, leader of the representative organisation of small industry: APEMIPE. This national institution gave Fujimori an immediate broad base of support, not only in the capital but also around the country. In the absence of a supportive party machinery backing him, institutions such as APEMIPE gave him an important network of popular support.

Vargas Llosa, in contrast, had the combined support of two of the established parties as well as his own. On the surface this organisational support would appear to have supplied him with a great advantage. Yet, this potential resource ultimately functioned as a liability. A large part of Vargas Llosa's initial

appeal was that he was a political outsider and inexperienced in the world of politics. Much of his initial popularity, therefore, was attributable to the fact that he was not a politician. However, by the time of the actual elections, Vargas Llosa had campaigned long and hard, and as a result lost his image of an innocent outsider. Libertad's intensive media campaign heightened this perception of Vargas Llosa as a professional politician and resulted in media overexposure. To make an important comparison, FREDEMO spent US\$12,234,386 on its campaign in the run up to the first election, while Fujimori's party, Cambio 90, spent a mere US\$197,916 (Grompone 1991:53).

In addition, Vargas Llosa's explicit support for a shock austerity programme and widespread recognition of the severe social impact which it could have upon the impoverished sectors of the population, was an additional factor which led to Libertad's rejection by the electorate. The election of Fujimori, whose economic policies had not been clearly articulated, can be seen as rejection of both the neo-liberal policies proposed by Fredemo and the statist and inflationary policies of his predecessor.

It is still too early to assess the future role of industrialists in the Peruvian political process. Although it achieved a minor presence in Congress after the elections, by 1990 it was only beginning an on-going process of political mobilisation and organisation. Of the four CONFIEP ex-presidents which ran for Congress, two were elected: Ricardo Vega Llona and Miguel Vega Alvear, both for Libertad. Somos Libres failed to gain a single seat.

The financial backing of the bourgeoisie failed to ensure that FREDEMO was elected to power, and possibly contributed to this failure, by saturating the media, and the general public, with campaign ads. This experience also illustrates the nature of mass politics in Peru. Within the democratic system with a large impoverished population, any group with political aspirations which is unable to gain and sustain multi-class support is destined to fail. This case also illustrates that the bourgeoisie's ability to present its own interests in terms of wider national

goals, will play an important role in its future political effectiveness.

This chapter has chronicled the politicisation of the bourgeoisie in Peru. While elements of the wider bourgeoisie clearly played an important role in the opposition to the expropriation, it is clear that it was the industrial bourgeoisie which played the key role in this process. The industrial bourgeoisie has become a more organised political and social actor as a result of these events, and it is not likely that this recent politicisation will easily be reversed.

7.5 Conclusions

The turmoil of the post-nationalisation period reflects a period of transition in Peruvian politics, consisting of political and ideological changes at all levels of Peruvian society. It was a period of reevaluation and redefinition of the social and political order, in which not only the role and power of the bourgeoisie was questioned, but also that of the state and political leadership.

Different social classes expressed different points of concern. The first issue of national debate, put on the agenda by Garcia, was the power and role of the bourgeoisie. Garcia attempted to resuscitate his declining popularity by reviving the mass-elite rhetoric to mobilise the popular sectors. This debate was rapidly overshadowed, however, by a questioning of the accepted active role of the state and of the basic national development orientation.

The rise of the New Right marked a fundamental shift in the dominant paradigm within many key groups in society, of which the bourgeoisie was one. Capitalists were able to unite around the anti-statist perspective, coinciding with other key elites, most notably intellectuals, think tanks, as well as the military. The rejuvenation of conservative thought, this chapter has argued, was initially an intellectual movement, which in the initial stages was able to capitalise on a perception shared with popular sectors of a massive and dysfunctional state.

The changes in the popular sectors, such as the urban poor, working class and peasantry are less easy to typify. It is clear that the state-society focus of the debate appealed to these sectors, as the crisis of the Peruvian state was felt most acutely by the poor. This message articulated an entrenched dissatisfaction with the state which until this point had found little voice within the existing political agenda.

While the message was appealing, however, the messenger was not. The popular sectors again shifted the tone and nature of the debate, rejecting instead

the closed and isolated nature of Peru's political elites, which were out of touch with current concerns. The 1990 elections suggest that the Right in Peru is still tarnished by its elitist and upper class image. Due to both the alliance with traditional parties, as well as to the circumstances surrounding the establishment of Libertad, this party appeared to be established for and by capitalists. Although it can be suggested there was, in the late 1980s, a fundamental political realignment of the middle and upper classes towards the global trend of neo-liberalism, the same can not be concluded of the other social classes. The extreme and pervasive wealth disparities, and the social conflict related to them, will continue to make these policies less palatable to the population at large. Reform will remain on the popular agenda, if not on the agenda of the established political parties.

The election results further illustrated a continued propensity for the electorate to respond to populism; first revealed in the initial support for Vargas Llosa, and later by the support for Fujimori. Although the outcome in this case was of a right wing populist, a revitalised left may emerge in the future. It is important to note that Fujimori presented his party in opposition to Vargas Llosa's proposal of an IMF stabilisation shock, and was not clearly conservative in his views prior to his election.

The late 1980s was a period of intense change in the political character of the industrial bourgeoisie. The expropriation led it to reject the emphasis it had placed on an interest group strategy, and participate directly in politics. These changes demonstrate a break from the past, not simply because of the new forms which the industrial bourgeoisie developed to structure its relationship with the state, but also because it also signalled a shift towards a more active interaction with the state. It no longer simply reacted against government initiatives and policies, but actively formulated its own strategies to influence policy makers. The implications of these changes will be considered in the final chapter.

CHAPTER EIGHT

THE POLITICAL EVOLUTION OF THE INDUSTRIAL BOURGEOISIE IN PERU

Introduction

The industrial bourgeoisie in Peru has undergone profound changes since the military government in 1968 acted to reduce the political and economic power of the oligarchy. This thesis has argued that the destruction of the oligarchic state paved the way for the emergence of the industrial bourgeoisie as the leading domestic economic force. Despite this enhanced economic position, industrialists felt that their power to influence policy making throughout the post-oligarchic period was too limited to be able to defend their interests. This thesis has argued that as a response to this limited political influence, a deepening of the process of political organisation of the bourgeoisie occurred, with the industrial fraction of the bourgeoisie playing a leading role in this process.

