THE FIRST EXCHANGE CONTROLS AFTER THE EXIT FROM THE GOLD STANDARD IN ARGENTINA (1931-1933)

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1. **Introduction**

More than 90 years after the introduction of the first exchange controls, Argentina has yet to find a stable monetary course, currently maintaining strict exchange controls. The exchange controls implemented in 1931 and 1933 ended the gold standard and paved the way for the creation of the Central Bank in 1935. The gold standard had been confined to the past. The abandonment of the gold standard was justified by a belief in a definitive solution based on two main pillars of economic policy: an exchange control regime and the eventual establishment of the Central Bank, with objectives incompatible with the gold standard.

The adjustments to the first exchange control in 1931, carried out in 1933, introduced a system with multiple exchange rates, which served as a tool of economic policy to transition a new system. In an international context of regime change, this approach did not ensure the desired monetary equilibrium but instead abandoned the idea of sound money, in the face of the change in the productive and distributive patterns of the Argentine economy.

To analyze the first exchange controls implemented in Argentina, we will review the pre-existing economic, monetary, and political contexts. Although these controls differed in their design,

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causes, and consequences, they unified their advancement of greater intervention under the pretext of seeking "monetary equilibrium". This process led to the definitive institutionalization of a state monopoly on currency issuance, enforced through legal tender status and the creation of the Central Bank of the Argentine Republic (BCRA) just two years later.

This analysis will explore the implications of these controls and their role as tools for economic policy intervention, which ultimately facilitated the abandonment of the gold standard and moved Argentina away from the concept of sound money.

Subsequent sections will review the economic and political context, incorporating a literature review from the perspective of the Austrian School of Economics. This review will elucidate the actors of the time and the theoretical and economic fundamentals underlying the various monetary events. These events progressively constrained individual freedom, denying the possibility of a sound money system. The institutional design of the initial exchange controls in Argentina will then be examined, highlighting how they led to the creation of the Central Bank of the Argentine Republic and the establishment of "monetary socialism." The final section will present the main conclusions of the analysis.

2. **The economic and political context**

The end of convertibility, which had been established in 1899, was solidified by the implementation of exchange controls in response to currency depreciation. This marked a significant shift in Argentine economic policy. The crisis of the 1890s prompted the establishment of a new monetary order in the country, characterized by the creation of the Currency Board. This new system, along with the Convertibility Law and the Banco Nación—established in 1891 and functioning as a "bank of banks" prior to the creation of the Central Bank—introduced mechanisms such as the rediscounting of commercial paper. Together, these elements constituted the framework of the new monetary order that prevailed until 1914.

Although the monetary scheme was fully implemented in 1899, it provided the necessary stability for coordinating and promoting

economic activities of the time. Nonetheless, it retained certain institutions that contributed to the failure leading to the 1890 crisis. Specifically, during the period 1822-1881, literature indicates that the Province of Buenos Aires was characterized by a monopoly on currency issuance and the imposition of legal tender status on the banknotes issued by these entities. The country's main province had adopted monetary institutions from United Kingdom, France, and other European countries, which stifled banking competition by establishing a monopoly on currency issuance through successive banks and enforcing legal tender status for their banknotes. This approach diverged from a system of healthy banking competition (Ravier, 2016). Additionally, evidence of monetary disorder in Buenos Aires supports the literature suggesting that financial crises, in the absence of a central bank, do not inherently indicate banking instability, but rather that fiscal imbalances are a typical factor contributing to such crises (Cachanosky and Ravier, 2022).

In 1890 the system of Guaranteed Banks entered a deep crisis that ended with the then President Miguel J. Celman. Quoting Zylberberg: "… the issues guaranteed by the Nation and with cancellable force in all the territory of the Republic unleashed the inflationary spiral, which culminated with the fall of President Miguel Juarez Celman in 1890. The Guaranteed Banks promoted with insolvent credits, irresponsible speculations, of all kinds, with whose negative results the Nation's debts multiplied…" (Zylberberg, 2017).

When Vice President Carlos Pellegrini assumed office on August 6, 1890, he implemented various economic measures to restore stability. Among these measures were the authorization of external debt issuance and the creation of the "Currency Board" following a bailout issuance. The main function of the Currency Board was to organize national issues and to attend to the circulation and gradual amortization of legal tender, independently of the National Government. (Giacomini, 2020).

Thus, by controlling the money supply, a return to gold parity was proposed, aiming to redeem the banknotes issued by the Guaranteed Banks within ten years. Once the gold standard was reestablished, the Currency Board would exchange national pesos

exclusively for gold, under stringent control over the money supply expansion, which precluded financing the Treasury. The redemption of the Guaranteed Banks' banknotes was to be achieved through the creation of the "Conversion Fund," financed by the remaining metallic reserves of the Guaranteed Banks, government budget surpluses, international debt placements, and new taxes proposed by President Carlos Pellegrini and submitted to Congress to support the currency and banking system following the crisis. In the subsequent year, the Banco Nacional and Banco Provincia were authorized to suspend payments on their deposits, and the Guaranteed Banks transferred their assets and liabilities to these institutions.

According to Giacomini*:* "… the internal debt bonds of the Nation with the provinces were redeemed, and the Nation assumed the provinces' debts in the European financial markets. In other words, the Nation was left with two liabilities: the monetary base of the Guaranteed Banks and the provinces' foreign debt…" Additionally, in the same year, the Banco Nación was established and commenced operations in December 1891. Giacomini further notes*:* "… In summary, Pellegrini achieved, in monetary terms, what all previous Argentine presidents had failed to accomplish during the first 30 years of the union between the Confederation and the Province of Buenos Aires: the Nation was left with a monopoly institution for monetary policy ("Currency Board") at the national level, as well as a large National State bank capable of guiding credit policy. The objective was to establish a gold standard. The path to this goal was monetary responsibility…" (Giacomini, 2020).

However, until the Currency Board became fully operational in 1899, the monetary base expanded, causing a decline in the demand for money, which led to increased inflation and a surge in the exchange rate. Subsequently, monetary prudence was maintained, and as secondary money creation diminished, economic stabilization was achieved. Consequently, the real exchange rate stabilized, as there was no surplus of pesos, and individuals could demand the preferred currency: gold, since the peso was backed by metal reserves. Later, the currency even appreciated with the inflow of capital, which facilitated the full operation of the Currency Board on October 31, 1899. (Giacomini, 2020).

Once the Currency Board was fully operational under Law 3,861, and in Liliedal's words: "… While the country's situation was improving significantly, the economic recovery was becoming stronger, and the country was visibly recovering from the effects of the crisis it had suffered. International trade figures became favorable, immigration was increasing, and the construction of new railway lines was incorporating these areas of wealth into productive activity. The political climate also began to stabilize, and under the influence of these factors, the peso gradually recovered. Consequently, the gold premium on paper was falling. The peso was naturally seeking its own level, tending toward parity. The increase in wealth on the one hand, and the cessation of emissions on the other, were driving this phenomenon, which, in essence, is a confirmation of the well-known quantitative theory of money, according to which the unit value of currency is directly related to demand and inversely related to supply…" (Liliedal, 1950).

It can be seen how monetary stability fosters an environment for the generation of wealth and prosperity, which allows the full operation of the entrepreneurial function, where the amount of money is not a determining factor, but rather the stability of supply, if it is the currency that individuals freely wish to demand. The essence of Law 3,871 is found in its article 7: "…The Currency Exchange Bureau will deliver to whoever requests it, legal tender bills, for stamped gold coin, in the proportion of one peso of legal tender for forty-four cents of stamped gold weight and will deliver the gold it receives by this means to whoever requests it in exchange for paper currency at the same exchange rate…".

The system implemented was like that of the United Kingdom, featuring both a conversion office for metallic and banknotes and a prominent commercial bank larger than the rest. However, there was a significant difference regarding the initial backing of the currency, as the Argentine scheme did not have gold at the time of the creation of the Currency Board (Gerchunoff, 2016). Thus, a Conversion Fund was created, which was sustained by the growth of exports in both volume and price of exportable products. In this way, the system was consolidated. The growth of exports increased the Conversion Fund, thereby increasing the holdings of gold and

its counterpart in the expansion of the monetary base. This, in turn, stimulated economic growth and the demand for money.

It was observed that the system guaranteed monetary stability, supported by a gold standard in which paper money was freely convertible into gold within the Currency Board. As exports increased, leading to a rise in aggregate demand, the liquidation of gold by the Currency Board provided the economy with the necessary pesos to meet the increased demand resulting from economic expansion.

In this way, the system would adjust according to the fluctuations and needs of commerce. The then Minister of Finance, J.M. Rosa, expressed this sentiment: "… There is no other system of circulation more perfect than one that allows gold to leave the country or flow into it according to the needs of our international exchanges, or paper to circulate according to the needs of our internal market…". This is what the Minister referred to as "free and elastic" circulation.

