

# Monetary disorder in Buenos Aires (1822-1881): Market failure or government failure?

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## Abstract

Repeated attempts to create a stable monetary system in Buenos Aires between 1822 and 1881 failed due to the monopolies granted for the issue of legal tender. This paper analyzes five such attempts: the Discount Bank (1822-1826), the National Bank (1826-1836), the Mint (1836-1853), the Bank and Mint of the Province of Buenos Aires (1853-1872) and the National Bank (1872-1881). Sound money was an impossibility because the state infringed on the independence of each of these institutions in order to deal with armed conflicts and other emergencies.

Key words: monetary institutions, free banking, central bank, currency monopoly

JEL codes: E5; N1; N2

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## **MONETARY DISORDER IN BUENOS AIRES (1822-1881):**

### **MARKET FAILURE OR GOVERNMENT FAILURE?**

Governments have come to supply currency, and to restrict the private supply of currency and deposits, not to remedy market failures, but to provide themselves with seigniorage and loans on favorable terms. Government currency monopolies and bank regulations can thus be understood as part of the tax system. The “strong revealed preference in history for a sole issuer” is, fundamentally, the preference of fiscal authorities, not of consumers.

(Selgin and White, 1999, p. 155)

### **Introduction**

Two centuries after independence, a stable monetary system continues to elude Argentina. Not surprisingly, Argentine academics have devoted considerable attention to the reasons underlying the instability of their currency. Classic studies of the history of Argentine monetary institutions include Agote, (1881), de Vedia (1890), Quesada (1901), Hansen (1916), Piñero (1921), Prebisch (1921), Casarino (1922), Pinedo (1942), Curcoresse (1967), Cortés Conde (1989), Alemann (1990) and Della Paolera and Taylor (2003). The chronic instability of the Argentine currency in recent years intensified interest in this subject. The annual meeting of the Argentinian Association of Political Economy (AAEP) held in Trelew in November, 2012 was devoted to this issue (Ortiz Batalla, 2014).

The objective here is not to reprise earlier studies, but rather to supplement our understanding of this issue by focusing attention on Buenos Aires over the period 1822 – 1881. A synthesis of both classic and more recent work on the subject is outlined to make the case

that the root cause of monetary disorder lay in the monopolies granted by the government to a succession of banking institutions to supply of legal tender. The consequences in Buenos Aires over this period contrast starkly with the example of Scotland, where monetary stability derived from healthy competition in the banking sector (White 1984, Selgin 1988, Dowd 1992).

In essence, this paper supports the conclusion expressed in the reference above. Rather than following the Scottish precedent, Buenos Aires chose to adopt monetary institutions patterned on those of England, France and other European countries which prevented banking competition by granting monopoly privileges for the emission of legal currency to a succession of banks. The motivation behind the monopolies granted in these countries was not the promotion of economic development but the financial objectives of the state. This motive was identified in Smith's classic study of the history of banking in England, France, Germany and the United States (Smith, 1936: 185).

In each of these cases, the state obtained preferential treatment as a borrower from the bank to which it granted the monopoly. These banking monopolies also became the precursors central banks in these countries. This paper argues that the situation in Buenos Aires in the period considered is consistent with the patterns identified in Smith's study: the succession of banking monopolies prevented competition among banks which would have benefited private borrowers; the state exploited the implied obligation on the part of the bank to which the monopoly was granted; and once the principle of a monopoly source of currency was adopted, it was a logical consequence that the state would seek to maximize the benefits it could obtain from direct control over monetary policy by creating a central bank.

A similar conclusion is reached in the work of Charles P. Kindleberger (2011). He however emphasizes the fundamental influence of *conflict* on the history of financial institutions in Europe. War perverts the functioning of the normal economy and places enormous strain on the resources at the disposal of the state. Waging war requires extraordinary mobilization of financial resources and Kindleberger notes a correlation between financial innovation and

conflicts: the Bank of England was established in the middle of the Nine Years' War (known on the continent as the War of the League of Augsburg) and the Bank of France was established by Napoleon in 1800 to help finance his military adventures. In the Middle Ages, bankers were brought to ruin, not by the collapse of markets, but by the inability of kings to meet the debts they had incurred in order to raise mercenary armies and provide military support to allies (Kindleberger, 2011: 19).

Recent work by Kingston (2014) points out that effective competition among private banks is possible only when their owners are legally required to cover its liabilities. The prudent lending closely associated with Scottish banking was inevitable under such restrictions. The ability of all borrowers to repay their loans must be dispassionately assessed. Preferential treatment of the state under such circumstances is clearly impossible. Kingston considers the extension of *limited* liability to banks and the "lender-of- the-last-resort" role of central banks a dangerous combination because it encourages imprudent lending, as recently evident in the financial melt-down of 2008-9. Granting a monopoly to issue currency to a private bank whose owners have limited liability has the same result. In Buenos Aires, periodically declaring the currency non-convertible was symptomatic of the underlying monetary disorder.

Against the backdrop of studies of the history of financial institutions elsewhere, this paper examines the monetary history of Buenos Aires from the founding of the first bank in 1822 until 1881 when a national currency was formally adopted. Using a methodology similar to Smith (1936), we show that the succession of failures to achieve "monetary order" over this period should not be blamed on a scarcity of precious metals, as this 'shortage' was an unintended consequence of the system in place rather than a determining factor. Nor can the prevalent monetary disorder be attributed to market failure given the legal barriers erected to prevent the operation of a market -- particularly the entry of new participants -- during the time period considered. Instead, the "monetary disorder" evident throughout this period should be interpreted as a failure of political planning: the stable monetary system which developed where competitive or decentralized banking regimes prevailed was not possible in

Buenos Aires where a single institution was given a monopoly to issue legal tender (Smith 1936, White 1984, Selgin 1988, Dowd 1992).

It should be noted that economic historians often conflate banking in Buenos Aires with banking in Argentina. Raul Prebisch (1921) is a case in point. Buenos Aires was one of the main protagonists in conflicts among the “United” Provinces of the River Plate which recurred during this period. The possibility of decentralized banking in jurisdictions other than Buenos Aires has received little attention (an exception is Gómez, 1994). Prebisch follows the mainstream approach which considers the history of financial arrangements in provinces other than Buenos Aires inconsequential.

In Section 1 we examine the Discount Bank (Banco de Descuentos)(1822-1826); in Section 2 the National Bank (Banco Nacional of 1826-1836); in Section 3 the Mint (Casa de la Moneda)(1836-1853); and in Section 4 the Bank and Mint of the Province of Buenos Aires (Banco de la Provincia de Buenos Aires y la Casa de la Moneda) (1853-1872); and in section 5 the National Bank (the Banco Nacional of 1872-1881). The final section draws conclusions from the discussion of the evolution of the banking system in Buenos Aires over the entire period 1822-1881.