The 1980s were a period characterised by intense changes in the way in which the industrial bourgeoisie sought to relate to the Peruvian state, to society and to itself. Unlike in 1968, when measures from above acted as a stimulus to the development of the industrial bourgeoisie, in the 1980s it was the industrial bourgeoisie which attempted to shape the nature of the relationship between itself and the state. In a relatively short period of time, business leaders and industrialists had begun a process which entailed the reassessment of the role of the industrial bourgeoisie in the Peruvian power structure and the adoption of two strategies to attempt to enhance its power relative to that of the state; first, through the development of a confederation of industrial organisations known as CONFIEP, and second, through direct political participation by business leaders and prominent industrialists.

This chapter will consider the implications of these transformations for the future political and economic development of Peru. The first section will attempt

to reassess the impact of the Garcia government on the political role of the industrial bourgeoisie, and consider in particular, what this case study reveals about the ability of the bourgeoisie in Peru to engage in effective collective class action. The second section will attempt to place these changes in a historical context, and will consider what these changes suggest for the future relationship between state and industrial bourgeoisie in the 1990s.

8.1 The Industrial Bourgeoisie and Collective Action in the 1980s

The creation of CONFIEP in 1984 represented a departure from the previously passive and reactive strategy which had characterised industrialists' political behaviour. Creating a confederation that united various industrial organisations which previously had dealt individually with the government, the industrial bourgeoisie allied itself with other fractions of the bourgeoisie in order to create a structure for collective expression and thereby increase the negotiating power of the bourgeoisie. This strategy was reinforced shortly thereafter by the *concertación* policy which thrust CONFIEP into a high profile role in the political arena. For the bourgeoisie, this was a propitious situation. Having just created a structure which would allow it to speak and act collectively, the development of a policy providing the opportunity to express these interests would appear to have placed capitalists in a potentially powerful and influential position.

The Garcia government's rhetoric of *concertación* with industrialists gave them high expectations of the influence they would wield in the discussions of economic policy. When the National Council of Investment was installed in 1987 institutionalising the relationship between the state and industrialists, for example, Finance Minister Alva Castro stated that its function would be to:

elaborate and approve the policies, criteria and priorities to be followed in the promotion, development and negotiations regarding investment.¹

In practice, however, the level of negotiation proved to be minimal. Although CONFIEP did benefit from privileged access to policy makers on a regular basis, its political leverage with regard to economic planning was almost nonexistent. The negotiations consisted primarily of meetings determined by the government, ranging from thirty or forty top industrialists being invited to the presidential palace to listen to what amounted to a pep talk encouraging investment, to smaller and more intense discussions on policy issues. In most cases, industrialists assert,

¹ The emphasis is mine. Interview with Luis Alva Castro (Finance Minister 1985-87), in *Presencia*, April 1987, p.10.

these meetings were used by the government to announce decisions which were already taken, rather than to consult with industrialists on policies under consideration, or to attempt to assess the potential impact of measures on private sector investment plans.² The Treasury Bond policy in April 1987 which contributed to the rupture of dialogue provides clear evidence for these claims. According to an SNI statement, 'there was neither *concertación*, nor consultation.'³ It gradually became evident to business leaders that access to policy makers did not necessarily imply influence. In addition, the selective *concertación* policy developed in late 1986, resulted in the government bypassing CONFIEP in favour of negotiations with the economic groups. The ability of the government to grant legitimacy to CONFIEP and later withdraw it, left industrialists in a vulnerable position. Their elected representatives were suddenly shunted to the side, while the economic groups, which represented no one but themselves, became the most influential fraction of the bourgeoisie in the *concertación* process.

In doing so, the legitimacy of CONFIEP was called into question by the government. In explaining the policy of selective *concertación*, the Minister of Industry suggested that negotiation with the business leaders was not the most viable strategy, because they are 'professional representatives' with no real investment power of their own.⁴ The government felt that it was preferable, therefore, to dialogue directly with the economic groups which were in the position to make concrete and immediate investment commitments. Government officials, moreover, worried that a general appeal for investment through institutions such as CONFIEP or the SNI would simply result into a political debate without yielding economic results.⁵

² Rafael Villegas asserts that the concertacion meetings were primarily used to announce, rather than discuss, government policy. Interview, Rafael Villegas (CONFIEP President 1988), April 9, 1992, Lima.

³ *Presencia*, April 1987, p.4.

⁴ Interview, Manuel Romero Caro (Minister of Industry 1985-1987), March 25, 1992, Lima.

⁵ *The Andean Report*, October 1986. p. 145.

This experience revealed the vulnerability of CONFIEP vis-à-vis the state. The government was not only able to determine the channels of communication, the frequency of dialogue, but, most importantly, the agenda. When the government installed the National Council of Investment which included representatives of capital and labour, for example, the private sector was not even entitled to choose its own representatives.⁶ These experiences revealed to the CONFIEP leadership the vulnerability of depending exclusively upon an interest group, a feeling further magnified by the selective negotiation policy with the economic groups, which marginalised the majority of industrialists.

The weaknesses inherent in this position were revealed even more clearly when the government attempted to expropriate the financial system. Few options were available to the bourgeoisie given the confines of existing framework of interest group-government relations. Pressure in advance to counter the proposal did not exist as an option, as there was no public debate regarding the expropriation before the decision was made. Neither capitalists or labour, or in fact most of the government's own ministers, were aware of the plans for nationalisation, until announced live on television on July 28, 1987.

