



# Economic Liberalism in Peru

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As in most Latin American countries, (classical) liberalism in Peru lacks a strong tradition. One can hardly talk about liberalism in Peru as a cohesive movement extending through time; its standing among the general population and ruling elites has generally been weak. But in comparison to other Latin American countries studied in this series, and thanks to the important—albeit incomplete—reforms implemented in the last three decades, Peru is currently less like Venezuela (Faria and Filardo 2015), Ecuador (Romero, Hodgson, and Gomez 2018), and Mexico (Kuchar 2016), and rather more like Guatemala (Marroquin and Thomas 2015), which has over the past several decades had a strong locus of institutions and networks advancing liberalism, either by disseminating its ideas or by implementing its policies.

Peru's institutional context explains much of the lack of cohesiveness of Peruvian classical liberalism. The following sections of this paper expand on that idea and trace relevant history.

## Pre-Columbian economic institutions

The Andes run right through Peru, in slightly from the Pacific coast. The geographic conditions require creativity to manage intensive farming. Along the coast there is no rain and irrigation is necessary. In the extensive Andean region, soil management is required. Nevertheless, Peru's economy since the early formative periods has been one based in agriculture: the earliest evidence of economic

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activity is centered in working the land (Kosok 1965). This dependence on agriculture and the infrastructure projects required for intensive farming relate to an institutional framework of collectiveness rather than individuality.

The Chavin culture arose between 900 and 300 BCE, and it gives us one of the earliest clues about a collective economy. Judging by architectural complexity, a large population must have been employed in the construction of its large buildings, presumably under some stability of government and organization, employing communal labor for such purposes (Burger 1992). Evidence from the Chavin period also points to organizational precursors of the *ayllu*, a socially recognized organization of blood relatives to which access to property and benefits

of production were assigned. The necessity of pooling labor resources together in order to farm the land intensively is believed to have been the root cause of the formation of the *ayllu*. The members of the *ayllu* benefited by sharing resources to work the land, distributing the work of the land as well as the products that resulted from it. The economic relationship among the members of the *ayllu* was one of reciprocity. However, some of the works of architecture and infrastructure found during the pre-Incan era show a greater measure of organization than mere reciprocity within and between these socioeconomic units. Some degree of larger public undertakings must have been present. Similar conclusions can be drawn from analyzing the Tiwanaku culture, post Chavin and pre-Inca Empire, that arose between 300 and 1000 CE.

A degree of central planning definitely marks the Inca Empire, the societal structure of which was built around the *ayllu*. During the Inca Empire, belonging to an *ayllu* had greater significance than merely blood ties. It brought with it a series of rights and responsibilities that both secured and preserved birthrights and survivors' legacy (Contreras 2008a). There was a paternalistic administration of reciprocity and distribution that worked as follows: each *ayllu* had a head, the *curaca*, who was supposed to be the eldest and therefore the wisest among the members of the *ayllu*. The *curaca*'s main responsibilities were the allocation of land within the *ayllu*, delegation of maintenance of the irrigation mechanisms and delineating and safeguarding the security of the parcels' limits, conflict resolution, provision for 'orphans' not belonging to any *ayllu*, organization of the communal labor, and



storage and distribution of surpluses.

Curacas were the link between the ayllu and the Incas, and they selected and delivered 'gifts' from the ayllu to the Inca. The Incas governed by 'divine authority,' therefore those gifts from the ayllu to the Incas were some form of worship. Curacas also administered Incan directives and law, including ruthless punishment of those deemed lawbreakers.

The people in the ayllu performed three types of work: the communal work (called *minka*), assistance work for other members of the ayllu (called *ayni*), and the work they performed for the Inca (called *mita*) which was the closest thing to a tax that existed during the Inca empire. Ayllus were self-sufficient, hence the absence of trade, but the curacas administered the surplus, which was doled out of the Incas' stores in times of drought. It has been estimated that at its height the Inca empire reached a population level of between 7 to 10 million inhabitants.

Central planning, community, and reciprocity were thus the major principles of the Incan economy. Individuality was a concept neither desired nor sought after; individuals not belonging to an ayllu were considered orphans, and curacas would quickly seek to incorporate them into one, and thus secure their subsistence. The Incan form of societal organization played an important role in the dynamics between the arriving Spaniards and the indigenous Peruvians.

## The colonial period

When the Spaniards arrived in the sixteenth century, the highly religious Inca civilization was experiencing its own civil war. The last Inca before the arrival of the Spaniards, Huayna Capac, died suddenly, and although he had designated his son Huascar as his heir, his younger son Atahualpa rebelled. Atahualpa had been born in the recently conquered northern part of the empire, and therefore during his campaign to dethrone his brother, he had the support of the population that inhabited those regions. Atahualpa ended up defeating his brother Huascar.

When Francisco Pizarro arrived in Peru, and upon capturing the now reigning Atahualpa in the battle of Cajamarca, he found a kingdom divided, and now headless. He also found a people used to centrality in social organization, and heavily theocentric. And he found a country rich in natural resources, especially gold and silver. The Spanish conquest of the Americas was mainly motivated by a quest for riches, whether by resource extraction or trade, and a desire to spread Catholicism. The abundance of gold and silver, the absence of a ruler, the theocentric nature of rule, and the established tributary labor that the Incan people had assimilated into their empire created an environment highly conducive to the Spanish Crown's purposes in conquering Peru. There were, however, multiple

rebellions during the thirty-six years between the arrival of the Spanish forces and the suppression of the last rebel stronghold.