### **1. The Discount Bank (1822-1826)**

In 1822, the Minister of Finance of the Province of Buenos Aires, Manuel José García, convened a meeting to present a proposal to create a bank. Martín Rodríguez was the Governor of the Province of Buenos Aires and Bernardino Rivadavia, at the time Minister of Government, exerted considerable influence. The decision to create the Discount Bank (occasionally referred to as the Bank of Buenos Aires (Banco de Buenos Aires)) was made at that meeting. This bank, which was the first incorporated company founded in Argentina, was organized as a private, limited liability company.

The shareholding structure of the company was diverse and included landowners, military personnel, clergy, professionals and creoles. Various nationalities were represented, including English, Spanish, French and German. English shareholders, familiar with the

banking practices of their country, were particularly well represented. It is therefore a plausible hypothesis that the knowledge these individuals had about the prior creation of the Bank of England (in 1695) was instrumental in bringing pressure to bear on the government of Buenos Aires to give this first bank its twenty-year monopoly over the issuing of money.

Casarino (1922) notes that the first interim Chairman of the Board was British, and that three out of the nine directors of the Bank elected by shareholder in 1822 were British. At the shareholders' meeting of January 18, 1825, of 702 votes, 381 were cast by British shareholders; and in the meeting of January 9, 1826, 454 shares voted out of the total of 838 shares were in British hands. Right from the outset, British capital played a dominant role in Argentine banking.

Vedia claimed that there were two formal arguments for the creation of the bank: the need to finance the development of production and the shortage of specie (metals from which coins could be minted locally to serve as proxies of value) to satisfy the influx of foreign capital attracted by opportunities for expanding trade (Vedia, 1890, p. 59).

However, as Raul Prebisch pointed out (citing Manuel José García, the Minister of Finance at the time), the real intent lay elsewhere. He argued that the close relationship created between the Bank and the Treasury would facilitate access to lower cost loans than the government was able to obtain when it borrowed in competition with commercial enterprises and individuals. *"The birth of the first (Argentine) Bank (in 1822) was more a response to the fiscal emergency than to the needs of an embryonic commerce"*. (Prebisch, 1921, p. 125; emphasis added).

The Bank's capital was one million 'sound pesos' ('pesos fuertes'), divided into shares of one hundred pesos each to be delivered by public subscription. In practice, however, the shares were subscribed, as Agote (1881: 81) pointed out, partly in specie and partly in notes issued by the bank itself. Hence, right from the beginning, there was a shortfall in the underlying capital of the bank.

As shown in Table No. 1, the bullion capital of this bank never exceeded a third of the level at which it was nominally set, even when it reached its peak level of 285,000 ‘sound pesos’ in 1825.

**Table No. 1: THE FINANCIAL POSITION OF THE DISCOUNT BANK**

**(Thousands of ‘sound pesos’)**

Year	Date	Nominal Capital	Currency in Circulation	Bullion Reserves	Loans Outstanding
1823	August 31	445	291	270	705
1824	February 28	469	910	154	1352
1824	August 31	1000	1680	204	2565
1825	February 28	1000	1698	285	2457
1825	August 31	1000	1934	253	2594
1826	February 28	1000	2694	255	3280

*Source: Raúl Prebisch (1921, p. 126)*

Just two years after being created, the Bank was credited with a capital base of a million ‘sound pesos’ as required according to its founding charter if we accept the data provided by Prebisch. However, these data are a fiction.

According to Agote, in 1824 -- two years after the bank was created -- the rest of the nominal capital was not covered, and the bank badly needed funds to finance its day-to-day operations. The Board sought to increase its capital base by issuing additional shares. On paper, these efforts were successful as the Bank’s capital was increased by five hundred additional shares. However, in fact it was the Bank’s liabilities that increased, not the capital base: shares were paid for with notes or loans at agreed interest rates, but loans were either renewed indefinitely or redeemed with the proceeds of subsequent loans (Agote, p. 1881: 90). It is for this reason that the nominal capital base jumped sharply from 445,000 ‘sound pesos’ in 1824 to the statutory million in 1825, while the outstanding loan portfolio also experienced a remarkable increase over exactly the same period

According to Vedia (1890: 73), the standard response to any suggestion that such a fictitious increase in nominal capital was dangerous was that since classical antiquity the theory of establishing banks with reserves consisting entirely of bullion has been held up as an exquisitely beautiful ideal which is generally impractical. This excuse was readily adopted in Argentina given the situation that existed in the country at the time. The first Argentine bank began its operations with an extremely meager capital base (Prebisch, 1921, p. 126).

The expansion of credit that resulted from the attempt to increase the Bank's "capital" reduced interest rates by at least half. Alemann (1990: 63) indicates that the Bank was lending at 9% annually, when non-Bank interest rates ranged between 18% and 24% annually. The issue of common currency 'silver' pesos, supposedly representing the amount of silver in eight 'reales' at a rate equivalent to seventeen ounces of silver to one ounce of gold, raised the amount of notes in circulation to 2.7-million-peso bank notes by the end of the Bank's short life. This is consistent with the information provided by Prebisch (Table 1).

At the outset, the bank was managed conservatively, but historians explain that the war with Brazil which began in 1825 led the bank to abandon caution. This conflict pitted the United Provinces of the River Plate against the Empire of Brazil. At stake was control of the territory corresponding to the current Republic of Uruguay and part of the Brazilian state of Rio Grande do Sul. As had happened in England under Charles II, and in France under Napoleon, the combination of an increase in demand for funds occasioned by the war and wholly inadequate reserves led to the bankruptcy of the first Argentine bank.

Alemann (1990: 63) describes the consequences as follows:

The bank itself asked the government at the end of 1825 to relieve it of the obligation to convert their notes at their par value in silver because it was unable to do so. The government fulfilled its request and created a new bank.

Before turning attention to the successor bank which absorbed its predecessor's residual reserves, it remains to deal with the misunderstanding that prevails among historians with



respect to the recorded events. It is true that, as shown in Table 1, issuance of notes multiplied dramatically in 1824, the year before the war with Brazil began, going from 291 to 910 thousand 'sound pesos'. Over the same period, the bullion reserves of the Bank declined from 270 to 154 thousand 'sound pesos'

However, it may be the case that this expansion of credit was not caused by the war which at the time lay in future but by the earlier war whereby the United Provinces had obtained their independence. Alternatively, this remarkable credit expansion may be attributed to a political attempt to stimulate economic activity and bring short-term prosperity to the population by fomenting a boom in the business cycle.<sup>2</sup>

At the time he was writing about the Discount Bank, the young Raul Prebisch was a disciple of the monetarist economists, and was therefore quick to focus attention on the delicate relationship between monetary policy and the economic cycle. He quotes Lopez (1891, p.19) who pointed out that the "illusion prompted by the appearance four hundred thousand pesos of subscribed capital, led [the Bank] to maintain a circulation of more than two million common currency paper pesos, ('pesos corrientes') making amazing profits while the whole country prospered, and believing it had solved once and for all the problem of circulation.... [Until then] the obstacle to the development of rural production had been the lack of working capital at sufficiently low interest rates, not only for advance payments of the means of production but also for price discovery and animation of the market. This bottleneck [to generating production and stimulating land values] was relieved by the liquidity the Discount Bank provided.