It was suggested earlier that the expropriation could be seen as an illustrative test case of the influence and power of the bourgeoisie as a whole. What, then, did this case demonstrate? The legislation was ultimately repealed years later after a protracted legal battle and political opposition. The repeal of the legislation was touted by many fundamental victory for the Peruvian bourgeoisie. It has also led some observers to characterise the economic groups as the 'new oligarchy', economically powerful and increasingly able to influence policy outcomes (Anaya 1990). However, there is a danger of attributing many of the events of 1987-90 to the impact of the bourgeoisie's newly politicised behaviour. The case study of the Garcia administration presented in this thesis shows capitalists not to have been very effective in persuading the government to

⁶ *Presencia*, editorial, February 1989, p. 2.

reformulate policies which they felt may negatively impact on the industrial sector. The fact that the expropriation policy was in fact drawn up and initially implemented, furthermore, demonstrates a certain degree of state autonomy, in that the government was able to implement a policy which was contrary to the interests and demands of the bourgeoisie.

When behind the scenes negotiations between the bankers and government failed to resolve the crisis, CONFIEP had few options available. In this case, the business leaders - rather than the bankers themselves - attempted to bring pressure to bear on the government by the mobilisation of public opinion. This was by no means a task guaranteed of success.

The bourgeoisie was unable to resist the measure of its own accord. The government began to take notice of the opposition campaign only as other social groups joined in the protest. The opposition to the measure succeeded largely because the interests of capitalists coincided with those of intellectuals, politicians, and even labour leaders, who were beginning to feel that yet another experiment with statism was destined to fail. The expropriation became a trigger incident which mobilised latent and widespread disenchantment with the state. The successful resistance to the measure does not necessarily demonstrate a newfound political power of the bourgeoisie in the post-Velasco era, nor an effective lobby strategy. Had Garcia's populist attempt to revive popular support been successful - a more probable scenario - the bourgeoisie could have been seriously weakened, both politically and economically.

The industrial bourgeoisie, allied with other fractions of the bourgeoisie, mounted an effective opposition. The forcefulness of the industrial bourgeoisie's response to the expropriation surprised the government and analysts alike. There was nothing in their past behaviour which would have indicated that the response would be as aggressive and forceful in the defense of the financial system. Again, this can be contrasted with the Mexican case where even though some fractions of the bourgeoisie disagreed with the takeover, they did not attempt to resist or

prevent the policy from being implemented.⁷

After the events of 1987, the business leaders began to doubt the capacity of the interest group structure to become an effective political base for the representation and defence of the bourgeoisie's class interests. Given the most fundamental threat - the violation of private property - business leaders rapidly became politicised. Motivated by this political frustration, leading industrialists began to participate in partisan politics. While it is more difficult to consider the actions of some individuals as class action, it does represent a departure in the way many industrialists viewed their role in the political structure, and signalled a shift in the way elected business leaders attempted to represent the class interests which they attempt to promote and defend.

Recalling the arguments which suggest that collective action is infrequent and unlikely, and driven primarily by a cost-benefit analysis of its members, this experience demonstrates the importance of non-quantifiable factors.⁸ Although the economic stakes were important, and the industrial bourgeoisie may have feared further expropriations, the experience with the Garcia government provided exceptional circumstances which acted to motivate the capitalists across all sectors of the economy into aggressive class action in 1987. The *concertación* policy of the 1985-87 period was essential in mobilising the bourgeoisie in the political sphere prior to the expropriation. Nothing is more revolutionary than heightened expectations, goes the old political science adage. Or according to Albert Hirschman, instances of protest are often explained by disappointment and dashed expectations (1985, 1987). The relevance of this to the Peruvian case is clear. The activism of capitalists was motivated by exceptional circumstances; first, by a government which led industrialists to believe that they would play an influential role in policy making, and second, by the aggressive attack on domestic capital

⁷ In Peru, some bankers staged sit-ins in their banks, challenging the government to bring them out by force, while the Banco de Credito owners sold their shares to the banks employees. The bankers did not simply protest the measure, but resisted it.

⁸ See chapter one for a brief review of collective action theories.

which served to unify entrepreneurs. The expropriation of the financial system in the context of *concertación*, meant that capitalists had been mobilised for some degree of participation in policy making and politics. Industrialists, in particular, felt that they had been deceived by Garcia's promises and misled by the *concertación* rhetoric.

The efforts of CONFIEP were also bolstered by support from the international community, in the form of a large grant from the United States Agency for International Development. In 1987, CONFIEP received a US\$1.5 million grant over a two year period which enabled it to fortify its administrative and institutional base.⁹ The considerable financial resources at its disposal during this key period in its history undoubtedly assisted CONFIEP in its efforts. This international support, possibly part of a strategy by the United States government to strengthen the neo-liberal opposition to the Garcia government, acted to reinforce and legitimise the role this association was attempting to perform within the political process. This international legitimacy gave the association a degree of prestige which contributed to its growing membership, peaking at thirty-one industrial organisations in 1989.

The exceptional circumstances which gave great impetus to the increasing politicisation of industrialists and growing class unity raises questions regarding the long term nature of these changes. It is uncertain whether the effectiveness or dynamism of CONFIEP will be sustained in the absence of these circumstances. It is possible that in the post-expropriation period, once the common objectives have been achieved and the immediate threat wanes, the degree of unity among the different fractions of the bourgeoisie within CONFIEP may gradually dissipate. Although it is beyond the scope of this study to examine the evolution of CONFIEP beyond the Garcia years, it can be mentioned that the number of member organisations within CONFIEP has since been in decline from thirty one

⁹ Interview, *Eduardo Iriarte Jimenez* (Vice-President of CONFIEP 1984-87), April 7, 1992, Lima. See also Durand (1992:250) who stresses that USAID assistance to CONFIEP came after the organisation was already established. It was not instrumental in getting the private sector organised.

in 1989 to twenty-four in 1992.¹⁰

This era also presented an important and rare opportunity for the bourgeoisie to forge alliances with other social classes. This may be attributable in part to the ability of CONFIEP and the SNI to elaborate and present a wider development oriented discourse which was not only non-threatening, but also very attractive to many sectors of society. It was perhaps expected that much of the middle class, with upwardly mobile aspirations and a certain degree of personal accumulation would be responsive to lofty appeals for the defensive of democracy and private property rights. It is less easy to explain why other classes would side with industrialists, or worse yet, bankers. As remarked by Mario Vargas Llosa, 'no one loves bankers' (1992). Yet this call to halt the aggression against Peru's bankers was heeded by the working class, informal sector workers and middle class alike. CONFIEP was careful to present a broad spectrum of principles which it claimed to be upholding: freedom, democracy, and social justice. Its ability to construct and strategically manage its defence illustrates the potential effectiveness of CONFIEP. It was able to recognise the potential convergence of interests, and enlist other social classes in its struggle with the state.