Until the Currency Board became fully operational, the exchange rates of the gold peso exhibited the following declines relative to the legal tender peso from 1894 to 1899: -3.62, -3.42, -3.00, -2.92, -2.43, and -2.27, falling below the value of 2.07, which was intended to be stabilized according to the law of its creation. Certain influential commercial circles opposed the sustained appreciation of the currency due to its unfavorable impact compared to the depreciations to which they were accustomed, such as agricultural and livestock producers who were affected by the export of their goods. However, the impact on economic development was highly favorable: "… Its inspiring purpose was, as I have already said on another occasion, to consolidate the then existing situation, providing a certain basis in contracts, business, and all economic factors, with the aim of eventually achieving a sound money capable of ensuring and promoting the future development of the country. The insecurity that had characterized the currency, directly affecting commercial transactions, industrial development, and inhibiting legitimate business, were factors that undermined the higher interests of the community and needed to be addressed. That was precisely the aim of the law…" (Liliedal, 1950).

Furthermore, beyond the context, the readjustment of the tax system and the fundamental trend towards fiscal balance played a

crucial role. Consequently, the country accumulated a substantial gold reserve, which enabled it to maintain a cash coverage over the circulating currency that exceeded 80% at certain points in its operation, making it one of the highest gold reserves in the world. It is important to emphasize that, in economic terms, it was the monetary stability provided by the system that facilitated the availability of the money individuals wished to demand. The gold implicitly backed by the Currency Board ensured this stability. This stability, in turn, fostered economic growth by enabling better social coordination and responding to the increased demand for money generated by economic expansion with a correspondingly greater amount of gold-backed currency. Thus, it was not the increased money supply that drove economic activity; rather, it was the stability of the monetary system itself that contributed to sustained economic growth. Similarly, a reduced money supply would not necessarily curtail the economic growth facilitated by this monetary stability.

Politically, the adoption of this monetary scheme offered stability in contrast to the prior turbulent experience of unbacked currency issuance during the 1880s, which had culminated in the most severe financial crisis of that decade. Additionally, the gold standard was the monetary system adopted by the leading world powers, a prestigious club to which Argentina aspired to belong.

2.1. *World War I: Balance of Payments and Exchange Rate System.*

In 1914, with the onset of World War I, the monetary system implemented in Argentina faced its first significant shock. As noted by Pablo Gerchunoff: "… it was the first indication that the system would not last forever…" (Gerchunoff, 2016). In 1913, following an increase in interest rates by United Kingdom, Argentina experienced a substantial outflow of capital. Under the existing monetary system, this outflow led to a reduction in the Currency Board's gold reserves, which in turn resulted in a decrease of approximately 5% in the currency in circulation. The literature indicates that this external shock was being absorbed by the system in this manner.

Company bankruptcies increased, and real estate prices fell significantly. A notable observation is that while deposits in private banks experienced substantial declines, deposits in Banco Nación grew, likely due to the perceived security of state backing (Gerchunoff, 2016). This period marked the early signs of a "statist" perspective gaining traction in economic institutions, extending into the monetary sphere. As Mises observed: "…For the statist, money is the creation of the state, and the esteem in which it is held is the economic expression of the respect or prestige enjoyed by the state…" (Mises, 2012).

Under the current monetary system, the money supply could only increase in proportion to the gold entering the Currency Board. This requirement ensured that the currency in circulation was fully backed by gold, thereby allowing individuals to demand and pay with the money they required, which in turn guaranteed monetary stability. Nonetheless, there was an ongoing belief in the need for a larger money supply and greater flexibility within the system. With the outflow of capital, the system became increasingly dependent on the external sector to bolster gold reserves—an effort hindered by the poor harvest of the 1913-1914 campaign. Consequently, the system faced a decline in deposits and a bank run, leading to a temporary suspension of the monetary scheme and a halt in the delivery of gold. This measure aimed to mitigate the contractionary effects of rising interest rates and slow the reduction in the money supply, a phenomenon automatically triggered by the system. However, such actions were undermining the very monetary stability that the system was designed to provide.

The bank run occurred because the system did not guarantee 100% of deposits in cash, leaving it inherently vulnerable from the outset. Instead of honoring contracts and acknowledging the misallocation of credit by certain banks, the decision was made to socialize the losses. This was achieved by violating property rights through the suspension of gold deliveries and injecting liquidity into the system without proper backing. This approach was intended to prevent losses for major companies connected to powerful banking circles while also financing the government deficit.

Faced with the erroneous concept of a currency shortage, the government authorized Banco Nación to rediscount commercial

papers from other banks with backing from the Currency Exchange Fund. This action partially fulfilled the functions of a Central Bank, which did not yet exist. Additionally, in response to the increasing fiscal deficit, resulting from spending that exceeded the decrease in tax revenue from imports due to the war, Banco Nación, despite its limited capacity to assist the Treasury, used the rediscounting of treasury bills held by private banks to finance the fiscal deficit. In doing so, Banco Nación acted as a "lender of last resort," anticipating the role of a Central Bank.

Law 9,479 on the "Conversion Fund and Rediscount Operations," published on August 13, established:

> "… Art. 1: While Banco de la Nación Argentina is not permitted to use the conversion fund for the exchange operations described in Article 6 of Law 3,871, it is authorized to convert and mobilize the Fund in a manner deemed appropriate by its Board of Directors.
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> Art. 2: With prior authorization from the Executive Branch, the Currency Board is authorized to perform rediscount operations on commercial documents, or at Banco de la Nación Argentina, by issuing the necessary banknotes in the types currently in circulation, provided that the metallic backing of the legal currency does not fall below forty percent.
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> Art. 3: The Currency Board will only rediscount documents with a term not exceeding 180 days from Banco de la Nación Argentina's own portfolio and those it has rediscounted from other banks within the Republic…."

Through these mechanisms, the economy was "stimulated" by increasing credit without corresponding backing, set against an unfavorable international context and a decline in economic activity. This shift opened the way to discretionary monetary policy. In what would now be considered a "liquidity" crisis, fiduciary currency was introduced without gold backing, expanding the money supply amid declining demand. Consequently, the quantity of money increased without gold backing, despite a reduced demand for it by individuals. This mismatch between the amount of money in circulation and the actual demand led to a depreciation of the currency, initiating an inflationary period as described by Mises.

The deliberate policy of increasing the money supply without proper backing was a significant factor in the resulting monetary imbalance. However, under the system proposed by the Currency Board, the quantity of money in circulation was not just a minor issue, it was fundamentally irrelevant. The system was designed to ensure stability and provide monetary equilibrium, effectively countering the forces that contributed to the crisis.

In this manner, the possibility of financing the fiscal deficit was introduced through the issuance of currency without gold backing. Politically, however, it was crucial to avoid publicly acknowledging the use of this power, as it would have undermined the foundational principles of the monetary system. Thus, between 1914 and 1927, an asymmetrical "one-handed" gold standard system operated (Gerchunoff, 2016). Under this system, the Currency Board monetized inflows of gold, but refrained from selling gold, thereby avoiding monetary contraction. As a result, gold prices remained above the imposed parity, while the agency intervened to buy gold at the established parity of 2.27 paper pesos per gold peso.

Signs of the abandonment of the gold standard system began to emerge as the system, initially requiring 100% gold reserves, started to fail. This failure led to the allowance of credit creation without gold backing by the banking system. The concept of a "one-handed" gold standard is inherently flawed, as it contradicts the principle of ensuring currency circulation backed by gold. Essentially, it permits the issuance of fiduciary money without gold support and disrupts the free market mechanisms that provide the currency individuals wish to demand. The Currency Board was designed to ensure that individuals could obtain the currency they desired, thereby upholding the principle of private property. When the Currency Board's mechanism fails to uphold this promise and individuals cannot obtain the currency they need, the monetary system no longer fulfills one of the basic principles essential for human development in society.

However, during the years of World War I, the inflow of capital ceased, and there was also a significant decline in imports, resulting in a trade surplus and a positive balance of payments. Under the "asymmetric" gold standard system, this situation enabled the growth of the Currency Board's reserves and a corresponding

increase in the currency in circulation, with the paper peso maintaining a value very close to its parity. This development led to the belief among contemporary political leaders that the end of the war would facilitate a full return to the gold standard, heralding a "return to normalcy".