The Peruvian indigenous peoples were during this period all but destroyed by the Spanish colonization. Warring, rampaging disease, and extreme exploitation—largely, forced labor in mining—caused the population to fall by some 90 percent from its peak.

From the Spanish Crown's desire to expand Catholicism—together with the necessity of preserving some of the labor force—a reprieve was instituted for those members of the Peruvian indigenous population who agreed to convert to Catholicism. If they agreed to it, then they became subjects to the Spanish Crown bound by its political, social, and economic administration, thus, obligated to pay taxes, in their usual form of forced labor, and put under the pretext of teaching the Incans a new way of life, which included the Christian faith. If they refused, then war was waged on them (Contreras 2008b). For the organization of their new 'subjects,' the conquerors took advantage of the existing structure and established the *encomienda* system. The term *encomienda* stems from the Latin *in comendam*, which means 'in care of.' The *encomendero* was in charge of collecting the taxes from the indigenous population, but also was supposed to provide education and training for them, and to have a church for them to meet. The primary aspect of the *encomienda*, however, was the collection of tributes, executed by incorporating the figure of the *mita* and the *curaca* into this system. It looked to perpetuate the centrality that the indigenous population was accustomed to, but rather than for the mutual benefit of the rulers and the ruled, it was used for the extraction of labor and riches from them.

Indeed, a stark difference between the Incan *mita* and the Spanish *mita* was that under Incan rule a *mita* worker spent only a fragment of his time at the labor site, his needs were provided for, and then he was able to return home and continue with his farming labors. The Spanish *mita* did not provide for the workers, who had to pay for their own subsistence out of their meager salaries. The workers often sunk into a vicious circle of debt, which commonly caused abandonment of their farming activities. The result on a societal level was a significant fall in subsistence agricultural production and, later, famine.

High level of extraction caused the gold and silver to dry up relatively quickly. But the Spanish elite was heavily motivated by consumption, and once gold and silver dwindled the tribute took the form of other goods and even some services for the *encomendero*. Soon it became clear that the *encomienda* would not be a temporary system while the indigenous population was educated. Rights to 'inherit' the *encomienda* in perpetuity were established. This form of exploitation was not sustainable and sparked some of the first moves towards liberalism of that era. Former *encomendero* and priest Bartolome de las Casas advocated passionately for

the end of the *encomienda* system, and he supported the creation of the New Laws of the Indies for the Good Treatment and Preservation of the Indians (or simply “New Laws”) issued by King Charles V, which eventually ended the system. The New Laws prohibited the enslavement of the native population, declaring them free people who, although required to pay tribute to the *encomendero*, were to be paid wages for their labor and were not to be inherited as possessions. Fair treatment of the native population was specifically stipulated in the New Laws, and work in mines was restricted to particular circumstances.

With the depletion of the mines and the end of the *encomienda* system, in time, the core of the economic activity turned again towards agriculture and the development of other industries, which set the stage for the first steps towards the development of greater individual economic freedom. Though it took time to actually enact the New Laws, from the resistance of the *encomenderos*, the changes in economic activity in colonial Peru meant that it had become more valuable to own land and capital than forced labor, and the *hacienda* system replaced the *encomienda* system. Key to the *hacienda* system was private property. Spanish and their *criollo* descendants were the ones legally allowed to own large holdings of land, and to employ the remaining of the indigenous population as laborers on such land. Social structure determined a specific group’s set of rights. In general, many possible rights were held only by the Spanish and the *criollos*, who were considered the elite. *Criollos* were those of full Spanish descent but born in Peru, and although they did enjoy many of the benefits of those born in the Spanish Peninsula, they were not considered entirely equal, which was a source of resentment and played a significant role in the eventual crusade for Peru’s independence from Spain.

The Spanish elite had wasted much of the riches and fallen into ruin. On the other hand, many individuals of mixed race who had not been afforded the privileges of the elite had developed an aptitude for trade and commerce that had resulted in material prosperity. The almost bankrupt elite were impelled to open their doors to mixed race individuals to occupy important positions in the government. Meanwhile, in the lower social strata, the social system held that only indigenous Peruvians could be part of an *encomienda*. Any individual of mixed race could not be part of the forced labor and exploited population, and was also guaranteed access to a certain level of education. This prompted indigenous Peruvians to intermix with those of Spanish origin and have children with them, often leading to better lives for their progeny.

Many individuals with strong local or indigenous ties but educated as one of Spanish ancestry had access to or even could become part of the ruling elite. These dynamics gave roots to the movement for independence. Also important was the work of the Jesuits who, prior to their expulsion in 1767, played a significant role in educating the mixed race population, advocated for better treatment and better

salaries of the natives, and perhaps plotted to decrease the power of the Spanish Crown in the region (Lockhart and Schwartz 1983).