The ability of the bourgeoisie to influence other social classes is an important prerequisite for hegemony, demonstrated by its being able successfully to present its interests as coinciding with those of other classes, and impose a high degree of cultural or ideological influence over society. This ideological hegemony, a concept developed by Gramsci, suggests that it would be difficult for a class or class fraction to attain hegemony if it is continually in conflict with other classes (Benton 1984, Pellican 1981, Gramsci 1977). These tensions can be significantly eased by ideological transmission which can legitimise the role and interests of the bourgeoisie as being compatible with the nation as a whole. Hegemonic prospects of the bourgeoisie can be greatly improved if it can present its interests in terms of wider, national development ideals which are attractive

¹⁰ Interview with Marian de Carreras, (public relations officer CONFIEP), April 3, 1992. Lima.

other to social classes.

The expropriation itself improved the public perception of the business sector. Various public opinion campaigns throughout 1987 and 1988 showed a gradual change from a generally negative view of entrepreneurs to one of them being a positive force in society.¹¹ This has increased the legitimacy of the bourgeoisie, at least in the period immediately following the expropriation. Although this change in perception may enhance its overall position in the socio-political structure, the electoral outcome suggests that has failed in the longer term transmission of broader ideals.

What of the effectiveness of Peru's capitalists to engage in collective class action in the 1980s? There is little doubt that through CONFIEP, class interests began to obtain higher degrees of cohesion. The founder of CONFIEP, Julio Piccini, remarked in 1989 that one of CONFIEP's most notable achievements was the elimination of the public bickering which previously characterised the bourgeoisie.¹² However, one should be cautious about concluding that intra-class conflicts have been eliminated or even reduced. The potential for considerable intra-class struggle continues to exist. Fundamental conflicts of interests will continue to surface as economic policies threaten to impact differently on different sectors of the economy. The bourgeoisie cannot be seen as a homogenous and monolithic actor, but as being comprised of individuals whose opinions will be guided by their specific economic interests. As a prominent industrialist explained, CONFIEP unites entrepreneurs 'whose interests are basically similar, but not identical...'.¹³

The structure of CONFIEP was designed to reflect the diversity of interests

¹¹ See, for example, Apoyo poll, results published in *Presencia*, January 1989, p. 8.

¹² Interview with Julio Piccini, *Presencia*, August 1989 p. 12.

¹³ Speech by Eduardo Iriarte Jimenez (Vice-President of CONFIEP 1984-87) reprinted in part in, *Presencia*, February 1987, p.11.

which it represents. As a response to the failure of previous attempts at unification of capitalists transcending sectoral lines, CONFIEP has clearly defined policies delineating its range of action in order not to encroach upon issues which relate specifically its member trade groups.¹⁴ It restricts its action to issues where there is unanimity and consensus among its member associations. In so doing, it only advocates policies which are of general interest all entrepreneurs, leaving the specific sectoral lobbying to its member organisations. The logic behind this strategy is that by becoming involved only in issues in which it can present a unified front to the government, the resulting appearance of unity will improve its bargaining position.¹⁵ The structure of CONFIEP allows any one member association to veto any statement or policy which CONFIEP has prepared.

This policy has both benefits and disadvantages. While this policy of unity increases the legitimacy of CONFIEP's claims to represent the entire bourgeoisie, it also reduces the sphere of action in which it operates. Its policy is clearly to avoid any issues on which there may be conflicting interests, which restricts its scope of action. CONFIEP's position could be strengthened if there was an effective forum for conflict resolution, which would enable it to become involved in a broader range of issues. A weakness of this structure is that it prioritises conflict avoidance over conflict mediation and conflict resolution. It could be suggested, however, that while there are no apparent mechanisms in CONFIEP's present structure for conflict resolution, it is possible that behind closed doors this structure does address intra-class conflicts and resolve disagreements. The negotiation and discussion of policy statements may provide the opportunity for reaching consensus on important policy issues.

¹⁴ The first effort of unification in the 1970s, the UEPP, failed in part because it attempted to involve itself in sectoral issues, causing dissent and conflict between different fractions of the bourgeoisie. See chapter two above.

¹⁵ See for example, Gladstone (1984:26), who argues that an important role of employers organisations is to keep conflicts behind closed doors and to display a united front. Decision makers will be more inclined to feel that the organisation is adequately reflecting the views of its members.

There are signs, however, that a lack of unity continues to plague the business sector. The Minister of Industry in 1985-87, Manuel Romero Caro, who often represented the government at meetings with business leaders put it more harshly. The negotiations, according to Romero, revealed significant conflict:

Within one industrial organisation, textiles for example, the thread makers attack the clothing manufacturers, which in turn attack the knitters. And the textile sector attacks the metal mechanic organisation. That's not even mentioning the conflicts between the industrialists and miners. But if the business sector has those problems, it is the responsibility of CONFIEP organise them...

But no, negotiating with the private sector is easy. Because you destroy them and they fight among themselves. And because they have not reached any agreements between themselves they can't do anything. Take note. What is good for one is bad for the other.¹⁶

Signs of more significant internal conflicts arose in 1989, when traditional exporters, which had policy disagreements with the non-traditional exporters which control ADEX, broke away from the organisation and set up the Society of Exporters.¹⁷ This association has since been incorporated within CONFIEP, but this event reveals marked cleavages within the bourgeoisie which show no sign of fading. This also suggests that cohesion is likely on a long-term basis be found at specific trade levels sharing closely tied economic interests, with a lesser degree of allegiance at a broader level.

CONFIEP has also been less successful in encouraging a pervasive and shared ideological framework within the bourgeoisie. Although one may argue that this is not one the role of a business association, there are signs that business leaders had aspired to increase ideological cohesion. The vice president of CONFIEP reminded members in 1987 that it was not created solely as a

¹⁶ Interview, Manuel Romero Caro (Minister of Industry 1985-87), March 25, 1992, Lima.