2.2. *Mises and the Balance of Payments*

The historical analysis of the events argues that the end of World War I exposed the weaknesses of the gold standard for Argentina, particularly the rigid relationship between the balance of payments and the money supply. According to this perspective, the gold standard exhibited procyclical behavior, exacerbating the crisis by contracting the money supply in response to a deficit balance of payments and worsening the economic recession due to declining exports. In reaction, the government implemented a series of changes in exchange regulations that eroded confidence in the monetary orthodoxy imposed by the gold standard. This led to a further depreciation of the peso against gold and gold-convertible currencies such as the dollar. Increasing intervention distanced individuals from the currency they wished to demand, resulting in a monetary imbalance that eroded the currency's value relative to other goods, gold, and the dollar, driven by inflationary policies. Mises, in his work on the theory of money and credit, argues:

> "… According to the current view, the maintenance of sound monetary conditions is possible only by a 'creditor balance of payments.' A country with a 'debtor balance of payments' is assumed to be incapable of permanently stabilizing the value of its currency; the depreciation of the currency is assumed to have an organic basis and to be irremediable unless the organic defects are eliminated. The refutation of this thesis and the corresponding objections are implicit in the quantity theory and Gresham's law. The quantity theory says that money can never permanently flow abroad from a country in which only metal money is used (the 'purely metal money' of the monetary principle) … State intervention to secure the necessary amount of money for the community by regulating its international movements is superfluous. An unwanted flow of

> money can never be anything other than the result of state intervention in providing currencies of different values with the same legal tender. All that the state needs and can do in order to protect the monetary system from disturbance is to abstain from such intervention. This is the essence of the monetary theory of the classical economists and their immediate successors, the Monetary School. This doctrine can be refined and extended with the help of modern subjective theory; but it cannot be eliminated, nor can it be put somewhere else… When a country has substituted credit money or token money for its metal money, and as a result of the legal proportion between the excess of banknotes and metal money setting in motion the mechanism described by Gresham's law, it is often asserted that the balance of payments determines the exchange rate. But this is also a totally inadequate explanation. The exchange rate is determined by the purchasing power of the monetary unit of each kind of money… No country, not even the poorest, should give up hope of a sound currency. What depreciates the currency is not the poverty of individuals and of the community, nor indebtedness to foreign nations, nor unfavorable conditions of production, but inflation. Hence all the means employed to prevent a depreciation of the currency are useless…" (Mises, 2012)

2.3. *Money Supply and Demand in Response to Economic Growth*

Beyond the immediate economic challenges, a significant structural change was unfolding, one that was not fully acknowledged by the leaders of the time and was inconsistent with the monetary framework established by the gold standard. This change involved a shift in the productive and distributive patterns of the economy. During this period, there was a relative expansion in sectors such as industry and services, while agricultural activity declined. Industry and services are inherently more money-intensive due to the higher volume of transactions required, which contributed to an increased demand for money within the Argentine economy. As Pablo Gerchunoff explains:

> "…To generate a value-added unit in a production such as wheat, grains from the previous harvest were needed for sowing, available

> land, the work of the field man, and the help of the climate, among other elements, among which money must not have played an essential role. On the other hand, to generate a value-added unit in the industrial sector, given the typical plurality of companies involved in the production of the same product, money surely played a much more relevant role, as it was vital to facilitate the multiple exchanges required by the activity. It can also be assumed that services such as trade demanded more money per value-added unit than the primary sector…" (Gerchunoff, 2016).

Exports, for their part, experienced a decline in demand relative to domestic spending, with increased consumption and investment also reflecting a shift in the distribution pattern. This shift favored wage earners, a segment of society that retained a larger proportion of their income in monetary form. As a result, the change in the distribution pattern contributed to a heightened demand for money.

From the Austrian School of Economics perspective, we can identify at least three key flaws in the underlying arguments. First, there is the erroneous notion of an "optimal money supply," which implicitly fears deflation without distinguishing between its various types or causes, and thus fails to differentiate their consequences, while arguing for the "inelasticity" of the system. Second, the theory of the balance of payments as it relates to monetary policy, as outlined by Mises in his 1912 work, "The Theory of Money and Credit," is presented as a foundational element of statism's monetary policy. Third, the shift in the productive and distributive patterns, driven by the relative growth of the industrial sector compared to the agro-export sector, which required more money, indicates that the gold standard system established by the Currency Board was not an impediment to economic development. In fact, one could argue that it was the institutional mechanism that provided the economy with a stable and predictable monetary system, thereby enabling individuals of that time to optimally exercise their "entrepreneurial function"[1].

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[1] As Huerta de Soto defines it, *La Escuela Austriaca: mercado y creatividad empresarial*, ob.cit. 2da edición, p. 35: «Para los austriacos, en sentido general o amplio, la

2.4. *Financial Inelasticity, Optimal Money Supply, and Deflation*

The increase in economic activity generates a greater demand for money, which, during the war period, was guaranteed by the monetary scheme due to a trade surplus. The inflow of gold, converted through the Currency Board, created the monetary base required by the economic expansion.

However, the Currency Board scheme did not respond with an increased money supply to the shift in the productive and distributive patterns occurring in the 1920s, which demanded more money. The scheme did not generate an automatic mechanism for increasing the money supply in response to rising economic activity (and aggregate demand), particularly from the industrial, construction, or service sectors aimed at the domestic market. It did not generate this, nor was it necessary. The shift in the productive and distributive patterns did not contribute to an imbalance in the monetary market. Contrary to the assertions of many authors, the demand for money grew faster than the output while the money supply grew slower than the output (Gerchunoff 2016), citing Joseph Schumpeter in his *Theory of Economic Development,* indicating that financial scarcity was a serious obstacle to growth.

2.4.1. The Flawed Argument of "Financial Inelasticity"

The issue of "financial inelasticity" posed by the system was thus brought into question. However, a change in regime was politically unacceptable, as the system itself provided for an automatic adjustment mechanism through capital inflows in response to rising domestic interest rates. This gold inflow was converted into paper pesos by the Currency Board, restoring equilibrium. Nevertheless, it is argued that the new problems of the era, particularly the changing nature of money demand, were being ignored.

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función empresarial coincide con la *acción humana* misma. En este sentido podría afirmase que ejerce la función empresarial cualquier persona que actúa para modificar el presente y conseguir su objetivo en el futuro».

Thus, the "one-handed" gold standard was established, which did not solve the problem but was politically more viable than a regime change. The Radical governments used various tools to alleviate the supposed monetary imbalance:

i) paying debt using the gold from the Currency Board at the legal parity without reducing the currency in circulation, and
ii) manipulating the money supply through the money multiplier without affecting the monetary base by altering bank reserves.

The increase in the money multiplier due to the reduction in reserve requirements was a response to the changes occurring in the productive and distributive patterns of the economy. This tool, although innovative, brought costs and risks by weakening the system's solidity through reduced bank reserves. The literature also presents econometric evidence of the actions of Banco Nación, which decreased reserves to increase loans given their deposits, thereby affecting the money supply through an increase in the money multiplier (Salama, 1997). All of this was done without any gold backing, thus weakening the banking system.

The subsequent capital inflow into the economy, coupled with the global consolidation of the gold standard, helped overcome the challenges posed by the system's inelasticity. As a result, full convertibility under the gold standard was restored, highlighting the importance of not only belonging to an elite group of countries but also the expectation of a robust system that moved away from the monetary mismanagement experienced at the end of the century. Based on this argument, we might then investigate whether the return to the full operation of the Currency Board was driven by "economic theory" or by the political benefits that the leaders of the time gained, given the negative experience individuals had, culminating in the crisis of 1890.

However, the context had changed. The shift in production and distribution patterns was evident in the demand for money. When the economy faced an external crisis due to a new outflow of capital and a decline in import prices, it led to a balance of payments

crisis, making the parity between the peso and the dollar unsustainable. The global context did not help, and with the financial crisis of 1929, the Currency Board was discontinued.

2.4.2. The Mistake of Optimal Money Quantity and the Fear of Deflation

Money is an instrumental good, lacking subjective value once used as such. It functions to acquire other goods, which do possess subjective value. According to Mises in *The Theory of Money and Credit*, which builds on Menger's contributions to monetary theory, the subjective value we attribute to money can be viewed as the utility of the goods we could acquire with it, either presently or in the future (Giacomini, 2020). In other words, money serves as both a store of value and an "intertemporal" medium of exchange. Thus, the demand for money is always connected to the demand for goods and services, whether as a medium of exchange in the present or as a store of value for the future. Consequently, as economic activity increases, so does the demand for money, and vice versa.

Recall that Mises describes deflation as "… is a decrease in the quantity of money (in the broadest sense) that is not counterbalanced by a corresponding decrease in the demand for money (in the broadest sense), so that there must be a rise in the objective exchange value of money…" (Mises, 2012). If the money supply grows less than the demand for money due to an increase in the production of goods and services, a potential "deflation" occurs. This deflation is not a cause of decreased economic activity but rather an increase in the purchasing power of the currency. However, as Phillip Bagus explains, the causality of these events is often misunderstood when they occur simultaneously (Bagus, 2021). Deflation is a response of the currency to the increase in the production of goods and services. It is the rise in economic activity that drives an increase in the demand for money, as it is "tied" to the demand for goods and services.