A prime example of said dynamics as one of the foundations for independence from Spain was the rebellion in 1780 of Tupac Amaru II, regarded as one of the precursors of individual political freedom in Peru. Tupac Amaru II was the son of a curaca, and it has been speculated that he was of mixed race, what they called *mestizo*, the mix of Spanish and indigenous Peruvian. He was educated by the Jesuits at the San Francisco de Borja school. He governed the chiefdom of Tungasuca near Cusco, on behalf of the Spanish governor. In 1780 he rebelled against the local Spanish authorities, and with the support of the indigenous people, battled the Spanish forces, overpowering them initially but suffering defeats after most of the criollos withdrew their support once he indicated that he intended to kill the Spanish leaders. He and his family were executed shortly thereafter, but his legacy was the beginning of many indigenous insurrections in the search for liberty from the Spanish oppression throughout the Spanish colonies in South America (Walker 2015).

The independence movement, and ideas of liberty in general, were notably fostered and strengthened through the institutions of higher education in Peru. The first university of the Americas, National University of San Marcos, had been officially established in Lima, the capital of Peru, in May 1551, and it centuries later it would become the birthplace of the main currents of liberal thought in Peru, as it spread Enlightenment ideologies of republicanism, political equality, secular government, private property, and the rights of citizenship. Some of the thinkers that were considered precursors of Peruvian independence either studied, taught, or gathered there. The early secularization of the university was likely an important factor. Until 1581, provosts in the University were only members of the clergy. In that year, Viceroy Francisco Alvarez de Toledo authorized the election of secular provosts (Valcarcel 2001), which was a crucial development that redefined the university as a space of freedom of thought and opened the way for questioning and criticism of the colonial system.

Among those who paved the road for Peruvian independence were the Jesuit Juan Pablo Vizcardo y Guzman (1748–1798), Toribio Rodriguez de Mendoza (1750–1825), Jose Baquijano y Carrillo (1751–1817), and Hipolito Unanue (1755–1833), all of whom participated in the Academic Society of Lovers of the Country and its main publication, the *Mercurio Peruano*, which operated within San Marcos university in the late eighteenth century. The society and its newspaper were initially created to discuss literature and public news, but it soon became the voice of those who desired to see Peru as an independent nation (Grupo Historiem 2001). Their line of thought, however, was more one of constitutional reform and political rights than of liberalism proper. Baquijano, for example, editor of *Mercurio*

*Peruano* between 1791 and 1795 and the president of the Academic Society of Lovers of the Country, was quite mercantilist and advocated for promoting mineral exports as the leading activity of the Peruvian economy (Riva-Aguero 1953). Baquijano had been influenced by Pablo de Olavide, another Peruvian criollo whose Madrid home was one of the main meeting points for Enlightenment thinkers (Defourneaux 1959). Baquijano had also to some extent been influenced by Gaspar Melchor de Jovellanos, who was in turn influenced by Adam Smith's *Wealth of Nations* and had sought to eliminate large ownership of land by the Catholic Church in favor of private property, a position that Baquijano did maintain. The focus of their advocacy, however, was mostly centered in political freedom—political voice and representation—and a connection to individual liberty had not yet been established and was not yet strongly pursued.

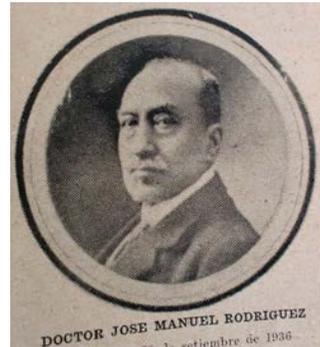
Political freedom was fiercely pursued, and in the early nineteenth century, through the efforts of the Argentinian Jose de San Martin and the Venezuelan Simon Bolivar, Peru obtained its independence from Spain and thus began a new era in the life of Peru, now as a Republic. San Martin was a criollo soldier, who initially fought for the Spanish crown, but later switched allegiances when confronted with the unequal treatment that not having been born in the Spanish peninsula afforded him. Bolivar was a criollo as well, who had been educated in Europe and exposed to Enlightenment ideas, and who also witnessed the coronation of Napoleon, events that left a large imprint in him and lead him to swear to overthrow the Spanish reign in colonial America (Arizmendi Posada 1983).

## Independent Peru

A focus on political rather than economic freedom continued after Peru's independence from Spain. Hipolito Unanue, a physician, precursor of Peruvian independence, and member of the Academic Society of Lovers of the Country, became in 1824 the first Finance Minister of Peru. He continued the mercantilist regime by heavily taxing imports and directing the country's focus onto exports.

The first century of independent life of the new Republic of Peru oscillated around protectionism and high taxation. There was no clear line of thought nor theory that drove economic policy, other than that which served the purposes of the politicians and gained them the support of the relevant segments of the population at each point in time (Contreras 2011). The nineteenth century saw continued uprisings from the provinces, as the situation of the indigenous population had changed very little after independence was achieved, and the prevailing extractive institutions had simply been renamed.

