

The Economic Modernization of Chile

In March 1973 annual inflation reached 183%, rising above 300% in the first half of the year to end with a record increase of 508.1%. In twelve months, real salaries dropped 5.7% in January 1973 and 20.4% in July of that year. Production was also collapsing. Between January and July 1973 industrial production dropped 94% compared to the same period the previous year.

These circumstances established a scenario where the economic system in effect in Chile, which had been distant from the Communist orbit and more closely associated with the western tradition, was approaching its end, giving way to the establishment of a new system where the State owned the means of production and assigned economic resources. In short, we were facing the grave threat of the birth of a Popular Republic of Chile with an economic and political system similar to the ones in various countries behind the Iron Curtain at that time.

In the last few weeks of Salvador Allende's administration, the paralyzation of the country and its economic collapse were almost complete. This situation, together with the heightened violence, created a scenario that presaged an outcome everyone regretted but

few did anything to avoid. On September 11, 1973 Chile's destiny started to change.

Rebuilding the Country

The situation described above led the Military Government, headed by President Augusto Pinochet, to implement a new economic strategy that was preceded by a political definition: create the conditions for freedom to reign in Chilean society.

When the Armed Forces handed over power on March 11, 1990, Chile had undergone a profound political and economic transformation, founded on a society of freedom where democracy has been profiled not only as a form of government to elect authorities but more importantly as a way of life that provides the appropriate conditions for the exercise of individual responsibilities.

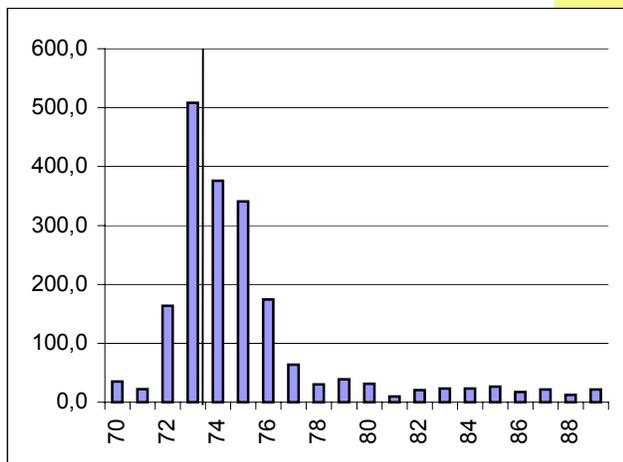
The most relevant aspects of the new economic strategy were: the opening of the Chilean economy to international competition with a substantial reduction in tariffs and a realistic exchange policy. Permitting markets to operate freely in order to orient the efficient assignment of resources. The order of subsidiarity in the sense of providing opportunities for the exercise of individual freedom. The presence of the eminently non-discretionary rule, which

made political events and economic activity independent of one another. In defining economic policy goals, special emphasis was placed on focusing social spending on growing human capital, especially in lower income sectors, leaving aside decades of preaching about the social issue that were not related to State social programs, which actually favored

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**Graph No. 1
Annual inflation**



Fuente: INE

medium and high-income sectors. This was the case for housing programs, spending on higher education, and many health programs before the Military Government.

President Pinochet's strength and conviction made it possible for the economic strategy adopted in 1973 to become permanent. In managing the crisis of 1982 with realism and coherence, he created the conditions for the Chilean economy to undergo a period of growing prosperity starting in 1985, which was based on privatization and important structural reforms like the consolidation of the new pension system, health, education, and the gradual elimination of poverty.

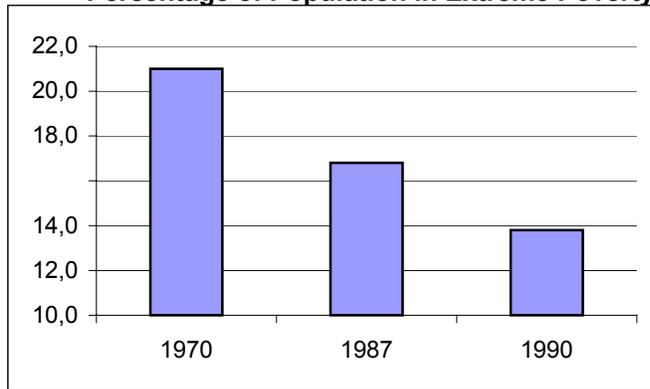
Despite the fact that during the entire reform process it was criticized by the leaders of the coalition that is in government today, the coalition maintained the basic principles and policies that were implemented during the government of the Armed Forces.

The economic task cannot be accomplished by itself. The vision of a country, in a long-term perspective, requires that modernization of the economy be supported by an institutional reference. That reference must provide the necessary stability to orient savings, investments, and sustained economic growth. The strengthening and autonomy of intermediary bodies, guarantee of the right to property, exercise of the non-discretionary rule, exclusive responsibility of the President of the Republic for budget management, limitation of subjects that are characteristic of the law, and presence of an independent Central Bank are essential in that institutional dimension. All of those aspects were included in the Political Constitution of the State which, together with constitutional criteria of limited powers, have enabled the country to develop a permanent economic strategy.

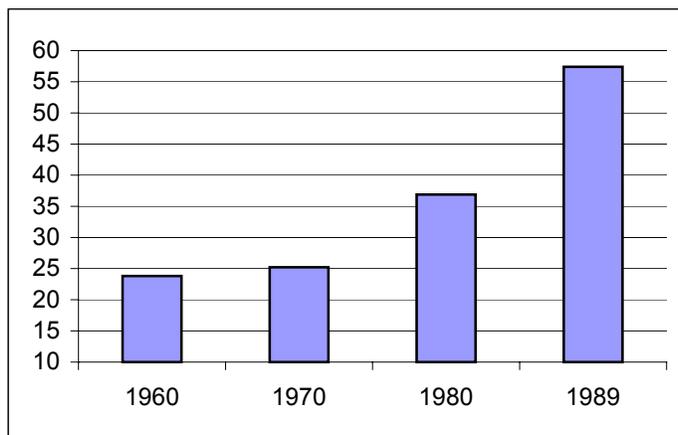
When evaluating the Chilean economy during the Military Government, its realism, coherence, and long-term vision should be highlighted as significant elements. A society of freedoms was founded, where democracy has been profiled not only as a form of government to elect authorities, but more importantly as a way of life that provides the appropriate conditions for the exercise of individual responsibilities. Those are the factors that have given a permanent nature to the major reforms carried out since 1973. When the Armed Forces handed the power over on March 11, 1990, Chile had experienced a profound political and economic transformation.

Long-Term Outlook

Graph No. 2
Percentage of Population in Extreme Poverty



Graph No. 3
International Trade as % of GDP



Source: Central Bank

free trade agreements, the enhancement of the private social security system, and the privatization of sanitation services, highways, and other public services.

Those characteristics have enabled Chile to grow vigorously, more than ever before, doubling its per capita income and thereby making it one of the highest in the region. Poverty has continued to decrease and, due to the improvement in coverage of educational services, income distribution in the younger generations in Chile has been improving, despite the fact the Concertation has lacked conviction about the merits of a free market economy like the one that was launched in the mid-70s. What is missing is the conviction and will that President Pinochet's government had to make reforms that will enable the country to aspire realistically to being a developed nation in the short term •

The Wisdom of the Concertation

Despite the fact that the leaders of the coalition that is currently in government criticized the reform during the entire process, they maintained the basic principles and policies that were implemented during the government of the Armed Forces. In some areas the coalition has even improved those policies, as it did with the opening of trade through multiple