The justification for implementing this "one-handed" scheme, which violates property rights and breaches contracts between commercial banks and depositors, is to avoid falling into "deflation,"

which is considered by mainstream economics to be the greatest macroeconomic evil. The supposed scarcity of money not only does not hinder economic growth but does not necessitate a higher amount of money under the argument of an "optimal quantity." As described, the subjective value of money derives from the utility of the goods it can acquire, both presently and in the future, depending on the extent to which it is used, with the general price level varying for each amount of money. Therefore, there is no optimal growth rate of the money supply required by the economy (Giacomini, 2020). According to Bagus, economists from the Austrian School of Economics with a "Misesian" tradition do not see problems with price deflation caused by economic growth due to an increase in the demand for money (Bagus, 2021). This was the case observed in Argentina under the gold standard, which ensured the full operation of the Currency Board. A similar situation was observed in the United States from 1865 to 1896. However, as Bagus notes, in some cases, they do consider monetary deflation to be harmful, and thus efforts are made to prevent it. This means addressing its causes to prevent it from occurring. Among the causes of deflation are those originating from economic growth, increases in treasury balances, and increased demand for wealth accumulation in money, among others. This is different from increased demand due to uncertainty. But deflation from economic growth occurs in a context of monetary stability, where the production of goods and services is exchanged for a money supply with a lower growth rate, thereby increasing its purchasing power and resulting in a tendency for other prices in the economy to fall. According to Bagus, it does not matter if economic growth is due to innovations, increased division of labor, increased net savings, or a combination of these factors, as possibly occurred during the early development of local industry under the Currency Board. This also challenges one of the most widespread monetary fallacies, which argued against the Currency Board: that economic growth is only possible if accompanied by an increase in the money supply. As Bagus argues, deflation could, in fact, reduce the power of the state.

Moreover, the prevailing idea at the time to justify the discontinuation of the full operation of the Currency Board was the argument of "monetary anemia," which was believed to cause a drop in

prices and, consequently, pose a serious problem for entrepreneurs. However, this perspective is limited if only the Consumer Price Index (CPI) is considered as an aggregate measure. The CPI is tied to the selling price of producers, which focuses solely on the final good's price, neglecting the prices of various production factors. These factors represent only a small portion of the overall prices in an economy.

The argument for needing a more elastic and flexible system will paradoxically and inevitably lead to deflation caused by bank credit. In other words, the same intervention by monetary authority's "exchanges" a "good" deflation for a "bad" one. According to Huerta de Soto (2010):

> "… the fractional-reserve banking system can contract and drastically reduce the money supply just as easily as it expands credit and increases the money supply. In other words, the system generates an elastic and extremely fragile stock of money which is subject to great convulsions that are very difficult, if not impossible, to mitigate or stop. This monetary and banking system contrasts with inelastic systems (for example, the one that combines the classic gold standard with a 100-percent reserve requirement), which do not permit disproportionate expansion of the money supply (the worldwide production of gold has been growing in recent centuries at the rate of 1 to 2 percent per year). Moreover they offer the following advantage: due to the fact that these systems are inelastic (gold is indestructible and throughout history the world has accumulated a very inflexible stock of it), they do not permit any abrupt decline, nor (logically) any credit or monetary squeezes which exert debilitating effects on the economy, as opposed to the current situation for which the existing banking system is responsible…"

Moreover, a monetary and banking system based on a pure gold standard, with a 100-percent reserve requirement, is a fundamental social institution for the proper functioning of any market economy.

The Great Depression did not merely result in the temporary closure of the Currency Board but prompted a profound reform of the monetary system. Following a severe depreciation of the currency and a decline in international reserves, the authorities departed from the monetary orthodoxy imposed by the gold standard under

the Currency Board. The Currency Board was granted the authority to discount commercial documents, and progress was made towards establishing Argentina's first "exchange control."

In practice, the gold standard was abandoned. The conviction that this represented a definitive solution was grounded in two pillars of economic policy: the implementation of an exchange control regime and the future establishment of a Central Bank, with objectives incompatible with the gold standard, amidst a context of international regime change.

2.5. *The Crash of 1929*

The financial crisis of 1929 led to a collapse in international trade, severely depressing the global economy, which would take several years to recover. Argentina, with its extensive trade links with the rest of the world and particularly with developed countries, experienced a significant economic downturn (see Table 1). Export prices dropped sharply, and although import prices also fell, they did so to a lesser extent. This deterioration in the terms of trade, combined with a capital outflow, placed substantial pressure on the exchange rate

TABLE 1.
THE IMPACT OF THE 1929 CRISIS

	Términos de intercambio[1] 1938-40=100	Variación reservas internac.[2]	Cuenta corriente[2]	Déficit fiscal[1] *	PBI[1]	Inflación[1]
		(US$ millones corrientes)		(% PBI)	(% variac. anual)	
1929	97	- 294	- 159	2,5	4,6	- 2,2
1930	94	- 42	- 311	4,9	- 4,1	- 3,9
1931	70	- 280	- 75	3,2	- 6,9	- 14,2
1932	73	- 8	- 15	1,7	- 3,3	- 7,5
1933	69	- 17	- 76	1,8	4,7	4,9

* De la Administración Nacional.
Fuente: 1. IEERAL (1986); 2. Apéndice Estadístico.

Source: FIEL (1989).

It was believed that the government needed, under the concept of "monetary anemia" or "financial inelasticity," to find a mechanism that would allow it to safeguard the gold reserves, which had been eroding since 1928 due to capital outflows. At the same time, it had to meet the demand for pesos required by the new production and distribution patterns, without neglecting the health of the financial system and the solidity of the banks. This task was deemed impossible according to Hayek*:* "… whenever a traditional rule of conduct is broken, either

> through institutional government coercion or the granting of special privileges by the state to certain people or organizations, sooner or later grave, undesirable consequences always ensue and cause serious damage to the spontaneous process of social cooperation…" (Huerta de Soto, 2010)

After the closure of the Currency Board, it was no longer possible to exchange pesos for gold at the official exchange rate. However, such currency exchange operations could still occur in a market governed freely by the interaction between supply and demand. The belief in a return to normalcy, with the expectation of reinstating the gold standard, played a significant role in business and government decisions. These decisions led to a moderate devaluation of the currency due to short-term borrowing, with the conviction that, after some time, the peso would return to its previous parity.

However, the literature argues that the government's decision to suspend the Currency Board mechanism early was prudent, leaving Argentina in a strong position regarding gold reserves. According to this perspective, it allowed for the "decoupling" of the money supply from external shocks, thus alleviating the inelasticity of the gold standard regime. However, it also left the door open for a currency devaluation in the context of falling export prices and the disappearance of external financing. The question then was the magnitude of the currency devaluation that would occur.

According to Gerchunoff and Machinea, the authors present data showing that:

> "… As a consequence of the fall in export prices and the poor harvest, exports in 1930 were US$ 397 million lower than in 1929: a drop of 45%. This was partially mitigated by the 12% drop in the price of imports, which meant saving some US$ 100 million. In spite of the surplus of US$ 88 million, the current account deficit was US$ 159 million in 1929, which was funded entirely by the drop in international reserves. To maintain 1929's level of activity and import volume in 1930 without losing reserves and maintaining a neutral capital account, the current account had to be balanced, which meant reducing the imbalance by some US$ 456 million. That figure is the result of adding the fall in export value to the 1929 current account deficit and subtracting thedrop in import value caused by falling prices (US$ 100 million). Since 1929 imports totalled US$ 750 million and exports would not react immediately, imports had to fall by 60%, or by around US$ 450 million. A reduction of that magnitude required not only an extraordinary hike in the exchange rate, but also a reduction of absorption. Consequently, without a recession or quantitative restrictions, the devaluation to balance the current account was substantially larger than that seen in the markets. In part, this was because the situation was believed to be only temporary. However, the 18% drop in exports in 1931 would show that the imbalance was more than a passing phenomenon… "(Gerchunoff & Machinea, 2015)

The crisis intensified, further complicating the economic situation and the sustainability of the peso. The terms of trade continued to decline due to a sharp drop in export prices, which fell at a much faster rate than import prices. Despite this, given the global and local context, the decision was made to meet the debt payments. In this regard, the authors identify three possible reasons for this decision in a context where countries in the region were entering into default: 1) to avoid repeating the crisis of 1890, which had significantly disrupted economic growth; 2) to maintain international reputation, given the belief that a return to "normalcy" was imminent; and 3) to emulate the behavior of higher-ranking economies such as Canada and Australia, which, despite having a higher level of debt, were meeting their debt obligations (Gerchunoff & Machinea, 2015). Additionally, it was argued that such a decision would come with costs: the loss of reserves would erode the

health of the financial system and risk a significant depreciation of the currency due to the inability to secure external financing.