In the 1880s, one of the first vocal classical-liberal economists arose in Peru. Jose Manuel Rodriguez (1857–1936) was a congressman who openly criticized the inconsistent character of Peruvian public policy, the extractive nature of taxation, and the lack of economic sense in such policies. He advocated for a contractual relationship between the civil society and the government, which he said needed to specify mutually established rights and obligations. Rodriguez's most renowned work is 1895's *Estudios económicos y financieros y ojeada sobre la Hacienda pública del Perú y la necesidad de su reforma* (*Economic and Financial Studies and a Look at the Public Treasury of Peru and the Need for Its Reform*). Unfortunately, many of his works have been lost (Contreras Carranza 2016), but still he is considered a founder of the economics profession in Peru; there was no individual nor group before Rodriguez who formulated and organized Peruvian economic discourse like he did.



Rodriguez started the monthly journal *Economista Peruano*, which ran from 1909 to 1940 and in whose pages were often cited such thinkers as Smith, David Ricardo, John Stuart Mill, John Locke, Frédéric Bastiat, Jean-Baptiste Say, and A. R. J. Turgot (Molina, Montes, and Romero 2008). Rodriguez's ideas and efforts inspired the first generation of Peruvian economists, including Cuban-Peruvian Jose Payan (1844–1919), Pedro Emilio Dancuart (1847–1911), Alejandro Garland (1852–1912), Luis Esteves, Jose Manuel Osoreo (b. 1815), and Luis Larrañaga (Contreras Carranza 2016).

Tax reform was a chief topic of discussion in this platform that Rodriguez had created. Rodriguez advocated liberalizing policies such as lower tariffs and fiscal reforms, but he also advocated interventions including capital controls, as Peru was exporting heavily and running a negative financial-account balance.



At the end of the nineteenth century a segment of the Peruvian oligarchy vocally favored laissez faire. The leading group in favor of a more open economy were the owners of plantations and haciendas, whose agricultural products were the main export commodity. This group was represented by the Camara de Comercio de Lima (Lima Chamber of Commerce), through the voices of two of its members, J. Russell Gubbins (1845–1935) and the aforementioned Alejandro Garland. They argued that tariffs increased the cost of living of all Peruvians in

favor of non-competitive industries. On the other side of this debate was the Sociedad Nacional de Industrias (National Industry Society), representing local industry through the voice of Felipe Barreda y Osma, who defended Peru's tariff rate, arguing that it was even lower than that of Argentina and Chile. These groups still exist and continue in nearly the same policy positions.

## In the 20th century

Greatly dependent on natural resources, with a heavily protected industry, and a war with neighboring country Chile who seized some of the most resource-rich lands, Peru began the twentieth century with severe fiscal problems. Peru's economic activity was centered in agricultural exports, with an elite holding the majority of the lands and receiving government benefits that perpetuated their position, relying heavily on foreign debt, while the rest of the country suffered from low productivity, exploitation or abandonment.

Rodriguez and Garland were put in charge of the Ministry of Finance and Ministry of Development, but their efforts were short-lived, as Augusto B. Leguia became president of Peru first from 1908–1912, and then 1919–1930. His regime was unequivocally protectionist in the economic realm and tyrannical and dictatorial in the political. Foreign capital did flow freely into the country, although a significant portion of it went into government coffers for the construction of enormous works of infrastructure. Thus, at the end of Leguia's government in 1930, which coincided with the Great Depression—which in fact contributed to the end of his government—Peru was deeply in debt. It was also during his regime that the Peruvian Central Bank had been created.

It was a military coup that ousted Leguia, and thereafter the economy turned inwards once more. It had not been truly open to begin with, but the free flow of capital gave the illusion that Peru's economy was an open one. After the devastation that, supposedly, dependence on foreign capital had brought to the country, the new agenda was promotion of the local industry—protectionism, the creation of public banks to promote economic activity, large infrastructure projects, and price and exchange rate controls. Economic policies were patchwork, with no continuity but rather catering to the needs imposed by the international economy and by local lobbying. Peru had also become an economically concentrated country in a geographic sense: goods and services were more accessible to the population in the cities along the Pacific coast, but not so beyond the Andes. That caused massive migration influxes to coastal cities and the depopulation of the mountain region, with a consequent abandonment of agriculture for internal consumption, which, in conjunction with closed import markets, caused the internal market to fall off

dramatically.

From 1930, military coups became a frequent method of installing new governments. That's how Colonel Manuel Odría became Peru's president in the late 1940s. Although his government was of populist character, he did end the price and exchange-rate controls. Odría also liberalized trade and capital mobility, mostly with the aim to promote exports. He limited government expenditure to infrastructure provision, some basic services, rule of law, and regulation. Odría governed until 1956, and the period was generally one of economic prosperity, partly because the Korean war increased Peru's opportunities to export. Production for local consumption, however, did not enjoy the same prosperity. The Korean war ended, and with it the export-driven prosperity (Contreras 2014).