¹⁷ Interviews with Roberto Persivale, (former President of ADEX, and Minister of Industry during the Belaunde administration) April 7, 1992, Lima; and Hernan Lanzara, (General Manager of ADEX 1992), April 2, 1992, Lima.

'defensive entity, such as is ordinarily carried out by a trade association.'¹⁸ It was claimed that CONFIEP should also seek to 'develop an economic doctrine within businessmen.'¹⁹

The heterogeneity of the bourgeoisie and its varied economic interest suggests that this is a structural factor which will allow it to obtain only limited levels of cohesion. On issues where more general class interests are at stake, CONFIEP has the potential to become a powerful tool in their defense. Its unity on policies concerning issues affecting businesses in general, such as the labour stability legislation or price regulation, did strengthen its position vis-à-vis the government. Without overemphasizing the unity which CONFIEP has brought about, it can be concluded that throughout the period of Garcia government, class interests did begin to obtain higher levels of cohesiveness, and the sometimes contradictory lobbying of associations such as the SNI and ADEX which occurred prior 1984, was greatly reduced. A more in-depth assessment of the level of cohesion between different class fractions within the bourgeoisie, however, would require a long-term perspective, which would permit fundamental and recurring cleavages to be observed. The period of this study (1985-1990), furthermore, represents a period of low intra-class conflict for two reasons. First, the economic prosperity brought about by the first stage of the heterodox model was widespread, benefiting all commercial and industrial sectors in the economy. The generalised concrete economic gains, meant that policies in the initial period did not have a divisive impact on the bourgeoisie. Secondly, as the previous chapter established, unity was enhanced in the 1987-1990 period by the government's attack on private property rights. Under these exceptional circumstances, the bourgeoisie was able draw together and overlook immediate and sectoral interests.

¹⁸ *Presencia*, February 1987, p. 11.

¹⁹ *Presencia*, October 1987, p. 6.

8.2 The Industrial Bourgeoisie and State in Peru, 1980-90

This thesis has attempted to shed light on important questions regarding the changing role of the industrial bourgeoisie in Peru's political and economic development. This study has a particular salience in a historical context. The conditions which characterised Peru's economic and social structure have made the advent of the domestic industrial bourgeoisie as a clearly identifiable class fraction a late and slow phenomenon. This slow process can be contrasted with the Mexican case, for example, in which the power of the agro-export elite was challenged early in the century, thereby facilitating the development of a domestic industrial bourgeoisie (Story 1986:199). In Peru, however, late industrialisation, the persistent power of the landed oligarchy, and the preeminent role of foreign capital in the initial growth of manufacturing, led to a more active state role to stimulate the domestic industrial bourgeoisie.

Scholarly interest in this question, therefore, was intensified by the ownership reforms of 1968 which reduced the power of the landed oligarchy and promoted domestic industry. Of particular interest was the military government's dual objective of modernising the economic structure and stimulating the development of Peru's nascent industrial bourgeoisie. The long term impact of these reforms, it was suggested in the first chapter of this study, is only now becoming fully apparent. Significant changes have occurred throughout the past two decades in the economic role of the industrial bourgeoisie in Peru and its relationship with the state.

The immediate impact of the Velasco government on the development of the domestic industrial bourgeoisie was mixed. This thesis has offered evidence to suggest that the policies of the Velasco government which restricted the role of foreign capital may have tipped the balance in favour of domestic capital at a decisive period in the development of domestic industry. Yet, while the partial withdrawal of foreign capital in heavy industry, manufacturing and the financial system, facilitated the expansion of local economic industrial groups, the

deepening statism of the Velasco government had an adverse impact on business confidence and alienated industrialists. Elements of the military government's programme, which included policies such as worker participation in manufacturing, provoked a precipitous decline in domestic private investment. These contradictory policies were, in part, responsible for the hesitant response of the domestic industrial bourgeoisie.

The landed oligarchy was not only displaced abruptly as an economic power, but also as a political force. The relationship between Peru's political and economic elites which existed under the oligarchic state was broken decisively by the Velasco reforms. A question which has been implicit in this study is whether the industrial fraction of the bourgeoisie has been able to forge a more or less stable accommodation with policy makers for the common objective of industrial accumulation. The importance of elite convergence for democratic consolidation and political stability has been stressed by Higley and Burton (1989).²⁰ They argue that a structure which allows important elites access and input into the policy making process is needed to avoid political instability, autocratic or short lived democratic governments. A degree of convergence between political and economic elites is also essential for economic stability and sustained growth. In his influential study on Brazil, Evans argues that the ability of local, foreign and state capital to develop a collaborative and mutually beneficial relationship has facilitated the industrialisation of the Brazilian economy. A shared sense of the broad parameters of economic direction, or as Evans found in Brazil, consensus built upon the 'common respect for the logic of profitability', are important prerequisites for establishing a stable political and economic regime favourable to long-term industrial growth (1979:287).

This thesis has revealed considerable disunity and recurring friction between the industrial bourgeoisie and government in the democratic period in Peru. The relationship between industrialists and successive governments since

²⁰ See also Dietz (1992) on the Peruvian case.

Velasco has been characterised by short periods of consensus and agreement, followed by growing disagreement over both the content and direction of economic policy. While the administrations of Fernando Belaunde (1980-85) and Alan Garcia (1985-90) both recognised the need to engage the backing of the domestic industrial bourgeoisie in order to sustain their economic growth strategies, in both cases, they were unable to maintain the support of these sectors. Issues such the reduction in CERTEX tax incentives for exports in 1983 and adverse impact of the international economy in the case of Belaunde; the implementation of pro-labour policies and the attempted expropriation of domestically owned banks under Garcia, have contributed to a long-term deterioration in the levels of business confidence.