By January 1931, the accumulated devaluation was 40% compared to November 1929, with a similar impact on the real exchange rate when considering the price of both local and foreign goods. Additionally, the Banco Nación was intervened, acting in accordance with the decree of January 31, 1930, by exporting gold pesos through direct purchases from the Currency Board. This measure helped maintain the devaluation at reasonable levels until the failure to secure an external loan again accelerated the sharp devaluation of the currency.

Thus, the rediscounting of commercial paper by the Currency Board allowed the institution to perform functions like those of a "Central Bank," which did not exist at the time, thereby disconnecting the relationship between the money supply and the balance of payments. However, the outcomes were far from satisfactory, with the shortcomings stemming more from the policy arguments than from the actual circumstances. In this context, the tool aimed to achieve two flawed economic policy objectives simultaneously: preventing monetary contraction resulting from debt repayment with reserves and supporting certain banks. This represented a shift in macroeconomic policy, which some authors interpret as a regime change (Della Paolera & Taylor, 2013), while others contend that it was viewed at the time as an isolated measure in response to the uncertainty of the context, not fully understood by all stakeholders of the era (Gerchunoff & Machinea, 2015).

3. **Foreign Exchange Control: A (Flawed) Economic Policy Tool**

In September 1931, United Kingdom suspended the convertibility of the pound sterling, breaking a symbol of the stability of the global monetary order. This led to a sharp depreciation of the peso in Argentina, which was allowed to float freely amid global confusion and deflationary conditions. The devaluation of the currency jeopardized the monetary regime and made it difficult for the Treasury to service its debt. Consequently, Argentina adopted a

new economic policy tool: foreign exchange control, which was being implemented by most countries at the time.

3.1. *Concept of Foreign Exchange Control*

A foreign exchange market is considered free when there is a single exchange rate at which foreign currencies can be bought and sold freely, reflecting transactions with the outside world through both commercial and financial channels. Conversely, a foreign exchange control scheme involves various modalities: i) the presence of differentiated segments and ii) a single segment with access restrictions (De León, 2014).

Additionally, it is important to consider other mechanisms of exchange control that arise from various trade policies. If free trade is not permitted, a structure is established that can have effects like exchange controls. For example, if a country imposes export tariffs without taxing or subsidizing imports, the exchange rate applicable to the export sector will be lower than the rate for imports. This can be seen as a system of multiple exchange rates. Similarly, an import quota on certain products can also be considered a restriction on access to the foreign exchange market.

The reasons commonly cited for implementing exchange controls under a "managed" economy can be diverse:

1. Mitigating External Shocks: Capital flight due to changes in the international context can lead to significant depreciation of the national currency if the central bank is unwilling or unable to use reserves to maintain parity. Exchange controls are introduced to avoid this depreciation, particularly for commercial transactions, which are often deemed crucial for the real economy. They can also be used to ration imports in response to a sudden decline in export purchasing power, typically caused by a deterioration in terms of trade. Thus, exchange controls can help mitigate the impact of temporary external shocks or make the adjustment to permanent shocks more gradual.

2. Maintaining Short-Term Economic Policies: Expansive monetary, fiscal, and wage policies can lead to increased demand and pressures on the balance of payments, potentially causing depreciation. Like the previous case, exchange controls can help prevent currency depreciation and its effects on domestic prices in the short term.
3. Generating Fiscal Revenue: When there are two exchange rates—one for exports and a higher one for imports—the government can generate revenue by selling foreign currency at a higher rate than it pays to purchase it, known as the "exchange margin." The public sector can also accumulate reserves through a trade surplus achieved via controls.
4. Favoring Transactions with Certain Countries: Regulating foreign transactions, such as granting exchange permits for imports from specific origins, can favor some countries over others. This is significant when international relations are governed by bilateral compensation agreements.
5. Protecting Against Imports: Setting a relatively high exchange rate for certain imports or directly prohibiting access to foreign currency for specific purchases protects domestic industries.
6. Promoting Exports: This occurs when certain exports are favored with a higher exchange rate compared to others. This can also be achieved through trade policy measures, such as subsidies for these goods.

All these reasons, driven by short-term objectives set by the authorities, disrupt the incentive structures necessary for the proper coordination of a market economy. Furthermore, these controls are implemented in the monetary domain without the formal establishment of a central bank.

3.2. **Exchange Rate Gap (known as the *"brecha"* in Spanish)**

A natural consequence of implementing exchange controls with currency restrictions is the emergence of a parallel exchange rate. The "gap" is defined as the difference between the exchange rate

in the parallel market, which is often institutionally considered illegal if it arises from transactions in an "unofficial" market (Caporale & Cerrato, 2008). A parallel currency market is one where transactions occur in multiple markets, with at least one—whether legal or illegal—determining prices through market forces, i.e., the interaction between supply and demand (Kiguel & O'Connell, 1995).

Considering that the sources of supply and demand for foreign currency vary from country to country and depend on the nature and effectiveness of controls, the factors influencing supply and demand in the parallel or illegal market, as outlined by Gahn (2016), can be classified as follows: (Table 2)

TABLE 2.
FACTORS INFLUENCING SUPPLY AND DEMAND IN THE PARALLEL EXCHANGE MARKET

Influencias por el lado de la oferta	**Influencias por el lado de la demanda**
Contrabando de exportaciones	Contrabando de mercancías
Turistas extranjeros	Turistas locales
Remisiones a través de canales no oficiales	Inversores/ahorristas que divesifican portfolio
Precios de transferencia	Precios de transferencia
Subdeclaración de exportaciones	
Sobredeclaración de importaciones	
Divisas con origen oficial	

Source: Gahn (2016)

The factors influencing the magnitude of the exchange rate gap are not only related to the supply and demand for foreign currency in the parallel market but may also involve institutional components in its determination. There is substantial empirical evidence, supported by theoretical foundations, that the exchange rate gap is a consequence of currency restrictions.

3.3. *The 1931 Exchange Control*

The implementation of exchange controls was in line with international trends which persisted for many years due to fears of losing international reserves in the post-war period. Argentina was no exception, and this tool was utilized for several decades. The 1931 Exchange Control originated from a decree that established the administration of available foreign currency, setting out a hierarchy of priorities:

1) External obligations of the national, provincial, and municipal governments.
2) Raw materials, fuels, and essential consumer goods.
3) Remittances for immigrants and travel expenses.
4) Non-essential goods, including capital goods, remittances of profits, and dividends from foreign companies.

In the context of a regime attempting to maintain currency parity, and after the failure to reach an agreement with banks to support a floating exchange rate, the partial satisfaction of foreign currency demand led to the emergence of a parallel market and the creation of an exchange rate "gap."

As observed until the establishment of the Exchange Control Commission in 1931, there was a single exchange rate and unrestricted international capital mobility (FIEL, 1989). The international situation was critical, as the 1929 crisis had deteriorated exports, resulting in a deep current account deficit, compounded by a poor harvest in 1930. In hindsight, exchange control was a flawed response to these circumstances.

Several measures were implemented, including: 1) Foreign exchange transactions had to be conducted through banks authorized by the Exchange Control Commission; 2) Exporters were required to surrender all their foreign currency; 3) Payment for imports was rationed and transfers were restricted through permits, though imports themselves were not curtailed; 4) An official exchange rate was established. Concurrently, the exchange rate in the parallel market increased, resulting in an exchange rate gap of up to 40% during the period 1932-1933.

In December 1931, a decision was made to peg the peso to the US dollar and the French franc. As detailed in various studies (Gerchunoff & Machinea, 2015), while the idea of returning to normalcy was ever-present, the context suggested otherwise, creating a sense of being in a "labyrinth" (Gerchunoff, 2016). Thus, the exchange control was combined with a fixed exchange rate, linking the peso to the franc and the dollar. The expectation for stability was high, but the prevailing crisis context deepened the recession and deflation. In this environment of uncertainty, Argentina effectively aligned itself with the countries adhering to the gold standard, and to prevent the loss of reserves and to align with other nations, quantitative restrictions were imposed, establishing the "exchange control."

However, the practices associated with the rediscounting system did not vanish; for instance, the "patriotic loan" was introduced. Unable to place the entire amount through the private sector, the government resorted to rediscounting, placing the remaining amount with the Currency Board, which led to the issuance of additional money.