The main promoter of liberalism throughout these decades was Pedro Beltrán Espantoso (1897–1979, pictured at right). Beltrán had a bachelor's degree in economics from the London School of Economics. He was President of the Peruvian Central Bank in the late 1920s and again in the late 1940s, and from there he espoused a more liberal trade and monetary policy, free of controls on exchange rates and prices (Contreras 2014). Beltrán was also the founder of the newspaper *La Prensa*, and from there became the main liberal voice and opposing force to Odría. When Odría's government



ended in 1956 and Manuel Prado became president, Peru was facing again an economic crisis due to the end of the export prosperity, excessive money printing, and renewed price and exchange-rate controls. Beltrán was asked to become Prime Minister and Minister of Finance between 1959 and 1961, and during his administration he put an end to the controls and the money emission. For a brief period of time Peru enjoyed increased growth rates.

The prosperity did not last too long. In 1963 Fernando Belaúnde became president. His government was populist and the economic focus, just as it had been during the past decades, was on exports. Although Odría's government and subsequent presidents until 1968—Prado and Belaúnde—had made efforts to improve communication within Peru, building ports, railroads and highways that allowed transport from and to the provinces along the coast and beyond the Andes, and even into the Amazon basin, the people in the provinces were in a constant state of discontent. The basis of this discontent was the governments' catering to certain elites, particularly the interests of the export industries. Between 1950 and 1966, annual income growth rates in the export sector averaged 4.1 percent, whereas annual income growth in the rural sector averaged 1.3 percent, and for

medium and small farmers only 0.8 percent (Caballero 1981).

In 1968 another coup overthrew President Belaunde. The military governments that followed blamed the failure of the Peruvian economy on oligarchic-foreign capital arrangements, and their policies were centered around two axes: nationalizing industries, and transferring production from the putative oligarchy to the people. Notorious among those efforts was the agrarian reform of the Armed Forces Revolutionary Government led by Juan Velasco Alvarado. Promulgated on June 24, 1969 as Decree No. 17716, the reform:

- eliminated all forms of large estates,
- established that agricultural production had to be communitarian and based on peasant farmers,
- rebuilt the farmer communities (an attempt to recreate ayllus),
- attempted to create new markets through a supposedly more egalitarian distribution of wealth, and
- aimed at the development of industries that supposedly could transform agricultural production. (Ministerio de Agricultura y Riego del Peru 2015)

Under the military government from 1968 to 1980, 15,826 estates were dissolved and about 9 million hectares of land were apportioned to 368,817 small farmers. The reform reduced discontent in the provinces, but economically speaking it was a failure. The reform forsook economies of scale by dissolving large estates, apportioned the land into excessively small productive units, eliminated the market for land, significantly reduced investment in agriculture, and stifled the influx of new technologies. The history of Peruvian economic institutions also meant that the small farmers to whom land had been allocated didn't take full individual nor collective ownership of the land—which had been handed over to them as communities—but continued to look at the state for guidance (Castillo Dieza 2011).

Broadly, the 1970s were an inward-looking decade characterized by central control, nationalism, state-owned industries, and so-called import substitution. The crisis created by such policies urged a stabilization program that included the participation of the International Monetary Fund, which prepared a plan that included adjustments in the economy and general elections. In July 1980, Belaunde was elected again as president. Although highly populist, Belaunde's government attempted to return to a more export-favorable economy by applying the IMF's stabilization plan. It slowly dismantled the import substitution system by lowering tariffs, liberalizing the financial system, renegotiating foreign debt, and making large adjustments in fiscal policies (Abusada et al. 2000).

The measures, although beginning to show results, were highly unpopular. The discontent of the population that again felt marginalized from government's policies was embodied by paramilitary groups, mainly the terrorist group Shining Path. Belaunde's government mostly ignored the social problems, focusing on the debt crisis and other shocks to the economy such as El Niño, deploying fiscal and monetary policies to absorb these shocks. The Shining Path then reached a magnitude that could not be ignored, and terrorist attacks intensified towards the end of Belaunde's government.

In 1985 began one of the most memorable administrations in Peruvian history: the presidency of Alan Garcia Perez. He represented the popular discontent with the few reforms and the direction (or lack thereof) of economic policy, and his government brought the country back to nationalization, import substitution, and government-managed aggregate demand. To that he added price and exchange-rate controls. Those were also the most vicious years of the Shining Path. Garcia's first government is remembered for one of the highest rates of hyperinflation in world history. The combination of more than generous fiscal and monetary policies, and price and exchange rate controls led to a hyperinflation episode (Kiguel and Liviatan 1995). The Peruvian currency lost nine zeroes: first, the Sol de Oro was replaced by the Inti, where one Inti was equivalent to one thousand Soles de Oro. Towards the end of Garcia's government, the Inti was replaced by the Nuevo Sol, where one Nuevo Sol was equivalent to one million Intis. Thanks to the operation of the Central Bank's printing machine at the insistence of the Treasury, Peru's net international reserves were not only exhausted but even negative.

To a severe debt crisis and hyperinflation, Garcia attempted to add the nationalization of the banks. It was then, around 1987, that a libertarian movement arose in Peru, and it appeared to have gained political and public acceptance in the face of the disastrous economic outcome of Garcia's government. It was called the Liberty Movement, led by writer and later Nobel Prize winner Mario Vargas Llosa. The movement set its sights on the 1990 elections, but they were very active in opposing the further nationalizing attempts by President Garcia. The Liberty Movement and Vargas Llosa led a march to oppose the nationalization of the banks that gathered about one hundred and thirty thousand people in one of the main plazas of downtown Lima. The movement succeeded in impeding the nationalization of banks. The Liberty Movement joined forces with the parties Accion Popular (Popular Action), the Popular Christian Party, and Solidarity and Democracy to form the center-right coalition FREDEMO (Frente Democratico, or Democratic Front).