However, Prebisch observes that this prosperity, which Lopez had probably exaggerated when he described it as "perfect equilibrium", did not last long. He notes that the effectiveness of credit is constrained by real conditions, including the amount of capital allocated to

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<sup>2</sup> It is important to remember that the Buenos Aires Stock Exchange was created in 1824. As soon as the government made the local currency inconvertible into specie, the stock exchange became the market in which the value of an ounce of gold in local currency was determined, and hence more of an exchange market than a capital market.

production. He emphasizes that credit does not create capital but merely enhances the impact of the capital available. In other words, when underlying conditions are not conducive to production, or when capital is unavailable, the impact of additional credit is purely inflationary. This indeed seems to be what happened: the credit created by the Discount bank initially filled a real need, but later exceeded the capacity of the economy to utilize them effectively, creating a fictitious atmosphere of economic prosperity and business expansion, inflating prices in general and property prices in particular.

The situation deteriorated when an increase in imports led to a trade balance deficit which necessitated the exportation of bullion reserves. Ongoing reduction of reserves forced the bank to restrict its commercial lending, raising interest rates and leading to the liquidation of many of the investment projects that had been encouraged by the low interest rates referred to above. The onset of a crisis was merely the inevitable consequence.

“Thus” Prebisch writes (1921: 129) “our first, somewhat artificial, bank failed. Its two original sins – being conceived out of fiscal rather than commercial necessity and the inadequacy of its capital base – were compounded during its development by the no less serious error of excessive expansion of the money supply, provoked by the atmosphere of fictitious prosperity which it had itself created and the urgent need for public funds, to the point where a balance became impossible to maintain.”

## **2. The National Bank (1826-1836)**

The suspension of bullion payments requested by the Discount Bank led to plans to create a national bank from the rubble of its predecessor. The decision involved a degree of urgency, as there was fear, given the context of the war with Brazil, that the remaining reserves and gold borrowed from the London bank Barings would quickly disappear financing the war and that it would therefore be inadequate bullion (specie) reserves to restore monetary order.

The National Bank was founded in 1826, with the official title of the Bank of the United Provinces of the River Plate. Its initial capital base was ten million pesos, divided into shares valued at 200 pesos each. The capital base was to be made up as follows:

- a) One million ‘sound pesos’ obtained from the dissolution of the Discount Bank. However, as previously mentioned, a large part of the capital of this bank consisted of credits held by the same establishment. Nonetheless, and with the objective of creating a good impression with shareholders and the London Stock Exchange, each old share of 1000 ‘sound pesos’, was exchanged for seven new shares valued at 200 ‘sound pesos’, implying an overnight profit of 40%.
- b) Three million ‘sound pesos’ from the Baring loan (which was initially extended to finance the construction of infrastructure in the port of Buenos Aires). Agote (1881: 92) points out that this capital was largely imaginary, because the war had consumed the bulk of it and the balance remaining was divided between promissory notes issued to individuals and Treasury Bills”. Of this loan there remained no more than the insignificant amount of 20 thousand “strong pesos” in cash, as indicated in table Nº 2.-

**Table No. 2: COMPOSITIÓN OF THE BALANCE OF THE BARING LOAN ALLOCATED TO THE NATIONAL BANK**

(Thousands of ‘sound pesos’)

Concept	Amount
In Treasury bills...	\$ 2.655.464,55
In Treasury reserves...	\$ 19.829,30
Property assets of the Bank...	\$ 572,00
Promissory notes	\$ 323.133,70
<b>TOTAL</b>	<b>\$ 3.000.000,00<sup>3</sup></b>

Source: Agote (1881)

<sup>3</sup> The sum is not exact. The author cautions that “the rest was in credit documents, and it is probable that the majority were not redeemable, and even if they were, payment was made late and at a loss (Agote, 1881: 92)

- c) and the balance of six million to be raised by public subscription. This attempt to raise capital failed miserably. In September of 1826 the total subscription barely reached 781.000 ‘sound pesos’ of which the net amount available to boost the capital of the Bank was only 420.000.

Agote (1881-93) acknowledges that the new bank temporarily resolved a political impasse, but lacked the foundation necessary to fulfil the role of a reliable financial institution in the medium and longer term. The ten-year monopoly granted for the issue of legal tender was insufficient to offset the Bank’s precarious capital base and its obligation to stand behind the 2.7 million ‘strong pesos’ that had been issued previously by the Discount Bank.

This obvious dilemma was solved by political expedient: the Congress legislated non-convertibility of paper currency into specie as a component of the financial reform process which created the National Bank. As a result, a paper peso was created, distinct from the former ‘silver’, or “sound”, peso’. This first period of inconvertibility continued until 1867 (see Table 3).

**Table No. 3. Monetary Systems and Exchange Regimes (XIX Century)**

Event	Years
Specie coinage and appearance of quasi-currency	1810-1822
Convertibility	1822-1826
Inconvertibility	<b>1826-1867</b>
Convertibility	1867-1876
Inconvertibility	1876-1883
Convertibility	1883-1885
Inconvertibility	1885-1899
Convertibility	1899-1914

Fuente: Ortiz Batalla, 2014, p. XVIII.

Juan Bautista Alberdi (1895: 374) outlined the circumstances under which the National Bank came into existence quite bluntly:

It started out with 4,741,200 pesos in nominal capital of which 3 million originated in the English loan to Buenos Aires which was an obligation of the government. At the same time the government owed the bank 9,422,565 pesos and the available capital was a mere 626,004 pesos. *The Bank was born bankrupt* (emphasis added).

The Law of the 28 of January of 1826 gave the new National Bank (non-convertible) pesos the status of legal tender throughout the Republic. However, these notes were not accepted outside the Province of Buenos Aires because they were regarded as a mechanism whereby residents of the capital (“porteños”) in general and the English shareholders of the Bank in particular would dominate the entire economy.

There was also discontent on the part of the shareholders who believed in the “wholesome theory” of convertibility and who anticipated that inconvertibility would precipitate an inevitable collapse. They did however accept the creation of the new bank as the only means of protecting their interests and privileges under the prevailing circumstances.

According to Prebisch (1921: 132) had the government not consented to the suspension of convertibility as a pre-condition for the bank serving as a basis for the new institution, the only alternative open to the shareholders would have been the liquidation of the Discount Bank. This was already an unattractive option due to the depletion of the Discount Bank’s bullion capital due to the exigencies of the war. Even so, the government confiscated the remaining bullion reserves, in effect leaving an IOU [“I owe you”] in exchange. Faced with this *fait accompli*, the shareholders were left no option but to accept shares in the new National Bank in exchange for their stake in the Discount Bank.