Alan Garcia demonstrated an earnest determination to forge a productive alliance between his administration and local industrialists. The heterodox economic strategy provided a promising opportunity for the government to enlist the industrial bourgeoisie into a collaborative and fruitful relationship. The emphasis on reactivation rather than austerity as the key short-term policy objective made this an attractive strategy for industrialists, while the policy of *concertación* did help to revive investor confidence. In addition, the depth of the industrial crisis in the early 1980s, made industrialists more tolerant of reformist and interventionist policies. Garcia's ability to incorporate the industrial bourgeoisie into a multi-class coalition of support for his policies, therefore, further enhanced the prospects for the success of the strategy.

Concertación was born not from a pro-business ideological orientation, but from a judicious assessment of investment requirements. This thesis has argued that *concertación* was essentially a tactical political alliance, which Garcia believed would allow the state to monitor the private sector's investment decisions and enable it to influence the allocation of resources. The heterodox policy makers recognised the need for a profit oriented approach towards investment and explicitly acknowledged the need to preserve profit margins, expand the internal market, and provide incentives for productive investment, in order to create the

conditions favourable to domestic capital accumulation. However, this pragmatic approach towards investment in theory was not evident in practice. In its zeal to appear reformist, and to extend the benefits of the economic reactivation to the popular sectors, Garcia failed to make any tangible concessions which would have indicated to industrialists that the government was responsive their interests and aware of the impact of policies on industry. Moreover, the administration's overriding concern to maximise returns for workers led to high wages and extreme labour stability legislation. Although profits did rise in 1985 and 1986, there is some evidence to suggest that price controls, high wages and the mounting cost of imports did begin to put pressure on profit margins. More importantly, it affected business confidence.

Although the emphasis of this study has been on the political role of industrialists and its evolving relationship with the state, a few reflections can be made regarding the role of the Peruvian industrial bourgeoisie in the development process. It is important to consider, at least in a preliminary fashion, what this case study reveals about the economic role of the domestic industrial sector in Peru.

The economic objectives of Garcia's investment policy necessitated particular political alliances, most notably with the economic groups which controlled the banks and leading industries. Garcia recognised the large scale investment potential of these groups, and gave them a privileged position in the negotiation process. This elite fraction of the bourgeoisie has demonstrated itself to be economically dynamic and adept at developing patterns of organisation which enable capital accumulation to take place despite harsh economic conditions. For the most part, these groups are allied closely with foreign capital, which acts to facilitate their access to technology and capital, and can act to reduce risk through the establishment of joint ventures.

Garcia's focus on the elite and most vibrant fraction of domestic capital has parallels with the triple alliance in Brazil, where all but the transnational element

of the national bourgeoisie are excluded from the alliance (1979). Evans further suggests that the elite consensus which underlies the Brazilian model is fragile and unable to survive if policies serving the interests of the majority are enacted. Dependent development is possible only with the exclusion of both the subordinate fractions of the bourgeoisie and the masses.

This study has suggested that the Garcia case was unusual in that it was a reformist government with redistributive objectives, which nonetheless was able to gain the support and backing of the industrial bourgeoisie for these policies. This support, however, soon faded. Does the industrial bourgeoisie's declining support for Garcia's policies suggest that this exclusionary growth model is inevitable, as Evans hypothesised?

Garcia's economic strategy attempted to achieve rapid industrial growth while extending the benefits throughout society. However, the inflexible handling of the *concertación* strategy, and the failure to make concessions to the industrial sector gave rise to the first tensions within the relationship in the early boom years of the heterodox strategy. The handling of the *concertación* policy illustrates that Garcia failed to develop the astute and delicate balancing of interests which may have prevented the outright opposition of industrialists. This inflexible and uncompromising approach is illustrated most clearly when, in 1987, faced with the growing apprehension of industrialists, Garcia chose to abandon all attempts at *concertación*, rather than renew efforts to negotiate and revive flagging confidence in the administration's policies. Garcia mistakenly believed that the demand induced strategy could be sustained despite the support of the business sector. It is possible that more adept policies by the economic team could have led to improved chances for sustaining the alliance and avoiding the economic collapse.

Despite some policy disagreements, private sector investment did increase steadily from 1985 until the economic collapse in 1988. The policy of selective *concertación* was also successful, having stimulated the development of significant investment proposals from the top twelve groups totalling nearly US\$100 million

for projects in designated priority areas of the economy.²¹

The response of domestic capital as a whole is more difficult to evaluate. While industrialists demonstrated a willingness to accept some elements of reforms, in exchange for an expanded internal market, at the same time they remain sensitive to state intervention. On balance, however, the conditions for domestic capital throughout the 1980s have been largely unfavourable. While there have been short periods of industrial growth, the repeated and prolonged economic crises have eroded the confidence of the industrial bourgeoisie. Given the absence of economic stability and predictable policy, the assessment of future returns on investment become uncertain and risks difficult to estimate. Inconsistent industrial policies and successive industrial collapses have contributed to a pervasive atmosphere of economic crisis and investor instability. While the Peruvian industrial bourgeoisie is much maligned, the lack of domestic economic dynamism can be attributable to a large degree to the adverse conditions in which it operates. Peru has not recently experienced a long-term period of economic stability, accompanied by an expanding internal market, which are needed in order for domestic industry to flourish. While the external constraints on development are considerable and should not be underestimated, a chief impediment facing industrialists is undoubtedly the incoherent economic management and the absence of a consistent policy regime which could provide stable conditions for investment and economic growth. As suggested in chapter two, recurring economic crises give rise to conditions conducive to monopoly capital and reinforce the dominant market position of the economic groups, which have grown to dominate the domestic manufacturing scene by the 1980s.

The discordance between state and industrial bourgeoisie both contributes to and is reinforced by economic instability. Ideological swings from inward looking outward and open industrialisation strategies have been experienced by both the state and industrial bourgeoisie. The state in Peru has been subject to

²¹ See Chapter five. The execution of many of these projects were preempted by the nationalisation and the economic collapse in 1988. Therefore, few were actually implemented.

ideological oscillations, not only between administrations but also within them, and has failed to develop a clear development orientation.

The depth of the crisis under Garcia and evidence of another failed attempt at state directed development, led industrialists to embrace neo-liberalism. The renewed opportunity of industrial support for reform is now a distant prospect. The confidence in any statist policy has been fatally undermined by the inept approach of the Garcia administration and the economic chaos which ensued.