As the 1990 elections approached, Vargas Llosa representing FREDEMO was viewed as the main contender for President. His reform agenda was very

open about the ‘shock’ economic policies that his government would implement if he was elected president. An independent candidate then emerged, promising less drastic measures: engineer Alberto Fujimori, of Japanese descent, representing Cambio 90 (Change 90), a new party founded in a grassroots campaign that included support from small firms and evangelicals. Vargas Llosa was not only regarded as representing a shock-treatment reform, but also the elite that many Peruvians for so long had resented, while Fujimori was a charismatic underdog, belonging to none of the conflicting races in Peru, and he used the fear of the ‘shock’ to his advantage, promising the people not to implement such a policy, and showing favor for a more gradual approach. Fujimori had neither an economic plan nor economic advisors, but nevertheless he obtained the majority of the popular vote in a runoff and was duly elected president in 1990.

## **The reforms of the 1990s**

Fujimori and his party quickly decided, however, that shock therapy was indeed the way out of the economic crisis. The day after Fujimori’s election, he communicated with another of the important classical liberal voices of the country: Hernando De Soto. Fujimori offered De Soto the headship of his minister’s cabinet, which De Soto refused to accept, because Fujimori had been intent on not implementing needed economic reforms. But shortly thereafter, after hearing De Soto’s and the IMF’s arguments, Fujimori agreed, and De Soto, together with Peruvian banker Carlos Rodriguez-Pastor, prepared a reform plan. A reintegration of Peru to good standing with the international financial community took place, and the economic reforms were publicly announced in the *New York Times* shortly after the meetings with the IMF (Ortiz Martinez 2015).

On August 8, 1990, at 9 p.m., Fujimori’s finance minister Juan Carlos Hurtado Miller made a televised announcement of economic ‘shock’ reforms to take place starting the following day. Price controls were being eliminated, which meant that formal-market prices for the basic commodities of a family’s consumption basket would increase between 200 and 3,000 percent. To stabilize prices, Peru’s Central Bank opted for a monetary rule. The exchange rate was left to float freely. The reduction of public expenditure was strictly enforced. Free capital mobility was guaranteed once again.

According to De Soto, Hurtado Miller was not sufficiently supportive of liberalization, and so he was replaced by Carlos Boloña (Instituto Libertad y Democracia 2015b), a liberal economist with a bachelor’s in Economics from Universidad del Pacifico and a Ph.D. from Oxford University. Boloña, who stepped into the Minister of Finance position in February 1991, with Roberto

Abusada, a Cornell economist, as advisor, continued the economic reforms. Most of the state's presence in the production of goods and services was privatized, markets were deregulated and liberalized, in particular the land and labor market, and a tax reform was enacted, which included the reduction of tariffs to no more than 25 percent (Wise 2003).

These reforms, however, faced strong resistance from the Congress. Presumably seeking to avoid legislative opposition, Fujimori soon dissolved the Congress. Although well-received by part of the population, this self-coup signified a constitutional crisis for the country. The international community did not appreciate such action and threatened economic and political sanctions. But new elections were called, and a new Constitutional Congress was elected. As the name suggests, the newly elected Congress, which ratified Fujimori as president, was charged with drafting a new constitution. The constitution draft was open to the public for criticism and suggestions, and it was approved by popular referendum in 1993.

Some changes to the draft constitution suggested by De Soto and his Institute for Liberty and Democracy (ILD) were implemented, but some were not, among the latter being certain measures for checks and balances and accountability. In fact, the 1993 Constitution concretely gives more power to the President, as it allows for reelection, a unicameral Congress instead of the previous bicameral one, veto power, and easier dissolution of Congress. De Soto actively opposed this attempt to seize power with such few limitations, but the economy's stabilization and the war against terrorism that Fujimori's government had begun seemed a priority in the people's minds, and De Soto wasn't able to rally much support for his cause (Instituto Libertad y Democracia 2015a). Vargas Llosa's Liberty Movement also disbanded shortly thereafter.

In September 1992, leaders of the Shining Path including its head Abimael Guzman were captured. The social and economic outlook of the country improved, as this allowed promotion of further investment and the reintegration of the abandoned provinces. The renewed capital influx enabled the program of privatizations of state-owned enterprises to accelerate (Gonzales de Olarte 2007).

The following years, once inflation had been contained and terrorism virtually eliminated, were of sustained growth. Even as Fujimori consolidated his power, the main line of economic reforms continued. The Constitution had been elaborated to guarantee the continuation of relatively more sound economic policy through three of its articles:

- Article 84 guarantees the independence of the Central Bank, and establishes its function as one of preserving monetary stability.
- Article 60 makes explicit that there shall not be public enterprises unless expressly defined by law, and then only in a subsidiary role.

- Article 58 guarantees that Peru's economy shall be a market economy, where private enterprise's freedom is guaranteed.