The problem of determining the amount of currency required to settle contracts agreed prior to inconvertibility immediately arose. Debtors wished to cancel their debts by delivering the specified quantity of common currency paper pesos; the creditors expected the quantity of

non-convertible pesos equivalent to the value of silver that reflected the value of the convertible pesos in silver when the contract was made.

Alemann (1990: 64) recognized that this conflict pitted the Executive Branch, which was predisposed to recognize the settlement power of the common currency at its nominal value by decree, against the Commercial Court, which held the opposite view. In 1828 a law eventually resolved the issue by declaring that any contract prior to the declaration of inconvertibility was deemed to be a contract in convertible currency, whereas contracts subsequent to inconvertibility legislation that did not specify payment in specie were considered paid in full by the delivery of (non-convertible) banknotes.

The same solution was subsequently used whenever non-convertibility was declared.<sup>4</sup> However the legal conflict outlasted the established precedents, and resurfaces each time the, legally sanctioned nominal value of the currency differs from the market or specie currency value agreed in contracts (Pinedo, 1942, quoted by Alemann, 1990: 64)

It is important to remember that the National Bank was established during the war with Brazil which exaggerated the fiscal needs of the government. Releasing the new bank from the requirement to redeem its currency for silver paved the way for the government to cover its deficit by issuing bonds which were held by the Bank.

It is clear that those responsible for establishing monetary institutions failed to learn from the failure of the Discount Bank. Perversely, that experience seems to have enhanced the attraction of the initial phase of credit expansion and its concomitant but illusory economic upturn. The capital required to develop production remained in short supply, and pressure on the government to alleviate this scarcity exaggerated the damage done when it became necessary to reign-in lending.

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<sup>4</sup> The Supreme Court decision dealing with the issue of peso equivalents in the wake of the end of convertibility in 2001/2002 is probably the only instance when the alternative opposite to the historical cases discussed was implemented. In that instance large numbers of individuals who had American dollars on deposit in their bank accounts received pesos at a conversion rate of only 1.4 pesos per dollar, when those pesos could only be reconverted at a rate exceeding 3 pesos per dollar. A number of individuals took the time to appeal for the return of their savings in dollars, but had to wait years before they were able to recoup their capital.

However, the “wholesome theory” of sound money was not completely swamped in the confusion of false concepts which proliferated around the time Argentina’s first banks were created. In 1825, the author of an anonymous pamphlet<sup>5</sup> regarding plans for the National Bank began by laying out this fundamental principle in a way that confirms both the maturity of his thoughts and the strength of his doctrine. Prebisch (1921, p. 130) echoes the same doctrine when he writes, “[b]anks, by themselves do not create wealth, but where wealth pre-exists, they increase the productivity of capital, and benefits arise from its more rapid and advantageous use.” Pretending that banks are themselves agents of production reflects “a desire for the effect to precede the cause, totally reversing the order of things” (Prebisch 1921: 130).

Quite apart from the faulty rationale regarding the potential role the National Bank might play in economic development, the bank also became an instrument for financing the public sector. Five months after its foundation, the new bank doubled the currency in circulation to 5,418.000 million pesos, and the price of specie rose 138% in terms of the non-convertible peso currency. The government’s reliance on the Bank and the depreciation of the currency is evident from the data in Table No. 4:

**Table No. 4: THE FINANCIAL STATUS OF THE NATIONAL BANK**  
(Thousands of common currency pesos)

Dates	Government Debt	Currency In Circulation	Specie value in terms of common currency pesos
December 1826	8.990	7.164	300 %
July 1827	11.365	10.215	330 %
June 1829	18.006	15.287	480 %

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<sup>5</sup> Printed by the National Press. The original document has not survived, and Prebisch relied on Vedia, (1890: 90), for the quote. Manuel Moreno, one of the founders of the Federalist party in Buenos Aires and brother of Mariano Moreno – a prominent Argentine political activist during the revolutionary period -- was assumed to have been the author.

*Source: Raúl Prebisch (1921, p. 134)*

Once again it is clear that the cause of failure to achieve any semblance of monetary order was governmental reliance on the Bank, in this particular case in order to finance the war with Brazil between 1825 and 1828.

The logical consequence was that the common currency peso depreciated sharply in value relative to the silver peso, and it was worth only a seventh of its initial value by the beginning of the 1830. The value of an ounce of gold rose to 120 common currency pesos given the gold-to-silver price ratio of 1:17 (Pinedo, 1961, p.53, cited by Alemann, 1990, p.65).

### **3. The Mint (1836-1853)**

For half a century after the May Revolution of 1810, failure to achieve monetary order was frustrated by a succession of armed conflicts. The first of these were the wars of independence which pitted the United Provinces against the Spaniards. These were followed by civil wars (1829-1861) between a Unitary faction which favored provincial autonomy and a Federal faction which favored strong central government from Buenos Aires. Other conflicts of shorter duration were no less important in terms of their impact on the monetary system. These conflicts are summarized in Table No. 5.



**Table No. 5: Main Armed Conflicts (XIX century)**

Event	Years
Independence war between the United Provinces of the River Plate and Spain.	1810-1824
Civil Wars	1820-1861
War against the Empire of Brazil	1825-1828
The 'Big War' (conflict with Uruguay)	1836-1851
War against the Peru -Bolivia Confederation	1837-1839
French Blockade	1838-1840
Anglo-French Blockade	1845-1849
War of the Triple Alliance	1865-1870
Conquest of the Desert (War against indigenous peoples)	1874-1880

Source: Ortiz Batalla, 2014, p. XIII.

Juan Manuel de Rosas assumed control of the government in Buenos Aires and took responsibility for international relations in 1830 after defeating the unitary faction in a major civil war battle. His first objective was to restore order and end the anarchy which prevailed due to the civil war.

In the monetary sphere, however, Rosas made no immediate changes. He respected the 10-year monopoly over the issue of currency granted to the National Bank until it expired in 1836 when he created a new monopoly source of legal tender. The process of liquidating the National Bank began immediately but dragged on for 18 years until finally, in 1854, the government ordered reimbursement of the shareholders.

The new entity created by decree in 1836 was known as The Mint. It was given a mandate to receive deposits, make loans and issue currency and was required to maintain a reserve ratio of 50 per cent (Cuccorese, 1967, quoted by Alemann, 1990: 86).

As was the case with the Discount Bank and the National Bank, the main activity of the new monetary authority was to issue currency to finance the fiscal deficit. Even Rosas, who rejected this approach when writing on monetary issues, found himself forced to rely on the Mint to finance public expenditure, particularly the cost of the war. Between 1830 and 1851 the volume of currency issued for government use increase from 15 to 120 million common currency pesos (Alemann, 1990, p. 86).