The conflictual relationship between industrial bourgeoisie and state, however, peaked in the late 1980s. The increased presence of Sendero Luminoso in Lima and the magnitude of the economic crisis in the latter years of the Garcia government revealed the fragility of the existing order, and led the bourgeoisie not only to unify as a class, but also to ally itself with other important political actors. The shared perception of growing threats to the economic and political structure provided an important point of convergence between the state, bourgeoisie and the military. These key groups in society entered the 1990s with a greater degree of unity than had existed at any time in the previous decade. The existence of various common enemies, not just the subversive movements but also the APRA party and the Left in general, and the emergence of a shared ideology has cemented this new found alliance between state and bourgeoisie.

This new pact has its origin in the rise of the New Right in Peru. The revitalisation of conservative thought provided an important element of ideological cohesion and justification for a shared direction of national policy. The resurgence of the Right in Peru is not restricted to the bourgeoisie or the intelligentsia, but has received widespread support from sectors which traditionally backed the parties of the left. The potential stability of the alliance was therefore further strengthened by the popular support which the Fujimori government and the New Right has received in Peru. Despite the harsh impact of the orthodox stabilisation on living standards, the popularity of the government remained remarkably high.

The resurgence of neo-liberalism in Peru shadows a shift in development paradigm throughout much of Latin America. Peruvian industrialists anticipate that this new development paradigm will provide the foundation for consensus and a framework for a clear development orientation. While the New Right indicates a basic framework for the broad parameters of economic direction and predictable policy, it also has its limitations. The characteristics of the Peruvian economy which preoccupied the heterodox policy makers, such as the regional concentration of production, the existence of monopoly capital, and the extreme disparities of wealth and income, are unlikely to be remedied purely through a free market approach. The issues of a more equitable distribution of wealth and the provision of health and education, remain essential but formidable tasks requiring an adept and efficient state. Yet, the policy prescriptions of the New Right end at the sharply cutting back the state, rather than reconsidering and redirecting the role of the state to constructive social ends. In this single minded focus on deregulation and free markets, the New Right reveals its fundamental weakness (Philip 1990).

Moreover, the long-term prospects of the alliance of state and industry based on liberalising the economy are uncertain. The ambivalence of businessmen who backed the New Right after the disastrous experience with the heterodox interventionist policies is reflected in statements such as that made by Julio Piccini, founder of CONFIEP, in 1992:

I don't believe in policies which are entirely liberal or conservative. If I could quantify it, I would say that I'm 80 percent liberal and 20 percent protectionist.²²

This ambivalence illustrates that the political views of capitalists are shaped by their assessments of the potential for accumulation. In other words, while industrialists in the late 1980s may espouse neo-liberal economic principles, in practice, the free market will only be accepted by individual businessmen if they feel they will benefit. This hesitant approach to liberalisation became apparent during the election campaign. In 1990, the President of the SNI, Salvador Majluf,

²² Julio Piccini (founding President of CONFIEP), interview in *La Banca*, January 1992, p. 18.

had various meetings with FREDEMO and Libertad policy makers, encouraging them reconsider their policy on tariffs, which he worried would be 'drastic'. The policies being proposed, he claimed, could have a detrimental effect on many sectors of industry.²³ The industrial bourgeoisie's support for Libertad's neo-liberal stance, even at the height of the rise of the New Right, was not unqualified.

However, in the 1990s, the state and industrial bourgeoisie have demonstrated a new found consensus. The extent of this unity was most clearly revealed in 1992, when the democratically elected President Alberto Fujimori closed Congress, suspended the constitution and in an alliance with the military assumed dictatorial powers. In the days after the coup, business leaders scarcely veiled their support for these measures in public statements. The basis of support underlying the 'auto-coup' was an alliance between Peruvian elites, in which Fujimori was backed by the military, as well as the industrial bourgeoisie. In the months following the coup, Fujimori made repeated overtures to industrialists in order to ensure their backing. When the Minister of Finance Carlos Bologna resigned in 1992, he was replaced by Jorge Camet, a former president of CONFIEP. The government's active courting of industrialists to cement its power has reinforced the industrial bourgeoisie's new-found role in politics.

However, one must be cautious about making conclusions regarding the stability of this alliance at this stage. The increasing conflicts within the military, are one indication that this alliance, born from a period of intense political instability and threats the existing order, may be fragile. As noted by Higley and Burton (1989), transitions from elite disunity to elite consensus are usually temporary, and not enduring. In the Peruvian case in particular, this coalition was created principally as a response an immediate crisis, which may dissolve once the shared perception of threats to the system wane.

²³ *Resumen Semanal*, quoting the major dailies, January 17, 1990.

This thesis has shown, therefore, that there is a fluid and intense process of social change and political transformation under way in Peru. This thesis has examined the changes in one class fraction, the industrial bourgeoisie, and has highlighted the circumstances under which this fraction can form alliances with other fractions of the bourgeoisie. The period of this study has illustrated the changes in the changes in the way in which the bourgeoisie perceives its role in the political process and suggests that this may have an important impact on contemporary Peruvian politics. This study, therefore, raises as many questions as it answers. Does this process of unification of the bourgeoisie and evidence of at least an incipient class project indicate the hegemonic potential of this class? Will the recent alliance between state and industrial bourgeoisie under the Fujimori government indicate an era of stable policy and elite consensus leading to an 'alliance for profits', or will this recent unification prove once again to be a temporary coalition?

According to Higley and Burton (1989) an alliance between political and economic elites is a necessary prerequisite for democratic consolidation. It is clear from this examination of the relationship between industrialists and the state in the 1980s that a degree of collaboration and consensus is needed to enhance the prospects for economic growth. This hypothesis will soon be tested, as the Fujimori attempts to implement a Peruvian version of the 'alliance for profits'. However, this purely capitalist growth model may turn out to be exclusionary as the 'Triple Alliance' in Brazil (Evans 1979) and in so many other developing countries.