3.4. *The 1933 Exchange Control*

The unintended but foreseeable outcomes of such intervention inevitably led to increased state intervention. Numerous criticisms were directed at the exchange control implemented in 1931, but none argued for the benefits of a "sound currency" achieved through freedom. Criticisms focused on technical errors, such as limiting the supply of foreign currency for imports while failing to control spending on imported goods. This discrepancy often resulted in unmet commitments, increasing debt levels. The system itself was unsustainable. The control, which only temporarily prevented currency depreciation, eventually contributed to future depreciation by expanding fiduciary means through the rediscounting documents at the Currency Board. At the same time, it stimulated imports and discouraged exports. The Commission issued daily exchange permits equivalent to the amount of foreign currency purchased at the fixed rate, leading to unmet demand and creating a parallel market with an exchange rate gap.

By 1933, the artificially strong peso was boosting imports, which put pressure on the balance of payments due to the poor performance of exports. The existing exchange control scheme did not impose a limit on the imports that could be made but only set a priority order for the allocation of foreign currency. This was problematic because it not only failed to restrict imports but also, in a way, incentivized them at the expense of exports due to the distortions in the currency market. Importers deposited the value of their purchases at the official exchange rate in authorized banks, but foreign sellers were only paid as the Commission's availability of foreign currency allowed, leading to delays in payments abroad. Furthermore, the controls, which imposed quantitative restrictions on the exchange market for both imports and financial flows, led to the emergence of a parallel market known as the "black market." As mentioned, the gap reached levels close to 40%, creating an incentive to evade controls through various practices. In conclusion, although the government had managed to momentarily and partially stop the peso's depreciation without sacrificing reserves, the deficiencies of the scheme were evident.

Finally, and not insignificantly undermining the coordinating forces that the market provides to individuals living in society, was the precariousness and arbitrariness with which exchange permits were granted. Regarding the individuals responsible for this task, Pinedo, who was the Minister of Finance, remarked in 1933:

> "… They acted with good intentions, driven by what they considered to be the country's best interests. However, they did so more or less arbitrarily, without statistics; they made decisions simply from their desks: this merchant who brings thread is a good firm and receives this amount; that other merchant who also brings thread is not a good firm and receives less… The exchange was for the chosen few who could obtain it. It was not for others who had to buy on the black market, committing a crime and exposing themselves to penalties. It was not for those who had to import using those Chinese pesos. Nor was it for those who saw their funds blocked and, in order to unblock them, had to subscribe to Argentine securities that they could only trade at a loss …" (Gerchunoff, 2016)

A modification the system was clearly needed. Interventionism had gained prominence in Argentina's economic policy, affecting various aspects of institutional economics. Therefore, instead of considering a possible solution that would restore the previous conditions that had promoted Argentine development, the focus was increasingly on "pragmatism", seeking remedies that were worse than the disease. By 1933, authorities were aware of the poor results, but not of their causes. Likewise, major countries around the world were failing to recover their levels of economic activity and trade, which severely impacted Argentina due to its dependence on the external sector. The effects of mismanaged fiscal and monetary policies were becoming apparent. However, could the industry have maintained its momentum without intervening in the monetary system?

Under these conditions and in this context, there was no convergence towards a stable situation. The Ottawa Agreement of August 1932, in which members of the British Commonwealth agreed to prioritize trade relations among themselves, exacerbated the issue. This agreement resulted in a restriction on Argentine meat exports to the United Kingdom, benefiting Australian and British producers. What was initially viewed as a temporary disruption to the global economic order gradually solidified into a persistent reality. Prebisch reflects: "… In 1931, we never stopped believing that recovery was just around the corner. That was the phrase used worldwide: around the corner (…). Witnessing the prolonged and intensifying global depression, which could not be addressed with orthodox measures in either the major countries or ours, led me to seriously question everything I had learned and taught as a university professor. This was a fundamental shift in my economic perspective …" Consequently, the authorities urgently sought a reassessment, leading to a mission in London. In May 1933, the Roca-Runciman Pact was signed, in which the United Kingdom assured a market for Argentine beef, while Argentina granted benefits to British imports and promised preferential treatment in currency matters (Gerchunoff, 2016).

Regarding the exchange control scheme, a reform was implemented starting in 1933. The 1931 exchange control regime had resulted in deficiencies related to debt accumulation. Measures

were introduced to settle both overdue and future debts at a preferential exchange rate compared to other creditors. Argentina, in turn, secured a "unlocking loan" in pounds at a 4% interest rate to address this debt. In essence, the approach of increasing intervention led to the establishment of a new exchange control system.

This involved a complex financial engineering process. Holders of blocked funds received government bonds, which were purchased by the newly established company *The Argentine Convention Trust*. This company, in turn, was financed through certificates placed on the British market (Cortes Conde, 2014). While negotiations between Argentina and the United Kingdom were ongoing, Franklin D. Roosevelt assumed the presidency of the United States. Following sixty days of bank runs and gold flight, he decreed the abandonment of the dollar's parity with gold. In response, the Argentine Minister of Finance adopted a stance of monetary orthodoxy: not only did he peg the peso to the French franc, the last bastion of the gold standard, but he also prevented the peso from aligning with the dollar. Despite external sector problems, the decision was made to appreciate the peso relative to the dollar and all currencies that depreciated against it. This decision may be explained by the weight of the debt, further increased by British loans (Gerchunoff, 2016).

The attempt to adhere to the gold standard was short-lived. Federico Pinedo, a member of the Independent Socialist Party, was appointed Minister of Finance. In November 1933, Pinedo, with the support of Raúl Prebisch, announced his Economic Action Plan. To counter the currency appreciation, the authorities implemented a devaluation of around 20% for traditional exports and 30% for imports with exchange permits. Additionally, a significant development considering the emerging regime change was the announcement of a bill to establish a mixed central bank to manage monetary policy. A notable feature of this proposal was that the new monetary policy would be framed within a new type of exchange control, aimed at addressing the shortcomings of the regulations imposed in October 1931 and meeting the demands of the British as outlined in the Roca-Runciman Treaty.

At the beginning of 1934, Pinedo, the then Minister of Finance, explained the new version of exchange control, an instrument

aimed at multiple objectives: "…The outlook for our exports did not suggest the possibility of settling exchange debts in the immediate future, as the available exchange was insufficient for the current year's needs. Thus, the government faced a problem with two distinct aspects. One was the cancellation of this mass of overdue commitments to prevent them from continuing to put pressure on the exchange market, and the other was to avoid the future accumulation of new unsatisfied commitments…" *(Revista Económica, 1934).*

When Federico Pinedo took charge of the Ministry of Finance, several modifications were made to the scheme:

1) Import permits were established, effectively limiting imports.
2) The exchange rate was split, creating a system of multiple exchange rates: the higher rate was free-floating, while the lower rate was fixed. Under the fixed rate, a portion of traditional exports was settled (through quotas), while non-traditional exports and any excess of traditional exports beyond the quota were settled under the free-floating rate.

When analyzing the new scheme, it becomes clear that there would be an official exchange rate and a free market rate. Access to cheap foreign currency at the official exchange rate would be regulated by permits distributed by the Exchange Control Commission. Priority for these permits would be given to those importing goods from countries with which payment agreements had been signed and those remitting profits and dividends to those countries, notably the United Kingdom. In 1934, Belgium, Switzerland, the Netherlands, and Germany were added, with several other countries following in subsequent years. Conversely, countries without payment agreements, such as the United States, would have their goods and profits remitted at the official exchange rate only when priority demand had been satisfied. Otherwise, they would have to turn to the more expensive free market. Indeed, in the first half of 1934, the free-market exchange rate averaged more than 20% above the official exchange rate.

The exchange control, with the new characteristics of the November 1933 regime (Table 3), would remain in place for almost

the entire decade: multiple exchange rates and no quantitative restrictions on imports. As a result, there was no parallel exchange market during those years. In contrast, as mentioned, the October 1931 exchange control regime had led to the emergence of a parallel market (known as the "black market") with a gap of around 40% compared to the official exchange rate.

TABLE 3.
THE NEW SCHEME

Currency control reforms of November 1933

Free exchange rate		
Foreign currency supply	Foreign currency demand	
Non-traditional exports Foreign investments Exports to neighbouring countries Regional crops	Partial imports (approximately 40%) from countries without payment arrangements Partial remittances to countries without payment arrangements	
Official exchange rate		
Foreign currency supply	Government	Foreign currency demand
Traditional exports	Exchange differential	Total imports from countries with payment arrangements Total remittances to countries with payment arrangements Partial imports (approximately 60%) from countries without payment arrangements Partial remittances to countries without payment arrangements

Source: Pablo Gerchunoff, "Circulando en el laberinto: la economía argentina entre la depresión y la guerra (1929-1939)", *Cuadernos de Trabajo IELAT*, No. 10, Alcalá de Henares, University of Alcalá, 2010.