The literature emphasizes the fact that expansion of the currency in circulation was motivated not only by the need for public funds to finance the civil war, but also for other reasons. External conflicts such as the French and Anglo-French blockades that took place between 1838-1840 and 1845-1849 are sometimes used to justify the printing of money. . Blockades caused a sharp drop in trade and reduced the customs duties collected in the port of Buenos Aires, normally a major source of government revenue. The issuance of currency was ramped up to cover the shortfall. Efforts to employ monetary policy to “dampen” business cycle troughs have also been put forward as an explanation. Alemann (1990: 88) highlights the important role increases in the money supply played when crops were poor, a policy from which even provinces beyond Buenos Aires seem to have benefited. This contention warrants further investigation.<sup>6</sup>

Prebisch (1921, p. 135), provides information on the use of pesos issued by the Mint given in Table No. 6 (below), citing Lorini (1902, p. 350) as his source. In 1846 Rosas prohibited use of gold and silver metallic coins to ensure that common currency pesos were used in all transactions.

After the overthrow of Rosas in 1852, the Mint continued with its regular activities. 13,500,000 common currency pesos were issued to cover government obligations and a further 57.7 million to sustain the Mint’s operations. Hence, by the time the institution was

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<sup>6</sup> Ortiz Batalla states that the relative importance of a floating exchange rate, the monetary and fiscal policies followed during conflicts (particularly the three most important from a monetary point of view: the War with Brazil and the two Blockades) and efforts to stabilize the business cycle are unclear. However, the information presented in Table 6 suggests that financing government expenditure played a dominant role (Ortiz Batalla, 2014, pp. XVII-XVIII). Further study is required to confirm this hypothesis.

replaced in 1853, the volume of non-convertible and depreciated notes reached 210 million common currency pesos (Prebisch, 1921, p. 135).

**Table No. 6. Destination of the Currency Issued by the Mint**

	National Bank currency circulating when it closed in 1836	<b>15.287</b>
<b>Dates</b>	<b>Reasons for the Issue of Currency</b>	<b>Amount Issued:</b>
March 1837	Government Déficit	4.200
December 1838	Government Déficit	16.575
September 1839	Renewal of Paper and a 10% increase	3.605
March 1840	Government Déficit	12.000
January 1846	Anglo-French Blockade	75.056
January 1852	For discount operations.	10.300
		<b>137.023</b>

*Source: Lorini (1902) and Prebisch (1921)*

The depreciation of the common currency peso against bullion continued unchecked. An ounce of gold traded at 118 common currency pesos in 1830 and 300 pesos in 1851, while the price of silver increased from 7 to 17 common currency pesos in the same period (Agote, 1881, Volume I).

#### **4 The Bank and Mint of the Province of Buenos Aires (1853-1876)**

It is obvious from the work of Manuel Belgrano, perhaps the first Argentine economist, that an active debate was underway within the country at this time regarding the respective merits of mercantilism and *laissez-faire*. The central dispute of economic politics in the first half century after the revolution was whether to continue colonial privileges or reject them in order to embrace free trade. The Constitution of 1853 gave a clear answer to the outcome of this debate which would have major repercussions for the nation's institutions and economic

policy: the colonial ideology was to be abandoned, and liberalism reflecting the ideas of the Physiocrats in France and Adam Smith in Scotland adopted in its place.

In the introduction to his study of the economic impact of the 1853 constitution on the country, Juan Bautista Alberdi -- the father of that Constitution -- clearly states that, mercantile and socialist ideologies run contrary to the economic doctrine upon which the Constitution of Argentina rests.

Alberdi regards Physiocracy, represented by Quesnay, and the Liberalism espoused by Adam Smith as the preferable alternative. According to Alberdi, the Constitution of Argentina explicitly chose to maximize economic freedom for its citizenry for three main reasons: first and foremost, because economic freedom was acknowledged to be the most effective means of increasing the wealth of the nation; second, because the country needed to be open to immigrants and investment in order to transform itself from a sparsely populated and poorly developed nation, and third because, after struggling for independence from Spain, it would be inconsistent to adopt the colonial economic restrictions which had impoverished Spain and put the hard won political freedom at risk as a consequence (Alberdi, 1854).

According to the Constitution, Argentina is organized as a federal country, open to the world to attract immigrants and foreign investment to populate the land and expand agriculture. Notwithstanding the many changes that have occurred during the country's turbulent history, the Constitution of 1853 is still theoretically in force.

Regarding the currency, however, the National Constitution contradicts *laissez-faire* principles and allocates responsibility for establishing and regulating a national bank in Buenos Aires and branches in the provinces to Congress. Thus the Constitution reserves the exercise of monetary policy for the federal government, requires Congress to authorize the issue of legal tender bank notes (Art. 108), gives Congress authority over production of legal tender and the right to fix its value in terms of foreign currency (Art. 108, Part 10), reserves the monopoly right to issue currency to the Bank of the Province of Buenos Aires (Art. 104, Part 5), and prohibits provincial banks from "coining currency" (Art 108) (Alemann, 1990, p. 97).

Once it was implemented, Article 108 of the Constitution became an insurmountable obstacle to sound money. It prevented the creation of a free, competitive and decentralized system of banking along Scottish lines in Argentina. In the next section, we analyze the difficulties encountered bringing this Article into force. Only when these difficulties were dealt with would a centralized monetary system completely eliminate competition from banking practices which had arisen spontaneously in the hinterland.

#### **4.1 The Bank of the Province of Buenos Aires under Inconvertibility (1852-1867)**

The period 1852-1881 is especially rich in monetary reforms. The Province of Buenos Aires inherited the Mint established by Rosas and it was renamed the Bank and Mint of the Province of Buenos Aires in 1853.

The initial capital of this Bank was 4,112 pesos in specie currency and 5,312,109 depreciated common currency pesos. It took over the property previously occupied by the Mint, which includes furniture and the equipment required to coin and print money.

This capital base was, once again, woefully insufficient to support a viable credit structure. Pressure from the government for help financing expenses increased by the civil war ensured operations were mired in increasingly serious difficulties. In combination these difficulties led inexorably to collapse. It is worth recalling at this juncture that both Rivadavia and Rosas spoke out against depreciating the currency early in their administrations, but both eventually acted against their own advice.

According to Prebisch, the Bank was forced to take over large sums of securities and loans that the country could not absorb, and later, for the benefit of the government, to resort to printing money. Thus, the total amount of currency issued, which included the sum received from its predecessor, rose by the end of the civil war in 1861 to 395.2 million common currency pesos, an exorbitant sum that further depressed the real value of the notes (Prebisch, 1921, p. 136).

