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Chile as a laboratory of economic reforms

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Chile is often cited by the WB/IMF as a model for others to follow. Chile is probably the country with the longest running free-market reforms in Latin America, which began with General Augusto Pinochet's 1973 bloody coup against the democratically elected government of President Salvador Allende. Structural Adjustment (i.e., free market reforms) took a particularly radical form as Chilean economists trained at the University of Chicago sought to transform, via dictatorial power, an economy marked by heavy state intervention into a free-market paradise sketched out by Adam Smith in *The Wealth of Nations*. Not only were all the standard policies of a free-market economy brought into play, free-market pricing, trade and financial liberalisation, monetary devaluation, export-oriented manufacturing, privatisation and deregulation were applied with an ideological vengeance.

By the end of the 1980s, Chile's economy had indeed been transformed: some 600 state enterprises had been sold off, with fewer than 50 remaining in private hands; the country had gone from one of the most to one of the least protected Latin American economies, with all quantitative restrictions on trade abolished and tariffs [illegible] at a single flat rate of 10 per cent for all items; foreign investors had a strong presence in the economy, as part owners of the former state enterprises in such strategic sectors as steel, telecommunications, and airlines; radical deregulation of the domestic financial market had been accomplished; the economy had become substantially more integrated into the international economy, with total trade amounting to more than 57 per cent of the GDP in 1991, compared to 35 per cent in 1970.

The World Bank/IMF had been central to the drastic changes in the economic policies of Chile and they were proud of the result. However, many others raised the question: was its transformation benefiting the poor? If success is to be measured by the levels of the external accounts, then structural adjustment has had dubious results: Chile's external debt of US$19 billion in 1992 was higher than it had been at the start of the debt crisis in 1982; total debt stood at 49 per cent of GNP in 1992; and at that time close to 9 per cent of GDP was flowing out of the country to service the debt.

If sustained growth is regarded as the key measure of the success of structural adjustment, then the results could hardly qualify as a success. Indeed, the growth in GDP during the Pinochet years (1974-89) averaged only 2.6 per cent a year, below the rate registered in the state interventionist decades: 4 per cent in 1950-61 and 4.6 per cent in 1961-71. The results of structural adjustment were more dismal when viewed in terms of growth in per capita GDP: this averaged 1.1 per cent in the 1970s and 0.9 per cent in the 1980s.

The results are indeed meagre when one considers that in order to obtain them, free market policies plunged Chile into major depressions, as pointed out by Lance Taylor, twice in one decade – first in 1975, when GDP fell by 12 per cent, then again in 1982, when it dropped by 15 per cent. In fact, this restructuring of the Chilean economy was negative in more ways than one. The combination of a lower rate of investment and trade liberalisation resulted in deindustrialisation: the manufacturing sector lost ground, declining from an average of 26 per cent of the GDP in 1970 to an average of 20 per cent in 1990. Indeed, from 1979 to 1981 manufacturing shrank in absolute terms, and it was not until 1988 that industrial value-added surpassed the absolute levels attained in 1974. As John Sheahan notes, "The Chilean economy in the market-oriented liberalisation phase...seemed to be moving towards deindustrialisation in the name of efficiency and avoiding inflation."

When one considers the social impact of free-market policy then one moves towards the negative. Despite the free-market optimism that the benefits would filter down to the poor, the benefits were monopolised by the rich. The burden of reform was imposed on the poor and the middle class through a drastic cutback in public spending, a freeze on wages, and a steep devaluation of the peso. The 24 per cent contraction of domestic expenditure provoked a 15 per cent drop in GDP and triggered unemployment, which rose to 30 per cent in the mid-1980s. And the 50 per cent devaluation of the peso reduced real wages by 20 per cent. Yet, after more than a decade of free-market reforms, some 45 per cent of those in work were earning less than a subsistence wage, and where the introduction of "flexible labour market" is making labourers more insecure. Low wage employment is now the main cause of poverty in Chile. Oxfam works with some of the victims of this Latin American "miracle", among them women labourers in Santiago's textile industries. The result is that local labour intensive industries are collapsing and poverty and unemployment are worsening. Oxfam's *Report on Latin America* (1994) points out that WB/IMF reforms have deepened the crisis in Chile. The report also points out the crisis was rooted in a complex array of external and internal factors, including the unequal patterns of land and income distribution. The report further notes that the deregulation of markets under free-market reforms has exacerbated these inequalities, excluding the poorest sections of society from benefits of growth.

At the same time, the rich received subsidies, more than 50 per cent unemployed received no subsidy and the rest obtained only minor benefits. Thus, by 1990 both poverty and inequality had increased. The proportion of families living below the 'poverty line' rose from 24 to 26 per cent between 1980 and 1991. This meant that at the end of the Pinochet period some 40 per cent, or 5.2 million, of a population of 13 million people were defined as poor in a country that had once boasted of having a large middle class. Poverty translated into hunger and malnutrition, for 40 per cent of the population the daily calorie intake dropped to 1629 in 1991, from 2019 in 1970, and 1751 in 1980.

In terms of income distribution, the share of national income going to the poorest 20 per cent of the population fell from 4.6 per cent in 1980 to 4.2 in 1991; over the same period the share going to the poorest 50 per cent declined from 20.4 to 16.8 per cent; while the share going to the richest 10 per cent rose from 36.5 per cent to 47 per cent. In structure terms, the Chilean economy, with its extreme dependence on export of primary or processed goods and its shrinking manufacturing base, was likely to be more fragile by the end of 1990s than it had been before the Pinochet period. We must also add the undermining of democracy that Chilean 'Chicago economists' felt was necessary to translate Milton Friedman's theories into reality.

After ten years of experimentation of free-market by the Pinochet regime, the economy did not show any signs of long-term growth. As concluded by Chilean economist Patricio Meller, "Chile's worst economic crisis in 50 years", and government had to intervene massively to bail out the sinking ship. The leading proponent of state intervention, economist David Felix notes, was "an institute which is a stronghold of Hayekian libertarianism and the major think-tank of Pinochetist wing of the Chilean elite." The Treasury Minister in 1983 has promised the "foreign banks that the government was taking responsibility for servicing their loans to private Chilean firms."

Reviewing Chile's "economic miracle", Latin American economist Cathy Schneider comments that, quite apart from the standard economic features of market reforms – sharply increasing poverty rates and inequality: "the transformation of the economic and political system has had a profound impact on the world view of the typical Chilean. Most Chileans today, whether they own small business or sub-contract their labour on a temporary basis, work alone. They are dependent on their own initiative and the expansion of the economy. They have little contact with other workers or with neighbours, and only limited time with their family. Their exposure to political or labour organisations is minimal, and with the exception of some important public service sectors such as health care, they lack either the resources or the disposition to confront the state. The fragmentation of opposition communities has accomplished what brute military repression could not. It has transformed Chile, both culturally and politically, from a country of active participatory grassroots communities, to a land of disconnected, apolitical individuals."

In short, through government intervention in a free-market experiment, the Chilean rich had substantially increased their economic dominance. It is, therefore, understandable that a recent study for the Organisation for Economic Cooperation and Development (OECD) asserted that the costs of Chilean adjustment were 'among the largest in Latin America,' and concluded by posing the question: 'Would this type of adjustment have been feasible in a democratic regime?' The so-called "success story" regarding Chile is dubious. It is aid-driven or based on exports of primary products; Chile, the most heralded example, relies on copper for more than 30 per cent of export revenues and agroexport for most of the rest, and thus is highly subject to "terms of trade shock" from policies of the rich nations.

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