Source: Gerchunoff & Machinea (2015)

In 1933, the Argentine government hired Sir Otto Niemeyer, an English expert and director of the Bank of tableand, who completed two key projects: the establishment of a Central Bank and a banking regulation law. The Central Bank was tasked with assuming the functions of the Currency Board, while also introducing a rediscount and exchange control commission to "flexibilize the system." The Central Bank was granted exclusive rights to issue banknotes under a fractional reserve system, coordinating the expansion and contraction of credit, and ensuring greater liquidity in banks through the formation of a central reserve fund (reserve

requirements), as well as managing banking activities related to government borrowing and issuance. Thus, the Banco Central de la República Argentina (B.C.R.A.) was created by Law N° 12.155 on March 28, 1935, based on Niemeyer's recommendations (Lilideal, 1950). However, even the existence of multiple exchange rates led to a classic mechanism of export under-invoicing.

4. **Monetary Stability as a Source of Growth**

During the period of full operation of the Currency Board, if the quantity of goods grew faster than the quantity of money, it could lead to a deflationary period where the price level decreases. This reduction in prices would mean that agents require less money to purchase goods—whether final goods, intermediate goods, or inputs—and services. Consequently, the real returns to productive factors would increase, incentivizing stable economic growth without disturbing the interest rate.

How much did this process contribute to the stable environment necessary for industrial development? The currency should be chosen spontaneously by individuals within a system where money supply is managed freely. Eliminating the "lender of last resort" would avoid disrupting incentive schemes and interfering with the interest rate, which serves as a crucial signal for individuals' decision-making processes, including saving and investment. Such interference can hinder economic growth. Furthermore, it undermines the right to private property—a fundamental principle of liberalism—by socializing losses through inflationary policies proposed by the lender of last resort. This is a consequence of a fractional reserve system that imposes a constant vulnerability on the financial and economic system.

Without a Central Bank and with deposits backed by gold under the full operation of the Currency Board, the production of goods and services would increase more than the amount of money, and society would experience a gradual, sustained, and healthy deflation. The Currency Board, established to provide a framework for monetary stability, was guided by this principle.

However, the modifications aimed at achieving specific objectives faced the inherent limitations of centralized planning, particularly its inability to perform accurate economic calculations. Without the capacity to quantify costs or the value of forgone alternatives, the administration struggled to manage resources effectively due to lack of information (Giacomini, 2020). Attempts to address these shortcomings through increased restrictions and interventions only led to greater distortions and inefficiencies in the market.

This approach necessitated even more intervention, as evidenced by the evolution from the Currency Board system, initially based on weak theoretical arguments like "monetary anemia" or "financial inelasticity". These assumptions, which presumed an "optimal" money supply, ultimately led to rediscounting, exchange controls, and the creation of a central banking system with fractional reserve banking and other interventions. This progression marked a departure from the possibility of maintaining a sound currency.

The most significant issue with monetary intervention is that it disrupts the market process by hindering the inherent entrepreneurial function of human action. Interventions in the monetary market often stem from the mistaken belief that an optimal amount of money exists, which individuals, acting freely and spontaneously, would demand to meet their needs. This optimal amount is presumed to be discoverable by some governmental or institutional body.

In practice, exchange controls that restrict access to foreign currency or gold exacerbate the very problems they aim to solve. Instead of achieving their intended goals, these controls often reduce the demand for the local currency while increasing the demand for foreign currency or gold. Such controls essentially impose price controls in the currency market, setting a maximum price for foreign currency (underpriced) and a minimum price for domestic currency (overpriced). This results in individuals preferring the undervalued foreign currency and rejecting the overvalued domestic currency, leading to a decline in the demand for local money and worsening the situation (Giacomini, 2020).

Dynamically, monetary intervention not only impacts the currency exchange market, exacerbating the devaluation of the domestic

currency due to decreased demand, but it also leads to an increased demand for foreign currency. This shift can create an oversupply of goods, which in turn, results in a decline in economic activity. Under interventionist logic, these negative outcomes are often seen as justification for further intervention. In this context, it is argued that previous interventions, such as exchange controls, were intended to institutionalize mechanisms like the "lender of last resort" and discounting practices. However, these interventions are grounded in theoretical errors regarding the nature of money, rather than addressing the actual economic issues.

The discounting system, which suspends the Currency Board, deviates from its original purpose and exacerbates existing problems. This leads to increased control and intervention mechanisms, ultimately resulting in the establishment of exchange controls and, subsequently, central banking. The rationale behind this shift is that expansions become more robust and sustained when the banking system has an institution providing liquidity within a fractional reserve system.

However, the interventionist perspective dominating the Argentine monetary market at the time led to the adoption of exchange controls. In retrospect, these controls facilitated the creation of a central banking system, which, according to Giacomini, exemplifies "the fatal arrogance (Hayek), the impossibility of economic calculation (Mises), and the road to serfdom (Hayek)" (Giacomini, 2020). This approach represents the full exercise of monetary socialism.

Understanding socialism as defined by Huerta de Soto "… as any system of institutional aggression on the free exercise of entrepreneurship. By aggression or coercion we mean all physical violence or threats of physical violence which another person or group of people initiates and employs against the actor. As a result of this coercion, the actor, who otherwise would have freely exercised his entrepreneurship, is forced, in order to avoid greater evils, to act differently than he would have acted in other circumstances, and thus to modify his behavior and adapt it to the ends of the person or persons who are coercing him…" (Huerta de Soto, 2010)

Under the Currency Board system, which tied the currency to the gold standard, exports increased significantly. This surge led

to a substantial influx of capital and a strong accumulation of reserves, resulting in genuine monetary expansion. The resulting monetary stability also contributed to exchange rate stability. The real exchange rate appreciated by 10%, which, coupled with the influx of external capital and increased domestic savings facilitated by monetary stability, supported a gross capital formation rate of 9.5%. During the full operation of the Currency Board from 1899 to 1914, exports grew by 6.7%, and real GDP increased by an average annual rate of 4.9%.

In terms of economic growth, the real GDP grew at an average annual rate of nearly 5%. A significant measure of development during this period was population growth, which was not solely due to natural increase but also driven by migration, reflecting the level of wages. According to the president of the commission responsible for the third census of Argentina conducted in 1914, no other region in the world, not even the burgeoning Canada, matched Argentina's population growth rate: "… Canada took just under forty years to double its population… Meanwhile, in Argentina, from 1895 to 1914, the absolute growth was 3.960.392 people, a relative increase of 100%, and an annual growth rate of 5.2% …" (Gerchunoff & Llach, 2018). The text also notes that many shipping companies recorded the drop of their crew members in Argentine ports, attracted by better job opportunities. Additionally, the census highlighted progress in education, with the illiteracy rate dropping to 35% in 1914 from 78% in 1869.

According to Gerchunoff and Llach (2018), between 1900 and 1913, Argentina's economy grew at an annual rate of 6.4%, and from 1918 to 1929, it grew at 3.9% annually. Even with interruptions and modifications that undermined the currency board system, the economy continued to grow at a rate close to 4% annually for eleven consecutive years. How much of this growth can be attributed to the monetary stability provided by the system? And how much of the decline in growth rate can be attributed to the modifications that weakened the system, moving away from a "sound" currency?

Nevertheless, during the 1920s, before the onset of the Great Depression, Argentina experienced growth rates that exceeded those of the United States, Canada, and Australia. According to

Gerchunoff and Llach (2018), for the entire period from 1913 to 1929, Argentina was only surpassed by the United States. This was largely due to the dependency of the U.S. economy on European capital during the war period. Even so, Argentina's population was growing faster than that of the United States, and by 1929, its total GDP had surpassed that of Australia and was approaching that of Canada.

One of the most historically detrimental consequences for Argentina was the disruption of capital flows, primarily British, starting in 1914 due to the war. The impact of a reduction in foreign investment on growth then depended on the magnitude of domestic savings. With a decline in external capital inflows, lower domestic savings would result in less capital formation and, consequently, a lower expected growth rate in the future. Although exact data are not available due to methodological discrepancies, capital formation may have increased by between 15% and 33% between 1925 and 1929, but its evolution can be traced (Gerchunoff & Llach, 2018). As the authors note, "… it is undeniable that internal investment in the 1920s was lower than in the first fifteen years of the century; the difference may have been around 25%. The capitalization of industry and agriculture did not compensate for the stagnation in railway expansion…" The authors attribute the lower savings and investment rates to a higher dependency ratio compared to Canada and Australia, suggesting that Latin American immigrants had more children than their Anglo counterparts. However, they overlook the impact of Argentina's careless management of prosperity, which they themselves describe, on the government's tendency to spend excessively and save little during times of boom and optimism, resulting in dissaving. This characteristic even surprised the writer of the Espasa Calpe Encyclopedia, who noted in an article dedicated to Argentina that there was a real luxury in multiplying jobs, increasing salaries, and granting costly concessions to the public treasury, as if public funds were inexhaustible. (Gerchunoff & Llach, 2018). Clearly, they were not; the appearance of abundance was only masked by the exploitation of the Currency Board system, which allowed the discounting of documents to finance government deficits without explicitly or formally breaking with the Currency Board.