The government of Argentina attempted to create a new National Bank in 1854 after the province of Buenos Aires joined the Republic. This failed within a year due lack of bullion

capital, notwithstanding the fact that its creation was consistent with the constitutional clause which reserves the right to issue legal tender for a national bank created by Congress.

As a consequence, paper currency only circulated in Buenos Aires. Repeated issuance of new bank notes by successive governments in the province of Buenos Aires further depreciated the value of the common currency peso. The price of an ounce of gold soon exceeded 400 pesos of common currency at the rate of 16 silver pesos per ounce of gold. One third of the money in circulation, or more than 400 million common currency pesos, was 'rescued' by the provincial government and burnt, as was the practice of the time to counteract the consequences of too liberal issuance of bank notes.

In the 1860, the Bank of the Province of Buenos Aires remained an official provincial government agency. Proposals that it be transferred to private ownership were rejected. In 1864, the Executive Branch of the Province of Buenos Aires tried another strategy to resolve the problem of excessive printing of bank notes and the consequent monetary instability. It sent a draft of a conversion law to the legislature which provided for the conversion of paper currency to gold at the rate of 400 common currency pesos per ounce or 16 silver pesos. The law also stated emphatically that the government would issue no more bank notes. Although the legislature approved the law, it proved impossible to implement. The price of an ounce of gold rose above the legally specified conversion rate, the bullion reserves were insufficient despite a foreign loan denominated in gold. Difficulties encountered selling public lands associated with the Western Railway and the cost of the war with Paraguay also contributed to the failure of the conversion (Cuccorese, 1969: 115).

#### **4.2 The Exchange Office and the Return to Convertibility (1867-1881)**

Three years after the failure of the conversion law of 1864 an Exchange Office was created. It was associated with the Bank of the Province of Buenos Aires but its operations were independent of those carried out by the Bank. The mandate of the Exchange Office was to buy gold with common currency paper pesos and common currency paper pesos with gold at a statutory rate of 25 common currency (paper) pesos for one (specie) 'sound peso'.

Surprisingly, and despite its limited reserves of bullion, the Exchange Office was relatively successful. Convertibility was restored after forty years of non-convertibility and fluctuating exchange rates, and would remain in effect until 1876.

Despite the war, for a while neither the provincial government nor the national authorities tried to monetize public deficits, relying instead on foreign loans. The expansion of the sheep raising industry brought in foreign exchange, and the common currency peso improved its open market value on the Stock Exchange of Buenos Aires which had reopened in 1854. The Bank also became better established and, in combination with the overall economic improvement and the adoption of some effective policies, paved the way for monetary equilibrium and a currency which was convertible in practice as well as in theory (Piñero, 1921: 193)

These improvements prompted Prebisch (1921, p 137) to pose the following questions: first, what caused the sudden improvement in the economic situation? and second, was the abundance of gold in the country the visible consequence of this sudden economic upturn or the result of specific financial policies?

Prebisch bases his own answer on information provided by Agote (1881). Table No. 7 shows the unfavorable trade balance from 1865 to 1875 which amounted to a negative balance of 137.6 million pesos. This trade deficit was the result of a continuous and pronounced increase in imports. Only in the last two years of the Table does the trade balance shift to a surplus. In this same period, the bullion reserves of the Exchange Office increased by 64.8 million pesos. These must necessarily have arisen from the favorable balance in the capital account which was itself the product of the institutional changes originating in the Constitution of 1853. These changes enabled Argentina to attract foreign capital and provided access to foreign loans.

The table presented by Prebisch (1921, p. 137) does not include information on capital flows, but it is possible to estimate these from the data provided. We therefore include a column showing Capital Inflow in Table No. 7 (above). The capital inflow between 1867 and 1875 is

estimated to have approached 188.6 million pesos, but swung the other way in 1876 and 1877, with a capital outflow of 11.3 million pesos.

Prebisch provides an explanation which is consistent with the capital flow information added in Table 7. He notes that foreign loans begin to increase in 1868 and reach their peak between 1871 and 1873. They collapsed in 1874 and did not revive until the following decade. The sum officially borrowed by the national government in the foreign exchange markets during the period 1868 to 1873 rose to 15,546,884 pounds sterling. In addition to these and other loans, at that time the private sector began to borrow abroad to develop productive capacity within the country. In both cases, the relative peace that prevailed during these years was a major factor.

Prebisch also indicates that by the end of 1873, the national government's indebtedness to the Bank of the Province of Buenos Aires had risen to 7,637,108 'sound pesos' (= to 188 million common currency paper pesos and the debt of the provincial government reached 176 million common currency paper pesos. After that date debts continue to grow rapidly reducing the value of common currency in terms of sound pesos' (Prebisch, 1921, pp. 138-141).



**Table No. 7. The Evolution of Foreign Trade and The Financial Position of the Exchange Office  
(Thousands of pesos)**

Years	Foreign trade (1)			Capital Inflow (sound pesos)	Exchange Office Transactions (2)	
	Imports (sound pesos)	Exports (sound pesos)	Trade Balance(3) (sound pesos)	(Estimated by difference)	Bullion Reserves	Common Currency Paper Pesos 1=25
1865	30.284	26.126	- 4.157	-	-	-
1866	37.401	26.740	-10.660	-	-	-
1867	38.792	33.196	-5.596	9.076	3.480	-88.022
1868	42.412	29.709	-12.702	18.042	5.340	133.509
1869	41.195	32.449	-8.746	12.623	3.877	96.942
1870	49.127	30.223	-18.901	25.902	7.001	175.039
1871	45.629	26.996	-18.632	29.159	10.527	264.139
1872	61.585	47.267	-14.317	29.730	15.413	385.330
1873	73.434	47.398	-26.035	36.192	10.157	253.941
1874	57.826	44.541	-13.285	19.527	6.242	156.055
1875	57.624	53.009	-5.615	8.438	2.823	79.599
1876	36.070	48.090	12.020	-7.148	4.872	121.823
1877	40.443	44.769	4.326	-4.168	158	3.720

*Source: Compiled by the author, based on Prebisch (1921, p. 137)*

(1) Data from the Department of Statistics of the Nation

(2) Data based on the numbers given by Agote, op. cit. p. 129, on transactions through the Exchange Office.

(3) Data are indicative only. We are aware that in some years the balance is not calculated correctly, but chose not to alter the data provided by these authors.