Even though its desirability is still questioned by some in Congress, Peru currently appears to be the only country in the world that has such provision for public enterprise etched in its constitution. The 1993 Constitution does leave room for some exceptions, and it certainly allows for regulation and for public expenditure in social policies. The latter was critical for Fujimori as he established his dictatorship, seeing that he used transfers to the poor to enhance his popularity. The resources for those transfers came from increasing tax revenue due to sustained growth and the funds coming from privatizations.

Fujimori formed an alliance with the military and the major business groups, and thanks to the economic reforms he also had the approval of the international financial community. Such support, together with his social policies that kept previously alienated segments of the population relatively content, ensured that his authoritarian rule went uncontested for many years. Many economic reforms were consolidated over the remaining years of Fujimori's mandate, which was extended until the year 2000, when a corruption scandal was revealed. Charged in the scandal, Fujimori fled the country and attempted to abdicate via fax.

## Modern-day liberal economic thought in Peru

Peru-style liberal economic thought does not take a hard line, for the most part. Free private enterprise and free markets are central to it, but they go hand-in-hand with the provision of public services and social policies. This section enumerates the institutions in Peru that promote private enterprise and investment, liberalization of markets where plausible, fiscal and monetary discipline, and other social and government reforms.

### Academia

There are 65 universities in Peru that teach economics, 28 of which are public and the remaining 37 private. Although great philosophers have arisen from centuries-old universities in Peru, the faculties of many of the schools do not necessarily align with liberalism but rather seek a more active role of the state in the economic activity. Exceptions are:

**Universidad del Pacifico (University of the Pacific):** Founded in 1962 by an alliance of Peruvian entrepreneurs and Jesuit priests, its line of thought is markedly liberal. Many of the former and current government officials leading or

continuing the economic and commercial side of the reforms are current faculty of this university. Some of the most distinguished ones are Mercedes Araoz, currently Prime Minister and Second Vice President; Julio Velarde, Renzo Rossini, and Adrian Armas, current President, General Manager, and Chief of Economic Studies of the Central Bank; Carlos Boloña, Minister of Finance during Fujimori's presidency and executor of most of the economic reforms; and Jorge Gonzalez Izquierdo, Minister of Labor and Minister of Foreign Relations during the Fujimori regime, and former Dean of the Economist Society of Lima.

**Universidad Peruana de Ciencias Aplicadas (Peruvian University of Applied Sciences):** Founded in 1994, it is the only Peruvian university that offers a course in 'Austrian' economics. Its faculty includes some of the leading classical liberal thinkers of Peru, such as Enrique Gherzi, professor of law and economics, member of the Liberty Movement, and director of the Mont Pelerin Society between 2008 and 2010; Guillermo Cabieses, also professor of law and economics; and economist Carlos Adrianzen, chair of the economics department.

## Think tanks

**Instituto Libertad y Democracia (Institute for Liberty and Democracy):** Considered one of the world's important think tanks, it was founded by Hernando De Soto (pictured, right). The ILD is a strong advocate of property rights and institutional reform across the globe. As mentioned earlier, De Soto and the ILD were during the 1990s architects of the macroeconomic and institutional reforms and leaders in the return to democracy after Fujimori's coup. They campaigned actively for the creation of Peru's Office of the Ombudsman, which did not exist until then, and whose role was to defend the public interest in lawmaking. Another significant line of work of the ILD is administrative and bureaucratic simplification, and the integration of the informal economy into the legal system. The ILD conducts ongoing projects that promote the inclusion of the population in economic activity through property rights and to draw attention to the role of private-enterprise institutions in the defeat of terrorism in Peru and the promise of the same in the rest of the world.



**Instituto Peruano de Economía (Peruvian Institute of Economics):** Founded by economist Roberto Abusada, who was economic advisor of the Ministry of Finance during Fujimori's government and co-author of many reforms. One of the most important think tanks in Peru, the institute is devoted to

increasing competitiveness in the productive sector of the economy and to the completion of economic and political reforms. It advocates for labor reform and the elimination of excessive regulation of productive sectors and of red tape in the public sector. The general manager, Diego Macera, is a former columnist for *El Comercio* and also senior economist in the Peruvian Institute of Business Administration.

**Grupo Apoyo:** Founded by businessman and engineer Felipe Ortiz de Zevallos, formerly the president of Universidad del Pacífico. Its mission is to advance the global competitiveness of Peruvian firms through provision of information, analysis, and consulting. Apoyo Consulting president Gianfranco Castagnola is a vocal advocate of economic liberty.

**Macroconsult:** The notable partners in this consulting group are Raul Salazar, who was the author of Vargas Llosa's economic plan for the elections of 1990, which would later be implemented by Fujimori, and Elmer Cuba, who was the economic advisor of Keiko Fujimori, daughter of the former president and twice candidate for the Peruvian presidency; she leans toward free-market policies.

**Instituto de Libre Empresa (Institute for Free Enterprise):** Founded and led by Jose Luis Tapia, it promotes freedom of contract, market liberalization, and clear property rights.