This propensity for consumption, at the expense of savings, which extended to the private sector, was a product of government intervention in the monetary and banking system. This intervention incentivized a lower savings rate and, consequently, a lower internal investment rate and growth compared to the early years of the Currency Board's full operation. Between the various events from 1914 to 1930, when Argentina began to definitively abandon the gold standard, and prior to the establishment of exchange controls as a mechanism that laid the groundwork for the creation of the Central Bank, the money supply was already being altered through the reduction of reserves. This allowed the financial system to increase the money supply and disrupted the relationship between savings and investment.

Regarding GDP, public expenditure increased from 8.5% in 1920 to 13% in 1929, and the national administration's deficit reached 4% of GDP. This was only possible through the circumvention of monetary institutions, allowing financing via an increase in the money supply. The argument that considers the relative growth of industry as a deliberate process of import substitution due to the war is also debatable. According to Gerchunoff and Llach, "… The decline in foreign purchases during 1914-18 was an initial episode in which the Argentine economy naturally closed itself off, without a deliberate economic policy decision. This, as an unintended consequence, repeated itself during the Great Depression and the Second World War. Argentina had to rely much more on itself to obtain manufactures, and industrialists found that, for a time, they did not have to worry as much about foreign competition. As occurred in other peripheral countries, the protection provided by the war allowed for an initial, localized, and nascent stage of import-substituting industrialization…" (Gerchunoff & Llach, 2018).

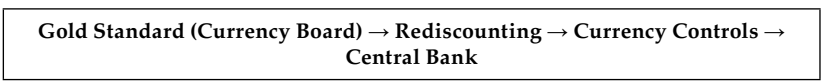
It is crucial to emphasize the connection between monetary policy and the advancement of "socialism" in Argentina. First, there was no actual "monetary anemia" that triggered a crisis due to a lack of currency, as there is no optimal amount of money. Second, the increased demand for money arose in an industry that had been growing in the previous years under a framework of free trade and monetary stability. There is no need for either of these

conditions, as mentioned throughout the literature, for industrial development. Following an evolutionary logic, industrial growth in its initial stages is always "localized and nascent," as it develops spontaneously with the available resources. As the monetary system created the necessary conditions and stability, it provided the information needed for a more effective management of resources, which were likely utilized during the war context for the free exercise of entrepreneurial function. There was no need for additional unbacked money, manipulated interest rates, or protectionist measures like import restrictions or exchange controls to foster development. Instead, the incentives provided by the context allowed individuals of the time to take advantage of available means to transition from one improved situation to another, exercising their *entrepreneurial function* fully.

5. **Conclusions**

The currency controls led to the establishment of a Central Bank, which gave governments full control over the provision of money. The precursor to the creation of the Central Bank of Argentina (BCRA) was the system of currency controls first implemented in 1931 and then reformed in 1933. These controls were introduced to permanently eliminate the Currency Board system under the gold standard, thus preventing the automatic conversion of national currency into gold. This process halted the appreciation of the currency, which began with the rediscounting and was ultimately solidified with the creation of the Central Bank.

FIGURE 1.



The results of the Central Bank of Argentina's (BCRA) operations relative to its original purposes are outside the scope of this work,

but for illustration: between 1935 and 1946, average inflation was 6% under a mixed public-private system. From 1946 to 1991, it reached 225%, with the system fully state-controlled, including two hyperinflation episodes in 1989 and 1991. After the implementation of the Convertibility Law, inflation was below 3% annually from 1992 to 2001. Following the repeal of the Convertibility Law and the restoration of the central banking system, inflation again rose, reaching an average of 9.4% annually from 2003 to 2007, 19.8% from 2008 to 2011, 28.3% from 2011 to 2013, and 41.1% from 2015 to 2019 (Giacomini, 2020). By December 2023, inflation had accelerated to over three-digit figures. *Paradoxically, over 90 years later, Argentina's monetary-exchange regime still maintains currency controls.*

In this context, the currency controls established in Argentina in 1931 required increasing intervention, leading to the creation of new state institutions for their "refinement" in 1933. Rather than evolving spontaneously, these controls imposed greater restrictions and adjustments, failing to meet their objectives and preventing the creation of new information to coordinate the actions of individuals exercising their entrepreneurial function freely. As a result, two years later, after several attempts in previous years, the Central Bank of Argentina (BCRA) was established in 1935, marking the advent of "monetary socialism" in Argentina up to the present day. Currency controls thus paved the way for the creation of the BCRA, facilitating the definitive abandonment of the gold standard.

We might consider the "Currency Board" as a stable monetary system providing money in accordance with the demand of individuals, while the "Currency Controls" served as the instrument to achieve monetary socialism by establishing a central bank with a monopoly, a forced currency system, and a lender of last resort.

The Currency Board, though formally in place until the creation of the Central Bank, effectively functioned only until the first currency control was established in November 1931, which was four years before the definitive establishment of the central bank. Beyond historical specifics, it is crucial to highlight the role of currency controls in disabling the operation of the Currency Board and, consequently, the gold standard, thereby definitively precluding Argentina's opportunity to establish a sound currency.

In 1914, because of World War I, the Currency Board was suspended. The arguments for this decision included the system's lack of flexibility and the need for a "national" currency, as the existing currency was deemed "scarce," which was believed to hinder trade and economic growth. From the perspective of the Austrian School of Economics, these arguments are flawed.

First, for any good to have economic value in subjective terms, it must be useful, meaning it serves to achieve an end, and it must also be scarce. The money provided under the Currency Board was indeed scarce, as it was desired and demanded by individuals of that time due to the adoption of the gold standard. The Currency Board system ensured its backing with metal reserves, making it scarce and in line with the money demand that supported economic growth during that era, which was facilitated by monetary stability. Therefore, rather than hindering trade and economic growth, the Currency Board system provided the necessary stability for individuals to optimally perform their entrepreneurial functions.

Second, it is important to remember that, from the Austrian perspective, there is no optimal amount of money: "…any amount of money is used to its full extent…" (Giacomini, 2020). The only distinction made is that different amounts of money will result in different price levels. Thus, the robust growth of the Argentine economy from 1899 to 1914 was not impeded by the hypothesis of a greater need for circulating money; it did not hinder trade, immigration, or literacy. Rather, it served as a foundation for growth, generating a higher proportion of internal savings compared to the 1920s. During that period, despite the Currency Board's regulation, the system was undermined by mechanisms like rediscounting, which allowed for monetary relaxation to finance government deficits.

Conversely, the increased share of wages in national income, which drove greater money demand due to economic growth and industrial activity, did not necessitate more intervention to increase the money supply. Instead, a "healthy" deflation imposed by the monetary mechanism itself was sufficient. Indeed, the industrial growth, which now demanded more money, resulted from a stable monetary system that facilitated not only economic calculation but

also provided the conditions necessary for entrepreneurial activity. The alteration of the system through reduced bank reserves, which led to an excessive increase in the money supply, was primarily motivated by the need to finance government deficits. This approach granted privileges to banks through fractional reserve banking and violated depositors' property rights during periods of inconvertibility, benefiting more concentrated power groups linked to the agro-export sector. These groups gained from the increased money supply, which depreciated the currency and made their products more competitive in international markets.

Third, monetary sovereignty constitutes a false argument, which persists in the current Argentine economy. It is not about having a state-issued, monopolistic currency, but about enabling individuals to make decisions freely that foster prosperity (Giacomini, 2020). In this sense, what is necessary is a framework of "monetary stability." According to the author: "…the more stable the money and the greater its purchasing power, the more goods and services can likely be acquired, leading to higher quality of life and prosperity…" The fear of deflation was a fear of the government losing its monopoly on currency, and thereby forgoing the privileges it enjoyed in conjunction with the fractional reserve banking system.

Indeed, the increase in the purchasing power of money, when used as a medium of exchange and unit of account, results in a decrease in the price of other goods measured in that money. This is a consequence, not a cause, of a healthy economic growth (Bagus, 2021), such as that described during the full operation of the Currency Board. In that context, the demand for money increased due to monetary stability, as the government was not allowed to issue money without gold backing, nor could banks create money through the banking multiplier. This enhanced savings and investment, increasing capital formation as demonstrated by the Austrian Theory of Capital, leading to economic expansion and development in a period of prosperity.

The gold standard was left behind. The exchange controls established in 1931 and 1933 ended the Currency Board and paved the way for the creation of the Central Bank in 1935. The belief that this was a definitive solution was based on two pillars of economic

policy: an exchange control regime and the future establishment of the Central Bank, which, as events showed, definitively moved Argentina away from the idea of a sound currency.

Conflict of Interest

The author declares that he has no conflict of interest.

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