**Table No. 8. Inflation of the Money Supply (1866-1973)**

Year	Rise or Decrease of Currency Issued		Changes in the Portfolio of the Bank of the Province of Buenos Aires.		
	Common currency pesos\$	Equivalent value in 'sound pesos'	Common currency pesos	Equivalent value in 'sound pesos'	Total obligations in terms of 'sound pesos'
1866 (end)	298.457	11.938	47.292	4.903	6.974
1867	88.022	3.480	122.650	6.697	11.603
1868	45.487	1.860	159.523	7.698	14.058
1869	-36.567	-1.463	272.638	11.344	22.248
1870	78.097	3.124	339.405	11.953	25.529
1871	89.100	3.526	369.975	15.910	30.706
1872	121.191	4.886	510.328	20.714	41.126
1873	-97.866	-5.256	588.894	21.695	45.247
Total Emission	552.398	22.095			
Plus the Metallic notes emission of 1867-73	135.575	5.423			
	687.973	27.518			

*Source: Prebisch (1921, p. 140)*

Under such circumstances the credit structure required for expansion existed, and significant growth in business activity therefore occurred. If the amount of notes in circulation given at the time of the opening of the Exchange Office was in fact 298 million common currency paper pesos, the outstanding obligations of the Exchange Office would increase continuously over time if the amount of currency in circulation and the associated obligations of the Exchange Office moved in tandem. This growth of Exchange Office obligations is shown in Table No. 8 (above). Note that during this time of the boom and prosperity, it was not necessary to take advantage of the opportunity to convert paper money at the Exchange Office because exports of gold were not necessary.

The growth brought by the credit expansion was the cause of the crisis of 1873-1875, although some authors prefer to identify it with speculation. At the time it was said that "[t]here was no warning", since excessive credit extraordinarily stimulated trade and speculation equitably for all classes of society, and resulted in price inflation (Balbin, 1877: 6).

In Argentina, speculation, according to Prebisch, was directed mainly at real estate. This was also the case in many other countries at a similar stage of development (e.g. in Canada). Fabulous price increases which bore no relationship to the capital employed occurred despite the fact that the land in question did not produce any return.... ... a piece of land in Lincoln, in Tapalqué, or at other more or less deserted locations in the country passed from hand to hand and huge profits were made in a matter of hours until finally the process ended with the creation of wholly imaginary towns. Every industry, every speculation, risky though they may have been, attracted attention, and those who showed least prudence in the risky calculations were hailed as "business geniuses". At that time in history credit was not used in a rational way in conjunction with existing capital, and those who did so were denigrated as "narrow minded and incapable" of assessing the future. (Prebisch, 1921: 140-141).

It is now widely accepted that speculation is not the cause of business cycles. The primary cause of these cycles is the credit policy which we are discussing here in the Argentine context.

The expansion of currency in circulation gives rise to an increase in loans outstanding which is in reality a result of that expansion.<sup>7</sup>

If we refer back to Table No. 7, it becomes evident that the peak in the capital account occurred in 1873, decreasing thereafter and causing the outbreak of a crisis.

Borrowing abroad by the country between 1867 and 1873 must have been considerable. It not only permitted an increase in domestic circulation of money, but it also financed the extraordinary bulge in imports. Imports rose dramatically because inflated prices and the atmosphere of artificial prosperity incited many importers to dramatically increase their orders. Imports of 23 million pesos in 1865 (see Table 7) rapidly rose to 73 million in 1873, tripling in the short space of nine years, while exports barely doubled. As the trade balance was slightly unfavorable at the beginning of the period, its reversal was dramatic after 1873 when imports reach their peak. Without access to foreign loans, the country would not have been able to pay the large sums required for the volume of imports indicated. This would also explain the paradox of unfavorable trade balances and the increased bullion reserves in the country. In 1873 this artificial prosperity ended abruptly, and confidence evaporated (Prebisch, 1921: 142)

The causes of this crisis still need to be more thoroughly researched, but in the existing literature both local and external causes share the responsibility.

Locally, as Prebisch points out, the government put the Bank in a difficult position, by withdrawing most of the bullion deposits obtained as loans and which, as has already been stated, the establishment was then using to back long term loans. Although he was unable to point to evidence for the reasons behind such withdrawals, he suggests that as was usually the case, the government probably required the gold to meet its commitments abroad (Prebisch, 1921, p. 143).

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<sup>7</sup> This theme is dealt with in detail in my book *In Search of Full Employment (En busca de pleno empleo* (Ravier, 2010)).

**Table No. 9: Fluctuations in interest rates charged by the Bank of the Province of Buenos Aires (BBA) and other banking institutions**

DATES	1873		1874		1875		1876	
	BBA	Other Institutions	BBA.	Others	BBA	Others	BBA.	Others
January	6	7 – 9	9	12 - 15	8	10,5 – 15	7	8 ‘- 12
February	6	8 – 9	9	12 - 15	8	10 – 15	7	8 ‘- 10
March	6	7,5 - 9	9	10,5 - 15	8	10 – 15	7	10 ‘- 12
April	6	9 - 12	8	10 - 10	8	10 ‘- 15	7	10 ‘- 12
May	6	10 ‘- 15	8	12 ‘- 15	8	9 ‘- 15	7	7 ‘- 10
June	8	12 ‘- 15	8	12 ‘- 15	8	10 ‘- 15	7	6 ‘- 10
July	9	12 ‘- 15	8	10,5 ‘- 15	8	10 ‘- 15	7	6 ‘- 10
August	9	12 ‘- 15	8	9 ‘- 12	8	10 ‘- 15	7	5 ‘- 8
September	9	12 ‘- 15	8	9 ‘- 12	8	8 ‘- 15	6	5 ‘- 8
October	9	15 ‘- 18	8	9 ‘- 12	8	8 ‘- 15	6	4,5 ‘- 6
November	9	15 ‘- 18	8	12 ‘- 18	8	8 ‘- 15	-	-
December	9	9 ‘- 15	8	12 ‘- 18	8	8 ‘- 15	-	-

*Source: Prebisch (1921, p. 144)*

It is also important to remember that in 1873 Britain increased interest rates sharply from 4.5% in January to 6% in October and 9% in November. These sharp increases restricted foreign borrowing and were symptomatic of a change of international circumstances that influenced Argentina’s economy. Exogenous factors may therefore have complemented the usual list of domestic culprits – military conflicts, the deficits of the national and provincial governments, and the exchange disequilibrium – to precipitate the downturn of 1873.

This combination of domestic and international circumstances led to restrictions in the domestic credit market in the middle of 1873 which caused interest rates to rise. Table No. 9 (above) summarizes the dynamics of the interest rate of the provincial Bank and other banking

institutions, illustrating the interest rate policy of the provincial bank. While other institutions raised their interest rates in April 1873 in anticipation of the credit contraction, the Bank of the Province of Buenos Aires followed suit only in June, when it increased rates from 6 to 8%. The reverse situation occurred in 1876: whereas other institutions began reducing their rates in April, the provincial bank did so only in September.

In the period of crisis between 1873 and 1876 Exchange Office reserves declined, probably due to fears that a new declaration of non-convertibility was imminent. Reserves fell from 10 million in 1873 to 6,000,000 in 1874 and to 2 million in 1875. Eventually, the government did issue a decree making the paper peso non-convertible on May 16, 1876.