## Media

*El Comercio:* It is the oldest newspaper in Peru and a traditional platform for supporters of economic liberty. Back in the early twentieth century it was used by Jose Manuel Rodriguez, and today it features libertarian voices such as lawyer Alfredo Bullard, economist Ivan Alonso, and economist and IPE general manager Diego Macera.

*Peru 21:* Now a subsidiary of *El Comercio*, the newspaper was initially founded by economist Augusto Alvarez Rodrich, a professor at Universidad del Pacifico, who was notorious for making the government somewhat uncomfortable with his editorials. It is now led by economist Juan Jose Garrido Koechlin, another important voice in favor of economic liberty.

**Canal N:** It is a news cable channel linked to *El Comercio*. Juan Jose Garrido Koechlin conducted a program called *Rumbo Economico (Economic Course)*, exploring liberal policy reforms. Jaime De Althaus now conducts the program *La Hora N*, an interview program with a clear non-left slant.

There are other notable journalists who over the last years have advanced reforms towards greater economic and political freedom. Two of the more prominent ones are Federico Salazar, who conducts the morning news show *Primera Edición (First Edition)* on América Televisión, and Jose Luis Sardon, lawyer,

political scientist and economist, and professor in Universidad del Pacifico, with columns in *El Comercio* and *Peru 21*.

## Business associations

**Comexperu (Peruvian Foreign Trade Association):** It is the private association of companies involved in foreign trade in Peru. Its mission is to promote the development and competitiveness of trade, defend the market economy, and promote private investment.

**IPAE (Peruvian Institute of Business Administration):** Created in 1959 by a group of businessmen, it promotes good business practices and competitiveness of Peruvian firms. IPAE organizes the annual Conferencia Annual de Ejecutivos (CADE), an important forum gathering businesses, academia, and government for discussion of economic policy.

## Liberty Movement and Mario Vargas Llosa

Possibly together with the Institute for Liberty and Democracy, the Liberty Movement is one of the most influential forces in favor of liberty over the last thirty years in Peruvian history. The Liberty Movement, even though short-lived (1987–1993), generated vital momentum towards economic liberalism in Peruvian policy. Its leader, Mario Vargas Llosa (pictured at right), who was awarded the Nobel Prize in Literature in 2010, has declared himself a liberal with a ‘defender of liberty’ connotation. Vargas Llosa opposed Alan Garcia’s government during his attempt to continue nationalizing private firms, and he was the main promoter of open markets and monetary and fiscal discipline after Garcia’s catastrophic first presidency. He continues to advocate for liberty through his writings, the most recent one being *The Call of the Tribe* (2018), in which he recounts his journey towards embracing liberal thought and discusses thinkers that influenced him in this evolution of his thought.



## Concluding remarks

Like other Latin American countries studied in this series, Peru has had great difficulty finding a path toward stable and trustworthy government and a liberal

market economy. In earlier times, some voices, such as Jose Manuel Rodriguez and Pedro Beltran, spoke up for liberal principles, but it took the crisis of the late 1980s—hyperinflation, debt, and fiscal crisis—for a liberal movement to rise up and become a durable part of the Peruvian cultural landscape. However, Fujimori's government, because of corruption, and subsequent governments, because of lack of support, did not sustain an impetus for liberal reform.

I recently asked three prominent economists about need and prospects for renewed liberal reform in Peru, and before closing I share some of their remarks.

Jorge Gonzalez Izquierdo, former Minister of Labor, Foreign Relations and professor at Universidad del Pacifico, emphasized that structural reforms to the Peruvian economy remain important, including education reform, health system reform, institutional reform, infrastructure reform, and public-sector reform.

Diego Macera of the Peruvian Institute of Economics indicated that labor reform is crucial for reactivation of the local economy. In 2001 the Constitutional Court of Peru basically subverted the liberalization of the labor market, making labor mobility extra costly, and as a result employers have resorted to short-term contracts instead of long-term hiring. Macera also pointed out that, although the role of the public sector is meant to be subsidiary according to the Constitution, politicians have found ways to be more institutionally extractive, for personal gain, particularly by means of regulation. Macera believes that certain sectors are overregulated, to the point that it inhibits their performance, yet in a way that favors companies of relations of the authors and enactors of such regulation.

Elmer Cuba from Macroconsult finds that the structure of incentives for the continuation of the reforms has been perverted. He indicated that one of the government's mechanisms to execute works of infrastructure is the Works for Taxes program. Under that program, large companies are allowed to finance and execute public works instead of paying the cost of those works in taxes. Cuba noted that the wages of the agent hired to supervise the proper execution of said work are often incorporated within the cost of the work itself, thus creating a principal-agent problem. Another issue pointed out by Cuba is the lack of accountability in public services, because the beneficiaries of those services are not the same ones who are paying the taxes that finance those.

With the election in 2016 of economist Pedro Pablo Kuczynski, a free-market advocate, there were renewed hopes that liberal reform would be revitalized, but President Kuczynski lacked a majority in Congress, and political maneuvering from the opposing party forced him to step out early, leaving his first vice-president, Martin Vizcarra, as the new President of Peru. In spite of the political instability, Peru has the opportunity to establish itself as reasonably secure and honest market economy. For now, Peru seems to have reached a plateau, but the prospects for further improvement are strong.

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