The experience of the Garcia government discussed in this thesis, however, presented tantalising evidence to suggest that private sector investment can be generated in a context of a reformist model designed to spread the benefits of economic growth downward. Rather than dismissing non-orthodox approaches to economic development, it should be remembered that the Garcia government's efforts failed largely as a result of economic mismanagement and political misjudgments, rather than because of the incompatibility of his objectives. It is

this lesson of the Garcia government which must be underscored. We can only hold out hope that this potentially more stable alliance of the 1990s can be used as a basis for long-term, consistent economic growth with benefits extending to the marginalised groups of Peruvian society.

Appendix 1: Ownership in the Manufacturing and Mining Sectors

Table 1 Textile Sector: Top 15 Companies in 1986 (gross income and origin of capital)

Company Name	Income ¹	Origin ²	Group
La Union	970,448,100	domestic	Brescia
Textile Piura	389,367,600	domestic	Romero
Michell y Compania	330,127,500	domestic	Michell
Universal Textile	316,495,800	domestic	Romero
Tejidos San Miguel	293,957,600	domestic	-
Vitarte Victoria	279,077,600	domestic	Brescia
Fabritex	221,673,000	domestic	-
Credisa	201,652,000	n.a. ³	-
San Jacinto	188,213,500	domestic	-
Hilos Cadena Llave ⁴	185,469,400	foreign	-
Industra Nacional	181,560,000	domestic	-
La Parcela	179,154,600	domestic	Ferand
Textile San Pedro	156,942,600	n.a.	-
El Progreso	153,136,000	n.a.	-
La Bellota	131,118,000	domestic	Nicolini

¹ The income and group ownership of the top fifteen companies is drawn from The Peru Report, *The Top 1500*. 1988. Income is shown in intis.

² The origin of capital was drawn primarily from Ludvico Alcorta, *Concentracion y Centralizacion de Capital en el Peru: Descripcion, Efectos y Politica Publica*. 1987. Lima: Fundacion Friedrich Ebert; *The Andean Report*, 'The Andean Report 1,000', January 1989 and *The Andean Report*, 'Groups 250', April 1990.

³ Information not available.

⁴ Hilos Cadena Llave is listed as foreign owned in the Andean Report (1989) list of foreign top fifty companies and as owned by the Brescia group in the Peru Report's *The Top 1500*. This suggests that it is of mixed capital. It should also be pointed out that the ownership classifications used here do not necessarily mean that ownership is either 100 percent foreign or domestically owned, rather it refers to the majority shareholders.

Table 2 Agro-industrial Sector⁵: Top 15 Companies in 1986 (gross income and origin of capital)

Company Name	Income	Origin	Group
Nicolini Hermanos	1,832,100,000	domestic	Nicolini
Backus y Johnson	1,534,212,000	domestic	Bentin
Nacional de Cerveza	1,259,900,000	domestic	Lanatta
Industrias Pacocha	1,100,096,000	domestic	-
Gloria	1,048,751,000	domestic	Berckemeyer
Cia. Molinera	999,276,000	domestic	Nicolini
Molinos Mayo	812,659,000	domestic	Ikeda
Molinera Santa Rosa	810,860,000	foreign	La Fabril
Perulac	763,454,000	foreign	-
Cia. Cerveza sur	583,607,000	domestic	-
Ind. Del Sur	532,592,000	foreign	-
Tabacalera	501,290,000	foreign	Fierro
Molitalia	422,509,000	domestic	Lanatta
D'onofrio	408,879,000	domestic	-
Molinera Inca	391,350,000	domestic	Nicolini

⁵ Fishing and fishmeal production has been excluded from this table.

Table 3 Mining Sector: Top 15 Companies in 1986 (gross income and origin of capital)

Company Name	Income	Origin	Group
Minpeco	8,674,200,000	state	-
Centromin	4,671,800,000	state	-
Southern Peru	4,146,500,000	foreign	-
Empresa Minera Peru	1,964,400,000	state	-
Hierro Peru	979,700,000	state	-
Tintaya	775,300,000	state	-
San Ignacio	476,800,000	domestic	Arias
Minera Milpo	442,900,000	domestic	-
Minas Orcopampas	398,600,000	domestic	Buenaventura
Minas de Arcata	328,700,000	domestic	Hoschild
Minas Buenaventura	324,600,000	domestic	Buenaventura
Minera Atacocha	287,500,000	domestic	Brescia
Minera Santa Luisa	268,000,000	domestic	-
Minsur	257,300,000	domestic	Brescia
Minera Raura	232,700,000	foreign	-

Table 4 Petro-chemical Sector: Top 15 Companies in 1986 (gross income and origin of capital)

Company Name	Income	Origin	Group
Quimica Suiza	971,357,000	foreign	-
Bayer Industrial	918,317,000	foreign	-
Cia. Goodyear	744,285,000	foreign	-
Lima Gaucho	541,563,000	foreign	-
Productos Favel	495,016,000	domestic	-
Rayon y Celanese	490,091,000	foreign	-
Bayer Quimicas	400,043,000	foreign	-
Shell	360,487,000	foreign	-
Filamentos Ind.	351,876,000	n.a.	-
Peruplast	316,880,000	domestic	-
Hoeschst	316,407,000	foreign	-
Bekelita y Anexos	262,743,000	n.a.	-
Tecnoquimica	236,472,000	n.a.	-
Industrias Vencedor	229,670,000	domestic	-
Emsal	206,802,000	n.a.	-

Table 5 Capital Goods Sector: Top 15 Companies in 1986 (Gross Income and Origin of Capital)

Company Name	Income	Origin	Group
Toyota	872,559,000	foreign	-
National	610,340,000	foriegn	-
Nissan	581,715,000	foriegn	-
Volvo	453,947,000	foreign	-
Industrias Reunidas	408,879,000	domestic	Lanatta
Fessa	349,590,000	n.a.	-
Indeco Peruana	338,940,000	foreign	-
Philips	298,091,000	foreign	-
Motores Diesel	267,681,000	state	-
Envases Metalicos	263,864,000	n.a.	-
Fabrica de Aluminio	215,900,000	n.a.	-
Sunbeam	191,315,000	foreign	-
Motor Peru	184,122,000	foreign	-
Industria Electrico	160,507,000	n.a.	-
Manufactura Record	160,217,000	domestic	-

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