Prebisch, 1921, p. 146) points out that these regulatory changes were immediately disruptive because up until this point the sound pesos in circulation could be readily exchanged for their specie/bullion equivalent at the exchange office. In the first half of May, however, the value of a 'sound peso', or the 25 common currency pesos to which it was equivalent ranged between 49.25 and 48.50 pence on the London market; in the second half of May, the same 25 common currency pesos, now no longer convertible and therefore of lower value than the 'sound peso', depreciated to 40 pence; in subsequent months, this depreciation continued until the value of 25 common currency pesos reached 37 pence. In April 1877, quotation of the 'sound peso' resumed, and the devaluation of the common currency peso is not available in terms of international exchange rates but can only be worked out via a valuation in terms of gold

### **The National Bank of 1872 and its coexistence with the Bank of the Province of Buenos Aires**

After 1853, the national government had a constitutional mandate to effect a uniform monetary regime throughout the nation. In 1872 it enacted a law to create a National Bank (the third with the same name: its predecessors were established in 1826 and 1854, respectively). In this iteration, the National Bank was to be privately managed. Its capital base was to be 20 million 'sound (i.e. silver) pesos'. The government contributed the equivalent of 2 million sound pesos in the form of public debt securities and the founding shareholders

listed in the law contributed a further 5 million. The remaining 13 million were to be raised by public subscription.

This National Bank coexisted with the Bank of the Province of Buenos Aires, and bank notes issued by both circulated in competition with each other. The National Bank was legally entitled to issue notes payable to the bearer on demand, while the provincial bank, through its Exchange Office, issued common currency pesos convertible to gold or silver.

The crisis of 1873-1875 coincided with the first few years during which this National Bank operated. Table No. 10 summarizes the Bank's response to these difficulties. These difficulties are reflected in the increase in the notes issued in the first two years of the Bank's existence, and the decrease registered in those same accounts in 1875, when the process of winding up the bank began.

**Table No. 10. The Financial Position of the National Bank**  
(Thousands of 'sound pesos')

Date	Real Capital		Cash	Private Deposits	Notes Issued	Loan Portfolio
	Bullion	Funds and Bonds				
1873	2.551	449	1.908	156	2.251	2.663
1874	-	-	3.887	6.606	5.248	9.110
1875	4.030	441	2.551	1.618	3.407	5.573
1876	5.124	555	208	216	911	5.523

*Source: Quesada (1901), quoted by Prebisch (1921, p. 151)*

Between the date it commenced operations and June 30 of 1874 the National Bank issued no less than four and a half million of 'sound pesos' (equivalent to 112 million common currency pesos), and loaned out a further 9.5 million 'sound pesos' (about 250 million common currency pesos). The resultant problems quickly became apparent, and on May 16 of 1876 the Bank of the Province of Buenos Aires abandoned convertibility. The National Bank tried to

maintain convertibility, but only managed to do so for a couple of weeks. On the 29th of May it too was forced to declare inconvertibility.

The situation was already precarious for the National Bank, but the final blow came when currency issued by the Bank of the Province of Buenos Aires was granted legal tender status throughout the Republic. Beyond the borders of the Province of Buenos Aires complications arose because currency of various origins was already circulating. There was therefore a reluctance to use the new currency being imposed from Buenos Aires because these local monetary instruments were generally much more stable than the currency issued by the Bank of the Province of Buenos Aires.

1875 proved to be a significant year in the monetary history of Argentina. Law 733 created the gold 'strong peso' of 1.66 grams and 900/1000 purity, as well as coins equivalent to 1/10 of a gold peso. The gold peso was subsequently broken down into hundredths to create a decimal currency. The currency representing ten gold pesos was known as the 'Columbus' ("*Colon*"). Twenty pesos was thus a 'double Columbus' and five pesos "half a Columbus". As a result, the monetary system envisaged but not realized when the Confederation of the "provinces on the River Plate occurred in 1858 finally came into effect.

The government headed by Avellaneda, in which Victorino de la Plaza was Minister of Finance, completed the monetary reforms. The Mint was created in 1877, but became operational only in 1881. Monetary legislation (Law 1130), also enacted in 1881, codified the national monetary system for Argentina. The peso became the legal currency. One 'gold' peso contained 1.6129 grams of gold and one 'silver' peso 25 grams of silver. The paper peso was pegged to the value of these metals and could therefore theoretically be converted to a given quantity of gold or fifteen and a half times the same quantity in silver.

This monetary system has been adopted in the Latin Union since the Paris Convention of 1865. This Union now comprises twenty countries, including the Argentine Republic (Alemann, 1990, p. 120).



Law 1130 sought to end the use of foreign currencies and prohibited their use once eight million gold pesos and four million silver pesos were in circulation. Until this happened, foreign currencies continue to be recognized at values set by decrees issued by the Executive Branch of the national government. According to the hypothesis put forward by Maria Cristina Gomez (1994), competition among local and foreign currencies -- to whatever extent it might have occurred -- ended abruptly when Law 1130 was eventually enacted in 1881.

This law did not only end the use of specie coins of the interior provinces. It also included a provision whereby the common currency peso bank notes of the Bank of the Province of Buenos Aires could be converted to gold or silver pesos at a ratio of 25 to one. This ended circulation of common currency pesos and the national peso became the sole legitimate currency throughout the country. This national peso remained in circulation until 1969, when a new peso was substituted for one hundred 'old' pesos (Law 18188).

The one to 25 conversion could be made only because the price of the silver "strong peso" dropped in 1881 to nearly 30 common currency pesos, so the opportunity to convert it to the new peso at 25 to one was attractive. The monetary and economic crisis of 1873 was therefore resolved. Around the same time the defeat of the aboriginal peoples and the resolution of the longstanding dispute regarding the location of the federal capital completed the institutional framework for the nation. These events facilitated foreign loans denominated in gold, exports and capital investment (Hansen, 1916, p. 391).

### **Concluding Remarks**

In these five sections we have shown that repeated attempts to attain monetary order in Buenos Aires over the period from 1822 to 1881 were undermined by the government's determination to enforce a monopoly over the issue of legal tender currency. This paper has traced the evolution of this strategy through a succession of monetary institutions: the Discount Bank (1822-1826), the National Bank (1826-1836), the Mint (1836-1853), the Bank and Mint of the Province of Buenos Aires (1853-1872) and the National Bank (1872-1881). The independence of each of these institutions was eroded by the demands placed on them by

governments in perpetual need of funds to deal with armed conflicts and other emergencies. These conditions made the development of sound money impossible.

These constraints on the independence of monetary institutions in Argentina continued through the remainder of the nineteenth century and most of the twentieth century, and any pretense of independent monetary policy ended completely with the creation of the Central Bank of Argentina in 1935. In this sense, any differences between the era of central banking and the history of banking institutions reviewed here are superficial. Should Argentina ever seriously aspire to a sound money regime, monetary institutions insulated from political interference are an essential condition.

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